

the merger. After the merger, Wis. Corp. ceases to exist as a corporation. This transaction qualifies as an "F" reorganization as defined in sec. 368(a)(1)(F) of the Internal Revenue Code (IRC).

For federal purposes, Del. Corp. succeeds to Wis. Corp.'s tax attributes under IRC sec. 381. Accordingly, Del. Corp. files a single federal income tax return covering the fiscal year ending July 31, 1990, and Wis. Corp. will not file any federal return for any part of the same period. Rev. Rul. 57-276, 1957-1 C.B. 126.

What are the filing requirements of Wis. Corp. and Del. Corp. for Wisconsin franchise or income tax purposes?

Answer: Del. Corp. must file a Wisconsin franchise or income tax return for the entire fiscal year ending July 31, 1990, for both Wis. Corp. and itself. Wis. Corp. is not required to file a short-period return for the period from August 1, 1989, through the date of the merger.

The "taxable year" for Wisconsin purposes is the taxable period upon the basis of which the taxable income of the taxpayer is computed for federal income tax purposes. Sec. 71.22(10), Wis. Stats. (1987-88), as amended by 1989 Wisconsin Act 31. Applying sec. 71.22(10), the taxable years of Wis. Corp. and Del. Corp. must be the same for Wisconsin franchise or income tax purposes as they are for federal income tax purposes. Accordingly, only Del. Corp. must compute a tax liability for the fiscal year ending July 31, 1990, and Wis. Corp. will not compute any tax liability for any part of that fiscal year. Wis. Corp. and Del. Corp. are treated as if no change in corporate entities had occurred, the same as federally.



## 5. Wisconsin Research Facilities Credit

Statutes: Sections 71.28(4)(b) through (i) and (5) and 71.47(3)(b) through (i) and (4), Wis. Stats. (1987-88), and sec. 71.09(12r)(b) through (L) and (12rf), Wis. Stats. (1985-86).

Background: For 1984 and subsequent years, any corporation may credit against taxes otherwise due under chapter 71 an amount equal to 5% of the amount paid or incurred by that corporation during the taxable year to construct and equip new facilities or expand existing facilities used in Wisconsin for qualified research, as defined in section 41 of the Internal Revenue Code (IRC). Only amounts paid or incurred for tangible, depreciable property are eligible. Amounts paid or incurred for replacement property are not eligible.

Facts and Question 1: Corporation A purchases a desktop personal computer and related software for use in analyzing research data in its advanced research laboratory. Although the corporation uses several other computers in the laboratory, this unit will be used by employees performing experiments in new and different phases of product development, which is qualified research under IRC sec. 41. Does the expenditure qualify for the Wisconsin research facilities credit?

Answer 1: Yes. The expenditure constitutes an expansion of Corporation A's research capabilities and, therefore, is eligible for the Wisconsin research facilities credit.

Facts and Question 2: Corporation B purchases an advanced model desktop personal computer and related software for use in analyzing research data in its advanced research laboratory. The corporation currently uses several other computers in the laboratory, and this unit will replace and upgrade an older model personal computer used by employees performing experiments in various phases of product development, which is qualified research under IRC sec. 41. The new computer has a larger memory and faster operating speed than the old computer which enables it to perform more sophisticated analyses on larger volumes of data. The new computer is priced at \$10,000. A computer with essentially the same capabilities as the old computer is available for \$4,500.

Does the expenditure qualify for the Wisconsin research facilities credit?

Answer 2: In this situation, \$5,500 of the \$10,000 expenditure qualifies for the Wisconsin research facilities credit. Only a portion of the expenditure qualifies for the credit because the new computer both replaces an existing computer and expands Corporation B's research capabilities. A reasonable allocation of the expenditure between the amount paid for replacement property and the amount paid to expand research capabilities must be made. That portion of the expenditure which is attributable to the expansion of Corporation B's research capabilities qualifies for the credit, whereas the cost of replacement property does not qualify.

Since a computer with essentially the same capabilities as the old computer would cost \$4,500, that portion of the \$10,000 purchase price is considered to be a nonqualifying expenditure for replacement property. The remaining \$5,500 is treated as an amount paid to expand Corporation B's research capabilities.

