tion of the 12% interest rate to this assessment is beyond the Commission's jurisdiction to decide.

Neither the taxpayer nor the department has appealed this decision.

All-Power, Inc. vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, November 1, 1985). This was a timely filed appeal objecting to the department changing the taxpayer's method of reporting its Wisconsin income for taxation from separate accounting to apportionment and the assessment of additional income taxes resulting therefrom for the period October 1, 1975 through September 30, 1979. The sole issue for the Commission to determine was whether, during the period involved, the taxpayer's business activities in Wisconsin were an integral part of a multistate unitary business within the meaning of s. 71.07(2), Wis. Stats., with its income thus subject to apportionment.

All-Power, Inc. is a corporation engaged in the business of distributing truck parts with its main office or principal place of business located at 3435 South Racine Avenue, in Chicago, Illinois. In addition to its main office in Chicago, the taxpayer also has facilities located in Decatur, Illinois and Butler, Wisconsin.

The taxpayer's facility at Butler, Wisconsin, known as Drive Shaft Clutch and Gear Division, is staffed by one store manager and eight employes which include three salesmen and five counter and shop employes who repair truck and driveshafts. The taxpayer has no corporate officers located in the State of Wisconsin.

Virtually all activities of the taxpayer's Wisconsin operation are directed or controlled by its Chicago headquarters, including accounting, advertising, hiring and firing, inventory control, markup or profit margin, expense account approval, selection of items to be sold, and credit approval.

Except for a small petty cash fund, all monies received by the taxpayer's Wisconsin operation are forwarded to its Chicago headquarters.

The Commission held that the taxpayer's Wisconsin operation, known as Drive Shaft Clutch and Gear Division, is not a discrete business enterprise, but rather is an integral part of the taxpayer's multistate unitary business. The department acted properly in changing the taxpayer's method of reporting its Wisconsin income for taxation from separate accounting to apportionment.

The taxpayer has not appealed this decision.

American Telephone & Telegraph Company vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, October 31, 1985). American Telephone & Telegraph Company timely filed its Wisconsin income tax returns for its tax years ending December 31, 1972 through 1976 inclusive. On December 14, 1978, the department issued a Notice of Assessment of Additional Tax for the taxpayer's tax years ending December 31, 1972 through 1976 inclusive. The total amount of the deficiency assessed, including tax and interest computed to February 15, 1979, is $3,597,288.90.

American Telephone & Telegraph Company is a New York corporation with its principal office located in New York City, New York. It is a regulated public utility which furnished interstate and international (referred to as "interstate") telecommunications services and is the parent corporation of 21 operating telecommunications companies (known as Associated Companies), Western Electric Company, Incorporated (Western)—a manufacturer and supplier of telecommunications equipment—and Bell Telephone Laboratories, Incorporated—a research and development company. The taxpayer, together with these subsidiaries and two operating telecommunications companies (Associated Companies) in which the taxpayer holds a minority interest, are known as the Bell System.

Each of the 23 Associated Companies furnishes local exchange, wide area and message toll intrastate telecommunications services in its operating territory within each state and participates within this territory jointly with the taxpayer and other non-Bell System telecommunications companies in the furnishing of interstate telecommunications services. Each is a separate corporate enterprise with its own Board of Directors and its own officers. A majority of the members of each company's Board of Directors is composed of persons in the fields of business and finance who are knowledgeable as to local conditions in the operating territory of the company of whose Board they serve. Only one of the members of each of these Boards is an officer of the taxpayer, and none is a director of the taxpayer. These companies are subject to regulation by state and federal regulatory agencies. As of December 31, 1976, these 23 companies collectively employed over 735,000 employes and had investment in telecommunications plant totalling almost 89 billion dollars. The taxpayer has only a minority ownership in two of these companies. The remaining 21 are either wholly owned (16, including the Wisconsin Telephone Company) or more than 85% owned by the taxpayer. Wisconsin Telephone Company has property and employes within the state, and files its own separate Wisconsin income and gross revenues tax returns.

Bell Labs, owned half by the taxpayer and half by Western, conducts scientific research, development and design work in all aspects of the telecommunications business. Funded for this purpose by the taxpayer, Western and the Associated Companies, Bell Labs is a separate corporation with its own Board of Directors and officers. That portion of the expenses of Bell Labs funded by the taxpayer and the Associated Companies is subject to continuous regulatory scrutiny.

