

ownership of a limited partnership interest in ABC Limited Partnership which is doing business in Wisconsin. Ownership of an interest in a limited partnership that does business in Wisconsin does not establish nexus with Wisconsin under Wis. Adm. Code Sec. Tax 2.82.

**Facts - Situation 2:** GHI Limited Partnership does business in Wisconsin and 20 other states and reports its income on a calendar-year basis. JKL Limited Partnership, a calendar-year limited partnership organized under Delaware law that is not engaged in business in Wisconsin, owns a limited partnership interest in GHI Limited Partnership during 1991. Individuals throughout the United States are limited partners in JKL Limited Partnership.

**Question 2(a):** Does JKL Limited Partnership's interest in GHI Limited Partnership, which is doing business in Wisconsin, require JKL Limited Partnership to file a 1991 Wisconsin partnership return?

**Answer 2(a):** Yes. JKL Limited Partnership is required to file a 1991 Wisconsin partnership return. The net income of a partnership, except a publicly traded partnership, is computed under sec. 71.21(1), Wis. Stats. (1989-90), in the same manner and on the same basis as provided for computing the income of persons other than corporations. Since income from a limited partnership is classified as business income for persons other than corporations, JKL Limited Partnership is considered to have income from business transacted in Wisconsin.

**Question 2(b):** Are JKL Limited Partnership's nonresident individual limited partners required to file 1991 Wisconsin individual income tax returns?

**Answer 2(b):** Yes. The nonresident individual limited partners of JKL Limited Partnership are required to file Wisconsin individual income tax returns for their taxable year in which the partnership's 1991 year ends. They are subject to Wisconsin income tax on their distributive shares of JKL Limited Partnership's distributive share of GHI Limited Partnership's income derived from business transacted in Wisconsin.

**Facts - Situation 3:** MNO Limited Partnership does business in Wisconsin and 20 other states and reports its income on a calendar-year basis. PQR Limited Partnership, a calendar-year master limited partnership organized under Delaware law, is not engaged in business in Wisconsin. PQR Limited Partnership owns a limited partnership interest in MNO Limited Partnership during 1991. Investment units in PQR Limited Partnership are held by individuals throughout the United States. PQR Limited Partnership is taxed as a corporation for federal income tax purposes because it is a publicly traded partnership under sec. 7704 of the Internal Revenue Code (IRC). PQR's unit interest holders' distributions are taxed federally as if they are dividend income.

**Question 3(a):** Since PQR Limited Partnership is treated as a corporation for federal income tax purposes, is it also treated as a corporation for Wisconsin franchise and income tax purposes?

**Answer 3(a):** Yes. Since PQR Limited Partnership is treated as a corporation for federal income tax purposes, it is also treated as a corporation for Wisconsin franchise and income tax purposes, regardless of whether or not it has nexus in Wisconsin. The term "corporation," as defined in sec. 71.22(1), Wis. Stats. (1989-90), includes publicly traded partnerships treated as corporations in IRC sec. 7704. This definition applies to an entity regardless of whether or not it has nexus with Wisconsin.

**Question 3(b):** If PQR Limited Partnership is treated as a corporation for Wisconsin franchise and income tax purposes, must it file a 1991 Wisconsin franchise or income tax return?

**Answer 3(b):** No. PQR Limited Partnership is not required to file a Wisconsin franchise or income tax return. Because it is treated as a corporation, it does not have nexus with Wisconsin. The ownership of a limited partnership interest under these circumstances does not create nexus with Wisconsin.

**Question 3(c):** Are the individual limited partners owning interests in PQR Limited Partnership subject to Wisconsin individual income taxation on their distributive shares of the partnership income?

**Answer 3(c):** No. The nonresident individual limited partners owning interests in PQR Limited Partnership are not subject to Wisconsin individual income taxation since their partnership distributions are treated as dividends.



## TEMPORARY SURCHARGE

### 1. Deductibility of Temporary Surcharge

**Statutes:** Sections 71.05(6)(a)13, 71.07(5)(a)2, 71.22(4m), 71.26(1)(a), (2)(b), and (3)(g), 71.34(1)(ag), and 71.45(2)(a)5, Wis. Stats. (1989-90)

**Note:** The temporary surcharge applies to taxable years ending after April 1, 1991, and ending before April 1, 1999. For additional information about the temporary surcharge, refer to Publication 400, *Wisconsin's Temporary Surcharge*, which may be obtained from any Department of Revenue office.

