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February 17, 2020

TO: Members
Joint Committee on Finance

FROM: Bob Lang, Director

SUBJECT: Assembly Bill 754/Senate Bill 720: Modifications to the Department of Revenue and State Tax Laws

Assembly Bill 754 (AB 754) and Senate Bill 720 (SB 720) are companion bills that would make a number of changes to laws administered by the Department of Revenue (DOR).

AB 754 was introduced on January 17, 2020, and was referred to the Assembly Committee on Ways and Means. That committee held a public hearing on the bill on January 23, 2020. On February 6, 2020, that committee recommended Assembly Substitute Amendment 1 (ASA 1), as amended by Assembly Amendment 1 (AA 1) to ASA 1, for passage by a vote of 12-0.

SB 720 was introduced on January 24, 2020, and was referred to the Senate Committee on Agriculture, Revenue, and Financial Institutions. That committee held a public hearing on the bill on January 29, 2020. On February 6, 2020, that committee recommended Senate Substitute Amendment 1 (SSA 1), as amended by Senate Amendment 1 (SA 1) to SSA 1, for passage by a vote of 9-0.

ASA 1 and SSA 1 were introduced as identical substitute amendments. As recommended for passage, ASA 1, as amended by AA 1, and SSA 1, as amended by SA 1, are identical.

SUMMARY OF SUBSTITUTE AMENDMENTS, AS AMENDED

The substitute amendments would make a number of changes to state and local tax laws administered by DOR. The following section describes each provision in the substitute amendments, as amended and recommended for passage by both committees.

Inflation Certification. Under current law, DOR is required to annually determine and certify a specified rate of inflation to the State Superintendent of Public Instruction no later than the fourth Monday in June. The substitute amendments would specify that this certification would

only be done if requested by the State Superintendent.

This certification has not been used since the 2008-09 school year. Prior to 2009-10, the revenue limit per pupil adjustment was adjusted annually by the percentage change, if not negative, in the consumer price index (CPI) for all urban consumers between the preceding March and second-preceding March. This is the figure that DOR certified to the State Superintendent. Beginning with the 2009-11 biennium, the revenue limit per pupil adjustment for each year of the biennium has been set at a specified amount in each budget act.

[Section: 87]

Shared Revenue Program Payments. Specify that any reductions in shared revenue payments required under current law could come from the county and municipal aid, utility aid, or expenditure restraint program payments that counties and municipalities receive on the fourth Monday in July and the third Monday in November. Amend various cross-references to reflect this modification. Specify that this modification first applies to distributions made in 2021. In addition, upon certification by DOR, permit the Department of Administration to distribute expenditure restraint program payments before the fourth Monday in July under certain circumstances.

[Sections: 1, 2, 5 thru 7, 9, 12, 114 thru 119, and 122(3)]

Payments from Counties to Towns. Delete the current law provision that prohibits county treasurers from making payments of money owed to town treasurers between the third Monday in March until 10 days after the annual town meeting.

[Section: 3]

Annual Inflation Adjustments. Modify the current law period used in determining the annual CPI change for specific DOR-administered programs from the 12-month period ending on September 30 to the 12-month period ending on August 31. Specify that this modification would apply to the allowable growth in joint fire service charges for the purpose of the annual municipal levy limit and for the allowable growth in municipal budgets under the expenditure restraint program. In addition, amend the date on which DOR must report the allowable change in the municipal budgets under the expenditure restraint program from November 1 to October 1 of each year.

[Sections: 4, 120, and 121]

Board of Review Training. Modify the training requirements for members of a local Board of Review of property tax assessments to require that all members complete annual training. Allow all but one of the members to complete this training online. Specify that this modification takes effect on the first January 1 after publication.

[Sections: 8 and 123(2)]

Administrative Fees Related to Local Property Assessments. Modify the current law fees

relating to DOR's administrative role in local property tax assessments, effective the first January 1 after publication, as follows: (a) increase the fee for filing an appeal of a manufacturing property assessment to the state Board of Assessors from $45 to $200; and (b) delete the existing $20 recertification fee for assessors and specify that if either DOR or a test service administers and grades an examination, the fee would equal the Department's best estimate of the actual costs to administer and grade the examination, but could not exceed $75. DOR estimates that the increase to the fee associated with manufacturing assessment appeals would increase GPR-Earned by $31,000 annually. If passed into law in 2020, the fee increase would take effect on January 1, 2021, which would increase GPR-earned by $15,500 in FY2021.

[Sections: 10, 11, 88, 89, 123(1), and 123(4)]

Inclusion of Omitted Property Taxes on Tax Rolls. Modify the current law provision that property be placed on a taxation district's next tax roll if the total amount of omitted taxes for that property exceeds $5,000 to instead be included on that tax roll if the omitted taxes for any single description of property is $250 or greater. Specify that any omitted taxes on a property in a tax incremental financing district may not be included on the omitted tax roll, unless the current value of the district is lower than the tax incremental base of that district in the assessment year for which the tax is collected. Require DOR to determine the amount of omitted taxes to be shared with each taxing jurisdiction for which the taxation district collected taxes and notify the taxation district. These provisions would first take effect on January 1, 2021.

