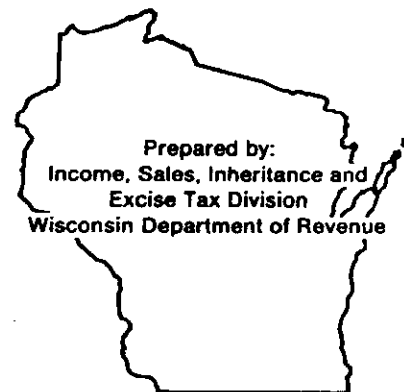


WISCONSIN TAX BULLETIN

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INCOME TAX FORMS TO INCLUDE LINE FOR WISCONSIN SALES/USE TAX ON OUT-OF-STATE PURCHASES

If a person makes any taxable purchases from out-of-state firms on which no sales tax is charged, that person must report Wisconsin sales/use tax on these pur-

chases. The 1988 Wisconsin Forms 1, 1A, WI-Z, and 1NPR will include a line for such persons to report sales/use tax on out-of-state purchases.

For example, you order from C Company in Ohio a set of golf clubs for \$500 plus a shipping charge of \$25. The company does not charge Wisconsin sales tax on your purchase because it is not required to collect Wisconsin sales/use tax. You owe

a Wisconsin sales/use tax on the out-of-state purchase equal to 5% of the purchase price plus shipping on the purchase. An additional 1/2% county tax is imposed if you obtain delivery of the golf clubs in a county that has adopted a county sales and use tax ordinance.

Although this method of collecting sales/use tax is new for Wisconsin for 1988, other states have had a similar line on their income tax forms in prior years.

IN THIS ISSUE

	Page
Income Tax Forms to Include Line for Wisconsin Sales/Use Tax on Out-of-State Purchases	1
Schedule WD to Be Included in 1988 Form 1 and 1NPR Income Tax Booklets	1
Department Takes Action as a Result of Kuhn Decision	2
For 1988 Taxable Year a 10% Credit of Farm Property Taxes Is Allowed	2
Reminder: New Exemption Provisions for Nonprofit Organizations Take Effect January 1, 1989	3
Reminder: Wisconsin Filing Requirements for Dependent Children Different Than Federal	3
Reminder: Tax-Exempt Organizations May Be Taxed on Unrelated Business Taxable Income	3
Form Changes for 1988	3
Correction to Shareholders' Instructions for 1988 Schedule 5K-1	4
Combined Wisconsin Return for Nonresident Tax-Option (S) Corporation Shareholders	4
Wisconsin and Federal Capital Gain Holding Periods Continue to Differ for 1988	4
1988 Package WI-X Will Be Available	5
Bulk Orders of Tax Forms	5
Tax Return Statistics for 1988	5
Contributions to Endangered Resources Program Increase	5
Taxpayers Designate \$449,211 to State Election Campaign Fund	6
Reminder: Employers Must Submit Copies of Certain Employee Withholding Exemption Certificates	6
Reminder: Notify Department of Federal Adjustments and Amended Returns	6
Reminder: Filing Deadlines for 1987 Homestead and Farmland Preservation Credit Claims	6
Reminder: Nonresident Entertainers Required to File Surety Bond or Cash Deposit	6
Criminal Enforcement Activities	7
New ISI&E Division Rules and Rule Amendments in Process	7
Report on Litigation	8
Tax Releases	
Individual Income Taxes	12
Individual and Corporation Franchise or Income Taxes	14
Corporation Franchise or Income Taxes	15
Sales/Use Taxes	19
Proof of 1988 Forms 1, 1A, WI-Z, and 1NPR	23

SCHEDULE WD TO BE INCLUDED IN 1988 FORM 1 AND 1NPR INCOME TAX BOOKLETS

A large number of taxpayers filed a Wisconsin Schedule WD with their 1987 Wisconsin income tax returns to report Wisconsin capital gains and losses. For the convenience of taxpayers, the 1988 Form 1 and Form 1NPR tax booklets will contain copies of Wisconsin Schedule WD for reporting Wisconsin capital gains and losses for 1988.

Note that for 1988, if a taxpayer's capital gain or loss reportable to Wisconsin consists only of a capital gain distribution from a mutual fund, the taxpayer does not have to complete Schedule WD. The 1988 instructions for Form 1 and Form 1NPR contain information about claiming an exclusion on a portion of the capital gain distribution.

DEPARTMENT TAKES ACTION AS A RESULT OF KUHNEN DECISION

In its decision dated January 14, 1988, the Wisconsin Court of Appeals, District IV, held that in the class action suit of *Michael W. Kuhn, Cynthia J. Kuhn, James J. Schmitz, Joanne E. Schmitz on behalf of themselves and all former residents of the State of Wisconsin in 1980, similarly situated v. Mark E. Musolf*, for the 1980 taxable year, sec. 71.05(1)(a)5, Stats. (1979-80), was unconstitutional and that the department could not impose an income tax on the gain from the sale in 1980 of a taxpayer's principal residence located in Wisconsin if the taxpayer purchased a qualified residence under section 1034 of the Internal Revenue Code outside of Wisconsin.

As a result of the *Kuhn* decision, the department has notified, by letter, potential members of the class of their right to receive a refund of Wisconsin income tax, interest, and penalties paid on the gain from the 1980 sale of their principal residence located in Wisconsin when a qualified replacement residence was purchased outside Wisconsin. The department has also published legal notices describing the *Kuhn* litigation in the *Wall Street Journal*, *Milwaukee Journal* and *Wisconsin State Journal*.

Note: A refund is only allowed for the 1980 sale of a personal residence located in Wisconsin. Sales in other years do not qualify.

FOR 1988 TAXABLE YEAR A 10% CREDIT OF FARM PROPERTY TAXES IS ALLOWED

As of October 1, 1988, the Director of the Agriculture Stabilization and Conservation Service certified that at least 40% of the crops in Wisconsin have been lost due to the drought. Therefore, sec. 71.09

(12fd), Stats., as created by 1987 Wisconsin Act 422 allows a 10% credit of farm property taxes to certain owners of farmland for the 1988 taxable year.

Who is eligible for the credit?

Any individual (including partners and shareholders of tax-option (S) corporations), corporation, trust, or estate is eligible for the drought credit, provided they own Wisconsin farmland of at least 35 acres and that farmland provided not less than \$6,000 of gross farm profits in taxable year 1988 or not less than \$18,000 of gross farm profits in taxable years 1986, 1987, and 1988. If the farmland is rented, the renter's gross farm profits are used to satisfy this requirement. The claimant need not be a resident of Wisconsin to be eligible for the credit. Only one claimant per household (husband, wife, and dependents while under age 18) may claim the credit.

How is the credit computed?

The credit is equal to 10% of Wisconsin farm real property taxes (up to \$10,000) for the taxable year 1988. Therefore, the credit is limited to \$1,000 (10% x \$10,000). The credit is further limited in that the amount of farmland preservation credit plus the amount of the drought credit may not exceed 95% of the farm property taxes for taxable year 1988. If any reduction is necessary, it is made against the drought credit.

Example: A calendar year Wisconsin taxpayer has farm property taxes for 1988 of \$2,000. The taxpayer computed a 1988 farmland preservation credit of \$1,800 and a drought credit of \$200 (10% x \$2,000). Since the credits added together (\$2,000) exceed 95% of property taxes for 1988 (\$1,900), the taxpayer will be allowed a farmland preservation credit of \$1,800 and a drought credit of \$100 or a total credit of \$1,900.

Example: A calendar year Wisconsin taxpayer has total farm property taxes of \$2,500. However, only \$2,000 of those taxes may be used for computing farmland preservation credit because only a

portion of the land is zoned exclusively for agricultural use. The taxpayer computed a 1988 farmland preservation credit of \$1,800 and a drought credit of \$250. Since the credits added together (\$2,050) do not exceed \$2,375 (95% of total farm property taxes of \$2,500), the taxpayer is allowed a farmland preservation credit of \$1,800 and a drought credit of \$250 or total credits of \$2,050.

What are property taxes for 1988?

Property taxes for 1988 are the real property taxes on the farm, including improvements, (exclusive of charges for special assessments, delinquent interest, and charges for service) that were levied during the taxpayer's 1988 taxable year. The taxes do not have to be paid to qualify for credit.

Example 1: A taxpayer has a calendar taxable year. Property taxes for 1988 are those taxes levied in December 1988 which are generally paid in 1989.

Example 2: A taxpayer has a 1988 taxable year that begins August 1, 1987, and ends July 31, 1988. Property taxes for 1988 are those taxes levied in December 1987, as this is the levy date that falls within the taxpayer's 1988 taxable year.

Example 3: A taxpayer has a 1988 taxable year that begins June 1, 1988, and ends May 31, 1989. Property taxes for 1988 are those taxes levied in December 1988, as this is the levy date that falls within the taxpayer's 1988 taxable year.

How is the credit claimed?

The credit will be claimed by individuals on 1988 Wisconsin Form 1 or 1NPR; by corporations on 1988 Wisconsin Form 4 or 5; and by trusts and estates on 1988 Wisconsin Form 2. The Forms 1, 1NPR, and 2 will have a separate line to claim the drought credit.

Because the Form 4 and Form 5 had been printed prior to October 1, corporations will be required to obtain a schedule from the department to compute the drought credit. The credit computed will be en-

tered on the line for farmland preservation credit on Form 4 or 5.

The claim for credit must be made within 12 months following the close of the taxpayer's 1988 taxable year.

REMINDER: NEW EXEMPTION PROVISIONS FOR NONPROFIT ORGANIZATIONS TAKE EFFECT JANUARY 1, 1989

Effective January 1, 1989, sales of tangible personal property and services, including admissions or tickets to an event, conducted by a nonprofit organization are exempt from sales tax if:

1. There is no professional entertainment,
2. The organization is not engaged in a trade or business, and
3. The organization is not otherwise required to have a Wisconsin seller's permit.

An organization is deemed to be engaged in a trade or business if its sales of tangible personal property or services (not including sales of tickets to events), or its events occur on more than 20 days during the year. However, if an organization's receipts do not exceed \$15,000 for the year, it is not considered to be engaged in a trade or business even if its sales and/or events exceed 20 days.

REMINDER: WISCONSIN FILING REQUIREMENTS FOR DEPENDENT CHILDREN DIFFERENT THAN FEDERAL

The Wisconsin filing requirements for dependent children are different than the

federal filing requirements. For federal tax purposes, when a parent can claim a child as a dependent, that child may be required to file a federal income tax return when his or her gross income exceeds \$500.

For Wisconsin tax purposes, a child who can be claimed as a dependent is not required to file a 1988 Wisconsin income tax return unless he or she has either \$1,000 or more of nonwage income or \$5,200 or more of gross income.

