

HOW THREE-FACTOR APPORTIONMENT PENALIZES IN-STATE INVESTMENT

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Criteria for a "Good" Tax

An essential first step in evaluating the pros and cons of any proposed change in tax policy is to clearly identify the government's objectives with respect to taxation. Although different groups may suggest different criteria, there is general agreement regarding the following core criteria for what makes a good tax.

- **Raising revenues:** The purpose of taxation is to raise revenues to provide public services, the level of which is determined by elected officials. A good tax should provide adequate revenues to cover budgeted outlays.
- **Economic growth:** A good tax does not impede economic growth by distorting the incentives of taxpayers to work hard, save and invest. In a free-market economy, consumers and businesses are assumed to be the best judges of what goods and services should be produced, and how resources should be allocated. Taxes can interfere with this natural efficiency since taxing an activity will tend to reduce the level of that activity. Therefore, a good tax neither favors nor disfavors particular types of economic activity, but instead allows free market forces to shape the decisions of consumers and businesses.
- **Simplicity:** A good tax is easy for taxpayers to understand and compute. A bad tax is complex and administratively costly, causing taxpayers to expend undue amounts of time and money to compute and pay their taxes, and making it burdensome for state authorities to administer the tax.
- **Fairness:** A good tax distributes the total tax burden among taxpayers in an equitable manner. Unfortunately, the concept of tax equity is difficult to define or measure, and ultimately involves ethical issues and value judgements. Nevertheless, tax reforms always invoke discussions of equity and fairness, and the accompanying debate is often an emotional one for lawmakers and taxpayers alike.

Disincentives Created by Property and Payroll Factors

Wisconsin's economic future depends on the degree to which businesses are encouraged to locate, expand or retain their operations in Wisconsin. Businesses consider a number of factors when deciding where to locate their operations, including the quality and cost of labor, proximity to markets, transportation costs, the cost of utilities, and the quality of local schools and other public services. To a great extent, this is a cost-minimization decision, and therefore differential tax burdens can play a significant role in determining where a business chooses to locate or expand. Economists have done extensive research on this issue, and have found that corporate income taxes and other tax factors can have a significant effect on a region's economic development.⁴ The impact of differential tax burdens can be particularly strong when a business is choosing between alternative sites within the same regional area (e.g., the economic corridor that lies along Interstate 94 between Chicago and Milwaukee), since non-tax factors such as labor costs may be quite similar within that region.

A three-factor apportionment formula attempts to measure the contribution of a corporation's capital (property), labor (payroll) and market (sales) in generating its business profits, and apportions that contribution to the state in which the underlying property, payroll or sales are located. Unfortunately, by apportioning income to a state in direct proportion to the amount of property and payroll located in the state, the three-factor formula imposes a tax penalty on businesses that choose to add jobs or expand their facilities within that state. In effect, including property and payroll in an apportionment formula transforms a state corporate income tax into a direct tax on the amount of property and payroll located within the state.⁵

⁴ For reviews of this research, see Phillips and Goss, "The Effect of State and Local Taxes on Economic Development: A Meta-Analysis," *Southern Economic Journal*, October 1995; Bartik, "The Effects of State and Local Taxes on Economic Development: A Review of Recent Research," *Economic Development Quarterly*, February 1992; and Wasylenko, "Taxation and Economic Development: The State of the Economic Literature," *New England Economic Review*, March-April 1997.

⁵ Gordon and Wilson, "An Examination of Multijurisdictional Corporate Income Taxation Under Formula Apportionment," *Econometrica*, November 1986.

To illustrate, assume a large corporation is interested in locating a major new manufacturing plant, structured as a separate subsidiary, somewhere along Interstate 94 between Chicago and Milwaukee. This manufacturing company is expected to generate an annual profit of \$10 million and will be subject to taxation in several states. Assume 20 percent of the plant's output will be sold in Wisconsin. Under current law, the subsidiary's Wisconsin apportionment percentage will be 10 percent if the plant is located south of the Illinois-Wisconsin border,⁶ but increases to 60 percent if the plant is located north of the border.⁷ Given Wisconsin's 7.9 percent corporate tax rate, the 50 percentage point difference in the Wisconsin apportionment percentage results in an additional \$395,000 per year in Wisconsin corporate income taxes.⁸ In contrast, under a single factor sales apportionment formula, the taxpayer's Wisconsin apportionment percentage would equal its Wisconsin sales factor of 20 percent regardless of where the plant is located, in which case there is no tax penalty for locating the plant in Wisconsin as opposed to Illinois.

In sum, Wisconsin's current three-factor formula creates a disincentive for businesses that require large investments in tangible property and payroll to locate their facilities in Wisconsin. The solution to this problem lies in removing this negative from the site location decision by applying the Wisconsin corporate income tax equally to all businesses, regardless of whether they locate facilities in Wisconsin. Eliminating this bias will allow business location decisions to be based primarily on non-tax factors.

Nationwide Trend Toward Emphasizing the Sales Factor

Historically, most states have used an equally-weighted three-factor apportionment formula.⁹ In recent decades, however, a significant number of states have

⁶ $[0\% \text{ property in WI} + 0\% \text{ payroll in WI} + (2)(20\% \text{ sales in WI})] \div 4 = 10\%$.

⁷ $[100\% \text{ property in WI} + 100\% \text{ payroll in WI} + (2)(20\% \text{ sales in WI})] \div 4 = 60\%$.

⁸ $[\text{Taxable income of } \$10,000,000] \times [50 \text{ percentage point increase in the Wisconsin apportionment percentage}] \times [7.9\% \text{ tax rate}] = \$395,000$. Because state income taxes are deductible for federal tax purposes, any increase in Wisconsin taxes is partially offset by a corresponding decrease in federal income taxes.