[Sections: 90 thru 93 and 123(3)]

Railroad Assessments and Interest on Amounts Owed Public Utility Taxpayers. Change the deadlines for railroad companies filing their annual reports with DOR from April 15 to May 1 and for DOR determining railroad company assessments from August 1 to September 15, to conform with the treatment of other public utility companies subject to the state ad valorem tax. Reduce the annual rate of interest paid by the state on amounts owed by DOR to public utility taxpayers from 9% to 3%, beginning on the general effective date of the substitute amendments. The provision would increase state general fund tax revenues by an estimated $5,000 in 2019-20 and by $25,000 annually beginning in 2020-21. Refunds to airline and railroad taxpayers would affect the transportation fund, and refunds to other public utility taxpayers would affect the general fund. Due to the small amount of the estimated effect, this analysis attributes the entire amount of the estimate to the general fund, which received 88% of public utility tax collections in 2018-19. A state tax in lieu of local property taxes is imposed on public utilities, including airlines, conservation and regulation companies, municipal electric associations, pipeline companies, railroads, and telephone companies subject to an ad valorem (property) tax and carline companies, electric cooperatives, and municipal and private light, heat, and power companies subject to a gross revenues tax. An identical reduction in the interest rate on refunds paid to other state taxpayers was enacted in 2013 Wisconsin Act 20.

[Sections: 94 thru 101]

Clarification of Subtraction for Disability Payments. Current law provides a subtraction

from federal adjusted gross income (AGI) for disability payments, provided the individual receiving the payments meets certain other criteria. The amount of the subtraction is based on calculation procedures and eligibility requirements that were referenced in an Internal Revenue Code (IRC) provision which was repealed in 1983. The substitute amendments would remove the IRC reference and replace it by specifying calculation procedures and eligibility requirements identical to those in the repealed IRC provision. DOR does not report a fiscal effect associated with the provision.

[Sections: 25 and 26]

Homestead Credit Modifications. Under current law, for homestead credit claims filed in 2018 and thereafter, claimants with no earned income are not eligible for the credit, unless the claimant, or the claimant's spouse, is at least 62 years of age or disabled in the year for which the claim is filed. However, earned income is not currently defined for purposes of the homestead credit. The substitute amendments would define earned income as wages, salaries, tips, and other employee compensation that are includible in federal AGI for the taxable year, plus the amount of the claimant's net earnings from self-employment for the taxable year. A claimant's earned income would be computed without regard to any marital property laws, and a claimant could elect to treat as earned income amounts excluded from federal AGI as tax-exempt combat zone compensation. Earned income would not include: (a) any amount received as a pension or annuity; (b) certain other income received by a nonresident of the United States; (c) income received while a person is incarcerated; or (d) amounts received for service performed in work activities under the federal temporary assistance for needy families program, including work experience and community service programs, to the extent such amounts are subsidized under the program.

Current law requires the addition of certain disqualified losses to income for purposes of the homestead credit, unless the claimant is a farmer whose primary income is from farming and whose farming generates less than $250,000 in gross receipts from the operation of farm premises for the year to which the credit claim relates. The substitute amendments would specify that a claimant's primary income is from farming if the claimant's gross income from farming for the year to which the claim relates is greater than 50 percent of the claimant's total gross income from all sources for the year to which the claim relates. "Gross income" would have the same definition as under the individual income tax.

These modifications would first apply to homestead credit claims filed for tax year 2020. According to DOR, this provision is estimated to increase program expenditures by $140,000 GPR on an annual basis, beginning in 2020-21.

[Sections: 81, 82, and 122(1)]

Medical Care Insurance Deduction for Self-Employed Individuals. A deduction is provided under current law for medical care insurance premiums paid by self-employed individuals. The deduction amount is limited to an individual's aggregate net earnings from a trade or business that are subject to Wisconsin tax. Nonresidents or part-year residents of Wisconsin are required to reduce the amount of the deduction according to the proportion of their total net earnings from a trade or business which are taxable in Wisconsin.

Beginning in tax year 2020, the substitute amendments would direct that the deduction amount instead be limited to the individual's total wages, salary, tips, unearned income, and net trade or business earnings that are taxable in Wisconsin. The substitute amendments would similarly modify the proration calculation for nonresidents and part-year residents (described above) to provide that the deduction be reduced according to the percentage of the person's total wages, salary, tips, unearned income, and net trade or business earnings that are subject to Wisconsin tax. DOR estimates this provision would decrease individual income tax revenues by $9,500,000 in 2020-21, and by $9,100,000 annually thereafter.

[Sections: 28 thru 31]

Repeal Obsolete Subtraction Statutes. The substitute amendments would repeal several individual income tax subtraction provisions that have been sunset and do not apply to current tax years. The provisions authorize reductions to federal AGI based on medical care insurance costs incurred between tax years 1993 and 2012.

