



CHAPTER 3

**INDIVIDUAL INCOME
TAXES**

Introduction

Of the major components of Wisconsin's tax system, the individual income tax is one of the most poorly structured, ranking 39th on our *State Business Tax Climate Index*.³⁵

Wisconsin's individual income tax has a graduated-rate structure, with four brackets levying different rates on different levels of marginal income. At 7.65 percent, Wisconsin's top marginal individual income tax rate is higher than the top rates in all but eight states and the District of Columbia.³⁶ In addition, Wisconsin's individual income tax brackets and standard deduction are structured such that married taxpayers filing jointly face higher tax burdens than single individuals with the same combined income, resulting in a marriage penalty.

In fiscal year 2016, Wisconsin's individual income tax generated nearly \$7.5 billion for the state, accounting for 42.5 percent of Wisconsin's total state tax collections, higher than the 37 percent national average.³⁷

Individual income taxes are not, of course, exclusively of interest to individual taxpayers, as "pass-through" businesses, including sole proprietorships, partnerships, limited liability companies (LLCs), and S corporations pay taxes on their business profits under the individual income tax code. Since these taxes impact Wisconsin employers, it is important to consider impacts on businesses as well as individual payers when contemplating changes to the individual tax code.

In this chapter, we provide a broad overview of Wisconsin's individual income tax, outline issues with the current system, and discuss potential reform options.

A Brief History of Wisconsin's Individual Income Tax

In 1911, Wisconsin became the first state to adopt and successfully retain an individual income tax, doing so even before the federal individual income tax was established in 1913.³⁸ Before 1911, 16 states attempted to tax income but were unable to generate significant revenue from the tax due to enforcement difficulties. Wisconsin's individual income tax, however, was initially characterized less as a source of new revenue and more as a means to reduce property taxes on farmers.³⁹

Prior to adopting an individual income tax, Wisconsin relied almost exclusively on property taxes, in accordance with the system of taxation established in the Wisconsin Constitution. Wisconsin's property tax included both real property (such as land,

35 Jared Walczak, Scott Drenkard, and Joseph Bishop-Henchman, *2019 State Business Tax Climate Index*, Tax Foundation, Sept. 26, 2018, 3, <https://taxfoundation.org/publications/state-business-tax-climate-index/>.

36 Morgan Scarboro, *Facts and Figures 2018: How Does Your State Compare?* Tax Foundation, March 21, 2018, Table 12, <https://taxfoundation.org/facts-figures-2018/>.

37 U.S. Census Bureau, "2016 State & Local Government Finance Historical Datasets and Tables," <https://www.census.gov/data/datasets/2016/econ/local/public-use-datasets.html>.

38 Scott Drenkard and Richard Borean, "When Did Your State Adopt Its Income Tax?" Tax Foundation, June 10, 2014, <https://taxfoundation.org/when-did-your-state-adopt-its-income-tax/>.

39 Wisconsin Historical Society, "Wisconsin Income Tax is 100 Years Old," accessed Nov. 8, 2018, <https://www.wisconsinhistory.org/Records/Article/CS322>.

buildings, and fixtures) and tangible personal property (assets that can be touched and moved, such as furniture and appliances). However, taxes on movable assets proved unpopular and easy to evade, so proponents of the individual income tax presented it as a more viable alternative to the existing system.⁴⁰

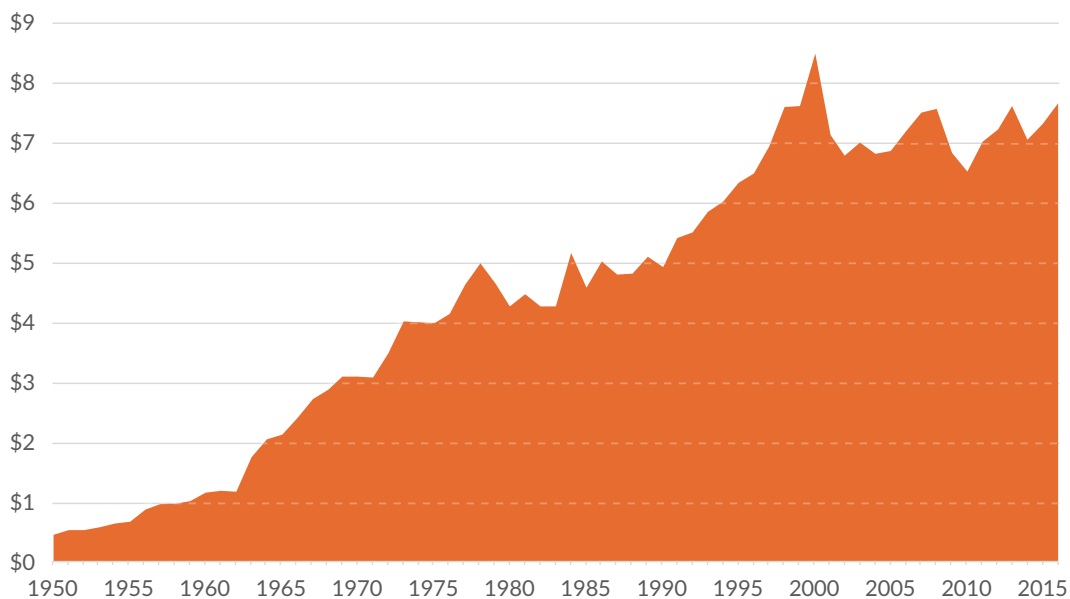
While the Wisconsin Constitution established strong parameters for uniform application of the property tax (the Uniformity Clause⁴¹) to prevent different classes of property from being assessed or taxed at different rates or assessment ratios, the individual income tax was structured as a progressive tax from the outset. Wisconsin's individual income tax has seen numerous significant changes since its inception, but it has never departed from its progressive structure and remains one of the most progressive individual income taxes in the U.S.

