

**WISCONSIN DEPARTMENT OF REVENUE
DIVISION OF INCOME, SALES, AND EXCISE TAX**

NOTICE OF PROPOSED GUIDANCE DOCUMENTS

Pursuant to sec. 227.112, Wis. Stats., the Wisconsin Department of Revenue, Division of Income, Sales, and Excise Taxes hereby seeks comment on the proposed guidance document listed in the table below.

SUBMITTING PUBLIC COMMENTS

Public comments on proposed or adopted guidance documents may be submitted online at: <https://www.revenue.wi.gov/Pages/contactUs/proposed-Guidance.aspx>.

DEADLINE FOR SUBMISSION

The period for public comment for proposed guidance documents ends 21 days after publication in the Administrative Register, unless the Governor approves a shorter commenting period.

Document Number	Document Title
100176	Passive Activity Losses - Common Questions

State of Wisconsin
Department of Revenue

Passive Activity Losses

This is a proposed guidance document. The document has been submitted to the Legislative Reference Bureau for publication in the Administrative Register for public comment as provided by sec. 227.112(1), Wis. Stats.

1. What is a passive activity?
2. What are the passive activity limitations?
3. Are Wisconsin passive activity losses always the same as on the federal return?
4. What is Wisconsin Schedule I used for?
5. What amount is included in the Wisconsin column of Form 1NPR if a passive activity loss is not affected by a Schedule I adjustment?
6. What amount is included in the Wisconsin column if a passive activity loss is affected by a Schedule I adjustment?

1. **What is a passive activity?**

A passive activity is an activity which involves the conduct of a trade or business in which you do not materially participate. Rental activities are included in this definition, even if you do materially participate in them, unless you are a real estate professional. A passive activity loss for the tax year is the excess of your passive activity deductions over your passive activity gross income.

2. **What are the passive activity limitations?**

Your passive activity losses are limited to the amount of your passive activity income for the taxable year. Any excess passive activity loss must be carried forward to the next year to be offset against any additional passive activity income.

A special allowance may be allowed under which some or all of your passive activity loss is allowed. If you or your spouse actively participated in a passive rental real estate activity, the amount of the passive activity loss that is disallowed is decreased and you may be able to deduct up to \$25,000 (\$12,500 in the case of married individuals filing a separate return who lived apart from their spouse all year) of loss from the activity from your nonpassive income.

This amount is reduced by 50% of the amount of your modified federal adjusted gross income that is more than \$100,000 (\$50,000 if you are married filing separately). If your modified adjusted gross income (MAGI) is \$150,000 or more (\$75,000 or more if you are married filing separately), you generally cannot use the special allowance. For more information, see federal [Publication 925, Passive Activity and At-Risk Rules](#).

3. Are Wisconsin passive activity losses always the same as on the federal return?

No. The amount of passive activity loss allowed is based on the Wisconsin definition of the Internal Revenue Code (IRC). If computation of the allowable passive activity loss is affected by the Wisconsin definition of the IRC, you must file Wisconsin [Schedule I, Adjustments to Convert 2019 Federal Adjusted Gross Income and Itemized Deductions to the Amounts Allowable for Wisconsin](#).

4. What is Wisconsin Schedule I used for?

Schedule I is used whenever there is a difference in the tax treatment of an item due to a difference in the federal IRC and the Wisconsin definition of the IRC. For example, the Wisconsin definition of the IRC does not allow the federal special bonus depreciation deduction. Schedule I must be filed to adjust depreciation. To adjust for this difference, the amount of depreciation reported on your federal return would be added to federal income on line 2c. The amount of your recomputed Wisconsin depreciation would be subtracted from federal income on line 4b. This difference in the depreciation deduction would cause income or losses from the activity to be adjusted which could also affect passive activity losses.

If passive activity losses are affected by the Schedule I adjustment, federal [Form 8582, Passive Activity Loss Limitations](#), must be recomputed. Any difference between the passive activity loss allowed on the federal Form 8582 and on the recomputed Form 8582 is also a Schedule I adjustment. To adjust for this difference, the amount of the passive activity loss allowed for federal purposes would be added back to federal income on line 2h. Write "passive activity loss" on the line provided. The amount of passive activity loss allowed for Wisconsin purposes would be subtracted from federal income on line 4g. Write "passive activity loss" on the line provided.

Note: Once a Form 8582 is recomputed for a year, Form 8582 will need to be recomputed in future years to reflect the federal and Wisconsin difference in passive activity losses for the prior year. A Schedule I adjustment will be required each year in which the amount of passive activity losses allowable on the Form 8582 prepared for federal tax purposes are different than the losses allowable on the recomputed Form 8582.

By adjusting for differences in the federal IRC and the Wisconsin definition of the IRC and for passive activity loss differences on Schedule I, the amount on line 5 of Schedule I is the federal adjusted gross income (FAGI) for the purpose of determining Wisconsin taxable income. The amount from line 5 of Schedule I is carried to line 1 of Form 1. No additional adjustment to passive activity losses is required for full-year residents.

The FAGI from Schedule I also applies to Form 1NPR which is filed by nonresidents and part-year residents. Because Form 1NPR requires each item from the federal return to be listed separately, nonresidents must complete an additional federal schedule that reflects the federal difference due to the Schedule I adjustments. The amount on line 5 of Schedule I should generally equal the amount entered on line 32 of Form 1NPR.

5. What amount is included in the Wisconsin column of Form 1NPR if a passive activity loss is not affected by a Schedule I adjustment?

