

To make the election, Corporation Y must take the following action on or before October 15, 1995:

- File Wisconsin Form 5E, "Election by an S Corporation Not to Be Treated as a Tax-Option (S) Corporation," and
- File an amended Wisconsin franchise or income tax return, Form 4 or 5, as a regular (C) corporation.

Once a Wisconsin return has been filed in accordance with the "opt-out" election, the election is completed and remains effective for the corporation and its successors for at least the next 4 taxable years after the taxable year to which the election first applies.

Facts and Question 6: Corporation Z, which was organized under Virginia law and is engaged in business solely in Virginia, elects to be treated as an S corporation for federal income tax purposes. Individual A, a full-year Wisconsin resident, owns 75% of the stock of Corporation Z. Corporation Z files its federal S corporation income tax returns on a calendar year basis. Corporation Z is not required to file Wisconsin franchise or income tax returns because it does not have nexus with Wisconsin.

May Corporation Z elect not to be a tax-option (S) corporation for Wisconsin franchise and income tax purposes?

Answer 6: Yes. Corporation Z may elect out of Wisconsin tax-option (S) corporation status with the consent of persons who hold more than 50% of the shares of the corporation on the day on which the election is made. To make the election, Corporation Z must file Form 5E, "Election by an S Corporation Not to Be Treated as a Tax-Option (S) Corporation," by the

due date, including extensions, for filing its federal income tax return. After the due date for filing the federal return has passed, the "opt-out" election cannot be withdrawn, and it remains effective for the corporation and its successors for at least the next 4 taxable years after the taxable year to which the election first applies.

Note: If Corporation Z opts out of Wisconsin tax-option (S) status, Individual A calculates his Wisconsin adjusted gross income and Wisconsin itemized deduction credit by excluding all items of S corporation income, loss, and deduction that were included in his federal taxable income and including in income taxable dividends received from the corporation. □

7 Tax-Option (S) Corporation's Treatment of Certain Exempt Bond Interest

Statutes: Sections 71.34(1) and 71.36(1m), Wis. Stats. (1993-94)

Wis. Adm. Code: Section Tax 3.095, January 1994 Register

Background: For the 1987 taxable year and thereafter, Wisconsin treats tax-option (S) corporations as pass-through entities, the same as for federal purposes. Items of income, loss, and deduction retain their character as business income or loss but pass through to the shareholders and are included in the shareholders' returns as if received or accrued, paid or incurred, directly by the shareholders.

A tax-option (S) corporation may deduct from its net income all amounts included in the Wisconsin adjusted gross income of its shareholders, the capital gain deduction under sec. 71.05(6)(b)9, Wis. Stats., and all amounts not taxable to nonres-

ident shareholders under secs. 71.04(1) and (4) to (9) and 71.362, Wis. Stats. For purposes of the tax-option corporation deduction, interest on federal obligations is not included in shareholders' income. Section 71.36(1m), Wis. Stats. (1993-94). As a result, tax-option (S) corporations are subject to Wisconsin franchise tax measured by the amount of interest and dividend income received from obligations of the United States government and its instrumentalities, which is allocable to Wisconsin.

Facts and Question: In addition to interest and dividends from U.S. government obligations, interest income on certain bonds issued by the government of Puerto Rico, other U.S. territories and possessions, and state and local governments is exempt from the Wisconsin individual income tax. See section Tax 3.095, Wis. Adm. Code for a list of exempt securities.

Is a tax-option (S) corporation subject to Wisconsin franchise tax measured by interest income on bonds issued by the government of Puerto Rico, other U.S. territories and possessions, and state and local governments when that interest is exempt from the Wisconsin individual income tax?

Answer: No. Although sec. 71.36(1m), Wis. Stats. (1993-94), requires a tax-option (S) corporation to include interest income on federal obligations in its taxable income for corporate franchise tax purposes, the Wisconsin Legislature has not specifically authorized the inclusion in the corporation's taxable income of interest income on bonds issued by the government of Puerto Rico, other U.S. territories and possessions, and state and local governments when that interest is exempt from the Wisconsin individual income tax. □

SALES AND USE TAXES

Note: The following tax releases interpret the Wisconsin sales and use tax law as it applies to the 5% state sales and use tax. The ½% county sales and use tax may also apply. For information on sales or purchases that are subject to the county sales and use tax, refer to the January 1995 issue of the Sales and Use Tax Report. A copy can be found in *Wisconsin Tax Bulletin* 90 (January 1995), pages 39 to 42.

8 Claims for Refund — Construction Activities

Note: This tax release applies to claims for refund of sales or use tax filed on or after September 1, 1994.

