



# State of Wisconsin

## LEGISLATIVE REFERENCE BUREAU

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STEPHEN R. MILLER  
CHIEF

February 7, 2006

## MEMORANDUM

**To:** Representative Strachota

**From:** Joseph T. Kreye, Sr. Legislative Attorney, (608) 266-2263  
Robert P. Nelson, Sr. Legislative Attorney, (608) 267-7511

**Subject:** Technical Memorandum to **2005 AB-968** (LRB 05-4358/1)

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We received the attached technical memorandum relating to your bill. This copy is for your information and your file. If you wish to discuss this memorandum or the necessity of revising your bill or preparing an amendment, please contact me.

## MEMORANDUM

February 6, 2006

**TO:** Joseph Kreye and Robert Nelson  
Legislative Reference Bureau

**FROM:** Rebecca Boldt  
Department of Revenue

**SUBJECT:** Technical Memorandum on Assembly Bill 968 (LRB 4358/1) – DOR Duties and Authority

The department has the following technical concerns related to the bill:

### Interest Rates

The bill specifies the interest rate charged on delinquent and late payments is to be tied to the 2-year U.S. Department of Treasury rate as of December 1 of the prior year. It is unclear which Treasury rate is intended. DOR recommends Treasury's 2-year yield rate, which is 4.45% for December 1, 2005.

Also, it is unclear how interest is computed when a determination goes unpaid past the end of a calendar year. The language should specify that separate computations of interest are needed when the time period extends across years for which different interest rates apply.

Section 22 of the bill creates s. 73.14(8) specifying that all the changes are applicable to all taxes and fees administered by the Department of Revenue (DOR). The bill makes changes to current law interest rates but does not change the language of all the relevant statutes (e.g., ch. 72.23; 78.22(5); 139.03(2x)(e); 139.25(2), (2)intro; 139.315(5); 139.33(3); 139.44(9), (11); and 168.12(6)(c), (d)2, (e)1). This will be confusing to readers of the statute who will see an interest rate provision in the tax specific statute and be unaware of the overriding interest rate in Chapter 73.

Section 49, Part (3) of the bill makes the changes in interest rates effective for audits and assessments issued and claims for refund filed on January 1, 2007. Since DOR does not issue audits, this reference is inappropriate. Reference to "assessments and refunds (or determinations) issued after December 31, 2006," would be more appropriate and would avoid confusion in cases where assessments or refunds issued after January 1, 2007, relate to taxes overpaid or underpaid in periods prior to January 1, 2007.

### Settlements

The amendment to s. 73.03(25) is not necessary because sec. 73.13 provides DOR with the authority to compromise tax liability on the basis of the taxpayer's ability to pay.

### Reliance on Published Guidance

In section 22 of the bill (on page 13, line 19, and page 14, line 1), the words "adverse to any taxpayer" should be removed. The statute should be consistent that any published position must be followed. Therefore, DOR should not be able to take any position that is beneficial to a taxpayer if it is contrary to what is published. Similarly, an amendment to our published position should benefit the taxpayer retroactively or prospectively as long as DOR is within the statute of limitations.

Also in section 22 of the bill (page 13, line 23) the phrase "in any material manner" should be removed. The intent of this language is unknown. It would be subjective to determine what is material and would create confusion for both taxpayers and DOR. The author may wish to replace "in any material manner" with "by the department, legislature, commission or court."

With respect to any audit or assessment, the facts in such an audit must be identical to those set forth in the guidance. Language should be inserted in this section to state that for reliance to apply, the facts in the guidance must be the same as the facts in the audit, assessment, etc. Otherwise, taxpayers and practitioners may try to extend guidance on a particular issue to a different set of facts that they may see as similar.

### Relying on Past Audits

In section 73.14(3), a time limitation should be added. In addition, the term "knew or should reasonably have known of the condition" should be further defined.

In sec. 73.14(3)(a), the application of the provision is too broad and could be narrowed by removing the phrase "including any subsidiary, heir, assignee, or related party of the person." Furthermore, "related party" is not defined.

Sec. 73.14(3)(a)1 is too broad. DOR performs audits of limited scope and does not attest to the accuracy of all tax information of a taxpayer or its subsidiaries or related parties after an audit. Also, the taxpayer decides what information to provide in response to DOR requests and may not provide all information about conditions, activities, attributes, or transactions. Language should be inserted that for this reliance to apply, the tax treatment must have been specifically addressed in the prior audit. DOR should specifically identify in its audit reports and determinations what was audited.

Sec. 73.14(3)(a)2 is unclear. The phrase "knew or should reasonably have known of the condition, activity, attribute, or transaction" should be replaced with language requiring that DOR specifically identify in its audit reports and determinations what was audited and that the taxpayer can rely on determinations of the tax treatment of those items.

In sec. 73.14(3)(b), reliance on past audits does not apply to any assessment or audit that is subsequent to a rule, guidance or statute that "clearly and unequivocally" imposes the liability for conditions or activities present in the prior audit. Also, this exception does not account for the possibility of a court case establishing a new position on an issue. Court decisions, as finally determined, should be added to the list of exceptions. Paragraph (b) only applies when an audit occurs before a rule, guidance or statute becomes effective. Also, this provision should

refer to audit determination. The phrase "to the general public" should be deleted so DOR can continue to provide informal advice to thousands of taxpayers. The phrase "as result of the condition, activity, attribute, or transaction described in par. (a)1" should be deleted and replaced with tax treatments specifically audited and identified in audit reports and determinations.