[Sections: 27, 32, and 34]

Convert Retirement Income Exemption to a Subtraction. Current law provides an exemption from taxable income for up to $5,000 annually of payments or distributions received from a qualified retirement plan under the IRC or an individual retirement account by an individual aged 65 or older. This treatment is limited to taxpayers with federal AGI below $15,000 ($30,000 if married). The substitute amendments would convert this exemption to a subtraction. According to DOR, eligible taxpayers must claim the exemption described above, whereas a taxpayer may choose whether to claim (or not claim) any of the subtractions provided under current law.

In certain instances, requiring a taxpayer to claim the retirement income exemption can lead to the taxpayer receiving a lesser homestead credit than if the exemption were optional. This is most likely to occur for individuals who would not owe state income tax regardless of whether they claim the exemption. As a result, their decision whether to claim the subtraction under the substitute amendments would not impact individual income tax revenues. However, homestead credit expenditures would increase under the substitute amendments, in cases where electing not to claim the subtraction would lead to receipt of a greater homestead credit.

Because the homestead credit is refundable, the state budget system records the credit as a GPR expenditure. DOR estimates the provision would increase GPR expenditures by $200,000 on an annual basis. The provision would first apply in tax year 2020, and the fiscal effect would be realized beginning in 2020-21.

[Sections: 22 thru 24, 33, 86, and 122(2)]

Internal Revenue Code Update. Update statutory references to the IRC under the state individual and corporate income/franchise taxes to adopt provisions in effect as of December 31, 2019, with exceptions. The provisions that would be adopted are described in detail in a memorandum to Senator Marklein and Representative Wittke from this office, dated February 5,

2020. The memorandum was released by Senator Marklein and Representative Wittke at the executive sessions on SB 720 and AB 754, held by the respective Senate and Assembly standing committees on February 6, 2020. The memorandum is included as an attachment to the analysis of the substitute amendments. On page 5, the memorandum reports the fiscal effect of adopting the IRC provisions would be to: (a) reduce state tax collections (GPR-Tax) by an estimated $4,300,000 in 2019-20, $4,500,000 in 2020-21, $2,500,000 in 2021-22, and $2,100,000 in 2022-23; and (b) increase state GPR expenditures by $900,000 in 2019-20 and $700,000 in 2020-21. The net effect on the state's general fund is estimated at -$5,200,000 in 2019-20, -$5,200,000 in 2020-21, -$2,500,000 in 2021-22, and -$2,100,000 in 2022-23. These fiscal effects are limited to provisions in the Bipartisan Budget Act of 2018 (P.L. 115-123) and the Further Consolidated Appropriations Act of 2020 (P.L. 116-94), as reported in Table 1.

TABLE 1

Fiscal Effects of Adopting IRC Update

	2019-20	2020-21	2021-22	2022-23	Source
Bipartisan Budget Act of 2018					
Qualified Opportunity Zones	-$300,000	-$900,000	-$900,000	-$900,000	GPR-Tax
Contract Employees in Combat Zones	-200,000	-600,000	-600,000	-600,000	GPR-Tax
Retirement Plan Hardship Distributions	600,000	600,000	600,000	600,000	GPR-Tax
Further Consolidated Appropriations Act of 2020					
Retirement Plan Distributions - Disaster	-200,000	-300,000	-100,000	-100,000	GPR-Tax
Charitable Contributions - Disaster	-1,700,000	0	600,000	300,000	GPR-Tax
Casualty Losses - Disaster	-2,000,000	-2,300,000	-1,100,000	-400,000	GPR-Tax
College Savings Plans	-100,000	-100,000	-100,000	-100,000	GPR-Tax
Unrelated Business Income	-400,000	-900,000	-900,000	-900,000	GPR-Tax
Earned Income Tax Credit	900,000	700,000	0	0	GPR
Total Fiscal Effect					
GPR-Tax	-$4,300,000	-$4,500,000	-$2,500,000	-$2,100,000	
GPR	900,000	700,000	0	0	
Net Effect on General Fund	-$5,200,000	-$5,200,000	-$2,500,000	-$2,100,000	

[Sections: 13 thru 21, 36 thru 60, and 62 thru 79]
[Simple Amendment Items: 1 thru 3]

Supplement to the Federal Historic Rehabilitation Credit. Federal law provides a 20% tax credit for qualified rehabilitation expenditures (as defined under the IRC) for certified historic structures. A state credit of 20% is a supplement to the federal credit. Any person, including nonprofit entities, may sell or transfer the credit to any other Wisconsin taxpayer if the transferor notifies DOR in writing and submits a copy of the transferring documents.

The federal Tax Cuts and Jobs Act of 2017 provides that the federal tax credit must be claimed ratably over a five-year period (4% per year) for expenditures paid or incurred after December 31, 2017, instead of claiming the entire credit in the year the structure is placed in service. The state

credit must be claimed at the same time that the federal credit is claimed, and thus must also be claimed ratably over a five-year period.

