

particularly where the leased items were used by the drivers in the course of taxpayer's business. The taxpayer also claimed that because the department took no steps to notify him of the taxability of such transactions, the department is estopped from making him pay.

The department argued the taxability issue is controlled by the Commission's holding in *Peterson v. Wisconsin Department of Revenue*, 203-026 Wisconsin Tax Reporter (WTAC 1989), wherein it held, in similar circumstances, cab leases to be taxable retail transactions. The department also argued that it is not estopped from collecting the tax; it had no duty to notify taxpayer and isn't collaterally estopped by the DILHR case.

The Commission held that the lease payments are taxable retail receipts. The transactions were retail transactions because, among other things, the drivers — not the fare-paying consumers — were the ultimate users of the property and provided only services, not property, to the fare-payers.

The Commission also held that even if it accepted as binding the court's decision that the taxpayer and the drivers had employment relationships, it still could not say that those relationships legally exclude lease relationships with respect to the cabs. The Commission ruled that an employee can be his employer's lessee of property used in the course of the employer's business, and

accordingly, the department is not estopped by the court ruling establishing an employment relationship.

Finally, the Commission ruled that the department is not estopped by its "failure" to notify the taxpayer of the taxability of the lease payments, that to impose such a duty to notify the taxpayers would be to impose an impossible burden, and that the existence of published statutory law constitutes notice to the state's taxpayers.

The taxpayer has appealed this decision to the Circuit Court. □

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. Distributions From Keogh and Deferred Compensation Plans (p. 17)
2. Farmers' Drought Credit and Its Effect on 1989 Federal and Wisconsin Income Tax Returns (p. 18)
3. Property Taxes/Rent Allowable for School Property Tax Credit Computation (p. 20)
4. Small Business Stock (p. 21)
5. Taxable Status of Interest Income Received from Certain Securities (p. 22)
6. Taxation of Dependents With Unearned Income (p. 22)
7. Wisconsin Tax Treatment of Lump-Sum Distributions (p. 23)

Homestead Credit

1. Homestead Credit - Ownership of Homestead (p. 24)

Corporation Franchise or Income Taxes

1. Difference Between Wisconsin Basis and Federal Basis of Assets Disposed of in Taxable Transactions (p. 25)

Sales/Use Taxes

1. Cost-Sharing of Telecommunications Equipment and Services (p. 26)
2. Electricity Used in Industrial Waste Treatment Facility (p. 26)
3. Leased Automobiles Used by Employees (p. 26)
4. License, Maintenance, and Enhancement of Computer Software (p. 27)
5. Sale of Waste Removal Services and Transfer of Tangible Personal Property (p. 28)
6. Supplies Used in Delivering Newspapers (p. 28)
7. "Transport" Natural Gas and Transportation Charges (p. 29)
8. When Is a Sale in Wisconsin for Purposes of Imposing Wisconsin Sales Tax (p. 31)

INDIVIDUAL INCOME TAXES

1. Distributions From Keogh and Deferred Compensation Plans

Statutes: Section 71.05(6)(b)1, Wis. Stats. (1987-88)

Background: In a Tax Release titled "Distributions from IRAs Which Invest in U.S. Government Securities," WTB 61, page 13, it stated that amounts withdrawn from an IRA which are attributable to interest from U.S. Government securities may be excluded from Wisconsin taxable income under sec. 71.05(6)(b)1, Wis. Stats. (1987-88), pursuant to 31 USCS § 3124.

Question 1: When amounts are withdrawn from a Keogh or deferred compensation plan which invests in securities issued by the U.S. Government, will a portion of the amount withdrawn constitute interest from U.S. Government securities which is exempt from Wisconsin income tax?

Answer 1: Yes. The portion of the amount withdrawn from a Keogh plan or deferred compensation plan attributable to interest from U.S. Government securities may be excluded from Wisconsin taxable income under sec. 71.05(6)(b)1, Wis. Stats. (1987-88), pursuant to 31 USCS § 3124, provided the plan is a "qualified retirement plan."

Question 2: Is the formula for determining what portion of a Keogh plan or deferred compensation plan distribution is considered U.S. Government interest the same as provided for IRAs in WTB 61?

Answer 2: Yes. The formula and examples provided on pages 13 and 14 of WTB 61 explaining how to determine what portion of an IRA distribution is U.S. Government interest may be used to determine what portion of a Keogh plan or deferred compensation plan distribution is considered U.S. Government interest.



