The Commission concluded that during the period involved the claimant was deemed to have an ownership interest of only 50% in the homestead in question, as record title was held jointly by her with her adult son. The department acted properly when it adjusted the claimant's 1982 property taxes accrued to 50% of the tax bill on the homestead plus 25% of the remaining 50% of the 1982 tax bill as rent constituting property taxes accrued.

The claimant has not appealed this decision.

Alice L. Szymczyk vs. Wisconsin Department of Revenue (Wisconsin Tax Appeals Commission, January 29, 1985). The only issue pending before the Commission is whether the claimant, who resided in a nursing home and received medical assistance under Title XIX at the time she filed her 1983 homestead credit claim, is entitled to a homestead credit refund for 1983.

The claimant filed a 1983 homestead credit claim and attached a real estate tax bill addressed to John Szymczyk at 1901 Hamilton Street, Manitowoc, Wisconsin. The claimant claims that she paid the real estate taxes in 1983.

On December 23, 1983, the claimant entered the Park Lawn Nursing Home. While residing in the nursing home, she received medical assistance under Title XIX. The claimant filed her 1983 homestead claim while a resident of the nursing home.

The Commission held that the claimant is not eligible for homestead credit for 1983 because at the time she filed for the credit she resided in a nursing home and was receiving medical assistance under Title XIX.

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

Individual Income Taxes

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INDIVIDUAL INCOME TAXES

1. Political Contributions

Statutes: section 71.02(2)(b), 1983 Wis. Stats.

Facts: Taxpayer A contributes a painting to the campaign fund of a political candidate. The painting has a fair market value of $100. The campaign committee immediately sells the painting in a fund raising auction to Taxpayer B for $130.

Question 1: For Wisconsin purposes, may Taxpayer A claim a deduction for a political contribution?

Answer 1: No, Taxpayer A may not claim a deduction for the contribution of the painting. Only contributions or gifts of money may be deducted. Wisconsin follows the federal Internal Revenue Code Section 218, as it existed immediately prior to its repeal in 1978. Section 218 allowed as a deduction any political contribution, which was defined in Code Section 41(c)(1) as "a contribution or gift of money to ...."

Question 2: Are there any tax consequences to Taxpayer A as a result of donating the painting?

Answer 2: Yes, under Section 84 of the Internal Revenue Code, the contribution must be treated as a sale. Taxpayer A is considered to have realized an amount equal to the fair market value of the painting at the time of transfer. If the fair market value exceeds Taxpayer A's basis in the painting, short or long term capital gain is realized. If Taxpayer A's basis is greater than the fair market value, the loss is not deductible.

Question 3: For Wisconsin purposes, may Taxpayer B claim a deduction for a political contribution?

Answer 3: Yes, Taxpayer B may claim a deduction of $30. The fair market value of the painting is $100. If Taxpayer B pays $130 for the painting, Taxpayer B may deduct $30 ($130 purchase price minus the $100 actual value of the asset acquired).

Question 4: If the painting is not immediately resold, how would the political contribution be determined?

Answer 4: The amount of political contribution is dependent upon the fair market value of the painting at the time

of purchase from the political organization. If the amount paid for the painting is greater than the fair market value determined at the time of purchase, the excess is considered a political contribution.

2. Taxability of Layoff Benefits

Statutes: section 71.02(2)(b), 1983 Wis. Stats.

Facts and Question: Under Section 14 of the Wisconsin State Employes Collective Bargaining Agreement a laid off employe, upon written request at the time of layoff, may have his or her accumulated unused sick leave converted to cash at the current base pay rate for credits to be used to pay health insurance premiums during the time of the layoff. The employer will make the premium payments directly to the insurer. Premium payments will expire at the earlier of five years from the date of layoff or the first of the month following the employe's acceptance of any other employment. At the time of reinstatement or recall, unused cash credits will be reconverted to sick leave at the same rate for the original conversion and restored to the employe's sick leave account.

Are these payments of health insurance premiums considered taxable income to the employe for federal and state income tax purposes?