The amount of passive activity loss allowed for Wisconsin is the same as the amount allowed on the federal Form 1040 or 1040-SR. Federal Form 8582 is completed to determine the allowable passive activity loss. The passive activity loss allowed is then carried to the appropriate federal schedule and included in federal income. A nonresident of Wisconsin would include the federal amount in the federal column of Form 1NPR. The amount to include in the Wisconsin column would be the same amount included in the federal column that relates to Wisconsin sources.

Example: A nonresident of Wisconsin is a partner in two partnerships – Partnership A, which conducts business only in Illinois, and Partnership B, which conducts business only in Wisconsin. Both partnerships are determined to be passive activities. The taxpayer completes federal Form 8582 to determine the amount of passive activity loss allowed as a subtraction for each partnership for the taxable year. The allowed passive activity losses are carried to federal Schedule E which determines the amount of income/loss to be reported on Form 1040 or 1040-SR for each partnership. The amount included in federal income from Schedule E is a loss of \$10,000 (\$2,500 loss for Partnership A and \$7,500 loss for Partnership B). When completing Form 1NPR, the nonresident would include (\$10,000) in the federal column and (\$7,500) in the Wisconsin column. Income/loss from Partnership A is not from Wisconsin sources and would not be taxable to Wisconsin.

6. What amount is included in the Wisconsin column if a passive activity loss is affected by a Schedule I adjustment?

When a passive activity loss is affected by a Schedule I adjustment, the federal Form 8582 would have to be recomputed for Wisconsin. The recomputed Form 8582 substitutes the Wisconsin income, as computed under Wisconsin law, for the amount reported on the federal Form 8582. Any difference between the amount of passive activity loss allowed on the federal Form 8582 and the recomputed Form 8582 is also a Schedule I adjustment. (**Note:** The entire Form 8582 must be recomputed. The Wisconsin statutes do not permit the taxpayer to recompute allowable passive activity losses by excluding the income and losses that are not taxable by Wisconsin and to make a modification for the difference.)

Any federal IRC difference and the recomputed passive activity losses must be adjusted for on the appropriate federal forms (e.g., Schedule C, E, F, etc.) and the adjusted amount would be included in the federal column of Form 1NPR. The amount to include in the Wisconsin column would be the amount from the federal column that is from Wisconsin sources.

Example: A nonresident of Wisconsin is a shareholder in a tax-option (S) corporation (Corporation B) and a partner in Partnerships A and C. Partnership A does business only in Illinois. Corporation B and Partnership C do business only in Wisconsin. The nonresident reports the following income on his federal income tax return:

Wages earned in Illinois	\$115,000
Interest income	8,000
Passive activity losses allowed*	(3,500)
Gain on sale of Wisconsin real estate	<u>20,000</u>
Federal adjusted gross income	\$139,500

*Rental passive activity losses from federal Form 8582 consist of the following:

	Total	Federal Allowed*
Partnership A (Illinois)	(\$5,000)	(\$1,944)
Corporation B (Wisconsin)	(3,000)	(1,167)
Partnership C (Wisconsin)	<u>(1,000)</u>	<u>(389)</u>
Totals	(\$9,000)	(\$3,500)

*Limited due to MAGI

There is a depreciation adjustment on Schedule I that results in an adjustment to the passive loss for Corporation B:

Corporation B loss:	(\$3,000)
Depreciation adjustment:	<u>10,000</u>
Corporation B income:	7,000

	Total Passive Activity Income/Loss with Depreciation Adjustment	Wisconsin Amounts Allowed on Form 8582
Partnership A (Illinois)	(\$5,000)	(\$5,000)
Corporation B (Wisconsin)	7,000	7,000

Partnership C (Wisconsin)	(<u>1,000</u>)	(<u>1,000</u>)
Totals	\$1,000	\$1,000

The adjustment to the income of Corporation B also affects passive activity losses. The taxpayer then recomputes the federal Form 8582 and includes an additional adjustment on Schedule I for the difference in the amount of passive activity loss as determined on the federal Form 8582 and the recomputed Form 8582. In this example, the recomputed Form 8582 would show that all passive losses for the year would be allowed.

	Federal Allowed	Wisconsin Adjusted Amount	Difference
Partnership A (Illinois)	(\$1,944)	(\$5,000)	(\$3,056)
Corporation B (Wisconsin)	(1,167)	7,000	8,167
Partnership C (Wisconsin)	(<u>389</u>)	(<u>1,000</u>)	(<u>611</u>)
Schedule I passive activity loss adjustment:	(\$3,500)	\$1,000	\$4,500

A nonresident must also recompute federal Schedule E to reflect the Schedule I difference in Corporation B's income for depreciation and the passive activity loss. The amount from this recomputed Schedule E is used to complete the federal column of Form 1NPR:

Partnership A (Illinois)	(\$5,000)
Corporation B (Wisconsin)	7,000
Partnership C (Wisconsin)	(<u>1,000</u>)
Federal column	\$1,000

The amount included in the Wisconsin column of Form 1NPR is also determined from the recomputed Schedule E:

Corporation B (Wisconsin)	7,000
Partnership C (Wisconsin)	(<u>1,000</u>)
Wisconsin column:	\$6,000

The amount in the federal column for Property A would not be included in the Wisconsin column.

Applicable Laws and Rules

This document provides statements or interpretations of the following laws and regulations in effect as of October 22, 2019: Sections 71.01, 71.03, 71.04, 71.19, 71.22, 71.25 and 71.32, Wis. Stats., sec. Tax 2.08, Wis. Adm. Code, and 26 U.S. Code § 469.

Laws enacted and in effect after October 22, 2019, new administrative rules, and court decisions may change the interpretations in this document. Guidance issued prior to October 22, 2019, that is contrary to the information in this document is superseded by this document, pursuant to sec. 73.16(2)(a), Wis. Stats.

FOR QUESTIONS OR COMMENTS CONTACT:

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