

## Chapter Tax 2

INCOME TAXATION, RETURNS, RECORDS AND  
GROSS INCOME

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**Tax 2.01 Residence.** (s. 71.02, Stats.) Individuals claiming a change of residence, i.e., domicile, from Wisconsin to another state shall file form I-827, "Residence Questionnaire", or the "Residence Questionnaire" which is a part of the 1NPR income tax form, with the Wisconsin department of revenue by attaching it to their Wisconsin income tax return for the year they claim to have changed residence, and shall furnish other information the department may require.

*Note:* Form I-827 or form 1NPR may be obtained from the Department of Revenue at 4638 University Avenue, Madison, or from any other Department of Revenue office located throughout the state, or by mail request to Wisconsin Department of Revenue, P.O. Box 8903, Madison, WI 53708.

*History:* 1-2-56; r. (1); renum. (2) to be (1); renum. (3) to be (2) and am., Register, September, 1964, No. 105, eff. 10-1-64; am. Register, February, 1975, No. 230, eff. 3-1-75; r. (1), renum. (2) and am., Register, July, 1987, No. 379, eff. 8-1-87; am. Register, February, 1990, No. 410, eff. 3-1-90.

**Tax 2.02 Reciprocity.** (ss. 71.05 (2) and 71.64 (8), Stats.) (1) **PURPOSE.** This section explains the reciprocity agreements between Wisconsin and other states.

(2) **DEFINITIONS.** The following definitions pertain only to Wisconsin. Definitions of the same terms in other states may vary. In this section:

(a) "Personal service income" means all salaries, wages, commissions and fees earned by an employe and all commissions and fees earned by a self-employed person in the conduct of a profession or vocation. Personal service income does not include income derived from activities involving the substantial use of capital or labor of others.

(b) "Resident" means a natural person who is domiciled in this state.

(3) **WISCONSIN LAW.** (a) Under s. 71.05 (2), Stats., income earned by a nonresident individual for performing personal services in Wisconsin shall be excluded from Wisconsin gross income to the extent the individual's state of residence imposes an income tax on the personal service income, if the state of residence allows either of the following:

1. A similar exclusion for personal service income earned by individuals domiciled in Wisconsin while working in that state.

2. A credit against the tax imposed by that state on the personal service income equal to the Wisconsin tax on the personal service income.

(b) Under s. 71.64 (8), Stats., a Wisconsin employer of a nonresident individual residing in a state with which Wisconsin has a reciprocity agreement under sub. (4) need not withhold Wisconsin income tax from personal service income earned in Wisconsin by the nonresident.

(4) **AGREEMENTS WITH OTHER STATES.** (a) Wisconsin has formal reciprocity agreements with:

1. Kentucky, for the years beginning on and after January 1, 1961.

In this section, "person" means an individual, a trust, estate, partnership, association, or corporation.

(2) **COMPENSATION FOR SERVICES.** Under ss. 71.65 (2), 71.71 (2), and 71.72, Stats., all persons carrying on activities within this state, whether taxable or not under ch. 71, Stats., are required to file with the department of revenue, on federal form W-2 or W-2P or on Wisconsin form 9b or on other forms approved by the department, a statement of certain payments made within the preceding calendar year. For individuals who are residents of Wisconsin, the statement shall set forth the salaries, wages, bonuses, commissions, annuities, pensions, retirement pay, fees or other remuneration paid for services whether subject to withholding or not. For individuals who are nonresidents, the statement shall include all payments for the performance of personal services in Wisconsin, whether subject to withholding or not, except retirement plan distributions identified in s. Tax 3.085 as being exempt from Wisconsin income tax. A copy of federal form 1099 may be filed in lieu of Wisconsin form 9b. The following shall also apply with respect to compensation for services:

(a) All payments which are wages within the statutory definition under s. 71.63 (6), Stats., regardless of amount, shall be reported on form W-2.

(b) All payments which are not wages within the definition under s. 71.63 (6), Stats., but from which Wisconsin income tax has been withheld, shall be reported on form W-2 or W-2P.

(c) Payments of \$600 or more which are not within the statutory definition of wages under s. 71.63 (6), Stats., and from which no Wisconsin income tax has been withheld, shall be reported on a Wisconsin form 9b. However, if the payment was to an employe for whom a form W-2 is required under par. (a) or (b), the payment, regardless of amount, shall be included on form W-2.

(d) All statements required shall be filed by January 31. Forms W-2 or W-2P shall be mailed or delivered to the Department of Revenue at 4638 University Avenue, P.O. Box 8920, Madison, WI 53708. Form WT-7, Annual Reconciliation of Wisconsin Income Tax Withheld From Wages, shall accompany the wage statements submitted, if the employer is required to be registered to withhold Wisconsin income taxes from employe's wages. Corporations shall mail or deliver Wisconsin forms 9b or substitute forms to the Department of Revenue at 4638 University Avenue, P.O. Box 8908, Madison, WI 53708. Payors other than corporations shall mail or deliver Wisconsin forms 9b or substitute forms to the Department of Revenue at 4638 University Avenue, P.O. Box 59, Madison, WI 53785. A letter of transmittal identifying the sender shall accompany the forms 9b or substitute forms.

(e) Sections 71.65 (5) and 71.73 (2), Stats., permit a thirty-day extension of time to file the forms described in this subsection. A written request may be sent to the department at P.O. Box 8920, Madison, WI 53708 and to be effective shall be postmarked on or before the due date of the statements. The department's approval of the extension shall be attached to the statements when they are filed with the department.

(3) **RENTS AND ROYALTIES.** All persons making payments of rents and royalties of \$600 or more to individuals who are residents of Wisconsin,

regardless of where the property is located, and to nonresident individuals if the property is located in Wisconsin, shall file with the department of revenue, on form 9b or an approved substitute form, reporting the payments made in the preceding calendar year. The following shall also apply with respect to rents and royalties:

(a) A copy of federal form 1099 may be filed in lieu of Wisconsin form 9b.

(b) Corporations shall file by March 15, by mailing or delivering the statements to the Department of Revenue at 4638 University Avenue, P.O. Box 8908, Madison, WI 53708. Payers other than corporations shall file by April 15, by mailing or delivering the statements to the Department of Revenue at 4638 University Avenue, P.O. Box 59, Madison, WI 53785.

(c) No extensions of time for filing forms 9b or substitute forms to report payments of rents or royalties shall be allowed.

(4) Items to be reported on forms W-2, W-2P, 9b, or substitute forms may be disallowed as deductions from gross income if not properly reported.

(5) Payers who participate in the combined federal/state filing program with the internal revenue service and report items required to be filed on a Wisconsin form 9b to the internal revenue service, are not required to file separate information returns for those items with the department of revenue.

**Note:** Under the combined federal/state filing program, the internal revenue service will forward information from the information returns to the department of revenue.

**History:** 1-2-56; am. Register, September, 1964, No. 105, eff. 10-1-64; am. Register, February, 1975, No. 230, eff. 3-1-75; am. Register, September, 1977, No. 261, eff. 10-1-77; am. (1), (3), (4) and (6), cr. (7), Register, September, 1983, No. 333, eff. 10-1-83; r. and recr. Register, June, 1990, No. 414, eff. 7-1-90.

**Tax 2.05 Transfers of capital stock, information return.** (s. 71.69, Stats.)

(1) All corporations doing business within this state, whether subject to the franchise or income tax or not, shall file with the department of revenue on or before March 15 of each year reports of transfers of capital stock, including disposals, by individuals who were residents of Wisconsin during the preceding calendar year.

(2) Transfers of capital stock shall be reported on Wisconsin form 8 or on other substitute forms approved by the department and shall be mailed to the Wisconsin Department of Revenue, P.O. Box 8908, Madison, WI 53708.

**Note:** Blank forms may be obtained by mail request addressed to Wisconsin Department of Revenue, P.O. Box 8903, Madison, WI 53708.

**History:** 1-2-56; am. Register, September, 1964, No. 105, eff. 10-1-64; am. Register, March, 1966, No. 123, eff. 4-1-66; am. Register, February, 1975, No. 230, eff. 3-1-75; am. Register, September, 1983, No. 333, eff. 10-1-83; am. Register, July, 1987, No. 379, eff. 8-1-87; r. and recr. Register, February, 1990, No. 410, eff. 3-1-90.

**Tax 2.08 Returns of persons other than corporations.** (ss. 71.03 (2), 71.20 (1) and 71.55 (3), Stats.) (1) For the purpose of filing income tax returns, the secretary of revenue has designated the following forms for the use of persons other than corporations:

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Note: Refer to s. Tax 2.105 for additional information regarding amended Wisconsin returns required as a result of filing amended federal returns or amended returns of other states and amended Wisconsin returns required as a result of adjustments made to a federal return by the Internal Revenue Service.