A dependent child required to file a 1988 Wisconsin income tax return must file on Form 1. A dependent child who is not required to file a Wisconsin return, but is doing so to obtain a refund of Wisconsin tax withheld from wages, will generally file a Form 1A or Form WI-Z.

REMINDER: TAX-EXEMPT ORGANIZATIONS MAY BE TAXED ON UNRELATED BUSINESS TAXABLE INCOME

Beginning with the 1988 taxable year, organizations filing federal Form 990-T that have \$1,000 or more of gross income from an unrelated trade or business must report such income to Wisconsin if:

- The organization is exempt from Wisconsin taxation under sec. 71.01 (3)(a), Stats., or
- The organization is a trust exempt from taxation under section 501(a) of the Internal Revenue Code, or
- The organization is an individual retirement arrangement (IRA).

Wisconsin unrelated business income is reported and tax liability is computed on Wisconsin Form 4T.

Form 4T is due by the 15th day of the 5th month following the close of the organization's 1988 taxable year, except

that an employee's trust defined in section 401(a) of the Internal Revenue Code and an IRA must file Form 4T by the 15th day of the 4th month following the close of their taxable year.

Most Wisconsin exempt organizations who filed a 1987 federal Form 990-T will be sent a 1988 Wisconsin Form 4T. If an organization does not receive a copy, one may be obtained by writing to Wisconsin Department of Revenue, P.O. Box 8903, Madison, Wisconsin 53708 or by calling (608) 266-1961. Practitioners requesting Form 4T should call (608) 267-2025.

FORM CHANGES FOR 1988

Following is a brief description of major changes made to the income tax, homestead credit, and farmland preservation credit forms for 1988.

1. Income Tax (Forms 1, 1A, WI-Z, and 1NPR)

- A line is added to report Wisconsin sales tax on out-of-state purchases (see article on page 1).
- A line is added to Forms 1 and 1NPR for the 1988 farmers' drought credit (see article on page 2).
- The format of the school property tax credit entry area on Form WI-Z is revised. Separate entry spaces are provided for amounts claimed by renters and homeowners.
- A separate line for capital gain distributions and IRA distributions is added to Form 1NPR.
- Check boxes for aliens and dependents are relocated on Form 1NPR.
- A reminder to attach a Residence Questionnaire is added to Form 1NPR.

2. Homestead Credit (Schedule H)

- Line 9 regarding reporting income from income tax returns is revised.
- The rent certificate is revised by adding entry lines to report the value of medical and other personal services provided.

3. Farmland Preservation Credit (Schedule FC)

- The entire Schedule FC is redesigned to conform more closely to the Schedule H.
- Publicly traded partnerships are included for the corporation check box.
- A question is added as to whether 1987 property taxes have been paid.
- Only farm income of dependents is to be included on Schedule 1 on the back of Schedule FC.
- The addback items to household income have been consolidated into one schedule on the back of Schedule FC (Schedule 2).

Proof copies of the 1988 Wisconsin Forms 1, 1A, WI-Z, and 1NPR are included on pages 23 through 31 of this issue.

CORRECTION TO SHAREHOLDERS' INSTRUCTIONS FOR 1988 SCHEDULE 5K-1

The 1988 Schedule 5K-1 (Form IC-156) instructions for shareholders contain an incorrect line reference. In the instructions for lines 14a through 14f, shareholders are instructed to carry the net amount from column C lines 14a through 14f of their 1988 Schedule 5K-1 to line 8 or 9 of

their 1988 Schedule MT, as appropriate. The instructions should read that the shareholders should report the net amount from column C of lines 14a through 14f of Schedule 5K-1 on line 8 or 10 of their 1988 Schedule MT, as appropriate.

COMBINED WISCONSIN RETURN FOR NONRESIDENT TAX-OPTION (S) CORPORATION SHAREHOLDERS

A tax-option (S) corporation that does business in Wisconsin and has two or more nonresident shareholders who derive no taxable income from Wisconsin other than their distributive share of the Wisconsin tax-option (S) corporation income may file a combined individual income tax return on behalf of those shareholders, beginning in 1988. The tax-option (S) corporation files this return on Form 1CNS.

A shareholder may not participate in this combined return if:

- The shareholder is a trust or estate.
- The shareholder files his or her individual income tax return on a fiscal year basis.
- The shareholder is a Wisconsin resident during any part of 1988.
- The shareholder derives taxable income from Wisconsin in 1988 other than his or her distributive share of tax-option (S) corporation income.

Each qualifying and participating shareholder's distributive share of tax-option (S) corporation income for the corporation's taxable years ending during the period January 31, 1988, through December 31, 1988, is reported on a 1988 Form 1CNS. The combined return replaces the separate 1988 Wisconsin individual income tax return that otherwise would be filed by each of the qualifying

and participating nonresident shareholders.

Form 1CNS will require the tax-option (S) corporation to compute the tax on the net Wisconsin tax-option (S) corporation income of each of the qualifying and participating shareholders. No deductions or credits will be allowed. The tax-option (S) corporation can make combined estimated tax payments of behalf of the nonresident shareholders. The shareholders' balances due or overpayments will be totaled on Form 1CNS, and one remittance will be submitted by the corporation or one refund check will be issued to the corporation.

The 1988 Form 1CNS is due on April 17, 1989. If the corporation is granted an extension by the Internal Revenue Service for filing its federal return, this automatically gives a Wisconsin extension to file Form 1CNS to the same extended due date. A copy of the federal extension must be attached to the Form 1CNS filed with the department.

Form 1CNS will be available in late December 1988 from any Department of Revenue office or by calling (608) 266-1961. Practitioners should call (608) 267-2025 to obtain copies of Form 1CNS. Additional information about the combined individual income tax return may be obtained by writing to Diane Hardt, Director, Tax Processing Bureau, Post Office Box 8903, Madison, Wisconsin 53708 or by calling (608) 267-5190.

WISCONSIN AND FEDERAL CAPITAL GAIN HOLDING PERIODS CONTINUE TO DIFFER FOR 1988

When the Wisconsin capital gain deduction was enacted for the 1987 taxable year and thereafter, a one-year holding period was established. Wisconsin law allows 60% of the net capital gain from assets held for more than one year to be deducted from Wisconsin taxable income.

Capital gains from assets held one year or less do not qualify for the deduction.

For federal purposes, a 6-month holding period was prescribed for 1987 for computing short-term versus long-term capital gains and losses. The difference in the holding periods used for Wisconsin and federal income tax purposes for 1987 created some difficulties for taxpayers who received capital gains as the result of investments in other entities, typically mutual funds.

A difference in the length of the Wisconsin and federal long-term capital gain and loss holding period will continue to exist through 1988. Although federal law has changed for 1988 and now also prescribes a "more than one year" holding period, the same as Wisconsin law, the change in the federal holding period requirement applies only to assets acquired after December 31, 1987. Assets acquired before January 1, 1988, continue to have a 6-month holding period for federal purposes.

Even though a difference continues to exist in the Wisconsin and federal holding period for 1988, it is anticipated that fewer filing difficulties will result. Mutual funds were alerted of this difference in a letter sent to each fund in January of 1988.

1988 PACKAGE WI-X WILL BE AVAILABLE

The department will again be offering Package WI-X which will contain actual size copies of most 1988 Wisconsin individual, fiduciary, and corporation income tax, gift tax, inheritance tax, motor fuel tax, sales tax, and withholding tax forms.

Package WI-X should be available by December 31, 1988. The cost is \$5.00 per copy. It may be ordered on the bulk order blank (Form P-744). The bulk order blank was mailed in September. See the following article for more information on bulk orders.

If you do not receive an order blank and wish to purchase copies of 1988 Package WI-X, requests indicating the number of copies along with the amount due should be mailed to: Wisconsin Department of Revenue, Shipping and Mailing Section, Post Office Box 8903, Madison, Wisconsin 53708.

BULK ORDERS OF TAX FORMS

In late September, the department mailed the order blank (Form P-744) which tax preparers should use to request bulk orders of 1988 Wisconsin income tax forms. There is a handling charge on their orders.

In late September, the department also mailed order blanks (Forms P-744b and P-744L) which banks, post offices, and libraries should use to request bulk orders of 1988 Wisconsin income tax forms. No charge is made for forms used for distribution to the general public (for example, in a bank, library, or post office).

This year's mailing list for bulk order blanks contains the names of all persons and organizations who placed orders for 1987 forms. If you are not on this mailing list and do not receive a Form P-744, P-744b, or P-744L you may request the bulk order blank by contacting any department office or by writing to the Wisconsin Department of Revenue, Central Services Section, Post Office Box 8903, Madison, Wisconsin 53708. You may also call the Shipping and Mailing Section at (608) 267-2025.

Orders should be placed as early as possible after you receive the order blank. Orders received by December 1, 1988, will be mailed early in January.

TAX RETURN STATISTICS FOR 1988

There were 2,357,000 Wisconsin individual income tax returns filed during the period July 1, 1987, to June 30, 1988. This compares to 2,256,000 income tax returns filed for the prior 12 months. The 2,357,000 returns were filed by 3,415,000 individuals.

There were 263,000 homestead credit claims and 23,000 farmland credit claims filed during the year. This compares to 265,000 homestead credit claims and 23,000 farmland credit claims filed for the prior year.

Taxpayers were issued a total of 1,711,600 income tax refunds during the 12 months ending June 30, 1988, for an average refund of \$329. The average refund for the prior year was \$314.

Homestead credit refunds averaged \$399 per claimant, an increase from the average refund of \$392 issued last year. About 49% of the claimants were age 65 or older. Of all individuals claiming homestead credit, 47% were renters and 53% were homeowners.

An average farmland preservation credit of \$1,286 was issued to each claimant. The average payment for 1986 was \$1,557.

An itemized deduction credit was claimed by 18% of the taxpayers on 1987 tax returns. The average credit allowed was \$242.13.

CONTRIBUTIONS TO ENDANGERED RESOURCES PROGRAM INCREASE

The 1987 Wisconsin income tax returns, Forms 1, 1A, 1NPR, and WI-Z included a line for taxpayers to contribute to the Wisconsin Endangered Resources Fund. These donations either reduce a taxpayer's income tax refund or increase the

amount of income tax 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 1987 Wisconsin income tax returns filed, 55,662 taxpayers contributed \$533,712 to the Endangered Resources Fund. This compares with 1986 income tax returns where 57,825 taxpayers contributed \$515,965.

TAXPAYERS DESIGNATE \$449,211 TO STATE ELECTION CAMPAIGN FUND

The 1987 Wisconsin income tax returns, Forms 1, 1A, INPR, and WI-Z, included a box for taxpayers to designate \$1 to the State Election Campaign Fund. If the box was checked "yes," there was no increase in tax liability or reduction in refund for making the designation.