2. Farmers' Drought Credit and Its Effect on 1989 Federal and Wisconsin Income Tax Returns

Statutes: Sections 71.01(6), 71.05(6)(b)5, and 71.07(2fd) and (9), Wis. Stats. (1987-88)

Note: This Tax Release applies only with respect to taxable year 1989. The information regarding the federal treatment of the farmers' drought credit is based on a letter from the IRS district office in Milwaukee.

Background: Section 71.07(2fd), Wis. Stats. (1987-88), provides a refundable credit to owners of Wisconsin farmland equal to 10% of 1988 farm property taxes accrued, subject to certain requirements. The maximum credit is \$1,000 and may be claimed on the taxpayer's 1988 Wisconsin income tax return. Most taxpayers will receive the credit in their 1989 taxable year.

Section 111 of the Internal Revenue Code and Treasury Reg. § 1.111-1, provide that the recovery of an amount a taxpayer deducted or claimed as a credit in a prior year must be included in taxable income to the extent the taxpayer received a tax benefit from the prior year's deduction or credit.

If the recovery and the deductible expense or credit occur in the same taxable year, the recovery reduces the deduction or credit and is not included in income. If the recovery is attributable to more than one taxable year, the recovery first reduces the deduction or credit not previously claimed. Any remaining recovery is included in income to the extent the taxpayer received a tax benefit from a prior year's deduction or credit.

Wisconsin follows the provisions of sec. 111, IRC under sec. 71.01(6), Wis. Stats. (1987-88).

Section 71.05(6)(b)5, Wis. Stats. (1987-88), provides that any amounts included in federal adjusted gross income which are recoveries of federal itemized deductions for which no tax benefit was received for Wisconsin tax purposes may be subtracted from federal adjusted gross income in computing Wisconsin adjusted gross income.

Question 1: If a taxpayer claimed the farmers' drought credit on his or her 1988 Wisconsin income tax return, is the amount of the credit considered a recovery and governed by sec. 111, IRC, for federal and Wisconsin income tax purposes.

Answer 1: Yes. The farmers' drought credit is considered a recovery of farm property taxes in taxable year 1989 governed by sec. 111, IRC, for federal and Wisconsin income tax purposes.

FEDERAL TAX TREATMENT

Question 2: How is the amount of the 1988 farmers' drought credit received in 1989 reported on a taxpayer's 1989 federal income tax return.

Answer 2: The answer depends on when the deduction for property taxes used in computing the farmers' drought credit was claimed by the taxpayer. There are 3 possibilities:

1. If the property taxes used in computing the farmers' drought credit were deducted in taxable year 1988, the amount of the farmers' drought credit is included in 1989 federal taxable income to the extent the taxpayer received a federal tax benefit from the 1988 deduction.

Example 1: A calendar year taxpayer paid 1988 property taxes accrued of \$8,000 during 1988. Of the \$8,000 of property taxes, 90% (\$7,200) was deducted on 1988 federal Schedule F as farm property taxes. The remaining \$800 of property taxes relating to the personal residence was deducted on 1988 federal Schedule A. The taxpayer received a federal tax benefit from the deductions of property taxes on 1988 federal Schedules A and F. The taxpayer claimed a farmers' drought credit of \$800 (10% of \$8,000) on his or her 1988 Wisconsin income tax return.

The entire amount of farmers' drought credit of \$800 must be reported as income on the taxpayer's 1989 federal income tax return. Of the \$800, 90% (\$720) is reported as income on federal Schedule F and 10% (\$80) is reported as "other income" on line 22 of 1989 federal Form 1040.

Example 2: Assume the same facts as in Example 1, except that the taxpayer claimed the standard deduction rather than itemized deductions on his or her 1988 federal income tax return.

Because the taxpayer deducted only 90% of property taxes paid (\$7,200) in computing federal income, only 90% of the farmers' drought credit (\$720) must be reported as income on the taxpayer's 1989 federal income tax return. The \$720 of

farmers' drought credit is reported as income on federal Schedule F.

2. If the property taxes used in computing the farmers' drought credit are deducted in taxable year 1989, the amount of farmers' drought credit reduces the amount of property taxes paid in 1989 for purposes of determining the deduction allowable on the taxpayer's 1989 federal income tax return.

Example 3: A calendar year taxpayer paid 1988 property taxes accrued of \$10,000 during 1989. Of the \$10,000 of property taxes, 90% (\$9,000) are farm property taxes deductible on Schedule F. The remaining \$1,000 of property taxes relate to the personal residence and are deductible on federal Schedule A. The taxpayer claimed a farmers' drought credit of \$1,000 (10% of \$10,000) on his or her 1988 Wisconsin income tax return.

