27a

General Fund Taxes

Individual and Corporate Income Taxes

(LFB Budget Summary Document: Page 20)

LFB Summary Items for Which Issue Papers Have Been Prepared

Item #	Title
1	Individual Income Tax Modifications: Taxation of Social Security Benefits (Paper #100)
1	Individual Income Tax Modifications: Rates and Brackets (Paper #101)
1	Individual Income Tax Modifications: Personal Exemptions and Credits (Paper #102)
1	Individual Income Tax Modifications: Eliminate the Property Tax/Rent Credit (Paper #103)
1	Individual Income Tax Modifications: Increase Married Couple Credit (Paper #104)
1	Individual Income Tax Modifications: Working Families Credit (Paper #105)
1	Individual Income Tax Modifications: Miscellaneous Itemized Deductions (Paper #106)
1	Individual Income Tax Modifications: Temporary Tax Reductions (Paper #107)
1	Individual Income Tax: Indexing (Paper #108)
1	Individual Income Tax Modifications: Withholding Table Adjustment (Paper #109)
2&3	Homestead Tax Credit (Paper #110)
4	Earned Income Tax Credit (see Paper #1082 -- TANF)
9	Corporate Income and Franchise Tax--Single-Sales Factor Apportionment Formula (Paper #111)
10	Corporate Income and Franchise Tax -- Combined Reporting (Paper #112)
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11	Development Zone Tax Credit Modifications (Paper #114)
11	Development Zone and Enterprise Development Zone Program Modifications (Paper #115)
-	Internal Revenue Code Update (Paper #116)

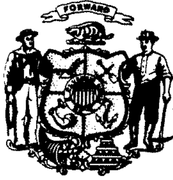
(Gov) Agency: General Fund Taxes - Individual & Corporate Taxes
Taxation of Social Security Benefits

Recommendations:

Paper No. 100: Alternative 1 (no action needed)

Comments: Go with the governor and federalize the tax treatment of social security benefits for people with incomes above $34,000 (single) and $44,000 (married). If you don't do it, you lose $32.4 million.

prepared by: Barry



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June 7, 1999 | Joint Committee on Finance | Paper #100

Individual Income Tax Modifications: Taxation of Social Security Benefits (General Fund Taxes -- Individual and Corporate Income Taxes)

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

CURRENT LAW

Wisconsin currently follows pre-1994 federal law and taxes up to 50% of social security benefits for taxpayers with provisional income above the following thresholds: $25,000 if single, $32,000 if married-joint and zero if married-separate. The taxable portion is the lesser of: (a) one-half of net social security benefits; or (b) one-half of the amount by which provisional income exceeds the threshold amount. Provisional income is defined as one-half of social security plus federal adjusted gross income (AGI), tax-exempt interest and other specified amounts that are excluded from gross income. No benefits are taxed for taxpayers with provisional income below these threshold amounts.

The federal taxation of social security was modified under the Revenue Reconciliation Act of 1993, which increased the amount of taxable social security benefits from 50% to 85% for taxpayers with income above a higher threshold level beginning in 1994. The pre-1994 law still applies to taxpayers with income below $34,000 if single and $44,000 if married filing a joint return. However, the taxable portion of social security for taxpayers with provisional income above these thresholds is the lesser of: (a) 85% of social security; or (b) the amount included under the 1993 law (not to exceed $4,500 if single and $6,000 if married-joint) plus 85% of the excess of provisional income over the income thresholds. Married taxpayers who file separate returns pay taxes on up to 85% of social security benefits.

The following table summarizes the taxation of social security under current state law and under federal law for single and married-joint taxpayers, based on income.

Provisional Income	Taxable Portion Under Current State Law	Taxable Portion Under Federal Law
$0 to $25,000 if Single $0 to $32,000 if Married-Joint	None	None
$25,000 to $34,000 if Single $32,000 to $44,000 if Married-Joint	Up to 50%	Up to 50%
$34,000 and Over if Single $44,000 and Over if Married-Joint	Up to 50%	Up to 85%

GOVERNOR

Federalize the treatment of social security benefits and tax up to 85% of social security for taxpayers with provisional income above $34,000 if single and $44,000 if married-joint and for all married-separate taxpayers. Taxpayers with income below these amounts would not be impacted by the modification.

DISCUSSION POINTS

1. One of the tax policy principles to be considered in structuring an individual income tax is the goal of tax equity, which holds that the tax structure should provide equal treatment of equals and include only reasonable differences in the taxation of unequals. Specifically, the principle of horizontal equity indicates that taxpayers with the same amount of economic income should pay the same amount of tax. Economic income may be adjusted to reflect distinctions for lesser ability to pay taxes, such as unusual medical expenses and casualty losses, or to recognize the higher subsistence costs of taxpayers with large families.

2. It could be argued that both the current state and federal tax treatments of social security benefits violate the principle of horizontal equity because taxpayers with social security income do not pay taxes on all of their income, while a taxpayer with the same total income that is comprised entirely of wages does not receive a similar exclusion. On the other hand, the complete exclusion for social security that is provided to lower-income taxpayers and the partial exclusion provided to upper-income taxpayers could be considered an adjustment to reflect a lesser ability to pay that is typically associated with social security recipients who may have relatively high medical expenses and fixed incomes.

3. A rationale for the current state tax treatment of social security for higher-income taxpayers is that one-half of a worker's combined payroll tax is paid by the employer from before-tax income. The other half is paid by the employe from after-tax earnings. Therefore, higher-income taxpayers are currently taxed on the social security payments attributable to the employer's before-

tax contributions. On the other hand, since retirees generally receive more in benefits than they contributed into the system, it could be argued that increasing the share of taxable social security for retirees with higher income would not impose an undue burden. The rationale used at the federal level when increasing the taxable share to 85% was that the 15% nontaxable share was roughly comparable to the portion of other pension benefits that were not subject to taxation (the portion attributable to after-tax contributions), as estimated at that time by the Congressional Budget Office.

