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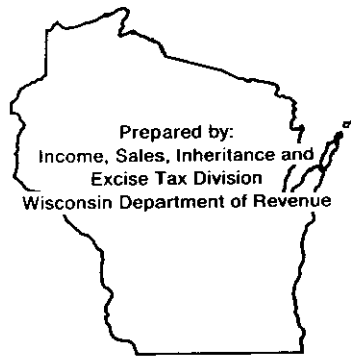

FEDERAL TAX LAWS ENACTED IN 1986 DO NOT APPLY FOR WISCONSIN

Federal tax laws enacted during 1986 generally may not be used in determining Wisconsin taxable income for 1986. There are two exceptions: (1) any federal law which changes the amount of taxable unemployment compensation required to be included in federal adjusted gross income will apply for Wisconsin tax purposes, and (2) at the taxpayer's option, any revisions to the federal Internal Revenue Code that relate to the taxation of income derived from any source as a direct consequence of participation in the milk production termination program (P.L. 99-198) will apply for Wisconsin tax purposes.

The fact that federal tax laws enacted during 1986 may not be used in determining Wisconsin taxable income for 1986 results in certain income and deduction items being different on 1986 Wisconsin and federal income tax returns. As in prior years, Wisconsin Schedule I should be used to adjust for these differences.

The federal laws enacted during 1986 which may result in a differences between Wisconsin and federal income for 1986 are Public Law 99-272 and the Tax Reform Act of 1986. A comprehensive list of the provisions of federal law which may not be used for Wisconsin purposes can be found in the instructions of Wisconsin Schedule I which will be available at Department of Revenue offices about January 2, 1987. The list will include items that affect calendar year taxpayers as well as those taxpayers who file on a fiscal year basis.

IN THIS ISSUE

NEW FOR 1986 — WISCONSIN PACKAGE WI-X

A new package of Wisconsin tax forms is available for 1986. It is titled Package WI-X and contains actual size copies of most of the Wisconsin individual, fiduciary and corporation income tax, gift tax, inheritance tax, motor fuel tax, sales tax and withholding tax forms.

This forms package should be available December 15, 1986. The cost is $5.00 per copy. An order blank to purchase Package WI-X will be sent with the bulk order form in October.

If you do not receive an order blank and wish to purchase copies of Package WI-X, requests indicating the number of copies wanted along with the amount due should be mailed to: Wisconsin Department of Revenue, Shipping and Mailing Section, Post Office Box 8903, Madison, WI 53708.

TWO NEW FORMS FOR 1986

1. New Simplified Tax Form

   Form WI-Z is a simplified tax form similar to federal Form 1040EZ. Form WI-Z may be filed by persons who

   - file federal Form 1040EZ,
   - were Wisconsin residents for all of 1986,
   - did not have interest income from U.S. bonds or from state or municipal bonds in 1986,

- do not claim any Wisconsin tax credits other than the Wisconsin renter's and home owner's credits (such as Wisconsin homestead credit),

- will be claimed as a dependent on another person's income tax return, and have less than $5,200 of total income.

The department encourages persons who meet these conditions to file Form WI-Z.

2. New Form for Nonresidents and Part-Year Residents

Nonresidents and part-year residents of Wisconsin must file Form 1NPR. As a result of changes in the Wisconsin income tax law, Form 1NPR has been designed to make it easier for these persons to report their Wisconsin income. Form 1NPR has 2 columns. The first column is labeled "Federal column." In this column, a nonresident or part-year resident will fill in the same amounts that were reported on the federal return. The second column is labeled "Wisconsin column." In this column, the person will fill in the amounts that apply to Wisconsin.

3. Other Form Changes

Income Tax Forms (Form 1 and 1A)

- Married couples will be able to file a "joint" return for Wisconsin. The separate entry columns for spouses are eliminated.

- The entry line for the standard deduction is eliminated. The standard deduction has been built into the tax tables, eliminating the need for the separate entry line.

- The entry line for itemized deductions is eliminated. A Wisconsin itemized deduction credit is allowed in place of a subtraction for itemized deductions.

- The number of entry lines on Form 1 is reduced from 70 lines for 1985 to 27 lines for 1986. The number of entry lines on Form 1A is reduced from 30 lines for 1985 to 17 lines for 1986.

- Form 1 has been redesigned as a one-page form with four supporting schedules appearing on the reverse side of the form.

- Entry lines detailing federal income and deductions are eliminated on Form 1. Taxpayers will enter their federal adjusted gross income rather than amounts from each separate line of their federal return.

- The section of the forms where credits are claimed is revised to reflect several law changes. The child-dependent care credit and earned income credit are eliminated. The married couple credit and itemized deduction credit are new for 1986. The personal exemption credits are revised to include only a dependent credit and a senior citizen credit.

- Form 1 includes a filing status for "married filing separate returns." Married persons filing a separate return must file on Form 1. Married persons filing a joint return may file on either Form 1 or 1A.

- Schedule MT, Wisconsin Minimum Tax, is eliminated for 1986. The Wisconsin Minimum Tax is computed on Form 1, and no additional schedule is needed.

Homestead Credit (Schedule H)

- Two new questions have been asked relating to marital status (see Questions 6b and 6c).

- The entry lines for reporting the separate Wisconsin income of each spouse are revised. Only one entry line is needed as spouses may file a joint Wisconsin tax return.

Copies of the 1986 Wisconsin Form 1, 1A, WI-Z, 1NPR and Schedule H are included on pages 31 through 42 of this issue. Form 1NPR is still subject to change before being printed.

1986 INCOME AND FRANCHISE TAX FORMS

For tax practitioners and others who wish to print their own supplies of Wisconsin tax forms, camera copy of the 1986 Wisconsin income and franchise tax forms and the 1987 declaration of estimated tax forms may be purchased from the WISCOMP Center. The cost is $15 per side of a page which includes the 5% Wisconsin sales tax, handling and shipping. The camera copy of 1986 corporation forms is available immediately. Camera copy for most of the other tax forms is expected to be available about November 1, 1986.

A clip out order form is located on the last page of this bulletin. Address orders to WISCOMP, One West Wilson Street, Room B355, Madison, WI 53702. Make your remittance payable to WISCOMP. Your remittance must accompany your order. Orders are processed on a 24-hour basis.

WISCONSIN JOINS INTERSTATE SALES COMPACT TO ENFORCE USE TAX LAWS

Wisconsin, along with Illinois, Indiana, Michigan, Minnesota, and Ohio, has signed the Great Lakes States Interstate Sales Compact to increase compliance with the use tax laws, primarily as it applies to transactions made across state boundaries.

The compact calls for an increase in cooperative enforcement and exchange of information by 1) encouraging voluntary registration with the other states by those instate vendors who, while not being required to register, make regular sales to consumers in the other states; 2) encouraging and enforcing registration by those instate vendors who are required to register with one or more other states; and 3) providing information to the other states on untaxed sales made by instate vendors to consumers in the other states. Audits will be used to discover untaxed sales made by vendors to consumers in the various Great Lakes states.

Although the compact specifically applies to sales and use taxes, the states may enter into agreements creating cooperative administrative efforts for other taxes, including corporate franchise tax, income tax, motor fuel tax, cigarette tax, and other excise taxes.

TAXPAYERS TO RECEIVE FORMS 1099-G IN JANUARY 1987

An information return, Form 1099-G, will be mailed to taxpayers who received a Wisconsin income tax refund in 1986. Only such taxpayers who claimed itemized deductions on their 1985 federal income tax returns should receive Forms 1099-G. Section 6050E of the Internal Revenue Code requires the Department of Revenue to send this 1986 information return to taxpayers.

If a married person had offset part or all of his or her refund against tax owed by his or her spouse on a combined return, the full amount of the refund (amount before the offset) will be reported on Form 1099-G. For example, on their 1985 return spouse A had a refund of $400 which was applied against spouse B's tax due of $150. A refund check of $250 ($400 - $150 = $250) was issued to spouse A in 1986. The full amount of refund ($400 in this example) will be reported on the 1986 Form 1099-G for spouse A.

If both a husband and wife receive a refund when filing a combined return, a separate Form 1099-G will be prepared for each spouse showing that spouse's refund. For example, on their 1985 combined return spouse A showed a refund of $75 and spouse B a refund of $125. One refund check of $200 was sent to them in 1986. The Form 1099-G for spouse A will show a $75 refund. The Form 1099-G for spouse B will show a $125 refund.

DEPENDENTS WITH UNEARNED INCOME — WHICH FORM TO FILE

Persons who are claimed as a dependent by another taxpayer and who have unearned income (for example, interest or dividends) of $1,000 or more are required to file a 1986 Wisconsin income tax return. Which tax form should be filed?

A dependent with unearned income

- *must* file Wisconsin Form 1 if his or her unearned income for 1986 is $1,000 or more, or the total income is $5,200 or more.
- may file Wisconsin Form 1A only if his or her unearned income is less than $1,000 *and* the total income is less than $5,200. Form 1A can be used only if all income is from wages, salaries, tips, unemployment compensation, interest, or dividends.
- may file Wisconsin Form WI-Z only if his or her total income is less than $5,200 *and* he or she files Form 1040EZ for federal income tax purposes. Federal Form 1040EZ can be filed only by single persons under 65 years of age who meet certain income limitations and have no dependents.

If a dependent with unearned income is a nonresident or part-year resident of Wisconsin, he or she cannot use Wisconsin Form 1, 1A or WI-Z. All nonresidents and part-year residents must file Wisconsin Form 1NPR.

BULK ORDERS OF TAX FORMS

In October, the Department will mail out the order blank (Form P-744) which practitioners and other persons or organizations should use to request bulk orders of 1986 Wisconsin income tax forms. As in past years, professional tax preparers are subject to a handling charge on their orders. No charge is made for forms used for distribution to the general public (for example, in a bank, library or post office).

Orders should be placed as early as possible after you receive the order blank. By receiving the orders early, the Department can better identify possible shortages of specific forms.

This year's mailing list for bulk order blanks contains the names of all persons and organizations who placed orders for 1985 forms. If you are not on this mailing list and do not receive a Form P-744 you may request the bulk order blank by contacting any Department office or by writing to the Wisconsin Department of Revenue, Central Services Section, P.O. Box 8903, Madison, WI 53708.

TAX RETURN STATISTICS FOR 1986

There were 2,280,000 Wisconsin income tax returns filed in 1986. In addition, 277,000 homestead credit claims and 20,000 farmland preservation credit claims were filed during the year.

The 2,280,000 income tax returns were filed by 3,227,000 individuals. (The combined return of a husband and wife is considered one return.)

Taxpayers were issued a total of 1,818,000 income tax refunds in 1986, averaging $264 each. The average refund for 1984 returns was $267.

Homestead credit refunds averaged $375 per claimant, an increase from the average refund of $360 issued last year. About 43% of the claimants were age 65 or older. Of the individuals claiming homestead credit, 45% were renters and 55% were homeowners.

An average payment of $1,671 was issued to each farmland preservation credit claimant. The average payment for 1984 claims was $1,666.

Itemized deductions were claimed by 27% of the taxpayers, and the standard deduction was claimed by 73%.

As a result of Wisconsin's 5% minimum tax, 22,650 persons made an average payment of $2,426 each.

OVER 60,000 TAXPAYERS CONTRIBUTE TO ENDANGERED RESOURCE PROGRAM

The 1985 Wisconsin income tax returns, Form 1 and 1A, included a line for taxpayers to contribute to the Wisconsin Endangered Resources Fund. These donations either reduce a taxpayer's refund or increase the amount owed. Amounts contributed go to the Wisconsin Department of Natural Resources to help protect and care for Wisconsin's endangered species, nongame wildlife and rare plant and animal habitats.

On 1985 Wisconsin income tax returns filed, 61,081 taxpayers contributed

$441,235 to the Endangered Resource Fund. This compares with 1984 income tax returns where 68,993 taxpayers contributed $470,313.

TAXPAYERS CHECK OFF OVER $400,000 TO STATE ELECTION CAMPAIGN FUND

The 1985 Wisconsin income tax returns, Form 1 and 1A, included a box for taxpayers to designate $1 to the State Election Campaign Fund. If the box is checked "yes," it does not increase or reduce the taxpayer's tax liability.

During the period July 1, 1985, to June 30, 1986, taxpayers designated $476,536 to the election campaign fund on their Wisconsin tax returns. This compares to $430,351 for the prior twelve months ending June 30, 1985.

REMINDER: FILING DEADLINES FOR 1985 HOMESTEAD AND FARMLAND PRESERVATION CREDIT CLAIMS

December 31, 1986, is the deadline for filing a 1985 homestead credit claim. Farmland preservation credit claims for 1985 must be filed no later than 12 months after the farmland owner's 1985 taxable year ends. December 31, 1986 is the deadline for filing a 1985 farmland preservation credit claim for farmland owners who are calendar year taxpayers.

No extensions of time are available for filing claims for these two credits.

REMINDER: NOTIFY DEPARTMENT OF FEDERAL ADJUSTMENTS AND AMENDED RETURNS

If a taxpayer's federal income tax return is adjusted by the Internal Revenue Service (IRS), and the adjustments affect the amount of Wisconsin income reportable or tax payable, such adjustments must be reported to the Wisconsin Department of Revenue within 90 days after they become final.

In addition, taxpayers filing an amended return with the IRS or another state must also notify the Department within 90 days of filing if information in the amended return affects the amount of Wisconsin income reportable or tax payable.

Wisconsin Administrative Code section Tax 2.105 provides additional information regarding this reporting requirement and indicates when adjustments made by the IRS are considered final.

An amended Wisconsin return or copy of the federal audit report should be sent to the Wisconsin Department of Revenue, Audit Bureau, P.O. Box 8906, Madison, Wisconsin 53708.

REMINDER: EMPLOYERS MUST SUBMIT COPIES OF CERTAIN EMPLOYE WITHHOLDING EXEMPTION CERTIFICATES TO THE DEPARTMENT

Wisconsin law requires employers to submit copies of employe withholding exemption certificates to the Department whenever they are required to provide such information to the Internal Revenue Service (IRS). The copies must be submitted to the Department within 15 days after they are filed with the IRS. For both federal and Wisconsin purposes, employers are required to submit copies of any employe's withholding exemption certificate if (1) the number of exemptions claimed is more than 14 or (2) the employe is claiming complete exemption from withholding and he or she earns more than $200 per week.

REMINDER: NONRESIDENT ENTERTAINERS REQUIRED TO FILE SURETY BOND OR CASH DEPOSIT

A "nonresident" entertainer who performs in Wisconsin for a contract price that exceeds $3,200 is required to file a surety bond or cash deposit with the Department of Revenue in an amount of 6% of his or her total contract price.

If the bond or deposit is not filed, the "employer" at the event is required to withhold the 6% from the nonresident entertainer's payment. If the employer fails to withhold the required amount, the employer will be held liable for the amount that should have been withheld.

A "nonresident entertainer" is a nonresident person who furnishes amusement, entertainment or public speaking services, or performs in one or more sporting events, and includes a foreign corporation (one not organized under the laws of Wisconsin) not regularly engaged in business in Wisconsin which derives income from any of these activities or from these services performed by a nonresident person.

An "employer" is any Wisconsin resident person or firm which contracts for the services of a nonresident entertainer. In the absence of such resident contracting person, the employer is the last resident person or firm to have receipt, custody or control of the proceeds of the event. If there is neither a resident contracting person nor a resident with control of the proceeds, the employer is any nonresident person or firm who contracts for or has control of the proceeds of the event.

Amounts of cash deposited with the Department of Revenue with Form WT-10 and amounts withheld by employers and reported on Form WT-11 may be claimed as a credit by the nonresident entertainer on his or her Wisconsin individual income tax return or on the corporation's franchise/income tax return for the year in which the appearance was made. Any amounts deposited or withheld that are in excess of the nonresident entertainer's Wisconsin tax liability per the return will be refunded.

Surety bonds filed with the Department of Revenue with Form WT-10 will be released upon request when the nonresident entertainer's tax liability for the year involved has been satisfied.

