



# Wisconsin TAX BULLETIN



## FOCUS ON . . .

### Tax Season Gear-Up

See articles on pages 1 to 6.

## Forms Changes for 1994

Following are brief descriptions of the major changes to the Wisconsin individual income tax forms for 1994.

- Check boxes are added to Forms 1A, 1, and 1NPR for the new "head of household" filing status which is available for Wisconsin for 1994. Persons who qualify to file as "head of household" for federal tax purposes may now also use that filing status for Wisconsin.
- Spaces for providing information on qualifying children and the amount of federal earned income credit have been deleted from the earned income credit line on Forms 1A, 1, and 1NPR. The Wisconsin earned income credit for 1994 will be computed on a new form, Wisconsin Schedule EICW.
- Capital gain distribution line has been deleted from Form 1NPR. Also, a line has been added for reporting moving expenses. These changes are made to conform the Form 1NPR to the 1994 federal Form 1040.

- It is no longer necessary to fill in the preparer's address on Form 1. The space marked "For Department Use Only" at the bottom of Form 1 has been increased. The department enters a validation number in this area; therefore it is very important that you leave this area blank.

Preliminary copies of the 1994 Forms WI-Z, 1A, 1, and 1NPR, the new earned income credit Schedule EICW, and the homestead credit and farmland preservation credit claim forms, Schedule H and Schedule FC, are reproduced on pages 20 to 34 of this Bulletin. The copies are subject to further revisions. □

## 1994 Income Tax Law Changes

Following are brief descriptions of some of the Wisconsin law changes which affect individuals in completing 1994 Wisconsin income tax returns.

- **Head of household filing status** Persons who qualify to file their federal income tax returns using the head of household filing status may also file their Wisconsin returns using that filing status.
- **Educational assistance benefits** The exclusion provided by federal law for up to \$5,250 of educational assistance benefits received by an employee applies for Wisconsin for the 1994 taxable year.
- **Taxable social security** For federal tax purposes up to 85% of

social security benefits may be taxable. The maximum amount of social security benefits taxable for Wisconsin remains at 50%.

- **Medical care insurance deduction** The deduction for medical care insurance costs paid by a self-employed person or by an employee whose employer does not contribute toward the cost of such insurance is 50% of the medical care insurance costs. For 1993 returns, the percentage was 25%.
- **Earned income credit** In prior years, the Wisconsin earned income credit was equal to a percentage of the federal earned income credit. The Wisconsin credit is no longer tied to the federal credit. A new form, Schedule EICW, is used to compute the Wisconsin earned income credit.
- **Alternative minimum tax** The exemption amounts for alternative minimum tax purposes are increased to conform to the federal exemption amounts. The new exemption amounts are: \$45,000 if married filing jointly; \$33,750 if single or head of household; or \$22,500 if married filing separately. □

## Milwaukee Exposition District Taxes Begin January 1

The City of Milwaukee has created an exposition center tax district, to help fund a new exposition center in Mil-

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administers the 0.5% county sales tax).

Following is information about the different types of local exposition district taxes.

### • Food and Beverage Tax

The District's food and beverage tax will be 0.25% on sales in Milwaukee County. Generally, if sales of food and beverages are subject to the 5% state sales tax, they are also subject to this 0.25% food and beverage tax.

### • Room Tax

The District's basic room tax will be 2% on the furnishing of rooms or lodging to any person residing for a continuous period of less than one month in a hotel, motel, or other furnished accommodations available to the public.

The District has also adopted an additional room tax of 7%. This additional room tax applies **only to room rentals described above located within the City of Milwaukee**. This additional 7% District tax replaces the City of Milwaukee room tax, effective January 1, 1995.

### • Rental Car Tax

The District's rental car tax will be 3% on the receipts from the rental, for 30 days or less, of Type 1 automobiles without drivers within the District's jurisdiction. The renter shall collect the rental car tax from the person to whom the Type 1 automobile is rented.

A "Type 1 automobile" is defined as a motor vehicle designed and used primarily for carrying persons but which does not come within the definition of motor bus, motorcycle, moped, or motor bicycle. For purposes of imposing the rental car tax, the lease or rental of a Type 1

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waukee (the Wisconsin Center). The District has the authority to impose a food and beverage tax, a room tax, and a rental car tax to fund the exposition center. The District adopted resolutions which provide that these taxes become effective January 1, 1995.

The District is made up of all municipalities located wholly or partially in Milwaukee County. Although these taxes are locally imposed, the law directs the Department of Revenue to administer them on behalf of local authorities (much as the department

automobile is considered to take place at the location where the automobile comes into the lessee's possession.

During November 1994 the department will contact businesses located within Milwaukee County. These businesses will be provided with information regarding the local exposition district taxes. They will also be asked to complete and return a questionnaire, to provide information the department needs to administer these taxes.

If you have questions regarding these local exposition district taxes, please call the department in Madison at (608) 266-2776 or Milwaukee at (414) 227-4600, or write to Wisconsin Department of Revenue, P.O. Box 8902, Madison, WI 53708-8902. □

## Postcards Save Over \$4,000

In December of 1993, the Department of Revenue mailed 257,000 postcards with a mailing label to taxpayers, in place of a 1993 Form 1 tax booklet. The postcard recipients were taxpayers whom the Internal Revenue Service identified as having used a tax preparer to complete their return in prior years.

Instructions on the postcard advised taxpayers to take the postcard to their tax preparer so the preparer could transfer the mailing label to the tax return filed. For taxpayers who still wanted a tax booklet, the postcard included a detachable order blank which could be completed and mailed to the department to request a booklet.

Comments from the public indicated that the postcard mailing was well received by taxpayers. The use of postcards produced a cost savings of \$4,000.

An improvement will be made to the postcard for 1994, with respect to taxpayers who have moved. Last year 12,000 taxpayers did not receive their postcard because they no longer lived at the address to which it was mailed.

This year the postal endorsement "FORWARDING AND RETURN POSTAGE GUARANTEED" will be added to the postcard. With the addition of this endorsement, most taxpayers who have moved will still receive a postcard. Use of the postcard label on the returns these taxpayers file will reduce the department's cost of processing these returns, even though the address on the label has been corrected. □

## Electronic Filing — It's Not Just for Refunds

Over 800 Wisconsin tax preparers participated in the Wisconsin Federal/State Electronic Filing Program for 1993 tax returns. The vast majority of 1993 returns filed electronically were refund returns. When tax preparers are asked why they aren't participating, the most common answer is "Most of my returns are complex and have a balance due."

While the fast turnaround for receiving refunds is a major benefit of filing refund returns electronically, there are also many advantages to filing those complex, balance due returns electronically. These advantages include the following:

- Both the IRS and the Department of Revenue provide proof of filing, with quick acknowledgment. This is not possible with paper returns.
- The error rate for electronic returns is much lower than paper returns (1.5% vs. 7% for 1993 returns).
- Electronic filing is more efficient than copying, sorting, labeling,

mailing, and keeping track of paper returns.

- The return can be filed early, and no payment is necessary until the due date. If an adjustment is made, your client will be notified of the correct amount due.
- Most Wisconsin full-year resident returns may be filed electronically, including (for 1994 returns) forms with Schedules EICW, I, MT, U, WD, and 2440W.
- Returns with extensions may be filed electronically through August 15.

With electronic filing, you can give your customers the best possible service, reduce your overall preparation and mailing costs, save paper, and get high quality results. To participate, follow these easy steps:

1. File the federal application, Form 8633, with the IRS. Contact Gerri Ness at the IRS Milwaukee office, (414) 297-3385, for forms.
2. After you are issued a federal Electronic Filer Identification Number (EFIN) by the IRS, make a photocopy of your Form 8633, enter you EFIN on the top of the application, and mail it to:  
  
Wisconsin Electronic Filing  
P.O. Box 8903  
Madison, WI 53708-8903  
  
or FAX it to (608) 264-6884.
3. Watch your IRS electronic filing newsletters for dates, times, and places of IRS/Wisconsin free electronic filing seminars.

If you're interested in more information, write to the Electronic Filing Coordinator at the above address, or call (608) 264-6886. If you're interested in participating, welcome. □

## Guidelines for Substitute Tax Forms

Tax returns may generally be filed on forms that have been reproduced or on substitute forms that have been approved by the department. However, certain guidelines must be followed to ensure that the reproduced or substitute forms are compatible with the department's processing system and present information in a uniform manner.

