

paid to the state, or a receipt from a retailer with the tax separately stated. The department's assessment of use tax

against the taxpayer rather than the sales tax against the various vendors is permitted by law and is fair and proper.

The taxpayer has not appealed this decision.

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## TAX RELEASES

*("Tax Releases" are designed to provide answers to the specific tax questions covered, based on the facts indicated. However, the answer may not apply to all questions of a similar nature. In situations where the facts vary from those given herein, it is recommended that advice be sought from the Department. Unless otherwise indicated, Tax Releases apply for all periods open to adjustment. All references to section numbers are to the Wisconsin Statutes unless otherwise noted.)*

The following Tax Releases are included:

### Individual Income Taxes

1. Basis and Depreciation Allowable for Property Located Outside Wisconsin Acquired by an Individual Before Becoming a Wisconsin Resident (p. 10)
2. Holding Period for Public Utility Stock (p. 11)
3. Wisconsin Taxation of Partnership Income Received by Part-Year Residents (p. 12)
4. Gain or Loss on the Sale of a Partnership Interest by a Non-resident (p. 13)
5. Advance Payment of Real Estate Taxes (p. 13)

### Income and Franchise Taxes

1. Taxpayer Elections for Wisconsin Income and Franchise Taxes (p. 14)
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### Corporation Franchise/Income Taxes

1. Deductions for Waste Treatment Facility (p. 29)

## INDIVIDUAL INCOME TAXES

1. **Basis and Depreciation Allowable for Property Located Outside Wisconsin Acquired by an Individual Before Becoming a Wisconsin Resident**

Statutes: Sections 71.02(2)(c), (d) and (i) and 71.05(1)(m), 1985 Wis. Stats.

Wis. Adm. Code: Section Tax 2.30, July 1982 Register

Question: If a nonresident individual acquires and places in service depreciable property located outside Wisconsin, what is the Wisconsin basis and what depreciation method is allowable

for Wisconsin purposes when this individual becomes a Wisconsin resident?

### Answer:

- A. If Federal Basis and Federal Depreciation Are Determined in a Manner Allowable Under the Internal Revenue Code in Effect for Wisconsin

The Wisconsin basis of the property is the same as the federal basis, provided the federal basis was determined under the Internal Revenue Code in effect for Wisconsin for the taxable year in which the individual becomes a Wisconsin resident. Also, depreciation for Wisconsin purposes is the same as the federal depreciation, provided the federal depreciation method is allowable under the Internal Revenue Code in effect for Wisconsin for the taxable year in which the individual becomes a Wisconsin resident.

Example: Taxpayer A became a Wisconsin resident on January 1, 1985. Prior to that date, he had been an Illinois resident. On July 1, 1984, Taxpayer A had purchased and placed in service rental property located in Illinois. The cost of the property, not including the land, was \$200,000.

On his 1984 federal return, Taxpayer A claimed \$8,000 of depreciation on this rental property, computed using the 18-year ACRS recovery period. The federal adjusted basis of the property on January 1, 1985 is \$192,000 (\$200,000 cost - \$8,000 depreciation allowable). (The Tax Reform Act of 1984 provided that for real property placed in service after March 15, 1984, the ACRS recovery period was increased from 15 to 18 years.)

On his 1985 federal return, Taxpayer A claims \$18,000 of depreciation on this rental property.

Since Wisconsin has adopted the Internal Revenue Code as of December 31, 1984 for the 1985 taxable year, the Wisconsin basis of the property on January 1, 1985 is the same as the federal basis, \$192,000. To compute the depreciation allowable for Wisconsin for 1985, Taxpayer A uses the same basis and depreciation method that he is using for federal purposes. Thus, his 1985 Wisconsin depreciation is \$18,000, the same as his 1985 federal depreciation.

Note: For Wisconsin purposes, the taxpayer may elect to recompute both the basis and the depreciation using another method allowable under the Internal Revenue Code in effect for Wisconsin instead of using the federal basis and federal depreciation method. For instance, in the above example Taxpayer A may elect to use the alternate ACRS method for Wisconsin with an 18-year recovery period. Under this method, the 1984 deprecia-

tion would have been \$6,000. The adjusted basis of the rental property on January 1, 1985, the date Taxpayer A became a Wisconsin resident, would be \$194,000 (\$200,000 cost - \$6,000 depreciation allowable). On his 1985 Wisconsin return, Taxpayer A would claim \$12,000 of depreciation, instead of the \$18,000 allowable on his 1985 federal return.

