

# Shareholder's Instructions for 2010 Schedule 5K-1

## General Instructions

**Purpose of Schedule 5K-1** – Similar to federal Schedule K-1, the tax-option (S) corporation uses Schedule 5K-1 to report your pro rata share of the corporation's income, deductions, credits, etc., for Wisconsin purposes. Please keep it for your records. You must also file a copy of Schedule 5K-1 with your tax return if:

- You are claiming a tax credit passed through from the tax-option (S) corporation,
- You are filing an amended return based on an amended Schedule 5K-1, or
- The tax-option (S) corporation withheld tax on your share of the corporation's distributable income (applicable if you are not a Wisconsin resident).

Although the tax-option (S) corporation may have to pay a built-in gains tax, a franchise tax measured by certain federal, state, and municipal government interest income, and a recycling surcharge, you are liable for Wisconsin income tax on your share of the tax-option (S) corporation income, whether or not distributed, and you must include your share on your Wisconsin income tax return if a return is required.

**Inconsistent Treatment of Items** – Generally, you must report tax-option (S) corporation items shown on your Schedule 5K-1 and any accompanying schedules the same way that the tax-option (S) corporation treated the items on its return. If your treatment is (or may be) inconsistent with the tax-option (S) corporation's treatment, you must include a statement with your return to identify and explain any inconsistency.

**Errors** – If you believe the tax-option (S) corporation has made an error on your Schedule 5K-1, notify the corporation and ask for a corrected Schedule 5K-1. Don't change any items on your copy. Be sure that the corporation sends a copy of the corrected Schedule 5K-1 to the Wisconsin Department of Revenue.

**Elections** – Generally, the tax-option (S) corporation decides how to figure taxable income from its operations. For example, it chooses the accounting method and depreciation methods it will use. However, certain elections are made by you separately on your tax return and not by the corporation. These include elections under Internal Revenue Code section 59(e)(2), relating to the deduction of certain qualified expenditures ratably over the period of time specified in that section.

## Limitations on Losses, Deductions and Credits

**CAUTION:** The amount of loss and deduction that you may claim on your Wisconsin return may be less than the amount reported on Schedule 5K-1. It is the shareholder's responsibility to consider and apply any applicable limitations.

There are three separate potential limitations on the amount of tax-option (S) corporation losses that you may deduct on your return. These limitations are as follows:

1. The basis of your stock,
2. The at-risk limitations, and
3. The passive activity limitations.

**1. Basis of Your Stock** – You are responsible for maintaining records to show the computation of the basis of your stock in the corporation for Wisconsin income tax purposes. Schedule 5K-1 provides information to help you make the computation at the end of each corporate taxable year. The Wisconsin basis of your stock (generally, its cost) is adjusted as follows (this list is not all-inclusive):

Basis is first *increased* by:

- All income, including tax-exempt income, as computed under Wisconsin law, reported on Schedule 5K-1, column d. **Exception:** Basis is not increased by the corporation's excluded discharge of indebtedness income, generally applicable for discharges of indebtedness after October 11, 2001.

**NOTE:** You must report the taxable income on your Wisconsin income tax return (if you are required to file a return) for it to increase your basis.

Basis is then *decreased*, but not below zero, by:

- Property distributions, including cash, made by the corporation, reported on Schedule 5K-1, line 16d, that are not includable in income. (Distributions in excess of Wisconsin basis reported on Schedule 5K-1, line 16d, and dividend distributions reported on Schedule 5K-1, line 17c, don't decrease basis.)
- Nondeductible expenditures not due to timing differences, as computed under Wisconsin law from Schedule 5K-1, column (d).
- All deductible losses and deductions, as computed under Wisconsin law, reported on Schedule 5K-1, column (d).
- Your share of the supplement to the federal historic rehabilitation tax credit or early stage seed investment credit computed.

When figuring the Wisconsin basis in stock of a multistate corporation, use your share of the total company amounts, as computed under Wisconsin law from Schedule 5K-1, column (d), rather than the income, losses, and deductions attributable to Wisconsin activities from Schedule 5K-1, column (e).