Western is a manufacturing corporation with its own Board of Directors and officers, doing business in all 50 states. It is principally engaged in the business of manufacturing and supplying communications equipment and products to the Associated Companies and the taxpayer, and the provision of related engineering and installation services. This work is done pursuant to standard supply contracts between it and its customers. Under these contracts, Western is obligated to meet the equipment needs of the Bell System operating units.

Western's prices and profits are continuously reviewed by the National Association of Regulatory Utility Commissioners (NARUC) - Federal Communications Commission (FCC) Staff Subcommittee on Manufacturing and Service Affiliates with the objective that any savings to Western or a Bell System operating unit which

could arise from its being a part of the Bell System are ultimately passed on to the subscribers. It conducts business in Wisconsin and has property and employes within the state with respect to which it files its own separate Wisconsin income tax returns. As shown by such filed Wisconsin returns, Western conducts approximately 1% of its total business in the state.

The taxpayer is responsible alone or jointly with the other Bell System and non-Bell System telecommunications companies for the construction, ownership, operation and maintenance of a network of interstate telecommunications facilities to provide for interconnection of the Associated Companies and other telecommunication companies in the United States and telephone systems in most other countries throughout the world. Some of these facilities extend into and through the State of Wisconsin, or originate or terminate in Wisconsin. In performing this business, the taxpayer operates, and thus has property or employes or both, in 49 states, including Wisconsin.

As of December 31, 1976, the taxpayer's activities in Wisconsin consisted of the operation and maintenance of the interstate telecommunications system, including a portion of two interstate cable routes (one terminating at Watertown Junction and the other terminating at Stevens Point) and several radio relay routes crossing the state. The property owned and used in Wisconsin in the operation of its interstate business consisted of land, buildings, central office equipment, cable, furniture and office equipment, motor vehicles and materials and supplies. This property had a gross book cost of approximately 99 million dollars, which was about 1.5% of the total gross book cost of property owned and used by the taxpayer in its interstate business operations (approximately 6.8 billion dollars). Approximately 80% of this property in Wisconsin was central office equipment (for purposes of switching, signaling or carrying interstate communications) in eleven central offices in seven Wisconsin cities. The taxpayer also maintained an administrative office in Madison and a District sales office in Milwaukee. It employed at that time 235 employes within the state, 218 of them involved in the operation, control or maintenance of the interstate communications system and 17 involved in the sales of interstate communications services throughout Wisconsin. While the details may have varied from time to time, at all material times prior thereto its property and activities in Wisconsin were substantially the same or similar.

The taxpayer is responsible for (a) the provision to all of the Associated Companies pursuant to license contract agreements of technical assistance, advice and research in all aspects of the communications business, for which it receives fees, the payments of which by the licensees are subject to scrutiny by the various state and federal regulatory commissions; and (b) the investments in its subsidiaries (approximately 29 billion dollars, as of December 31, 1976), which includes the custody and control of securities, receiving dividends, and providing capital to these subsidiaries through either the purchase of additional stock or the making of cash advances. Advances are extended at the prevailing interest rate and repaid to the taxpayer in cash or additional stock. The dividends, interest and license contract fees received by the taxpayer are managed and directed by it in New York, and constitute the taxpayer's principal sources of income other than the income generated by it in connection with the interstate telecommunications business.

The taxpayer files schedules of rates and charges with the FCC with respect to interstate telecommunications services, which schedules are concurred in by other Bell System and non-Bell System carriers who join in the furnishing of such services. In furtherance of its mission (a) to create and maintain a rapid, efficient communications network; (b) to ensure that adequate facilities are provided for the network; and (c) to require the provision of service pursuant to tariffs which offer just and reasonable rates, practices, procedures and regulations, the FCC has been given authority under The Communications Act of 1934 to determine proper rates and promulgate rules affecting interstate services and facilities and has exclusive jurisdiction over the interstate activities and property of all telecommunications carriers, including the taxpayer, the Associated Companies and the over 1,700 other telecommunications companies. All charges for interstate services must be submitted to the FCC for approval and permission must be obtained from the FCC before undertaking any new construction, acquisition or operation of interstate facilities or the introduction, discontinuance or reduction of interstate telecommunications services.

