

## A. INCOME TAXES

1. Update Reference to Internal Revenue Code for Individuals, Estates and Trusts (1987 Act 27, amend s. 71.02(2)(d)12, create s. 71.02(2)(d)13, effective for taxable year 1987 and thereafter.)

For the 1987 taxable year and thereafter, individuals, estates and trusts, except nuclear decommissioning trust or reserve funds, will use the Internal Revenue Code as amended to December 31, 1986, as it applies to taxable year 1987 and subsequent years, with the following exceptions:

- a. Residential real property and certain farm property placed in service during the 1986 taxable year must be depreciated under the Internal Revenue Code in effect on December 31, 1980. (See Item A.20.)
  - b. Federal treatment of capital gains and losses does not apply for Wisconsin. (See Items A.16. and A.17.)
  - c. Taxable unemployment compensation continues to be computed under section 85 of the Internal Revenue Code as it existed on December 31, 1985. (See Item A.15.)
  - d. Railroad retirement benefits continue to be nontaxable for Wisconsin.
  - e. Sick pay benefits paid under the Railroad Unemployment Insurance Act continue to be nontaxable for Wisconsin.
  - f. The disability income exclusion of up to \$5,200 which was allowed to persons under age 65 who retired on disability and received disability income while permanently and totally disabled, as provided under section 501(d) of the Internal Revenue Code immediately prior to its repeal in 1983 by Public Law 98-21, continues to apply for Wisconsin.
2. Revise Standard Deduction for Married Persons (1987 Act 27, amend ss. 71.02(2)(km)2m, 71.09(6r)(b) and 71.10(2)(a)5.a, create s. 71.02(2)(km)2n and 2p, see effective dates below.)
    - a. For the taxable year 1987, the Wisconsin standard deduction for married persons will be as follows.
      - (1) Married persons filing jointly.
        - (a) If their total Wisconsin adjusted gross income is less than \$10,000, the standard deduction is \$7,560.
        - (b) If their total Wisconsin adjusted gross income is at least \$10,000 but not more than \$70,480, the standard deduction is the amount obtained by subtracting from \$7,560 12.5% of total Wisconsin adjusted gross income in excess of \$10,000 but not less than \$0.
        - (c) If their total Wisconsin adjusted gross income is more than \$70,480, the standard deduction is \$0.

- (2) Married persons filing separately.
  - (a) If Wisconsin adjusted gross income is less than \$4,750, the standard deduction is \$3,590.
  - (b) If Wisconsin adjusted gross income is at least \$4,750 but not more than \$33,470, the standard deduction is the amount obtained by subtracting from \$3,590 12.5% of Wisconsin adjusted gross income in excess of \$4,750 but not less than \$0.
  - (c) If Wisconsin adjusted gross income is more than \$33,470, the standard deduction is \$0.
- b. For the taxable year 1988 and thereafter, the Wisconsin standard deduction for married persons will be as follows.
  - (1) Married persons filing jointly.
    - (a) If their total Wisconsin adjusted gross income is less than \$10,000, the standard deduction is \$8,900.
    - (b) If their total Wisconsin adjusted gross income is at least \$10,000 but not more than \$55,000, the standard deduction is the amount obtained by subtracting from \$8,900 19.778% of total Wisconsin adjusted gross income in excess of \$10,000 but not less than \$0.
    - (c) If their total Wisconsin adjusted gross income is more than \$55,000, the standard deduction is \$0.
  - (2) Married persons filing separately.

- (a) If Wisconsin adjusted gross income is less than \$4,750, the standard deduction is \$4,230.
- (b) If Wisconsin adjusted gross income is at least \$4,750 but not more than \$26,140, the standard deduction is the amount obtained by subtracting from \$4,230 19.778% of Wisconsin adjusted gross income in excess of \$4,750 but not less than \$0.
- (c) If Wisconsin adjusted gross income is more than \$26,140, the standard deduction is \$0.

The standard deduction for single persons for 1987 and thereafter remains the same as for the 1986 taxable year.

The filing requirements for married persons for 1987 and thereafter will be adjusted to reflect the changes in the standard deduction.

- 3. Repeal Indexing of Standard Deduction (1987 Act 27, repeal s. 71.02(2)(kr) and amend s. 71.09(2f), effective August 1, 1987.)

