

Dragonwood Pub & Cafe, which was accepted by the taxpayer. On April 13, 1983, the seller, Egg Plant, Inc., and the buyer, Gregory L. Vallee, closed the transaction and the taxpayer purchased the business assets of the seller, Egg Plant, Inc., pursuant to the closing statement and inventory taken by the buyer as of April 12, 1983.

On April 5, 1983, Gregory L. Vallee, as owner of the Dragonwood Pub & Cafe, applied for a Wisconsin Department of Revenue seller's permit. The department issued seller's permit number 354010 to the taxpayer on April 6, 1983 for said business.

On September 9, 1983, the former owner, Egg Plant, Inc., was issued an assess-

ment of additional sales and use tax for the period May 1982 through February 1983 by the department based upon information furnished to the department by the former owner. On April 13, 1984, the former owner of the business Egg Plant, Inc. was issued a notice of assessment of additional sales and use tax for April 1983 regarding the sale of the business assets to the taxpayer. Gregory L. Vallee, purchaser, and the seller, Egg Plant, Inc., did not request a clearance certificate pursuant to s. 77.52(18), Wis. Stats.

The Commission concluded Gregory L. Vallee was successor to the seller's business under s. 77.52(18), Wis. Stats., and s. Tax 11.91(1)(a), Wis. Adm. Code. At the time of sale of the business to the

taxpayer, the seller was liable for unpaid sales tax for the period under review. Not having received from the seller a receipt from the department that all amounts of sales tax had been paid, or a certificate stating that no amount was due pursuant to s. 77.52(18), Wis. Stats., the taxpayer's failure to withhold from the purchase price an amount sufficient to cover this liability renders him liable for that amount. The department is not estopped from assessing such tax.

The taxpayer has not appealed this decision.

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## TAX RELEASES

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

The following Tax Releases are included:

### Individual Income Taxes

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2. Reinvestment of Condemnation Awards (p. 10)
3. Wisconsin Net Operating Loss Carryover (p. 11)

### Corporation Franchise/Income Taxes

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### Farmland Preservation Credit

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## INDIVIDUAL INCOME TAXES

### 1. Interest Income Received from Bonds Issued by the Wisconsin Housing Finance Authority

Statutes: Section 71.05(1)(a)1, 1985 Wis. Stats.

Note: This Tax Release supercedes the Tax Release published in Wisconsin Tax Bulletin 32 titled "Is Interest Income Received from Bonds Issued by the Wisconsin Housing Finance Authority Taxable?"

Facts and Question: Is interest income which an individual receives from bonds issued by the Wisconsin Housing Finance Authority excludable from his or her Wisconsin taxable income.

Answer: Yes. Federal law (42 U.S.C.) provides that interest income received from an obligation of a Housing Authority is exempt from federal income tax. Because this interest is not included in the federal adjusted gross income starting point used for Wisconsin tax purposes, it is not included in Wisconsin taxable income unless an add modification is provided for in the Wisconsin Statutes. The only add modification Wisconsin law provides in regard to interest is one that pertains to interest income excluded from federal income under section 103 of the Internal Revenue Code (IRC). Interest income received from a Housing Authority is not excluded from federal income under IRC section 103.

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### 2. Reinvestment of Condemnation Award

Statutes: Section 71.02(2), 1983 Wis. Stats.

Facts and Question: Section 1033 of the federal Internal Revenue Code allows for postponement of recognition of gain

on an involuntary conversion of property when replacement property is purchased within a specified period of time. If the replacement property costs less than the net proceeds received from the involuntary conversion, the gain must be included in income to the extent of the unexpended portion.

Wisconsin follows this provision of the Internal Revenue Code. However, for taxable years 1985 and prior, Wisconsin law requires that husband and wife report their income separately, using the separate federal return rules.

**Example:** On August 15, 1983 an Illinois resident received a \$240,000 net condemnation award for his sole interest in involuntarily converted property located in Wisconsin. The property had a basis of \$100,000 and he realized a gain of \$140,000. On April 5, 1985 the taxpayer and his spouse jointly acquired qualified replacement property located in Wisconsin for \$260,000, which exceeded the net condemnation award by \$20,000. No partnership exists between the taxpayer and his spouse; nor did the taxpayer gift one-half of the property to his spouse. (Note: Illinois is not a marital property state.)