**Background:** The Department of Revenue has received an opinion from the Internal Revenue Service (IRS) regarding the deductibility of the temporary surcharge that is imposed on certain corporations, exempt organizations, partnerships, individuals, estates, and trusts.

For federal income tax purposes, the IRS is going to treat the temporary surcharge as a state tax within the meaning of sec. 164(a) of the Internal Revenue Code (IRC). Therefore, it may be deducted from income as provided under sec. 164(a), IRC. The department has asked the Internal Revenue Service for further clarification of the federal treatment of the temporary surcharge by S corporations

and partnerships that have income which is classified under the federal passive activity loss rules as portfolio income, rental income, or passive activity income.

**Question:** Based on the IRS opinion, is the temporary surcharge paid deductible for Wisconsin franchise or income tax purposes?

**Answer:** Based on the information currently available, the Wisconsin treatment of the temporary surcharge paid is as follows:

Entity	Wisconsin Treatment
C corporations (except RICs, REITs, and REMICs)	Not deductible — add back to federal taxable income on Form 4 or 5, Schedule V. [sec. 71.26(3)(g), Wis. Stats.]
Exempt corporations	Deductible in computing Wisconsin unrelated business taxable income. [secs. 71.22(4m) and 71.26(1)(a), Wis. Stats.]
Insurance companies	Not deductible — add back to federal taxable income on Form 4I, Schedule A. [sec. 71.45(2)(a)5, Wis. Stats.]
RICs, REITs, and REMICs	Deductible in computing Wisconsin net income. [sec. 71.26(2)(b), Wis. Stats.]
S corporations	Not deductible — add back to federal income if deductible in computing federal income. Generally, add back to federal ordinary (nonseparately stated) income from trade or business activities on Form 5S, Schedule 5K, line 1, column c. [sec. 71.34(1)(ag), Wis. Stats.]
Partnerships	Deductible in computing Wisconsin ordinary income if deductible in computing federal ordinary income. If the partnership has only portfolio, rental, or passive activity income, the treatment is unknown.
Individuals	Not deductible and not includable in the itemized deduction credit. [sec. 71.07(5)(a)2, Wis. Stats.]
Estates and trusts	Not deductible — add back to federal taxable income on Form 2, Schedule A. [sec. 71.05(6)(a)13, Wis. Stats.]
Exempt estates and trusts	Not deductible — add back to federal unrelated business taxable income on Form 4T, Schedule V. [sec. 71.05(6)(a)13, Wis. Stats.]

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## 2. Estimated Temporary Surcharge Payments

**Statutes:** Section 77.96(2), Wis. Stats. (1989-90), as amended by 1991 Wisconsin Act 39

**Note:** The temporary surcharge applies to taxable years ending after April 1, 1991, and ending before April 1, 1999. For additional information about the temporary surcharge, refer to Publication 400, *Wisconsin's Temporary Surcharge*, which may be obtained from any Department of Revenue office.

**Background:** The temporary surcharge is due on the due date of the taxpayer's Wisconsin franchise or income tax return. Taxpayers subject to the temporary surcharge must make an estimated temporary surcharge payment if (a) an extension of time to file the Wisconsin franchise or income tax return has been granted, and (b) the unextended due date of that return is on or after December 1, 1991. The estimated payment must be based on 100% of the Wisconsin gross tax liability or 100% of the Wisconsin net business income, as appropriate, for the prior taxable year (or for the current taxable year, if less). Section 77.96(2), Wis. Stats. (1989-90), as amended by 1991 Wisconsin Act 39.

**Facts and Question 1:** Corporation X, which is incorporated during 1991 and elects to report its income on the basis of a calendar year, receives a 6-month extension of time until September 15, 1992, to file its 1991 Wisconsin franchise or income tax return. On its 1991 Wisconsin return, Corporation X reports a Wisconsin gross tax liability of \$10,000 and a temporary surcharge of \$550 (\$10,000 x 5.5%).