⁹ Hellerstein and Hellerstein, *State Taxation, Volume I: Corporate Income and Franchise Taxes* (Warren Gorham and Lamont, 1993), ¶8.06.

amended their apportionment formulae to place more weight on the sales factor with a corresponding reduction in the weight placed on the property and payroll factors. State lawmakers are attracted to such formulae for a couple of reasons. First, as discussed above, a single factor sales apportionment formula removes a tax disincentive for business expansion. Locating additional property or payroll in a state that use a sales-only formula has no effect on the amount of income taxable in that state. Second, a single factor sales formula shifts a greater portion of the corporate income tax burden from in-state corporations that have large amounts of property and payroll in the state but with sales nationwide to out-of-state corporations that have relatively low proportions of property and payroll but with substantial sales in the state.

At present, 11 states and the District of Columbia use an equally-weighted three-factor formula, while 35 states use formulae that place more weight on the sales factor.¹⁰ Wisconsin adopted a double-weighted sales formula in 1973. The following states use formulae that emphasize the sales factor:

- **Single factor sales formula**
 - » **Iowa, Nebraska and Texas** currently use a single factor sales formula.
 - » **Connecticut** enacted legislation in 1998 which allows financial service companies to use a single factor receipts formula. In addition, corporations deriving income from businesses other than the manufacture, sale or use of tangible property may also use a single factor sales formula. Businesses deriving income from the manufacture, sale or use of tangible property use the double-weighted sales formula.
 - » **Illinois** currently uses a double-weighted sales formula, but law changes enacted in 1998 increase the weight placed on the sales factor to 66.67

¹⁰ Boucher and Healy, *1998 Multistate Corporate Tax Guide, Volume 1* (Panel Publishers, 1998); and Donovan and Nakamura, 1160 T.M., *Income Taxes: State Formulary Apportionment Methods*. The 11 states that use an equally-weighted three-factor formula are Alabama, Alaska, Delaware, Hawaii, Kansas, Montana, North Dakota, Oklahoma, Rhode Island, Utah and Vermont. The remaining four states (Nevada, South Dakota, Washington and Wyoming) do not impose taxes measured by corporate income.

percent in 1999, 83.33 percent in 2000, and 100 percent (a single factor sales formula) starting in 2001.

- » **Massachusetts** amended its laws in 1996 to allow defense contractors to elect to use a single factor sales formula. Certain mutual fund service corporations may also use a sales-only formula. The formula used by manufacturers was also amended to weight the sales factor 60 percent in 1996, 70 percent in 1997, 80 percent in 1998, 90 percent in 1999, and 100 percent (a single factor sales formula) starting in 2000. Businesses other than defense contractors and manufacturers use a double-weighted sales formula.
- » **Mississippi** allows retailers, wholesalers and service companies to use a single factor sales formula. Manufacturers use either an equally-weighted three-factor formula or a double-weighted sales formula, depending on whether they sell their products principally at the wholesale or retail level.
- » **Missouri** offers businesses the option of using a single factor sales formula or an equally-weighted three-factor formula.
- » **South Carolina** permits companies other than manufacturers or dealers in tangible personal property to use a single factor sales formula. Manufacturers or dealers in tangible personal property use a double-weighted sales formula.
- **Double-weighted sales formula**
 - » **Arkansas, Arizona, California, Florida, Georgia, Idaho, Indiana, Kentucky, Louisiana, Maine, Maryland, New Jersey, New Mexico (through 1999), New York, North Carolina, Oregon, Pennsylvania, Tennessee (effective in 1999), Virginia (effective in 2000), West Virginia, and Wisconsin** all use a formula that weights the sales factor 50 percent, and the property and payroll factors 25 percent each.

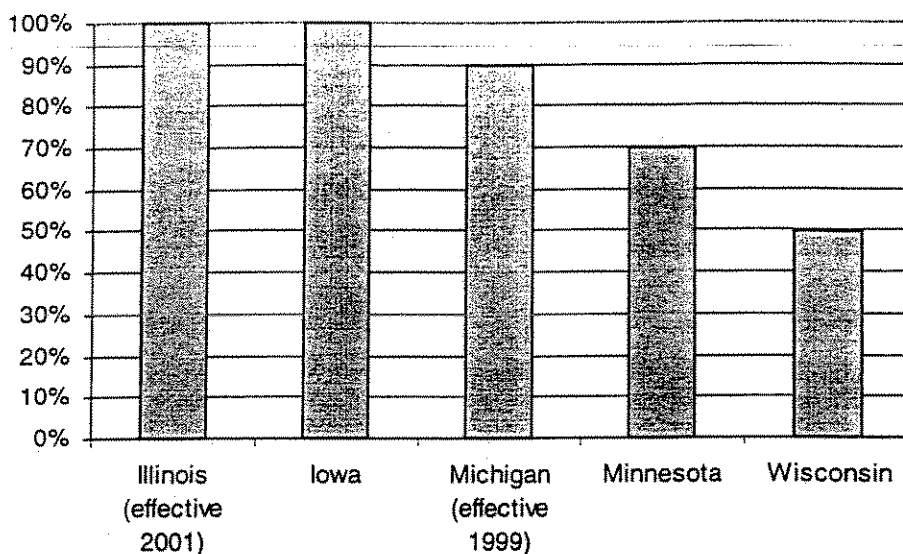
- **Other formulae that emphasize the sales factor**
 - » **Colorado** allows taxpayers to elect a two-factor formula that weights sales and property 50 percent each.
 - » **Michigan** used a double-weighted sales formula until 1996, when its formula was amended to increase the weight on the sales factor to 80 percent in 1997 and 1998, and 90 percent starting in 1999 (property and payroll will then be weighted 5 percent each).
 - » **Minnesota** uses a formula that weights sales 70 percent and property and payroll 15 percent each.
 - » **New Hampshire** uses a formula that weights sales 42.8 percent and property and payroll 28.6 percent each.
 - » **Ohio** currently uses a double-weighted sales formula. Effective in 1999, Ohio will use a formula that weights sales 60 percent and property and payroll 20 percent each.

Preemptive Strikes by Border States

The 1998 state business climate rankings of *Site Selection* magazine gave Wisconsin an overall ranking of 19th in the nation, whereas Michigan was ranked 3rd, Illinois 11th, Iowa 17th and Minnesota 18th.¹¹ It is worth noting that Wisconsin's border states have been particularly aggressive in changing their apportionment formulae to attract new business and expand economic growth with their borders. As Figure 1 indicates, Illinois, Iowa, Michigan and Minnesota all weight the sales factor more heavily than Wisconsin. Therefore, if Wisconsin were to increase the weight it places on the sales factor, it would merely be catching up with the competition.

