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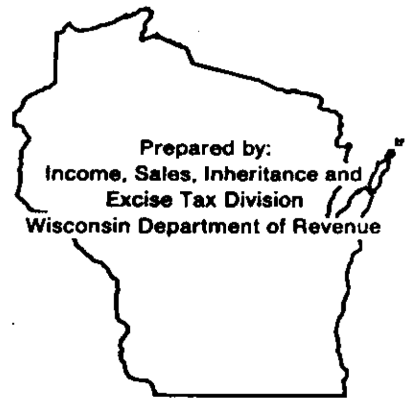

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Subscribe to the Wisconsin Department of Revenue's new Topical and Court Case Index. This index will help you find a particular Wisconsin statute, administrative rule, Wisconsin Tax Bulletin article or tax release, publication, Attorney General opinion, or court decision that deals with your particular Wisconsin tax question.

The index is divided into two parts. The first part, called the "Topical Index", gives references to alphabetized subjects for the various taxes. The taxes include individual income, corporation franchise or income, sales/use, withholding, gift, estate and inheritance, cigarette, tobacco products, beer, intoxicating liquor and wine, and motor fuel. An excerpt from the individual income tax section of the topical index appears on page 37 of this Bulletin.

The second part, called the "Court Case Index", lists Wisconsin Tax Appeals Commission, Circuit Court, Court of Appeals, and Wisconsin Supreme Court decisions by alphabetized subjects for the various taxes. An excerpt from the corporation section of the court case index appears on page 38 of this Bulletin.

This index will be available in December, 1990. The annual cost is $14 per copy, plus sales tax. Subscribers will receive the full index in December, 1990 and also an addendum providing updated information in May, 1991. To order your copy of the index, complete the order blank that appears on page 39 of this Bulletin. By ordering early, you can expect to receive your copy in December, 1990.

In This Issue

EIGHT PERSONS CHARGED WITH CRIMINAL VIOLATIONS OF INCOME TAX LAWS

Income Tax

John P. Dewane, 1030 North 16th Street, Manitowoc, an attorney, was charged in Manitowoc County Circuit Court on April 12 with 3 counts of failing to file state income tax returns for each of the years 1986, 1987, and 1988. James R. Pope, 314 Tower Court, Dodgeville, also an attorney, was charged in Dane County Circuit Court with 3 counts of failing to timely file state income tax returns for each of the years 1986, 1987, and 1988. Attorney James C. Cotter, 1619 Dee Ann Court, Wisconsin Dells, was charged on April 12 with failing to timely file a state income tax return for 1986.

James A. Sneeden, 134 Wood Avenue, Nekoosa, also known as James A. Beckholt, was charged April 11 with failing to file state income tax returns for each of the years 1986, 1987, and 1988. Beckholt's court appearance has not been scheduled because he is being held in the Waupaca County Jail on a first-degree intentional-homicide charge.

Criminal charges have been initiated against Gerald W. Wenger and his wife, Karen R. Wenger, 1420 Church Avenue, Wisconsin Rapids. The Wengers were charged on April 6 with 3 counts of failing to file state income tax returns for each of the years 1986, 1987, and 1988. The Wengers did not appear in Wood County Circuit Court as scheduled, and a bench warrant was issued for their arrest.

The criminal complaint on file against the Wengers states he is a self-employed truck driver and she is a waitress and also a truck driver. It also states their combined gross income was $34,646 in 1986, $41,559 in 1987, and $38,341 in 1988.

Wisconsin Rapids businessman and Wood County Board member John T. Siewert Sr., 70, and his wife, Ida Lee Siewert, 65, have been charged in Dane County Circuit Court with failing to file state income tax returns for each of the years 1986, 1987, and 1988.

According to the criminal complaint against them, the Siewerts earned in excess of $300,000 for each of the calendar years 1986, 1987, and 1988, but filed no tax returns.

The bulk of the income in the three years for which they are charged came from John Siewert's share of the partnership gross of the Coldwell Banker-Siewert Realtors firm. The complaint states Siewert's share of the gross for the three years in question was $250,855, $286,611, and $270,503.

In addition, John Siewert was paid $24,000 in each of the three years by Siewert-Moog Inc., and earned a total of $2,732 for the three years as a member of the Wood County Board. Siewert also collected $7,433 during the three-year period from his share of ownership in the King Richards Courts health club in Wisconsin Rapids, the complaint states.

Ida Siewert, a special education teacher in the Wisconsin Rapids School District, was paid $21,464, $21,298, and $22,880 by the school for the three years, and was paid more than $5,500 from her husband's firm in each of the three years.

The Siewerts were released on $500 signature bonds following a brief court appearance in which not guilty pleas were entered on their behalf.

Court appearances or actions were scheduled for each of the above-listed defendants. Failing to file a Wisconsin state income tax return at the time required by law is a crime punishable by a fine of not more than $10,000 or imprisonment not to exceed nine months or both. In addition to the criminal penalties, Wisconsin law provides for substantial civil penalties on the civil tax liability. Assessment and collection of the taxes, penalties and interest due follows conviction for criminal violation.

Excise Tax

A former Waterford businessman has been charged with criminal violations of the Wisconsin state fuel tax laws. Charles R. Guschl, 3386 Highway 45 South, Conover, who formerly operated Dick's Towing in Waterford, was charged in Dane County Circuit Court, Madison, on April 30 with fraudulently withholding and appropriating special fuel taxes belonging to the state in excess of $14,000 from May 20, 1984 until January 19, 1987.

Theft of state motor fuel or special fuel tax money is a felony punishable by a fine not to exceed $10,000 or imprisonment not to exceed ten years or both when the amount of the misappropriation exceeds $2,500.

SELLER'S PERMIT RENEWAL INSERT, FORM S-801, SENT TO RETAILERS

Background

Seller's permits expire every two years on the last day of the original issuance month. Permits are automatically renewed unless the permittee has a liability of $400 of delinquent taxes and any portion has been delinquent for five months or longer.

New Process

The department has recently implemented a new form to be inserted with a renewed seller's permit sent to a registered seller. The new form provides basic information regarding the requirement to timely file sales and use tax returns, the need to post the renewed seller's permit at the place of business, and the necessity to keep the department updated on changes to the basic account information. Revisions to account information include changes in ownership and mailing/business address, or the discontinuance of the business.

The department currently inactivates approximately 21,000 permits each year as a result of notification from the discontinued seller. This amount may slightly increase as a result of the additional notification to sellers of their responsibility to keep the department informed of changes to the status of the account. This will save the department from maintaining and monitoring the compliance of sellers that have discontinued their business but have neglected to provide proper notification to the department. The new form also makes an attempt to have the registered seller provide the department with its related Wisconsin employer's account number and Federal Employer Identification Number.

Of the 159,000 active registered seller's locations, approximately half of the accounts receive renewed seller's permits each year. The renewed seller's permit is mailed early in the month that the old permit expires, unless nonrenewed because the permittee owes delinquent taxes.

The new form has been included with all renewed seller's permits printed and mailed after March 5, 1990. A copy of the Seller's Permit Renewal Insert, Form S-801, appears on pages 42 and 43 of this Bulletin.

TAXPAYER COULD OWE ALTERNATIVE MINIMUM TAX BECAUSE OF SCHOOL PROPERTY TAX/RENT CREDIT

A flyer was sent to all persons receiving the additional school property tax/rent credit. The flyer is reproduced on pages 44 and 45 of this Bulletin. One of the questions and answers indicated that if a taxpayer had a Wisconsin alternative minimum tax (WAMT) liability in 1987 or 1988, the taxpayer's additional school property tax/rent credit for that year would be zero. Because a taxpayer's regular tax is used to compute WAMT, as the amount of regular tax decreases (which it does as a result of the additional credit), the WAMT increases by the same amount.

Example: On line 18 of 1988 Schedule MT, Taxpayer A filled in a minimum tax of $6,000. On line 19 of 1988 Schedule MT, Taxpayer A filled in regular tax of $5,000 from his or her originally filed 1988 Wisconsin Form 1. Taxpayer A computed a WAMT liability of $1,000 for 1988 ($6,000 minimum tax less $5,000 regular tax). Assuming Taxpayer A is entitled to an additional school property tax credit of $130 for 1988, Taxpayer A's WAMT liability is recomputed to account for the reduced regular tax, resulting in a WAMT liability of $1,130 ($6,000 minimum tax less $4,870 regular tax). The additional school property tax/rent credit ($130) is used to offset the additional WAMT liability that results ($130). Therefore, Taxpayer A receives no check for 1988 additional credit. The taxpayer will receive no notice stating that the additional credit has been offset against the increase in WAMT liability.

The flyer does not mention that some taxpayers who had no WAMT liability on their 1987 or 1988 returns may now incur a liability for WAMT because of the additional school property tax/rent credit. The taxpayer's additional credit was not adjusted for this liability before the check was sent, because the department's computer history file for the taxpayer does not contain information which can be used to compute WAMT liability. This liability can only be determined by examination of the taxpayer's Wisconsin income tax return. Therefore, an adjustment to the taxpayer's Wisconsin return may be necessary. This adjustment can be made either by the department in its audit of returns or it can be made on an amended return filed by the taxpayer.

Example: On line 18 of 1988 Schedule MT, Taxpayer B filled in a minimum tax of $6,000. On line 19 of 1988 Schedule MT, Taxpayer B filled in a regular tax of $6,100 from his originally filed Wisconsin 1988 Form 1. Taxpayer B computed no WAMT liability because the taxpayer's regular tax ($6,100) was greater than the minimum tax ($6,000). Assuming Taxpayer B is entitled to an additional school property tax/rent credit of $130 for 1988, Taxpayer B now has a WAMT liability of $30 ($6,000 minimum tax less $5,970 regular tax) because of the reduction in the amount of regular tax. The taxpayer was sent the additional credit of $130. The department may subsequently make an adjustment to the taxpayer's 1988 Wisconsin Form 1 to account for the $30 WAMT liability still outstanding.

HOMESTEAD AND FARMLAND PRESERVATION CREDITS ARE POPULAR

For the fiscal year ending June 30, 1989, homestead credits totaling almost $100 million were issued to over 260,000 claimants, and farmland preservation credits totaling over $28 million were issued to almost 24,000 claimants.

The average homestead credit was $380, and the average farmland preservation credit was $1,192. The schedule below shows additional data about homestead credit and farmland preservation credit for the past two fiscal years.

	1987-88	1988-89
Homestead Credit		
Total credit allowed	$103,829,374	$99,449,998
Number of claims filed	261,349	261,924
Average credit per claim	$397	$380
Farmland Preservation Credit		
Total credit allowed	$ 29,414,590	$28,342,642
Number of claims filed	23,373	23,776
Average credit per claim	$1,258	$1,192

PROPERTY TAX DEFERRAL LOANS ARE BEING GRANTED

In 1989, loans totaling $400,000 were granted by the Department of Revenue to over 300 persons, to help them pay the property taxes on their Wisconsin homestead.

Property tax loans are granted through the Property Tax Deferral Loan Program, which began in 1986. To obtain a loan, a participant must be age 65 or older, and total household income cannot exceed $20,000 for the year. Up to $1,800 per year may be borrowed. The loan does not have to be repaid until the participant sells or moves out of the home, though all or any part of the loan may be repaid at any time.

The average loan in 1989 was for $1,270. The schedule below shows additional data about property tax deferral loans for the past two calendar years.

	1988	1989
Property Tax Deferral Loans		
Number of loans allowed	314	311
Average amount of loan	$ 1,246	$ 1,270
Average household income	$10,250	$10,445
Average age of participant	75	76
Loans outstanding at year-end	763	967

ESTIMATED TAX REQUIREMENTS FOR GRANTOR TRUSTS FUNDED ON ACCOUNT OF A DECEDENT'S DEATH

An article in *Wisconsin Tax Bulletin* 66 (page 5) reported that trusts are subject to Wisconsin's estimated tax requirements for 1990. It should be noted that grantor trusts which are funded on account of a decedent's death are only required to make estimated tax payments for tax years which end two or more years after the decedent's death.

Example: An individual died on April 25, 1990. A grantor trust which was funded on account of her death is not required to make estimated tax payments for any tax year ending before April 25, 1992.

INFORMATION OR INQUIRIES?

Madison - Main Office
Area Code (608)

Beverage, Motor Fuel, Cigarette,
Tobacco Products 266-6701
Corporation Franchise/Income 266-3645
Estimated Taxes 266-9940
Fiduciary, Inheritance, Gift. 266-1231

Homestead Credit	266-8641
Individual Income	266-2486
Property Tax Deferral Loan	266-1983
Sales, Use, Withholding	266-2776
Audit of Returns: Corporation, Individual, Homestead, Sales	266-2772
Appeals	266-0185
Refunds	266-8100
Delinquent Taxes	266-7879
Copies of Returns: Homestead, Individual	266-2890
All Others	266-0678
Forms Request: Taxpayers	266-1961
Practitioners	267-2025

District Offices

Appleton	(414) 832-2727
Eau Claire	(715) 836-2811
Milwaukee	(414) 227-4000

WE ARE FREQUENTLY ASKED ...

1. *Question:* Can I obtain an extension of time to file an appeal with the Department of Revenue's Appellate Bureau?

   Answer: No. An appeal must be filed within 60 days from the receipt of a notice of assessment, refund, refund denial, or credit adjustment. The 60-day period cannot be extended, but once an initial appeal is filed a taxpayer may subsequently amend or expand upon the appeal or object to additional items, as long as the appeal is still pending with the Appellate Bureau.

2. *Question:* Must I pay the assessment in order to appeal to the Appellate Bureau?

   Answer: No. You do not have to pay any amount until the appeal process is completely ended. However, to stop the further accumulation of interest you would have to deposit the full amount of the assessment; the Appellate Bureau cannot accept partial deposits. If, however, you agree to a portion of the assessment, you may recompute and pay the tax and interest on the agreed portion.

3. *Question:* When will a conference be scheduled for my appeal?

   Answer: Appeals are handled in the order they are received by the conferee. Depending on the conferee's backlog, it may take 3 or 4 months before a conference can be scheduled.

4. *Question:* Can I obtain a Private Letter Ruling from the department regarding an issue that is under appeal?

   Answer: No, unless unique and compelling reasons justify a ruling. Based on Wisconsin Publication 111, "How to Get a Private Letter Ruling From the Wisconsin Department of Revenue," the department ordinarily will not provide a ruling on an issue involved in an audit which has been completed. This would include an issue which has been appealed to the Appellate Bureau.

5. *Question:* If I disagree with a decision from the Appellate Bureau, how can I appeal the decision?

   Answer: You may file a "petition for review" with the Wisconsin Tax Appeals Commission at 217 S. Hamilton St., Suite 501, Madison, WI 53702. The petition for review must be in writing and must be filed within 60 days of your receipt of the notice of action from the Appellate Bureau.

NEW ISI&E DIVISION RULES AND RULE AMENDMENTS IN PROCESS

Listed below, under Parts A, B, and C, 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 June 25, 1990. Part D lists new rules and amendments which were adopted in the period from March 16, 1990 through June 25, 1990. Part E lists Rules adopted in 1990 but not yet effective. ("A" means amendment, "NR" means new rule, "R" means repealed and "R&R" means repealed and recreated.)

A. Rules at Legislative Council Rules Clearinghouse

1.11	Requirements for examination of returns-R&R
2.02	Reciprocity-R&R
2.39	Apportionment method-R&R
2.95	Reporting of instalment sales by natural persons and fiduciaries-A
4.54	Security requirements-NR
4.55	Ownership and name changes-NR
9.67	Cigarette tax credit-R&R
9.68	Ownership and name changes-NR
11.002	Permits, application, department determination-A
11.01	Sales and use tax return forms-R&R
11.03	Elementary and secondary schools and related organizations-A
11.08	Medical appliances, prosthetic devices and aids-A
11.09	Medicines-A
11.14	Exemption certificates (including resale certificates)-A
11.15	Containers and other packaging and shipping materials-A
11.17	Hospitals, clinics and medical professions-A
11.19	Printed material exemption-A
11.28	Gifts, advertising specialities, coupons, premiums and trading stamps-A
11.40	Exemption of machines and processing equipment-A
11.41	Exemption of property consumed or destroyed in manufacturing-A
11.45	Sales by pharmacies and drug stores-A
11.47	Commercial photographers and photographic services-A
11.48	Landlords, hotels and motels-A
11.49	Service stations and fuel oil dealers-A
11.53	Temporary events-A
11.54	Temporary amusement, entertainment, or recreational events or places-A
11.57	Public utilities-A
11.62	Barbers and beauty shop operators-R&R
11.65	Admissions-A
11.66	Telecommunication and CATV services-A
11.78	Stamps, coins and bullion-A
11.83	Motor vehicles-A
11.85	Boats, vessels and barges-A

11.925 Sales and use tax security deposits-A
11.95 Retailer's discount-A
11.97 "Engaged in business" in Wisconsin-A
11.98 Reduction of delinquent interest rate under s. 77.62(1), Stats.-A
14.01 Administrative provisions-A
14.04 Property taxes accrued-A
14.05 Gross rent and rent constituting property taxes accrued-A

B. Rules at Revisor of Statutes Office for Publication of Hearing Notice

2.41 Separate accounting method-A
2.46 Apportionment of business income of interstate air carriers-R&R
2.49 Apportionment of net business incomes of interstate finance companies-R&R
17.01 Administrative provisions-A
17.02 Eligibility-A
17.03 Application and review-A

C. Rules at Legislative Standing Committee

7.01 Purchases and invoices-A
7.23 Activities of brewers, bottlers and wholesalers-A

D. Rules Adopted in Period from March 16, 1990 to June 25, 1990 (effective date is given in parentheses)

11.10 Occasional sales-A (5/1/90)
11.16 Common or contract carriers-A (5/1/90)
11.18 Dentists and their suppliers-A (5/1/90)
11.26 Other taxes in taxable gross receipts and sales price-A (5/1/90)
11.32 "Gross receipts" and "sales price"-A (5/1/90)
11.41 Exemption of property consumed or destroyed in manufacturing-A (5/1/90)
11.57 Public utilities-A (5/1/90)
11.66 Communications and CATV services-R&R (5/1/90)
11.67 Service enterprises-A (5/1/90)
11.68 Construction contractors-A (5/1/90)
11.84 Aircraft-A (5/1/90)
11.85 Boats, vessels and barges-A (5/1/90)

E. Rules Adopted in 1990 But Not Yet Effective

1.06 Application of federal income tax regulations for persons other than corporations-A
1.10 Depository bank requirements for withholding, motor fuel, general aviation fuel and special fuel tax deposit reports-A
2.03 Corporation returns-A
2.04 Information returns and wage statements-R&R
2.06 Information returns required of partnerships and persons other than corporations-R
2.08 Returns of persons other than corporations-A
2.10 Copies of federal returns, statements, schedules, documents, etc., to be filed with Wisconsin returns-A
2.30 Property located outside Wisconsin - depreciation and sale-A
2.69 Income from Wisconsin business-R
2.89 Penalty for underpayment of estimated tax-R
2.955 Credit for income taxes paid to other states-A
3.03 Dividends received, deductibility of-R&R
3.08 Retirement and profit-sharing payments by corporations-A
3.085 Retirement plan distributions-A
3.096 Interest paid on money borrowed to purchase exempt government securities-A
3.10 Salesmen's and officers' commissions, travel and entertainment expense of corporations-R
3.12 Losses on account of wash sales by corporations-R&R
3.37 Depletion of timber by corporations-A
3.38 Depletion allowance to incorporated mines and mills producing or finishing ores of lead, zinc, copper, or other metals except iron-A
3.47 Legal expenses and fines—corporations-R
3.54 Miscellaneous expenses not deductible—corporations-R&R
3.81 Offset of occupational taxes paid against normal franchise or income taxes-A
3.91 Petition for redetermination-A
3.92 Informal conference-A
3.93 Closing stipulations-A
3.94 Claims for refund-A
8.01 Tax liability-NR
8.02 Revenue stamps—occupational tax-R&R
8.03 Affixing stamps-R
8.04 Refunds-R&R
8.05 Special tax on intoxicating liquor-R
8.06 Mixture of specially taxed and regularly taxed intoxicating liquors-R
8.11 Reports-A
8.12 Samples-NR
8.21 Purchases by the retailer-A
8.22 Purchases made outside of state-A
8.23 Sales to non-licensees-NR
8.31 Sales out of Wisconsin-A
8.51 Labels-R
8.61 Advertising-A
8.66 Merchandise on collateral-A
8.71 Bitters-R
8.76 Salesperson-R&R
8.81 Transfer of retail liquor stocks-A
8.87 Intoxicating liquor tied-house prohibitions-A
11.05 Governmental units-A
11.09 Medicines-A
11.12 Farming, agriculture, horticulture and floriculture-A
11.19 Printed material exemption-A
11.40 Exemption of machines and processing equipment-A
11.51 Grocers' guidelist-A
11.535 Operators of a swap meet, flea market, craft fair or similar event-NR
11.57 Public utilities-A
11.61 Veterinarians and their suppliers-A
14.03 Household income and income-A
14.06 Marriage, separation, or divorce during a claim year-A

REPORT ON LITIGATION

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

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

The following decisions are included:

INDIVIDUAL INCOME TAXES

Minimum tax—1986. *Edward J. and Eleaner L. Blakely vs. Wisconsin Department of Revenue, and Richard N. and Marlene O. Mastenbrook vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, February 19, 1990). The issue in this case is whether the taxpayers owed federal alternative minimum tax (AMT) under sec. 55 of the Internal Revenue Code (IRC) for purposes of application of the 1986 Wisconsin minimum tax (WMT) under sec. 71.60(1), Wis. Stats.

