

# Partner's Instructions for 2011 Schedule 3K-1

## General Instructions

**Purpose of Schedule 3K-1** – Similar to federal Schedule K-1, the partnership uses Schedule 3K-1 to report your share of the partnership's income, deductions, credits, etc., for Wisconsin purposes. Please keep it for your records. You must also file a copy of Schedule 3K-1 with your tax return if:

- You are claiming a tax credit passed through from the partnership,
- You are filing an amended return based on an amended Schedule 3K-1, or
- The partnership withheld tax on your share of the partnership's distributable income (applicable if you are not a Wisconsin resident).

Although the partnership may have to pay an economic development surcharge, you are liable for Wisconsin franchise or income tax on your share of the partnership income, whether or not distributed, and you must include your share on your Wisconsin franchise or income tax return if a return is required.

**Inconsistent Treatment of Items** – Generally, you must report partnership items shown on your Schedule 3K-1 and any accompanying schedules the same way that the partnership treated the items on its return. If your treatment is (or may be) inconsistent with the partnership's treatment, you must include a statement with your return to identify and explain any inconsistency.

**Errors** – If you believe the partnership has made an error on your Schedule 3K-1, notify the partnership and ask for a corrected Schedule 3K-1. Don't change any items on your copy. Be sure that the partnership sends a copy of the corrected Schedule 3K-1 to the Wisconsin Department of Revenue.

**Elections** – Generally, the partnership 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 partnership. 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 3K-1. It is the partner's responsibility to consider and apply any applicable limitations.

There are three separate potential limitations on the amount of partnership losses that you may deduct on your return. These limitations and the order in which you must apply them are as follows:

1. The basis rules,
2. The at-risk limitations, and
3. The passive activity limitations.

Other limitations may apply to specific deductions, such as the section 179 expense deduction. These limitations on specific deductions generally apply before the basis, at-risk, and passive loss limitations.

**1. Basis Rules** – Generally, you may **not** claim your share of a partnership loss (including a capital loss) to the extent that it is greater than the adjusted basis of your partnership interest at the end of the partnership's taxable year. Compute the Wisconsin adjusted basis of your partnership interest by adding items that increase your basis and then subtracting items that decrease your basis.

Items that **increase** your basis include:

- Money and your adjusted basis in property contributed to the partnership.
- Your share of the increase in the partnership's liabilities.
- Your share of the partnership's income as computed under Wisconsin law.

Items that **decrease** your basis, but not below zero, include:

- Money and the adjusted basis of property distributed to you.
- Your share of the decrease in the partnership's liabilities.
- Your share of the partnership's losses as computed under Wisconsin law.
- Your share of the partnership's section 179 expense deduction.
- Your share of the partnership's nondeductible expenses.
- Your share of the supplement to the federal historic rehabilitation tax credit, early stage seed investment credit, or angel investment credit computed.

When figuring the Wisconsin adjusted basis in a multistate partnership, use your share of the total partnership amounts, as computed under Wisconsin law, rather than just the income, losses, and deductions attributable to Wisconsin activities.

**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 partnership, 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 partners 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 partnership 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 partnership 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 13, 16, 17, and 20** – 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 partners, the entries also show your share of the amount attributed to Wisconsin (column (e)). For additional information about the taxation of nonresident and part-year resident partners, see the 2011 Form 3 instructions.

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

If the amount under Wisconsin law for any share item on lines 1 through 13, 16, 17, and 20 differs from the federal amount, your Schedule 3K-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.

**Column (c) for Individuals, Estates, and Trusts.** 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 partnership 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, 4, 6, 7, 11, 12, 16, and 20:

- If you are filing Form 1, account for any modification to one of these share items by combining the amount from Schedule 3K-1, column (c), with any other Wisconsin 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 3K-1, column (c), on Form 2, Schedule A.

### Interest Income Modifications on Lines 5 and 18a:

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 5, column (c), and as a **subtraction** on line 18a, column (c).

- If you are filing Form 1, combine the interest income amount from Schedule 3K-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 3K-1, column (e).
- If you are filing Form 2, account for any modification by entering the amount from Schedule 3K-1, column (c), on Form 2, Schedule A.

Capital Gain Modifications on Lines 8 and 9:

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 10a:

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

Portion of gain on Line 10a Attributable to Gains on Sale of Farm Assets on Line 10b:

Enter portion of the net gain attributable to the sales of farm assets held more than one year. Neither include amounts treated as ordinary income for federal income tax purposes because of recapture of depreciation, or for any other reason, nor amounts treated as capital gain for federal income tax purposes from the sale or exchange of a lottery prize. "Farm assets" means livestock, farm equipment, farm real property, and farm depreciable property.

Itemized Deduction Modifications on Lines 13 and 20:

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 3K-1, column (c).

**Column (c) for Partnerships.** If you are filing Form 3, account for any difference between the Wisconsin and federal amount of a share item that is allowable in computing Wisconsin net income by entering the amount from Schedule 3K-1, column (c), on the appropriate line of Form 3, Schedule 3K, column (c).

**Column (c) for Corporations.** If you are filing Form 4 or 5, account for any difference between the Wisconsin and federal amount of a share item that is allowable in computing Wisconsin net income by entering the amount from Schedule 3K-1, column (c), on Schedule V or W, as appropriate.