Wisconsin's Individual Income Tax Collections: Then and Now

Wisconsin's individual income tax collections have grown significantly over time but have seen sizable swings, dipping notably during recessionary periods (Figure 3a). In real terms, Wisconsin's individual income tax generates approximately seven times more revenue today than it did in 1960.⁴²

FIGURE 3a.

Wisconsin Individual Income Tax Collections, 1950-2016 (Billions of 2017 Dollars)



Note: Dollar amounts are inflation-adjusted based on the annual average Consumer Price Index for All Urban Consumers (CPI-U) with a 2017 base year.

Source: U.S. Census Bureau, *State and Local Government Finances*; Bureau of Labor Statistics, *Consumer Price Indexes* (All Urban Consumers).

40 Kossuth Kent Kennan, "The Wisconsin Income Tax," in *The Annals of the American Academy of Political and Social Science* 58 (March 1915): 65-76, <http://www.jstor.org/stable/1012848>.

41 Article VIII, section 1 of the Wisconsin Constitution.

42 See U.S. Census Bureau, "2016 State & Local Government Finance Historical Datasets and Tables."

While collections grew during the early decades of Wisconsin's individual income tax, they began to skyrocket starting in 1963. This spike in collections occurred for a combination of reasons, including rapid population growth, a growing economy, and individual income tax rate increases in 1962, 1971, and 1972.⁴³ In addition, Wisconsin's individual income tax brackets were not yet indexed for inflation, and high rates of inflation pushed taxpayers into higher-than-usual tax brackets, even without increases in real income, a concept known as "bracket creep." During the 1960s and 1970s alone, collections quadrupled (in real terms).

Collections briefly dropped in 1979, when the state's 16 income tax brackets were consolidated into eight as part of a tax reform and reduction law spearheaded by Governor Lee Sherman Dreyfus (R). In 1980, the state's individual income tax brackets were indexed for inflation for the first time, stabilizing collections. In addition, a "double-dip" recession occurred in 1980 and 1981-1982, slowing collections growth.⁴⁴

From 1983 until 2001, indexing was again suspended, and bracket creep contributed to another sharp increase in real collections, which nearly doubled during the 1980s and 1990s alone. In the middle of that period, the Tax Reform Act of 1986 broadened the federal individual income tax base and lowered rates. Wisconsin adopted many of the federal base-broadening reforms into its own tax code, which enabled the state to lower its own individual income tax rates even while collections continued to increase.⁴⁵

Shortly before the turn of the century, Wisconsin's individual income tax collections reached an all-time high, but during the tenure of Governor Tommy Thompson (R), the 1997-1999 budget consolidated four brackets into three, reduced rates, created a deduction for higher education tuition expenses, and conformed to new federal provisions, including the new Roth IRA. As a result, Wisconsin's individual income tax collections again declined.

The 1999-2001 legislative session brought further tax changes, including an increase in the standard deduction, the creation of personal exemptions, the addition of a fourth bracket, the indexing of brackets for inflation, and a reduction in rates, which led to further collections reductions.

Within the past decade, several additional policy changes have impacted the state's individual income tax collections. In 2008, during Governor Jim Doyle's (D) second term, the state stopped taxing Social Security benefits. The 2008-2009 recession saw revenue decline, so in response, lawmakers added a new top bracket at a rate of 7.75 percent, increasing collections. In 2013, during Governor Scott Walker's (R) first term, all marginal rates were reduced, and five brackets were consolidated into the current four, with a top rate of 7.65 percent.