Answer: No, the employer's payment of health insurance premiums through conversion of accumulated sick leave under the WSEU Collective Bargaining Agreement is not taxable income.

In s. 71.02(2), 1983 Wis. Stats., Wisconsin adjusted gross income is defined as federal adjusted gross income, with certain prescribed modifications. Internal Revenue Code Section 61 provides that gross income means all income from whatever source derived, including compensation for services, unless specifically exempt. Gross income does not include the employer's contributions to accident or health plans for compensation (through insurance or otherwise) to employes for personal injuries or sickness, pursuant to Section 106 of the Internal Revenue Code.

Federal Revenue Ruling 75-539 discusses the tax treatment of medical insurance premiums paid for a retired employe in two situations. In the first situation, the employe has the option upon retirement to receive a cash payment for accumulated sick leave or to have the payment applied to the cost of health insurance. The amount of the cash payment which the employe is entitled to receive is considered taxable income at the time available to the employe, whether paid in cash or used to continue medical insurance coverage. In the second situation, the unused sick leave credits may be used to pay insurance premiums, but under no circumstances may the employe or the employe's spouse or dependents receive any of the amount in cash. Any amount not spent for health insurance premiums reverts to the employer. Such amounts are not considered constructively received by the employe, but are contributions by the employer to the health plan. These payments are excludable from taxable income.

Section 14 of the WSEU Collective Bargaining Agreement does not grant laid off employes the right to receive cash over which they have complete control. Because the employer makes premium payments directly to the insurer, the continuation of health insurance premiums is similar to the sick leave provision in the second situation discussed in Revenue Ruling 75-539. The cash value of the accumulated unused sick leave credits that are used by the employer to pay the health insurance premiums of the laid off employes qualifies as excludable income under Section 106 of the Internal Revenue Code.

3. Taxability of Railroad Retirement Benefits

Statutes: section 71.03(2), 1983 Wis. Stats.

Facts and Question: The enactment of the Social Security Amendments Act of 1983 (Public Law 98-21, April 20, 1983) made a portion of social security benefits subject to federal income taxes in certain situations. Section 231m of Title 45 of the United States Code was amended by Congress during 1983 to make some railroad retirement benefits equivalent to social security benefits and thus subject to federal tax. No provision in federal law prohibits state and local governments from taxing social security benefits.

Can Wisconsin impose an income tax on amounts of railroad retirement benefits which are taxable for federal income tax purposes in certain situations?

Answer: No, railroad retirement benefits are exempt from Wisconsin income tax. Section 231m of the United States Code continues to bar state and local taxation of railroad retirement benefits. On a 1984 Form 1, the Tier 1 railroad retirement benefits included in federal adjusted gross income are removed from Wisconsin taxable income when Columns B and C of line 14 are completed. Tier 2 or supplemental railroad retirement benefits included in federal adjusted gross income are subtracted from federal income on line 34 on a 1984 Form 1.

4. Treatment of Gain on Involuntarily Converted Property Replaced Outside Wisconsin

Statutes: sections 71.02(2)(b) and 71.05(1)(a)6, 1983 Wis. Stats.

Facts and Question: Section 1033 of the federal Internal Revenue Code (IRC) allows for postponement of recognition of gain on an involuntary conversion of property when replacement property is purchased within a specified period of time. Wisconsin, because of its reference to the definition of the IRC in s. 71.02(2), 1983 Wis. Stats., follows the provisions of the IRC unless an exception is noted.

Thus s. 71.02(2), 1983 Wis. Stats., allows the postponement of recognition of gain realized from the involuntary conversion of property by a Wisconsin resident, whether the replacement property is located within or outside of Wisconsin. Under s. 71.02(2), 1983 Wis. Stats., the deferral of gain on an involuntary conversion of property by a nonresident individual, estate or trust is also allowable when the replacement property is located in Wisconsin.

