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Wisconsin TAX BULLETIN

New Wisconsin Tax Laws

The Wisconsin Legislature in October 1997 enacted a number of changes to the Wisconsin tax laws. This issue of the *Wisconsin Tax Bulletin* contains an index and brief descriptions of the major individual and fiduciary income, corporation franchise or income, homestead credit, sales/use, withholding and excise tax provisions.

All of these provisions are contained in 1997 Wisconsin Act 27.

The description for each provision indicates the sections of the statutes affected and the effective date of the new provision.

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Note: This Wisconsin Tax Bulletin includes the provisions in 1997 Wisconsin Act 27 relating to updating the reference to the Internal Revenue Code to December 31, 1996. (See Items A.1 on page 7 and B.1 and B.3 on pages 14 and 15.) However, in a September 29, 1997, letter to the Department of Revenue, Legislators Ben Brancel and Charles Chvala state that their intent is to further update the reference to the Internal Revenue Code during the Legislative floor period of November 4-6, 1997. At this November floor period, the updating of the Internal Revenue Code reference for Wisconsin would adopt those provisions of Public Laws 105-33 and 105-34 that took effect for federal purposes for the 1997 tax year or earlier tax years. The issue of whether federal laws passed in 1997 should be adopted for the tax year 1998 and later years will be considered during the Spring 1998 Legislative session.

A. Individual and Fiduciary Income Taxes

1. Internal Revenue Code Reference Updated for 1997 for Individuals, Estates, and Trusts (1997 Act 27, repeal sec. 71.01(6)(d), amend sec. 71.01(6)(k) and (7r), and create sec. 71.01(6)(L), effective for taxable years beginning on or after January 1, 1997.)

For taxable years that begin on or after January 1, 1997, "Internal Revenue Code" for individuals, estates, and trusts (except nuclear decommissioning trust or reserve funds) means the federal Internal Revenue Code as amended to December 31, 1996, with the exceptions indicated below. The Internal Revenue Code applies for Wisconsin purposes at the same time as for federal purposes.

- Section 1311 of federal Public Law 104-188 relating to the reduction of an S corporation's accumulated earnings and profits by an amount equal to the portion (if any) of such accumulated earnings and profits which were accumulated in any taxable year beginning before January 1, 1983, does not apply for Wisconsin.
- Section 13113 of federal Public Law 103-66 relating to the exclusion for 50% of the gain from the sale or exchange of qualified small business stock held for more than five years does not apply for Wisconsin.
- For property placed in service in taxable years beginning on or after January 1, 1997, individuals and fiduciaries may compute depreciation or amortization under either the federal Internal Revenue Code in effect for the taxable year for which the return is filed or the federal Internal Revenue Code as amended to December 31, 1996, at the taxpayer's option.

2. Federal Laws Enacted During 1996 Apply Simultaneously for Wisconsin Purposes (1997 Act 27, amend secs. 71.01(6)(e), (f), (g), (h), (i), (j), and (k) and 71.77(3) and (5), effective for taxable years beginning before January 1, 1997, at the same time as for federal tax purposes.)

Except as indicated below, the following federal laws enacted during 1996 apply for Wisconsin income tax purposes at the same time as for federal purposes:

- The Small Business Job Protection Act of 1996 (Public Law 104-188), enacted August 20, 1996.
- The Health Insurance Portability and Accountability Act of 1996 (Public Law 104-191), enacted August 21, 1996.
- The Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (Public Law 104-193), enacted August 22, 1996.

The following provisions of Public Law 104-188 do not apply for Wisconsin income tax purposes for taxable years beginning before January 1, 1997:

- Section 1123 relating to the exclusion for the value of lodging furnished by an academic health center.
- Section 1202 relating to the extension of the exclusion for employer-provided educational assistance program benefits and the limitation of the exclusion to education below the graduate level.
- Section 1204 relating to the research credit.
- Section 1311 relating to the reduction of an S corporation's accumulated earnings and profits by an amount equal to the portion (if any) of such accumulated earnings and profits which were accumulated in any taxable year beginning before January 1, 1983.
- Section 1605 relating to the repeal of the exclusion for punitive damages and for damages not attributable to physical injuries or sickness.

Note: See the *Wisconsin Tax Bulletin* 100 (January 1997), pages 46 through 50, for a description of the various provisions of Public Law 104-188 and Public Law 104-191 which affected taxable years which began before January 1, 1997.