43 *The Wisconsin Taxpayer*, "One Hundred Years and Counting: Wisconsin's Income Tax: History, Process, and Filers" 84, no. 3 (March 2016): 4, https://wispolicyforum.org/wp-content/uploads/2018/07/1603_State-Income-Tax.pdf.

44 *Ibid.*

45 *Ibid.*

Today, the individual income tax accounts for a substantial share of Wisconsin's tax revenue, generating 42.5 percent of total state tax collections in 2016, more than the general sales tax and corporate income tax combined. Wisconsin's reliance on its individual income tax is high compared to other states; on average, state individual income taxes generate only about 37 percent of total state tax collections.⁴⁶

Comparing Wisconsin's Individual Income Tax Structure to Regional and National Competitors

Wisconsin's individual income tax system ranks 39th on the individual income tax component of our *State Business Tax Climate Index*, signaling much room for improvement in terms of rates and structure. While Iowa and Minnesota rank even lower than Wisconsin due to higher top rates and worse structures, several of Wisconsin's regional competitors rank significantly better on individual income taxes, including Michigan (12th), Illinois (13th), and Indiana (15th).

TABLE 3a.
State Business Tax Climate Index
Individual Income Tax Component Rankings

Wisconsin and Select Regional Competitors (2019)

| State | Component Ranking |
|-----------|-------------------|
| Wisconsin | 39th |
| Illinois | 13th |
| Indiana | 15th |
| Iowa | 42nd |
| Michigan | 12th |
| Minnesota | 46th |

Source: Tax Foundation, 2019 *State Business Tax Climate Index*.

Illinois, Michigan, and Indiana each have a well-structured flat individual income tax, with low rates of 4.95 percent, 4.25 percent, and 3.23 percent, respectively. (While Illinois has a flat individual income tax rate of 4.95 percent, the state imposes a 1.5 percent surtax on business income, bringing the rate to 6.45 percent for owners of pass-through businesses.)

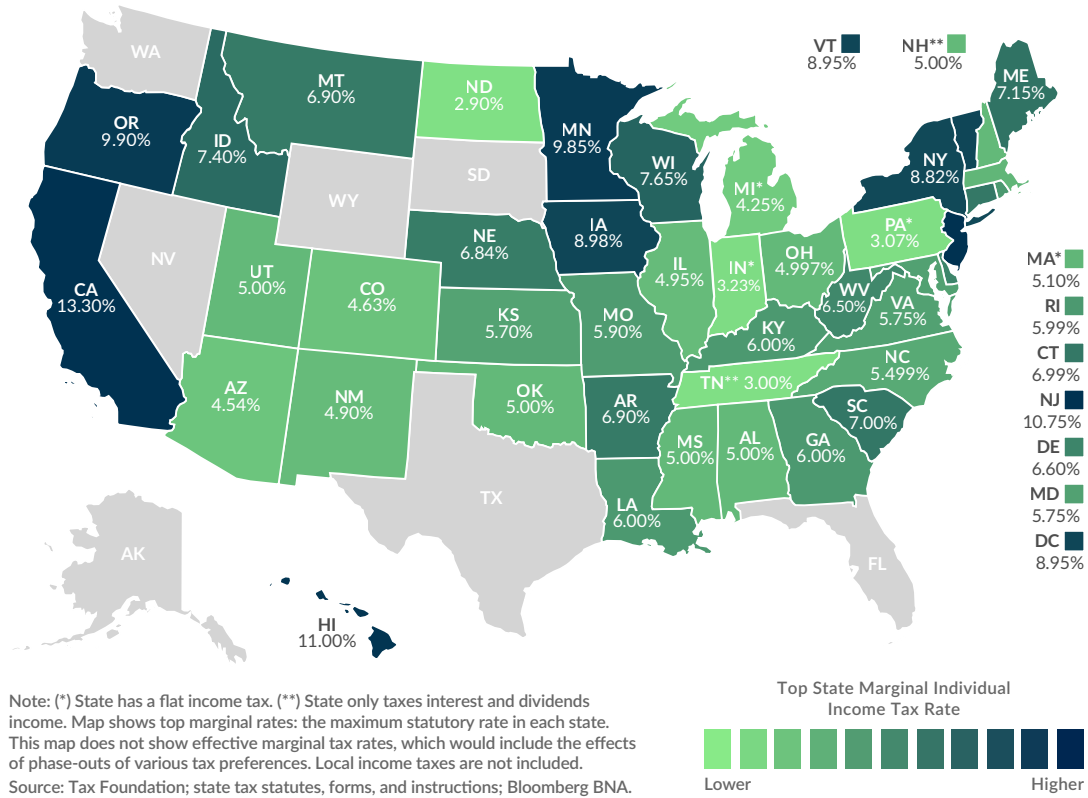
Wisconsin's four-bracket graduated-rate tax stands in sharp contrast to the low, flat rates in Illinois, Indiana, and Michigan. At 7.65 percent, Wisconsin's top marginal individual income tax rate is higher than the top rates in all but eight states (California, Hawaii, New Jersey, Oregon, Minnesota, Vermont, Iowa, and New York) and the District of Columbia.⁴⁷ Figure 3b shows the top individual income tax rate in each state.

