5. The preservation or rehabilitation work must be completed within 2 years after the date the physical work of construction or destruction in preparation for construction begins. However, for any preservation or rehabilitation initially planned for completion in phases, the work must be completed within 5 years.

6. The expenditures for preservation or rehabilitation must exceed $10,000.

7. The costs may not be incurred to acquire a building or interest in a building or to enlarge an existing building.

8. The costs must not be incurred before the Historical Society approves the proposed plan.

Facts and Question: Individual A owns and occupies a personal residence in Wisconsin which is listed on the National Register of Historic Places. The home's heating, plumbing, and electrical systems need to be replaced. In addition, the house needs a new roof, siding, and windows. The total cost of the rehabilitation work will exceed $40,000.

May Individual A separate the rehabilitation work into 2 or more preservation or rehabilitation projects in order to qualify for tax credits of up to $10,000 for each project?

Answer: Yes. Individual A may separate the rehabilitation work into 2 or more preservation or rehabilitation projects. The separate preservation or rehabilitation projects may run consecutively or concurrently. A tax credit would be available for 25% of the qualifying preservation or rehabilitation costs, but not more than $10,000, for each project.

For example, if the interior mechanical work and the exterior work are separated into 2 projects, and the qualifying preservation or rehabilitation costs for each project are $40,000, Individual A would be eligible for $20,000 of income tax credits ($10,000 for each project). □

CORPORATION FRANCHISE AND INCOME TAXES

5 Dividends Received Deduction for Corporations

Statutes: Section 71.26(3)(j), Wis. Stats. (1991-92), as amended by 1993 Wisconsin Act 16

Note: For more information, see the tax release titled "Deductible Dividends Received From Subsidiaries" in *Wisconsin Tax Bulletin* 58 (October 1988), page 16.

Background: For taxable years beginning on or after January 1, 1993, a corporation may deduct dividends received from a corporation with respect to its common stock if the corporation receiving the dividends owns, directly or indirectly, during the entire taxable year at least 70% of the total combined voting stock of the payor corporation. To qualify for the deduction for taxable years beginning before January 1, 1993, the corporation was required to own, directly or indirectly, 80% or more of the total combined voting stock of the payor corporation.

Facts and Question: Corporation P does business in Wisconsin and files Wisconsin franchise tax returns on a calendar year basis. Corporation P owned 100% of the total combined voting stock in both Subsidiary S1 and Subsidiary S2 until July 1, 1993. On that date Subsidiaries S1 and S2 were merged into Corporation P. Thus, Corporation P owned them as divisions during the second half of the 1993 taxable year.

On March 15, 1993, and June 15, 1993, Subsidiary S1 paid Corporation P common stock dividends of $100,000 and $125,000, respectively. On each of these dates, Subsidiary S2 paid Corporation P common stock dividends of $200,000.

Are the $225,000 of dividends received from Subsidiary S1 and $400,000 of dividends received from Subsidiary S2 deductible by Corporation P in computing its 1993 Wisconsin net income?

Answer: No. Since Corporation P did not own, directly or indirectly, **during the entire taxable year** at least 70% of the total combined voting stock in Subsidiary S1 and at least 70% of the total combined voting stock in Subsidiary S2, the $225,000 of dividends received from Subsidiary S1 and $400,000 of dividends received from Subsidiary S2 are not deductible in computing its 1993 Wisconsin net income. □

6 Wisconsin Treatment of Section 179 Expense Deduction

Statutes: Sections 71.22(4) and (4m), 71.26(2) and (3), 71.34(1) and (1g), 71.42(2), 71.45(2), and 71.49(2), Wis. Stats. (1991-92), and as affected by 1993 Wisconsin Acts 16 and 437

Background: Under Internal Revenue Code (IRC) section 179, a corporation may elect to deduct as an expense, rather than depreciate, all or a portion of the cost of "section 179 property" that is placed in service during the taxable year. Section 179 property is new or used tangible personal property that is acquired by purchase for use in the active conduct of the taxpayer's trade or business. The section 179 expense deduction is subject to a dollar limitation and a taxable income limitation.