¹¹ "1998's Business Climate Rankings: The Playing Field Levels," *Site Selection*, October/November 1998. The rankings are determined by the number of new and expanded facilities in a state, as well as a survey of corporate real estate executives.

Figure 1: Weighting of Sales Factor in Apportionment Formula



Increasing the weight assigned to the sales factor not only makes a state like Illinois a more attractive place to invest, it also has the effect of “exporting” the Illinois state tax burden from Illinois-based businesses to Wisconsin-based businesses. To illustrate, consider two corporations, Illinois Corp. and Wisconsin Corp. Each corporation does business only in Illinois and Wisconsin, has an annual profit of \$10 million, and has sales that are split 50-50 between Illinois and Wisconsin. The only difference between the two corporations is that Illinois Corp. has all of its property and payroll located in Illinois while Wisconsin Corp. has all of its property and payroll located in Wisconsin. Illinois and Wisconsin currently both use a double-weighted sales formula. Therefore, in 1998 Illinois Corp. apportioned 75 percent of its income to Illinois,¹² while Wisconsin Corp. apportioned 25 percent of its income to Illinois.¹³ Effective in 2001, Illinois will switch to a single factor sales formula. This will cause Illinois Corp.’s apportionment percentage to decrease from 75 percent to 50 percent, while Wisconsin Corp.’s apportionment percentage will increase from 25 percent to 50 percent. As the following table indicates, although Illinois’s adoption of a sales-only formula does not affect the total amount of Illinois tax paid by the two corporations,

¹² $[100\% \text{ property in IL} + 100\% \text{ payroll in IL} + (2)(50\% \text{ sales in IL})] \div 4 = 75\%$

\$182,500 of the total Illinois tax burden is exported from the Illinois-based corporation to the Wisconsin-based corporation.

	1998 Illinois tax (3-factor formula)	2001 Illinois tax (sales-only formula)	Change in Illinois tax
Illinois Corp.	\$547,500 ^a	\$365,000 ^c	-\$182,500
Wisconsin Corp.	<u>\$182,500^b</u>	<u>\$365,000^c</u>	+\$182,500
Totals	<u>\$730,000</u>	<u>\$730,000</u>	

^a Income of \$10 million × 75% apportionment percentage × 7.3% Illinois corporate tax rate

^b Income of \$10 million × 25% apportionment percentage × 7.3% Illinois corporate tax rate

^c Income of \$10 million × 50% apportionment percentage × 7.3% Illinois corporate tax rate

The only way for Wisconsin to mitigate this shifting of corporate tax burdens and thereby “level the playing field” is to also adopt a single factor sales apportionment formula.

13 $[0\% \text{ property in IL} + 0\% \text{ payroll in IL} + (2)(50\% \text{ sales in IL})] \div 4 = 25\%$

BENEFITS OF ADOPTING SINGLE FACTOR SALES APPORTIONMENT

Job Creation and Tax Revenues

Methodology and Sample Selection

Following earlier research conducted by Goolsbee and Maydew,¹⁴ we compile a panel data set on the apportionment formulae and corporate tax rates for states from 1978 to 1995. There have been approximately 20 different state apportionment formula changes over this period and this variation allows us to develop reasonably precise estimates of their economic effects. Because of the long time period, we are also able to control for economic factors that independently influence employment.

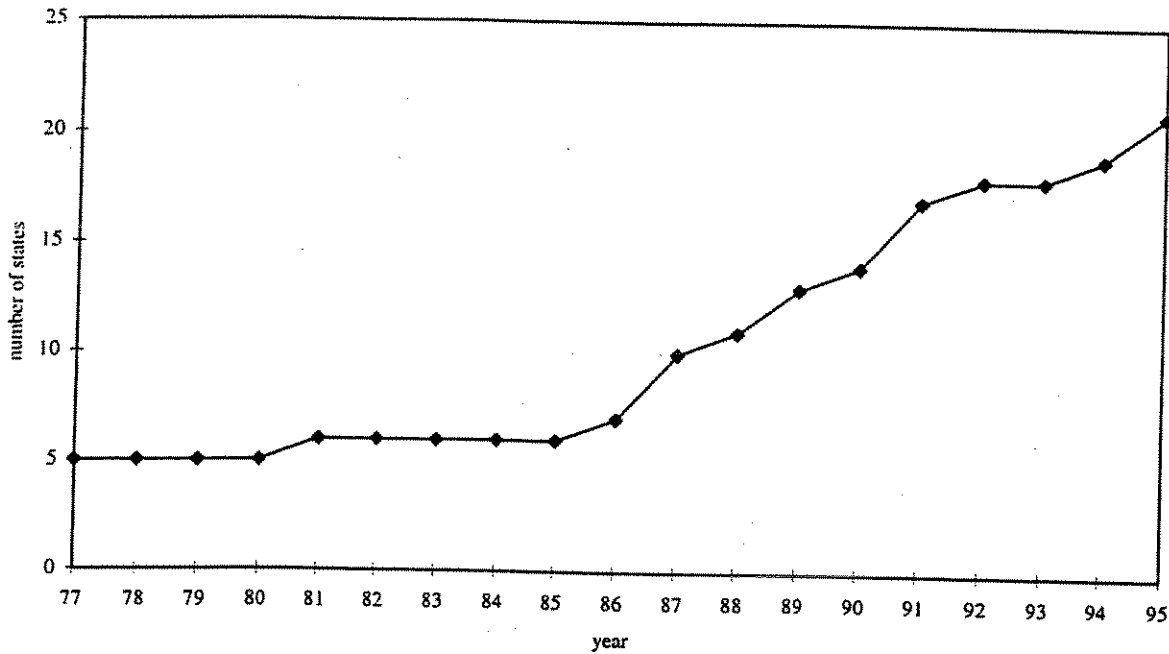
The data used in our study are as follows. First, the time series on the apportionment formulae cover all states with a corporate income tax. These data were gathered from Commerce Clearing House's *State Tax Handbook*, various state tax codes, issues of *Significant Features of Fiscal Federalism* (published by the Advisory Commission on Intergovernmental Relations) and discussions with selected state departments of revenue.

