

## Chapter Tax 3

## INCOME TAXATION, DEDUCTIONS FROM GROSS INCOME, EXCLUSIONS AND EXEMPTIONS, ETC.

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**Tax 3.01 Rents paid by corporations.** (s. 71.04 (2), Stats.) (1) **DEDUCTIBLE RENTAL PAYMENTS.** Rents paid on property used in producing taxable income are deductible from gross income. The cost of leaseholds, acquired for cash or property, represents rent paid in advance and as such is deductible from gross income in equal amounts over the life of the leaseholds. Taxes paid by the lessee for the lessor are to be treated as additional rent paid and are a deductible expense.

(2) **APPLICABILITY.** As a result of 1987 Wisconsin 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; renun. to be (1) and cr. (2), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.03 Dividends received, deductibility of.** (s. 71.04 (4), Stats.) (1) In determining whether 50% or more of the net income or loss for the preceding year of the corporation paying the dividend was used in computing taxable income, if the corporation paying the dividend was subject to the franchise tax measured by net income, interest income from the federal government and its instrumentalities must be included but deductible dividends must be disregarded. If the corporation paying the dividend was subject to the net income tax, non-taxable interest from the

federal government or its instrumentalities and deductible dividends must both be disregarded.

(2) When a corporation keeps its records on the basis of a fiscal year ending not later than June 30, the dividends received from such corporation during the calendar year will be presumed to have been paid from the income of the corporation for its fiscal year ending within the calendar year when such dividends are paid. When a corporation keeps its records on the basis of a fiscal year ending subsequent to June 30, the dividends received from such corporation during the calendar year will be presumed to have been paid from the income of the corporation for its fiscal year ending in the year prior to the calendar year when such dividends are paid.

(3) All dividends must be reported in full on the income tax return of the person receiving them, regardless of the deductibility of certain dividends received by corporations. Corporate taxpayers should deduct such dividends as they believe to be deductible. Whether or not the dividends are deductible will be determined in accordance with the records on file with the department of revenue and proper adjustment will be made.

(4) All corporations doing business within Wisconsin must report the dividends paid to residents of Wisconsin on forms 9b. (See s. Tax 2.04).

(5) Distributions received from corporations which may deduct dividends paid from gross income for tax purposes do not qualify as deductible dividends.

**History:** 1-2-56; am. Register, September, 1964, No. 105, eff. 10-1-64; am. (1), Register, March, 1966, No. 123, eff. 4-1-66; am. Register, February, 1975, No. 230, eff. 3-1-75; cr. (5), Register, July, 1978, No. 271, eff. 8-1-78.

**Tax 3.05 Profit-sharing distributions by corporations.** (s. 71.04 (1), Stats.) (1) **DEDUCTION.** Payments made to officers and employes for services rendered under the terms of a profit-sharing agreement, in lieu of or in addition to fixed salaries or other compensation, are proper deductions from gross income. Payments made to the stockholders of a corporation who are not actively engaged in the business are not allowable deductions. If profit-sharing distributions are based on stock holdings, they will be treated as dividends and, therefore, are not allowable deductions.

(2) **FORM OR METHOD OF FIXING COMPENSATION.** The form or method of fixing compensation is not decisive as to the deductibility thereof. If payments are made pursuant to a profit-sharing agreement entered into between employer and employe before services are rendered, which are not influenced by any consideration on the part of the employer other than that of securing the services of the employe on fair and advantageous terms, they will be allowable as deductions from gross income even though in the actual working out of the contract the payments may prove to be greater than the amounts which would ordinarily be paid.

(3) **APPLICABILITY.** As a result of 1987 Wisconsin 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. Register, March, 1966, No. 123, eff. 4-1-66; renun. (1) (a) to be (2) and am., cr. (3), Register, July, 1989, No. 403, eff. 8-1-89.

Register, February, 1990, No. 410

**Tax 3.07 Bonuses and retroactive wage adjustments paid by corporations.** (s. 71.04 (1), Stats.) (1) **GENERAL.** Bonuses for services actually rendered but not based upon a prearranged bonus agreement or established policy are allowable when actually paid, provided the payments when added to the stipulated salaries or other compensation do not exceed a reasonable compensation for the services rendered. Bonuses paid to employes and others which do not have in them the element of compensation or are excessive in comparison to the services rendered are not deductible from gross income. Christmas bonuses, if paid as additional compensation, are proper deductions from gross income if included on federal form W-2 or Wisconsin form 9b as a part of the compensation paid. Retroactive wage adjustments, if reasonable in amount, may be taken as a deduction from gross income in the year in which they are finally determined to be payable. The adjustments are to be reported on federal form W-2 or Wisconsin form 9b.

(2) **APPLICABILITY.** As a result of 1987 Wisconsin 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, July, 1987, No. 379, eff. 8-1-87; renum. to be (1), cr. (2), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.08 Retirement and profit-sharing payments by corporations.** (s. 71.04, Stats.) (1) Retirement payments to retired officers or employes or to their families or dependents, to be deductible from gross income must:

- (a) Qualify as ordinary and necessary expense.
- (b) Be made pursuant to a retirement plan agreement.
- (c) Be reasonable in amount.
- (d) Have been reported on informational returns when required by s. Tax 2.04 or 2.06.

Credits to retirement reserves are not deductible, but actual retirement payments made and charged against such reserves may be deductible in the year made.

(2) Payments to an employe retirement or profit-sharing trust are deductible if:

- (a) Such payments qualify as ordinary and necessary expense.
- (b) The trust is an irrevocable trust and no part of its funds may revert to the employer.
- (c) Payments to the trust are made in accordance with an established policy or agreement.
- (d) The trust is established for the benefit of officers or employes.
- (e) Such payments are reasonable in amount.