A copy of the "Guidelines for Reproduced and Substitute Tax Forms" appears on pages 35 and 36 of this Bulletin. □

### Information or Inquiries?

#### Madison - Main Office Area Code (608)

Beverage, Cigarette, Tobacco Products . . . . .	266-6701
Corporation Franchise and Income . . . . .	266-1143
Estimated Taxes . . . . .	266-9940
Fiduciary, Inheritance, Gift, Estate . . . . .	266-2772
Homestead Credit . . . . .	266-8641
Individual Income . . . . .	266-2486
Motor Fuel . . . . .	266-3223
Sales, Use, Withholding . . . . .	266-2776
Audit of Returns: Corporation, Individual, Homestead . . . . .	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

## Focus on Publications: Magnetic Media Filing Required for Some Forms

Persons who are required to file federal wage statements and information returns on magnetic media with the Internal Revenue Service or Social Security Administration may also be required to file those forms on magnetic media with the Wisconsin Department of Revenue. Wisconsin Publication 509, "Filing Wage Statements and Information Returns on Magnetic Media," describes what forms must be filed on magnetic media for Wisconsin, the magnetic media requirements, and when and where to file on magnetic media. A copy of Publication 509 is reproduced on pages 37 and 38 of this Bulletin. □

## IRS 1994 Mileage Rates Apply for Wisconsin

The 1994 optional standard mileage rates specified by the IRS for computing automobile expenses for business, charitable, medical, and moving expense purposes also apply for Wisconsin.

For 1994 the IRS increased the business standard mileage rate from 28¢ per mile to 29¢ per mile for all business miles driven. The 29¢ per mile rate is allowed without regard to whether the automobile was previously considered fully depreciated.

If the standard mileage rate of 29¢ per mile is used, depreciation is considered to be allowed at 12¢ per mile for 1994, up from 11.5¢ per mile for 1993. However, no portion of the 29¢ per mile rate is considered to be depreciation after the adjusted basis of the automobile reaches zero.

For 1994 the mileage rate allowed for calculating automobile expenses for charitable deduction purposes remains

at 12¢ per mile, and the rate allowed for medical expense deductions and moving expense deductions remains at 9¢ per mile. These are the same rates that were allowed for 1993. □

## 1994 Package WI-X Available

The 1994 edition of Wisconsin's Package WI-X will be available by January 31, 1995. The Package WI-X will contain actual size copies of most 1994 Wisconsin individual and fiduciary income tax, corporation franchise and income tax, partnership, estate tax, motor vehicle fuel tax, sales and use tax, and withholding tax forms.

The cost of the 1994 Package WI-X is \$7.00 per copy, which includes sales tax. It may be ordered on the bulk order blank (Form P-744). The bulk order blank is being mailed in October. See the following article for more information on bulk orders.

If you do not receive an order blank and you wish to purchase copies of 1994 Package WI-X, mail your request indicating the number of copies, along with the amount due, to Wisconsin Department of Revenue, Shipping and Mailing Section, P.O. Box 8903, Madison, WI 53708-8903. □

## Tax Form Order Blanks Mailed

During October, the department is mailing order blanks (Form P-744) to 8,500 tax preparers. Use these original order blanks (not copies) to request bulk orders of 1994 Wisconsin tax forms.

Two changes have been made to the order blank. A space is provided for your telephone number, in the event there is a problem or question regarding your order. Also, the Wisconsin

earned income credit schedule, Schedule EICW, has been added.

Some of the forms you order will be accompanied by additional information. For example, your order will include instructions for the forms you request; Schedules 2K-1 and 2 WD will be included with fiduciary Form 2 orders; and Schedules 3K-1 will be included with partnership Form 3 orders.

The department is also mailing order blanks (Forms P-744b and P-744L) to banks, post offices, and libraries for their use in requesting bulk orders of 1994 Wisconsin income tax forms. No charge is made for forms used for distribution to the general public (for example, in a bank, library, or post office).

If you do not receive an order blank by October 31, 1994, you may request one by contacting any department office; by writing to Wisconsin Department of Revenue, Shipping and Mailing Section, P.O. Box 8903, Madison, WI 53708-8903; or by calling (608) 267-2025.

You should place your order as early as possible after receiving the order blank. Orders are expected to be filled in late December and early January.

Package WI-X will be mailed separately in late January. Most forms in Package WI-X may be reproduced. ☐

## Tax Publications Available

The Department of Revenue publishes over 35 publications that are available, free of charge, to taxpayers or practitioners. To order any of the publications, write or call Wisconsin Department of Revenue, Shipping and

Mailing Section, P.O. Box 8903, Madison, WI 53708-8903 (telephone (608) 266-1961).

Number	Title of Publication (and last revision date)		
102	Wisconsin Tax Treatment of Tax-Option (S) Corporations and Their Shareholders (12/93)	202	Sales and Use Tax Information for Motor Vehicle Sales, Leases, and Repairs (7/94)
103	Reporting Capital Gains and Losses for Wisconsin by Individuals, Estates, Trusts (11/93)	203	Sales and Use Tax Information for Manufacturers (9/93)
104	Wisconsin Taxation of Military Personnel (8/94)	205	Do You Owe Wisconsin Use Tax? (Individuals) (5/94)
109	Tax Information for Married Persons Filing Separate Returns and Persons Divorced in 1994 (10/94)	206	Sales Tax Exemption for Nonprofit Organizations (9/90)
111	How to Get a Private Letter Ruling From the Wisconsin Department of Revenue (3/94)	207	Sales and Use Tax Information for Contractors (7/94)
112	Wisconsin Estimated Tax for Individual, Estates, Trusts, Corporations, Partnerships (12/92)	210	Sales and Use Tax Treatment of Landscaping (5/94)
113	Federal and Wisconsin Income Tax Reporting Under the Marital Property Act (11/93)	211	Sales and Use Tax Information for Cemetery Monument Dealers (10/91)
114	Wisconsin Taxpayer Bill of Rights (2/94)	212	Businesses: Don't Forget About Use Tax (9/94)
117	Guide to Wisconsin Information Returns (9/94)	213	Travelers: Don't Forget About Use Tax (3/94)
200	Sales and Use Tax Information for Electrical Contractors (7/94)	214	Do You Owe Wisconsin Use Tax? (Businesses) (9/93)
201	Wisconsin State and County Sales and Use Tax Information (9/94)	400	Wisconsin's Temporary Recycling Surcharge (12/93)
		500	Tax Guide for Wisconsin Political Organizations and Candidates (12/92)
		501	Field Audit of Wisconsin Tax Returns (12/92)
		502	Directory of Free Publications (12/93)
		503	Wisconsin Farmland Preservation Credit (12/93)
		504	Directory for Wisconsin Department of Revenue (12/93)

- 505 Taxpayers' Appeal Rights of Office Audit Adjustments (6/92)
- 506 Taxpayers' Appeal Rights of Field Audit Adjustments (11/91)
- 507 How to Appeal to the Tax Appeals Commission (8/92)
- 508 Wisconsin Tax Requirements Relating to Nonresident Entertainers (8/94)
- 509 Filing Wage Statements and Information Returns on Magnetic Media (3/94)
- 600 Wisconsin Taxation of Lottery Winnings (11/93)
- 601 Wisconsin Taxation of Pari-Mutuel Wager Winnings (3/94)
- 700 Speakers Bureau presenting ... (2/93)
- W-166 Wisconsin Employer's Withholding Tax Guide (9/90) ☐

## Topical and Court Case Index Available

Are you looking for an easy way to locate reference material to research a Wisconsin tax question? The *Wisconsin Topical and Court Case Index* will help you find reference material to research your Wisconsin tax questions. This index references Wisconsin statutes, administrative rules, *Wisconsin Tax Bulletin* articles, tax releases, publications, Attorney General opinions, and court decisions.

The first part of the index, the "Topical Index," gives references to alphabetized subjects for the various taxes, including individual income, corporation franchise and income, withhold-

ing, sales and use, gift, inheritance and estate, cigarette, tobacco products, beer, intoxicating liquor and wine, and motor vehicle fuel, alternate fuel, and general aviation fuel.

