

Chapter Tax 3

INCOME TAXATION, DEDUCTIONS FROM GROSS INCOME, EXCLUSIONS AND EXEMPTIONS

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Tax 3.01 Addback and disclosure of related entity expenses. c1d

SCOPE. This section provides further interpretation and explanation relating to the addition and subtraction modifications and disclosure provisions in ch. 71, Stats. In general, the addback statutes provide that a taxpayer shall modify federal income to add back interest, rental, and intangible expenses and management fees that are directly or indirectly paid, accrued, or incurred to a related entity or related person. If certain tests are satisfied, the taxpayer may subsequently deduct the expenses. The addback statutes also impose a disclosure requirement for related entity expenses. Notwithstanding a taxpayer satisfying the tests allowing the deductions of related entity expenses, the department has express authority to reallocate a taxpayer[s] income, deductions, credits, or allowances to prevent tax evasion or to clearly reflect income. The department also has express authority to disregard transactions that lack economic substance.

c2d DEFINITIONS. In this section:

cad XAddbackY means the addition and subtraction modifications and disclosure requirement required by ss. 71.05 c6d cad 24. and cbd 45., 71.26 c2d cad 7. and 8., 71.34 c1kd cjd and ckd, 71.45 c2d cad 16. and 17., and 71.80 c23d, Stats. Where applicable, XaddbackY also refers to subtraction modification to a related entity pursuant to ss. 71.05 c6d cbd 46., 71.26 c2d cad 9., 71.34 c1kd cLd, and 71.45 c2d cad 18., Stats.

cbd XAggregate effective tax rate,Y for a related entity, is the sum of its effective tax rates for each state, U.S. possession, or foreign country where it is engaged in business. In determining whether a related entity is engaged in business in a state, U.S. possession, or foreign country, the legal standard set forth under s. 71.22 c1rd, Stats., shall apply to such other jurisdiction for purposes of applying the addback provisions.

ccd XCaptive insurance company,Y for purposes of applying the addback provisions, means an insurer that issues any policy of insurance or reinsurance with respect to which the person insured is related under section 267 or 1563 of the Internal Revenue Code.

cdd XCaptive REITY means a real estate investment trust other than a qualified real estate investment trust under s. 71.22 c9add, Stats.

ced XCombined unitary incomeY has the meaning given in s. Tax 2.60 c2d ced.

efd XEffective tax rateY, for a particular jurisdiction for a related entity, means the maximum tax rate imposed by that jurisdiction multiplied by the related entity[s] apportionment percentage, if any, computed for that particular jurisdiction.

cgd XIntangible expenseY has the meaning given in s. 71.01

c5nd, 71.22 c3gd, 71.34 c1cd, or 71.42 c1sgd, Stats., as applicable.

chd XIntangible propertyY has the meaning given in s. 71.01 c5pd, 71.22 c3hd, 71.34 c1dd, or 71.42 c1shd, Stats., as applicable.

cid XInterest expenseY has the meaning given in s. 71.01 c5sd, 71.22 c3md, 71.34 c1ed, or 71.42 c1td, Stats., as applicable.

cjd XManagement feesY has the meaning given in s. 71.01 c7vd, 71.22 c6dd, 71.34 c1hd, or 71.42 c3cd, Stats., as applicable.

ckd XPass-through entitiesY include tax-option cSd corporations, partnerships, limited liability companies treated as partnerships, estates, and trusts.

cLd XRental expensesY or Xrent expensesY has the meaning given in s. 71.01 c9and, 71.22 c9and, 71.34 c1rd, or 71.42 c4nd, Stats., as applicable.

cmd XRelated entityY or Xrelated entitiesY has the meaning given in s. 71.01 c9amd, 71.22 c9amd, 71.34 c1pd, or 71.42 c4md, Stats., as applicable. The terms include related individuals. In determining relatedness under section 267 of the Internal Revenue Code, section 267 cbd controls, which defines relationships through which taxpayers would be considered related for purposes of disallowing losses or deductions on transactions between related taxpayers. Section 707 cbd of the Internal Revenue Code, incorporated by reference into section 267, applies in determining whether partnerships and limited liability companies treated as partnerships and their respective partners are related. The stock attribution rules of section 318 cad of the Internal Revenue Code otherwise apply for purposes of establishing indirect stock ownership and thereby determine related entities.

Examples: The following relationships involving partnerships and limited liability companies cLLCd constitute related entities:

1. A partnership and a partner who holds a direct or indirect capital or profits interest in that partnership of more than 50%.
2. An LLC and a member who holds a direct or indirect interest in that LLC of more than 50%.
3. Two partnerships or LLCs if a single partner or member owns, directly or indirectly, more than 50% of both entities.

cnd XRelated entity expensesY means interest, rent, or intangible expenses, and management fees, either as an individual expense type or a combination of expense types in a transaction or series of transactions whether paid, accrued, or incurred directly or indirectly.

Examples: 1d Corporation A is the parent company of Corporation B and Corporation C, which are related entities. B owns intangible property that C uses in its manufacturing process. C incurs a royalty expense as a result. A purchases the goods from C that A will hold and sell as inventory. This increased cost due to the royalty is reflected in A[s] cost of goods sold. The royalty portion of the cost of goods sold represents an indirect related entity expense that must be added back to A[s] income.

2d Corporation A, Corporation B, Corporation C, and Corporation D are related

entities. A and D have nexus in Wisconsin, but B and C do not. B is not subject to tax in any state. Previously, D owned intangible property which A used in operating its business. In a series of transactions, D transfers the intangible property to B. B then licenses the intellectual property to C, the inventory purchasing company. A purchases the inventory from C. The royalty portion of A's cost of goods sold represents an indirect related entity expense that must be added back to A's income.

3d Corporation O, Corporation H, and Corporation S are related entities. O, the operating company, transfers various items of intangible property to H in conformity with section 351 of the Internal Revenue Code. H enters into an agreement with S that will allow S to license H's intangible property. S and O are related entities. S licenses the intangible property to O whereby O pays fees to S based on a percentage of sales. The intangible expense between O and S is a related entity expense that must be added back to O's income.

c3d ADDITION MODIFICATION. *cad General.* A corporation, individual, or pass-through entity shall modify federal income for Wisconsin purposes so that related entity expenses that were paid, accrued, or incurred to a related entity are added back to income.

cbd Taxpayers required to modify income. The addition modification applies to any individual, corporation, or pass-through entity that has deducted or excluded under the Internal Revenue Code any amounts for related entity expenses that are directly or indirectly paid, accrued, or incurred to, or in connection directly or indirectly with one or more direct or indirect transactions with, one or more related entities.

ccd Interest expense. Interest expenses include interest expenses otherwise deductible under section 163 of the Internal Revenue Code and otherwise deductible in the computation of Wisconsin adjusted gross income or Wisconsin net income. Expenses deductible as interest expenses under section 163 of the Internal Revenue Code include:

1. Interest paid or accrued within the taxable year on indebtedness.
2. Original issue discount.
3. Non-separately stated interest included in carrying charges for installment purchases.
4. Redeemable ground rents, excluding amounts paid in redemption.
5. Premiums paid or accrued for mortgage insurance.