The substitute amendments would provide for technical changes to the procedure for transferring the credit to account for the federal law changes made to the timing for claiming the credit. Under the substitute amendments, at the time of the transfer request, the transferor of the credit would be able to claim the credit for more than one taxable year and would compute all years of the credit on a form prescribed by DOR. The substitute amendments would allow the transferee to claim, use, and carry forward the credit in the same manner allowed for the original claimant.

[Sections: 35, 61, and 80]

Partnership Adjustment. Under current law, Wisconsin taxpayers are required to amend their state tax returns any time the Internal Revenue Service (IRS) adjusts the taxpayer's federal income tax payable and the adjustment affects the state net tax payable. Pursuant to new partnership audit procedures provided under the federal Bipartisan Budget Act of 2015, the IRS now assesses additional tax on a partnership's current year tax return at the entity level. As a result of the change in federal law, Wisconsin law no longer requires a partner to file an amended Wisconsin tax return after an IRS partnership assessment because the federal partnership adjustment does not affect the individual partners' net tax payable. Since the partners are not required to notify DOR or amend their state tax returns, DOR may not know whether a taxpayer's state tax owed is affected until after receiving notice of the adjustment from the IRS. By that time, the statute of limitations may be closed or close to expiring for making an assessment or issuing refunds to the partners. The substitute amendments would require a partnership and its partners to report to DOR, within 180 days after the final determination, the IRS partnership adjustment and either concede the accuracy of the adjustment or state how the adjustment is erroneous. Further, the partnership and its partners must submit amended returns for the tax years to which the partnership adjustments relate. DOR anticipates that this provision would not have a fiscal effect.

[Section: 84]

Reporting of IRS Adjustments. Under current law, if the IRS changes or corrects the amount of federal net income tax payable, a credit claimed or carried forward, or a net operating loss or capital loss carried forward, the taxpayer must report such changes to DOR within 90 days of the IRS determination. Such changes need only be reported if they affect the corresponding amounts payable, claimed, or carried forward in Wisconsin. Similarly, a taxpayer filing an amended return with the IRS or with another state that affects any net tax, credit, or loss carry-forward amounts in Wisconsin must also file an amended return with DOR within 90 days of the filing date of the original amended return. Also under current law, DOR may make an assessment or refund if the Department provides notice to the taxpayer within 90 days of receipt of a required report or filing described above. The substitute amendments would extend these statutory deadlines to 180 days, rather than 90 days.

[Sections: 83 and 85]

Examination of Sales Tax Returns and Related Reports. In general, current law prohibits DOR from allowing any person to examine the sales tax returns and associated documents submitted by any person, unless specifically authorized in statute. The substitute amendments would stipulate that the State Auditor and the employees of the Legislative Audit Bureau are authorized to examine such documents to the extent necessary for the Bureau to carry out its duties set forth in statute. This provision is not anticipated to have a fiscal effect.

[Section: 113]

Sales Tax Economic Nexus Threshold. Under current law, an out-of-state retailer (remote seller) is required to collect and remit sales tax if its annual gross sales or separate sales transactions in Wisconsin exceed $100,000 or 200 transactions, respectively. The substitute amendments would remove the transactions portion from this economic nexus threshold, so that only a remote seller's annual gross sales would be considered in determining whether the seller must collect and remit sales tax. The substitute amendments would specify that a calendar year is the time period for determining annual gross sales. DOR indicates this provision would have a minimal fiscal effect.

[Sections: 102 thru 109]

Sales Tax Treatment of Certain Services. Under current law, a person who sells certain taxable services may purchase otherwise taxable goods without paying sales tax, only if those goods are physically transferred to the customer in conjunction with the taxable sale of the service. This treatment applies to taxable landscaping, printing, and photographic services, as well as taxable services to tangible personal property. The substitute amendments would specify that this treatment applies regardless of whether the sale is made to a customer who claims an exemption from the tax.

Under current law, a sales tax exemption is provided for containers, boxes, labels, and other packaging and shipping materials if used by the purchaser to transfer merchandise to customers. The substitute amendments would expand this exemption to also apply when such materials are physically transferred to the customer in conjunction with the provision of the types of services mentioned above, regardless of whether those services are subject to sales tax.

The substitute amendments would clarify that these provisions do not apply to services provided by veterinarians. According to DOR, these provisions are expected to reduce state tax revenues by a minimal amount.

[Sections: 110 and 111]

Sales Tax Treatment of Nonprofit Entities. Under current law, otherwise taxable goods and services are exempt from sales tax when sold to nonprofit organizations that are operated exclusively for religious, charitable, scientific, or educational purposes, or for the prevention of cruelty to children or animals. The substitute amendments would modify this exemption to apply to an organization that is exempt from federal income tax under section 501(c)(3) of the IRC and has received a determination letter from the IRS certifying its tax-exempt status. The substitute amendments would specify that this exemption also applies to churches and religious organizations

that meet the requirements under 501(c)(3), but are not required to apply for and obtain tax-exempt status from the IRS. DOR indicates that this provision would clarify its current treatment of such entities.

