

## PROPOSED ORDER OF THE DEPARTMENT OF REVENUE AMENDING AND CREATING RULES

The Wisconsin Department of Revenue proposes an order to: **amend** Tax 2.82 (3) (b) 3. a. and (4) (a) and (d); and **create** Tax 2.82 (2) (d); **relating to** income and franchise tax provisions.

The scope statement for this rule, SS 014-17, was approved by the Governor on January 23, 2017, published in Register No. 733B on January 30, 2017, and approved by the Secretary of Revenue on February 10, 2017.

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### *Analysis by the Department of Revenue*

**Statutes interpreted:** ss. 71.22 (1r), 71.23 (1) and (2), 71.255 (5), and 77.93, Stats.

**Statutory authority:** ss. 71.80 (1) (c) and 227.11 (2) (a), Stats.

**Explanation of agency authority:** Under s. 71.80 (1) (c), Stats., the department may make such regulations as it shall deem necessary in order to carry out chapter 71 of the Wisconsin Statutes, relating to income and franchise taxes. This provision applies to the revision of s. Tax 2.82.

Section 227.11 (2) (a), Stats., provides “[e]ach agency may promulgate rules interpreting the provisions of any statute enforced or administered by the agency, if the agency considers it necessary to effectuate the purpose of the statute...” This provision applies to the revision of s. Tax 2.82.

**Related statute or rule:** Section Tax 2.39(6)(b) provides that sales of tangible personal property are included in the numerator of the sales factor of the apportionment percentage if the taxpayer ships the property from a location in Wisconsin to a destination state in which the taxpayer does not have nexus. Section Tax 2.39(6)(b)5. provides that the standards set forth in s. Tax 2.82 are used to determine whether a taxpayer has nexus in another state. Therefore, any changes to the standards in s. Tax 2.82 will affect the apportionment percentage and amount of income taxable to Wisconsin by certain taxpayers.

Section 71.22 (1r), Stats., lists activities that are considered to be "doing business in this state."

Section 71.23 (3), Stats., lists activities that do not create nexus.

**Plain language analysis:** The rule clarifies the level of activity and/or types of activities that, when performed by an out-of-state business, establishes nexus in Wisconsin and requires the filing of a Wisconsin income/franchise tax return.

Currently s. Tax 2.82 provides a listing of activities that constitute nexus for an unlicensed foreign corporation, and require the filing of Wisconsin corporate income or franchise tax returns. The current list of activities uses the terms "usual or frequent" or "regularly" to describe certain activities that create nexus. The department wishes to establish a standard of "usual or frequent" or "regularly" that can be administered clearly and consistently.

In addition, the department wishes to clarify that ownership of a tangible personal property in Wisconsin (e.g., inventory or equipment) establishes nexus in Wisconsin.

**Summary of, and comparison with, existing or proposed federal regulation:** Federal constitutional provisions: 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.

Federal Public Law 86-272: Under Public Law 86-272, a state may not impose its franchise or income tax on a business selling tangible personal property, if the only activity of that business is the solicitation of orders by its salesperson 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. This law does not prohibit states from imposing franchise/income tax on out-of-state businesses that sell services, real estate, or intangibles into a state.

**Comparison with rules in adjacent states:** Most states do not have laws or regulations that establish a clear threshold or standard of activities that create nexus. Nexus is often determined on a case-by-case basis.

Michigan – A corporation has nexus with Michigan for corporate income tax purposes if that corporation has a physical presence in the state for a period of more than one day during the tax year, if the corporation actively solicits sales in the state and has gross receipts of \$350,000 or more sourced to the state, or if the corporation has an ownership interest or beneficial interest in a flow-through entity, directly, or indirectly through one or more flow-through entities, that has substantial nexus in the state.

Illinois: – The question of nexus in Illinois is highly fact-dependent. Tax is imposed on every corporation for the privilege of earning or receiving income in the state. The only threshold imposed relates to sample or display rooms. Maintaining a sample or display room in excess of 14 days will create income tax nexus for an out-of-state business.

Minnesota – There is no standard or threshold that would create nexus in Minnesota. Tax is imposed on every entity that obtains or regularly solicits trade or business from within the state.

**Summary of factual data and analytical methodologies:** Based on research of other states' laws and regulations, case law, and suggestions from Wisconsin Institute of Certified Public Accountants-Tax Committee.

**Analysis and supporting documents used to determine effect on small business:** Current Wisconsin law and regulations determine whether small businesses must file Wisconsin tax returns, and, in the case of multi-state businesses, determine the amount of income taxable to Wisconsin.

**Anticipated costs incurred by private sector:** Out-of-state businesses may incur costs to file a Wisconsin income/franchise tax return if they are considered to have nexus because of the rule changes.

