

1999 DRAFTING REQUEST

Assembly Amendment (AA-AB133)

Received: **06/11/99**

Received By: **shoveme**

Wanted: **As time permits**

Identical to LRB:

For: **Legislative Fiscal Bureau 7-7417**

By/Representing: **Doty**

This file may be shown to any legislator: **NO**

Drafter: **shoveme**

May Contact:

Alt. Drafters:

Subject: **Tax - individual income**

Extra Copies:

Pre Topic:

LFB:.....Doty -

Topic:

Changes in miscellaneous itemized deductions

Instructions:

See Attached. LFB paper # 106, with attached changes

Drafting History:

<u>Vers.</u>	<u>Drafted</u>	<u>Reviewed</u>	<u>Typed</u>	<u>Proofed</u>	<u>Submitted</u>	<u>Jacketed</u>	<u>Required</u>
/1	shoveme 06/12/99	ygeller 06/13/99	mclark 06/13/99	_____	lrb_docadmin 06/13/99		

FE Sent For:

<END>

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/1	shoveme	1 6/12/99	6/13 MRC	_____	_____	_____	_____
/1 MES 6/12/99				MRC/FS			
FE Sent For:				6/13			
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Shovers, Marc

From: Doty, Kelsie
Sent: Friday, June 11, 1999 9:45 AM
To: Shovers, Marc
Subject: Income tax drafting request

I have six items that need drafts. Give me a call if you need clarification.

1. Paper #100 -- Alt 2. Maintain the current law tax treatment of social security benefits.
2. Paper #101 -- Alt 2. Retain indexing of the income tax brackets. Start indexing the newly created top tax bracket in 2001.
3. ~~Add the provisions of Substitute Amendment T to SB 49 (filing thresholds).~~
4. Paper #106 -- Alt 1 (as modified). Approve the Governor's recommendation to eliminate miscellaneous itemized deductions with two changes.
 - a. Continue to allow professional dues and union dues to be included as a miscellaneous itemized deduction under the credit.
 - b. Create a subtract modification from federal AGI for the amount claimed as a federal miscellaneous itemized deduction for repayment of income that was taxed in a prior year. Specify that the amount claimed under the claim of right credit can not be claimed under the subtraction.
5. ~~Paper #108 -- Alt 1. Modify the current indexing provisions to incorporate the federal indexing method into state law. Specifically, eliminate the maximum income amounts for the standard deduction from the statutes and specify that the tax brackets and standard deduction be indexed based on the 1998 amounts.~~
6. Motion #1407. Modify current law as it relates to the taxation of inter vivos trusts. I'll fax over a copy of the motion and the language that the lobbyist attempted to draft.

Kelsie Doty
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June 7, 1999

Joint Committee on Finance

Paper #106

Individual Income Tax Modifications: Miscellaneous Itemized Deductions (General Fund Taxes -- Individual and Corporate Income Taxes)

[LFB 1999-01 Budget Summary: Page 20, #1]

CURRENT LAW

The itemized deduction credit is equal to 5% of the excess of allowable itemized deductions over the state's sliding scale standard deduction. State itemized deductions generally conform to the expenses permitted as federal itemized deductions and currently include charitable contributions; medical expenses exceeding 7.5% of federal adjusted gross income (AGI); interest expenses for a principal residence or a second home in Wisconsin; interest expenses for property sold on a land contract; other interest expenses, except personal interest; and miscellaneous itemized deductions.

GOVERNOR

Eliminate miscellaneous itemized deductions as eligible expenses under the state's itemized deduction credit. This modification would first apply to tax years beginning on January 1, 2000.

DISCUSSION POINTS

1. The itemized deductions allowed under the state credit generally conform to the federal itemized deductions with two exceptions. First, property taxes paid on a principal residence are claimed for purposes of the state's property tax/rent credit and long-term care insurance premiums are subtracted directly from income, rather than being claimed under the itemized deduction credit. Second, the following itemized deductions may not be claimed for Wisconsin tax purposes: (a) interest paid on a second home located outside of Wisconsin or on a residence that is a boat; (b) interest paid to purchase or hold U.S. Government securities; (c) state income taxes; (d) casualty and theft losses; and (e) moving expenses for moves out of state.