May recognition of the \$140,000 gain from the involuntary conversion be postponed for Wisconsin income tax purposes as it is for federal purposes?

**Answer:** No, since the original property was solely owned by the taxpayer but the replacement property was jointly purchased, only \$30,000 of the \$140,000 gain may be postponed for Wisconsin income tax purposes as computed below:

Gain		\$140,000
Net condemnation award to taxpayer (100%)	\$240,000	
Purchase price of replacement property (50%)	<u>130,000</u>	
Taxable gain		<u>110,000</u>
Gain postponed		<u>\$ 30,000</u>

As the taxpayer reported on his original 1983 return that he had elected to postpone recognizing the entire gain, he will now be required to file an amended 1983 Wisconsin income tax return and report a \$110,000 taxable gain.

The basis of the replacement property is the cost of the replacement property decreased by the amount of gain postponed. The taxpayer's basis will be \$100,000 as shown below:

Purchase price of replacement property (50%)	\$130,000
Gain postponed	<u>30,000</u>
Basis of replacement property	<u>\$100,000</u>

The spouse's basis will be \$130,000.



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

**Background:** Section 71.05(1)(d)2, 1985 Wis. Stats., provides that "a Wisconsin net operating loss may be carried forward against Wisconsin taxable incomes of the next 15 taxable years to the extent not offset against other income of the year of loss and to the extent not offset against Wisconsin modified taxable income of any year between the loss year and the taxable year for which the loss carry-forward is claimed".

"Wisconsin modified taxable income" is defined in s. 71.05(1)(d)2, 1985 Wis. Stats., as Wisconsin adjusted gross income less the Wisconsin standard deduction with the following exceptions:

- A. A net operating loss deduction or offset for the loss year or any taxable year thereafter is not allowed.
- B. The deduction for long-term capital gains under Section 1202 of the Internal Revenue Code is not allowed.
- C. The amount deductible for losses from sales or exchanges of capital assets may not exceed the amount includable as income for gains from sales or exchanges of capital assets.
- D. "Wisconsin modified taxable income" may not be less than zero.

The 15-year loss carryforward provision in s. 71.05(1)(d)2, 1985 Wis. Stats., applies to losses incurred in taxable years ending after June 30, 1980 and the provision to offset a net operating loss against "Wisconsin modified taxable income" applies to taxable year 1986 and thereafter.

**Question 1:** Is the amount of a net operating loss carryover to 1986 affected by "Wisconsin modified taxable income" for the years between the loss year and 1986?

**Answer 1:** No. A net operating loss carryover to 1986 is not affected by "Wisconsin modified taxable income" for years prior to 1986. The amount of net operating loss carryover absorbed (used up) for tax years 1981 thru 1985 is equal to the amount allowed as a deduction to offset Wisconsin taxable income in those years.

**Example:** A single taxpayer sustained a Wisconsin net operating loss of \$50,000 for the 1980 tax year. For tax years 1981-1985 he was allowed the following amounts on his Wisconsin income tax returns as net operating loss deductions.

1981	\$ 3,000
1982	2,000
1983	5,000
1984	6,000
1985	<u>4,000</u>
Total	<u>\$20,000</u>

Therefore, \$30,000 (\$50,000 – \$20,000) is available as a net operating loss deduction for 1986.

**Question 2:** Is a net operating loss which is carried forward from years prior to 1986 affected by 1986 "Wisconsin modified taxable income" when such loss is carried forward to 1987?

**3. Wisconsin Net Operating Loss Carryover**

**Statutes:** Section 71.05(1)(d)2, 1985 Wis. Stats.

Answer 2: Yes. Effective for 1986 tax year and thereafter, the amount of net operating loss absorbed (used up) in the year to which the loss is carried is equal to the "modified taxable income" as computed for that year.

Example: The same taxpayer in the previous example computes his deduction for the Wisconsin net operating loss for 1986 as follows:

Self-employment income from Schedule C	\$15,000
Gain on sale of stock	\$10,000
Less 60% capital gain exclusion	6,000
Taxable capital gain	4,000
Wisconsin adjusted gross income (without NOL)	19,000
Less standard deduction based on single filing status and income of \$19,000	3,820
Allowable NOL deduction for 1986	<u>\$15,180</u>

Thus the taxpayer is allowed to deduct \$15,180 as a net operating loss on his Wisconsin income tax return for 1986. However, the amount of loss absorbed for 1986 is not equal to the amount of the net operating loss allowable as a deduction for 1986. Rather, the amount absorbed is equal to "modified taxable income."