Example: Taxpayer A and Taxpayer B are related and A paid, accrued, or incurred \$3,000 of original issue discount to B. Taxpayer C and Taxpayer D are related and C paid, accrued, or incurred \$3,000 of interest that have been capitalized under section 263A of the Internal Revenue Code. Taxpayer E and Taxpayer F are unrelated and E has paid, accrued, or incurred \$100,000 of indebtedness interest to F. A is required to add back \$3,000 to its income since it paid, accrued, or incurred this amount to a related entity and it is the type of interest expense deductible under section 163 of the Internal Revenue Code. C is not required to add back \$3,000 to its income since this type of interest is not the type of interest that is deductible under section 163 of the Internal Revenue Code. E is not required to add back \$100,000 since the addback provisions do not apply to unrelated taxpayers.

cdd Rental expense. 1. Rent expenses include expenses otherwise deductible in computing Wisconsin adjusted gross income or Wisconsin net income which are attributable to, for the use of, or for the right to use, real property, including the following:

- a. Tangible personal property affixed to real property if the owner of the tangible personal property is the same as or related to the owner of the real property.
- b. Services rendered in connection with rented real property if the owner of the property is the same as or related to the entity providing the service.

2. For purposes of the addition modification, the method used to compute the expense and the manner in which it is reported for financial accounting purposes are immaterial.

Example: Amounts paid under capital leases might not be called Xrent expenses Y in the financial accounting records of a taxpayer, but these expenses are considered Xrent expenses Y for purposes of the addition modification.

ced Management fees. 1. Other than services provided by the taxpayer's own employees, management fees include expenses and costs otherwise deductible in computing Wisconsin adjusted gross income or Wisconsin net income for the purchase or reten-

tion of services, including services that pertain to any of the following:

- a. Accounts receivable or payable.
- b. Employee benefit plans.
- c. Insurance, including self-insurance.
- d. Legal matters.
- e. Payroll.
- f. Data processing.
- g. Purchasing.
- h. Taxation.
- i. Financial matters.
- j. Securities.
- k. Accounting.
- L. Reporting or compliance matters.
- m. Activities similar to those described in this subd. 1. a. to L.

2. Subdivision 1. a. to m. are in no way intended to and should not be construed as limiting the scope of the activities subject to this paragraph.

efd Intangible expenses. 1. Intangible expenses include any of the following expenses to the extent they would otherwise be deductible in the computation of Wisconsin adjusted gross income or Wisconsin net income:

- a. Royalty, patent, technical, and copyright fees.
- b. Licensing fees.
- c. Losses related to, or incurred in connection directly or indirectly with, factoring transactions or discounting transactions.
- d. Amortization expenses.
- e. Other expenses, losses, or costs for, related to, or directly or indirectly in connection with acquiring, using, maintaining, managing, owning, selling, exchanging, or disposing of intangible property.

2. For a taxpayer purchasing amortizable intangible property from a related entity, the amortization expenses on that property are intangible expenses subject to the addition modification. This also applies to any other amortizable intangible expenses paid, accrued, or incurred between a taxpayer and a related entity.

c4d SUBTRACTION MODIFICATION. *cad General.* Related entity expenses paid, accrued, or incurred to a related entity may be deducted to the extent such expenses meet the requirements of s. 71.80 c23d *cad*, Stats., and this subsection.

cbd Requirements. 1. Section 71.80 c23d *cad*, Stats., provides that if a taxpayer added back related entity expenses, the taxpayer may then deduct such expenses if the taxpayer meets the requirements under s. 71.80 c23d *cad* 3., Stats. The taxpayer shall establish it meets the requirements under s. 71.80 c23d *cad* 3., Stats., by clear and convincing evidence. The taxpayer shall meet all of the following requirements:

- a. The primary motivation for the transaction was one or more business purposes other than the avoidance or reduction of state income or franchise taxes.
- b. The transaction changed the economic position of the taxpayer in a meaningful way apart from tax effects.
- c. The expense was paid, accrued, or incurred using terms that reflect an arm's length relationship.

2. This paragraph is the primary test for establishing whether related entity expenses may be deducted. The tests in pars. **cbd** and **ced** are indicators that the test under this paragraph may have been met.

ccd Factors indicating requirements are not met. Factors in-

dicating that the related entity expense does not meet the requirements under par. [cbd](#) include:

1. There was no actual transfer of funds from the taxpayer to the related entity.

Example: A book or journal entry alone is not considered an actual transfer of funds.

2. There was an actual transfer of funds, then the funds were substantially returned to the taxpayer, either directly or indirectly. Such return need not be immediate in order for this factor to be applicable.

3. If the transaction was entered into on the advice of a tax advisor, regardless of whether a client relationship exists or existed at the time of the advice, the advisor's fee was determined by reference to the tax savings. XTax advisorY includes a Xmaterial advisorY under s. [71.81 c1d cbd](#), Stats.

4. The related entity does not regularly engage in similar transactions with unrelated parties on terms substantially similar to those of the subject transaction.

5. The transaction was not entered into at terms comparable to an arm's length transaction as determined by Treas. Reg. section 1.482-1cbd.

6. There was no reasonable expectation of profit from the transaction apart from the tax benefits.

7. The transaction resulted in the improper matching of income and expenses.

8. The expense for the transaction was accrued under Financial Accounting Standards Board Interpretation number 48. For purposes of this section, this factor applies to both income and franchise taxes.

Note: Financial Accounting Standards Board Interpretation number 48 is available on the Financial Accounting Standards Board's web site at www.fasb.org.

9. If the related entity expense is a rental expense, the rent was paid, accrued, or incurred to a captive real estate investment trust.

10. If the related entity expense is an interest expense, additional factors specific to interest expenses include any of the following:

a. The taxpayer is not sufficiently capitalized or has no reasonable expectation to make payment on the debt underlying the interest expense.

b. There is no written contract underlying the interest expense.

c. There is a contract, but the contract does not reflect an interest obligation resulting from an arm's length transaction.

d. The interest is attributable to an unpaid charge that is not an allowable expense, a loan from a captive insurance company, a dividend note, a loan from a related entity with net business loss carryforwards or net operating loss carryforwards, or a loan from a related entity that is an intermediary set up in a jurisdiction that imposes no corporate-level income or franchise tax.

Related entity acts as a conduit. 1. ZRequirements.[Section [71.80 c23d cad](#), Stats., provides that if a taxpayer added back related entity expenses, the taxpayer may then deduct such expenses if the taxpayer meets the requirements under s. [71.80 c23d cad 1.](#), Stats. The taxpayer shall establish it meets the requirements under s. [71.80 c23d cad 1.](#), Stats., by clear and convincing evidence. The taxpayer shall meet all of the following requirements:

a. The related entity to which the taxpayer paid, accrued, or incurred related entity expenses during the taxable year directly or indirectly paid, accrued, or incurred such amounts in the same taxable year to a person who is not a related entity. In this subdivision, Xtaxable yearY means the taxable year of the taxpayer claiming the deduction for related entity expenses paid, accrued,

or incurred to the related entity. The department will consider such expenses the related entity pays, accrues, or incurs to an unrelated entity by the unextended due date of the taxpayer's income or franchise tax return to be paid, accrued, or incurred within the taxpayer's Xtaxable year.Y However, such expenses that occur after the end of the taxpayer's taxable year may not then be counted again as occurring in the subsequent taxable year.

b. Except as provided in subd. 2., the related entity to which the taxpayer paid, accrued, or incurred such expenses is a holding company or a direct or indirect subsidiary of a holding company, as defined in [12 USC 1841cad](#) or [cld](#) or [12 USC 1467acad c1dcDd](#).

2. ZInvestments of a bank, subsidiary, or affiliate.[Related entity expenses may not satisfy the test in subd. 1. b. when such expenses are paid, accrued, or incurred directly or indirectly to an entity that is organized under the laws of another jurisdiction and that primarily holds and manages investments of a bank, subsidiary, or affiliate, unless the related entity expenses satisfy the provisions in subd. 1. a.

3. ZInterest on acquisition of stock.[As specifically provided under s. [71.80 c23d cad 1.](#), Stats., interest expense paid, accrued, or incurred in connection with any debt incurred to acquire taxpayer's assets or stock under section 368 of the Internal Revenue Code may not satisfy the test under this paragraph.