During the period July 1, 1987, to June 30, 1988, taxpayers designated \$449,211 to the election campaign fund on their Wisconsin tax returns. This compares to \$396,700 for the prior twelve months ending June 30, 1987.

REMINDER: EMPLOYERS MUST SUBMIT COPIES OF CERTAIN EMPLOYEE WITHHOLDING EXEMPTION CERTIFICATES

Wisconsin law requires employers to submit copies of employee withholding exemption certificates to the department whenever they are required to provide such information to the Internal Revenue Service (IRS). The copies must be sub-

mitted 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 employee's withholding exemption certificate if (1) the number of exemptions claimed is more than 10 or (2) the employee is claiming complete exemption from withholding and he or she earns more than \$200 per week.

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.

For taxable years prior to 1987, if a taxpayer does not report adjustments made by the IRS or amended returns are not filed in the time period specified above, the department may make an assessment against the taxpayer or a refund to the taxpayer within 10 years after the date which the original tax return was filed or within 2 years after the date when the federal determination of tax became final, whichever is later.

For taxable years 1987 and thereafter, if a taxpayer does not report adjustments made by the IRS or amended returns are not filed in the time period specified above, the department may make an assessment against the taxpayer or a refund to the taxpayer within 4 years after discovery by the department.

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

REMINDER: FILING DEADLINES FOR 1987 HOMESTEAD AND FARMLAND PRESERVATION CREDIT CLAIMS

January 3, 1989, is the deadline for filing a 1987 homestead credit claim. Farmland preservation credit claims for 1987 must be filed no later than 12 months after the farmland owner's 1987 taxable year ends. January 3, 1989, is the deadline for filing a 1987 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: 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 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 (Nonresident Entertainer's Application & Receipt for Surety Bond or Cash Deposit) and amounts withheld by employers and reported on Form WT-11 (Nonresident Entertainer's Receipt for Withholding by Employer) 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 or 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, "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 Karl Foss, Wisconsin Department of Revenue, P. O. Box 8906, Madison, Wisconsin 53708, telephone (608) 266-3645.

CRIMINAL ENFORCEMENT ACTIVITIES

Excise Tax

Raymond DeChant, 2655 Highway 51, McFarland, was referred to Dane County's First Offender Program on March 23, 1988, for possessing 229 packs of Indian stamped cigarettes at his retail establishment, Ra Dar's 4077.

DeChant paid a \$50 fine and is required to do 80 hours of community service. Charges had been brought by the department's Alcohol & Tobacco Enforcement Section, which had seized 229 packs of Indian stamped cigarettes from DeChant's tavern.

NEW ISI&E DIVISION RULES AND RULE AMENDMENTS IN PROCESS

Listed below, under Part A 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 30, 1988. Part B lists rules approved by Legislative Standing Committee but not yet effective. Part C lists new rules and amendments which are adopted. ("A" means amendment, "NR" means new rule, "R" means repealed and "R&R"

means repealed and recreated.)

A. Rules at Legislative Council Rules Clearinghouse

- 2.16 Change in method of accounting for corporations-A
- 2.19 Installment method of accounting for corporations-A
- 2.20 Accounting for acceptance corporations, dealers in commercial paper, mortgage discount companies and small loan companies-A
- 2.21 Accounting for incorporated contractors-A
- 2.22 Accounting for incorporated dealers in securities-R&R
- 2.24 Accounting for incorporated retail merchants-A
- 2.25 Corporation accounting generally-A
- 2.26 "Last in, first out" method of inventorying for corporations-A
- 2.45 Apportionment in special cases-A
- 2.50 Apportionment of net business income of interstate public utilities-A
- 2.505 Apportionment of net business income of interstate professional sport clubs-A
- 2.53 Stock dividends and stock rights received by corporations-A
- 2.56 Insurance proceeds received by corporations-A
- 2.65 Interest received by corporations-A
- 2.72 Exchanges of property by corporations generally-A
- 2.721 Exchanges of property held for productive use or investment by corporations-A
- 2.83 Requirements for written elections as to recognition of gain in certain corporation liquidations-A
- 2.88 Interest rates-A
- 3.44 Organization and financing expenses—corporations-R&R
- 3.45 Bond premium, discount and expense—corporations-A
- 11.05 Governmental units-A
- 11.09 Medicines-A
- 11.10 Occasional sales-A
- 11.16 Common or contract carriers-A
- 11.18 Dentists and their suppliers-A

- 11.19 Printed material exemptions-A
- 11.26 Other taxes in taxable gross receipts and sales price-A
- 11.32 "Gross receipts" and "sales price"-A
- 11.40 Exemption of machines and processing equipment-A
- 11.41 Exemption of property consumed or destroyed in manufacturing-A
- 11.51 Grocers' guidelist-A
- 11.57 Public utilities-A
- 11.61 Veterinarians and their suppliers-A
- 11.66 Communications and CATV services-A
- 11.67 Service enterprises-A
- 11.68 Construction contractors-A
- 11.84 Aircraft-A
- 11.85 Boats, vessels and barges-A
- 14.01 Administrative provisions - R&R
- 14.02 Qualification for credit - R&R
- 14.03 Household income - R&R
- 14.04 Property taxes accrued - R&R
- 14.05 Rent constituting property taxes accrued - R&R

B. Rules Approved by Legislative Standing Committee But Not Yet Effective

- 11.12 Farming, agriculture, horticulture and floriculture - A

C. Rules Adopted in 1988

- 3.095 Interest income from federal obligations-R&R (effective 5/1/88)
- 11.10 Occasional sales-A (effective 1/1/88)

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 the Commission's decision).

The following decisions are included:

Individual Income Taxes

Capital Preservation Fund, Inc., et al. (p. 8)

Interest income—mutual funds

Allen M. Taylor (p. 9)

Foreign taxes

Homestead Credit

David A. Jensen (p. 9)

Filing deadline

Corporation Franchise or Income Taxes

Hammermill Paper Company (p. 9)

Equitable recoupment

Northern States Power Company (p. 10)

Appeals—timely

Sales/Use Taxes

Bank Equipment Lease, Inc. (p. 10)

Leases and rentals

International Business Machines Corporation (p. 11)

Computer and data processing—programs

INDIVIDUAL INCOME TAXES

Interest income—mutual funds. *Capital Preservation Fund, Inc., Trust for Short Term U.S. Government Securities, Lee V. Hribar, Urquhart L. Meeter, Barbara C. Meeter, and James E. Bartelt vs. Wisconsin Department of Revenue* (Court of Appeals, District IV, July 21, 1988). The Wisconsin Department of Revenue appeals from a summary judgment declaring that dividend distributions from the Capital Preservation Fund (the Fund) and the Trust for Short Term U.S. Government Securities (the Trust) are not subject to the Wisconsin income tax. The issue is whether 31 U.S.C., §3124(a), which declares "obligations of the United States Government are exempt from [State] taxation," precludes Wisconsin from taxing the distributions insofar as this results from (a) investments in direct obligations of the federal government, and (b) transactions under repurchase agreements involving federal securities.

The Fund and the Trust are mutual or "money market" funds. They are diversified investment companies which invest in various types of interest-bearing securities and sell their shares to individual and institutional investors in Wisconsin and elsewhere. They distribute substantially all of the income earned from these investments to their shareholders.

The Fund invests solely in direct obligations of the federal government — U.S. Treasury bills, notes, and zero coupon securities. The Trust also invests exclusively in treasury obligations and those of other federal agencies, such as the Federal Home Loan Banks. The Trust also enters into "repurchase agreements" through which it purchases government obligations from a third party — normally a bank — pursuant to a contract in which the bank agrees to repurchase the obligations from the Trust on a specified date (usually within a day or so of the initial sale to the Trust) and at a set price and rate of interest.

The department argues that *Rockford Life Ins. Co. v. Ill. Dept. of Rev.*, 96 L. Ed.2d 152 (1987), and a recent decision of the Court, *Savings League v. Revenue Dept.*, 141 Wis. 2d 918, 416 N.W. 2d 650 (Ct. App. 1987), compel a different result. Here, however, the issue is not whether a particular security is a federal "obligation." There is no question that neither the Fund nor the Trust deals in anything but direct obligations of the federal government. The issue is the scope of the exemption; and once a security is found to be an "obligation of the United States Government" in the statutory sense, the exemption provided by sec. 3124(a) is, in the words of the United States Supreme Court, to be "broad[ly]" and "sweeping[ly]" construed.

The department argues that in such transactions the interest paid to the Trust is not interest on the transferred and retransferred government securities, but rather is the equivalent of interest on the Trust's "loan" to the bank.

The Court of Appeals concluded that the state may not tax any of the investment distributions, but that distributions based on income from the Trust's repurchase agreements are taxable. Because both the Fund and the Trust invest solely in direct obligations of the federal government, distribution to their shareholders (or trustees) of the income from those investments may not be subjected to state income taxes. However, the same result does not obtain with respect to distributions representing interest income to the Trust arising out of its repurchase agreements.

The department and the taxpayer have not appealed this decision.

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Foreign taxes. *Allen M. Taylor vs. Wisconsin Department of Revenue* (Court of Appeals, District I, May 18, 1988). Allen M. Taylor paid foreign income taxes of \$11,015 and \$17,982 during 1979 and 1980, respectively, in connection with his

activities as an insurance underwriting member of Lloyd's of London. Taylor deducted these foreign taxes on his Wisconsin income tax returns for those years. In 1982, the Wisconsin Department of Revenue disallowed these deductions. The Wisconsin Tax Appeals Commission upheld the department's decision, holding that sec. 71.02(2)(f), Stats., excluded Taylor's deductions.

The Circuit Court affirmed the finding and conclusion of the Commission. The Circuit Court held that IRC section 164 (a)(3) authorized the deduction of foreign income taxes but that sec. 71.02(2)(f), Stats., specifically excluded such a deduction. The Circuit Court further concluded that Taylor's foreign income tax liability was a remote expense connected with the conduct of his trade or business and, hence, was not deductible as a business expense under IRC section 162.

The Court of Appeals concluded the memorandum decision of the trial court properly analyzed and applied sec. 71.02(2)(f), Stats., and the applicable federal code and treasury regulations to the facts of this case and, therefore, adopted the trial court's decision as its own.

The taxpayer has appealed this decision to the Wisconsin Supreme Court.

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HOMESTEAD CREDIT

Filing deadline. *David A. Jensen vs. Wisconsin Department of Revenue* (Circuit Court of Dane County, February 19, 1987). Before the Court is a Ch. 227, Stats., proceeding for judicial review of an administrative decision of the Wisconsin Tax Appeals Commission, dated July 29, 1986. That decision affirmed an assessment made by the Wisconsin Department of Revenue against the claimant.

