



State of Wisconsin
2015 - 2016 LEGISLATURE

LRB-4157/1
KRP&JK:emw&kjf

2015 ASSEMBLY BILL 623

December 29, 2015 – Introduced by Representatives MACCO, KOYENGA, KATZMA, JARCHOW, NOVAK, TAUCHEN, DUCHOW, KNODL, E. BROOKS, R. BROOKS, JACQUE and MURPHY, cosponsored by Senators MARKLEIN, GUDEX and ROTH. Referred to Committee on Ways and Means.

1 **AN ACT** *to repeal* 20.566 (1) (hn), 71.10 (1m) (b) 1. and 2., 71.30 (2m) (b) 1. and
2 2., 71.80 (1m) (b) 1. and 2. and 73.03 (28d); *to renumber and amend* 71.10
3 (1m) (b) (intro.), 71.30 (2m) (b) (intro.), 71.80 (1m) (b) (intro.) and 77.54 (60) (a);
4 **to amend** 71.07 (5n) (a) 3., 71.07 (5n) (a) 4., 71.10 (1m) (c), 71.28 (5n) (a) 3.,
5 71.28 (5n) (a) 4., 71.30 (2m) (c), 71.80 (1m) (c), 71.80 (9m) (intro.), 73.16 (3) (b),
6 77.51 (2), 77.51 (11d), 77.54 (60) (b), 77.54 (60) (c) and 77.61 (19) (intro.); and
7 **to create** 73.03 (72), 73.03 (73), 77.51 (12t), 77.54 (60) (bm) and 77.54 (60) (d)
8 2., 3. and 4. of the statutes; **relating to:** individual and corporate income and
9 franchise taxes; sales and use taxes; administration of tax laws; providing an
10 exemption from emergency rule procedures; and requiring the exercise of
11 rule-making authority.

Analysis by the Legislative Reference Bureau

This bill makes various changes to Wisconsin tax law related to individual and corporate income and franchise taxes, sales and use taxes, and the administration of tax laws.

ASSEMBLY BILL 623

Under current law, the Department of Revenue (DOR) may impose certain penalties if a taxpayer fails to produce records and documents requested by DOR to substantiate amounts or other information required to be shown on a tax return. This bill provides that those penalties may not be imposed until after DOR has issued a summons seeking the records and documents, and the taxpayer has failed to comply with the summons.

Under current law, if a taxpayer engages in a transaction without economic substance to create a loss, to reduce taxable income, or to increase credits allowed in determining Wisconsin tax, DOR may disregard the transaction for purposes of calculating the taxpayer's tax liability. This bill eliminates the factors under current law that determine whether a transaction has economic substance and replaces those factors with the factors set forth in federal law.

Under current law, a person may claim an income or franchise tax credit based on the person's qualified production activities income derived from manufacturing or agriculture in this state. Qualified production activities income includes certain direct costs and indirect costs, which are defined to include ordinary and necessary expenses paid or incurred in carrying on a trade or business that are deductible under the Internal Revenue Code. This bill changes the definitions of direct costs and indirect costs to also include a reasonable allowance for the exhaustion and wear and tear (including a reasonable allowance for obsolescence) of property that is deductible as depreciation under the Internal Revenue Code.

For income tax purposes, current law provides that any income of a nonresident individual, estate, or trust may be taxed by the state in which the business, property, or service from which the income is derived is located. This bill requires DOR to promulgate rules establishing the criteria to be used in determining whether a business, property, or service is located in this state for income and franchise tax purposes. The bill also prohibits DOR from relying on any factors not set forth in the rules when making the determination.

Under current law, DOR may tax the income of a taxpayer if the taxpayer is subject to the jurisdiction of this state, and DOR only taxes so much of the taxpayer's income that is allocated or apportioned to this state under a set of rules set forth in current law. Current law also provides that, if certain income of a taxpayer is not taxable by another state because the taxpayer is not subject to the jurisdiction of that state, DOR may tax that income under the state's throwback law. This bill requires DOR to promulgate rules establishing the criteria to be used in determining whether a taxpayer is subject to the jurisdiction of this state or any other state for income and franchise tax purposes. The bill also prohibits DOR from relying on any factors not set forth in the rules when making the determination.