(b) Because an amended return is not the original return, it shall not begin or extend the statute of limitation periods for assessing additional tax or claiming a refund.

(c) If an amended return shows a refund, it shall be filed within 4 years of the unextended due date of the original return. However, there are 2 exceptions, as follows:

1. A claim for refund of the tax paid as a result of an office audit or field audit may be filed within 2 years of the date the tax was assessed if no petition for redetermination was filed.

2. A claim for refund of the tax paid as a result of a federal audit adjustment may be filed within 90 days of the date on which the federal audit adjustment became final.

Note: Refer to s. Tax 2.105 (4) (a) 1 for information regarding when a federal audit adjustment is final.

(2) FORMS. Amended returns may be filed using form 1X for individuals and form 4X for corporations. Other forms may be used, but such forms shall be clearly marked "AMENDED RETURN" across the top of the first page.

Note: 1) The department accepts amended individual income tax and corporate franchise and income tax returns to allow taxpayers to correct overstatements or understatements of net income and computations of tax contained on their original, previously amended, or previously adjusted return.

2) Although the use of forms 1X and 4X is not mandatory, the department prefers that they be used. They are designed to simplify the filing and expedite the processing of the information. Copies may be obtained from any Wisconsin department of revenue office.

History: Cr. Register, August, 1976, No. 248, eff. 9-1-76; am. (1) (a), Register, September, 1983, No. 333, eff. 10-1-83; am. (1) (a) and (b), r. and recr. (1) (c) and (2), Register, February, 1990, No. 410, eff. 3-1-90.

**Tax 2.13 Moving expenses.** (s. 71.05 (1) (a)7 and (b)4, 1985 Stats., and s. 71.07 (5), Stats.) (1) GENERAL. Certain moving expenses qualify for a deduction in arriving at federal adjusted gross income. When a person *moves into* Wisconsin, such expenses are allowed as a deduction in computing Wisconsin adjusted gross income. The deductibility of moving expenses incurred in *moving from* Wisconsin was changed for 1975 and subsequent taxable years by the enactment of s. 71.05 (1) (a)7, Stats., which provides for an add modification for "Moving expenses incurred to move from this state".

(2) TREATMENT OF MOVING EXPENSES INCURRED IN MOVING FROM WISCONSIN. Moving expenses may be deducted in arriving at federal adjusted gross income for federal income tax purposes. Under s. 71.05 (1) (a) 7, Stats., in determining Wisconsin adjusted gross income an add modification shall be made for "moving expenses incurred to move from this state". This add modification applies when the taxpayer becomes domiciled in another state, i.e., becomes a nonresident for Wisconsin tax purposes, either on the day he or she moves to the other state or prior to the move. However, the add modification is not required if the taxpayer retains his or her Wisconsin domicile after moving to another state and continues to be subject to Wisconsin's taxing jurisdiction.

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**Example:** The following example illustrates the add modification for moving expenses for a taxpayer moving from Wisconsin to New York when the taxpayer's Wisconsin domicile is not retained:

Wisconsin Gross Income	\$18,000
New York Gross Income	600
Moving Expenses to New York	<u>(4,000)</u>
Federal Adjusted Gross Income	\$14,600
*Add Modification for Moving Expenses to New York	4,000
Subtract Modification: New York Gross Income	<u>(600)</u>
Wisconsin Adjusted Gross Income	<u><u>\$18,000</u></u>

\*The \$4,000 of moving expenses to New York is entered as an add modification on the Wisconsin income tax return, Form 1.

(3) **APPLICABILITY.** As a result of 1987 Wis. Act 27 which updated the reference to the internal revenue code as amended to December 31, 1986, subs. (1) and (2) do not apply to taxable years 1987 or thereafter. Effective with taxable year 1987 and thereafter, the internal revenue code allows moving expenses as an itemized deduction rather than as a deduction in computing adjusted gross income; and for Wisconsin income tax purposes, under s. 71.07 (5), Stats., moving expenses except expenses to move from this state, are included in the computation of the itemized deduction credit.

**History:** Cr. Register, February, 1978, No. 266, eff. 3-1-78; r. and recr. (2), Register, September, 1983, No. 333, eff. 10-1-83; Cr. (3), Register, February, 1990, No. 410, eff. 3-1-90; r. and recr. (3), Register, June, 1990, No. 414, eff. 7-1-90.

**Tax 2.14 Aggregate personal exemptions.** (s. 71.09 (6p) (a) and (b), 1985 Stats.) For taxable years prior to 1986, the aggregate personal exemptions allowable under s. 71.09 (6p) (a) and (b), Stats., when each files a return, may be divided between husband and wife according to their choice.

**History:** 1-2-56; am. Register, February, 1958, No. 26, eff. 3-1-58; am. Register, February, 1960, No. 50, eff. 3-1-60; r. and recr., Register, September, 1964, No. 105, eff. 10-1-64; am. Register, March, 1966, No. 123, eff. 4-1-66; am. Register, November, 1977, No. 263, eff. 12-1-77; am. Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.15 Methods of accounting for corporations.** (s. 71.11 (8), 1985 Stats.) (1) No uniform method of accounting can be prescribed for all corporations, and the law contemplates that each corporation may report its income in accordance with the method of accounting regularly employed in keeping its books. If no method of accounting is regularly employed or if the method employed does not clearly reflect the income, the department of revenue may prescribe the method to be used. A method of accounting will not be regarded as clearly reflecting the income unless all items of gross income and all deductions are treated with reasonable consistency.

(2) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, sub. (1) does not apply to taxable year 1987 or to taxable years thereafter.

**History:** 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66; am. Register, February, 1975, No. 230, eff. 3-1-75; renum. to be (1) and am., cr. (2), Register, February, 1990, No. 410, eff. 3-1-90.

**Tax 2.16 Change in method of accounting for corporations.** (s. 71.11 (8) (b), 1985 Stats.) (1) **GENERAL.** (a) The computation of adjustments necessary for a change in the method of accounting by corporations shall be made under the provisions of s. 71.11 (8) (b), 1985 Stats.

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(b) A change in a corporation's method of accounting may involve an overall change of the entire accounting system or it may involve only a single item.

(c) No change in the method of accounting used in reporting income may be made without first obtaining the written permission of the department. Applications for changes shall be made in the manner described in sub. (5).

(d) In changing from a cash basis of accounting to an accrual basis of accounting, income accrued but not yet collected as of the close of the year of change shall be added to income actually received in cash during the year, and expenses accrued but not yet paid as of the close of the year shall be added to expenses actually paid during the year.

(2) CHANGE IN METHOD OF ACCOUNTING FOR SINGLE ITEMS. Any change in the accounting treatment of a single item, if "material", is deemed a change in the method of accounting under s. 71.11 (8) (b), 1985 Stats. If an item is "material" for federal income tax purposes, it generally will be "material" for Wisconsin franchise and income tax purposes.

(3) 1953 ACCOUNT BALANCES. (a) *Taxpayer-initiated change.* On a taxpayer-initiated change, the net 1953 account balances may not be allowed as an offset in the year of change.

(b) *Department-initiated change.* 1. On a department-initiated change, the net 1953 balances shall be allowed as an offset in the year of change in accordance with the internal revenue code and federal regulations.

2. Net 1953 account balances shall be computed by the taxpayer and adequately supported by its accounting records in order for them to be allowed as offsets in the year of change.

3. No offset is available for taxpayers incorporated after December 31, 1953 or in connection with changes involving LIFO inventories.

(c) Paragraphs (a) and (b) shall apply to all tax years open to assessment or refund.

(4) TRANSITIONAL ADJUSTMENTS. The entire impact of a change in method of accounting shall be reflected in net income of the year of change for Wisconsin franchise and income tax purposes.

Note: Wisconsin's treatment of transitional adjustments represents a significant difference from the federal treatment which, in general, permits a 10-year amortization of the net transitional adjustment at the beginning of the year of change.

(5) APPLICATION FOR CHANGE IN METHOD OF ACCOUNTING. (a) Applications to use the LIFO inventory method and subsequent changes in inventory accounting method shall be filed with the department pursuant to s. Tax 2.26. All other applications shall contain the following:

1. Nature of the taxpayer's business;
2. The method of accounting used in keeping its books;
3. The reason or reasons for requesting the change;
4. A legible copy of federal form 3115, "Application for Change in Accounting Method";

5. Legible copies of all subsequent correspondence with the internal revenue service pertaining to such application;

6. A statement, and whenever possible a schedule showing the computation of adjustments to income for each year, which clearly indicate the manner in which it proposes to effect the change for Wisconsin franchise or income tax purposes;

7. A copy of the entry, its date and explanation, made on the books to accomplish the change or when no book entry is made, the reason for its absence; and

8. Any other pertinent information.

(b) 1. Applications shall be filed before the end of the taxable year for which the change is to be effective. The applications shall be in letter form with supporting schedules and data and mailed to: Wisconsin Department of Revenue, P.O. Box 8906, Madison, WI 53708.