According to DOR, one intent of this provision is to simplify the process for obtaining a certificate of exempt status from DOR. The Department currently requires organizations to submit their IRS determination letter, their articles of incorporation or bylaws, and their statement of receipts and expenses for their last accounting period in order to obtain a certificate. The substitute amendments are intended to provide that only the IRS determination letter is necessary when applying for a certificate. According to DOR, it is anticipated that this provision will not change the number of entities who hold a certificate, and as such will not have a fiscal impact.

[Section: 112]

FISCAL EFFECT

The substitute amendments are estimated to: (a) reduce general fund tax revenues by $4,295,000 in 2019-20, $13,975,000 in 2020-21, $11,575,000 in 2021-22, and $11,175,000 in 2022-23; (b) increase GPR-Earned from DOR by $15,500 in 2020-21 and $31,000 in 2021-22 and annually thereafter; and (c) increase estimated GPR expenditures for refundable tax credits by $900,000 in 2019-20, $1,040,000 in 2020-21, and $340,000 in 2021-22 and annually thereafter. Table 2 provides detail regarding each of the proposed law changes that would have a fiscal effect on the general fund.

Under s. 16.518(3) of the statutes, if actual tax collections exceed the amounts estimated in the state's biennial budget act, one-half of such excess is deposited into the budget stabilization fund. On January 23, 2020, this office prepared a memorandum projecting general fund tax revenues for the remainder of the 2019-21 biennium, and estimated that the amounts in the budget stabilization fund would total $845.0 million at the end of 2019-20 and $1,080.0 million at the end of 2020-21.

With the provisions included under the substitute amendments, general fund tax revenues are estimated to decrease by $4,295,000 in 2019-20 and $13,975,000 in 2020-21. The estimated effect of these provisions on the budget stabilization fund would be a decrease in the estimated stabilization fund transfer of $2,147,500 in 2019-20 and $6,987,500 in 2020-21. As a result, these amounts would remain in the general fund.

As shown in Table 2, the GPR-Transfer amounts associated with the stabilization fund that are reported as negative numbers reflect that the estimated transfer is being reduced. However, when calculating the net effect to the general fund, these amounts are considered positive numbers because those revenues remain in the general fund. GPR expenditures that are shown as positive values reduce the general fund balance. As a result, the substitute amendments would reduce the amounts available in the general fund by $3,047,500 in 2019-20, $8,012,000 in 2020-21, $11,884,000 in 2021-22, and $11,484,000 in 2022-23.

TABLE 2

Net Fiscal Effect of Substitute Amendments to General Fund (Millions)

	2019-21 Biennium			2021-23 Biennium			
	2019-20	2020-21	Total	2021-22	2022-23	Total	Source
Provisions of Substitute Amendments							
IRC Update	-$4.300	-$4.500	-$8.800	-$2.500	-$2.100	-$4.600	GPR-Tax
IRC Update EITC	0.900	0.700	1.600	0.000	0.000	0.000	GPR
Medical Care Insurance for Self-Employed	0.000	-9.500	-9.500	-9.100	-9.100	-18.200	GPR-Tax
Utility Tax Interest Rates	0.005	0.025	0.030	0.025	0.025	0.050	GPR-Tax
Objections to Manufacturing Assessments	0.000	0.016	0.016	0.031	0.031	0.062	GPR-Rev
Homestead, Defining Primary Income	0.000	0.140	0.140	0.140	0.140	0.280	GPR
Homestead, Retirement Interaction	0.000	0.200	0.200	0.200	0.200	0.400	GPR
Reduced Stabilization Fund Transfer	-2.148	-6.988	-9.136	N/A	N/A	N/A	GPR-Transfer
Totals							
GPR-Tax	-$4.295	-$13.975	-$18.270	-$11.575	-$11.175	-$22.750	
GPR-Rev	0.000	0.016	0.016	0.031	0.031	0.062	
GPR	0.900	1.040	1.940	0.340	0.340	0.680	
GPR-Transfer	-2.148	-6.988	-9.136	N/A	N/A	N/A	
Net Effect on General Fund Balance	-$3.047	-$8.011	-$11.058	-$11.884	-$11.484	-$23.368	

Attachment

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February 5, 2020

TO: Senator Howard Marklein
Representative Robert Wittke
State Capitol

FROM: Rick Olin, John Gentry, and Sean Moran

SUBJECT: Update Income and Franchise Tax References to the Internal Revenue Code

At your request, this memorandum provides a description of your proposal to update state tax references to the Internal Revenue Code (IRC). State individual income tax and corporate income/franchise tax provisions are generally referenced to definitions under federal law. With limited exceptions, changes to federal law take effect for state purposes only after action by the Legislature. Generally, the Legislature periodically reviews federal law changes to update state references to the IRC. Under current law, state tax references generally refer to IRC provisions enacted as of December 31, 2017.

State references to federal law generally provide greater simplicity for taxpayers in preparing returns and reduce the administrative burden and cost for both taxpayers and the 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. The state uses separate tax rates and brackets and separate provisions regarding standard deductions, personal exemptions, itemized deductions, and tax credits. Therefore, federal changes to rates, brackets, deductions, and credits typically have no effect for state tax purposes.