Figure 2 shows the number of states that have adopted more than the standard one-third weight on sales in their apportionment formulae over this sample, not counting states with optional apportionment formulae. There is a consistent upward trend that begins after 1978 with the *Moorman* case in which the Supreme Court ruled that Iowa's use of the single factor sales apportionment formula was constitutional.¹⁵

¹⁴ Goolsbee and Maydew, "Coveting Thy Neighbor's Manufacturing: The Dilemma of State Income Apportionment," 1998, NBER working paper No. 6614.

¹⁵ *Moorman Manufacturing Co. v. Bair*, 437 U.S. 267, 1978.

Figure 2: Number of States That Have Adopted an Increased Weighting on the Sales Factor



We match these apportionment formulae with state employment and earnings data compiled by the Bureau of Economic Analysis. These data include total private employment and total manufacturing employment by year for each state and are compiled from the ES-202 series of the Bureau of Labor Statistics and reported in the Bureau of Economic Analysis *State Personal Income* database. We also include the growth rate of average state personal income from the same source. For the national economy, we use data on the unemployment rate and the log of national employment. We allow the coefficient on the latter to vary by state in an attempt to control for population changes in a way that is not endogenous. The descriptive statistics for all the data in our sample are listed in Table 1.

Using these data, our basic empirical specification will regress the log of employment in state j in year t as follows:

$$\ln(EMPL_{jt}) = \alpha_j + \beta_1(Tax_{jt}) + \beta_2(\overline{Tax}_t) + \Gamma_1'Z_t + \Gamma_2'X_{jt} + \varepsilon_{jt}$$

where TAX_{jt} includes measures of the apportionment induced tax burden on payroll in the state, \overline{Tax}_t is the weighted average tax burden on payroll for all states in that year, the Z_t are

annual controls to account for macroeconomic factors that independently influence state employment (e.g., the national unemployment rate) or year dummies which absorb common macro variation, and the X_{jt} are state-level controls as well as state-specific time trends.

The basic approach is to estimate whether, conditional on the state of the economy and other variables, employment is higher when a state puts less weight on the payroll factor in its apportionment formula. The results below support the proposition.

Findings

Column (1) of Table 2 presents a basic panel regression for the log of manufacturing employment in a state on the tax terms, state fixed effects, state time trends, the state personal income growth rate, the national unemployment rate, and the log of national employment interacted with the state dummies to account for growth in the labor force. Following the theory presented above, our tax terms are the state corporate income tax rate interacted with the payroll weight in the apportionment formula and the weighted average of the same variable for all states in that year (states are weighted by average manufacturing employment over the sample).

In this basic specification, the coefficients are significant and have the predicted signs. The non-tax variables are unsurprising and the tax variables are statistically significant. Reducing the tax burden on payroll in the state by reducing the corporate rate or the payroll weight in the apportionment formula increases manufacturing employment significantly. When other states reduce their payroll tax burden it does the opposite. The magnitude of the own-tax coefficient indicates that for a state with the mean corporate tax rate, changing from a one-quarter to zero payroll weight (i.e., moving from double-weighted sales to single factor sales apportionment) increases manufacturing employment by 3.5 percent in the average state.

In column (2) we take federal corporate taxation into account, assuming that all states' corporate income taxes are deductible from the federal tax, for simplicity. We do this by replacing the state tax rate with the state rate times one minus the federal rate. Here again the evidence supports the view that higher payroll tax burdens within a state reduce employment and vice versa for the payroll tax burden in other states. The magnitudes are

also very similar. Moving from one-quarter weighting to zero weighting on payroll increases manufacturing employment by 2.4 percent for the average state.

While these specifications seem to indicate that the apportionment formula is important, both specifications impose that the apportionment formula and the corporate tax rate have identical effects. The apparent effect of apportionment changes, however, might be caused by spurious correlation with some other variable. Firms may respond only to the corporate rate, for example, and by including only an interaction term this makes the payroll weight look significant. On the other hand, if the true marginal tax rate facing the firm differs from the statutory rate, this will tend to reduce the estimated effect of the apportionment formula in the interaction term.

Columns (3) and (4), therefore, repeat the specifications of (1) and (2), but break the income tax induced payroll burden into two components: the payroll weight and the corporate tax rate. In both specifications, the corporate tax rate does not reduce the importance of the payroll weight. Indeed, in both cases the coefficient on the tax rate is not significantly different from zero while the coefficient on the payroll weight is both significant and the estimated effect is quite large.

Thus there probably is error in the true tax rate facing firms which reduces the coefficient on taxes and by separating the two components we can isolate the effect of the formula directly. In all four regressions, the state tax rate has no significant impact and the payroll weight does. Columns (5) and (6) simply verify that excluding state tax rates does not change the statistical significance of the payroll weight. The magnitude of the effect does increase, giving an upper-bound estimate of a 9.5 percent long-run increase in manufacturing employment from switching from double-weighted sales apportionment to single factor sales apportionment.

Finally, in column (7), we examine the impact on non-manufacturing employment. We expect the results to be proportionally smaller here than in the manufacturing sector. The coefficient on the tax rate shows that, indeed, apportionment changes do have a smaller effect on non-manufacturing but the effect is still statistically significant. For the average state, changing from one-quarter to zero payroll weight increases non-manufacturing employment by approximately 1.9 percent.

Projected Benefits for Wisconsin

In this section we look in detail at the employment effects on Wisconsin and the consequent revenue implications for the state. Since the specific estimates vary with the empirical specification, we present our most conservative point estimates, which are those presented in Table 2 column (2). Based on this analysis, we estimate that switching to a single factor sales apportionment formula will have a long-run impact of increasing the number of manufacturing jobs in Wisconsin by about 2.9 percent. At Wisconsin's base of about 619,000 manufacturing jobs (1995 estimate), this translates into about 18,000 new jobs just in manufacturing. Outside of manufacturing, the same data gives Wisconsin's employment at 2,035,000. The results in column (7) suggest that for Wisconsin, changing to single factor sales would raise non-manufacturing employment 2.4 percent, or 49,000 new jobs.

