



Legislative Fiscal Bureau

One East Main, Suite 301 • Madison, WI 53703 • (608) 266-3847 • Fax: (608) 267-6873
Email: fiscal.bureau@legis.wisconsin.gov • Website: <http://legis.wisconsin.gov/lfb>

March 11, 2024

TO: Members
Joint Committee on Finance

FROM: Bob Lang, Director

SUBJECT: Assembly Bill 793/Senate Bill 752: College Savings Accounts and Employee College Savings Account Contribution Credit

On December 8, 2023, Assembly Bill 793 (AB 793) was introduced and referred to the Assembly Committee on Ways and Means. That Committee held a public hearing on the bill on January 4, 2024. Assembly Amendment 1 to AB 793 (AA 1) was introduced on January 5, 2024. On January 11, 2024, that Committee, by separate votes of 11 to 0, adopted AA 1 and recommended AB 793, as amended, for passage. On February 13, 2024, the Assembly adopted AA 1 on a voice vote, and passed AB 793 on a vote of 96 to 0. The bill was immediately messaged to the Senate and referred to the Senate Committee on Financial Institutions and Sporting Heritage. That Committee concurred in the bill and recommended passage by a vote of 5 to 0 on February 27, 2024.

An identical companion bill, Senate Bill 752 (SB 752), was introduced and referred to the Senate Committee on Financial Institutions and Sporting Heritage on December 8, 2023. Senate Amendment 1 to SB 752 (SA 1) was introduced on January 9, 2024, and is identical to AA 1. That Committee held a public hearing on the bill on February 21, 2024. On February 27, 2024, the Committee, by separate votes of 5 to 0, adopted SA 1 and recommended SB 752, as amended, for passage.

AB 793/SB 752 are herein referred to as the "bill," and AA 1/SA 1 are referred to as the "amendment."

BACKGROUND

College Savings Accounts. College tuition programs and college savings plans are authorized under Section 529 of the Internal Revenue Code (IRC) and may be offered by states and private institutions. Under the plans, individuals may establish accounts and make contributions on behalf of beneficiaries who use amounts from the accounts to pay for their educational expenses. Account earnings accrue on a tax-free basis, and account withdrawals are tax-free if used to pay for the

beneficiary's qualified education expenses. Generally, distributions may be used for a wide range of educational expenses such as: college tuition and other fees; educational supplies; special needs services; room and board; computers; software; and internet access services. Beginning in tax year 2018, plans may also be used for a beneficiary's tuition expenses at an elementary or secondary public, private, or religious school, but such withdrawals are limited to no more than \$10,000 annually. Beginning in tax year 2019, distributions may be used for up to \$10,000 of principal and interest on the repayment of qualified student loans, and for expenses related to participation in apprenticeship programs. Wisconsin has adopted the federal tax treatment with regards to earnings and distributions.

Under advisement by the College Savings Program Board, Wisconsin offers two Section 529 college savings plans, Edvest and Tomorrow's Scholar, through the Department of Financial Institutions (DFI). Contributions to the Edvest and Tomorrow's Scholar programs may be deducted for state individual income tax purposes, but not for federal tax purposes. Since tax year 2014, claimants may deduct contributions to the account of any beneficiary, regardless of the claimant's relationship to the beneficiary. For tax year 2024, each claimant's deduction is limited to no more than \$4,000 (filing single or married-joint) or \$2,000 (for a divorced parent or if married and filing separately) per beneficiary. The maximum deduction is adjusted annually for inflation.

If an individual rolls over a 529 account from another state into a Wisconsin Edvest or Tomorrow's Scholar account, the principal amount contributed into the account may be deducted, but not the earnings in that account, subject to the annual deduction limits. If an individual rolls over a Wisconsin Edvest or Tomorrow's Scholar account into another state's 529 account, the individual must add back to their taxable income any amount that had been previously deducted from tax in Wisconsin. Under DOR administrative practice, contributions are considered to be rolled over based on the first in, first out method of accounting.

Beginning in tax year 2014, contributions in excess of the maximum may be carried forward and deducted in future years, but carryforwards are prohibited if the contribution is withdrawn from an account within one year of the contribution. If any amount is withdrawn from a qualified account and not used for qualified expenses, the amount that was previously deducted must be added back to the income of the claimant and the amount that the claimant can carry forward must be reduced by the amount not used for qualified expenses. If any amount that was previously deducted was withdrawn from a qualified account within one year of its contribution, that amount must also be added back to the income of the claimant. Under DOR administrative practice, contributions are considered to be withdrawn based on the first in, first out method of accounting.

Employee College Savings Account Contribution Credit. A nonrefundable credit is available for employers equal to 25% of the amount an employer pays into an employee's college savings account. The maximum amount of employer contribution that is eligible for the credit is equal to 25% of the maximum amount an individual employee may deduct for state income tax purposes. For example, in tax year 2024, an employee's maximum deduction for each beneficiary is \$4,000, or \$2,000 if a divorced parent or married filing separate. Therefore, the maximum employer contribution eligible for the credit in tax year 2024 is \$1,000 per beneficiary ($\$4,000 \times 25\%$) and \$500 per beneficiary for an employee who is divorced or files separately ($\$2,000 \times 25\%$). As a result,

the maximum credit for the employer's contributions is \$250 (\$1,000 x 25%) and \$125 (\$500 x 25%), respectively.