3. **Taxation of Nonresidents and Part-Year Residents** (1997 Act 27, create sec. 71.06(2s), effective for taxable years beginning in 1997.)

For nonresident individuals, including individuals changing their domicile into or from Wisconsin during the taxable year, the income tax brackets shall be multiplied by a fraction, the numerator of which is Wisconsin adjusted gross income and the denominator of which is federal adjusted gross income.

For married persons filing separately, "adjusted gross income" means the separate adjusted gross income of each spouse. For married persons filing jointly, "adjusted gross income" means the total adjusted gross income of both spouses.

If an individual and that individual's spouse are not both domiciled in Wisconsin during the entire taxable year, the tax brackets on a joint return shall be multiplied by a fraction, the numerator of which is their joint Wisconsin adjusted gross income and the denominator of which is their joint federal adjusted gross income.

Example: The 1997 tax brackets for a single individual are:

- the first $7,500 of taxable income is taxed at 4.9%,
- the second $7,500 of taxable income is taxed at 6.55%, and
- taxable income over $15,000 is taxed at 6.93%.

Assume a single individual is a nonresident of Wisconsin for 1997. The individual has Wisconsin adjusted gross income of $15,000 and federal adjusted gross income of $30,000. The ratio of Wisconsin adjusted gross income to federal adjusted gross income is 50% ($15,000 ÷ $30,000 = 1/2 or 50%).

The 1997 tax brackets for this individual are:

- the first $3,750 ($7,500 x 50%) of taxable income is taxed at 4.9%,
- the second $3,750 ($7,500 x 50%) of taxable income is taxed at 6.55%, and
- taxable income over $7,500 ($15,000 x 50%) is taxed at 6.93%.

4. **Subtraction Allowed for Long-Term Care Insurance** (1997 Act 27, amend sec. 71.07 (5)(a)15, effective October 14, 1997; and create sec. 71.05 (6)(b)26, effective for taxable years beginning on or after January 1, 1998.)

For taxable years beginning on or after January 1, 1998, a subtraction from federal adjusted gross income is allowed when computing Wisconsin adjusted gross income for the amount paid by a person for a long-term care insurance policy, determined as follows:

(a) Subtract the amounts deducted from gross income for a long-term care insurance policy in the calculation of federal adjusted gross income from the amount paid by the person for a long-term care insurance policy.

(b) For a person who is a nonresident or a part-year resident of Wisconsin, modify the amount calculated under (a) by multiplying the amount by a fraction the numerator of which is the person's wages, unearned income, and net earnings from a trade or business that are taxable by Wisconsin and the denominator of which is the person's total wages, unearned income, and net earnings from a trade or business.

(c) Reduce the amount calculated under (a) or (b) above (whichever applies) to the person's aggregate wages, unearned income, and net earnings from a trade or business that are taxable by Wisconsin.

"Long-term care insurance policy" means a disability insurance policy or certificate advertised, marketed, offered or designed primarily to provide coverage for care that is provided in the insured person's home or in institutional and community-based settings and that is convalescent or custodial care or care for a chronic condition or terminal illness. The term does not include a medicare supplement policy or medicare replacement policy or a continuing care contract. "Long-term care insurance policy" applies to a policy that covers the person and his or her spouse.

Note: The amount claimed as a subtraction for a long-term care insurance policy cannot be used in the computation of the Wisconsin itemized deduction credit.

5. **Penalty Imposed on Certain Distributions From Medical Savings Accounts** (1997 Act 27, amend sec. 71.10(4)(j), and repeal and recreate sec. 71.83(1)(c), effective for taxable years beginning on or after January 1, 1997.)

For federal purposes, an additional tax of 15 percent is imposed under sec. 220(f)(4) of the Internal Revenue Code on any amount paid or distributed out of a medical savings account which is not used exclusively to pay the qualified medical expenses of the account holder.

A penalty is imposed on such distributions for Wisconsin tax purposes. The Wisconsin penalty is equal to 33 percent of the federal penalty tax. The department shall assess, levy, and collect the penalty in the same manner as it assesses, levies, and collects taxes under Chapter 71.

6. **Provisions Relating to Medical Savings Accounts Repealed** (1997 Act 27, repeal secs. 71.05(6)(a)19 and (b)24, and 71.07(5)(a)7, effective for taxable years beginning on or after January 1, 1997.