2. The department has no form comparable to federal form 3115.

(6) **APPLICABILITY.** As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, this section does not apply to taxable year 1987 or to taxable years thereafter.

**Note:** 1) As to a change in method of accounting for a single item refer to *Ladish Co. v. Dept. of Revenue*, 69 Wis. 2d 723 (1975).

2) As to a change of method of accounting from cash to accrual basis refer to the decisions of the Wisconsin Tax Appeals Commission in *Streets and Roads Construction Corp. v. Dept. of Revenue*, Docket No. I-6239 (July 28, 1981) and *Wisconsin Railroad Services Corp. v. Dept. of Revenue*, Docket No. I-6813 (June 5, 1985).

3) Refer to ss. Tax 2.25, "Corporation accounting generally", and 2.26, "Last-in, first-out method of inventorying for corporations", for departmental interpretations with respect to methods of accounting for inventories.

**History:** 1-2-56, am. Register, September, 1964, No. 105, eff. 10-1-64; am. Register, February, 1975, No. 230, eff. 3-1-75; am. Register, November, 1977, No. 263, eff. 12-1-77; r. and recr. Register, May, 1978, No. 269, eff. 6-1-78; am. (1) (a), Register, September, 1983, No. 333, eff. 10-1-83; am. (1) (a), (c), (2), (3) (a), (4), (5) (a) (intro.), 3., 4., 6., 7., (b) 1. and 2., cr. (6), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.165 Change in taxable year.** (ss. 71.02 (1) (b) and (2) (h) and 71.10 (3m) and (16), 1985 Stats.). (1) **DEFINITIONS.** In this rule:

(a) "Calendar year" means a 12 month period ending on December 31.

(b) "Fiscal year" means a 12 month period ending on the last day of any month other than December 31.

(c) "Taxable year" or "income year" means a calendar year, a fiscal year or a short period of less than 12 months resulting from a change in reporting from a calendar to a fiscal, a fiscal to a calendar, or a fiscal to a different fiscal year and is the period for which the taxable income is reported.

(2) **CORPORATIONS.** (a) *General.* A new corporation may elect the taxable year on which it will report. A taxable year must end on the last day of a month and, if accounting records are kept on a 52-53 week period, the taxable year shall be considered to end on the last day of the month closest to the end of the 52-53 week period.



(b) *Change in taxable year.* A corporation may not change its taxable year without first obtaining approval from the department. The request to change shall be made in writing to the Wisconsin Department of Revenue, P.O. Box 8906, Madison, WI 53708 prior to the close of the proposed new taxable year. The request shall contain the following information:

1. Name and address of corporation.
2. Taxable year presently used.
3. Proposed taxable year.
4. Effective date of change.
5. Reason for requesting the change.

(c) *Computation of tax.* The income for the short taxable year shall be computed on an annual basis and the tax for the short taxable year shall be a fractional portion of the tax computed on such annual income. As an example, in changing from a calendar year to a fiscal year ending September 30, with net income for the 9 month period of \$18,000, the tax on the income of the short taxable year may be computed as follows:

1. Multiply short period income by 12.  $\$18,000 \times 12 = \$216,000$
2. Divide by number of months in the short period to obtain annualized income.  $\$216,000 \div 9 = \$24,000$
3. Compute the tax on the annualized income. Tax on \$24,000 equals \$1,676 (1977 rates).
4. Prorate this tax to obtain the tax for the short period.  $\$1,676 \times 9/12 = \$1,257.$

(3) **PERSONS OTHER THAN CORPORATIONS.** (a) *General.* A person other than a corporation is required to adopt the same taxable year for Wisconsin as for federal income tax purposes. The taxable year is established with the filing of the first income tax return.

(b) *Change in taxable year.* For federal purposes, approval is requested by filing federal form 1128 on or before the 15th day of the second calendar month following the close of the short taxable year for which the return is required. The change is effected for Wisconsin purposes by attaching a copy of form 1128 and the federal approval to the Wisconsin tax return for the short taxable year, which return is due on or before the 15th day of the 4th month after the end of the short taxable year.

(c) *Computation of tax.* The Wisconsin taxable income for the short taxable year shall be computed on an annual basis. For natural persons, the tax computed on the annualized income, reduced by the amount for personal exemptions, is multiplied by the number of months in the short taxable year and divided by 12. As an example, in changing from a calendar year to a fiscal year ending June 30, with Wisconsin taxable income for the 6 months of \$14,000, and claiming 4 exemptions as of June 30, the tax on the income of the short taxable year may be computed as follows:

1. Multiply short period income by 12.  $\$14,000 \times 12 = \$168,000$
2. Divide by number of months in the short period to obtain annualized income.  $\$168,000 \div 6 = \$28,000$

3. Compute the tax on the annualized income. Tax on \$28,000 equals \$2,577 (1977 tax rates).

4. Subtract personal exemptions.  $\$2,577 - \$80 = \$2,497$

5. Prorate this tax to obtain tax for the short period.  $\$2,497 \times 6/12 = \$1,248.50$ .

For estates and trusts, the computation is the same except that step 4 ("Subtract personal exemptions") is omitted; in the example, the tax equals \$1,288.50 ( $\$2,577 \times 6/12$ ).

(4) **PARTNERSHIPS.** (a) *General.* A partnership is required to adopt the same taxable year for Wisconsin as for federal income tax purposes. If federal approval of the taxable year adopted for the first return is required, a copy of federal form 1128 and approval shall be attached to the first Wisconsin return filed.

(b) *Change in taxable year.* If federal approval is required for a change in taxable year, a copy of the federal form 1128 and the federal approval shall be attached to the Wisconsin partnership return for the short taxable year.

(c) *Computation of income.* Partnership income for the short taxable year shall be determined under the internal revenue code as defined under s. 71.02 (2) (b), Stats.

(5) **APPLICABILITY.** As a result of 1989 Wis. Act 31 which generally federalized Wisconsin's treatment of taxable years, this section does not apply to taxable years beginning on or after August 1, 1988.

History: Cr. Register, February, 1979, No. 278, eff. 3-1-79; cr. (5), Register, June, 1991, No. 426, eff. 7-1-91.

**Tax 2.19 Instalment method of accounting for corporations.** (s. 71.11 (8), 1985 Stats.). (1) Subject to the approval of the department of revenue, a sale or other disposition by a corporation of real property, or a casual sale or other casual disposition of personal property, other than personal property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, may be reported on the instalment basis. On the instalment basis there shall be reported as income from the instalment sale in any taxable year that proportion of the instalment payments actually received in that year which the gross profit realized or to be realized when payment is completed, bears to the total contract price.

Note: Refer to *Castle Corporation vs. Wis. Dept. of Revenue*, 142 Wis. 2d 716 (1987).

(2) Use of the instalment method, in each instance, shall be conditional upon the implied agreement of the corporation to take into income in any year in which it distributes the instalment obligation, the unreported balance of gain on the instalment sale or exchange. But the transfer of an instalment sale obligation by merger or consolidation pursuant to s. 71.368 (1) (a) 1, 1985 Stats., is not a distribution by the merged or consolidated corporation as long as the surviving or consolidated corporation continues to report the gain to the state.

Note: Refer to *Falls Communications, Inc. v. Wis. Dept. of Revenue*, 131 Wis. 2d 545 (1986). Register, June, 1991, No. 426

(3) The instalment method shall not be permitted with respect to any instalment sale or exchange made subsequent to adoption of a plan of liquidation to which s. 71.337, 1985 Stats., applies.

(4) Corporations regularly engaged in the business of selling personal property and keeping records on the instalment basis will be required to report for franchise or income tax purposes on the accrual basis.

(5) The expenses incident to each instalment sale or exchange must be deferred on the same basis that the profit arising from the sale or exchange is deferred.

(6) When property is sold or exchanged on the instalment basis at a loss, the loss may not be deferred beyond the taxable year in which the sale or exchange takes place.

(7) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, this section does not apply to taxable year 1987 or to taxable years thereafter.

**History:** 1-2-56; am. (2), Register, March, 1966, No. 123, eff. 4-1-66; r. and recr. Register, October, 1966, No. 130, effective with respect to income years beginning on and after January 1, 1967; am. Register, February, 1975, No. 230, eff. 3-1-75; am. (1), Register, September, 1983, No. 333, eff. 10-1-83; am. (1) to (3) and (6), cr. (7), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.20 Accounting for acceptance corporations, dealers in commercial paper, mortgage discount companies and small loan companies.** (s. 71.11 (8), 1985 Stats.) (1) Except as otherwise provided in sub. (2), acceptance corporations and dealers in commercial paper shall report the discount on the purchase of paper as income in the year of purchase.