Example: Corporation A borrows money from Corporation B. No portion of the debt was used to acquire A's own stock or assets under section 368 of the Internal Revenue Code. In order to obtain the funds to loan to A, B borrows money from Bank C. A is a calendar year taxpayer, while B is on a fiscal year beginning July 1 and ending June 30. During the calendar year 2008, A accrued \$100,000 of interest expense attributable to the loan from B. In turn, B accrued \$90,000 of interest expense attributable to the loan from C during that same time period of January 1, 2008, through December 31, 2008. During the period of January 1, 2009, through March 15, 2009, B accrued \$10,000 of interest expense to C. For purposes of determining if the test under subd. 1. a. applies to A's interest expense, B may be considered to have accrued \$100,000 of interest expense c\$90,000 + \$10,000 to C in A's 2008 taxable year. However, in A's 2009 taxable year, A cannot consider the \$10,000 of interest expense accrued by B to C during the period of January 1, 2009, through March 15, 2009, to be accrued during A's 2009 taxable year.

4. ZAllocation of expense paid to unrelated entity.[If less than 100 percent of the total related entity expenses paid, accrued, or incurred to the related entity from the taxpayer and all other related entities is paid, accrued, or incurred to an unrelated entity, a pro rata share of the taxpayer's related entity expenses is considered to satisfy the test under subd. 1. a.

Example: Taxpayer A made a \$200,000 interest payment to Taxpayer B. No portion of the underlying debt was used to acquire the taxpayer's own stock or assets under section 368 of the Internal Revenue Code. B received a total of \$800,000 of related entity interest income during A's taxable year. Of this amount, \$200,000 was from A and \$600,000 from other related entities. In A's taxable year, B paid \$400,000 of interest expense to unrelated entities. In this case, \$100,000 c\$200,000{\$800,000d x \$400,000d of the interest A paid to B would be considered paid, accrued, or incurred to unrelated entities in A's taxable year.

Related entity included income in tax base. 1. ZRequirements.[Section [71.80 c23d cad](#), Stats., provides that if a taxpayer added back related entity expenses, the taxpayer may then deduct such expenses if the taxpayer meets the requirements under s. [71.80 c23d cad 2.](#), Stats. The taxpayer shall establish it meets the requirements under s. [71.80 c23d cad 2.](#), Stats., by clear and convincing evidence. The taxpayer shall meet all of the following requirements:

a. The related entity was subject to tax on, or measured by, its net income or receipts in this state or any state, U.S. possession, or foreign country.

b. The related entity's tax base in such state, U.S. possession, or foreign country included the income received from the taxpayer corresponding to the related entity expenses.

c. The related entity's aggregate effective tax rate applied to

such income or receipts was at least 80 percent of the taxpayer[s aggregate effective tax rate.

d. The related entity is not a real estate investment trust under section 856 of the Internal Revenue Code, other than a qualified real estate investment trust.

2. ZDiffering taxable years.[For both the taxpayer and the related entity, compute the aggregate effective tax rate for the taxable year that included the transaction date. If the related entity is on a taxable year that ends after the taxpayer[s taxable year, the aggregate effective tax rate shall be determined as follows:

a. If in the related entity[s most recently ended taxable year the related entity was subject to a tax on or measured by net income or receipts in a state, U.S. possession, or foreign country, the related entity[s aggregate effective tax rate shall be computed based on the related entity[s most recently ended taxable year.

b. If the related entity was not subject to such tax for its most recently ended taxable year, the related entity shall modify the computation of the aggregate effective tax rate as provided in subd. 2. c.

c. The related entity uses 100 percent as the related entity[s apportionment percentage and the related entity uses the statutory tax rate of the state where the related entity is incorporated, organized, formed, or, if the related entity is an individual, where the individual resides.

3. ZItems not includable in aggregate effective tax rate.[The following are not included in the computation of the aggregate effective tax rate:

a. If the related entity expense was paid, accrued, or incurred to a pass-through entity, any tax rate that is imposed at the shareholder, partner, member, or beneficiary level rather than at the pass-through entity level for that state, U.S. possession, or foreign country.

b. If the related entity is a pass-through entity, only taxes imposed at the entity level that are on or measured by net income or receipts may be included in the pass-through entity[s effective tax rate for a particular jurisdiction. A pass-through entity[s aggregate effective tax rate cannot include taxes imposed against the entity[s shareholders, partners, members, or beneficiaries. If a pass-through entity elects to file a composite return in a jurisdiction on behalf of some or all of its shareholders, partners, members, or beneficiaries, the tax rate applicable to that composite return cannot be included in the entity[s effective tax rate for that jurisdiction.

c. The tax rate of any jurisdiction where the taxpayer files with the related entity or the related entity files with another entity a combined or consolidated report or return if the report or return results in eliminating the tax effects of transactions, directly or indirectly, between either the taxpayer and the related entity or between the related entity and another entity.

4. ZItems includable in aggregate effective tax rate.[The following are included in the computation of the aggregate effective tax rate:

a. Withholding taxes, such as the one imposed by s. 71.775, Stats., paid on income distributable to owners or beneficiaries of the pass-through entity, may be considered entity-level taxes if the state, U.S. possession, or foreign country imposes the withholding as a tax on the income of the pass-through entity.

b. The Wisconsin economic development surcharge, which is imposed on tax-option cSd corporations pursuant to s. 77.93 c1d, Stats.

5. ZDividends paid deduction.[If the related entity is not taxed on some or all of its income in a state, U.S. possession, or foreign country because the entity is eligible for a dividends paid

deduction under the laws of that jurisdiction, the amount of income considered to be included in its tax base in that jurisdiction is the amount of income after applying the dividends paid deduction. If the dividends paid deduction is less than 100 percent of the related entity[s total income, a pro rata share of its income from the transaction is deemed to be excluded from its tax base in that jurisdiction.

6. ZRelated entity has loss or credit carryforwards.[For purposes of applying the test under par. ced, the related entity[s aggregate effective tax rate is computed without regard to loss carryforwards or credit carryforwards. If the related entity has no tax liability in a particular state, U.S. possession, or foreign country because of its loss or credit carryforwards, the related entity[s effective tax rate in that jurisdiction still remains that jurisdiction[s maximum statutory tax rate multiplied by the related entity[s apportionment percentage in that jurisdiction.

Example: Taxpayer A makes a \$500,000 interest payment to Corporation C, a related corporation. Corporation C has no other income and is engaged in business only in State X. Corporation C has a \$1,000,000 loss carryforward in State X and uses this carryforward to offset the \$500,000 related entity interest income from Taxpayer A. Therefore, Corporation C owes no tax to State X. State X has a maximum corporation income tax rate of 6.2%. Corporation C[s aggregate effective tax rate would be 6.2%.

c5d DISALLOWED RELATED ENTITY EXPENSES. cad *General.* A related entity may subtract income that corresponds to related entity expenses if such expenses are disallowed to the taxpayer.

cbd *Subtraction for disallowed expenses.* Except as provided in par. cfd, if a taxpayer cannot deduct a related entity expense it paid, accrued, or incurred to a related entity because the expense did not meet one of the tests under sub. c4d, the related entity may subtract the income that corresponds to the expense that was disallowed to the taxpayer.

ccd *Form required to substantiate income exclusion.* Unless otherwise provided by the department, both the taxpayer and the related entity shall complete the form prescribed by the department to substantiate the income exclusion. The related entity shall file the completed form prescribed by the department with its Wisconsin income or franchise tax return on which it is claiming the subtraction from income. If the related entity is not doing business in Wisconsin, neither the taxpayer nor the related entity has to complete the form prescribed by the department to substantiate the income exclusion.

cdd *Expense below disclosure threshold.* Except as provided in par. ced, the subtraction from income provided in this subsection may apply even if the disallowed related entity expense was below the threshold of \$100,000 under sub. c7d cbd 3.

ced *Related entity income exclusion limitation.* A taxpayer may not use the form prescribed by the department to disallow related entity expenses to claim a related entity expense if all of the following conditions apply:

1. The primary motivation for the transaction was one or more business purposes other than the avoidance or reduction of state income or franchise taxes.