Statutes: Sections 77.51(2), 77.52(1) and (2)(a)10, and 77.59(4)(a) and (c), Wis. Stats. (1993-94)

Background: Section 77.59(4)(a), Wis. Stats. (1993-94), provides that a buyer or seller may file a claim for refund with the Department of Revenue for sales or use tax paid in error to a seller or the department if certain conditions are met.

Section 77.59(4)(c), Wis. Stats. (1993-94), provides that a seller who receives a refund of sales or use tax from the Department of Revenue that the seller has collected from buyers shall return the taxes and related interest to the buyers from whom the taxes were collected. The seller shall return to the Department of Revenue any part of a refund that the seller does not return to a buyer. Failure by the seller to return the refund to a buyer or the department may result in penalties.

Facts and Questions 1: Contractor A sells and installs a furnace in the home of Individual B. This transaction is a real property improvement.

However, Contractor A incorrectly assumes that the furnace is tangible personal property when installed and invoices Individual B as follows:

Materials	\$1,000
Labor	750
Subtotal	\$1,750
Sales Tax (\$1,750 x 5%)	88
Amount Due	<u>\$1,838</u>

Individual B pays the contractor \$1,838. Subsequently, Individual B files with the Department of Revenue a timely claim for refund for the \$88 of sales tax it paid to the contractor on the real property improvement. The claim is properly completed and filed on forms prescribed by the Department of Revenue.

Will the Department of Revenue refund the \$88 of tax plus applicable interest to Individual B under sec. 77.59(4)(a), Wis. Stats. (1993-94)?

Answer 1: Yes. Note, however, that Contractor A is liable for Wisconsin use tax on its purchase price of the materials (e.g., furnace) used in the real property improvement.

Facts and Question 2: Contractor A invoices Individual B for the sale and installation of cabinets in Individual B's home. This transaction is a real property improvement. Contractor A purchased the materials it used in installing the cabinets (e.g., cabinets, handles, hinges, etc.) without Wisconsin sales or use tax. Contractor A invoices Individual B for the sale and installation of the cabinets as follows:

Materials	
(\$1,200 cost + markup)	\$1,500
Labor	800
Subtotal	\$2,300
Sales Tax (\$2,300 x 5%)	115
Amount Due	<u>\$2,415</u>

Later, Contractor A determines it incorrectly charged Individual B Wisconsin sales tax on the sale and installation of the cabinets.

The sales tax paid in error on the sale of the cabinets by Contractor A to Individual B is \$115. Use tax of \$60 (\$1,200 X 5%) is due from Contractor A on the purchase price of the materials it used in installing the cabinets. The department issues a net refund of \$55 (\$115 - \$60), plus interest, to Contractor A.

What is the amount of refund and interest Contractor A must pass on to Individual B under sec. 77.59(4)(c), Wis. Stats. (1993-94)?

Answer 2: Contractor A is required to return to Individual B the \$115 of sales tax collected from Individual B in error, even though the net refund by the department to Contractor A was \$55. Contractor A must also remit to Individual B interest related to the \$115 of sales tax being refunded to Individual B. Interest is refunded at 9%, under sec. 77.60(1), Wis. Stats. (1993-94), from the due date of Contractor A's sales and use tax return for the period in which the sale and installation occurred to the date the refund was issued by the department to Contractor A. □

9 Claims for Refund — Seller With Tax Delinquency

Note: This tax release applies to claims for refund of sales or use tax filed on or after September 1, 1994.

Statutes: Section 77.59(4)(a) and (c) and (5), Wis. Stats. (1993-94)

Background: Section 77.59(5), Wis. Stats. (1993-94), provides in part that the department **may** offset the amount of any refund for a period, together with interest on the refund, against deficiencies for another period, and against penalties and interest on the deficiencies, or against any amount of whatever kind, due and owing on the books of the department from the person claiming the refund.

Facts and Question 1: Seller A requests a refund from the Department of Revenue for sales tax collected from buyers on sales that were not subject to tax. Seller A has provided with its claim for refund a list of the buyers who were incorrectly charged sales tax.

Seller A has a delinquency with the Department of Revenue for unpaid sales tax.

Will the department refund the tax and interest to Seller A under sec. 77.59(4)(a), Wis. Stats. (1993-94), or use the refund to offset Seller A's delinquency under sec. 77.59(5), Wis. Stats. (1993-94)?

Answer 1: Under sec. 77.59(5), Wis. Stats. (1993-94), the Department of Revenue has the option of issuing the refund to the seller or offsetting the seller's delinquency. In this situation, the Department of Revenue will refund the tax and related interest to the seller so that the seller can pass the refund on to the buyers.