Under current law, there is a sales and use tax exemption for property, items, and services sold by a contractor as part of a lump sum contract for real property construction activities if the total sales price attributable to the taxable materials is less than 10 percent of the total contract price. Under the bill, the exemption for lump sum contracts is expanded to apply to all construction contracts involving real property construction activities if the total sales price of the taxable materials is less

ASSEMBLY BILL 623

than 10 percent of the total contract price. If the exemption applies, the contractor is the consumer of, and pays the sales tax on, the materials.

The bill also provides that, if the prime contract qualifies for the exemption, the exemption applies to all subcontracts entered into with respect to the real property construction activities. If the exemption applies to a subcontract, the subcontractor is the consumer of, and pays the sales tax on, the materials.

This bill also eliminates DOR's obligation and authority to participate in the Multistate Tax Commission Audit Program.

Because this bill relates to an exemption from state or local taxes, it may be referred to the Joint Survey Committee on Tax Exemptions for a report to be printed as an appendix to the bill.

For further information see the *state and local* fiscal estimate, which will be printed as an appendix to this bill.

The people of the state of Wisconsin, represented in senate and assembly, do enact as follows:

1 **SECTION 1.** 20.566 (1) (hn) of the statutes is repealed.

2 **SECTION 2.** 71.07 (5n) (a) 3. of the statutes, as affected by 2015 Wisconsin Act
3 55, is amended to read:

4 71.07 **(5n)** (a) 3. "Direct costs" includes all of the claimant's ordinary and
5 necessary expenses paid or incurred during the taxable year in carrying on the trade
6 or business that are deductible as business expenses, and a reasonable allowance for
7 the exhaustion and wear and tear, including a reasonable allowance for obsolescence,
8 of property that is deductible as depreciation, under the Internal Revenue Code, as
9 defined in s. 71.01 (6), other than the sum of the cost of goods sold that are allocable
10 to the claimant's production gross receipts under subd. 8., and identified as direct
11 costs in the claimant's managerial or cost accounting records.

12 **SECTION 3.** 71.07 (5n) (a) 4. of the statutes, as affected by 2015 Wisconsin Act
13 55, is amended to read:

14 71.07 **(5n)** (a) 4. "Indirect costs" includes all of the claimant's ordinary and
15 necessary expenses paid or incurred during the taxable year in carrying on the trade

ASSEMBLY BILL 623

1 or business that are deductible as business expenses, and a reasonable allowance for
2 the exhaustion and wear and tear, including a reasonable allowance for obsolescence,
3 of property that is deductible as depreciation, under the Internal Revenue Code, as
4 defined in s. 71.01 (6), other than cost of goods sold and direct costs, and identified
5 as indirect costs in the claimant's managerial or cost accounting records.

6 **SECTION 4.** 71.10 (1m) (b) (intro.) of the statutes is renumbered 71.10 (1m) (b)
7 and amended to read:

8 71.10 (1m) (b) A transaction has economic substance only if ~~the taxpayer shows~~
9 ~~all of the following:~~ the transaction is treated as having economic substance under
10 section 7701 (o) of the Internal Revenue Code.

11 **SECTION 5.** 71.10 (1m) (b) 1. and 2. of the statutes are repealed.

12 **SECTION 6.** 71.10 (1m) (c) of the statutes is amended to read:

13 71.10 (1m) (c) With respect to ~~transactions~~ a transaction between members of
14 a controlled group, as defined in section 267 (f) (1) of the Internal Revenue Code, ~~such~~
15 ~~transactions~~ the transaction shall be presumed to lack economic substance, and the
16 taxpayer shall bear the burden of establishing by ~~clear and convincing a~~
17 preponderance of the evidence that ~~a~~ the transaction or ~~a~~ the series of transactions
18 between the taxpayer and one or more members of the controlled group has economic
19 substance.

