

item bills the administrator of Medicare claims for a taxable item, the portion billed to Medicare is not subject to Wisconsin sales or use tax.

The charge to Customer A of \$280 is subject to Wisconsin sales or use tax.

Facts and Question 3: Customer A purchases a hospital bed from Company B which sells for \$1,000. The approved Medicare amount for the hospital bed is \$900. Company B has signed an agreement to accept assignment on all Medicare claims. Company B files a claim with the administrator of Medicare claims for \$720 (\$900 X 80%) and bills Customer A \$180 (\$900 X 20%).

What are the Wisconsin sales and use tax implications of this transaction?

Answer 3: The charge to the administrator of Medicare claims for \$720 is not subject to Wisconsin sales or use tax.

The charge to Customer A for \$180 is subject to Wisconsin sales or use tax. This is true even though Company B may not collect the tax from Customer A because the Medicare program prohibits Company B from charging more than \$180 to Customer A.

Facts and Question 4: Assume the same facts as in Facts and Question 3. Can Company B reduce its gross receipts as a result of being prohibited from collecting the Wisconsin sales or use tax on the amount billed to Customer A thereby getting a credit for the sales tax that is uncollectable?

Answer 4: No. Sections 77.52(1) and 77.53(1), Wis. Stats. (1989-90), impose a sales or use tax on the retailer for tangible personal property sold, stored, used, or consumed in Wisconsin. Under sec. 77.52(3), Wis. Stats. (1989-90), a retailer may collect the tax from the consumer or user. There is no provision that allows the retailer to reduce its gross receipts for amounts it is unable to collect from the customer.

Section 77.51(4)(b)4, Wis. Stats. (1989-90), does provide for the reduction of gross receipts for accounts found to be worthless. If the customer pays the amount billed to him or her as provided under the assigned method, the account is not worthless even though the tax may not be collected from the customer. Therefore, the reduction under sec. 77.51(4)(b)4, Wis. Stats. (1989-90), does not apply.

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3. Real Property Leases Involving Tangible Personal Property

Statutes: Sections 77.51(13)(n) and 77.52(1), Wis. Stats. (1989-90)

Wis. Adm. Code: Sections Tax 11.29, June 1991 Register, and 11.48, March 1991 Register

Background: Section 77.52(1), Wis. Stats. (1989-90), imposes a sales tax on receipts from leasing or renting tangible personal prop-

erty at retail in Wisconsin. Special rules may apply when tangible personal property is included in a lease of real property.

Section 77.51(13)(n), Wis. Stats. (1989-90), provides that "retailer" includes a person selling household furniture, furnishings, equipment, appliances, or other items of tangible personal property to a landlord for use by tenants in leased or rented living quarters.

Facts and Question 1: A landlord rents furnished apartments for \$600 a month and unfurnished apartments for \$550 a month. In addition to a stove and refrigerator, which are provided in all apartments, living room and bedroom furniture are provided in furnished apartments. Is any portion of the landlord's rental receipts subject to sales tax?

Answer 1: No. The landlord's rental receipts are not subject to sales tax, even though a different amount is charged for furnished apartments. Section Tax 11.48(1)(a), Wis. Adm. Code, provides that the landlord is considered the consumer of the appliances and furniture and is subject to sales or use tax when purchasing these items.

Facts and Question 2: ABC Co. rents furniture, appliances, and other household items to persons who own their homes or live in apartments, and to landlords who use the items in residential rental property. Are ABC Co.'s rental receipts subject to sales tax?

Answer 2: Yes. ABC's receipts from the rental of furniture, appliances, and other household items are subject to sales tax.

Facts and Question 3: Restaurant Operator A decides to discontinue her business. She owns the building and trade fixtures (tangible personal property such as cooking equipment, coolers, and furniture). She will lease the entire business, including real property and tangible personal property, to Restaurant Operator B. Is any portion of Restaurant Operator A's lease receipts subject to sales tax?

Answer 3: Yes. The portion of the lease receipts attributable to the tangible personal property is subject to sales tax.

Note: Restaurant Operator A must hold a seller's permit for the collection and payment of sales tax on the taxable portion of the lease receipts.

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PRIVATE LETTER RULINGS

"Private letter rulings" are written statements issued to a taxpayer by the department that interpret Wisconsin tax laws to the taxpayer's specific set of facts. Any taxpayer may rely upon the ruling to the same extent as the requestor, provided the facts are the same as those set forth in the ruling.

The number assigned to each ruling is interpreted as follows: The "W" is for "Wisconsin," the first two digits are the year the ruling

becomes available for publication (80 days after the ruling is issued to the taxpayer), the next two digits are the week of the year, and the last three digits are the number in the series of rulings issued that year. The date following the 7-digit number is the date the ruling was mailed to the requestor.