**History:** 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66.

**Tax 3.085 Retirement plan distributions.** (s. 71.07 (1), Stats.) (1) **NON-RESIDENTS.** Employe annuity, pension, profit-sharing or stock bonus plan distributions (including self-employed retirement plan distributions) received by a person while a nonresident of Wisconsin shall be exempt from the Wisconsin income tax, regardless of whether any of these

distributions may be attributable to personal services performed in Wisconsin.

(2) **RESIDENTS.** Employee annuity, pension, profit-sharing or stock bonus plan distributions (including self-employed retirement plan distributions) received by a person while a resident of Wisconsin shall be subject to the Wisconsin income tax, regardless of whether any of these distributions may be attributable to personal services performed outside of Wisconsin.

*History:* Cr. Register, March, 1978, No. 267, eff. 4-1-78.

**Tax 3.09 Exempt compensation of military personnel.** (s. 71.01 (3) (f), Stats.) (1) **APPLICABILITY.** This section applies to compensation received prior to the 1986 tax year, due to the repeal of s. 71.01 (3) (f), Stats., by Chapter 29, Laws of 1985.

(2) **COMPENSATION.** In determining the income tax exemption of the first \$1,000 of compensation received from the United States as a reserve or active member of the armed forces under s. 71.01 (3) (f), Stats.:

(a) Compensation received by members of the Wisconsin national guard from the state for weekend highway patrol duty, civil disturbance or riot duty shall not qualify for this exemption.

(b) Compensation received as retirement pay by retired officers and enlisted personnel of the armed services from the United States shall not qualify for this exemption except as provided under par. (d).

(c) Compensation received by commissioned officers of the United States, such as public health officers or coast and geodetic survey officers, who are not members of the armed services shall not qualify for this exemption.

(d) Compensation received by retired, enlisted personnel of the armed services who upon retirement are transferred to reserve units until completion of 30 years of service shall qualify for this exemption. This includes compensation received by retired army and air force personnel who are transferred to reserve units and by retired navy and marine personnel who are transferred to fleet reserve and fleet marine corps reserve, respectively.

*Note:* Under s. 71.01 (3) (f), Stats., the first \$1,000 of compensation received from the United States for service as a reserve or active member of the armed forces is exempt from income taxation. This rule clarifies how several types of payments will be treated under this exemption.

*History:* Cr. Register, August, 1976, No. 248, eff. 9-1-76; renum. (intro.) to (4) to be (2) (intro.) to (d) and am. (2) (intro.) and (b), cr. (1), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.095 Income tax status of interest and dividends from municipal, state and federal obligations received by individuals and fiduciaries.** (s. 71.05 (1) (a) 1 and (b) 1, Stats.) (1) Interest and dividends, less related expenses, payable on the following securities shall be subject to state income tax on individuals and fiduciaries:

(a) District of Columbia Development Land Agency bonds, 42 U.S.C. § 1452.

(b) Export-Import Bank of the United States debentures, 12 U.S.C. § 635.

*Register,* July, 1989, No. 403

(c) Farmer's Home Administration insured notes, 7 U.S.C. §§ 1928 and 1929.

(d) Federal Home Loan Bank dividends, 12 U.S.C. §§ 1426 and 1436.

(e) Federal National Mortgage Association certificates, 12 U.S.C. § 1718.

Note: In 1968, the Federal National Mortgage Association became 2 separate corporations. One corporation retained the original name and the other is known as the Government National Mortgage Association.

(f) Federal National Mortgage Association dividends, 12 U.S.C. § 1719.

(g) Government National Mortgage Association (Ginnie Mae) bonds, 12 U.S.C. §§ 1720 and 1721.

(h) Insured Merchant Marine bonds, 46 U.S.C. § 1273.

(i) Inter-American Development Bank bonds, 22 U.S.C. § 283.

(j) Interest paid on deposits in any federal bank or agency.

(k) International Bank for Reconstruction and Development bonds, 22 U.S.C. § 286.

(l) Small Business Investment Company debentures, 15 U.S.C. §§ 683 and 687.

(m) Tennessee Valley Authority bonds, 16 U.S.C. § 831n-3.

(n) Transit bonds of the Washington Metropolitan Area Transit Authority.

(2) Interest and dividends payable on the following federal securities shall be exempt from the state income tax on individuals and fiduciaries. For purposes of this subsection, the term, "federal securities" means only securities which are direct and primary obligations of the United States and securities the interest of which federal law prohibits states from taxing. Federal securities do not include securities for which the United States is merely a guarantor and, therefore, has an obligation which is secondary and contingent to that of the issuer of the security.

(a) Bank for Cooperative debentures, 12 U.S.C. § 2134.

(b) Bank repurchase agreements for U.S. Government treasury bills, notes, and bonds, if interest is paid by the federal government directly to the taxpayer.

(c) Commonwealth of Puerto Rico public improvement bonds, 48 U.S.C. § 745.

(d) Federal Farm Credit Banks Consolidated Systemwide Securities, 12 U.S.C. § 2055.

(e) Federal Home Loan Bank bonds, debentures, and notes, 12 U.S.C. § 1433.

(f) Federal Housing Authority debentures, 12 U.S.C. §§ 1710 (d) and 1747g (g).

(g) Federal Intermediate Credit Bank debentures, 12 U.S.C. § 2079.

