STATE OF WISCONSIN

TAX APPEALS COMMISSION

MICHAEL AND LINDA BLISS
2813 Sherwood Drive
Janesville, WI 53545,

Petitioners,

vs.

WISCONSIN DEPARTMENT OF REVENUE
P.O. Box 8907
Madison, WI 53708-8907,

Respondent.

DOCKET NO. 03-I-303

DECISION AND ORDER

DIANE E. NORMAN, COMMISSIONER:

The above-entitled matter was called for hearing on February 17, 2005. Petitioners appeared in person and were represented by Attorney Richard F. Rice. Respondent, Wisconsin Department of Revenue (respondent), appeared by Attorney Michael J. Buchanan. Both parties filed post-hearing briefs.

Having considered the entire record before it, the Commission finds, concludes, and orders as follows:

FINDINGS OF FACT

Jurisdictional Facts

1. By notice dated November 18, 2002, respondent issued an income tax assessment against petitioners for the years 1998, 1999, and 2000 (period under review) in the amount of $7,361.55, including interest computed to January 20, 2003 (Exhibit 1).

2. Petitioners filed a timely petition for redetermination by correspondence received by respondent on January 8, 2003 (Exhibit 2).

3. By notice of action dated November 17, 2003, respondent denied petitioners' petition for redetermination (Exhibit 3).

4. On December 3, 2003, petitioners filed a timely petition for review with the Commission.

Other Facts

5. During the period under review and up to the date of the hearing in this matter, petitioners resided in Janesville, Wisconsin, and were both employed full-time with GM North American Operations in Janesville, Wisconsin (Tr. pp. 15, 55-56).

6. In January of 1996, petitioners purchased 160 acres of wooded real property (the property) in Richland County, Wisconsin, on a land contract (Tr. pp. 16-17, 53).

7. The property had been previously logged, resulting in some bare patches of land on the property (Tr. pp. 16, 58-59).

8. Petitioner Michael Bliss testified that petitioners purchased the property because they wanted to have some wooded property where they could get away from other people, hunt, and relax (Tr. pp. 50-51, 77-78). Petitioners obtained hunting licenses each year during the period under review (Exhibit 13, Interrogatory 13, and Exhibit 12, Response 13).

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9. Petitioner Michael Bliss testified that petitioners also wanted to own wooded property that could be logged as a tree farm for income during retirement,

so that they could spend part of each year on the property and part of the year in a southern climate (Tr. pp. 17-18). No evidence was presented as to when petitioners planned on retiring.

10. Petitioners did no research prior to purchasing the property to determine the profitability of tree farming (Tr. pp. 59-62). They did not know the value of the trees on the property or the market price of lumber (Tr. pp. 59-61).

11. Petitioners have never belonged to any tree farming associations (Tr. p. 74).

12. Petitioners had neither prior experience in working on tree farms nor any background in logging prior to purchasing the property (Tr. pp. 56-57).

13. On January 1, 1997, petitioners entered into a Managed Forest Lands Stewardship Forestry Plan (the Plan) with the Wisconsin Department of Natural Resources (DNR) for 80 acres of the property (Exhibit 12). This property had been in the Plan with the previous owners of the property. The Plan was in effect for the entire period under review. The Plan provided that petitioners "wish[ed] to favor the tree species necessary to provide quality habitat for turkey, deer and grouse" as their objective for management of the 80-acre parcel (Exhibit 12).

14. Prior to cutting or logging any trees on the parcel of land in the Plan, petitioners must obtain permission from the DNR (Tr. pp. 75-76).

15. Another 8.9 acres of the property was in the Conservation Reserve Program (CRP) during the period under review (Exhibits 14 and A). Petitioners were prohibited from planting any trees on the 8.9-acre parcel in the CRP (Tr. p. 65). The CRP required that the 8.9-acre parcel be maintained in existing vegetation and

protected from grazing by domestic livestock (Exhibit 14). Petitioners agreed to plant a "wildlife food plot" on .8 acres of the CRP parcel in August 1997 (Tr. p. 67).