2. Miscellaneous itemized deductions allowed under federal and state law include unreimbursed employe expenses (such as business insurance premiums, travel expenses, professional dues, home office expenses, tools and supplies, and work clothes if not suitable for everyday use), tax preparation fees, repayments of income, safe deposit box rent and legal expenses to produce or collect taxable income. These expenses may be deducted to the extent that they exceed 2% of federal AGI. In addition, casualty and theft losses from income producing property, gambling losses (up to the amount of gambling winnings), unrecovered investments in a pension of a deceased taxpayer and impairment-related work expenses of disabled persons are also deductible as miscellaneous itemized deductions with no limit based on AGI.

3. Of the 43 states, plus the District of Columbia, that imposed an individual income tax in 1997, 10 states did not provide for itemized deductions. Of the remaining 34 states, four provided a different tax treatment of miscellaneous itemized deductions from federal law: California limited the amount of Legislators' travel expenses that could be deducted; Maine required an adjustment of expenses incurred in the production of Maine income; Massachusetts did not allow a deduction for gambling losses; and Oregon limited the deduction for gambling losses to the amount of gambling winnings that were taxable by the state (Oregon exempts state lottery winnings from taxation).

4. The following table provides information on the amount of itemized deductions claimed by Wisconsin taxpayers by type in 1997. This information is from 1997 aggregate data and reflects information reported on the state tax forms. The table shows that of all itemized deductions claimed in 1997, 8.6% was made up of miscellaneous itemized deductions. Of the 2.6 million taxpayers in 1997, approximately 147,100 taxpayers (5.7% of the total) claimed miscellaneous deductions subject to the 2% limit and 22,600 taxpayers (0.9% of the total) claimed miscellaneous deductions that are not subject to the limit. The itemized deduction credit was equal to \$271.9 million in 1997, which is 5% of the amount that allowable itemized deductions (\$7,040.3 million) exceeded the state's sliding scale standard deduction.

Itemized Deductions Claimed in Tax Year 1997

	<u>Count</u>	<u>Amount</u>	<u>% of Amount</u>
Medical and Dental	129,169	\$609,137,357	8.7%
Interest Expenses	734,503	4,033,100,239	57.3
Charitable Contributions	807,873	1,786,590,136	25.4
Misc. Deductions subject to 2% Limit	147,072	509,754,920	7.2
Other Miscellaneous Deductions	<u>22,629</u>	<u>101,702,998</u>	<u>1.4</u>
Total Itemized Deductions	938,786	\$7,040,285,650	100.0%

5. There is limited detailed information available on the types of miscellaneous itemized deductions claimed by Wisconsin taxpayers. According to the 1997 tax sample, 159,100 Wisconsin

taxpayers claimed a total of \$592.3 million in miscellaneous itemized deductions on the federal Schedule A. Of this amount, \$487.6 million (82.3%) were miscellaneous deductions subject to the 2% limit, which included unreimbursed employe expenses (\$351.6 million), tax preparation fees (\$27.9 million) and other deductions (\$108.1 million). A total of 138,500 taxpayers claimed deductions that were subject to the 2% limit.

There were 24,000 taxpayers who claimed \$104.7 million (17.7% of the total) in miscellaneous deductions that were not subject to the 2% limit. Of those individuals, 3,600 taxpayers claimed \$16.2 million in gambling expenses and the remaining \$88.5 million was made up of other miscellaneous deductions.

6. Attachments 1 and 2 to this paper provide distributional information from the 1997 Wisconsin tax sample on the Governor's income tax proposal for tax years 2000 and 2001, respectively, on taxpayers affected by the recommendation to delete miscellaneous itemized deductions. The information in the attachments shows the impact of all of the Governor's proposed income tax modifications, except the proposed homestead credit expansion.

7. The following table compares all taxpayers with a tax decrease or tax increase under the individual income tax modifications recommended by the Governor to only those who are impacted by the provision to eliminate miscellaneous itemized deductions. As shown in the table for the 2001 tax year, about 87% of all taxpayers would have a tax decrease under the bill and 13% would have a tax increase. In contrast, only 57.1% of taxpayers affected by the miscellaneous itemized deduction provision would have a tax decrease and 42.9% would pay more taxes. Taxpayers affected by the miscellaneous itemized deduction provision make up 23.4% of all taxpayers with a tax increase in 2001.