Note: The Department of Revenue may not issue the refund directly to a buyer unless the buyer has filed a claim for refund with the Department of Revenue.

Caution: Under sec. 77.54(4)(c), Wis. Stats. (1993-94), if a seller is refunded tax and interest by the Department of Revenue for tax collected from a buyer, and the seller fails to return the tax and related interest to the buyer or the department due to negligence, the seller is subject to a penalty of 25% of the amount not returned. If a seller fails to return the tax and related interest to the buyer or the department due to fraud, the seller is subject to a penalty of 100% of the amount not returned.

Facts and Question 2: Seller A requests a refund from the Depart-

ment of Revenue for use tax it paid to the Department of Revenue on a purchase that was not subject to tax. Seller A has a delinquency with the Department of Revenue for unpaid sales tax.

Will the department refund the tax and interest to Seller A under sec. 77.59(4)(a), Wis. Stats. (1993-94), or use the refund to offset Seller A's delinquency under sec. 77.59(5), Wis. Stats. (1993-94)?

Answer 2: The Department of Revenue will use the refund to offset Seller A's delinquency. (**Note:** In this situation, the tax refunded to Seller A was not collected from a buyer.) □

10 Claims for Refund — Time Limitations

Note: This tax release replaces the tax releases on claims for refund of sales or use tax that appeared in *Wisconsin Tax Bulletins* 49 (January 1987), pages 13 to 15, and 69 (October 1990), pages 22 to 25, and *Tax Report* articles on claims for refund of sales or use tax appearing in issues dated June 1975, June 1980, and September 1984.

This tax release applies to claims for refund filed with the Department of Revenue on or after September 1, 1994.

This tax release only addresses time limitations for filing claims for refund of sales or use tax by a seller or buyer. Other information on filing claims for refund, such as which form to use, offsets, etc., may be found in Wisconsin Publication 216, *Filing Claims for Refund of Sales or Use Tax*.

Statutes: Section 77.59(3m), (4), (6), and (8m), Wis. Stats. (1993-94)

Background: Section 77.59(3m), (4), and (8m) of the Wisconsin Statutes contain provisions regarding the time in which a claim for refund of sales or use tax may be filed by a seller or buyer.

The following information sets forth the time limitations for filing a claim for refund. The time limitations depend on whether the seller or buyer was audited by the department. The information is separated between claims for refund by a seller and claims for refund by a buyer.

Note: A claim for refund of a seller or buyer that is mailed is timely filed if (1) it is mailed in a properly addressed envelope with the postage duly prepaid, (2) the envelope is postmarked before midnight of the last day of the limitation period, and (3) the claim for refund is received by the Department of Revenue within 5 days after the last day of the limitation period.

Claims for Refund by Seller:

A. No Office Audit Determination Was Made for the Transaction and No Field Audit Determination Was Made for Period of Claim (sec. 77.59(4)(a), Wis. Stats. (1993-94))

If the transaction in the claim for refund (1) was not included in a prior office audit determination and (2) was not in the periods or years included in a prior field audit determination (neither (1) nor (2) occurred), claims for refund may be filed as follows:

- within 4 years after the unextended due date of the seller's Wisconsin income or franchise tax return, or
- if exempt from filing Wisconsin income or franchise tax returns, within 4 years of the 15th day of

the 4th month of the year following the close of the calendar or fiscal year.

Example: Seller J, an individual, overpaid sales tax to the Department of Revenue on her January 1994 sales and use tax return. The unextended due date of Seller J's 1994 income tax return is April 15, 1995.

Seller J has until April 15, 1999 to file a claim for refund for the overpaid sales tax reported on her January 1994 sales and use tax return.

B. Office Audit Determination Was Made for the Transaction (sec. 77.59(4)(b), Wis. Stats. (1993-94))

Claims for refund of the tax assessed by an office audit may be filed within two years of the issuance of the notice of determination of sales or use tax assessed by office audit, if the seller paid the tax and the tax was not protested by filing a petition for redetermination.

Example: In an office audit determination dated and issued July 15, 1994, the Department of Revenue assessed Seller K \$800 of sales tax on equipment Seller K sold to Buyer L in June 1992. Seller K paid the \$800 of sales tax on July 31, 1994, and did not file a petition for redetermination.

In January 1995, Buyer L provides Seller K with an exemption certificate, claiming the manufacturing exemption on the equipment.

Seller K has until July 15, 1996 (two years from the date the notice of office audit determination was issued) to file a claim for refund with the Department of Revenue for the \$800 of tax, since the overpaid tax was part of the July 15, 1994 office audit determination.