The second part, 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.

If you need an easy way to research Wisconsin tax questions, subscribe to the *Wisconsin Topical and Court Case Index*. The annual cost is \$18, plus sales tax. The \$18 fee includes a volume published in December, and an addendum published in May.

To order your copy, complete the order blank on page 39 of this Bulletin. The order blank may also be used for subscribing to the *Wisconsin Tax Bulletin* and for ordering the Wisconsin Administrative Code. ☐

## Wisconsin Tax Bulletin Annual Index Available

Once each year the *Wisconsin Tax Bulletin* includes an index of materials that have appeared in past Bulletins. The latest index available appears in *Wisconsin Tax Bulletin* 88 (July 1994), pages 37 to 61, and includes information for issues 1 (October 1976) to 85 (January 1994). ☐



## Need a Speaker?

Are you planning a meeting or training program? The Wisconsin Department of Revenue provides speakers to business, community, and educational organizations.

Department representatives are available to speak on a variety of topics that can be targeted toward your group's particular areas of interest, including:

- New income and corporate tax laws.
- How sales tax affects contractors, landscapers, manufacturers, non-profit organizations, or businesses in general.
- What to expect in an audit.
- Common errors discovered in audits.
- Homestead credit.
- Farmland preservation credit.

To arrange for a speaker, please write to Wisconsin Department of Revenue, Speakers Bureau, P.O. Box 8933, Madison, WI 53708-8933, or call (608) 266-1911. ☐

## Direct Pay Allowed for Eligible Businesses

The direct pay method for reporting and paying Wisconsin sales and use taxes will be allowed, starting with taxable years beginning on or after January 1, 1995.

### What is direct pay?

Under direct pay, a buyer who has a direct pay permit may buy tangible personal property or taxable services without sales or use tax, with certain exceptions, even though no exemption applies. The buyer is liable for use tax when it stores, uses, or consumes the property or service in a taxable manner.

The amount subject to use tax is the purchase price of the tangible personal property or taxable services. Use tax is reported on the direct pay holder's sales and use tax return.

**Who is eligible?**

The Department of Revenue will issue a direct pay permit to an applicant, at the beginning of the applicant's taxable year, if the following seven requirements are fulfilled:

1. because of the nature of the applicant's business, issuing the permit will significantly reduce the work of administering the sales and use taxes;
2. the applicant's accounting system will clearly indicate the amount of tax the applicant owes;
3. the applicant makes enough taxable purchases to justify the expense of regular audits by the Department of Revenue;
4. the applicant is not liable under ch. 71, 72, 76, 77, 78, or 139, Wis. Stats., for delinquent taxes (including costs, penalties, surcharges, and interest) of \$400 or more if any part of the tax is delinquent for at least 5 months;
5. it is in the state's best interests to issue the permit;
6. the applicant purchases enough tangible personal property under circumstances that make it difficult to determine whether the property will be subject to sales or use tax; and
7. the applicant holds a seller's permit under sec. 77.52(7), Wis. Stats., or a use tax registration certificate under sec. 77.53(9), Wis. Stats.

A person may apply for a direct pay permit by submitting to the Department of Revenue at the address listed in the next paragraph, a completed application form, along with an application fee of \$5.

**Questions?**

If you have any questions, please write to Wisconsin Department of Revenue, P.O. Box 8902, Madison, WI 53708-8902, or call (608) 266-2776. □

**Claims for Refund of Sales Tax**

When a buyer pays Wisconsin sales or use taxes in error to a seller, the buyer may, under certain conditions, file a claim for refund of the taxes with the Department of Revenue. This provision is a result of a new law enacted by the Wisconsin Legislature for 1994. It became effective for claims filed on or after September 1, 1994.

Additional information about claims for refund of sales or use taxes, by both sellers and buyers, will be included in a new publication, Wisconsin Publication 216, titled "*Filing Claims for Refund of Sales or Use Tax*." This publication will be available in December 1994. It will explain who may file claims for refund, how and when to file, which forms to use, and other information. □

**Tax Evasion Is Costly**

In July 1994, Patricia G. Hass, 46, 2091 Joy Lane, LaCrosse, was found guilty by a LaCrosse County Circuit Court jury, on three counts of income tax evasion. Hass had been charged in August 1992, with three counts of filing false and fraudulent income tax returns, including original 1988 and 1989 returns and an amended 1988 return. Hass failed to report income of nearly \$100,000 which she embezzled during 1988 and 1989, from Olsten Temporary Services, a temporary employment agency she operated. Hass was convicted of the embez-

zlement and sentenced on that charge in March 1993, to three years in prison.

In addition to the embezzlement sentence, Hass faces up to 15 years in prison and \$30,000 in fines for the tax evasion conviction. 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 convictions for criminal violations.

Also in LaCrosse County Circuit Court, dentist Frederick G. Kriemelmeyer, 45, 1120 Caledonia St., LaCrosse, was sentenced in September 1994, to two years in jail for failing to file Wisconsin income tax returns for 1990, 1991, and 1992. Circuit Judge Dennis Montabon then stayed the sentence, placed Kriemelmeyer on three years probation, and ordered him to pay a \$7,500 fine, court costs, and \$6,640 prosecution costs. He was also ordered to file 1987 through 1993 Wisconsin income tax returns and pay all Wisconsin taxes, penalties, and interest within one year, and to make a full disclosure of his assets within six months. The two year jail sentence will be reinstated if he does not abide by all conditions of the probation. □

**LaCrosse County Tax Extended**

The LaCrosse County ½% sales and use tax will not expire on December 31, 1994. Although it was scheduled to expire on that date, the LaCrosse County Board passed an ordinance in July 1994, to repeal the expiration date of December 31, 1994. As a result of this ordinance, there no longer is an expiration date for the LaCrosse County tax. □

## Question and Answer

**Q** My company has software maintenance agreements with several vendors who provide technical support for their licensed computer software. Some of the vendors collect sales tax on the cost of the maintenance agreements, but others don't. When are maintenance agreement contracts subject to Wisconsin sales tax?

**A** Charges for providing maintenance for computer equipment and prewritten or "canned" programs are subject to Wisconsin sales tax. Charges for providing maintenance for custom programs are not taxable. Note: For more information about "custom" vs. "canned" computer programs, refer to the tax release titled "Taxability of Computer Programs (Software)" in *Wisconsin Tax Bulletin 79* (October 1992), page 23.

**Q** I am going to be in charge of organizing an antique fair at a mall. Each participant will be responsible for sales or use tax on the items they sell at the antique fair. Do I have any sales tax responsibilities as a result of organizing the antique fair?

**A** Yes. You are required to provide to the Department of Revenue, within 10 days following the close of the event, a report which includes the name of the event, the location and date or dates of the event, and the real

name, business name, address, social security number, and seller's permit number (if available) of each vendor at the event. Failure to provide this information could result in a penalty of \$200 (\$500 for each subsequent failure).

Form S-240 may be used to obtain the information from vendors. Copies of this form are available by calling or writing to Wisconsin Department of Revenue, P.O. Box 8902, Madison, WI 53708-8902 (telephone (608)266-2776).

**Q** I am a Wisconsin retailer, and when I buy items for resale I don't pay sales tax. Sometimes I use some of these items rather than selling them. How do I report and pay the sales or use tax on the items I use?

**A** For the items you use, report the purchase price on line 17 of your sales and use tax return. Report the items and pay the tax on the sales and use tax return for the period the items are first used.

**Q** Many of my customers pay by credit card. When I prepare my sales and use tax return, may I deduct the fees I pay to the credit card companies to arrive at state taxable receipts on line 11 of the return?

**A** No. These fees are a cost of doing business, but do not reduce state taxable receipts. ☐

## Did You Correctly Report the County Tax?

In September 1994, the department began contacting sales and use tax registrants who are located in a county that has adopted the ½% county tax but have not reported any county sales tax. Registrants are asked to review their records for the length of time they have been doing business in a county, and to verify or correct their previous reporting.

A ½% county tax is imposed upon retailers that sell, lease, rent, store, or consume tangible personal property, or furnish taxable services in a county that has adopted the ½% tax. On the sales and use tax return (Form ST-12), retailers are required to enter their taxable receipts subject to sales tax and purchases subject to use tax separately for each county. As of July 1, 1994, 46 counties have adopted the ½% county sales tax.