The claimant filed Wisconsin income tax returns for 1980-1983 on February 27, 1985. In so doing, he attempted to use

homestead credits for those years to offset taxes owed. The Department of Revenue refused to allow the homestead credits because they were not filed before December 31 of the year following the year(s) for which the claim was made.

The claimant contends that Wisconsin income tax law subsumes homestead credit regulation. Therefore, where the department permits the filing of homestead credit on income tax returns, so too should it permit the late filing of the homestead credits that would have been attached to any late returns.

The Circuit Court found that the homestead credit provision neither comprises part of the Wisconsin income tax, nor fails under the uniformity clause of the Wisconsin Constitution. The Department of Revenue correctly disallowed the claim for homestead credit offset against income taxes for the years 1980-1983; therefore, the decision of the Wisconsin Tax Appeals Commission was affirmed.

The claimant has not appealed this decision.

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CORPORATION FRANCHISE OR INCOME TAXES

Equitable recoupment. *Hammermill Paper Company vs. Wisconsin Department of Revenue* (Circuit Court of Dane County, April 5, 1988). The Hammermill Paper Company seeks review of a Wisconsin Tax Appeals Commission dismissal of its claim for a refund of manufacturer's sales tax credit for the years 1973 through 1975.

The department sent Hammermill a notice of amount due relating to the uncontested portions of a 1981 assessment, plus interest. Hammermill objected to the department's determination. The taxpayer filed a claim for refund and objection to notice of amount due with the department. Hammermill objected to a calculational error in the department's notice of

amount due and claimed a refund, for the first time, of a manufacturer's sales tax credit not originally sought in returns filed for 1973 through 1975.

In response to the taxpayer's request, the department amended the notice of amount due, but rejected Hammermill's claim for a manufacturer's sales tax credit refund. Hammermill petitioned the Commission for review after the department rejected a request for redetermination. The taxpayer argued that it was entitled to a refund of the sales tax credit to offset its tax liability under the doctrine of equitable recoupment. On October 30, 1987, the Commission granted the department's motion to dismiss on grounds that it lacked "subject matter jurisdiction" to hear and decide claims based upon the doctrine of equitable recoupment because such claims were not timely and properly raised during the original redetermination of tax liability.

The Circuit Court concluded that the Commission's decision and order must be affirmed on two grounds. First, the present case does not fall within the doctrine of equitable recoupment. Second, the taxpayer's failure to raise its claim for a refund in a timely manner resulted in waiver of the claim.

The taxpayer has not appealed this decision.

□

Appeals—timely. *Northern States Power Company v. Wisconsin Department of Revenue* (Court of Appeals, District III, May 10, 1988). Northern States Power Company (NSP) petitioned the Circuit Court to review a Wisconsin Tax Appeals Commission decision. NSP claims to have mailed, by certified mail, a copy of the petition for review to the Department of Revenue. The department, however, did not receive the copy. The Circuit Court dismissed the petition due to lack of jurisdiction for failure of timely service on the department.

NSP appeals the dismissal order, contending that (1) timely service was accomplished, (2) because the Commission's determination was not final, it was not appealable, and (3) the Circuit Court had jurisdiction in any event to resolve the constitutionality of the statute in question.

The Court of Appeals concluded that the right to judicial review of administrative agency orders is dependent upon strict compliance with sec. 227.16, Stats. Failure to comply with this section deprives the Circuit Court of subject matter jurisdiction. Because the Court was without jurisdiction, adjudication of the tax laws' constitutionality would have been inappropriate.

The taxpayer appealed this decision to the Wisconsin Supreme Court. The Supreme Court denied the taxpayer's petition for review.

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SALES/USE TAXES

Leases and rentals. *Bank Equipment Lease, Inc. vs. Department of Revenue* (Court of Appeals, District IV, March 10, 1988). Bank Equipment Lease, Inc. appeals from a judgment affirming a Tax Appeals Commission decision which upheld a sales tax assessment against the taxpayer. The issues are:

- A. Whether the taxpayer's transactions were leases and, therefore, subject to the sales tax.
- B. Whether the taxpayer was properly found to be a "retailer."
- C. Whether the taxpayer should be relieved of liability for worthless accounts.
- D. Whether the finding that it held title to the leased equipment is erroneous.
- E. Whether the financial institutions, rather than the taxpayer, are liable for the

tax since the leases were completely assigned.

F. Whether the statute of limitations as to 1976, 1977, and 1978 has run.

G. Whether the assessment is invalid because it was based on projections of payments that were not made.

H. Whether the Department of Revenue should be estopped from assessing the tax.

The taxpayer, a Wisconsin corporation, was assessed a sales tax of \$67,379.04 on May 28, 1982, for 1976 through 1981. The taxpayer challenged the assessment, contending it had not made transactions subject to the sales tax. The Commission found that the taxpayer had applied for a Wisconsin seller's permit in 1977, representing that its business purpose was retail and that it would engage in equipment leasing. The permit was issued August 16, 1977. The taxpayer bought equipment requested by companies, then leased the equipment to the companies for amounts exceeding the value of the equipment. It obtained loans from various financial institutions to purchase the equipment. Upon obtaining a signed lease from the company, it assigned the rental receipts to the lending institution, which applied the rent against the taxpayer's loan. It also assigned its rights, title, and interest in and to the property described in the lease and all of its rights and remedies, but agreed to perform the obligations of a lessor under the lease.

The Commission concluded that receipts from the leases were subject to the sales tax under sec. 77.52(1), Stats., that the statute of limitations had not run on 1976 through 1978 sales tax liability due to taxpayer's failure to file annual information returns as required by sec. 77.58 (2)(a), Stats., and that the department was not estopped from collecting the tax. The Circuit Court affirmed.

The taxpayer argues that the evidence shows it did not lease personal property but instead acted as a "loan broker" and argues that since no payments were made

to it, it cannot be a retailer under sec. 77.51 (13)(k), Stats., which defines "retailer" to include "any person deriving rentals from a lease of tangible personal property situated in the state." The taxpayer also contends that since its customers went bankrupt and the accounts were determined to be worthless, it should be relieved from liability for the sales tax under sec. 77.51 (4)(b)4, Stats. This section relieves a retailer from liability for accounts found to be worthless and charged off for income tax purposes.

The taxpayer contends that the department erroneously computed the assessment based on the full price of the lease if all the payments were made, despite its witness's admission that most of the companies went bankrupt, and challenges the finding that it held title to tangible personal property, claiming the testimony was uncontradicted that at no time did it own any equipment.

The taxpayer contends that the statute of limitations has run as to 1976 through 1978 pursuant to sec. 77.54(3), Stats. The taxpayer also contends that if these were taxable transactions, the financial institutions should have collected the sales tax since the leases were assigned to them and they received the payments. It relies on *Tullgren v. School Dist.*, 16 Wis. 2d 135, 142, 113 N.W. 2d 540, 544 (1962), which held that a particular assignment of a contract was absolute.

The taxpayer argues that the department should be estopped from assessing any sales tax since it previously accepted the taxpayer's returns showing no sales tax was due.

The Court concluded that:

A. The assessment was based on 23 transactions involving the taxpayer and various companies and financial institutions. All are evidenced by assignments of leases between the taxpayer and a company to a financial institution, by leases between the taxpayer and the company, or both. In addition, the taxpayer's application for a seller's permit states it is in the business of equipment leasing. This is

sufficient evidence to support the finding that the transactions were leases.

B. The taxpayer derived the proceeds, but used them to pay off its loans. That the proceeds were received by the lending institutions directly, rather than initially by the taxpayer, does not alter the fact that they were derived by the taxpayer from the leases. The finding that taxpayer was a retailer is supported by substantial evidence.

C. There was no finding that the accounts were worthless. There was no evidence that these accounts were charged off for income tax purposes. Section 77.51(4)(b)4, Stats., does not absolve the taxpayer of liability.

D. The department properly computed the assessment. Under sec. 77.51(4)(a), Stats., "gross receipts" means "the total amount of the . . . lease price . . . from sales at retail of tangible personal property, . . . valued in money, whether received in money or otherwise . . ." Under this section, the lease price, rather than the actual payments made, is the basis for the assessment of sales tax liability.

E. All of the transactions are evidenced by documents which refer to the transactions as leases of equipment. The taxpayer presented no evidence that it did not hold title to the property which was the subject of the leases. The finding is supported by substantial evidence.

F. The Commission correctly concluded that the statute of limitations had not run for the years 1976 through 1978 since the annual returns have not yet been filed. The monthly returns filed by the taxpayer are not the annual information returns referred to in the statute.

G. The assignments in this case reserved to the taxpayer all of its obligations under the leases. The assignments were not absolute.

H. Equitable estoppel may be applied against the Department of Revenue where the elements are clearly present. Those elements are action or inaction by one

party which reasonably induces reliance by the other party to the latter party's detriment. The taxpayer does not contend, and did not offer evidence, that it reasonably relied on the department's prior inaction to its detriment.

The taxpayer has not appealed this decision.

□

Computer and data processing—programs. *Wisconsin Department of Revenue v. International Business Machines Corporation* (Court of Appeals, District IV, June 23, 1988). The Wisconsin Department of Revenue appeals an order affirming a decision of the Wisconsin Tax Appeals Commission. The department sought to collect sales taxes from IBM on revenues from the license of made-to-order computer programs to Wisconsin customers. The Commission and the trial court held that IBM's transactions were tax exempt.

At issue here is whether the computer programs IBM made to order for its Wisconsin customers were tangible personal property for tax purposes. The department argues that the transfer involved tangible property because IBM delivered the programs on magnetic tapes, similar to music tapes. IBM contends that the transfers were nontaxable because their essential purpose was to provide the customer with intangible programmed information.

The Court concluded that the transactions at issue here were not taxable under sec. 77.52(1), Stats. In *Janesville Data Center v. Dept. of Revenue*, 84 Wis. 2d 346, 267 N.W.2d 658 (1978), the Supreme Court held that although the sales of computer programs may include the transfers of tangible property, such as tapes, they are not taxable under sec. 77.52, Stats., if the "essence of the transaction" was the transfer of intangible property such as coded or processed data. There is no dispute that the essence of these transactions was the data on the tapes IBM delivered to its

customers, and not the tapes themselves. *Data Center* therefore controls the decision.

The department has appealed this decision to the Supreme Court.