4. Of the 43 states, plus the District of Columbia, that imposed an individual income tax in 1997, 29 exempted all social security benefits from taxation. Fifteen states taxed a portion of social security benefits as follows: three, including Wisconsin, taxed up to 50% of benefits as under pre-1994 federal law; nine followed current federal practice and taxed up to 85%; and three states provided their own taxation scheme. No state taxed 100% of social security benefits.

5. Exempting all social security benefits from taxation would reduce income tax revenues by an estimated $66.5 million each year from current law. As compared to the bill, this would reduce revenues by $98.2 million on an annualized basis.

6. Since the current state treatment of social security does not conform with federal law, taxpayers with income above the higher threshold amounts ($34,000 if single, $44,000 if married-joint and zero if married-separate) are required to complete a separate state worksheet to calculate the difference. The federal worksheet that must be used by most taxfilers with social security income for the 1998 tax year contains 18 steps. The state's social security benefits worksheet requires six steps to be completed to calculate the amount of benefits to be subtracted from federal AGI to determine Wisconsin AGI. Federalizing the treatment of social security would simplify the state tax form for affected taxfilers and the Department.

7. According to data from the Social Security Administration, a total of $7,534 million in social security benefits was paid to Wisconsin residents in 1997. The 1997 Wisconsin tax sample shows that 155,000 Wisconsin residents paid federal taxes on $1,121 million in benefits. For state tax purposes, 95,000 taxpayers subtracted $365.4 million from the federally taxable amount. State taxes were paid on $756 million in benefits.

8. Federalizing the calculation of taxable social security benefits may result in high marginal tax rates on other sources of income for affected taxpayers. For example, under current law, a married couple with $16,000 of social security benefits is not required to include any of these benefits in taxable income if other sources of provisional income are $24,000 or less. Once other sources of provisional income equal $24,000 for these taxpayers (total provisional income equals $32,000), the amount of taxable social security is phased up until it reaches $8,000 when other provisional income is $40,000 or more (the phase-in range is based on the amount of social security benefits and other provisional income and therefore is different for each taxpayer). In this phase-in range, each additional dollar of income from other sources is taxed as if it were $1.50. This effect would be enhanced under the bill because, in the new phase-in range, each additional dollar of income would be taxed as if it were $1.85. It is argued that these provisions create a disincentive for social security recipients to work and penalize individuals who saved for retirement.

9. In addition to federalizing the treatment of social security benefits, the Governor recommends a number of other modifications to the state's individual income tax, including increasing the sliding scale standard deduction, creating personal exemptions, creating a fourth income tax bracket, reducing the income tax rates, eliminating miscellaneous deductions from the itemized deduction credit, increasing the married couple credit, eliminating certain income tax credits and expanding the homestead credit. Many of the tax reduction provisions would offset the effects of the social security provision and even result in a tax decrease for some taxpayers. The other bill provisions are discussed further in separate issue papers prepared by this office.

10. Attachments 1 and 2 to this paper provide distributional information on the Governor's income tax proposal on taxpayers affected by the social security provision for tax years 2000 and 2001, respectively. This information is from the 1997 Wisconsin tax sample, which has data from over 20,000 tax returns, weighted to reflect all taxpayers in 1997. However, changes over time in the number of taxpayers and the kinds and amounts of income, deductions and credits they claim cannot be shown. To the extent possible, changes in tax laws between 1997 and later years have been included.

11. 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 would be impacted by the social security provision. 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 29.2% of taxpayers affected by the social security provision would have a tax decrease and 70.8% would pay more taxes. Taxpayers affected by the social security provision make up 26.8% of all taxpayers with a tax increase in 2001.

	Count of All Taxpayers Affected by Governor's Proposal	Percent of Total	Count of Taxpayers Affected by Social Security Provision	Percent of Total	Percent of All Taxpayers
Tax Year 2000					
Tax Decrease	1,532,000	80.2%	17,900	19.1%	1.2%
Tax Increase	378,400	19.8	75,800	80.9	20.0
Total	1,910,400	100.0%	93,700	100.0%	4.9%
Tax Year 2001					
Tax Decrease	1,667,000	87.0%	27,400	29.2%	1.6%
Tax Increase	248,300	13.0	66,300	70.8	26.8
Total	1,915,300	100.0%	93,700	100.0%	4.9%

12. Deleting the social security provision from the Governor's budget recommendation and retaining the current law tax treatment of social security would reduce income tax revenues by $32.4 million in tax year 2000 and $32.2 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 modifications, the fiscal effect of this change would differ if other revisions are made to the Governor's proposal.

ALTERNATIVES TO BILL

1. Approve the Governor's recommendation to federalize the treatment of social security benefits.

2. Retain the current state income tax treatment of social security benefits. Compared to the bill, this would reduce income tax revenues by $32.4 million 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)	- $32,400,000