During the last legislative session, the Legislature adopted IRC provisions in effect as of December 31, 2017, although certain IRC provisions were excluded from the adoption. Since then, seven federal laws have been enacted that affect the IRC. The seven acts are:

- the Bipartisan Budget Act of 2018 (P.L. 115-123);
- the Consolidated Appropriations Act of 2018 (P.L. 115-141);
- the Taxpayer First Act (P.L. 116-25);
- the Fostering Undergraduate Talent by Unlocking Resources for Education Act (P.L. 116-91);
- the National Defense Authorization Act for Fiscal Year 2020 (P.L. 116-92);

- the Further Consolidated Appropriations Act of 2020 (P.L. 116-94); and
- the Virginia Beach Strong Act (P.L. 116-98).

The proposal would amend the most recent definition of the IRC to apply only to tax years 2018 and 2019 and create a new definition of the IRC to include changes to the IRC adopted through December 31, 2019, effective for tax years 2020 and thereafter. The proposal would exclude certain items from the definition. These are items excluded under the current law definition, as well as certain provisions included in the Bipartisan Budget Act (BBA), the Consolidated Appropriations Act, and the Further Consolidated Appropriations Act. The excluded items were either enacted on a temporary basis, relate to provisions where Wisconsin has adopted a treatment different from the federal treatment (such as depreciation), or have a sizable fiscal effect. For example, the federal Tax Cuts and Jobs Act of 2017 (TCJA) included a number of provisions increasing business taxes that partially offset other tax reductions in the Act. Wisconsin did not previously adopt those provisions, and neither would this proposal adopt them. The federal provisions to be adopted would take effect at the same time for state purposes as for federal purposes, with limited exceptions.

Several of the seven enumerated acts are federal spending measures pertaining to federal fiscal years 2018 and 2020, but also include an assortment of federal tax provisions. Among the tax provisions in the Acts, not all of the tax law changes would have a state fiscal effect if adopted. The fiscal effects described below were provided by DOR. Depending on when the proposal would become law, some or all of the fiscal effects for 2019-20 may not be realized until 2020-21.

Bipartisan Budget Act. The BBA extended over 30 tax provisions that had been adopted on a temporary basis, but had expired at the end of 2016. These provisions were extended for one to four years, with the extension retroactive to tax year 2017. Many of the provisions relate to federal tax credits, which are not tied to state tax provisions. Other provisions in the federal act relate to tax relief for hurricane and California wildfire victims or to federal excise taxes. For these reasons, federalizing most of the permanent tax provisions in the BBA would not affect state tax collections. Nonetheless, several provisions would result in a state fiscal effect beginning in tax year 2020, if adopted by the state.

Qualified Opportunity Zones. Federal law allows states to designate certain low-income census tracts as qualified opportunity zones, and taxpayers may exclude certain capital gains from their taxable income if the gain is reinvested in a qualified opportunity zone within 180 days. The BBA designates each low-income census tract in Puerto Rico as a qualified opportunity zone. Because a limited number of Wisconsin taxpayers are likely to make a qualifying investment, a minimal effect on state revenues is estimated, reducing individual income tax collections by $300,000 in 2019-20 and $900,000 in 2020-21 and annually thereafter.

Contract Employees Serving in a Combat Zone. The BBA allows contractors or employees of contractors supporting the U.S. Armed Forces in designated combat zones to exclude their foreign earned income for tax purposes even if the individual has an abode in the United States. Adopting this provision would reduce individual income tax collections by an estimated $200,000 in 2019-20 and $600,000 in 2020-21 and annually thereafter.

Hardship Distributions from Retirement Plans. The BBA directs the Internal Revenue Service

(IRS) to modify existing regulations related to hardship distributions from retirement plans by removing the six-month prohibition on making elective and employee contributions to a retirement plan after the receipt of a hardship distribution. Because contributions to retirement plans are generally made on a pre-tax basis, except for ROTHs, withdrawals are subject to tax. Under this provision, state tax revenues are estimated to increase by $600,000 in 2019-20 and annually thereafter.

Further Consolidated Appropriations Act. The Further Consolidated Appropriations Act of 2020 became law on December 20, 2019. It sets the overall spending limits for federal agencies and programs for the federal fiscal year ending September 30, 2020, and contains a number of retirement-related provisions that have been described as the most comprehensive retirement reform since the Pension Protection Act of 2006. In addition, the Act also contains a number of federal tax provisions, including the following provisions that would have a measurable effect on state tax revenues if adopted by the state.