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- (h) Federal Land Bank bonds, 12 U.S.C. § 2055.
  - (i) Federal Reserve Bank dividends, 12 U.S.C. § 531.
  - (j) Production Credit Association debentures, 12 U.S.C. § 2098.
  - (k) Puerto Rico Aqueduct and Sewer Authority revenue bonds, 48 U.S.C. § 745.
  - (l) Puerto Rico Electric Power Authority electric revenue bonds, 48 U.S.C. § 745.
  - (m) Puerto Rico Electric Power Authority power revenue bonds, 48 U.S.C. § 745.
  - (n) Puerto Rico Highway Authority revenue bonds, 48 U.S.C. § 745.
  - (o) Puerto Rico Industrial Development Company bonds, 48 U.S.C. § 745.
  - (p) Puerto Rico Municipal Finance Agency 1974 Series A bonds, 48 U.S.C. § 745.
  - (q) Puerto Rico Ports Authority revenue bonds, 48 U.S.C. § 745.
  - (r) Puerto Rico Public Buildings Authority revenue bonds, 48 U.S.C. § 745.
  - (s) Puerto Rico Public Buildings Authority public education and health facility bonds, 48 U.S.C. § 745.
  - (t) Puerto Rico Telephone Authority revenue bonds, 48 U.S.C. § 745.
  - (u) Student Loan Marketing Association obligations, 20 U.S.C. § 1087-2l.
  - (v) Tennessee Valley Authority bonds, 16 U.S.C. § 831n-4(d).
  - (w) Territory of Hawaii bonds.
  - (x) Territory of Puerto Rico bonds, 48 U.S.C. § 745.
  - (y) United States Postal Service bonds, 39 U.S.C. § 2005.
  - (z) United States savings bonds, 31 U.S.C. § 3124.
  - (za) United States Treasury bills and notes, 31 U.S.C. § 3124.
  - (zb) University of Puerto Rico university system revenue bonds, 48 U.S.C. § 745.
- (3) Interest and dividends, less related expenses, payable on the following state, municipal, and other local government securities shall be subject to the state income tax on individuals and fiduciaries.
- (a) District of Columbia general obligation bonds issued after January 28, 1987, s. 47-33, District of Columbia Code.
  - (b) Municipal bonds.

(c) Public housing agency bonds issued after January 28, 1987, and by agencies located outside Wisconsin. Public housing agency bonds issued on or prior to January 28, 1987, by agencies located outside Wisconsin where the interest from the bonds qualifies for exemption from federal Register, August, 1989, No. 404

income taxation solely because of section 103 of the internal revenue code. "Public housing agency" as used in this paragraph and in sub. (4) (c) means any state, county, municipality, or other governmental entity or public body, or agency or instrumentality thereof, which is authorized to engage in or assist in the development or operation of lower income housing, under 42 U.S.C. § 1437a (b) (6).

(d) Virgin Islands Housing Authority bonds issued after January 28, 1987, 48 U.S.C. § 1408(a).

(e) Wisconsin Health Education Assistance Loan revenue obligation bonds, s. 39.374, Stats.

(f) Wisconsin Housing and Economic Development Authority (WHEDA) bonds issued after January 28, 1987, and all business development revenue bonds, economic development revenue bonds, and Community Housing Alternatives Program (CHAP) housing revenue bonds issued by WHEDA, regardless of when issued, ch. 234, Stats.

(4) Interest and dividends payable on the following state, municipal, and other local government securities shall be exempt from the state income tax on individuals and fiduciaries:

(a) Public housing authority bonds issued by municipalities located in Wisconsin, s. 66.40 (14) (a), Stats.

(b) Wisconsin Housing Finance Authority bonds, 42 U.S.C. § 1437i(b).

(c) Public housing agency bonds issued on or prior to January 28, 1987, by agencies, as defined in sub. (3) (c), located outside Wisconsin where the interest from the bonds qualifies for exemption from federal income taxation for a reason other than or in addition to section 103 of the internal revenue code.

(d) Wisconsin Housing and Economic Development Authority (WHEDA) bonds issued on or prior to January 28, 1987, except business development revenue bonds, economic development revenue bonds and CHAP housing revenue bonds issued by WHEDA.

(e) District of Columbia general obligation bonds issued on or prior to January 28, 1987, where the interest from the bonds qualifies for exemption from federal income taxation for a reason other than or in addition to section 103 of the internal revenue code.

(f) Virgin Island Housing Authority bonds issued on or prior to January 28, 1987, where the interest from the bonds qualifies for exemption from federal income taxation for a reason other than or in addition to section 103 of the internal revenue code.

Note: This rule sets out examples of interest and dividends payable on state, municipal and federal obligations which are taxable and tax exempt.

Section 71.05 (1) (a) 1, Stats. (1985-86), provides for the inclusion in Wisconsin income of natural persons and fiduciaries of any interest, less related expenses, received on state and municipal obligations.

Section 71.05 (1) (b) 1, Stats. (1985-86), provides for the exclusion from Wisconsin income of natural persons and fiduciaries of any interest or dividend income which is by federal law exempt from taxation by Wisconsin.

For periods prior to August 1, 1987, interest accrued from District of Columbia Development Land Agency bonds, Export-Import Bank of the United States debentures, Farmer's Home Administration insured notes, Government National Mortgage Association bonds, Small Business Investment Company debentures and transit bonds of the Washington Met-

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ropolitan Area Transit Authority was not subject to the Wisconsin income tax if payment of principal and interest on such obligations was guaranteed by the United States. As a result of the U.S. Supreme Court decision in the case of *Rockford Life Insurance Company v. Illinois Department of Revenue et al.*, 96 L Ed 2nd 152, the Department of Revenue does not consider these financial instruments to be direct and primary obligations of the United States so as to qualify for exemption from state income taxation. Therefore, by emergency rule effective August 1, 1987, the Department of Revenue amended this rule to reverse its prior interpretation and to provide that interest which accrues on these financial instruments on or after August 1, 1987, is subject to Wisconsin income tax.

Subsection (4) provides that interest accrued on certain state, municipal and other local government securities issued on or before January 28, 1987, is not subject to Wisconsin income tax. This is due to the fact that no modification is provided for in Wisconsin law that would add to federal adjusted gross income interest from these securities if the interest has been excluded from federal adjusted gross income by any reason other than or in addition to section 103 of the Internal Revenue Code.