2. The transaction changed the economic position of the taxpayer in a meaningful way apart from tax effects.

3. The expenses were paid, accrued, or incurred using terms that reflect an arm[s length relationship.

cfd *Evasion of taxes and distortion of income.* A taxpayer meeting the criteria to deduct related entity expenses under s. 71.80 c23d, Stats., but fails, whether intentionally or not, to disclose such related entity expenses as prescribed, the department at its discretion may disallow the corresponding income exclusion to the related entity and allow the expense to the taxpayer.

Example: Taxpayer A and Taxpayer B are related entities. A[s net income for the year is \$50,000 and B[s net income is \$750,000. A incurred \$100,000 in interest expenses to B. Realizing there is a benefit to not disclosing the related entity expenses, A reports \$150,000 in net income, and B reports \$650,000 in net income. The de-

partment may disallow the interest income exclusion to B and allow the interest expense to A. As a result, A must report \$50,000 of net income and B must report \$750,000 of net income.

c6d MISCELLANEOUS RULES. *cad Combined groups.* 1. As provided in s. [Tax 2.61 c6d cad 6.](#), for related entity expenses paid, accrued, or incurred between combined group members, including pass-through entities owned by those members to the extent of their distributive shares of income, the addition modifications for related entity expenses under ss. [71.26 c2d cad 7.](#) and [71.45 c2d cad 16.](#), Stats., are not required to the extent the recipient of the income includes the income in the combined unitary income. The provisions under s. [Tax 2.61 c6d cad 6.](#) only apply to corporations that are combined group members at the time of the transactions resulting in related entity expenses.

2. The addition modifications for addbacks are required in cases where related entity expenses are included in combined unitary income but the corresponding income is or was not included in the combined unitary income. To illustrate, without limiting the application of this subdivision in any way, a related entity expense paid, accrued, or incurred to a related entity that is not a combined group member is subject to the addback provisions. Likewise, a related entity expense paid, accrued, or incurred to a combined group member that excluded the corresponding income from the combined unitary income is subject to the addback provisions.

cbd Pass-through entities. Shareholders of a tax-option cSd corporation, members of a limited liability company treated as a partnership, partners of a general or limited partnership, and beneficiaries of trust and estates need not make an addition modification to their respective incomes in cases where their respective schedules K-1 report the related entity expenses as fully deductible.

ccd Disregarded entities. Transactions resulting in related entity expenses between an entity that is disregarded for Wisconsin income and franchise tax purposes and its owner need not be reported and disclosed.

cdd Individual itemized deduction credit. An individual who has paid, accrued, or incurred related entity expenses is not required to disclose such expenses on a form prescribed by the department if the individual reports the expenses as part of the individual[s] itemized deduction credit under s. [71.07 c5d](#), Stats. An individual wishing to treat related entity expenses as business expenses shall disclose such expenses on a form prescribed by the department as applicable.

ced Taxpayers subject to apportionment. If a taxpayer is subject to apportionment, the taxpayer shall report and disclose the amounts that are required to be added back before apportionment. For purposes of determining the threshold amount of \$100,000 under sub. [c7d cbd 3.](#), the taxpayer shall use the apportioned amounts. However, the taxpayer shall not multiply by the apportionment percentage those amounts of related entity expenses added back to income that are not attributable to apportionable income. The apportionment percentage shall be recomputed after any addbacks.

c7d ADMINISTRATION AND COMPLIANCE. *cad Authority to distribute or disregard.* Notwithstanding the modifications provided under ss. [71.05 c6d cbd 45.](#), [71.26 c2d cad 8.](#), [71.34 c1kd ckd](#), and [71.45 c2d cad 17.](#), Stats., the department has express authority under ss. [71.30 c2d](#) and [71.80 c1d cbd](#), Stats., to distribute, apportion, or allocate income, deductions, credits, or allowances between or among related entities in order to prevent evasion of taxes or to clearly reflect the income of the entities. Additionally, the department has express authority under ss. [71.30 c2md](#) and [71.80 c1md](#), Stats., to disregard transactions be-

tween related entities if those transactions lack economic substance. This authority is also applicable to the modifications under ss. [71.05 c6d cbd 46.](#), [71.26 c2d cad 9.](#), [71.34 c1kd cLd](#), and [71.45 c2d cad 18.](#), Stats.

cbd Timely disclosure. 1. A taxpayer with related entity expenses shall disclose such expenses on or before the extended due date of the return for the year in which the expenses are reported. The department is authorized to disallow related entity expenses, even if the expenses meet the conditions in s. [71.80 c23d cad](#), Stats., and sub. [c4d](#) for failure to timely disclose such expenses. The form prescribed by the department to disclose related entity expenses shall not be accepted by the department if filed with an amended return after the extended due date. Failure to disclose or untimely disclosure by a taxpayer subjects the taxpayer and related entities to the provisions of sub. [c5d cfd](#).

2. A pass-through entity is responsible for timely disclosing related entity expenses on a form prescribed by the department. The shareholder, partner, member, or beneficiary is not responsible for disclosing related entity expenses if such expenses are passed through to them. A shareholder, partner, member, or beneficiary having related entity expenses independent of those passed through to them shall disclose such expenses on a form prescribed by the department as applicable.

3. A taxpayer is not required to disclose related entity expenses on a separate form prescribed by the department if the total interest, rent, and intangible expenses and management fees paid, accrued, or incurred to all related entities reduces the taxpayer[s] net income by a total amount that is equal to or less than \$100,000. If the taxpayer has related entity expenses that reduce the taxpayer[s] net income by more than a total of \$100,000, the taxpayer shall file and disclose such expenses on a form prescribed by the department. For multistate taxpayers, the \$100,000 threshold is determined after applying the Wisconsin apportionment percentage. If the taxpayer is a pass-through entity, the \$100,000 threshold is determined at the entity level. The fact that a taxpayer[s] total related entity expenses do not surpass the \$100,000 threshold amount does not preclude the department from enforcing the addback provisions against the taxpayer.

History: CR 10-095: cr. Register November 2010 No. 659, eff. 12-1-10; correction in c2d cmd and renumbering of c2d chd and cid made under s. [13.92 c4d cbd 1.](#) and 7., Stats., Register November 2010 No. 659; CR 12-011: am. c4d ced 4. b. Register July 2012 No. 679, eff. 8-1-12; CR 14-005: am. c4d ced 4. b. Register August 2014 No. 704, eff. 9-1-14; CR 17-019: am. c7d cbd 1., Register June 2018 No. 750 eff. 7-1-18.

Tax 3.02 Pass-through entity withholding. c1d

PURPOSE. This section provides additional guidance with respect to the treatment of withholding tax for pass-through entities.

c2d CREDIT FOR NONRESIDENT ENTERTAINER, LOTTERY, AND PARI-MUTUEL WITHHOLDING. A pass-through entity may elect to allocate nonresident entertainer, lottery, and pari-mutuel withholding to its nonresident partners, members, shareholders, or beneficiaries, but only to the extent the income subject to withholding is allocated to those partners, members, shareholders, or beneficiaries. A pass-through entity may credit amounts withheld under ss. [71.64 c5d](#) and [71.67 c4d](#) and [c5d](#), Stats., or amounts paid or deposited under s. [71.80 c15d cbd](#) or [ccd](#), Stats., against the withholding amounts required under s. [71.775 c2d](#), Stats., to such extent, in the manner and form prescribed by the department.