You may elect to decrease your basis by deductible losses and deductions prior to decreasing your basis by nondeductible expenses. If you make this election, any nondeductible expenses that exceed the basis of your stock and debt owed to you by the corporation are treated as nondeductible expenses for the following taxable year. To make the election, file a statement with your timely filed original or amended return, as provided in the federal regulations. Once made, the election applies to the year for which it is made and all future taxable years for that corporation, unless the Department agrees to revoke your election.

**2. At-Risk Limitations** – For federal purposes, if you have a loss or other deduction from any activity carried on as a trade or business or for the production of income by the tax-option (S) corporation, and you have amounts in the activity for which you aren't at risk, you generally will have to figure the allowable loss. The at-risk rules generally limit the amount of loss (including loss on disposition of assets) and other deductions (such as the section 179 expense deduction) that you can claim to the amount you could actually lose in the activity. The at-risk rules also apply for Wisconsin purposes.

**3. Passive Activity Limitations** – Internal Revenue Code section 469 limits the deduction of certain losses. The rules apply to shareholders who are individuals, estates, trusts, closely held corporations, or personal service corporations and have a passive activity loss for the taxable year. Passive activities include trade or business activities in which you didn't materially participate and rental activities, as defined in the federal regulations. Rental real estate activities in which you materially participated are not passive activities if you meet certain eligibility requirements. The tax-option (S) corporation will identify separately each activity that may be passive to you. You must determine whether your losses are limited by the passive activity rules.

The passive activity loss limits also apply for Wisconsin purposes. However, if there are differences between your federal and Wisconsin income, you may have to recompute the amount of passive activity loss deductible for Wisconsin. There are three types of differences between federal and Wisconsin income:

- a. Schedule I adjustments,
- b. Differences resulting from making different elections for federal and Wisconsin purposes, and
- c. Modifications to federal adjusted gross income prescribed in section 71.05(6) to (12), (19), and (20), Wisconsin Statutes.

A Schedule I adjustment may arise if a provision of the Internal Revenue Code doesn't apply for Wisconsin or if a federal law change becomes effective at a different time for Wisconsin than for federal purposes. Modifications to federal adjusted gross income include the addition of state and local government bond interest income and the subtraction of the capital gain deduction.

For differences resulting from Schedule I adjustments or different elections, you must recompute the passive activity loss limits for Wisconsin. However, you may not recompute the loss limits for modifications. The tax-option (S) corporation should tell you the reason for any adjustment in column (c) so that you will know whether you must recompute the passive activity loss limits.

## Specific Instructions

**Lines 1 through 12, 14, 15, and 17d** – The entries on these lines show your share of the federal amount (column (b)), adjustment (column (c)), and amount reportable under Wisconsin law (column (d)) for each of the items. For nonresident and part-year resident shareholders, the entries also show your share of the amount attributed to Wisconsin (column (e)).

These amounts don't take into account limitations on losses or other items that may have to be adjusted because of the adjusted basis of your stock and debt in the corporation, the at-risk limitations, or the passive activity limitations.

If the amount under Wisconsin law for any share item on lines 1 through 12, 14, 15, and 17d differs from the federal amount, your Schedule 5K-1 will have an amount in column (c). You must account for this difference on your Wisconsin franchise or income tax return. How you account for the difference depends on the return you are filing, the share item, and the reason for the difference.

If the difference in column (c) arises because a provision of the Internal Revenue Code doesn't apply for Wisconsin or a federal law change becomes effective for Wisconsin at a different time, you must complete Wisconsin Schedule I (Schedule B for estates and trusts) before filling in your Wisconsin income tax return. If the difference results from the tax-option (S) corporation making different elections for federal and Wisconsin purposes, you must recompute the federal adjusted gross income that you report on your Wisconsin return.

If the difference is a modification allowed in computing Wisconsin adjusted gross income, the treatment depends on which share item is affected and the return you are filing:

### Modifications on Lines 1, 2, 3, 5, 6, 10, 11, 12, 14, and 17d:

- If you are filing Form 1, account for any modification to one of these share items by combining the amount from Schedule 5K-1, column (c), with any other Wis-

consin modification and entering the total on the appropriate line of Form 1.

- If you are filing Form 1NPR, include in column B on the appropriate line of Form 1NPR, along with any other Wisconsin income or loss, the Wisconsin amount from column (e) of any share item reported on one of these lines.
- If you are filing Form 2, account for any modification to one of these share items by entering the amount from Schedule 5K-1, column (c), on Form 2, Schedule A.