The employee college savings account contribution credit may not be claimed by individuals or sole proprietors, but can be claimed by partners of a partnership, members of a limited liability company (LLC), or shareholders of a tax-option (S) corporation.

SUMMARY OF AB 793, AS AMENDED

College Savings Accounts. Beginning in tax year 2024, the individual income tax deduction for 529 account contributions would be increased under the bill to \$5,000 (from \$4,000), and to \$2,500 for married-separate filers (from \$2,000). The contribution maximum would continue to be indexed to inflation annually thereafter. The bill would prohibit this deduction from being claimed if the same amounts were used to claim the employee college savings account contribution credit. The bill would remove a provision applicable to divorced parents that stipulates that the maximum deduction claimed by each former spouse generally cannot exceed the amounts able to be claimed by married-separate filers. As a result, the maximum deduction for each divorced parent would increase from \$2,000 under current law to \$5,000 under the bill.

Beginning in tax year 2022, the bill would provide that any federal changes to Sections 529 and 221 (e) (1) of the IRC related to college savings plans are automatically adopted for state tax purposes.

The bill would make various technical changes, such as codifying: (a) specific references to federal law that enumerate eligible expenses allowed under current state law (such as apprenticeship program expenses, qualified student loan repayments, and K-12 tuition expenses mentioned previously); and (b) the first in, first out method of accounting that applies to account contributions, withdrawals, and rollovers under current administrative practice.

The amendment would make an additional technical change to current law DFI statutes governing the college savings program, to clarify that the college savings accounts under the program are fully conformed to the federal provisions of Section 529 on an ongoing basis.

The technical modifications under "(a)" above would first apply retroactively to tax year 2018 (for K-12 expenses) or tax year 2019 (for apprenticeship expenses and qualified student loan repayments). The modifications under "(b)" would first apply to tax year 2024, provided the bill is enacted before August 1, 2024, or tax year 2025 if enacted thereafter.

Employee College Savings Account Contribution Credit. The following changes to the employee college savings account contribution credit would first apply for taxable years beginning on January 1, 2024.

The bill would change the computation of the college savings account contribution credit as follows: (a) increase the credit rate from 25% of the employer's contribution to the employee's account to 50% of the employer contribution; and (b) replace the maximum credit amount from 25%

of the maximum amount an individual employee may deduct for state income tax purposes with a maximum amount of \$800 (implying maximum contributions of \$1,600 per employee eligible to compute the credit). The maximum would no longer depend on the employee's tax filing status.

For example, under current law, the maximum credit for the employer's college savings account contributions is \$250 per employee (and \$125 if that employee is filing separate or divorced). Under the bill, the maximum would be \$800. If an employer contributes \$1,600 to an employee's 529 account, under the bill, the credit amount would increase from \$100 (or \$50) to \$800.

Beginning in tax year 2025, the \$800 maximum would be adjusted for inflation, rounded to the nearest \$10, based on the U.S. consumer price index for all urban consumers (CPI) for the month of August of the previous year compared to the CPI for August, 2023.

Under current law, for purposes of the credit for individual income tax filers, an eligible claimant includes a partnership, an S corporation, or an LLC, but not a sole proprietor. The bill would change the definition of "employer" to mean a person for whom an individual performs or performed any service as an employee of that person and who is required to furnish a W-2 form to the employee for federal income tax purposes. As a result, sole proprietors could now claim the credit for contributions to 529 accounts of their employees.

The bill would specify that the employee college savings account contribution credit could only be claimed under the individual income tax and corporate income/franchise tax for contributions for employees whose compensation is reported, or required to be reported, on a W-2 form issued by the claimant. The credit would therefore not apply to contributions to 529 accounts on behalf of independent contractors or by self-employed workers.

Finally, the bill would make a technical change to the employer contribution credit to remove a duplicative reference to the computation of credits by partnerships.

FISCAL EFFECT

The Department of Revenue (DOR) provided a fiscal estimate of the bill prior to the submission of the amendment. Based on a DOR analysis of existing claimants of the deduction for account contributions, the Department estimated that the provision increasing the contribution limit to \$5,000 would reduce state individual income tax revenues by \$1.7 million annually, beginning in 2024-25. The provision authorizing automatic adoption of federal law changes related to college savings plans would have no measurable fiscal impact at present, as Wisconsin currently conforms to all relevant federal law provisions.

DOR noted that the employer contribution credit has generated minimal claims, and thus expects the increase under the bill to reduce revenues by a minimal amount. DOR stated that the expansion of the credit to sole proprietors would increase claims by an indeterminate amount.

Based on claims of the employer contribution credit from aggregate individual income tax data for 2022 and corporate income/franchise tax data from 2020 (the most recent available), it is

estimated that the expansion of the employer contribution credit would reduce revenues by \$0.1 million annually, beginning in 2024-25.

In total, the bill is estimated to reduce income and franchise tax collections by \$1.8 million annually, beginning in 2024-25. To the extent additional Section 529 federal law changes with a revenue impact are enacted in the future, state income and franchise tax revenues would correspondingly increase or decrease.

Prepared by: John Gentry and Dan Spika