**Column (c) for Tax-Option (S) Corporations.** If you are filing Form 5S, account for any difference between the Wisconsin and federal amount of a share item by entering the amount from Schedule 3K-1, column (c), on the appropriate line of Form 5S, Schedule 5K, column (c).

**Credits on Lines 15a through 15n** – Compute the credits on lines 15a through 15n in the same manner for partners who are full-year, part-year, or nonresidents of Wisconsin. For part-year and nonresident partners, also enter the allowable credits in column e. For each credit, enter the partner's proportionate or specially allocated share of the amount on Schedule 3K. (**Note:** Only the early stage seed investment credit may be specially allocated. See the Schedule VC instructions for details.) Enter the abbreviation of the credit you are claiming next to the word "schedule" on line 15. The abbreviation for each credit is located in the upper left hand corner of the credit schedule and in the instructions for Schedule 3K. Use a separate line for each credit you are claiming. For example, if you are claiming the enterprise zone jobs credit, enter "EC" next to the "Schedule" line.

**Line 15o. Credit for Tax Paid to Other States** – Complete this line only for full-year Wisconsin resident partners and part-year Wisconsin resident partners. Enter zero for partners who are nonresidents of Wisconsin or corporations.

For a full-year resident, enter in column d the partner's proportionate share of the tax credits on Schedule 3K, line 15o. For a part-year resident, enter in column d the amount computed by multiplying the credit on Schedule 3K, line 15o, by the partner's profit and loss percentage, multiplied by the ratio of days that the partner was a resident of Wisconsin during the partnership's taxable year to the total days in the partnership's taxable year. Enter the result in column e.

**Line 15p. Wisconsin Tax Withheld** – Enter the amount from line 15p, 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 1CNP), you must file a copy of Schedule 3K-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 17. Alternative Minimum Tax Items** – Instructions depend on the type of partner:

- **Individuals, estates, and trusts** enter the net amount from column (c) of line 17 on Wisconsin Schedule MT, line 8. If you are a nonresident of Wisconsin for any part of the partnership's taxable year, enter the difference between column (b) and column (e) on Schedule MT, line 8.
- **Partnerships and tax-option (S) corporations** enter the amounts from column (c) on the appropriate lines of Schedule 3K or Schedule 5K, column (c).
- **Corporations** may disregard this line.

**Lines 18a through 18c. Tax Exempt Interest and Nondeductible Expenses** – Differences in the amount of income that is exempt for federal and Wisconsin purposes are shown on lines 18a and 18b, column (c). Increases or decreases in the amount of nondeductible expenses are shown on line 18c, column (c).

Use the amount from column (d) when computing the Wisconsin basis of your partnership interest. Partners that are partnerships and tax-option (S) corporations enter the amounts from column (c) on the appropriate lines of Schedule 3K or Schedule 5K, column (c).

**Line 19. Distributions** – Reduce the Wisconsin basis of your partnership interest by the Wisconsin distributions shown on line 19, column (d). If these distributions exceed the Wisconsin basis of your partnership interest and you were a Wisconsin resident when you received the distributions, treat the excess as a gain from the sale or exchange of property. Enter any Wisconsin gain on the appropriate line of Wisconsin Schedule WD.

**Line 20. Other Information** – If applicable, the partnership has provided supplemental information or has listed in the space provided or on attached schedules your share of items not included on lines 1 through 19. Account for these items as necessary to include the taxable or deductible amount of each item as computed under Wisconsin law in your Wisconsin income.

For individuals, estates, and trusts, if line 20 includes interest income from United States government obligations, you must make an adjustment on your Wisconsin return because this income is not taxable for Wisconsin income tax purposes. If you are filing Form 1, subtract this interest income on Form 1, line 7. If you are filing Form 1NPR, don't include this interest income on Form 1NPR, line 2, column B. If you are filing Form 2, subtract the United States government interest on Schedule A, line 8.

**Lines 21a and 21b. Related Entity Expenses** – If the partnership paid, accrued, or incurred management fees or interest, rental or intangible expenses to a related person or entity, the partnership completes lines 21a and 21b, 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 21a and 21b should already be included in column (c) corresponding to one or more other lines of Schedule 3K-1.

Instructions for lines 21a and 21b depend on the type of partner:

- **Individuals** may disregard these lines.
- **Partnerships and tax-option (S) corporations** must enter these amounts on lines 21a and 21b of Schedule 3K or lines 18a and 18b of Schedule 5K.
- **Corporations** must enter the amount from line 21a on Schedule V (if not already included) and the amount from line 21b on Schedule W (if not already included), even if the net total of those amounts is zero.

**Line 22. 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.

**Lines 23 Through 25. Share of Apportionment Factors** – Partnerships, corporations, and tax-option (S) corporations must generally include their share of the numerator and denominator of the partnership's apportionment factors in the numerator and denominator of their apportionment factors. Include these amounts on Form 4A-1, *Wisconsin Apportionment Data for Single Factor Formulas* or Form 4A-2, *Apportionment Data for Multiple Factor Formulas*, as appropriate.