C. Field Audit Determination Was Made for Period of Claim

If the transaction occurred during the period or years included in a prior field audit determination, the time limitations for filing a claim for refund for such transaction are as follows:

1. **Transaction Not Assessed in Field Audit Determination** (sec. 77.59(4)(a), Wis. Stats. (1993-94))

a. *Field Audit Not Appealed to Department's Appellate Bureau*

Seller has until the earliest of the following to file a claim for refund:

- Four years from the unextended due date of the seller's income or franchise tax return or if exempt from filing Wisconsin income or franchise tax returns, within 4 years of the 15th day of the 4th month of the year following the close of the calendar or fiscal year (or date extended by waiver under sec. 77.59(3m), Wis. Stats. (1993-94)).
- Date the amount of the notice of determination is paid.
- 60 days after the date the seller received the notice of determination.

b. *Field Audit Determination Appealed to Department's Appellate Bureau, But Not to Wisconsin Tax Appeals Commission*

Seller has until the earliest of the following to file a claim for refund:

Four years from the unextended due date of the seller's income or franchise tax return or if exempt from filing Wisconsin income or franchise tax returns, within 4 years of the 15th day of the 4th month of the year following the close of the calendar or fiscal year (or date extended by waiver under sec. 77.59(3m), Wis. Stats. (1993-94)).

- Date the amount of the notice of determination is paid (this does not include deposits of tax under sec. 77.59(6)(c), Wis. Stats. (1993-94), while appeal is pending).
 - 60 days after the date the seller received the Appellate Bureau's notice of redetermination.
- c. *Seller Appeals Field Audit Determination to Wisconsin Tax Appeals Commission or Court*

Seller has until the earliest of the following to file a claim for refund:

- Four years from the unextended due date of the seller's income or franchise tax return or if exempt from filing Wisconsin income or franchise tax returns, within 4 years of the 15th day of the 4th month of the year following the close of the calendar or fiscal year (or date extended by waiver under sec. 77.59(3m), Wis. Stats. (1993-94)).
- Date the amount of the notice of determination is paid (this does not include deposits of tax under sec. 77.59(6)(c), Wis. Stats. (1993-94), while appeal is pending).

- 60 days after the date the seller received the Appellate Bureau's notice of redetermination, even though seller files the appeal with the Wisconsin Tax Appeals Commission before the 60 days have expired.
2. Transaction Assessed in Field Audit Determination (sec. 77.59(4)(b), Wis. Stats. (1993-94))

Claims for refund of the tax assessed by a field audit may be filed within two years of the issuance of the notice of determination of sales or use tax assessed by field audit, if the seller paid the tax and the tax was not protested by filing a petition for redetermination.

Example: Seller O is field audited by the Department of Revenue for the period January 1991 through December 1994, and is assessed \$5,000 of sales tax on sales made by Seller O. The notice of determination is dated and issued April 5, 1995.

Seller O pays the \$5,000 of sales tax on April 20, 1995, and does not file a petition for redetermination.

Seller O has until April 5, 1997, to file a claim for refund with the Department of Revenue for all or part of the \$5,000 of sales tax assessed.

D. Field Audit Determination Was Made and Customer Files Valid Claim With Seller (sec. 77.59(8m), Wis. Stats. (1993-94))

Even though a seller has been field audited, claims for refund may be filed within 4 years after the unextended due date of the seller's Wisconsin income or franchise tax return, or if exempt from filing Wisconsin

income or franchise tax returns, within 4 years of the 15th day of the 4th month of the year following the close of the calendar or fiscal year, if the seller's customers have filed valid claims for refund with the seller.

Example: Seller Q, a sole proprietor, is field audited by the Department of Revenue for the period January 1991 through December 1994. Seller Q is assessed \$2,000 of use tax on equipment purchased by Seller Q from vendors located outside Wisconsin. The notice of field audit determination is dated and issued June 10, 1995. Seller Q does not file a petition for redetermination.

Seller Q files its income tax return on a calendar year basis.

In November 1995, Seller Q receives a request from a church for a refund of \$500 of sales tax which it charged to the church on landscaping services provided by Seller Q in July 1993. The church has provided Seller Q with its certificate of exempt status number. Seller Q reported the \$500 of tax on its July 1993 sales and use tax return.

Since Seller Q reported the \$500 of tax on its July 1993 sales and use tax return, Seller Q has until April 15, 1998 (four years from the unextended due date of its 1993 income tax return), to file a refund claim with the Department of Revenue for the \$500 of sales tax.