**B. If Federal Basis and Federal Depreciation Are Determined in a Manner Not Allowable Under the Internal Revenue Code in Effect for Wisconsin**

If the federal basis and federal depreciation were computed in a manner not allowable under the Internal Revenue Code in effect for Wisconsin purposes for the taxable year in which the individual becomes a Wisconsin resident, both the basis and the depreciation must be recomputed under the Internal Revenue Code in effect for Wisconsin.

Example: Taxpayer B became a Wisconsin resident on December 1, 1984. Prior to that date, he had been an Illinois resident. On July 1, 1984, Taxpayer B had purchased and placed in service rental property located in Illinois. The cost of the property, not including the land, was \$200,000.

On his 1984 federal return, Taxpayer B claimed \$8,000 of depreciation on this property, computed using the 18-year ACRS recovery period. The federal adjusted basis of the property on January 1, 1985 is \$192,000 (\$200,000 cost - \$8,000 depreciation allowable). On his 1985 federal return, Taxpayer B claims \$18,000 of depreciation on this rental property.

Wisconsin had adopted the Internal Revenue Code as of December 31, 1983 for the 1984 taxable year, which provided that real property placed in service during 1984 has a 15-year ACRS recovery period. Therefore, Taxpayer B must recompute his depreciation for Wisconsin. Since he had placed the property in service during 1984 and depreciation is calculated only at the end of the taxable year, his federal adjusted basis as of December 1, 1984, computed under the December 31, 1983 Code, is \$200,000. The depreciation allowable under the December 31, 1983 Code is \$12,000. Since Taxpayer B was a Wisconsin resident for only one of the six months during which he owned the property in 1984, 1/6, or \$2,000, of the depreciation expense computed under the December 31, 1983 Code is allowable on his Wisconsin return.

For Wisconsin purposes, the adjusted basis of the property on January 1, 1985 is \$188,000 (\$200,000 adjusted basis on December 1, 1984 - \$12,000 depreciation allowable under the December 31, 1983 Code). For 1985, Taxpayer B's Wisconsin depreciation on this property is \$22,000.

**C. If Residential Real Property or Certain Property Used in Farming Is Placed in Service During 1986 or Thereafter**

For taxable year 1986 and subsequent years, Wisconsin law provides that for residential real property and for certain property used in farming, the depreciation deduction and gain or loss on disposition of such property must be computed under the Internal Revenue Code in effect on December 31, 1980. If such property is placed in service by the taxpayer during the taxable year 1986 or thereafter, but before the property is used in the production of income subject to Wisconsin taxation, the property's adjusted

basis and depreciation schedule aren't required to be changed from the amounts allowable on the owner's federal returns.

Example: Taxpayer C becomes a Wisconsin resident on January 1, 1987. Prior to that date, he is an Illinois resident. On July 1, 1986, Taxpayer C purchases and places in service residential real property located in Illinois. On his 1987 Wisconsin return, Taxpayer C's adjusted basis and depreciation on this property will be the same as the amounts shown on his 1987 federal return. He does not have to recompute the basis of the property and depreciate it using one of the methods permitted under the December 31, 1980 Code (such as the straight-line method or declining balance method).



**2. Holding Period for Public Utility Stock**

Statutes: Section 71.05(1)(a)12, 1983 Wis. Stats.

Note: This Tax Release applies only with respect to taxable years 1982 and thereafter.

Background: Internal Revenue Code Section 305(e) provides special tax treatment for taxable stock dividends issued by qualified public utilities. The special rule for public utility stock dividends distributed after 1981 and before 1986 in taxable years ending after 1981 allows a shareholder to elect to exclude from income up to \$750 per year (\$1,500 on a joint return) of the stock dividends received if he or she chooses a dividend of qualified common stock instead of cash or property. The shareholder elects the exclusion, with respect to any share, on his or her federal tax return for the tax year in which the dividend would otherwise have been included in income.