For taxable years beginning after December 31, 1992, the maximum section 179 expense deduction for most taxpayers is $17,500. The deduction was limited to $10,000 for taxable years beginning before January 1, 1993. The dollar limitation is reduced by the amount by which the cost of section 179 property placed in service during the taxable year exceeds $200,000. Members of a controlled group of corporations are treated as one taxpayer in applying the dollar limitation. A controlled group of corporations has the meaning in IRC sec. 1563(a), except that a more-than-50% (instead of an at-least-80%) control test applies. IRC sec. 179(d)(6). The dollar limitation amount can be allocated to the group members by the common parent corporation when the parent files a consolidated federal return. If separate federal returns are filed, the amount must be allocated according to an agreement made by the members. However, the amount of expense allocated to any group member cannot exceed the cost of the qualifying property actually purchased by the member and placed in service. Treas. Reg. §1.179-2(b)(7).

The section 179 expense deduction may not exceed the corporation's taxable income derived from the active conduct of a trade or business for the taxable year. The portion of the cost that may not be expensed for a taxable year because it exceeds the taxable income limitation may be carried forward for an unlimited number of years.

The election to claim the section 179 expense deduction must be made on the corporation's original federal income tax return filed for the taxable year in which the property was placed in service or on an amended return filed within the time prescribed by law, including extensions, for filing the return for that taxable year. Once made, the election and the selection of the property to be expensed may not be revoked without the consent of the Internal Revenue Service. Treas. Reg. §1.179-5.

Question 1: Does the increase in the section 179 expense deduction from $10,000 to $17,500 apply for Wisconsin franchise and income tax purposes? If so, when is it effective?

Answer 1: Yes. The increase in the section 179 expense deduction from $10,000 to $17,500 applies for Wisconsin purposes. It is effective at the same time as for federal purposes, applying to property placed in service in taxable years beginning after December 31, 1992.

The Wisconsin net income of a corporation is computed under the Internal Revenue Code as defined for Wisconsin purposes, with certain modifications. For taxable years beginning after December 31, 1992, and before January 1, 1994, the Internal Revenue Code means the Code as amended to December 31, 1992, except that most changes made by the Omnibus Budget Reconciliation Act of 1993 (Public Law 103-66) apply for Wisconsin purposes at the same time as for federal purposes. For taxable years beginning after December 31, 1993, the Code as amended to December 31, 1993, applies. Sections 71.22(4)(h) and (i) and (4m)(f) and (g), 71.26(2)(b)8 and 9, 71.34(1g)(h) and (i), and 71.42(2)(g) and (h), Wis. Stats., as affected by 1993 Wisconsin Acts 16 and 437.

Question 2: Does the dollar limitation of controlled groups of corporations in IRC sec. 179(d)(6) apply for Wisconsin franchise and income tax purposes?

Answer 2: Yes. Members of a controlled group of corporations are treated as one taxpayer in applying the dollar limitation for Wisconsin purposes. The limitation applies even though Wisconsin does not allow the filing of consolidated returns. The dollar limitation for members of controlled groups applies since it is contained in IRC sec. 179 and this Code section is not modified for Wisconsin purposes.

For Wisconsin, the section 179 expense deduction must be allocated according to an agreement made by the members of the controlled group. However, the amount of expense allocated to any group member cannot exceed the cost of the qualifying property actually purchased by the member and placed in service.

Question 3: Must corporations claim the same section 179 expense deduction for Wisconsin purposes as for federal purposes?

Answer 3: Corporations, except insurance companies, are not required to claim the same section 179 expense deduction for federal and Wisconsin purposes. A corporation which takes a federal section 179 expense deduction may elect not to claim it, or to claim a different amount to the extent allowable under IRC sec. 179, for Wisconsin purposes. A corporation may elect to claim a section 179 expense deduction for Wisconsin but not for federal purposes. A controlled group of corporations may have a different allocation of the section 179 expense deduction among its members for federal and Wisconsin purposes.

Insurance companies, however, must take the same section 179 expense deduction for Wisconsin purposes as for federal purposes. Members of a controlled group of corporations must allocate the deduction in the same manner as federally. For insurance companies, elections authorized by

and made in accordance with the Internal Revenue Code, except an election to file consolidated returns or to claim a credit against federal tax liability rather than a deduction from income, are deemed elections for Wisconsin purposes. Sec. 71.49(2), Wis. Stats. (1991-92).