Certain information contained in the ruling that could identify the taxpayer requesting the ruling has been deleted. Wisconsin Publication 111, "How to get a Private Letter Ruling From the Wisconsin Department of Revenue," contains additional information about private letter rulings.

W9146007, August 23, 1991

Type Tax: Individual Income

Statutes: Section 71.05(6)(a)1, Wis. Stats. (1989-90)

Issue: Interest Income — Federal Bonds — Stripped Certificates

This letter responds to your request for a Private Letter Ruling on behalf of Company A in regard to the tax status of income received by individuals and fiduciaries from Company A's stripped general obligation bond certificates ("ABC Certificates").

Facts

Company A wishes to sell ABC Certificates to certain individuals and fiduciaries residing in the State of Wisconsin. Company A wishes to represent to potential individual and fiduciary purchasers that the income received by them that is attributable to the ABC Certificates is exempt from Wisconsin state income taxation to the same extent that such income is excluded from gross income for federal income tax purposes.

ABC Certificates represent direct ownership interests in specific interest payments and principal payments attributable to certain District of Columbia general obligation bonds issued on or prior to January 28, 1987 (the "Bonds"). The Bonds have been issued by the District of Columbia pursuant to Section 661(a) of the District of Columbia Self-Government and Governmental Reorganization Act (the "Act"), as codified in D.C. Code Ann. §47-321(a). The interest income received by the holders of the Bonds is excluded from gross income for federal income tax purposes pursuant to Section 685 of the Act, as codified in D.C. Code Ann. §47-332.

An ABC Certificate is created when Company A purchases a District of Columbia general obligation bond issued on or prior to January 28, 1987, separates the interest and principal portions of the bond, and issues certificates representing the interest and principal portions of the bond. The Bonds, the interests in which the ABC Certificates represent, are held in the custody of Company A on behalf and for the benefit of the owners of the ABC Certificates.

ABC Certificates will be offered at discounts from their face amounts. Payments to the holders of the ABC Certificates will be made by Company A when the corresponding interest or principal payments on the Bonds are made. No payment will be made with respect to an ABC Certificate prior to the stated due date of the corresponding interest or principal payment on the Bonds (except in the case of certain

extraordinary events, such as a redemption of the Bonds), and no payment will be made with respect to an ABC Certificate from any sources other than those for which provision is made in the terms of the Bonds. The amount and nature of the income received by a holder of an ABC Certificate will be governed, for federal income tax purposes, by Section 685 of the Act and Section 1286 of the Internal Revenue Code of 1986, as amended.

Ruling Requested

You ask whether the income received by the individual and fiduciary holders of the ABC Certificates will be exempt from Wisconsin state income taxation to the same extent that such income is excluded from gross income for federal tax purposes.

Ruling

Income attributable to ABC Certificates received by any individual or fiduciary holders thereof is exempt from Wisconsin state income taxation.

Analysis

Wisconsin Administrative Code sec. Tax 3.095(4)(a) provides that interest payable on District of Columbia general obligation bonds issued on or prior to January 28, 1987, is exempt from the Wisconsin state income tax on individuals and fiduciaries (i.e., is not subject to the "add back" provisions of sec. 71.05(6)(a)1, Wis. Stats. (1989-90)), provided that the interest from such bonds qualifies for exemption from federal income taxation for a reason other than or in addition to Section 103 of the Internal Revenue Code.

As described above, any interest income on general obligation bonds issued by the District of Columbia under Section 661(a) of the Act is excluded from gross income for federal income tax purposes pursuant to Section 685 of the Act (D.C. Code Ann. §47-332). Therefore, such interest income is excluded from gross income for federal income tax purposes for a reason other than or in addition to Section 103 of the Internal Revenue Code. Any such interest income that is received by an individual or fiduciary on District of Columbia bonds issued on or before January 28, 1987 is thus exempt from Wisconsin state income taxation.

The question then becomes one of whether the tax-exempt status of the interest flows through the ABC Certificates. In *Capital Preservation Fund, Inc. et al. vs. Wisconsin Department of Revenue*, 145 Wis. 2d 841, 429 N.W. 2d 551 (1988), the Court of Appeals held that if a mutual fund invested solely in federal obligations, the dividends received by the individual investors in the mutual fund would be exempt from state taxation to the extent the dividends were attributable to interest from federal obligations. Thus, an individual did not need to own a federal obligation to receive the benefits of state tax exemption. An ownership interest in a mutual fund which invested in a federal obligation was enough to receive the benefits of state tax exemption.