Prepared by: Kelsie Doty
Attachments

ATTACHMENT 1

Distribution of Taxpayers Affected by the Social Security Provision 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	Percent of Amount	Average Decrease	Count	Percent of Count	Amount of Tax Increase	Percent of Amount	Average Increase
Under $5,000	0	0.0%	$0	0.0%	$0	0	0.0%	$0	0.0%	$0
5,000 to 10,000	0	0.0%	0	0.0%	0	0	0.0%	0	0.0%	0
10,000 to 15,000	0	0.0%	0	0.0%	0	1,700	2.2%	331,000	1.7%	195
15,000 to 20,000	200	1.1%	-36,000	1.8%	-180	2,000	2.6%	400,000	2.1%	200
20,000 to 25,000	600	3.4%	-44,000	2.2%	-73	2,800	3.7%	616,000	3.2%	220
25,000 to 30,000	800	4.5%	-94,000	4.8%	-118	4,000	5.3%	776,000	4.0%	194
30,000 to 40,000	4,100	22.9%	-426,000	21.7%	-104	9,300	12.3%	2,105,000	10.9%	226
40,000 to 50,000	7,000	39.1%	-895,000	45.6%	-128	12,400	16.4%	2,645,000	13.7%	213
50,000 to 60,000	2,800	15.6%	-266,000	13.6%	-95	14,100	18.7%	3,267,000	16.9%	232
60,000 to 80,000	900	5.0%	-46,000	2.3%	-51	13,400	17.7%	3,872,000	20.0%	289
80,000 to 100,000	300	1.7%	-8,000	0.4%	-27	7,300	9.7%	2,370,000	12.2%	325
100,000 to 200,000	700	3.9%	-47,000	2.4%	-67	6,200	8.2%	1,985,000	10.2%	320
200,000 to 300,000	200	1.1%	-18,000	0.9%	-90	1,200	1.6%	446,000	2.3%	372
300,000 and Over	300	1.7%	-82,000	4.2%	-273	1,200	1.6%	553,000	2.9%	461
TOTALS	17,900	100.0%	-$1,962,000	100.0%	-$110	75,600	100.0%	$19,366,000	100.0%	$256

Wisconsin Adjusted Gross Income	Taxpayers With a Tax Change				
	Count	Percent of Count	Amount of Tax Change	Percent of Amount	Average Change
Under $5,000	0	0.0%	$0	0.0%	$0
5,000 to 10,000	0	0.0%	0	0.0%	0
10,000 to 15,000	1,700	1.8%	331,000	1.9%	195
15,000 to 20,000	2,200	2.4%	364,000	2.1%	165
20,000 to 25,000	3,400	3.6%	572,000	3.3%	168
25,000 to 30,000	4,800	5.1%	682,000	3.9%	142
30,000 to 40,000	13,400	14.3%	1,679,000	9.6%	125
40,000 to 50,000	19,400	20.7%	1,750,000	10.1%	90
50,000 to 60,000	16,900	18.1%	3,001,000	17.2%	178
60,000 to 80,000	14,300	15.3%	3,826,000	22.0%	268
80,000 to 100,000	7,600	8.1%	2,362,000	13.6%	311
100,000 to 200,000	6,900	7.4%	1,938,000	11.1%	281
200,000 to 300,000	1,400	1.5%	428,000	2.5%	306
300,000 and Over	1,500	1.6%	471,000	2.7%	314
TOTALS	93,500	100.0%	$17,404,000	100.0%	$186

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 social security provision in tax year 2000.

According to the 1997 sample, approximately 93,500 taxpayers would be affected by the social security provision under the Governor's proposal.

Of all affected taxpayers with a tax change, 17,900 (19.1%) would have a tax decrease. The average decrease would be $110.

Of all affected taxpayers with a tax change, 75,600 (80.9%) would have a tax increase. The average increase would be $256.

SOURCE: 1997 Wisconsin Tax Sample

ATTACHMENT 2

Distribution of Taxpayers Affected by the Social Security Provision 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: Count	% of Count	Amount of Tax Decrease	Percent of Amount	Average Decrease	Taxpayers With a Tax Increase: Count	Percent of Count	Amount of Tax Increase	Percent of Amount	Average Increase
Under $5,000	0	0.0%	$0	0.0%	$0	0	0.0%	$0	0.0%	$0
5,000 to 10,000	0	0.0%	0	0.0%	0	0	0.0%	0	0.0%	0
10,000 to 15,000	0	0.0%	0	0.0%	0	1,700	2.6%	291,000	2.0%	171
15,000 to 20,000	500	1.8%	-50,000	1.5%	-100	1,800	2.7%	338,000	2.3%	188
20,000 to 25,000	700	2.6%	-64,000	1.9%	-91	2,700	4.1%	511,000	3.4%	189
25,000 to 30,000	1,100	4.0%	-138,000	4.1%	-125	3,700	5.6%	613,000	4.1%	166
30,000 to 40,000	5,600	20.4%	-641,000	19.1%	-114	8,000	12.1%	1,709,000	11.5%	214
40,000 to 50,000	9,700	35.4%	-1,417,000	42.3%	-146	10,800	16.3%	1,979,000	13.3%	183
50,000 to 60,000	4,500	16.4%	-526,000	15.7%	-117	12,200	18.4%	2,392,000	16.1%	196
60,000 to 80,000	1,800	6.6%	-139,000	4.2%	-77	11,400	17.2%	2,995,000	20.1%	263
80,000 to 100,000	1,400	5.1%	-66,000	2.0%	-47	6,300	9.5%	1,852,000	12.4%	294
100,000 to 200,000	1,100	4.0%	-132,000	3.9%	-120	5,700	8.6%	1,441,000	9.7%	253
200,000 to 300,000	400	1.5%	-46,000	1.4%	-115	1,100	1.7%	328,000	2.2%	298
300,000 and Over	600	2.2%	-129,000	3.9%	-215	900	1.4%	450,000	3.0%	500
TOTALS	27,400	100.0%	-$3,348,000	100.0%	-$122	66,300	100.0%	$14,899,000	100.0%	$225

Taxpayers With a Tax Change

Wisconsin Adjusted Gross Income	Count	Percent of Count	Amount of Tax Change	Percent of Amount	Average Change
Under $5,000	0	0.0%	$0	0.0%	$0
5,000 to 10,000	0	0.0%	0	0.0%	0
10,000 to 15,000	1,700	1.8%	291,000	2.5%	171
15,000 to 20,000	2,300	2.5%	288,000	2.5%	125
20,000 to 25,000	3,400	3.6%	447,000	3.9%	131
25,000 to 30,000	4,800	5.1%	475,000	4.1%	99
30,000 to 40,000	13,600	14.5%	1,068,000	9.2%	79
40,000 to 50,000	20,500	21.9%	562,000	4.9%	27
50,000 to 60,000	16,700	17.8%	1,866,000	16.2%	112
60,000 to 80,000	13,200	14.1%	2,856,000	24.7%	216
80,000 to 100,000	7,700	8.2%	1,786,000	15.5%	232
100,000 to 200,000	6,800	7.3%	1,309,000	11.3%	193
200,000 to 300,000	1,500	1.6%	282,000	2.4%	188
300,000 and Over	1,500	1.6%	321,000	2.8%	214
TOTALS	93,700	100.0%	$11,551,000	100.0%	$123

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 social security provision in tax year 2001.