(2) Acceptance corporations and dealers in commercial paper may elect to report their income on the deferred profit basis, provided that their books and records are kept on that basis and provided further that both the deferment of income, and the expenses incurred in producing the income are made in accordance with generally accepted accounting principles and practice. The election of or change to the deferred profit basis shall be made before the close of the year for which the return is made, and after having made the election or change, the deferred profit basis of reporting shall be adhered to in all subsequent periods. Those corporations which report their income on the accrual method are not required to obtain authorization from the department to change from the method under sub. (1) to the deferred profit basis if notice of this change is given to the department in writing before the close of the year in which the change is to be made.

(3) Where the records of acceptance corporations and dealers in commercial paper are kept on the deferred profit basis, schedules shall be attached to the tax returns clearly setting forth the unrealized profit accounts and reconciling the income and surplus per books with net income.

(4) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, this section does not apply to taxable year 1987 or to taxable years thereafter.

**History:** 1-2-56; correction in (1) made under s. 13.93 (2m) (b) 4, Stats., Register, July, 1987, No. 379; am. (1), renum. (2) and (3) to be (3) and (2) and am., cr. (4), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.21 Accounting for incorporated contractors.** (ss. 71.11 (8), 1985 Stats. and 71.25 (5), Stats.) (1) The general rules for reporting income on the accrual basis apply to incorporated contractors except that, in the case of contracts upon which work is performed in 2 or more consecutive taxable years, the percentage of completion basis may be used provided such basis clearly reflects the income taxable under ch. 71, Stats. Under the percentage of completion method, a portion of the total contract price is treated as sales for the current period. This portion may be determined by an engineer's or an architect's estimate or by another method which will clearly reflect the income realized to date. The difference between the sales thus determined and the actual cost incurred, adjusted for inventories of materials at the end of the year, is reported as gain or loss for the taxable year.

(2) The profit on jobs taken on a cost plus basis and uncompleted at the close of a taxable year shall be computed in accordance with the terms of the contract and reported at that time, and may not be deferred until the year in which the contract is completed.

(3) The income derived from the performance of construction activities within Wisconsin by a nonresident contractor is attributable to Wisconsin and is subject to the Wisconsin franchise or income tax. If the operations in Wisconsin of the nonresident contractor are part of a unitary business, the apportionment method shall be used to determine Wisconsin income, and the separate accounting method may not be used without permission from the department.

(4) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, subs. (1) and (2) do not apply to taxable year 1987 or to taxable years thereafter.

**History:** 1-2-56; am. (1), Register, March, 1966, No. 123, eff. 4-1-66; am. Register, February, 1975, No. 230, eff. 3-1-75; am. (1) and (2), r. and recr. (3), cr. (4), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.22 Accounting for incorporated dealers in securities.** (s. 71.11 (8), 1985 Stats.) (1) Dealers in securities shall report for franchise or income tax purposes on the accrual method of accounting.

(2) Inventories of securities held for sale shall be reported on a consistent basis conforming to that used in the trade or business.

(3) Securities held for investment purposes shall be reported at cost, and any increase or decrease in value shall be reported only at the time of sale.

(4) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, this section does not apply to taxable year 1987 or to taxable years thereafter.

**History:** 1-2-56; r. and recr. Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.24 Accounting for incorporated retail merchants.** (s. 71.11 (8), 1985 Stats.) (1) The "retail method" of valuing inventories is acceptable when it is consistently followed and adequate records are kept. When a change is made to the retail method of valuing inventories from another method of valuing inventories, the difference between the beginning inventory, taken on the old basis, and the beginning inventory, taken on the basis of the "retail method," will constitute an increase or decrease in income for Register, June, 1991, No. 426

the year in which the change is made. Retail merchants shall report all other items of income and expense on the accrual method.

(2) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, this section does not apply to taxable year 1987 or to taxable years thereafter.

History: 1-2-56; am., cr. (2), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.25 Corporation accounting generally.** (s. 71.11 (8) and (9), 1985 Stats.) (1) In a business requiring the use of inventories, income is properly computed by the accrual method of accounting. Inventories taken in accordance with the best accounting practice in the trade or business and used by the taxpayer to clearly reflect income are accepted.

(a) Except for other methods of computing inventory recognized in this chapter, the 2 most commonly used bases in valuing inventories are cost and lower of cost or market.

(b) Whether the cost or the lower of cost or market basis of valuing inventories is used, the basis adopted must be applied with reasonable consistency to the entire inventory, and no change from one basis to the other will be permitted without written permission from the department of revenue.

(2) Inventories and inventory records must be preserved as a part of the accounting records of the taxpayer and available for examination and verification.

(3) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, this section does not apply to taxable year 1987 or to taxable years thereafter.

History: 1-2-56; am. (1) (b), Register, September, 1964, No. 105, eff. 10-1-64; am. Register, February, 1975, No. 230, eff. 3-1-75; am. (1) (intro.) and (a), cr. (3), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.26 "Last in, first out" method of computing inventory for corporations.** (s. 71.11 (9), 1985 Stats.) Any corporation permitted or required to take inventories pursuant to s. 71.11 (9), 1985 Stats., may elect to compute its inventory in accordance with the method provided by section 472 of the internal revenue code, provided that:

(1) The same method of computing inventory is used in reporting income to the internal revenue service, and the inventories used in reporting income to the internal revenue service and to the department of revenue agree both as to computation and amounts except as provided in sub. (5).

(2) Except as otherwise provided in this section, the change to and the use of the last in, first out method of inventorying shall be subject to and conditioned upon all of the regulations promulgated with respect to this method of computing inventory by the internal revenue service.

(3) A statement of election to use the last in, first out method shall be filed with the department of revenue in the same form as required by the internal revenue service, and shall be filed with the return for the taxable year in which the change is to be made effective. The opening inventory for the period in which the election to change is exercised shall be taken on the basis previously accepted and approved.

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(4) Except as provided in sub. (5), any corporation which has been computing its inventory for Wisconsin franchise or income tax purposes in accordance with s. 472 of the internal revenue code and which has been authorized or directed by the internal revenue service to change its method of inventory valuation for federal income tax purposes shall also change its method of inventory valuation for Wisconsin franchise or income tax purposes. To correlate its Wisconsin basis with the federal basis, the opening inventory for the taxable year in which the change is made shall be reported on the basis previously accepted and approved whereas the closing inventory shall be on the new method of valuation. No adjustment is to be made to the closing inventory of the preceding taxable year. Notice of the change in method shall be filed with the return on which it is effective and shall be supported by a copy of the authorization or order to change inventory method for federal income tax purposes.

(5) Any corporation which has been authorized or directed by the internal revenue service to treat the cutting of timber as a sale or exchange of timber for purposes of computing its federal income tax liability and has included in its inventory for federal income tax purposes, the excess of the fair market value of the timber over its adjusted basis, may exclude from its inventory, for Wisconsin franchise or income tax purposes, the excess of the fair market value of the timber over its adjusted basis, or may, with the consent of the department of revenue, include the excess in its inventory for Wisconsin franchise or income tax purposes subject to the conditions the department may prescribe.

(6) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, this section does not apply to taxable year 1987 or to taxable years thereafter.

**History:** 1-2-56; am. (2) and (6), and cr. (7), Register, March, 1960, No. 51, eff. 4-1-60; am. intro. par., (6) and (7), Register, March, 1966, No. 123, eff. 4-1-66; am. Register, February, 1975, No. 230, eff. 3-1-75; am. (5), (6) and (7), Register, September, 1983, No. 333, eff. 10-1-83; r. (1) and (5), renum. (2) to (4) and (6) and (7) to be (1) to (5) and am., cr. (6), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.30 Property located outside Wisconsin — depreciation and sale.** (ss. 71.05 (12) (a), (b) and (c), (15), (16), (17) and (18) and 71.04 (1) (a), Stats.) (1) **SCOPE.** This section applies only with respect to resident individuals, estates, and trusts.

(2) **DEFINITION.** In this section, "internal revenue code" means the internal revenue code in effect for the taxable year specified in s. 71.01 (6), Stats.

**Example:** For taxable year 1988, "internal revenue code" means the internal revenue code in effect on December 31, 1987.

(3) **RESIDENT INDIVIDUALS, ESTATES, AND TRUSTS.** Income or loss derived from property and business located outside Wisconsin by resident individuals, estates, and trusts, is taxable or deductible as appropriate under ch. 71, Stats. Except as provided in sub. (4), the basis for depreciation and for determining gain or loss on disposition of property for these taxpayers is the same as the basis determined under the internal revenue code, whether the property was acquired before becoming or while a resident of this state.