The Wisconsin standard deduction will not be indexed. Under prior law, indexing was to begin for the 1987 taxable year.

4. Change Definition of "Small Business Stock" (1987 Act 27, repeal s. 71.02(2)(fr)5, amend s. 71.02(2)(fr)(intro.) and 3, effective for stock acquired on or after August 31, 1987.)

"Small business stock" means an equity security that a taxpayer has held for at least 5 years which was issued by a corporation that meets the requirements on the December 31 before acquisition by the taxpayer, or for a corporation which was incorporated during the calendar year the stock is issued, as of the date of acquisition of the stock. Under prior law, all corporations had to meet the requirements on the December 31 before acquisition by the taxpayer.

The corporation must derive no more than 25% of its gross receipts from rents, interest, dividends, and sales of intangible investment assets combined unless the corporation derives less than \$3,000 of that income and has not been incorporated for more than 2 calendar years. Under prior law, any sales of assets were taken into consideration.

The requirement that the corporation may not have conducted a trade or business in any form for a period exceeding 5 years has been repealed.

5. Broaden Addition Modification for Certain Interest Income (1987 Act 27, amend s. 71.05(1)(a)1, create s. 66.4325(5m), effective for bonds issued after January 28, 1987.)

The amount of any interest which is not included in federal adjusted gross income, except interest which by federal law is exempt from Wisconsin taxation, less related expenses, must be added back to federal adjusted gross income. Previously, only interest, less related expenses, excluded for federal tax purposes under section 103 of the Internal Revenue Code had to be added back to federal adjusted gross income.

Interest on bonds issued by a Wisconsin community development authority continues to be exempt from Wisconsin taxation.

6. Repeal Surplus Language (1987 Act 27, repeal s. 71.05(1)(a)7 and 17, amend s. 71.05(1)(b)1, effective for taxable year 1987 and thereafter.)

The following modifications are repealed to reflect changes to the Internal Revenue Code:

s. 71.05(1)(a)7 - moving expenses to move from Wisconsin

s. 71.05(1)(a)17 - federal married couple deduction

In addition, s. 71.05(1)(b)1 has been amended to eliminate the requirement that interest which by federal law is exempt from Wisconsin taxation must be reduced by the amount of related expenses allowable as itemized deductions. Instead, the related expenses are not includable in the computation of the Wisconsin itemized deduction credit. (See Item A.26.)

7. Clarify Modification for Farm Losses (1987 Act 27, amend s. 71.05(1)(a)26, effective for taxable year 1986 and thereafter.)

In calculating the amount of farm losses that must be added back to federal adjusted gross income, net gains from the sale or exchange of capital or business assets and net profits may not be offset against farm losses.

In addition, the dollar amounts of nonfarm Wisconsin adjusted gross income will not be indexed. Indexing was to begin with taxable year 1987.

8. Clarify Modifications for Nondeductible 1986 Travel and Entertainment Expenses (1987 Act 27, amend s. 71.05(1)(a)27.a and c to g, effective for taxable year 1986.)

These provisions clarify that certain travel and entertainment expenses allowable under sections 162 or 212 of the Internal Revenue Code and not disallowed under section 274 of the Internal Revenue Code must be added back to federal adjusted gross income.

9. Repeal Modifications for Nondeductible Travel and Entertainment Expenses (1987 Act 27, repeal s. 71.05(1)(a)27, effective for taxable year 1987 and thereafter.)

Beginning with the 1987 taxable year, the provisions requiring addition modifications for certain travel and entertainment expenses are repealed. Instead, the limitations on travel and entertainment expenses provided in the Internal Revenue Code as amended to December 31, 1986, apply for Wisconsin tax purposes.

10. Limit Deductions for Part-Year Residents and Nonresidents (1987 Act 27, create s. 71.05(1)(a)29, effective for taxable year 1987 and thereafter.)

Part-year residents and nonresidents are required to add back to federal adjusted gross income the following amounts deducted for federal tax purposes and paid while a nonresident of Wisconsin: alimony, penalties for early withdrawals from time savings accounts and deposits, repayments of supplemental unemployment compensation benefits and reforestation payments related to property not in Wisconsin.