An exception to Section 1033 of the IRC is provided by s. 71.05(1)(a)6, 1983 Wis. Stats. Section 71.05(1)(a)6, 1983 Wis. Stats., provides an add modification by nonresident individuals, estates or trusts for the gain on the involuntary conversion of Wisconsin property excluded under Section

1033 of the IRC if the replacement property is located outside the State of Wisconsin.

Example: On June 30, 1983 a taxpayer received $10,000 for involuntarily converted property with a basis of $7,500. The taxpayer became a resident of Illinois on September 15, 1983 and purchased replacement property in Illinois on April 1, 1984 for $11,000.

Can the recognition of the $2,500 gain ($10,000 less $7,500 cost basis) from the involuntary conversion be postponed for Wisconsin income tax purposes?

Answer: Yes, recognition of gain on the involuntary conversion may be postponed for Wisconsin income tax purposes under s. 71.02(2), 1983 Wis. Stats. An add modification under s. 71.05(1)(a)6, 1983 Wis. Stats., is not required to include the gain in Wisconsin taxable income. The taxpayer's residency at the time the gain was realized is the controlling factor, not the taxpayer's residency at the time of replacement. As long as the taxpayer is a Wisconsin resident when the gain is realized, the gain on the involuntary conversion can be deferred as long as the taxpayer adheres to the provisions of Section 1033 of the IRC. (NOTE: If the taxpayer is a nonresident when the gain is realized, an add modification is required under s. 71.05(1)(a)6, 1983 Wis. Stats., to include the gain in Wisconsin taxable income.)

CORPORATION FRANCHISE/INCOME TAXES

1. Assessments by Wisconsin Public Service Commission

Statutes: section 71.04(2)(a), 1983 Wis. Stats.

Facts and Question: The Wisconsin Public Service Commission (PSC) is supported by all the public utilities, power districts and sewerage systems which it regulates. Under s. 196.85, 1983 Wis. Stats., the PSC bills these utilities directly for the cost of investigations, appraisals, and engineering or accounting services which it renders for them. At the end of each year the PSC assesses the public utilities, power districts and sewerage systems for the costs attributable to regulation but not directly related to any one utility. This assessment is called a remainder assessment and is based on the gross receipts of each utility.

Is the remainder assessment under s. 196.85(2), 1983 Wis. Stats., deductible on a Wisconsin franchise/income tax return of a regulated utility corporation?

Answer: Yes, the remainder assessment is deductible as an ordinary expense of doing business for a regulated utility corporation (s. 71.04(2)(a), 1983 Wis. Stats.). While the remainder assessment is based on gross receipts, it is not a tax; it is a fee imposed primarily to cover the cost and expense of regulation.

2. Nexus for Foreign Corporations Holding Wisconsin Partnership Interests

Statutes: sections 71.07(1m) and (2), 1983 Wis. Stats.

Wis. Adm. Code: sections Tax 2.39 and 2.82, September 1983 Register

Facts: Wis. Adm. Code section Tax 2.82 establishes certain activities of foreign corporations which constitute nexus for Wisconsin franchise/income purposes. Some of the more frequently encountered activities stated in the rule are maintenance of any business location in Wisconsin, including any kind of office, and ownership of real estate in Wisconsin.

Wis. Adm. Code section Tax 2.39 states that any person doing business both in and outside Wisconsin shall report by the statutory apportionment method when the person's business in this state is an integral part of a unitary business unless the department, in writing, allows reporting on a different basis.

Question 1: A general partnership has a sales office in Wisconsin. One of the partners is a corporation incorporated in a state outside Wisconsin. Does the partnership's sales office establish nexus with Wisconsin for the foreign corporation?

Answer 1: Yes. All partners, including the corporation, must file Wisconsin franchise/income tax returns and report their share of the partnership income.

Question 2: Foreign Corporation X is a member of a Wisconsin partnership with a sales office in Wisconsin which is an integral part of the corporation's unitary business. Can Corporation X use separate accounting to report its share of the Wisconsin net income from the operation of the Wisconsin partnership?

Answer 2: No. Because the Wisconsin partnership operation is a part of the corporation's unitary business operation, Corporation X must combine its share of the partnership income with the income from its regular business operations and use the statutory apportionment formula to determine Wisconsin net income.