(4) **EXCEPTIONS.** (a) When an individual acquires a new residence, the adjusted basis of the new residence is not reduced for nonrecognized gain Register, June, 1991, No. 426

from the sale or exchange of an old residence located outside Wisconsin if:

1. The sale or exchange of the old residence occurred in taxable year 1975 or thereafter when the individual was not a resident of Wisconsin; or
2. The sale or exchange of the old residence occurred before taxable year 1975, whether the individual was a resident or not at the time of the sale or exchange.

(b) When an individual sells or exchanges a principal residence located outside Wisconsin and the nonrecognition of gain provisions do not apply, the adjusted basis of the residence sold or exchanges is not reduced for nonrecognized gain from any previous sale or exchange of a principal residence located outside Wisconsin if:

1. The previous sale or exchange occurred in taxable year 1975 or thereafter when the individual was not a resident of Wisconsin; or
2. The previous sale or exchange occurred before taxable year 1975, whether the individual was a resident or not at the time of the sale or exchange.

**Example:** A taxpayer becomes a Wisconsin resident on July 1, 1988. Prior to becoming a Wisconsin resident the taxpayer had owned several different homes. Each time a new home was acquired, the federal nonrecognition of gain provisions applied with respect to the gain realized from the sale of the previous home. Upon becoming a Wisconsin resident, the taxpayer owned a home in Missouri with a federal adjusted basis of \$65,000 (\$95,000 cost, less \$30,000 of gains postponed from prior sales). The Missouri home was sold for \$97,000 in August 1988. The taxpayer decides not to purchase a new residence. The Wisconsin adjusted basis of the Missouri home is \$95,000.

(c) For residential real property and certain agricultural real property placed in service during taxable year 1986, depreciation and gain or loss on disposition of the property shall be computed under the internal revenue code in effect on December 31, 1980 unless:

1. The property is placed in service out-of-state by a taxpayer during taxable year 1986 before the taxpayer becomes a Wisconsin resident. In this case, the property's adjusted basis and depreciation are the same as the amounts allowable for federal tax purposes.

**Example:** A taxpayer becomes a Wisconsin resident on January 1, 1987. Prior to that date, the taxpayer is an Illinois resident. On July 1, 1986, the taxpayer purchases and places in service residential real property located in Illinois. On the taxpayer's 1987 Wisconsin return, the taxpayer's adjusted basis and depreciation on this property will be the same as the amounts shown on the taxpayer's 1987 federal return. The taxpayer does not have to recompute the basis of the property and depreciate it using one of the methods permitted under the December 31, 1980 Code.

2. The property located out-of-state is acquired in a transaction occurring in taxable year 1986 or thereafter where the basis of the property in the hands of the transferee is the same as the adjusted basis of the property in the hands of the transferor. The adjusted basis of the property on the date of the transfer is the same as the federal adjusted basis.

**Example:** A taxpayer is a Wisconsin resident. The taxpayer receives by gift on January 1, 1986, residential real property located in Illinois. The adjusted basis of the property to the donor, transferor, is \$200,000. In acquiring the property by gift, the taxpayer, transferee, receives the same adjusted basis in the property as the transferor. The Wisconsin adjusted basis will be the federal adjusted basis on January 1, 1986.

**Note:** 1) In the case of *Wisconsin Department of Revenue vs. Romain A. Howick*, 100 Wis. 2d 274 (1981), the Wisconsin supreme court held that for the purpose of determining a loss on a sale, the basis of property located outside Wisconsin acquired before the owner became a Wisconsin resident is the basis determined under the internal revenue code. In this section the same principle is applied to gains realized on the disposition of such property. This principle was codified into s. 71.05 (1) (m), Stats., by 1985 Wis. Act 261, effective for the earliest tax-

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ble year in respect to which additional assessments or refunds may be made. Section 71.05 (1) (n) and (o), Stats., was also created by 1985 Wis. Act 261 to provide exceptions with respect to a principal residence effective for the same period of time. Section 71.05 (1), (m), (n), and (o), Stats., was renumbered s. 71.05 (12) (a), (b), and (c), Stats., by 1987 Wis. Act 312.

2) Section 71.07 (1), Stats., was amended by Chapter 39, Laws of 1975, effective with the 1975 taxable year. Prior to the 1975 taxable year, income or loss derived from real property or tangible personal property followed the situs of the property from which derived. Section 71.07 (1), Stats., was renumbered ss. 71.04 (1) (a) and 71.362 (1), Stats., by 1987 Wis. Act 312.

**History:** Cr. Register, April, 1978, No. 268, eff. 5-1-78; r. and recr. (3), Register, July, 1982, No. 319, eff. 8-1-82; r. (2), renum. (1) to be (2) and am., cr. (1) and (4), am. (3), Register, June, 1990, No. 414, eff. 7-1-90.

**Tax 2.31 Taxation of personal service income of nonresident professional athletes.** **History:** Cr. Register, December, 1980, No. 300, eff. 1-1-81; r. Register, June, 1993, No. 450, eff. 7-1-93.

### Determination of Income from Multistate Operations

**Tax 2.39 Apportionment method.** (ss. 71.04 (4), (5), (6), (7), (9), (10) and (11) and 71.25 (5), (6), (7), (8), (9), (11) and (12), Stats.) (1) **GENERAL.** Except as provided in sub. (3) (a), any person, except resident individuals, resident estates and resident trusts, engaged in business both within and without Wisconsin shall report by the statutory apportionment method when the person's business in Wisconsin is an integral part of a unitary business unless the department, in writing, allows reporting on a different basis.

**Note:** Refer to ss. 71.04 (4) and 71.25 (6), Stats.

(2) **DEFINITIONS.** In this section:

(a) "Apportionable income" has the meaning in s. 71.25 (5) (a), Stats.

(b) "Engaged in business within and without Wisconsin" means having business activity which is sufficient to create nexus in Wisconsin and at least one other state or foreign country.

(c) "Gross receipts" means gross sales less returns and allowances, plus service charges, freight, carrying charges or time-price differential charges incidental to the sales. Federal and state excise taxes, including sales and use taxes, shall be included as part of the receipts if the taxes are passed on to the purchaser or included as part of the selling price of the product.

(d) "Nexus" means that a taxpayer's business activity in a state or foreign country is of such a degree that the state or foreign country has jurisdiction to impose an income tax or franchise tax measured by net income on the taxpayer. Nexus may exist even if a state or foreign country does not impose a tax on the taxpayer. Conversely, voluntary filing and paying income or franchise taxes when not required to do so, or paying a fee for qualification, organization or for the privilege of doing business in that state or foreign country does not, in itself, create nexus.

**Note:** Refer to s. Tax 2.82 for a description of factors which are recognized in determining whether nexus exists.

**Examples:** 1) State A imposes a corporation franchise tax measured by net income for the privilege of doing business in that state. Corporation X files a return and pays the \$50 minimum tax, although it carries on no activities in State A. Corporation X does not have "nexus" in State A under these circumstances.

2) State B requires all nonresident corporations which qualify or register to do business in State B to pay to the Secretary of State an annual license fee or tax for the privilege of doing business in the state regardless of whether the privilege is in fact exercised. The amount paid is determined according to the total authorized capital stock of the corporation; the rates are progressively higher by bracketed amounts. The statute sets a minimum fee of \$50 and a maximum fee of \$500. Failure to pay the tax bars a corporation from utilizing the state courts for enforcement of its rights. State B also imposes a corporation income tax. Nonresident

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Corporation Y is qualified to do business in State B and pays the required fee to the Secretary of State but does not carry on any activities in State B other than utilizing its courts. Corporation Y does not have "nexus" in State B under these circumstances.

3) State C requires all nonresident corporations qualified or registered to do business in State C to pay to the Secretary of State an annual permit fee or tax for doing business in the state. The base of the fee or tax is the sum of (1) outstanding capital stock, and (2) surplus and undivided profits. The fee or tax base attributable to State C is determined by a three-factor apportionment formula. Nonresident Corporation Z, which operates a plant in State C, pays the required fee or tax to the Secretary of State. Corporation Z by virtue of its operation of a plant in State C has "nexus" in State C.

4) State D imposes a corporation franchise tax measured by net income for the privilege of doing business in that state. Corporation W files a return based upon its business activities in the state but the amount of computed liability is less than the minimum tax. Corporation W pays the minimum tax. Corporation W has "nexus" in State D under these circumstances.

5) Corporation U is actively engaged in manufacturing farm equipment in State E. State E imposes a net income tax but exempts corporations engaged in manufacturing farm equipment. Corporation U has "nexus" in State E under these circumstances.

6) Corporation V has a sales office and warehouse located in State F. State F doesn't impose a corporation franchise or income tax. Corporation V has "nexus" in State F.

(e) "Nonapportionable income" has the meaning in s. 71.25 (5) (b), Stats.

(f) "State" means any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, and any territory or possession of the United States. A foreign country is not a state.