Additional information may be obtained by requesting Publication 508, entitled Wisconsin Tax Requirements Relating to Nonresident Entertainers.

Copies of Publication 508, Form WT-10, Form WT-11 and the Nonresident Entertainer's Surety Bond may be obtained from the Wisconsin Department of Revenue, Central Services Section, P.O. Box 8903, Madison, Wisconsin 53708.

Any questions about the requirements of this law may be directed to Edward Pelner, Wisconsin Department of Revenue, P.O. Box 8906, Madison, Wisconsin 53708, telephone (608) 266-3645.

CONVICTIONS FOR FAILURE TO FILE INCOME TAX RETURNS

A Menomonee Falls man has been ordered to serve 6 months in jail and pay $1,000 in fines for criminal violations of the Wisconsin state income tax law. David J. McCarville was sentenced on May 14, 1986, in Dane County Circuit Court, Branch 9, Madison, by Circuit Judge William D. Byrne on two counts of failing to file Wisconsin state income tax returns. Judge Byrne ordered McCarville to serve 90 days in the Dane County jail on the first count and 90 days on the second count to run consecutively and fined him $500 on each count.

McCarville was charged with failing to file state income tax returns on gross income of more than $25,000 for 1980 and more than $30,000 for 1981. He was found guilty on both counts after a jury trial.

An Ozaukee county man has been ordered to serve probation for criminal violations of the Wisconsin state income tax law. Knox M. Mitchell of Mequon, Wisconsin, was convicted on August 13, 1986, in Ozaukee County Circuit Court, Branch 2, Port Washington, after he plead no contest to one count of failing to file a state income tax return. Circuit Judge Warren A. Grady sentenced Mitchell to 6 months in jail, stayed execution of the sentence and ordered Mitchel to serve 2 years probation. Under the conditions of probation, Mitchell must file a Wisconsin income tax return for 1984 and pay the tax due within one year.

Failure to file a Wisconsin state income tax return is a crime punishable by a fine of not more than $500 or imprisonment not to exceed 6 months or both for income tax returns due prior to July 20, 1985. Beginning July 20, 1985, the criminal penalty is a $10,000 fine or imprisonment not to exceed 9 months or both. In addition to the criminal penalties, Wisconsin law provides for substantial civil penalties on the civil tax liability.

PRISON TERM FOR INCOME TAX EVASION

A Green Bay area man has been ordered to pay $6,000 in fines and serve jail time for state income tax violations. Richard Nachreiner, President of Richard's Hair Stylist's, Inc., Oneida, Wisconsin was sentenced on June 25, 1986 in Dane County Circuit Court, Branch 11, by Circuit Judge Daniel R. Moeser on 2 counts of state income tax evasion. Judge Moeser sentenced Nachreiner to 2 years in prison on the first count, stayed execution of the sentence and placed Nachreiner on 5 years probation on both counts, to be served concurrently. Under the conditions of probation, Nachreiner must serve 60 days in jail, pay a $3,000 fine on each count, contribute 100 hours of community service and make restitution of income taxes, penalties and interest exceeding $14,000.

Nachreiner was charged with failing to report more than $147,000 in taxable income for the years 1979, 1980, and 1981 and evading more than $14,000 in state income taxes for those years. He pled guilty to two of the charges on April 22.

Filing a false state income tax return is a crime punishable by a maximum fine of $10,000 or imprisonment for 5 years or both. In addition to the criminal penalties provided by statute, Wisconsin law provides for substantial civil penalties on the civil tax liability.

NEW ISI&E DIVISION RULES AND RULE AMENDMENTS IN PROCESS

Listed below, under Parts A and B, are proposed new administrative rules and amendments to existing rules that are currently in the rule adoption process. The rules are shown at their state in the process as of October 1, 1986. Part C lists new rules and amendments which were adopted in 1986. Part D lists emergency rules now in effect. ("A" means amendment, "NR" means new rule, "R" means repealed and "R&R" means repealed and recreated.)

A. Rules at Legislative Council Rules Clearinghouse

1.06 Application of federal income tax regulations for persons other than corporations-A
1.10 Depository bank requirements for withholding, motor fuel, general aviation fuel and special fuel tax deposit reports-A
1.13 Power of attorney-A
2.01 Residence-A
2.03 Corporation returns-A
2.05 Information returns, forms 8 for corporations-A
2.08 Returns of persons other than corporations-A
2.99 Minimum tax—individuals, estates and trusts-NR
3.03 Dividends received, deductibility of-A
3.07 Bonuses and retroactive wage adjustments paid by corporations-A
3.08 Retirement and profit-sharing payments by corporations-A
3.10 Salesmen's and officers' commissions, travel and entertainment expense of corporations-R
3.12 Losses on account of wash sales by corporations-A
3.37 Depletion of mineral deposits by corporations-A
3.38 Depletion allowance to incorporated mines and mills producing or finishing ores of lead, zinc, copper or other metals except iron-A
3.47 Legal expenses and fines--corporations-R
3.54 Miscellaneous expenses not deductible--corporations-A
3.81 Offset of occupational taxes paid against normal franchise or income taxes-A
3.91 Petition for redetermination-A
3.92 Informal conference-A
3.93 Closing stipulations-A
3.94 Claims for refund-A

B. Rules at Legislative Standing Committees

2.395 Sales factor option-NR

C. Rules Adopted But Not Yet Effective (Effective 11/1/86)

11.001 Definitions and use of terms-A
11.32 "Gross receipts" and "sales price"-A
11.68 Construction contractors-A
11.83 Motor vehicles-A
11.92 Records and record keeping-A
11.95 Retailer's discount-A
11.97 "Engaged in business" in Wisconsin-A

D. Rules Adopted in 1986 (in parentheses is the date the rule became effective)

2.045 Information returns; form 9c for employers of nonresident entertainers, entertainment corporations or athletes-R (1/1/86)
3.22 Real estate and personal property taxes of corporations-R (1/1/86)
3.30 Depreciation and amortization, leasehold improvements: corporations-R (1/1/86)
3.31 Depreciation of personal property of corporations-R (1/1/86)
3.61 Mobile home monthly parking permit fees-R (1/1/86)
11.71 Computer industry-NR (3/1/86)
11.83 Motor vehicles-A (3/1/86)
17.01 Administrative provisions-NR (9/1/86)
17.02 Eligibility-NR (9/1/86)
17.03 Application and review-NR (9/1/86)
17.04 Repayment of loan-NR (9/1/86)

E. Emergency Rules

2.395 Sales factor option-NR

The following sales tax rules to incorporate county sales/use tax provisions were published and became effective on March 24, 1986:

11.001 Definitions and use of terms-A
11.32 "Gross receipts" and "sales price"-A
11.68 Construction contractors-A
11.83 Motor vehicles-A
11.92 Records and record keeping-A
11.95 Retailer's discount-A
11.97 "Engaged in business" in Wisconsin-A

REPORT ON LITIGATION

This portion of the WTB summarizes recent significant Tax Appeals Commission and Wisconsin court decisions. The last paragraph of each decision indicates whether the case has been appealed to a higher court.

The last paragraph of each WTAC decision in which the department's determination has been reversed will indicate one of the following: (1) "the department appealed," (2) "the department has not appealed but has filed a notice of nonacquiescence" or (3) "the department has not appealed" (in this case the department has acquiesced to Commission's decision).

The following decisions are included:

Individual Income Taxes

James Keane (p. 6)
Domicile—Wisconsin domicile not abandoned

Corporation Franchise/Income Taxes

American Brands, Inc. (p. 7)
Nexus

Falls Communications, Inc. (p. 7)
Installment sales

Luebke Corporation (p. 8)
Interest expense—purchase of own stock

Regency Nursing Home, Inc. (p. 8)
Net business loss carryforward

Sales/Use Taxes

Bargo Foods North, Inc. (p. 9)
Meals—transportation companies
Gross receipts

Reichard Yamaha, Inc. (p. 9)
Successor's liability

Wisconsin Bell, Inc. (p. 9)
Definitions of storage and use
Liability of user

INDIVIDUAL INCOME TAXES

Domicile — Wisconsin domicile not abandoned. *James Keane vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, June 19, 1986). The sole issue for the Commission to determine was whether the taxpayer during the years 1982 and 1983 was a resident of Racine, Wisconsin and domiciled in this state for income tax purposes.

The taxpayer was employed by the S.C. Johnson Company of Racine, Wisconsin from June 1974 until the present where he is the marketing vice-president, International Division. The taxpayer's home office is located in Racine, Wisconsin.

Prior to his purchase of a condominium in the State of Florida, the taxpayer and his wife resided at 3101 Michigan Road, Racine, Wisconsin. This home was sold in January 1982. The taxpayer testified that he and his wife purchased a condominium located in West Palm Beach, Florida where he took up Florida residency and obtained a Florida driver's license, Florida auto registration, Florida voting registration, Florida bank account and Florida savings account.

The taxpayer also testified that after he and his wife sold their home in Racine, Wisconsin in January 1982, they rented an apartment in Racine, Wisconsin. The taxpayer resided in that apartment approximately 65% of the year.

The taxpayer continued maintaining his Wisconsin driver's license and Wisconsin auto registration. The taxpayer also had personal property located in Wisconsin, maintained a bank account and safety deposit box in Wisconsin, and held membership in the Racine Country Club and St. Mary's Church of Racine, Wisconsin, all during 1982 and 1983.

The taxpayer's wage and tax statement in 1982 and 1983 lists his address as 111 East 11th Street, Racine, Wisconsin, and S.C. Johnson Company withheld Wisconsin state income tax from the taxpayer.

The Commission concluded that the taxpayer, during the period under review, did not abandon his Wisconsin domicile and establish a new domicile elsewhere. During the period under review, the taxpayer was legally domiciled in the State of Wisconsin, and thus, under the provisions of

s. 71.01, Wis. Stats., he was deemed to be residing within this state for the purposes of determining his liability for Wisconsin income taxes. The department's action was proper in imposing a Wisconsin income tax on the taxpayer covering the years 1980 through 1983, inclusive.

The taxpayer has not appealed this decision.

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CORPORATION FRANCHISE/INCOME TAXES

Nexus. *American Brands, Inc. vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, July 3, 1986). The principal issue for determination was whether the taxpayer was subject to Wisconsin franchise or income tax liability for its fiscal years ended December 31, 1972 through December 31, 1976.

The taxpayer is a New Jersey corporation. Its principal business is the manufacture of tobacco products. For each of the years at issue, the taxpayer held a Certificate of Authority from the State of Wisconsin and filed annual reports with the Secretary of State.

During the years in question, the taxpayer maintained no sales offices in Wisconsin and did not have any employes or independent contractors receiving or accepting orders or making collections in Wisconsin. The taxpayer sold its tobacco products only to licensed distributors such as wholesale jobbers, chain stores, vending machine operators and the United States Government. Customers sent all orders for the taxpayer's tobacco products to the taxpayer's customer service center in Richmond, Virginia. The customer service center accepted, rejected or reduced orders and established credit terms.

The taxpayer stored inventories of tobacco products in two public warehouses in Wisconsin during the period 1963 through December 31, 1976. When processing of orders was completed, instructions were issued from the taxpayer's customer service center in Virginia for the release of the merchandise from the stock of one of such public warehouses or from one of the taxpayer's factories outside Wisconsin, depending on the location of the customer and the brands involved. All shipments to customers in Wisconsin were made by common carrier. During the period at issue, the storage of goods was not an activity protected by P.L. 86-272 from the assertion of Wisconsin franchise or income taxes. The department has conceded that the taxpayer engaged in no activities in Wisconsin, other than storage of goods in public warehouses, which would subject it to Wisconsin franchise/income tax liability.

For tax years prior to 1973, the department did not assert jurisdiction to tax foreign corporations which only maintained inventories in public warehouses from which goods are delivered in the state by common carrier.

In 1971, the Wisconsin Legislature enacted an amendment to Chapter 71 of the Wisconsin Statutes, creating a new statutory apportionment formula patterned after the formula in the Uniform Division of Income for Tax Purposes Act, establishing a three factor formula utilizing property, sales and payroll ratios. As a result of this statutory change, a company in a position such as the taxpayer regarding its activities in Wisconsin, would have a substantially increased tax liability in Wisconsin. The new statutory apportionment formula became effective with the income year 1973.

As a result of the amendment effective in 1973 to Chapter 71, the department began to reconsider its previous policies with regard to "nexus" with foreign corporations. Where previously the revenue which would have been generated by asserting jurisdiction over a foreign company which only maintained inventories in public warehouses in Wisconsin was minimal, under the new apportionment formula the revenue generated would be substantially increased.

The Commission concluded that for the tax years ending December 31, 1972 through December 31, 1974, the department is barred from collecting Wisconsin franchise/income tax from the tax-payer because an assertion of such liability would be beyond the department's administrative authority and an abuse of discretion. For the tax years ending De-ember 31, 1975 and December 31, 1976, the department properly asserted jurisdiction over the taxpayer for franchise/ income tax purposes and the taxpayer is liable for Wisconsin franchise/income tax for that period. The taxpayer has not shown that all the elements of estoppel are present, and therefore, the department is not estopped from asserting jurisdiction over the taxpayer in any of the years at issue.

The department has appealed this decision to the Circuit Court.

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Installment Sales. *Falls Communications, Inc. vs. Wisconsin Department of Revenue* (Court of Appeals, District IV, April 24, 1986). The Wisconsin Department of Revenue appealed from a judgment reversing the Wisconsin Tax Appeals Commission's decision which had upheld the department's assessment of additional income tax against Falls Communications for 1979. The question is whether the transfer of an installment sale obligation by merger of one corporation with another is a "distribution" to the merged corporation under Wis. Adm. Code section Tax 2.19(2).

Falls Communications, a Wisconsin corporation, sold a business asset in 1978. The purchase price was to be paid in installments. Falls Communications reported the sale by the installment method of tax accounting for state tax purposes, as permitted by s. 71.11(8), Wis. Stats.

Falls Communications and C.K. of Tennessee, Inc., a Tennessee corporation, had common shareholders. The corporations and the shareholders approved a plan of merger by which Falls Communications was merged into C.K., effective April 1, 1979. After the merger, C.K. continued to report gain from the 1978 sale by the installment method. The department subsequently made the $20,072.16 assessment at issue on grounds that by the 1979 merger, Falls Communications distributed the installment obligation to C.K. and C.K. therefore lost or did not acquire the right to use the installment method. The department included the remaining unrecognized gain on the installment sale obligation in Falls Communications' taxable income for the year of the merger.

The effect of the merger statutes is such that once the conditions for merger have been met, title to the property of the merged corporation passes to the surviving corporation by operation of law. Nothing more is necessary to accomplish

the passage of title. A corporation merged into another therefore "distributes" nothing to the surviving corporation within the meaning of Wis. Adm. Code section Tax 2.19(2).

The Court of Appeals held that because Falls Communications distributed nothing to C.K., Wis. Adm. Code section Tax 2.19(2) is inapplicable, and the assessment based on that rule is void.

The department has not appealed this decision.

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Interest expense–purchase of own stock. *Luebke Corporation vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, April 2, 1986). Luebke Corporation is a Wisconsin corporation engaged in the manufacture and sale of screw machine products, with its principal offices in Brookfield, Wisconsin. The issue in this case was whether or not the interest paid on the taxpayer's Marine Bank note constituted nondeductible interest paid on money borrowed or interest on notes or securities issued by a corporation to purchase its own capital stock.

On December 14, 1976, the taxpayer purchased and redeemed 162.5 shares of its common stock and 3,905 shares of preferred stock owned by Arthur and Josephine Luebke, representing all of their stock in the corporation, for a total price of $1,500,000. The terms of purchase were $100,000 to be paid at closing on January 6, 1977, together with a promissory note ("the Luebke note") issued by the taxpayer in the amount of $1,400,000, providing for quarterly payments of interest and principal for a 15-year period. Payments of interest and principal were made during 1977 and in early 1978.

The effect of this redemption was to place the taxpayer's ownership fully in the hands of the remaining shareholders, Dane and Gregory Luebke, sons of Arthur and Josephine Luebke.