1987 Wisconsin Act 27 amended s. 71.05 (1) (a) 1, Stats. (1985-86), to provide for the addition to federal adjusted gross income, of any interest not included in federal adjusted gross income which is not specifically exempted from state taxation. This change applies only to securities issued after January 28, 1987. Prior to this act, this addition only applied to interest excluded from federal adjusted gross income solely by section 103 of the Internal Revenue Code.

**History:** Cr. Register, August, 1976, No. 248, eff. 9-1-76; emerg. cr. (1) (g) to (i), am. (2) (intro.), r. (2) (b), (h) and (j), eff. 7-31-87; r. and recr. Register, April, 1988, No. 388, eff. 5-1-88; emerg. am. (3) (intro.) and (c), cr. (3) (g), r. and recr. (4) (b), eff. 1-1-89; am. (2) (intro.), (3) (intro.), (c), (f), (4) (intro.) and (b), cr. (4) (c) to (f), Register, August, 1989, No. 404, eff. 9-28-89.

**Tax 3.096 Interest paid on money borrowed to purchase exempt government securities** (s. 71.05 (1) (b) 1, Stats.). (1) Any amount of interest or dividend income which is by federal law exempt from the Wisconsin income tax shall be reduced by any related expense before it is claimed as a subtraction modification on a Wisconsin income tax return.

(2) Interest expense is a "related expense" if it is incurred to purchase securities producing exempt interest or dividend income and if it is deducted in computing Wisconsin taxable income.

(3) Interest expense is not a "related expense" if it is incurred to purchase securities producing exempt interest or dividend income but is not deducted in computing Wisconsin taxable income (for example, because the taxpayer elects the standard rather than to itemize deductions).

**Note:** The following examples illustrate the proper treatment of the interest expense described in this rule:

<i>Example A:</i>	U.S. bond interest exempt from Wisconsin income tax.	\$ 600
	Interest which was paid on funds used to acquire exempt securities and which was claimed as an itemized deduction.	<u>400</u>
	Subtraction modification.	<u>\$ 200</u>
<i>Example B:</i>	U.S. bond interest exempt from Wisconsin income tax.	\$ 400
	Interest paid to acquire the exempt securities which was claimed as an itemized deduction.	<u>600</u>
	Subtraction modification.	<u>\$ 0</u>
<i>Example C:</i>	U.S. bond interest exempt from Wisconsin income tax.	\$ 400
	Interest paid to acquire the exempt securities but <i>not</i> claimed as an itemized deduction	<u>600</u>
	Subtraction modification	<u>\$ 400</u>



DEPARTMENT OF REVENUE

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History: Cr. Register, January, 1977, No. 253, eff. 2-1-77.

**Tax 3.098 Railroad retirement supplemental annuities.** (s. 71.05 (6) (b) 3, Stats.). Railroad retirement supplemental annuities paid under 45 U.S.C.S. s. 231m are exempt from the Wisconsin taxable income of their recipients.

Note: The Railroad Retirement Act of 1974 as amended by P.L. 98-76 (45 U.S.C.S. s. 231m), effective August 12, 1983, provides that:

“(a) Except as provided in subsection (b) of this section and the Internal Revenue Code of 1954 [26 USCS §§ 1 et seq.], notwithstanding any other law of the United States, or of any State . . . no annuity or supplemental annuity shall be . . . subject to any tax. . . .

(b) (1) This section shall not operate to exclude the amount of any supplemental annuity paid to an individual under section (2) (b) of this Act [45 USCS § 231a (b)] from income taxable pursuant to Federal income tax provisions of the Internal Revenue Code of 1954 [26 USCS § 1 et seq.]”

45 U.S.C.S. s. 231m prohibits states from taxing railroad retirement supplemental annuity payments. Taxpayers may make a modification to federal adjusted gross income to remove this income in computing Wisconsin adjusted gross income.

History: Cr. Register, January, 1977, No. 253, eff. 2-1-77; am. Register, July, 1989, No. 403, eff. 8-1-89.



**Tax 3.10 Salesmen's and officers' commissions, travel and entertainment expense of corporations.** (s. 71.04 (1) and (2), Stats.) (1) Commissions, lump sum and per diem allowances for travel, entertainment and other expenses, or allowances for use of automobiles, are deductible from gross income, if such items are reported on form WT-9 or 9b. Reimbursement of amounts actually expended by officers, employees or others for ordinary and necessary expenses of a taxpayer are deductible if it is proven that the amounts thus reimbursed were actually so expended.

(2) Effective for the 1976 taxable year and thereafter, money or the value or cost of property given to or spent on behalf of a public official is not deductible. "Public official" includes any elected or appointed official, any candidate for public office and any employee of the United States or any state or a political subdivision thereof.

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, July, 1978, No. 271, eff. 8-1-78.

**Tax 3.12 Losses on account of wash sales by corporations.** (s. 71.04 (7), Stats.) The provision for the disallowance of losses from so-called "wash sales" is not applicable to dealers in securities or to persons who continually deal in securities on the stock market and who do not retain possession of their securities for any substantial period of time.

History: 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66.

**Tax 3.14 Losses from bad debts by corporations.** (ss. 71.04 (7), (8), and (9) (b), 1985 Stats.) (1) REGULAR CORPORATIONS. Under s. 71.04 (7), 1985 Stats., corporations, except savings and loan associations, mutual loan corporations, mutual savings banks, production credit associations, credit unions and corporations subject to ss. 71.01 (4) and 71.02 (1) (c), 1985 Stats., may claim losses from bad debts only for losses actually sustained within the year, subject to the following:

(a) Additions to a reserve for bad debts are not deductible.

(b) Partial losses are not deductible, except for regulated companies as set forth in subs. (2) and (3).