The taxpayers were all Wisconsin residents throughout 1986 and at all times relevant to their petitions. They timely filed joint Forms 1040 and Forms 1 for their 1986 tax years. Both of their 1986 Forms 1040 showed an AMT on Line 51. However, in each case the total tax shown on Line 55 was in the same amount as it would have been had there been no AMT, due to the computational mechanics of subtracting out general business credits on Line 47 and adding them back in as AMT on Line 51. The taxpayers' federal AMT shown at Line 51, Form 1040, resulted solely from the method of computation as set forth on the Form 1040 and other federal forms attached thereto.

The taxpayers' Wisconsin Forms 1 included an attached statement reducing the federal AMT to zero on the grounds that "federal AMT is reduced by general business credits for which the taxpayer received no federal or Wisconsin tax benefit in 1986." Accordingly, the taxpayers included no WMT under sec. 71.60, Wis. Stats., on Line 16 of their respective Forms 1.

The taxpayers' 1986 federal taxable income differed from their 1986 Wisconsin taxable income in various respects, including the following:

(1) Through their ownership interests in various partnerships and corporations, for 1986 federal income tax purposes the taxpayers had 1986 general business credits under IRC sec. 38, more specifically known as investment credits and targeted jobs credits. Through the same sources they had general business credit carryforwards to 1986 from prior years 1978 and 1982 through 1985. Such credits or credit carryforwards were not allowed for Wisconsin income tax purposes.

(2) The Mastenbrooks in 1986 had federally taxable interest on U.S. government obligations. Wisconsin does not tax such interest.

(3) In 1986 the taxpayers had federally taxable refunds of 1985 Wisconsin income taxes they overpaid. Wisconsin neither allows state income taxes as deductions from income nor taxes state income tax refunds.

(4) The taxpayers recognized federal depreciation recapture income in 1986 because of the liquidation during 1986 of Martichick, Inc., an S corporation they owned. Wisconsin does not provide for or tax such depreciation recapture.

(5) A portion of the wages paid by the taxpayers' S corporations and partnerships were used for federal targeted jobs tax credits and were therefore not deductible from income under IRC sec. 280C(a).

(6) By virtue of their ownership of Alpha Distributors Ltd., the taxpayers federally deducted a reserve for bad debts under IRC sec. 166(c). The federal reserve for 1986 was smaller than the bad debts which became worthless during such year and were therefore deductible from Wisconsin income under sec. 71.04(7), Wis. Stats.

The taxpayers' 1986 federal AMT was calculated under IRC sec. 55, as it read prior to the Tax Reform Act of 1986. Their federal AMT was calculated by: starting with their adjusted gross income (AGI); reducing AGI by certain items set forth in IRC sec. 55(b)(1); increasing the result by the items of tax preference referred to in IRC sec. 55(b)(2) and described in IRC sec. 57, the result being the "alternative minimum taxable income"; subtracting an exemption amount of $40,000; multiplying the result by 20%; and subtracting the regular tax for the year 1986. This computation had the following results, among others:

(A) The taxpayers' AGI included the income differences listed in parts (2), (3), and (4) above. These three items were, by means of the calculation described above, subjected to federal AMT. Under the department's determination, they were also made subject to WMT under application of sec. 71.60, Wis. Stats.

(B) The taxpayers' federal AGI was not reduced by the income differences listed in parts (5) and (6) above. These wages and bad debts, deductible from Wisconsin but not regular federal income, were by means of the calculation described above subjected to federal AMT. Under the department's determination, these wages and bad debts were also made subject to WMT.

(C) In computing their 1986 AMT, the entire amount of the taxpayers' federal general business credit carryovers from prior years, as listed in part (1) above, were subtracted from their 1986 regular federal income tax to determine their "regular tax for the taxable year" for AMT purposes under IRC sec. 55(a). This subtraction caused their "regular tax for the taxable year" to fall below the amount equal to 20% of their alternative minimum taxable income less their $40,000 exemption.

Had the general business credit carryforwards referred to in part (C) above only been subtracted from the taxpayers' regular income tax to the extent that they generated a 1986 federal tax benefit, their "regular tax for the taxable year" would have been equal to the 20% amount described in IRC sec. 55(a), and there would have been no AMT. Under the calculation as required by the IRS forms, however, the excess federal credit carryforwards were used to reduce the "regular tax for the taxable year" below the 20% amount, giving rise to a nominal AMT in the same amount as the excess credit carryforwards. These excess credit carryforwards therefore provided the taxpayers with no 1986 federal tax benefit, and were allowed to be carried forward to 1987 and later years, under IRC sec. 55(c)(3). Under the department's determination, the taxpayers' federal general business credit carryforwards from years prior to 1986 were made subject to WMT, even though the taxpayers received no Wisconsin tax benefit from the excess credit carryforwards in any year, and no federal tax benefit from such excess credit carryforwards for the year 1986 or any prior year.

Had the taxpayers' federal AMT for 1986 been calculated under IRC sec. 55, as it read as a result of amendment by the Tax Reform Act of 1986, the calculation would have been similar to that set forth above, with the following relevant differences (in parts (1) to (4) below, all references to "IRC" are the Internal Revenue Code as amended by the Tax Reform Act of 1986):

(1) The starting point would have been the taxpayers' taxable income for the year, adjusted as provided in IRC secs. 56 and 58, and increased by the items of tax preference listed in IRC sec. 57, the result being the "alternative minimum taxable income", per IRC sec. 55(b)(2).

(2) The "exempt amount", or $40,000 in the taxpayers' cases, is subtracted, per IRC sec. 55(d).

(3) The result is multiplied by 20%, per IRC sec. 55(b)(1)(A); the result (since the taxpayers had no alternative minimum tax foreign tax credit) is called the "tentative minimum tax", per IRC sec. 55(b).

(4) If the tentative minimum tax is greater than the "regular tax for the taxable year", the excess is the amount of the federal AMT, per IRC sec. 55(a).

Of these differences, the only one which would affect the amount of the WMT is the definition of "regular tax for the taxable year" under part (4). Under the Tax Reform Act of 1986, the definition of "regular tax" was clarified in such a way that the taxpayers' excess general business credits **could not possibly** be subtracted as part of the calculation, as they were on their 1986 federal Forms 1040 as filed, per IRC sec. 55(c), as amended by sec. 701(a) of the Tax Reform Act of 1986. The result would have been that there would have been no 1986 federal AMT for purposes of the 1986 WMT.

The taxpayers received no 1986 federal tax benefit from the amount of general business credit carryforwards equal to the AMT shown on Line 51, Forms 1040. Wisconsin law does not allow (and has never allowed) federal general business credits to offset any Wisconsin tax liability. The taxpayers received no Wisconsin tax benefit in any year from their general business credit.

The Commission concluded as follows:

(1) Section 71.60(1), Wis. Stats., as amended by 1987 Wis. Act 27, applies in this case and requires application of sec. 55 of the Internal Revenue Code as it existed prior to amendments made by sec. 701(a) of the Tax Reform Act of 1986, which was enacted October 22, 1986, but first effective in 1987.

(2) Wisconsin individual income tax law requires only compliance with the Internal Revenue Code. Taxpayers are not bound in every instance to apply the Code identically for federal and Wisconsin tax purposes.

(3) Under the Internal Revenue Code, the taxpayers would have been permitted to claim less than the full amount of their available general business credits against regular tax, so as to eliminate the alternative minimum tax under IRC sec. 55. This would have increased their regular tax liability and current payment required by the amount of AMT avoided.

(4) Determination of the federal alternative minimum tax "owed" for Wisconsin minimum tax purposes under sec. 71.60(1), Wis. Stats., is not necessarily limited by calculations made on the federal alternative minimum tax forms, and the taxpayers may file their Wisconsin returns, including Wisconsin minimum tax, reflecting an alternative but proper application of the Internal Revenue Code.

(5) Where, as here, the taxpayers demonstrate that they would have been permitted federally to decrease their claims of credit against regular income tax liability, thereby increasing the current regular income tax payment required, in **lieu of** paying an equal amount of alternative minimum tax, they must be held to have owed no alternative minimum tax for purposes of sec. 71.60(1), Wis. Stats. Accordingly, they owe no Wisconsin minimum tax under said section.

The Commission therefore reversed the department's actions denying redetermination of the assessments in these cases.

The department has appealed this decision to the Circuit Court.

❑

Allocation of Expense—solely-owned property. *Robert and Marcia Stark vs. Tax Appeals Commission, Department of Revenue, State of Wisconsin* (Court of Appeals, District II, January 31, 1990). The Tax Appeals Commission, Department of Revenue and State of Wisconsin (collectively, the state), have appealed from that portion of a Circuit Court judgment of a Commission decision wherein the Circuit Court stated: "The taxpayer and his wife are specifically allowed to recompile tax returns which are the subject of this proceeding, in compliance with generally accepted accounting principles as they apply to interest and bad debts expense." The taxpayers did not file a cross-appeal.

The issue in this case is the handling of interest expense relating to a rental condominium property. The warranty deed for the condominium was issued to Robert Stark and Marcia Stark, as husband and wife. Both Robert and Marcia signed the purchase money mortgage. Only Robert, however, signed the mortgage note for the property. On the challenged tax returns, Robert claimed all the rental losses and interest expense from the condominium property. The Department of Revenue reallocated 50 percent of the claimed rental loss and interest expense to the taxpayer's wife because she was an owner of the property in joint tenancy. The Commission affirmed the department's reallocation. The Circuit Court agreed with the Commission that both the rental expense and interest expense must be split between the joint tenants and could not be claimed exclusively by the taxpayer, and its decision affirmed the Commission in all respects.

After the issuance of the decision, the taxpayer filed a reconsideration letter with the Court concerning the allowability of the interest expense deduction. The taxpayer requested that he and his wife be allowed to recompile the tax returns in compliance with "generally accepted accounting principles" as they apply to interest and bad debts expense. The state opposed the addition of that language. The Circuit Court entered a judgment that included the language requested by the taxpayer.

The Appeals Court concluded that the Circuit Court's order represents a modification of the Commission's decision, and that the modification is not justified. The Appeals Court therefore ordered that that portion of the order that allows the taxpayer to recompile tax returns for the years in question be reversed, and that the remainder of the order that affirmed the Commission's decision be affirmed.

The taxpayer has not appealed this decision.

□

Assessments—failure to file. *Urban P. Van Susteren, vs. Wisconsin Department of Revenue* (Wisconsin Supreme Court, April 23, 1990). This is a review of a decision of the Court of Appeals, which reversed an order of the Circuit Court of Outagamie County. The order of the Circuit Court affirmed an order of the Wisconsin Tax Appeals Commission that upheld the penalty imposed by the department against the taxpayer under sec. 71.11(6)(b), Wis. Stats. (1983-84). See *Wisconsin Tax Bulletin* 59, page 8, for a summary of that decision.

The issues in this case are whether the provision under which the taxpayer was penalized, sec. 71.11(6)(b), Wis. Stats., applies to the case at hand, and if so, whether the taxpayer failed to file timely returns with intent to defeat the tax assessment for the years in question. There is no claim that the taxpayer is guilty of tax evasion.

The Wisconsin Supreme Court concluded that the penalty provision, sec. 71.11(6)(b), Wis. Stats. (1983-84), could be applied to untimely filers, but that it was improper to apply it in this case. The Court held that there is insufficient evidence in the record to sustain the Commission's finding that the taxpayer failed to file timely returns with the intent to defeat the tax assessments for the years in question.

The department has not appealed this decision.

□

FARMLAND PRESERVATION CREDIT

Farmland preservation credit—constitutionally. *Jack McManus, as Personal Representative of the Estate of Dorothy McManus vs. Wisconsin Department of Revenue* (Court of Appeals, District IV, March 29, 1990). This is an appeal from an order of the Circuit Court of Dane County, affirming a decision of the Wisconsin Tax Appeals Commission declaring constitutional the Farmland Preservation Credit statute, sec. 71.09(11), Wis. Stats. (1977-78). The issues in this case are whether sec. 71.09(11), Wis. Stats., is a tax provision; and if so, whether it violates the uniformity of taxation clause, article VIII, section 1 of the Wisconsin Constitution.

In 1978, Dorothy and Jack McManus owned 331.3 acres of farmland as joint tenants. That year the McManuses had $180,987 is household income. Dorothy's income was approximately $6,000. Dorothy applied for a farmland preservation credit based on her interest in the land. The department denied her claim because her household income exceeded $38,429, the maximum allowed under the statute. The Commission upheld the determination on the same ground. The Circuit Court affirmed the Commission's decision, and also declared that the statute was constitutional after rejecting due process, equal protection, and uniformity of taxation claims. On appeal, the estate maintains only its uniformity of taxation challenge to sec. 71.09(11), Wis. Stats., under article VIII, section 1 of the Wisconsin Constitution.

The Court of Appeals concluded that the farmland preservation credit law, sec. 71.09(11), Wis. Stats. (19877-78), is a relief statute, not a tax statute, and that it is therefore not subject to the uniformity requirement.

The taxpayer has not appealed this decision.

□

CORPORATION FRANCHISE OR INCOME TAXES

Manufacturer's sales tax credit—manufacturing defined. *Astra Plating, Inc. vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, March 14, 1990). This decision and order is the result of the Commission's reconsideration of the prior decision and order, as reported in *Wisconsin Tax Bulletin* 63, page 9. This decision supersedes the prior decision. The issue in the case is whether the taxpayer's automobile "bumper-recycling" operation constitutes manufacturing.

In the Commission's reconsideration of its previous decision in this case, it concluded that it reached the right result, even though the mode of analysis was wrong. It concluded that the taxpayer established the elements of manufacturing and held that the taxpayer is a manufacturer. It also concluded that in the taxpayer's operation, the materials processed by the taxpayer have no actual market value as bumpers, before processing, and consequently the taxpayer's operations cannot be deemed to be repairs.

The department has not appealed this decision.

❐

Allocation of income—separate accounting. *Nelson Brothers Furniture Corporation vs. Wisconsin Department of Revenue* (Court of Appeals, District IV, October 26, 1989). This is an appeal from a judgment affirming a decision of the Wisconsin Tax Appeals Commission, which upheld a determination of the Department of Revenue that Nelson Brothers, an Illinois corporation carrying on a portion of its business in Wisconsin, had underpaid Wisconsin franchise taxes in the years 1974 through 1978. The issues in this case are:

(A) The appropriate scope of the Court of Appeals' review of the Commission's decision where its inquiry was limited to whether the department abused its discretion in carrying out a specific statutory duty.

(B) Whether the department abused its discretion in directing a change in the taxpayer's accounting methods which led to increased Wisconsin franchise tax liability.

(C) Whether the change violated the taxpayer's right to due process of law.

The department cross-appeals from that portion of the judgment remanding the matter to the Commission with directions to consider the taxpayer's argument that, should the assessment stand, it is entitled to an "equitable recoupment" in the form of an adjustment to the apportionment formula.

The Department of Revenue, after an audit, determined that because Nelson Brothers' Wisconsin operations were an integral part of a "unitary" business, the separate accounting method failed to properly reflect taxable income for the years in question. The department recomputed the company's income using a different method — the "apportionment" or "formula" method — and ordered Nelson Brothers to use the apportionment method to calculate its Wisconsin income in the future.

Nelson Brothers also raised an "alternative" argument before the Commission, contending that, should the assessment be affirmed, the company should be allowed an "equitable recoupment" — an offset against the newly-assessed liability representing an adjustment to the "sales factor" of the apportionment equation to reflect intangible income. The net effect of the adjustment would be to lower the tax due. Because Nelson Brothers had not raised the recoupment issue before the department, but argued it for the first time in its brief to the Commission, the Commission held that it lacked jurisdiction to consider it.

The Court concluded that:

(A) The scope of its review is to look to the facts found by the Commission, and the evidentiary basis for such findings; and then to consider whether, on those facts, the department exercised its discretion in a reasonable, nonarbitrary manner. The Court owes no deference to the Commission's conclusions.

(B) The record satisfies the Court that the decision to require the change in Nelson Brothers' accounting methods was neither unconsidered nor irrational. It was a reasoned and reasonable decision and thus a proper exercise of discretion. Therefore, in light of the directions in sec. 71.07(2), Wis. Stats. (1985-86), the department reasonably and properly exercised its discretion to direct the change in Nelson Brothers' accounting practices.