In the minutes of the taxpayer's board of directors meeting on May 12, 1978, the directors expressed concern about impairment in the operations of the business resulting from the security arrangements underlying the Luebke note. It was indicated that the South Milwaukee Marine Bank would be willing to loan up to $1,300,000 at a 10% interest rate to provide the funds for the purpose of prepaying the Luebke note. Accordingly, resolutions were adopted to (1) prepay the Luebke note including a $50,000 prepayment penalty; (2) borrow the sum of $1,300,000 from the South Milwaukee Marine Bank; and (3) authorize and direct the corporate officers to execute all documents reasonable and necessary to effect prepayment and consummate the loan transaction at the bank. In the same minutes the directors adopted resolutions to purchase a machine for approximately $194,000 and certain equipment for $1,000,000.

The taxpayer proceeded to obtain the $1,300,000 loan ("the Marine note") on June 15, 1978, secured by a first mortgage on corporate real estate, a general business security agreement, 325 shares of corporate stock, certain life insurance policies, and personal guarantees of the stockholders. Of the amount borrowed, $1,252,483.34 was directly applied to satisfaction of the Luebke note, $13,068 to loan and title insurance fees, and $34,448.66 was deposited in the corporate checking account available for general business purposes.

On its Wisconsin franchise tax returns for the fiscal years ending July 1, 1978, June 30, 1979 and June 28, 1980, filed on the accrual basis of accounting, the taxpayer deducted interest accruals on the Marine note.

The department disallowed the Marine note interest based upon its conclusion that the interest was "paid on money borrowed or interest on notes and securities issued by a corporation to purchase its own capital stock" and was, therefore, not deductible by operation of s. 71.04(2)(a)3, Wis. Stats. The disallowance was prorated to allow that portion of the interest reflecting 2.65% of loan proceeds that went into the taxpayer's general checking account. Interest paid on the Luebke note was also disallowed under that provision, an adjustment which the taxpayer conceded was proper and did not contest administratively.

There is no evidence that the taxpayer could have satisfied the Luebke note at the time it did, on June 15, 1978, from corporate funds *then* available without substantial borrowing. The only specific reason for prepayment set forth in the corporate minutes was "the impairment in the operations of the business which had resulted from the security interest of Arthur J. and Josephine Luebke in the corporation's property, and inability to obtain desired consents and waivers under the security arrangements."

The term as well as the interest rate of the Luebke note was more favorable than the Marine note. The impairment to the taxpayer's business operations occasioned by the Luebke note security and waiver provisions was evidently of sufficient magnitude to move the corporation to act when it did to satisfy that note by borrowing funds from the South Milwaukee Marine Bank rather than wait until funds were generated from business operations. The Marine note funds were borrowed for the purpose of paying off the Luebke note.

The Commission held that the interest on the Marine bank loan was paid on money borrowed by the taxpayer to purchase its own capital stock and was, therefore, nondeductible under s. 71.04(2)(a)3, Wis. Stats.

The taxpayer has not appealed this decision.

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Net business loss carryforward. *Regency Nursing Home, Inc. vs. Wisconsin Department of Revenue* (Circuit Court of Milwaukee County, April 29, 1986). Regency Nursing Home petitioned for review of the decision and order of the Wisconsin Tax Appeals Commission dated November 13, 1984. That decision upheld the Wisconsin Department of Revenue when the latter denied the taxpayer's carryforward of certain existing business losses. Thus, the issue was whether or not the Commission correctly decided that the gain from the sale of the business does not constitute "net business income" as that term is defined in s. 71.06, Wis. Stats., so that the prior net business losses may not be used as an offset. (See WTB 41 for a summary of the Wisconsin Tax Appeals Commission's decision.)

The Circuit Court concluded that the ongoing operation of a particular business is essential in order to utilize the subject gain as "net business income" against which to offset a "net business loss." The Court therefore found that the Commis-

sion did not err and correctly applied the law. The Court further found that the Commission correctly determined that it did not have the authority to review the taxpayer's additional arguments which were raised for the first time in its petition for redetermination. The Circuit Court was likewise without the authority to do so by virtue of s. 227.20(1), Wis. Stats.

The taxpayer has appealed this decision to the Court of Appeals.

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SALES/USE TAXES

Meals—transportation companies, gross receipts. *Bargo Foods North, Inc. and Republic Airlines vs. Wisconsin Department of Revenue* (Circuit Court of Dane County, March 13, 1986). The matter before the Court was an appeal from an assessment made by the department for additional sales and use taxes against Bargo Foods North, Inc. (Bargo) for the years 1978 through 1981. Bargo is a catering company providing food and beverage kits at Mitchell Field in Milwaukee to commercial airlines for in-flight use. The sales tax assessment is for meals that the taxpayer sold to Republic Airlines (Republic) at Mitchell Field. Republic has an indemnification agreement with Bargo regarding this sales tax assessment. Bargo and Republic brought this appeal from a decision and order of the Wisconsin Tax Appeals Commission, dated October 2, 1985, affirming the department's assessment.

The Commission determined that Bargo's sale of meals to Republic was subject to Wisconsin's sales tax; that this transaction was not a sale for resale exempt from sales tax; and that Bargo's sale to Republic was for use or consumption, not for a subsequent transfer for valuable consideration.

Further, the Commission determined that the fee Bargo paid Milwaukee County for the right to operate at Mitchell Field, 8% of Bargo's total gross receipts, was not a tax and therefore was not deductible from Bargo's gross receipts under s. 77.51(11)(a)4, Wis. Stats. Bargo passed this user fee along to Republic as part of its total gross receipts. (See WTB 45 for a summary of the Wisconsin Tax Appeals Commission's decision.)

The Circuit Court concluded that Bargo's sales of meal kits to Republic at Mitchell Field were not sales for resale. Republic provided meals to passengers as a commercial amenity, not for valuable consideration; therefore, Bargo's sales to Republic were taxable transactions. The Wisconsin Department of Revenue properly assessed the sales tax for these transactions. Further, Bargo is not entitled to a deduction on its assessment for airport charges paid to Milwaukee County; this was not a tax on a tax.

The taxpayer has appealed this decision to the Court of Appeals.

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Successor's liability. *Reichard Yamaha, Inc. vs. Wisconsin Department of Revenue* (Circuit Court of Dane County, July 7, 1986). The taxpayer raised two issues:

A. Is the taxpayer a successor and therefore subject to sales tax liability under s. 77.52(18), Wis. Stats.?

B. If so, did the department comply with Administrative Code requirements that it first proceed against Classic Motorcycles, Inc. before assessing the taxpayer with tax liability?

Reichard Yamaha, Inc. is a motorcycle sales and service business. In June 1982, the taxpayer was asked to purchase the business and/or assets of Classic Motorcycles, Inc. (Classic), another motorcycle sales and service business located in Cudahy, Wisconsin. The taxpayer declined the offer. The taxpayer later learned that Classic had begun the process of liquidating its business. In July 1982, the taxpayer purchased certain accessories, parts and office equipment from Classic. The items purchased represented only a portion of the total inventory of Classic. The taxpayer later occupied the premises vacated by Classic. It used its own name, Reichard Yamaha, at the new location. It obtained its own phone number, occupancy permit and motor vehicle permit. It did not obtain receivables, customer lists or payables from Classic. Nor did it honor obligations for warranty work for customers of Classic.

The Circuit Court concluded that the taxpayer is a successor, as that term is used in s. 77.52(18), Wis. Stats. The Court remanded the case to the Wisconsin Tax Appeals Commission for further fact-finding on the department's collection efforts relative to Classic and its former officers.

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Definitions of storage and use, liability of user. *Wisconsin Bell, Inc. vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, April 14, 1986). The issues in this case were as follows:

A. Whether the taxpayer stored, used or otherwise consumed telephone directories partially completed in this state and printed in another state, delivered to the taxpayer's agent in this state for distribution to the taxpayer's customers.

B. Whether the taxpayer is liable for use tax on tangible personal property purchased for its own use in Wisconsin from vendors subject to Wisconsin sales and use tax laws, where the department is unable due to statutes of limitation to audit the vendors and collect sales or use tax.

The Commission held as follows:

A. For sales and use tax purposes, upon delivery by the printer to the taxpayer's agent for receipt, warehousing, and distribution, Directory Distributing Associates, Inc., the taxpayer owned and possessed the telephone directories in Wisconsin. The taxpayer's ownership and possession of the directories in Wisconsin together with its exercise of rights and powers over them in Wisconsin constituted "use" as defined in s. 77.51(15), Wis. Stats. The warehousing of the directories in Wisconsin by the taxpayer's agent constituted "storage" as defined in s. 77.51(14), Wis. Stats. The taxpayer having engaged in both "storage" and "use" of the directories in Wisconsin was subject to use tax measured by the printing and transportation charges from the printer.

B. The taxpayer was liable for use tax on its purchases of various tangible personal property from Wisconsin vendors and non-Wisconsin vendors holding Wisconsin seller's permits or such vendors doing business as retailers in Wisconsin for use in Wisconsin. The taxpayer's liability for use tax was not extinguished absent evidence that the sales or use tax has been

paid to the state, or a receipt from a retailer with the tax separately stated. The department's assessment of use tax against the taxpayer rather than the sales tax against the various vendors is permitted by law and is fair and proper. The taxpayer has not appealed this decision.

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TAX RELEASES

("Tax Releases" are designed to provide answers to the specific tax questions covered, based on the facts indicated. However, the answer may not apply to all questions of a similar nature. In situations where the facts vary from those given herein, it is recommended that advice be sought from the Department. Unless otherwise indicated, Tax Releases apply for all periods open to adjustment. All references to section numbers are to the Wisconsin Statutes unless otherwise noted.)

The following Tax Releases are included:

Individual Income Taxes

Income and Franchise Taxes

Corporation Franchise/Income Taxes

INDIVIDUAL INCOME TAXES

1. Basis and Depreciation Allowable for Property Located Outside Wisconsin Acquired by an Individual Before Becoming a Wisconsin Resident

Statutes: Sections 71.02(2)(c), (d) and (i) and 71.05(1)(m), 1985 Wis. Stats.

Wis. Adm. Code: Section Tax 2.30, July 1982 Register

Question: If a nonresident individual acquires and places in service depreciable property located outside Wisconsin, what is the Wisconsin basis and what depreciation method is allowable for Wisconsin purposes when this individual becomes a Wisconsin resident?

Answer:

A. If Federal Basis and Federal Depreciation Are Determined in a Manner Allowable Under the Internal Revenue Code in Effect for Wisconsin

The Wisconsin basis of the property is the same as the federal basis, provided the federal basis was determined under the Internal Revenue Code in effect for Wisconsin for the taxable year in which the individual becomes a Wisconsin resident. Also, depreciation for Wisconsin purposes is the same as the federal depreciation, provided the federal depreciation method is allowable under the Internal Revenue Code in effect for Wisconsin for the taxable year in which the individual becomes a Wisconsin resident.

Example: Taxpayer A became a Wisconsin resident on January 1, 1985. Prior to that date, he had been an Illinois resident. On July 1, 1984, Taxpayer A had purchased and placed in service rental property located in Illinois. The cost of the property, not including the land, was $200,000.

On his 1984 federal return, Taxpayer A claimed $8,000 of depreciation on this rental property, computed using the 18-year ACRS recovery period. The federal adjusted basis of the property on January 1, 1985 is $192,000 ($200,000 cost – $8,000 depreciation allowable). (The Tax Reform Act of 1984 provided that for real property placed in service after March 15, 1984, the ACRS recovery period was increased from 15 to 18 years.)

On his 1985 federal return, Taxpayer A claims $18,000 of depreciation on this rental property.

Since Wisconsin has adopted the Internal Revenue Code as of December 31, 1984 for the 1985 taxable year, the Wisconsin basis of the property on January 1, 1985 is the same as the federal basis, $192,000. To compute the depreciation allowable for Wisconsin for 1985, Taxpayer A uses the same basis and depreciation method that he is using for federal purposes. Thus, his 1985 Wisconsin depreciation is $18,000, the same as his 1985 federal depreciation.

Note: For Wisconsin purposes, the taxpayer may elect to recompute both the basis and the depreciation using another method allowable under the Internal Revenue Code in effect for Wisconsin instead of using the federal basis and federal depreciation method. For instance, in the above example Taxpayer A may elect to use the alternate ACRS method for Wisconsin with an 18-year recovery period. Under this method, the 1984 deprecia-

tion would have been $6,000. The adjusted basis of the rental property on January 1, 1985, the date Taxpayer A became a Wisconsin resident, would be $194,000 ($200,000 cost – $6,000 depreciation allowable). On his 1985 Wisconsin return, Taxpayer A would claim $12,000 of depreciation, instead of the $18,000 allowable on his 1985 federal return.

B. If Federal Basis and Federal Depreciation Are Determined in a Manner Not Allowable Under the Internal Revenue Code in Effect for Wisconsin

If the federal basis and federal depreciation were computed in a manner not allowable under the Internal Revenue Code in effect for Wisconsin purposes for the taxable year in which the individual becomes a Wisconsin resident, both the basis and the depreciation must be recomputed under the Internal Revenue Code in effect for Wisconsin.

Example: Taxpayer B became a Wisconsin resident on December 1, 1984. Prior to that date, he had been an Illinois resident. On July 1, 1984, Taxpayer B had purchased and placed in service rental property located in Illinois. The cost of the property, not including the land, was $200,000.

On his 1984 federal return, Taxpayer B claimed $8,000 of depreciation on this property, computed using the 18-year ACRS recovery period. The federal adjusted basis of the property on January 1, 1985 is $192,000 ($200,000 cost - $8,000 depreciation allowable). On his 1985 federal return, Taxpayer B claims $18,000 of depreciation on this rental property.

Wisconsin had adopted the Internal Revenue Code as of December 31, 1983 for the 1984 taxable year, which provided that real property placed in service during 1984 has a 15-year ACRS recovery period. Therefore, Taxpayer B must recompute his depreciation for Wisconsin. Since he had placed the property in service during 1984 and depreciation is calculated only at the end of the taxable year, his federal adjusted basis as of December 1, 1984, computed under the December 31, 1983 Code, is $200,000. The depreciation allowable under the December 31, 1983 Code is $12,000. Since Taxpayer B was a Wisconsin resident for only one of the six months during which he owned the property in 1984, 1/6, or $2,000, of the depreciation expense computed under the December 31, 1983 Code is allowable on his Wisconsin return.

For Wisconsin purposes, the adjusted basis of the property on January 1, 1985 is $188,000 ($200,000 adjusted basis on December 1, 1984 - $12,000 depreciation allowable under the December 31, 1983 Code). For 1985, Taxpayer B's Wisconsin depreciation on this property is $22,000.

C. If Residential Real Property or Certain Property Used in Farming Is Placed in Service During 1986 or Thereafter

For taxable year 1986 and subsequent years, Wisconsin law provides that for residential real property and for certain property used in farming, the depreciation deduction and gain or loss on disposition of such property must be computed under the Internal Revenue Code in effect on December 31, 1980. If such property is placed in service by the taxpayer during the taxable year 1986 or thereafter, but before the property is used in the production of income subject to Wisconsin taxation, the property's adjusted basis and depreciation schedule aren't required to be changed from the amounts allowable on the owner's federal returns.

Example: Taxpayer C becomes a Wisconsin resident on January 1, 1987. Prior to that date, he is an Illinois resident. On July 1, 1986, Taxpayer C purchases and places in service residential real property located in Illinois. On his 1987 Wisconsin return, Taxpayer C's adjusted basis and depreciation on this property will be the same as the amounts shown on his 1987 federal return. He does not have to recompute the basis of the property and depreciate it using one of the methods permitted under the December 31, 1980 Code (such as the straight-line method or declining balance method).

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2. Holding Period for Public Utility Stock

Statutes: Section 71.05(1)(a)12, 1983 Wis. Stats.

Note: This Tax Release applies only with respect to taxable years 1982 and thereafter.