(c) Where the surrounding circumstances indicate that a debt is worthless and uncollectible and that legal action to enforce payment would in all probability not result in the satisfaction of execution on a judgment, a showing of these facts will be sufficient evidence of the worthlessness of the debt for the purpose of deduction. The fact that the debtor is in bankruptcy does not in itself justify deduction unless the amount of the creditor's dividend is fixed by the end of the taxable year in which the deduction is claimed.

(d) Bad debts arising from items of income are not deductible unless the items in question have been included in income.

**Example:** Bad debts arising from unpaid rents and similar items of income will not be allowed as a deduction unless the rent or similar income has been included in income on the return for the year the bad debt deduction is claimed or for a previous year.

(2) REGULATED CORPORATIONS. Under s. 71.04 (8), 1985 Stats., a regulated corporation may claim a deduction for the amount of any receivable charged down or written off pursuant to the demand or order of any state or federal regulatory authority. In addition, a state bank may claim a deduction for any account written off pursuant to an order of the examining committee of the bank in accordance with s. 221.09, Stats.

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(a) The deduction may only be claimed in the year set forth in the demand or order requiring the charge-down or write-off.

(b) An election to claim or not claim the charge-down or write-off is made with the filing of the completed tax return. The election, once made, is irrevocable.

(3) **ALLOWABLE LOSS RESERVES.** Under s. 71.04 (9) (b), 1985 Stats., savings and loan associations, mutual savings banks, production credit associations and credit unions may claim as a deduction 2/3 of the reasonable additions to their required loss reserves.

(a) Only reasonable additions to a loss reserve may be included in the computation of the deduction under s. 71.04 (9) (b), 1985 Stats. Additions to a loss reserve that are in excess of the maximum amount required to be allocated to the reserve by a state or federal supervisory authority are not deductible.

(b) An actual transfer to the reserve shall be made in order to receive the deduction. A transfer from loss reserves does not constitute an addition to a loss reserve.

(c) The deduction under s. 71.04 (9) (b), 1985 Stats., is in lieu of a deduction for actual losses under s. 71.04 (7), 1985 Stats. A deduction may not be claimed for both 2/3 of the reasonable addition to the required loss reserve and actual losses sustained.

(d) A deduction for bad debts may be claimed under the method in either s. 71.04 (7), 1985 Stats., or 71.04 (9) (b), 1985 Stats., but not both, for any taxable year. There is no requirement to use the same method from year to year.

(4) **RECOVERIES.** Any amount received on account of a bad debt allowed as a deduction in a prior year under sub. (1) or (2) shall be included in gross income for the taxable year in which it is received or accrued, if the deduction resulted in a tax benefit. The deduction resulted in a tax benefit if a tax benefit is received in the deduction year or in any subsequent year to which the loss in the deduction year is carried forward and used.

(5) **APPLICABILITY.** As a result of 1987 Wisconsin Act 27 which generally federalized Wisconsin's corporate franchise and income tax law, subs. (1), (2), (3), and (4) 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. (1), r. (4), renum. (2) and (3) to be (1) (d) and (4) and am., cr. (2), (3) and (5), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.17 Corporation losses, miscellaneous.** (s. 71.04 (7), 1985 Stats., s. 71.26 (2) (a) and (3) (L), Stats.) (1) Premiums paid on bonds purchased are part of the cost of the bonds, and no portion of the premiums will be allowed as deductions from gross income until the bonds are sold or redeemed.

(2) Losses sustained from illegal transactions are not deductible.

(3) Anticipated losses set up on the books through reserves for contingencies, etc., are not deductible.

(4) Losses from the sale or other disposition of assets are not deductible if a gain on the disposition of the same assets would have resulted in wholly exempt income.

(5) **APPLICABILITY.** As a result of 1987 Wisconsin 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. (1), cr. (4) and (5), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.24 Corporation taxes, miscellaneous.** **History:** 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66; r. Register, February, 1990, No. 410, eff. 3-1-90.

**Tax 3.35 Depletion, basis for allowance to corporations.** (s. 71.04 (2), Stats.) (1) **BASIS.** The capital sum recoverable through depletion allowances is the tax cost of the depletable property. In the absence of competent evidence to the contrary, it will be assumed that the fair market value at January 1, 1911, is represented by the actual cost less depletion sustained to that date. No depletion is deductible on property acquired subsequent to January 1, 1911, the cost of which was deducted as current expense at the time of purchase and allowed for income tax purposes. After depletion of the tax cost to the extent of 100% has been allowed, no further deduction is permissible.

(2) **APPLICABILITY.** As a result of 1987 Wisconsin 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), cr. (2), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.36 Depletion of timber by corporations.** (s. 71.04 (2), Stats.) (1) **COMPUTATION.** The computation of the allowance for depletion of timber for a given year shall be based upon the number of units of timber cut during that year and the tax cost of each unit. The unit cost is determined by dividing the sum of the tax cost at the beginning of the taxable period and the additions at cost during the period by the sum of the units on hand at the beginning of the taxable period and the number of units acquired during such period.

(2) **APPLICABILITY.** As a result of 1987 Wisconsin 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), cr. (2), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.37 Depletion of mineral deposits by corporations.** (s. 71.04 (2), Stats.) The computation of the allowance for depletion of mineral deposits for a given year shall be based upon the number of units of ore or other deposits extracted during the year and the income tax cost per unit.

**History:** 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66.

**Tax 3.38 Depletion allowance to incorporated mines and mills producing or finishing ores of lead, zinc, copper or other metals except iron.** (s. 71.046, Stats.) Section 71.046, created by chapter 370, Laws of 1947 and amended by chapter 438, Laws of 1953, provides for a deduction of prescribed percentages of gross income from sales of the ore or ore products

of lead, zinc, copper or other mines, (except iron mines) and of mills finishing the products of such mines for the smelter.

(1) This depletion deduction may be taken only if the saving in tax due to such deduction is used by the taxpayer in prospecting for ore and duly verified proof thereof is furnished the department of revenue.