Facts and Question 3: Corporation C produces adaptor plates used in various products manufactured by its customers. These adaptor plates typically require a large number of threaded holes of varying depths and diameters to secure the plate to the customer's product and also to affix various accessories. To expedite the product development process, Corporation C purchases a new multi-spindle drill for use in its prototype model shop. The drill is designed to enable the operator to rapidly set up a large number of different drilling jobs, but is not suited to or used for large quantity production runs. However, if time is available, the drill occasionally is used to rework adaptor plates sent from the manufacturing plant for redrilling.

The new drill replaces several single-spindle drills presently used in the model shop. The new drill enables the corporation to drill and tap more holes with significantly greater precision and speed than the single-spindle drills it replaced. The new drill substantially reduces the cost and time required to develop new model adaptor plates. The new multi-spindle drill costs \$25,000, whereas the single-spindle drills which it replaces would cost a total of \$20,000.

A review of the drill operator's time cards used to report his work indicates that 40% of the time the machine is used to produce new pilot models, which is qualified research under IRC sec. 41, and the remainder of the time the machine is used in nonqualifying activities.

Is the new multi-spindle drill which is used in the prototype model shop eligible for the Wisconsin research facilities credit?

**Answer 3:** In this situation, \$2,000 of the cost of the new multi-spindle drill qualifies for the Wisconsin research facilities credit. Only a portion of the expenditure qualifies for the credit because the new multi-spindle drill both replaces existing single-spindle drills and expands Corporation C's research capabilities. A further allocation is required because the drill is used only 40% of the time in qualified research.

Since the single-spindle drills would cost \$20,000, that portion of the \$25,000 purchase price is considered to be a nonqualifying expenditure for replacement property. Forty percent of the \$5,000 difference between the cost of the new multi-spindle drill and the cost of the single-spindle drills it replaces is treated as an amount paid to expand Corporation C's research capabilities.

**Facts and Question 4:** In 1987, Corporation D purchases land for \$1,000,000 and begins construction of a new 50,000 square foot research laboratory facility, remitting \$5,000,000 in progress payments to the contractor during the year. The structure is completed near the end of 1988, and an additional \$5,000,000 is remitted to the contractor. Previously, Corporation D's product development work was performed in various areas amounting to 2% of the floor space of the 500,000 square foot manufacturing plant. The research areas in the manufacturing plant are vacated and converted to other uses.

During 1988, Corporation D spends \$1,000,000 to landscape the grounds, provide parking, and furnish the 5,000 square feet devoted to activities which are not qualified research under IRC sec. 41.

Corporation D also orders \$8,000,000 of specialized research instruments and equipment in 1988. The equipment is highly specialized, and the vendor will not permit the orders to be cancelled. Some research work is commenced during 1988, but \$2,000,000 of the equipment is not received and installed until 1989. The equipment does not represent replacement property.

In what year and in what amounts may Corporation D claim the Wisconsin research facilities credit?

**Answer 4:** Corporation D may claim a research facilities credit on its 1987 Wisconsin franchise or income tax return based on \$7,000,000 of costs for the building. Since 5,000 square feet of the total 50,000 square feet of the building are not used in the conduct of qualified research, they do not qualify for the credit. Additionally, 10,000 square feet of space in the new facility replaces the product development areas formerly located within the manufacturing plant. Accordingly, the costs associated with a total of 15,000 square feet of the facility's total 50,000 square feet (30% of the total) are not eligible.

Therefore, \$7,000,000 of the \$10,000,000 cost of the building is eligible for the Wisconsin research facilities credit.

While it is required that the facility be used for the conduct of research, it is not required that the research use occur in the year the costs are paid or incurred. Therefore, D Corporation may claim a credit based on the costs of the building in 1987 because that is when the costs are incurred, even though payments are made in 1988 and the building is placed in service in 1988.

Corporation D may claim a research facilities credit on its 1988 return based on the \$8,000,000 of costs for instruments and equipment incurred in 1988, even though some of the equipment is not delivered or paid for until 1989. The \$8,000,000 obligation to pay the equipment vendors is irrevocably incurred in 1988.