If the shareholder elects to exclude the dividend, the federal basis of the stock then becomes zero. Therefore, the full amount of sales proceeds would be taxable. Section 1222 of the Internal Revenue Code states that capital assets acquired after June 22, 1984 and before January 1, 1988, will be subject to capital gains treatment if held for 6 months or more. However, Section 305(e) requires that public utility stock, received as a dividend rather than cash or property, has a holding period of one year before capital gains treatment will apply.

For Wisconsin purposes, if a shareholder elects the exclusion available under Section 305(e) of the Internal Revenue Code, an add modification is required on the Wisconsin income tax return for the amount excluded on the federal return (s. 71.05(1)(a)12, Wis. Stats.).

Facts and Question: A Wisconsin resident received public utility stock dividends during 1984 and after June 22, 1984. For federal income tax purposes, this individual elected to use the provisions of Section 305(e) of the Internal Revenue Code and excluded these dividends from federal adjusted gross income for 1984. On the federal Form 1040 which was attached to the 1984 Wisconsin return filed by this individual, the public utility stock dividend was not included in federal adjusted gross income. On the 1984 Wisconsin return, the value of the public utility stock dividend

was entered as an addition to federal income as required by s. 71.05(1)(a)12, 1983 Wis. Stats.

During the 1985 taxable year (and before the stock was held for one year), the public utility stock received as a dividend after June 22, 1984 was sold. Because the stock was held for less than one year, for federal income tax purposes, the entire gain realized from the sale in 1985 must be treated as ordinary income. Is the holding period for receiving capital gain treatment on this stock for Wisconsin tax purposes 6 months under Section 1222 of the Internal Revenue Code or one year under Section 305(e) of the Internal Revenue Code?

**Answer:** The holding period for the stock sold is 6 months. Wisconsin does not follow federal tax treatment of public utility dividends and requires by s. 71.05(1)(a)12, Wis. Stats., that dividends reinvested in public utility stock be added back to Wisconsin taxable income in the year of receipt of the dividend. The result is that Wisconsin does not recognize Section 305(e) of the Internal Revenue Code for Wisconsin tax purposes. Therefore, the 6-month holding period applies as provided for by Section 1222 of the Internal Revenue Code.

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### 3. Wisconsin Taxation of Partnership Income Received by Part-Year Residents

**Statutes:** Section 71.07(1), 1985 Wis. Stats.

**Note:** See the Tax Release titled "Taxation of Partnership Income for Wisconsin Income Tax Purposes" in *Wisconsin Tax Bulletin* 41.

**Facts And Question:** A partnership is an association of two or more persons to carry on as co-owners of a business for profit. In a general partnership, all partners have equal rights in the management of the partnership business and may act on behalf of the partnership, and each partner can be held individually liable for obligations of the partnership. In a limited partnership, the activities of certain partners are limited, and the liabilities of these partners are limited to a stated amount. Wisconsin law requires one of the partners of a limited partnership to be a general partner with unlimited liability.

Under Internal Revenue Code Section 706(a), a partner must report his or her distributive share of partnership items or guaranteed payments in the partner's taxable year in which the partnership year ends.

How is partnership income taxed to part-year residents of Wisconsin?

**Answer:** For the portion of the partnership's taxable year the partner is a Wisconsin resident, the partner's share of all partnership income is taxable, regardless of the situs of the partnership or the nature of the partnership income, such as business income, service income or professional income, unless otherwise exempt (such as U.S. government interest). This applies both to general partners and to limited partners.

For the portion of the partnership's taxable year the partner is not a Wisconsin resident, the treatment depends on the situs of the partnership, the nature of the partnership income and the nature of the partner's interest in the partnership.

#### A. General Partners

That portion of the partnership income attributable to a business located in Wisconsin, services performed in Wisconsin, or rental property located in Wisconsin is taxable to nonresidents of Wisconsin. The income to be reported is based on the activities of the partnership and is not dependent upon whether or not the individual partner conducts business or performs services in Wisconsin. Section 71.07(1), 1985 Wis. Stats., provides that income or loss of nonresident individuals follows the situs of the business from which derived. Income from personal services of nonresidents, including income from professions, follows the situs of the services.