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

1. Reclassifying Income Received Under Wisconsin's Marital Property Law (p. 12)
2. Reporting Gain on the Sale of a Home Under Wisconsin's Marital Property Law (p. 13)

Individual and Corporation Franchise or Income Taxes

1. Deductibility of Federal Minimum Tax (p. 14)

Corporation Franchise or Income Tax

1. Bad Debt Deduction Transition Adjustments Required for Certain Financial Institutions (p. 15)
2. Deductible Dividends Received from Subsidiaries (p. 16)
3. Deduction for Bad Debts by Corporations Other Than Certain Financial Organizations (p. 16)
4. Sales Included in Sales Factor in Same Year That Income Is Recognized (p. 17)
5. When a Sale Is in Wisconsin for Computing the Sales Factor of the Apportionment Formula (p. 18)

Sales/Use Taxes

1. Are Certain Charges Related to the Construction of a Golf Course Taxable Landscaping Services? (p. 19)

2. Laboratory Testing in a Creamery (p. 19)
3. Parking Is Provided for Monies Intended to Cover Costs (p. 20)
4. Refuse Derived Fuel Plant Is a Recycling Facility (p. 20)
5. Retailers' Receipts for Handling Manufacturers' Coupons (p. 20)
6. Sales to Government and Other Exempt Organizations' Employees (p. 21)
7. Wax Purchased by Car Wash Operators (p. 22)

INDIVIDUAL INCOME TAXES

1. Reclassifying Income Received Under Wisconsin's Marital Property Law

Statutes: Sections 71.02(2)(me) and 71.11(2m) and (2r), Stats. (1985-86), as amended by 1987 Wisconsin Act 393

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

Background: Generally, under Wisconsin's marital property law, income of spouses received up until the date of divorce is marital property and one-half is reportable by each spouse. However, certain income may be classified as individual property by a marital property agreement, unilateral statement, or court decree. Income classified as individual property is reportable by the owner.

Facts: A husband and wife, who have been separated since January 1987, are divorced on May 31, 1988. The husband earned wages of \$15,000 from January 1 to May 30, 1988, and \$25,000 thereafter. The wife earned wages of \$2,000 from January 1 to May 30, 1988, and \$8,000 thereafter. Incorporated into their divorce decree is a property settlement agreement which provides that the wages earned up until the date of divorce are individual income and must be reported by the wage earner on his or her tax return.

Question 1: Does this court order, which classifies the spouses' wages as individual property, apply for Wisconsin income tax purposes?

Answer 1: No. The court order would not apply for Wisconsin income tax purposes, since for tax purposes spouses may not agree to retroactively reclassify income previously received.

Question 2: What amount of wages must the spouses report on their 1988 Wisconsin individual income tax returns?

Answer 2: The amount of wages reportable by the spouses on their individual returns depends on whether the spouses notified each other of the amount and nature of their marital property income.

A. If both spouses notified the other of the amount and nature of their marital income—

	Total	Husband	Wife
Husband's wages 1/1-5/30	\$15,000	\$7,500	\$ 7,500
Husband's wages 5/31-12/31	25,000	25,000	-0-
Wife's wages 1/1-5/30	2,000	1,000	1,000
Wife's wages 5/31-12/31	8,000	-0-	8,000
Total	<u>\$50,000</u>	<u>\$33,500</u>	<u>\$16,500</u>

B. If the husband notified the wife of his marital property income but the wife didn't notify the husband of her marital property income—

	Total	Husband	Wife
Husband's wages 1/1-5/30	\$15,000	\$ 7,500	\$ 7,500
Husband's wages 5/31-12/31	25,000	25,000	-0-
Wife's wages 1/1-5/30	2,000	-0-	2,000
Wife's wages 5/31-12/31	8,000	-0-	8,000
Total	<u>\$50,000</u>	<u>\$32,500</u>	<u>\$17,500</u>

C. If the wife notified the husband of her marital property income but the husband didn't notify the wife of his marital property income—

	Total	Husband	Wife
Husband's wages 1/1-5/30	\$15,000	\$15,000	\$ -0-
Husband's wages 5/31-12/31	25,000	25,000	-0-
Wife's wages 1/1-5/30	2,000	1,000	1,000
Wife's wages 5/31-12/31	8,000	-0-	8,000
Total	<u>\$50,000</u>	<u>\$41,000</u>	<u>\$ 9,000</u>

D. If neither spouse notified the other of the amount and nature of their marital property income—

	Total	Husband	Wife
Husband's wages 1/1-5/30	\$15,000	\$15,000	\$ -0-
Husband's wages 5/31-12/31	25,000	25,000	-0-
Wife's wages 1/1-5/30	2,000	-0-	2,000
Wife's wages 5/31-12/31	8,000	-0-	8,000
Total	<u>\$50,000</u>	<u>\$40,000</u>	<u>\$10,000</u>

Question 3: If the husband was required to pay the wife \$5,000 of alimony between January 1, 1988, and May 30, 1988, is this amount deductible by the husband and taxable to the wife?

Answer 3: No. The \$5,000 of alimony paid up until the date of divorce is not deductible by the husband nor taxable to the wife. Until the payor spouse's payments exceed one-half of the total combined marital property income (in this case, \$17,000), there has been no transfer recognized for tax purposes. The husband's payment merely gave the wife control of the \$5,000, not ownership, which she already had under the marital property law. This position is consistent with that of the Internal Revenue Service (see IRS Publication 504). The answer would be unchanged even if the "innocent spouse" rules in sec. 71.11(2m) and (2r), Stats. (1985-86), as amended by 1987 Wis. Act 393, apply since those provisions do not reclassify marital property income to individual income.



2. Reporting Gain on the Sale of a Home Under Wisconsin's Marital Property Law

Facts and Question: A husband and wife were married in 1984. In 1974, while single, the husband bought a home. He made major improvements to the home between 1974 and 1980. No improvements were made after 1984. In December 1986, the home was sold at a gain of \$25,000, which was computed as follows:

Selling price	\$45,000
Cost plus improvements	20,000
Gain on sale	<u>\$25,000</u>

Title to the home was in the husband's name alone. Mortgage payments were made from the husband's wages, which in 1986 were classified as marital property. No marital property agreement, unilateral statement, or court order reclassifying the property exists.

The couple is divorced in 1988. The husband intends to buy a replacement home, but the wife doesn't.

How must the gain on the sale of the home be reported?

Answer: The treatment of the gain on the sale of the home depends on how the property is classified. Is it marital, individual, mixed, or unclassified (and thus treated "as if" individual) property?

The Wisconsin Marital Property Act presumes that all property of spouses is marital property (sec. 766.31(2), Stats. (1985-86)). However, this presumption may be rebutted, either by the taxpayer or by the department, when there is adequate proof to show that the property's classification is something other than marital property. In the case of mixed property (property having marital and nonmarital components), the property is entirely reclassified to marital property if the nonmarital component cannot be traced (sec. 766.63(1), Stats. (1985-86)).

The following steps would be taken to classify the home in this instance:

Step 1. Establish the determination date for the spouses: January 1, 1986.

Step 2. Establish the initial classification: The home is predetermination date property because it was acquired before January 1, 1986.

Step 3. Establish whether an agreement, statement, gift, or court order affects the initial classification: No.

Step 4. Establish whether mixing has occurred: Yes, mixing has occurred because the taxpayer used wages (marital property) for the mortgage payments made during 1986. Since it appears that the marital and nonmarital components can be traced, the home would be classified as mixed property.

Step 5. Establish the value of the marital and nonmarital components: Wisconsin's marital property law does not specify how this is to be done. Instead, it will be up to the courts to determine, on a case-by-case basis, the value of the marital and nonmarital components of mixed property. Under sec. 766.63(1), Stats. (1985-86), the burden is on the party objecting to the classification of the asset as marital property to show how much is not marital property. The department may rely on the presumption, if the evidence is determined to be inadequate, or it may take the position that the Tax Appeals Commission must determine the amount of nonmarital property in the mixed asset.

If the home in this example is presumed to be marital property, one-half of the gain would be allocated to each spouse. The husband could defer his \$12,500 gain if he purchases a qualifying replacement home. The wife would be taxed on her \$12,500 gain if she doesn't purchase a replacement home. However, if the spouses can show the value of the marital and nonmarital components, the non-marital component plus one-half of the marital component would be allocated to the husband and the other half of the marital component would be allocated to the wife. The department's position coincides with the Internal Revenue

Service's position, based on conversations with federal personnel.

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INDIVIDUAL AND CORPORATION FRANCHISE OR INCOME TAXES

1. Deductibility of Federal Minimum Tax

Statutes: Sections 71.02(2)(c), (d) and (i) and 71.04(3), Stats. (1985-86), sec. 71.02(1)(bg), Stats. as created by 1987 Wis. Act 27 and sec. 71.02(1)(c) and (3), Stats. (1985-86) as amended by 1987 Wis. Acts 27 and 399

Facts and Question: Section 55 of the Internal Revenue Code (IRC) imposes an alternative minimum tax on all taxpayers which is equal to the amount by which the minimum tax exceeds the regular tax for the taxable year.

Is this federal alternative minimum tax deductible for Wisconsin tax purposes?

Answer: Persons other than corporations - No. Sections 71.02(1)(c) and (d), Stats. (1985-86), as amended by 1985 Wis. Acts 27 and 399 and sec. 71.02(2)(c), (d) and (i), Stats. (1985-86), provide that Wisconsin adjusted gross income or net income is determined under the Internal Revenue Code in effect on a given date. In the case of *Trainer vs. U.S.*, the U.S. Court of Appeals held that the federal minimum tax is an income tax and not an excise tax. It cannot be deducted for federal tax purposes under IRC Section 275. Therefore, because the tax is not deductible for federal tax purposes in determining adjusted gross income, it is not deductible for Wisconsin tax purposes.

Corporations (Prior to 1987 taxable year) - No. Section 71.04(3), Stats. (1985-86), provides that income taxes are not deductible. Because the federal alternative minimum tax is an income tax, it is not deductible for Wisconsin tax purposes.

Corporations (1987 taxable year and thereafter) - No. Section 71.02(1)(bg), Stats., as created by 1987 Wis. Act 27, and sec. 71.02(1)(c), Stats. (1985-86) as amended by 1987 Wis. Acts 27 and 399 provide that a corporation's net income is computed under the Internal Revenue Code in effect on a given date. Therefore, because the federal alternative minimum tax is not deductible for federal tax purposes, it is not deductible for Wisconsin tax purposes.

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CORPORATION FRANCHISE OR INCOME TAXES

1. Bad Debt Deduction Transitional Adjustments Required for Certain Financial Institutions

Statutes: Section 71.02(1)(bg), Stats., as created by 1987 Wis. Act 27, sec. 71.02(1)(c), Stats. (1985-86) as amended by 1987 Wis. Acts 27 and 399, sec. 71.04(7) and (9)(b), Stats. (1985-86), and sec. 3047(1)(a), 1987 Wisconsin Act 27

Background: For 1986 and prior taxable years, savings and loan associations, mutual savings banks, production credit associations, and credit unions were allowed to claim a bad debt deduction of either (a) two-thirds of the amount they were required to allocate to their loss reserves pursuant to statutory provisions or rules and regulations or orders of any state or federal governmental supervisory authority (sec. 71.04(9)(b), Stats. (1985-86)), or (b) the actual bad debts sustained during the year (sec. 71.04(7), Stats. (1985-86)).