Corporation D may not claim a research facilities credit for the \$1,000,000 incurred in 1987 for the land because it is not depreciable property and, therefore, does not qualify for the credit. The \$1,000,000 incurred in 1988 for landscaping the grounds, providing parking, and furnishing the non-research areas is not used in the conduct of qualified research and is not eligible for the credit.

**Note:** If, after claiming the credits, Corporation D does not use the building or the equipment in the conduct of qualified research, Corporation D must file amended returns and pay back the research facility credits previously received for nonqualifying property.

**Facts and Question 5:** Corporation E is about to commence a major scientific research project related to the improvement of its product line. The activities are considered qualified research under IRC sec. 41. Additional engineers and scientists are hired in connection with the project, and the corporation finds that additional floor space will be required to accommodate product development operations. Corporation E fulfills its temporary need for additional laboratory facilities by leasing a new building owned by Corporation F. Corporation F is a real estate development and management firm that does not conduct any qualified research.

Are the leased facilities eligible for the Wisconsin research facilities credit?

**Answer 5:** Yes. Corporation E may claim a Wisconsin research facilities credit because it is expanding its research capabilities by leasing the laboratory facility. Corporation F may not also claim a research facilities credit based on the new building.

The Wisconsin research facilities credit is available for amounts paid or incurred for tangible, depreciable property used in Wisconsin for qualified research. There is no requirement that the party conducting the research own the property. Both the lessor and the lessee may not claim a credit for the same property. Since Corporation E is using the property for qualified research, the amounts Corporation E pays or incurs to lease the facility are eligible for the credit.

Corporation E may not claim a credit based on amounts attributable to the costs of the land because it is not depreciable. Claims for the

credit must also exclude amounts attributable to any portion of the property not used in the actual conduct of qualified research.



#### 6. Wisconsin Tax Treatment of a Net Operating Loss Incurred in a Short Taxable Year Resulting From a Change in Accounting Period

**Statutes:** Sections 71.22(4) and 71.26(2)(a), (3), and (4), Wis. Stats. (1987-88).

**Note:** This tax release applies with respect to the 1987 taxable year and thereafter.

**Facts and Question:** On January 4, 1989, Corporation P acquires 100 percent of the stock of Corporation S. Corporation P had been filing its income tax returns on a calendar-year basis, while Corporation S had been filing on the basis of a fiscal year with an August 31 year-end.

Corporations P and S begin filing consolidated income tax returns for federal purposes, and they change their taxable years for reporting purposes to fiscal years ending March 31.

For federal purposes, Corporation S files a separate income tax return for the period from September 1, 1988, through January 4, 1989. Corporation S joins in the filing of a consolidated return with Corporation P for the period beginning January 5, 1989, and ending March 31, 1989. Corporation S determines that it incurred a net operating loss for each of the short periods.

For federal purposes, the 3-year carryback and 15-year carryforward provisions of sec. 172 of the Internal Revenue Code (IRC) apply to Corporation S's net operating loss for the period from September 1, 1988, through January 4, 1989. However, Corporation S must deduct the net operating loss for the period from January 5, 1989, through March 31, 1989, ratably over a 6-year period beginning with the first taxable year after the short period. Revenue Procedure 84-34, 1984-1 CB 508.

For Wisconsin purposes, Corporations P and S may not file a consolidated return. Sec. 71.26(3)(x), Wis. Stats. (1987-88). Instead, Corporations P and S each must file a separate return and report its own income. Since Corporation S must file two short-period returns for federal purposes, it also must file two short-period Wisconsin returns: the first for the period from September 1, 1988, through January 4, 1989, and the second for the period from January 5, 1989, through March 31, 1989. Sec. 71.22(10), Wis. Stats. (1987-88), as amended by 1989 Wisconsin Act 31. Corporation S determines that it also incurred a net operating loss for each of the short periods for Wisconsin purposes.

Must Corporation S prorate over 6 years its net operating loss for the period from January 5, 1989, through March 31, 1989, for Wisconsin purposes?

**Answer:** No. Corporation S is not required to prorate its net operating loss for the period from January 5, 1989, through March 31, 1989, over 6 years. Instead, Corporation S may carry forward the net operating loss for each of the short periods for up to 15 taxable years, as provided in sec. 71.26(4), Wis. Stats. (1987-88).