Question 4: How does a corporation, other than an insurance company, elect a different section 179 expense deduction for Wisconsin purposes?

Answer 4: A corporation elects a different Wisconsin section 179 expense deduction by completing a federal Form 4562, Depreciation and Amortization, in accordance with the Wisconsin election. Form 4562 must be attached to the corporation's original Wisconsin franchise or income tax return or to an amended return filed no later than the due date, including extensions, for its return for the year the property is placed in service. Once made, the election cannot be revoked without the permission of the Department of Revenue.

Question 5: If a corporation claimed a $17,500 section 179 expense deduction on its 1993 federal return but only $10,000 on its 1993 Wisconsin franchise or income tax return because the Wisconsin law adopting the increase to $17,500 (1993 Wisconsin Act 437, published May 9, 1994) had not been enacted by the due date of its return, may the corporation file an amended return to increase its section 179 expense deduction?

Answer 5: Yes. A corporation, including an insurance company, may file an amended 1993 Wisconsin return to increase its section 179 expense deduction. An insurance company must claim the same section 179 expense deduction for Wisconsin purposes as allowed on its 1993 federal return. The amended return is due within 4 years of the original due date of the 1993 Wisconsin return.□

INDIVIDUAL INCOME AND CORPORATION FRANCHISE AND INCOME TAXES

7 Amortization of Intangible Assets for Wisconsin Purposes

Statutes: Sections 71.01(6) and (7r), 71.22(4) and (4m), 71.26(2)(b) and (3)(y), 71.34(1g), 71.365(1m), 71.42(2), and 71.45(2)(a)13, Wis. Stats. (1991-92), and as affected by 1993 Wisconsin Acts 16 and 437

Background: Internal Revenue Code (IRC) section 197, as added by the Omnibus Budget Reconciliation Act of 1993 (Public Law 103-66, signed August 10, 1993), allows taxpayers to claim amortization deductions with respect to a broad range of intangible assets called "amortizable section 197 intangibles." The deduction is calculated by amortizing the adjusted basis of an eligible section 197 intangible ratably over a 15-year period beginning with the month in which the intangible is acquired. No other depreciation or amortization deduction is permitted with respect to any section 197 intangible.

Section 197 intangibles include goodwill and going concern value; workforce in place; information base; know-how; customer-based intangibles; supplier-based intangibles; government licenses and permits; franchises, trademarks, and trade names; insurance policy expirations; and bank deposit base.

Assets acquired in connection with the acquisition of a business that are treated as section 197 intangibles include covenants not to compete; computer software; films, sound recordings, video tapes, and books; copyrights and patents; rights to receive tangible property or services; interests in patents and copyrights; mortgage servicing rights secured by residential real property; and contract rights good for less than 15 years or fixed in amount.

Self-created intangibles, such as goodwill created through advertising, are not amortizable under IRC section 197.

The federal treatment of section 197 intangibles applies for property acquired after August 10, 1993, or, at the taxpayer's option, to all section 197 intangibles acquired after July 25, 1991.

The Internal Revenue Service has issued temporary regulations (Treas. Reg. §1.197-1T, effective March 15, 1994) for making an election to apply IRC section 197 retroactively. The regulations provide that the retroactive election must be made by the due date, including extensions, for filing the taxpayer's federal income tax return for the taxable year that includes August 10, 1993. If the taxpayer's original federal income tax return was filed before April 14, 1994, the election may be made by amending that return no later than September 11, 1994. Once made, the election may be revoked only with the consent of the Internal Revenue Service.

Question: What is the Wisconsin treatment of intangible assets that qualify as "amortizable section 197 intangibles" for federal income tax purposes?

Answer: The Wisconsin treatment of amortizable section 197 intangibles depends on when the assets are acquired.

a. Acquisitions in taxable years beginning in 1994 or thereafter

Amortizable section 197 intangible assets acquired in taxable years beginning on or after January 1, 1994, must be amortized under IRC sec. 197 for Wisconsin purposes. Secs.

