

(6) Except as provided in subsection (7), any corporation which has been computing its inventory for Wisconsin income tax purposes in accordance with section 472 of the United States internal revenue code and which has been authorized or directed by the United States commissioner of internal revenue to change its method of inventory valuation for federal income tax purposes shall also change its method of inventory valuation for Wisconsin income tax purposes. To correlate its Wisconsin basis with the federal basis, the opening inventory for the income 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.

(7) Any corporation which has been authorized or directed by the United States Commissioner of Internal Revenue 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 such timber over the adjusted basis thereof, may exclude from its inventory, for Wisconsin income tax purposes, the excess of the fair market value of such timber over the adjusted basis thereof, or may, with the consent of the Wisconsin department of taxation, include such excess in its inventory for Wisconsin income tax purposes subject to such conditions as said department may prescribe.

**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.

## DETERMINATION OF INCOME FROM MULTISTATE OPERATIONS *u*

**Tax 2.41 Separate accounting method.** (Section 71.07 (2), Wis. Stats.) (1) When the separate accounting method is used, separate records must be kept of sales, cost of sales and expenses for the Wisconsin business as distinct from the remainder of the business. Overhead items of income and expense must then be allocated to the business within and without Wisconsin upon a basis or combination of bases justified by the facts and conditions. For example: The ratio of Wisconsin sales to total sales usually represents a satisfactory basis for a merchandising business, while the ratio of direct cost of material and labor in Wisconsin to the total gives a more accurate result for a construction business. Federal income taxes are based upon income and should, therefore, be allocated to Wisconsin business on the basis of income. Federal income taxes are deductible only on the cash basis, and the allocation to Wisconsin business for any year, therefore, must be based upon the ratio of income within Wisconsin to the total income of the year on which the federal income taxes are assessed, even though that ratio differs from the ratio of the year in which the taxes are actually paid.

(a) The relationship of the general overhead items to Wisconsin operations will determine whether the home office income and expense

should be allocated to the Wisconsin business. Such overhead items as officers' salaries, office salaries, office rent and sundry office expenses should ordinarily be included in the allocation.

(2) Rentals received from real estate held purely for investment purposes and not used in the operation of the business are not subject to allocation. All expenses connected with the interest, dividends and rentals realized from investments such as the above are not subject to allocation but must be applied against the investment income. The taxability of the net investment income depends upon the situs of the investment property or the residence of the recipient.

**History:** 1-2-56; am. Register, February, 1958, No. 26, eff. 3-1-58.

**Tax 2.42 Apportionment method.** (Section 71.07 (2), Wis. Stats.)

Any person engaged in business within and without the state must report by the statutory apportionment method when the business of such person within the state is an integral part of a unitary business, unless the department of taxation expressly permits reporting on a different basis. The factors used in the apportionment method are as follows:

(1) Tangible property includes land, buildings, machinery and equipment, inventories and other tangible personal property actually owned and used in producing apportionable income. Tangible property which is used in producing nonapportionable or nontaxable income cannot be included in the property factor. The value at which tangible property should be included in the apportionment factor is the average of the beginning and close of year values on a comparable basis within and without the state. If the average at the beginning and end of the year does not fairly represent the average of the property owned during the year, the average may be obtained by dividing the sum of the monthly balances by 12.

(2) The cost of manufacturing, collecting, assembling or processing within Wisconsin must be determined in all cases in the same manner and under the same rules as the cost for the entire business within and without Wisconsin is determined. When a product is partially completed outside of the state and then shipped into the state for further processing or completion, only the labor and manufacturing expense incurred from the time that the product is brought into the state becomes a part of the cost within Wisconsin, and the total material used in manufacturing both within and without the state shall be allocated on some equitable basis such as the ratio of direct labor and manufacturing expense within Wisconsin to the total thereof. Unless inconsistent with the best accounting practice in the trade or business, amounts realized on the sale of scrap produced in the manufacturing process shall be treated as a recovery of, and in reduction of, cost of manufacturing, for purposes of the cost of manufacturing factor.