For Wisconsin purposes, Corporation S computes its net income under the Internal Revenue Code, with certain modifications. One of those modifications excludes the net operating loss provisions of IRC sec. 172 and replaces them with the treatment of net business loss carryforwards under sec. 71.26(4). Sec. 71.26(3)(i), Wis. Stats. (1987-88). This statute does not require a corporation to deduct over a 6-year period a net operating loss incurred during a short taxable year resulting from a change in accounting period.



#### 7. Wisconsin Tax Treatment of Corporations With Net Operating Loss and Charitable Contribution Carryovers

**Statutes:** Section 71.26(2)(a), (3), and (4), Wis. Stats. (1987-88).

**Note:** This tax release applies with respect to the 1987 taxable year and thereafter.

**Background:** For federal income tax purposes, a corporation's deduction for charitable contributions may not exceed 10 percent of taxable income as computed without regard to the charitable contribution deduction, the special deductions for corporations under Internal Revenue Code (IRC) secs. 241-247 and 249-250, any net operating loss carryback to the taxable year under IRC sec. 172, and any capital loss carryback to the taxable year under IRC sec. 1212(a)(1). Sec. 170(b)(2), Internal Revenue Code. A 5-year carryover period applies to charitable contributions in excess of the 10 percent limitation. In the case of a corporation with a net operating loss carryover, the charitable contribution is taken into account and reduces taxable income before applying the net operating loss carryover. Sec. 170(d)(2)(B), Internal Revenue Code.

**Example:** Corporation X, which reports its income on a calendar-year basis, sustained a federal net operating loss in 1988 of \$100,000. In 1989, Corporation X earned federal taxable income of \$80,000 before deducting a \$10,000 charitable contribution made in 1989 and before applying the federal net operating loss carryover from 1988.

For federal purposes, in determining the amount of 1988 net operating loss which is used in 1989, \$8,000 (10% of \$80,000) of Corporation X's 1989 charitable contribution is taken into account and reduces 1989 taxable income to \$72,000 before applying the net operating loss carryover. The remaining \$2,000 of the 1989 charitable contribution may be carried over to 1990. Since the taxable income is reduced to \$72,000, only \$72,000 of the 1988 net operating loss is used as a carryover to 1989, leaving \$28,000 of the 1988 loss available as a carryover to 1990.

**Facts and Question 1:** Assume that all of Corporation X's income is attributable to Wisconsin because the corporation is doing business only in Wisconsin. For Wisconsin purposes, Corporation X sustained a net business loss in 1988 of \$100,000 and earned Wisconsin taxable income in 1989 of \$80,000 before deducting the \$10,000 charitable contribution made in 1989 and before applying the Wisconsin net business loss carryforward from 1988.

What are Corporation X's Wisconsin charitable contribution carryover and Wisconsin net business loss carryforward to 1990?

**Answer 1:** In this situation, Corporation X's Wisconsin charitable contribution carryover and Wisconsin net business loss carryforward are the same as the federal amounts. Corporation X's Wisconsin charitable contribution carryover to 1990 is \$2,000 and its Wisconsin net business loss carryforward to 1990 is \$28,000.

For Wisconsin franchise and income tax purposes, a corporation computes its Wisconsin net income under the Internal Revenue Code, with certain modifications. Sec. 71.26(2)(a), Wis. Stats. (1987-88). One of these modifications excludes IRC sec. 172 and replaces it with the treatment of net business loss carryforwards under sec. 71.26(4). Sec. 71.26(3)(i), Wis. Stats. (1987-88). However, the state statutes do not modify IRC sec. 170, relating to the treatment of the charitable contribution deduction and carryover. Since IRC sec. 170 is not modified for Wisconsin purposes, the Wisconsin charitable contribution deduction and carryover are determined in the same manner as the federal amounts.

**Facts and Question 2:** Now assume that Corporation X does business in and outside Wisconsin and is required to determine its net income allocable to Wisconsin using the apportionment method. For Wisconsin purposes, Corporation X sustained a total company net business loss in 1988 of \$100,000 and its 1988 Wisconsin apportionment percentage was 55 percent. Therefore, Corporation X's Wisconsin net business loss carryforward to 1989 is \$55,000 (55% of \$100,000). In 1989, Corporation X earned taxable income of \$80,000 before deducting the \$10,000 charitable contribution made in 1989, before applying its 1989 Wisconsin apportionment percentage of 60 percent, and before applying the \$55,000 Wisconsin net business loss carryforward from 1988.