(C) The fact that application of the apportionment formula results in an increase of Wisconsin-allocated income—according to the department, an average 13.68 percent increase over the five-year audit period — and thus an increase in the company's Wisconsin tax liability has been upheld over similar objections in *Container Corp. vs. Franchise Tax Bd.*, 463 U.S. 159, 170 (1983) and *Underwood Typewriter Co. vs. Chamberlain*, 254 U.S. 113 (1920). The Court was not persuaded that the increase in Nelson Brothers' tax liability renders the department's action unconstitutional.

In the matter of the department's cross-appeal, the court concluded that the statutory procedures for appealing department decisions do not specify the contents of the appeal documents, and nothing in the statutes suggests that the review must be strictly confined to the claims raised before the department. In addition, the Court was not convinced that Nelson Brothers' recoupment claim is a "grievance [ ] to the assessment," within the meaning of sec. Tax 3.91(1), Wis. Adm. Code. It is an equitable claim for an offset to the reassessment which is not barred from the Commission's consideration by the taxpayer's failure to argue it to the department.

The taxpayer and the department have not appealed this decision.

❐

Allocation of income—between affiliates. *Wisconsin Department of Revenue vs. Sentry Financial Services Corporation, and Sentry Financial Services Corporation vs. Wisconsin Department of Revenue* (Circuit Court of Portage County, February 20, 1990). This decision arises from petitions by both parties to review a decision of the Wisconsin Tax Appeals Commission. The petitions for review involve two issues:

(A) Whether the Commission's finding that a bargain sale occurred was supported by substantial evidence in the record.

(B) Whether the department abused its discretion when it reallocated income to Sentry Financial Services Corporation (SENCO) pursuant to sec. 71.11(7m), Wis. Stats. (1981-82).

This case arises out of a transaction between SENCO, a wholly owned subsidiary of the Sentry Corporation (SENCOR), and

SENCOR, which itself is a wholly owned subsidiary of Sentry Insurance, a Mutual Company (SIAMCO). In 1972, SENCO purchased an aircraft for $4,623,560.85, with the intention to lease it to SIAMCO. On September 1, 1973, SENCO as lessor, and SIAMCO as lessee, entered into a written lease for the aircraft. The lease term was for 10 years, including a period of use beginning January 1, 1973. The lease expired on December 31, 1982. During the term of the lease, SENCO included in its income a total amount of $6,355,560.85, pursuant to the lease. Records and testimony of SENCO employes indicated an intention to sell the aircraft to SIAMCO at the expiration of the lease, for 10% of its original purchase price. The right to purchase was not contained in the lease document.

On December 31, 1982, the lease ended. On that date, SENCO transferred the aircraft to SENCOR and received in return from SENCOR a payment of $453,560.85, or 10% of the original purchase price of the aircraft. The transfer was made to SENCOR, SIAMCO's subsidiary, rather than to SIAMCO itself due to a corporate decision to house all aircraft owned by the Sentry group of companies in SENCOR. The sale price was included in SENCO's income for 1982. SENCO paid sales tax on the sale. The sale of the aircraft by SENCO to SENCOR was not done pursuant to a plan of tax avoidance, and the department stipulated that it did not base its assessment on the grounds that an adjustment was necessary in order to prevent evasion of taxes within the meaning of sec. 71.11(7m), Wis. Stats. After the December 31 transfer, the aircraft continued in use by corporations within the Sentry group. For that use, SENCOR received fees and reimbursements. In June 1986, SENCOR sold the aircraft to an unrelated third-party for approximately $4,600,000.00.

The department assessed SENCO for additional income taxes for 1982, based upon the allocation of a taxable gain for the sale of the aircraft to SENCOR. The assessment was determined by adding the fair market value of the aircraft less its adjusted basis, to SENCO's taxable income. The Commission found that the sale of the aircraft by SENCO to SENCOR was a "bargain sale", and was not made pursuant to an arms length right to purchase under the lease. The Commission also held: 1) that the department failed to properly consider the substantive provision of secs. 71.301 and 71.311, Wis. Stats., which govern the tax consequences of a "subsidiary to parent" bargain sale, 2) that the sale of assets by a corporation to its shareholders for less than fair market value is treated as a distribution under IRC sec. 301 (sec. 71.301, Wis. Stats.), and 3) that therefore, by reallocating income under sec. 71.11(7m), Wis. Stats., despite the tax-free provisions of secs. 71.301 and 71.311, Wis. Stats., the department abused its discretion, applying the wrong legal standard to the facts.

The Circuit Court concluded that the Commission clearly had substantial evidence in the record to support its decision that the transfer of the aircraft from SENCO to SENCOR was a "bargain sale". The Court also concluded that the original plan to lease with the option to purchase and the resulting tax consequences to SENCO did not require a reallocation of income to correctly reflect its income upon a transfer of the aircraft between related companies, and thus declined to reverse the Commission's decision that the department abused its discretion in reallocating the income.

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

□

SALES/USE TAXES

Waste reduction and recycling. *Parks-Pioneer Corporation vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, March 23, 1990). The issue is whether the purchases and sales described below were exempt under sec. 77.54(26m), Wis. Stats., which exempts from sales and use tax the gross receipts from the sale of or use or other consumption of waste reduction or recycling machinery and equipment, including parts therefor, exclusively and directly used for waste reduction or recycling activities which reduce the amount of solid waste generated or recycle solid waste. The exemption applies even though an economically useful end product results from the use of the machinery and equipment.

During the period under review, the taxpayer was a corporation registered to operate a business in Wisconsin and engaged in recycling solid waste, including scrap metal. The taxpayer's business operation includes all functions which directly relate to the preparing, sorting, weighing, and processing scrap metal into prepared grades of metal so as to be used by industries such as smelting, foundries, and steel mills. These functions commenced with the initial collection of scrap metal and ended with sale and delivery of the prepared grades of metal to its customers.

The taxpayer purchased scrap metal from various suppliers. In most instances, the taxpayer picked up and transported to its place of business the scrap metal from various collection sites on the suppliers' premises. The suppliers would fill the taxpayer's lugger and roll-off boxes with scrap metal. When full, the taxpayer picked them up and left replacement boxes.

The following items were purchased for the taxpayer's operations without payment of sales/use tax:

(A) Lugger boxes and roll-off boxes used to collect and transport scrap metal to the premises and recycled metal to the taxpayer's customers.

(B) Tarps and bands used to cover the lugger boxes when scrap metal was in transit.

(C) Starting fluid used to start diesel engines in cold weather on cranes used in the recycling yard to move heavy pieces of scrap metal.

(D) Truck scales, including repairs and replacement parts, used to weigh the scrap metal on the taxpayer's premises.

(E) Platform scales used to weigh scrap metal to assist in pricing of recycled metal held for sale.

(F) A dead lift roll-off hoist mounted on one of the taxpayer's trucks and used at the collection points of scrap metal.

(G) Replacement hydraulic hose for trucks used to collect and transport scrap metal.

The lugger and roll-off boxes were equipment used by the taxpayer for the sole purpose of collecting and transporting of scrap metal to the taxpayer's place of business and delivering recycled metal to customers. Use in customer delivery did not exceed 10% of the time used. Tarps and bands were equipment used solely to cover the boxes to prevent material from falling out in transit. The scales in question were equipment used solely in weighing the unprepared and prepared scrap metal to determine purchase or sale price. Weight and grade of metal combined is the industry's method of pricing scrap metal. The dead lift roll-off hoist was mounted on a truck and used only to lift lugger and roll-off boxes on to and off trucks for movement and scales in order to weigh and price the scrap metal. The hydraulic hoses were used as replacement parts in the taxpayer's trucks used in metal transportation. Although appropriated on the taxpayer's books to trucks, the starting fluid in question was used in cold weather to start diesel engines on cranes used on the taxpayer's premises solely to move heavy pieces of scrap metal. The fluid is sprayed into the engine, clearing moisture and enabling starting.

The taxpayer sold a load lugger box in October 1984 to Johnson Metal of Racine. The taxpayer collected no sales tax, believing that the sale would be exempt under the recycling exemption in question. The use of the equipment by the purchaser, however, was not established. The taxpayer sold 3 self-dumping hoppers to A.E.F. Salvage, a small, one-man trucking operation. The testimony of the taxpayer's witness concerning possible resale by A.E.F. was somewhat contradictory and was insufficient to establish that or any other exemption to the sales tax requirement.

The Department of Revenue's assessment included sales or use tax on the items discussed previously.

The Commission concluded that items purchased by the taxpayer were "recycling machinery and equipment, including parts therefor, exclusively and directly used for ... or recycling activities which reduce the amount of solid waste generated [or] ... recycle solid waste," within the meaning of sec. 77.54(26m), Wis. Stats. The Commission also held that the burden of proving that a sale of tangible personal property is not a taxable sale at retail is upon the seller unless a certificate of resale or exemption described in sec. 77.52(14), Wis. Stats., is taken from the purchaser. The taxpayer's sales were not supported by a resale or exemption certificate produced by the purchasers and were not otherwise shown to be exempt from tax.

This decision has been appealed to the Circuit Court.

❑

When and where sale takes place. *Republic Airlines, Inc. vs Wisconsin Department of Revenue* (Circuit Court of Dane County, February 12, 1990). This is a petition for judicial review of a decision of the Wisconsin Tax Appeals Commission which affirmed the Wisconsin Department of Revenue's assessment against Republic Airlines, Inc. (Republic) for the sales and use tax in 1981-1984 on liquor and soda pop served to passengers during flights in Wisconsin's airspace. The decision also denied the department's assessment of a use tax on complimentary peanuts that Republic gave to passengers. See *Wisconsin Tax Bulletin* 61, page 11, for a review of this case.

Republic Airlines, Inc., now Northwest Airlines, Inc., was a Wisconsin corporation engaged in the business of interstate commercial air transportation in Wisconsin and elsewhere, with principal offices in Minneapolis, Minnesota. Republic maintained offices in Wisconsin, had equipment and personnel located at airports in Wisconsin, and flew regularly-scheduled flights into, between, and out of a number of Wisconsin cities. Some of Republic's flights used Wisconsin airspace but never touched down. The latter are referred to as "overflights".

Republic sold liquor on its flights and gave out complimentary soda pop, peanuts, and sometimes also liquor to its passengers. Republic did not keep records of the location of its aircraft during the above transactions, i.e., whether the aircraft was in Wisconsin airspace or in another state's airspace.

To apportion Wisconsin sales tax to Republic's gross receipts for liquor sales, and Wisconsin use tax to Republic's purchases of complimentary items, Republic applied a ratio of revenue passenger miles (RPMs) flown in Wisconsin (the numerator) to RPMs flown everywhere (the denominator). The ratio's numerator included flights which either departed from or landed in Wisconsin but did not include overflights. The department adjusted the numerator to include RPMs for overflights.

The taxpayer contended that:

(A) The Commission was erroneous in its findings that sales occurring over Wisconsin are sales "in this state" as that phrase is used in sec. 77.52(1), Wis. Stats., and that the use or consumption of complimentary soda pop, peanuts, and liquor used or consumed on overflights are used and consumed "in this state" as that phrase is used in sec. 77.53(1), Wis. Stats. The taxpayer contended that the language "in this state" in secs. 77.52(1) and 77.53(1) does not mean "over this state".

(B) The application of Wisconsin's sales and use tax to overflights violates the Commerce Clause and Due Process Clause of the United States Constitution.

(C) The taxes at issue lack internal consistency because of the potential for cumulative burdens posed by multiple taxation.

(D) The final prong of *Complete Auto* is not satisfied because the taxation of overflights is not fairly related to benefits provided by the state.

Regarding the department's use tax assessment on complimentary peanuts and other snacks served by Republic, the Commission found that these items are exempt from use tax under sec. 77.54(20), Wis. Stats. The department argued that the Commission was without jurisdiction to raise sec. 77.54(20), Wis. Stats., because Republic did not affirmatively assert the exemption as a defense.

The Circuit Court concluded that:

(A) The phrase "in this state" in those sections is unambiguous, and that it does mean "over this state."

(B) The mere fact that the taxpayer's airplanes fly over Wisconsin does not suffice to meet the substantial nexus test, but that the substantial nexus test is satisfied by the fact that the taxpayer maintains offices, equipment, and personnel in Wisconsin and is incorporated in Wisconsin.

(C) The mere possibility of multiple taxation is insufficient to invalidate the tax.

(D) The United States Supreme Court has held that the "fairly related" prong is satisfied literally by the state providing "the advantages of a civilized society." *Exxon Corp. vs. Wisconsin Department of Revenue*, 447 U.S. 207, 228 (1980). Wisconsin has indeed provided Republic with such advantages, for example, the protection of Wisconsin's laws, opportunities for further commerce, the availability of fire and other emergency services, and ground preparation for emergency landings.

Pursuant to sec. 227.57(9), Wis. Stats., the Court also concluded that the complimentary snacks and peanuts provided by Republic are exempt from Wisconsin use tax under sec. 77.54(20), Wis. Stats.

The taxpayer and the department have appealed this decision to the Court of Appeals.

❑

Boats, vessels and barges—storage outside Wisconsin. *Leonard W. Vanasse vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, February 19, 1990). The issue in this case is whether the Department of Revenue correctly assessed a use tax against the taxpayer on the purchase of the boat in question, pursuant to sec. 77.53, Wis. Stats.

The taxpayer, a resident of Hudson, Wisconsin, entered into a purchase agreement regarding a 44 foot Trojan boat from a Minnesota resident. The closing on the sale occurred in August 1981, and the boat was delivered by a marina service to the taxpayer at a marina near Hudson, Wisconsin. No sales tax was paid to the state of Minnesota. On the first trip out with the boat, about 75 feet from the dock, the prop and other component parts were damaged by rocks. This necessitated towing the boat to the Hudson marina. The boat remained there for a few weeks while arrangements were made to take it to Stillwater, Minnesota for repairs. It was moved to Stillwater and remained there for the winter. The next season, in 1982, the boat was kept at dock in Stillwater, taken out once, and the taxpayer decided to sell the boat. Harris Yacht Sales of Prescott, Wisconsin handled the sale in July 1982. The boat, because of its type, was documented with the Coast Guard and not registered by the State of Wisconsin.

The Commission concluded that the taxpayer, a Wisconsin resident, did purchase the boat for use in Wisconsin, and that since the taxpayer did not pay a use tax on the boat, the department correctly assessed a use tax under Wisconsin Statutes.

The taxpayer has not appealed this decision.

❑

TAX RELEASES

("Tax Releases" are designed to provide answers to the specific tax questions covered, based on the facts indicated. In situations where the facts vary from those given herein, the answers may not apply. 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

Individual and Fiduciary Income Taxes

Corporation Franchise or Income Taxes

Farmland Tax Relief Credit

Sales/Use Taxes

County Sales/Use Taxes

INDIVIDUAL INCOME TAXES

1. A Shareholder's Share of a Tax-Option (S) Corporation's Farm Income for Estimated Tax Purposes

Statutes: Sections 71.09(1), (3), and (4) and 71.36(1) and (1m), Wis. Stats. (1987-88).

Note: This tax release applies with respect to items passed through from a tax-option (S) corporation beginning with its 1987 taxable year and to the shareholder's 1987 or 1988 taxable year as appropriate to conform the shareholder's treatment of tax-option items to the corporation's treatment.

Background: Generally, individuals deriving income subject to Wisconsin income tax, other than wages upon which taxes are withheld by the employer, must pay estimated taxes. Sec. 71.09, Wis. Stats. (1987-88). Individuals, other than farmers or fishers, who file returns on a calendar-year basis must pay estimated tax in 4 installments due April 15, June 15, and September 15 of the taxable year and January 15 of the following taxable year. A special rule applies to farmers and fishers.

Individuals who are farmers or fishers may either make only one installment payment due by January 15 or file a return and pay the tax due by March 1 of the following taxable year. Individuals are farmers or fishers if their gross income from farming or fishing for the taxable year is at least two-thirds of the total gross income from all sources shown on the income tax return for that year. Sec. 71.09(1)(a), (3), and (4), Wis. Stats. (1987-88).

Facts and Question: Taxpayer X, a Wisconsin resident individual who files income tax returns on a calendar-year basis, is a shareholder of Corporation S, a tax-option (S) corporation. All of Corporation S's gross income is from farming.

Is Taxpayer X's pro rata share of Corporation S's gross income from farming treated as gross income from farming for Wisconsin estimated tax purposes?

Answer: Yes. Taxpayer X's pro rata share of Corporation S's gross income from farming is treated as gross income from farming for Wisconsin estimated tax purposes. Shareholders of a tax-option (S) corporation must include in their Wisconsin adjusted gross income their pro rata share of the corporation's items of income, loss, and deduction. Sec. 71.36(1), Wis. Stats. (1987-88). Tax-option items included in a tax-option (S) corporation shareholder's income retain the character they would have if attributed to the corporation. Sec. 71.36(1m), Wis. Stats. (1987-88). Thus, tax-option items are included on the shareholder's return as if received or accrued, or paid or incurred, directly by the shareholder. Accordingly, Taxpayer X's pro rata share of the farm income from Corporation S is treated as gross income from farming.

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2. Amortization of Bond Premium on State and Local Bonds

Statutes: Section 71.05(6)(a)1, Wis. Stats. (1987-88).

Facts and Question: An individual who is a full-year Wisconsin resident earns interest income from state or local bonds that had been purchased at a premium. The interest income is exempt from federal income tax under sec. 103 of the Internal Revenue Code (IRC). However, such interest is subject to Wisconsin income tax pursuant to sec. 71.05(6)(a)1, Wis. Stats. (1987-88), which requires the addition to federal adjusted gross income of any amount of interest, less related expenses, which is not included in federal adjusted gross income.

For federal purposes, IRC sec. 171(a)(2) prohibits the deduction of the amortizable bond premium on federally tax-exempt state and local bonds. However, IRC sec. 1016(a)(6) requires the basis of such a tax-exempt state or local bond to be reduced each year by the amortizable bond premium which is disallowed as a deduction. Therefore, if a tax-exempt state or local bond is purchased at a premium and held to maturity, the holder will not recognize any loss on the redemption of the bond for federal purposes.

What is the proper treatment of the bond premium on state and local bonds for Wisconsin income tax purposes?

Answer: The state and local bond premium should be amortized as provided in IRC sec. 171 and deducted from the interest income which must be added to federal adjusted gross income to arrive at Wisconsin adjusted gross income. The payment of bond premium is a cost of acquiring bonds that yield more than the going rate of interest. The amortization of bond premium is an expense directly related to the interest received on state and local bonds. Therefore, the addition modification for state and local bond interest is equal to the interest income earned reduced by the amortizable bond premium which is not deductible federally.