**Interest Income Modifications on Lines 4, 16a, and 17a:**

Interest income that is exempt from federal income taxes but taxable by Wisconsin, such as state and local government bond interest, is shown as an **addition** on line 4, column (c) and as a **subtraction** on line 16a, column (c).

- If you are filing Form 1, combine the interest income amount from Schedule 5K-1, column (c), with any other interest modification and enter the total on the appropriate line of Form 1.
- If you are filing Form 1NPR, include in column B on Form 1NPR, along with any other Wisconsin interest income, the Wisconsin source amount of interest income from Schedule 5K-1, column (e).
- If you are filing Form 2, account for any modification by entering the amount from Schedule 5K-1, column (c), on Form 2, Schedule A.

**Capital Gain Modifications on Lines 7 and 8:**

Enter the Wisconsin amounts from column (d) (column (e) for nonresidents and part-year residents) of these share items on the appropriate lines of Wisconsin Schedule WD (Schedule WD (Form 2) for estates and trusts).

**Section 1231 Gain/Loss Modifications on Line 9:**

See the instructions for Part II of Wisconsin Schedule T and recompute a federal Form 4797 as instructed.

**Itemized Deduction Modifications on Lines 12 and 17b:**

Adjust the deduction items from federal Schedule A when figuring the Wisconsin itemized deduction credit (Form 1, Schedule 1, or Form 1NPR, Schedule 1). Increase or decrease, as appropriate, the amount from federal Schedule A by the amount on Schedule 5K-1, column (c).

**Note:** Rather than including the tax-option items deductible on federal Schedule A in the Wisconsin itemized deduction credit, you may treat these items as subtraction modifications to arrive at Wisconsin adjusted gross income. Your modification is limited to the amount actually deductible for federal purposes. If you are a nonresident of Wisconsin for any part of the corporation's taxable year, your modification is further limited to that portion of the deductible amount which is at-

tributable to Wisconsin based on apportionment or separate accounting, as appropriate.

**Credits on Lines 13a through 13yy** – Enter the amounts from lines 13a through 13yy, column (d) or (e), on the appropriate line of the credit computation schedules you file with your return. The credit computation schedules corresponding to the credits on lines 13a through 13yy are as follows:

Line	Credit	Schedule
13a	Manufacturing Investment Credit – From Carryover at Shareholder Level	MI
13b	Manufacturing Investment Credit – From Carryover at Entity Level	MI
13c	Dairy and Livestock Farm Investment Credit	DI
13d	Health Insurance Risk-Sharing Plan Assessments Credit	HI
13e	Ethanol and Biodiesel Fuel Pump Credit	EB
13f	Development Zones Credit	DC
13g	Development Opportunity Zone Investment Credit	DC
13h	Development Zone Capital Investment Credit	DC
13i	Economic Development Tax Credit	ED
13j	Technology Zone Credit	TC
13k	Early Stage Seed Investment Credit	VC
13l	Supplement to Federal Historic Rehabilitation Tax Credit	HR
13m	Internet Equipment Credit	IE
13n	Dairy Manufacturing Facility Investment Credit	DM
13o	Dairy Cooperatives Credit	DM
13p	Meat Processing Facility Investment Credit	MP
13q	Enterprise Zone Jobs Credit	EC
13r	Film Production Services Credit	FP
13s	Film Production Company Investment Credit	FP
13t	Food Processing Plant and Food Warehouse Investment Credit	FW
13u	Jobs Tax Credit	JT
13v	Postsecondary Education Credit	PE
13w	Woody Biomass Harvesting and Processing Credit	WB
13x	Water Consumption Credit	WC
13yy	Credit for Net Tax Paid to Another State	OS

**Line 13zz. Wisconsin Tax Withheld** – Enter the amount from line 13zz, column (e), on the “Wisconsin income tax withheld” line of your Wisconsin income or franchise tax return. Unless you elect to be included in a composite return (Form 1CNS), you must file a copy of Schedule 5K-1 with your Wisconsin income or franchise tax return if you claim this credit.

**CAUTION:** Do not enter your share of pass-through entity withholding as an estimated tax payment on your Wisconsin return.