Example: Basement Rockers is a four-member rock band. Basement Rockers is a tax-option cSd corporation and its four rock stars are the corporation[s] shareholders. They are nonresidents of Wisconsin. The band plays in three different venues in Wisconsin during the taxable year and each venue pays the band \$10,000. For Venue 1, neither a surety bond is filed nor cash deposited. The venue withholds 6% and immediately pays the amount withheld to the department. For Venue 2, a bond is not filed, cash is not deposited, and no amounts are withheld. For Venue 3, Basement Rockers files a surety bond for 6% of the total contract price. Basement Rock-

ers may only elect to allocate to its shareholders the amounts for Venue 1 and Venue 3.

History: CR 10-095; cr. Register November 2010 No. 659, eff. 12-1-10.

Tax 3.03 Dividends received deduction — corporations. c1d PURPOSE. This section clarifies the deduction from gross income allowed to corporations for dividends received. Dividends may be deductible due to the recipient[s] ownership of the payer corporation, as provided in sub. c3d.

c2d DEFINITION. XDividends receivedY means gross dividends minus taxes on those dividends paid to a foreign nation and claimed as a deduction under ch. 71, Stats.

Note: Refer to s. 71.26 c3d cjd, Stats.

c3d DIVIDENDS DEDUCTIBLE DUE TO OWNERSHIP. A corporation may deduct from gross income 100 percent of the dividends received from a payer corporation during a taxable year if both of the following occur:

cad The dividends are paid on common stock of the payer corporation.

cbd The corporation receiving the dividends owns directly or indirectly during the entire taxable year in which the dividends are received at least 70 percent of the total combined voting stock of the payer corporation.

Note: 1d Refer to s. 71.26 c3d cjd, Stats.

2d Only cash dividends were deductible by the recipient in taxable years 1980 through 1986. This limitation was eliminated by 1987 Wis. Act 27.

3d For taxable years 1980 through 1983 the deduction was limited to 50% of the dividends received.

4d For the taxable year 1984 the deduction was limited to 75% of the dividends received.

5d For taxable years 1985 and thereafter the deduction equals 100% of the dividends received.

6d For taxable years beginning before January 1, 1993, the corporation receiving the dividends was required to own directly or indirectly during the entire taxable year in which the dividends were received at least 80% of the total combined voting stock of the payer corporation. The percentage of ownership requirement was changed from 80% to 70% by 1993 Wis. Act 16.

c4d LIMITATION ON DEDUCTION. The deduction under sub. c3d may not exceed the dividend received and included in gross income for a taxable year.

c5d DIVIDENDS INCLUDABLE IN GROSS INCOME. All dividend income shall be included in full in gross income on the franchise or income tax return of the recipient, whether or not certain dividends are deductible.

c6d COMBINED GROUPS. The dividends elimination provisions of s. Tax 2.61 c6d ced only apply to the extent that the dividends received deduction under this section and s. 71.26 c3d cjd or 71.45 c2d cad 8., Stats., do not apply.

Note: This section interprets ss. 71.22 c4d, 71.255 c4d cfd, 71.26 c2d and c3d cjd, 71.42 c2d and 71.45 c2d cad 8., Stats.

History: 1-2-56; am. Register, September, 1964, No. 105, eff. 10-1-64; am. c1d, Register, March, 1966, No. 123, eff. 4-1-66; am. Register, February, 1975, No. 230, eff. 3-1-75; cr. c5d, Register, July, 1978, No. 271, eff. 8-1-78; r. and recr. Register, June, 1990, No. 414, eff. 7-1-90; r. and recr. Register, December, 1995, No. 480, eff. 1-1-96; CR 10-095; cr. c6d Register November 2010 No. 659, eff. 12-1-10.

Tax 3.04 Subtraction for military pay received by members of a reserve component of the armed forces. c1d

PURPOSE. This section limits the application of the phrase Xcalled ... into special state service authorized by the federal department of defense under 32 USC 502 cfd, that is paid to the person for a period of time during which the person is on active dutyY as used in s. 71.05 c6d cbd 34., Stats., as created by 2003 Wis. Act 183.

c2d LIMITATION ON SUBTRACTION. A person who is a member of a reserve component of the U.S. armed forces, who is serving on active duty or full-time duty in the active guard reserve program under 32 USC 502 cfd, does not qualify for the subtraction.

History: Emerg. cr. eff. 9-17-04; CR 04-116; cr. Register March 2005 No. 591, eff. 4-1-05.

Tax 3.05 Job creation deduction. c1d PURPOSE. The purpose of this section is to clarify certain terms as they apply to the job creation deduction under ss. 71.05 c6d cbd 47m., 71.26 c1d chd, and 71.45 c1d ccd, Stats.; define Xemployee,Y Xfull-time equivalent employee,Y and Xgross receiptsY; prescribe the methods by which the average employee count is computed for purposes of determining the amount of the deduction; and clarify how the deduction applies to partnerships, limited liability companies, tax-option corporations, and professional employer organizations.

c2d DEFINITIONS. In this section and in ss. 71.05 c6d cbd 47m., 71.26 c1d chd, and 71.45 c1d ccd, Stats.:

cad XCommonly controlled groupY has the meaning given in s. 71.255 c1d ccd, Stats.

cbd XEmployeeY has the meaning given in section 3121 cdd of the Internal Revenue Code.

ccd XFull-time equivalent employeeY means an employee who is a resident of this state, is employed in a regular, nonseasonal job, and who, as a condition of employment, is required to work at least 2,080 hours per year, including paid leave and holidays.

cdd XGross receiptsY means gross sales, gross premiums earned, gross dividends, gross interest income, gross rents, gross royalties, the gross sales price from the disposition of capital assets and business assets, gross income from pass-through entities, and all other receipts that are included in gross income, other than life insurance income, before apportionment for Wisconsin franchise or income tax purposes.

ced XPersonY has the meaning given in ss. 71.01 c9d, 71.22 c9d, and 71.42 c4d, Stats.

cfd XRelated entityY has the meaning given in ss. 71.01 c9amd, 71.22 c9amd, and 71.42 c4amd, Stats.

cgd XTaxable yearY has the meaning given in ss. 71.01 c12d, 71.22 c10d, and 71.42 c5d, Stats.

c3d AMOUNT OF DEDUCTION. Sections 71.05 c6d cbd 47m., 71.26 c1d chd, and 71.45 c1d ccd, Stats., provide for an income and franchise tax deduction, prior to January 1, 2015, in an amount equal to the increase in the number of full-time equivalent employees employed by the taxpayer in this state during the taxable year, multiplied by \$4,000 for a business with gross receipts of no greater than \$5,000,000 in the taxable year or \$2,000 for a business with gross receipts greater than \$5,000,000 in the taxable year.

c4d AVERAGE EMPLOYEE COUNT. The average employee count for purposes of determining the increase in the number of full-time equivalent employees employed by the taxpayer in this state for a taxable year shall be computed using one of the following methods:

cad 1. Except as provided in subd. 2., for a taxable year during which the taxpayer is required, under ch. 108, Stats., to file quarterly unemployment insurance wage reports with the department of workforce development, the average employee count shall be computed using the average number of full-time equivalent employees employed by the taxpayer in this state from the claimant[s] quarterly wage reports required to be filed during the taxable year. An amount computed under this subdivision shall be rounded to the nearest whole number.