(3) APPORTIONMENT FRACTION. (a) For the reporting of income for the purposes of franchise or income taxation, all businesses except financial organizations and public utilities as defined in ss. 71.04 (8) and 71.25 (10), Stats., shall use an apportionment fraction composed of a sales factor representing 50% of the fraction, a property factor representing 25% of the fraction and a payroll factor representing 25% of the fraction. Property, payroll or sales related to the production of nonapportionable income described in s. 71.04 (1) and (4) or 71.25 (5) (b), Stats., may not be included in either the numerator or the denominator of any of the apportionment factors. If one of these factors is omitted pursuant to s. 71.04 (10) or 71.25 (11), Stats., the percentages of the fraction represented by the remaining factors shall be adjusted as follows:

1. If either the property factor or payroll factor is omitted, the other factor shall represent 33 $\frac{1}{3}$  % of the fraction and the sales factor shall represent 66% % of the fraction.

2. If the sales factor is omitted, the property factor and the payroll factor shall each represent 50% of the fraction.

Note: See ss. Tax 2.46, 2.47, 2.48, 2.49, 2.50 and 2.505 for special apportionment fractions of interstate air carriers, motor carriers, pipelines, finance companies, public utilities and professional sports clubs.

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(d) *Player contracts, franchises, etc.* Income from player contract transactions, franchise fees, and other similar sources shall be excluded from the numerator and the denominator of the sales fraction.

History: Cr. Register, December, 1980, No. 300, eff. 1-1-81; am. (1) to (3) (intro.), (c) and (d), Register, July, 1989, No. 403, eff. 8-1-89.

### Gross Income

**Tax 2.51 Rent received by corporations from Wisconsin real estate.** (s. 71.03 (1) (b), 1985 Stats.) (1) Rentals must be included in the gross income when they accrue or are actually received by the taxpayer, depending upon the method of accounting used in reporting income. Rentals which have not actually been received in cash will be treated as received if available to or subject to the disposal of the landlord.

(2) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, sub. (1) does not apply to taxable year 1987 or to taxable years thereafter.

History: 1-2-56; renum. to be (1), cr. (2), Register, February, 1990, No. 410, eff. 3-1-90.

**Tax 2.53 Stock dividends and stock rights received by corporations.** (ss. 71.03 (1) (d) and (k), 71.305 and 71.307 (2), 1985 Stats.) (1) BASIS. If a shareholder receives new stock or stock rights as a distribution on old stock held before the distribution and under s. 71.305 (1), 1985 Stats., the distribution is not includable in gross income, then except as provided in s. 71.307 (2), 1985 Stats., the basis of the old stock with respect to which the distribution was made shall be allocated between the old and new stocks or rights in proportion to the fair market values of each on the date of distribution. If a shareholder receives new stock or stock rights as a distribution on old stock held before the distribution, and under s. 71.305 (1), 1985 Stats., a part of the distribution is not includable in gross income, except as provided in s. 71.307 (2), 1985 Stats., the basis of the old stock with respect to which the distribution is made shall be allocated between the old and new stocks or rights in proportion to the fair market values of each on the date of distribution without regard to the fair market value of any part of the distribution which is includable in gross income, pursuant to s. 71.305 (2), 1985 Stats. The date of distribution in each case shall be the date the stock or the rights are actually distributed to the stockholder and not the record date. The general rule in this subsection will apply to the stock rights only if these rights are exercised or sold.

(2) EXCEPTION. Under s. 71.307 (2), 1985 Stats., the basis of rights to buy stock which is excluded from gross income under s. 71.305 (1), 1985 Stats., shall be zero if the fair market value of the rights on the date of distribution is less than 15% of the fair market value of the old stock on that date, unless the shareholder elects to allocate part of the basis of the old stock to the rights. The election shall be made by a shareholder for all the rights received by the shareholder in a particular distribution and includes all the stock of the same class owned by the shareholder in the issuing corporation at the time of the distribution. The election to allocate basis to rights shall be in the form of a statement attached to the shareholder's return for the year in which the rights are received. This statement shall disclose the number of shares of the old stock owned by the shareholder on the date of distribution, the basis of these shares and the fair market value of the old shares and of the rights on the date of distribution. This election, once made, shall be irrevocable with respect

to the rights for which the election was made. Any shareholder making this election shall retain a copy of the election and of the return with which it was filed, in order to substantiate the use of an allocated basis upon a subsequent disposition of the stock acquired by exercise.

(3) **APPLICABILITY.** As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, this section does not apply to taxable year 1987 or to taxable years thereafter.

**History:** 1-2-56; am. (1) (intro.), renum. (1) (a) to be (2) and am., cr. (3), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.56 Insurance proceeds received by corporations.** (s. 71.03 (1) (d), 1985 Stats.) (1) Generally, interest on insurance proceeds paid to policy owners or beneficiaries is includable in income.

(2) Under an interest option clause in which all the principal proceeds are retained and interest is paid on the principal periodically, the interest is includable in income.

(3) Under an income option clause in which the principal proceeds and interest on the proceeds are paid in periodical instalments to the policy owner, the interest paid is includable in income.

(4) When, under an income option clause chosen by the beneficiary, payments are made to the beneficiary, the interest paid is includable in income.

(5) When, under an income option clause designated by the insured, payments are made to the beneficiary and the instalment payments are made under the insurance contract, no part of the payment is includable in income.

(6) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, this section does not apply to taxable year 1987 or to taxable years thereafter.

**History:** 1-2-56, r. (1), (3) (b), (3) (c) and (3) (d) and renum. (2) to be (1) and (3) (a) to be (1) (d), Register, March, 1966, No. 123, eff. 4-1-66; am. (1) (intro.), renum. (1) (a) to (d) to be (2) to (5) and am., cr. (6), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.57 Annuity payments received by corporations.** (s. 71.03 (1) (k), 1985 Stats.) (1) **AMOUNTS INCLUDABLE IN INCOME.** Annuity payments under an endowment or annuity contract are income to the extent of any payment after the Wisconsin adjusted tax basis has been recovered. However, when the contract provides for the separation of the periodic payments into principal and interest, the interest so received is income when received.

(2) **APPLICABILITY.** As a result of 1987 Wis. Act 27 which generally federalized Wis. corporate franchise and income tax law, sub. (1) does not apply to taxable year 1987 or to taxable years thereafter.

**History:** 1-2-56; renum. to be (1) and am., cr. (2), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.60 Dividends on stock sold "short" by corporations.** (s. 71.03 (1) (d), 1985 Stats.) (1) **DIVIDENDS PAID BEFORE DELIVERY.** When stock is sold "short" for later delivery and a dividend is paid before delivery, the purchaser, as owner of the borrowed stock, receives the dividend and shall include the dividend in taxable income. The amount credited to the lender of the stock and charged to the "short" seller is income upon Register, June, 1991, No. 426

which the lender is subject to tax. The amount charged to the "short" seller becomes part of the cost of the stock sold.

(2) **APPLICABILITY.** As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, sub. (1) does not apply to taxable year 1987 or to taxable years thereafter.

History: 1-2-56; renum. to be (1) and am., cr. (2), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.63 Dividends accrued on stock.** (s. 71.03 (1) (d), 1985 Stats.) (1) **AMOUNT INCLUDABLE IN INCOME.** In the case of stock purchased by a corporation between dividend dates, the entire amount of the future dividend when received is income to the purchaser and must be included in its income. The amount advanced by the purchaser to the seller in contemplation of the next dividend payment is an investment of capital and becomes part of the cost of the stock purchased.

(2) **APPLICABILITY.** As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, sub. (1) does not apply to taxable year 1987 or to taxable years thereafter.

History: 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66; renum. to be (1) and am., cr. (2), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.65 Interest received by corporations.** (ss. 71.03 (1) (c), 1985 Stats., and 71.26 (2), Stats.) (1) In general, all interest is includable in the income by which the franchise tax is measured, including interest received on monies invested in obligations of the United States government and its instrumentalities and agencies. If a corporation is not subject to the franchise tax, but is subject to net income taxation, interest on federal obligations is not taxable, but interest on postal savings and federal tax refunds is taxable. Profit or loss on the sale or other disposition of federal obligations is a taxable gain or deductible loss for purposes of both the franchise tax measured by net income and the net income tax.

(2) Interest is deemed to be received when accrued or received in cash, depending upon the method of accounting used by the taxpayer corporation. Interest becomes taxable to a corporation reporting on a cash basis when it is made available to it. Coupons on bonds which are due but have not been cashed are considered as received provided that the cash for payment of the coupons is available. Accrued interest paid on bonds purchased between interest payment dates shall be treated as a deduction from the interest received.

(3) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, sub. (2) does not apply to taxable year 1987 or to taxable years thereafter.