Background: Internal Revenue Code Section 305(e) provides special tax treatment for taxable stock dividends issued by qualified public utilities. The special rule for public utility stock dividends distributed after 1981 and before 1986 in taxable years ending after 1981 allows a shareholder to elect to exclude from income up to $750 per year ($1,500 on a joint return) of the stock dividends received if he or she chooses a dividend of qualified common stock instead of cash or property. The shareholder elects the exclusion, with respect to any share, on his or her federal tax return for the tax year in which the dividend would otherwise have been included in income.

If the shareholder elects to exclude the dividend, the federal basis of the stock then becomes zero. Therefore, the full amount of sales proceeds would be taxable. Section 1222 of the Internal Revenue Code states that capital assets acquired after June 22, 1984 and before January 1, 1988, will be subject to capital gains treatment if held for 6 months or more. However, Section 305(e) requires that public utility stock, received as a dividend rather than cash or property, has a holding period of one year before capital gains treatment will apply.

For Wisconsin purposes, if a shareholder elects the exclusion available under Section 305(e) of the Internal Revenue Code, an add modification is required on the Wisconsin income tax return for the amount excluded on the federal return (s. 71.05(1)(a)12, Wis. Stats.).

Facts and Question: A Wisconsin resident received public utility stock dividends during 1984 and after June 22, 1984. For federal income tax purposes, this individual elected to use the provisions of Section 305(e) of the Internal Revenue Code and excluded these dividends from federal adjusted gross income for 1984. On the federal Form 1040 which was attached to the 1984 Wisconsin return filed by this individual, the public utility stock dividend was not included in federal adjusted gross income. On the 1984 Wisconsin return, the value of the public utility stock dividend

was entered as an addition to federal income as required by s. 71.05(1)(a)12, 1983 Wis. Stats.

During the 1985 taxable year (and before the stock was held for one year), the public utility stock received as a dividend after June 22, 1984 was sold. Because the stock was held for less than one year, for federal income tax purposes, the entire gain realized from the sale in 1985 must be treated as ordinary income. Is the holding period for receiving capital gain treatment on this stock for Wisconsin tax purposes 6 months under Section 1222 of the Internal Revenue Code or one year under Section 305(e) of the Internal Revenue Code?

Answer: The holding period for the stock sold is 6 months. Wisconsin does not follow federal tax treatment of public utility dividends and requires by s. 71.05(1)(a)12, Wis. Stats., that dividends reinvested in public utility stock be added back to Wisconsin taxable income in the year of receipt of the dividend. The result is that Wisconsin does not recognize Section 305(e) of the Internal Revenue Code for Wisconsin tax purposes. Therefore, the 6-month holding period applies as provided for by Section 1222 of the Internal Revenue Code.

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3. Wisconsin Taxation of Partnership Income Received by Part-Year Residents

Statutes: Section 71.07(1), 1985 Wis. Stats.

Note: See the Tax Release titled "Taxation of Partnership Income for Wisconsin Income Tax Purposes" in *Wisconsin Tax Bulletin* 41.

Facts And Question: A partnership is an association of two or more persons to carry on as co-owners of a business for profit. In a general partnership, all partners have equal rights in the management of the partnership business and may act on behalf of the partnership, and each partner can be held individually liable for obligations of the partnership. In a limited partnership, the activities of certain partners are limited, and the liabilities of these partners are limited to a stated amount. Wisconsin law requires one of the partners of a limited partnership to be a general partner with unlimited liability.

Under Internal Revenue Code Section 706(a), a partner must report his or her distributive share of partnership items or guaranteed payments in the partner's taxable year in which the partnership year ends.

How is partnership income taxed to part-year residents of Wisconsin?

Answer: For the portion of the partnership's taxable year the partner is a Wisconsin resident, the partner's share of all partnership income is taxable, regardless of the situs of the partnership or the nature of the partnership income, such as business income, service income or professional income, unless otherwise exempt (such as U.S. government interest). This applies both to general partners and to limited partners.

For the portion of the partnership's taxable year the partner is not a Wisconsin resident, the treatment depends on the situs of the partnership, the nature of the partnership income and the nature of the partner's interest in the partnership.

A. General Partners

That portion of the partnership income attributable to a business located in Wisconsin, services performed in Wisconsin, or rental property located in Wisconsin is taxable to nonresidents of Wisconsin. The income to be reported is based on the activities of the partnership and is not dependent upon whether or not the individual partner conducts business or performs services in Wisconsin. Section 71.07(1), 1985 Wis. Stats., provides that income or loss of nonresident individuals follows the situs of the business from which derived. Income from personal services of nonresidents, including income from professions, follows the situs of the services.

Example 1. An individual is a general partner, with a one-fifth interest in partnership profits, of a Certified Public Accounting Firm whose income is attributable one-fourth to professional services performed in Wisconsin and three-fourths to professional services performed in other states. The partner reports income on a calendar-year basis. The partnership reports income on an August 31 fiscal-year basis. The partner, who was a full-year Wisconsin resident in 1984, moved out of Wisconsin on August 1, 1985. The partnership books show a profit of $200,000 for its fiscal year ending August 31, 1985. Of that amount, $190,000 was attributable to the first 11 months of the fiscal year. After moving from Wisconsin, the partner does not personally perform any services in Wisconsin. The partner is taxed on $38,500, which is computed as follows: (a) one-fifth of all partnership income ($190,000) for the period from September 1, 1984 to August 1, 1985, plus (b) one-fifth of the $2,500 (1/4 of $10,000) of partnership income attributable to professional services performed in Wisconsin by the partnership for the period from August 1, 1985 through August 31, 1985.

Example 2. An individual is one of two equal general partners of a partnership whose income is attributable to a business located in Minnesota. The partner and the partnership report income on a calendar-year basis. The partner, who was a full-year Wisconsin resident in 1984, moved out of Wisconsin on June 1, 1985. The partnership books show a profit of $5,000 for the first 5 months of 1985.

The partner must file a 1985 Wisconsin return reporting all income (partnership income and any other income) until June 1, 1985. This includes $2,500 (1/2 of $5,000), which is the partner's distributive share of actual partnership income earned until June 1, 1985. Since the partnership business is located outside Wisconsin, no part of the partnership income for the period June 1, 1985 through December 31, 1985 is taxable to the partner for Wisconsin income tax purposes.

Example 3. A general partner owns a two-thirds interest in a partnership whose income is attributable to rental properties located in Iowa. The partner reports income on a calendar-year basis. The partnership reports income on a March 31 fiscal-year basis. The partner, who was a full-year Wisconsin resident in 1984, became an Iowa resident on August 1, 1985. The partnership books show a profit of $12,000 for the fiscal year ending March 31,

1985. In addition, the partnership books show a profit of $3,000 for the period from April 1, 1985 to August 1, 1985.

The partner must file a 1985 Wisconsin return reporting all income (partnership income and any other income) until August 1, 1985. This includes $8,000 (2/3 of $12,000), which is the partner's distributive share of the partnership income for the fiscal year ending March 31, 1985.

In addition, the partner must file a 1986 Wisconsin return and report $2,000 (2/3 of $3,000), which is the partner's distributive share of the partnership in come that was earned from April 1, 1985 to August 1, 1985. Under Section 706(a) of the Internal Revenue Code, if a partner's taxable year differs from the partnership's taxable year, the partner must report on his or her return the distributive share of partnership income for the partnership's fiscal year ending with or within the partner's taxable year.

B. Limited Partners

A nonresident limited partner in a partnership engaged in business in Wisconsin is not taxed on any income distributable to the partner from the partnership, provided that the partner is precluded from taking any part in the management of the business or affairs of the partnership and is not authorized to act for or bind the partnership in any way. If the partner is limited in this manner, the distribution of income represents income which follows the residence of the individual. Section 71.07(1), 1985 Wis. Stats., provides that income or loss of nonresident individuals from intangible personal property follows the residence of the individual. In the case *Sweitzer v. Revenue*, 65 Wis. 2d 235 (1974), the Wisconsin Supreme Court ruled that a limited partnership interest is analogous to the interest held by a corporate shareholder, resulting in intangible income which follows the residence of the recipient. Thus, a nonresident of Wisconsin is generally not taxed on income from a limited partnership.

Example. An individual owns a 10% interest as a limited partner of a partnership engaged in business in Wisconsin. The partner and the partnership report income on a calendar-year basis. The partner became a Wisconsin resident on September 1, 1985. The partner must file a 1985 Wisconsin return reporting all income (partnership income and any other income) for the period September 1, 1985 to December 31, 1985.

Even if an individual is defined as a "limited partner," if that individual may take part in any of the management of the business or affairs of the limited partnership, or is authorized to act for or bind the partnership in any way, the individual is treated the same as a nonresident general partner. The individual is taxed on his or her proportionate share of the partnership's Wisconsin income.

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4. Gain or Loss on the Sale of a Partnership Interest by a Nonresident

Statutes: Section 71.07(1), 1985 Wis. Stats.

Facts and Question 1: Taxpayer X is a resident of Illinois. Taxpayer X is a limited partner in a Wisconsin partnership and a general partner in another Wisconsin partnership. In 1986, Taxpayer X sells his partnership interests in both Wisconsin partnerships. Is the gain or loss Taxpayer X realized on the sale of the limited partnership interest taxable income to Wisconsin? Is the gain or loss Taxpayer X realized on the sale of the general partnership interest taxable income to Wisconsin?

Answer 1: The gain or loss from the sale of both the limited and general partnership interests is not taxable to Wisconsin. The limited partnership interest is considered intangible personal property. A general partnership interest is also considered to be intangible personal property.

Section 71.07(1), 1985 Wis. Stats., provides that income or loss from the sale of intangible personal property shall follow the residence of nonresidents.

Facts and Question 2: Taxpayer Y is a resident of Texas. Taxpayer Y is a limited partner in a Wisconsin partnership and a general partner in another Wisconsin partnership. In 1986, both partnerships sell all the assets of the partnership including land, buildings, office equipment and goodwill. Is Taxpayer Y's distributive share of the gain or loss realized on the sale of the assets by the limited partnership taxable to Wisconsin? Is Taxpayer Y's distributive share of the gain or loss realized on the sale of assets by the general partnership taxable to Wisconsin?

Answer 2: If a partnership sells its assets, the gain or loss realized on the sale is passed through to the partners. The gain or loss realized by the limited partnership is considered to be intangible income to a limited partner as a result of the Wisconsin Supreme Court case Sweitzer v. Revenue, 65 Wis. 2d 235 (1974). The gain or loss will follow the residence of a nonresident; therefore, Taxpayer Y will not report his or her share of the gain or loss from the sale of the limited partnership assets to Wisconsin (s. 71.07(1), 1985 Wis. Stats.).

Taxpayer Y's share of the gain or loss realized by the general partnership, other than goodwill, is taxable to Wisconsin. Section 71.07(1), 1985 Wis. Stats., provides that the income or loss from the sale of property of a nonresident follows the situs of the property. Because the property is located in Wisconsin, the gain or loss is reportable to Wisconsin by Taxpayer Y. Goodwill is an intangible asset; therefore, Taxpayer Y will not report his or her share of the gain from the sale of goodwill by the general partnership to Wisconsin.

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5. Advance Payment of Real Estate Taxes

Statutes: Section 71.53, 1983 Wis. Stats., and section 71.54, 1985 Wis. Stats.

Facts and Question: During 1984, Taxpayer A paid the following amounts for real estate taxes on his principal dwelling located in Milwaukee, Wisconsin:

1983 real estate taxes assessed (payable in 1984)	$2,500
1984 real estate taxes assessed (payable in 1985)	2,800
Estimated 1985 real estate taxes (payable in 1986)	2,300
Total Payment	$7,600

During 1985, Taxpayer A paid the following amounts for real estate taxes:

1985 real estate taxes assessed (payable in 1986) of $3,100 less the $2,300 paid in 1984	$ 800
Estimated 1986 real estate taxes (payable in 1987)	2,500
Total Payment	$3,300

During 1986, Taxpayer A pays the following amounts for real estate taxes:

1986 real estate taxes assessed (payable in 1987) of $3,400 less the $2,500 paid in 1985	$ 900
Estimated 1987 real estate taxes (payable in 1988)	1,100
Total Payment	$2,000

What is the allowable home owner's credit for 1984 and 1985, pursuant to s. 71.53, and the allowable home owner's credit for 1986, pursuant to s. 71.54?

Answer: Section 71.53, 1983 Wis. Stats., provides a 10% tax credit for real estate taxes paid by a claimant on the claimant's principal dwelling during the taxable year. For the 1986 taxable year, s. 71.54, 1985 Wis. Stats., provides a one-time 7.9% tax credit for up to $2,000 of real estate taxes paid by the claimant on the claimant's principal dwelling during the taxable year.

The Wisconsin Supreme Court in *Trepte v. Wisconsin Department of Revenue*, 56 Wis. 2d 81 (1972), concluded that "a tax prepayment can only be deducted in the year made—providing a liability exists for which a prepayment might be made." Therefore, prepayments of real estate taxes are merely deposits and a home owner's credit cannot be claimed until an actual liability arises and the deposit is applied to that liability.

The credit allowable to Taxpayer A each year is computed as follows:

1984:	1983 real estate taxes (payable in 1984)	$2,500
	1984 real estate taxes (payable in 1985)	2,800
	Total	5,300
		x 10%
	1984 Home Owner's Credit	$530
1985:	1985 real estate taxes (payable in 1986)	$3,100
		x 10%
	1985 Home Owner's Credit	$310
1986:	1986 real estate taxes (payable in 1987), but not more than $2,000	$2,000
		x 7.9%
	1986 Home Owner's Credit	$158

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INCOME AND FRANCHISE TAXES

1. Taxpayer Elections for Wisconsin Income and Franchise Taxes

Statutes: Sections 71.04(2b), (2d), (2e), (2f), (2g), (5), (8), (11), (15) and (16); 71.046; 71.047; 71.05(1)(h) and (i); 71.10(1)(b); 71.11(8) and (9); 71.305; 71.307; and 71.333, 1985 Wis. Stats.

Wis. Adm Code: Sections Tax 2.16, 2.19, and 2.83, September 1983 Register; sections Tax 2.20, 2.24, and 2.53, January 1956 Register; sections Tax 2.21, 2.25, 2.26, and 3.38, February 1975 register; section Tax 3.44, August 1970 Register; and section Tax 3.48, February 1978 Register.

Note: This Tax Release applies to all years open to adjustment unless otherwise noted.

Chapter 71, Wis. Stats., includes various provisions under which a taxpayer may elect one of several methods of claiming a deduction, reporting income, or filing a return. This Tax Release briefly describes each of the elections listed below, how the election is made, when it must be made and other related information. After the title of each election is listed the type of taxpayer to whom the election applies. (Example: "K. Iron Ore Depletion - Corporations" applies only to corporations.)

As used in this Tax Release, "corporation", as defined in s. 71.02 (1)(f), 1985 Wis. Stats., includes corporations, joint stock companies, associations or common law trusts organized or conducted for profit. References to statutes are to the Wisconsin Statutes, except where indicated otherwise.

NOTE: The elections listed in this Tax Release are not available to insurance companies, regulated investment companies and real estate investment trusts. Insurers compute taxable income under s. 71.01(4), 1985 Wis. Stats. Corporations or common law trusts which qualify as regulated investment companies or real estate investment trusts compute taxable incomes under s. 71.02(1)(c), 1985 Wis. Stats.

The following elections are covered in this Tax Release:

A. Waste Treatment Facilities - Corporations, Individuals, Estates and Trusts
B. Forest Croplands - Corporations
C. Renewable Energy Resource Systems - Corporations
D. Research or Experimental Expenditures - Corporations
E. Trademark or Trade Name Expenditures - Corporations
F. Organizational Expenses - Corporations
G. Ordered Charge Downs or Write-Offs - Corporations
H. Charitable Contributions - Corporations
I. Depreciation or Amortization - Corporations
J. Mineral Ores Depleton - Corporations
K. Iron Ore Depletion - Corporations
L. Installment Sales - Corporations
M. Percentage of Completion Method of Accounting - Corporations
N. Deferred Profit Method of Accounting - Corporations
O. Valuation of Inventories - Corporations
P. Declaration of Inactivity - Corporations
Q. Distributions of Stock and Stock Rights - Corporations and Individuals
R. Gain on Corporate Liquidation - Corporations and Individuals

A. WASTE TREATMENT FACILITIES - Corporations, Individuals, Estates and Trusts

Description: Corporations may elect a fast write-off of the cost of certified waste treatment plants and equipment located in Wisconsin, for three distinct periods of time: (1) prior to 1969, (2) 1969 through July 30, 1975, and (3) after July 30, 1975 (s. 71.04(2b) and (2g), 1985 Wis. Stats.).