20 **SECTION 7.** 71.28 (5n) (a) 3. of the statutes, as affected by 2015 Wisconsin Act
21 55, is amended to read:

22 71.28 (5n) (a) 3. "Direct costs" includes all of the claimant's ordinary and
23 necessary expenses paid or incurred during the taxable year in carrying on the trade
24 or business that are deductible as business expenses, and a reasonable allowance for
25 the exhaustion and wear and tear, including a reasonable allowance for obsolescence,

ASSEMBLY BILL 623

1 of property that is deductible as depreciation, under the Internal Revenue Code, as
2 defined in s. 71.01 (6), other than the sum of the cost of goods sold that are allocable
3 to the claimant's production gross receipts under subd. 8., and identified as direct
4 costs in the claimant's managerial or cost accounting records.

5 **SECTION 8.** 71.28 (5n) (a) 4. of the statutes, as affected by 2015 Wisconsin Act
6 55, is amended to read:

7 71.28 **(5n)** (a) 4. "Indirect costs" includes all of the claimant's ordinary and
8 necessary expenses paid or incurred during the taxable year in carrying on the trade
9 or business that are deductible as business expenses, and a reasonable allowance for
10 the exhaustion and wear and tear, including a reasonable allowance for obsolescence,
11 of property that is deductible as depreciation, under the Internal Revenue Code, as
12 defined in s. 71.01 (6), other than cost of goods sold and direct costs, and identified
13 as indirect costs in the claimant's managerial or cost accounting records.

14 **SECTION 9.** 71.30 (2m) (b) (intro.) of the statutes is renumbered 71.30 (2m) (b)
15 and amended to read:

16 71.30 **(2m)** (b) A transaction has economic substance only if ~~the taxpayer shows~~
17 ~~both of the following:~~ the transaction is treated as having economic substance under
18 section 7701 (o) of the Internal Revenue Code.

19 **SECTION 10.** 71.30 (2m) (b) 1. and 2. of the statutes are repealed.

20 **SECTION 11.** 71.30 (2m) (c) of the statutes is amended to read:

21 71.30 **(2m)** (c) With respect to ~~transactions~~ a transaction between members of
22 a controlled group, as defined in section 267 (f) (1) of the Internal Revenue Code, ~~such~~
23 ~~transactions~~ the transaction shall be presumed to lack economic substance, and the
24 taxpayer shall bear the burden of establishing by ~~clear and convincing~~ a
25 preponderance of the evidence that ~~a~~ the transaction or a ~~the~~ series of transactions

ASSEMBLY BILL 623

1 between the taxpayer and one or more members of the controlled group has economic
2 substance.

3 **SECTION 12.** 71.80 (1m) (b) (intro.) of the statutes is renumbered 71.80 (1m) (b)
4 and amended to read:

5 71.80 **(1m)** (b) A transaction has economic substance only if ~~the taxpayer shows~~
6 ~~both of the following:~~ the transaction is treated as having economic substance under
7 section 7701 (o) of the Internal Revenue Code.

8 **SECTION 13.** 71.80 (1m) (b) 1. and 2. of the statutes are repealed.

9 **SECTION 14.** 71.80 (1m) (c) of the statutes is amended to read:

10 71.80 **(1m)** (c) With respect to ~~transactions~~ a transaction between members of
11 a controlled group, as defined in section 267 (f) (1) of the Internal Revenue Code, ~~such~~
12 ~~transactions~~ the transaction shall be presumed to lack economic substance, and the
13 taxpayer shall bear the burden of establishing by ~~clear and convincing a~~
14 preponderance of the evidence that ~~a~~ the transaction or ~~a~~ the series of transactions
15 between the taxpayer and one or more members of the controlled group has economic
16 substance.

17 **SECTION 15.** 71.80 (9m) (intro.) of the statutes is amended to read:

18 71.80 **(9m)** FAILURE TO PRODUCE RECORDS. (intro.) A person who fails to produce
19 records or documents, as provided under ss. s. 71.74 (2) and 73.03 (9), that support
20 amounts or other information required to be shown on any return required under
21 this chapter and fails to comply in good faith with a summons issued pursuant to s.
22 73.03 (9) seeking those records and documents may be subject to any of the following
23 penalties, as determined by the department, except that the department may not
24 impose a penalty under this subsection if the person shows that under all facts and

ASSEMBLY BILL 623

1 circumstances the person's response, or failure to respond, to the department's
2 request was reasonable or justified by factors beyond the person's control:

3 **SECTION 16.** 73.03 (28d) of the statutes is repealed.