Although federal law permits individuals to elect whether or not to amortize premiums on federally taxable bonds, such an election is not provided under Wisconsin law with respect to bonds which are federally tax-exempt but taxable for Wisconsin purposes. Thus, an individual may not elect to deduct the bond premium as an adjustment to the federal gain or loss upon disposition of the bonds rather than amortizing the premium. Additionally, sec. 71.07(5)(a), Wis. Stats. (1987-88), does not permit an individual to use the bond premium on federally tax-exempt bonds in the computation of the Wisconsin itemized deduction credit.

The treatment of bond premium described above also applies to state and local bond interest income passed through to individuals from pass-through entities, including partnerships, tax-option (S) corporations, and trusts. Therefore, the pass-through entity should advise the partner, shareholder, or beneficiary, as appropriate, of the total amount of state and local interest income and the reduction required for any related bond premium.

Example: An individual purchased at a premium a federally tax-exempt state bond which pays $600 of interest annually. The individual computed an amortizable bond premium of $80 for 1989. Thus, the amount of interest income that the individual must report as an addition modification on his or her 1989 Wisconsin income tax return is $520 ($600 interest minus $80 amortizable bond premium).

❒

3. Credit for Taxes Paid to Other States on Tax-Option (S) Corporation and Partnership Income

Statutes: Section 71.07(7)(b), Wis. Stats. (1987-88), formerly section 71.09(8)(c), Wis. Stats. (1985-86).

Background: Section 71.07(7)(b), Wis. Stats. (1987-88), formerly numbered sec. 71.09(8)(c), provides that a Wisconsin resident who pays a net income tax to another state may claim a credit against tax otherwise payable to Wisconsin on income of the same year. The credit is allowed only if the income taxed by the other state is considered income for Wisconsin. In addition, the tax paid is deemed a net income tax paid to another state only in the year in which the income tax return for the other state was required to be filed.

If only part of the income taxed by the other state is considered taxable income for Wisconsin purposes, the allowable credit for taxes paid to other states is computed using the following formula:

$$\frac{\text{Income taxable by both states}}{\text{Income taxable by other state}} \times \text{Other state tax paid} = \text{Credit}$$

Facts and Question 1: Taxpayer A, a full-year Wisconsin resident, was a shareholder of ABC Corporation, a unitary, multistate corporation which elected to be treated as a tax-option (S) corporation for federal and state purposes. In 1985, ABC Corporation changed its method of accounting. ABC Corporation was required to make an adjustment of $3,000,000 in order to prevent amounts from being duplicated or omitted as a result of the change in method of accounting.

For federal purposes, ABC Corporation subtracted $500,000 of this $3,000,000 adjustment from its net income each year for the next 6 years beginning in 1985, as provided in sec. 481 of the Internal Revenue Code (IRC).

For states other than Wisconsin, ABC Corporation computed its income under the Internal Revenue Code and spread the $3,000,000 adjustment over 6 years, as it did for federal purposes.

For Wisconsin purposes, ABC Corporation was required to subtract the entire $3,000,000 adjustment from net income in the year of change pursuant to sec. 71.11(8)(b), Wis. Stats. (1985-86).

As a result of the difference in treatment of the $3,000,000 adjustment, ABC Corporation realized net income for both federal and other state tax purposes but realized a net loss for Wisconsin for 1985. Taxpayer A's pro rata share of ABC Corporation's 1985 federal ordinary income was $610,000. His share of ABC Corporation's ordinary income that was taxable in states other than Wisconsin was $200,000, and he paid $20,000 of income taxes to other states on that income. His share of the total company net loss as computed under Wisconsin law was $15,000. Since Taxpayer A was a full-year Wisconsin resident, he was required to include in the computation of his Wisconsin adjusted gross income his pro rata share of ABC Corporation's entire net income or net loss as computed under Wisconsin law, regardless of where it was earned or incurred.

In 1985, Taxpayer A received a $175,000 salary from ABC Corporation for services performed in Wisconsin. The salary was taxable for federal and Wisconsin purposes but was not taxable by any other state. In addition, Taxpayer A received a $125,000 distribution from ABC Corporation. The distribution was not taxable for federal and other state purposes but was a taxable dividend for Wisconsin. Taxpayer A computed his adjusted gross income as follows:

	Federal	Wisconsin	Other States
Wages from ABC Corporation	$175,000	$175,000	$ 0
Dividends from ABC Corporation	0	125,000	0
ABC Corporation income (loss)	610,000	(15,000)	200,000
Adjusted gross income	$785,000	$285,000	$200,000

May Taxpayer A claim a credit on his Wisconsin income tax return for the $20,000 of income taxes that he paid to other states?

Answer 1: No. Taxpayer A may not claim a credit on his Wisconsin income tax return for any part of the $20,000 of income taxes he paid to other states. Section 71.09(8)(c), Wis. Stats. (1985-86), prohibits an individual from receiving a credit in excess of the tax due on the same income for that taxable year. Since ABC Corporation computed a total company net loss for 1985 under Wisconsin law, Taxpayer A did not pay any tax to Wisconsin on income that was taxable by other states.

Note: As a result of the federalization of Wisconsin's corporation and tax-option (S) corporation laws, IRC sec. 481 applies for Wisconsin purposes for the 1987 taxable year and thereafter.

Facts and Question 2: Taxpayer B, a full-year Wisconsin resident, was a general partner in XYZ Partnership, which had nonunitary operations in Wisconsin and Ohio. Since the Wisconsin and Ohio operations were nonunitary, the partnership determined its 1989 income or loss from Wisconsin operations and Ohio operations by means of separate accounting. The partnership had the following income (loss):

	Wisconsin Operations	Ohio Operations	Total Operations
Ordinary income (loss)	$(1,500)	$ 500	$(1,000)
Capital gain	1,000	5,000	6,000

Taxpayer B reported to Ohio ordinary income of $500 and capital gain income of $5,000 and paid $500 of income tax. Since Taxpayer B was a full-year Wisconsin resident, she was required to report on her Wisconsin income tax return her distributive share of XYZ Partnership's entire income or loss, regardless of where it was earned or incurred. On her Wisconsin income tax return, Taxpayer B reported an ordinary loss of $1,000 and capital gain income of $2,400 (40% of $6,000).

What amount of credit may Taxpayer B claim on her Wisconsin income tax return for taxes paid to other states?

Answer 2: Taxpayer B may claim a credit of $227 for income taxes paid to other states. This credit is computed as follows:

$$\frac{\$500 \text{ ordinary income } + \ \$2{,}000 \text{ capital gain}}{\$500 \text{ ordinary income } + \ \$5{,}000 \text{ capital gain}} \times \$500 = \$227$$

The $500 of partnership ordinary income is considered taxable by both states, and included in the numerator of the formula, because the ordinary income or loss from both Wisconsin and Ohio operations is included in Wisconsin adjusted gross income. Since $5,000 of the capital gain income passed through from the partnership was taxed by Ohio, and only 40% of the $5,000 of capital gain income taxed by Ohio is taxable by Wisconsin, $2,000 of capital gain income is included in the numerator of the formula. The denominator consists of the $500 of ordinary income and $5,000 of capital gain that was taxable by Ohio. This fraction establishes the percentage of the total tax of $500 paid to Ohio that is a credit against Wisconsin income tax.

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4. Disability Income Exclusion

Statutes: Section 71.05(6)(b)4, Wis. Stats. (1987-88).

Background: Section 71.05(6)(b)4, Wis. Stats. (1987-88) provides that certain disability payments may be subtracted from federal adjusted gross income when computing Wisconsin taxable income. The disability payments may be subtracted to the extent those payments are excludable under sec. 105(d) of the Internal Revenue Code (IRC) as it existed immediately prior to its repeal in 1983.

Under IRC sec. 105(d) an individual who qualifies for the disability income exclusion may claim the exclusion until the earliest of (a) the first day of the tax year in which he or she turns 65 years of age, (b) the first day of the tax year for which he or she chooses to treat the disability income as a pension, or (c) the day he or she reaches the age when the employer's retirement program would have required retirement (mandatory retirement age).

As a result of the repeal of IRC sec. 105(d), there no longer is a federal election to report disability income as either wages or as a pension. Disability income is reported on the federal income tax return as wages until the individual reaches minimum retirement age. Once the individual reaches minimum retirement age, disability income is reported as a pension.

Question: A taxpayer is totally and permanently disabled. For several years, the taxpayer has reported disability income as wages on his or her federal income tax return and qualified to claim the Wisconsin disability income exclusion. The employer's retirement program requires an employe to retire at age 64 and has a minimum retirement age of 62. The taxpayer became age 62 on January 1, 1989. For federal tax purposes, because the taxpayer has reached minimum retirement age, he or she must now report the disability income as a pension.

Since the taxpayer has not reached age 65 or mandatory retirement age under the employer's plan, can he or she claim the Wisconsin disability income exclusion on the 1989 Wisconsin return, even though the disability income is now reported as a pension on the federal return?

Answer: Yes, the taxpayer can claim the Wisconsin disability income exclusion for 1989 to the extent the payment is excludable under IRC sec. 105(d). The disability income exclusion is available for Wisconsin until the earliest of (a) the first day of the tax year in which a taxpayer turns 65 years of age, or (b) the day he or she reaches the age when the employer's retirement program would have required retirement (mandatory retirement age). The fact that the disability income is reported as a pension on the federal return has no affect on whether or not the exclusion may be claimed for Wisconsin.

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5. Exclusion of Capital Gains on Small Business Stock

Statutes: Sections 71.01(10) and 71.05(6)(b)6, Wis. Stats. (1987-88).

Note: This tax release supersedes the tax release titled "Small Business Stock" which appeared in *Wisconsin Tax Bulletin* 65, page 21.

Background: Under sec. 71.05(6)(b)6, Wis. Stats. (1987-88), capital gains from "small business stock" may be subtracted from federal adjusted gross income when computing Wisconsin taxable income. The small business stock capital gains exclusion may be claimed only by a taxpayer who is an individual or a fiduciary. The exclusion is available if the taxpayer did not acquire the stock by gift, and the taxpayer submits with the Wisconsin income tax return a copy of a certification from the corporation issuing the stock. Section 71.01(10), Wis. Stats. (1987-88), defines "small business stock" and lists the items which must be included on the certification.

Under sec. 71.01(10), Wis. Stats. (1987-88), small business stock means an equitable security which the taxpayer has held for at least five years and which is issued by a corporation that meets certain requirements as of specific dates and so certifies to the taxpayer. The requirements and applicable dates are specified in sec. 71.01(10).

The small business stock capital gains exclusion is a result of 1985 Wisconsin Act 29, which created secs. 71.02(2)(fr) and 71.05(1)(b)12, Wis. Stats., effective with stock issued to a taxpayer on or after January 1, 1986. Sections 71.02(2)(fr) and 71.05(1)(b)12 were subsequently renumbered secs. 71.01(10) and 71.05(6)(b)6, Wis. Stats. (1987-88), respectively, effective January 1, 1989.

<u>Question 1</u>: What are the small business stock requirements under sec. 71.01(10), Wis. Stats. (1987-88), and what are the applicable dates on which those requirements must be met?

<u>Answer 1</u>: The answer depends on when the stock is issued to the taxpayer. The requirements and applicable dates for meeting the requirements were amended by 1987 Wisconsin Act 27, effective with stock issued on or after August 31, 1987. The requirements were again amended by 1987 Wisconsin Act 399, effective with stock issued in the corporation's taxable year 1988 and thereafter. The requirements and applicable dates for meeting them for the various dates of acquisition are as follows:

A. For stock issued from January 1, 1986 to August 30, 1987, the small business stock requirements and the applicable dates for meeting those requirements are as follows:

   1. At least 50% of the corporation's property and at least 50% of its payroll were in Wisconsin on the December 31 before issuance of the stock.

   2. The corporation had no more than 200 employes covered by Wisconsin unemployment insurance, including employes of any corporation that owned more than 50% of the issuing corporation's stock, on the December 31 before issuance of the stock.

   3. The corporation derived no more than 25% of its gross receipts from rents, interest, dividends, and sales of assets combined in the calendar year prior to issuance of the stock.

   4. The corporation had no stock listed on the New York Stock Exchange, the American Stock Exchange, or the National Association of Securities Dealers' Automated Quotation system on the December 31 before issuance of the stock.

   5. The corporation had not conducted a trade or business in corporate or noncorporate form, or a combination thereof, for a period of more than five years prior to the December 31 before issuance of the stock.

   6. The corporation had never liquidated its assets in whole or in part for tax purposes only in order to fulfill requirements 1 to 5 above and then reorganized, as of the December 31 before issuance of the stock.

B. For stock issued on August 31, 1987 or thereafter by a corporation incorporated prior to the calendar year in which the stock is issued, the small business stock requirements and the applicable dates for meeting those requirements are as follows:

   1. At least 50% of the corporation's property and at least 50% of its payroll were in Wisconsin on the December 31 before issuance of the stock.

   2. The corporation had no more than 500* employes covered by Wisconsin unemployment insurance, including employes of any corporation that owned more than 50% of the issuing corporation's stock, on the December 31 before issuance of the stock.

      *<u>Note</u>: For stock issued from August 31, 1987 to the end of the corporation's taxable year 1987, the number of employes is 200 rather than 500.

   3. The corporation derived no more than 25% of its gross receipts from rent, interest, dividends, and sales of intangible investment assets combined in the calendar year prior to issuance of the stock. However, if the corporation had been incorporated for two calendar years or less as of the date the stock is issued and derived less than $3,000 of that type of income during that time, the 25% gross receipts limitation does not apply.

      <u>Example 1</u>: XYZ Corporation, incorporated prior to January 1, 1988, issues stock to a taxpayer on June 30, 1988. The 25% gross receipts limitation applies to XYZ's gross receipts for calendar year 1987. However, if XYZ was incorporated on or after June 30, 1986 (two years or less prior to the issuance of the stock), the 25% gross receipts limitation does not apply if XYZ derived less than $3,000 of gross receipts from rents, interest, dividends, and sales of intangible investment assets combined from the date of incorporation to June 30, 1988.

   4. The corporation had no stock listed on the New York Stock Exchange, the American Stock Exchange, or the National Association of Securities Dealers' Automated Quotation system on the December 31 before issuance of the stock.

   5. The corporation had never liquidated its assets in whole or in part for tax purposes only in order to fulfill requirements 1 to 4 above and then reorganized, as of the December 31 before issuance of the stock.

C. For stock issued on August 31, 1987 or thereafter by a corporation incorporated during the calendar year in which the stock is issued, the small business stock requirements and the applicable dates for meeting those requirements are as follows:

1. At least 50% of the corporation's property and at least 50% of its payroll were in Wisconsin on the date the stock was issued.

2. The corporation had no more than 500* employes covered by Wisconsin unemployment insurance, including employes of any corporation that owned more than 50% of the issuing corporation's stock, on the date the stock was issued.

   *Note: For stock issued from August 31, 1987 to the end of the corporation's taxable year 1987, the number of employes is 200 rather than 500.

3. The corporation derived no more than 25% of its gross receipts from rent, interest, dividends, and sales of intangible investment assets combined from the date of incorporation to the date the stock was issued. However, if the corporation derived less than $3,000 of that type of income during that time, the 25% gross receipts limitation does not apply.

   Example 2: RST Corporation, incorporated in 1988, issues stock to a taxpayer on June 30, 1988. The 25% gross receipts limitation applies to RST's gross receipts from the date of incorporation to June 30, 1988. However, if RST's gross receipts from rents, interest, dividends, and sales of intangible investment assets combined were less than $3,000 for that time period, the 25% gross receipts limitation does not apply.

4. The corporation had no stock listed on the New York Stock Exchange, the American Stock Exchange, or the National Association of Securities Dealers' Automated Quotation system on the date the stock was issued.

5. The corporation had never liquidated its assets in whole or in part for tax purposes only in order to fulfill requirements 1 to 4 above and then reorganized, as of the date the stock was issued.

Question 2: With respect to stock issued from January 1, 1986 to August 30, 1987 (Part A of answer 1), how do the requirements apply for a corporation that was not yet incorporated as of the December 31 before issuance of the stock?

Answer 2: Requirements 1, 2, 3, 4, and 6 in Part A of answer 1 would automatically be met as of the December 31 before the stock issuance. Only failure to fulfill requirement 5 would preclude stock issued by such a corporation from qualifying as "small business stock."

Question 3: To which year's tax return must the certification be attached by the taxpayer?

Answer 3: The certification must be attached to the tax return on which the capital gains exclusion is claimed. Do not submit the certification with the tax return for the year in which the stock is acquired.

Question 4: To qualify for the capital gains exclusion in sec. 71.05(6)(b)6, Wis. Stats. (1987-88), must the certification required under sec. 71.01(10), Wis. Stats. (1987-88), be given by the issuing corporation to the taxpayer at the time of issuance of the stock?

Answer 4: No. However, since the taxpayer must include the certification with the income tax return, the certification must be given to the taxpayer prior to the time the taxpayer must include it with the tax return. The Department of Revenue prefers that it be given as soon as reasonably possible after the stock is issued.

Question 5: Is there a form on which the issuing corporation may make the required certification?

Answer 5: No, there is no prescribed form. However, for a guideline of what information to include on a certification, refer to the three samples at the end of this tax release. The three samples reflect the requirements and applicable dates for meeting them, as described in answer 1.

The issuing corporation must provide a separate certification for each separate block of stock issued.

Question 6: If a corporation meets the small business stock requirements as of the December 31 before the stock is issued (or as of the date of issuance, for stock issued by a new corporation after August 30, 1987) and the corporation so certifies, would the capital gains exclusion continue to apply if the corporation subsequently fails to meet all of the requirements?

Answer 6: Yes. If the corporation meets the requirements as of the applicable dates and so certifies, the fact that one or more of the requirements are subsequently not met does not alter the character of the stock as small business stock.

Question 7: Does the capital gains exclusion apply only to the original holder of the stock shares?

Answer 7: Yes. The capital gains exclusion applies only to the person who initially acquired the stock from the corporation. The stock must be issued directly by the corporation to the person claiming the capital gains exclusion. It cannot be acquired from a secondary source, such as through a purchase from a shareholder of a corporation rather than from the corporation itself.

The taxpayer's stock acquisition from the corporation may be by purchase or it may be by some other means, such as a stock dividend or a stock split; however, the acquisition may not be by gift.

Question 8: How does the capital gains exclusion for small business stock apply with respect to a merger of two or more corporations?

Answer 8: The answer depends on whether the merger is into a new corporation or into a surviving corporation, and which stock shares are reissued, illustrated as follows:

A. When two or more corporations merge into a new corporation which issues all replacement stock shares, all of the shares issued pursuant to the merger are considered small business stock if the new corporation meets the requirements at the time it issues the replacement stock and so certifies, and the taxpayer holds the replacement stock for at least five years. Since the acquisition is not by gift, the capital gains exclusion applies, provided the taxpayer submits the certification with the tax return on which the capital gains are reported.