Sections 71.05(1)(h) and (i), 1985 Wis. Stats., provide similar benefits to individuals, estates and trusts.

Prior to Taxable Year 1969: Section 71.04(2b), 1985 Wis. Stats., allows a corporation to write off in taxable year 1969 the remaining cost of a certified waste treatment plant or pollution abatement equipment installed prior to taxable year 1969.

Section 71.05(1)(h), 1985 Wis. Stats., allows individuals, estates and trusts a subtraction modification in taxable year 1969 for the federal adjusted basis, as of the end of taxable year 1968, of certified waste treatment plant or pollution abatement equipment.

Taxable Year 1969 Through July 30, 1975: For a certified waste treatment or pollution abatement plant or equipment purchased or constructed in taxable year 1969 and prior to July 31, 1975 (or purchased and constructed in fulfillment of a written construction contract or formal written bid made prior to July 31, 1975), a corporation may elect one of three methods of deducting the applicable costs. The three methods are as follows:

(1) Deduct the entire cost in the year paid or accrued, or
(2) Deduct one-fifth of the cost each year for a period of 5 years, or
(3) Depreciate.

To be deductible, the property must be depreciable, but where wastes are disposed of through a lagoon process, both the cost of lagooning and the cost of the land containing the lagoons may be written off under one of the three above methods.

Section 71.05(1)(h), 1985 Wis. Stats., allows individuals, estates and trusts to deduct as a subtraction modification in the years paid or accrued, dependent on the method of accounting employed, the cost of certified waste treatment plant or pollution abatement equipment (less any federal depreciation or amortization taken). In subsequent years, addition modifications must be made to reverse any federal depreciation or amortization, or to correct gain or loss on disposition.

After July 30, 1975: Under s. 71.04(2g), 1985 Wis. Stats., a corporation may elect one of the three methods listed above to deduct the cost of an approved facility in Wisconsin to treat industrial wastes or air contaminants, for the purpose of abating or eliminating pollution of the air and water of this state. The cost of lagooning, including land, may also be written off under one of the three prescribed methods.

Section 71.05(1)(i), 1985 Wis. Stats., allows individuals, estates and trusts to deduct as a subtraction modification in the year paid or accrued, dependent on accounting method, the cost of depreciable property purchased or constructed as an approved waste treatment facility utilized for the treatment of industrial wastes or air contaminants, for the purpose of abating or eliminating pollution of the air or water of this state. The cost of lagooning, including land containing lagoons, is considered deductible depreciable property for this purpose.

In subsequent years, addition modifications are required to reverse any federal depreciation or amortization, or to correct gain or loss on disposition.

When and How Election Made: For corporations, the election is made by either deducting, amortizing or depreciating the cost of the facility on a Wisconsin franchise/income tax return for the year in which the election is first available.

The election to take an immediate deduction is made on the tax return for the year in which the expenditures were paid or incurred, depending on the corporation's method of accounting.

Deductions for amortization or depreciation may begin either with the month following the month in which the facility is completed or acquired, or with the first month of the taxable year succeeding the taxable year in which such facility is completed or acquired.

Individuals, estates and trusts make the election by claiming the subtraction modification on a tax return filed for the year or years in which the costs are paid or incurred, depending on the method of accounting employed.

Changing or Revoking the Election: For corporations, the election to deduct under any of the three methods, once made, is irrevocable.

If depreciation is taken under s. 71.04(15), 1985 Wis. Stats., prior to approval of the facility under s. 70.11(21)(a), 1985 Wis. Stats., such depreciation is not an election under s. 71.04(2g), 1985 Wis. Stats. Once the facility is approved, an election to deduct under any one of the three methods of s. 71.04(2g), 1985 Wis. Stats., may be made. If years have intervened between the expenditure for the facility and approval of the facility, amended returns may be filed to claim whichever method of deduction is elected under s. 71.04(2g), 1985 Wis. Stats. Such amended returns must be filed within the 4-year statutory period provided by s. 71.11(21)(bm), 1985 Wis. Stats.

For individuals, estates and trusts, an election may be made, changed or revoked anytime within the 4-year statutory period in s. 71.11(21)(bm), 1985 Wis. Stats., by filing an amended return. In such case, addition modifications may also be required to subsequent returns to reverse federal depreciation or amortization, or to correct gain or loss on disposition.

Alternative Federal Election for Individuals: For taxable years 1977 through 1981, Wisconsin's reference to the Internal Revenue Code (IRC) ". . .does not include the changes to the code enacted by section 2112 (relating to tax treatment of certain pollution control facilities) of P.L. 94-455. . ." (s. 71.02(2)(d)3, 4, 5, 6, and 7, 1985 Wis. Stats.).

Effective for taxable year 1982 and thereafter, the above prohibition to amortize pollution control facilities under IRC Section 169 has been eliminated.

Therefore, an individual, estate or trust may (as an alternative to the one-year write-off under s. 71.05(1)(i), 1985 Wis. Stats.) elect the federal 60-month amortization allowable for a pollution control facility added to or used in connection with a plant in operation before 1976, pursuant to IRC Section 169.

B. FOREST CROPLANDS - Corporations

Description: Under s. 71.04(11), 1985 Wis. Stats., a corporation may elect to deduct currently, or defer until the crop or property is sold or disposed of, certain expenses relating to forest croplands. Forest croplands are those which come within the provisions of Chapter 77, Wis. Stats.

The expenses which may be deducted currently, or deferred, are those expended for the following:

(1) The purchase of seeds
(2) The purchase of tree plants
(3) Preparing land for planting
(4) Planting and caring for forest crops
(5) Maintaining forest crops
(6) Fire protection for forest crops

When and How Election Made: Notice of the election to deduct currently or to defer until the crop is sold, must be given to the department by a signed statement attached to the tax return for the first year in which the corporation is engaged in this activity. The statement should explain which election is chosen.

If a statement is not submitted, the treatment accorded the deduction on the first return will be deemed the election chosen. For example, if the expenses are deducted on the first return, subsequent expenses must be deducted currently. If expenses are not deducted on the first return, the election to defer will be deemed to have been made and all subsequent expenses must be deferred until the crop or property, or any portion thereof, is sold or disposed of.

Changing or Revoking Election: The method, once elected, is irrevocable.

C. RENEWABLE ENERGY RESOURCE SYSTEMS - Corporations

Description: Under s. 71.04(16), 1985 Wis. Stats., expenses incurred by a corporation during the period April 20, 1977 through taxable year 1979, for designing, constructing (including the cost of equipment) and installing a renewable energy resource system may be deducted in one of three ways. Such expenses may be:

(1) Fully deducted in year paid or incurred, or
(2) Depreciated over the system's useful life, or
(3) Amortized over a period of 5 years.

To qualify for the election, the system must be located in Wisconsin and be certified by the Department of Industry, Labor and Human Relations as meeting required performance standards.

When and How Election Made: The election is made on Wisconsin Schedule AE and filed with the franchise/income tax return for the taxable year in which expenses for the system were incurred.

If depreciation is claimed on a franchise/income tax return under s. 71.04(15), 1985 Wis. Stats., prior to the time of certification of the system under s. 101.57(3), 1981 Wis. Stats., such depreciation is not an election under 71.04(16), 1985 Wis. Stats. Once the system is certified under s. 101.57(3), 1981 Wis. Stats., an election to deduct under any one of the three methods in 71.04 (16), 1985 Wis. Stats., may be made. If years have intervened between the expenditure for the system and certification of the system by the Department of Industry, Labor and Human Relations, amended returns may be filed to claim whichever method of deduction is elected under 71.04(16), 1985 Wis. Stats. Such amended returns must be filed within the 4-year statutory period provided by s. 71.11(21)(bm), 1985 Wis. Stats.

Changing or Revoking Election: The election, once made, is irrevocable.

D. RESEARCH OR EXPERIMENTAL EXPENDITURES - Corporations

Description: Section 71.04(2f), 1985 Wis. Stats., allows a corporation to elect one of three methods of deducting certain expenditures for research and development costs (in the experimental or laboratory sense), incurred in a taxable year beginning after December 31, 1969. The three methods are as follows:

(1) Deduct the costs in the year paid or incurred, or
(2) Amortize the expenses ratably over not less than 60 months if the property to which they relate has no determinable life, or
(3) Depreciate over the useful life of the property to which the expenditures relate.

Wis. Adm. Code section Tax 3.48 explains the election in detail.

When and How Election Made: The election shall be made no later than the time (including extensions) prescribed by law for filing the return for the taxable year for which the method is to be adopted. The election to deduct the expenses currently (method 1 above) is made by claiming such expenses as a deduction on the franchise/income tax return for the year in which paid or incurred. The election to defer the deduction and to amortize over 60 months (method 2) is made by attaching a signed statement to the franchise/income tax return for the first taxable year to which the election applies. The signed statement shall include the following information required by Treas. Reg. section 1.174-4(b)(1):

(1) Set forth the name and address of the taxpayer;
(2) Designate the first taxable year to which the election is to apply;
(3) State whether the election is intended to apply to all expenditures within the permissible scope of the election, or only to a particular project or projects, and, if the latter, include such information as will identify the project or projects as to which the election is to apply;
(4) Set forth the amount of all research or experimental expenditures paid or incurred during the taxable year for which the election is made;
(5) Indicate the number of months (not less than 60) selected for amortization of the deferred expenses for each project; and
(6) State that the taxpayer will make an accounting segregation in its books and records of the expenditures to which the election relates.

Changing or Revoking Election: In order to change the method elected to deduct these expenses, or to change the amortization period, a written application must be sent to the Wisconsin Department of Revenue, Post Office Box 8906, Madison, Wisconsin 53708, and written approval received by the taxpayer before the change can be effected. The application shall include the name and address of the taxpayer, shall be signed by the taxpayer (or his duly authorized representative), and shall be filed no later than the last day of the first taxable year for which the change in method or period is to apply. The request for change of method must include the information required by Treas. Reg. section 1.174-3(b)(3), as follows:

(1) State the first year to which the requested change is to be applicable;
(2) State whether the change is to apply to all research or experimental expenditures paid or incurred by the taxpayer, or only to expenditures attributable to a particular project or projects;
(3) Include such information as will identify the project or projects to which the change is applicable;
(4) Indicate the number of months (not less than 60) selected for amortization of the expenditures, if any, which are to be treated as deferred expenses under section 174(b);
(5) State that, upon approval of the application, the taxpayer will make an accounting segregation on its books and records of the research or experimental expenditures to which the change in method is to apply; and
(6) State the reasons for the change.

If permission is granted to make the change, the taxpayer shall attach a copy of the letter granting permission to the franchise/income tax return for the first taxable year in which the different method is effective.

In addition to the above, an application for change to a different method or amortization period must set forth the following information required by Treas. Reg. section 1.174-4(b)(2), as follows:

(1) Total amount of research or experimental expenditures attributable to each project;
(2) Amortization period applicable to each project; and
(3) Unamortized expenditures attributable to each project at the beginning of the taxable year in which the application is filed.

In addition, the application shall set forth the length of the new period or periods proposed, or the new method of treatment proposed, the reasons for the proposed change, and such information as will identify the project or projects to which the expenditures affected by the change relate. If permission is granted to make the change, the taxpayer shall attach a copy of the letter granting the permission to the franchise/income tax return for the first taxable year in which the different method or period is to be effective.

E. TRADEMARK OR TRADE NAME EXPENDITURES - Corporations

Description: A corporation may elect, under s. 71.04(2e), 1985 Wis. Stats., and Wis. Adm. Code section Tax 3.43, to treat as a deferred expense and amortize over a period of not less than 60 months, commencing with the first month of the first taxable year covered by the election, certain expenses relative to trademarks or trade names. The expenses are those:

(1) Paid or incurred in a taxable year beginning after December 31, 1969, and
(2) Directly connected with the acquisition, protection, expansion, registration (federal, state or foreign), or defense of a trademark or trade name, and
(3) Chargeable to capital account, and
(4) Not part of the consideration paid for a trademark, trade name or business.

When and How Election Made: The election is made no later than the due date (including extensions) for filing the franchise/income tax return for the taxable year during which the expenditures are paid or incurred. No election may be made on amended returns filed after the due date (including any extensions) of the original return. A statement indicating the election chosen shall be attached to the return, setting forth the following information as required by Treas. Reg. section 1.177-1(c):

(1) Name and address of the taxpayer, and the taxable year involved;
(2) An identification of the character and amount of each expenditure to which the election applies and the number of continuous months (not less than 60) during which the expenditures are to be ratably deducted; and
(3) A declaration by the taxpayer that it will make an accounting segregation on its books and records of the trademark and trade name expenditures for which the election has been made, sufficient to permit an identification of the character and amount of each such expenditure and the amortization period selected for each expenditure.

Separate elections may be made with respect to each trademark or trade name expenditure.

Changing or Revoking Election: The election for a particular trademark or trade name expenditure, once made, is irrevocable. The period selected for amortization may not be changed after the date (including extensions) for filing the return, but must be adhered to in computing taxable income for the taxable year for which the election is made and all subsequent taxable years.

F. ORGANIZATIONAL EXPENSES - Corporations

Description: A corporation may elect under s. 71.04(2d), 1985 Wis. Stats., and Wis. Adm. Code section Tax 3.44 to treat organizational expenditures as deferred expenses subject to amortization over a period of not less than 60 months, beginning with the month in which the corporation begins business. The term "organizational expenditures" means any expenditure which:

(1) Is incident to the creation of the corporation;
(2) Is chargeable to capital account; and
(3) Is of a character which, if expended incident to the creation of a corporation having a limited life, would be amortizable over such life.

The following are not organizational expenditures:

(1) Expenditures connected with issuing or selling shares of stock or other securities, such as commissions, professional fees and printing costs. This is true even where the particular issue of stock to which the expenditures relate is for a fixed term of years.

(2) Expenditures connected with the transfer of assets to a corporation.
(3) Expenditures connected with the reorganization of a corporation, unless directly incident to the creation of a new corporation, as possibly in the case of a split-up or consolidation (but not a merger of existing corporations).

The expenses must have been paid or incurred on or after February 19, 1970 and in a taxable year beginning after December 31, 1969.

When and How Election Made: The election is made no later than the due date (including extensions) for filing the franchise/income tax return for the year in which the corporation began business. No elections may be made on amended returns filed after the due date (including extensions) for filing the original return. A statement shall be attached to the return containing the following:

(1) A description and amount of the expenditures to which the election applies;
(2) The dates on which the expenditures were incurred;
(3) The month in which the corporation began business;
(4) The number of months selected for the amortization period (not less than 60).

Changing or Revoking Election: The period selected for amortization may not be changed after the due date (including extensions) for filing the returns, but must be adhered to in computing taxable income for the taxable year for which the election is made and all subsequent taxable years.

G. ORDERED CHARGE DOWNS OR WRITE-OFFS - Corporations

Description: A corporation may elect under s. 71.04(8), 1985 Wis. Stats., to deduct the amount by which any asset has been charged down or written off by order of any state or federal regulatory authority, body, agency or commission which has the power to make such order, or by the examining committee of any state bank in accordance with s. 221.09. The deduction is not mandatory, but elective. An election to charge down or write off a single asset is deemed an election for purposes of all assets affected by the particular demand or order.

When and How Election Made: The election is made by deducting the amount charged down or written off, consistent with the demand or order, in the franchise/income tax return covering the first taxable year in which the charge-down or write-off is demanded or ordered. The entire amount is deducted in that year. Even though federal law may allow or require an amortization over a period of months, s. 71.04(8), 1985 Wis. Stats., provides for a one-year write-off.