Example: For Taxpayer A[s] taxable year beginning August 1, 2011 and ending July 31, 2012, Taxpayer A uses the number of full-time equivalent cFTED employees employed in Wisconsin from the quarterly wage reports required to be filed October 31, 2011, January 31, 2012, April 30, 2012, and July 31, 2012 to compute the average employee count. The information from the reports filed is as follows:

Report Due Date	Total Employees Reported	FTE Employees
October 31, 2011	43	22

January 31, 2012	58	36
April 30, 2012	57	39
July 31, 2012	71	63
TOTAL	229	160

The average employee count in this example is 40, the sum of the full-time equivalent employees employed in Wisconsin reported c160d divided by the number of reports filed c4d.

2. If only one quarterly wage report is required to be filed during the taxable year, the average employee count shall be the number of full-time equivalent employees employed by the taxpayer in this state from that report.

3. For purposes of computing the average employee count under this paragraph, the number of full-time equivalent employees employed in this state does not include any employee who worked for a related person or related entity of the taxpayer or member of the same commonly controlled group as the taxpayer at any time during the 12 months prior to the due date of the quarterly wage report from which the number is derived.

cbd 1. Except as provided in subds. 2. and 3., for a taxable year during which a taxpayer is not required under ch. 108, Stats., to file quarterly unemployment insurance wage reports with the department of workforce development, the average employee count shall be computed using the average number of full-time equivalent employees employed by the taxpayer in this state on January 31, April 30, July 31, and October 31 within the taxable year. A January 31, April 30, July 31, or October 31 that does not occur within the taxable year is disregarded for purposes of the computation under this subdivision. An amount computed under this subdivision shall be rounded to the nearest whole number.

Example 1d For Taxpayer B[s taxable year beginning July 1, 2011, and ending June 30, 2012, the number of full-time equivalent employees employed by Taxpayer B in this state on July 31, 2011, October 31, 2011, January 31, 2012, and April 30, 2012, are used to compute the average employee count.

Example 2d To compute the average employee count for Taxpayer C[s short-period taxable year beginning March 15, 2011, and ending December 31, 2011, Taxpayer C divides the sum of the number of full-time equivalent employees employed by Taxpayer C in this state on April 30, 2011, July 31, 2011, and October 31, 2011, by three.

2. If only one of the dates, January 31, April 30, July 31, and October 31 occur within a taxable year, the average employee count shall be the number of full-time equivalent employees employed by the taxpayer in this state on that date.

3. If none of the dates January 31, April 30, July 31, or October 31, occurs within a taxable year, the average employee count shall be the number of full-time equivalent employees employed by the taxpayer in this state on the last day of the taxable year.

4. For purposes of computing the average employee count under this paragraph, the number of full-time equivalent employees employed in this state does not include any employee who worked for a related person or related entity of the taxpayer or member of the same commonly controlled group as the taxpayer at any time during the 12 months prior to the date on which the number is derived.

c5d PARTNERSHIPS, LIMITED LIABILITY COMPANIES, AND TAX-OPTION CORPORATIONS. Partnerships, limited liability companies, and tax-option corporations may not claim the job creation deduction under ss. 71.05 c6d cbd 47m., 71.26 c1d chd, or 71.45 c1d ccd, Stats., but the eligibility for, and the amount of, the deduction shall be based on the increase in the number of full-time equivalent employees employed by the partnership, limited liability company, or tax-option corporation in this state and the gross receipts of the partnership, limited liability company, or tax-option corporation. A partnership, limited liability company, or tax-option corporation shall compute the amount of deduction that each of its partners, members, or shareholders may claim and shall provide that information to each of them.

Example: Partnership C has two equal partners, Individual D and Individual E.

Individual D and Individual E are both Wisconsin residents. For its 2011 taxable year, Partnership C computes \$450,000 of ordinary business income for federal income tax purposes and a job creation deduction of \$40,000. Partnership C reports the following amounts to both Individual D and Individual E:

	Federal Amount	Adjustment	Wisconsin Amount
Ordinary business income	225,000	c20,000d	205,000

c6d PROFESSIONAL EMPLOYER ORGANIZATIONS. The provisions of s. 202.24 c4d cbd, Stats., apply to this section and ss. 71.05 c6d cbd 47m., 71.26 c1d chd, and 71.45 c1d ccd, Stats.

Example: Company F, a professional employer organization, hires Employee G to perform services in Wisconsin for Taxpayer H, a client of Company F. For purposes of determining the job creation deduction, Employee G is considered to be an employee solely of Taxpayer H.

History: EmR1105: emerg. cr. eff. 4-7-11; CR 11-024: cr. Register November 2011 No. 671, eff. 12-1-11; CR 14-005: am. c6d Register August 2014 No. 704, eff. 9-1-14; CR 17-019: am. c3d, Register June 2018 No. 750 eff. 7-1-18.

Tax 3.085 Retirement plan distributions. c1d NON-RESIDENTS. Employee annuity, pension, profit-sharing or stock bonus plan distributions, including self-employed retirement plan distributions, and distributions from qualified deferred compensation plans under ss. 401 ckd, 403 cbd and 457 of the internal revenue code 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.

c2d RESIDENTS. Employee annuity, pension, profit-sharing or stock bonus plan distributions, including self-employed retirement plan distributions, and distributions from qualified deferred compensation plans under ss. 401 ckd, 403 cbd and 457 of the internal revenue code 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.

Note: This section interprets s. 71.04 c1d cad, Stats.

History: Cr. Register, March, 1978, No. 267, eff. 4-1-78; am. Register, June, 1990, No. 414, eff. 7-1-90.

Tax 3.095 Income tax status of interest and dividends received from government and other securities by individuals and fiduciaries. c1d PURPOSE. This section lists federal, state, municipal and other government securities, and certain nongovernment securities, and specifies whether interest and dividends payable on those securities are exempt from or subject to the Wisconsin income tax on individuals and fiduciaries. The lists are not all-inclusive.

Note: Information regarding the income tax status of interest and dividends received from securities not listed in this section may be obtained by writing to Wisconsin Department of Revenue, Technical Services Staff, P.O. Box 8933, Madison, WI 53708-8933.

c2d DEFINITIONS. In this section:

cad XCHAPY means XCommunity Housing Alternatives Program.Y

cbd XFederal securitiesY means only securities which are direct and primary obligations of the United States and securities the interest on 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.

ccd XPublic housing agencyY 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 USC 1437a cbd c6d.

cdd XWHEDAY means XWisconsin Housing and Economic Development Authority.Y

ced XWHEFAY means XWisconsin Health and Educational Facilities Authority.Y

c3d GENERAL. cad Under s. 71.05 c6d cad 1., Stats., interest income which is subject to the Wisconsin income tax on individuals and fiduciaries, but which is not included in federal adjusted gross income, shall be added to federal adjusted gross income in computing Wisconsin taxable income.

Note: Section 71.05 c1d cad 1., 1985 Stats., was amended by 1987 Wis. Act 27, 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 enactment of 1987 Wis. Act 27, the addition applied only to interest excluded from federal adjusted gross income solely by s. 103 of the internal revenue code. Section 71.05 c1d cad 1., 1985 Stats., was renumbered s. 71.05 c6d cad 1., Stats., by 1987 Wis. Act 312, effective January 1, 1989.

cbd Under s. 71.05 c6d cbd 1., Stats., interest and dividend income which is included in federal adjusted gross income but which is by federal law exempt from state income taxation, shall be subtracted from federal adjusted gross income in computing Wisconsin taxable income.

c4d EXEMPT SECURITIES. Interest and dividends payable on the following securities shall be exempt from the Wisconsin income tax on individuals and fiduciaries:

cad *State, municipal and other government securities exempt from Wisconsin income tax.* 1. 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 s. 103 of the internal revenue code.

2. Higher education bonds issued by the state of Wisconsin, s. 71.05 c6d cad 1., Stats.

3. 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 income taxation for a reason other than or in addition to s. 103 of the internal revenue code.