In a situation analogous to the present case, the department took the position that the tax-exempt status of interest income attributable to United States Government obligations flowed through certain "proprietary zero-coupon certificates" issued with respect to "stripped"

United States Treasury notes and bonds. *Wisconsin Tax Bulletin*, No. 66, p. 12, Wisconsin Department of Revenue, April 1990. The "proprietary zero-coupon certificates" that were the focus of the above Wisconsin Tax Release (the "Tax Release") were described as certificates of ownership in United States Treasury obligation cash flows, which were created when a brokerage firm purchased a United States Treasury note or bond, "stripped" the note or bond (i.e., separated the interest and coupon portions of the obligation) and then issued certificates giving rights to the coupon and principal cash flows. The Tax Release stated that the investors purchasing such certificates were purchasing the right to receive an interest or principal payment from the Treasury obligation, but were not purchasing the actual Treasury obligation. The Tax Release held that "[t]he tax-exempt status of interest from U.S. Government obligations flows through the proprietary zero-coupon certificate."

ABC Certificates provide a situation analogous to that of the mutual funds and the "proprietary zero-coupon certificates". Because an ABC Certificate is a pass-through certificate, any income attributable to an ABC Certificate that is received by an individual or fiduciary is exempt from Wisconsin state income taxation to the extent that such income is excluded from gross income for federal income tax purposes for a reason other than or in addition to Section 103 of the Internal Revenue Code.

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W9148008, September 5, 1991

Type Tax: Individual Income

Statutes: Section 71.05(1)(a), Wis. Stats. (1989-90)

Issue: Federal Retirement Benefits

This letter is in response to your request for a private letter ruling regarding the initial date of the taxpayer's ("Taxpayer X") membership in the United States Civil Service Retirement System for purposes of taxability of retirement benefits attributable to such membership.

Facts

Taxpayer X had numerous periods of active military service between November 1943 and November 1965 and from July 17, 1970, through August 29, 1970. He was employed by the federal government in a civil service position from April 1966 until a reduction-in-force on July 16, 1970, at which time he did not withdraw his Civil Service Retirement contributions but left them on deposit with the Civil Service Retirement System. Taxpayer X was re-employed by the federal government in a civil service position from February 1971 through his retirement on July 31, 1990.

Taxpayer X made deposits in the Civil Service Retirement System for post-1956 periods of military service. Therefore, all periods of military service were considered "creditable service" under the Civil Service Retirement System.

Although Taxpayer X first became a federal civil service employe in April 1966, his service computation date is November 29, 1959. (The federal Standard Form 50-B submitted describes "service computation date" as the date when federal service began unless there is prior

creditable service. If this is the case, the date is constructed and reflects the total years, months and days of prior creditable civilian and military service.)

Ruling Request

You have requested a ruling that Taxpayer X's membership in the federal Civil Service Retirement System began on November 29, 1959, allowing Taxpayer X to exclude from Wisconsin taxable income payments received from the Civil Service Retirement System.

Ruling

Section 71.05(1)(a), Wis. Stats. (1989-90), excludes from Wisconsin taxation all payments received from the federal Civil Service Retirement System which are paid on the account of a person who was a member of the retirement system as of December 31, 1963. Based on the facts in this case, Taxpayer X was not a member of the Civil Service Retirement System as of December 31, 1963, and thus does not qualify for the exclusion provided by sec. 71.05(1)(a), Wis. Stats. (1989-90).

Analysis

The exclusion from income for payments received from certain retirement systems (including the federal Civil Service Retirement System) is provided in sec. 71.05(1)(a), Wis. Stats. (1989-90). To qualify for the exclusion, the payments must be made on the account of a person who was a member of, or retired from, one of the specified retirement systems as of December 31, 1963.

In this instance Taxpayer X is a member of the federal Civil Service Retirement System. He first became a federal civil service employe in April 1966, at which time amounts would have been withheld from his pay as a contribution to the Civil Service Retirement System. Thus membership in the retirement system was established at the time of employment.

Taxpayer X's pre-1964 active military service, however, does not grant him membership in the Civil Service Retirement System because such military service does not qualify him as an employe eligible to participate in this retirement system (5 USCS § 8331 (1)(A)).

Notwithstanding his failure to qualify as a member of the Civil Service Retirement System before 1964, Taxpayer X is using this pre-1964 (as well as post-1964) active military service as creditable service included in the computation of his annuity. The granting of creditable service alone does not establish membership in the Civil Service Retirement System during the period of service when the taxpayer and his employer were making no contributions to the system.

Furthermore, Taxpayer X's exercise of the right to make deposits to the Civil Service Retirement System for post-1956 periods of military service establishes creditable service to use toward calculating the annuity; its exercise does not establish membership in the retirement system.

Therefore, because Taxpayer X was not a member of the Civil Service Retirement System as of December 31, 1963, he does not qualify for the exclusion under sec. 71.05(1)(a), Wis. Stats. (1989-90).

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