For the 1987 taxable year and thereafter, sec. 71.02(1)(bg), Stats., as created by 1987 Wis. Act 27 and sec. 71.02(1)(c), Stats. (1985-86) as amended by 1987 Wis. Acts 27 and 399, provide that Wisconsin corporation net income is determined under the Internal Revenue Code (IRC) as amended to December 31, 1986, with certain exceptions. Therefore, for the 1987 taxable year, financial institutions must determine their deduction for bad debts under the method allowed by the IRC as amended to December 31, 1986.

Sections 585 and 593 of the IRC as amended to December 31, 1986, provide that financial institutions, other than large banks, are allowed to deduct bad debts on either the specific charge-off method or an allowable reserve method. A bank, for purposes of the deduction for bad debts, is a large bank if the average adjusted bases of all assets of the bank exceeded \$500,000,000 or the bank was a member of a parent-subsidiary controlled group and the average adjusted bases of the group exceeded \$500,000,000. Large banks must use the specific charge-off method.

As a result of the change in the Wisconsin corporate franchise or income tax law for the 1987 taxable year, a nonstatutory transitional provision in sec. 3047(1)(a) of 1987 Wisconsin Act 27 provides that each corporation must calculate, as of the close of its 1986 taxable year, the amount that, because of the Wisconsin law change, is required to be added to, or subtracted from, income in order to avoid the double inclusion, or omission, of any item of income, loss, or deduction. If the amount required to be added or subtracted (transitional adjustment) is \$25,000 or less, the amount must be added or subtracted for taxable year 1987. If the transitional adjustment is more than \$25,000, it must be added or subtracted ratably over 5 taxable years beginning with 1987.

Facts and Question 1: Corporation X, a calendar year Wisconsin savings and loan association incorporated on January 1, 1967, deducts bad debts on a reserve method for federal income tax

purposes. Corporation X made annual additions to the bad debt reserve of \$100,000 for each year from 1967 through 1986 for a total deduction of \$2,000,000. For each of 10 years, actual bad debt losses of \$80,000 were charged off. For each of the other 10 years, actual bad debt losses of \$50,000 were charged off. Therefore, the federal bad debt reserve balance was \$700,000 on December 31, 1986.

For Wisconsin tax purposes, for the 20 years prior to the 1987 taxable year, the actual bad debt losses of \$80,000 were deducted for 10 years and a bad debt deduction of two-thirds of the addition to the federal insurance reserve (\$66,667) was deducted for the other 10 years for a total deduction of \$1,466,670 for the 20 year period.

Since, for the 1987 taxable year and thereafter, the Wisconsin deduction for bad debts is determined under the IRC, what adjustment, if any, is necessary in order to account for the difference between the federal and Wisconsin bad debt deductions for 1986 and prior years?

Answer 1: The difference of \$533,330 (total federal deductions of \$2,000,000 minus total Wisconsin deductions of \$1,466,670) should be subtracted, as a transitional adjustment, in arriving at Wisconsin net income in order to prevent the omission of a deduction. The \$533,330 is netted with any other required transitional adjustments. If the total adjustment is greater than \$25,000, the adjustment is amortized ratably over 5 taxable years, starting in 1987. Assuming that the bad debt adjustment is the only transitional adjustment required to be made by Corporation X, \$106,666 should be deducted in arriving at Wisconsin net income for 1987 and each of the next 4 taxable years.

Facts and Question 2: Corporation A, a calendar year Wisconsin savings and loan association incorporated in 1980, deducts bad debts on a reserve method for federal income tax purposes and had a reserve balance of \$420,000 on December 31, 1986. For 1986 and prior taxable years, the Wisconsin bad debt deduction claimed by Corporation A was always two-thirds of the amount transferred to its federal insurance reserve. The balance of the Wisconsin bad debt reserve was \$280,000 on December 31, 1986. The Wisconsin reserve balance is determined by increasing the reserve by two-thirds of the amount transferred to the federal insurance reserve for each year (1980 through 1986), reducing the reserve by the bad debts actually charged off during each year, and increasing the reserve by the amount of any recoveries of amounts previously charged off.

Since, for the 1987 taxable year and thereafter, the Wisconsin deduction for bad debts is determined under the IRC, what adjustment, if any, is necessary in order to account for the difference between the federal and Wisconsin bad debt reserve on December 31, 1986?

Answer 2: Since the federal reserve exceeds the Wisconsin reserve, the difference (\$140,000) should be subtracted, as a

transitional adjustment, in arriving at Wisconsin net income in order to prevent the omission of a deduction. The \$140,000 is netted with any other transitional adjustments that are required. If the total adjustment is greater than \$25,000, the adjustment is amortized ratably over 5 taxable years, starting in 1987. Assuming that the bad debt adjustment is the only transitional adjustment required to be made by Corporation A, \$28,000 should be deducted in arriving at Wisconsin net income for 1987 and each of the next 4 taxable years.

Facts and Question 3: Corporation B, a calendar year bank located in Wisconsin, deducts bad debts on a reserve method for federal purposes and had a reserve balance of \$300,000 on December 31, 1986. For 1986 and prior taxable years, the Wisconsin bad debts were deducted on the direct write-off method.

Since, for the 1987 taxable year and thereafter, the Wisconsin deduction for bad debts is determined under the IRC, what adjustment, if any, is necessary in order to account for the federal bad debt reserve of \$300,000 on December 31, 1986?

Answer 3: Since for 1987, the Wisconsin bad debt deduction will be on the reserve method and since the \$300,000 has not previously been deducted for Wisconsin corporate franchise or income tax purposes, the \$300,000 should be subtracted, as a transitional adjustment, in arriving at Wisconsin net income. Assuming that this is the only transitional adjustment required to be made by Corporation B, \$60,000 should be deducted in arriving at Wisconsin net income for 1987 and each of the next 4 taxable years.

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2. Deductible Dividends Received From Subsidiaries

Statutes: Section 71.04(4)(b), Stats. (1985-86), and sec. 71.02(1)(bg)11, Stats., as created by 1987 Wis. Act 27

Law: Section 71.02(1)(bg)11, Stats., as created by 1987 Wis. Act 27, provides in part that a corporation may deduct from its income, dividends received from a corporation with respect to its common stock if the corporation receiving the dividends owns, directly or indirectly, during the entire taxable year at least 80% of the total combined voting stock of the payor corporation. Prior to 1987 Wisconsin Act 27, which created sec. 71.02(1)(bg)11, the same deduction was allowed by sec. 71.04 (4)(b), Stats., (1985-86). However, the deduction under sec. 71.04 (4)(b) was limited to cash dividends, while under sec. 71.02 (1)(bg)11, which is effective for the 1987 taxable year and thereafter, both cash and property dividends may be deducted if the conditions are met.

Facts and Question 1: Corporation A does business in Wisconsin

and files its Wisconsin franchise tax return on a calendar year basis. On March 1, 1987, Corporation A forms a new subsidiary, Corporation B. Corporation A holds 100% of the voting stock of Corporation B from March 1, 1987, through December 31, 1987. Corporation B does not apportion more than 50% of its net income to Wisconsin for 1987.

If Corporation B pays Corporation A \$100,000 of common stock dividends on December 1, 1987, is the \$100,000 deductible by Corporation A in determining its Wisconsin net income for 1987?

Answer 1: No. Since Corporation A did not own during the entire taxable year at least 80% of the total combined voting stock of Corporation B, the \$100,000 of dividends received is not deductible in arriving at Wisconsin net income.

Facts and Question 2: Corporation X, a calendar year Wisconsin holding company, formed a subsidiary, Corporation Y, in Ohio during 1986. Corporation X owned 100% of the stock of Corporation Y for all of 1987. On July 1, 1987, Corporation Y acquired 100% of the stock of Corporation Z, a Texas corporation. Neither Corporation Y nor Corporation Z conducts any business in Wisconsin.

On September 1, 1987, Corporation Z paid Corporation Y \$50,000 of common stock dividends. On December 15, 1987, Corporation Y paid Corporation X \$100,000 of common stock dividends. Part of the \$100,000 in dividends paid by Corporation Y to Corporation X is comprised of the \$50,000 of dividends paid by Corporation Z to Corporation Y.

Is the \$100,000 of dividends received from Corporation Y deductible by Corporation X in arriving at its Wisconsin net income for 1987 even though the dividends are comprised of dividends received from Corporation Z, the stock of which was not owned by Corporation Y for all of 1987?

Answer 2: Yes. Since Corporation X owned at least 80% of the total combined voting stock of Corporation Y during the entire 1987 taxable year, the \$100,000 of dividends received from Corporation Y is deductible in arriving at the 1987 Wisconsin net income of Corporation X. The fact that part of the dividends was comprised of dividends received by Corporation Y from Corporation Z has no bearing on the deductibility of the dividends by Corporation X.

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3. Deduction for Bad Debts by Corporations Other Than Certain Financial Organizations

Statutes: Section 71.02(1)(bg) Stats. as created by 1987 Wis. Act 27, sec. 71.02(1)(c), Stats. (1985-86), as amended by 1987 Wis.

Acts 27 and 399, sec. 71.04(7), Stats. (1985-86), and sec. 3047, 1987 Wisconsin Act 27

Background: Prior to the Tax Reform Act of 1986 (Act), section 166(c) of the Internal Revenue Code (IRC) allowed most corporations to claim a deduction for bad debts on the reserve method. Section 805 of the Act repealed sec. 166(c), IRC, effective for taxable years beginning after December 31, 1986. Therefore, corporations, other than certain financial organizations which may continue to claim a deduction for bad debts on the reserve method, may not claim a deduction for bad debts on the reserve method for federal purposes for taxable years beginning after December 31, 1986. A deduction for bad debts is allowed on the direct write-off (or charge-off) method.

Section 805 of the Act also provides that the change from the reserve method to the direct write-off method is a change in accounting method initiated by the taxpayer with IRS' consent. To prevent the duplication of deductions, the balance in any reserve account on the effective date of the change must be taken into income ratably over 4 years. For reserves for guaranteed debt obligations, the reserve balance is first reduced by the suspense account balance. The remaining balance is taken into income ratably over 4 years.

Effective for the Wisconsin 1987 taxable year (which is taxable years ending July 31, 1987, through June 30, 1988) and thereafter, 1987 Wisconsin Act 27 provides that a corporation must determine its Wisconsin net income under the IRC as amended to December 31, 1986, as it applies to the taxable year 1987 and subsequent years, with certain exceptions. Therefore, for the 1987 taxable year and thereafter, Wisconsin allows bad debts to be deducted under the method provided in the IRC as amended to December 31, 1986. For corporations, other than certain financial organizations, that is the direct write-off method.