**Example 1.** An individual is a general partner, with a one-fifth interest in partnership profits, of a Certified Public Accounting Firm whose income is attributable one-fourth to professional services performed in Wisconsin and three-fourths to professional services performed in other states. The partner reports income on a calendar-year basis. The partnership reports income on an August 31 fiscal-year basis. The partner, who was a full-year Wisconsin resident in 1984, moved out of Wisconsin on August 1, 1985. The partnership books show a profit of \$200,000 for its fiscal year ending August 31, 1985. Of that amount, \$190,000 was attributable to the first 11 months of the fiscal year. After moving from Wisconsin, the partner does not personally perform any services in Wisconsin. The partner is taxed on \$38,500, which is computed as follows: (a) one-fifth of all partnership income (\$190,000) for the period from September 1, 1984 to August 1, 1985, plus (b) one-fifth of the \$2,500 (1/4 of \$10,000) of partnership income attributable to professional services performed in Wisconsin by the partnership for the period from August 1, 1985 through August 31, 1985.

**Example 2.** An individual is one of two equal general partners of a partnership whose income is attributable to a business located in Minnesota. The partner and the partnership report income on a calendar-year basis. The partner, who was a full-year Wisconsin resident in 1984, moved out of Wisconsin on June 1, 1985. The partnership books show a profit of \$5,000 for the first 5 months of 1985.

The partner must file a 1985 Wisconsin return reporting all income (partnership income and any other income) until June 1, 1985. This includes \$2,500 (1/2 of \$5,000), which is the partner's distributive share of actual partnership income earned until June 1, 1985. Since the partnership business is located outside Wisconsin, no part of the partnership income for the period June 1, 1985 through December 31, 1985 is taxable to the partner for Wisconsin income tax purposes.

**Example 3.** A general partner owns a two-thirds interest in a partnership whose income is attributable to rental properties located in Iowa. The partner reports income on a calendar-year basis. The partnership reports income on a March 31 fiscal-year basis. The partner, who was a full-year Wisconsin resident in 1984, became an Iowa resident on August 1, 1985. The partnership books show a profit of \$12,000 for the fiscal year ending March 31,

1985. In addition, the partnership books show a profit of \$3,000 for the period from April 1, 1985 to August 1, 1985.

The partner must file a 1985 Wisconsin return reporting all income (partnership income and any other income) until August 1, 1985. This includes \$8,000 (2/3 of \$12,000), which is the partner's distributive share of the partnership income for the fiscal year ending March 31, 1985.

In addition, the partner must file a 1986 Wisconsin return and report \$2,000 (2/3 of \$3,000), which is the partner's distributive share of the partnership income that was earned from April 1, 1985 to August 1, 1985. Under Section 706(a) of the Internal Revenue Code, if a partner's taxable year differs from the partnership's taxable year, the partner must report on his or her return the distributive share of partnership income for the partnership's fiscal year ending with or within the partner's taxable year.

#### B. Limited Partners

A nonresident limited partner in a partnership engaged in business in Wisconsin is not taxed on any income distributable to the partner from the partnership, provided that the partner is precluded from taking any part in the management of the business or affairs of the partnership and is not authorized to act for or bind the partnership in any way. If the partner is limited in this manner, the distribution of income represents income which follows the residence of the individual. Section 71.07(1), 1985 Wis. Stats., provides that income or loss of nonresident individuals from intangible personal property follows the residence of the individual. In the case *Sweitzer v. Revenue*, 65 Wis. 2d 235 (1974), the Wisconsin Supreme Court ruled that a limited partnership interest is analogous to the interest held by a corporate shareholder, resulting in intangible income which follows the residence of the recipient. Thus, a nonresident of Wisconsin is generally not taxed on income from a limited partnership.

**Example.** An individual owns a 10% interest as a limited partner of a partnership engaged in business in Wisconsin. The partner and the partnership report income on a calendar-year basis. The partner became a Wisconsin resident on September 1, 1985. The partner must file a 1985 Wisconsin return reporting all income (partnership income and any other income) for the period September 1, 1985 to December 31, 1985.

Even if an individual is defined as a "limited partner," if that individual may take part in any of the management of the business or affairs of the limited partnership, or is authorized to act for or bind the partnership in any way, the individual is treated the same as a nonresident general partner. The individual is taxed on his or her proportionate share of the partnership's Wisconsin income.