16. The only income petitioners earned from the property during the period under review was the CRP rent payments for complying with the CRP on the 8.9-acre parcel (Exhibit A).

17. In order to cut trees on the remaining 71.1-acre parcel, a logger would be required to cross over the 8.9-acre parcel subject to the CRP (Tr. pp. 66-67). In order to cross this parcel, permission must be obtained from the U. S. Department of Agriculture (Tr. pp. 66-67).

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18. For each year during the period under review, petitioners attached a Schedule F to their Wisconsin and federal tax returns in which they claimed they were engaged in farming during that calendar year (Exhibits 6, 7, and 8).

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19. During the period under review and up to the hearing date in this matter, petitioners did not harvest or sell any trees from the property (Tr. p. 70).

20. Petitioners never intended to log the property themselves, but planned to hire a logging company to harvest trees on the property (Tr. p. 82).

21. Petitioners began planting tree seedlings on the property in 1997 (Tr. pp. 36-37). Petitioners planted various types of seedlings in the springtime that they obtained from various sources (Tr. pp. 27-29). Petitioners did not have a plan for planting or harvesting certain types of trees (Tr. pp. 61-62). Petitioner Michael Bliss testified that he planted "any trees I could get my hands on" (Tr. p. 17).

22. Petitioners estimate that they planted approximately 500 to 1,000 seedlings in the spring each year, but do not know how many trees were planted

during the period under review (Tr. p. 29). Petitioners have no written records of the amount or type of trees planted (Tr. p. 29).

23. Petitioners were only able to work on the property during weekends and on one full week of vacation from General Motors each year (Tr. pp. 26-27, 48-49).

24. Petitioners maintained no books of account for the tree farm business (Tr. p. 78). There were no journals or ledger accounts (Tr. p. 78). Petitioners saved receipts for their expenses and gave those receipts to their tax preparer (Tr. p. 78).

25. Petitioners claimed depreciation deductions for farm expenditures for the period under review (Exhibits 6, 7, and 8). The items depreciated and their purchase price included the following (Exhibit 14):

a. A camper placed on the property in 1996 and used until a new mobile home was purchased for $8,500.[1]

b. Installation of utilities for the camper in 1999 for $18,493.

c. A 12'x33' mobile home placed on the property in 1999, along with an attached deck, for $25,000.

d. A trailer and 3 all terrain vehicles (ATVs) purchased in 1995 for $25,000.

e. A generator for power purchased in 1996 for $2,500.

f. A log splitter purchased in 1998 for $1,249.

g. A lawn mower purchased in 1998 for $750.

h. A chain saw purchased in 1998 for $739.

[1] This camper was traded by petitioners in 1999, but they continued to deduct a depreciation expense for this item during the entire period under review.

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i. Welders purchased in 2000 for $2,269.

j. A cut-off saw purchased in 2000 for $2,074.

26. Petitioners also deducted mileage expense for farming on the property (Exhibits 6, 7, and 8). Petitioners kept no contemporary mileage log (Tr. p. 76). They simply computed the mileage from their home in Janesville, Wisconsin, to the property and back for each weekend during the year (Tr. pp. 76-77).

27. Petitioners deducted corn and seed used to feed deer as an expense of farming the property for each year during the period under review (Tr. pp. 73-74).

28. Petitioners also deducted the cost of mortgage interest, repairs and maintenance, utilities, property taxes, and small tools as farming expenses of the property during the period under review (Exhibits 6, 7, and 8).

29. Petitioners reported the following non-farm income, farm income, farm expenses, and farm loss as stated on their tax returns (Exhibits 6, 7, and 8):

Year	Non-farm income	Farm income[2]	Farm expenses	Farm loss
1998	$111,597	$511	$21,236	$20,725
1999	122,016	511	32,646	32,135
2000	128,054	511	33,252	32,741

CONCLUSION OF LAW

Petitioners have failed to present clear and satisfactory evidence that the respondent erred in determining that, during the period under review, petitioners did not operate their tree farm for profit within the intent and meaning of § 183 of the

[2] This income was annual rent payments for participation in the CRP and had nothing to do with tree farming.

