

Reporting Capital Gains and Losses for Wisconsin by Individuals, Estates, and Trusts

For Use in Preparing 2009 Returns

IMPORTANT CHANGE

The Wisconsin capital gain exclusion is reduced from 60 percent of net long-term capital gain to 30 percent of net long-term capital gain. Gain on the sale of farm assets remains subject to a 60% exclusion. See page 1.

CAUTION

The information in this publication reflects the position of the Wisconsin Department of Revenue of laws enacted by the Wisconsin Legislature as of November 1, 2009. Laws enacted after this date, administrative rules, and court decisions may change the interpretations in this publication.

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I. INTRODUCTION

Gains and losses from sales or other dispositions of capital assets are reportable for both Wisconsin and federal income tax purposes. However, differences exist in the manner in which Wisconsin and federal law treat such income and loss.

This publication explains the differences between Wisconsin and federal law in reporting capital gains and losses on Wisconsin and federal income tax returns. It does not, however, explain all of the details concerning how capital gain and loss are classified and computed under federal income tax law. For further information about federal law pertaining to this type of income, Internal Revenue Service Publication 544 entitled *Sales and Other Dispositions of Assets* is suggested as a reference guide.

Before 1987, individuals were allowed to deduct 60% of their net long-term capital gain from both their Wisconsin and federal income. This provision was eliminated for federal tax purposes. However, 30% of the net capital gain on assets held more than one year continues to be deductible for Wisconsin (60% of net capital gain on farm assets). In addition, Wisconsin law generally limits the amount of capital losses in excess of capital gains that may be deducted each year to \$500. The amount of capital gains and losses to include in Wisconsin taxable income is figured on Wisconsin Schedule WD, *Capital Gains and Losses*. Schedule WD is available from any Department of Revenue office or our web site at www.revenue.wi.gov.

NOTE: The examples appearing throughout this publication refer only to the Wisconsin Form 1. Although the differences in reporting capital gain income and loss which are described in this publication are most likely to affect taxpayers filing Form 1, they can also affect Form 1NPR filers. A Form 1NPR filer would make the required adjustments when completing column B of Form 1NPR.

II. DEFINITIONS

A. Short-term and long-term capital gains and losses

Gains or losses resulting from sales or other dispositions of capital assets are classified as either “short-term” or “long-term.” If a capital asset is owned for more than one year, gain or loss resulting from its disposition is “long-term” gain or loss. Gain or loss from an asset held for one year or less is considered “short-term.”

B. Capital loss carryover

Because annual limitations exist regarding the amount of net capital loss which may be deducted against other income in any one taxable year, the entire amount of capital loss determined for a taxable year may not always be fully deductible in such year. The amount of loss exceeding the annual limitation is treated as a “carryover” loss which may be deducted in subsequent years. Losses may be carried forward for an unlimited time, until completely used.

III. CAPITAL GAIN OR LOSS DIFFERENT FOR WISCONSIN AND FEDERAL INCOME

Even though federal adjusted gross income is used as the starting point for computing Wisconsin taxable income, the amounts of capital gain or loss includible in Wisconsin and federal income may differ for a particular taxable year. Differences can occur both in the year a gain or loss is realized and also in carryover years. A difference results in 2009 because a deduction for 30% of the net capital gain from assets held more than one year is allowable when computing Wisconsin taxable income (60% of net capital gain on farm assets). Another difference results in 2009 because of the \$500 limit on the Wisconsin deduction for capital losses. These and other differences are discussed in greater detail in the following paragraphs. Part IV of this publication explains how to report these differences on a 2009 Wisconsin income tax return.

A. A portion of net capital gain from assets held more than one year is deductible for Wisconsin

Capital gains are fully taxable for federal purposes.

Wisconsin law generally allows a deduction for 30% of the net capital gain from assets held more than one year. The deduction is 60% of net long-term capital gain from farm assets.

B. The amount of net capital loss that can be offset against other income on the Wisconsin return is limited to \$500

Under federal law, capital losses are allowed in full against capital gains. If the losses are more than the gains, up to \$3,000 of the excess loss is allowed as a deduction against other income. Capital losses in excess of the amount of the allowable loss may be carried over and used in later years.

Under Wisconsin law, capital losses are allowed in full against capital gains. If the losses are more than the gains, up to \$500 of the excess loss is allowed as a deduction against other income. Capital losses in excess of the amount of the allowable loss may be carried over and used in later years.