History: 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66; am. (1) and (2), cr. (3), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.70 Gain or loss on capital assets of corporations; basis of determining.** (s. 71.03 (1) (g), 1985 Stats.) (1) Profits or losses resulting from the sale or other disposition of capital assets are ordinarily taxable income or deductible losses for the year in which the sale or other disposition takes place. In certain cases of real estate sales involving deferred payments, the profit may be treated as not wholly realized in the year of sale and may be deferred in accordance with the terms of payment.

Note: Refer to s. Tax 2.19.

(2) The fair market value at January 1, 1911, shall be determined in the light of the facts and circumstances known as of that date. In the absence of competent evidence to the contrary, cost less depreciation sustained to January 1, 1911 will be considered the fair market value as of that date. The method of arriving at the January 1, 1911 value shall be clearly set forth in the franchise or income tax returns.

(3) Stocks, bonds and other securities are considered as capital assets when held by a person other than a dealer in securities. The profit or loss on sale or other disposition of securities is, therefore, determined in the same manner and on the same basis as that used for other capital assets.

Note: Refer to s. Tax 2.22.

(4) In determining the profit or loss on the sale of stock received as a stock dividend, the total Wisconsin adjusted tax basis of the original shares on which the dividend was declared is allocated to the new and old shares with due regard to the fair market value of the new and old shares at the date of the dividend.

(5) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, subs. (1), (2) and (3) do not apply to taxable year 1987 or to taxable years thereafter.

History: 1-2-56; am. (1) (intro.), renum. (1) (a) to (c) to be (2) to (4) and am., cr. (5), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.72 Exchanges of property by corporations generally.** (s. 71.03 (1) (g), 1985 Stats.) (1) Except when specifically provided by ch. 71, Stats., where property is exchanged for other property which has a fair market value, a taxable gain or deductible loss may be realized, and the fair market value shall be treated as the price realized for the property exchanged and the cost price of the property received, for purposes of future sale. When the property received in exchange has no determinable market value, the property received takes the place of the property exchanged, and no profit or loss is recognized, and in the event of future sale, the adjusted tax basis of the original property exchanged becomes the basis for computing the gain or loss on the property received in exchange.

(2) Except when specifically provided by ch. 71, Stats., where property of 2 different kinds is received in exchange for property, one kind having a determinable fair market value and the other no determinable fair market value, the gain is measured by the excess of the fair market value of the property received over the adjusted tax basis of the property exchanged. The property received which has no determinable fair market value is considered as having no cost in case of future sale, the entire proceeds of the sale being income. If the adjusted tax basis of the property exchanged is in excess of the fair market value of the property received in exchange, the excess shall be taken as the adjusted tax basis of the property received which has no determinable fair market value, no loss being recognized.

(3) In general there are 3 types of exchanges upon which exemption from tax may be claimed:

(a) Exchanges made pursuant to a plan of reorganization.

(b) Exchanges in which the property received in trade has no determinable market value.

(c) Exchanges of property held for productive use or investment pursuant to s. 71.03 (5), 1985 Stats.

(4) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, this section does not apply to taxable year 1987 or to taxable years thereafter.

**History:** 1-2-56; am. Register, February, 1958, No. 26, eff. 3-1-58; r. (4) (c) and renum. (4) (d) to be (4) (c) and am., Register, March, 1966, No. 123, eff. 4-1-66; r. (3) and renum. (4) to be (3), Register, February, 1975, No. 230, eff. 3-1-75; am. (1), (2) and (3) (c), cr. (4), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.721 Exchanges of property held for productive use or investment by corporations.** (s. 71.03 (5), 1985 Stats.) (1) Property held for productive use in a trade or business may be exchanged without recognition of gain or loss for property of a like kind held for investment as well as for property of a like kind held for productive use in a trade or business, and similarly, property held for investment may be exchanged without recognition of gain or loss for property of a like kind held for productive use in trade or business as well as for property of a like kind held for investment.

(2) The phrase "of a like kind" has reference to the nature or character of the property and not its grade or quality. One kind or class of property may not be exchanged tax free for property of a different kind or class.

**Examples:** 1) Unimproved real estate may be exchanged for unimproved real estate without recognition of gain or loss by a taxpayer not a dealer in real estate, because the properties are "like kind."

2) If unimproved real estate is exchanged for personal property, gain or loss is recognized, since the properties are not "like kind."

3) In an exchange of real estate for real estate by a dealer in real estate, gain or loss is recognized, since the property is part of its stock in trade.

**Note:** For taxable years prior to 1984, if the property transferred was located in Wisconsin, nonrecognition of gain or loss is only applicable if the property acquired was located in Wisconsin. For the taxable year 1984 and subsequent taxable years, s. 71.03 (5), 1985 Stats., was amended to remove the requirement that the replacement property be located in Wisconsin in order to qualify for nonrecognition of gain or loss.

(3) A leasehold interest in land cannot be exchanged tax free for a fee title unless the lease has 30 years or more to run.

(4) Where, as part of the consideration to the taxpayer, another party to the exchange assumed a liability of the taxpayer or acquired from the taxpayer property subject to a liability, the assumption or acquisition in the amount of the liability shall be considered as money received by the taxpayer on the exchange.

(5) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, this section does not apply to taxable year 1987 or to taxable years thereafter.

**History:** Cr. Register, February, 1958, No. 26, eff. 3-1-58; am. Register, March, 1966, No. 123, eff. 4-1-66; am. (1) and (4), cr. (5), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.73 Involuntary conversion by corporations.** (s. 71.03 (1) (g) 3, 1985 Stats.) (1) In all cases of gain on involuntary conversion where such gain is not recognized for franchise or income tax purposes, the property acquired in the replacement is deemed to take the place of the property destroyed for purposes of depreciation, depletion and profit or loss on subsequent sale or other disposition.

(2) In all cases of involuntary conversion which result in losses, such losses are allowable in the year in which the conversion takes place.

(3) (a) For 1980 and preceding taxable years, this section does not apply when insurance money received on the conversion of Wisconsin assets is used in replacement outside of Wisconsin. In this case, the gain or loss shall be reported in the year of conversion.

(b) For 1981 and subsequent taxable years, this section does not apply when insurance money received on the conversion of nonbusiness assets located in Wisconsin is used in replacement with similar property outside of Wisconsin. Also, this section does not apply when insurance money received on the conversion of business assets located in Wisconsin is used in replacement with similar property outside of Wisconsin, and at the time of replacement, the taxpayer is not subject to taxation under ch. 71, Stats. In these cases the gain or loss shall be reported in the year of conversion.

(4) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, subs. (1), (2) and (3) do not apply to taxable year 1987 or to taxable years thereafter.

*History:* 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66; am. (3), Register, September, 1983, No. 333, eff. 10-1-83; cr. (4), Register, February, 1990, No. 410, eff. 3-1-90.

**Tax 2.75 Recoveries by corporations.** (s. 71.03 (1) (k), 1985 Stats.) (1) Recoveries of items previously charged off as loss or as expense are income in the year of recovery.

(2) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, sub. (1) does not apply to taxable year 1987 or to taxable years thereafter.

*History:* 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66; am. (1), cr. (2), Register, February, 1990, No. 410, eff. 3-1-90.

**Tax 2.76 Refunds of taxes to corporations.** (s. 71.03 (1) (k), 1985 Stats.) (1) Refunds of federal, state or local taxes together with interest thereon which were allowed as deductions from gross income in previous years are includable in net income.

(2) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, sub. (1) does not apply to taxable year 1987 or to taxable years thereafter.

*History:* 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66; am. (1), cr. (2), Register, February, 1990, No. 410, eff. 3-1-90.

**Tax 2.80 Improvements on leased real estate, income to corporate lessor.** (s. 71.03 (1) (k), 1985 Stats.) (1) If improvements are made on leased property and the life of such improvements extends beyond the terms of the lease, the lessor derives income at the expiration of the lease measured by the fair market value of the improvements at that time.

(2) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, sub. (1) does not apply to taxable year 1987 or to taxable years thereafter.

*History:* 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66; am. (1), cr. (2), Register, February, 1990, No. 410, eff. 3-1-90.

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**Tax 2.81 Damages received by corporations.** (s. 71.03 (1) (k), 1985 Stats.) (1) Damages may result in income when recovered on account of injury to property or interference with property rights, when the amounts received as damages are in excess of the adjusted basis of the property destroyed. Damages, including punitive damages, recovered for libel of business reputation, breach of contract, or antitrust injury, are includable in income.

(2) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, sub. (1) does not apply to taxable year 1987 or to taxable years thereafter.

History: 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66; am. (1), cr. (2), Register, February, 1990, No. 410, eff. 3-1-90.