46 See U.S. Census Bureau, "2016 State & Local Government Finance Historical Datasets and Tables."

47 Morgan Scarborough, *Facts and Figures 2018: How Does Your State Compare?* Table 12.

FIGURE 3b.

Top State Marginal Individual Income Tax Rates, 2018



Wisconsin’s four-bracket, graduated-rate income tax is currently levied at rates of 4 percent, 5.84 percent, 6.27 percent, and 7.65 percent. Table 3b shows Wisconsin’s individual income tax rate schedules for single filers and married couples filing jointly.

TABLE 3b. Individual Income Tax Rates (Tax Year 2018)

| Single Filers | | Married Filing Jointly | |
|----------------|-------|------------------------|-------|
| Taxable Income | Rate | Taxable Income | Rate |
| \$0+ | 4.00% | \$0+ | 4.00% |
| \$11,450+ | 5.84% | \$15,270+ | 5.84% |
| \$22,900+ | 6.27% | \$30,540+ | 6.27% |
| \$252,150+ | 7.65% | \$336,200+ | 7.65% |

Source: Wisconsin Department of Revenue.

Wisconsin’s income tax brackets are structured such that taxpayers whose taxable income falls entirely within the 4 percent bracket are taxed at a lower rate than they would be with the same amount of taxable income in most other states. However, compared to other states, Wisconsin’s rates increase quickly with increases in marginal income.⁴⁸ Wisconsin’s rates and bracket widths are structured such that most middle- and high-income taxpayers pay more in income taxes to Wisconsin than they would with the same amount of taxable income in most other states.

In fact, the second-lowest rate in Wisconsin's graduated-rate income tax (5.84 percent) is higher than the *top* income tax rate in 20 of the states that have an income tax.⁴⁹

Wisconsin's income tax is even more progressive than the rate structure shows. The state provides a number of other provisions which serve to lower the tax burden for low- and middle- income filers, such as an earned income tax credit (EITC). In fact, according to a report from the Institute on Taxation and Economic Policy (ITEP), Wisconsin ranks in the top 20 of states for its progressivity.⁵⁰ Excessive taxes on income discourage wealth creation and are therefore generally less desirable than taxes on consumption. In a comprehensive review of international econometric tax studies, Arnold et al. (2011) found that individual income taxes are among the most detrimental to economic growth, outstripped only by corporate income taxes. The authors found that consumption and property taxes are the least harmful.⁵¹

The economic literature on graduated-rate income taxes is particularly unfavorable.⁵² The Arnold et al. study concluded that reductions in top marginal rates would be beneficial to long-term growth, and Mullen and Williams (1994) found that higher marginal tax rates reduce gross state product growth. This finding even adjusts for the overall tax burden of the state, lending credence to the precept of broad bases and low rates.⁵³

Structural Elements

In addition to having high individual income tax rates compared to regional and national competitors, Wisconsin's income tax contains several additional features that hurt the state's competitiveness and warrant reexamination and improvement.

Marriage Penalty

An ideal individual income tax structure doubles bracket widths for married couples filing jointly to ensure that they do not face higher burdens than they would if filing separately. As can be seen in Table 3b (previous page), however, Wisconsin's marginal income thresholds are only about 33 percent higher for married couples filing jointly than they are for single filers, resulting in a substantial marriage penalty.

In addition to having significant tax implications for households, marriage penalties carry serious ramifications for pass-through businesses. The top quintile of income earners is dominated (85 percent) by married couples, and this same quintile also has the highest

49 Morgan Scarboro, *Facts and Figures 2018: How Does Your State Compare?* Tax Foundation, Table 12.

50 The Institute on Taxation and Economic Policy (ITEP) ranks Wisconsin 34th in its "Tax Inequality Index," with 1 representing the least equitable state and 51 representing the most equitable state. This means Wisconsin ranks in the top third of states for equitable tax treatment, according to ITEP's ranking. ITEP's Tax Inequality Index measures the effects "of each state's tax system on income inequality," asking one simple question: "Are incomes more or less equal after state taxes than before taxes?" For more on ITEP's ranking, see Meg Weihe, Aidan Davis, Carl Davis, Matt Gardner, Lisa Christensen Gee, and Dylan Grundman, "Who Pays? A Distributional Analysis of the Tax Systems in All 50 States, 6th Edition," Institute on Taxation and Economic Policy, October 2018, <https://itep.org/wp-content/uploads/whopays-ITEP-2018.pdf>.