"Modified taxable income" is computed as follows:

Self-employment income from Schedule C	\$15,000
Gain on sale of stock (60% capital gain exclusion not allowed)	10,000
Net operating loss deduction	-0-
Total	25,000
Less standard deduction based on single filing status and income of \$25,000	3,100
Wisconsin modified taxable income	<u>\$21,900</u>

The amount of net operating loss carryover to 1987 is computed as follows:

Amount of net operating loss carried to 1986	\$30,000
Less "Wisconsin modified taxable income" for 1986	21,900
Amount of net operating loss carryover available for 1987	<u>\$ 8,100</u>

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## CORPORATION FRANCHISE/INCOME TAXES

### 1. Payroll Factor-Section 401(k) Earnings

Statutes: Section 71.07(2)(b), 1985 Wis. Stats.

Wis. Adm. Code: Section Tax 2.39(4), January 1978 Register

Facts and Question: Section 71.07(2)(b), 1985 Wis. Stats., provides in part that the payroll factor of the standard 3-factor Wisconsin apportionment formula includes the total compensation paid during the taxable year. Wisconsin Administrative

Code section Tax 2.39(4) defines the term compensation to include wages, salaries, commissions and any other form of remuneration paid to employees for personal services rendered.

A qualified cash or deferred arrangement under Section 401(k) of the Internal Revenue Code is any arrangement which is part of a profit-sharing or stock bonus plan which meets the requirements of Section 401(a):

1. under which a covered employee may elect to have the employer make payments as contributions to a trust under the plan on behalf of the employee, or to the employee directly in cash;
2. under which amounts held by the trust which are attributable to employee contributions made pursuant to the employee's election may not be distributable to participants or other beneficiaries earlier than upon retirement, death, disability, or separation from service (or in the case of a profit-sharing or stock bonus plan, hardship or the attainment of age 59 1/2) and will not be distributable merely by reason of the completion of a stated period of participation or the lapse of a fixed number of years; and which provides that an employee's right to his or her accrued benefit derived from employer contributions made to the trust pursuant to his or her election are nonforfeitable.
3. which provides that an employee's right to his or her accrued benefit derived from employer contributions made to the trust pursuant to his or her election are nonforfeitable.

Are wages included in a qualified cash or deferred arrangement under Section 401(k) of the Internal Revenue Code which are excluded (deferred) from taxable income included in the computation of the payroll factor?

Answer: Yes. Total wages are included in the payroll factor computation under s. 71.07(2)(b), 1985 Wis. Stats., and Wis. Adm. Code section Tax 2.39(4) in the period in which they are earned. An employee's election to defer from taxation until a later time a portion of his or her salary does not also defer inclusion of these wages in the payroll factor computation until that later date.

Example: ABC Corporation has a total company payroll of \$5,500,000 for its 1985 taxable year, including a Wisconsin payroll of \$2,200,000. Certain employees have elected under Section 401(k) of the Internal Revenue Code to defer a portion of their 1985 wages. These deferred wages include \$185,000 attributable to Wisconsin employees and \$500,000 overall. In computing its 1985 payroll factor for Wisconsin apportionment purposes, ABC Corporation will include the entire \$2,200,000 Wisconsin payroll in the numerator and the entire total company payroll of \$5,500,000 in the denominator resulting in a payroll factor percentage of 40%. The payroll factor is not reduced for the wages deferred under Section 401(k) plan.

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## SALES/USE TAXES

### 1. Animal Bedding Used by Farmers

Statutes: Section 77.54(3m), 1985 Wis. Stats.

Wis. Adm. Code: Section Tax 11.12(4)(b), September 1984 Register

Facts and Question: A sales/use tax exemption for animal bedding purchased by farmers was added to s. 77.54(3m), Wis. Stats., by 1985 Wisconsin Act 29, effective July 1, 1986. Does this exemption apply to a farmer's purchases of absorbent litter for farm animals to sleep on, such as straw, shavings, and sawdust and to nonabsorbent items, such as rubber floor.