As a result of the difference in the amount of excess loss allowable as a deduction for 2009, a larger capital loss carryover may be available for Wisconsin than for federal in later years.

C. Capital gain or loss may be affected when a different election is chosen for federal and Wisconsin purposes

Under federal law, certain elections are allowed regarding the federal tax treatment of some items. For example, gain on an installment sale is generally reported as payments are received, but an election is available to report the entire gain in the year of sale.

A different federal election may be chosen for Wisconsin and federal tax purposes.

Example: An individual sells real estate in Iowa while an Iowa resident. The gain is reported under the installment method for federal income tax purposes. Subsequently, the individual becomes a Wisconsin resident. For Wisconsin purposes, it is assumed that a nonresident individual who sells property located outside Wisconsin elects to report the entire gain in the year of sale, when none of the gain would have been taxable to Wisconsin. Any gain from this installment sale is not taxable for Wisconsin.

Example: For property placed in service after December 31, 1982, and before January 1, 1986, a taxpayer electing to claim the investment tax credit for federal tax purposes either (1) claimed the full 10% credit and reduced the depreciable basis of the property by one-half of such credit, or (2) in the case of regular investment tax credit property, claimed a reduced investment credit and depreciated the full cost of the property. A taxpayer who claimed the higher investment credit for federal tax purposes (and made a reduction in the basis of the depreciable property) was not required to use the reduced basis for computing depreciation for Wisconsin income tax purposes. This may result in a different basis when determining gain or loss on a sale or other disposition of the property.

D. Federal capital losses incurred while a taxpayer was a nonresident of Wisconsin are not deductible for Wisconsin

Wisconsin law does not permit the deduction of any capital losses incurred prior to the date Wisconsin residence is established.

E. Wisconsin and federal income tax basis of certain assets may differ

Because of various differences between Wisconsin and federal law, the Wisconsin basis may not always be the same as the federal basis of property. As a result, the amount of gain or loss included in income when the asset is disposed of will also differ for Wisconsin and federal purposes. Examples of such situations are the following:

1. Property acquired by inheritance has been valued differently for Wisconsin inheritance and federal estate tax purposes. (For example, for federal purposes the alternate valuation date is used, but for Wisconsin the value as of the date of death is required to be used.) This applies only to deaths which occurred before January 1, 1992.
2. Business property has been depreciated at different rates for Wisconsin and federal purposes. Starting in 1975, Wisconsin law was changed to no longer automatically adopt changes made to federal income tax law each year. As a result, in some years different rates of depreciation have had to be used for Wisconsin and federal purposes in the case of certain types of property.
Example: Federal law permits an additional 50% first-year depreciation on certain property. Wisconsin law does not recognize this provision.
3. A tax-option (S) corporation's pre-1979 federal undistributed taxable income, distributions, and tax losses affect a shareholder's federal basis in the stock, but not the Wisconsin basis, since 1979 was the first year to which the Wisconsin tax-option (S) corporation law applies.
4. Beginning with the 1979 taxable year, a shareholder's Wisconsin basis in tax-option (S) corporation stock is adjusted each year. The basis adjustment may not be the same for Wisconsin as for federal purposes or, for 1987 and thereafter, the basis adjustment does not apply if the corpora-

tion elected to opt out of Wisconsin tax-option status. See Publication 102, *Wisconsin Tax Treatment of Tax-Option (S) Corporations and Their Shareholders*, for further information.

F. Gain (loss) may be reportable in different taxable years for Wisconsin purposes than for federal purposes

Changes in federal law may not be effective for Wisconsin until after the year in which they become effective for federal purposes. As a result, capital gain or loss may be reportable in different taxable years for Wisconsin and federal purposes.

Example: A deferred payment sale occurred in 1980. Over 30% of the sales price was received in 1980. The gain on this sale could not be reported under the installment method for Wisconsin tax purposes for 1980 (Wisconsin did not recognize the provisions of the federal Installment Sales Revision Act of 1980 for the 1980 tax year). The gain was taxed in full on a 1980 Wisconsin return. However, for federal purposes, the gain is being reported on the installment method.

G. Capital gain or loss from the exchange of a marital property interest between a surviving spouse and a distributee is not taxable or deductible for Wisconsin

A personal representative of an estate may, under certain conditions, exchange all or a part of the decedent's interest in marital property between a surviving spouse and a distributee. The exchange may result in a taxable gain or a deductible loss for federal tax purposes. Any gain or loss on such an exchange is not taxable or deductible for Wisconsin. (**Note:** The exchange results in a different basis in the property for Wisconsin and federal tax purposes.)