According to the 1997 sample, approximately 93,700 taxpayers would be affected by the social security provision under the Governor's proposal in 2001.

Of all affected taxpayers with a tax change, 27,400 (29.2%) would have a tax decrease. The average decrease would be $122.

Of all affected taxpayers with a tax change, 66,300 (70.8%) would have a tax increase. The average increase would be $225.

SOURCE: 1997 Wisconsin Tax Sample

(Gov) Agency: General Fund Taxes - Individual & Corporate Taxes
Income Tax Rates & Brackets

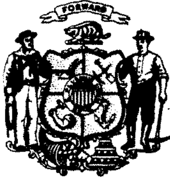
Recommendations:

Paper No. 101: Alternative 2

Comments: Alternative 2 approves the gov's proposal to create a fourth income tax bracket, but retains indexing in tax years 2000 and 2001. It costs $20.6 million, but is a more honest approach to tax cutting.

You could lower the amounts for the fourth bracket (i.e. $125,000 married filing joint) and recoup some of the revenue lost by not suspending indexing.

prepared by: Barry



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June 7, 1999 Joint Committee on Finance Paper #101

Individual Income Tax Modifications: Rates and Brackets (General Fund Taxes -- Individual and Corporate Income Taxes)

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

CURRENT LAW

The individual income tax rates and brackets for tax years 1999, 2000 and 2001 are outlined below. The tax rates were enacted as part of 1997 Wisconsin Act 237 (the 1997-99 budget adjustment act) and first took effect with the 1998 tax year. The rates were 4.9%/6.55%/6.93% from tax year 1987 through 1997. The bracket structure for 1999 reflects one year of indexing over the previous structure, which had been in place since tax year 1987. The 1997-99 biennial budget (1997 Wisconsin Act 27) provided for annual adjustments to the tax brackets for changes in inflation beginning with tax year 1999. Under current law, the brackets will continue to be indexed for tax years 2000 and thereafter.

Current Law Rates and Brackets
Tax Year 1999

Taxable Income Brackets			Marginal
Single	Married-Joint	Married-Separate	Tax Rates
Less than $7,620	Less than $10,160	Less than $5,080	4.77%
7,620 to 15,240	10,160 to 20,320	5,080 to 10,160	6.37
15,240 and Over	20,320 and Over	10,160 and Over	6.77

Estimated Current Law Rates and Brackets
Tax Year 2000

Taxable Income Brackets			Marginal
Single	Married-Joint	Married-Separate	Tax Rates
Less than $7,790	Less than $10,380	Less than $5,190	4.77%
7,790 to 15,580	10,380 to 20,770	5,190 to 10,380	6.37
15,580 and Over	20,770 and Over	10,380 and Over	6.77

Estimated Current Law Rates and Brackets
Tax Year 2001

Taxable Income Brackets			Marginal
Single	Married-Joint	Married-Separate	Tax Rates
Less than $7,970	Less than $10,620	Less than $5,310	4.77%
7,970 to 15,940	10,620 to 21,250	5,310 to 10,630	6.37
15,940 and Over	21,250 and Over	10,630 and Over	6.77

GOVERNOR

Create a fourth income tax bracket and reduce the tax rates in tax years 2000 and 2001. The rate and bracket schedules under the Governor's proposal are shown below. As drafted under the bill, the first three tax brackets would return to the 1998 amounts (the current law amounts prior to any indexing adjustments). Bracket indexing would resume in 2002 and thereafter.

Governor's Proposed Rates and Brackets
Tax Years 2000 and 2001

Taxable Income Brackets			Marginal Tax Rates	
Single	Married-Joint	Married-Separate	2000	2001 and Thereafter
Less than $7,500	Less than $10,000	Less than $5,000	4.73%	4.60%
7,500 to 15,000	10,000 to 20,000	5,000 to 10,000	6.33	6.15
15,000 to 112,500	20,000 to 150,000	10,000 to 75,000	6.55	6.50
112,500 and Over	150,000 and Over	75,000 and Over	6.75	6.75

DISCUSSION POINTS

1. The administration indicates that the intent was for the tax brackets to be maintained at their 1999 levels for tax years 2000 and 2001 and their fiscal estimate of the bill modifications reflects the 1999 brackets. The intended tax brackets are shown below. An amendment would need to be adopted to reflect the Governor's intent. This modification would increase the cost of the bill by $4.8 million in tax year 2000 and $5.2 million in 2001. The withholding table adjustment would reduce revenues by an additional $2.2 million for a total cost of $7.1 million in the 2000-01 fiscal year as compared to the reestimates of the bill. Due the interaction of the various income tax modifications proposed in the bill, the fiscal effect of this change and other changes would differ if other revisions are made to the Governor's proposal.

Governor's Intended Rates and Brackets
Tax Years 2000 and 2001

Taxable Income Brackets			Marginal Tax Rates	
Single	Married-Joint	Married-Separate	2000	2001 and Thereafter
Less than $7,620	Less than $10,160	Less than $5,080	4.73%	4.60%
7,620 to 15,240	10,160 to 20,320	5,080 to 10,160	6.33	6.15
15,240 to 112,500	20,320 to 150,000	10,160 to 75,000	6.55	6.50
112,500 and Over	150,000 and Over	75,000 and Over	6.75	6.75

2. The tax brackets could continue to be indexed for changes in inflation in 2000 and 2001 as shown below. The first three bracket amounts would be the same as under current law. The top brackets for 2000 reflect the statutory amounts proposed in the bill and the top brackets for 2001 reflect one year of indexing over the 2000 amounts. An alternative to not suspend indexing in 2000 and 2001 would increase the cost of the proposal by an estimated $11.4 million in tax year 2000 and $20.5 million in 2001 and withholding adjustments would increase the cost by an additional $9.2 million in the first year. In total, this option would reduce revenues by an estimated $20.6 million in the 2000-01 fiscal year. It should be noted that since the tax brackets in 2001 would be higher under this option than under the bill (as intended), income tax collections in tax years 2002 and thereafter would also be lower.