(2) Only expenditures in prospecting for ore made during or within 12 months after the close of the year for which the depletion deduction is taken will serve to fulfill the requirement that the tax savings be so used. Unless proof of expenditure is furnished within 24 months after the close of the income year for which the deduction for depletion was made, the taxpayer will be subject to an additional assessment based on the disallowance of the deduction taken.

**History:** 1-2-56; am. (1); Register, September, 1964, No. 105, eff. 10-1-64; am. Register, February, 1975, No. 230, eff. 3-1-75.

**Tax 3.43 Amortization of trademark or trade name expenditures—corporations.** (s. 71.04(2e), 1985 Stats.) (1) **ELECTION.** If a corporation elects to amortize trademark or trade name expenditures under s. 71.04(2e), 1985 Stats.:

(a) The election for a particular trademark or trade name expenditure is irrevocable.

(b) Each trademark or trade name expenditure may be treated differently by the taxpayer.

*Example:* A taxpayer may elect to amortize one trademark but not another, and the length of amortization periods for 2 trade names may vary.

(c) The corporation shall attach to its tax return a statement similar to that required by reg. section 1.177-1 (c) of the internal revenue code. The statement shall include the name and address of the corporation, taxable year involved, character and amount of expenditure, number of months the expenditure will be ratably deducted and a declaration regarding accounting segregation of books and records.

(2) **RECORD KEEPING.** Trademark or trade name expenditures amortized under s. 71.04(2e), 1985 Stats., shall be kept in separate accounts on a taxpayer's books and records.

(3) **EFFECT OF ELECTION ON BASIS.** Upon sale or other disposition of a trademark or trade name amortized under s. 71.04(2e), 1985 Stats., in which gain or loss is recognized, an adjustment to basis shall be made in computing gain or loss for any such amortization allowed or allowable.

(4) **APPLICABILITY.** As a result of 1987 Wisconsin 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:** Cr. Register, July, 1977, No. 259, eff. 8-1-77; am. (1) (intro), (b) and (c), (2) and (3), cr. (4), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.44 Organization and financing expenses—corporations.** **History:** 1-2-56 am. Register, March, 1966, No. 123, eff. 4-1-66; am. Register, August, 1970, No. 176, eff. 9-1-70; r. Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.45 Bond premium, discount and expense—corporations.** (s. 71.04(2) and (15) (g), 1985 Stats.) (1) **GENERAL.** If bonds are issued at a discount or premium, the issuing corporation shall amortize the net amount Register, February, 1990, No. 410

of the discount or premium and the bond expenses over the life of the bonds.

(2) **RETIREMENT.** Except as provided in s. 71.04 (15) (g), 1985 Stats., if bonds are retired at a price in excess of or less than the issuing price, the profit or loss resulting is taxable income or deductible expense in the year in which the bonds are retired, if proper adjustment is made for the discount, bond expense, or premium previously reflected in income.

(3) **REFINANCING.** (a) If a bond issue is refinanced with another bond issue before the first issue matures, any unamortized discount or expense that is applicable to the first issue shall be deducted as current expense in the year that the refinancing takes place and any unamortized premium shall be taken up as income in that year.

(b) If old bonds are exchanged for new bonds instead of being refinanced by the proceeds of a new issue, then any unamortized premium, discount or expense attributable to the old issue shall be combined with similar items attributable to the new issue and amortized over the life of the new issue.

(c) If a bond issue is retired in exchange for stock of the issuing corporation, the transaction is considered a readjustment of the corporation's capital structure and any unamortized discount or expense is not deductible.

(4) **MERGERS.** The surviving corporation in a merger may not deduct the unamortized discount and expense applicable to a bond issue put out by the merged company when the issue is retired by the survivor. Neither may the surviving corporation deduct amortization of the bond discount and expense applicable to a bond issue put out by the merged company.

(5) **APPLICABILITY.** As a result of 1987 Wisconsin 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: Refer to *Great Western Power Co. of California vs. Commissioner*, 297 U.S. 543; *Liquid Carbonic vs. Commissioner*, 34 BTA 1191; and *Wisconsin Electric Power Company vs. Department*, 251 Wis. 346.

History: 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66; am. Register, July, 1978, No. 271, eff. 8-1-78; am., cr. (3) (b), (c), (4) and (5), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.47 Legal expenses and fines—corporations.** (s. 71.04 (2), Stats.) Legal expenses incurred in connection with the operation of a taxpayer's business are proper deductions, unless such business is conducted in violation of law. Fines are not deductible.

History: 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66.

**Tax 3.48 Deductions for research or experimental expenditures—corporations.** (ss. 71.03 (1) (j) and 71.04 (2f), 1985 Stats. and s. 71.26 (2) (a), Stats.) (1) **DEFINITIONS.** In this section:

(a) "Paid or incurred" shall be construed according to the method of accounting used by the taxpayer in computing taxable income.

(b) "Research or experimental expenditures" means expenditures paid or incurred in connection with the taxpayer's trade or business which represent research and development costs in the experimental or labora-

tory sense. The term includes costs incident to the development of an experimental or pilot model, a plant process, a product, a formula, an invention or similar property, and improvements to these types of already existing property and the costs of obtaining a patent, such as attorney's fees expended in making or perfecting a patent application. The term does not include expenditures paid or incurred for acquiring another person's patent, model, production or process; the ordinary testing or inspection of materials or products for quality control; management studies, consumer surveys, advertising or promotions; or research in connection with literary, historical, or similar projects. Neither does the term include expenditures paid or incurred for the acquisition or improvement of land or depreciable property whether incurred by the taxpayer or by another person or organization on its behalf, to the extent of the cost of the component materials of the depreciable property and the costs of labor or other elements involved in its construction and installation.