51 Jens Arnold, Bert Brys, Christopher Heady, Åsa Johannsson, Cyrille Schwellnus, and Laura Vartia, "Tax Policy for Economic Recovery and Growth," *The Economic Journal* 121, no. 550 (February 2011).

52 See William McBride, "What is the Evidence on Taxes and Growth?" Tax Foundation, Dec. 18, 2012, <https://taxfoundation.org/what-evidence-taxes-and-growth>.

53 John K. Mullen and Martin Williams, "Marginal Tax Rates and State Economic Growth," *Regional Science and Urban Economics* 24, no. 6 (December 1994).

concentration of business owners of all income groups.⁵⁴ Therefore, marriage penalties have the potential to affect a significant share of pass-through businesses. Wisconsin is one of only 15 states with a marriage penalty.⁵⁵

In an attempt to abate this marriage penalty, Wisconsin offers a “married couple credit” available to married couples filing jointly when both spouses are employed. The married couple credit is available at a rate of 3 percent of qualified earned income, up to a maximum credit of \$480. In most cases, the married couple credit is enough to offset the impact of the disparity in bracket widths, but it is not a perfect fix.

There are some instances in which the credit is insufficient to negate the impact of the marriage penalty. This is most likely to be the case when two married taxpayers have high incomes, widely disparate incomes, or a significant amount of business income. There are also plenty of instances in which the married couple credit overcompensates for the disparity in bracket widths, resulting in a de facto marriage bonus. A more neutral and transparent system would simply double the bracket widths for married couples filing jointly.

Standard Deduction

Unlike most states that offer a uniform standard deduction regardless of income, Wisconsin has a sliding-scale standard deduction that is available only to taxpayers with taxable income below a specified amount. Even within the eligibility range, Wisconsin’s standard deduction is distinctly progressive, phasing out with increases in income.

In tax year 2018, the maximum standard deduction that can be claimed is \$10,580 for single filers and \$19,580 for married couples filing jointly.⁵⁶ This amount, which is adjusted annually for inflation, decreases quickly as income rises. Specifically, in tax year 2018, the standard deduction begins to phase out for single taxpayers with over \$15,500 in Wisconsin income and married couples with over \$22,000 in Wisconsin income. Taxpayers with Wisconsin income above a certain amount (\$103,500 for single filers and \$121,009 for married couples filing jointly) are not eligible to claim a standard deduction at all. Due to this sliding-scale feature, Wisconsin’s standard deduction can hardly be considered “standard” at all, as the actual deduction claimed varies from taxpayer to taxpayer and from one tax year to the next.

Like the state’s income tax bracket widths, Wisconsin’s standard deduction contains a marriage penalty, meaning married taxpayers generally receive a smaller standard deduction than they would if filing as two single individuals with the same amount of combined income. In the 2015-2017 biennial budget (2015 Wisconsin Act 55), Wisconsin legislators mitigated the total marriage penalty in the state’s standard deduction by

54 Scott A. Hodge, “Married Couples File Less than Half of All Tax Returns, But Pay 74 Percent of All Income Taxes,” Tax Foundation, March 25, 2003, <http://taxfoundation.org/article/married-couples-file-less-half-all-tax-returns-pay-74-percent-all-income-taxes>; Scott A. Hodge, “Own a Business? You May Be Rich: Two-Thirds of Taxpayers Hit by Highest Tax Rate Have Business Income,” Tax Foundation, May 5, 2003, <http://taxfoundation.org/article/own-business-you-may-be-rich-two-thirds-taxpayers-hit-highest-tax-rate-have-business-income>.

55 Jared Walczak, Scott Drenkard, and Joseph Bishop-Henchman, 2019 *State Business Tax Climate Index*, Tax Foundation, 67.

56 See “2018 Standard Deduction Table,” Wisconsin Income Tax, Form 1 Instructions, 55, <https://www.revenue.wi.gov/TaxForms2017through2019/2018-Form1-inst.pdf>.

\$20.9 million annually.⁵⁷ Specifically, for married couples filing jointly and married taxpayers filing separately, this law increased the amounts that could be claimed in the standard deduction while raising the phaseout level so more married taxpayers would be eligible to claim a standard deduction.