Is Corporation X required to make an estimated temporary surcharge payment for 1991 and, if so, how is the payment computed?

**Answer 1:** Yes. Corporation X must make an estimated temporary surcharge payment because it received an extension of time to file its Wisconsin franchise or income tax return and the due date of that return (March 15, 1992) is after December 1, 1991. Since Corporation X did not have a tax liability for the prior taxable year, it must make an estimated temporary surcharge payment of \$25, which is the minimum temporary surcharge payment based on a 1990 zero gross tax, by March 15, 1992. The balance of the temporary surcharge (\$525) must be paid when Corporation X files its return or September 15, 1992, whichever occurs first.

**Facts and Question 2:** Corporation Y, which has done business in Wisconsin since 1980 and reports its income on a calendar-year basis, elects to become a tax-option (S) corporation for its taxable year beginning January 1, 1991. Corporation Y receives a 6-month extension of time until September 15, 1992, to file its 1991 Wisconsin franchise or income tax return. For the 1990 taxable year, Corporation Y had Wisconsin net income of \$1,000,000, and a Wisconsin gross tax liability of \$79,000. On its 1991 Wisconsin tax-option (S) corporation return, Corporation Y reports Wisconsin net income of \$1,500,000 and a temporary surcharge of \$6,518 (\$1,500,000 x 0.4345%).

Is Corporation Y required to make an estimated temporary surcharge payment and, if so, how is the payment computed?

**Answer 2:** Yes. Corporation Y is required to make an estimated temporary surcharge payment because it received an extension of time to file its 1991 Wisconsin franchise or income tax return and the due date of that return (March 15, 1992) is after December 1, 1991. Since Corporation Y had income for the prior taxable year, its required estimated payment is \$4,345, which is 0.4345% of its 1990 Wisconsin net income (or 5.5% of its 1990 Wisconsin gross tax). The balance of the temporary surcharge (\$2,173) must be paid when Corporation Y files its return or September 15, 1992, whichever occurs first.

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## 3. Temporary Surcharge - Computation of Net Business Income of Individuals

**Statutes:** Section 77.93(2), Wis. Stats. (1989-90), as amended by 1991 Wisconsin Act 39, secs. 77.92(4) and 77.93(5), Wis. Stats., as created by 1991 Wisconsin Act 39, and sec. 77.94(1)(b) and (c), as repealed and recreated by 1991 Wisconsin Act 39.

**Note:** The temporary surcharge applies to taxable years ending after April 1, 1991, and ending before April 1, 1999. For additional information about the temporary surcharge, refer to Publication 400, *Wisconsin's Temporary Surcharge*, which may be obtained from any Department of Revenue office.

**Background:** Individuals who must file a Wisconsin income tax return and who have a profit or loss from a trade or business, not including farming, for federal income tax purposes are subject to the temporary surcharge. Section 77.93(2), Wis. Stats., as amended by 1991 Wisconsin Act 39. The temporary surcharge is the greater of \$25 or 0.4345% of net business income, but not more than \$9,800. Section 77.94(1)(b), Wis. Stats., as repealed and recreated by 1991 Wisconsin Act 39. "Net business income" means profit from a trade or business for federal income tax purposes. Section 77.92(4), Wis. Stats., as created by 1991 Wisconsin Act 39.

Individuals engaged in farming are subject to a temporary surcharge of \$25, if they have a net farm profit of at least \$1,000. Section 77.93(5), Wis. Stats., as created by 1991 Wisconsin Act 39, and sec. 77.94(1)(c), Wis. Stats., as repealed and recreated by 1991 Wisconsin Act 39.

**Facts and Question:** Taxpayer B operates a bookstore as a sole proprietor. For 1991, she reports \$50,000 of net profit from the business on federal Schedule C, line 31. She is required to pay \$7,065 of federal self-employment tax based on her business income. During 1991, Taxpayer B pays \$4,000 for health insurance for herself.

When computing her federal adjusted gross income, Taxpayer B may deduct \$3,533, which is 50% of the federal self-employment taxes imposed for the taxable year, on federal Form 1040, line 25.