71.01(7r), 71.26(3)(y), 71.365(1m), and 71.45(2)(a)13, Wis. Stats. (1991-92), as affected by 1993 Wisconsin Act 437.

b. Acquisitions after August 10, 1993, in taxable years beginning before 1994

For Wisconsin purposes, amortizable section 197 intangible assets acquired after August 10, 1993, in taxable years beginning before January 1, 1994, are treated as follows:

- Individuals, fiduciaries, partnerships, C corporations (except as indicated below), tax-option (S) corporations, and insurance companies may elect to amortize their eligible section 197 intangibles under IRC sec. 197. For taxable years beginning in 1993, these taxpayers have the option of computing amortization under either the federal Internal Revenue Code in effect for the taxable year for which the return is filed or the Internal Revenue Code as amended to December 31, 1992. Similarly, for taxable years beginning in 1992, they may use either the amortization methods allowable for federal income tax purposes or the Internal Revenue Code as amended to December 31, 1991. Secs. 71.01(7r), 71.26(3)(y), 71.365(1m), and 71.45(2)(a)13, Wis. Stats. (1991-92), and as affected by 1993 Wisconsin Act 16.

- Exempt corporations, regulated investment companies, real estate investment trusts, and real estate mortgage investment conduits are required to amortize their eligible section 197 intangibles under IRC sec. 197, the same as for federal purposes. These taxpayers must compute their Wisconsin net income for taxable years beginning in 1993 under the December 31, 1992, Internal Revenue Code as amended by the Omnibus Budget Reconciliation Act of 1993. They must compute their Wisconsin net income for taxable years beginning in 1992 under the December 31, 1991, Internal Revenue Code as amended by certain federal laws enacted after 1991, including the Omnibus Budget Reconciliation Act of 1993. Secs. 71.22(4m)(f) and 71.26(2)(b)8, Wis. Stats., as affected by 1993 Wisconsin Acts 16 and 437.

c. Acquisitions after July 25, 1991, and before August 11, 1993

Taxpayers may retroactively elect to amortize their eligible section 197 intangibles acquired after July 25, 1991, and before August 11, 1993, for Wisconsin purposes as provided in IRC sec. 197. The federal rules in Treas. Reg. §1.197-1T for making the election also apply for Wisconsin purposes. Secs. 71.01(7r), 71.26(3)(y), 71.365(1m), and 71.45(2)(a)13, Wis. Stats. (1991-92), and secs. 71.22(4m)(d), (e), and (f) and 71.26(2)(b)6, 7, and 8, Wis. Stats., as affected by 1993 Wisconsin Acts 16 and 437.

The election must be made within the time prescribed by the federal regulations. It is made by attaching a copy of the federal election statement to the Wisconsin return filed.

A taxpayer may make different federal and Wisconsin elections with respect to eligible section 197 intangibles acquired after July 25, 1991, and before August 11, 1993. One who elects to apply the rules in IRC sec. 197 to intangibles acquired before August 11, 1993, for federal purposes is not required to make the same election for Wisconsin purposes. Alternatively, a taxpayer may elect to amortize such eligible section 197 intangibles under IRC sec. 197 for Wisconsin purposes but not for federal purposes. The requirements of Treas. Reg. §1.197-1T apply to taxpayers making the retroactive election only for Wisconsin purposes. A taxpayer who is making different elections for federal and Wisconsin purposes must attach an election statement to the Wisconsin return filed. □

SALES AND USE TAXES

Note: The following tax release interprets the Wisconsin sales and use tax law as it applies to the 5% state sales and use tax. The ½% county sales and use tax may also apply. For information on sales or purchases that are subject to the county sales and use tax, refer to the December 1993 issue of the *Sales and Use Tax Report*. A copy can be found in *Wisconsin Tax Bulletin* 85 (January 1994), pages 37 to 40.

8 Bottled Water

Statutes: Sections 77.54(20)(intro.) and (b) and 97.29(1)(i), Wis. Stats. (1991-92)

Wis. Adm. Code: Section Tax 11.51(2), December 1992 Register

Background: Section 77.54(20) (intro.), Wis. Stats. (1991-92), provides that gross receipts from the sale of food, food products, and beverages for human consumption are exempt from Wisconsin sales or use tax.