The taxpayer provides only interstate telecommunications services pursuant to interstate tariffs and is regulated by the FCC. The Associated Companies furnish both intrastate and interstate telecommunications services and are subject both to state regulatory authorities (e.g., Wisconsin Telephone Company is regulated by the Wisconsin Public Service Commission) with respect to intrastate services, and the FCC with respect to services they provide within each of their specific operating territories in connection with the interstate communications systems. It is required that separate regulatory policies be administered by separate regulatory authorities. Whereas the FCC has jurisdiction over only interstate services, each state regulatory authority is authorized to regulate only the intrastate services of carriers within its jurisdiction. The degree of control over intrastate telecommunications services within that jurisdiction is similar to that exercised by the FCC over interstate telecommunications services. All charges for intrastate services must be submitted to the appropriate state regulatory authority for approval and permission must be obtained before a carrier may undertake any new construction, acquisition or operation of intrastate telecommunications facilities or introduce, discontinue or reduce intrastate telecommunications services.

The taxpayer receives revenues from its interstate business activities based upon a fair rate of return as determined by the FCC. Each of the Associated Companies and other telecommunications companies receives revenues from its intrastate business activities based upon a fair rate of return as determined by the appropriate state regulatory authority, and revenues from its interstate business activities based upon a fair rate of return as determined by the FCC. A fair rate of return is that which permits a carrier to earn only that amount of income sufficient to meet the demands for telecommuni-

cations services in its operating territory at a reasonable cost to the public, to compensate investors fairly and to continue to attract capital on reasonable terms.

It is necessary for each telecommunications carrier, except the taxpayer, to determine the proportion of its expenses incurred in, and of its plant devoted to, the furnishing of interstate as distinguished from intrastate services. This is done in accordance with the methods set forth in the Separations Manual developed by NARUC and the FCC. These procedures were prescribed by an FCC order and have become part of its rules and regulations. They have been accepted for use by state regulatory bodies. Based upon these procedures, approximately 75-80% of an Associated Company's property and activities is related to the provision of intrastate telecommunications services.

Charges for interstate telecommunications services are in most instances billed to customers by the local carrier and each carrier accounts for this revenue to the taxpayer. These revenues are then divided among all the participating carriers under what is known as the Division of Revenues and Settlements process. In accordance with this process, non-Bell System carriers are first compensated for their participation in furnishing interstate services. Then each of the Associated Companies is reimbursed for its respective expenses attributable to furnishing interstate services determined in accordance with the Separations Manual and the taxpayer is reimbursed for its expenses. The residue is then divided amongst the Associated Companies and the taxpayer to provide a uniform rate of return on the relative value of their net plant investment devoted to the furnishing of interstate services—determined pursuant to the Separations Manual for the Associated Companies. During the period involved, approximately three-quarters of these net interstate revenues went to the Associated Companies and approximately one-quarter went to the taxpayer.

To determine what portion of the interstate revenues received by the taxpayer is attributable to Wisconsin, it utilizes a "50-state study" under which such revenues are divided among the states subject to procedures similar to those used in the Division of Revenues process. During the years in question the Wisconsin percentage was between 1% to 1.5%.

In the years 1975 and 1976, the taxpayer received dividend income from its subsidiaries and nonsubsidiaries of $2,605,840,385 and $2,871,718,743, respectively, as accounted for in its books. These dividends were included by the department in the taxpayer's gross income for the purpose of computing the taxpayer's apportionable income as the department considered to be required by s. 71.07(1m), Wis. Stats.

The dividends from one of the taxpayer's subsidiaries, Wisconsin Telephone Company, were included in the taxpayer's gross income, since they were included in the "General Department Net Income," but the dividends from Wisconsin Telephone Company were deducted as a deductible dividend in arriving at net income subject to apportionment.

Dividends paid by the taxpayer to its stockholders in 1975 and 1976 were $2,166,360,000 and $2,488,875,000 respectively, as accounted for in its annual report to stockholders in those respective years.

Interest paid by the taxpayer to its debt holders in 1975 and 1976 amounted to $538,791,291 and $543,775,611 respectively, as accounted for in its books.