Alternative to Continue Indexing
the Governor's Intended Brackets
Tax Year 2000

Taxable Income Brackets			Marginal
Single	Married-Joint	Married-Separate	Tax Rates
Less than $7,790	Less than $10,380	Less than $5,190	4.73%
7,790 to 15,580	10,380 to 20,770	5,190 to 10,390	6.33
15,580 to 112,500	20,770 to 150,000	10,390 to 75,000	6.55
112,500 and Over	150,000 and Over	75,000 and Over	6.75

Tax Year 2001

Taxable Income Brackets			Marginal Tax Rates
Single	Married-Joint	Married-Separate	
Less than $7,970	Less than $10,620	Less than $5,310	4.60%
7,970 to 15,940	10,620 to 21,250	5,310 to 10,630	6.15
15,940 to 115,090	21,250 to 153,450	10,630 to 76,730	6.50
115,090 and Over	153,450 and Over	76,730 and Over	6.75

3. Of the 43 states, plus the District of Columbia, that imposed an individual income tax in 1997, seven imposed a flat tax rate on all taxable income ranging from 2.8% in Pennsylvania to 6.0% in Tennessee. The state of Massachusetts had four flat tax rates, each of which was applied to different sources of income and three states incorporated the federal tax brackets by calculating the state tax as a percentage of federal tax liability.

The remaining states used a marginal rate and bracket structure. The lowest rate ranged from less than 1.0% (four states) to 6.0% (in four other states), and the top tax rate ranged from 3.0% in Illinois to 11% in Montana. The number of tax brackets also varied from two in Connecticut to 11 in Oklahoma. Finally, the point at which the top tax rate takes effect was significantly different. Maryland had four tax brackets with the top bracket at $3,000 for all taxpayers. On the other hand, Arizona's top bracket, the fifth, was $300,000 for married-joint taxpayers ($150,000 if single).

4. The tax rates could be increased or decreased from the rates provided in the bill to modify the amount of income tax collections. A change in the lowest tax rate would impact all taxpayers, whereas a change in the top tax rate would only affect those taxpayers with taxable income in the top tax bracket. An across-the-board rate change would affect all taxpayers proportionately to their income.

5. The tax brackets could also be modified. For example, lowering the proposed top tax bracket ($150,000 for married-joint taxpayers) would increase the amount of income tax collections from the amounts provided in the bill. Alternatively, raising the top bracket amounts would reduce income tax revenues.

ALTERNATIVES

This paper provides alternatives to the bill to incorporate the Governor's intent and to retain indexing. There are an unlimited number of other rate and bracket options that could be adopted by the Committee.

1. Adopt the Governor's recommendation to create a fourth income tax bracket and reduce the tax rates in tax years 2000 and 2001. In addition, modify the provision to incorporate the Governor's intent to maintain the 1999 tax brackets in tax years 2000 and 2001 rather than the 1998

amounts. This alternative would reduce income tax revenues by $7,100,000 in 2000-01 from the reestimates of the bill if the other income tax provisions recommended by the Governor are not modified.

Alternative 1	GPR
1999-01 REVENUE (Change to Base)	- $7,100,000

2. Modify the Governor's recommendation by continuing to index the tax brackets in tax years 2000 and 2001. This alternative would reduce income tax revenues by $20,600,000 in 2000-01 from the reestimates of the bill if the other income tax provisions recommended by the Governor are not modified.

Alternative 2	GPR
1999-01 REVENUE (Change to Base)	- $20,600,000

Prepared by: Kelsie Doty

(Gov) Agency: General Fund Taxes - Individual & Corporate Taxes
Personal Exemptions and Credits

Recommendations:

Paper No. 102: Alternatives 4 & 7

Comments: I would maintain current law and retain the dependent and senior credits. The gov's personal exemption is expensive and not necessarily progressive.

prepared by: Barry

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June 7, 1999 | Joint Committee on Finance | Paper #102

Individual Income Tax Modifications: Personal Exemptions and Credits (General Fund Taxes -- Individual and Corporate Income Taxes)

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

CURRENT LAW

Under current law, Wisconsin provides a $50 credit for each dependent of the taxpayer. The taxpayer or spouse are not eligible for the credit. The state also provides a $25 credit for taxpayers who are 65 years of age or older. For married couples filing a joint return, a total of $50 may be provided if both individuals are over 65. Beginning with the 1997 tax year, the senior credit is phased out for married taxpayers filing joint returns with Wisconsin adjusted gross income (AGI) over $40,000, single taxpayers with AGI over $30,000 and married-separate taxpayers with AGI over $20,000. The credit phases out over the next $1,000 in income until it is eliminated. Both the dependent and senior credits are nonrefundable; that is, they may be used to reduce tax to zero, but a check from the state is not provided if the amount of the credit exceeds tax liability.

GOVERNOR

Eliminate the dependent and senior credits and, instead, provide personal exemptions beginning in tax year 2000. For the 2000 tax year, a $600 personal exemption would be provided for each taxpayer, the taxpayer's spouse and for each dependent. The personal exemption would increase to $700 in tax year 2001 and thereafter.

Provide an additional $200 exemption in tax year 2000 for each taxpayer who has reached age 65 before the end of the tax year (two exemptions would be provided if both the taxpayer and their spouse are 65 at the end of the year). The additional exemption would be increased to $250 for tax year 2001 and thereafter. Thus, for each taxpayer age 65 or over the total exemption would be $800 in 2000 and $950 in 2001 and thereafter.