4. Public housing authority bonds issued by municipalities located in Wisconsin, s. 66.1201 c14d cad, Stats.

5. Redevelopment authority bonds issued by municipalities located in Wisconsin, s. 66.1333 c5d cad 4. c., Stats.

6. Stripped general obligation bond certificates attributable to certain 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 under section 1286 of the internal revenue code and D.C. Code Ann. 47-332.

Note: Stripped general obligation bond certificates meeting the criteria of subd. 6. include Stripped Tax-Exempt Participations, or ZSTEPS.[]

7. 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.

8. 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.

10. WHEDA bonds issued under s. 234.65, Stats., to fund an economic development loan to finance construction, renovation or development of property that would be exempt under s. 70.11 c36d, Stats.

11. Wisconsin Housing Finance Authority bonds, 42 USC 1437i cbd.

12. WHEDA bonds or notes issued under s. 234.08 or 234.61, Stats., on or after January 1, 2004, if the bonds or notes are issued to fund multifamily affordable housing projects or elderly housing projects.

13. Bonds or notes issued by a local exposition district created under subch. II of ch. 229, Stats.

14. Bonds or notes issued by a local professional baseball park district created under subch. III of ch. 229, Stats.

15. Bonds or notes issued by a local professional football stadium district created under subch. IV of ch. 229, Stats.

16. Bonds or notes issued by a local cultural arts district created under subch. V of ch. 229, Stats.

17. Bonds or notes issued by the Wisconsin Aerospace Authority.

18. Wisconsin Health and Educational Facilities Authority bonds or notes issued under s. 231.03 c6d, Stats., on or after October 27, 2007, if the proceeds from the bonds or notes that are issued are used by a health facility, as defined in s. 231.01 c5d, Stats., to fund the acquisition of information technology hardware or software.

19. Bonds or notes issued by a commission created under s. 66.0304, Stats., if any of the following applies:

a. The bonds or notes are used to fund multifamily affordable housing projects or elderly housing projects in this state, and WHEDA has the authority to issue its bonds or notes for the project being funded.

b. The bonds or notes are used by a health facility, as defined in s. 231.01 c5d, Stats., to fund the acquisition of information technology hardware or software, in this state, and the Wisconsin Health and Educational Facilities Authority has the authority to issue its bonds or notes for the project being funded.

c. The bonds or notes are issued to fund a redevelopment project in this state or a housing project in this state, and the authority exists for bonds or notes to be issued by an entity described under s. 66.1201, 66.1333, or 66.1335, Stats.

20. WHEDA bonds or notes, if the bonds or notes are issued to provide loans to a public affairs network under s. 234.75 c4d, Stats.

21. WHEFA bonds or notes, if the bonds or notes are issued for the benefit of a person who is eligible to receive the proceeds of bonds or notes from another entity for the same purpose for which the bonds or notes are issued and the interest income received from the other bonds or notes is exempt from taxation under subch. I of ch. 71, Stats.

Note: Under par. cad, interest and dividends payable on certain securities issued on or before January 28, 1987, is exempt from Wisconsin income tax. This is because prior to enactment of 1987 Wis. Act 27, which amended s. 71.05 c1d cad 1., 1985 Stats., effective with securities issued after January 28, 1987, no modification was provided to add to federal adjusted gross income interest and dividends which were excludable from federal adjusted gross income for any reason other than or in addition to s. 103 of the internal revenue code. Section 71.05 c1d cad 1., 1985 Stats., was renumbered s. 71.05 c6d cad 1., Stats., by 1987 Wis. Act 312, effective January 1, 1989.

22. Bonds or notes issued by a sponsoring municipality to assist a local exposition district created under subch. II of ch. 229, Stats.

cbd *Federal securities exempt from Wisconsin income tax.* 1. Armed Services Housing Mortgage Insurance debentures, 12 USC 1748b cfd.

2. Bank for Cooperative debentures, 12 USC 2134.

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

4. Commodity Credit Corporation bonds, 15 USC 713a-5.

5. Commonwealth of Puerto Rico public improvement bonds, 48 USC 745.

6. Farm Credit System Financial Assistance Corporation notes, bonds and debentures, 12 USC 2278b-10 cbd.

7. Federal Deposit Insurance Corporation bonds, [12 USC 1825](#).
 8. Federal Farm Credit Banks Consolidated Systemwide Securities, [12 USC 2023](#).
 9. Federal Home Loan Bank bonds, debentures and notes, [12 USC 1433](#).
 10. Federal Housing Authority debentures, [12 USC 1710 cdd](#) and [1747g cgd](#).
 11. Federal Intermediate Credit Bank debentures, [12 USC 2023](#).
 12. Federal Land Bank Association bonds, notes and debentures, [12 USC 2098](#).
 13. Federal Land Bank bonds, [12 USC 2055](#).
 14. Federal Reserve Bank dividends, [12 USC 531](#).
 15. Federal Savings and Loan Insurance Corporation bonds, [12 USC 1725 ccd](#).
 16. Financial Assistance Corporation bonds, notes and debentures, [12 USC 2278b-10 cbd](#).
 17. Financing Corporation obligations, [12 USC 1441](#).
 18. General Insurance Fund debentures issued to acquire housing projects, [12 USC 1747g cgd](#).
 - 18e. General Insurance Fund debentures issued under the National Defense Housing Insurance, [12 USC 1750c cdd](#).
 - 18m. General Insurance Fund debentures issued under the Neighborhood Conservation Housing Insurance, [12 USC 1715k chd c7d](#).
 - 18s. General Insurance Fund debentures issued under the Rental Housing Insurance, [12 USC 1713 cid](#).
 19. General Insurance Fund debentures issued under the War Housing Insurance Law, [12 USC 1739 cdd](#).
 20. General Services Administration Public Building Trust Participation certificates, [31 USC 3124](#).
 21. Guam bonds, [48 USC 1423a](#).
 - 21g. National Credit Union Central Liquidity Facility, [12 USC 1795k cbd](#).
 - 21r. Northern Mariana Islands, [48 USC 1801](#) and s. 607 cad of the Covenant to Establish a Commonwealth of the Northern Mariana Islands.
 22. Industrial Development bonds of East Samoa, [48 USC 1670](#).
 23. Panama Canal Zone bonds, [31 USC 743-745](#).
 24. Production Credit Association obligations, [12 USC 2077](#).
 25. Proprietary zero-coupon certificates, [31 USC 3124](#).
- Note:** Proprietary zero-coupon certificates include CATS, TIGRs, Cougars, ETRs, Lions, STARS, Zebras, etc.
26. Puerto Rico Aqueduct and Sewer Authority revenue bonds, [48 USC 745](#).
 27. Puerto Rico Electric Power Authority electric revenue bonds, [48 USC 745](#).
 28. Puerto Rico Electric Power Authority power revenue bonds, [48 USC 745](#).
 29. Puerto Rico Highway Authority revenue bonds, [48 USC 745](#).
 30. Puerto Rico Industrial Development Company bonds, [48 USC 745](#).
 31. Puerto Rico Municipal Finance Agency 1974 Series A bonds, [48 USC 745](#).
 32. Puerto Rico Ports Authority revenue bonds, [48 USC 745](#).
 33. Puerto Rico Public Buildings Authority public education and health facility bonds, [48 USC 745](#).
 34. Puerto Rico Public Buildings Authority revenue bonds, [48 USC 745](#).
 35. Puerto Rico Telephone Authority revenue bonds, [48 USC 745](#).
 36. Puerto Rico Water Resource Authority Series B debentures, [48 USC 745](#).
 37. Resolution Funding Corporation bonds, [12 USC 1441b cfd c7d](#).
 38. Student Loan Marketing Association obligations, [20 USC 1087-2 cLd](#).
 39. Tennessee Valley Authority bonds, [16 USC 831n-4 cdd](#).
 40. Territory of Hawaii bonds.
 41. Territory of Puerto Rico bonds, [48 USC 745](#).
 42. United States Postal Service bonds, [39 USC 2005](#).
 43. United States savings bonds, [31 USC 3124](#).
 44. United States Treasury bills and notes, [31 USC 3124](#).
 45. University of Puerto Rico university system revenue bonds, [48 USC 745](#).
 46. Virgin Islands general obligation bonds, [48 USC 1574 cbd ciid cAd](#).
 47. Virgin Islands Public Improvement bonds, [48 USC 1574 cbd cid](#).
- c5d TAXABLE SECURITIES.** Interest and dividends payable on the following securities shall be subject to the Wisconsin income tax on individuals and fiduciaries:
- cad *Taxable state and municipal government securities.*
 1. District of Columbia Development Land Agency bonds, [42 USC 1452](#).
 2. District of Columbia general obligation bonds issued after January 28, 1987, D.C. Code 47-33.
 3. Municipal bonds.
 4. 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 income taxation solely because of section 103 of the internal revenue code.
 5. Robert F. Kennedy Stadium bonds, D.C. Code 2-1720 et seq.
 6. Transit bonds of the Washington Metropolitan Area Transit Authority.
 7. Wisconsin Health Education Assistance Loan revenue obligation bonds, s. 39.374, Stats.
 8. WHEDA bonds issued after January 28, 1987, and all business development revenue bonds, economic development revenue bonds and CHAP housing revenue bonds issued by WHEDA, regardless of when issued, unless specifically exempt by law, ch. 234, Stats.
 - cbd *Other taxable securities.*
 1. Asian Development Bank bonds, [22 USC 285h](#).
 2. College Construction Loan Insurance Association obligations, [20 USC 1132](#).
 3. Environmental Financing Authority obligations, [33 USC 1281](#).
 4. Export-Import Bank of the United States debentures, [12 USC 635](#).
 5. Farmer[s] Home Administration insured notes, [7 USC 1928 and 1929](#).
 6. Federal Assets Financing Trust participation certificates, [12 USC 1717 ccd](#).
 7. Federal Financing Bank bonds, [12 USC 2288](#).

