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# Budget Briefs

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## TAX CHANGES IN 2005 WISCONSIN ACT 25

The biennial state budget act, 2005 Wisconsin Act 25, passed by the legislature and signed by Governor Jim Doyle on July 25, 2005, includes a number of provisions affecting the tax liability of Wisconsin residents. Other tax changes were eliminated or modified by some of the governor's 139 vetoes.

### TAX REDUCTIONS

2005 Wisconsin Act 25 will reduce the taxes of some Wisconsin taxpayers.

**Social Security Benefits Excluded from Income Tax (Sections 1286gm, 1286hm, and 1286im).** Beginning in 2008, Wisconsin will no longer collect income tax on social security benefits. Currently, single taxpayers who receive more than \$25,000 in income in a year, or joint filers whose income exceeds \$32,000 in a year have 50% of their social security benefits taxed as income. Those whose income falls below these thresholds pay no income tax on their social security benefits. By taxable year 2008 all Wisconsin residents' social security benefits will be excluded from income tax. The legislature proposed phasing-in the social security benefits income tax exclusion over the course of three years. Under the legislature's plan, the currently taxable share of social security benefits would be reduced by 30% in taxable year 2007, by 60% in taxable year 2008, and by 100% in taxable year 2009 and thereafter. The governor used his partial veto power to eliminate the phase-in period so the 100% exclusion will begin in 2008.

**Income Tax Deduction for Tuition Increased (Sections 1287, 1288, and 9341 (15)).** 2005 Wisconsin Act 25 also increases the income tax deduction for higher education tuition. Prior to Act 25 this income tax deduction was a flat \$3000 per eligible student. The

new deduction will be equal to twice the average amount charged by the University of Wisconsin Board of Regents at four-year institutions for resident undergraduate academic fees for the most recent fall semester. This amount will be determined based on the fees set by September 1 of each year, and can be applied to any public or private two- or four-year institution of higher learning in Wisconsin, and at certain public institutions in Minnesota. The deduction will first apply to taxable year 2005.

**Income Tax Deduction for Health Insurance Premiums Increased (Sections 1286e, 1288e, 1288f, 1288g, and 1288h).** There are two provisions in 2005 Wisconsin Act 25 that will allow income tax deductions for health insurance premiums. The first provision will increase the current income tax deduction for health insurance premiums paid by a person whose employer does not contribute to his or her health insurance. The second provision will create a new deduction for health insurance premiums paid by a person who has no employer and no self-employment income. The income tax deduction in the first provision will increase from the currently available 50% to a 100% deduction for health insurance premiums paid beginning in taxable year 2006. The newly created deduction in the second provision will be phased in, starting with taxable year 2006 with a deduction of about 33%, depending on the taxpayer's circumstances, and ending with a 100% deduction by taxable year 2009 and thereafter.

**Petroleum Inspection Fee Reduced (Section 2094f and 9408 (1x)).** Beginning May 1, 2006, 2005 Wisconsin Act 25 will cut the petroleum inspection fee from three cents per gallon to two cents per gallon. The petroleum inspec-

tion fee is currently used to reimburse property owners for costs associated with removing underground fuel tanks that are leaking fuel into the groundwater. The program will have sufficient funds to continue functioning even after the one cent reduction.

**Property Tax Credit for Certain Veterans or their Spouses Created (Sections 1311j and 9341).** 2005 Wisconsin Act 25 creates an income tax credit equal to 100% of the real estate and property taxes paid by some veterans or their unremarried surviving spouses. The credit may be claimed by veterans over 65 with 100% service-related disability, unremarried spouses of veterans killed on duty, or spouses of deceased veterans with 100% service-related disability who were over the age of 65 when they died. The credit cannot be claimed if the taxpayer claims the property tax/rent credit, the farmland tax relief credit, the homestead credit, or the farmland preservation credit. The credit, which only applies to a principal residence, will first be available for taxable year 2005.

#### **TAX PROVISIONS VETOED**

2005 Wisconsin Act 25 contained other tax reductions that were vetoed by the governor.

**Income Tax Deduction for Health Savings Accounts Created (Sections 1432m, 1450g, and 9341 (5m)).** 2005 Wisconsin Act 25 would have adopted certain portions of the federal Internal Revenue Code (IRC) to allow pre-tax contributions to qualified health savings accounts beginning in taxable year 2005. This would have updated Wisconsin references to the IRC to conform to existing federal income tax exclusions and deductions for health savings accounts. Under federal law, these contributions could only be made by eligible individuals covered by a high-deductible health insurance plan, and only to an eligible health savings account, to cover qualified

medical expenses. In his veto message, the governor indicated he vetoed this measure because health savings accounts are linked to high-deductible health insurance and this link could discourage employer-sponsored health insurance. Instead, the veto message suggested that the issue of health savings accounts should be addressed in a comprehensive health care package.

**Income Tax Credit for Adopted Children Created (Sections 1286Lm, 1311ia, and 9341 (4k)).** 2005 Wisconsin Act 25 would have created an income tax *credit* for adoption expenses and eliminated the income tax *deduction* for those expenses. The new income tax credit of up to \$5,000 would have been allowed for eligible adoption expenses that exceeded the amount of the federal income tax adoption credit. Any unused portion of the \$5,000 credit could have been carried forward for up to five future tax years. The governor stated in his veto message that he vetoed these sections of the budget because adoptive parents already receive an income tax deduction under existing law.

**Income Tax Credit for Home School and Private School Dependents Created (Sections 451u, 1311p, and 9341 (10p)).** 2005 Wisconsin Act 25 would have created an individual income tax credit for each of a taxpayer's dependents enrolled in kindergarten through twelfth grade at an eligible private school or dependents in that grade range who are home-schooled. The credit would have been \$100 per eligible student and would have been available beginning in taxable year 2006. The governor indicated in his veto message that he vetoed the measure because it undermined the state's ability to fund public education at the same time as it gave money to residents whose children are not enrolled in the public school system.