Answer: This new sales/use tax exemption for farm animal bedding applies to a farmer's purchases of loose items which will absorb urine, such as straw, shavings, and sawdust. The exemption does not apply to a farmer's purchases of non-absorbent items, such as rubber floor mats.

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### 2. Claim for Refund of Sales and Use Tax

Statutes: Sections 77.59(4), (4)(a), (8m), 1985 Wis. Stats.

Background: The Wisconsin Statutes contain four provisions for filing claims for refund of sales and use tax. The time periods for filing the claims for refund are as follows:

#### 1. Claims For Refund Where No Office Audit or Field Audit Determination Was Made (s. 77.59(4), 1985 Wis. Stats.)

Claims for refund may be filed within 4 years after the unextended due date of the taxpayer's Wisconsin income or franchise tax return, or if exempt from filing Wisconsin income or franchise tax returns, within 4 years of the 15th day of the 4th month of the year following the close of the calendar or fiscal year. (Note: This applies to refund claims relating to the 1969 taxable year and thereafter.)

#### 2. Claims For Refund Where an Office Audit Determination Was Made (s. 77.59(4)(a), 1985 Wis. Stats.)

Within two years of a determination of sales or use tax assessed by office audit and paid, a claim for refund of the tax assessed by office audit may be filed if the tax was not protested by the filing of a petition for redetermination. (Note: This applies to refund claims relating to office audit determinations dated on or after January 1, 1975.)

#### 3. Claims For Refund Where a Field Audit Determination Was Made (s. 77.59(4)(a), 1985 Wis. Stats.)

Within two years of a determination of sales or use tax assessed by field audit and paid, a claim for refund of the tax assessed by field audit may be filed if the tax was not protested by the filing of a petition for redetermination.

(Note: This applies to refund claims relating to field audit determinations dated on or after April 30, 1986.)

#### 4. Claims For Refund Where a Field Audit Determination Was Made and the Refund is Passed Along to the Customer (s. 77.59(8m), 1985 Wis. Stats.)

Claims for refund may be filed within 4 years after the due date of the taxpayer's Wisconsin income or franchise return, or if exempt from filing Wisconsin income or franchise tax returns, within 4 years of the 15th day of the 4th month of the year following the close of the calendar or fiscal year, if (a) the applicant's customers have filed valid claims for refunds with the applicant and (b) the refund is passed along by the applicant to the customers. (Note: This applies on or after April 30, 1986.)

Note: (a) Of the above four provisions for filing claims for refund of sales and use taxes, only number "4" (s. 77.59(8m), 1985 Wis. Stats.) requires the person, as a condition of the refund claim, to pass along the refunded taxes to the customers. This refund provision applies to taxes paid by customers to retailers and remitted through self-assessment to the Department of Revenue even if the person applying for the refund has been field audited in respect to those taxes. A retailer may not benefit under this provision. It is intended to put the customer on the same basis as customers of other retailers that have not been audited.

(b) The refund provisions in Background numbers "2" and "3" apply to additional taxes assessed by office or field audit.

The following examples illustrate how these four refund provisions apply to various situations. (Note: In all ten examples, assume the taxpayer is a corporation which files corporate franchise tax returns on a calendar-year basis and that petitions for redetermination are *not* filed in regard to any office audit or field audit determinations, except examples "6," "9" and "10" in which a petition for redetermination is filed. The taxpayer has paid any office audit or field audit assessment prior to filing the claim for refund.)

Facts and Question 1: A taxpayer files a claim for refund under s. 77.59(4) on April 30, 1986, for the 1981 through 1984 tax years. The taxpayer has not been issued an office audit or field audit determination. Does the taxpayer have a timely claim for refund?

Answer 1: The taxpayer has a timely claim for refund for the years 1982 through 1984. The claim for 1981 is not timely because the 1981 year expired on March 15, 1986, which is 4 years after the due date of the 1981 corporate franchise tax return.

Facts and Question 2: An office audit determination was issued on January 15, 1985, to the taxpayer for the tax years 1980 and 1981. Taxpayer then files a claim for refund under s. 77.59(4)(a) for the tax years 1980 through 1981 for items included in an office audit determination. The claim for refund does not include a claim for taxes self assessed. Does the taxpayer have a timely claim for refund if filed January 10, 1987?, if filed January 30, 1987?