If you have questions about the state and county sales and use tax, call or visit any Wisconsin Department of Revenue office or write to Wisconsin Department of Revenue, P.O. Box 8902, Madison, WI 53708-8902. ☐

## Over 1.7 Million Refunds Issued

Taxpayers were issued more than 1.7 million income tax refunds during January to July 1994 (primarily 1993 returns), for an average refund of \$320. The average refund for 1992 returns was \$309.

There were 2,593,000 Wisconsin individual income tax returns filed during the twelve months ending



June 30, 1994. This compares to 2,522,000 returns for the prior year. The 2,593,000 returns, which included joint tax returns, were filed by 3,718,000 individuals.

An itemized deduction credit was claimed by 25% of the taxpayers on their 1993 returns. The average credit was \$343, compared to \$322 on 1992 returns.

There were 235,000 homestead credit claims filed during the year, and the average credit was \$457. This compares to 239,000 homestead credit claims averaging \$439 for the prior year. About 46% of the claimants were age 65 or older, 47% were renters, and 53% were homeowners.

About 24,300 farmland preservation credit claims, averaging \$1,240 per claim, were filed during the year ending June 30, 1994. During the prior year 24,500 farmland preservation credit claims were filed, and the average payment was \$1,182. ☐

### **PartnerCare Enrollment Cards Mailed**

In October 1994, the department is mailing PartnerCare enrollment cards and an explanatory flyer to approximately 25,000 individuals. The mailing is based on a listing of 1993 homestead credit claimants and their spouses age 65 or older, whose household income for 1993 did not exceed \$19,154, and who were not mailed a PartnerCare card by the department in 1992 or 1993.

PartnerCare is a program sponsored by the State Medical Society of Wisconsin and the Coalition of Wisconsin Aging Groups. Its purpose is to help low-income senior citizens get the

medical care they need. Participating doctors volunteer to charge PartnerCare cardholders no more than the amount Medicare approves, for Medicare-covered services.

Prior to 1992, PartnerCare cards mailed by the department were temporary or "annual" cards, with an expiration date (the cards mailed in October 1991, for example, expired December 31, 1992). The cards mailed out beginning October 1992, however, are "permanent" cards, with no expiration date. Individuals are no longer issued a new card each year; those who were mailed a permanent card in October 1992 or 1993 will not receive one this year.

To enable more eligible persons to receive a PartnerCare card, the homestead credit claim, Schedule H, includes a check box near the box for the claimant's age. By checking the box if the claimant has a spouse age 65 or older, the department is able to issue a PartnerCare card to the spouse if applicable, as well as to the claimant. ☐

### **Endangered Resources Contributions Increase to \$614,000**

The 1993 Wisconsin income tax returns, Forms WI-Z, 1A, 1, and 1NPR, included a line for taxpayers to designate a contribution to the Wisconsin Endangered Resources Fund. These donations either reduce a taxpayer's income tax refund or increase the amount of income tax owed. Amounts contributed go to the Wisconsin Department of Natural Resources to help protect and care for Wisconsin's endangered species, nongame wildlife, and rare plant and animal habitats.

Donations to the Endangered Resources Fund can be made on both paper filed tax returns and electronically filed returns.

During July 1993 through June 1994 (primarily 1993 returns), 54,052 taxpayers contributed \$613,548 to the Endangered Resources Fund. This compares with 1992 income tax returns, where 56,574 taxpayers contributed \$609,549. ☐

### **Taxpayers Designate \$359,662 to State Election Campaign Fund**

Wisconsin income tax returns, Forms WI-Z, 1A, 1, and 1NPR, include a box for taxpayers to designate \$1 to the State Election Campaign Fund. Checking the election box does not increase the tax liability or reduce a taxpayer's refund.

During July 1993 to June 1994 (primarily 1993 tax returns), taxpayers designated \$359,662 to the election campaign fund on their Wisconsin tax returns. This compares to \$378,824 for the prior year. ☐

### **New York State Tax Amnesty Program**

*Note: Information in this article is from a press release submitted by the New York State Department of Taxation and Finance. This amnesty program expires November 30, 1994.*

Starting September 1, 1994, New York State began a limited three-month amnesty program aimed at specific taxpayers during particular years. Those who qualify must pay any taxes owed, plus interest, but will be protected from any related criminal prosecution or administrative penalty.

The *income tax* component applies only to nonresidents of New York who have failed to file any required income tax returns for tax years beginning on and after January 1, 1986 and ending before December 31, 1993. Thus, 1992 would be the last calendar year for which participants can file for amnesty. Excluded is anyone currently under criminal investigation, anyone who has already been contacted by the Tax Department, and anyone who participated in New York's 1985 general Amnesty Program.

Similarly, the *business tax* component applies only to out-of-state businesses that have been doing business in New York and who should have filed returns between 1986 and December 1, 1993. Thus, 1992 would be the last calendar year, and November 1993 the last month for which participants can file for amnesty. Once again, any business under criminal investigation or already contacted by the Tax Department is ineligible.

A *use tax* component of the New York amnesty program applies only to New York resident individuals and smaller businesses with a New York payroll.

Additional information and amnesty forms can be obtained by writing: Amnesty, New York State Department of Taxation and Finance, Building 8, W.A. Harriman Campus, Albany, New York 12227. From outside New York you may call 1-518-438-8581. ☐

## Administrative Rules in Process

Listed below are proposed new administrative rules and changes to existing rules that are currently in the rule adoption process. The rules are shown at their stage in the process as of October 1, 1994, or at the stage in which action occurred during the period from July 2, 1994, to October 1, 1994.

Each affected rule lists the rule number and name, and whether it is amended (A), repealed (R), repealed and recreated (R&R), or a new rule (NR).

### Rules at or Reviewed by Legislative Council Rules Clearinghouse

- 2.03 Corporation returns-R&R
- 2.04 Information returns and wage statements-R&R
- 2.08 Returns of persons other than corporations-R&R
- 2.10 Copies of federal returns, statements, schedules, documents, etc. to be filed with Wisconsin returns-R&R
- 2.39 Apportionment method-A

### Rules Sent to Revisor for Publication of Hearing Notice

- 2.97 Earned income credit eligibility-NR
- 11.04 Constructing buildings for exempt entities-A

### Rules Sent to Legislative Committees

- ch. 4 (title) MOTOR VEHICLE AND GENERAL AVIATION FUEL TAXATION-A
- 4.01 Portable motor equipment-A
- 4.02 Resellers' personal claims for refund-A
- 4.03 Public highways closed to public travel-A
- 4.04 No printing on back of original invoice-R
- 4.05 Taxicabs-A
- 4.10 Motor vehicle fuel tax liability-NR
- 4.11 Tax exemption for dyed diesel fuel-NR
- 4.12 Uncollected motor vehicle fuel taxes and repossessions-NR
- 4.50 Assignment, use and reporting of document number-A
- 4.51 Measuring withdrawals-A
- 4.52 Separate schedules-A
- 4.53 Certificate of authorization-A
- 4.54 Security requirements-A
- 4.55 Ownership and name changes-A
- 4.65 Motor vehicle fuel tax refunds to vendors and tax deductions for suppliers-NR
- 4.75 Payment of motor vehicle fuel tax-NR ☐



## Report on Litigation

Summarized below are recent significant Wisconsin Tax Appeals Commission (WTAC) and Wisconsin Court decisions. The last paragraph of each decision indicates whether the case has been appealed to a higher Court.

The following decisions are included:

### Individual Income Taxes

Interest — deduction limitation  
*Robert and Margaret Yunker*  
(p. 11)

Nonresidents — S corporation liquidations  
*William W. and Cecelia G. Hansen, and Harry D. and Nancy W. Jacobs, Jr.*  
(p. 12)

### Individual Income and Corporation Franchise and Income Taxes

Liquidating corporations — installment sales  
*Mil/Cos, Inc., Mil/Tan, Inc., Lucille A. Knoernschild, and Carl Knoernschild Estate* (p. 12)

### Sales and Use Taxes

Computer software — tangible vs. intangible  
*Manpower International, Inc.* (p. 13)  
Waste reduction and recycling  
*Ruef's Sanitary Service, Inc.*  
(p. 14)

## INDIVIDUAL INCOME TAXES

**Interest — deduction limitation.** *Robert and Margaret Yunker vs. Wisconsin Department of Revenue* (Court of Appeals, May 24,

1994). The taxpayers appeal from an order of the Circuit Court for Milwaukee County affirming a decision of the Wisconsin Tax Appeals Commission. See *Wisconsin Tax Bulletin* 85 (January 1994), page 16, for a summary of the Circuit Court decision.

