

WISCONSIN TAX BULLETIN

July 1986
NUMBER 47

Subscription available from:

Wisconsin Department of
Administration
Document Sales
P.O. Box 7840
Madison, WI 53707
Annual Cost - \$5.00 (plus sales tax)

CORPORATIONS: FOURTH QUARTER ESTIMATES DUE EARLIER

A corporation must make installment payments of estimated tax if it can expect to have a tax liability for the year of over \$500. Installment payments for 1986 taxable years are due on the fifteenth day of the third month, sixth month, ninth month and twelfth month of the taxable year (under prior law, the fourth quarter installment payment was not due until the fifteenth day of the first month after the close of the taxable year).

If a required installment is not paid by its due date, an addition to the tax may be assessed on the amount of the underpayment for the period of the underpayment. In determining the underpayment for 1986, the percentage of tax that is required to be prepaid is 90% of the net tax liability shown on the return.

Corporations should keep in mind the change in Wisconsin law (1983 Wisconsin Act 27) concerning exceptions 1 and 2 (s. 71.22(10)(a) and (b), Stats.) to avoid the addition to the tax. Beginning with 1984 taxable years, corporations with Wisconsin net income of \$250,000 or more are no longer eligible for these exceptions. These exceptions continue to apply to corporations with less than \$250,000 of net income.

Corporations' installment payments of estimated tax are reported on Form 4-ES, the Wisconsin Corporation Declaration Voucher. Corporations who received a preprinted Form 4-ES in the mail are urged to file on that form rather than on a facsimile, since the

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preprinted forms are color coded and are less costly and faster to process.

NEW WISCONSIN TAX LAWS

The Wisconsin Legislature enacted several changes to the Wisconsin tax laws during March and April 1986. The following are brief descriptions of the major income, corporation franchise/income, sales/use, inheritance and excise tax provisions. The description for each item indicates the act number, the sections of the statutes

affected and the effective date of the provision.

INCOME TAXES

1. Update Reference to Internal Revenue Code for Individuals, Trusts, Estates and Tax-Option Corporations (1985 Wisconsin Act 261, amend s. 71.02(2)(d)12, create s. 71.05(1)(km), and 1985 Wisconsin Act 153, create s. 71.02(3), effective for the 1986 taxable year and thereafter.)

For the 1986 taxable year and thereafter, individuals, trusts, estates and tax-option corporations will use the Internal Revenue Code in effect on December 31, 1985, with the following exceptions.

a. The depreciation deduction and gain or loss on the sale or other disposition of the following depreciable property placed in service by the taxpayer during the 1986 taxable year and thereafter must be computed under the Internal Revenue Code in effect on December 31, 1980:

(1) Residential real property.

(2) Property used in farming, as defined in Section 464(e)(1) of the Internal Revenue Code, if (a) the taxpayer's nonfarm Wisconsin adjusted gross income exceeds \$55,000, or exceeds \$27,500 for a married person filing separately, or (b) the gross farm profit exceeds \$155,000, or exceeds \$77,500 for a married person filing separately.

b. Taxable unemployment compensation benefits must be determined using the provisions of the Internal Revenue Code for the current year.

c. At the taxpayer's option, "internal revenue code" for the 1986 taxable year and thereafter includes any revisions to the federal Internal Revenue Code adopted after January 1, 1986 that relate to the taxation of income derived from any source as a direct consequence of participation in the milk production termination program created by Section 101 of Public Law 99-198.

d. Certain entertainment and travel expenses allowable under Section 162, 212 or 274 of the Internal Revenue Code may not be claimed for Wisconsin.

e. Certain farm losses allowable for federal tax purposes may not be deductible for Wisconsin tax purposes. (See Item 3.)

f. Railroad retirement benefits continue to be nontaxable for Wisconsin.

g. Sick pay benefits paid under the Railroad Unemployment Insurance Act continue to be nontaxable for Wisconsin.

h. The deduction from gross income allowed two-earner married couples does not apply for Wisconsin.

i. The charitable contributions deduction allowed to persons who do not claim itemized deductions does not apply for Wisconsin.

j. The disability income exclusion of up to \$5,200 which was allowed to persons under age 65 who retired on disability and received disability income while permanently and totally disabled, as provided under Section 105(d) of the Internal Revenue Code immediately prior to its repeal in 1983 by Public Law 98-21, continues to apply for Wisconsin.

k. For tax-option corporations, the Internal Revenue Code applies only to the election and termination of Subchapter S status and not to the computation of net income, etc.