8. Federal Home Loan Bank dividends, [12 USC 1426](#) and [1436](#).
 9. Federal Home Loan Mortgage Corporation obligations, [12 USC 1455](#).
 10. Federal National Mortgage Association certificates, [12 USC 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.
11. Federal National Mortgage Association dividends, [12 USC 1719](#).
 12. Government National Mortgage Association, or Ginnie Mae, bonds, [12 USC 1721](#).
 13. HUD{New Communities Program obligations, [12 USC 1701g-5a](#).
 14. Insured Merchant Marine bonds, [46 USC 1273](#).
 15. Inter-American Development Bank securities, [22 USC 283h](#).
 16. Interest paid on deposits in any federal bank or agency.
 17. International Bank for Reconstruction and Development bonds, also known as World Bank bonds, [22 USC 286k-1](#).
 - 17m. National Consumer Cooperative Bank, [12 USC 3017 ccd](#).
 18. Rural Telephone debentures, [7 USC 947 cad](#).
 19. Small Business Administration notes, [15 USC 633](#).
 20. Small Business Investment Company debentures, [15 USC 683](#) and [687](#).
 21. Tennessee Valley Authority bonds, [16 USC 831n-3](#).
 22. Virgin Islands Housing Authority bonds issued after January 28, 1987, [48 USC 1408a](#).
 23. World Bank bonds, also known as International Bank for Reconstruction and Development bonds, [22 USC 286k-1](#).

Note: This section interprets s. [71.05 c6d cad 1](#), and [cbd 1](#), Stats.

History: Cr. [Register, August, 1976, No. 248](#), eff. 9-1-76; emerg. cr. c1d cgd to cid, am. c2d cintro.d, r. c2d cbd, chd and cjd, eff. 7-31-87; r. and recr. [Register, April, 1988, No. 388](#), eff. 5-1-88; emerg. am. c3d cintro.d and ccd, cr. c3d cgd, r. and recr. c4d cbd, eff. 1-1-89; am. c2d cintro.d, c3d cintro.d, ccd, cfd, c4d cintro.d and cbd, cr. c4d ccd to cfd, [Register, August, 1989, No. 404](#), eff. 9-28-89; cr. c1d cad, cbd, cfd, cgd, cid, cqd, crd and cvd, c2d cad, cdd, cfd, cgd, cmd, cod, cpd to cud, cwd, czhd, czqd and czrd, c4d cbd and ced; renum. c1d cad to cmd, c2d cad to czbd, c4d cad, cbd, cdd and ced to be c1d ccd to ced, chd, cjd to cpd, csd to cud, c2d cbd, ccd, ced, chd to cld, cmd, cvd, cxd to czdd, czfd, czed, czgd, czid to czpd, c4d cdd, chd, cgd and cad and am. c1d cpd, [Register, June, 1991, No. 426](#), eff. 7-1-91; r. and recr. [Register, January, 1994, No. 457](#), eff. 2-1-94; corrections in c4d cad 4. and 5. made under s. 13.93 c2md cbd 7., Stats., [Register October 2002 No. 562; CR 12-011](#): r. c4d cad 9., cr. c4d cad 12. to 20. [Register July 2012 No. 679](#), eff. 8-1-12; [CR 14-005](#): cr. c2d ced, c4d cad 21. [Register August 2014 No. 704](#), eff. 9-1-14; [CR 17-019](#): cr. c4d cad 22., [Register June 2018 No. 750](#) eff. 7-1-18; [CR 19-096](#): am. c4d cad cttled, cbd cttled, 8., 11., 12., 16, cr. c4d cbd 18e., 18m., 18s., 21g., 21r., am. c4d cbd 24., 38., c5d cbd 1., 12., 13., 15., 17., cr. c5d cbd 17m., am. c5d cbd 22., 23. [Register April 2020 No. 772](#), eff. 5-1-20.

Tax 3.096 Interest paid on money borrowed to purchase exempt government securities. c1d Any amount

of distributable and nondistributable 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 fiduciary income tax return.

c2d Interest expense is a Xrelated expenseY if it is incurred to purchase securities producing exempt interest or dividend income and if it is deducted in computing Wisconsin taxable income.

c3d Interest expense is not a Xrelated expenseY if it is incurred to purchase securities producing exempt interest or dividend income but is not deducted in computing Wisconsin taxable income cfor example, because the taxpayer elects the standard rather than to itemize deductionsd.

Examples: 1d 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>
2d 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>
3d U.S. bond interest exempt from Wisconsin income tax.	\$400
Interest paid to acquire the exempt securities but not claimed as an itemized deduction	<u>600</u>
Subtraction modification	<u>\$400</u>

History: Cr. [Register, January, 1977, No. 253](#), eff. 2-1-77; am. c1d, [Register, June, 1990, No. 414](#), eff. 7-1-90.

Tax 3.098 Railroad retirement supplemental annuities. Railroad retirement supplemental annuities paid under [45 USC 231m](#) are exempt from the Wisconsin taxable income of their recipients.

Note: 1d The Railroad Retirement Act of 1974 as amended by P.L. 98-76 c45 USC s. 231md, effective August 12, 1983, provides that:

Xcad Except as provided in subsection cbd 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. . . .

cbd c1d This section shall not operate to exclude the amount of any supplemental annuity paid to an individual under section c2d cbd of this Act [45 USCS 231a cbd] from income taxable pursuant to Federal income tax provisions of the Internal Revenue Code of 1954 [26 USCS 1 et seq.]Y

2d 45 USCS. 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.

Note: This section interprets s. [71.05 c6d cbd 3](#), Stats.

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