**Line 15. Alternative Minimum Tax Items** – Enter the net amount from column (c) of line 15 on Wisconsin Schedule MT, line 8. If you are a nonresident of Wisconsin for any part of the corporation's taxable year, enter the difference between column b and column e on Schedule MT, line 8.

**Lines 16a through 16c. Tax-Exempt Interest and Nondeductible Expenses** – Differences in the amount of income that is exempt for federal and Wisconsin purposes are shown on lines 16a and 16b, column (c). Increases or decreases in the amount of nondeductible expenses are shown on line 16c, column (c). Use the amount from column (d) when computing the Wisconsin basis of your stock.

**Line 16d. Property Distributions** – Reduce your Wisconsin basis in stock of the corporation by the Wisconsin distributions on line 16d, column (d). If these distributions exceed your Wisconsin basis in stock and you were a Wisconsin resident when you received the distributions, treat the excess as a Wisconsin gain from the sale or exchange of property. Enter any Wisconsin gain on the appropriate line of Wisconsin Schedule WD.

**Line 16e. Repayment of Loans from Shareholders** – If the repayments on line 16e are made on indebtedness with a reduced Wisconsin basis and you received the repayments while you were a Wisconsin resident, the repayments result in income to you to the extent the repayments are more than the adjusted Wisconsin basis of the loan.

If you are filing Form 1, enter the amount of Wisconsin income realized on Wisconsin Schedule WD, if the loan was a capital asset. If the loan wasn't a capital asset, enter the difference between federal income and Wisconsin income on Form 1, line 4 or 11, as appropriate.

If you are filing Form 1NPR, enter the amount of Wisconsin income realized on Wisconsin Schedule WD, if the loan was a capital asset, or in column B of the appropriate line on Form 1NPR, if the loan wasn't a capital asset.

**Line 17c. Dividend Distributions** – You must report the amount from column (d) or (e), as appropriate, as dividend income if you were a Wisconsin resident on the date you received it. The federal amount of the dividend distribution should have been reported to you on Form 1099-DIV.

If you are filing Form 1, enter the amount from line 17c, column (c), on Form 1, line 4 or 11, as appropriate. If you are filing Form 1NPR and the dividend distribution is reportable to Wisconsin, enter the amount from line 17c, column (e), on Form 1NPR, line 3, column B, along with any other dividend income reportable to Wisconsin.

**Line 17d. Other Items and Amounts** – If applicable, the corporation has provided supplemental information or has listed in the space provided, your pro rata share of items not included on lines 1 through 17c. This listing should include the federal amount, adjustment, amount under Wisconsin law,

and Wisconsin source amount, if applicable, for each item. Account for any other share items listed on line 17d as necessary to include the taxable or deductible amount of each item as computed under Wisconsin law in your Wisconsin income.

If interest income from United States government obligations is listed, you must make an adjustment on your Wisconsin return since this income is taxable for federal income tax purposes, but not for Wisconsin purposes. If you are filing Form 1, include the federal amount of this interest income on line 7. If you are filing Form 1NPR, don't include this interest income on Form 1NPR, line 2, column B.

**Lines 18a and 18b. Related Entity Expenses** – If the tax-option (S) corporation paid, accrued, or incurred management fees or interest, rental or intangible expenses to a related person or entity, the corporation completes lines 18a and 18b, as appropriate, to separately disclose the modifications it made to those items under the Wisconsin law requiring "addback" of related entity expenses. The amounts on lines 18a and 18b should already be included in column (c) corresponding to one or more other lines of Schedule 5K-1. Shareholders should verify that any amounts on lines 18a and 18b are included in column (c). If they are not, the shareholder should enter the modifications from lines 18a and 18b on the appropriate lines of Form 1, Form 1NPR, or Form 2, as applicable.

**NOTE:** You must make separate addition and subtraction modifications on your return for related entity interest and rental expenses, even if the modifications offset one another.

**Line 19. Gross Income** – Individuals combine the amount from column (d) or (e), as appropriate, with gross income from other sources (if any) that is reportable to Wisconsin to determine whether they must file a Wisconsin income tax return. See the instructions for Form 1 or Form 1NPR for information about the filing requirements.