Disaster-Related Distributions from Retirement Plans. The Act creates special disaster-related rules for uses of retirement funds in three areas related to federally declared disasters occurring between January 1, 2018, and 60 days after the Act's date of enactment. First, distributions from retirement plans, including Individual Retirement Accounts (IRAs), are not subject to the 10% additional tax on early withdrawals if the withdrawal is a qualified disaster distribution, does not exceed $100,000, and is repaid within three years. Distributions are included in the taxpayer's income for federal tax purposes, but may be allocated up to three years. Second, individuals who withdraw funds from a retirement plan for a first-time home purchase, but are unable to complete the purchase because of a disaster, may recontribute the funds to the plan without penalty, depending on the time of the withdrawal and the period of the disaster. Third, the Act increases the limit on funds that may be withdrawn from a qualified employer retirement plan as a loan, and not treated as a plan distribution, from $50,000 to $100,000, provided the loan is made within 180 days of the Act's date of enactment. Such loans are subject to repayment requirements, and the Act increases the five-year repayment period by one year for an individual whose residence is located in a qualified disaster area. Without adoption, Wisconsin taxpayers would be required to pay tax and a penalty on early retirement distributions. Adopting the provision would reduce state tax collections by an estimated $200,000 in 2019-20, $300,000 in 2020-21, and $100,000 in 2021-22 and 2022-23.

Charitable Contributions for Relief Efforts in Qualified Disaster Areas. The Act provides an increase in the limitation on charitable contributions allowed as deductions, provided the contribution is made for relief efforts in one or more qualified disaster areas and is made between January 1, 2018, and 60 days after enactment of the Act (December 20, 2019). For individuals, qualified disaster area contributions may not exceed the excess of the taxpayer's contribution base over the amount of all other contributions (not qualified disaster area contributions). For corporations, qualified disaster area contributions may not exceed the excess of the corporation's taxable income over the amount of all other (non-disaster) contributions. Adopting the provision would decrease state tax collections by an estimated $1,700,000 in 2019-20. No fiscal effect is estimated for 2020-21, and tax collection increases are estimated of $600,000 in 2021-22 and $300,000 in 2022-23. The increase would occur because the higher limitation would allow taxpayers to reduce their amount of carryover contributions deducted in subsequent years.

Casualty Losses in Qualified Disaster Areas. The Act increases the amount of casualty loss due to qualified disasters that may be claimed for federal tax purposes. The Act removes the requirement that the loss exceed 10% of federal adjusted gross income and allows the loss to be claimed either as an itemized deduction or as an increase in the standard deduction. Adopting the provision would reduce state tax collections by an estimated $2,000,000 in 2019-20, $2,300,000 in 2020-21, $1,100,000 in 2021-22, and $400,000 in 2022-23.

College Savings (529) Plans. The Act expands the definition of qualified education expense to allow 529 distributions to be used to pay for: (a) expenses associated with registered apprenticeship programs; and (b) principal or interest on qualified student loans of the account's beneficiary or a sibling of the beneficiary, limited to a lifetime maximum of $10,000. Regarding the latter provision, distributions used in this manner would not qualify for the student loan interest deduction that currently may be claimed as an adjustment to income for federal and state purposes. Adopting the provision would reduce state tax collections by an estimated $100,000 annually beginning in 2019-20.

Earned Income Tax Credit (EITC). The Act modifies the federal EITC and the refundable component of the child tax credit by allowing qualified individuals whose residence is in a disaster area to calculate their credit using their earned income from the prior year, instead of their earned income from the current year, provided their earned income from the prior year is higher. Typically, changes to the federal EITC are automatically adopted for purposes of the state EITC because the state credit is calculated as a percentage of the federal credit. However, this change is a non-IRC provision, so state adoption is not automatic. Because the state credit is refundable, the state budget system records the credit as a GPR expenditure. DOR reports that adopting this provision would increase GPR expenditures by an estimated $900,000 in 2019-20 and $700,000 in 2020-21. The provision would have no effect in 2021-22 and 2022-23.

Unrelated Business Income. Tax exempt organizations must pay tax on their unrelated business income, which is the income from a trade or business regularly carried on by the organization that is not substantially related to the organization's exercise or performance of its tax exempt functions or purpose. Effective for taxable years beginning after December 31, 2017, the TCJA required tax exempt organizations to add the cost of the following fringe benefits as unrelated business income for federal tax purposes: (a) qualified transportation fringe benefits (including qualified parking, transit passes, vanpool benefits, and qualified bicycle commuting reimbursements); (b) parking facilities in connection with qualified parking; and (c) on-premises athletic facilities. For example, the cost of employee parking provided by charities, churches, and other nonprofit entities is taxed as unrelated business income. Pursuant to 2017 Wisconsin Act 231, this treatment was adopted as part of state law. However, in December, 2019, the Further Consolidated Appropriations Act retroactively repealed this provision of the TCJA. The proposal would update state law to adopt the repeal prospectively, such that nonprofit organizations that pay certain fringe benefits relating to transportation, parking, and the use of athletic facilities would not be required to file a Wisconsin income tax return to pay taxes on such amounts for tax years beginning on and after January 1, 2020. Adopting the sunset of this provision would reduce revenues by $400,000 in 2019-20 and $900,000 annually thereafter beginning in 2020-21.