The taxpayer may only deduct \$8,100 of 1988 farm property taxes on 1989 federal Schedule F (\$9,000 farm property taxes less \$900 farmers' drought credit) and \$900 of 1988 property taxes relating to the personal residence on 1989 federal Schedule A (\$1,000 property taxes less \$100 farmers' drought credit).

Example 4: Assume the same facts as in Example 3 except that the taxpayer claims the standard deduction rather than itemized deductions on his or her 1989 federal income tax return.

The taxpayer may deduct \$8,100 of 1988 farm property taxes on 1989 federal Schedule F (\$9,000 farm property taxes less \$900 farmers' drought credit). No reduction of the standard deduction for the remaining \$100 of farmers' drought credit is necessary.

3. If the property taxes used in computing the farmers' drought credit are partially deductible in taxable years 1988 and 1989, the farmers' drought credit first reduces the deduction available for 1988 property taxes paid in 1989. The remainder of the farmers' drought credit is reported as income on the taxpayer's 1989 federal income tax return to the extent the taxpayer received a federal tax benefit from the 1988 property tax deductions.

Example 5: A calendar year taxpayer had 1988 property taxes accrued of \$6,000. The taxpayer paid \$4,000 of the 1988 property taxes in 1988 and the remaining 1988 property taxes (\$2,000) in 1989. The taxpayer deducted 90% of property taxes paid in 1988 (\$3,600) on 1988 federal Schedule F. The remaining \$400 (10% of \$4,000) of 1988 property taxes paid relating to the personal residence were deducted on 1988 federal Schedule A. The taxpayer received a federal tax benefit from the 1988 property tax deductions.

The taxpayer claimed a farmers' drought credit of \$600 (10% of \$6,000) on his or her 1988 Wisconsin income tax return.

On the 1989 federal income tax return, the taxpayer is allowed a total property tax deduction of \$1,400 (\$2,000 1988 property taxes paid in 1989 less \$600 farmers' drought credit). Of the \$1,400 of property taxes, the taxpayer may deduct 90% (\$1,260) on 1989 federal Schedule F and 10% (\$140) on 1989 federal Schedule A. None of the farmers' drought credit is reported as income on the 1989 federal income tax return.

Example 6: Assume the same facts as in Example 5 except that the taxpayer paid \$5,500 of 1988 property taxes in 1988 and the remaining \$500 of 1988 property taxes in 1989.

On the 1989 federal income tax return, no deduction is allowed for 1988 property taxes on federal Schedule A or F because the farmers' drought credit first reduces 1988 property taxes not yet deducted (\$500). The remaining farmers' drought credit (\$100) must be reported as income on the 1989 federal income tax return. Of the \$100 of income, \$90 is reported on federal Schedule F and the remaining \$10 is reported as "other income" on line 22 of 1989 federal Form 1040.

WISCONSIN TAX TREATMENT

Question 3: What effect does the farmers' drought credit have on a taxpayer's 1989 Wisconsin income tax return?

Answer 3: The answer depends on how the farmers' drought credit is reported on the taxpayer's 1989 federal income tax return. Based on the 3 possibilities of reporting for federal purposes given in Answer 2, the following would apply for Wisconsin income tax purposes:

1. If the taxpayer reported the farmers' drought credit as income on his or her 1989 federal income tax return and received a Wisconsin tax benefit from the 1988 property taxes, no modification is necessary for Wisconsin.

The taxpayer does not receive a Wisconsin tax benefit from property taxes deducted on federal Schedule A. However, if those same taxes are used to compute the school property tax credit on the taxpayer's 1988 Wisconsin income tax return and the credit reduces the taxpayer's Wisconsin tax liability, the taxpayer is considered to receive a Wisconsin tax benefit from the 1988 property taxes relating to the personal residence.

If the taxpayer did not receive a tax benefit from the school property tax credit on his or her 1988 Wisconsin income tax return, the taxpayer may claim a subtraction modification from federal adjusted gross income on his or her 1989 Wisconsin income tax return for the portion of farmers' drought credit included in federal income that relates to the 1988 property taxes itemized on federal Schedule A.

Example 7: Assume the same facts as in Example 1 and that the property taxes claimed as a deduction on federal Schedule A (10% of \$8,000 or \$800) were also used to claim the school

property tax credit on the taxpayer's 1988 Wisconsin income tax return.

Assuming the taxpayer received a tax benefit from the 1988 Wisconsin school property tax credit, the farmers' drought credit is also taxable for Wisconsin. Therefore, no subtraction modification from federal adjusted gross income may be claimed.