Internal Revenue Code, and that the expenses claimed for operation of the tree farm are not deductible from income.

OPINION

Standard of Review

Under Wisconsin law, tax exemptions, deductions, and privileges are a matter of legislative grace and are to be strictly construed against the granting of the same. *Fall River Canning Co. v. Dep't of Taxation*, 3 Wis. 2d 632, 637, 89 N.W.2d 203 (1958). Furthermore, assessments made by the respondent are presumed to be correct, and the burden is upon the petitioner to prove by clear and satisfactory evidence in what respects the Department erred in its determination. *Edwin J. Puissant, Jr. v. Dep't of Revenue,* Wis. Tax Rptr. (CCH) ¶202-401 (WTAC 1984).

Trade or Business

Petitioners have claimed that they are operating the business of a tree farm, and that they should be allowed to deduct the expenses of the tree farm. Respondent's assessment against petitioners is based upon respondent's denial of petitioners' deductions of expenses claimed in connection with the property in question.

Under § 162 of the Internal Revenue Code (I.R.C.), all "ordinary and necessary" expenses paid or incurred in carrying on a "trade or business" during the taxable year are deductible by individuals. I.R.C. § 183 provides that if an individual is not engaged in the activity for profit, only limited deductions attributable to that

activity are allowed.[3]

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Factors for determination of "activity not engaged in for profit"

Since there is no presumption that petitioners' tree farming was a trade or business engaged in for profit, Treas. Reg. § 1.183-2(b) provides that in determining whether or not an activity is engaged in for profit, "all facts and circumstances with respect to the activity are to be taken into account. No one factor is determinative in making this determination." The Regulation lists the following nine factors to consider in making this determination: (1) *The manner in which the taxpayer carries on the activity*; (2) *The expertise of the taxpayer or his advisors*; (3) *The time and effort expended by the taxpayer in carrying on the activity*; (4) *The expectation that assets used in the activity may appreciate in value*; (5) *The success of the taxpayer in carrying on similar or dissimilar activities*; (6) *The taxpayer's history of income or losses with respect to the activity*; (7) *The amount of occasional profits, if any, which are earned*; (8) *The financial status of the taxpayer*; and (9) *Any elements of personal pleasure or recreation*. Each factor is discussed individually below.

1. The Manner in Which the Taxpayers Conducted the Activity

Maintaining complete and accurate books and records, conducting the activity in a manner substantially similar to comparable businesses which are profitable, and making changes in operations to adopt new techniques or abandon unprofitable

[3]I.R.C. § 183(d) establishes presumptions to help define an "activity not engaged in for profit". One of the presumptions is that "if the gross income derived from an activity for 3 or more of the taxable years in the period of 5 consecutive taxable years which ends with the taxable year exceeds the deductions attributable to such activity", then the activity is engaged in for profit. The case currently before the Commission cannot qualify as an activity engaged in for profit under this presumption. During all 3 years here under review - 1998 to 2000 - petitioners sustained substantial farming losses. They have also continued to sustain such losses up to the date of the hearing in this matter since they have yet to harvest or sell any trees on the property. The presumption of the I.R.C. that their farming activity was engaged in for profit is not applicable here. *Also see* Treas. Reg. § 1.183-1(c).

methods suggest that a taxpayer conducted an activity for profit. Treas. Reg. § 1.183-2(b)(1). There is no evidence in this case of a business plan. Petitioners wanted to sell trees at some time in the future to supplement their retirement income. However, the fact that petitioners planted trees without keeping records of the number planted, and that they had no specific plan for operating a profitable tree farm, shows that they did not have a business plan.

Petitioners kept no books or records for the tree farm. The only records kept were of the income received from the CRP and receipts for expenses. These records do not establish any profit potential for the tree farm.

Petitioners also had no information as to what sales of trees they expected or what profit might be realized from such future sales. There is no evidence in the record to show that the future sale of trees will enable petitioners to realize a net profit.