H. Capital gain or loss from a federal S corporation that elects not to be treated as a Wisconsin tax-option corporation is not reportable to Wisconsin

A shareholder of a federal S corporation that elects not to be treated as a Wisconsin tax-option corporation must reverse all items of S corporation income, loss, or deduction included on the federal return and then add his/her pro rata share of any distributions made by the corporation of earnings and profits accumulated during a year in which the corporation was not a tax-option corporation. If a Wisconsin Schedule WD will be completed, a shareholder should not reverse any

item of S corporation income or loss reported on federal Schedule D. These items are removed from Wisconsin income when Wisconsin Schedule WD is completed.

I. Capital gain treatment not available for Wisconsin purposes for a lump-sum distribution from a retirement plan or profit-sharing plan

Under federal law, a taxpayer may elect on federal Form 4972 to compute the tax on the capital gain portion of a lump-sum retirement or profit-sharing plan distribution at a 20% rate. This election is not available for Wisconsin. For Wisconsin purposes, the capital gain portion of a lump-sum distribution reported on federal Form 4972 is treated as ordinary income and must be included on line 4 of Form 1 as an addition to income.

J. Amounts considered long-term capital gain for federal purposes may be short-term capital gain for Wisconsin purposes

Under federal law, gain from the sale of property acquired after June 22, 1984, and before January 1, 1988, is considered long-term capital gain if the property is held for more than 6 months. Under Wisconsin law, gain from the sale of property qualifies for a 30% capital gain exclusion only if the property is held for more than one year (60% if the gain is from the sale of farm assets). Therefore, any gain from an installment sale which occurred prior to 2009 which is long-term capital gain for federal purposes is short-term capital gain for Wisconsin if, at the time of sale, the property had been held for one year or less.

K. Gain on the disposition of small business stock

Both Wisconsin and federal law provide an exclusion for all or a portion of the gain on the disposition of small business stock.

1. Under federal law, an exclusion is allowed for 50% (75% for stock acquired after February 17, 2009, and before January 1, 2011) of the gain on the disposition of certain small business stock (as defined in the Internal Revenue Code) issued after August 10, 1993, and held for more than five years.

The federal exclusion does not apply for Wisconsin.

2. Under Wisconsin law, net capital gain from the disposition of qualified small business stock (as defined in the Wisconsin Statutes) is exempt from Wisconsin tax. The small business stock must have been acquired on or after January 1, 1986, and been held for at least five years. The stock cannot have been acquired by gift or in a stock for stock exchange, and the corporation must have certified that it met certain requirements in order for the stock to qualify for the exemption.

L. Capital loss carryover may be adjusted when the taxpayer excludes income from discharge of indebtedness

Under federal law, income from discharge of indebtedness (cancellation of debts) may be excluded from gross income when the debt is cancelled in a bankruptcy case or during insolvency, or when the debt that is cancelled is qualified farm debt or qualified real property business debt. The excluded amount must generally be used to reduce certain tax attributes in the following order: net operating losses, general business credit carryovers, minimum tax credit, capital loss carryovers, basis of property, passive activity loss and credit carryovers, and foreign tax credit carryovers.

Under Wisconsin law, a taxpayer who excludes income from discharge of indebtedness from gross income must use the amount of the Wisconsin net operating loss, Wisconsin carryover credits, and the Wisconsin capital loss carryover instead of the federal amounts to reduce tax attributes for Wisconsin purposes. As a result, a different amount of capital loss carryover may be available for Wisconsin than for federal purposes.