The issue in this case is whether an apartment complex owned by the taxpayers was investment property, and thus deductions for mortgage interest payments were limited to \$1,200 per year, or whether the property was held for sale in the course of a business, and thus the deductibility of the interest payments for Wisconsin tax purposes was not subject to the \$1,200 limitation.

In 1974, Robert Yunker built a 120-unit apartment complex in Fond du Lac. From the time the complex was completed until it was sold in 1982, the apartments were rented out. The complex was sold on a land contract, with the taxpayer maintaining the underlying mortgage on the complex. On their Wisconsin income tax returns for 1986, 1987, and 1988, the taxpayers deducted interest paid on the mortgage. The Department of Revenue reviewed the taxpayers' Wisconsin tax returns, concluded that the complex was investment property and that the interest deduction was thus subject to a \$1,200 limitation, and adjusted their tax returns for those years accordingly. The taxpayers appealed to the Commission, which upheld the department's assessment. The taxpayers again appealed, to the Circuit Court, which also affirmed the assessment. On appeal, the Court of Appeals reviewed the Commission's decision, not that of the Circuit Court.

The taxpayers claim that the Commission's decision resulted from an erroneous application of the law. They contend that the Commission improperly focused almost exclusively on the manner in which they characterized the apartment complex on their tax returns, which is irrelevant, and that the Commission should have looked at other factors when considering whether the property was held for investment or for sale in the course of business. The taxpayers also claim that the Commission's decision is not supported by substantial evidence.

The Court of Appeals affirmed the Commission's decision, concluding that the apartment complex was held as investment property and that therefore the interest expense deduction was subject to the \$1,200 per year limitation.

The Court held that the Commission applied the correct analysis in its decision. The information on a tax return is relevant, and in addition the Commission's decision clearly indicated that sufficient other factors were considered. The Court also concluded that the Commission's decision was supported by substantial evidence, including the following:

1. The complex was held for eight years before it was sold.
2. There were never any "For Sale" signs in front of the complex, and the taxpayer did not appear to have a written contract with brokers to sell the property.
3. There was no evidence that he ever advertised the property for sale.

4. Most importantly, the taxpayers reported the gain from the sale of the apartment complex as a capital gain on their tax returns, which is not permissible for "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business." Further, as the taxpayers admit, if the apartment was held for sale in the ordinary course of business, this activity should have been, but was not, reported on Schedule C of their tax returns.

The taxpayers have not appealed this decision. □

**— Nonresidents — S corporation liquidations.** *William W. and Cecelia G. Hansen, and Harry D. and Nancy W. Jacobs, Jr. vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, June 27, 1994). The sole issue in this case is whether the disparity of income tax treatment between Wisconsin residents and nonresidents renders sec. 71.337(1), Wis. Stats. (1985-86), unconstitutional under either the Privileges and Immunities Clause or the Interstate Commerce Clause of the United States Constitution.

All of the taxpayers were at all relevant times residents of Illinois and were shareholders of two Wisconsin tax-option (S) corporations. Prior to September 30, 1986, both of the corporations were liquidated under Internal Revenue Code Section 337.

The final Wisconsin corporate tax returns for both corporations, for their taxable years ending September 30, 1986, were filed in December 1986. Both returns showed income allocable to the corporations' shareholders, which consisted of both net profit or loss from operations and gain upon liquidation.

In April 1987, amended final Wisconsin tax returns were filed for both

corporations, eliminating from the net income allocable to their shareholders the gains upon liquidation which the corporations had previously recognized. The basis of the amendments was that the statute requiring the reporting of gains upon liquidation by nonresidents but not by Wisconsin residents had been declared unconstitutional. The income from the gains upon liquidation were not reported on the 1986 individual income tax non-resident returns of any of the taxpayers.

The Commission concluded that the taxpayers failed to meet their burden to show in what respects sec. 71.337(1), Wis. Stats. (1985-86), unjustifiably discriminates against nonresident shareholders and contravenes either the Privileges and Immunities Clause or the Interstate Commerce Clause of the United States Constitution.

The taxpayers have appealed this decision to the Circuit Court. □

## INDIVIDUAL INCOME AND CORPORATION FRANCHISE AND INCOME TAXES

**— Liquidating corporations — installment sales.** *Mil/Cos, Inc., Mil/Tan, Inc., Lucille A. Knoernschild, and Carl Knoernschild Estate vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, June 20, 1994). The issue in this case is whether the taxpayers are liable, under sec. Tax 2.19(2), Wis. Adm. Code (1985), for additional franchise or income taxes on unreported gain from a 1981 installment agreement distributed in liquidation in 1985, notwithstanding the language of sec. 71.336, Wis. Stats. (1985-86).

Taxpayers Mil/Cos, Inc. and Mil/Tan, Inc. were Wisconsin corporations. Taxpayer Carl Knoernschild

Estate was a Florida estate, created upon the death of Carl Knoernschild on or about April 2, 1983. Taxpayer Lucille Knoernschild is the surviving spouse of Carl Knoernschild, was the recipient of all of the assets of the estate, and at all times relevant to this matter was a Florida resident.

All of the matters in this case involve tax assessments based upon one event, the distribution of an installment obligation by Mil/Cos, Inc. during the taxpayer corporations' respective 1985 tax years. During the 1985 tax years, pursuant to plans of complete liquidation, all of the assets of both corporations were distributed to their respective shareholder(s) (Mil/Tan, Inc. owned all of the stock of Mil/Cos, Inc., and Carl and Lucille Knoernschild owned all of the Mil/Tan, Inc. stock). The 1985 tax year was the final fiscal year for both corporations.

Liquidation of taxpayer Mil/Cos, Inc. took place pursuant to secs. 71.332 and 71.336, Wis. Stats. (1983-84). The liquidation qualified under sec. 71.332, Wis. Stats., because at all times taxpayer Mil/Tan, Inc. owned at least 80 per cent of its stock. Liquidation of taxpayer Mil/Tan, Inc. took place pursuant to sec. 71.336, Wis. Stats. (1983-84).

In July 1988, the department issued a notice of assessment to taxpayer Mil/Cos, Inc. for 1985, for the gain remaining to be reported on a 1981 installment sale at the time the corporation was liquidated. In December 1991, the department issued additional notices of assessment to taxpayers Mil/Tan, Inc., Carl Knoernschild Estate, and Lucille Knoernschild. In making the assessments, the department relied in part upon sec. Tax 2.19, Wis. Adm. Code, which provides that the installment method of reporting gains on the sale of property is contingent upon the implied agreement of the taxpayer to take into

income in the year of distribution all of the unreported balance of gain upon the installment sale.

The Commission concluded that sec. 71.336, Wis. Stats. (1985-86), exempts the taxpayers from recognizing their unreported gain on the liquidation distribution of the 1981 installment agreement. Section Tax 2.19(2), Wis. Adm. code, is unenforceable against the taxpayers because it directly conflicts with sec. 71.336, Wis. Stats. (1985-86), and because its companion provision, sec. Tax 2.19(1), has been held to be invalid because it exceeds the bounds of correct interpretation, in the decision of *Castle Corp. v. Rev. Dept.*, 142 Wis. 2d 716 (Ct. App. 1987).

The department has not appealed this decision. □

## SALES AND USE TAXES

➔ **Computer software — tangible vs. intangible.** *Manpower International, Inc. vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, August 15, 1994). The issues in this case are:

- A. Whether the computer software leased by the taxpayer from various vendors is tangible personal property and subject to sales or use tax.
- B. Whether the taxpayer's lease of computer software from various vendors is a purchase of taxable services.

The taxpayer is a corporation organized in Delaware with its main offices located in Milwaukee, Wisconsin.