In addition to the obvious benefits of greater employment, there are also important tax revenue implications from the new jobs. Using 1995 Bureau of Economic Analysis data, we find that the average worker in Wisconsin made \$20,700 per year with manufacturing workers averaging \$31,400 and non-manufacturing \$17,500. If the jobs created by the apportionment change are like these average jobs, we estimate that this will generate on the order of \$51 million in individual income tax revenue. There is also likely to be a positive dynamic effect on other tax revenues such as sales and property tax but we do not have data on the magnitudes of these effects.

Overall, we find clear evidence that the adoption of single factor sales apportionment should increase employment, generating additional personal income and individual income tax revenues for the State of Wisconsin. Any estimate of the corporate tax revenue losses caused by the adoption of single factor sales apportionment needs to be balanced against the gains in individual tax revenue from job creation. Failing to consider this dynamic effect may result in a significant underestimation of the revenue aspects of this policy.

Tax Simplification

The costs incurred by taxpayers to comply with the tax laws represent a significant diversion of resources from other, more productive, economic activities. Compliance costs include the costs of gathering and interpreting the information needed to calculate the tax, documentation and record-keeping to support such computations, filing returns, and resolving disputes with tax authorities. A 1992 survey of large U.S. corporations found that these taxpayers spent an average of \$1.5 million per year to comply with federal, state and local corporate income taxes. The study also found that, on average, the costs of complying with state and local taxes comprise 30 percent of total compliance costs. The complexity of the apportionment formula was identified as an important factor contributing to the state and local compliance burden.¹⁶ Removing the property and payroll factors from the Wisconsin apportionment formula would ease the compliance burden by eliminating the need to compute and maintain records regarding these two factors. It would also make it easier for state tax authorities to administer the tax laws by reducing the amount of information state tax authorities must analyze to determine the appropriate amount of tax.

¹⁶ Slemrod and Blumenthal, "The Income Tax Compliance Cost of Big Business," *Public Finance Quarterly*, October 1996.

CAVEATS AND IMPLEMENTATION ISSUES

Projected Economic Benefits Are Not a Sure Thing

A valid concern regarding any proposed tax reform is that the predicted economic benefits may be overstated. This study predicts that a single factor sales apportionment formula will enhance future job growth in Wisconsin. This prediction is not based on a theoretical model of job growth, but rather the actual experiences of other states that have modified their apportionment formulae from 1978 to 1995. Nevertheless, the past does not always predict the future, in part because circumstances can change over time. For example, Wisconsin's unemployment rate is currently at one of its lowest levels in decades and many Wisconsin businesses are experiencing a shortage of skilled labor.¹⁷ This robust job market may limit the ability of a single factor sales formula to impact job growth, at least in the short-run.

This study also predicts that a single factor sales formula will raise an additional \$51 million in individual income tax revenues per year. All revenue estimates should be approached with a degree of caution, however.¹⁸ It is simply not possible to know with certainty how much revenue will be raised or lost by adopting a single factor sales formula. For example, increasing the weight placed on the sales factor may lead to corporate income tax revenue losses. In fact, based on a static model of revenue-estimation (which assumes that economic growth is unaffected by the law change), a 1994 Wisconsin Department of Revenue study estimated that the adoption of a single factor sales formula would result in an annual loss of \$22 million in corporate tax revenues.¹⁹ However, any estimate of the corporate tax revenue losses caused by the adoption of single factor sales apportionment needs to be balanced against the gains in individual tax revenue from job creation, which are estimated to be up to \$51 million.

¹⁷ Bureau of Labor Statistics, *Local Area Unemployment Statistics*, 1998.

¹⁸ Auerbach, "Dynamic Revenue Estimation," *Journal of Economic Perspectives*, Winter 1996.

¹⁹ Division of Research and Analysis, Wisconsin Department of Revenue, *Background Paper on Corporate Apportionment Formula*, November 10, 1994.

The Fairness Issue

Some Businesses Will Experience Tax Increases

Any change in tax policy typically creates both winners and losers, particularly in the short run. A single factor sales apportionment formula is no exception. The winners will be companies with large amounts of property and payroll in Wisconsin but with sales nationwide. They will experience substantial reductions in their Wisconsin income tax liabilities. The losers will be companies that have substantial sales in Wisconsin but which have the majority of their employment and investment located out-of-state. They will end up paying more Wisconsin income taxes. In a 1994 Department of Revenue study (see footnote 19), it was estimated that while a single factor sales formula would reduce the taxes of approximately 1,800 corporations, nearly 3,000 corporations would see their taxes increase. According to this study, industries that would benefit the most include manufacturers of food, paper, chemicals, fabricated metal products, and electronic instruments, as well as wholesale and retail traders. Industries that would experience tax increases include construction companies, tobacco and petroleum manufacturers, and various service industries. The negative impact of a single factor sales formula on selected businesses and industries may raise concerns about the fairness of this proposed tax law change.

Most Small Businesses Will Not Be Affected

It is likely that a relatively small number of corporations with large amounts of property and payroll in-state will benefit disproportionately from the adoption of a single factor sales formula. In contrast, most of Wisconsin's small businesses will not be affected by a change in apportionment formulae. Two factors explain this discrepancy. First, the activities of Wisconsin's small businesses typically do not extend beyond the state's borders. As a result, they do not apportion their income for tax purposes. Second, a relatively small number of large corporations pay the lion's share of Wisconsin corporate income taxes, and therefore any change in corporate income tax policy will tend to have a disproportionate effect on these corporations. For example, in 1994 the largest 1 percent of corporate taxpayers (those with Wisconsin taxable income of \$1 million or

more) paid about \$412 million in Wisconsin income taxes, or roughly 78 percent of total Wisconsin corporate income tax collections in 1994.²⁰ Nevertheless, the disparate effects of this proposed tax law change on large versus small businesses may also raise equity concerns.²¹

Implementation Issues

Adopting an apportionment formula based solely on sales would significantly increase the importance of how "sales" are defined, measured and attributed to Wisconsin. Therefore, the adoption of a single factor sales formula would necessitate a thorough analysis of the current rules for computing the ratio of in-state sales to sales everywhere. One example is the so-called "throw-back" provision found in current law. Under this rule, if a Wisconsin-based company sells goods to a customer located in a state in which the Wisconsin company is not taxable, 50 percent of those sales are thrown back into the numerator of the Wisconsin sales factor. Throw-back does not apply if the customer is located in a foreign country.²² With the increased importance of the sales factor, lawmakers may wish to consider alternative approaches to throw-back, such as requiring throw back of 100 percent of a sale or eliminating throw back altogether.