4 **SECTION 17.** 73.03 (72) of the statutes is created to read:

5 73.03 (72) To promulgate rules establishing the criteria to be used in
6 determining whether a business, property, or service has its situs in this state,
7 including for purposes of determining situs of income under s. 71.04, 71.25, 71.255
8 (5), or 71.362. In determining whether a business, property, or service has its situs
9 in this state, the department may not consider criteria not specified in the rules.

10 **SECTION 18.** 73.03 (73) of the statutes is created to read:

11 73.03 (73) To promulgate rules establishing the criteria to be used in
12 determining to which states' jurisdiction a taxpayer is subject for income or franchise
13 tax purposes for any part of a taxable year, including for purposes of determining
14 apportionment of income under s. 71.04, 71.25, 71.255 (5), or 71.362. In determining
15 whether a taxpayer is subject to the jurisdiction of this state or another state for a
16 taxable year, the department may not consider criteria not specified in the rules.

17 **SECTION 19.** 73.16 (3) (b) of the statutes is amended to read:

18 73.16 (3) (b) This subsection does not apply to any period associated with an
19 audit determination, if the period begins after the promulgation of a rule,
20 dissemination of written guidance to the public or to the person who is subject to the
21 audit determination, the effective date of a statute, or the date on which a tax appeals
22 commission or court decision becomes final and conclusive and if the rule, guidance,
23 statute, or decision imposes the liability as a result of the tax issue described in par.

24 (a) 1. ~~This subsection does not apply to any period associated with an audit~~
25 ~~determination if the taxpayer did not give the department employee adequate and~~

ASSEMBLY BILL 623

1 ~~accurate information regarding the tax issue in the prior audit determination or if~~
2 ~~the tax issue was settled in the prior audit determination by a written agreement~~
3 ~~between the department and the taxpayer.~~

4 **SECTION 20.** 77.51 (2) of the statutes is amended to read:

5 77.51 (2) “Contractors” and “subcontractors” are the consumers of tangible
6 personal property or items or goods under s. 77.52 (1) (b) or (d) used by them in real
7 property construction activities, and the sales and use tax applies to the sale of
8 tangible personal property or items or goods under s. 77.52 (1) (b) or (d) to them. A
9 contractor engaged primarily in real property construction activities may use resale
10 certificates only with respect to purchases of tangible personal property or items or
11 goods under s. 77.52 (1) (b) or (d) which the contractor has sound reason to believe
12 the contractor will sell to customers for whom the contractor will not perform real
13 property construction activities involving the use of such tangible personal property
14 or items or goods under s. 77.52 (1) (b) or (d). ~~In this subsection, “real property~~
15 ~~construction activities” means activities that occur at a site where tangible personal~~
16 ~~property or items or goods under s. 77.52 (1) (b) or (d) that are applied or adapted to~~
17 ~~the use or purpose to which real property is devoted are affixed to that real property,~~
18 ~~if the intent of the person who affixes that property is to make a permanent accession~~
19 ~~to the real property.~~ In this subsection, “real property construction activities” does
20 not include affixing property subject to tax under s. 77.52 (1) (c) to real property or
21 affixing to real property tangible personal property that remains tangible personal
22 property after it is affixed.

23 **SECTION 21.** 77.51 (11d) of the statutes is amended to read:

24 77.51 (11d) For purposes of subs. (1ag), (1f), (3pf), and (9p) and ss. 77.52 (20)
25 and (21), 77.522, and 77.54 (51), and (52), ~~and (60)~~, “product” includes tangible

ASSEMBLY BILL 623

1 personal property, and items, property, and goods under s. 77.52 (1) (b), (c), and (d),
2 and services.