#### Fraud and Negligence Penalties

In sec. 73.14(6) DOR would be required to show the taxpayer's action was "clearly" contradicted by statute, guidance or rule, but "clearly" is not defined in the bill.

The provision states that all the changes are applicable to all taxes and fees administered by DOR. Changes are made in income/franchise tax and sales and use tax laws specifically to the negligence penalty and many of the special taxes and fees administered by DOR relating to these fees cross reference back to these sections. However, there are other sections in the statutes for taxes DOR administers where the negligence penalty is specifically mentioned and there is no change in the language (e.g., ch. 71.83(1), (b), (c); 72.235, 77.60(3); 78.68; and 139.25(3), (4)). This will be confusing to readers of the statute who will see a penalty provision in the tax specific statute and not know there is an overriding provision in chapter 73.

Proposed sec. 73.14(6) prohibits DOR from assessing fraud and negligence penalties unless DOR proves by a preponderance of the evidence that the taxpayer's action was "clearly contradicted" by statute, rule or Department guidance. There is no entity to prove such matters to by a preponderance of the evidence unless one is before the Tax Appeals Commission or a higher court, so by implication no fraud or negligence penalties may be assessed unless there is a finding by the TAC or a higher court to this effect.

Assessments are made by auditors who do not practice before the Tax Appeals Commission or the courts. However, TAC and court cases are handled by the attorneys of the Office of General Counsel and the Department of Justice, who lack authority to impose penalties. As currently written, this proposed language will remove DOR's ability to assess all fraud and negligence penalties. The statute could be revised to provide that DOR carries the burden of proof on fraud and negligence rather than the taxpayer. Attorneys could be given statutory authority to impose negligence penalties.

The proposed amendment to sec. 77.60(3) imposes the burden of proving that the error was due to good cause and not due to neglect on the taxpayer; this is inconsistent with the proposed amendment to sec. 76.68(3), which strikes such language.

Also, creation of sec. 73.14(6), which in general transfers the burden of proof regarding neglect to DOR, will affect many more statutes than are currently listed in the bill including the following: ss. 71.09(11)(d), 71.83(1)(a)1, 71.83(1)(a)1m, 71.83(1)(a)2, 71.83(1)(a)4, 71.83(3), 76.05(1), 76.05(2), 76.14, 76.28(6)(b), 76.39(3), 76.645(2), 77.60(2), and 78.68(4). Is that the author's intent?

#### Equitable Recoupment

In sec. 73.14(5), the two sentences are contradictory and should be clarified. It would be possible to narrow the impact of the statutory change by clarifying that the state or the taxpayer can counter with a "stale" claim, one barred by the statute of limitations, so long as the same year, income tax period, or audit period is involved. Sec. 71.07(1), Claim of Right would also be affected by this change.

### Buyer Claim for Refund

Section 77.59(4)(a) appears to conflict with sec. 77.59(5m) regarding the liability of a seller to a buyer for amounts erroneously collected by a seller. To protect the buyer's ability to collect refunds, the author may wish to replace the inserted language on page 17, line 4-5, with the following: "All claims for refund by a buyer shall be filed with the department. The seller shall not be liable to any buyer for amounts that the seller collected and paid to the department which are not subsequently paid by the department to the seller."

Because more buyers will be filing refund claims with DOR and the seller also retains the right to a refund of tax collected from the buyer, confidentiality provisions should be amended to allow DOR to inform a claimant if the refund has been provided to someone else.

The change to 77.59(8m) makes the provision nonsensical. If the buyer filed valid claims for refund with DOR, there is no reason for the seller to file under the expanded statute of limitations repeal.

### Promulgating Rules

Sections 227.12(3) and (4) are redundant to the Small Business Regulatory Fairness Act 145, sec. 895.59. The 90 day requirement is too restrictive with regard to promulgating rules and issuing declaratory rulings.

### Removing Limitations on Refund Claims or Offsets

Proposed subsection (5) to section 73.14 would essentially eliminate the statute of limitations for any refund claim, so long as the taxpayer had a present liability that it could offset against that claim. The only limitation would be that the refund could not go back further than the audit or assessment period. It is unclear from the language of this provision whether it could be used to reopen matters that have been resolved in a settlement agreement. This should be clarified.

### Effective Date

The initial applicability of sec. 803.08 should be the day after publication. The initial applicability of section 49, paragraph (2) and (3) should be for any determination on the day after publication. Prior case law also requires that the initial applicability date make known that the transactions to which the determination applies may have occurred before the effective date.

The effective date of the bill should be the sixth month beginning after publication in order to give DOR time to implement the changes.

### Administrative Costs

The proposed legislation makes no provision for the funding of the costs involved in administering the activities required. If the author wishes to provide funding, appropriation language could be developed and costs allocated in the following manner:

	<u>Chapter 20</u>	<u>Amount</u>	<u>FTE</u>
one-time	s. 20.566 (3) (a)	\$572,700	
annual	s. 20.566 (1) (a)	\$468,300	6.5
annual	s. 20.566 (3) (c)	\$45,000	

annual s. 20.566 (3) (a) \$24,000

If you have any questions regarding this technical memorandum, please contact Kirstin Nelson at (608) 261-8984; for administrative costs contact Jeff Whittow at (608) 267-1358.

cc: Representative Strachota