2. Define Basis of Assets Acquired Before Becoming a Wisconsin Resident (1985 Wisconsin Act 261, create s. 71.05(1)(m), (n) and (o), effective for the 1986 taxable year and thereafter as well as retroactively to the earliest taxable year in which

additional assessments or refunds may be made on April 30, 1986.)

Except in the case of a principal residence, the Wisconsin basis of an asset owned by an individual, estate or trust and acquired before the individual became a resident of Wisconsin or before the estate or trust became subject to Wisconsin taxation is the federal adjusted basis.

Whenever an individual acquires a new residence, as defined in Section 1034(a) of the Internal Revenue Code, in Wisconsin, the adjusted basis of the new residence is not required to be reduced by the amount of deferred gain on the sale or exchange of an old residence located outside Wisconsin (as provided by Sections 1016(a)(7) and 1034(e) of the Internal Revenue Code) if

a. The sale or exchange of the old residence occurred in taxable year 1975 or thereafter and the individual was not a Wisconsin resident at the time of the sale or exchange, or

b. The sale or exchange of the old residence occurred before taxable year 1975.

Example: Taxpayer A, a Minnesota resident, sold his Minnesota residence for \$75,000 on March 1, 1985. He realized a \$30,000 gain on the sale. On September 1, 1985, Taxpayer A became a Wisconsin resident. Also on that date, he purchased a Wisconsin residence for \$100,000. For federal tax purposes, the basis of his Wisconsin residence is \$70,000 (\$100,000 cost minus \$30,000 deferred gain on the sale of the Minnesota residence). For Wisconsin tax purposes, the basis of his Wisconsin residence is \$100,000.

Example: On January 1, 1986, Taxpayer B became a Wisconsin resident. She purchased a Wisconsin residence on January 31, 1986 for \$200,000. On April 1, 1986, Taxpayer B sold her California residence #2 for \$100,000. The federal adjusted basis of her California residence #2 was \$60,000 (\$75,000 cost minus \$15,000 deferred gain on the sale of her prior California residence #1). Taxpayer B thus realized a \$40,000 gain for federal tax purposes on the sale of California residence #2. The federal adjusted basis of her Wisconsin residence is

\$160,000 (\$200,000 cost minus \$40,000 deferred gain on the sale of California residence #2). For Wisconsin tax purposes, the basis of Taxpayer B's Wisconsin residence is \$175,000 (\$200,000 cost minus \$25,000 deferred gain realized on the sale of her California residence while Taxpayer B was a Wisconsin resident). The Wisconsin basis is not reduced by the \$15,000 deferred gain from the earlier sale of California residence #1 while Taxpayer B was a nonresident.

Example: Taxpayer C became a Wisconsin resident and purchased a Wisconsin residence for \$50,000 on July 1, 1974. On September 1, 1974, Taxpayer C sold her Illinois residence for \$45,000 and realized a \$7,500 gain. For federal purposes, the basis of her Wisconsin residence is \$42,500 (\$50,000 cost minus \$7,500 deferred gain on the sale of her Illinois residence). For Wisconsin tax purposes, the basis of her Wisconsin residence is \$50,000.

Whenever a Wisconsin resident sells or exchanges a principal residence located outside Wisconsin and the nonrecognition of gain provision of Section 1034(a) of the Internal Revenue Code does not apply to the sale or exchange, the adjusted basis of the residence sold or exchanged is not required to be reduced for any nonrecognized gain on the sale or exchange of any old principal residence located outside Wisconsin if

a. The sale or exchange of the old residence occurred in taxable year 1975 or thereafter and the individual was not a Wisconsin resident at the time of the sale or exchange, or

b. The sale or exchange of the old residence occurred before taxable year 1975.