Individuals who can be claimed as a dependent on another person's return would not be eligible for a personal exemption.

DISCUSSION POINTS

1. The personal exemptions proposed under the bill would be subtracted, along with the standard deduction, from Wisconsin AGI in calculating Wisconsin taxable income, which is the amount of income subject to tax. Wisconsin taxable income is multiplied by the applicable tax rates to arrive at gross tax. Finally, credits are subtracted from gross tax to arrive at net tax liability, which is the amount of tax due to the state. The current law dependent credit and the proposed personal exemption are a means to account for family size in the calculation of the amount of tax owed. The senior credit and proposed senior exemption are a way to account for a lesser ability to pay taxes due to a fixed income and higher medical expenses that may be experienced by senior taxpayers.

2. At the federal level, a family size adjustment is made by providing a $2,700 personal exemption for the taxpayer, spouse and dependent in 1998. The federal personal exemption is increased for changes in inflation and is projected to be $2,750 in 1999. In addition, a higher standard deduction above the regular standard deduction is provided for each federal taxpayer age 65 and over. The higher standard deduction is $850 per person for married-joint and married-separate taxpayers and $1,050 for single and head-of-household taxpayers in 1998. Although also indexed for changes in inflation, these amounts are not expected to change in 1999.

3. Of the 43 states, plus the District of Columbia, that imposed an individual income tax in 1997, all but four (Louisiana, New York, Pennsylvania and Wisconsin) provided a personal exemption or credit for the taxpayer or spouse and all but four (Connecticut, New Hampshire, Pennsylvania and Tennessee) provided an exemption or credit for each dependent. Finally, thirty states also provided an additional exemption or credit for senior citizens. In general, 34 states provided these tax benefits in the form of an exemption and nine provided a credit.

Personal Exemptions

4. Although all taxpayers would be eligible for a $600 personal exemption in 2000 and a $700 personal exemption in 2001 and thereafter, the exemption's impact on tax liability would be different based on which tax bracket the individual's taxable income falls in. The following chart shows the income tax rates and brackets under the bill.

Governor's Proposed Rates and Brackets
Tax Years 2000 and 2001

Taxable Income Brackets			Marginal Tax Rates	
Single	Married-Joint	Married-Separate	2000	2001 and Thereafter
Less than $7,500	Less than $10,000	Less than $5,000	4.73%	4.60%
7,500 to 15,000	10,000 to 20,000	5,000 to 10,000	6.33	6.15
15,000 to 112,500	20,000 to 150,000	10,000 to 75,000	6.55	6.50
112,500 and Over	150,000 and Over	75,000 and Over	6.75	6.75

5. The $700 personal exemption in 2001 would be worth $32 for taxpayers in the lowest tax bracket. This amount is derived by multiplying the exemption amount by the taxpayer's marginal tax rate as follows: $700 x 4.60% = $32. However, the $700 personal exemption would be worth $47 for taxpayers in the top tax bracket, calculated as follows: $700 x 6.75% = $47. The table below shows the value of the proposed personal exemption for each tax bracket in 2000 and 2001.

	Value of Personal Exemption Based on Taxable Income Bracket			
	1st Bracket	2nd Bracket	3rd Bracket	4th Bracket
$600 Exemption in 2000	$28	$38	$39	$41
$700 Exemption in 2001	32	43	46	47

6. Since credits are calculated after the tax rates and brackets are applied, the dependent credit provided under current law is the same for each dependent, regardless of income. In contrast, the value of the proposed personal exemptions would increase as the taxpayer's income rises. Therefore, it can be argued that replacing the current credit with an exemption would add an element of regressivity to the income tax.

7. The bill could be modified to replace the personal exemptions with a $40 credit in 2000 and a $46 credit in 2001. These amounts represent the value of the proposed personal exemption for the majority of taxpayers. A $40 credit was used in 2000 so that no taxpayer in the third bracket would pay more taxes under this alternative ($40 reflects "rounding-up" the value of the $600 exemption in 2000). Under this option, taxpayers in the first and second brackets would have a tax decrease and individuals in the top tax bracket would pay more taxes. The alternative would reduce income tax revenues by an estimated $8.6 million in tax year 2000 and $9.2 million in 2001 from the amounts provided in the bill. Due the interaction of the various income tax modifications proposed in the bill, the fiscal effect of this change and other changes would differ if other revisions are made to the Governor's proposal.

8. The table above also shows that the exemption would be worth less than the current $50 dependent credit, even for taxpayers in the top tax bracket. However, taxpayers would still receive a tax decrease under the bill because the proposed personal exemption would be provided for the taxpayer and spouse, who are currently not eligible for the dependent credit. An alternative

to retain the $50 dependent credit and to extend the credit to the taxpayer and spouse would increase the cost of the Governor's proposal by an estimated $49.8 million in tax year 2000 and $25.6 million in tax year 2001.

9. If the proposed personal exemption were deleted from the bill and the current law dependent credit were retained, it would increase revenues by an estimated $90.2 million in tax year 2000 and $115.4 million in 2001.

Senior Exemption

10. The same observations related to the proposed personal exemption also apply to the senior exemption. The $250 personal exemption in 2001 would be worth $12 for taxpayers in the lowest tax bracket ($250 x 4.60% = $12), whereas the same exemption would be worth $17 for taxpayers in the top tax bracket ($250 x 6.75% = $17). The table below shows the value of the proposed senior exemption for each tax bracket in 2000 and 2001.

	Value of Senior Exemption Based on Taxable Income Bracket			
	1st Bracket	2nd Bracket	3rd Bracket	4th Bracket
$200 Exemption in 2000	$9	$13	$13	$14
$250 Exemption in 2001	12	15	16	17

11. As with the personal exemption, the bill could be modified to replace the senior exemption with a $14 credit in 2000 and a $17 credit in 2001 at an estimated cost of $700,000 in tax year 2000 and $800,000 in tax year 2001. These credit amounts are the value of the proposed senior exemption for the majority of taxpayers "rounded-up" so there would be no taxpayers in the third bracket with an increase.