Moreover, petitioners placed over one-half of the property in government programs that would restrict their ability to log the property. The property in the CRP could not be logged, and the property in the Plan could only be logged with permission of the DNR.

Petitioners also failed to show that they made any changes in their operation of the tree farm to improve profit potential.

2. The Expertise of the Taxpayers or Their Advisors

Efforts to gain experience, a willingness to follow expert advice, and preparation for an activity by extensive study of its practices may indicate that a taxpayer has a profit objective. Treas. Reg. § 1.183-2(b)(2). A taxpayer's failure to obtain expertise in the economics of an activity indicates that he or she lacks a profit

objective. *See Burger v. Commissioner*, 87-1 USTC ¶ 9137, 809 F.2d 355, 359 (7th Cir. 1987), affg. T.C. Memo. 1985-523 [Dec. 42,428(M)].

Petitioners had no experience in tree farming. They did no research about tree farming methods, types or profitability either before or after purchasing the property. They did not consult with any experts or subscribe to any trade publications to learn how to run a tree farm.

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3. Taxpayers' Time and Effort

The fact that a taxpayer devotes much time and effort to an activity may indicate that he or she has a profit objective. Treas. Reg. § 1.183-2(b)(3).

Petitioners maintained their full-time jobs during the period under review, and could only work on the tree farm business on weekends and on one week of vacation a year. However, some of that time was not spent directly on the business of tree farming. Petitioners improved the property with a residential trailer, a deck, water for the residence, electricity, and a septic tank. Petitioners argued that this was necessary because they lived too far away from the tree farm to commute. While this is true, these activities are not directly related to the business of tree farming and do not alter the fact that petitioners maintained full-time employment elsewhere.

4. Expectation That Assets Used in the Activity Will Appreciate in Value

A taxpayer may intend to make an overall profit when appreciation in the value of assets used in the activity is realized. Treas. Reg. § 1.183-2(b)(4).

Petitioners did plant trees during the period under review, and they expect that these trees may be logged and sold for profit some day. However, petitioners did not track either the numbers or types of trees planted, nor did they

know the profitability of the trees that they planted. They had no way of knowing if the overall profit of tree farming would exceed the claimed expenses of the property.

5. Taxpayers' Success in Other Activities

The fact that a taxpayer previously engaged in similar activities and made them profitable may show that the taxpayer has a profit objective. Treas. Reg. § 1.183-2(b)(5). Since petitioners had no prior experience with tree farming, there is no history to indicate their ability to profitably operate a tree farm.

6. Taxpayers' History of Income or Losses

A history of substantial losses may indicate that the taxpayer did not conduct the activity for profit. However, a series of losses during the initial or start-up stage of an activity may not necessarily be an indication that the activity is not engaged in for profit. Treas. Reg. § 1.183-2(b)(6). Petitioners contend that it will take several years before trees can be harvested on the property because it had been logged prior to their purchase of it. Since petitioners' losses in the tree farm were incurred within the first 5 years of owning the property, the losses are not necessarily an indication that the tree farm was not conducted for profit. However, petitioners lack any business plan or projections of when they expect the property to make a profit in the future. This absence of any plan or profit projection combined with substantial losses each year tends to indicate a lack of intention to operate a profitable tree farm.

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7. Amount of Occasional Profits, If Any

The amount of any occasional profits the taxpayer earned from the activity may show that the taxpayer had a profit objective. Treas. Reg. § 1.183-2(b)(7). Petitioners have had no occasional profits from tree farming because no trees have been

logged on the property at all.[4]

8. Financial Status of the Taxpayer

The receipt of a substantial amount of income from sources other than the activity, especially if the losses from the activity generate large tax benefits, may indicate that the taxpayer does not intend to conduct the activity for profit, particularly if there are personal or recreational elements involved. Treas. Reg. § 1.183-2(b)(8). Petitioners were employed full-time during the period under review and did not rely on tree farming for income. The fact that they earned income from other sources indicates that the tree farming was not for profit when petitioners claimed substantial deductions for tree farming. In addition, there were elements of personal pleasure in owning the property, as addressed below.