   Example 3: Corporations A and B merge into new Corporation C on November 1, 1987. On that date, C issues replacement stock shares to the shareholders of the previous A and B stock. C meets the small business stock requirements as of November 1, 1987 and so certifies to each shareholder.

   Since the replacement stock was not acquired by gift, the capital gains exclusion applies to each taxpayer who holds the stock until at least November 1, 1992, and who submits the certification with the tax return on which the capital gain is reported.

B. When two or more corporations merge into a surviving corporation which reissues all stock shares, the replacement stock is considered small business stock if the surviving corporation meets the requirements as of the December 31 before the stock is reissued (assuming the surviving corporation was originally incorporated in a year prior to reissuance of the stock), the surviving corporation so certifies, and the taxpayer holds the replacement stock for at least five years. Since the replacement stock is not a gift, the capital gains exclusion applies, provided the taxpayer submits the certification with the tax return on which the capital gains are reported.

   Example 4: Corporations A and B, both incorporated in 1986, merge into Corporation B on November 1, 1987. On that date, B issues replacement stock shares to all of the shareholders of the previous A and B stock. B meets the small business stock requirements as of December 31, 1986 and so certifies to each shareholder.

   The solution is the same as in example 3.

C. When two or more corporations merge into a surviving corporation which reissues stock shares to replace those of the liquidated corporation but does not reissue those shares of stock previously issued by that surviving corporation, the small business requirements and five year holding period with respect to the shares which are not reissued go back to the original applicable date. The capital gains exclusion for those shares applies as if no merger had occurred.

   Example 5: Corporations A and B merge into Corporation B on November 1, 1987. On that date, B issues shares of stock to previous A shareholders to replace their A shares but does not reissue stock to B shareholders. Taxpayer Q had purchased stock from B on August 1, 1986, which qualified as small business stock and received a certification from B. Q sells the stock at a gain on September 1, 1991, and attaches the certification to the 1991 income tax return.

   The capital gains exclusion applies, since the stock was held for more than five years (August 1, 1986 to September 1, 1991.) This is true even though Q held the stock for less than five years after the merger (November 1, 1987 to September 1, 1991).

   Example 6: In example 5, assume Q had purchased stock from both A and B on August 1, 1986, and received certifications from both corporations. Q then sells all of the stock on September 1, 1991, consisting of both August 1, 1986, original B stock and November 1, 1987, replacement stock.

   The capital gains exclusion applies with respect to the August 1, 1986, stock as in example 5. However, the capital gains exclusion does not apply with respect to the replacement stock, because the five year holding period had not been met for those shares (those shares were held only from November 1, 1987 to September 1, 1991).

"A" SAMPLE CERTIFICATION OF SMALL BUSINESS STOCK REQUIREMENTS

(ABC Corporation Letterhead)

July 3, 1986

Mr. John Doe
123 Main Street
Anytown, WI 53000

NOTE: This sample certification is for stock issued from January 1, 1986, to August 30, 1987. Refer to Part A of answer 1 for a description of the requirements.

Dear Mr. Doe:

On July 1, 1986 you acquired 100 shares of stock of ABC Corporation for $5,000. You are the original owner of this stock, and you did not acquire it by gift.

For purposes of meeting the small business stock certification requirement under sec. 71.01(10), Wis. Stats., I, the undersigned officer of ABC Corporation, hereby certify that ABC Corporation fulfills all of the following requirements:

1. At least 50% of ABC Corporation's property and at least 50% of its payroll were in Wisconsin on December 31, 1985.

2. ABC Corporation had no more than 200 employes covered by Wisconsin unemployment insurance, including employes of any corporation that owned more than 50% of ABC Corporation's stock, on December 31, 1985.

3. ABC Corporation derived no more than 25% of its gross receipts from rents, interest, dividends, and sales of assets combined in calendar year 1985.

4. ABC Corporation had no stock listed on the New York Stock Exchange, the American Stock Exchange, or the National Association of Securities Dealers' Automated Quotation system on December 31, 1985.

5. ABC Corporation had not conducted a trade or business in corporate or noncorporate form, or a combination thereof, prior to December 31, 1980.

6. ABC Corporation had never liquidated its assets in whole or in part for tax purposes only in order to fulfill requirements 1 to 5 above and then reorganized, as of December 31, 1985.

To qualify for the small business stock capital gains exclusion under sec. 71.05(6)(b)6, Wis. Stats., you must attach a copy of this certification to your Wisconsin income tax return on which the exclusion is claimed. Please save this certification for that purpose. The certification is not transferable. You, as the original owner of this stock, are the only taxpayer who may use the certification or qualify for the exclusion.

Signed ____________________________
Iona Business
President, ABC Corporation

"B" SAMPLE CERTIFICATION OF SMALL BUSINESS STOCK REQUIREMENTS

(ABC Corporation Letterhead)

July 3, 1990

Mr. John Doe
123 Main Street
Anytown, WI 53000

NOTE: This sample certification is for stock issued on or after August 31, 1987, by a corporation incorporated prior to the calendar year in which the stock is issued. Refer to Part B of answer 1 for a description of the requirements.

Dear Mr. Doe:

On July 1, 1990 you acquired 100 shares of stock of ABC Corporation for $5,000. You are the original owner of this stock, and you did not acquire it by gift.

For purposes of meeting the small business stock certification requirement under sec. 71.01(10), Wis. Stats., I, the undersigned officer of ABC Corporation, hereby certify that ABC Corporation fulfills all of the following requirements:

1. At least 50% of ABC Corporation's property and at least 50% of its payroll were in Wisconsin on December 31, 1989.

2. ABC Corporation had no more than 500 employes covered by Wisconsin unemployment insurance, including employes of any corporation that owned more than 50% of ABC Corporation's stock, on December 31, 1989.

3. ABC Corporation derived no more than 25% of its gross receipts from rents, interest, dividends, and sales of intangible investment assets combined in calendar year 1989.

4. ABC Corporation had no stock listed on the New York Stock Exchange, the American Stock Exchange, or the National Association of Securities Dealers' Automated Quotation system on December 31, 1989.

5. ABC Corporation had never liquidated its assets in whole or in part for tax purposes only in order to fulfill requirements 1 to 4 above and then reorganized, as of December 31, 1989.

To qualify for the small business stock capital gains exclusion under sec. 71.05(6)(b)6, Wis. Stats., you must attach a copy of this certification to your Wisconsin income tax return on which the exclusion is claimed. Please save this certification for that purpose. The certification is not transferable. You, as the original owner of this stock, are the only taxpayer who may use the certification or qualify for the exclusion.

Signed ___________________________
Iona Business
President, ABC Corporation

"C" SAMPLE CERTIFICATION OF SMALL BUSINESS STOCK REQUIREMENTS

(ABC Corporation Letterhead)

July 3, 1990

Mr. John Doe
123 Main Street
Anytown, WI 53000

NOTE: This sample certification is for stock issued on or after August 31, 1987, by a corporation incorporated during the calendar year in which the stock is issued. Refer to Part C of answer 1 for a description of the requirements.

Dear Mr. Doe:

On July 1, 1990 you acquired 100 shares of stock of ABC Corporation for $5,000. You are the original owner of this stock, and you did not acquire it by gift.

For purposes of meeting the small business stock certification requirement under sec. 71.01(10), Wis. Stats., I, the undersigned officer of ABC Corporation, hereby certify that ABC Corporation fulfills all of the following requirements:

1. At least 50% of ABC Corporation's property and at least 50% of its payroll were in Wisconsin on July 1, 1990.

2. ABC Corporation had no more than 500 employes covered by Wisconsin unemployment insurance, including employes of any corporation that owned more than 50% of ABC Corporation's stock, on July 1, 1990.

3. ABC Corporation derived no more than 25% of its gross receipts from rents, interest, dividends, and sales of intangible investment assets combined from the date of incorporation to July 1, 1990.

4. ABC Corporation had no stock listed on the New York Stock Exchange, the American Stock Exchange, or the National Association of Securities Dealers' Automated Quotation system on July 1, 1990.

5. ABC Corporation had never liquidated its assets in whole or in part for tax purposes only in order to fulfill requirements 1 to 4 above and then reorganized, as of July 1, 1990.

To qualify for the small business stock capital gains exclusion under sec. 71.05(6)(b)6, Wis. Stats., you must attach a copy of this certification to your Wisconsin income tax return on which the exclusion is claimed. Please save this certification for that purpose. The certification is not transferable. You, as the original owner of this stock, are the only taxpayer who may use the certification or qualify for the exclusion.

Signed ____________________________
Iona Business
President, ABC Corporation

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

Statutes: Section 71.04(1), Wis. Stats. (1987-88).

Note: This tax release supersedes the tax release with the same title that was published in *Wisconsin Tax Bulletin* 48 (October 1986). This tax release applies for all periods open to adjustment.

Facts and Question 1: Taxpayer X, an Illinois resident, was a general partner in ABC Partnership and a limited partner in DEF Partnership. Both partnerships operated solely in Wisconsin. In 1989, Taxpayer X sold his partnership interests in both partnerships. Under terms of the agreement for the sale of his interest in ABC Partnership, Taxpayer X received payment for a specified percentage of the value of the partnership's outstanding receivables plus an amount for selling his interest in the other partnership assets. Although DEF Partnership held inventory items which had substantially appreciated in value, no part of the selling price was specifically allocated to these items in the sale agreement.

For federal purposes, Taxpayer X must treat the sale of his interest in each of the partnerships as the sale of two separate assets as provided in sec. 751 of the Internal Revenue Code. ABC Partnership's receivables and DEF Partnership's inventory items are sec. 751 property that, upon sale, are treated as ordinary gain or loss for federal purposes. Taxpayer X's interest in each partnership's non-sec. 751 property, upon sale, is treated as a capital gain or loss for federal purposes.

Is either the ordinary gain or loss on the sale of the sec. 751 property or the capital gain or loss on the sale of the non-sec. 751 property that Taxpayer X realized on the sale of his general partnership interest in Partnership ABC taxable income or a deductible loss for Wisconsin purposes? Is either the ordinary gain or loss on the sale of the sec. 751 property or the capital gain or loss on the sale of the non-sec. 751 property that Taxpayer X realized on the sale of his limited partnership interest in DEF Partnership taxable income or a deductible loss for Wisconsin purposes?

Answer 1: No. Taxpayer X's share of the ordinary gain or loss on the sale of the sec. 751 property and the capital gain or loss on the sale of the non-sec. 751 property of either partnership is not taxable income or a deductible loss for Wisconsin purposes. Both a general partnership interest and a limited partnership interest in a partnership are considered to be intangible personal property. In general, intangible assets follow the residence of the taxpayer for Wisconsin purposes. Sec. 71.04(1)(a), Wis. Stats. (1987-88). Because Taxpayer X is a nonresident and his partnership interests are intangible personal property, his shares of the sales of his interests in Partnerships ABC and DEF are not taxable by Wisconsin. The sale is considered to be one transaction consisting of the sale of the partnership interest, regardless of whether separate payments are made for partnership receivables or inventory items which have substantially appreciated in value. *Wisconsin Department of Revenue v. William B. Riley*, No. 79-CV-127, Dane County Circuit Court, November 27, 1979, CCH 201-534 and 201-749.

Facts and Question 2: Taxpayer Y, a Texas resident, is a general partner in Partnership GHI and a limited partner in Partnership JKL. Both partnerships have been operating solely in Wisconsin. In 1989, both partnerships sold all of the partnership assets located in Wisconsin, including land, buildings, office equipment, and goodwill.

Is Taxpayer Y's distributive share of the gain or loss realized by Partnership GHI on the sale of its assets taxable income or a deductible loss for Wisconsin purposes? Is Taxpayer Y's distributive share of the gain or loss realized by Partnership JKL on the sale of its assets taxable income or a deductible loss for Wisconsin purposes?

Answer 2: Taxpayer Y's share of the gain or loss realized by Partnership GHI, other than on the sale of its goodwill, is taxable income or a deductible loss for Wisconsin purposes. A partnership that sells its assets passes through any gain or loss realized on the sale to its partners. The income or loss from the sale of property of a nonresident follows the situs of the property. Sec. 71.04(1), Wis. Stats. (1987-88). Because the property was located in Wisconsin, Taxpayer Y's distributive share of Partnership GHI's gain or loss on the sale of its tangible property is taxable by Wisconsin.

Taxpayer Y's share of the gain or loss from the sale of Partnership GHI's goodwill is not taxable income or a deductible loss for Wisconsin purposes. Goodwill is an intangible asset. In general, intangible assets follow the residence of the taxpayer for Wisconsin purposes. Sec. 71.04(1)(a), Wis. Stats. (1987-88). Because the goodwill is intangible personal property, Taxpayer Y's share of the gain or loss from its sale is not taxable by Wisconsin.

Finally, Taxpayer Y's share of the gain or loss from the sale of Partnership JKL's assets is not taxable income or a deductible loss for Wisconsin purposes. A limited partner's share of the gain or loss from the sale of partnership assets is intangible personal property. *Sweitzer v. Revenue*, 65 Wis. 2d 235 (1974). In general, intangible assets follow the residence of the taxpayer. Sec. 71.04(1)(a), Wis. Stats. (1987-88). Because Taxpayer Y is a limited partner, his share of the gain or loss on the sale of Partnership JKL's assets is not taxable by Wisconsin.

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7. Penalties on Retirement Plans

Statutes: Sections 71.05(1)(a) and 71.83(1)(a)6, Wis. Stats. (1987-88)

Background: Section 71.05(1)(a), Wis. Stats. (1987-88), provides that certain payments received from the following retirement systems are exempt from Wisconsin taxation:

(1) Employe's Retirement System of the City of Milwaukee
(2) Milwaukee County Employes' Retirement System
(3) Sheriff's Annuity and Benefit Fund of Milwaukee County
(4) Police Officer's Annuity and Benefit Fund of Milwaukee
(5) Fire Fighter's Annuity and Benefit Fund of Milwaukee

(6) Milwaukee Public School Teachers' Annuity and Retirement Fund
(7) Wisconsin State Teachers Retirement System

To be exempt from Wisconsin tax, the payments must be paid on the account of a person who was a member of the retirement system or fund as of December 31, 1963, or was retired from any of the systems or funds as of December 31, 1963.

(Note: Effective for tax years beginning on or after January 1, 1989, sec. 71.05(1)(a), Wis. Stats. (1987-88), was amended by sec. 1817m of 1989 Wisconsin Act 31 to provide that payments received from federal retirement systems are also exempt from Wisconsin tax if paid on the account of any person who was a member of the retirement system as of December 31, 1963, or was retired from the retirement system as of December 31, 1963.)

Section 71.83(1)(a)6, Wis. Stats. (1987-88), provides a penalty for any person who is liable for certain federal penalties on retirement plans. One of the federal penalties is the 10% penalty on early distributions from qualified retirement plans (sec. 72(t), Internal Revenue Code). The Wisconsin penalty is 33% of the federal penalty.

Facts and Question: A person was a member of one of the above retirement systems as of December 31, 1963, and thus payments from the retirement system are exempt from Wisconsin tax. The person quit his/her job in 1989 and received a lump-sum distribution from the retirement system. The distribution is subject to the federal 10% penalty on an early distribution from a qualified retirement plan.

Is the person subject to the 33% Wisconsin penalty under sec. 71.83(1)(a)6, Wis. Stats. (1987-88), even though the payment from the retirement plan is exempt from Wisconsin income tax?

Answer: Yes, a person who is subject to the federal penalty on an early distribution from a qualified retirement plan is subject to the Wisconsin penalty, even though the payment from the retirement plan is exempt from Wisconsin income tax. The exemption in sec. 71.05(1)(a), Wis. Stats. (1987-88), is only from taxation. There is no exception for the penalty imposed under sec. 71.83(1)(a)6, Wis. Stats. (1987-88), for retirement plans when the payment from those plans is exempt from taxation.

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8. Wisconsin Income Tax Treatment of Passive Activity Losses

Statutes: Section 71.01(13), Wis. Stats. (1987-88).

Note: This tax release applies with respect to the 1987 taxable year and thereafter.

Background: Section 469 of the Internal Revenue Code (IRC) limits the deduction of passive activity losses for individuals, estates, trusts, closely held C corporations, and personal service corporations. Passive activities consist of trade or business activities in which the taxpayer does not materially participate during the taxable year and rental activities. Although the passive loss limits do not apply to grantor trusts, partnerships, and tax-option (S) corporations directly, they do apply to the individuals (or other covered taxpayers) who are beneficiaries, partners, or shareholders of such entities.

The passive activity loss limits also apply for Wisconsin purposes. However, the amount of passive activity income or loss depends on certain Wisconsin adjustments, including the following:

(A) Calculating Wisconsin adjusted gross income of individuals and fiduciaries based on federal adjusted gross income with the modifications prescribed in sec. 71.05(6) to (12), (19), and (20), Wis. Stats. (1987-88). Sec. 71.01(13), Wis. Stats. (1987-88).

(B) Determining federal adjusted gross income for Wisconsin purposes under the Internal Revenue Code as amended to a specified date and disregarding federal law changes enacted after that date which do not apply. Additionally, Wisconsin law may exclude certain provisions of the Internal Revenue Code. Sec. 71.01 (6), Wis. Stats. (1987-88). These differences between the federal Internal Revenue Code and the Internal Revenue Code in effect for Wisconsin purposes are called "Schedule I adjustments." They are accounted for on Wisconsin Schedule I.

(C) Deciding to recalculate federal adjusted gross income for Wisconsin purposes when the Internal Revenue Code permits an individual or fiduciary to make an election and the taxpayer decides to make one election for federal purposes and a different election for Wisconsin purposes.

Facts and Question 1: Taxpayer Z, a full-year Wisconsin resident, is a limited partner in ABC Partnership. Taxpayer Z determines that she must treat her interest in ABC Partnership as a passive activity. In 1986, ABC Partnership had placed in service residential rental property located in Wisconsin. For federal purposes, the partnership has been depreciating that rental property using the accelerated cost recovery system (ACRS) as provided in IRC sec. 168. Taxpayer Z's distributive share of ABC Partnership's federal ordinary loss for 1989 is $10,000.

For federal purposes, Taxpayer Z enters all of her passive activity income and losses, including her ordinary loss of $10,000 from ABC Partnership, on federal Form 8582, Passive Activity Loss Limitations. She determines that $10,600 of her passive activity losses, including $3,530 of her ordinary loss from ABC Partnership, is allowable in computing her 1989 federal adjusted gross income.

For Wisconsin purposes, federal ACRS deductions are not available for residential rental property placed in service in 1986. Instead, depreciation on such property must be computed under the Internal Revenue Code as amended to December 31, 1980. Sec. 71.02(2)(d)12, Wis. Stats. (1985-86), and sec. 71.05(16), Wis. Stats. (1987-88). As a result of these differing depreciation deductions, Taxpayer Z's distributive share of ABC Partnership's ordinary loss in 1989 is $6,000 for Wisconsin purposes.