Attached also to each return filed by the taxpayer was a written statement substantially the same as the following language contained in the 1976 return:

> "The (Petitioner) also derives revenues from sources other than, and separate from, the operations of the long distance communications system and such revenues are separately accounted for. These are dividends, interest, license contract and miscellaneous revenues, which result from its investments, its activities in communications research and its services in rendering technical advice and assistance to its associated telephone companies. None of these separate revenues arises from the property owned or business transacted in Wisconsin."
>
> "For reasons apparent from the above explanation, it is necessary to segregate the entire gross income and deductions of the (Petitioner) into two classes, non-apportionable items unrelated to Wisconsin and apportionable items partly related to Wisconsin, and such a segregation is shown on Schedule No. 1 attached to the return. The items segregated as non-apportionable relate to all activities of the (Petitioner) other than the operation of the long distance communications system and those segregated as apportionable relate to the operation of the long distance communications system, part of which is in Wisconsin."

Following the amendment of s. 71.07(1m), Wis. Stats., in 1975 pertaining to the treatment of certain types of intangible income, including dividends and interest, the department has for 1975 and subsequent tax years included in the taxpayer's apportionable Wisconsin income all dividends and interest received from the taxpayer's subsidiaries and other sources. The department also has included in the taxpayer's apportionable Wisconsin income for the tax years 1972 through 1976, the taxpayer's license contract revenues, rents, capital gains and other miscellaneous income, and for tax years 1973 through 1976, the taxpayer's royalty income.

On March 14, 1980, the taxpayer filed with the department a claim for refund, claiming that federal income taxes paid during 1975 and 1976 are deductible under ss. 71.04(3) and 71.02(1)(c), Wis. Stats. The taxpayer and the department agree and stipulate that the issue raised therein, and any refunds or reductions of tax liability resulting from resolution thereof, shall not be foreclosed by the Wisconsin Tax Appeals Commission's determination on other issues in this proceeding not presented by such claim. Any such deduction in tax liability or refund shall be computed and made by the Wisconsin Department of Revenue if and when such result is warranted by a determination addressing the substantive merits of the issue raised by such claim in some other proceeding before the Commission which has become final under ss. 73.01 or 73.015, Wis. Stats., and such reduction or refund shall be made notwithstanding that a final determination shall theretofore have been or thereafter is made with respect to any

other issues in this proceeding, the determination of the issue regarding deduction of federal income taxes being specifically reserved and governed by such final determination in such other proceeding and subject to such further proceedings thereon as the Commission shall deem appropriate to effect the purposes of this stipulation. The parties further stipulate and agree to seek leave of the Commission to amend the pleadings of this proceeding to conform hereto.

The taxpayer claimed that the above assessment is predicated upon the department for the first time departing from its acceptance of the multiform basis upon which the taxpayer had reported its income for more than fifty years and including within the taxpayer's apportionable base income and related expenses from sources other than and separate from the taxpayer's income and expenses attributable to its interstate telecommunications business within and without Wisconsin. Such inclusion of other income, excluding the taxpayer's dividend and interest income, and related expenses for tax years 1972 through 1974 resulted in a refund situation. The significant deficiency assessed for 1975 and 1976 resulted from the addition of the taxpayer's dividend and interest income to the other income included in its apportionable base without any corresponding inclusion in the prescribed apportionment formula of the underlying economic factors which generated the dividend and interest income.

The department's only basis for taxing the taxpayer arose from the taxpayer's conduct of its interstate telecommunications business activities in Wisconsin. For many years, the department accepted the taxpayer's tax returns which included in the taxpayer's apportionable income base only the taxpayer's income from such interstate activities. Section 71.07(1), Wis. Stats., was amended, effective 1975, and the department contended that the effect of such amendment is to require it to include in the taxpayer's apportionable base for tax years 1975 and 1976 several billion dollars of dividends and interest received from the taxpayer's subsidiaries outside Wisconsin without considering the property or activities which produced such income in the factors of the apportionment formula.

It was the taxpayer's contention that the Wisconsin statute does not require any variance from the method accepted by the department for many years and that the department has imposed an apportionment scheme on the taxpayer that taxes income which is not derived from its business or property in Wisconsin and which does not accurately reflect the business of the taxpayer in Wisconsin.