12. Again, as in the case of the personal exemption, the value of the proposed senior exemption would be worth less than the current $25 senior credit. However, all senior taxpayers would be eligible for the exemption regardless of income under the bill (as noted above, the senior credit is currently limited to taxpayers with income below certain thresholds). It would cost an estimated $2.1 million in tax year 2000 and $1.3 million in tax year 2001 to return to current law and retain the $25 senior credit for lower-income seniors. An option to retain the $25 credit and extend it to senior taxpayers at all income levels would cost an estimated $3.8 million in tax year 2000 and $3.0 million in tax year 2001 as compared to the bill.

Filing Thresholds

13. Under current law, individuals and married couples are not required to file a state individual income tax return unless their gross income exceeds a threshold amount established by the Department of Revenue (DOR) according to statutory guidelines. The current filing thresholds equal the maximum state standard deduction and an additional amount to reflect the senior citizen credit. The Department may adjust the thresholds annually to reflect changes in the standard deduction, senior credit and tax rates.

14. The current filing thresholds do not reflect the working families credit because statutory authority to do so was not granted when the credit was created. In addition, the bill would not grant authority for the thresholds to be adjusted to reflect the proposed personal exemption and senior exemption.

15. In April of 1999, the Joint Committee on Finance recommended Substitute Amendment 1 to 1999 Senate Bill 49 for passage. The substitute amendment directs DOR to annually adjust the filing thresholds to reflect the gross income level at which no taxpayer would have a state tax liability. The thresholds would be based on whether the taxpayer is filing a single, head-of-household, married-joint or married separate return and whether the taxpayer is 65 years of age or over. The substitute amendment was passed by the Senate on May 18.

16. The budget bill could be modified to incorporate the provisions of the substitute amendment to SB 49. This would allow DOR to adjust the filing thresholds to reflect the personal exemptions and senior exemptions, if enacted into law. It would also allow DOR to adjust the filing thresholds to reflect the working families credit in tax year 1999 and thereafter if the credit is retained. This modification would not be necessary if SB 49 is enacted into law prior to the Fall of 1999.

ALTERNATIVES

1. Adopt the Governor's recommendation to eliminate the dependent and senior credits and provide a $600 personal exemption in 2000 and a $700 personal exemption in 2001 and thereafter. Also, provide an additional $200 senior exemption in 2000 and a $250 exemption in 2001 and thereafter.

Personal Exemption

2. Modify the Governor's recommendation by eliminating the proposed personal exemption and providing a $40 personal exemption credit in 2000 and a $46 personal exemption credit in 2001 and thereafter at a cost of $8,600,000 in 2000-01. The personal exemption credit would be provided for the taxpayer, the taxpayer's spouse and each dependent.

Alternative 2	GPR
1999-01 REVENUE (Change to Bill)	- $8,600,000

3. Modify the Governor's recommendation by eliminating the proposed personal exemption and providing a $50 personal exemption credit in 2000 and thereafter at an estimated cost of $49,800,000 in 2000-01. The personal exemption credit would be provided for the taxpayer, the taxpayer's spouse and each dependent.

Alternative 3	GPR
1999-01 REVENUE (Change to Bill)	- $49,800,000

4. Maintain current law. Under this alternative, the proposed personal exemption would be deleted and the $50 dependent credit would be retained. The dependent credit is only provided for each dependent of the taxpayer. This alternative would increase revenues by an estimated $90,200,000 in 2000-01.

Alternative 4	GPR
1999-01 REVENUE (Change to Bill)	$90,200,000

Senior Exemption

5. Modify the Governor's recommendation by eliminating the proposed senior exemption and providing a $14 senior credit in 2000 and a $17 senior credit in 2001 and thereafter at an estimated cost of $700,000 in 2000-01. The credit would be provided to all taxpayers who are 65 or older, regardless of income.

Alternative 5	GPR
1999-01 REVENUE (Change to Base)	- $700,000

6. Modify the Governor's recommendation by eliminating the proposed senior exemption and providing a $25 senior credit in 2000 and thereafter for all taxpayers who are 65 or older, regardless of income. This alternative would reduce income tax revenues by an estimated $3,800,000 in 2000-01.

Alternative 6	GPR
1999-01 REVENUE (Change to Base)	- $3,800,000

7. Maintain current law. Under this alternative, the proposed senior exemption would be deleted and the $25 senior credit would be retained for lower-income taxpayers. Revenues would be reduced by an estimated $2,100,000 in 2000-01 under this alternative.

Alternative 7	GPR
1999-01 REVENUE (Change to Bill)	- $2,100,000

Filing Threshold

8. Allow DOR to adjust the filing thresholds to reflect the gross income level at which no taxpayer would have a state tax liability.

Prepared by: Kelsie Doty

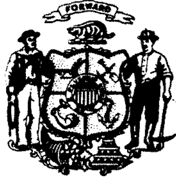
(Gov) Agency: General Fund Taxes - Individual & Corporate Taxes
Eliminate the Property Tax/Rent Credit

Recommendations:

Paper No. 103: Alternative 2 or 3

Comments: I would maintain current law and retain the property tax rent credit (i.e. Alternative 2). In fact, I would recommend increasing the amount of money available for the property tax rent credit (i.e. alternative 3).

prepared by: Barry



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June 7, 1999 | Joint Committee on Finance | Paper #103

Individual Income Tax Modification: Eliminate the Property Tax/Rent Credit (General Fund Taxes -- Individual and Corporate Income Taxes)

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

CURRENT LAW

With the exception of tax year 1998, a property tax/rent credit (PTRC) equal to 10% of property taxes or rent constituting property taxes paid on a principal residence up to a maximum of $2,000 in property taxes or rent is provided under the state individual income tax. The maximum credit is $200. The PTRC was increased to 14% of property taxes or rent constituting property taxes up to a maximum of $2,500 in taxes ($350 maximum credit) on a one-time basis in tax year 1998.