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#### 4. Gain or Loss on the Sale of a Partnership Interest by a Nonresident

**Statutes:** Section 71.07(1), 1985 Wis. Stats.

**Facts and Question 1:** Taxpayer X is a resident of Illinois. Taxpayer X is a limited partner in a Wisconsin partnership and a general partner in another Wisconsin partnership. In 1986, Taxpayer X sells his partnership interests in both Wisconsin partnerships. Is the gain or loss Taxpayer X realized on the sale of the limited partnership interest taxable income to Wisconsin? Is the gain or loss Taxpayer X realized on the sale of the general partnership interest taxable income to Wisconsin?

**Answer 1:** The gain or loss from the sale of both the limited and general partnership interests is not taxable to Wisconsin. The limited partnership interest is considered intangible personal property. A general partnership interest is also considered to be intangible personal property.

Section 71.07(1), 1985 Wis. Stats., provides that income or loss from the sale of intangible personal property shall follow the residence of nonresidents.

**Facts and Question 2:** Taxpayer Y is a resident of Texas. Taxpayer Y is a limited partner in a Wisconsin partnership and a general partner in another Wisconsin partnership. In 1986, both partnerships sell all the assets of the partnership including land, buildings, office equipment and goodwill. Is Taxpayer Y's distributive share of the gain or loss realized on the sale of the assets by the limited partnership taxable to Wisconsin? Is Taxpayer Y's distributive share of the gain or loss realized on the sale of assets by the general partnership taxable to Wisconsin?

**Answer 2:** If a partnership sells its assets, the gain or loss realized on the sale is passed through to the partners. The gain or loss realized by the limited partnership is considered to be intangible income to a limited partner as a result of the Wisconsin Supreme Court case *Sweitzer v. Revenue*, 65 Wis. 2d 235 (1974). The gain or loss will follow the residence of a nonresident; therefore, Taxpayer Y will not report his or her share of the gain or loss from the sale of the limited partnership assets to Wisconsin (s. 71.07(1), 1985 Wis. Stats.).

Taxpayer Y's share of the gain or loss realized by the general partnership, other than goodwill, is taxable to Wisconsin. Section 71.07(1), 1985 Wis. Stats., provides that the income or loss from the sale of property of a nonresident follows the situs of the property. Because the property is located in Wisconsin, the gain or loss is reportable to Wisconsin by Taxpayer Y. Goodwill is an intangible asset; therefore, Taxpayer Y will not report his or her share of the gain from the sale of goodwill by the general partnership to Wisconsin.

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#### 5. Advance Payment of Real Estate Taxes

**Statutes:** Section 71.53, 1983 Wis. Stats., and section 71.54, 1985 Wis. Stats.

**Facts and Question:** During 1984, Taxpayer A paid the following amounts for real estate taxes on his principal dwelling located in Milwaukee, Wisconsin:

1983 real estate taxes assessed (payable in 1984)	\$2,500
1984 real estate taxes assessed (payable in 1985)	2,800
Estimated 1985 real estate taxes (payable in 1986)	<u>2,300</u>
<b>Total Payment</b>	<b><u>\$7,600</u></b>

During 1985, Taxpayer A paid the following amounts for real estate taxes:

1985 real estate taxes assessed (payable in 1986) of \$3,100 less the \$2,300 paid in 1984	\$ 800
Estimated 1986 real estate taxes (payable in 1987)	<u>2,500</u>
<b>Total Payment</b>	<b><u>\$3,300</u></b>

During 1986, Taxpayer A pays the following amounts for real estate taxes:

1986 real estate taxes assessed (payable in 1987) of \$3,400 less the \$2,500 paid in 1985	\$ 900
Estimated 1987 real estate taxes (payable in 1988)	<u>1,100</u>
<b>Total Payment</b>	<b><u>\$2,000</u></b>

What is the allowable home owner's credit for 1984 and 1985, pursuant to s. 71.53, and the allowable home owner's credit for 1986, pursuant to s. 71.54?

**Answer:** Section 71.53, 1983 Wis. Stats., provides a 10% tax credit for real estate taxes paid by a claimant on the claimant's principal dwelling during the taxable year. For the 1986 taxable year, s. 71.54, 1985 Wis. Stats., provides a one-time 7.9% tax credit for up to \$2,000 of real estate taxes paid by the claimant on the claimant's principal dwelling during the taxable year.