Answer 2: The claim for refund filed on January 10, 1987 is timely because the claim was made within 2 years of January 15, 1985, the date of the office audit determination. The claim filed January 30, 1987 is not timely because it was filed later than 2 years after the office audit determination.

Facts and Question 3: Taxpayer was issued a field audit determination for 1982 and 1983, on March 1, 1985. On June 1, 1986, taxpayer files a claim for refund under s. 77.59(4)(a) for excess sales and use taxes assessed by field audit for the years 1982 and 1983. Is this a timely claim for refund?

Answer 3: No, because the field audit determination was dated before April 30, 1986. Section 77.59(4)(a), 1985 Wis. Stats., applies only to field audit determinations dated on or after April 30, 1986.

Facts and Question 4: Taxpayer was issued a field audit determination dated April 30, 1986 for the years 1982-1985. Taxpayer files a claim for refund under s. 77.59(4)(a) on May 30, 1986, for excess sales and use taxes assessed by field audit for the years. Is this a timely claim?

Answer 4: Yes, the taxpayer's claim is timely under s. 77.59(4)(a), 1985 Wis. Stats., because the taxpayer filed the claim within 2 years after the determination notice dated April 30, 1986.

Facts and Question 5: Taxpayer received claims for refunds of sales tax from his/her customers for the 1981-1983 tax years. Taxpayer files a claim for refund with the department on April 15, 1986 for the years 1981-1983 with the intent to pass it along to his/her customers. The claim for refund states that it is based on claims for refund filed with the taxpayer by its customers and the refund will be passed along to the customers. Taxpayer was field audited for 1981-1983 and the determination was dated April 20, 1985 and was not appealed by the taxpayer. As of April 30, 1986, the department had not issued a determination on the taxpayer's refund claim. May the refund claim filed on April 15, 1986 be paid by the department to the taxpayer.

Answer 5: Yes in part. The taxpayer would be granted the claim for refund on or after April 30, 1986, the date s. 77.59(8m), 1985 Wis. Stats., became effective for 1982 and 1983. However, the 1981 year is closed to adjustment under the four year statute in s. 77.59(4)(intro.), 1985 Wis. Stats.

Facts and Question 6: Taxpayer was issued a field audit determination for 1984 on May 3, 1986. The taxpayer filed a petition for redetermination on May 26, 1986. On July 1, 1986, while the petition is still pending, taxpayer filed a claim for refund for the year 1984 under s. 77.59(4)(a), 1985 Wis. Stats. Is the claim affected by the appeal?

Answer 6: Yes. The taxpayer must withdraw the petition for redetermination before the claim may be refunded.

Facts and Question 7: Taxpayer was field audited for the years 1983 through 1985. A "no change" letter was sent to the taxpayer on March 1, 1986, stating that no additional sales and use tax liability was determined. On June 1, 1986, taxpayer files a claim for refund under s. 77.59(8m), 1985 Wis. Stats., for excess taxes paid, with the intention of remitting the refund

to his/her customers. The customers had filed claims for refund with the taxpayer for those years. Is this a valid claim?

Answer 7: Yes, taxpayer meets the requirements of s. 77.59(8m), 1985 Wis. Stats. In the Moebius Printing Company case the Wisconsin Supreme Court held that a "no change" letter issued by the department constituted a field audit per s. 77.59(2), 1985 Wis. Stats. However, even though the taxpayer was issued a field audit determination (e.g., a no change letter) before April 30, 1986, a claim for refund may still be filed on or after April 30, 1986 under s. 77.59(8m), 1985 Wis. Stats.

Facts and Question 8: Taxpayer was issued a field audit determination for the taxable years 1984 and 1985 on July 1, 1986. The department made two adjustments, one to taxable sales of merchandise normally sold at retail and one to untaxed purchases. On December 1, 1986, the taxpayer filed a claim for refund, under s. 77.59(4)(a), 1985 Wis. Stats., for an overpayment of taxes regarding taxable sales of the merchandise adjusted by field audit and for an overpayment of taxes in regard to the sale of capital assets not adjusted by field audit. The department in acting on the claim disallows the portion of the claim regarding the sale of capital assets (on which the tax was self-assessed by the taxpayer) and also makes an additional assessment to the untaxed purchases adjusted by field audit. Is this action by the department correct?