For 1986 and prior taxable years, Wisconsin allowed bad debts to be deducted on the direct write-off method (except for certain financial organizations). Therefore, the changes in Wisconsin's corporate franchise or income tax law brought about by 1987 Wisconsin Act 27 did not result in any change in the allowable method of deducting bad debts for corporations, other than financial organizations.

Facts and Question 1: Corporation A, a calendar year taxpayer, deducted bad debts on the reserve method for federal tax purposes through the 1986 taxable year. As of December 31, 1986, the bad reserve balance of Corporation A was \$100,000. For federal tax purposes, \$25,000 of the reserve balance will be included in income for each of 4 years, starting with the 1987 taxable year.

How will the \$25,000 adjustment be treated on the 1987 Wisconsin corporate franchise or income tax return?

Answer 1: Since Corporation A had deducted bad debts on the direct write-off method for Wisconsin for 1986 and prior taxable

years, the \$100,000 reserve balance has not been previously deducted for Wisconsin corporate franchise or income tax purposes and does not have to be included in income for Wisconsin for 1987 through 1990. The \$25,000 should be subtracted from federal net income in arriving at Wisconsin net income for 1987. This is true for 1988, 1989, and 1990 as well.

Facts and Question 2: Corporation B, a July 31 fiscal year taxpayer, has deducted bad debts on the reserve method for federal tax purposes. Corporation B claimed a \$12,000 deduction for an addition to the bad debts reserve account on its federal return for the year ended July 31, 1987, a 1986 federal tax return. (This is the last year for which Corporation B may deduct bad debts on the reserve method for federal tax purposes.)

How is the \$12,000 deduction treated on the Wisconsin corporate franchise or income tax return for the year ended July 31, 1987?

Answer 2: Since, for Wisconsin, a July 31, 1987, fiscal year is a 1987 taxable year, and since for the 1987 taxable year Wisconsin corporation net income is determined under the IRC as amended to December 31, 1986, as it applies to the 1987 taxable year, a deduction for bad debts is not allowed on the reserve method for Wisconsin.

In determining Wisconsin net income for the year ended July 31, 1987, Corporation B should add back to federal taxable income the \$12,000 bad debt reserve expense and any recovery of bad debts written off in previous taxable years. The actual amount of any bad debts that become worthless during the year should be subtracted from federal taxable income.

Starting with the year ended July 31, 1988, Corporation B will be required to make adjustments similar to those required to be made by Corporation A in Question 1 above.



4. Sales Included in Sales Factor in Same Year That Income Is Recognized

Statutes: Section 71.07(2)(c), Stats. (1985-86)

Wis. Adm. Code: Section Tax 2.39(5), January 1978 Register

Question: In a situation where a taxpayer receives payment in one year but, due to the method of accounting employed, doesn't recognize the income for Wisconsin tax purposes until the following year(s), should the payment be included in the sales factor for Wisconsin apportionment purposes in the year received or in the year(s) the income is recognized?

Answer: Section 71.07(2)(c), Stats. (1985-86), provides in part that the sales factor is a fraction, the numerator of which is the total sales of the taxpayer in this state during the tax period, and

the denominator of which is the total sales of the taxpayer everywhere during the tax period. Therefore, if due to the method of accounting employed the sales are not recognized for Wisconsin franchise or income tax purposes, they are not included in the sales factor. The sales are included in the sales factor for the tax period in which the income is recognized.

Example: Corporation P, a calendar year, accrual basis taxpayer, is a multistate publisher of magazines which determines its Wisconsin net income by use of the three-factor apportionment formula. Corporation P has elected, under section 455 of the Internal Revenue Code, to recognize prepaid subscription payments as income ratably over the subscription period rather than in the year of receipt. The prepaid subscription payments should be included in the sales factor for Wisconsin apportionment purposes for the year(s) in which the income is recognized.



5. When a Sale Is in Wisconsin for Computing the Sales Factor of the Apportionment Formula

Statute: Section 71.07(2)(c), Stats. (1985-86)

Wis. Adm. Code: Tax 2.39(5), January 1978 Register

Background: Section 71.07(2), Stats. (1985-86), requires all multi-state corporations with operations in Wisconsin, when such operations are part of a unitary business, to file tax returns using the apportionment method. The basic apportionment formula used by most multi-state corporations is composed of a property factor representing 25% of the fraction, a payroll factor representing 25% of the fraction, and a sales factor representing 50% of the fraction.

The numerator of the sales factor is the total sales of the taxpayer in Wisconsin during the tax period and the denominator is the total sales of the taxpayer during the tax period. This Tax Release gives some examples of when sales of tangible personal property are included in the numerator.

Sales must be included in the apportionment factor in the same taxable period that they are included in apportionable income.

Facts and Question 1: The taxpayer is a Wisconsin manufacturer that sells batteries to an Illinois retailer which operates stores nation-wide. The purchaser directs the taxpayer to ship batteries to its warehouse in Wisconsin. Are these sales included in the Wisconsin numerator of the taxpayer's sales factor?

Answer 1: Yes. The destination of these sales is in Wisconsin even though the purchaser is in Illinois.

Facts and Question 2: The taxpayer is a Wisconsin manufacturer that sells batteries to a Michigan manufacturer. Title to the batteries passes to the purchaser after the batteries are manufactured. The taxpayer stores some of these batteries in its warehouse until directed to ship them to Michigan by the purchaser. Are these sales of batteries stored in Wisconsin included in the Wisconsin numerator of the taxpayer's sales factor?

Answer 2: No. The batteries are not delivered or shipped to a purchaser within Wisconsin since the purchaser's location is in Michigan and the product is shipped to Michigan. The passage of title and delay in shipment are conditions of the sale which do not affect the assignment of the sale. However, if the taxpayer is not subject to tax by the state of Michigan, the sales would be included in the numerator of the sales factor under the "throw-back" principle.

Facts and Question 3: The taxpayer is a Wisconsin manufacturer which makes engines for an Indiana manufacturer. Title to the engines passes to the purchaser after the engines are tested. The taxpayer, at the direction of the purchaser, ships the tested engines to a public warehouse in Wisconsin. The warehouse operator stores the engines until directed to ship them by the purchaser. Are these sales of engines included in the numerator of the taxpayer's Wisconsin sales factor?

Answer 3: Yes. The public warehouse is treated as a business location of the Indiana purchaser and Wisconsin is the destination state to which the taxpayer shipped the engines. The subsequent shipment of these engines is not controlled by the taxpayer.

Facts and Question 4: The taxpayer is a Wisconsin company (Company A) which manufactures and sells pipe. An Iowa purchaser submits an order, but wants the pipe waterproofed for underground installation. Company A recommends another Wisconsin company (Company B) to do the waterproofing. Company A ships the pipe to Company B and bills the Iowa purchaser for the cost of the pipe. Company B waterproofs the pipe, ships it to Iowa, and bills the purchaser for its service. Are these pipe sales by the Company A included in the Wisconsin numerator of its sales factor?

Answer 4: No. The pipe is not delivered to the purchaser in Wisconsin. Company B is an intermediary, like a common carrier. However, if Company A does not have nexus in Iowa, these sales would be included in the numerator of the sales factor under the "throwback" principle.



SALES/USE TAXES

1. Are Certain Charges Related to the Construction of a Golf Course Taxable Landscaping Services?

Statutes: Section 77.52(2)(a)20, Stats. (1985-86)

Facts and Question: A person in the landscaping business is constructing a new golf course. Among other things it involves the following types of construction work.

1. Constructing sand traps. This consists of buying sand, hauling it to the golf course and then installing the sand. It does not involve the preliminary work of digging, excavating, or shaping the trap.
2. Greens mix installation. Greens mix consists of 80% sand and 20% peat and this mixture is used to create proper drainage of the green. This mixture is purchased, installed, and fine-graded. Then grass is planted or installed on top of the greens mix.

Fine grading, such as the filling or leveling of topsoil for lawns and gardens, is a taxable landscaping service.

Are the gross receipts from constructing sand traps and installing greens mix a taxable landscaping service under sec. 77.52(2)(a)20, Stats. (1985-86)?

Answer: The construction of a sand trap is closely related to fine grading and as such is a taxable landscaping service. Therefore, the gross receipts from providing and installing sand is taxable. Greens mix is also fine graded and its installation is also considered a taxable landscaping service.

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2. Laboratory Testing in a Creamery

Statutes: Section 77.54(2) and (6)(a), Stats. (1985-86)

Wis. Adm. Code: Sections Tax 11.40, November 1981 Register and 11.41, July 1987 Register

Facts And Question: A creamery sells cheese, whey, butter, and buttermilk which it produces. This creamery carries on the following functions in its laboratory:

1. Research. This work is related to the flavoring of butter. Usually it is in connection with a special order. Instead of research into a new or existing product, this testing is done to make sure they have the proper flavor.
2. Raw product testing (a). This is testing on the raw product

before any manufacturing takes place. When the truck driver picks up a load of raw material, a sample is drawn. The load is placed in a raw products material tank, along with 20-30 other loads that were picked up from the area. The sample is tested, sometimes that day, sometimes the next day. That test is used to determine what type of raw product they are getting from that supplier. If the tests are below standard, they stop using that supplier. This is testing for payment purposes.

3. Raw product testing (b). This also is testing on the raw product before any manufacturing takes place. The sole purpose of this testing is to determine the butter fat content, which is another basis for payment.
4. Product testing. Depending on the specific product being manufactured (salted or unsalted butter, bulk or table size), the creamery tests the product at three or four different stages in the plant. They do not test the product once it has been packaged unless requested by the purchaser. This testing is conducted at about half hour intervals as the taxpayer operates around the clock.
5. The production of cultures that are used in yeast and mold formation. These cultures are part of the testing process or they become an ingredient of the product.

This laboratory contains various pieces of equipment, plus tubing attached to the equipment and glassware used to conduct the tests and collect the samples. The equipment is:

1. A special type of microwave oven.
2. Centrifuge.
3. Water bath.
4. UDY (protein analysis).
5. PH meter.
6. Sterilizer (clean up of glassware).
7. Tubing (rubber).
8. Glassware to take and test samples.

Certain chemicals used in the laboratory are only used for the purposes of determining payment to suppliers, or pre-manufacturing testing. The balance of the chemicals used in the laboratory are used mainly for manufacturing testing, but on occasion may be used for pre-manufacturing testing.

Section 77.54(6)(a), Stats. (1985-86), provides an exemption for machinery and equipment used directly and exclusively in the manufacturing process.

Are the equipment and tubing used in this testing laboratory exempt under sec. 77.54(6)(a), Stats. (1985-86), and are the chemicals and consumable supplies used in the laboratory exempt under sec. 77.54(2), Stats. (1985-86)?