(2) **DEDUCTION.** Subject to certain limitations, a corporate taxpayer may elect to either deduct research or experimental expenditures in the year paid or incurred, or to capitalize the expenditures and amortize them over a period of not less than 60 months selected by the taxpayer beginning with the month in which the taxpayer first realizes benefits from the expenditures, or to depreciate the expenditures over the useful life of the property to which they relate.

(a) *Election to treat as expense.* Election to treat research or experimental expenditures as expenses may be made by claiming the expenses as a deduction on the return for the year in which paid or incurred. The election shall apply to all research or experimental expenditures paid or incurred in the taxable year of adoption and all subsequent years unless a different method is authorized by the department.

(b) *Election to amortize.* 1. If the taxpayer has not elected to deduct research or experimental expenditures as currently deductible expenses, it may elect to treat expenditures which are chargeable to a capital account with no determinable useful life as deferred expenses which may be amortized ratably over a period of not less than 60 months as selected by the taxpayer. However, if the property resulting from the expenditures has a determinable useful life, the capitalized expenditures or the unamortized balance thereof shall be amortized or depreciated over the determinable useful life.

2. The election to defer the deduction and to amortize over 60 months shall be made by attaching a signed statement to the taxpayer's franchise or income tax return for the first taxable year to which the election is applicable and shall set forth the information required under reg. section 1.174-4 (b) (1) of the internal revenue code.

(c) *Change in method or period.* Permission to change to a different method of treating research or experimental expenditures or to a different period of amortization of deferred expenses shall be required from the department in writing. A request for permission shall be addressed to the Wisconsin Department of Revenue, P.O. Box 8906, Madison, Wisconsin 53708. The request shall include the name and address of the taxpayer, shall be signed by the taxpayer or the taxpayer's duly authorized representative, and shall be filed no later than the last day of the first taxable year for which the change in method or period is to apply. The request



shall set forth the information required under either reg. section 1.174-3 (a) (3) or reg. section 1.174-(4) (b) (2) of the internal revenue code.

(3) **EFFECT ON BASIS.** Research and experimental expenditures not deducted currently are chargeable to a capital account and shall be added to the basis of the property resulting from such expenditures. Upon the sale or other disposition of the property in which a gain or loss is recognized, an adjustment to basis shall be made in computing gain or loss for any amortization allowed or allowable.

(4) **RESEARCH CREDIT.** (a) For taxable years 1984 and 1985, s. 71.04 (2) (b) 5, 1983 Stats., requires that the deduction for expenses or expenditures for research shall be decreased by the full amount of the research credit and research facilities credit computed under the provisions of s. 71.09 (12r) and (12rf), 1983 Stats.

(b) For the taxable year 1986 and succeeding years, the deduction for research and experimental expenses is not required to be reduced, but the full amount of the credit computed is required to be taken into gross income in the year for which the credit was computed.

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

**History:** Cr. Register, February, 1978, No. 266, eff. 3-1-78; renum. (1) (a) to (b) to be (1) (b) and (a) and am. (1) (b), am. (2) (intro.), (a), (b), (c) and (3), cr. (4) and (5), Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.52 Automobile expenses—corporations.** (s. 71.04 (1) and (2), 1985 Stats.) (1) **BUSINESS USE.** If a corporation's automobile is used exclusively for its business purposes, the actual expenses of operating the vehicle, including gasoline, oil, license fees, insurance premiums and depreciation, are deductible from gross income.

(2) **BUSINESS AND PERSONAL USE.** If the corporation's automobile is used partly for business and partly for personal purposes, the expenses of operating the vehicle including gasoline, oil, license fees, insurance premiums and depreciation may be apportioned on the basis of the ratio of business mileage to total mileage.

(a) The amount allocated to business purposes is deductible from the corporation's gross income.

(b) The amount allocated to personal use is not allowable as automobile expense but may be deductible under s. 71.04 (1), 1985 Stats., if the amount is treated as additional compensation to the employe, is reported on a federal form W-2 or Wisconsin form 9b and is reasonable for the services performed.

(3) **APPLICABILITY.** As a result of 1987 Wisconsin 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. Register, March, 1966, No. 123, eff. 4-1-66; r. and recr. Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.54 Miscellaneous expenses not deductible—corporations.** (s. 71.04 (2), Stats.) Miscellaneous expenses which are not properly deductible in arriving at taxable net income include the following:

(1) Charges made by a corporation against its income or surplus covering expenses incurred for personal purposes of its officers, stockholders or employes, unless reported as compensation paid on form WT-9 or form 9b.

(2) Dues to fraternal orders, social clubs.

(3) Political contributions.

(4) For the 1976 taxable year and thereafter, any expenses incurred for or on behalf of a public official.

History: 1-2-56; am. Register, February, 1960, No. 50, eff. 3-1-60; am. Register, September, 1964, No. 105, eff. 10-1-64; am. Register, March, 1966, No. 123, eff. 4-1-66; am. Register, July, 1978, No. 271, eff. 8-1-78.

**Tax 3.55 Donations and contributions—corporations.** History: 1-2-56; am. Register, March, 1966, No. 123, eff. 4-1-66; r. Register, February, 1990, No. 410, eff. 3-1-90.

### Miscellaneous

**Tax 3.81 Offset of occupational taxes paid against normal franchise or income taxes.** (ss. 70.41 (1), (3) and 70.42 (1), (3), Stats.) (1) Occupational taxes are paid to the treasurer of the town, village or city where the elevator, warehouse or dock of the taxpayer is located on or before December 15th each year. The taxpayer may present his receipt showing payment of such tax to the department of revenue as so much cash in payment of normal franchise or income tax assessed against him in the following year on the tax roll for the same district. If the normal franchise or income tax on this roll exceeds the amount of the occupational tax receipt, only the excess need be paid in cash. All surtaxes must be paid in cash.