3 **SECTION 22.** 77.51 (12t) of the statutes is created to read:

4 77.51 (12t) “Real property construction activities” means activities that occur
5 at a site where tangible personal property or items, property, or goods under s. 77.52
6 (1) (b), (c), or (d) that are applied or adapted to the use or purpose to which real
7 property is devoted are affixed to that real property, if the intent of the person who
8 affixes that property is to make a permanent accession to the real property.

9 **SECTION 23.** 77.54 (60) (a) of the statutes is renumbered 77.54 (60) (d) and
10 amended to read:

11 77.54 (60) (d) In this subsection, “~~lump sum~~”:

12 1. “Construction contract” means a contract to perform real property
13 construction activities and to provide ~~tangible personal property, items or property~~
14 ~~under s. 77.52 (1) (b) or (c), or taxable services and for which the contractor quotes~~
15 ~~the charge for labor, services of subcontractors, tangible personal property, items and~~
16 ~~property under s. 77.52 (1) (b) and (c), and taxable services as one price, including~~
17 ~~a contract for which the contractor itemizes the charges for labor, services of~~
18 ~~subcontractors, tangible personal property, items and property under s. 77.52 (1) (b)~~
19 ~~and (c), and taxable services as part of a schedule of values or similar document~~
20 construction materials.

21 **SECTION 24.** 77.54 (60) (b) of the statutes is amended to read:

22 77.54 (60) (b) The sales price from the sale of and the storage, use, or other
23 consumption of ~~tangible personal property, items and property under s. 77.52 (1) (b)~~
24 ~~and (c), and taxable services~~ construction materials that are sold by a prime
25 contractor as part of a ~~lump sum~~ construction contract, if the total sales price of all

ASSEMBLY BILL 623

1 ~~such taxable products~~ construction materials is less than 10 percent of the total
2 amount of the ~~lump sum~~ construction contract. Except as provided in par. (c), the
3 prime contractor is the consumer of ~~such taxable products~~ the construction materials
4 and shall pay the tax imposed under this subchapter on the ~~taxable products~~
5 construction materials.

6 **SECTION 25.** 77.54 (60) (bm) of the statutes is created to read:

7 77.54 **(60)** (bm) 1. The sales price from the sale of and the storage, use, or other
8 consumption of construction materials that are sold by a subcontractor as part of a
9 construction contract, if any of the following applies:

10 a. The sales price is exempted under par. (b).

11 b. The sales price is less than 10 percent of the total amount of the construction
12 contract.

13 2. The subcontractor is the consumer of the construction materials exempted
14 under this paragraph and shall pay the tax imposed under this subchapter on the
15 construction materials.

16 **SECTION 26.** 77.54 (60) (c) of the statutes is amended to read:

17 77.54 **(60)** (c) If the ~~lump sum~~ construction contract under par. (b) is entered
18 into with an entity that is exempt from taxation under sub. (9a), the prime contractor
19 is the consumer of all ~~taxable products~~ construction materials used by the prime
20 contractor in real property construction activities, but the prime contractor may
21 purchase without tax, for resale, ~~tangible personal property, items and property~~
22 ~~under s. 77.52 (1) (b) and (c), and taxable services~~ construction materials that are sold
23 by the prime contractor as part of the ~~lump sum~~ construction contract with the entity
24 and that are not consumed by the prime contractor in real property construction
25 activities.

ASSEMBLY BILL 623

1 **SECTION 27.** 77.54 (60) (d) 2., 3. and 4. of the statutes are created to read:

2 77.54 **(60)** (d) 2. “Construction materials” means tangible personal property
3 the selling, licensing, leasing, or renting of which is taxable under s. 77.52 (1) (a);
4 items the selling, licensing, leasing, or renting of which are taxable under s. 77.52
5 (1) (b); property the leasing of which is taxable under s. 77.52 (1) (c); and services the
6 selling, licensing, performing, or furnishing of which are taxable under s. 77.52 (2).

7 3. “Prime contractor” means a contractor who enters into a construction
8 contract with an owner of real property.