Answer: The equipment and tubing located in this testing laboratory which are used in numbers 1 (research), 2 (raw product

testing), and 3 (raw product testing) are not exempt under sec. 77.54 (6)(a), Stats. (1985-86), because they are used in operations which are not manufacturing. The pieces of equipment which are used exclusively in number 4 (product testing) or number 5 (production of cultures) would be exempt if only used in these exempt manufacturing activities. If equipment is used in nonmanufacturing activities and exempt manufacturing activities, it does not meet the "exclusivity" requirement of sec. 77.54(6)(a), Stats. (1985-86).

The chemicals and other consumable supplies consumed in the manufacturing testing are exempt under sec. 77.54(2), Stats. (1985-86). However, chemicals and supplies used in pre-manufacturing testing are taxable as they are not used in the actual manufacture of tangible personal property.



3. Parking Is Provided for Monies Intended to Cover Costs

Statutes: Sections 77.51(4)(a) and (c) and 77.52(2)(a)9, Stats. (1985-86)

Wis. Adm. Code: Section Tax 11.84(2)(b), July 1987 Register

Facts and Question: A city owns and operates a parking ramp adjacent to a shopping mall operated by a private business (PB). The city asked PB for monthly payments to help maintain and operate the ramp and PB originally agreed to payments of \$65,000 a year. The amounts gradually increase with each new year. The ramp is open to the public and is used by persons shopping in the mall. The first two hours are free for anyone parking in the ramp and additional hours must be paid for. The city pays sales tax on these cash collections for additional hours. PB does not have any reserved spaces or special parking privileges in the ramp.

Section 77.51(4)(a), Stats. (1985-86), provides that "costs" may not reduce taxable gross receipts and (4)(c) provides that all receipts, cash, etc. received for providing a taxable service are subject to the sales tax. Are this city's recoveries of costs by contractual agreement in operating a parking ramp taxable parking receipts under sec. 77.52(2)(a)9, Stats. (1985-86)?

Answer: The amounts received by the city from the private business (PB) are taxable parking receipts under sec. 77.52(2)(a)9, Stats. (1985-86), even though the agreement between the parties indicate these payments are to reimburse the city for its costs.



4. Refuse Derived Fuel Plant Is a Recycling Facility

Statutes: Section 77.54(26m), Stats. (1985-86)

Facts and Question: A utility has agreed to take a county's refuse for the next 20 years and run the refuse through a refuse derived fuel (RDF) plant which the utility intends to construct in the near future. After ferrous materials, aluminum, and glass are recovered from the refuse and recycled, the remaining burnable materials (paper, wood, and plastic) will be used to produce fuel (RDF). A mixture of 54% RDF is to be used in combination with 46% wood to burn in the utility's boilers. This process then results in the production of electricity which is sold by the utility. The utility describes the project's number one criteria as maximum landfill avoidance.

Does the exemption in sec. 77.54(26m), Stats. (1985-86), for machinery and equipment used exclusively and directly in waste reduction or recycling apply to the construction of this RDF plant?

Answer: The machinery and equipment exclusively and directly used to produce refuse derived fuel is exempt under sec. 77.54(26m), Stats. (1985-86). However, this exemption would not apply to buildings or other real estate improvements nor personal property which is not used exclusively and directly in producing RDF.



5. Retailers' Receipts for Handling Manufacturers' Coupons

Statutes: Section 77.51(4) and (15), Stats. (1985-86)

Wis. Adm. Code: Sections Tax 11.28(3), July 1987 Register and 11.32(2), October 1986 Register

Facts and Question: A retailer accepts a manufacturer's coupon (25¢ value) in selling a 67¢ bar of soap to a customer. The coupon's value is 25¢ and the retailer receives an additional 7¢ from the manufacturer for handling the coupon. Therefore, the manufacturer actually pays 32¢ to the retailer. The retailer also accepts a 25¢ coupon on the purchase of a frozen pizza which is an exempt grocery item. The retailer also receives 32¢ from the manufacturer for this transaction.

Is the 7¢ received by the retailer for handling either of these coupons subject to the sales tax?

Answer: Section 77.51(4), Stats. (1985-86), which defines the receipts of a retailer which are subject to the sales tax, does not include receipts from handling coupons, whether related to taxable sales of soap or nontaxable sales of frozen pizza. There-

fore, receipts received by retailers from manufacturers for handling coupons are not taxable. However, the 25¢ received by the retailer for the coupon on the sale of the bar of soap is taxable.



6. Sales to Government and Other Exempt Organizations' Employees

Statutes: Sections 77.54(9a) and 77.55(1), Stats. (1985-86)

Wis. Adm. Code: Section Tax 11.05(4)(intro.), (a.) and (d), October 1987 Register

Background: The Wisconsin sales and use tax law in sec. 77.54 (9a), Stats. (1985-86), provides an exemption for sales of tangible personal property and services to the following governmental agencies and nonprofit organizations:

- A. State of Wisconsin or any agency thereof.
- B. Any county, city, village, town, or school district in Wisconsin.
- C. A county-city hospital established under sec. 66.47, Stats. (1985-86)
- D. A sewerage commission organized under sec. 144.07(4), Stats. (1985-86), or a metropolitan sewerage district organized under secs. 66.20 to 66.26 or 66.88 to 66.918, Stats. (1985-86).
- E. Any other unit of government in Wisconsin or any agency or instrumentality of one or more units of government in Wisconsin.
- F. Any corporation, community chest fund, foundation, or association organized and operated exclusively for religious, charitable, scientific, or educational purposes, or for the prevention of cruelty to children or animals (except hospital service insurance corporations under sec. 613.80(2), Stats. (1985-86)) no part of the net income of which inures to the benefit of any private stockholder, shareholder, member, or corporation.

Sales to the United States and its incorporated or unincorporated agencies and instrumentalities are exempt from Wisconsin sales and use tax under sec. 77.55(1), Stats. (1985-86).

Facts: Restaurants, motels, and other retailers sell meals and lodging to the above governmental agencies and nonprofit organizations or to their employees under various situations. In order for a sale to such governmental agencies or nonprofit organizations to be exempt from Wisconsin sales and use tax, the following three conditions must occur:

- A. The retailer (e.g., motel or restaurant) issues the billing or

invoice for the meal or lodging in the name of the exempt entity.

- B. The retailer receives from the exempt entity:

1. A purchase order or similar written document if the exempt entity is a governmental agency listed in A, B, C, D or E above, or is a United States agency or instrumentality, or
2. The Certificate of Exempt Status number of the exempt entity if it is a nonprofit organization described in F above. The retailer must enter this exempt status number on the retailer's copy of the invoice or billing document.

- C. The retailer keeps a copy of the documents mentioned in A and B to substantiate that the sale was exempt from Wisconsin sales and use tax.

NOTE: If these three conditions are met, the sale to the governmental agency or nonprofit organization is exempt from Wisconsin sales and use tax, regardless of whether such exempt entity or its employee pays the retailer for the sale of the meal or lodging.

Question 1: An employee of the State of Wisconsin purchased a meal and lodging in a motel. The billing is made in the employee's name and the employee pays the bill with his or her own funds. The employee is subsequently reimbursed by the employer (State of Wisconsin) for the amount of the meal and lodging. Is the sale of the meal and lodging subject to sales tax?

Answer 1: Yes. This sale is taxable because it is a sale to the employee, rather than to the State of Wisconsin. (Note: This sale of the meal and lodging would still be taxable, even though the employee submitted a letter from the State of Wisconsin indicating that it would ultimately be responsible for the cost of the meal and lodging.)

Question 2: An employee of a church purchases a meal and lodging and gives the retailer the Certificate of Exempt Status number of the church. The billing is in the name of the church and the church directly pays the retailer for the meal and lodging. Is the sale of the meal and lodging subject to sales tax?

Answer 2: No. This sale of the meal and lodging is exempt from sales tax under sec. 77.54(9a), Stats. (1985-86), because the sale is considered to be made to the church, rather than to the employee. The retailer must record the church's Certificate of Exempt Status number on the billing to substantiate that the sale was an exempt sale to the church. (Note: This sale would still be exempt if the employee (rather than the church) paid the retailer and was subsequently reimbursed by the church.)

Question 3: An employee of an agency of the State of Minnesota purchases a meal and lodging and submits a letter to the retailer (which is placed in the retailer's files) indicating that the employee is traveling on agency business and funds are being

provided to the employee to pay any expenses. The retailer's bill is made in the name of the Minnesota state agency. Is the sale of the meal and lodging subject to sales tax.

Answer 3: Yes. This transaction is subject to sales tax because agencies of other states are not entitled to the exemption under sec. 77.54(9a), Stats. (1985-86)

Question 4: A City of Madison employee, when purchasing a meal and lodging, submits a letter to the retailer from the city indicating that the employee is on city business and the city authorizes the employee to purchase meals and lodging relating to such city business. This letter is placed in the retailer's files. The retailer makes out the bill in the name of the City of Madison. The employee pays the bill with his or her own funds and is subsequently reimbursed by the city. Is the sale of the meal and lodging subject to sales tax?

Answer 4: No. This is an exempt sale to the City of Madison under sec. 77.54(9a), Stats. (1985-86)

Question 5: An employee of the federal government purchases lodging in a motel. The employee provided the motel with a letter from the federal agency (which is placed in the retailer's files) indicating the employee is traveling on agency business and the agency is responsible for payment of this employee's expenses. The billing is made out to the federal agency. The employee used a travel advance to pay for the lodging. Is the sale of lodging subject to sales tax?

Answer 5: No. This sale is exempt from tax under sec. 77.55(1), Stats. (1985-86), because it is considered a sale to the federal agency.

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7. Wax Purchased by Car Wash Operators

Statutes: Section 77.52(2)(a)10 and (2m)(b), Stats. (1985-86)

Wis. Adm. Code: Section Tax 11.67(3)(m), September 1984 Register

Facts and Question: The "incidental" test for resale items purchased by persons who provide taxable services went into effect on September 1, 1983, pursuant to 1983 Wis. Act 27. Section Tax 11.67(3)(m), Wis. Adm. Code, provides that wax transferred to the customer's vehicle may be purchased without tax by the car wash operator. The business of washing motor vehicles is a taxable service under sec. 77.52(2)(a)10, Stats. (1985-86), and sec. 77.52(2m)(b), Stats. (1985-86), provides that with respect to services subject to taxation under sec. 77.52(2)(a)10, all property physically transferred to the customer in conjunction with the service is a sale of tangible personal property which may be purchased for resale.

Do purchases of wax by car wash operators qualify as exempt purchases for resale under sec. 77.52(2m)(b), Stats. (1985-86), effective September 1, 1983?

Answer: Yes. The "resale" policy set forth in s. Tax 11.67(3)(m), Wis. Adm. Code, for purchases of wax by car wash operators continues to apply.

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