The election is available any time within the 4-year statute of limitations pursuant to s. 71.11(21)(bm), 1985 Wis. Stats. If a deduction or amortization was claimed incorrectly on a return, amended returns may be filed as appropriate.

If no deduction is taken, no election is made, and the cost remains a capital asset.

Upon a subsequent sale, exchange, or other disposition of either the asset or the business to which it relates, the remaining adjusted cost basis of the asset is deductible in determining any recognized gain or loss, pursuant to s. 71.03(1)(g), 1985 Wis. Stats.

Changing or Revoking Election: The election, once made, is irrevocable.

H. CHARITABLE CONTRIBUTIONS - Corporations

Description: Section 71.04(5)(b), 1985 Wis. Stats., provides to corporations reporting on the accrual method the option of electing to deduct charitable contributions in the year of authorization rather than the year of payment under s. 71.04(5)(a), 1985 Wis. Stats. The election to take the deduction in the year of authorization is permissible if the following two conditions are met:

(1) The contributions must have been authorized by the corporation's board of directors prior to the end of the taxable year, and
(2) Payment must be made on or before the 15th day of the third month after the close of the taxable year.

The deduction is limited to an amount not in excess of 5% of the corporation's net income for the taxable year computed without the benefit of the deduction.

When and How Election Made: The election is made by claiming a deduction on the franchise/income tax return filed by the due date (including extensions) for the year of authorization. No election is permitted on amended returns filed after the due date (including extensions) of the original return. A written notice should be attached to the return specifying the date of authorization, the name and address of the contributee and the date of the actual payment.

Changing or Revoking Election: The election, once made, is irrevocable.

I. DEPRECIATION OR AMORTIZATION - Corporations

Description: Section 71.04(15), 1985 Wis. Stats., provides that for taxable year 1972 and thereafter, corporations are limited to depreciation or amortization on depreciable property in the amount allowable as a deduction from gross income under the Internal Revenue Code for federal income tax purposes. Exceptions are made for pollution abatement plants and equipment, waste treatment facilities, renewable energy resource systems, intangible drilling and development costs, certain public utility property, and safe harbor leases.

Corporations are granted an option to compute depreciation or amortization under the Internal Revenue Code in effect for the current year, or the Code for 1972 (s. 71.04(15)(b), 1985 Wis. Stats.).

Section 71.04(15)(b), 1985 Wis. Stats., was amended effective for property first placed in service on or after January 1, 1983. For property located outside of Wisconsin and placed in service on or after January 1, 1983, ACRS is not allowed for Wisconsin

franchise/income tax purposes. Instead, depreciation for out-of-state property first placed in service by a corporation on or after January 1, 1983 must be computed under the methods permitted by the Internal Revenue Code in effect on December 31, 1980 or, in the alternative, the IRC applicable to the calendar year 1972.

How the Option is Made: The option to compute depreciation under the Internal Revenue Code in effect for 1972, rather than for the current year, is made by taking the deduction on a franchise/income tax return and indicating thereon that the amount is computed under the Internal Revenue Code in effect for 1972.

Changing or Revoking Option: Generally, a change in the method of computing depreciation is a change in method of accounting. Since corporation depreciation generally is federalized, if the Internal Revenue Service grants approval for a depreciation change, such approval is automatic for Wisconsin. However, if the corporation is computing depreciation for Wisconsin tax purposes under the Internal Revenue Code in effect for 1972, and it desires to change to another method for Wisconsin purposes, approval for such change must be obtained from the Department of Revenue, pursuant to Wis. Adm. Code section Tax 2.16.

NOTE: Beginning with the taxable year 1983, section 48(q) of the Internal Revenue Code provides that the basis of assets, for purposes of computing depreciation or ACRS deductions and for gain or loss, must be reduced by one-half of the regular investment tax credit claimed and allowed. As an alternative to basis reduction, a corporation may claim a reduced investment credit and claim depreciation on the full cost of the assets. For Wisconsin franchise/income tax purposes, a corporation that claims the higher investment tax credit (and makes a reduction in the basis of its assets) can elect one of the following:

(1) Claim the same depreciation for Wisconsin as it does for federal tax purposes and get a deduction for the basis difference in the year of disposition pursuant to s. 71.04(15)(e), 1985 Wis. Stats., or
(2) Assume for Wisconsin tax purposes that the reduced tax credit was claimed for federal purposes and therefore claim depreciation on the higher basis.

If a corporation chooses to claim the reduced investment tax credit on its federal return, depreciation will be claimed on the same full cost of the assets for both federal and Wisconsin income purposes. Refer to *Wisconsin Tax Bulletin* 35, dated January 1984, for further details.

J. MINERAL ORES DEPLETION - Corporations

Description: Corporations engaged in Wisconsin in the mining, milling or smelting of lead, zinc, copper or other metals (including sulphur and iron from processing such metals) except iron, are allowed to deduct percentage depletion in lieu of cost depletion (s. 71.046, 1985 Wis. Stats.).

In order to claim a deduction for percentage depletion, the mine must have had gross income from sales of ore and ore products of at least $100,000 in taxable year 1976. The deduction allowed in subsequent years is based on a diminishing percentage of the 1976 deduction, and the deduction is completely eliminated after nine years. The statute is effective until January 1, 1988.

The tax savings attributable to the depletion allowance must be used in prospecting for ore in Wisconsin, with proof furnished to the Department of Revenue (Wis. Adm. Code section Tax 3.38).

When and How Election Made: The election to deduct percentage depletion in lieu of cost depletion is made by claiming the deduction on a franchise/income tax return filed for the taxable year of claim.

Changing or Revoking Election: A change in the method of depletion is generally considered a change in the method of accounting and therefore approval is required from the Department of Revenue (Wis. Adm. Code section Tax 2.16).

K. IRON ORE DEPLETION - Corporations

Description: Corporations engaged in the mining of low grade iron ore in Wisconsin are allowed to deduct percentage depletion in lieu of cost depletion, pursuant to s. 71.047, 1985 Wis. Stats.

In order to claim a deduction for percentage depletion, the corporation must have had gross income from mining low grade iron ore, of at least $100,000 in taxable year 1976. The deduction allowed in subsequent years is based on a diminishing percentage of the 1976 deduction, and the deduction is completely eliminated after nine years. The statute is effective until January 1, 1988.

When and How Election Made: The election to deduct percentage depletion in lieu of cost depletion is made by claiming the deduction on a franchise/income tax return filed for the taxable year of claim.

Changing or Revoking Election: A change in the method of depletion is generally considered a change in the method of accounting and therefore approval is required from the Department of Revenue (Wis. Adm. Code section Tax 2.16).

L. INSTALLMENT SALES - Corporations

Description: Subject to approval by the Department of Revenue, a corporation may elect to report the profit from the sale of real estate, or from a casual sale of personal property for a price exceeding $1,000, on the installment method, pursuant to s. 71.11(8), 1985 Wis. Stats., and Wis. Adm. Code section Tax 2.19. To qualify for this method, payments in the first income year of sale may not exceed 30% of the selling price. The profit to be reported is the proportion of the installment payments received in the taxable year which the total gross profit bears to the contract price.

Corporations regularly engaged in the business of selling personal property and keeping records on the installment basis are required to report on the accrual basis for Wisconsin tax purposes.

When and How Election Made: The election to report gain from the sale of real estate or casual sales of personal property on the installment method is made by the corporation when it files its franchise/income tax return for the year in which the sale was made. It is not necessary to obtain authorization from the Department of Revenue. A corporation which elects to report qualifying gain on the installment method may assume that approval is granted unless notified otherwise by the department.

Changing or Revoking Election: A corporation electing to report the profit on a sale on the accrual method will not be permitted to change to the installment method at a later date.

M. PERCENTAGE OF COMPLETION METHOD OF ACCOUNTING - Corporations

Description: Most incorporated contractors are required to report their taxable incomes on the accrual basis. A variation of this method is allowed in computing income from contracts on which work is performed in two or more taxable years. This method is called the percentage of completion method and may be used by contractors if such method clearly reflects income pursuant to s. 71.11(8), 1985 Wis. Stats., and Wis. Adm. Code section Tax 2.21.

Under this method, a portion of the total contract price is treated as sales for the current period, based upon the percentage of completion which is usually determined by an engineer's or architect's estimate. Actual costs, adjusted for inventories of materials on hand at the end of the years, are deducted from the sales to compute taxable income.

When and How Election Made: The election to report on the percentage of completion method is generally made on the first franchise/income tax return filed by the contractor. However, if the contractor has previously reported under another accounting method, a change to the percentage of completion method represents a change in method of accounting which requires prior approval (see "Changing or Revoking Election").

Changing or Revoking Election: A method of accounting may not be changed without written approval of the department. For example, a change from the percentage of completion method to the completed contract method, or vice versa, requires departmental approval prior to the change (Wis. Adm. Code section Tax 2.16).

NOTE: The "completed contract" method is another method of accounting used by incorporated contractors. Although not authorized by rule, the same provisions for making, changing or revoking the election apply to the completed contract method as stated above for the percentage of completion method.

N. DEFERRED PROFIT METHOD OF ACCOUNTING - Corporations

Description: Acceptance corporations and dealers in commercial paper may elect to report their taxable incomes on the deferred profit basis, provided the books are kept on this basis and that both income and attributable expenses are deferred, pursuant to Wis. Adm. Code section Tax 2.20(3) and s. 71.11(8), 1985 Wis. Stats.

Under the deferred profit method, the discount on purchase of commercial paper is credited initially to a deferred profit account, and is transferred from this account to earned income ratably over the life of the paper.

When and How Election Made: Acceptance corporations and dealers in commercial paper reporting on the accrual method do not have to obtain authorization from the Department of Revenue to change to the deferred profit method. To effect the change, the taxpayer must notify the department in writing, before the close of the year in which the change is to be made, of the taxpayer's intent to report on the deferred profit method.

Schedules must be attached to the franchise/income tax return clearly setting forth the unrealized profit accounts and reconciling the income and retained earnings per books with taxable income.

Changing or Revoking Election: The deferred profit method, once elected, must be adhered to consistently thereafter.

O. VALUATION OF INVENTORIES - Corporations

Description: Section 71.11(9), 1985 Wis. Stats., provides that inventories shall be taken whenever, in the opinion of the Department of Revenue, their use is necessary to clearly determine income.

Wis. Adm. Code section Tax 2.25 authorizes the use of (1) the cost method and (2) the lower of cost or market method. Wis. Adm. Code section Tax 2.24 authorizes the retail method of inventory valuation for retail merchants. Wis. Adm. Code section Tax 2.26 authorizes the LIFO (last-in, first-out) method of identifying the particular goods in inventory.

A corporation may elect a method of inventory valuation which conforms to the best accounting practice in the particular trade or business and which clearly reflects income, pursuant to the above law and rules.

When and How Election Made: A new corporation selects the inventory valuation method which it will use when it files its first franchise/income tax return.

An election to use the LIFO method of identifying inventories can be made by filing an application with the Department of Revenue in substantially the same form as required by the Internal Revenue Service. It must be filed with the return for the taxable year as of the close of which the method is first to be used.

Treas. Reg. section 1.472-3 provides that the required statement be made on Form 970 pursuant to the instructions thereon and the requirements of the regulation, or in such manner as may be acceptable to the Internal Revenue Service commissioner. An analysis of beginning and ending inventories is also required by regulation. All provisions of the federal regulation apply for Wisconsin tax purposes.

Changing or Revoking Election: A method of inventory valuation, once chosen, must be adhered to consistently thereafter. Except for corporations reporting on the LIFO method, no change from one method to another can be made without written permission from the Department of Revenue.

Corporations reporting on the LIFO method of valuing inventories, which have been authorized or directed by the Internal Revenue Service to change their method of inventory valuation, shall also do so for Wisconsin tax purposes. Notice of the change in method must be filed with the franchise/income tax return on which it is effective. A copy of the federal authorization or order to change must also be attached to the return (Wis. Adm. Code section Tax 2.26(6)).

P. DECLARATION OF INACTIVITY - Corporations

Description: Section 71.10(1)(b), 1985 Wis. Stats., permits a corporation which has been completely inactive (both within and without Wisconsin) for an entire taxable year to file a Declaration of Inactivity (Form 4H) in lieu of filing a regular franchise/income tax return (Form 4, Form 5, Form 5A). Thereafter, the corporation need not file a franchise/income tax return or Form 4H for any subsequent year unless requested to do so by the Department of Revenue or unless in a subsequent year the corporation has been activated or reactivated.

When and How Election Made: The election is made by filing Form 4H with the Department of Revenue on or before the 15th day of the third month following the close of the taxable year. If not filed by the due date, a $10 late filing fee is due. If Form 4H is due on or after July 20, 1985 and is filed 60 or more days late, a $20 late filing fee is due.

Form 4H should be mailed to the Wisconsin Department of Revenue, Post Office Box 8908, Madison, Wisconsin 53708.

Section 71.10(1)(b), 1985 Wis. Stats., provides a civil penalty of $25 against the corporate officers, jointly and severally, for filing a false declaration, or for each failure to file a franchise/income tax return or to file required information returns, upon activation or reactivation.

Changing or Revoking Election: If the corporation is activated or reactivated, the corporation is required to file regular franchise/income tax returns thereafter, pursuant to s. 71.10(1), 1985 Wis. Stats.

Q. DISTRIBUTIONS OF STOCK AND STOCK RIGHTS - Corporations and Individuals

Description: Section 71.305(1), 1985 Wis. Stats., provides, under a general rule, that a distribution to shareholders by a corporation of its stock or rights to acquire stock, is not taxable. However, a distribution in lieu of money is taxable under s. 71.305 (2), 1985 Wis. Stats., if:

(1) In discharge of preference dividends, or
(2) The shareholder elects to receive stock (or stock rights), or property.

Section 71.307(1), 1985 Wis. Stats., provides that if the distribution of stock (or rights) is not taxable, the basis of the new stock is determined by allocating the basis of the old stock between the old and new stock.

Section 71.307(2), 1985 Wis. Stats., provides that if the fair market value of the stock rights is less than 15% of the fair market value of the old stock, the above allocation is not made and the basis of the rights will be zero. However, a shareholder may elect to allocate the basis between the old stock and the new rights.

When and How Election Made: The election to allocate part of the basis of the old stock to the rights is made by attaching a statement to the shareholder's franchise/income tax return filed by the due date (including extensions) for the years in which the rights are received.

Pursuant to Wis. Adm. Code section Tax 2.53, the statement must contain the following information:

(1) The number of old shares owned on the distribution date,
(2) The basis of the old shares, and
(3) The fair market value of the old shares, and of the rights, on the distribution date.

The election is made with respect to all rights received in a particular distribution in respect of all stock of the same class owned in the issuing corporation at the time of such distribution.

Changing or Revoking the Election: The election, once made, is irrevocable.

R. GAIN ON CORPORATE LIQUIDATION - Corporations and Individuals

Description: Section 71.333, 1985 Wis. Stats., provides that qualified electing shareholders (corporate or non-corporate) may avail themselves of partial non-recognition of gains on property distributed within one calendar month in complete liquidation of a corporation.

A corporate shareholder qualifies if corporate shareholders owning 80% of the combined voting power owned by corporate shareholders (other than excluded corporations) have filed written notices of election. If the owners of 80% or more have elected, then all which have elected qualify. An excluded corporation is one which, at any time between January 1, 1955 and the date of adoption of a plan of liquidation, owned 50% or more of the combined voting power of all classes of stock of the liquidating corporation.

A non-corporate shareholder qualifies if notices of election have been filed by such shareholders owning 80% or more of the total combined voting power owned by all non-corporate shareholders.

Qualified electing shareholders are taxed on their gain only to the extent of the greater of the following:

(1) The portion of the assets received which consists of money, or of stock or securities acquired by the liquidating corporation after January 1, 1955, or
(2) The shareholder's ratable share of the earnings and profits of the liquidating corporation accumulated after January 1, 1911, determined as of the close of the month in which liquidation occurs, without reduction for any distributions made during the month.