The Wisconsin Supreme Court in *Trepte v. Wisconsin Department of Revenue*, 56 Wis. 2d 81 (1972), concluded that "a tax prepayment can only be deducted in the year made—providing a liability exists for which a prepayment might be made." Therefore, prepayments of real estate taxes are merely deposits and a home owner's credit cannot be claimed until an actual liability arises and the deposit is applied to that liability.

The credit allowable to Taxpayer A each year is computed as follows:

1984: 1983 real estate taxes (payable in 1984)	\$2,500
1984 real estate taxes (payable in 1985)	<u>2,800</u>
<b>Total</b>	<b>5,300</b>
	<b>x 10%</b>
<b>1984 Home Owner's Credit</b>	<b><u>\$530</u></b>
1985: 1985 real estate taxes (payable in 1986)	\$3,100
	<u>x 10%</u>
<b>1985 Home Owner's Credit</b>	<b><u>\$310</u></b>
1986: 1986 real estate taxes (payable in 1987), but not more than \$2,000	\$2,000
	<u>x 7.9%</u>
<b>1986 Home Owner's Credit</b>	<b><u>\$158</u></b>

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## INCOME AND FRANCHISE TAXES

### 1. Taxpayer Elections for Wisconsin Income and Franchise Taxes

**Statutes:** Sections 71.04(2b), (2d), (2e), (2f), (2g), (5), (8), (11), (15) and (16); 71.046; 71.047; 71.05(1)(h) and (i); 71.10(1)(b); 71.11(8) and (9); 71.305; 71.307; and 71.333, 1985 Wis. Stats.

**Wis. Adm Code:** Sections Tax 2.16, 2.19, and 2.83, September 1983 Register; sections Tax 2.20, 2.24, and 2.53, January 1956 Register; sections Tax 2.21, 2.25, 2.26, and 3.38, February 1975 register; section Tax 3.44, August 1970 Register; and section Tax 3.48, February 1978 Register.

**Note:** This Tax Release applies to all years open to adjustment unless otherwise noted.

Chapter 71, Wis. Stats., includes various provisions under which a taxpayer may elect one of several methods of claiming a deduction, reporting income, or filing a return. This Tax Release briefly describes each of the elections listed below, how the election is made, when it must be made and other related information. After the title of each election is listed the type of taxpayer to whom the election applies. (Example: "K. Iron Ore Depletion - Corporations" applies only to corporations.)

As used in this Tax Release, "corporation", as defined in s. 71.02(1)(f), 1985 Wis. Stats., includes corporations, joint stock companies, associations or common law trusts organized or conducted for profit. References to statutes are to the Wisconsin Statutes, except where indicated otherwise.

**NOTE:** The elections listed in this Tax Release are not available to insurance companies, regulated investment companies and real estate investment trusts. Insurers compute taxable income under s. 71.01(4), 1985 Wis. Stats. Corporations or common law trusts which qualify as regulated investment companies or real estate investment trusts compute taxable incomes under s. 71.02(1)(c), 1985 Wis. Stats.

The following elections are covered in this Tax Release:

- A. Waste Treatment Facilities - Corporations, Individuals, Estates and Trusts
- B. Forest Croplands - Corporations
- C. Renewable Energy Resource Systems - Corporations
- D. Research or Experimental Expenditures - Corporations
- E. Trademark or Trade Name Expenditures - Corporations
- F. Organizational Expenses - Corporations
- G. Ordered Charge Downs or Write-Offs - Corporations
- H. Charitable Contributions - Corporations
- I. Depreciation or Amortization - Corporations
- J. Mineral Ores Depletion - Corporations
- K. Iron Ore Depletion - Corporations
- L. Installment Sales - Corporations
- M. Percentage of Completion Method of Accounting - Corporations
- N. Deferred Profit Method of Accounting - Corporations
- O. Valuation of Inventories - Corporations
- P. Declaration of Inactivity - Corporations
- Q. Distributions of Stock and Stock Rights - Corporations and Individuals
- R. Gain on Corporate Liquidation - Corporations and Individuals