Section 164(f), Internal Revenue Code (IRC). In addition, she may deduct \$1,000, which is 25% of her health insurance premiums, on Form 1040, line 26. Section 162(l), IRC.

For purposes of the temporary surcharge, is Taxpayer B's net income from a trade or business reduced by the deductions for 50% of her self-employment tax liability and 25% of her health insurance premiums?

**Answer:** Yes. Section 164(f)(2), IRC, provides that the deduction for one-half of the self-employment taxes is treated as attributable to a trade or business carried on by the taxpayer. One-fourth of the health insurance costs of self-employed individuals, with certain limitations, are deductible as an ordinary and necessary business expense under sec. 162(l), IRC. Therefore, for purposes of computing the temporary surcharge, the net income from a trade or business is reduced by the deductions for 50% of the federal self-employment taxes paid and 25% of the health insurance premiums paid.

Taxpayer B's net business income is \$45,467 (\$50,000 - \$3,533 - \$1,000). Therefore, she must pay a temporary surcharge of \$198 (\$45,467 x 0.4345%).

**Note:** Net farm profit is also reduced by the deductions allowable under IRC secs. 162(l) and 164(f) for health insurance premiums and self-employment taxes paid.



#### 4. Temporary Surcharge - Exempt Organization Having No Unrelated Business Taxable Income for the Current Taxable Year

**Statutes:** Section 77.93(1), Wis. Stats. (1989-90), as amended by 1991 Wisconsin Act 39

**Note:** The temporary surcharge applies to taxable years ending after April 1, 1991, and ending before April 1, 1999. For additional information about the temporary surcharge, refer to Publication 400, *Wisconsin's Temporary Surcharge*, which may be obtained from any Department of Revenue office.

**Background:** Tax-exempt organizations that have unrelated business taxable income as defined in sec. 512 of the Internal Revenue Code (IRC) and that must file Wisconsin unrelated business franchise or income tax returns, Form 4T, are subject to the temporary surcharge. Sec. 77.93(1), Wis. Stats. (1989-90), as amended by 1991 Wisconsin Act 39.

**Facts and Question:** Organization X is an exempt organization taxable as a corporation that reports its income on a calendar-year basis. For 1990, Organization X was required to file a Wisconsin unrelated business franchise or income tax return, Form 4T, because it had more than \$1,000 of gross income (gross receipts less the cost of goods sold) from an unrelated trade or business. It computed a net loss from its unrelated trade or business for both

federal and Wisconsin purposes in 1990. For 1991, Organization X does not have any income from an unrelated trade or business. However, it files a 1991 Wisconsin tax return to report its net operating loss carryover.

Is Organization X subject to the temporary surcharge for the 1991 calendar year?

**Answer:** No. Organization X is not subject to the temporary surcharge for the 1991 calendar year. It is not required to file a 1991 Wisconsin return since it does not have at least \$1,000 of gross income from an unrelated trade or business. See secs. 511 and 512, IRC, and secs. 71.24(1m) and 71.26(1)(a), Wis. Stats. (1989-90). Therefore, even though it files a Wisconsin tax return for informational purposes, Organization X is not subject to the temporary surcharge.

**Note:** If Organization X had at least \$1,000 of gross income from an unrelated trade or business for 1991, but the net operating loss carryover reduced its net income to zero, it would be subject to the \$25 minimum temporary surcharge for 1991.



#### 5. Temporary Surcharge - Members of Certain Religious Groups Who Are Exempt From Federal Self-Employment Tax

**Statutes:** Section 77.93(2), Wis. Stats. (1989-90), as amended by 1991 Wisconsin Act 39, and secs. 77.92(4) and 77.93(5), Wis. Stats., as created by 1991 Wisconsin Act 39.

**Note:** The temporary surcharge applies to taxable years ending after April 1, 1991, and ending before April 1, 1999. For additional information about the temporary surcharge, refer to Publication 400, *Wisconsin's Temporary Surcharge*, which may be obtained from any Department of Revenue office.