**Tax 2.82 Nexus.** (ss. 71.01 (1) and (2) and 71.10 (1), Stats.) (1) DEFINITIONS. In this rule:

(a) "Representative" does not include an independent contractor. A person may be considered a representative even though he or she may not be considered an employe for other purposes such as the withholding of income tax from commissions. If a person is subject to the direct control of the foreign corporation, he or she may *not* qualify as an independent contractor under P.L. 86-272. (*Herff Jones Company v. State Tax Commission*, Oregon Supreme Court, August 23, 1967, 430 P. 2d 998.)

(b) "Business location" includes a repair shop, parts department, purchasing office, employment office, warehouse, meeting place for directors, sales office, permanent sample or display room, research facility or a recreational facility for use of employes or customers. A residence of an employe or representative is not ordinarily considered a business location of the employer unless the facts indicate otherwise. It could be considered a business location under one or more of the following conditions: a portion of the residence is used exclusively for the business of the employer, the employe is reimbursed or paid a flat fee for the use of this space by the employer; the employe's phone is listed in the yellow pages under the name of the employer; the employe uses supplies, equipment or samples furnished by the employer; or the space is used by the employe to interview prospective employes, hold sales meetings, or discuss business with customers.

(2) BACKGROUND. (a) Every domestic corporation (one incorporated under Wisconsin's laws), except those exempt under s. 71.01 (3) Stats., and every "licensed" foreign corporation (one not incorporated in Wisconsin) is required to file a complete corporation franchise/income tax return (form 4 or 5) regardless of whether or not business was transacted.

(b) A foreign corporation is "licensed" if it has obtained a Certificate of Authority from the Wisconsin secretary of state to transact business in this state pursuant to s. 180.801, Stats. A "licensed" foreign corporation is presumed to be subject to Wisconsin franchise/income taxes.

(c) An unlicensed foreign corporation is subject to Wisconsin franchise/income taxes if it has "nexus" with Wisconsin. The purpose of this rule is to provide guidelines for determining what constitutes "nexus", that is, what business activities are needed for a foreign corporation to be subject to Wisconsin franchise/income taxes.



(3) FEDERAL LIMITATIONS ON TAXATION OF FOREIGN CORPORATIONS.

(a) *Federal constitutional provisions.* 1. Article I, Section 8 of the U.S. Constitution grants congress the power to regulate commerce with foreign nations and among the several states. States are prohibited from levying a tax which imposes a burden on interstate or foreign commerce. However, this does not mean states may not impose any tax on interstate commerce. A state tax on net income from interstate commerce which is fairly attributable to the state is constitutional. (*Northwestern States Portland Cement Co. v. Minnesota; Williams v. Stockham Valves & Fittings, Inc.*, 358 U.S. 450, 79 S. Ct. 357.)

2. Section I of the 14th Amendment protects taxpayers within any class against discrimination and guarantees a remedy against illegal taxation.

(b) *Federal Public Law 86-272.* 1. Under Public Law 86-272, a state may not impose its franchise/income tax on a business selling tangible personal property, if the *only* activity of that business is the solicitation of orders by its salesman or representative which orders are sent outside the state for approval or rejection, and are filled by delivery from a point outside the state. The activity must be *limited* to solicitation. If there is any activity which exceeds solicitation, the immunity from taxation under Public Law 86-272 is lost.

2. This law, enacted by congress in 1959, does not extend to:

a. Those businesses which sell services, real estate or intangibles in more than one state;

b. Domestic corporations; or

c. Foreign nation corporations, i.e., those not incorporated in the United States.

3. If the *only* activities in Wisconsin of a foreign corporation selling tangible personal property are those described below (a and b) such corporation is not subject to Wisconsin franchise/income taxes under P.L. 86-272:

a. Usual or frequent activity in Wisconsin by employes or representatives soliciting orders for tangible personal property which orders are sent outside this state for approval or rejection.

b. Solicitation activity by non-employe independent contractors, conducted through their own office or business location in Wisconsin.

(4) WHAT CONSTITUTES "NEXUS". (a) *Factors.* If a foreign corporation has one or more of the following activities in Wisconsin, it is considered to have "nexus" and shall be subject to Wisconsin franchise/income taxes:

1. Maintenance of any business location in Wisconsin, including any kind of office.

2. Ownership of real estate in Wisconsin.

3. Ownership of a stock of goods in a public warehouse or on consignment in Wisconsin.

4. Ownership of a stock of goods in the hands of a distributor or other non-employee representative in Wisconsin, if used to fill orders for the owner's account.

5. Usual or frequent activity in Wisconsin by employees or representatives soliciting orders with authority to accept them.

6. Usual or frequent activity in Wisconsin by employees or representatives engaged in a purchasing activity or in the performance of services (including construction, installation, assembly, repair of equipment).

7. Operation of mobile stores in Wisconsin (such as trucks with driver-salespersons), regardless of frequency.

8. Miscellaneous other activities by employees or representatives in Wisconsin such as credit investigations, collection of delinquent accounts, conducting training classes or seminars for customer personnel in the operation, repair and maintenance of the taxpayer's products.

9. Leasing of tangible property and licensing of intangible rights for use in Wisconsin.

10. The sale of other than tangible personal property such as real estate, services and intangibles in Wisconsin.

11. The performance of construction contracts and personal services contracts in Wisconsin.

(b) *How to obtain ruling.* The guidelines in par. (a) as to what activities constitute "nexus" should not be considered all-inclusive. A ruling may be requested about a particular foreign corporation as to whether it is subject to Wisconsin franchise/income taxes by writing to the Wisconsin Department of Revenue, Audit Technical Services Section, P.O. Box 8906, Madison, WI 53708.

History: Cr. Register, January, 1979, No. 277, eff. 2-1-79.

**Tax 2.83 Requirements for written elections as to recognition of gain in certain corporation liquidations.** (ss. 71.02 (2) (c) and (d), 71.317 (3) and 71.333, 1985 Stats.) (1) To qualify for the benefits of section 333 of the internal revenue code in computing Wisconsin net income, a qualified electing shareholder, other than a corporate shareholder, shall file with the department federal form 964 in accordance with the instructions contained thereon within 30 days of the adoption of the plan of liquidation.

(2) To qualify for the benefits of s. 71.333, 1985 Stats., a corporation, other than an excluded corporation, that is a qualified electing shareholder, shall file with the department federal form 964 in accordance with the instructions contained thereon within 30 days of the adoption of the plan of liquidation.

(3) Another copy of the form 964 shall be attached to and made a part of the shareholder's income or franchise tax return for the taxable year in which the transfer of all the property under the liquidation occurs.

(4) Once made, an election may not subsequently be changed.

(5) Written elections shall be mailed to the Wisconsin Department of Revenue, P.O. Box 8908, Madison, WI 53708.

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(6) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, this section does not apply to taxable year 1987 or to taxable years thereafter except if a corporation elects, under s. 3047 (1) (c) of the Act to apply to the transaction ss. 71.301 to 71.372, 1985 Stats.

**History:** Cr. Register, January, 1979, No. 277, eff. 2-1-79; am. (1), Register, September, 1983, No. 333, eff. 10-1-83; am. (1), (2) and (4), cr. (6), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 2.86 Income to corporations from cancellation of government contracts.** (s. 71.03 (1) (k), 1985 Stats.) (1) Amounts claimed under cancelled government contracts not reported in the return for the year in which the claim was filed shall be included as income in the year in which the claim is allowed.

(2) As a result of 1987 Wis. Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, sub. (1) does not apply to taxable year 1987 or to taxable years thereafter.

**History:** 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66; am. (1), cr. (2), Register, February, 1990, No. 410, eff. 3-1-90.

**Tax 2.87 Reduction of delinquent interest rate under s. 71.13 (1) (b), Stats.** ( s. 71.13 (1) (b), Stats.) (1) PROCEDURES. The secretary may reduce the delinquent interest rate from 18% to 12% per year when the secretary determines the reduction fair and equitable, if the person from whom delinquent taxes are owing:

(a) Requests the reduction in writing, addressed to the Wisconsin Department of Revenue, Delinquent Tax Collection System, P.O. Box 8901, Madison, WI 53708.

(b) Clearly indicates why it is fair and equitable for the rate of interest to be reduced. Information regarding one or more of the factors under sub. (2) may be indicated.

(c) Is current in all return and report filings and tax payments for all matters other than the delinquencies for which interest reduction is being sought.

(d) Pays the taxes, reduced amount of interest and any penalties associated with them within 30 days of receiving notice from the department of the reduction.

(2) FACTORS FOR SECRETARY'S CONSIDERATION. In determining whether an interest rate reduction is fair and equitable, the secretary may consider the following factors:

(a) The taxpayer's prior record of reporting and payment to the department.

(b) The taxpayer's financial condition.

(c) Any circumstances which may have prevented payment such as death, imprisonment, hospitalization or other institutionalization.

(d) Any unusual circumstances which may have caused the taxpayer to incur the delinquency or prevent its payment.

(e) Any other factor which the secretary believes pertinent.