	Count of All Taxpayers Affected by the <u>Governor's Proposal</u>	Percent of <u>Total</u>	Count of Taxpayers Affected by Misc. Itemized <u>Deduction Provision</u>	Percent of <u>Total</u>	Percent of <u>All Taxpayers</u>
Tax Year 2000					
Tax Decrease	1,532,000	80.2%	53,400	39.2%	3.5%
Tax Increase	<u>378,400</u>	<u>19.8</u>	<u>82,700</u>	<u>60.8</u>	<u>21.9</u>
Total	1,910,400	100.0%	136,100	100.0%	7.1%
Tax Year 2001					
Tax Decrease	1,667,000	87.0%	77,500	57.1%	4.6%
Tax Increase	<u>248,300</u>	<u>13.0</u>	<u>58,200</u>	<u>42.9</u>	<u>23.4</u>
Total	1,915,300	100.0%	135,700	100.0%	7.1%

8. Retaining miscellaneous itemized deductions under the itemized deduction credit would reduce income tax revenues by \$25.0 million in tax year 2000 and \$24.5 million in tax year 2001 (in 2000 dollars) from the bill. It should be noted that due to the interaction of the various income tax modification provisions, the fiscal effect of this change would differ if other revisions were made to the Governor's proposal.

9. Since the bill's introduction, the Department of Revenue has requested that a

modification be made to this proposal that would allow repayments of income to be subtracted from federal AGI when calculating Wisconsin AGI. Currently, if an individual repays \$3,000 or less in income that was taxed in a prior year, the amount repaid can be claimed as a miscellaneous itemized deduction (subject to the 2% limit). Repayments of income in excess of \$3,000 are eligible for a state credit. This modification is expected to reduce revenues by a minimal amount.

ALTERNATIVES

1. Approve the Governor's recommendation to eliminate miscellaneous itemized deductions from the calculation of the itemized deduction credit. Provide that the amount claimed as a federal miscellaneous itemized deduction for repayment of income that was taxed in a prior year may be subtracted from federal AGI.

2. Delete the Governor's recommendation and continue to allow miscellaneous itemized deductions to be used on calculating the itemized deduction credit. Compared to the bill, this would reduce income tax revenues by \$25,000,000 in 2000-01 if the other income tax provisions recommended by the Governor are not modified.

Alternative 2	GPR
1999-01 REVENUE (Change to Bill)	- \$25,000,000

Prepared by: Kelsie Doty
Attachments

ATTACHMENT 1

**Distribution of Taxpayers Affected by the Elimination of Miscellaneous Itemized Deduction
With a Tax Increase or Decrease Under the Governor's Income Tax Proposal
Tax Year 2000**

Wisconsin Adjusted Gross Income	Taxpayers With a Tax Decrease				Taxpayers With a Tax Increase			
	Count	% of Count	Amount of Tax Decrease	Average Decrease	Count	% of Count	Amount of Tax Increase	Average Increase
Under \$10,000	400	0.7%	-\$12,000	-\$30	1,800	2.2%	\$42,000	\$23
10,000 to 20,000	600	1.1%	-24,000	-40	2,100	2.5%	223,000	106
20,000 to 30,000	4,500	8.4%	-457,000	-102	4,700	5.7%	863,000	184
30,000 to 40,000	7,300	13.7%	-943,000	-129	11,500	13.9%	2,277,000	198
40,000 to 50,000	9,100	17.0%	-1,184,000	-130	11,900	14.4%	2,573,000	216
50,000 to 60,000	10,000	18.7%	-1,110,000	-111	11,500	13.9%	2,147,000	187
60,000 to 70,000	6,600	12.4%	-449,000	-68	11,100	13.4%	2,499,000	225
70,000 to 80,000	4,200	7.9%	-284,000	-68	8,400	10.2%	1,379,000	164
80,000 to 90,000	4,000	7.5%	-205,000	-51	5,900	7.1%	1,451,000	246
90,000 to 100,000	1,700	3.2%	-134,000	-79	4,000	4.8%	1,073,000	268
100,000 to 200,000	3,900	7.3%	-369,000	-95	8,000	9.7%	2,697,000	337
200,000 to 300,000	600	1.1%	-89,000	-148	900	1.1%	577,000	641
300,000 and Over	500	0.9%	-84,000	-168	900	1.1%	926,000	1,029
TOTALS	53,400	100.0%	-\$5,344,000	-\$100	82,700	100.0%	\$18,727,000	\$226

Comments:
This attachment shows the impact of all of the Governor's proposed income tax modifications, except the homestead credit expansion, on only those taxpayers affected by the provision to eliminate miscellaneous itemized deductions in tax year 2000.

Approximately 136,100 taxpayers would be affected by this provision under the Governor's tax proposal.

Of all affected taxpayers with a tax change, 53,400 (39.2%) would have a tax decrease. The average decrease would be \$100.