Part-year residents and nonresidents are required to add back to federal adjusted gross income contributions to individual retirement accounts, simplified employee pension plans and self-employment retirement plans and all deductible employee contributions in excess of the amount deducted for federal tax purposes multiplied by the ratio of the individual's wages and net earnings from a trade or business taxable by Wisconsin to the individual's total wages and net earnings from a trade or business.

Part-year residents and nonresidents are required to add back to federal adjusted gross income contributions to a Keogh plan in excess of the amount deducted for federal tax purposes multiplied by the ratio of the individual's net earnings from a trade or business taxable by Wisconsin to the individual's total net earnings from a trade or business.

11. Provide Modification for Expenses of Administering an Estate (1987 Act 27, create s. 71.05(1)(a)28 and (b)13, effective for returns filed for deaths occurring on or after August 1, 1987.)

Expenses paid by a fiduciary that have been deducted under section 212 of the Internal Revenue Code and have been or will be deducted for inheritance tax purposes may not be deducted for income tax purposes. However, expenses paid by a fiduciary that the fiduciary specifies in writing have not been deducted under section 212 of the Internal Revenue Code and are not or will not be deducted for inheritance tax purposes as administrative expenses may be deducted for income tax purposes.

12. Disallow Deductions on Fiduciary Income Tax Returns for Taxes (1987 Act 27, create s. 71.05(1)(a)30, effective for taxable year 1987 and thereafter.)

The amount claimed by a fiduciary as an itemized deduction for taxes under section 164 of the Internal Revenue Code on the federal fiduciary return is not allowed for Wisconsin tax purposes.

13. Change Modification for Amounts Not Taxable by Wisconsin (1987 Act 27, amend s. 71.05(1)(b)4, effective for taxable year 1987 and thereafter.)

Amounts not taxable by Wisconsin which are subtracted from federal adjusted gross income must be reduced by related expenses, except expenses used to calculate the Wisconsin itemized deduction credit.

14. Clarify Disability Income Exclusion for Married Persons (1987 Act 27, amend s. 71.05(1)(b)8m, effective for taxable year 1986 and thereafter.)

Married persons must file a joint return to be eligible to claim the disability income exclusion. If only one spouse is disabled, the maximum disability income exclusion is the lesser of \$100 for each week that payments are received or the amount of disability pay reported as income.

If persons are divorced during the taxable year, only the disabled spouse may claim a disability income exclusion. The exclusion is limited to the lesser of \$100 for each week that disability pay is received or the amount of disability pay reported as income by the disabled spouse.

15. Provide Subtraction Modification for Unemployment Compensation (1987 Act 27, repeal s. 71.05(1)(km), create s. 71.05(1)(b)15, effective for taxable year 1987 and thereafter.)

A subtraction modification may be made for any difference between the amount of unemployment compensation included in federal adjusted gross income and the amount computed under section 85 of the Internal Revenue Code as it existed on December 31, 1985.

16. Provide Capital Gain Subtraction Modification (1987 Act 27, create s. 71.05(1)(b)16, effective for taxable year 1987 and thereafter.)

A subtraction modification is provided for 60% of capital gains on assets held more than one year.

"Capital gain" means capital gain as computed under the Internal Revenue Code, not including amounts treated as ordinary income for federal income tax purposes because of the recapture of depreciation or any other reason. The capital gains and capital losses for all assets must be netted before application of the percentage.

17. Limit Capital Loss Deduction (1987 Act 27, create s. 71.05(1)(f)4, effective for taxable year 1987 and thereafter.)

Net capital losses may be offset against ordinary income only to the extent of \$500.

Losses in excess of \$500 may be carried forward to the next taxable year and offset against ordinary income up to the \$500 limit. Losses shall be used in the order they accrue.

18. Clarify Basis Adjustment for Property Acquired From a Decedent (1987 Act 27, amend s. 71.05(1)(g), effective for transfers because of deaths occurring on or after August 1, 1987.)

The Wisconsin basis of property acquired from a decedent is determined under the Internal Revenue Code, but the value used for property is the value properly includable for Wisconsin inheritance tax purposes instead of the value of property includable for federal estate tax purposes.