3. "No Tax Change" Field Audits

Statutes: sections 71.09(13)(a), 71.10(10), 71.11(20) and (21)(a) and 71.12, 1983 Wis. Stats.

Background: The Wisconsin Board of Tax Appeals held in the case of *Superior Water, Light and Power Company* (1 WBTA 274) that a "no tax letter' is not considered an additional assessment under Chapter 71 of the Wisconsin Statutes. It also indicated in its *Amber, Inc.* (2 WBTA 571) decision that an adjustment to a net business loss is not an additional assessment in the year of the net business loss. As a result of these cases, a field audit (s. 71.11(20), 1983 Wis. Stats.) does not finalize the tax or income shown on the return or audit report if a no change letter is issued or if business losses are adjusted but no additional tax is assessed. Such years do not become final and conclusive as a result of a field audit. Rather, these years may be later adjusted by the taxpayer or the department within the statute of limitations, or a refund may be claimed for such no change years as long as it also is within the statute of limitations. A net business loss, for carryover purposes, may be adjusted for years beyond the statute of limitations as long as the income year against which it is used is open to adjustment.

Net Business Loss Offsets

Question 1: Is a notice sent to a taxpayer pursuant to a field audit indicating "no tax change" in one year and an adjustment to the net business loss of another year considered an additional assessment or correction of assess-

ment per s. 71.11(21)(a), 1983 Wis. Stats., for either of those years?

Answer 1: No. A "no tax letter" is not considered an additional assessment (*Superior Water, Light and Power Company*) and an adjustment to a net business loss is not an additional assessment in the year of the net business loss (*Amber, Inc.*).

Question 2: Are the "no tax change" for one year and the adjustment to the net business loss of another year appealable under s. 71.12, 1983 Wis. Stats., or any other statute?

Answer 2: No. A taxpayer may not seek the appeal remedies specified in s. 71.12, 1983 Wis. Stats., because the relief provided therein is available only to those who are aggrieved by an assessment, refund or notice of denial of refund. Such would not be the case here (this was cited by the Wisconsin Board of Tax Appeals in the *Superior Water, Light and Power Company* case).

Question 3: Is the income as reported in the "no tax change" year and the adjusted net business loss as shown on the audit report of another year considered to be final and conclusive under s. 71.12, 1983 Wis. Stats., or any other statute?

Answer 3: The Wisconsin Board of Tax Appeals ruled in the *Superior Water, Light and Power Company* case that the "no tax letter" is not provided for in the statutes nor does it operate with the same legal finality as does an additional assessment. Thus, the income reported in the "no tax change" year and the net business loss as determined by the department in the audit report may be adjusted at a later date by both the taxpayer and the department as indicated above.

Question 4: If both the taxpayer and the department may adjust the business loss as shown in the "no tax change" audit report, may adjustments be made to items shown in the audit report or only to items not included in the audit report?

Answer 4: Because there are no appeal remedies available to a taxpayer in a year that a net business loss is adjusted and because such a year does not become final and conclusive as a result of a field audit, adjustments may be made by both the taxpayer and the department to items shown in the audit report as well as to other items.

Question 5: If the department conducted a field audit of a taxpayer and the department made an assessment for one or more years audited but the final year of the audit was a loss year both before and after adjustments, may the department or the taxpayer further adjust the loss year in a subsequent year in which the loss is carried forward?

Answer 5: Yes. Under the principles set forth in *Amber, Inc.* (2 WBTA 571) a net business loss may be adjusted for a year beyond the statute of limitations as long as the income year against which it is used is open to adjustment.

Claim for Refund

Question 6: If the department conducted a field audit of a taxpayer and the department made no adjustment in one or more years audited, may the taxpayer file a claim for refund for the "no tax change" year(s) after the field audit has been concluded and department notification has been received?