The provisions in the Wisconsin Statutes relating to Wisconsin medical savings accounts are repealed. (**Note:** These provisions were never implemented.)

Note: For taxable years beginning on or after January 1, 1997, Wisconsin has adopted the federal Internal Revenue Code (with some exceptions) as amended to December 31, 1996 (see Item A.1). Therefore, any exclusion from income or deduction relating to medical savings accounts which applies for federal tax purposes also applies for Wisconsin.

7. **Excess Distributions From Passive Foreign Investment Companies** (1997 Act 27, create sec. 71.05(6)(a)20, effective for taxable years beginning on or after January 1, 1997.)

The amount of any excess distribution from a passive foreign investment company is added to federal adjusted gross income when computing Wisconsin taxable income.

8. **Federal S Corporation Law Changes Adopted** (1997 Act 27, repeal sec. 71.01(15), renumber sec. 71.125 to 71.125(1) and amend sec. 71.125(1) as renumbered, amend sec. 71.05(6)(intro.), and create secs. 71.122 and 71.125(2), effective for taxable years beginning on or after January 1, 1997.)

See Item B.3.

9. **Estimated Tax Provisions for 1997 Modified** (1997 Act 27, create a nonstatutory provision, effective October 14, 1997.)

Any increase in estimated tax payments that are due before October 14, 1997, solely because of Act 27 shall be prorated among, and paid with, estimated payments that are due after October 14, 1997.

10. Income Tax Rates Reduced (1997 Act 27, renumber sec. 71.06(2s), as created by 1997 Act 27, to 71.06(2s)(a) and amend as renumbered, amend secs. 71.06(1)(intro.), (2)(intro.), (a)(intro.) and (b)(intro.), and (2m) and 71.67(4)(a) and (5)(a), and create sec. 71.06(1m), (2)(c) and (d), and (2s)(b), effective for taxable years beginning on or after January 1, 1998, and create sec. 71.06(2e), effective for taxable years beginning on or after January 1, 1999.)

For taxable years beginning on or after January 1, 1998

a. The tax rates for single persons, heads of households, and fiduciaries, except fiduciaries of nuclear decommissioning trust or reserve funds, are as follows:

(1) On all taxable income from $0 to $7,500, 4.85%.

(2) On all taxable income exceeding $7,500 but not exceeding $15,000, 6.48%.

(3) On all taxable income exceeding $15,000, 6.87%.

b. The tax rates for married persons filing jointly are as follows:

(1) On all taxable income from $0 to $10,000, 4.85%.

(2) On all taxable income exceeding $10,000 but not exceeding $20,000, 6.48%.

(3) On all taxable income exceeding $20,000, 6.87%.

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

(1) On all taxable income from $0 to $5,000, 4.85%.

(2) On all taxable income exceeding $5,000 but not exceeding $10,000, 6.48%.

(3) On all taxable income exceeding $10,000, 6.87%.

See Item A.3. for the treatment of nonresident and part-year resident individuals.

For taxable years beginning on or after January 1, 1999

The maximum dollar amount in each tax bracket, and the corresponding minimum dollar amount in the next bracket shall be increased each year by a percentage equal to the percentage change between the U.S. consumer price index for all urban consumers, U.S. city average, for the month of August of the previous year and the U.S. consumer price index for all urban consumers, U.S. city average, for the month of August of the year before the previous year, as determined by the federal Department of Labor. Each amount that is revised shall be rounded to the nearest multiple of $10 if the revised amount is not a multiple of $10 or, if the revised amount is a multiple of $5, such amount shall be increased to the next higher multiple of $10. The Department of Revenue shall annually adjust the changes in dollar amounts and incorporate the changes into the income tax forms and instructions.

11. Gain Excluded on Disposition of Certain Business and Farming Assets (1997 Act 27, create secs. 71.05(6)(b)25, 71.78(4)(p), and 71.83(1)(d), effective for taxable years beginning on or after January 1, 1998.)

Gain, as computed under the Internal Revenue Code, on the sale or disposition of business assets or on assets used in farming, including shares in a corporation or trust, is excluded from Wisconsin taxation if the following conditions are met:

- The assets must have been held more than one year.
- The assets are disposed of to persons who are related to the seller or transferor by blood, marriage, or adoption within the 3rd degree of kinship.