9. Elements of Personal Pleasure

The presence of recreational or personal motives in conducting an activity may indicate that the taxpayer is not conducting the activity for profit. Treas. Reg. § 1.183-2(b)(9).

There are elements of personal pleasure for petitioners in owning the property. They wanted a place to get away from people on weekends, and this wooded property has become that place. It is a weekend residence with a mobile home, attached deck, and all necessary utilities. This is also a place for petitioners to observe wildlife, hunt, and drive their ATVs. The property has been appropriate for this purpose. 8.9 acres of the property are in the CRP, upon which trees cannot be planted,

[4] The only income from the property has been the small amount of rental payments received from the CRP. The CRP rental payments are for maintaining a refuge for wildlife and have nothing to do with tree farming.

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in order to preserve a place for wildlife. Another 80 acres of the property is in the Plan with the DNR of Wisconsin and can only be logged with the permission of the DNR.

After reviewing these factors along with the testimony and other evidence in this case, we conclude that petitioners' activities on the property during the period under review constituted an "activity not engaged in for profit." Petitioner Michael Bliss intends to eventually log some trees on the property after he retires, as necessary, to insure adequate income for maintaining a home in Wisconsin and the ability to spend time in a southern state each winter. While this eventual activity may become a trade or business for profit at some time in the future, it is not one at this time. The evidence shows that the primary intent on the part of petitioners was to purchase a wooded parcel of land where they would be secluded from other people and could hunt and observe wildlife.

Petitioners' Case Law

Department of Revenue v. Hausmann

Petitioners cite *Department of Revenue v. Hausmann*, 148 Wis. 2d 945, 437 N.W.2d 234, 1988 WL 148284 (Ct. App. 1988, unpublished opinion) in support of their argument that their activities on the property constituted a tree farm business engaged in for profit. That case affirmed the Commission's decision regarding a practicing physician who also operated a tree farm at a loss during the audit period. The Commission had found that the tree farm was operated for profit, and the claimed business loss deductions associated with the tree farm were allowed. *Hausmann v. Dep't of Revenue*, Wis. Tax Rptr. (CCH) ¶ 202-713 (WTAC 1986), aff'd *Hausmann v. Dep't of Revenue*, Wis. Tax Rptr. (CCH) ¶ 202-893 (Waukesha Co. Cir. Ct. 1987), aff'd *Department*

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of Revenue v. Hausmann, 148 Wis. 2d 945, 437 N.W.2d 234, 1988 WL 148284 (Ct. App. 1988, unpublished opinion).

Hausmann is distinguishable from the present case. The taxpayer in *Hausmann* sought advice from experts on tree farming, he subscribed to periodicals about tree farming, he joined tree farming organizations, and he purchased machinery used exclusively for tree farming. *Hausmann* at 12,920-12,921 There was expert testimony in *Hausmann* indicating that the taxpayer exercised "intensive management" over the property, with the intent of making a profit. *Hausmann* at 12,921. Moreover, there was no finding of any personal or recreational use from tree farming in *Hausmann.*

In the instant case, petitioners did not operate their tree farm in a similarly businesslike manner. Each of the I.R.C. § 183 factors tend to show that their tree farm was not operated for profit and, therefore, was not a trade or business within the meaning of I.R.C. § 162. In view of the foregoing, petitioners have failed to meet their burden in this case, and respondent's assessment is therefore upheld.[5]

IT IS ORDERED

That respondent's action on petitioners' petition for redetermination is affirmed.

[5] Our conclusion that petitioners were not engaged in tree farming for profit during the period under review obviates the need to address respondent's argument that the claimed expenses were not "ordinary and necessary" expenses or that petitioners failed to substantiate those expenses as required by I.R.C. § 162.

Dated at Madison, Wisconsin, this 17th day of November, 2005.

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WISCONSIN TAX APPEALS COMMISSION

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Jennifer E. Nashold, Chairperson

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Diane E. Norman, Commissioner

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David C. Swanson, Commissioner

ATTACHMENT: **"NOTICE OF APPEAL INFORMATION"**