The department argued that (a) the taxpayer's Wisconsin operations constitute an integral part of a unitary business, subject to statutory apportionment of its corporate income, (b) apportionment of the taxpayer's income under the unitary principle is the proper method of taxation as opposed to the multiform method of reporting, (c) the statutory changes in 1975 compelled the department to treat the taxpayer as a single unitary business, (d) under Wisconsin law the apportionment formula may not include the factors of the taxpayer's subsidiary corporations, contrary to the taxpayer's assertion, (e) the department's assessment is not subject to challenge under the U.S. Constitution, and (f) the Commission should hold that the department has properly applied the governing statutes and rules in this case.

AT&T is functionally divided into two divisions, the Long Lines Department and the General Department. Long Lines is responsible generally for the construction, operation and maintenance of a nationwide system of interstate telecommunications facilities and related equipment which serve to interconnect the facilities of over seventeen hundred operating telecommunications companies in the United States as well as telecommunications systems abroad; and some of these facilities extend into and through the State of Wisconsin. In performing this interstate business, Long Lines operates and thus has property or employes or both, in 49 states, including Wisconsin.

The General Department holds and manages the stock owned in these subsidiaries and two minority-owned Associated Companies and provides capital, advice and assistance to them.

The Wisconsin Telephone Company, a wholly-owned subsidiary of the taxpayer, conducts its business, has property and has employes within the State of Wisconsin. The Wisconsin Telephone Company furnishes primarily intrastate telecommunications services entirely within Wisconsin, subject to regulation by the Wisconsin Public Service Commission and pursuant to tariffs on file therewith. It also participates within Wisconsin jointly with Long Lines and other telecommunications companies in the furnishing of interstate telecommunications services, subject to federal regulation.

During the periods involved, the taxpayer's Wisconsin operations constitute an integral part of a unitary business of which the operation of that portion of the taxpayer's business within the State of Wisconsin was dependent upon the operation of the business outside the state and the operation of that portion of the taxpayer's business within the State of Wisconsin was contributory to the operation of the business outside the state.

The assessment and action made by the department are presumed to be correct and the burden of proof is on the taxpayer to show in what respects the department erred in its determination. The taxpayer and its Bell System businesses were not discrete business enterprises, but rather were integral parts of the taxpayer, Bell System's unitary business during the period at issue, and therefore, the taxpayer failed to meet its burden of proof to show the department's assessment to be incorrect.

The Commission held as follows:

A. During the period at issue, the Bell System constituted a unitary business and the taxpayer's business within Wisconsin was an integral part of such unitary business.

B. During the period at issue, the taxpayer is not entitled to determine its income attributable to Wisconsin by an allocation or separate accounting method (or "multiform method"), and the department acted properly in requiring the taxpayer to utilize the apportionment method of determining its income attributable to Wisconsin, pursuant to s. 71.07(1m), Wis. Stats.

C. The 1975 amendment to s. 71.07(1), Wis. Stats., (creating 71.07(1m), Wis. Stats.), which permitted the department to include certain types of intangible income as Wisconsin apportionable income, does not compel inclusion of all of the tax-

payer's intangible income regardless of derivation in Wisconsin apportionable income. Under the holdings in *ASARCO, Inc. v. Idaho State Tax Commission,* 458 U.S. 307, 102 S.Ct. 3103, 73 L. Ed 2d 787 (1982) and *F. W. Woolworth Co. v. Taxation and Revenue Department of New Mexico,* 458 U.S. 354, 102 S.Ct. 3128, 73 L. Ed. 2d 819 (1982), intangible income earned by the taxpayer may only be subject to apportionment in Wisconsin where there exists a "rational relationship" between such income and the taxpayer's business in Wisconsin—that is where the intangible income is not derived from "discrete business enterprises" that in any business or economic sense have nothing to do with the taxpayer's activities in Wisconsin.

D. During the period at issue, the taxpayer's "General Division" was not a discrete business enterprise but rather was an integral part of the taxpayer's unitary business. Pursuant to s. 71.07(2), Wis. Stats., the taxpayer's income derived from the operations of this division including in part, fees from contract services, royalty income, interest earned in short-term investments, and dividend income, including all of the dividend income other than income from Wisconsin Telephone Company, was includable in its Wisconsin apportionable income.