**Effect on small business:** Out-of-state businesses may have nexus in Wisconsin and be required to file a Wisconsin income/franchise tax return. Small businesses already doing business in Wisconsin may have nexus in other states which could reduce the amount of income apportioned and taxable to Wisconsin.

**Agency contact person:** Please contact Jen Chadwick at (608) 266-8253 or [jennifer.chadwick@wisconsin.gov](mailto:jennifer.chadwick@wisconsin.gov), if you have any questions regarding this proposed rule.

**Where to submit comments and submission deadline:** Comments may be submitted to the contact person shown below no later than December 3, 2018. Information as to the place, date, and time of the public hearing will be published in the Wisconsin Administrative Register.

Jen Chadwick  
Department of Revenue  
Mail Stop 6-40  
2135 Rimrock Road  
P.O. Box 8933  
Madison, WI 53708-8933  
jennifer.chadwick@wisconsin.gov

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**SECTION 1.** Tax 2.82 (2) (d) is created to read:

Tax 2.82 (2) (d) For purposes of this section, "regular" and "regularly" mean 15 or more days of activity. Fifteen days of activity means one person for 15 days or 15 persons for one day, or any combination of persons and days that results in at least 15 person-days of activity. Days of activity include any day, or portion thereof, upon which business activity took place. Days of activity do not include travel days, holidays, or weekends, unless business activities were conducted on those days.

**SECTION 2.** Tax 2.82 (3) (b) 3. a. is amended to read:

Tax 2.82 (3) (b) 3. a. ~~Usual or frequent activity~~ Activity in Wisconsin by employees or representatives soliciting orders for tangible personal property which orders are sent outside this state for approval or rejection.

**SECTION 3.** Tax 2.82 (4) (a) is amended to read:

(4) (a) *General.* Any of the following activities constitute nexus:

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.~~ Ownership of tangible personal property in Wisconsin, including inventory held by a distributor, consignee, or other non-employee representative, whether or not used to fill orders for the owner's account, but not including personal property for use in an employee's or representative's home, residential office or automobile that is solely limited to conducting the activities protected by Public Law 86-272.
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~~ Regular activity in Wisconsin by employees or representatives soliciting orders with authority to ~~accept~~ approve them.
5. Regular activity in Wisconsin by employees or representatives performing services related to the sale of tangible personal property, including consulting, design, engineering, construction, installation, assembly of equipment.

6. ~~Usual or frequent~~ Regular 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. ~~Other usual and frequent 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, ~~or repair and,~~ or maintenance of the taxpayer's products.

**Example:** Training Company is a calendar year-end corporation headquartered outside Wisconsin. Training Company does not maintain a business location or have resident employees in Wisconsin. During the year, Training Company sends five employees to Wisconsin for three days to conduct a training seminar related to the operation of machinery that Training Company sold to the taxpayer. Training Company has nexus since its employees conducted activity in Wisconsin for 15 days.

87. Operation of mobile stores in Wisconsin, such as trucks with driver-salespersons, regardless of frequency, or whether the driver-salesperson is an employee.

98. Leasing of tangible property and licensing in Wisconsin, but not including personal property for use in an employee's or representative's home, residential office or automobile that is solely limited to conducting the activities protected by Public Law 86-272.

9. 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 by employees or representatives, the services of which are unrelated to the sale of tangible personal property.

**Example:** Repair Company is a calendar year-end corporation headquartered outside Wisconsin. Repair Company does not maintain a business location or have resident employees in Wisconsin. During the year, Repair Company sends four technicians to repair customer equipment located in Wisconsin. Each of the technicians perform repairs in Wisconsin for three days during the year. Repair Company has nexus in Wisconsin since its employees or representatives perform services in Wisconsin. Public Law 86-272 does not apply because services such as repair activities are not a protected activity.

12. Engaging in substantial activities that help to establish and maintain a market in Wisconsin.

**SECTION 4.** Tax 2.82 (4) (d) is amended to read:

(d) *How to obtain ruling.* Paragraph (a) and the statutory definitions summarized in par. (b) as to what activities constitute nexus are not all-inclusive. A ruling may be requested about a particular foreign corporation as to whether it is subject to Wisconsin franchise or income taxes by writing to the Wisconsin Department of Revenue, Audit ~~Technical Services Section~~ Bureau, Nexus Unit, P.O. Box 8906, Madison, WI 53708.

**Note:** Section 71.23 (3), Stats., provides specific activities that do not constitute nexus in Wisconsin even if they exceed the protection of P.L. 86-272.

**SECTION 5.** EFFECTIVE DATE; GENERAL. This rule shall take effect on the first day of the month following publication in the Wisconsin Administrative Register as provided in s. 227.22 (2) (intro.), Stats.