(2) If the taxpayer neglects to present his occupational tax receipt at the proper time and pays his entire normal franchise or income tax in cash, he cannot present the receipt at a later date and secure a refund of the normal franchise or income tax paid. A taxpayer cannot tender in payment of an additional normal franchise or income tax assessed at a later date an occupational tax receipt that might have been used had the proper franchise or income tax assessment been made in the first place. If the occupational tax receipt tendered in payment of a normal franchise or income tax exceeds the normal income tax, such excess cannot be applied in payment of additional normal franchise or income tax for the same year assessed at a later date. Occupational tax receipts issued in one taxing district cannot be offset against normal franchise or income tax appearing on the roll for another district.

**History:** 1-2-56; am. (1), 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.

**Tax 3.82 Evasion of tax through affiliated interests.** (ss. 71.10 (1) and 71.30 (2) and (8) (a) and (b), Stats.) (1) In administering s. 71.30 (8) (a) and (b), Stats., the department of revenue will apply the statute as interpreted by the following cases and any other applicable cases:

- (a) *Cliffs Chemical Co. v. Tax Commission*, 193 W 295
- (b) *Buick Motor Co. v. Milwaukee*, 43 F (2d) 385
- (c) *Curtis Companies v. Tax Commission*, 314 W 85
- (d) *Palmolive Co. v. Conway*, 37 F (2d) 114; 43 F (2d) 226; 56 F (2d) 83
- (e) *Burroughs Adding Machine Co. v. Tax Commission*, 237 W 423
- (f) *Northern States Power Co. v. Tax Commission*, 237 W 423
- (g) *Kansas City Star v. Department*, 8W (2d) 441.

(2) In administering ss. 71.10 (1) and 71.30 (2), Stats., the department will apply the statute as interpreted by the case of *WOKY, Inc. v. Department*, WTAC (7/5/84) CCH 202-405 and any other applicable cases.

(3) As a result of 1987 Wisconsin 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; renum. (intro.) and (1) to (6) to be (1) (intro.), (a) to (f) and am. (1) (intro.), cr. (1) (g), (2) and (3), Register, July, 1989, No. 403, eff. 8-1-89.

### Assessment, Abatement and Refund Procedure

**Tax 3.83 Domestic international sales corporations (DISCs).** **History:** Cr. Register, July, 1978, No. 271, eff. 8-1-78; r. Register, July, 1989, No. 403, eff. 8-1-89.

**Tax 3.91 Petition for redetermination.** (ss. 71.10 (13) and 71.12 (1), 71.09(7)(k) and 77.59(6), Stats.) (1) The petition for redetermination specified in ss. 71.12 (1), 71.09 (7) (k) and 77.59 (6), Stats., shall be written, preferably typed, on only one side of plain white paper not more than 8 ½ inches wide by 11 inches long and shall be filed in duplicate. It shall set forth clearly and concisely the specific grievances to the assessment or to parts thereof, including a statement of the relevant facts and propositions of law upon which the grievance is based. Every petition shall be signed by the taxpayer or by a duly authorized representative.

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(2) A petition for redetermination is not "filed" within the proper statutory 30-day time period unless it is actually received within the 30-day period, or unless it is mailed in a properly addressed envelope, with postage prepaid, which envelope is postmarked before midnight of the thirtieth day of the period provided in ss. 71.12 (1), 71.09 (7) (k) and 77.59 (6), Stats.

History: 1-2-56; am. Register, February, 1975, No. 230, eff. 3-1-75; am. Register, July, 1978, No. 271, eff. 8-1-78.

**Tax 3.92 Informal conference.** The taxpayer may request in its petition, or at any time before the department of revenue has acted thereon, an informal conference at which the facts and issues involved in the assessment or determination may be discussed. Any such conference will be held at a time and place determined by the department.

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, July, 1978, No. 271, eff. 8-1-78.

**Tax 3.93 Closing stipulations.** If the informal conference results in an agreement as to facts and issues and the law applicable thereto the taxpayer and the department of revenue may enter into a closing stipulation.

History: 1-2-56; am. Register, September, 1964, No. 105, eff. 10-1-64; am. Register, February, 1975, No. 230, eff. 3-1-75.

**Tax 3.94 Claims for refund.** (1) Claims for refund may be filed as provided in s. 71.10 (10) or 77.59 (4), Stats., and shall be in the same form as petitions for redetermination under s. Tax 3.91. A claim for refund is not "filed" within the proper time to meet the requirements of ss. 71.10 (10) and 77.59 (4), Stats., unless it is actually in the possession of the department prior to the expiration of the limitation period provided in s. 71.10 (10) or 77.59 (4), Stats., or unless mailed in a properly addressed envelope, with postage prepaid, which envelope is postmarked before midnight of the last day of the limitation period.

(2) Under s. 71.10 (11), Stats., the reduction of income resulting from renegotiation or price redetermination of any defense contract or subcontract is allowable as a deduction from income of the year in which such income was reported for taxation. A claim for refund filed under this subsection must be accompanied by a verified or photographed copy of the renegotiation agreement or price redetermination. No interest is payable on such refund.

(3) When by reason of the allowance of amortization of war facilities over a period shorter than computed in arriving at the original renegotiation adjustment, or for any other reason, a portion of the profits originally determined to be excessive are rebated to the taxpayer by the federal government, such rebate is to be treated as a further renegotiation adjustment, and should be allocated back to the year of the income which was adjusted. Where a refund of Wisconsin income taxes (due to renegotiation) has previously been made, the additional taxes payable by reason of a renegotiation rebate are to be assessed without interest for the reason that such taxes constitute a return to the state of a portion of the previous refund.

History: 1-2-56; am. (1) and (2), Register, September, 1964, No. 105, eff. 10-1-64; am. (1), Register, May, 1966, No. 125, eff. 6-1-66; am. Register, July, 1978, No. 271, eff. 8-1-78.