Example: Taxpayer D, who was 30 years old, became a Wisconsin resident on February 1, 1986. On May 1, 1986, Taxpayer D sold her Illinois residence for \$80,000. The Illinois residence was her first residence and had a federal basis (cost) of \$50,000. Taxpayer D did not purchase a replacement residence. Taxpayer D is subject to Wisconsin income tax on the \$30,000 gain she realized on the sale.

Example: Taxpayer E, who was 50 years old, became a Wisconsin resident on June 1, 1985. On October 1, 1985, Taxpayer E sold his New York residence for \$250,000. His New York residence had a federal basis of \$85,000, which was computed as follows: \$150,000 cost minus \$65,000 deferred gain on the sale of a prior New York residence. For federal tax purposes, Taxpayer E realized a \$165,000 gain on the sale. For Wisconsin purposes, the basis of the New York residence is its \$150,000 cost; the Wisconsin basis is not reduced by the deferred gain on the sale of the first New York residence. Taxpayer E has a taxable gain of \$100,000 for Wisconsin income tax purposes.

3. Provide Limit on Deduction for Certain Farm Losses Incurred by Married Persons Who File Separate Returns (1985 Wisconsin Act 261, amend s. 71.05(1)(a) 26, effective for the 1986 taxable year and thereafter.)

Beginning with the 1986 taxable year, combined net losses, exclusive of net gains, from businesses, rents, partnerships, S corporations, estates or trusts incurred in the operation of a farming business, as defined in Section 464(e)1 of the Internal Revenue Code, otherwise includable in calculating Wisconsin income, which can be used to offset nonfarm income are limited. The amounts applicable to married persons filing separate returns are 50% of the amounts applicable to other persons.

4. Amend Itemized Deductions Credit (1985 Wisconsin Act 153, amend s. 71.09(6r)(a), and 1985 Wisconsin Act 261, amend s. 71.09(6r)(a), effective for the 1986 taxable year and thereafter.)

a. For purposes of the itemized deductions credit, interest expense which is not subject to the \$1,200 cap includes interest allowed as an itemized deduction under Section 163 of the Internal Revenue Code and paid to acquire agricultural property, other than a residence, if that property was personally operated or leased as farmland by the taxpayer during the period of ownership and is subsequently sold by the taxpayer on a land contract, to a buyer who agrees, in writing, to continue to personally operate the property as farmland over the term of

the contract, for which interest income is reported by the taxpayer.

Agricultural property is defined in s. 93.50(1) and means real property that is used principally for farming, real property that is a farmer's principal residence and any land contiguous to the residence, personal property that is used as security to finance farming or personal property that is used for farming.

b. For married persons filing separate returns, the limit on interest which is allowed as an itemized deduction under Section 163 of the Internal Revenue Code, but which is subject to the cap, is \$600 instead of \$1,200.

5. Provide Limit on One-Time Property Tax and Rent Credit for Married Persons Filing Separate Returns (1985 Wisconsin Act 261, amend s. 71.54, effective for the 1986 taxable year.)

For the 1986 taxable year, a one-time credit equal to 7.9% of property taxes or rent constituting property taxes may be claimed. For married persons filing separate returns, the credit is allowed for up to \$1,000 of property taxes and rent constituting property taxes, instead of \$2,000 of property taxes and rent constituting property taxes.

6. Permit Married Persons to Compute Their Section 179 Deduction Based on the Amount Allowable on a Joint Federal Return (1985 Wisconsin Act 261, nonstatutory provision, effective for taxable years 1982 to 1985.)

For taxable years 1982 to 1985, married persons electing the expensing provisions of Section 179 of the Internal Revenue Code may compute the amount of deduction allowable on the same basis as married persons filing a joint federal return. The total amount of the deduction may be divided between spouses in any manner they choose.

**CORPORATION
FRANCHISE/INCOME TAXES**

1. Impose Franchise Tax on Corporations That Cease Doing Business in Wisconsin (1985 Wisconsin Act

261, amend s. 71.01(2), effective for the 1986 taxable year and thereafter.)