Where a decedent is gifted appreciated property within one year of his or her death, and the property is reacquired by the donor (or the spouse of the donor), the basis of the property is the adjusted basis in the hands of the decedent prior to the decedent's death. Consequently, there is no basis adjustment on account of the death.

19. Clarify Definition of Wisconsin Adjusted Gross Income (1987 Act 27, create s. 71.05(1)(gm), effective for taxable year 1986 and thereafter.)

An addition or subtraction modification from federal adjusted gross income is required for the following amounts:

- a. The amount necessary to reflect the inapplicability of section 66(a) of the Internal Revenue Code for Wisconsin income tax purposes.
- b. The amount necessary to reflect the applicability of ss. 71.01(1g) and (1r) and 71.11(2m) to the computation of Wisconsin taxable income.
- c. The amount necessary to reflect any other differences between the treatment of marital income for federal income tax purposes and the treatment of marital income for Wisconsin income tax purposes.

20. Provide for Depreciation Continuation (1987 Act 27, amend s. 71.05(2r), (2t) and (2u), create s. 71.05(2s), effective for taxable year 1987 and thereafter.)

Residential real property and certain farm property that under s. 71.02(2)(d)12 is required to be depreciated for the taxable year 1986 under the Internal Revenue Code as amended to December 31, 1980, must continue to be depreciated for the 1987 taxable year and thereafter under the Internal Revenue Code as amended to December 31, 1980.

21. Provide Treatment for Partnership Income or Loss Received by Part-Year Residents and Nonresidents (1987 Act 27, create s. 71.07(1g), effective for any partner's taxable year 1987 and thereafter.)

Partners who are not full-year residents of Wisconsin must compute taxes for that year on their share of partnership income or loss by (a) assigning an equal portion of each item of income, loss or deduction to each day of

the partnership's taxable year, (b) multiplying each daily portion of those items by a fraction that represents the partner's portion, on that day, of the total partnership interest, and (c) netting the items for the days during which the partner was a Wisconsin resident.

General partners who are not full-year Wisconsin residents must compute taxes for that part of the taxable year during which they are nonresidents by recognizing their proportionate share of all items of income, loss or deduction attributable to a business in, services performed in, or rental of property in Wisconsin.

Limited partners who are precluded from management of the partnership and who may not act for the partnership may not recognize any items of income, loss or deduction of the partnership for the part of the taxable year they are nonresidents of Wisconsin.

A partner must disregard all provisions in partnership agreements that do any of the following:

- a. Characterize payments to the partner as being for services or the use of capital.
- b. Allocate to the partner, as income from or gain from sources outside Wisconsin, a greater portion of the partner's distributive share of partnership income or gain than the ratio of partnership income or gain from outside Wisconsin to partnership income or gain from all sources.
- c. Allocate to a partner a greater proportion of a partnership item of loss or deduction from sources in Wisconsin than the partner's proportionate share of total partnership loss or deduction.
- d. Determine a partner's distributive share of an item of partnership income, gain, loss or deduction for federal income tax purposes if the principal purpose is to avoid or evade the tax under Chapter 71.

22. Reduce Income Tax Rates (1987 Act 27, amend ss. 71.09(1e)(intro.) and (1f)(intro.), 71.20(2m) and 71.65(1)(a), create s. 71.09(1g) and (1h), effective for taxable year 1987 and thereafter.)

- a. The tax rates for single persons and all fiduciaries, except fiduciaries of nuclear decommissioning trust or reserve funds, are as follows:
  - (1) On all taxable income from \$0 to \$7,500, 4.9%.
  - (2) On all taxable income exceeding \$7,500 but not exceeding \$15,000, 6.55%.
  - (3) On all taxable income exceeding \$15,000, 6.93%
- b. The tax rates for married persons filing jointly are as follows:
  - (1) On all taxable income from \$0 to \$10,000, 4.9%.

(2) On all taxable income exceeding \$10,000 but not exceeding \$20,000, 6.55%.

(3) On all taxable income exceeding \$20,000, 6.93%

c. The tax rates for married persons filing separately are as follows:

(1) On all taxable income from \$0 to \$5,000, 4.9%.

(2) On all taxable income exceeding \$5,000 but not exceeding \$10,000, 6.55%.