A typical sequence of events for the taxpayer in utilizing a new computer program is that the program arrives in the taxpayer's location on magnetic

tape or diskettes and is placed by the taxpayer into the magnetic tape or disk drive. Using a "utility" program, the taxpayer loads the new program, which is "read" from the tape or diskette and copied or reproduced on the computer's drive from which it can be conveniently used later on.

All the software involved in this matter is non-custom software, often referred to as "pre-written" or "canned" software, as opposed to "custom" software. "Custom" software is produced to the special order of the customer, usually after extensive review of the customer's computer hardware and operational needs. "Canned" software is produced in quantity, available for sale to the public, selected by the customer to meet the customer's hardware requirements, is generally usable by the customer as written, and is "loaded" into the computer memory by the customer.

A loaded program flows to the central processing unit of the computer electronically to perform the task of, or "execute," the program. If the program is provided in the form of magnetic tape or a diskette, the program is first usually copied into one of the tape or disk drives of the computer. When the program is to be used, it is copied from the disk drive into the computer's memory. Assuming nothing goes wrong with the process of copying the program onto the disk drive, the program can be used without making further use of the tape or diskettes originally provided. As long as the program remains stored in the disk drive intact, the program can continue being used without ever having to go back to the original tape or diskette. The program remains on the original tape or diskette unless obliterated by (1) recording new material over that already on the media or (2) by magnetic erasure. A copy of the tape or diskette is often retained by the customer for "archive" or backup purposes.

The heart of the computer is the "instruction processing unit" which actually "interprets" the coded instructions. The instructions are kept in a memory unit, either that of the computer itself — the "primary memory" — or in mass storage units such as a "disk drive" or a magnetic tape drive — the "secondary memory." When the program is to be used, instructions are transferred from memory into the instruction processing units where they are acted upon.

The coded instructions which flow to the instruction processing unit are sequences of zeros and ones referred to as "bits." These "bits" are copied from disk to memory, and one small group at a time is loaded into the instruction processing unit. A bit can be represented non-electronically by the presence or absence of a hole in a punched card or by magnetic impulses or electronically, all indicating either zeros or ones.

Bits have a physical presence. Every time a bit is copied, or "read," from a tape or disk, the presence of polarized signals on magnetic material is "observed." A "bit" in the form of a magnetic impulse has mass and volume. A "bit" represented on a key-punch card is a location on the card which either does or does not have a hole punched. The computer reads and acts on the bits and transforms them into the original form in which they were originally presented to the tape or disk drive when the recording took place.

The taxpayer received one or more magnetic tapes or diskettes, along with written manuals, for each purchase of software involved here. The cost of the blank medium used to transmit a copy of a program to the taxpayer is minimal in comparison to the total charge. The cost of blank diskettes would be about \$1.00 each, and the cost of blank magnetic tapes would be about \$5.00 each. The cost

of the magnetic tape(s) or diskette(s) used in transferring each purchased program to the taxpayer was not separately stated from the cost of the program.

The taxpayer is unable to demonstrate for any of the programs at issue whether it was instructed by any vendor or software producer to return any magnetic tapes or diskettes after "reading" or "loading" a program into the taxpayer's computer memory unit, or whether any such tapes or diskettes were in fact returned, retained, or destroyed.

The Commission concluded as follows:

- A. The computer software leased by the taxpayer from various vendors is not tangible personal property and is therefore not taxable under secs. 77.52(1) and 77.53, Wis. Stats.
- B. The taxpayer's lease of computer software from various vendors is not the purchase of a service enumerated in sec. 77.52(2), Wis. Stats., and is therefore not taxable under secs. 77.52(2) and 77.53, Wis. Stats.

The essence of the taxpayer's transactions under review was the lease of coded data, albeit "pre-written" or "canned," which brings it squarely within the articulated holding in *Janesville Data Center vs. Wisconsin Department of Revenue*, 84 Wis. 2d 341 (1977). In *Janesville Data*, the Wisconsin Supreme Court held that the sale of magnetic tapes which had been encoded by the seller with data furnished by the purchaser was neither the transfer of taxable tangible personal property nor the furnishing of a taxable service.

The department has appealed this decision to the Circuit Court. □

**Waste reduction and recycling.** *Ruef's Sanitary Service, Inc. vs. Wisconsin Department of Revenue* (Wisconsin Tax Appeals Commission, June 13, 1994). The issue in this case is whether the taxpayer qualifies for exemption from sales and use tax under sec. 77.54(26m), Wis. Stats. (1991-92), on its purchase of equipment used for collecting, sorting, and transporting recyclable items.

The taxpayer's principal business was the collection and disposal of rubbish and recyclables from several communities in southern Wisconsin. The taxpayer purchased two Kann Truck Side Dump Series Curb Sorters and two chassis upon which the Curb Sorters were mounted.

The two Curb Sorters were driven by the taxpayer's employees on regular routes. At curbside collection sites, the Curb Sorter operator separated recyclable items into five hydraulically operated compartments of the Curb Sorter and placed newspapers in a rack.

The taxpayer used the Curb Sorters to transport the recyclables to the taxpayer's truck yard where the recyclables were hydraulically lifted and dumped from the Curb Sorter bins into individual roll-off and yard boxes for each of the various items.

The taxpayer did not do any activity to convert the recyclables into usable items. The taxpayer sold or gave away the recyclables to others who converted the recyclables into usable products.

Section 77.54(26m), Wis. Stats., provides an exemption for "waste reduction or recycling machinery and equipment ... exclusively and directly used for waste reduction or recycling activities which reduce the amount of

solid waste generated, reuse solid waste, recycle solid waste, compost solid waste or recover energy from solid waste ...."

The Wisconsin Court of Appeals analyzed this exemption language in *Wisconsin Department of Revenue vs. Parks-Pioneer Corporation* (Court of Appeals, District IV, June 25, 1992), a case involving the taxability of, among other things, lugger and roll-off boxes used to collect scrap metal from the premises of the taxpayer's suppliers, which it then transported to its own premises for recycling and sale. The Court of Appeals determined that although the boxes were "exclusively used for recycling activities," they were *not* also "directly" used therefor because they did not perform "integral functions" in Parks-Pioneer's recycling activities since "[T]he scrap is recycled after it is collected and transported to the plant." In so ruling, the Court adopted the "integral function" test to find machinery there was "directly used" in a manufacturing process. For a summary of the Parks-Pioneer decision, see *Wisconsin Tax Bulletin* 79 (October 1992), page 16.

The Commission concluded that the taxpayer's Curb Sorters were not exempt from sales and use tax under sec. 77.54(26m), Wis. Stats. The Curb Sorters were used only "to transport the recyclables to the taxpayer's truck yard where the recyclables were ... dumped ..." and ultimately sold or given away for recycling. Although the taxpayer's Curb Sorters may have been used "exclusively" for recycling and/or waste reduction activities, they were not also used "directly" in such activities because they did not perform an "integral function" therein.

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

1. Effect of a Capital Gain Exclusion and a Capital Loss Carryover on the Credit for Income Taxes Paid to Other States (p. 15)
2. Eligibility for the State Historic Rehabilitation Tax Credit (p. 15)

### INDIVIDUAL INCOME TAXES

#### 1 Effect of a Capital Gain Exclusion and a Capital Loss Carryover on the Credit for Income Taxes Paid to Other States

**Statutes:** Section 71.07(7), Wis. Stats. (1991-92)

**Background:** Section 71.07(7)(b), Wis. Stats. (1991-92), provides that a Wisconsin resident who pays a net income tax to another state may claim a credit against the net income 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 also taxed by Wisconsin.

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:

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

**Facts and Question:** In 1993, a full-year Wisconsin resident sold real estate located in California and realized a \$30,000 long-term capital gain. The entire gain is taxable to California. The taxpayer has no other income or loss allocable to California, and paid \$1,950 of income tax to California for 1993.

For Wisconsin tax purposes, the taxpayer has a capital loss carryover of \$13,000. The net capital gain taxable to Wisconsin is as follows:

Long-term capital gain from sale of California	
real estate	\$30,000
Less capital loss carryover	<u>-13,000</u>
Net long-term capital gain	\$17,000
Less 60% capital gain exclusion	<u>-10,200</u>
Amount taxable	<u>\$ 6,800</u>

The taxpayer has other income taxable to Wisconsin and computes a Wisconsin net tax (before deducting a credit for income taxes paid to other states) of \$2,350.