For homeowners, the credit is equal to 10% (14% in 1998) of property taxes paid on a principal residence during the tax year. The credit is available to renters based on 10% (14% in 1998) of rent constituting property taxes. "Rent constituting property taxes" is defined as 25% of actual rent if payment for heat is not included in rent or 20% of actual rent if payment for heat is included in rent.

GOVERNOR

Eliminate the PTRC beginning in tax year 2000.

DISCUSSION POINTS

1. In determining federal tax liability, individuals are able to deduct the larger of federal itemized deductions or the federal standard deduction from federal adjusted gross income (AGI). Property taxes are an allowable itemized deduction and there is no limit on the amount of property taxes that can be deducted. However, individuals whose federal AGI exceeds a threshold amount are required to reduce the amount of certain itemized deductions, including property taxes.

2. Of the 43 states, plus the District of Columbia, that imposed an individual income tax in 1997, 40 provided either a credit or income deduction for property taxes and/or rent paid. Of these states, 33 provided an itemized deduction or credit for property taxes only, one state provided an income deduction only for rent paid and six states offered a deduction or credit for both property taxes and rent. A credit was used in five states, 28 states provided an itemized deduction, one state provided a separate deduction and six states provided both a credit and a deduction. Four states did not provide a credit or deduction for property taxes or rent.

3. The state's PTRC was first established in Chapter 1, Laws of 1979 and became effective with the 1979 tax year. Previously, property taxes were allowed as a state itemized deduction. The credit was created in order to respond to three concerns: (a) the property tax deduction was regressive because the amount of tax benefit a taxpayer received was based on their top marginal tax rate and thus increased as income rose; (b) as an itemized deduction it was not available to nonitemizers; and (c) the deduction was not available to renters.

4. In 1979, the PTRC was equal to 12% of property taxes or rent constituting property taxes. The credit percentage was gradually decreased from 12% in 1979 to 6.9% in 1987 and then increased to the current 10% rate in 1989. There was no maximum credit until the $2,000 limit was established beginning in 1988.

5. 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 would be impacted by the provision to eliminate the PTRC. 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. The share of taxpayers with an increase or decrease who would be affected by the elimination of the PTRC is similar: 85.5% would have a tax decrease and 14.5% would pay more taxes. The distribution is similar because the PTRC is a broader tax provision (affecting 81.0% of all taxpayers in 2001), as compared to federalizing the treatment of social security benefits and eliminating miscellaneous itemized deductions.

	Count of All Taxpayers Affected by the Governor's Proposal	Percent of Total	Count of Taxpayers Affected by the Elimination of the PTRC	Percent of Total	Percent of All Taxpayers
Tax Year 2000					
Tax Decrease	1,532,000	80.2%	1,210,400	77.7%	79.0%
Tax Increase	378,400	19.8	347,400	22.3	91.8
Total	1,910,400	100.0%	1,557,800	100.0%	81.5%
Tax Year 2001					
Tax Decrease	1,667,000	87.0%	1,325,700	85.5%	79.5%
Tax Increase	248,300	13.0	225,500	14.5	90.8
Total	1,915,300	100.0%	1,551,200	100.0%	81.0%

6. An alternative to restore the PTRC to 10% of property taxes or rent up to $2,000

($200 maximum credit) would reduce projected income tax revenues by $247.4 million in tax year 2000 and $245.1 million in 2001 from the bill. Another option would be to restore the PTRC, but at the level established on a one-time basis in 1998: 14% of property taxes or rent up to $2,500 ($350 maximum). This option would reduce revenues by an estimated $374.6 million in 2000 and $372.4 million in 2001 from the amounts in the bill.

7. Since the individual income tax provisions contained in the bill would retain the itemized deduction credit (with a modification to eliminate miscellaneous deductions), the bill could be modified to allow up to $2,000 in property taxes and rent constituting property taxes to be claimed under the state's itemized deduction credit (taxpayers who do not claim federal itemized deductions may still claim the state credit). The credit is equal to 5% of the amount by which itemized deductions exceed the state's standard deduction. Since the amount of the itemized deduction credit is based a flat percentage it is not as regressive as the pre-1979 itemized deductions. However, this option would provide a smaller tax benefit than the current law PTRC since the itemized deduction credit is 5% of expenses rather than 10% and the amount of any allowable standard deduction would be subtracted. This alternative would reduce income tax revenues by $53.9 million in tax year 2000 and $52.4 million in 2001 from the bill.

ALTERNATIVES

1. Adopt the Governor's recommendation to eliminate the PTRC effective with the 2000 tax year.

2. Delete the Governor's recommendation and retain the current law PTRC (10% of property taxes or rent up to $200). This alternative would reduce income tax revenues by an estimated $247,400,000 in 2000-01 if the other income tax provisions recommended by the Governor are not modified.

Alternative 2	GPR
1999-01 REVENUE (Change to Base)	- $247,400,000

3. Delete the Governor's recommendation and retain the PTRC at the level established for the one-time credit in 1998 (14% of property taxes or rent up to $350). This alternative would reduce income tax revenues by an estimated $374,600,000 in 2000-01 if the other income tax provisions recommended by the Governor are not modified.

Alternative 3	GPR
1999-01 REVENUE (Change to Base)	- $374,600,000

4. Adopt the Governor's recommendation with a modification to allow up to $2,000 in property taxes or rent constituting property taxes paid on a principal residence to be claimed under

the itemized deduction credit. This alternative would reduce income tax revenues by an estimated $53,900,000 in 2000-01 if the other income tax provisions recommended by the Governor are not modified.

Alternative 4	GPR
1999-01 REVENUE (Change to Base)	- $53,900,000

Prepared by: Kelsie Doty