However, some disparity still exists. Legislators should consider removing the marriage penalty altogether by offering married taxpayers double the standard deduction amount that is available to single filers. To make the tax code even simpler and more neutral, a marriage penalty fix could be accompanied by elimination of the sliding scale altogether, which would make the standard deduction available to all taxpayers. For context, as of January 1, 2018, Georgia and Kentucky are the only states besides Wisconsin that do not double their standard deduction for married filers.⁵⁸

Personal Exemption

Wisconsin offers a personal exemption of \$700 per filer, spouse, and dependent, the sum of which is subtracted from the taxpayer's Wisconsin income in determining a taxpayer's taxable income. The exemption is \$950 for each person age 65 or older. Wisconsin's personal exemption is not indexed for inflation, meaning the real value of this exemption has decreased over time. Indexing the personal exemption for inflation would help preserve the real value of the personal exemption.

Itemized Deductions Credit

Unlike in most other states, Wisconsin taxpayers do not face a choice between claiming the standard deduction and itemizing their deductions, since Wisconsin does not offer its own itemized deductions. In lieu of itemized deductions, Wisconsin offers an itemized deductions credit, worth up to 5 percent of the amount claimed in federal deductions in four categories: certain out-of-pocket medical and dental expenses, home mortgage interest paid, charitable contributions, and casualty losses. Taxpayers who are eligible to claim a Wisconsin standard deduction must first subtract the standard deduction from the sum of those four itemization categories before claiming the 5 percent itemized deductions credit.

The interaction between the Wisconsin standard deduction and the itemized deductions credit is unnecessarily complex. The state could achieve similar outcomes in a more neutral and transparent manner by offering a robust standard deduction with no phaseout in lieu of the itemized deductions credit.

57 Wisconsin Department of Revenue and Department of Administration, "Summary of Tax Exemption Devices," February 2017, <https://www.revenue.wi.gov/DORReports/17sumrpt.pdf>.

58 Morgan Scarborough, "State Individual Income Tax Rates and Brackets for 2018," Tax Foundation, March 5, 2018, <https://taxfoundation.org/state-individual-income-tax-rates-brackets-2018/>.

Capital Gains

Wisconsin is unique in that it provides preferential treatment to capital gains. The federal government taxes capital gains at a lower rate than ordinary income, in part to account for the double layer of tax on capital gains income. Wisconsin's approach is different. Wisconsin's tax code allows a 30 percent deduction on net capital gains for assets held for more than one year when computing taxable income (for farm assets, it's 60 percent of net capital gains).⁵⁹ This income is excluded from a taxpayer's capital gains tax basis.

Another way to think about this provision is that it helps ensure that an investor is taxed on their real gains, not their nominal gains. While 30 percent is a rough estimate, it helps reduce the cost of capital to investors in the state.⁶⁰

On the other hand, Wisconsin limits the ability of taxpayers to deduct their capital losses. The federal government allows investors to deduct \$3,000 in capital losses per year (with a carryforward), but Wisconsin limits this to \$500 per year (with a carryforward).⁶¹ Ideally, the tax code would allow investors to fully capture their capital losses to ensure the tax code only taxes their actual income, not an inflated paper income.⁶²

This treatment of losses creates an asymmetry in the tax treatment. Capital gains are subject to tax when they are realized, while losses do not provide an equal tax benefit. This is exacerbated by the fact that the capital losses, while allowed to be carried forward, lose value over time. A \$500 deduction 10 years from now is far less valuable than a \$500 deduction this year.⁶³

Pass-Through Businesses Pay Individual Income Taxes

Individual income taxes are of considerable importance to pass-through entities, businesses that pay the individual income tax in lieu of the corporate income tax because the earnings "pass through" to the income tax form of the owners or shareholders rather than being remitted by the business entity itself. Because sole proprietorships, partnerships, limited liability companies (LLCs), and S corporations remit their income tax payments through the individual income tax, the individual code is a significant policy issue for most Wisconsin businesses.⁶⁴ Figure 3c shows the share of employer firms in each sector that pay individual income taxes in Wisconsin (separated by pass-through business type).⁶⁵

59 Wisconsin Department of Revenue, "Reporting Capital Gains and Losses for Wisconsin by Individuals, Estates, and Trusts," Publication 103, January 2019, <https://www.revenue.wi.gov/DOR%20Publications/pb103.pdf>.

60 Stephen J. Entin, "Getting 'Real' by Indexing Capital Gains for Inflation," Tax Foundation, March 6, 2018, <https://taxfoundation.org/inflation-adjusting-capital-gains/>.

61 Wisconsin Department of Revenue, "Reporting Capital Gains and Losses for Wisconsin by Individuals, Estates, and Trusts."

62 Kyle Pomerleau, "Testimony: The Tax Code as a Barrier to Entrepreneurship," Tax Foundation, Feb. 15, 2017, <https://taxfoundation.org/tax-code-barrier-entrepreneurship/>.