Answer 8: Yes. Under s. 77.59(4)(a), 1985 Wis. Stats., no claim may be allowed for any tax self-assessed by the taxpayer because the years are closed to adjustment per s. 77.59(2), 1985 Wis. Stats. The department may make an additional assessment in respect to any item that was a subject of the prior assessment.

Facts and Question 9: Taxpayer was issued a field audit determination for 1983 and 1984 on May 30, 1986. The taxpayer filed a petition for redetermination with the department on June 15, 1986. The petition was denied by the department so the taxpayer appealed the matter to the Wisconsin Tax Appeals Commission. The taxpayer lost on appeal to the Commission and soon after filed a claim for refund for overpayment of sales and use taxes paid, under s. 77.59(8m), 1985 Wis. Stats. The claim for refund states that it is based on claims for refund filed with the taxpayer by its customers and the refund will be passed along to the customer. Is this a valid claim for refund if the overpayment claimed relates to items adjusted by field audit that were part of the taxpayer's appeal?

Answer 9: No. Pursuant to s. 73.01(4)(e), 1985 Wis. Stats., the decision and order of the Commission is final and binding upon the taxpayer unless an appeal is taken from the decision and order of the Commission. Therefore, any item adjusted by field audit which is decided by the Commission adversely to the taxpayer on an appeal may not be the subject of a claim for refund.

Facts and Question 10: Assume the same facts as in Facts and Question 9 except that the claim for refund involves items that were adjusted by field audit but were not part of the taxpayer's appeal. Is this a valid claim?

Answer 10: Yes. Taxpayer may make a claim for refund under s. 77.59(8m), 1985 Wis. Stats., if the item that is the subject of the claim for refund has not been appealed or if an appeal

was made was not decided adversely to the taxpayer and the claim otherwise meets the requirements of s. 77.59(8m), 1985 Wis. Stats.

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### 3. Federal Food Stamp Receipts of Grocers

Statutes: Section 77.54(1) and (20), 1985 Wis. Stats.

Wis. Adm. Code: Section Tax 11.51(2)(b), September 1984 Register.

Facts and Question: Federal law provides that federal food stamps may be used to purchase any food or food product for home consumption, except alcoholic beverages, tobacco and hot foods or hot food products ready for immediate consumption. Federal food stamps may also be used to purchase seeds and plants for use in gardens to produce food for the personal consumption of the eligible household.

Are a grocer's receipts from federal food stamps used to purchase items authorized under federal law subject to the state sales tax?

Answer: No, a grocer's receipts from federal food stamps are not subject to the Wisconsin sales tax and have never been subject to the state sales tax. This interpretation is set forth in subsection (2)(b) of section Tax 11.51, the "Grocers' guidelist," which is part of the Wisconsin Administrative Code.

Groceries sold for the home preparation of meals are exempt under s. 77.54(20), Wis. Stats. However, if federal food stamps are used to purchase food products, such as the following authorized items, which would otherwise be taxable because they are not exempt groceries under s. 77.54(20), 1985 Wis. Stats., the gross receipt from such sales are also exempt from the Wisconsin sales tax: candy, popcorn, gum, confections, snacks, soft drinks and concentrates and powders to produce soft drinks, ades, cocktails and punches which are not pure fruit juices, and seeds and garden plants used to produce food.

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## FARMLAND PRESERVATION CREDIT

### 1. Farmland Credit - Dairy Termination and Conservation Reserve

Statutes: Sections 71.09(11)(a)3 and 3m, 91.01(1) and 91.01(6), 1985 Wis. Stats.

Background: The federal Food Security Act of 1985 (P.L. 99-198) established a dairy termination program and a conservation reserve program. Under the dairy termination program, producers agree to sell for slaughter or export all dairy cattle in which the producers have an interest, and during a period of

three to five years after the sale not to acquire any interest in dairy cattle or in the production of milk. In return the producer receives two types of payments. The first payment is income from the slaughterhouse or exporter for the sale of the cattle. If the sale results in a gain, the gain will be treated as a capital gain if the cattle were raised or held for twenty-four months or more from their acquisition date. The second type of payment is a stream of income the producer will receive over a five-year period. The income depends on the producer's milk production base, bid, and contract with the federal government. These payments are treated as ordinary income.