Answer 6: Yes. In the *Superior Water, Light and Power Company* case, the Board of Tax Appeals ruled that a "no tax letter" sent by the department to the taxpayer at the conclusion of a field audit did not have the effect of barring the taxpayer's claim for refund of taxes within s. 71.10(10), 1983 Wis. Stats., since the letter was not a notice of an additional assessment within Chapter 71 of the Wisconsin Statutes.

Question 7: If the department conducted a field audit of a taxpayer for income or franchise taxes and made adjustments for all but the last year audited, may the taxpayer at some later date file a claim for refund (or the department make an assessment) for the last ("no tax change") year of the audit even though the field audit assessment has become final and conclusive?

Answer 7: Yes. If no timely petition for redetermination was filed, the years assessed would have become final and conclusive. However, the last year audited resulted in a "no tax change" and would not operate with the same legal finality as a year assessed (*Superior Water, Light and Power Company*).

Manufacturer's Sales Tax Credit

Question 8: Is a notice sent to a taxpayer pursuant to a franchise or income tax field audit indicating no change in tax in the years audited but reducing the manufacturer's sales tax credit carryforward to unaudited future years considered an additional assessment or correction of assessment under s. 71.11(21)(a), 1983 Wis. Stats.?

Answer 8: No. Pursuant to the *Superior Water, Light and Power Company* and *Amber, Inc.* cases, an "additional assessment" requires an assessment of tax liability greater than that reported.

Question 9: Is the reduction in the manufacturer's sales tax credit carryforward with no change in tax liability in the years field audited considered appealable under s. 71.12, 1983 Wis. Stats., or any other statute?

Answer 9: No. A taxpayer would have no reason to seek the appeal remedies specified in s. 71.12, 1983 Wis. Stats., because the relief provided therein is available only to those who are aggrieved by an assessment, refund or notice of denial of refund.

Question 10: Is the adjusted manufacturer's sales tax credit carryforward in Question 8 considered to be final and conclusive under s. 71.12, s. 71.10(10)(d), 1983 Wis. Stats., or any other statute?

Answer 10: No. In the *Superior Water, Light and Power Company* case, the Board of Tax Appeals ruled that "the no tax letter is not provided for nor does it operate with the same legal finality as does an additional assessment". Similarly, an adjustment to the manufacturer's sales tax credit carryforward, which is not considered an additional assessment, is not considered to be final and conclusive. The manufacturer's sales tax credit as determined by the department in the audit report may be adjusted at a later date within the statute of limitations by both the department and the taxpayer.

Farmland Preservation and Homestead Credits

Question 11: A notice is sent to a taxpayer pursuant to field audit indicating no change in the tax liability for a particular tax year but recovering a portion of the farmland preservation credit or homestead credit. (A) Is the income re-

ported in that tax year considered to be final and conclusive under s. 71.09(13)(a), s. 71.10(10)(d), 1983 Wis. Stats., or any other statute? (B) Is the farmland preservation credit or homestead credit as determined by the department considered to be final and conclusive if there was no timely appeal of the determination for the recovery of the farmland preservation credit or homestead credit?

Answer 11: (A) In accordance with the *Superior Water, Light and Power Company* case, there is no finality to the income because there was no "additional income or franchise tax assessment" under Chapter 71 of the statutes. (B) If no timely petition for redetermination of the farmland preservation credit or homestead credit is filed, the department's determination of the credit is final and conclusive under s. 71.90(13)(a), 1983 Wis. Stats.

4. Wisconsin Treatment of Foreign Sales Corporations and Domestic International Sales Corporations

Statutes: sections 71.04(4) and 71.11(7r), 1983 Wis. Stats.

Background: Under the Tax Reform Act of 1984 the system of Domestic International Sales Corporations (DISCs) will generally be replaced after December 31, 1984 with a new system of Foreign Sales Corporations (FSCs). Under the FSC system, a portion of the foreign trade income of an FSC will be exempt from federal tax at the corporate level, provided it is derived from the foreign presence and economic activity of the FSC. In contrast, under the DISC system there is no corporate income tax imposed on DISC income, and there is a partial deferral of taxes at the shareholder level. Although DISCs are not abolished by the Act, their tax benefits are limited and an interest charge for tax deferred amounts is imposed on DISC shareholders.