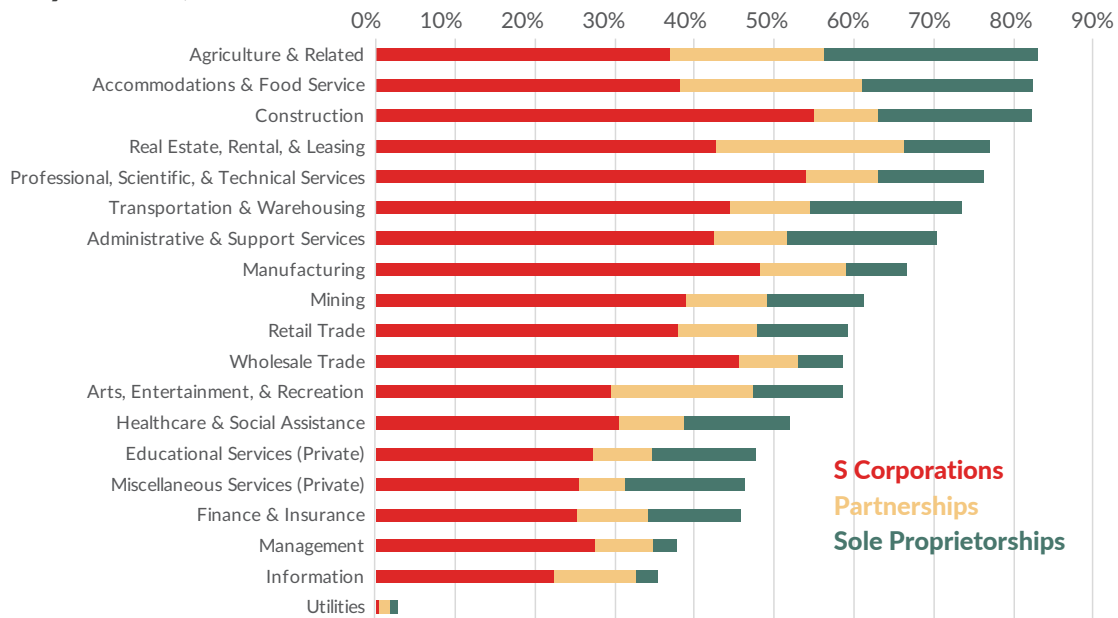
63 Ibid.

64 The issue is also a significant one for companies throughout the U.S. Over the past 30 years, the pass-through business sector has expanded significantly. Now, a majority of companies in the U.S. are pass-through businesses. See generally, Scott Greenberg, "Pass-Through Business: Data and Policy," Tax Foundation, Jan. 17, 2017, <https://taxfoundation.org/pass-through-businesses-data-and-policy/>.

65 U.S. Census Bureau, County Business Patterns, "Geographic Area Series: County Business Patterns by Legal Form of Organization," 2016.

FIGURE 3c.

Share of Employer Firms Paying the Individual Income Tax, By Sector, 2016



Source: Census Bureau, 2016 County Business Patterns.

While individual income taxes directly impact pass-through businesses, traditional C corporations care about these taxes as well, since high rates can impede their ability to attract and retain talented employees.

Individual Income Tax Reform Solutions

Our individual income tax reform solutions improve the tax code by consolidating brackets, reducing rates, and fixing the marriage penalty. These solutions will make the state more competitive with its neighbors, more attractive to prospective residents and employers, and more neutral in its application.

We have included four options for policymakers to consider. When paired with the other reforms outlined in the Executive Summary, each plan is roughly revenue neutral, although rates could be dialed up or down according to revenue needs.

All of our reform solutions reduce rates, consolidate brackets, and fix the marriage penalty. The following sections highlight the differences that exist among the four options.

Individual Income Tax Option A

Option A transitions the four-bracket, graduated-rate individual income tax to a flat tax with a rate of 4.82 percent. Under this plan, Wisconsin's rate would be lower than Illinois's flat rate of 4.95 percent and more competitive with the rates in Indiana (3.23 percent) and Michigan (4.25 percent).

In addition, Option A conforms to the federal standard deduction (set at \$12,000 for single filers and \$24,000 for married filers in Tax Year 2018, adjusted annually for inflation). As such, Wisconsin's standard deduction would be available to all Wisconsinites, without a complicated phaseout schedule or the marriage penalty that exists under current law. With a standard deduction that is available to all taxpayers, the state would have less reason to maintain its personal exemption or complicated itemized deductions credit, both of which would be repealed under this plan.