If the taxpayer had not received a tax benefit from the 1988 school property tax credit for Wisconsin income tax purposes, the taxpayer may claim a subtraction modification of \$80 (10% of the farmers' drought credit), which is that portion of the farmers' drought credit relating to 1988 property taxes on the personal residence which were claimed as an itemized deduction on federal Schedule A.

Example 8: Assume the same facts as Example 2 and that the taxpayer used the \$800 of property taxes on the personal residence to compute the school property tax credit on his or her 1988 Wisconsin income tax return and received a Wisconsin tax benefit from the credit.

The farmers' drought credit relating to property taxes on the personal residence (\$80 which was not taxable for federal) is not added to federal adjusted gross income in computing Wisconsin adjusted gross income. Even though the taxpayer received a Wisconsin tax benefit from the 1988 school property tax credit, there is no provision in Wisconsin income tax law to require the \$80 addition modification.

2. If the taxpayer is required to reduce property tax deductions on 1989 federal Schedules A and F for federal income tax purposes, the same adjustments apply for Wisconsin. The property taxes allowed as a deduction on federal Schedule A may be used to compute the 1989 Wisconsin school property tax credit.

Example 9: Assume the same facts as in Example 3. The farmers' drought credit also reduces the property taxes that may be claimed as a deduction on 1989 federal Schedule F for Wisconsin income tax purposes. Therefore, no modification to federal adjusted gross income is necessary.

The same amount of property taxes on the personal residence, as reduced by the farmers' drought credit, claimed on federal Schedule A (\$100) may be used to compute the school property tax credit on the taxpayer's 1989 Wisconsin income tax return.

Example 10: Assume the same facts as in Example 4. The farmers' drought credit also reduces the property taxes that may be claimed on 1989 federal Schedule F for Wisconsin income tax purposes. Therefore, no modification to federal adjusted gross income is necessary.

The property taxes used to compute the school property tax credit on the 1989 Wisconsin income tax return must be

reduced by the farmers' drought credit even though for federal purposes no adjustment is necessary because the taxpayer claims the standard deduction for 1989. The amount which may be used to compute the school property tax credit is \$900 (\$1,000 property taxes less \$100 farmers' drought credit = \$900).

3. If the taxpayer paid 1988 property taxes accrued in 1988 and 1989 and the taxpayer reduces his or her 1989 property tax deduction by the farmers' drought credit and includes a portion of the farmers' drought credit in income, the same reductions of property taxes apply for Wisconsin as for federal. Also, the portion of farmers' drought credit includable in 1989 federal adjusted gross income is also includable in Wisconsin adjusted gross income, provided the taxpayer received a tax benefit from the school property tax credit on his or her 1988 Wisconsin income tax return.

Example 11: Assume the same facts as in Example 5. The farmers' drought credit also reduces the property taxes that may be claimed as a deduction on 1989 federal Schedule F for Wisconsin income tax purposes (\$1,260). Therefore, no modification to federal adjusted gross income is necessary.

The same amount of property taxes as deductible on federal Schedule A (\$140) may be used to compute the school property tax credit on the taxpayer's 1989 Wisconsin income tax return.

Example 12: Assume the same facts as Example 6 and that the taxpayer received a Wisconsin tax benefit from the school property tax credit allowed on his or her 1988 Wisconsin income tax return. The same reduction of property taxes applies for Wisconsin purposes as for federal purposes. Therefore, the taxpayer may not use any of the 1988 property taxes paid in 1989 to compute the school property tax credit on his or her 1989 Wisconsin income tax return. The remaining \$100 of farmers' drought credit includable in federal income is also taxable for Wisconsin income tax purposes and no modification is necessary.

If the taxpayer had not received a tax benefit from the school property tax credit allowed on his or her 1988 Wisconsin income tax return, the taxpayer could subtract \$10 from federal adjusted gross income. That \$10 is that portion of the farmers' drought credit included in federal adjusted gross income that reflects property taxes on the personal residence (10% of \$100 or \$10).

□

3. Property Taxes/Rent Allowable for School Property Tax Credit Computation

Statutes: Section 71.07(9)(a)3. and 4., Wis. Stats. (1987-88)

Facts and Question 1: A woman receives a life estate in a home pursuant to a trust set up by her deceased husband. She uses this home as her principal dwelling. May she claim a school property tax credit under sec. 71.07(9), Wis. Stats. (1987-88), based on the entire amount of property taxes she pays on this home?