Since her ordinary loss from ABC Partnership differs for federal and Wisconsin purposes, must Taxpayer Z recompute her allowable passive activity losses for Wisconsin purposes?

Answer 1: Yes. Taxpayer Z must recompute her allowable passive activity losses. She prepares another Form 8582 for Wisconsin purposes and substitutes her ordinary loss, as computed under Wisconsin law, from ABC Partnership of $6,000 for her federal ordinary loss of $10,000.

She must recompute the allowable passive activity losses because she must recalculate her federal adjusted gross income under the Internal Revenue Code in effect for Wisconsin purposes. Wisconsin law excludes certain depreciation provisions of the Internal Revenue Code in arriving at Wisconsin adjusted gross income.

Assume that Taxpayer Z recomputes Form 8582 for Wisconsin purposes, and she determines that $9,800 of her passive activity losses, including $2,260 of her ordinary loss from ABC Partnership, is allowable in 1989 for Wisconsin purposes. The $800 difference between the $10,600 of passive activity losses allowable on Taxpayer Z's federal return and the $9,800 of passive activity losses allowable on her recomputed Form 8582 is a "Schedule I adjustment."

Taxpayer Z then must recompute her federal adjusted gross income for Wisconsin purposes by completing Wisconsin Schedule I. She will enter the $800 adjustment to the allowable passive activity losses on Wisconsin Schedule I as an addition to the federal adjusted gross income reported on her federal income tax return.

Finally, Taxpayer Z will enter her recomputed federal adjusted gross income from Schedule I on line 1 of her Wisconsin income tax return, Form 1.

Facts and Question 2: Taxpayer Y, a full-year Wisconsin resident, is a shareholder in DEF Corporation, a tax-option (S) corporation. Taxpayer Y determines that he must treat his interest in DEF Corporation as a passive activity. For federal purposes, DEF Corporation elected to claim the federal targeted jobs credit in 1989 in lieu of a deduction for that portion of the wages paid or incurred equal to the jobs credit computed. Taxpayer Y's pro rata share of DEF Corporation's federal ordinary income for 1989 is $4,000.

For federal purposes, Taxpayer Y enters all of his passive activity income and losses, including his ordinary income of $4,000 from DEF Corporation, on federal Form 8582. He determines that $10,600 of his passive activity losses is allowable in computing his 1989 federal adjusted gross income.

For Wisconsin purposes, DEF Corporation may not claim the federal targeted jobs credit. Instead, DEF Corporation elects to deduct the wages paid or incurred which were not allowed federally. As a result of deducting these wages, DEF Corporation realizes an ordinary loss in 1989 for Wisconsin purposes. Taxpayer Y's pro rata share of that loss is $7,000.

Since his ordinary income or loss from DEF Corporation differs for federal and Wisconsin purposes, must Taxpayer Y recompute his allowable passive activity losses for Wisconsin purposes?

Answer 2: Yes. Taxpayer Y must recompute his allowable passive activity losses. He prepares another Form 8582 for Wisconsin purposes and substitutes his ordinary loss, as computed for Wisconsin purposes, from DEF Corporation of $7,000 for his federal ordinary income of $4,000.

He must recompute the allowable passive activity losses because he is making a different election under the Internal Revenue Code with respect to the treatment of wages paid or incurred and he must figure his federal adjusted gross income accordingly for Wisconsin purposes.

Assume that Taxpayer Y recomputes Form 8582 for Wisconsin purposes, and he determines that $6,600 of his passive activity losses, including $1,250 of his ordinary loss from DEF Corporation, is allowable in 1989 for Wisconsin purposes.

Taxpayer Y then must recompute his federal adjusted gross income for Wisconsin purposes by preparing a pro forma federal return. He will substitute the $6,600 of passive activity losses allowable for Wisconsin for the $10,600 of passive activity losses allowable on the federal income tax return that he filed with the Internal Revenue Service.

Finally, Taxpayer Y will enter his recomputed federal adjusted gross income on line 1 of his Wisconsin income tax return, Form 1.

Facts and Question 3: Taxpayer X, a full-year Wisconsin resident, is a limited partner in GHI Partnership. He determines that he must treat his interest in GHI partnership as a passive activity. In 1989, GHI Partnership sold property used in its trade or business (section 1231 assets) which had been held more than one year and realized a gain on the sale. Taxpayer X's distributive share of that gain is $3,000. He determines that he must treat his share of the gain as a long-term capital gain.

For federal purposes, Taxpayer X enters all of his passive activity income and losses, including his section 1231 gain of $3,000 from GHI Partnership, on federal Form 8582. He determines that $10,600 of his passive activity losses is allowable in computing his 1989 federal adjusted gross income.

For Wisconsin purposes, Taxpayer X determines that his section 1231 gain qualifies for the 60% capital gain deduction under sec. 71.05(6)(b)9, Wis. Stats. (1987-88).

Since only $1,200 of his section 1231 gain is taxable for Wisconsin purposes, must Taxpayer X recompute his allowable passive activity losses for Wisconsin purposes?

Answer 3: No. Taxpayer X is not required to recompute his allowable passive activity losses. He must subtract from his federal adjusted gross income (on Wisconsin Form 1, line 4) the $1,800 of capital gain income which was included in his federal adjusted gross income but is not taxable by Wisconsin. Sec. 71.05(6)(b)9, Wis. Stats. (1987-88).

Taxpayer X does not need to recompute his allowable passive activity losses because the capital gain deduction is a modification to federal adjusted gross income when computing Wisconsin adjusted gross income rather than an exception to the federal Internal Revenue Code when computing federal adjusted gross income for Wisconsin purposes. Neither this nor any other Wisconsin modification requires Taxpayer X to recompute his allowable passive activity losses by excluding the 60% capital gain deduction and to report the difference as an addition modification.

Facts and Question 4: Taxpayer W, a full-year Wisconsin resident, is a shareholder in JKL Corporation, a federal S corporation. Taxpayer W determines that she must treat her interest in JKL Corporation as a passive activity. For 1989, Taxpayer W's pro rata share of JKL Corporation's ordinary income is $1,000. JKL Corporation did not make any distributions to its shareholders in 1989.

For federal purposes, Taxpayer W enters all of her passive activity income and losses, including her ordinary income of $1,000 from JKL Corporation, on federal Form 8582. She determines that $10,600 of her passive activity losses is allowable in computing her 1989 federal adjusted gross income.

For Wisconsin purposes, JKL Corporation elected, pursuant to sec. 71.365(4)(a), Wis. Stats. (1987-88), not to be a tax-option corporation. Therefore, Taxpayer W must subtract from her federal adjusted gross income the $1,000 of income that she reported which was passed through from JKL Corporation. Sec. 71.05(10)(d), Wis. Stats. (1987-88).

Since the undistributed ordinary income from JKL Corporation is not taxable to Taxpayer W for Wisconsin purposes, must Taxpayer W recompute her allowable passive activity losses for Wisconsin purposes?

Answer 4: No. Taxpayer W is not required to recompute her allowable passive activity losses. She must subtract from her federal adjusted gross income (on Wisconsin Form 1, line 4) the $1,000 of JKL Corporation's income which was included in her federal adjusted gross income but is not taxable by Wisconsin. Sec. 71.05(10)(d), Wis. Stats. (1987-88).

Taxpayer W does not need to recompute her allowable passive activity losses because the exclusion of the S corporation income is a modification to federal adjusted gross income when computing Wisconsin adjusted gross income rather than an exception to the federal Internal Revenue Code when computing federal adjusted gross income for Wisconsin purposes. Neither this nor any other Wisconsin modification requires Taxpayer W to recompute her allowable passive activity losses by excluding the S corporation income and to report the difference as an addition modification.

Facts and Question 5: Assume that the facts are the same as in Question 4 above except that JKL Corporation incurred an ordinary loss for 1989, and Taxpayer W's pro rata share of that loss is $5,000.

For federal purposes, Taxpayer W enters all of her passive activity income and losses, including her ordinary loss of $5,000 from JKL Corporation, on federal Form 8582. She determines that $10,600 of her passive activity losses, including $1,770 of her loss from JKL Corporation, is allowable in computing her 1989 federal adjusted gross income.

For Wisconsin purposes, Taxpayer W may not deduct the $5,000 ordinary loss from JKL Corporation because the corporation elected not to be treated as a tax-option corporation. Sec. 71.05(10)(d), Wis. Stats. (1987-88).

Since the ordinary loss from JKL Corporation is not deductible by Taxpayer W on her Wisconsin income tax return, may Taxpayer W recompute her allowable passive activity losses for Wisconsin purposes?

Answer 5: No. Taxpayer W may not recompute her allowable passive activity losses. She must add to her federal adjusted gross income (on Wisconsin Form 1, line 2) the $1,770 of ordinary loss from JKL Corporation actually included in her 1989 federal adjusted gross income.

When figuring her Wisconsin adjusted gross income in future years, Taxpayer W must add back to her federal adjusted gross income the portion of her 1989 ordinary loss from JKL Corporation allowed that year in the computation of her federal adjusted gross income.

Neither this nor any other Wisconsin modification permits Taxpayer W to recompute her allowable passive activity losses for 1989 by excluding the S corporation loss and to make a modification for the difference.

Facts and Question 6: Taxpayer V, a nonresident of Wisconsin, reports the following income on his 1989 federal income tax return:

Wages earned in Illinois	$58,000
Interest income	8,000
Passive activity losses allowed*	(6,600)
Gain on sale of Wisconsin real estate	20,000
Federal adjusted gross income	$79,400

*Taxpayer V's passive activity losses from federal Form 8582 consist of the following:

	Total	Allowed
MNO Properties (Illinois)	$5,000	$3,667
PQR Associates (Wisconsin)	3,000	2,200
STU Partnership (Illinois)	1,000	733
Totals	$9,000	$6,600

Taxpayer V is a general partner in PQR Associates and a limited partner in MNO Properties and STU Partnership. PQR Associates conducts a business solely in Wisconsin while the other two partnerships operate only in Illinois.

What is Taxpayer V's Wisconsin adjusted gross income for 1989?

Answer 6: Taxpayer V's 1989 Wisconsin adjusted gross income is $5,800 which is computed as follows:

Gain on sale of Wisconsin real estate	$20,000	
Less: Capital gain deduction (60%)	(12,000)	$8,000
Wisconsin passive activity loss allowed		(2,200)
Wisconsin adjusted gross income		$5,800

Nonresidents of Wisconsin are subject to Wisconsin income tax on income derived from property located or business transacted in Wisconsin and from the performance of personal services in Wisconsin. Sec. 71.02, Wis. Stats. (1987-88). Therefore, Taxpayer V's gain on the sale of Wisconsin real estate is taxable by Wisconsin.

In addition, since Taxpayer V was a general partner in PQR Associates and the partnership conducted business only in Wisconsin, Taxpayer V may deduct his distributive share of PQR Associates' loss for Wisconsin purposes. However, his allowable loss for 1989 is limited to the $2,200 that was allowed for federal purposes. The Wisconsin Statutes do not permit Taxpayer V to recompute his allowable passive activity losses by excluding the income and losses that are not taxable by Wisconsin and to make a modification for the difference.

INDIVIDUAL AND FIDUCIARY INCOME TAXES

1. Wisconsin Filing Requirements for Qualified Subchapter S Trusts

Statutes: Sections 71.13(1) and 71.17(5), Wis. Stats. (1987-88).

Background: Under sec. 1361 of the Internal Revenue Code (IRC), a Qualified Subchapter S Trust (QSST) may be a shareholder of an S corporation if the current income beneficiary or his or her legal representative elects to have the trust qualify as a QSST. A QSST is a trust whose terms require that

(1) during the life of the current income beneficiary there can be only one income beneficiary,

(2) corpus distributions during the current income beneficiary's life can be made only to him or her,

(3) the current income beneficiary's income interest must terminate on the earliest of his or her death or the termination of the trust, and

(4) if the trust terminates during the current income beneficiary's life, the trust's assets must all be distributed to the current income beneficiary.

In addition, all of the trust's income must be distributed or required to be distributed currently to only one individual who is a citizen or resident of the United States. Moreover, the current income beneficiary must make a separate election for each S corporation in which the trust owns stock. The beneficiary is treated as the deemed owner under IRC sec. 678 of that portion of the trust that consists of the stock in the S corporation.

Facts: The stock of a corporation which has elected tax-option (S) corporation status for federal and Wisconsin purposes is held, in part, by ten different trusts. The trusts qualify as QSSTs for federal S election purposes, and the beneficiaries of the trusts have made federal QSST elections.

Question 1: Must the beneficiaries make a separate QSST election for Wisconsin purposes?

Answer 1: No. The beneficiaries are not required to make a separate Wisconsin election.

Question 2: May the beneficiaries, rather than the QSSTs, be listed as the shareholders on the tax-option (S) corporation's Wisconsin Schedules 5K-1, Wisconsin Tax-Option (S) Corporation Shareholder's Schedule of Income, Deductions, etc.?

Answer 2: No. The trusts, not the beneficiaries, are considered to be the shareholders for purposes of the Wisconsin Schedules 5K-1. Thus, the QSSTs must be listed as the shareholders on the Schedules 5K-1.

Question 3: Who must file Wisconsin income tax returns to report their shares of the tax-option (S) corporation income?

Answer 3: The QSSTs must file Wisconsin fiduciary income tax returns to report their shares of the tax-option (S) corporation income. Such trusts which receive income from Wisconsin sources, except trusts exempt from federal income tax pursuant to subtitle A, chapter 1, subchapter F of the Internal Revenue Code, must file a Wisconsin fiduciary income tax return, Form 2. The QSSTs must file Forms 2 to report their shares of the tax-option (S) corporation income regardless of whether all of the trust income is distributed. In addition, the beneficiaries of the QSSTs must file individual income tax returns to report their shares of the trust income.

Question 4: If the beneficiaries of the QSSTs are nonresidents of Wisconsin, may they file Wisconsin Form 1CNS, the combined individual and fiduciary income tax return for nonresident tax-option (S) corporation shareholders, in lieu of the QSSTs and individuals filing separate Wisconsin fiduciary and individual income tax returns?

Answer 4: No. Neither such QSSTs nor their beneficiaries may file a Wisconsin Form 1CNS. This form may be used only by nonresident individuals who directly own tax-option (S) corporation stock and by nonresident trusts which do not distribute any of their income in the current year.

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CORPORATION FRANCHISE OR INCOME TAXES

1. Dividends Received Deduction - Requirement to Own Stock During Entire Taxable Year

Statutes: Sections 71.22(10) and 71.26(3)(j), Wis. Stats., as amended by 1989 Wisconsin Act 31.

Facts: Corporation A does business in Wisconsin and files a Wisconsin franchise tax return on a fiscal January 31 year end basis. From February 1, 1980 to June 30, 1989 Corporation A owned 100% of the voting stock of Corporation C. On June 30, 1989 the corporations underwent a reorganization. Corporation A formed a new subsidiary, Corporation B. Corporation A owns 100% of the voting stock of Corporation B. Corporation B in turn owns 100% of Corporation C. All of the corporations have a January 31 year end. On November 30, 1989, Corporation C distributed a $20,000 property dividend to Corporation B.

Question: Is the $20,000 property dividend received by Corporation B from Corporation C deductible by Corporation B in arriving at its Wisconsin net income for the year ended January 31, 1990?

Answer: Section 71.26(3)(j), Wis. Stats., as amended by 1989 Wisconsin Act 31, provides in part that a corporation may deduct from 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.

Section 71.22(10), Wis. Stats., as amended by 1989 Wisconsin Act 31, provides in part that the taxable year means the taxable period upon the basis of which the taxable income of the taxpayer is computed for federal income tax purposes.

Therefore, since the period from June 30, 1989 through January 31, 1990 is the taxable period upon which the taxable income of Corporation B will be computed for federal tax purposes and since Corporation B owned at least 80% of the voting stock of Corporation C during that entire period, the $20,000 property distribution from Corporation C to Corporation B is deductible by Corporation B in arriving at its Wisconsin net income for the year ended January 31, 1990.

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2. Due Dates and Estimated Tax Payment Requirements for Short-Period Corporate Returns

Statutes: Sections 71.22(10) and 71.24(1) and (9)(a), Wis. Stats. (1987-88), as amended by 1989 Wisconsin Act 31.

Note: This tax release applies with respect to taxable years beginning on or after August 1, 1988.

Background: Corporation franchise and income tax returns for less than a full taxable year must be filed on or before the due date applicable for federal income tax purposes under the Internal Revenue Code (IRC). Sec. 71.24(1), Wis. Stats. (1987-88), as amended by 1989 Wisconsin Act 31. The taxable year is the taxable period for which the taxpayer's taxable income is computed for federal purposes. Sec. 71.22(10), Wis. Stats. (1987-88), as amended by 1989 Wisconsin Act 31. Corporation franchise and income taxes not paid by the 15th day of the 3rd month following the close of the taxable year are deemed delinquent. Sec. 71.24(9)(a), Wis. Stats. (1987-88), as amended by 1989 Wisconsin Act 31.

Wisconsin corporate net income is computed under the Internal Revenue Code, with certain modifications. One of the modifications excludes IRC secs. 1501 to 1505, 1551, 1552, 1563, and 1564, relating to consolidated returns, for the purpose of computing corporate income. Secs. 71.22(4) and 71.26(3)(x), Wis. Stats. (1987-88). These modifications, however, do not eliminate the consolidated return provisions of the Internal Revenue Code for the purpose of establishing filing dates.

Situation 1 — Facts: Corporation P owns 100% of the stock of Corporation S. The corporations file consolidated federal returns on a calendar-year basis. On March 31, 1989, P sells all of the stock of S to third parties, thus severing the affiliated group. Neither P nor S changes its taxable year as a result of severing the relationship.

For federal purposes, P and S file a consolidated return for the period from January 1 through March 31, 1989. The consolidated return includes the income of P for the entire 1989 calendar year and the income of S for the period from January 1 through March 31, 1989. S files a separate federal return for the period from April 1 through December 31, 1989, or is included in the consolidated return of a new affiliated group, if appropriate.

Since Wisconsin does not permit the filing of consolidated returns, P and S must file separate Wisconsin franchise or income tax returns to report their respective incomes.

Question 1: What are the filing requirements of P and S for Wisconsin franchise or income tax purposes?

Answer 1: P must file one Wisconsin franchise or income tax return for the entire 1989 calendar year, the same as for federal purposes. P's Wisconsin return is due March 15, 1990, plus any extensions.

Since S must file two short-period federal returns, S must also file two short-period Wisconsin franchise or income tax returns. The first return covers the period from January 1 through March 31, 1989, and the second, the period from April 1 through December 31, 1989. S's Wisconsin returns are due no later than its federal income tax returns. Thus, both Wisconsin returns are due no later than March 15, 1990, plus any extensions. However, the tax due on the first short-period return is payable by June 15, 1989, and the tax due on the second short-period return is payable by March 15, 1990.