May the taxpayer claim a credit on his 1993 Wisconsin income tax return for the entire \$1,950 of income tax paid to California?

**Answer:** No. Because of the capital gain exclusion, Wisconsin tax was not paid on a portion of the capital gain. Since Wisconsin did not tax the capital gain to the same extent as California, the credit for income taxes paid to other states must be computed using the above formula. The amount of capital gain taxable to Wisconsin is \$19,800 (\$13,000 which is offset by the capital loss carryover, plus \$6,800 which is taxable after the capital gain exclusion is applied). The allowable credit for taxes paid to California is \$1,287, computed as follows:

$$\frac{\$19,800}{\$30,000} \times \$1,950 = \$1,287$$

#### 2 Eligibility for the State Historic Rehabilitation Tax Credit

**Statutes:** Section 71.07(9r), Wis. Stats. (1991-92), and as affected by 1993 Wisconsin Acts 16 and 471

**Background:** The state historic rehabilitation tax credit is available to natural persons for 25% of the costs of preserving or rehabilitating certain historic property located in Wisconsin. Sec. 71.07(9r)(a), Wis. Stats. The costs must be incurred and the claim must be submitted by the owner of the historic property. Sec. 71.07(9r)(b)1, Wis. Stats. The historic property must be an owner-occupied personal residence. Sec. 71.07(9r)(b)2, Wis. Stats. The expenditures for preservation or rehabilitation of the historic property must exceed \$10,000. Sec. 71.07(9r)(b)5, Wis. Stats.

**Facts and Question:** Corporation C is a residential housing cooperative which owns 10 contiguous single-family owner-occupied residential units. The property is listed on the National Register of Historic Places. The cooperative had been formed 70 years ago by the 10 owners of the residential units for the purpose of ensuring that all exterior maintenance, preservation, and renovation would be determined by a 7/10 vote of the owners and would apply to all the units as a whole.

The sale and purchase of a unit is individually negotiated at market

price, at which time the purchaser receives one share of no-par value stock which entitles the owner to one vote on corporate matters and a renewable 3-year lease to occupy the purchased unit.

Corporation C has incurred more than \$10,000 of costs for rehabilitating the historic property.

Assuming the rehabilitation costs are qualifying expenditures, may the shareholders of Corporation C claim the state historic rehabilitation tax credit?

**Answer:** No, the shareholders of Corporation C may not claim the state historic rehabilitation tax credit. Since the shareholders only lease their residential units from Corporation C, which is the owner of the property, the shareholders are not entitled to the credit even though each owns a 1/10 interest in the corporation. Since Corporation C, the owner of the property, is not a "natural person," Corporation C may not claim the credit either.



## Private Letter Rulings

"Private letter rulings" are written statements issued to a taxpayer by the department that interpret Wisconsin tax laws to the taxpayer's specific set of facts. Any taxpayer may rely upon the ruling to the same extent as the requestor, provided the facts are the same as those set forth in the ruling.

The number assigned to each ruling is interpreted as follows: The "W" is for "Wisconsin," the first two digits are the year the ruling becomes available for publication (80 days after the ruling is issued to the taxpayer), the next two digits are the week of the year, and the last three digits are the number in the series of rulings issued that year. The date following the 7-digit number is the date the ruling was mailed to the requestor.

Certain information contained in the ruling that could identify the taxpayer requesting the ruling has been deleted. Wisconsin Publication 111, "How to Get a Private Letter Ruling From the Wisconsin Department of Revenue," contains additional information about private letter rulings.

The following private letter rulings are included:

### Individual Income Taxes

Retirement pay — situs of income

Penalties — retirement plan distributions

W9431005, May 9, 1994

(p. 16)

Retirement pay — situs of income

W9431006, May 9, 1994

(p. 18)

### Sales and Use Taxes

Exemptions — advertising materials used out-of-state

W9431004, May 5, 1994

(p. 19)



**W9431005, May 9, 1994**

### Type Tax: Individual Income

**Issue:** Retirement pay — situs of income; Penalties — retirement plan distributions

**Statutes:** Sections 71.04(1)(a) and 71.83(1)(a)6, Wis. Stats. (1991-92)

**Wis. Adm. Code:** Section Tax 3.085, Wis. Adm. Code (June 1990 Register)

This letter is in response to your request for a private letter ruling regarding the Wisconsin taxability of and early withdrawal penalty for a distribution from a retirement plan, based on Mr. B's employment while he was not a legal resident of Wisconsin.

### Facts

In September 1992, you relocated to Wisconsin from another state. Shortly after relocating to Wisconsin, Mr. B requested that the funds from his previous employer's retirement plan under Internal Revenue Code (IRC) §401(k) be distributed directly to him. The reason he withdrew the money was to enable you to purchase a home.

Even though the money was requested from Mr. B's previous employer in September 1992, he did not actual-



ly receive the check from the previous employer until January 1993.

The payment was reported as income on your joint 1993 Wisconsin income tax return. In addition to the Wisconsin income taxes you paid on that amount, you also paid to Wisconsin a penalty for the early withdrawal from an IRC sec. 401(k) plan. Mr. B's age at the time of the withdrawal was 27 years.

Until you began preparing your 1993 Wisconsin income tax return, you were not aware that the money would be considered taxable to Wisconsin, since none of the money was actually earned in Wisconsin. You were advised that the reason it was taxable income was because the income was received in 1993, when Mr. B was a full-year Wisconsin resident.

### Ruling Request

You request a ruling that:

- A. The distribution from Mr. B's previous employer's IRC sec. 401(k) retirement plan is not taxable for Wisconsin income tax purposes.
- B. The distribution is not subject to a Wisconsin penalty for an early withdrawal from an IRC §401(k) plan.

### Ruling

- A. Since Mr. B was a legal resident of Wisconsin at the time he received the distribution from his previous employer's retirement plan, and since the payment is presumably taxable for federal income tax purposes, the distribution is taxable for Wisconsin income tax purposes (sec. 71.01(6)(h), Wis. Stats., as created by 1993 Wisconsin Act 16, and sec. 71.04(1)(a), Wis. Stats. (1991-92)).

- B. Since the income Mr. B received is not exempt from Wisconsin taxation, the distribution is subject to a Wisconsin penalty of 33% of the federal early withdrawal penalty imposed under the Internal Revenue Code (sec. 71.83(1)(a)6, Wis. Stats. (1991-92)).

### Analysis

#### A. Taxability

Section 71.04(1)(a), Wis. Stats. (1991-92), provides that all income or loss of resident individuals shall follow the residence of the individual. This statute is further interpreted in an administrative rule, sec. Tax 3.085, Wis. Adm. Code, June 1990 Register. This administrative rule provides that employee annuity, pension, profit-sharing, or stock bonus plan distributions, including distributions from qualified deferred compensation plans under sec. 401(k) and other sections of the Internal Revenue Code, received by a person while a resident of Wisconsin shall be subject to the Wisconsin income tax, *regardless of whether any of these distributions may be attributable to personal services performed outside of Wisconsin*.

Therefore, even though none of the funds came from earnings or employment within Wisconsin, Mr. B's retirement plan distribution is taxable to Wisconsin because the funds were received while he was a legal Wisconsin resident, and the funds were a distribution from a qualified deferred compensation plan under IRC sec. 401(k).

Wisconsin generally follows the federal Internal Revenue Code in determining what income is taxable to Wisconsin. While

your letter did not specifically state that the distribution is taxable for federal income tax purposes, it is presumed to be taxable federally, based on the facts presented in your letter. Therefore, the amount of the distribution from Mr. B's retirement plan which is presumably taxable on the 1993 federal income tax return is also taxable on the 1993 Wisconsin income tax return (sec. 71.01(6)(h), Wis. Stats., as created by 1993 Wisconsin Act 16).

Your statement that the distribution would not have been taxable to Wisconsin if Mr. B had received the payment prior to becoming a Wisconsin resident is correct. However, this is not the case since he received the distribution after he became a legal resident of Wisconsin.