(3) Sales are made in Wisconsin if made through or by offices, agencies or branches located within the state, regardless of the location of the purchaser. Sales made by a foreign corporation to customers in Wisconsin through the medium of solicitors or traveling salesmen are not Wisconsin sales unless such salesmen are identified with offices, agencies or branches located within Wisconsin. Sales made by a sales office in Wisconsin to customers located outside of Wisconsin are Wisconsin sales for purposes of apportionment. Goods

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sold through a sales office in Wisconsin may be shipped direct from a factory located outside the state to a customer located outside the state and still be Wisconsin sales. Goods sold through a sales office located outside of the state without the intervention of any Wisconsin office, branch or agency but shipped from a factory located in Wisconsin to a Wisconsin customer are not Wisconsin sales. As used in section 71.07 (2) (c), Wis. Stats., and in this regulation, the term "sales" shall extend to and include by-product sales, but shall not include scrap sales treated as a reduction of cost of manufacturing pursuant to subsection (2) hereof.

**History:** 1-2-56; am. (2) and (3), Register, January, 1968, No. 145, eff. 2-1-68.

**Tax 2.43 Nonapportionable income.** (Section 71.07 (2), Wis. Stats.)

(1) The expenses related to nonapportionable income must be deducted therefrom to determine the net nonapportionable income. In the case of dividends and interest received which follows the residence of the recipient, only the excess of the amounts received over the sum of interest paid and dividends deducted plus other related expenses can be considered as nonapportionable income. If the interest paid, deductible dividends received and related expenses exceed the total interest and dividends received, no deduction from total net income can be made for nonapportionable interest and dividends. All of the nonapportionable income must be deducted from the total net income of the business to determine the apportionable income to which the apportionment percentage is applied. Any nonapportionable income attributable to Wisconsin must be added to the apportionable income allocated to Wisconsin to determine the total Wisconsin net income.

**History:** 1-2-56; r. (1) (a), Register, August, 1960, No. 56, eff. 8-1-60.

**Tax 2.44 Permission to change basis of allocation.** (Section 71.07 (2) Wis. Stats.) Except when income must be reported on the apportionment basis, permission to make a change either from separate accounting to apportionment, or vice versa, must be obtained in writing from the commissioner of taxation upon written application setting forth in detail the reasons why the desired change will more clearly reflect the taxpayer's Wisconsin income. Such application must be filed before the end of the income year for which the change is desired.

**History:** 1-2-56, am. Register, September, 1964, No. 105, eff. 10-1-64.

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**Tax 2.45 Apportionment in special cases.** (Section 71.07 (5), Wis. Stats.) When the business of any person within Wisconsin is an integral part of a unitary business conducted within and without Wisconsin, but because of unusual or unique circumstances the portion of the income of such person derived from business transacted in Wisconsin cannot be ascertained with reasonable certainty by use of the apportionment formula provided in section 71.07 (2), Wis. Stats., (or by separate accounting in view of the unitary nature of the business), the department will substitute in the place of some or all of the statutory apportionment factors such other factor or factors as will reasonably apportion to Wisconsin the business income properly assignable to Wisconsin. In any case in which an apportionment of business income is made pursuant to this regulation, the taxpayer, at the time of the assessment, will be apprised of the factors used in the formula adopted. The business income of inter-

state air carriers shall be apportioned as provided in Wis. Adm. Code section Tax 2.46.

**History:** Cr. Register, December, 1956, No. 12, eff. 1-1-57.

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**Tax 2.46 Apportionment of business income of interstate air carriers.** (Section 71.07 (5), Wis. Stats.) The apportionable income of an interstate air carrier doing business in Wisconsin shall be apportioned to Wisconsin on the basis of the ratio obtained by taking the arithmetical average of the following 3 ratios: (1) The ratio which the aircraft arrivals and departures within this state scheduled by such carrier during the calendar or fiscal year bears to the total aircraft arrivals and departures within and without this state scheduled by such carrier during the same period; provided that in the case of nonscheduled operations all arrivals and departures shall be substituted for scheduled arrivals and departures; (2) The ratio which the revenue tons handled by such carrier at airports within this state during the calendar or fiscal year bears to the total revenue tons handled at airports within and without this state during the same period; (3) The ratio which such air carrier's originating revenue within this state for the calendar or fiscal year bears to the total originating revenue within and without this state for the same period.

**History:** Cr. Register, December, 1956, No. 12, eff. 1-1-57.

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**Tax 2.47 Apportionment of net business income of interstate motor carriers of property.** (1) (Section 71.07 (5), Wis. Stats.) The apportionable income of an interstate motor carrier of property, doing business in Wisconsin, shall be apportioned to Wisconsin, on the basis of the arithmetical average of the following 2 ratios:

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(a) The ratio of the gross receipts from carriage of property first acquired for carriage in Wisconsin to the total gross receipts from carriage of property everywhere;

(b) The ratio of ton miles of carriage in Wisconsin to ton miles of carriage everywhere.

