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**Testimony on AB 406**  
**Assembly Committee on Ways and Means**  
**Thursday, September 28<sup>th</sup>, 2023**

Thank you Representative Macco and Assembly Ways and Means Committee members for allowing me to testify in support of Assembly Bill 406 (AB 406).

Senator Marklein and I worked together on this legislation, which updates state tax references to the Internal Revenue Code (IRC), and provides additional clarity to tax-preparers and taxpayers.

State references to federal law provide greater simplicity for taxpayers in preparing returns and reduce the administrative burden and cost for both taxpayers and Department of Revenue (DOR) in assuring compliance with tax laws. The IRC references are used to determine which items of income are subject to taxation prior to specific state modifications.

This highly technical bill has been drafted in consultation with DOR and the Legislative Fiscal Bureau (LFB). Under current law, state tax references generally refer to the code in effect on December 31, 2020.

AB 406 updates many IRC references in response to a variety of federal legislation enacted during 2021 and 2022.

In conversations with DOR and other stakeholders, we have identified several items in the legislation that required updating. Assembly Substitute Amendment 1 is the result of those conversations.

Thank you again for allowing me to provide testimony in support of AB 406. I am available to answer any questions you may have.



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# HOWARD MARKLEIN

STATE SENATOR • 17<sup>TH</sup> SENATE DISTRICT

**September 28, 2023**

## **Assembly Committee on Ways and Means Testimony on Assembly Bill 406**

Good morning!

Thank you Chair Macco and committee members for hearing Assembly Bill 406 (AB 406), that will reconcile portions of the Wisconsin tax code with recent changes in the Internal Revenue Code (IRC). This bill simplifies the tax filing process for both individuals and businesses in Wisconsin.

The following federal laws modified the IRC and were enacted during 2021 and 2022: American Rescue Plan Act of 2021 (ARPA); Paycheck Protection Program Extension Act of 2021; Surface Transportation Extension Act of 2021; Further Surface Transportation Extension Act of 2021; Infrastructure Investment and Jobs Act (IIJA); Consolidated Appropriations Act of 2022 (CAA22); Supreme Court Security Funding Act of 2022; Inflation Reduction Act of 2022 (IRA); and Consolidated Appropriations Act of 2023 (CAA23).

Conformity between the Wisconsin tax code and the IRC reduces compliance costs and minimizes confusion for filers as it relates to tax compliance. My personal philosophy is to keep tax policy as simple as possible.

We have consulted with the Legislative Fiscal Bureau (LFB) and Department of Revenue (DOR) during the drafting of the proposal.

Some of the provisions to be considered include:

- Changes to the Earned Income Tax Credit (EITC) – credit allowed in cases of certain separated spouses; modification of the disqualified income test.
- Repeal of election to allocate interest on a worldwide basis.
- Extension of certain deadlines for taxpayers affected by federally declared disasters.
- Extension of certain deadlines for taxpayers affected by significant fires.
- Sustainable aviation fuel credit.
- Energy efficient commercial building deduction.
- Modification of the credit for small employer pension startup costs.
- Increase the age limit for initial occurrence of a disability for qualified ABLE programs from 26 to 46.
- Allow rollovers of 529s to a Roth IRA.

In discussions with DOR, there are some technical corrections necessary in the current language of the bill. We have drafted a substitute amendment to ensure the language properly conforms Wisconsin tax code to the IRC.

DOR is here to testify on the bill and answer questions on the technical aspects of the draft.

Again, this bill simplifies the tax filing process for both individuals and businesses in Wisconsin.

Thank you again for hearing AB 406 and your timely action on the bill.

## TAXATION SECTION

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**To:** Assembly Committee on Ways and Means  
**Date:** September 28, 2023  
**Re:** Support of AB 406 – Relating to: Adopting changes to federal Internal Revenue Code for state tax purposes

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This Memorandum provides a background discussion of Wisconsin's adoption of Code section 1202. Wisconsin adopted section 1202 of the Internal Revenue Code in 2013. That Code section allows an exclusion for gain on certain small business stock. Section 1202 originally provided that 50% of the gain was excluded.

At various points in time, Section 1202 was amended to provide a 100% exclusion for stock acquired at certain times. For example, in 2010, the statute was amended to provide a 100% gain for stock acquired in 2010 and 2022. The statute was further amended several times. It would basically say that the 100% applied to stock acquired during certain years.

Over time, Congress continued to add new years. So, for example, it might be amended as of the end of 2012 to say that stock acquired in 2010, 2011, 2012 and 2013 gets the 100% exclusion. As of the date it was amended to – stock acquired after those time periods, like say after December 31, 2013 – would revert back to the 50% exclusion. The current version of section 1202 provides for the full 100% exclusion for stock acquired in 2010 and thereafter.

In Wisconsin, the Internal Revenue Code is not adopted in whole. Instead, Wisconsin adopts the Code as it exists on certain dates. The Wisconsin statute adopting 1202 was created to read that for stock acquired *after* December 31, 2013, the exemption would apply as Code section 1202 amended to December 31, 2012.