Your statement that the distribution would not have been taxable to Wisconsin if Mr. B had received the payment in 1992 after becoming a legal Wisconsin resident, because he was not a full-year Wisconsin resident in 1992, is not correct. A taxpayer's Wisconsin residency status at the time income is received determines the Wisconsin taxability. A distribution received in 1992 after becoming a legal Wisconsin resident would be taxable in 1992.

The taxes you paid to the state you previously resided in (sales taxes, automobile license fees and taxes, etc.) have no bearing on your Wisconsin income tax liability. If that state had a state income tax and the distribution was subject to its income tax, you may have been eligible for a credit against Wisconsin income taxes for the other state's income taxes you paid. However, this is not the case.

## B. Penalty

Section 71.83(1)(a)6, Wis. Stats. (1991-92), provides that individuals who are liable for a federal penalty for an early distribution from a qualified retirement plan are liable for 33% of the federal penalty for Wisconsin income tax purposes, unless the income is not taxable to Wisconsin. While your letter did not specifically state that you were liable for the federal penalty, the facts presented in your letter indicate that the federal penalty did apply, and based on that presumption the Wisconsin penalty also applies. The federal penalty is 10% of the distribution, and 33% of that amount is the Wisconsin penalty. □

✱ **W9431006**, May 9, 1994

### Type Tax: Individual Income

**Issue:** Retirement pay — situs of income

**Statutes:** Section 71.04(1)(a), Wis. Stats. (1991-92)

**Wis. Adm. Code:** Section Tax 3.085, Wis. Adm. Code (June 1990 Register)

This letter is in response to your request for a private letter ruling regarding the Wisconsin taxability of a distribution from an employee stock ownership plan, based on employment while you were not a legal resident of Wisconsin.

### Facts

For nine years, from 1983 to 1992, you worked as an editor for Company C, a division of TUV Corporation (TUV) located in another state. As an employee of TUV, you were a participant in that company's

employee stock ownership plan (ESOP). One provision of the ESOP is that TUV's annual ESOP contribution is made only if the employee is employed through the end of TUV's fiscal year, which is September 30.

For the entire period of your employment at TUV, you were a resident of another state. You terminated your employment at TUV as of October 9, 1992, sold your home, and moved to Wisconsin later that month to join your wife. She had moved to Wisconsin in 1991.

Although the date for determining your ESOP account balance was September 30, 1992, you did not actually receive your distribution until April 1993, since it takes TUV several months to perform necessary calculations and paper work and mail out the distribution checks. The amount of the distribution was reduced for "taxes," and the balance was issued to you by a check dated April 12, 1993. You realized when you began preparing your 1993 Wisconsin income tax return in April 1994, that you may be subject, at least by the letter of the law, to Wisconsin taxation on the ESOP distribution.

### Ruling Request

You request a ruling that the distribution from your ESOP account with TUV is not taxable for Wisconsin income tax purposes, since it was entirely attributable to work done in another state while you were not a legal resident of Wisconsin.

### Ruling

Since you were a legal resident of Wisconsin at the time you received the distribution from your previous employer's retirement plan, and since the amount is presumably taxable for federal income tax purposes, the distribution is taxable for Wisconsin income tax purposes (sec.

71.01(6)(h), Wis. Stats., as created by 1993 Wisconsin Act 16, and sec. 71.04(1)(a), Wis. Stats. (1991-92)).

### Analysis

Section 71.04(1)(a), Wis. Stats. (1991-92), provides that all income or loss of resident individuals shall follow the residence of the individual. This statute is further interpreted in an administrative rule, sec. Tax 3.085, Wis. Adm. Code, June 1990 Register. This administrative rule provides that employee annuity, pension, profit-sharing, or stock bonus plan distributions, including distributions from qualified employee stock ownership plans under sec. 401 of the Internal Revenue Code, received by a person while a resident of Wisconsin shall be subject to the Wisconsin income tax, *regardless of whether any of these distributions may be attributable to personal services performed outside of Wisconsin.*

Therefore, even though none of your funds came from earnings or employment within Wisconsin, your retirement plan distribution is taxable to Wisconsin because you received the funds while you were a legal Wisconsin resident, and the funds were a distribution from a qualified plan under IRC sec. 401.

Wisconsin generally follows the federal Internal Revenue Code in determining what income is taxable to Wisconsin. While your letter did not specifically state that the distribution is taxable for federal income tax purposes, it is presumed to be taxable federally, based on the facts presented in your letter. Therefore, the amount of the distribution from your retirement plan which is presumably taxable on your 1993 federal income tax return is also taxable on your 1993 Wisconsin income tax return (sec. 71.01(6)(h), Wis. Stats., as created by 1993 Wisconsin Act 16).

Your statement that the distribution would not have been taxable to Wisconsin if you had received the payment prior to becoming a Wisconsin resident is correct. However, this is not the case since you received the distribution after you became a legal resident of Wisconsin.

The Wisconsin Tax Appeals Commission and Wisconsin Courts have ruled in a number of cases that income, including personal service income, pensions, deferred compensation, retirement plans, etc., received by Wisconsin residents is taxable to Wisconsin, regardless of where the services that generated the income were performed. In addition, a private letter ruling, #W9329003, was issued on April 28, 1993, affirming this position. □

✱ **W9431004**, May 5, 1994

**Type Tax:** Sales and Use

**Issue:** Exemptions — advertising materials used out-of-state

**Statutes:** Section 77.54(25), Wis. Stats. (1991-92)

This letter responds to your request for a private letter ruling regarding the sales and use tax treatment of advertising brochures.

#### Facts

XYZ Corporation (XYZ) contracted with Taxpayer A, a Wisconsin sole proprietorship, for the production and distribution of advertising brochures.

Taxpayer A contracted with Company W, an out-of-state company with a business location in Wisconsin, to print and distribute the advertising brochures. Company W had the brochures printed by both Wisconsin and

out-of-state printers which were combined with advertising materials of other persons to form a multiple page advertising "magazine." The printers delivered the advertising "magazine" to Company W outside Wisconsin. Company W mailed the advertising magazine from a location outside Wisconsin to XYZ customers outside Wisconsin.

#### Request

You ask the following:

1. Is the charge by Company W to Taxpayer A for the printing and distribution of advertising brochures which are mailed to XYZ customers outside Wisconsin subject to Wisconsin sales or use tax?
2. Is the charge by Taxpayer A to XYZ for the sale and distribution of the advertising brochures subject to Wisconsin sales or use tax?

#### Ruling

1. The charge by Company W to Taxpayer A for the printing and distribution of advertising brochures for XYZ is not subject to Wisconsin sales or use tax because the advertising brochures are for resale to Taxpayer A.
2. The charge by Taxpayer A to XYZ for the sale and distribution of the advertising brochures is not subject to Wisconsin sales or use tax because the advertising brochures, as part of an advertising "magazine" are distributed outside Wisconsin for use solely outside Wisconsin in advertising XYZ products.

#### Analysis

Section 77.51(14)(intro.), Wis. Stats. (1991-92), provides that sale at retail

for purposes of imposing Wisconsin sales or use tax includes the transfer of the ownership of, title to, possession of, or enjoyment of tangible personal property or services for use or consumption but not for resale as tangible personal property or services.

Company W is selling and distributing advertising brochures to Taxpayer A which Taxpayer A will resell to XYZ. The sale by Company W to Taxpayer A is not a sale at retail and, therefore, Wisconsin sales or use tax does not apply to the transaction. Taxpayer A should provide Company W with a properly completed resale certificate.

Section 77.54(25), Wis. Stats. (1991-92), provides an exemption from Wisconsin sales or use tax for gross receipts from the sale of and the storage of printed material which is designed to advertise and promote the sale of merchandise, or to advertise the services of individual business firms, which printed material is purchased and stored for the purpose of subsequently transporting it outside the state by the purchaser for use thereafter solely outside the state.

The advertising brochures sold by Taxpayer A to XYZ are designed to advertise the products of XYZ and are transported outside Wisconsin for use solely outside Wisconsin. Therefore, the charge by Taxpayer A for the advertising brochures is exempt from Wisconsin sales or use tax. XYZ should provide Taxpayer A with a Certificate of Exemption (Form S-207) indicating that all of the advertising brochures are exempt because they are transported outside Wisconsin for use solely outside Wisconsin in advertising XYZ products. □