Under the conservation reserve program, owners of highly erodible cropland agree to place the land in a conservation reserve. Under this agreement the owners may not use the land for agricultural purposes, and may not conduct any harvesting or grazing on the land, or otherwise make commercial use of the forage on the land. In return the owner will receive an annual rental payment in an amount necessary to compensate the owner for the conversion of the cropland to a conservation use, and the retirement of any cropland base that the owner agrees to retire permanently. The rental payments may be made as payments-in-kind with commodities.

Under Wisconsin law, farmland may be eligible for a farmland preservation credit if the farmland produces at least \$6,000 of gross farm profits for the taxable year resulting from the farmland's agricultural use (or \$18,000 of gross farm profits for the taxable year and the two prior years combined).

"Gross farm profits" means gross receipts, excluding rent, from the land's agricultural use including the fair market value at the time of disposition of payments-in-kind for placing land in federal programs, less the cost or other basis of livestock or other items purchased for resale which are sold or otherwise disposed of during the income year (s. 71.09(11)(a)3m, 1985 Wis. Stats.).

"Agricultural use" is defined to include dairying, livestock raising, raising of grain and seed crops, placing land in federal programs in return for payments in kind, and other farming activities listed in s. 91.01(1), 1985 Wis. Stats.

Question 1: If a farmer participates in a dairy termination program does the payment for the sale of the cattle qualify as gross farm profits resulting from the farmland's agricultural use for purposes of the farmland preservation credit \$6,000 gross profit requirement?

Answer 1: Yes, income from the sale of the cattle less the cost or other basis of the cattle is considered gross farm profits for purposes of the \$6,000 gross farm profits requirement. This income is considered to be gross farm profits resulting from the farmland's agricultural use since the farmland was used for the agricultural use of dairying or raising livestock.

Question 2: If a farmer participates in a dairy termination program, do the payments received pursuant to the producer's contract with the federal government for the purpose of terminating the farmer's milk production qualify as gross farm profits resulting from the farmland's agricultural use for purposes of the farmland preservation credit \$6,000 gross profit requirement?

Answer 2: No, these payments are a result of the farmer's production termination contract rather than a result of the farmland's agricultural use.

Question 3: If a farmer participates in a conservation reserve program, are cash rental payments considered gross farm profits resulting from the farmland's agricultural use for purposes of the farmland preservation credit \$6,000 gross profit requirement?

Answer 3: No, the definition of gross farm profits under s. 71.09(11)(a)3m, 1983 Wis. Stats., specifically exclude rental income. Thus, the cash rental payments may not be included in gross farm profits for purposes of the \$6,000 requirement.

Question 4: If a farmer participates in a conservation reserve program, does the disposition of payments-in-kind constitute gross farm profits resulting from the farmland's agricultural use for purposes of the farmland preservation credit \$6,000 gross profit requirement.

Answer 4: Yes, under Wisconsin Statutes gross farm profits are defined to include the fair market value at the time of disposition of payments-in-kind for placing land in federal programs.

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## 2. Gross Farm Profits Requirement

Statutes: Sections 71.09(11)(a)3 and 3m, and 91.01(6), 1985 Wis. Stats.

Background: For farmland preservation credit purposes, farmland must produce at least \$6,000 in gross farm profits for the

year of the farmland claim, or at least a total of \$18,000 in gross farm profits for the year of the claim and the two prior years combined.

"Gross farm profits" is defined under s. 71.09(11)(a)3m, 1985 Wis. Stats., to mean gross receipts, excluding rent, from agricultural use, less the cost or other basis of livestock or other items purchased for resale which are sold or otherwise disposed of during the income year.

Gross receipts means the total amount received from all sources. Gross receipts includes the total property, usually cash, received from the sale of farm products.

Facts and Question: Farmer A grows a crop of corn during the year which has a fair market value greater than \$6,000, but Farmer A does not receive cash for the crop during the year because the crop is stored rather than sold to a third party. Farmer B also grows more than \$6,000 worth of corn, but feeds the corn to his cattle which were not sold during the year.

For farmland preservation credit purposes, may Farmer A or B include the fair market value of the crop grown in determining whether the \$6,000 gross farm profits requirement is met for the year the crop is grown?

Answer: No, the fair market value of the crop grown by Farmers A and B may not be included in gross farm profits to determine if the \$6,000 requirement is met. No gross receipts were received from these crops.

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