Section 77.54(20)(b)4, Wis. Stats. (1991-92), provides that food, food products, and beverages exempt from Wisconsin sales or use tax do not include soda water beverages as defined in sec. 97.29(1)(i), Wis. Stats.; bases, concentrates, and powders intended to be reconstituted by consumers to produce soft drinks; and fruit drinks and ades not defined as fruit juices in sec. 97.02(27), Wis. Stats. (1967-68).

Section 97.29(1)(i), Wis. Stats. (1991-92), defines "soda water beverage" as all beverages commonly known as soft drinks or soda water, whether carbonated or uncarbonated, sweetened, or flavored.

In a decision dated April 8, 1994, the Wisconsin Tax Appeals Commission held in the case of *Artesian Water Company, Inc. vs. Wisconsin Department of Revenue* that bottled artesian spring water was a beverage and, therefore, the sale of the bottled artesian spring water was exempt from Wisconsin sales or use tax under sec. 77.54(20)(intro.), Wis. Stats. (1991-92). The department filed a notice of nonacquiescence with respect to this decision dated May 31, 1994.

Question: Is the sale of bottled water exempt from Wisconsin sales or use tax?

Answer: The sale of bottled water for human consumption that is not carbonated and is not sweetened or flavored is exempt from Wisconsin sales or use tax. However, bottled water that is carbonated and/or sweetened or flavored is not exempt from Wisconsin sales or use tax because such water is a "soda water beverage" specifically excluded from exemption. (sec. 77.54(20)(intro.) and (b)4, Wis. Stats. (1991-92)).

The size of the container in which the bottled water is sold is not a factor in determining whether the sale of bottled water is exempt from Wisconsin sales or use tax.

Caution: The following examples of bottled water reflect products and their content as of May 31, 1994. If the contents of the products listed were to change, the tax treatment may also change.

Examples of bottled water which are not subject to Wisconsin sales or use tax include (this list is not all-inclusive):

- Artesian Wells Natural Spring Water
- Buffalo Don Distilled Water
- Century Spring Water
- Chippewa Nonsparkling Spring Water
- Crystal Geyser Natural Alpine Spring Water
- Culligan Natural Spring Water
- Evian Natural Spring Water
- Grayson Pure Mountain Water
- Klarbrunn Drinking Water
- LaCrosse Premium Water
- Longbring Pure & Natural Spring Water
- Naya Canadian Natural Spring Water
- Poland Spring Natural Spring Water
- Sedona Mountain Spring Water
- Springside Pure Artesian Drinking Water
- Thorspring Iceland Pure Spring Water
- Vivant Natural Spring Water

Examples of bottled water subject to Wisconsin sales or use tax include (this list is not all-inclusive):

- Aqua Vil Spring Water Beverage (carbonated)
- Canada Dry Sparkling Water (original and flavored)
- Canada Dry Tonic Water
- Canfield's Clear Sparkling Mineral Water
- Canfield's Seltzer Water
- Cascadia Sparkling Water With Juice
- Chippewa Sparkling Spring Water
- Clearly Canadian Sparkling Water Beverage
- Clearly Canadian Sparkling Water Refresher
- Clearly Tea Sparkling Water Refresher
- Everfresh Juice & Sparkling Mineral Water
- Gold Medal Sparkling Mineral Water
- Hansens Natural Soda
- Klarbrunn Sparkling Water (natural and flavored)
- Koala Sparkling Fruit Juice Beverage
- Koala Sparkling Mineral Water & Fruit Juice
- LaCroix Sparkling Mineral Water (flavored and non-flavored)
- Mendota Springs Sparkling Mineral Water (natural and flavored)
- Mistic Flavored Fruit Beverage With Sparkling Water & Juice
- Original New York Seltzer Sparkling Water
- Perrier Sparkling Mineral Water (flavored and non-flavored)
- Quest Sparkling Spring Water
- Schweppes Seltzer Water
- Schweppes Tonic Water
- West End All Natural Soda Brew

Note: The sales and use tax treatment of bottled water in this tax release supersedes the treatment of bottled water as described in sec. Tax 11.51(2)(a), Wis. Adm. Code, December 1992 Register. Section Tax 11.51(2)(a), Wis. Adm. Code, December 1992 Register, will be revised to reflect the above treatment.

As stated in the introduction of the tax release section of this Bulletin, this tax release applies retroactively and prospectively to all periods open to adjustment. □