When and How Election Made: Wis. Adm. Code section Tax 2.83 provides that, to qualify for the benefits of s. 71.333, 1985 Wis. Stats., a qualified electing shareholder must file with the Wisconsin Department of Revenue within 30 days of the adoption of the plan of liquidation, a copy of federal Form 964 "Election of Shareholder Under Section 333 Liquidation" in accordance with the instructions thereon.

Another copy of the federal Form 964 must be attached to the shareholder's Wisconsin income or franchise tax return for the taxable year in which the transfer of all the property under the liquidation occurs.

The completed Forms 964 should be mailed to the Wisconsin Department of Revenue, Post Office Box 8908, Madison, Wisconsin 53708.

Changing or Revoking the Election: The election, once made, is irrevocable.

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2. Limitations on Travel, Entertainment and Gift Expenses

Statutes: Sections 71.01(4)(a)6m, 71.04(2)(b) and 71.05(1)(a)27, 1985 Wis. Stats .

Note: This Tax Release applies only with respect to taxable years 1986 and thereafter.

Background: Sections 71.01(4)(a)6m., 71.04(2)(b) and 71.05(1)(a)27., 1985 Wis. Stats., were created by 1985 Wisconsin Act 29. These statutes provide the following:

A. Deductions are not allowed for entertainment expenses other than admissions to organized athletic events or other public events or performances that take place in Wisconsin.

B. Deductions for business meals are limited to those meals which occur in a clear business setting. The amount deductible is limited to $25 plus half the meal expense over $25 per meal per person.

C. Deductions are not allowed for travel expenses of trips lasting one year or more in one city.

D. Deductions are limited for travel by luxury water transportation.

E. Deductions are not allowed for travel expenses in regard to conventions, meetings or seminars held on cruise ships unless such expenses are paid by an employer and the payment is treated as wages paid to an employe.

F. Deductions are not allowed for travel as a form of education.

G. Deductions for business gifts are not allowed other than for gifts of Wisconsin agricultural commodities not to exceed $15 per gift per recipient.

The limitations in A through F above apply to individuals (employes and self-employed persons), partnerships, tax-option (S) corporations, estates, trusts and corporations. Item G above applies only to corporations, including tax-option (S) corporations.

This tax release is divided into eight parts. The first part illustrates how the limitations apply in reimbursement situations. The remaining parts explain each of the above limitations (A-G) individually.

Part I

GENERAL When a reimbursement situation exists between an employe and an employer or between an independent contractor and customers or clients, the limitations on entertainment, business meals, travel or gift expenses apply as explained below. A chart at the end of this tax release summarizes the various reimbursement situations between an employer and employe.

Question 1: Will the travel, entertainment, business meal and gift expense limitations apply to an employe, employer, or both when an employe is being fully reimbursed by his or her employer for expenses which are fully or partially nondeductible for Wisconsin tax purposes?

Answer 1: The limitations apply only to the employer except as described below. It makes no difference whether the employe "accounts" or "does not account," per federal definitions, to his or her employer.

Exception: If the employer treats the expenditure as compensation and wages paid to the employe, the limitations apply to the employe, not the employer.

Example 1: An employe incurs expenses for entertainment that are deductible for federal tax purposes but not deductible for Wisconsin tax purposes. The employer reimburses the employe for the entire entertainment expense but does not treat the reimbursement as wages. The limitations on the entertainment will apply to the employer.

Example 2: Assume the same facts as in Example 1 except that the employer includes the reimbursement as wages on the employe's W-2 form. The Wisconsin limitation will apply to the employe, not to the employer.

Question 2: Will the limitations apply to an employe, an employer or both when an employe is partially reimbursed by his or her employer for an expense which is completely nondeductible for Wisconsin tax purposes?

Answer 2: The limitations apply to both the employe and employer except as described below. The employer may not deduct the portion of the expense reimbursed. The employe may not deduct the portion of the expense for which he or she did not receive reimbursement.

Exception: If the reimbursement is treated as compensation and wages paid to the employe, the limitations apply to the employe, not the employer.

Example 1: An employe incurs $1,000 of entertainment expenses that are not deductible for Wisconsin tax purposes. His or her employer reimbursed $600 of the expenses and did not treat the reimbursement as compensation and wages. Neither the employe nor the employer is allowed to deduct the entertainment expenses. The employer may not deduct the $600 reimbursement paid to the employe. The employe may not deduct the $400 ($1,000 – $600) of net expense he or she incurred.

Example 2: Assume the same facts as in Example 1 except the employer includes the reimbursement as wages on the employe's W-2 form. The employer deducts $1,000 as wage expense. The employe reports the $1,000 as wages but may not claim any deduction for the entertainment expenses.

Question 3: Will the limitations apply to an employe, employer or both when an employe is partially reimbursed by his or her employer and only a portion of the expense incurred by the employe is not deductible for Wisconsin tax purposes?

Answer 3a: If the expense relates solely to the employe (e.g., meal expenses incurred by an employe in travel status who eats alone), and

a) Reimbursement exceeds the portion of total expense allowable as a deduction - the limitations apply to both the employer and employe. The employer may not deduct the portion of the reimbursement that exceeds the deductible expense. The employe may not deduct the portion of the expense for which he or she did not receive reimbursement.

Exception: If the employer treats the expense as compensation and wages paid to the employe, the limitations apply to the employe, not the employer.

b) Reimbursement does not exceed the portion of total expense allowable as an expense - the limitations apply only to the employe.

Example 1: An employe in travel status incurs a meal expense of $50 and was reimbursed $40 by his or her employer. The employe dined alone. The deductible meal expense is $37.50 ($12.50, which is one-half of the $50 expense exceeding $25, is not deductible). The employer's deduction for the meal reimbursement is limited to $37.50. Therefore, the employer is not allowed to deduct $2.50 ($40 – $37.50) of the reimbursement paid to the employe. The employe is not allowed to deduct the $10 ($50 – $40) of expense for which he or she did not receive reimbursement.

Example 2: Assume the same facts as Example 1 except that only $37.50 of the meal expense was reimbursed by the employer. The employer would be allowed to deduct the full reimbursement because the amount reimbursed did not exceed the portion of total expense deductible. The employe is not allowed to deduct $12.50 ($50 – $37.50) of the total expense he or she paid.

Answer 3b: If the expense relates to the employe and others (e.g., customers or clients), the limitations apply to both the employe and employer except as described below. The employer may not deduct a portion of the reimbursement based on the following equation:

$$\frac{\text{Reimbursement}}{\text{Total expense}} \times \text{Expense not deductible} = \text{Amount which may not be deducted}$$

The employe may not deduct a portion of his or her expense based on the following equation:

$$\frac{\text{Expense not reimbursed}}{\text{Total expense}} \times \text{Expense not deductible} = \text{Amount which may not be deducted}$$

Exception: If the expense is treated as compensation and wages paid to the employe, the limitations apply to the employe, not the employer.

Example 1: An employe receives a monthly allowance of $1,000 which is used to entertain clients. The employe incurs $1,500 of expenses. A nondeductible amount of $600 is determined for Wisconsin purposes. The employe may not deduct $200 ($500/$1,500 x $600). The employer may not deduct $400 ($1,000/$1,500 x $600).

Example 2: Assume the same facts as in Example 1 except that the employer treats the reimbursement as wages on the employe's W-2 form. The employer deducts $1,000 as wage expense. The employe reports the $1,000 as wages and may claim a deduction of $900 ($1,500 – $600).

Question 4: An employe receives no reimbursement from his or her employer for entertainment expenses he or she incurred. The entertainment expenses are deductible for federal tax purposes and are partially or fully not deductible for Wisconsin tax purposes. Do the limitations apply to the employe, employer or both?

Answer 4: The limitations apply only to the employe.

Question 5: Will the limitations apply to an independent contractor, his or her customers or clients, or both when an independent contractor is being reimbursed by his or her customers or clients for expenses not deductible for Wisconsin tax purposes?

Answer 5: If the independent contractor does not "account" (itemize all expenses) to the client or customer, the limitations apply to the independent contractor. If the independent contractor does "account" to the client or customer, the limitations apply to the client or customer.

Example 1: A manufacturer's representative deducts certain travel expenses for federal tax purposes that are not deductible for Wisconsin tax purposes. The manufacturer's representative accounts to his or her client itemizing all expenses he or she incurred. The client reimburses the manufacturer's representative for the entire amount of travel expenses he or she incurred. The limitations apply to the client.

Example 2: Assume the same facts as Example 1 except the manufacturer's representative does not account to his or her client; instead, the client gives the independent contractor a monthly allowance to use as he or she wishes. The limitations apply to the manufacturer's representative.

Question 6: A multistate company incurs various expenses for travel, business meals, entertainment and gifts that are deductible for federal purposes but are not deductible for Wisconsin tax purposes. Will the limitations apply to only those expenses relating to Wisconsin or to all expenses incurred by the multistate company?

Answer 6: All travel, entertainment and gift expenses, whether or not the expenses are incurred in Wisconsin or elsewhere or by employes located in Wisconsin or elsewhere, are subject to the Wisconsin limitations.

Question 7: A Wisconsin taxpayer is a partner in an out-of-state partnership. The partnership incurs various travel and entertainment expenses that are not deductible for Wisconsin tax pur-

poses. The partnership does not file Wisconsin partnership returns and is not required to do so. To whom do the Wisconsin limitations apply?

Answer 7: Because the partnership is incurring the expense, the partnership would be subject to the Wisconsin limitations; however, this is not possible because the partnership does not file a Wisconsin partnership return. The Wisconsin partner of a partnership which conducts no business in Wisconsin is not subject to the limitations on his or her Wisconsin individual income tax return. This principle will also apply to a Wisconsin shareholder in an out-of-state tax-option (S) corporation that is not required to file a Wisconsin franchise or income tax return.

Part II

ENTERTAINMENT EXPENSES (Sections 71.01(4)(a)6m. a., 71.04(2)(b)11 and 71.05(1)(a)27.a, 1985 Wis. Stats.). Expenses allowable for federal tax purposes with respect to an activity, except admissions to an organized athletic event or other public event or performance that takes place in Wisconsin, that is of the type generally considered to constitute entertainment, amusement or recreation, or with respect to a facility used in connection with those activities, except to the extent that food, beverage and facility expenses are allowed as a deduction for business meals (see Part IV, BUSINESS MEALS, below), are not deductible for Wisconsin tax purposes.

Question 1: For purposes of entertainment expense limitations, will entertainment meals be subject to the entertainment expense limitations?

Answer 1: No. Expenses for all meals are subject to the limitations explained in Part IV, "BUSINESS MEALS", below.

Question 2: The law relating to entertainment expense provides that entertainment expenses are generally not deductible except for certain admission expenses and to the extent that food, beverage and facility expenses are allowed as a deduction for business meal expenses. Since there is no mention of facility expense in the business meal portion of the law, are facility expenses allowed as entertainment deductions?

Answer 2: No. Facility expenses are not allowed as a deduction with one exception. Expenses for facilities used in providing meals for employes, on an employer's premises, are still deductible in full as stated in the Part IV, "BUSINESS MEALS" introduction, below.

Question 3: A taxpayer owns a yacht which is used exclusively for entertaining clients. For federal tax purposes, the taxpayer deducts interest on a loan used to purchase the yacht. The operating expenses (including depreciation) are not deductible for federal tax purposes. May the taxpayer deduct the interest for Wisconsin tax purposes?

Answer 3: No. Interest paid on a loan used to purchase an entertainment facility is not deductible for Wisconsin tax purposes. While federal law as of December 31, 1985 provides that interest, taxes and casualty losses on an entertainment facility used in connection with a trade or business are deductible, Wisconsin law does not allow a deduction for all expenses with respect to an entertainment facility.

Question 4: A company owns a swimming pool which is used primarily by its employes. For federal tax purposes, the taxpayer deducts all interest, taxes and the costs of operating the pool, including depreciation and maintenance. The company sells the pool in 1986 and claims a loss on its federal tax return. Are any of the expenses or the loss on the sale allowable for Wisconsin purposes?

Answer 4: No. A loss on the sale of an entertainment facility is an expense with respect to the facility. Thus for Wisconsin tax purposes the taxpayer may not deduct the loss on the sale of the swimming pool or any of the expenses for interest, taxes and operating costs, including depreciation and maintenance.

Question 5: A taxpayer incurs expenses in giving a party (e.g., Christmas party, summer picnic) to his or her employes. The taxpayer deducts the cost on his or her federal income tax return. Do the Wisconsin entertainment limitations apply?

Answer 5: No. Such entertainment is considered to be a "de minimus fringe benefit." These fringe benefits are considered to be wages and compensation to the employe but are excluded from the employe's federal income. Because such entertainment is considered wages and compensation to employes, the limitations on entertainment expenses do not apply.

Question 6: An employe, who is an outside salesperson, takes several customers to the local golf course to play golf and discuss business. The cost of the outing is $125. The employe is reimbursed $50 by his or her employer which is not treated as wages on the employe's W-2 form. The employe takes a deduction on his or her federal tax return of $75 and the employer takes a deduction of $50 for federal tax purposes. How will the limitations apply for Wisconsin tax purposes?

Answer 6: The cost of golfing is a nondeductible entertainment expense for Wisconsin tax purposes. The employe and employer will not be allowed their entire deductions of $75 and $50, respectively, for Wisconsin tax purposes.

Part III

BUSINESS GIFTS (Sections 71.01(4)(a)6m.b and 71.04(2)(b)12, 1985 Wis. Stats.). Business gifts allowable for federal tax purposes are not deductible for Wisconsin tax purposes except for business gifts of Wisconsin agricultural commodities, not to exceed $15 per recipient per year.

Note: These provisions apply only to corporations, including tax-option (S) corporations.

Question 1: What are Wisconsin agricultural commodities?

Answer 1: Wisconsin agricultural commodities are defined in s. 96.01(3), 1985 Wis. Stats., as "any agricultural, horticultural (excepting floriculture), viticultural, vegetable, poultry and livestock produced in this state, including milk and milk products, bees and honey, or any class, variety or utilization thereof, either in their natural state or as processed by a producer for the purpose of marketing such product or by a processor, but not including timber and wood products."

Question 2: A corporation gives each of its clients a gift pack of California wines, each gift costing $25. It gives these to 100 clients and deducts $2,500 as gift expenses for federal income tax purposes. Are the business gifts deductible for Wisconsin tax purposes?

Answer 2: No. The entire business gift expense is not deductible because the wine is not a Wisconsin agricultural commodity.

Question 3: Assume the same facts as in question 2 except that the wine is Wisconsin wine. Are the business gifts deductible for Wisconsin tax purposes?

Answer 3: A portion of the business gift expense is deductible because the wine is a Wisconsin agricultural commodity. The amount deductible is $1,500 (100 gifts x $15 limit).

Question 4: A manufacturer's representative, who is an independent contractor, makes business gifts to ten customers on behalf of a corporate client. The gifts are not Wisconsin agricultural commodities and cost $200. The independent contractor accounts to his or her corporate client and receives a reimbursement of $150 from the corporate client. Do the Wisconsin business gift limitations apply?

Answer 4: The Wisconsin business gift limitations will apply as follows:

a. The independent contractor is not subject to the business gift limitations because ss. 71.01(4)(a)6m.b and 71.04(2)(b)12, 1985 Wis. Stats., do not apply to individuals.

b. The corporate client is subject to the business gift limitations and therefore, is not allowed a deduction for the $150 reimbursement because the independent contractor accounted to the corporate client.

Part IV

BUSINESS MEALS (Sections 71.04(4)(a)6m.c, 71.04(2)(b) 13 and 71.05(1)(a)27.c, 198 5 Wis. Stats.). Business meals deductible for federal tax purposes are not deductible for Wisconsin tax purposes unless they are incurred in a clear business setting. In addition, business meals incurred in a clear business setting are limited to $25 per meal per person, including tax and gratuities. Fifty percent of the amount over the $25 limit is also allowed as a deduction for Wisconsin tax purposes. This provision does not apply to expenses for food and beverages furnished primarily for employes on the taxpayer's premises.