As section 1202 was amended to December 31, 2012, the 100% exclusion was *not* applied to stock acquired *after* December 31, 2013. Instead, at that time, section 1202 had been amended to only allow the 100% exclusion for certain stock acquired beginning in 2010 through the end of 2013. Accordingly, the Code in effect as of December 31, 2012, reverted to 50% for stock acquired after December 31, 2013. While section 1202 was ultimately changed by Congress to allow for a 100% exclusion for stock acquired after December 31, 2013, this did not occur until sometime after December 31, 2012.

Admittedly, the Wisconsin statute is confusing, and the legislature may have thought that the exclusion as of December 31, 2012, was that stock being currently acquired would be subject to the 100% exclusion. However, Code section 1202 was being amended on an ad hoc basis from year to year to provide for the 100% exclusion only for certain time periods. Section 1202 is entitled "Partial Exclusion for gain from certain small business stock," and the amendments to it to make it a full exclusion were relatively clear that the 100% exclusion was being applied on a limited basis. Had Wisconsin wanted to apply to stock issuances after the latest extension of the 100% exclusion, the statute would have read as "amended from time to time."



STATE BAR OF WISCONSIN

The State Bar's Taxation Section reviewed the legislative history of the Wisconsin statute that adopted Code section 1202. There was virtually no history relating to what was intended when adopting section 1202. We also looked around for any informal commentary regarding the legislative action and were unable to find any commentary suggesting that the legislature had in fact intended to have the exclusion be 100%. The Wisconsin Department of Revenue (DOR) had published some guidance prior to 2021 saying that Wisconsin had adopted Code section 1202. No mention was made of the percentage of exclusion. In 2021, the guidance specified that the exclusion was 50% and the DOR has provided informal guidance to taxpayers that the exclusion is 50%. Because stock must be held for five (5) years to qualify for the exclusion, the level of exclusion was not really an issue until more recently.

Assembly Bill 406 was vetted by the State Bar's Taxation Law Section who voted to actively support a position in support. If you have any additional questions, please contact Cale Battles, Government Relations Coordinator, at (608) 250-6077 or [cbattles@wisbar.org](mailto:cbattles@wisbar.org).

*The State Bar of Wisconsin establishes and maintains sections for carrying on the work of the association, each within its proper field of study defined in its bylaws. Each section consists of members who voluntarily enroll in the section because of a special interest in the particular field of law to which the section is dedicated. Section positions are taken on behalf of the section only.*

*The views expressed on this issue have not been approved by the Board of Governors of the State Bar of Wisconsin and are not the views of the State Bar as a whole. These views are those of the Section alone.*



# State of Wisconsin • DEPARTMENT OF REVENUE

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*Tony Evers*  
Governor

*Peter W. Barca*  
Secretary of Revenue

## **Information Only Testimony on Assembly Bill 406 September 28, 2023 Peter Barca, Secretary of the Department of Revenue**

Good morning, Chairman Macco, Ranking Member Conley, and members of the Assembly Ways and Means Committee. I appreciate the opportunity to provide written testimony for information only on Assembly Bill 406, a bill to bring Wisconsin up to date with Internal Revenue Code (IRC) changes.

Substitute Amendment 1 before you today includes DOR's drafting corrections to ensure we are adopting the provisions intended. The bill now largely mirrors the IRC proposal that went into the Governor's budget with a few main differences.

- The current version does not include the provision allowing taxpayers with forgiven student loans under the more recent forgiveness plans to have those amounts excluded from income tax. Under this proposal, those forgiven student loan amounts will have to be added as income when filing Wisconsin tax returns.
- This version includes a provision regarding the sale of small business stock that had not previously been adopted. This version adopts this provision prospectively.
- This version does not adopt a definition for "covered employee" which limits the deductions for highly compensated employees. There was a related definition change in the Tax Cuts and Jobs Act that was also not adopted.
- The provisions regarding high deductible insurance are being removed and passed separately.

While the majority of the IRCs are highly technical and nuanced, federal conformity is important to Wisconsin taxpayers. Federal conformity allows them to avoid recalculating their income for Wisconsin income tax purposes.

The last IRC updates adopted in Wisconsin were in 2021 WI Act 1, which was enacted in February of 2021. Since then, Congress has passed a number of other tax law changes.

I greatly appreciate the support of the bill sponsors, Senator Marklein and Representative Katsma. I would also like to thank the WICPA for working closely with the department and for its support of this important bill.

I respectfully request that this bill pass as soon as possible, as DOR staff are hard at work putting together the forms and instructions for the 2023 tax year. We hope the bill will be enacted in early October.

Again, I appreciate this opportunity and as always, I will make myself and my staff available for any questions. Rachel Harvey, our Legislative Liaison, and Craig Kvammen, from our Technical Services Office are present for your convenience.