E. During the period at issue, the taxpayer's 23 subsidiaries (Associated Companies, Western Electric Company, Incorporated and Bell Telephone Laboratories, Incorporated) were not discrete business enterprises but rather were integral parts of the taxpayer's unitary business, and pursuant to ss. 71.07(1m) and 71.07(2), Wis. Stats., dividends received by the taxpayer from these subsidiaries were includable in its Wisconsin apportionable income.

F. Under the authority of s. 71.07(2)(e), Wis. Stats., the department adopted Wis. Adm. Code section Tax 2.50 defining the apportionment formula to be utilized in determining the Wisconsin apportionable income of public utilities. For the period at issue, the department acted properly in applying section Tax 2.50 in determining the taxpayer's business income attributable to Wisconsin, and the prescribed formula adopted in section Tax 2.50 did not result in a substantial distortion of the taxpayer's income attributable to Wisconsin.

G. Income from intangibles includable in the taxpayer's 1975 and 1976 Wisconsin apportionable income, come within the intent and meaning of s. 71.07(2)(c)1, Wis. Stats., as "total sales" includable in the denominator of the sales factor.

H. Except as provided in Conclusions of Law, Paragraph G, above, under Wisconsin law, the taxpayer is not entitled to combine the sales, payroll and property of dividend paying subsidiaries in the denominator of the three factors.

I. The Commission does not have the authority of jurisdiction to rule on the constitutional issues raised by AT&T.

The taxpayer has appealed this decision to the Circuit Court.

Cedarburg Mutual Insurance Company vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, November 1, 1985). In WTB #45 it was indicated that the department had appealed the Tax Appeals Commission's adverse decision dated November 1, 1985 to the Circuit Court. The department has dropped its appeal.

Central Wisconsin Wholesale, Inc. vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, January 10, 1986). Central Wisconsin Wholesale, Inc. was incorporated as a Wisconsin corporation in July of 1977. During its first full year of operation (1978), the taxpayer, who was on the accrual method of filing, reported and deducted its bad debts on an estimated reserve basis.

The department in the assessment under review converted the taxpayer's method of deducting its bad debts from the estimated reserve method to a direct write-off method and cited s. 71.04(7), Wis. Stats., as authority. This change resulted in an assessment of additional income taxes covering the years 1979 through 1982, which was issued by the department on March 12, 1984.

The taxpayer conceded that it was incorrect in using the reserve method of deducting its bad debt but alleged that the error has been corrected and the year 1978 was closed to change by the statute of limitations. The department argued that the correction it made constituted a change in the taxpayer's method of accounting and that the assessment involved was timely.

The Commission concluded that the taxpayer incorrectly reported and deducted its bad debts on an estimated reserve basis. The department properly converted the taxpayer's method of deducting its bad debts from the estimated reserve method to a direct write-off method per the clear and unambiguous language contained in s. 71.04(7), Wis. Stats. The department's conversion of the taxpayer's method of deducting its bad debts constituted a change in its method of accounting per the terms of Wis. Adm. Code section Tax 2.16(2). The taxpayer's tax years 1979 through 1982 were open to audit and assessment at the time the department's assessment was issued on March 12, 1984.

The taxpayer has not appealed this decision.

Consolidated Freightways Corporation of Delaware vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, January 17, 1986). The issue to be decided before the Commission was whether the apportionment formula for the apportionment of the income of interstate motor carriers of property provided for in section Tax 2.47, Wis. Adm. Code, imposes a tax on income derived from business transacted and property located outside of Wisconsin in violation of s. 71.07(2)(e), Wis. Stats.

Consolidated Freightways Corporation of Delaware (CF) is a "general commodity" common carrier operating in interstate commerce. CF serves small and large shippers in small and large communities, transporting manufactured and consumer goods. CF is not typically or principally a transporter of truckload and volume shipments but of small individual shipments. Traditionally, less-than-truckload (LTL) shipments weighing under 10,000 pounds have been considered small shipments.

Successful operation of a general commodity carrier requires consolidation of many small shipments for over-the-road or line-haul movement with the constant objective of minimizing the number of handlings of the shipment and the total miles of operation.