Question 1: A taxpayer takes five associates to a nightclub, which includes a floor show, for dinner. A substantial business discussion occurred earlier in the day. The cost of the meal, including tax and gratuities, is $50 per person and is deductible for federal tax purposes. The taxpayer deducts $300 on his or her federal income tax return. What amount is deductible for Wisconsin tax purposes?

Answer 1: No deduction is allowed for Wisconsin tax purposes because the cost of the meal is not incurred in a clear business setting. The floor show represents a substantial distraction to business discussion.

Question 2: Is the computation of the excess meal expense to be made for each meal separately or can it be made on a yearly basis?

Answer 2: The computation of the excess meal expense must be made for each meal separately. For example, a taxpayer gives two business dinners during the tax year. The first business dinner is for ten people at a cost of $50 per person. The second business dinner is for ten people at a cost of $20 per person. The expense not deductible for Wisconsin tax purposes is $125 computed as follows:

Cost of business meal #1	$ 500.00
$25 limit for 10 people	(250.00)
Excess	$ 250.00
Multiply by 50%	50%
Amount not deductible for business meal #1	$ 125.00

The expenses from the second business meal are deductible in full because each meal is under the $25 limit.

Question 3: An employe, who is an outside salesperson, takes three clients out to dinner (in a clear business setting) at a cost of $150. The employe is reimbursed $100 which is not treated as wages on the employe's W-2 form. What limitations apply for Wisconsin tax purposes?

Answer 3: The expense relates to employes and others. The amount not deductible is $25, computed as follows:

Cost of meal	$150.00
$25 limit for 4 people	100.00
Excess	$ 50.00
Multiply by 50%	50%
Amount not deductible	$ 25.00

The employer may not deduct $16.67 of the $100 reimbursement expense, which is the ratio of the amount reimbursed by the employer ($100) to the total expense ($150) multiplied by the $25 nondeductible expense. The employe may not deduct $8.33 of the $50 net expense he or she incurred, which is the ratio of expense not reimbursed by the employer ($50) to the total expense ($150) multiplied by the $25 nondeductible expense.

Question 4: A sole proprietor gives a business luncheon for twenty-four clients. He or she rents a meeting room for $200 and incurs meal expenses of $1,000. What limitations would apply for Wisconsin tax purposes?

Answer 4: The $200 expense is not deductible because it is an entertainment facility expense. The portion of the business meals that is not deductible is $187.50. This amount is computed as follows:

Cost of business meal	$1,000.00
$25 limit for 25 people	(625.00)
Excess	$ 375.00
Multiply by 50%	50%
Amount not deductible	$ 187.50

Question 5: A corporation owns a yacht which is used to provide business meals to clients in a quiet setting. The interest deduction for the yacht is $5,000 for 1986. The corporation provides

200 business meals on the yacht during the year at a cost of $4,000. None of the meals cost more than $25 per person. The corporation deducts $9,000 for federal tax purposes for 1986. What amount is deductible for Wisconsin tax purposes?

Answer 5: The corporation may deduct $4,000 for meals for Wisconsin tax purposes. Only the cost of the meals is deductible. The $5,000 interest expense in respect to the facility is not deductible for Wisconsin tax purposes.

Question 6: An employe for a regional CPA firm in Milwaukee travels to New York city to conduct an audit for his or her employer. The employe remains in New York overnight. The employe dines alone and incurs a meal expense of $50. The employe is reimbursed $50 by his or her employer. Does the $25 limit for meals apply in this situation? If so, how does the business meal expense limitation apply?

Answer 6: Yes. This limitation applies to **all** business meals whether dining alone or with someone else. The employer is not allowed to deduct $12.50 [($50 – $25) x 50%)] of the $50 reimbursement.

Part V

BUSINESS TRAVEL FOR MORE THAN A YEAR IN ONE CITY (Sections 71.01(4)(a)6m.d., 71.04(2)(b)14 and 71.05(1)(a)27.d., 1985 Wis. Stats.). Business travel expenses for trips lasting one year or more in one city that are deductible for federal tax purposes are not deductible for Wisconsin tax purposes.

Question 1: A taxpayer living in Wisconsin is given a temporary job assignment in Chicago in June, 1985. For federal and Wisconsin tax purposes, the taxpayer deducts $5,000 of travel expenses for 1985. The taxpayer remains in Chicago until September, 1986 (more than 1 year) and deducts $7,000 of travel expenses on his or her 1986 federal tax return. Are the travel expenses deductible for Wisconsin tax purposes in 1986? Are they deductible in 1985?

Answer 1: The taxpayer would not be allowed a deduction of $7,000 in 1986 because his or her stay in Chicago lasted one year or more. The deduction is allowable in 1985 because this travel limitation did not become effective until the 1986 taxable year.

Question 2: Assume the same facts as in Question 1 except the years involved are 1986 and 1987. Are the travel expenses deductible for Wisconsin tax purposes?

Answer 2: No. The taxpayer must amend his or her 1986 Wisconsin tax return once it is known that the job assignment will last one year or more to remove the deduction of $5,000. In 1987, the taxpayer is not allowed a deduction for $7,000 of travel expenses for Wisconsin tax purposes.

Part VI

BUSINESS TRAVEL BY LUXURY WATER TRANSPORTATION (Sections 71.04(4)(a)6m.e., 71.04(2)(b)15 and 71.05(1)(a)27.e., 1985 Wis. Stats.). Travel expense for luxury water transportation in excess of otherwise available business transportation, deductible for federal tax purposes, is not deductible for Wisconsin tax purposes.

Question 1: What is luxury water transportation?

Answer 1: Luxury water transportation includes travel by ocean liners, cruise ships or similar water transportation.

Question 2: What is "otherwise available business transportation?"

Answer 2: "Otherwise available business transportation" means twice the highest maximum per diem rate prescribed under paragraph 1-7.2 of Regulation § 5e. 274-8 (Federal Travel Regulations) for reimbursement of subsistence expenses incurred during official travel within CONUS (the conterminous United States), multiplied by the number of days engaged in luxury water travel. Any limited special exception to this amount (e.g., a higher limit that applies only to high ranking personnel) is disregarded. The applicable maximum per diem rate effective July 9, 1986, is $126 (New York City's maximum per diem rate).

Question 3: Are taxpayers required to allocate a portion of the total amount charged for luxury travel for meals or entertainment which could be limited under a different part of the law?

Answer 3: No. In the absence of separately stated meal or entertainment charges, taxpayers are not required to allocate a portion of the total amount charged to meals or entertainment unless the amounts to be allocated are clearly identifiable. If meal or entertainment expenses are separately stated, the business meal and entertainment expense limitations will apply to those charges. (See Question 5 below.)

Question 4: In 1986, a taxpayer travels to London on business by ocean liner. The trip takes six days and costs the taxpayer $2,000 which he or she deducts for federal tax purposes. Using the applicable maximum per diem amount stated in Answer 2 above, what amount is not deductible for Wisconsin tax purposes?

Answer 4: The amount not deductible is $488, computed as follows:

Cost of luxury water transportation	$ 2,000
Less: Two times the maximum per diem for six days (2 x $126 x 6)	(1,512)
Amount not deductible	$ 488

Question 5: Assume the same facts as in Question 4 except the $2,000 cost includes $300 for six meals ($50/meal). What amount is not deductible for Wisconsin tax purposes?

Answer 5: The amount not deductible is $263, computed as follows:

Cost of luxury water transportation	$ 1,700	
Less: Two times the maximum per diem for 6 days	(1,512)	
Amount not deductible for transportation		$188
Amount not deductible for meals [($300 – $150*) x 50%]		75
Total amount not deductible		$263

* $150 = 6 x $25/meal

Part VII

TRAVEL FOR CONVENTIONS, MEETINGS OR SEMINARS HELD ON CRUISE SHIPS (Sections 71.01(4)(a)6m.f., 71.04(2)(b)16 and 71.05(1)(a)27.f., 1985 Wis. Stats.). Travel expenses for conventions, meetings or seminars held on cruise ships and not treated as income, that are deductible for federal tax purposes, are not deductible for Wisconsin tax purposes.

Question 1: An employe incurs $2,000 of expense for travel on a cruise ship for a seminar. The employe is reimbursed $1,500 by his or her employer. The employe claims a deduction of $500 ($2,000 – $1,500) for federal tax purposes and the employer claims a deduction of $1,500 for federal tax purposes. Is the $1,500 reimbursement considered "income" for purposes of the Wisconsin limitation for travel expenses?

Answer 1: No. Reimbursement is not considered "income." "Income" for purposes of this Wisconsin limitation means wages and compensation subject to withholding taxes.

Question 2: What amount is not deductible for Wisconsin tax purposes based on the facts of Question 1?

Answer 2: The employe will not be allowed a deduction for the $500 portion of the total which was not reimbursed. His or her employer will not be allowed a deduction for $1,500.

Question 3: An employe attends a seminar on a cruise ship and incurs expenses of $1,500. The employe is reimbursed $1,000 by his or her employer. The employer treats the $1,000 reimbursement as wages on the employe's W-2 form. The employe deducts $1,500 of travel expenses for federal income tax purposes and includes as income the $1,000 of reimbursement from his or her employer. What amount is not deductible for Wisconsin tax purposes?

Answer 3: $500 is not deductible by the employe ($1,500 expense less the $1,000 expense treated as income). The employer may deduct the $1,000 reimbursement as wage expense.

Question 4: May the per diem rule under the limitations for luxury water transportation be used in the above cases?

Answer 4: No. If luxury water transportation expenses relating to a seminar, convention or meeting on board are incurred, only the limitations for travel for conventions, meetings or seminars held on cruise ships will apply.

Part VIII

BUSINESS TRAVEL AS A FORM OF EDUCATION (Sections 71.01(4)(a)6m.g., 71.04(2)(b)17 and 71.05(1)(a)27.g., 1985 Wis. Stats.). Business travel expenses that are deductible for federal tax purposes as a form of education are not deductible for Wisconsin tax purposes.

Question 1: What is meant by "travel as a form of education?"

Answer 1: "Travel as a form of education" means a travel deduction that would otherwise be allowable only on the ground that the travel itself serves as education. For example, a French teacher travels to France in order to maintain general familiarity with the French language and culture. The travel itself serves as a form of education.

Question 2: A scholar of French literature travels from the United States to France to take courses that are offered only at the Sorbonne. These classes maintain skills necessary in his or her present job. Does the limitation of travel as a form of education apply?

Answer 2: No. The limitation does not apply when a deduction is claimed with respect to travel that is a necessary adjunct to engaging in an activity that gives rise to a business deduction relating to education.

Question 3: A taxpayer is an instructor at a local university and also teaches a course at a local technical college. Are the automobile expenses the taxpayer incurs in traveling from the university to the technical college deductible for Wisconsin tax purposes?

Answer 3: Yes. These auto expenses are not considered to be travel as a form of education, but rather are considered to be ordinary and necessary business expenses.

Question 4: A Spanish interpretor enrolls in a course on Spanish culture. The course consists of informal instruction on Spanish customs that prepares the interpretor for a trip to Spain. The trip is the principal purpose of the course. The following travel expenses are claimed on the taxpayer's federal income tax return:

Travel, meals and lodging for the trip	$2,500
Car expenses from location of employment to the university	30

Are these travel expenses deductible for Wisconsin tax purposes?

Answer 4: No. The travel expenses for the trip to Spain are not allowed as a deduction because the travel itself has no other business purpose than to serve as a form of education. The car expenses are not deductible because they are only incurred for the preparation for the trip to Spain.

Question 5: Assuming the same facts as in Question 4, what amounts are not deductible for Wisconsin tax purposes if the interpretor is reimbursed $2,530 by his or her employer and the reimbursement is not treated as compensation and wages on the employe's W-2 form?

Answer 5: A $2,530 deduction for reimbursement may not be claimed by the employer. The employe claims no deduction because the travel expense less the reimbursement equals zero.

Question 6: A French teacher enrolls in a summer course at a university in Paris, France. The course maintains skills necessary in his or her job. The taxpayer spends four weeks attending classes and two additional weeks traveling in France. The following expenses are deducted for federal income tax purposes:

Air fare to and from Paris	$1,000
Meals and lodging ($200 per week)	1,200
Transportation expenses while attending classes in Paris	200
Transportation expenses while traveling in France	300

What amounts are not deductible for Wisconsin income tax purposes?

Answer 6: The amounts for meals, lodging and transportation expenses while traveling in France are not deductible ($700, which is two weeks of meals and lodging at $200 per week, and transportation expenses of $300) because the travel itself serves no other business purpose than as a form of education. Expenses for air fare, meals and lodging necessary to attend the classes and transportation expenses while attending classes are deductible for Wisconsin tax purposes because such expenses are necessary to engage in an activity that gives rise to a business deduction relating to education.

Question 7: A self-employed individual travels to Germany to observe techniques in a business similar to his or her business. For federal tax purposes, the individual deducts the travel expenses as education. Are these expenses deductible for Wisconsin tax purposes?

Answer 7: No. The travel itself serves no other business purpose than as a form of education.

SUMMARY OF REIMBURSEMENT SITUATIONS BETWEEN EMPLOYER AND EMPLOYE

Type of Reimbursement	Deductibility of Expense	Type of Expense	Reimbursement vs. Deductible Expense	Result	Part I Reference in Tax Release
I. Full reimbursement - not wages*	Fully nondeductible			Limitations apply to employer	Question 1
	Partially nondeductible			Limitations apply to employer	
II. Full reimbursement - wages**	Fully nondeductible			Limitations apply to employe	
	Partially nondeductible			Limitations apply to employe	
III. Partial reimbursement - not wages*	Fully nondeductible			Limitations apply to employer and employe	Question 2
	Partially nondeductible	Relates solely to employe	Reimbursement ≥ deductible expense	Limitations apply to employer and employe	Question 3
		Relates to employe and employer	Reimbursement < deductible expense	Limitations apply to employe	
IV. Partial reimbursement - wages**	Fully nondeductible			Limitations apply to employer and employe	Question 2
	Partially nondeductible			Limitations apply to employe	Question 3
V. No reimbursement	Fully nondeductible			Limitations apply to employe	Question 4
	Partially nondeductible			Limitations apply to employe	

*Not wages means the employe has not treated the reimbursement as wages subject to withholding and has not reported them on the employe's W-2 form.

**Wages means the employer has treated the reimbursement as wages subject to withholding and has reported them on the employe's W-2 form.

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CORPORATION FRANCHISE/INCOME TAXES

1. Deductions for Waste Treatment Facility

Statutes: Sections 71.02(1)(e) and 71.04(2g)(a), 1985 Wis. Stats.

Facts and Question: XYZ Corporation, which uses the accrual method of accounting, spent $100,000 during its 1984 taxable year to half-complete a qualifying waste treatment facility. In taxable year 1985, the remaining $100,000 was spent, and the facility was completed and placed in service.

The first sentence of s. 71.04(2g)(a), 1985 Wis. Stats., provides that the cost of a waste treatment facility may be deducted in the year paid, as defined in s. 71.02(1)(e). The last sentence of s. 71.04(2g)(a) states, "The deduction election, once made, cannot be changed, and it may be claimed beginning with the month following the month in which the facility is completed or acquired, or with the succeeding taxable year."

Is the $100,000 spent in taxable year 1984 deductible in that year, or is the entire $200,000 deductible in 1985 when the waste treatment facility was completed?

Answer: The cost of a qualifying waste treatment facility is deductible in the year paid, as defined in s. 71.02(1)(e), 1985 Wis. Stats. However, the deduction cannot be claimed until after the facility qualifies. Thus, if it takes more than one year to complete the waste treatment facility, the costs paid in prior years may be deducted on amended returns filed after the facility qualifies. In this example, a $100,000 deduction may be claimed for the 1984 taxable year on an amended return filed for the 1984 taxable year after the waste treatment facility achieved qualifying status in taxable year 1985. The $100,000 paid in 1985 may be claimed on a 1985 return.

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