Question 2: What were the estimated tax filing requirements for P and S for 1989? (Assume that the annualized installment method was not used.)

Answer 2: P was required to make four estimated tax installment payments. The payments, each for 25 percent of the estimated tax liability, were due March 15, June 15, September 15, and December 15, 1989.

S was required to make the following estimated tax installment payments:

(A) For the first short taxable year, one installment payment for 100% of the estimated tax liability was due March 15, 1989.

(B) For the second short taxable year, three installment payments were due. The first payment, for 50% of the estimated tax liability, was due June 15, 1989. The second and third payments, each for 25% of the estimated tax liability, were due September 15 and December 15, 1989.

Situation 2 — Facts: Corporation X buys 100 percent of the stock of Corporation Y on August 29, 1989. Both corporations compute their taxable incomes on a calendar-year basis. For federal purposes, X and Y file a consolidated income tax return for the period from August 30 through December 31, 1989. The consolidated return includes X's income for the entire 1989 calendar year and Y's income for the period from August 30 through December 31, 1989. Y files a separate federal return for the period from January 1 through August 29, 1989.

Question 3: What are the filing requirements of X and Y for Wisconsin franchise or income tax purposes?

Answer 3: X must file one Wisconsin franchise or income tax return for the entire 1989 calendar year, the same as for federal purposes. X's Wisconsin return is due March 15, 1990, plus any extensions.

Y must file two short-period Wisconsin franchise or income tax returns for 1989. The first return covers the period from January 1 through August 29, 1989, and the second, the period from August 30 through December 31, 1989. Both of these returns are due no later than March 15, 1990, the federal due date. However, the tax due on the first short-period return is payable by November 15, 1989, and the tax due on the second short-period return is payable by March 15, 1990.

Question 4: What were the estimated tax filing requirements for X and Y for 1989? (Assume that the annualized installment method was not used.)

Answer 4: X was required to make four estimated tax installment payments. The payments, each for 25 percent of the estimated tax liability, were due March 15, June 15, September 15, and December 15, 1989.

Y was required to make the following estimated tax installment payments:

(A) For the first short taxable year, three estimated tax installment payments were due. The first and second payments, each for 25 percent of the estimated tax liability, were due March 15 and June 15, 1989. The third payment, for 50 percent of the estimated tax liability, was due August 15, 1989.

(B) For the second short taxable year, two estimated tax installment payments were due. The first payment, for 75 percent of the estimated tax liability, was due November 15, 1989. The second payment, for 25 percent of the estimated tax liability, was due December 15, 1989.

Situation 3 — Facts: ABC Corporation, a calendar-year filer, merges into XYZ Corporation on October 6, 1989. The reorganization qualifies as an "A" reorganization under IRC sec. 368(a)(1).

Question 5: When is ABC Corporation's final Wisconsin franchise or income tax return due?

Answer 5: ABC Corporation's final return is due January 15, 1990. However, if ABC Corporation files a consolidated federal income tax return with XYZ Corporation, ABC Corporation's Wisconsin return is due no later than the federal consolidated return. The tax due on ABC Corporation's final return is payable by January 15, 1990.

Question 6: How many estimated tax installment payments was ABC Corporation required to make for 1989, and when were those payments due?

Answer 6: ABC Corporation was required to make four estimated tax installments due March 15, June 15, September 15, and October 15, 1989. Each payment should have been for 25 percent of ABC Corporation's estimated tax liability, unless the annualized installment method was used.

Question 7: If the merger of ABC Corporation into XYZ Corporation had occurred on July 6 rather than October 6, how many estimated tax payments would ABC Corporation have been required to make, and when would those payments have been due?

Answer 7: If the merger had occurred on July 6, 1989, ABC Corporation would have been required to make three estimated tax payments. The first and second payments, each for 25 percent of the estimated tax liability, would have been due March 15 and June 15, 1989. The third payment, for 50 percent of the estimated tax liability, would have been due July 15, 1989. (Note that the percentages would change if the annualized installment method were used.)

Situation 4 — Facts: Corporation P and its subsidiaries S1 and S2 file consolidated federal income tax returns on a calendar-year basis. Since Wisconsin law does not permit consolidated filing, the income and expense items are separated for Wisconsin franchise and income tax purposes. P made 1989 estimated tax payments of $10,000 each on March 15, June 15, September 15, and December 15, 1989, even though P did not operate in Wisconsin at all during 1989 and filed withdrawal papers with the Wisconsin Secretary of State's office in April 1989. Neither S1 nor S2 made any estimated tax payments for the taxable year that began in 1989.

Question 8: May either S1 or S2 claim the unused $40,000 of P's estimated tax payments for 1989 in order to avoid underpayment interest and delinquent interest on their 1989 Wisconsin franchise or income tax returns?

Answer 8: No. Each corporation is a separate entity for Wisconsin franchise or income tax purposes. Therefore, neither S1 nor S2 may claim P's estimated tax payments. *WTMJ, Inc. and Newspapers, Inc. v. Wisconsin Department of Revenue*, Wisconsin Tax Appeals Commission, Docket Nos. I-6306, I-6307 (October 23, 1980).

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3. Recognition of Adjustments Necessary as a Result of a Change in Method of Accounting

Statutes: Sections 71.26(2)and (3) and 71.30(1)(b), Wis. Stats. (1987-88).

Note: This tax release applies with respect to the 1987 taxable year and thereafter.

Background: Section 71.26(2), Wis. Stats. (1987-88), provides that Wisconsin net income is computed under the Internal Revenue Code (IRC) as defined for Wisconsin with certain modifications. The modifications are provided in sec. 71.26(3), Wis. Stats. (1987-1988). Since IRC secs. 381 and 481 are not excluded for Wisconsin, they generally apply for Wisconsin in computing Wisconsin net income.

IRC sec. 481 provides that when a change in method of accounting occurs, there shall be taken into account those adjustments which are determined to be necessary solely by reason of the change in order to prevent amounts from being duplicated or omitted. In certain situations the required adjustments to income are allowed or required to be spread over several taxable years.

IRC sec. 381 provides that in certain corporate reorganizations the tax attributes of a liquidated corporation are allowed or required to be carried over and reported by the surviving corporation. The adjustments required as a result of a change in method of accounting that are being spread over several years may be tax attributes that are to be reported by a surviving corporation in its computation of federal net income in certain corporate reorganizations.

Section 71.30(1)(b), Wis. Stats. (1987-88), provides that if a corporation changes its method of accounting while subject to franchise or income taxation by Wisconsin, it shall make the adjustments required under the IRC, except that in the last year that a corporation is subject to taxation by Wisconsin it shall take into account all remaining adjustments required as a result of the change in method of accounting.

Facts and Question: Corporation B, a calendar year Wisconsin bank, became a large bank (that is, it had assets of more than $500 million) during 1990. As a result, it is no longer allowed to claim a deduction for bad debts on the reserve method. Accordingly, it must change its method of accounting for bad debts and is required to include in income its bad debt reserve balance of $100,000 on December 31, 1989. IRC sec. 585 requires that ten percent of the adjustment required by IRC sec. 481 be reported in 1990, 20 percent in 1991, 30 percent in 1992, and 40 percent in 1993. Therefore, $10,000 will be included in the computation of federal net income for 1990. This would be included in the computation of Wisconsin net income as well.

If on December 31, 1991, Corporation B is merged into its parent, Corporation P, how is the remaining $90,000 of the adjustment to be accounted for?

Answer: Generally, for federal purposes, Corporation B will report $20,000 in 1991 and Corporation P will report $30,000 in 1992, and $40,000 in 1993 in the computation of net income.

Since sec. 71.30(1)(b), Wis. Stats. (1987-88), requires that in the last year that a corporation is subject to taxation by Wisconsin it shall take into account all remaining adjustments required as a result of a change in method of accounting, the entire $90,000 is required to be reported in the computation of Corporation B's Wisconsin net income on the 1991 Wisconsin return, the final Wisconsin return to be filed by Corporation B.

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4. Return Requirements Under an "F" Reorganization

Statutes: Section 71.22(10), Wis. Stats. (1987-88), as amended by 1989 Wisconsin Act 31.

Note: This tax release applies with respect to the 1987 taxable year and thereafter.

Facts and Question: A corporation incorporated in Wisconsin (Wis. Corp.) reports its income to Wisconsin on the basis of a fiscal year ending July 31. In 1989, for business reasons, the corporation desires to reincorporate in Delaware. To accomplish this, Wis. Corp. organizes and owns 100 percent of the stock of a subsidiary corporation incorporated in Delaware (Del. Corp.). In December 1989, Wis. Corp. merges into Del. Corp. The operations of Wis. Corp. become those of Del. Corp. and continue in all respects in the same manner as before the merger. After the merger, Wis. Corp. ceases to exist as a corporation. This transaction qualifies as an "F" reorganization as defined in sec. 368(a)(1)(F) of the Internal Revenue Code (IRC).

For federal purposes, Del. Corp. succeeds to Wis. Corp.'s tax attributes under IRC sec. 381. Accordingly, Del. Corp. files a single federal income tax return covering the fiscal year ending July 31, 1990, and Wis. Corp. will not file any federal return for any part of the same period. Rev. Rul. 57-276, 1957-1 C.B. 126.

What are the filing requirements of Wis. Corp. and Del. Corp. for Wisconsin franchise or income tax purposes?

Answer: Del. Corp. must file a Wisconsin franchise or income tax return for the entire fiscal year ending July 31, 1990, for both Wis. Corp. and itself. Wis. Corp. is not required to file a short-period return for the period from August 1, 1989, through the date of the merger.

The "taxable year" for Wisconsin purposes is the taxable period upon the basis of which the taxable income of the taxpayer is computed for federal income tax purposes. Sec. 71.22(10), Wis. Stats. (1987-88), as amended by 1989 Wisconsin Act 31. Applying sec. 71.22(10), the taxable years of Wis. Corp. and Del. Corp. must be the same for Wisconsin franchise or income tax purposes as they are for federal income tax purposes. Accordingly, only Del. Corp. must compute a tax liability for the fiscal year ending July 31, 1990, and Wis. Corp. will not compute any tax liability for any part of that fiscal year. Wis. Corp. and Del. Corp. are treated as if no change in corporate entities had occurred, the same as federally.

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5. Wisconsin Research Facilities Credit

Statutes: Sections 71.28(4)(b) through (i) and (5) and 71.47(3)(b) through (i) and (4), Wis. Stats. (1987-88), and sec. 71.09(12r)(b) through (L) and (12rf), Wis. Stats. (1985-86).

Background: For 1984 and subsequent years, any corporation may credit against taxes otherwise due under chapter 71 an amount equal to 5% of the amount paid or incurred by that corporation during the taxable year to construct and equip new facilities or expand existing facilities used in Wisconsin for qualified research, as defined in section 41 of the Internal Revenue Code (IRC). Only amounts paid or incurred for tangible, depreciable property are eligible. Amounts paid or incurred for replacement property are not eligible.

Facts and Question 1: Corporation A purchases a desktop personal computer and related software for use in analyzing research data in its advanced research laboratory. Although the corporation uses several other computers in the laboratory, this unit will be used by employes performing experiments in new and different phases of product development, which is qualified research under IRC sec. 41.
Does the expenditure qualify for the Wisconsin research facilities credit?

Answer 1: Yes. The expenditure constitutes an expansion of Corporation A's research capabilities and, therefore, is eligible for the Wisconsin research facilities credit.

Facts and Question 2: Corporation B purchases an advanced model desktop personal computer and related software for use in analyzing research data in its advanced research laboratory. The corporation currently uses several other computers in the laboratory, and this unit will replace and upgrade an older model personal computer used by employes performing experiments in various phases of product development, which is qualified research under IRC sec. 41. The new computer has a larger memory and faster operating speed than the old computer which enables it to perform more sophisticated analyses on larger volumes of data. The new computer is priced at $10,000. A computer with essentially the same capabilities as the old computer is available for $4,500.

Does the expenditure qualify for the Wisconsin research facilities credit?

Answer 2: In this situation, $5,500 of the $10,000 expenditure qualifies for the Wisconsin research facilities credit. Only a portion of the expenditure qualifies for the credit because the new computer both replaces an existing computer and expands Corporation B's research capabilities. A reasonable allocation of the expenditure between the amount paid for replacement property and the amount paid to expand research capabilities must be made. That portion of the expenditure which is attributable to the expansion of Corporation B's research capabilities qualifies for the credit, whereas the cost of replacement property does not qualify.

Since a computer with essentially the same capabilities as the old computer would cost $4,500, that portion of the $10,000 purchase price is considered to be a nonqualifying expenditure for replacement property. The remaining $5,500 is treated as an amount paid to expand Corporation B's research capabilities.

Facts and Question 3: Corporation C produces adaptor plates used in various products manufactured by its customers. These adaptor plates typically require a large number of threaded holes of varying depths and diameters to secure the plate to the customer's product and also to affix various accessories. To expedite the product development process, Corporation C purchases a new multi-spindle drill for use in its prototype model shop. The drill is designed to enable the operator to rapidly set up a large number of different drilling jobs, but is not suited to or used for large quantity production runs. However, if time is available, the drill occasionally is used to rework adaptor plates sent from the manufacturing plant for redrilling.

The new drill replaces several single-spindle drills presently used in the model shop. The new drill enables the corporation to drill and tap more holes with significantly greater precision and speed than the single-spindle drills it replaced. The new drill substantially reduces the cost and time required to develop new model adaptor plates. The new multi-spindle drill costs $25,000, whereas the single-spindle drills which it replaces would cost a total of $20,000.

A review of the drill operator's time cards used to report his work indicates that 40% of the time the machine is used to produce new pilot models, which is qualified research under IRC sec. 41, and the remainder of the time the machine is used in nonqualifying activities.

Is the new multi-spindle drill which is used in the prototype model shop eligible for the Wisconsin research facilities credit?

Answer 3: In this situation, $2,000 of the cost of the new multi-spindle drill qualifies for the Wisconsin research facilities credit. Only a portion of the expenditure qualifies for the credit because the new multi-spindle drill both replaces existing single-spindle drills and expands Corporation C's research capabilities. A further allocation is required because the drill is used only 40% of the time in qualified research.

Since the single-spindle drills would cost $20,000, that portion of the $25,000 purchase price is considered to be a nonqualifying expenditure for replacement property. Forty percent of the $5,000 difference between the cost of the new multi-spindle drill and the cost of the single-spindle drills it replaces is treated as an amount paid to expand Corporation C's research capabilities.

Facts and Question 4: In 1987, Corporation D purchases land for $1,000,000 and begins construction of a new 50,000 square foot research laboratory facility, remitting $5,000,000 in progress payments to the contractor during the year. The structure is completed near the end of 1988, and an additional $5,000,000 is remitted to the contractor. Previously, Corporation D's product development work was performed in various areas amounting to 2% of the floor space of the 500,000 square foot manufacturing plant. The research areas in the manufacturing plant are vacated and converted to other uses.

During 1988, Corporation D spends $1,000,000 to landscape the grounds, provide parking, and furnish the 5,000 square feet devoted to activities which are not qualified research under IRC sec. 41.

Corporation D also orders $8,000,000 of specialized research instruments and equipment in 1988. The equipment is highly specialized, and the vendor will not permit the orders to be cancelled. Some research work is commenced during 1988, but $2,000,000 of the equipment is not received and installed until 1989. The equipment does not represent replacement property.

In what year and in what amounts may Corporation D claim the Wisconsin research facilities credit?

Answer 4: Corporation D may claim a research facilities credit on its 1987 Wisconsin franchise or income tax return based on $7,000,000 of costs for the building. Since 5,000 square feet of the total 50,000 square feet of the building are not used in the conduct of qualified research, they do not qualify for the credit. Additionally, 10,000 square feet of space in the new facility replaces the product development areas formerly located within the manufacturing plant. Accordingly, the costs associated with a total of 15,000 square feet of the facility's total 50,000 square feet (30% of the total) are not eligible.

Therefore, $7,000,000 of the $10,000,000 cost of the building is eligible for the Wisconsin research facilities credit.

While it is required that the facility be used for the conduct of research, it is not required that the research use occur in the year the costs are paid or incurred. Therefore, D Corporation may claim a credit based on the costs of the building in 1987 because that is when the costs are incurred, even though payments are made in 1988 and the building is placed in service in 1988.

Corporation D may claim a research facilities credit on its 1988 return based on the $8,000,000 of costs for instruments and equipment incurred in 1988, even though some of the equipment is not delivered or paid for until 1989. The $8,000,000 obligation to pay the equipment vendors is irrevocably incurred in 1988.

Corporation D may not claim a research facilities credit for the $1,000,000 incurred in 1987 for the land because it is not depreciable property and, therefore, does not qualify for the credit. The $1,000,000 incurred in 1988 for landscaping the grounds, providing parking, and furnishing the non-research areas is not used in the conduct of qualified research and is not eligible for the credit.

Note: If, after claiming the credits, Corporation D does not use the building or the equipment in the conduct of qualified research, Corporation D must file amended returns and pay back the research facility credits previously received for nonqualifying property.

Facts and Question 5: Corporation E is about to commence a major scientific research project related to the improvement of its product line. The activities are considered qualified research under IRC sec. 41. Additional engineers and scientists are hired in connection with the project, and the corporation finds that additional floor space will be required to accommodate product development operations. Corporation E fulfills its temporary need for additional laboratory facilities by leasing a new building owned by Corporation F. Corporation F is a real estate development and management firm that does not conduct any qualified research.

Are the leased facilities eligible for the Wisconsin research facilities credit?

Answer 5: Yes. Corporation E may claim a Wisconsin research facilities credit because it is expanding its research capabilities by leasing the laboratory facility. Corporation F may not also claim a research facilities credit based on the new building.

The Wisconsin research facilities credit is available for amounts paid or incurred for tangible, depreciable property used in Wisconsin for qualified research. There is no requirement that the party conducting the research own the property. Both the lessor and the lessee may not claim a credit for the same property. Since Corporation E is using the property for qualified research, the amounts Corporation E pays or incurs to lease the facility are eligible for the credit.

Corporation E may not claim a credit based on amounts attributable to the costs of the land because it is not depreciable. Claims for the credit must also exclude amounts attributable to any portion of the property not used in the actual conduct of qualified research.

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6. Wisconsin Tax Treatment of a Net Operating Loss Incurred in a Short Taxable Year Resulting From a Change in Accounting Period

Statutes: Sections 71.22(4) and 71.26(2)(a), (3), and (4), Wis. Stats. (1987-88).

Note: This tax release applies with respect to the 1987 taxable year and thereafter.

Facts and Question: On January 4, 1989, Corporation P acquires 100 percent of the stock of Corporation S. Corporation P had been filing its income tax returns on a calendar-year basis, while Corporation S had been filing on the basis of a fiscal year with an August 31 year-end.

Corporations P and S begin filing consolidated income tax returns for federal purposes, and they change their taxable years for reporting purposes to fiscal years ending March 31.