What are Corporation X's Wisconsin charitable contribution carryover and Wisconsin net business loss carryforward to 1990?

**Answer 2:** Corporation X's Wisconsin charitable contribution carryover to 1990 is \$2,000 and its Wisconsin net business loss carryforward to 1990 is \$11,800. These amounts are computed as follows.

For Wisconsin purposes, \$8,000 (10% of \$80,000) of Corporation X's 1989 charitable contribution is taken into account and reduces its 1989 total company net income before apportionment and the net business loss offset to \$72,000. The remaining \$2,000 of the 1989 charitable contribution may be carried over to 1990. The \$72,000 of total company net income is then multiplied by 60 percent, the 1989 Wisconsin apportionment percentage, to arrive at \$43,200 of Wisconsin

net income before the net business loss offset. Therefore, only \$43,200 of the 1988 Wisconsin net business loss is used as a carryforward to 1989, leaving \$11,800 of the 1988 loss available as a carryforward to 1990.



## 8. Wisconsin Tax Treatment of Transactions Between Related Corporations

**Statutes:** Section 71.26(3), Wis. Stats. (1987-88).

**Note:** This tax release applies with respect to the 1987 taxable year and thereafter.

**Background:** Beginning with the 1987 taxable year, corporations compute their net income under the Internal Revenue Code (IRC), as amended to a specified date, and as modified by sec. 71.26(3), Wis. Stats. (1987-88). One of these modifications excludes the consolidated return rules in IRC secs. 1501 to 1505, 1551, 1552, 1563, and 1564 for Wisconsin franchise and income tax purposes. Sec. 71.26(3)(x), Wis. Stats. (1987-88).

**Facts and Question 1:** B Corporation, a corporation incorporated in Wisconsin, is a wholly-owned subsidiary of A Corporation, a non-Wisconsin corporation. B Corporation wholly owned its non-Wisconsin subsidiary, C Corporation. B Corporation is engaged in business in Wisconsin, but neither A nor C Corporation has activity in Wisconsin that would subject it to Wisconsin franchise or income taxation. During 1989, B Corporation sold all of its C Corporation stock to A Corporation and realized a loss on the sale.

For federal purposes, A, B, and C Corporations file a consolidated income tax return. B Corporation's loss on the intercompany sale is not recognized. Treasury Regulation sec. 1.1502-13(c). Additionally, B Corporation's loss on the sale or exchange of property between members of a controlled group of corporations is deferred until the property is transferred outside the group and the loss becomes recognizable under the consolidated return rules or federal regulations. IRC sec. 267(f).

For Wisconsin purposes, A, B, and C Corporations may not file a consolidated return. Sec. 71.26(3)(x), Wis. Stats. (1987-88). Instead, B Corporation must file a separate 1989 Wisconsin franchise or income tax return and report its own income. Neither A nor C Corporation is required to file a Wisconsin return because neither corporation has nexus with Wisconsin.

Is B Corporation's loss on the sale of its C Corporation stock recognizable in 1989 for Wisconsin franchise or income tax purposes?

**Answer 1:** No. B Corporation's loss on the sale of the stock is not recognizable in 1989 for Wisconsin franchise or income tax purposes. Although Wisconsin law excludes the consolidated return provisions from the Internal Revenue Code for the purpose of computing

Wisconsin net income, Wisconsin law includes the provisions for loss transactions between related taxpayers under IRC sec. 267. Therefore, a corporation's loss on the intercompany sale of stock is deferred under IRC sec. 267(f) for Wisconsin purposes.

**Facts and Question 2:** D Corporation, a Wisconsin corporation, is a subsidiary of E Corporation, another Wisconsin corporation. During 1989, D Corporation distributed appreciated property to E Corporation.

For federal purposes, a corporation that distributes property to a shareholder recognizes a gain on the distribution to the extent the fair market value of the property distributed exceeds its adjusted basis, as if the property were sold to the distributee at its fair market value. IRC sec. 311(b).