This provision imposes a special franchise tax on corporations that cease doing business in Wisconsin. The tax is measured by the corporation's entire net income for the taxable year during which the corporation ceases doing business in Wisconsin.

Under prior law, a franchise tax was imposed on corporations for the privilege of doing business in Wisconsin during the year the tax return was due. The tax was measured by the corporation's entire net income for the previous taxable year. Thus, when a corporation ceased doing business in Wisconsin, its income for the year of cessation was not subject to franchise tax. Instead, an income tax was imposed on the net income from the final year of operation in Wisconsin.

2. Update Reference to Internal Revenue Code for Insurance Companies (1985 Wisconsin Act 261, amend s. 71.01(4)(g)9, create s. 71.01(4)(g)10, effective for the 1986 taxable year and thereafter.)

For the 1986 taxable year and thereafter, insurance companies will compute their income under the Internal Revenue Code in effect on December 31, 1985, with certain exceptions.

a. The depreciation deduction and gain or loss on the sale or other disposition of the following depreciable property acquired in the 1986 taxable year or thereafter by a corporation must be computed under the Internal Revenue Code in effect on December 31, 1980:

(1) Residential real property.

(2) Property used in farming, as defined in Section 464(e)(1) of the Internal Revenue Code, if the taxpayer's Wisconsin gross farm receipts or sales exceed \$155,000 for taxable year 1986.

b. The special rules for safe harbor leases provided by Section 168(f)(8) of the Internal Revenue Code may not be used for Wisconsin.

c. Depreciation on out-of-state property placed in service by the taxpayer on or after January 1, 1983 must be

computed under the Internal Revenue Code in effect on December 31, 1980.

d. Certain entertainment, gift and travel expenses allowable under Section 162, 212 or 274 of the Internal Revenue Code may not be claimed for Wisconsin.

3. Update Reference to Internal Revenue Code for Regulated Investment Companies and Real Estate Investment Trusts (1985 Wisconsin Act 261, amend s. 71.02(1)(c)10, create s. 71.02(1)(c)11, effective for the 1986 taxable year and thereafter.)

For the 1986 taxable year and thereafter, regulated investment companies and real estate investment trusts will compute their income under the Internal Revenue Code in effect on December 31, 1985, with certain exceptions.

a. The depreciation deduction and gain or loss on the sale or other disposition of the following depreciable property acquired in the 1986 taxable year or thereafter by a corporation must be computed under the Internal Revenue Code in effect on December 31, 1980:

(1) Residential real property.

(2) Property used in farming, as defined in Section 464(e)(1) of the Internal Revenue Code, if the taxpayer's Wisconsin gross farm receipts or sales exceed \$155,000 for taxable year 1986.

b. The special rules for safe harbor leases provided by Section 168(f) (8) of the Internal Revenue Code may not be used for Wisconsin.

c. Depreciation on out-of-state property placed in service by the taxpayer on or after January 1, 1983 must be computed under the Internal Revenue Code in effect on December 31, 1980.

4. Amend Definition of Internal Revenue Code (1985 Wisconsin Act 153, create s. 71.02(3), effective for the 1986 taxable year and thereafter.)

For corporations, at the taxpayer's option, "internal revenue code" for the 1986 taxable year and thereafter includes any revisions to the federal Internal Revenue Code adopted after January 1, 1986 that relate to the taxation of income derived from any

source as a direct consequence of participation in the milk production termination program created by Section 101 of Public Law 99-198.

5. Clarify That Corporations Cannot Receive Both a Credit and a Deduction on Their Franchise or Income Tax Returns for Expenditures for Research or Research Facilities (1985 Wisconsin Act 261, repeal s. 71.04(2)(b)5, create s. 71.03(1)(j), effective for the 1986 taxable year and thereafter.)

To ensure that corporations cannot claim both a deduction and a tax credit for the same expenses, these provisions clarify that research expenses equal to the amount of any research credit or research facility credit computed under s. 71.09(12r) or (12rf) are not deductible.

Under prior law, s. 71.04(2)(b)5 required corporations claiming a tax credit for increasing research spending or investing in Wisconsin research facilities to adjust deductions by the amount of these credits.