Individual Income Tax Option B

Option B restructures Wisconsin's individual income tax to make it similar to the fast-growing states in the southeastern U.S., with lower marginal rates and less progressivity in bracket structure. While not a flat tax, the tax structure in Option B moves away from penalizing marginal increases in income.

Specifically, Option B consolidates Wisconsin's four brackets into three while reducing rates and lowering marginal income thresholds, such that rates of 4 percent, 5 percent, and 6.8 percent are applied to income thresholds of \$0, \$10,000, and \$40,000.

Like Option A, Option B conforms to the federal standard deduction while repealing the personal exemption and itemized deductions credit.

The rate schedule for Option B is below.

TABLE 3c. OPTION B.
Individual Income Tax Rate Schedule

| Single Filers | | Married Filing Jointly | |
|----------------|-------|------------------------|-------|
| Taxable Income | Rate | Taxable Income | Rate |
| \$0+ | 4% | \$0+ | 4% |
| \$10,000+ | 5% | \$20,000+ | 5% |
| \$40,000+ | 6.80% | \$80,000+ | 6.80% |

Individual Income Tax Option C

Option C, like Option A and Option B, conforms to the federal standard deduction of \$12,200 for single filers and \$24,400 for married couples, and repeals both the personal exemption and itemized deductions credit. Option C also retains the rate structure of Option B by consolidating Wisconsin's four brackets into three, and lowering marginal income thresholds. Like Option B, rates of 4 percent, 5 percent, and 6.8 percent are applied to income thresholds of \$0, \$10,000, and \$40,000.

In effect, Option C's personal income tax reforms are identical to Option B. Option C's reforms focus more heavily on the Badger State's corporate income tax.

Individual Income Tax Option D

Option D retains the progressivity of the existing system while taking steps to promote economic growth and competitiveness. Specifically, this plan consolidates four brackets into three, essentially collapsing Wisconsin's second and third brackets into a wider bracket at a lower rate. Option D also reduces the top rate slightly, from 7.65 percent to 7.5 percent.

Option D retains the existing progressive sliding-scale standard deduction and phase-out schedule, but it eliminates the marriage penalty in the standard deduction by allowing married couples to claim double the amount, at every income level, that is available to single filers. Option D retains the personal exemption as it exists under current law, but it repeals the itemized deductions credit.

The rate schedule for Option D is below.

TABLE 3d. OPTION D.
Individual Income Tax Rate Schedule

| Single Filers | | Married Filing Jointly | |
|----------------|-------|------------------------|-------|
| Taxable Income | Rate | Taxable Income | Rate |
| \$0+ | 4% | \$0+ | 4% |
| \$20,000+ | 5% | \$40,000+ | 5% |
| \$150,000+ | 7.50% | \$300,000+ | 7.50% |

Impact of Individual Income Tax Solutions on Real People

The chart below shows how individual taxpayers would be impacted by the individual income tax reform solutions offered in Options A, B, C, and D. Most taxpayers would receive a net income tax cut under each tax reform option.

How Wisconsin Tax Reform Options Affect Real People (State Income Tax Liability)

| | Current Wisconsin Tax System | Option A | Option B | Option C | Option D |
|---|------------------------------|----------|----------|----------|----------|
|  Abigail One child Income: \$15,000 Filing Status: Head of Household | -\$138* | -\$138* | -\$138* | -\$138* | -\$138* |
|  Patrick & Samantha Retired no children Income: \$36,000 Filing Status: Married Filing Jointly | \$0 | \$0 | \$0 | \$0 | \$0 |
|  Daniel Single no children Income: \$50,000 Filing Status: Single | \$2,296 | \$1,832 | \$1,800 | \$1,800 | \$1,946 |
|  Jason & Nicole Two children Income: \$75,000 Filing Status: Married Filing Jointly | \$3,547 | \$2,458 | \$2,350 | \$2,350 | \$2,872 |
|  Monique Single no children Income: \$100,000 Filing Status: Single | \$5,893 | \$4,242 | \$5,164 | \$5,164 | \$4,746 |
|  Peter & Kelsey Two children Income: \$150,000 Filing Status: Married Filing Jointly | \$8,791 | \$6,073 | \$6,928 | \$6,928 | \$6,960 |

*Liability is negative depending on Earned Income Tax Credit (EITC) eligibility; for ineligible taxpayers at that income level, tax liability is \$0. Options as prepared do not adjust Wisconsin EITC (4% of federal if one child, 11% of federal if two children, 34% of federal if three or more children).

Source: Tax Foundation calculations using data from Internal Revenue Service and Wisconsin Department of Revenue. Excludes federal tax liability and share of state corporate income tax reduction. Estimates are static analysis that assumes no immediate economic growth from tax changes. Assumes head of household standard deduction matches federal (\$18,000).