For federal purposes, Corporation S files a separate income tax return for the period from September 1, 1988, through January 4, 1989. Corporation S joins in the filing of a consolidated return with Corporation P for the period beginning January 5, 1989, and ending March 31, 1989. Corporation S determines that it incurred a net operating loss for each of the short periods.

For federal purposes, the 3-year carryback and 15-year carryforward provisions of sec. 172 of the Internal Revenue Code (IRC) apply to Corporation S's net operating loss for the period from September 1, 1988, through January 4, 1989. However, Corporation S must deduct the net operating loss for the period from January 5, 1989, through March 31, 1989, ratably over a 6-year period beginning with the first taxable year after the short period. Revenue Procedure 84-34, 1984-1 CB 508.

For Wisconsin purposes, Corporations P and S may not file a consolidated return. Sec. 71.26(3)(x), Wis. Stats. (1987-88). Instead, Corporations P and S each must file a separate return and report its own income. Since Corporation S must file two short-period returns for federal purposes, it also must file two short-period Wisconsin returns: the first for the period from September 1, 1988, through January 4, 1989, and the second for the period from January 5, 1989, through March 31, 1989. Sec. 71.22(10), Wis. Stats. (1987-88), as amended by 1989 Wisconsin Act 31. Corporation S determines that it also incurred a net operating loss for each of the short periods for Wisconsin purposes.

Must Corporation S prorate over 6 years its net operating loss for the period from January 5, 1989, through March 31, 1989, for Wisconsin purposes?

Answer: No. Corporation S is not required to prorate its net operating loss for the period from January 5, 1989, through March 31, 1989, over 6 years. Instead, Corporation S may carry forward the net operating loss for each of the short periods for up to 15 taxable years, as provided in sec. 71.26(4), Wis. Stats. (1987-88).

For Wisconsin purposes, Corporation S computes its net income under the Internal Revenue Code, with certain modifications. One of those modifications excludes the net operating loss provisions of IRC sec. 172 and replaces them with the treatment of net business loss carryforwards under sec. 71.26(4). Sec. 71.26(3)(i), Wis. Stats. (1987-88). This statute does not require a corporation to deduct over a 6-year period a net operating loss incurred during a short taxable year resulting from a change in accounting period.

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7. Wisconsin Tax Treatment of Corporations With Net Operating Loss and Charitable Contribution Carryovers

Statutes: Section 71.26(2)(a), (3), and (4), Wis. Stats. (1987-88).

Note: This tax release applies with respect to the 1987 taxable year and thereafter.

Background: For federal income tax purposes, a corporation's deduction for charitable contributions may not exceed 10 percent of taxable income as computed without regard to the charitable contribution deduction, the special deductions for corporations under Internal Revenue Code (IRC) secs. 241-247 and 249-250, any net operating loss carryback to the taxable year under IRC sec. 172, and any capital loss carryback to the taxable year under IRC sec. 1212(a)(1). Sec. 170(b)(2), Internal Revenue Code. A 5-year carryover period applies to charitable contributions in excess of the 10 percent limitation. In the case of a corporation with a net operating loss carryover, the charitable contribution is taken into account and reduces taxable income before applying the net operating loss carryover. Sec. 170(d)(2)(B), Internal Revenue Code.

Example: Corporation X, which reports its income on a calendar-year basis, sustained a federal net operating loss in 1988 of $100,000. In 1989, Corporation X earned federal taxable income of $80,000 before deducting a $10,000 charitable contribution made in 1989 and before applying the federal net operating loss carryover from 1988.

For federal purposes, in determining the amount of 1988 net operating loss which is used in 1989, $8,000 (10% of $80,000) of Corporation X's 1989 charitable contribution is taken into account and reduces 1989 taxable income to $72,000 before applying the net operating loss carryover. The remaining $2,000 of the 1989 charitable contribution may be carried over to 1990. Since the taxable income is reduced to $72,000, only $72,000 of the 1988 net operating loss is used as a carryover to 1989, leaving $28,000 of the 1988 loss available as a carryover to 1990.

Facts and Question 1: Assume that all of Corporation X's income is attributable to Wisconsin because the corporation is doing business only in Wisconsin. For Wisconsin purposes, Corporation X sustained a net business loss in 1988 of $100,000 and earned Wisconsin taxable income in 1989 of $80,000 before deducting the $10,000 charitable contribution made in 1989 and before applying the Wisconsin net business loss carryforward from 1988.

What are Corporation X's Wisconsin charitable contribution carryover and Wisconsin net business loss carryforward to 1990?

Answer 1: In this situation, Corporation X's Wisconsin charitable contribution carryover and Wisconsin net business loss carryforward are the same as the federal amounts. Corporation X's Wisconsin charitable contribution carryover to 1990 is $2,000 and its Wisconsin net business loss carryforward to 1990 is $28,000.

For Wisconsin franchise and income tax purposes, a corporation computes its Wisconsin net income under the Internal Revenue Code, with certain modifications. Sec. 71.26(2)(a), Wis. Stats. (1987-88). One of these modifications excludes IRC sec. 172 and replaces it with the treatment of net business loss carryforwards under sec. 71.26(4). Sec. 71.26(3)(i), Wis. Stats. (1987-88). However, the state statutes do not modify IRC sec. 170, relating to the treatment of the charitable contribution deduction and carryover. Since IRC sec. 170 is not modified for Wisconsin purposes, the Wisconsin charitable contribution deduction and carryover are determined in the same manner as the federal amounts.

Facts and Question 2: Now assume that Corporation X does business in and outside Wisconsin and is required to determine its net income allocable to Wisconsin using the apportionment method. For Wisconsin purposes, Corporation X sustained a total company net business loss in 1988 of $100,000 and its 1988 Wisconsin apportionment percentage was 55 percent. Therefore, Corporation X's Wisconsin net business loss carryforward to 1989 is $55,000 (55% of $100,000). In 1989, Corporation X earned taxable income of $80,000 before deducting the $10,000 charitable contribution made in 1989, before applying its 1989 Wisconsin apportionment percentage of 60 percent, and before applying the $55,000 Wisconsin net business loss carryforward from 1988.

What are Corporation X's Wisconsin charitable contribution carryover and Wisconsin net business loss carryforward to 1990?

Answer 2: Corporation X's Wisconsin charitable contribution carryover to 1990 is $2,000 and its Wisconsin net business loss carryforward to 1990 is $11,800. These amounts are computed as follows.

For Wisconsin purposes, $8,000 (10% of $80,000) of Corporation X's 1989 charitable contribution is taken into account and reduces its 1989 total company net income before apportionment and the net business loss offset to $72,000. The remaining $2,000 of the 1989 charitable contribution may be carried over to 1990. The $72,000 of total company net income is then multiplied by 60 percent, the 1989 Wisconsin apportionment percentage, to arrive at $43,200 of Wisconsin net income before the net business loss offset. Therefore, only $43,200 of the 1988 Wisconsin net business loss is used as a carryforward to 1989, leaving $11,800 of the 1988 loss available as a carryforward to 1990.

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8. Wisconsin Tax Treatment of Transactions Between Related Corporations

Statutes: Section 71.26(3), Wis. Stats. (1987-88).

Note: This tax release applies with respect to the 1987 taxable year and thereafter.

Background: Beginning with the 1987 taxable year, corporations compute their net income under the Internal Revenue Code (IRC), as amended to a specified date, and as modified by sec. 71.26(3), Wis. Stats. (1987-88). One of these modifications excludes the consolidated return rules in IRC secs. 1501 to 1505, 1551, 1552, 1563, and 1564 for Wisconsin franchise and income tax purposes. Sec. 71.26(3)(x), Wis. Stats. (1987-88).

Facts and Question 1: B Corporation, a corporation incorporated in Wisconsin, is a wholly-owned subsidiary of A Corporation, a non-Wisconsin corporation. B Corporation wholly owned its non-Wisconsin subsidiary, C Corporation. B Corporation is engaged in business in Wisconsin, but neither A nor C Corporation has activity in Wisconsin that would subject it to Wisconsin franchise or income taxation. During 1989, B Corporation sold all of its C Corporation stock to A Corporation and realized a loss on the sale.

For federal purposes, A, B, and C Corporations file a consolidated income tax return. B Corporation's loss on the intercompany sale is not recognized. Treasury Regulation sec. 1.1502-13(c). Additionally, B Corporation's loss on the sale or exchange of property between members of a controlled group of corporations is deferred until the property is transferred outside the group and the loss becomes recognizable under the consolidated return rules or federal regulations. IRC sec. 267(f).

For Wisconsin purposes, A, B, and C Corporations may not file a consolidated return. Sec. 71.26(3)(x), Wis. Stats. (1987-88). Instead, B Corporation must file a separate 1989 Wisconsin franchise or income tax return and report its own income. Neither A nor C Corporation is required to file a Wisconsin return because neither corporation has nexus with Wisconsin.

Is B Corporation's loss on the sale of its C Corporation stock recognizable in 1989 for Wisconsin franchise or income tax purposes?

Answer 1: No. B Corporation's loss on the sale of the stock is not recognizable in 1989 for Wisconsin franchise or income tax purposes. Although Wisconsin law excludes the consolidated return provisions from the Internal Revenue Code for the purpose of computing

Wisconsin net income, Wisconsin law includes the provisions for loss transactions between related taxpayers under IRC sec. 267. Therefore, a corporation's loss on the intercompany sale of stock is deferred under IRC sec. 267(f) for Wisconsin purposes.

Facts and Question 2: D Corporation, a Wisconsin corporation, is a subsidiary of E Corporation, another Wisconsin corporation. During 1989, D Corporation distributed appreciated property to E Corporation.

For federal purposes, a corporation that distributes property to a shareholder recognizes a gain on the distribution to the extent the fair market value of the property distributed exceeds its adjusted basis, as if the property were sold to the distributee at its fair market value. IRC sec. 311(b).

For federal purposes, D and E Corporations file a consolidated income tax return. They eliminate their intercompany stock distributions, including dividends and nonliquidating distributions, to determine their consolidated taxable income. Treasury Regulation sec. 1.1502-14. Therefore, D Corporation's gain on the distribution of appreciated property will be deferred in 1989 and recognized at a later time.

For Wisconsin purposes, D and E Corporations may not file a consolidated return. Sec. 71.26(3)(x), Wis. Stats. (1987-88). Instead, each must file a separate 1989 Wisconsin franchise or income tax return and report its own income.

Is D Corporation required to recognize the gain on the distribution of appreciated property to E Corporation in 1989 for Wisconsin franchise or income tax purposes?

Answer 2: Yes. D Corporation must recognize the gain on the distribution of appreciated property to E Corporation in 1989. Although Wisconsin law excludes the consolidated return provisions from the Internal Revenue Code for the purpose of computing Wisconsin net income, Wisconsin law includes the provisions for the taxability of corporate distributions under IRC sec. 311(b). Therefore, the distributing corporation must recognize the gain on distributions of appreciated property, including distributions made to another member of an affiliated group, under IRC sec. 311(b) for Wisconsin purposes.

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FARMLAND TAX RELIEF CREDIT

1. Land on Which Farmland Tax Relief Credit Is Based

Statutes: Sections 71.07(3m), 71.28(2m), and 71.47(2m), Wis. Stats., as created by sections 1864m, 1966m, and 2045m, respectively, of 1989 Wisconsin Act 31.

Note: This Tax Release applies only with respect to farmland tax relief credit for property taxes accrued during 1989 and thereafter.

Background: To be eligible for farmland tax relief credit, a claimant or a member of the claimant's household must be an owner of 35 or more acres of farmland, as defined in secs. 71.07(3m)(a)3, 71.28(2m)(a)3, and 71.47(2m)(a)3, Wis. Stats., as created by 1989 Wisconsin Act 31. The farmland tax relief credit may be claimed on the following 1989 Wisconsin tax returns: Form 1, line 27; Form 1NPR, line 54; Form 2, line 17; Form 4, line 18; Form 4I, line 22; Form 4T, line 21; and Form 5, line 12.

Question: For purposes of qualifying for the farmland tax relief credit, must all of the farmland be adjoining?

Answer: No. For farmland tax relief credit purposes, "farmland" means 35 or more acres of Wisconsin land which is part of a farm that meets certain gross farm profits requirements or is in the Conservation Reserve Program. The statutes do not require that all of the land be adjoining.

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SALES/USE TAXES

1. Nexus Standards for Foreign Corporations That Are Publishers

Statutes: Sections 77.51(13g) and 77.53(3), Wis. Stats. (1987-88) and 77.51(13h) Wis. Stats. (1987-88), as amended by 1989 Act 336.

A. **Background:** Every "retailer engaged in business in this state" (i.e., a retailer who has nexus in Wisconsin for use tax) for purposes of use tax, is required to collect use tax from the purchaser on sales of tangible personal property or taxable services in Wisconsin (sec. 77.53(3), Wis. Stats. (1987-88)).

"Retailer engaged in business in this state" is defined in sec. 77.51(13g), Wis. Stats. (1987-88), and means any of the following (except as provided in sec. 77.51(13h), Wis. Stats.).

- Any retailer owning any real property in this state or leasing or renting out any tangible personal property located in this state or maintaining, occupying or using, permanently or temporarily, directly or indirectly, or through a subsidiary, or agent, by whatever name called, an office, place of distribution, sales or sample room or place, warehouse or storage place or other place of business in this state.

- Any retailer having any representative, agent, salesperson, canvasser or solicitor operating in this state under the authority of the retailer or its subsidiary for the purpose of selling, delivering or the taking of orders for any tangible personal property or taxable services.

B. **New Nexus Standards for Foreign Corporations That Are Publishers:** Section 77.51(13h), Wis. Stats., was created by 1987 Act 399 and amended by 1989 Act 336. As a result of 1987 Act

399 and 1989 Act 336, a "retailer engaged in business in this state" (i.e., a retailer who has nexus in Wisconsin for use tax) does not include a foreign corporation that is a publisher of printed materials if its only activities in Wisconsin do not exceed the four activities described below:

1. The storage of the publisher's raw materials for any length of time in Wisconsin in or on property owned by a person other than the publisher and the delivery of the publisher's raw materials to another person in Wisconsin if that storage and delivery are for printing by that other person.

2. The purchase from a printer of a printing service or of printed materials in Wisconsin for the publisher.

3. The storage of the printed materials for any length of time in Wisconsin in or on property owned by a person other than the publisher.

4. Maintaining, occupying and using, directly or by means of another person, a place that is in Wisconsin, that is not owned by the publisher and that is used for the distribution of printed materials.

Note: (a) For a foreign corporation that is a publisher of books and/or periodicals other than catalogs, sec. 77.51(13h), Wis. Stats., is effective January 1, 1980. This includes publishers who publish 1) only books, 2) only periodicals other than catalogs, 3) books and periodicals other than catalogs, 4) either books and/or periodicals other than catalogs, and in addition, other materials (e.g., catalogs, advertising flyers).

(b) For all other publishers that are foreign corporations (other than those included in (a) above), sec. 77.51(13h), Wis. Stats., is effective January 1, 1990.

C. **Definitions**

1. "Foreign corporation", as used in sec. 77.51(13h), Wis. Stats., means any corporation not organized under Wisconsin law.

2. "Raw materials", as used in sec. 77.51(13h), Wis. Stats., means tangible personal property which becomes an ingredient or component part of the printed materials or which is consumed or destroyed or loses its identity in the printing of the printed materials.

3. "Publisher", as used in sec. 77.51(13h), Wis. Stats., means a foreign corporation which publishes printed material for distribution or sale.

   Example 1: A foreign corporation publishes a monthly magazine which it sells to subscribers. This magazine is printed by another company. This foreign corporation is considered a "publisher" for purposes of sec. 77.51(13h), Wis. Stats.

   Example 2: A foreign corporation engaged in the mail-order business has its catalogs printed by a printing company. This foreign corporation is considered a "publisher" for purposes of sec. 77.51(13h), Wis. Stats.

   Example 3: A foreign corporation manufactures auto parts and has advertising flyers printed by another company for distribution to the public. This foreign corporation is considered a "publisher" for purposes of sec. 77.51(13h), Wis. Stats.

4. "Periodical", as used in sec. 77.51(13h), Wis. Stats., means publications, each issue of which contains news or information written by different authors which is of general interest to the public, or to some particular organization or group of persons. Each issue must bear a relationship to prior or subsequent issues in respect to continuity of literary character or similarity of subject matter, and there must be some connection between the different issues of the series in the nature of the articles appearing in them. To be a periodical, the publication must qualify for the second class mail rate or as a controlled circulation publication under U.S. postal laws and regulations.

   A periodical does not include books complete in themselves, even those issued at stated intervals (for example, books sold by the Book of the Month Club or similar organizations); paperback books, a new one of which may be issued once a month or some other interval; or so-called "one-shot" magazines that have no literary or subject matter connection or continuity between prior or subsequent issues. Periodical also does not include catalogs, programs, scorecards, handbills, maps, real estate brokers' listings, price/order books, corporate reports to stockholders, house organs, or advertising materials which become a component part of a periodical.

COUNTY SALES/USE TAXES

1. County Use Tax - Purchaser's Liability if Seller Fails to Charge Sales Tax

Statutes: Sections 77.71 and 77.73(2), Wis. Stats. (1987-88).

Facts and Question: A seller engaged in business in County A (which adopted the county tax) sells taxable tangible personal property to a purchaser located in County B (which also adopted the county tax) and delivers that property to the purchaser in County B. County B has jurisdiction to tax the transaction because the seller makes deliveries in its own company-operated vehicles into County B. The seller collects the 5% Wisconsin state sales tax on the transaction, but erroneously does not collect County B's county sales tax on the sale, even though it is a taxable transaction.

Is the purchaser subject to County B's use tax on this transaction since the seller failed to collect county sales tax?

Answer: Yes. The purchaser is subject to County B's use tax in accordance with sec. 77.71(2), Wis. Stats. (1987-88), because the purchaser does not have a receipt indicating the county sales tax has been paid under sec. 77.71(1), Wis. Stats. (1987-88).

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2. County Use Tax - Purchasing From a Wisconsin Seller

Statutes: Section 77.71(2), Wis. Stats. (1987-88).

Facts and Questions: A customer in Dunn County (a county which adopted the county tax) ordered a chair from a seller located in Milwaukee county (which has not adopted the county tax as of April, 1990). The chair was shipped by the seller to Dunn County via common carrier. The customer uses the chair at his or her place of business in Dunn County. The seller billed the customer for the selling price of the chair plus the 5 percent Wisconsin state sales tax. The Milwaukee County seller does not conduct any nexus activities in Dunn County.

(A) Is the seller located in Milwaukee County liable for the Dunn County sales tax?

(B) Is the customer located in Dunn County liable for the Dunn County use tax?

Answers:

(A) No, because the seller does not have nexus in Dunn County.

(B) Yes, the customer is subject to the Dunn County use tax under sec. 77.71(2), Wis. Stats. (1987-88).

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