9 4. “Subcontractor” means a contractor who enters into a construction contract
10 with a prime contractor or another subcontractor.

11 **SECTION 28.** 77.61 (19) (intro.) of the statutes is amended to read:

12 77.61 **(19)** (intro.) A person who fails to produce records or documents, as
13 provided under s. ~~73.03 (9)~~ or 77.59 (2), that support amounts or other information
14 required to be shown on a return required under s. 77.58 and fails to comply in good
15 faith with a summons issued pursuant to s. 73.03 (9) seeking those records and
16 documents may be subject to any of the following penalties, as determined by the
17 department, except that the department may not impose a penalty under this
18 subsection if the person shows that under all facts and circumstances the person’s
19 response, or failure to respond, to the department’s request was reasonable or
20 justified by factors beyond the person’s control:

21 **SECTION 29. Nonstatutory provisions.**

22 (1) The repeal of sections 20.566 (1) (hn) and 73.03 (28d) of the statutes does
23 not affect the validity of any assessment based entirely or in part on information or
24 documents obtained from the multistate tax commission prior to the repeal.

ASSEMBLY BILL 623

1 (2) The department of revenue shall submit in proposed form the rules required
2 under section 73.03 (72) and (73) of the statutes, as created by this act, to the
3 legislative council staff under section 227.15 (1) of the statutes no later than the first
4 day of the 6th month beginning after the effective date of this subsection.

5 (3) Using the procedure under section 227.24 of the statutes, the department
6 of revenue shall promulgate rules required under section 73.03 (72) and (73) of the
7 statutes, as created by this act, for the period before the effective date of the
8 permanent rules promulgated under section 73.03 (72) and (73) of the statutes, as
9 created by this act, but not to exceed the period authorized under section 227.24 (1)
10 (c) of the statutes, subject to extension under section 227.24 (2) of the statutes.
11 Notwithstanding section 227.24 (1) (a), (2) (b), and (3) of the statutes, the department
12 is not required to provide evidence that promulgating a rule under this subsection
13 as an emergency rule is necessary for the preservation of the public peace, health,
14 safety, or welfare and is not required to provide a finding of emergency for a rule
15 promulgated under this subsection.

16 (4) Before the date on which the emergency rules under subsection (3) are
17 promulgated, the department of revenue shall administer chapter 71 of the statutes
18 according to policies and procedures established by the department, but not
19 promulgated as rules, notwithstanding the absence of rules to administer that
20 chapter.

SECTION 30. Initial applicability.

21 (1) The treatment of sections 71.07 (5n) (a) 3. and 4., 71.10 (1m) (b) (intro.), 1.,
22 and 2. and (c), 71.28 (5n) (a) 3. and 4., 71.30 (2m) (b) (intro.), 1., and 2. and (c), and
23 71.80 (1m) (b) (intro.), 1., and 2. and (c) of the statutes first applies to taxable years
24 beginning on January 1 of the year in which this subsection takes effect, except that
25

ASSEMBLY BILL 623

1 if this subsection takes effect after July 31, this act first applies to taxable years
2 beginning on January 1 of the year following the year in which this subsection takes
3 effect.

4 (2) The treatment of sections 20.566 (1) (hn), 73.03 (28d), 77.51 (11d), and 77.54
5 (60) (a), (b), (bm), (c), and (d) 2., 3., and 4. of the statutes first applies to a contract
6 that is entered into or extended, modified, or renewed on the effective date of this
7 subsection.

8 (3) The treatment of sections 71.80 (9m) (intro.) and 77.61 (19) (intro.) of the
9 statutes first applies to an audit commenced, or a summons issued, on the effective
10 date of this subsection.

11 (4) The treatment of section 73.16 (3) (b) of the statutes first applies to an audit
12 commenced on the effective date of this subsection.

13 **SECTION 31. Effective dates.** This act takes effect on the day after publication,
14 except as follows:

15 (1) The treatment of sections 77.51 (11d) and 77.54 (60) (a), (b), (bm), (c), and
16 (d) 2., 3., and 4. of the statutes takes effect on the first day of the 3rd month beginning
17 after publication.

18 (END)