Summary of Tax Law Changes with a Fiscal Effect. The combined effect of the preceding nine provisions would be to: (a) reduce state tax collections (GPR-Tax) by an estimated $4,300,000 in 2019-20, $4,500,000 in 2020-21, $2,500,000 in 2021-22, and $2,100,000 in 2022-23; and (b) increase state GPR expenditures by $900,000 in 2019-20 and $700,000 in 2020-21. The net effect on the state's general fund is estimated at -$5,200,000 in 2019-20, -$5,200,000 in 2020-21, -$2,500,000 in 2021-22, and -$2,100,000 in 2022-23. These effects are limited to provisions in the Bipartisan Budget Act and the Further Consolidated Appropriations Act. The other federal acts containing IRC provisions are not expected to measurably affect state tax collections. A brief description of each act follows.

Consolidated Appropriations Act. The Consolidated Appropriations Act of 2018 became law on March 23, 2018. The Act made technical corrections to IRC provisions that had been enacted in 2015. Changes include correcting spelling and grammatical errors, as well as cross-references. Wisconsin had previously adopted the 2015 provisions, so the bill would adopt the technical corrections. In addition, the Act made technical corrections to the TCJA. Wisconsin adopted many of the TCJA changes in 2018 when it enacted Act 231, which also adopted some provisions from the Disaster Tax Relief and Airport and Airway Extension Act of 2017 (P.L. 115-63). Therefore, adopting the Consolidated Appropriations Act clarifies that the provisions adopted in Act 231 will have the intended effects. Adopting these provisions is not expected to result in a state fiscal effect.

Taxpayer First Act. The Taxpayer First Act was signed into law on July 1, 2019. The Act revises provisions relating to the IRS, its customer service, enforcement procedures, cybersecurity and identity protection, management of information technology, and use of electronic systems. With one exception, adopting these provisions would not affect state tax collections. The Act's provision regarding equitable relief from joint liability could have a minimal state fiscal effect if adopted.

Fostering Undergraduate Talent by Unlocking Resources for Education (FUTURE) Act. The FUTURE Act became law on December 19, 2019, and "permanently authorizes funding for minority-serving institutions of higher education and increases the authorization of appropriations for Pell Grants." In addition, the Act authorizes the IRS, at the request of the Department of Education, to disclose tax return information to authorized persons related to student eligibility for several income-contingent or income-based determinations. DOR indicates that the tax-related provisions would have no tax effect on Wisconsin if adopted.

National Defense Authorization Act. The National Defense Authorization Act for Fiscal Year 2020 became law on December 20, 2019. The Act authorizes appropriations and sets forth policies for Department of Defense programs and activities, including military personnel strengths for the federal fiscal year ending on September 30, 2020. Also, the Act makes several changes to the IRC related to the definitions of qualified disaster, qualified disaster area, qualified disaster zone, and incident period, but these provisions would not have a fiscal effect on state tax collections if adopted, according to DOR.

Virginia Beach Strong Act. The Virginia Beach Strong Act became law on December 20, 2019, in response to the May 31, 2019, shootings in Virginia Beach, Virginia, which killed 12 people and wounded four others. The Act contains two tax provisions. One provision allows cash contributions for the relief of victims' families to be treated as charitable contributions. By adopting

this provision, Wisconsin taxpayers could include such contributions in the calculation of the state itemized deduction tax credit. The second provision allows charitable organizations to make payments to the spouses or dependents of victims without violating the conditions of the organization's tax-exempt status. While no fiscal effect is estimated for these provisions, adopting the two provisions could reduce state tax collections by a minimal amount.

Other Proposed Changes. The proposal would also extend certain provisions in these acts to prior years, but those changes are not expected to have a fiscal effect. For example, a limited number of the technical corrections described under the Consolidated Appropriations Act would be extended to tax years 2014, 2015, and 2016. The retroactive provision also includes several pension and retirement related changes made by the Further Consolidated Appropriations Act.

The pension and retirement provisions in the Further Consolidated Appropriations Act would also be extended retroactively to tax year 2017, along with two provisions in the BBA. The two provisions, which had expired and been extended by the BBA through tax year 2017, pertain to the election to expense mine safety equipment and the deduction for energy efficient commercial buildings. These provisions are authorized under Section 179 of the IRC, and Wisconsin state statutes automatically adopted these federal changes.

For tax years 2018 and 2019, the proposal would extend provisions included in the BBA related to Section 179 expensing, the Taxpayer First Act related to equitable relief from joint liability, the Further Consolidated Appropriations Act related to retirement and pension plans, tax extenders, disaster relief, and unrelated business income, and the Virginia Beach Strong Act related to payments by charitable organizations to victims' families.

While the preceding provisions describe the IRC as it relates to the individual income tax, the proposal contains comparable provisions, where appropriate, to the definition of the IRC as it applies to the taxation of corporations, tax-option corporations, and insurance companies.

The proposal would also repeal obsolete references to the IRC for tax years 2005 through 2013. According to the Legislative Reference Bureau, repeal of these obsolete provisions would delete approximately 30 pages from the printed version of the statutes.

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