6. Provide Consistent Tax Treatment of Incentive Stock Options (1985 Wisconsin Act 261, amend 1985 Wisconsin Act 29, Section 3203(46)(g)2 and Section 3204 (46)(c), create 1985 Wisconsin Act 29, Section 3203(46)(g)4, effective for the 1985 or 1986 taxable year and thereafter.)

Under provisions included in 1985 Wisconsin Act 29 the state adopted, effective with the 1986 taxable year, the federal income tax treatment of incentive stock options. As a result, individuals are not taxed on the difference between the option price and the market value of the stock when the option is exercised. Corporations are not permitted to deduct this amount as employee compensation [s. 71.04(1) and (2)(b)10].

This amendment makes technical changes to the initial applicability provisions in 1985 Wisconsin Act 29. It provides that the treatment of s. 71.04(1) and (2)(b)10 first applies to taxable year 1985 or 1986, as appropriate, to conform the treatment with that of the person exercising the option as required under s. 71.02(2)(d)11 or 12. Thus, if an employee is taxed at

the time of exercise, the corporation is allowed a deduction. If the employee is not taxed, the corporation is not allowed a deduction.

7. Update Reference to Internal Revenue Code for Incentive Stock Option Provisions (1985 Wisconsin Act 261, amend s. 71.04(1) and (2)(b)10, effective for the 1986 taxable year and thereafter.)

Corporations may not deduct the value of incentive stock options as defined in Section 422A of the Internal Revenue Code as amended to December 31, 1985.

8. Provide That Drop Shipment Sales Are Attributable to Wisconsin (1985 Wisconsin Act 261, amend s. 71.07 (2)(c)2m, effective for the 1986 taxable year and thereafter.)

Under prior law, sales of tangible personal property were included in the sales factor of the corporate apportionment formula of a corporation doing business in Wisconsin if the sales were made by or through the corporation's Wisconsin sales office to a purchaser in another state which did not have jurisdiction to tax the seller, if the property was shipped by a third party to the purchaser, and if the state from which the property was shipped also did not have jurisdiction to tax the seller. These sales are often referred to as drop shipment sales.

This amendment provides that drop shipment sales are attributable to Wisconsin and thus includable in the apportionment formula no matter who ships or delivers the property, if the other conditions are met.

SALES/USE TAXES

1. Clarify Exemption for Mobile Home Rental (1985 Wisconsin Act 149, amend s. 77.52(2)(a)1, create s. 77.54(33), effective July 1, 1986.)

Prior law provided a sales tax exemption for certain mobile home rentals. This amendment clarifies that the rental of a mobile home which is used as a residence for a continuous period of one month or more is exempt from sales tax, regardless of whether the mobile home is classified as real or personal property.

2. Provide Exemption for Manufacturing Machinery Safety Attachments (1985 Wisconsin Act 149, amend s. 77.54(6)(a), effective June 1, 1986.)

Prior law provided a sales tax exemption for safety attachments sold as part of the original manufacturing machinery. This amendment extends the sales tax exemption to new safety attachments added to manufacturing machinery and equipment.

3. Clarify Exemption for Local Government Agencies (1985 Wisconsin Act 149, amend s. 77.54(9a)(e), effective June 1, 1986.)

Prior law provided a sales tax exemption for any unit of government or any agency of 2 or more units of government. This amendment provides an exemption for any agency of any unit of government, not just an agency of 2 or more units.

4. Clarify Exemption for Controlled Circulation Publications (1985 Wisconsin Act 149, amend s. 77.54(15), effective September 1, 1983.)

Prior law provided a sales tax exemption for periodicals sold to publishers for distribution without charge. This provision clarifies that the exemption applies only to sales by a printer of a controlled circulation publication to the commercial publisher of the publication. The amendment defines "controlled circulation publication" as a publication that has at least 24 pages, is issued at regular intervals not exceeding 3 months, that devotes not more than 75% of its pages to advertising and that is not conducted as an auxiliary to, and essentially for the advancement of, the main business or calling of the person that owns and controls it.