Answer 1: Yes, subject to the dollar limitations under sec. 71.07(9)(b), Wis. Stats. (1987-88), (\$2,000 for 1988). A life estate is not merely a right to occupy property; it is a freehold estate. A life tenant is an owner of the property for the duration of his or her life. Since the woman is in possession of a life estate interest she is considered to be the owner and is, therefore, entitled to claim the property taxes which she pays in computing the homeowner's school property tax credit.

Facts and Question 2: A husband and wife own a home in joint tenancy, tenancy in common, or as marital property. The wife lives in the home all year, while the husband maintains a separate home elsewhere. The wife pays all the property taxes using her wages. May the wife claim a homeowner's school property tax credit based on the taxes for her ownership share of the homestead and a renter's school property tax credit based on the taxes for her husband's ownership share of the property, which she pays?

Answer 2: Yes. Under sec. 71.07(9)(a)3., Wis. Stats. (1987-88), the definition of property taxes as it pertains to the school property tax credit provides that if the principal dwelling is owned by 2 or more persons or entities, property taxes is that part of the property taxes paid that reflects the ownership percentage of the claimant. Therefore, the wife may claim the percentage of property taxes she pays which reflects her ownership interest (generally 50%, unless designated otherwise) in the computation of the homeowner's school property tax credit.

Since the wife pays all the taxes for her principal dwelling and can claim only her ownership share for computing the homeowner's school property tax credit, the balance of those taxes is considered to be rent just as it is for homestead credit purposes. She may claim the balance as rent in the computation of the renter's school property tax credit under sec. 71.07(9)(a)4., Wis. Stats. (1987-88), whereby 25% of the rent constitutes property taxes if heat is not included, or 20% if heat is included.

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4. Small Business Stock

Statutes: Sections 71.01(10) and 71.05(6)(b)6, Wis. Stats. (1987-88)

Background: Net capital gains on small business stock are excludable from Wisconsin adjusted gross income provided the taxpayer acquired the stock on or after January 1, 1986, did not acquire the stock by gift, and submits with his or her Wisconsin tax return a copy of the certification issued by the corporation.

"Small business stock" means an equity security that the taxpayer has held for at least 5 years and that is issued by a corporation that, on the December 31 before acquisition by the taxpayer, or, for a corporation which was incorporated during the calendar year in which the stock is issued, as of the date of the acquisition of the stock, fulfills all of the following requirements and so certifies to the taxpayer upon acquisitions:

- a. Has at least 50% of its property and at least 50% of its payroll in Wisconsin.
- b. Has no more than 500 employees (200 employees for stock acquired prior to the 1988 taxable year) covered by Wisconsin unemployment insurance, including employees of any corporation that owns more than 50% of the stock of the issuing corporation.
- c. Derives no more than 25% of its gross receipts from rents, interest, dividends, and sales of intangible investment assets combined, unless the corporation derives less than \$3,000 of that income and has not been incorporated for more than 2 calendar years.
- d. Has not issued stock that is listed on the New York Stock Exchange, the American Stock Exchange, or the National Association of Securities Dealers automated quotation system.
- e. Has not liquidated its assets in whole or in part for tax purposes only in order to fulfill the above requirements and then reorganized.

For stock acquired after January 1, 1986, but before August 31, 1987 it is also required that the corporation may not have conducted a trade or business in any form for a period exceeding 5 years and for the required under item c, above, the sales of any assets had to be used in determining the percentage of gross receipts. In addition, the corporation had to meet all of the requirements on the December 31 before acquisition of stock by the taxpayer.

Facts: On March 15, 1987, SBS, Inc. sold 100 shares of its stock to John Smith and certified to Mr. Smith that the stock in SBS, Inc. qualified as "small business stock". On January 10, 1989 Mr. Smith sold 50 shares of his SBS, Inc. stock to Mary Jones.

Question: If Mary Jones holds her 50 shares of SBS, Inc. for at least 5 years, can she exclude from her Wisconsin adjusted gross income the amount of any net capital gains realized from her sale of SBS, Inc. stock?

Answer: No. The stock only qualifies as small business stock if it is acquired by the taxpayer from the issuing corporation. Since Ms. Jones purchased the stock from Mr. Smith, the exclusion is not available to Ms. Jones. The certification issued by SBS, Inc. is not transferable. Assuming Mr. Smith holds his remaining 50 shares of SBS, Inc. stock the required 5 years, he would be able to exclude from his Wisconsin adjusted gross income the amount of any net capital gain realized from his sale of this stock.

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