For federal purposes, D and E Corporations file a consolidated income tax return. They eliminate their intercompany stock distributions, including dividends and nonliquidating distributions, to determine their consolidated taxable income. Treasury Regulation sec. 1.1502-14. Therefore, D Corporation's gain on the distribution of appreciated property will be deferred in 1989 and recognized at a later time.

For Wisconsin purposes, D and E Corporations may not file a consolidated return. Sec. 71.26(3)(x), Wis. Stats. (1987-88). Instead, each must file a separate 1989 Wisconsin franchise or income tax return and report its own income.

Is D Corporation required to recognize the gain on the distribution of appreciated property to E Corporation in 1989 for Wisconsin franchise or income tax purposes?

**Answer 2:** Yes. D Corporation must recognize the gain on the distribution of appreciated property to E Corporation in 1989. Although Wisconsin law excludes the consolidated return provisions from the Internal Revenue Code for the purpose of computing Wisconsin net income, Wisconsin law includes the provisions for the taxability of corporate distributions under IRC sec. 311(b). Therefore, the distributing corporation must recognize the gain on distributions of appreciated property, including distributions made to another member of an affiliated group, under IRC sec. 311(b) for Wisconsin purposes.



## FARMLAND TAX RELIEF CREDIT

### 1. Land on Which Farmland Tax Relief Credit Is Based

**Statutes:** Sections 71.07(3m), 71.28(2m), and 71.47(2m), Wis. Stats., as created by sections 1864m, 1966m, and 2045m, respectively, of 1989 Wisconsin Act 31.

**Note:** This Tax Release applies only with respect to farmland tax relief credit for property taxes accrued during 1989 and thereafter.

**Background:** To be eligible for farmland tax relief credit, a claimant or a member of the claimant's household must be an owner of 35 or more acres of farmland, as defined in secs. 71.07(3m)(a)3, 71.28(2m)(a)3, and 71.47(2m)(a)3, Wis. Stats., as created by 1989 Wisconsin Act 31. The farmland tax relief credit may be claimed on the following 1989 Wisconsin tax returns: Form 1, line 27; Form 1NPR, line 54; Form 2, line 17; Form 4, line 18; Form 4I, line 22; Form 4T, line 21; and Form 5, line 12.

**Question:** For purposes of qualifying for the farmland tax relief credit, must all of the farmland be adjoining?

**Answer:** No. For farmland tax relief credit purposes, "farmland" means 35 or more acres of Wisconsin land which is part of a farm that meets certain gross farm profits requirements or is in the Conservation Reserve Program. The statutes do not require that all of the land be adjoining.



## SALES/USE TAXES

### 1. Nexus Standards for Foreign Corporations That Are Publishers

**Statutes:** Sections 77.51(13g) and 77.53(3), Wis. Stats. (1987-88) and 77.51(13h) Wis. Stats. (1987-88), as amended by 1989 Act 336.

**A. Background:** Every "retailer engaged in business in this state" (i.e., a retailer who has nexus in Wisconsin for use tax) for purposes of use tax, is required to collect use tax from the purchaser on sales of tangible personal property or taxable services in Wisconsin (sec. 77.53(3), Wis. Stats. (1987-88)).

"Retailer engaged in business in this state" is defined in sec. 77.51(13g), Wis. Stats. (1987-88), and means any of the following (except as provided in sec. 77.51(13h), Wis. Stats.).

- Any retailer owning any real property in this state or leasing or renting out any tangible personal property located in this state or maintaining, occupying or using, permanently or temporarily, directly or indirectly, or through a subsidiary, or agent, by whatever name called, an office, place of distribution, sales or sample room or place, warehouse or storage place or other place of business in this state.
- Any retailer having any representative, agent, salesperson, canvasser or solicitor operating in this state under the authority of the retailer or its subsidiary for the purpose of selling, delivering or the taking of orders for any tangible personal property or taxable services.

**B. New Nexus Standards for Foreign Corporations That Are Publishers:** Section 77.51(13h), Wis. Stats., was created by 1987 Act 399 and amended by 1989 Act 336. As a result of 1987 Act