M. Gain on the sale or disposition of business assets or assets used in farming to a related person

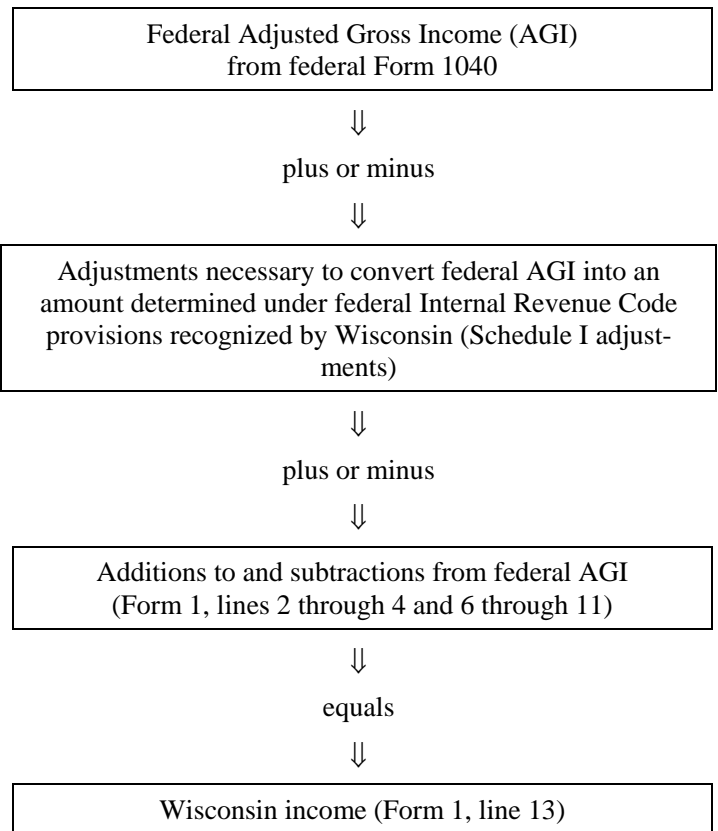
Under Wisconsin law, net capital gain from the sale or other disposition of business assets or assets used in farming to a related person may be deducted when computing Wisconsin taxable income. The deduction only applies to amounts treated as long-term capital gain for federal income tax purposes; it does not apply to gain treated as ordinary income.

The deduction applies to gain on shares in a corporation or trust if, at the time of the sale or disposition, the following standards are met:

- Shareholders of the corporation or beneficiaries of the trust do not exceed 15 in number.
- The corporation or trust does not have more than two classes of shares.
- All shareholders or beneficiaries, other than any estate, are natural persons.

IV. HOW TO REPORT DIFFERENCES BETWEEN WISCONSIN AND FEDERAL CAPITAL GAIN AND LOSS ON THE WISCONSIN RETURN

Before explaining the manner in which capital gain and loss differences are to be reported on the Wisconsin income tax return, it might be helpful to review the steps involved in computing Wisconsin taxable income. The following chart illustrates the steps which an individual must follow in completing a 2009 Wisconsin return.



When an individual's capital gain or loss for Wisconsin differs from the amount includible in federal income, certain adjustments must be made to federal adjusted gross income, the starting point in computing Wisconsin taxable income.

Referring back to Part III of this publication to the listing of the specific reasons (items A through M) that differences occur, each of those differences would be adjusted for in the following manner:

Reason for Difference (See Part III)	Where Adjusted on 2009 Wisconsin Return (Form 1)
A A portion of net capital gain from assets held more than one year is deductible for Wisconsin.	Complete Wisconsin Schedule WD before completing line 10 of Form 1. (Schedule WD does not have to be completed if the only capital gain or loss is a capital gain distribution from a mutual fund or real estate investment trust.)
B The amount of net capital loss that can be offset against other income is limited to \$500.	Complete Wisconsin Schedule WD before completing line 3 of Form 1.
C Capital gain or loss may be affected when a different election is chosen for federal and Wisconsin purposes.	Complete "pro forma" federal return.
D Federal capital losses incurred while a taxpayer was a nonresident of Wisconsin are not deductible for Wisconsin.	Complete Wisconsin Schedule WD.
E(1), (3),(4) Wisconsin and federal income tax basis of certain assets may differ.	Complete Wisconsin Schedule T before making the required adjustment on Schedule WD or on line 4 or 11 as appropriate.
E(2) Wisconsin and federal income tax basis differ because Wisconsin did not adopt federal law change.	Complete Wisconsin Schedule I before completing line 1 of Form 1.
F Gain (loss) may be reportable in different taxable years for Wisconsin purposes than federal purposes.	Complete Wisconsin Schedule I before completing line 1 of Form 1.
G Capital gain or loss from the exchange of a marital property interest between a surviving spouse and a distributee is not taxable or deductible for Wisconsin.	Line 3 or 10, as appropriate. (Complete Wisconsin Schedule WD and Form 4797, if appropriate, if there are additional capital gain or loss transactions.)
H Capital gain (loss) not reportable to Wisconsin when federal S corporation elects not to be treated as a Wisconsin tax-option corporation.	Line 3 or 10, as appropriate. (Complete Wisconsin Schedule WD if there are additional capital gain or loss transactions.)