Claims for Refund by Buyer — Tax Paid to Department of Revenue:

A. No Office Audit Determination Was Made for the Transaction and No Field Audit Determination Was Made for Period of the Claim (sec. 77.59(4)(a), Wis. Stats. (1993-94))

If the transaction in the claim for refund (1) was not included in a prior

office audit determination and (2) was not in the periods or years included in a prior field audit determination (neither (1) nor (2) occurred), claims for refund may be filed as follows:

- within 4 years after the unextended due date of the buyer's Wisconsin income or franchise tax return, or,
- if exempt from filing Wisconsin income or franchise tax returns, within 4 years of the 15th day of the 4th month of the year following the close of the calendar or fiscal year.

Example: Buyer J, an individual, overpaid use tax to the Department of Revenue on its January 1994 sales and use tax return. The unextended due date of Buyer J's 1994 income tax return is April 15, 1995.

Buyer J has until April 15, 1999 to file a claim for refund for the overpaid use tax reported on the January 1994 sales and use tax return.

B. Office Audit Determination Was Made for the Transaction (sec. 77.59(4)(b), Wis. Stats. (1993-94))

Claims for refund of the tax assessed by an office audit may be filed within two years of the issuance of the notice of determination of sales or use tax assessed by office audit, if the buyer paid the tax and the tax was not protested by filing a petition for redetermination.

Example: In an office audit determination dated and issued July 15, 1994, the Department of Revenue assessed Buyer K \$800 of use tax on equipment Buyer K purchased in June 1992. Buyer K paid the \$800 of use tax on July 31, 1994, and did not file a petition for redetermination.

Buyer K has until July 15, 1996 (two years from the date the notice of office audit determination was issued) to file a claim for refund with the Department of Revenue for the \$800 of tax, since the tax was part of the July 15, 1994 office audit determination.

C. Field Audit Determination Was Made for Period of Claim

If the transaction occurred during the period or years included in a prior field audit determination, the time limitations for filing a claim for refund for such transaction are as follows:

1. Transaction Not Assessed in Field Audit Determination (sec. 77.59(4)(a), Wis. Stats. (1993-94))

a. Field Audit Not Appealed to Department's Appellate Bureau

Buyer has until the earliest of the following to file a claim for refund:

- Four years from the unextended due date of the buyer's income or franchise tax return or if exempt from filing Wisconsin income or franchise tax returns, within 4 years of the 15th day of the 4th month of the year following the close of the calendar or fiscal year (or date extended by waiver under sec. 77.59(3m), Wis. Stats. (1993-94)).
- Date the amount of the notice of determination is paid.
- 60 days after the date the buyer received the notice of determination.

b. Field Audit Determination Appealed to Department's

Appellate Bureau, But Not to Wisconsin Tax Appeals Commission

Buyer has until the earliest of the following to file a claim for refund:

- Four years from the unextended due date of the buyer's income or franchise tax return or if exempt from filing Wisconsin income or franchise tax returns, within 4 years of the 15th day of the 4th month of the year following the close of the calendar or fiscal year (or date extended by waiver under sec. 77.59(3m), Wis. Stats. (1993-94)).

- Date the amount of the notice of determination is paid (this does not include deposits of tax under sec. 77.59(6)(c), Wis. Stats. (1993-94), while appeal is pending).

- 60 days after the date the buyer received the Appellate Bureau's notice of redetermination.

c. Buyer Appeals Field Audit Determination to Wisconsin Tax Appeals Commission or Court

Buyer has until the earliest of the following to file a claim for refund:

- Four years from the unextended due date of the buyer's income or franchise tax return or if exempt from filing Wisconsin income or franchise tax returns, within 4 years of the 15th day of the 4th month of the year

following the close of the calendar or fiscal year (or date extended by waiver under sec. 77.59(3m), Wis. Stats. (1993-94)).

- Date the amount of the notice of determination is paid (this does not include deposits of tax under sec. 77.59(6)(c), Wis. Stats. (1993-94), while appeal is pending).
- 60 days after the date the buyer received the Appellate Bureau's notice of redetermination, even though the buyer files the appeal with the Wisconsin Tax Appeals Commission before the 60 days have expired.

2. Transaction Assessed in Field Audit Determination (sec. 77.59(4)(b), Wis. Stats. (1993-94))

Claims for refund of the tax assessed by a field audit may be filed within two years of the issuance of the notice of determination of sales or use tax assessed by field audit, if the buyer paid the tax and the tax was not protested by filing a petition for redetermination.

Example: Buyer O is field audited by the Department of Revenue for the period January 1991 through December 1994, and is assessed \$5,000 of use tax on purchases made. The notice of determination is dated and issued April 5, 1995.

Buyer O pays the \$5,000 of use tax on April 20, 1995, and does not file a petition for redetermination.