Over the next 25 years, employment in the service sector of the Wisconsin economy is expected to grow faster than manufacturing employment.²³ Therefore, the adoption of a single factor sales formula should also prompt a re-evaluation of the rules for attributing sales of services to Wisconsin. Under current law, sales of services are attributed to Wisconsin to the extent the underlying income-producing activity is performed in Wisconsin.²⁴ As a consequence, if employee salaries are a significant cost in providing a service, the computation of the sales factor tends to mimic that of a payroll

²⁰ Wisconsin Legislative Fiscal Bureau, *Corporate Income Tax*, 1997.

²¹ As a comparison, when Illinois enacted its single factor sales apportionment formula, a local newspaper quoted Illinois state tax officials as stating that while the change would save about 7,000 Illinois corporations \$217 million in state taxes annually, \$60 million of those savings would go to just five corporations. *The State Journal-Register*, July 10, 1998.

²² Wis. Sec. 71.25(9)(a)-(c).

²³ Division of Research and Analysis, Wisconsin Department of Revenue, *Wisconsin Long-Term Economic Forecast*, 1998.

factor. For this reason, some states, such as Minnesota, attribute sales of services based on the location of the customer receiving the service rather than the location of the costs incurred in performing the service.²⁵

Finally, the adoption of a single factor sales formula should also trigger a re-evaluation of the industry-specific apportionment formulae used by air carriers, motor carriers, railroads, pipeline companies, finance companies, and public utilities.²⁶ For example, under current Wisconsin law, interstate banks use a special two-factor formula that includes a gross receipts and a payroll factor. Likewise, interstate motor carriers use a special two-factor formula that includes a gross receipts and a ton miles factor. If a single factor sales formula is adopted, lawmakers may wish to extend the concept to banks, motor carriers, and other industries that are currently required to use specialized formulae.

²⁴ Wis. Sec. 71.25(9)(d).

²⁵ Minn. Sec. 290.191.5(j).

²⁶ Wisconsin Admin. Code 2.46, 2.47, 2.475, 2.48, 2.49, and 2.50.

SUMMARY

This study estimates the impact that switching to a single factor sales apportionment formula would have on job creation and tax revenue for Wisconsin. Our estimates are based on the actual experiences of states that have modified their apportionment formula over the period 1978 to 1995. The analysis controls for other factors that can affect employment, such as state trends, changes in national unemployment rates, and the actions of other states regarding their apportionment formulae. Our results establish two important facts about state tax policy.

First, we provide evidence that the apportionment formula has a large and significant effect on a state's economy. The payroll weight is a significant determinant of state employment. We find that reducing the payroll weight from one-quarter to zero increases manufacturing employment by approximately 2.4 percent for the average state during the sample period. The same change increases non-manufacturing employment approximately 1.9 percent. Second, we show that these significant employment effects imply that although increasing the sales weight in a state may lead to corporate income tax revenue losses, the increased employment generates additional individual income tax revenue. Failing to consider this dynamic effect may result in a significant underestimation of the revenue aspects of this policy.

Applying these results to the State of Wisconsin, we find that increasing the sales weight in Wisconsin from 50 percent to 100 percent would have a long-run impact of increasing manufacturing employment by about 18,000 jobs and non-manufacturing employment by as many as 49,000 jobs. These new jobs would have a significant positive impact on individual income tax revenue for the State of Wisconsin, creating an estimated \$51 million in additional tax revenue per year. Coupled with neighboring states' aggressive modification of their own apportionment formulae, these results underscore the need for the State of Wisconsin to act promptly to remain competitive and avoid revenue and job losses to other states.

Table 1*Descriptive Statistics for State Panel from 1978-95*

Variables ^a	Mean	Standard deviation
<i>Payroll weight</i>	0.314	0.047
<i>State payroll burden</i>	0.013	0.004
<i>State corporate tax rate</i>	0.073	0.022
<i>Federal corporate tax rate</i>	0.406	0.058
<i>Ln(national employment)</i>	4.688	0.079
<i>State personal income growth rate</i>	0.017	0.022
<i>National unemployment rate</i>	0.069	0.012
<i>Share of national manufacturing</i>	0.023	0.023
<i>Ln(manufacturing employment)</i>	12.432	1.095
<i>Ln(total employment)</i>	14.135	0.95
<i>Ln(real manufacturing wage)</i>	3.33	0.161
<i>Number of Observations</i>	732	

^a *Payroll weight* is the payroll weight in the apportionment formula (e.g., 33 percent, 50 percent, or 100 percent).

State payroll burden is the payroll weight x (state corporate tax rate)(1 - federal corporate tax rate).

State corporate tax rate is the top corporate statutory rate imposed by the state.

Federal corporate tax rate is the top corporate statutory rate.

Ln(national employment) is the log of national total employment

State personal income growth rate is the state's growth rate in per capita personal income.

National unemployment rate is the national unemployment rate in percent.

Share of national manufacturing is the state's share of national manufacturing employment.

Ln(manufacturing employment) is the log of manufacturing employment.

Ln(total employment) is the log of total employment.

Ln(real manufacturing wage) is the log of the state's real manufacturing wage.