Reason for Difference (See Part III)	Where Adjusted on 2009 Wisconsin Return (Form 1)
I Capital gain treatment not available for Wisconsin purposes for a lump-sum distribution from a retirement plan or profit-sharing plan.	Line 4.
J Amounts considered long-term capital gain for federal purposes may be short-term capital gain for Wisconsin purposes.	Complete Wisconsin Schedule WD.
K(1) The federal exclusion for 50% (or 75%) of the gain on the disposition of small business stock does not apply.	Complete Wisconsin Schedule I before completing line 1 of Form 1.
K(2) Wisconsin excludes gain on the disposition of small business stock.	Line 10 (Complete Wisconsin Schedule WD if there are additional capital gain or loss transactions.)
L Wisconsin and federal adjustments due to discharge of indebtedness differ.	Complete Wisconsin Schedule WD.
M Gain on the sale or disposition of business assets or assets used in farming to a related person may be deducted.	Line 11

As A through M above illustrate, adjustments to account for differences between the Wisconsin and federal capital gain or loss are to be made in one of five ways, depending on the reason such difference exists. The five methods are:

1. By completing Wisconsin Schedule I before federal income is entered on line 1 of Wisconsin Form 1. (This method is to be used for differences of the type described in paragraphs E(2), F, and K(1) of Part III of this publication.)
2. By completing Wisconsin Schedule WD (Schedule WD of Form 2 for estates and trusts) to compute the amount of capital gain or loss to be included in Wisconsin taxable income. Any adjustment computed on Schedule WD is reflected on line 3 or 10 of Form 1 (line 4 or 9 of Schedule A, Form 2). (This method is used for differences of the type described in paragraphs A, B, D, J, and L of Part III of this publication. It is also used for differences of the type described in paragraphs G, H, and K(2) when the person has additional capital gain or loss transactions.)
3. By making additions to or subtractions from federal income on lines 3, 4, 10, and 11 of Form 1. These additions and subtractions are called "modifications." (This method is to be used for differences of the type

described in paragraphs I and M of Part III. It is also used for differences of the type described in paragraphs G, H, and K(2) when a person does not have any additional capital gain or loss transactions.)

4. By completing Wisconsin Schedule T to determine the required adjustment on line 4 or 11 of Form 1 and the required adjustment to use in completing Wisconsin Schedule WD. (This method is used for differences of the type described in paragraphs E (1), (3), and (4).)
5. By redoing the federal return based on the election chosen for Wisconsin. This recomputed or “pro forma” return is used as the basis for computing Wisconsin taxable income and should be attached to the Wisconsin return when filed. (This method is used for differences of the type described in paragraph C.)

V. HOW SPOUSES SHOULD REPORT CARRYOVER LOSSES ON A 2009 RETURN

A. Spouses file joint return

If you are married and filing a joint return, you and your spouse must combine your capital loss carryovers. On a joint 2009 Wisconsin return, your yearly capital loss deduction limit is \$500.

Example: As the result of losses incurred prior to their marriage in 2009, a married couple has the following long-term capital loss carryovers to 2009:

Wife’s loss carryover to 2009	\$200
Husband’s loss carryover to 2009	\$800

The couple has no capital gain or loss transactions in 2009. On a joint 2009 Wisconsin return the separate loss carryovers of each spouse are combined. A total carryover loss of \$1,000 (\$200 plus \$800) is available. The deduction allowable in computing this couple’s 2009 Wisconsin taxable income is \$500.

B. Spouses file separate returns

If you are married and filing a separate return, your yearly capital loss deduction is limited to \$500. If (1) you and your spouse are filing separate returns for 2009 but filed a joint return for the year in which the capital loss was incurred, or (2) you are a widow(er) and your spouse died before the beginning of your 2009 tax year, you can only deduct the portion of the capital loss carryover that belongs to you. For a capital loss carryover incurred during a year before the Wisconsin marital property law applies to you, title to the property must be used to determine what portion of the loss is yours. For a capital loss carryover incurred during a year to which the marital property law applies, the classification of the property must be used to determine what portion of the loss is yours.

VI. ADDITIONAL INFORMATION

If you have any questions about how capital gains and losses should be reported for Wisconsin income tax purposes, contact any Wisconsin Department of Revenue office or write or call: Customer Service Bureau, Wisconsin Department of Revenue, Mail Stop 5-77, P.O. Box 8949, Madison, WI 53708-8949 (telephone: (608) 266-2772). You may also e-mail your questions to: income@revenue.wi.gov.