STATE OF WISCONSIN

REPORT OF THE JOINT SURVEY COMMITTEE ON TAX EXEMPTIONS

2003 SENATE BILL 346

[Introduced by Senators Kedzie, Reynolds, A. Lasee, Roessler, Lazich, Kanavas, Schultz, Stepp and Coggs; cosponsored by Representatives Nass, Gunderson, Ziegelbauer, Suder, Towns, Ladwig, Taylor, Krawczyk, Bies, F. Lasee, Pope-Roberts, Vrakas, Jeskewitz, Gronemus, Pettis, Kreibich, Townsend, Petrowski, Weber, Lothian, Johnsrud, Musser, Nischke, Schooff, Gottlieb, Grothman, Hundertmark, Stone, Gundrum, Hines, Rhoades, M. Lehman, Freese, Colon, J. Wood, Loeffelholz and Albers.]

General Nature of Proposal

The federal Internal Revenue Code authorizes states to establish, and persons to contribute to, a qualified tuition program. Accounts established under these programs grow tax free if the amounts in the accounts are used for certain qualified educational expenses. These programs are commonly referred to as "section 529 plans" in reference to that section of the Code under which they are authorized. Under current state law, persons may open an account in the state's section 529 plan, known as EdVest II. Contributions to such an account under EdVest II may be deducted from a contributor's income, up to a limit of $3,000 each year for each beneficiary, in the calculation of the contributor's state income taxes if the beneficiary of the account is either the claimant, the claimant's child and dependent, or the claimant's grandchild.

The bill modifies the state's income tax law to authorize an income tax deduction as provided under current law for contributions to the section 529 plan of any state, not just Wisconsin's.

The provisions of the bill would first apply to taxable years beginning on January 1, 2004, unless the bill passes after July 31, 2004, in which case they would first apply to tax years beginning January 1, 2005.

Legality Involved

There are no questions of legality involved.

Fiscal Effect Upon the State and Its Subdivisions

The Department of Revenue explains the fiscal effect of the bill as follows:

> According to limited information received from the College Savings Plans Network and the college savings plan programs in several states, about 0.75% of the total section 529 accounts in each state, other than Wisconsin, are owned by Wisconsin residents. Therefore, Wisconsin residents own an estimated 41,200 section 529 accounts in states other than Wisconsin. The average annual contribution made by parents to an EdVest account is $2,300. Assuming that each of the 41,200 account owners annually contribute $2,300 to an account, under the proposed bill, $94.8 million (41,200 X $2,300) in contributions would be excluded from

income. Assuming an average marginal tax rate of 5.5%, this would result in a decrease in income tax revenue of $5.2 million ($94.8 million X .055). However, this estimate is based on limited information, and therefore, the fiscal effect of the proposed bill could be much higher or lower.

According to EdVest, there are many requests from EdVest account owners to move their dollars to the Virginia program, the largest section 529 program. This may be a sign that encouraging investments in the section 529 plans of other states could lead to a decrease in participation in the EdVest program over time.

The proposed bill would provide an incentive for Wisconsin residents to invest in section 529 plans in other states and therefore, the number of accounts held by Wisconsin taxpayers would increase. The number of these accounts is also expected to increase with the growing popularity of these accounts. If both these scenarios occur, the revenue loss could grow to a substantially higher amount in future years.

Public Policy Involved

The bill is good public policy if it is amended to provide that the provisions of the bill first apply to taxable years beginning on January 1, 2005.