Table 2

Regressions of Manufacturing Employment, Total Employment, Real Manufacturing Wages and Non-Manufacturing Employment on the Weight on Payroll in the Apportionment Formula and Control Variables

Dependent variables ¹	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Independent variables	Ln(Manufacturing Employment)			Ln(Non-manufacturing employment)			
State payroll burden	-1.920 (0.794)						
State corporate tax rate		-2.231 (1.331)	-0.229 (0.308)				-1.852 (0.806)
State payroll burden (incl. federal)				-0.059 (0.519)			
State corporate tax rate (incl. federal)				-0.309 (0.127)	-0.367 (0.116)		
Payroll weight					5.367 (2.927)		
Mean of all states' payroll burden	6.252 (2.961)						
Mean of all states' payroll burden (incl. fed.)		10.439 (3.683)		8.111 (3.863)		7.651 (3.496)	-0.741 (1.903)
State personal income growth rate	0.380 (0.082)	0.430 (0.084)	0.390 (0.082)	0.447 (0.084)	0.391 (0.082)	0.445 (0.083)	0.170 (0.052)
National unemployment rate	-2.092 (0.286)	-2.062 (.278)	2.005 (0.288)	-1.899 (0.284)	-2.018 (0.287)	-1.987 (0.280)	-2.587 (1.765)
(Nat'l employment) x (state dummy variables)	Yes	Yes	Yes	Yes	Yes	Yes	Yes
State fixed effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes
State trends	Yes	Yes	Yes	Yes	Yes	Yes	Yes
R ²	0.793	0.795	0.794	0.797	0.794	0.797	0.794
Number of observations	732	732	732	732	732	732	732

standard errors in parentheses

¹ See Table 1 for variable definitions.

**Comments to Joint Finance Committee
University of Wisconsin-Parkside, Kenosha
April 10, 2001**

Chairperson Burke, Chairperson Gard, members of the Committee.

My name is Chip Brewer, and I am Director of Government Relations for S. C. Johnson & Son, Inc, which has its global headquarters in Racine and which employs about 3,000 people in Southeastern Wisconsin.

SC Johnson appreciates the gesture of the Committee to visit our area and to hear the opinions and concerns of all those who will speak today. Senator Plache, we are particularly grateful for your efforts to bring government closer to the people and your kind invitation to appear today.

I will limit my remarks to just one issue – “single factor” corporate income tax reform – a revenue issue of considerable statewide significance, but particularly to communities like Kenosha and Racine which are adjacent to bordering states, such as Illinois.

SC Johnson very much supports Governor McCallum's initiative to reform Wisconsin's corporate income tax, and to adopt the so-called “single factor” apportionment method. I won't go into the details of this proposal. But I do want to mention a few reasons why we think this is important, as well as timely.

To do so, I'd like to cite a study of economic impacts of single-factor sales apportionment which was undertaken by the UW-Milwaukee School of Business Administration in 1999.

First, the study concludes adoption of single-factor will have significant positive effects on employment in Wisconsin, and will create over the long-term an estimated 18,000 new manufacturing jobs and 49,000 new non-manufacturing jobs.

Second, the authors note that states bordering Wisconsin have been particularly aggressive in changing their apportionment formulae to attract new business and expand economic growth within their borders. Illinois, Iowa, Michigan and Minnesota all weight the sales factor more heavily than Wisconsin, to the benefit of their in-state companies. The authors conclude that in terms of corporate income tax, these neighboring states have become a more attractive place to invest.

Therefore, to help assure continued economic growth and prosperity in Wisconsin, SC Johnson joins with other companies in the Racine Area Manufacturers and Commerce (RAMAC) in urging adoption of single-factor apportionment.

Members of the Committee, that concludes my remarks, but I would be pleased to entertain questions, and to make available to the Committee a copy of the complete UW-Milwaukee study.

Testimony of UW-Platteville Chancellor David J. Markee
Joint Committee on Finance
April 10, 2001
Kenosha, Wisconsin

Thank you for the opportunity to speak with you today about how two of our proposed partnerships would help drive economic growth in Wisconsin.

First, I want to talk with you about our initiative with UW-Fox Valley to deliver a full undergraduate **engineering degree program in the Fox River Valley**.

Although the **Fox Valley is Wisconsin's second largest industrial region, no undergraduate engineering program is available there**. This initiative would help employees advance their education and career development, and would provide Fox Valley business and industry with the qualified engineers they need.

UW-Platteville and UW-Fox Valley, in partnership with companies in the Fox Valley, would accomplish this with **existing infrastructure**, with no new bricks and mortar.

Creating an engineering program from scratch in the Fox Valley would cost tens of millions of dollars, but an investment of approximately \$500,000 in each year of the biennium would allow us to **leverage existing state and private resources** to provide a steady stream of qualified engineers in the Fox Valley.

We have already received **commitments from corporations** who would provide both direct financial support and use of their facilities as laboratories.

A **needs assessment revealed abundant demand** for the program from both employers and employees. In fact, with no advertising or promotion, we have already received more than 200 calls from working adults who are interested.

I believe this initiative **exemplifies the benefits of the UW System Economic Stimulus Package**, and when making your difficult decisions about this budget, please consider this initiative not as an expense, but a solution.

OFFICE OF THE
COMPTROLLER

**JOINT FINANCE COMMITTEE PUBLIC HEARING
ON 2001-03 STATE BUDGET**

Tuesday, April 10 - Kenosha

Co-chairs Gard and Burke ... Senator Plache ... committee members ... welcome to Kenosha and thanks for this opportunity to comment on the state budget proposal. I am Scott Sharp and I work for the City of Racine. I am also chairman of the Street and Highway Workers Advisory Committee of the American Federation of State, County and Municipal Employees, Council 40.

I'm here to ask for your support on a couple of issues that affect how we deliver services at the local level.

The first deals with properly maintaining state highways and supporting a solid transportation system for local governments. I have been supportive of our former governor's Corridors 2020 program because I believe it fosters economic growth and provides mobility for the vast majority of our citizens. But now that we have enumerated the final segments of that system, I think it's time to step back and take a look at how we can take better care of what we've built.

Over the last seven budgets, the Legislature has increased the Major Highway Program by 64% and the State Highway Rehabilitation Program by nearly 50%. These are inflation-adjusted dollars. At the same time the State Highway Maintenance Program – which funds the county highway crews that plow and take care of the state highway system – has seen an 8% decrease in funding. That's more miles of highway to take care of with fewer dollars.