(3) On all taxable income exceeding \$10,000, 6.93%

23. Repeal Indexing of Income Tax Brackets (1987 Act 27, repeal s. 71.09(2e), amend ss. 71.09(2) and 71.20(2m), effective August 1, 1987.)

The income tax brackets will not be indexed. Under prior law, indexing was to begin for the 1987 taxable year.

24. Correct References to the Internal Revenue Code (1987 Act 27, amend ss. 71.02(2)(eg) and 71.09(6p)(b), effective for taxable year 1987 and thereafter.)

To reflect changes made to the Internal Revenue Code (IRC) by the federal Tax Reform Act of 1986, the following references to the IRC in the Wisconsin Statutes have been changed:

a. The IRC reference with respect to a married person or spouse is changed from section 143(a) to 7703(a).

b. The IRC reference with respect to a dependent is changed from section 151(e) to 151(c).

25. Permit Repayments of Income Previously Taxed to Be Used in Computing the Itemized Deduction Credit (1987 Act 27, amend s. 71.09(6r)(a), effective for taxable year 1986.)

Federal law provides that if a taxpayer has to repay an amount that had been properly included in the taxpayer's income in an earlier year, the taxpayer may deduct the amount repaid from income for the year in which it was repaid. Repayments of income deductible as an itemized deduction for federal income tax purposes may be included in the computation of the itemized deduction credit, if that income was previously taxed by Wisconsin.

26. Change Itemized Deduction Credit (1987 Act 27, repeal and recreate s. 71.09(6r)(a), effective for taxable year 1987 and thereafter.)

Amounts allowed as itemized deductions under the Internal Revenue Code as amended to December 31, 1986, may be used to calculate the Wisconsin itemized deduction credit, except for the following:

a. Interest paid to purchase or hold securities issued by the federal government or by any of its instrumentalities the interest on which is exempt from taxation under s. 71.05(1)(b)1.



- b. Taxes allowed under section 164 of the Internal Revenue Code.
- c. Casualty and theft deductions allowed under section 165(c)(3) of the Internal Revenue Code.
- d. Expenses to move from this state allowed under section 217 of the Internal Revenue Code.
- e. Interest incurred to purchase a residence that is neither a primary residence nor is in this state and interest incurred to purchase a residence that is a boat.
- f. Interest in excess of \$1,200, or \$600 for married persons filing separately, not paid on a loan to purchase or refinance a residence and not paid on a land contract.

27. Simplify Computation of Itemized Deduction Credit for Part-Year Residents and Nonresidents Who File Joint Returns (1987 Act 27, amend s. 71.09(6r)(d), effective for taxable year 1987 and thereafter.)

If married persons are not both domiciled in Wisconsin during the entire taxable year, they will use the standard deduction actually claimed on their return (based on their federal adjusted gross income) to compute their itemized deduction credit. Under prior law, for purposes of computing their itemized deduction credit, these married persons were to use the standard deduction that would have been available to them if both spouses had been domiciled in Wisconsin all year.

28. Change Definition of "Earned Income" for Married Couple Credit (1987 Act 27, amend s. 71.09(7m), effective for taxable year 1987 and thereafter.)

For purposes of computing the married couple credit, "earned income" means qualified earned income, as defined in section 221(b) of the Internal Revenue Code as amended to December 31, 1985, plus employee business expenses under section 62(2)(B), (C) or (D) of that Code, allocable to Wisconsin under s. 71.07, minus disability income excluded under s. 71.05(1)(b)8m and minus any other amount not subject to Wisconsin individual income tax.

The married couple credit may not be claimed by married persons who reduce their gross income under section 911 or 931 of the Internal Revenue Code.

29. Provide School Property Tax Credit (1987 Act 27, create s. 71.53, effective for taxable year 1987 and thereafter.)

Individuals may claim as a credit against, but not to exceed the amount of, taxes under s. 71.01(1), 6.9% of the first \$2,000 of property taxes or rent constituting property taxes paid on their principal dwelling.

"Rent constituting property taxes" means 25% of rent paid if heat is not included or 20% of rent paid if heat is included, excluding any payment for domestic, food, medical or other services.

Part-year residents must prorate the credit based on the ratio of Wisconsin adjusted gross income to federal adjusted gross income. No credit is allowed to nonresidents of Wisconsin.