To qualify as an FSC, a corporation must meet six requirements designed to ensure that it has adequate foreign presence. If a corporation meets all six requirements, and makes an election that complies with the procedural requirements of section 927(f)(i) of the Internal Revenue Code, it will be treated as an FSC by the Internal Revenue Service. The six requirements are:

A. The FSC must be a foreign corporation created or organized under the laws of a qualified foreign country.

B. The FSC must not have more than 25 shareholders.

C. The FSC may not have any preferred stock.

D. The FSC must maintain an office located outside the United States (or in any U.S. possession) at which there is a permanent set of tax records, including invoices.

E. The board of directors of an FSC must always include at least one individual who is not a resident of the United States.

F. An FSC cannot be a member of any controlled group of corporations of which a DISC is a member.

In lieu of forming FSCs, taxpayers may continue to use their DISCs for annual export receipts up to $10 million. DISCs that continue in existence or are formed after 1984 will be known as "interest-charge" DISCs. As with other DISCs, their accumulated DISC income through 1984 will be exempt from federal tax. Most of the former DISC rules will continue to apply, including the gross receipts and assets tests. However, the former "incremental rule" will not apply, and the deemed distribution of DISC income is reduced from one-half to one-seventeenth.

Therefore, most DISC income after December 31, 1984 may be deferred for federal tax purposes although the shareholders of DISCs will be required to pay an interest charge on the deferred tax, the rate of which will be determined annually by the United States Treasury based on Treasury bill yields. The year-end of the FSC or an interest-charge DISC must conform to the year-end of its shareholder. If there is more than one shareholder, the year-end must conform to the year-end of the majority shareholder or the year-end of one of the shareholders owning equal highest percentage interests in the stock of the FSC or DISC.

This new federal legislation terminates the old DISC provisions as of December 31, 1984. A special transition rule treats distributions after January 1, 1985 as nontaxable amounts paid from previously taxed income of the DISC. Thus, the deferred tax liability is forgiven for federal income tax purposes.

Question 1: What is the Wisconsin treatment of FSCs?

Answer 1: Since the Wisconsin statutes contain no special provisions for FSCs, the net income of an FSC will not be subject to the combining provisions of s. 71.11(7r), 1983 Wis. Stats. The net income of an FSC is not to be combined with its parent or affiliate; it will be subject to Wisconsin taxation as a separate corporation provided it has nexus in Wisconsin.

Question 2: What is the Wisconsin treatment of interest-charge DISCs?

Answer 2: The net income of the newly created interest-charge DISC will also be subject to Wisconsin taxation as a separate corporation if the DISC has Wisconsin nexus. Since this type of DISC does not have the meaning specified in section 992 of the Internal Revenue Code, as amended to December 31, 1979, its net income also is not subject to the combining provisions of s. 71.11(7r), 1983 Wis. Stats.

Question 3: The Tax Reform Act of 1984 provides that as of December 31, 1984 the accumulated income of a DISC will be deemed previously taxed income and will be exempt from federal tax liability. Assume a corporation has a fiscal year ending October 31, 1985 and has a 100% owned DISC. Can this corporation deduct under s. 71.04(4)(b), 1983 Wis. Stats., 100% of any DISC dividends to be issued in January, 1985 or subsequently?

Answer 3: Yes, the corporation can under s. 71.04(4)(b), 1983 Wis. Stats., deduct 100% of any DISC dividends issued in January, 1985 or subsequently.

Since the Wisconsin statutes do not contain a provision similar to the federal provision which deems all accumulated DISC income to be previously taxed income exempt from tax after December 31, 1984, the distribution of such income will be taxed as dividends for Wisconsin corporation tax purposes, to the extent not excludable under s. 71.11(7r), 1983 Wis. Stats.

All dividends received from a DISC that are not excludable under s. 71.11(7r), 1983 Wis. Stats., may, however, be de-