5. Provide Exemption for Peat and Fuel Cubes for Residential Use (1985 Wisconsin Act 149, amend s. 77.54(30)(a)1 and (f), effective April 2, 1986.)

This amendment provides a sales tax exemption for fuel cubes produced from solid waste, such as paper and cardboard, and for peat sold to a residential user for fuel. Prior law provided a sales tax exemption for coal, fuel

oil, propane, steam and wood used for residential fuel.

6. Clarify Exemption for Copying Public Records (1985 Wisconsin Act 149, amend s. 77.54(32), effective April 2, 1986.)

Prior law provided a sales tax exemption for copying public records. This provision clarifies that the sales tax exemption applies to charges incurred for copies of confidential records of an authority, such as a state agency.

A nonstatutory provision states that any person who on April 2, 1986 has a liability for sales taxes on charges for copying records under s. 19.35(1) is absolved of that liability. No refunds may be made of sales taxes paid before April 2, 1986 in respect to those charges.

7. Alert Taxpayers to Venue for Sales Tax Cases (1985 Wisconsin Act 149, amend s. 227.16(1)(a), effective April 2, 1986.)

This bill adds a cross reference to the statutes to alert taxpayers that the venue for review of sales tax decisions by the Tax Appeals Commission is in Dane County Circuit Court.

8. Provide Sales Tax Refunds for Defective Motor Vehicles Returned to the Manufacturer (1985 Wisconsin Act 205, amend s. 218.015(2)(b), create s. 218.015(2)(e), effective for motor vehicles for which the contract to purchase is entered into on or after April 22, 1986.)

If a motor vehicle, which is covered by a warranty, has a defect which after a reasonable attempt to repair is not repaired, the consumer may return the motor vehicle to the manufacturer, and the manufacturer shall refund the purchase price plus sales tax, less a reasonable allowance for use. The Department of Revenue will refund to the manufacturer any sales tax which the manufacturer refunded to the consumer. The manufacturer must provide to the Department a written request for a refund along with evidence that the sales tax was paid when the motor vehicle was purchased and that the manufacturer refunded the sales tax to the consumer.

INHERITANCE AND GIFT TAXES

1. Update Reference to Internal Revenue Code for Power of Appointment, Qualified Retirement Plans and Installment Payments (1985 Wisconsin Act 261, amend ss. 72.01(17), 72.12(4)(c)1 and 72.22(4)(a), effective for transfers because of deaths on or after April 30, 1986.)

The references to the Internal Revenue Code relating to power of appointment (s. 72.01(17)), qualified retirement plans (s. 72.12(4)(c)1) and installment payments (s. 72.22(4)(a)) are updated to December 31, 1985.

2. Eliminate Requirement to File an Inheritance Tax Return if No Federal Estate Tax Return Is Required (1985 Wisconsin Act 278, renumber s. 72.30(1) to s. 72.30(1)(a) and amend s. 72.30(1)(a) as renumbered, amend ss. 72.30(1)(title), 72.30(3)(e), 72.33(1), 867.01(3)(e) and 867.02(2)(e), create s. 72.30(1)(b) and (3)(bm), effective for transfers because of deaths on or after April 30, 1986.)

No inheritance tax return is required to be filed if no federal estate tax return is required to be filed in regard to the transfer of property and if the inheritance tax exemptions that may be properly claimed clearly exceed the heir's or beneficiary's share of the estate.

Courts and probate registrars are required to accept as presumptive proof the determination of the distributive share and the applicable exemptions submitted on an inheritance tax report by the personal representative, special administrator, trustee, distributee or other interested person. The Department of Revenue and other interested parties may attempt to rebut that presumption.

EXCISE TAXES

1. Exempt Regular Leaded Gasoline Sold for Nonhighway Use From the Motor Fuel Tax (1985 Wisconsin Act 153, repeal s. 78.73(5), amend s. 78.73(1) (intro.), (d) and (e), create ss. 78.01(2)(e), 78.12(3m) and 78.73(1)(dm) and (f), effective July 1, 1986.)

Regular leaded gasoline sold for nonhighway use in mobile machinery