Of all affected taxpayers with a tax change, 82,700 (60.8%) would have a tax increase. The average increase would be \$226.

SOURCE: 1997 Wisconsin Tax Sample

Wisconsin Adjusted Gross Income	Taxpayers With a Tax Change			
	Count	% of Count	Amount of Tax Change	Average Change
Under \$10,000	2,200	1.6%	\$30,000	\$14
10,000 to 20,000	2,700	2.0%	199,000	74
20,000 to 30,000	9,200	6.8%	406,000	44
30,000 to 40,000	18,800	13.8%	1,334,000	71
40,000 to 50,000	21,000	15.4%	1,389,000	66
50,000 to 60,000	21,500	15.8%	1,037,000	48
60,000 to 70,000	17,700	13.0%	2,050,000	116
70,000 to 80,000	12,600	9.3%	1,095,000	87
80,000 to 90,000	9,900	7.3%	1,246,000	126
90,000 to 100,000	5,700	4.2%	939,000	165
100,000 to 200,000	11,900	8.7%	2,328,000	196
200,000 to 300,000	1,500	1.1%	488,000	325
300,000 and Over	1,400	1.0%	842,000	601
TOTALS	136,100	100.0%	\$13,383,000	\$98

ATTACHMENT 2

**Distribution of Taxpayers Affected by the Elimination of Miscellaneous Itemized Deduction
With a Tax Increase or Decrease Under the Governor's Income Tax Proposal
Tax Year 2001**

Wisconsin Adjusted Gross Income	Taxpayers With a Tax Decrease				Taxpayers With a Tax Increase			
	Count	% of Count	Amount of Tax Decrease	Average Decrease	Count	% of Count	Amount of Tax Increase	Average Increase
Under \$10,000	1,000	1.3%	-\$17,000	-\$17	1,200	2.1%	\$30,000	\$25
10,000 to 20,000	900	1.2%	-43,000	-48	1,900	3.3%	176,000	93
20,000 to 30,000	5,400	7.0%	-658,000	-122	3,700	6.4%	715,000	193
30,000 to 40,000	9,900	12.8%	-1,321,000	-133	8,800	15.1%	1,817,000	206
40,000 to 50,000	11,000	14.2%	-1,811,000	-165	9,600	16.5%	1,974,000	206
50,000 to 60,000	14,000	18.1%	-1,980,000	-141	7,500	12.9%	1,563,000	208
60,000 to 70,000	10,300	13.3%	-1,135,000	-110	7,300	12.5%	1,843,000	252
70,000 to 80,000	8,100	10.5%	-823,000	-102	4,400	7.6%	899,000	204
80,000 to 90,000	6,700	8.6%	-647,000	-97	3,400	5.8%	1,068,000	314
90,000 to 100,000	2,900	3.7%	-330,000	-114	2,900	5.0%	801,000	276
100,000 to 200,000	5,900	7.6%	-868,000	-147	6,100	10.5%	2,028,000	332
200,000 to 300,000	800	1.0%	-171,000	-214	700	1.2%	493,000	704
300,000 and Over	600	0.8%	-144,000	-240	700	1.2%	843,000	1,204
TOTALS	77,500	100.0%	-\$9,948,000	-\$128	58,200	100.0%	\$14,250,000	\$245

Comments:
This attachment shows the impact of all of the Governor's proposed income tax modifications, except the homestead credit expansion, on only those taxpayers affected by the provision to eliminate miscellaneous itemized deductions in tax year 2001.

Approximately 135,700 taxpayers would be affected by this provision under the Governor's tax proposal.

Of all affected taxpayers with a tax change, 77,500 (57.1%) would have a tax decrease. The average decrease would be \$128.

Of all affected taxpayers with a tax change, 58,200 (42.9%) would have a tax increase. The average increase would be \$245.