**Background:** Individuals who must file a Wisconsin income tax return and who have a profit or loss from a trade or business, not including farming, for federal income tax purposes are subject to the temporary surcharge. Section 77.93(2), Wis. Stats., as amended by 1991 Wisconsin Act 39. A trade or business is an activity regularly carried on for a livelihood or with the intention of making a profit. Trade or business income includes income, other than from farming, which is subject to federal self-employment tax. Section 77.92(4), Wis. Stats., as created by 1991 Wisconsin Act 39, and sec. 77.93(2), Wis. Stats., as amended by 1991 Wisconsin Act 39. Individuals engaged in farming are subject to a temporary surcharge of \$25, if they have a net farm profit of at least \$1,000. Section 77.93(5), Wis. Stats., as created by 1991 Wisconsin Act 39, and sec. 77.94(1)(c), Wis. Stats., as repealed and recreated by 1991 Wisconsin Act 39.

**Facts and Question 1:** Taxpayer A operates a bakery as a sole proprietorship. He is a member of a recognized religious group that has conscientious objections to any private or public insurance

which makes payments on account of death, disability, old age, or retirement or makes payments toward the cost of, or provides services for, medical care (including social security benefits). Taxpayer A files federal Form 4029, Application for Exemption From Social Security and Medicare Taxes and Waiver of Benefits, and receives the Internal Revenue Service's approval to be exempt from social security and Medicare taxes.

Is Taxpayer A subject to the temporary surcharge?

**Answer 1:** No. For purposes of the temporary surcharge, "trade or business" is defined in sec. 1402(c) of the Internal Revenue Code (IRC), relating to the federal self-employment tax. Generally, individuals who are exempt from self-employment tax (other than certain statutory employees) are not considered to have trade or business income for purposes of the temporary surcharge. Since IRC sec. 1402(g) provides an exemption from self-employment tax for members of certain recognized religious groups, their income is not treated as trade or business income. Therefore, Taxpayer A is not subject to the temporary surcharge.

**Facts and Question 2:** Taxpayer B, who is engaged in farming as a sole proprietorship, has a net farm profit of \$5,000 for calendar year 1991. He files federal Form 4029 and receives the Internal Revenue Service's approval to be exempt from social security and Medicare taxes because he is a member of a recognized religious group that is conscientiously opposed to private or public insurance.

Is Taxpayer B subject to the temporary surcharge?

**Answer 2:** Yes. For purposes of the temporary surcharge imposed on noncorporate farms, "farming" is defined in IRC sec. 464(e)(1). Section 77.92(1), Wis. Stats. (1989-90). That Code section does not refer to a definition of a trade or business, and the definition of "trade or business" in IRC sec. 1402(c) does not apply to farming. Therefore, an individual who is engaged in the business of farming is not exempted from the temporary surcharge just because he or she is exempt from federal self-employment tax. Since Taxpayer B has at least \$1,000 of net farm profit, he is subject to the \$25 temporary surcharge imposed on individuals engaged in farming.



## 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.*

The following rulings are included:

**W9202001, October 18, 1991**

**Type Tax:** Sales/Use

**Statutes:** Sections 77.51(14) and 77.52(1), (2)(a)10, and (2m), Wis. Stats. (1989-90)

**Issue:** Computer software

This letter responds to your request for a private letter ruling regarding the Wisconsin sales and use tax implications of the sale of computer software.

### Facts

Corporation A is an affiliate of a trade association. It sells forms developed by the trade association.

In order to make these forms available to institutions through an automated loan origination system, Corporation A has entered into an agreement with the owner of a software product to integrate the standard forms which Corporation A sells into its software. The integrated software is called "Link B."

The Link B software, without further modifications, will only produce a particular set of forms consisting of the standard forms which Corporation A sells. Nearly all of the purchasers of Link B use some forms in addition to, or in place of, these standard forms.

In order to accommodate customers' desires to customize the loan document package which the software will produce, Corporation A will modify the Link B software for the customer. Corporation A will charge the customer for the basic Link B software plus a fee for making modifications, based on an hourly rate for the time involved.

The cost of a Link B software varies, depending upon whether it is installed on a single computer or a network system and the extent of modifications made for the customer.

Corporation A installs or assists the customer in installing the software on the customer's computer system and tests or assists the customer in testing to ensure it works properly.

A diskette with a copy of the program is provided to the customer, primarily as a backup. User manuals are also provided to the customer. There is no separate charge for the backup diskettes or manuals.