(2) Whenever gross receipts' data is not available, the department may authorize or direct substitution of a similar factor (e.g. gross tonnage) and whenever ton mile data is not available the department may similarly authorize substitution of a similar factor (e.g. revenue miles).

(3) For purposes of this regulation a "ton mile" reflects the movement of one ton of freight for the distance of one mile.

(4) This regulation shall not apply to mercantile or manufacturing businesses which engage in some interstate hauling as an incident of such mercantile or manufacturing businesses.

(5) This regulation shall apply with respect to the determination of income tax or franchise tax liability for any income year open to assessment or refund on the effective date hereof.

**History:** Cr. Register, April, 1966, No. 124, eff. 5-1-66.

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**Tax 2.48 Apportionment of net business incomes of interstate pipeline companies.** (Section 71.07 (5), Wis. Stats.) (1) With respect to the imposition of the Wisconsin income or franchise tax on or measured by income of the calendar year 1969, or corresponding fiscal year, and thereafter, the apportionable income of a pipeline company operating within and without Wisconsin shall be apportioned to

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Wisconsin on the basis of the arithmetical average of the following 3 ratios:

(a) The ratio of tangible property owned, and used by the taxpayer in Wisconsin to produce apportionable income, to the total of such property owned and used by him to produce apportionable income everywhere. The amount of such property for purposes of both the numerator and denominator shall be Wisconsin income tax net cost. In any case in which the property factor is distorted by reason of the taxpayer depreciating property in Wisconsin by a method different from that used to depreciate property outside Wisconsin, or in any case in which Wisconsin income tax net cost cannot be ascertained, the department may authorize or direct such other method of determining the property fraction as will produce an equitable result.

(b) The ratio of traffic units (e.g. barrel miles, cubic foot miles or other appropriate measure of product movement) in Wisconsin to the total of such units everywhere.

(c) The ratio of the total compensation paid to employes located in this state to the total compensation paid to employes located everywhere. An employe shall be deemed located in Wisconsin if his services are performed entirely within Wisconsin, or if services performed without the state are incidental to services within Wisconsin, or if some of the service is performed in Wisconsin and the base of operations is in Wisconsin, or if there is no base of operations and the place from which the service is directed and controlled is in Wisconsin, or if the base of operations or place from which the service is directed or controlled is not in any state in which some part of the service is performed, but the individual's residence is in this state. Compensation paid to retired employes shall be excluded from both the numerator and the denominator.

(2) In any case in which the company has no employes or in which the department determines that employes are not a substantial income producing factor, it may order or permit the elimination of the compensation factor and the use of the arithmetical average of the other 2 factors to arrive at the Wisconsin apportionment percentage.

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*50* **History:** Cr. Register, November, 1969, No. 167, eff. 12-1-69.

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**GROSS INCOME**

**Tax 2.51 Rent received by corporations from Wisconsin real estate.** (Section 71.03 (1) (b), Wis. Stats.) 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.

**Tax 2.53 Stock dividends and stock rights received by corporations.** (1) If a shareholder receives stock or stock rights as a distribution on stock previously held and under section 71.305, Wis. Stats., such distribution is not includable in gross income then, except as provided in section 71.307 (2), Wis. Stats., the basis of the 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 stock or stock rights as a distribution on stock previously held and under section 71.305 (1), Wis. Stats., a part of the distribution is not includable in gross income (except as provided in 71.307 (2), Wis. Stats.), the basis of the 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 such distribution which is includable in gross income pursuant to section 71.305 (2), Wis. 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 will apply with respect to stock rights only if such rights are exercised or sold.

(a) *Exception.* The basis of rights to buy stock which are excluded from gross income under section 71.305 (1) Wis. Stats., shall be zero if the fair market value of such 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 with respect to all the rights received by him in a particular distribution in respect of all the stock of the same class owned by him in the issuing corporation at the time of such distribution. Such 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. Such statement shall disclose the number of shares of the old stock by the shareholder on the date of distribution, the basis of such 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 such an 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.

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

(a) Under an interest option clause under which all the principal proceeds are retained and interest paid thereon periodically, the interest is taxable income.

(b) Under an income option under which the principal proceeds and interest thereon are paid in periodical instalments to the policy owner, the interest so paid is taxable income.

(c) When, under the same option, payments are made to the beneficiary (the option having been selected by the beneficiary), the interest so paid is taxable income.

(d) When, under the same option, payments are made to the beneficiary (the option having been designated by the insured), the instalment payments are made under the insurance contract, and no part of the payment is taxable income.

**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.