SOURCE: 1997 Wisconsin Tax Sample

Wisconsin Adjusted Gross Income	Taxpayers With a Tax Change			
	Count	% of Count	Amount of Tax Change	Average Change
Under \$10,000	2,200	1.6%	\$13,000	\$6
10,000 to 20,000	2,800	2.1%	133,000	48
20,000 to 30,000	9,100	6.7%	57,000	6
30,000 to 40,000	18,700	13.8%	496,000	27
40,000 to 50,000	20,600	15.2%	163,000	8
50,000 to 60,000	21,500	15.8%	-417,000	-19
60,000 to 70,000	17,600	13.0%	708,000	40
70,000 to 80,000	12,500	9.2%	76,000	6
80,000 to 90,000	10,100	7.4%	421,000	42
90,000 to 100,000	5,800	4.3%	471,000	81
100,000 to 200,000	12,000	8.8%	1,160,000	97
200,000 to 300,000	1,500	1.1%	322,000	215
300,000 and Over	1,300	1.0%	599,000	538
TOTALS	135,700	100.0%	\$4,302,000	\$32

Wisconsin Department of Revenue
IS&E Division
February 5, 1999

TITLE: Provide Subtraction for Repayments of Income Previously Taxed

DESCRIPTION OF CURRENT LAW AND PROBLEM:

The Governor's Budget Bill proposes to eliminate the use of miscellaneous itemized deductions in the computation of the Wisconsin itemized deduction credit. The problem is that for persons who reported income in one year and had to repay all or a portion of such income in a later year, they may lose the tax benefit for the repayment.

If the repayment of income previously taxed is more than \$3,000, Wisconsin law allows a credit for such repayment (sec. 71.07(1)). If the repayment is \$3,000 or less and is ordinary income, under federal law the amount of the repayment may only be claimed as a miscellaneous itemized deduction. Wisconsin law currently allows such miscellaneous itemized deduction in the computation of the Wisconsin itemized deduction credit.

For example, a person received \$2,500 of unemployment compensation in 1998. The entire amount is reported as income on his/her 1998 Wisconsin income tax return. The person is required to repay the \$2,500 in year 2000 and reports such amount on federal Schedule A as a miscellaneous itemized deduction. Under the Budget Bill proposal, this person would not be allowed a deduction or credit for the repayment even though the income was previously taxed by Wisconsin.

Note: There may be other types of miscellaneous deductions that are also controversial. For example, a person who reports gambling winnings can only claim gambling losses (up to the amount of winnings) as a miscellaneous itemized deduction, and when a person dies, any unrecovered investment in a pension plan can only be claimed as a miscellaneous itemized deduction.

RECOMMENDATION FOR ACTION:

Create a subtraction in sec. 71.05(6)(b) to allow a subtraction from federal adjusted gross income for the amount claimed as a federal miscellaneous itemized deduction for repayment of an amount included in income in a prior year. The subtraction should apply only to the extent the repayment was previously included in Wisconsin adjusted gross income and to the extent not used in computing the credit under sec. 71.07(1).

FISCAL/ADMINISTRATIVE IMPACT

Unknown, but will decrease revenue.

DRAFTING INSTRUCTIONS:

See Recommendation for Action above.

Post-It [®] Fax Note		7671	Date	6/12	# of pages	2
To	Marc		From	Kelsien		
Co./Dept.			Co.			
Phone #			Phone #			
Fax #			Fax #			

EFFECTIVE DATE OR INITIAL APPLICABILITY

Taxable years beginning on or after January 1, 2000.

PERSON TO CONTACT:

~~Clay Seth~~
266-8920

Prepared by: Marcy Stock
February 5, 1999
I:leg/misc deduction

7-5023



State of Wisconsin
1999 - 2000 LEGISLATURE

LRBb0667/1

MES.....

JG

LFB:.....Doty – Changes in miscellaneous itemized deductions

FOR 1999-01 BUDGET — NOT READY FOR INTRODUCTION

LFB AMENDMENT

TO 1999 ASSEMBLY BILL 133 AND 1999 SENATE BILL 45

1 At the locations indicated, amend the bill as follows:

2 **1.** Page 843, line 19: after that line insert:

3 “SECTION 1688d. 71.05 (6) (b) 29. of the statutes is created to read:

4 71.05 (6) (b) 29. The amount claimed as a federal miscellaneous itemized
5 deduction under the Internal Revenue Code for repayment of an amount included in
6 income in a previous year to the extent that the repayment was previously included
7 in Wisconsin adjusted gross income, except that no amount that is used in calculating
8 the credit under s. 71.07 (1) may be included in the calculation under this
9 subdivision.”



State of Wisconsin
1999 - 2000 LEGISLATURE

LRBb0667/1
MES;jlg:mrc

LFB:.....Doty – Changes in miscellaneous itemized deductions

FOR 1999-01 BUDGET — NOT READY FOR INTRODUCTION

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7 in Wisconsin adjusted gross income, except that no amount that is used in calculating
8 the credit under s. 71.07 (1) may be included in the calculation under this
9 subdivision.”.