The standard answer is that our county highway crews have more technology at their disposal and they simply have to become "more efficient." The truth is that the manpower at the county level for this type of work has been cut to the bone ... and that if we become any more efficient those snowplows will be driving themselves!

Mobility means more than simply building new highways. It also means keeping them open throughout the year so our citizens can safely use them. We need increased State Highway Maintenance funding to make that happen.

And if you're not willing to do that, at least be honest with the citizens and tell them that the state highways are in poor driving condition because the state is unwilling to pay the counties for higher service levels under the maintenance contracts. Right now, it's the highway commissioners and county crews that take the brunt of the criticism for the funding decisions you make.

JOINT FINANCE COMMITTEE

1. INCREASE FUNDING FOR PUBLIC DEFENDER'S OFFICE AND YOUTH AIDS.
2. FULL FUNDING OF COURT SYSTEM
3. INCREASE FUNDING FOR COP, CIP AND BIRTH TO THREE PROGRAMS
4. REQUEST MONEY FOR KENOSHA COUNTY'S CARE PILOTS.
5. FIND MORE D.M. FOR KENOSHA COUNTY.
6. INCREASE PAROLE HOLD REVENUE

RONALD A JOHNSON
7401-28TH AVE
KENOSHA

COMMENTS:

WITH THE ECONOMY IN FLUX AND
● RESTRICTIONS SUCH AS LEVY LIMITS
THIS BUDGET SEVERELY IMPACTS
KENOSHA COUNTY.

YOU MUST FIND WAYS TO FUND
YOUR DEFACTO MANDATES;

JUVENILE DETENTION
● PUBLIC DEFENDER'S OFFICE
HUMAN SERVICES
ETC.

WHEN THE STATE REQUIRES THE
COUNTY TO PROVIDE SERVICES, THE
STATE NEEDS TO PROVIDE APPROPRIATE
FUNDING TO SUPPORT THEM.

● THE CURRENT ECONOMIC CONDITIONS
DO NOT LEAVE THE COUNTY OR PUBLIC
TO PICK UP THE SLACK.

- PROGRAMS FOR THE DISABLED NEED TO BE SUPPORTED NOT CUT.

● STATE AGENCIES NEED TO BE MORE ATTUNED TO THE PUBLIC'S INTERESTS.

MANY CHOICES THAT ARE AND NEED TO BE MADE AT THE STATE LEVEL HAVE AN IMPACT ON THE QUALITY OF OUR LIVES. WE NEED

● TO KNOW THAT OUR VOICES ARE BEING HEARD.

THANK YOU,
Jimmy O Larson
KANOSAA COUNTY BOARD
SUPERVISOR - DIST. 18



April 9, 2001

Comments to Joint Finance Committee U.W.P. – April 10, 2001

Dear Chairperson Burke and Members of the Finance Committee:

My name is Roger Caron, President of the Racine Area Manufacturers and Commerce, a business association of approximately 800 employees representing 35,000 employees.

RAMAC appreciates the time you're investing in coming to the campus of UW-Parkside to hear about our issues and concerns.

For brevity purposes, RAMAC would like to list our support of the following issues:

1. **Adoption of the "single factor" apportionment method for computing Wisconsin Corporate Income Tax** – RAMAC believes that this corporate tax reform would positively benefit Southeastern Wisconsin's currently "weak" economic climate by creating new jobs and attract more corporate expansions here in Wisconsin versus other midwestern states.
2. **Commuter Rail** – As a member of the Governor's Blue Ribbon Committee on Passenger Rail, my support and RAMAC's support for commuter rail from Kenosha through Racine to Milwaukee is well documented. RAMAC believes this issue is another extremely important part of our economic future.
3. **Charter School Legislation** – Based on experience to date, the only way to get independent charter schools open in Wisconsin is through granting independent chartering authority to public institutions outside of local school boards. The politics of charter school decisions are such that no local board will likely approve one. It is telling that, while over 400 school boards in the State of Wisconsin have the authority to charter independent charter schools, not one has done so – the only non-instrumentality charter school exists in Milwaukee, and has been chartered by the City and the University of Wisconsin. (Also please see remarks by Carol Barkow, RAMAC's Director of Education.)
4. **YMCA** – Continuation of their property tax exemption.
5. **UW-Parkside and Systems Funding** – RAMAC believes UW-Parkside should not be forced to cut programs because of funding shortfalls. UW-Parkside has become an economic "partner" in the overall economic development of Southeast Wisconsin. The Governor's budget would cut approximately \$150,000 from its current ongoing initiatives. This budget would forestall the investment they are currently making to achieve excellence in education, community involvement, and stimulating the new economy here in the Racine area.

Thank you for your attention and interest in these matters.

Sincerely,

Roger Caron
President

RACINE AREA MANUFACTURERS AND COMMERCE

300 5th Street, Racine, WI 53403
Ph. (262) 634-1931 Fax (262) 634-7422
www.racinechamber.com

Budget Overview

- ◆ Revenue estimates: The growth in state revenue is not increasing as quickly as it has in previous biennia. It is unlikely that new revenue estimates will provide legislators with additional funds to utilize during the state budget debate. This is the first time many legislators have been faced with tight fiscal conditions.
- ◆ State agencies have been requested to cut their budgets by 5%. Portions of many agency budgets have been exempted from these budget cuts (i.e. local assistance and aids to individuals and organizations). Some agency budget cuts will have a direct impact on counties (state public defender's office).
- ◆ Budget Stabilization Fund / Tax Relief Fund: The Governor's budget provides an automatic procedure for the transfer of certain revenue to the budget stabilization fund. If more tax revenue is collected than projected, 50% of the additional tax revenue must be transferred to the budget stabilization fund. The Governor's budget creates a non-lapsable trust fund titled the tax relief fund. Revenues to the fund come from the other 50% of additional tax revenue not placed in the budget stabilization fund (could be higher if transfer not made to budget stabilization fund if the fund balance equals or exceeds 5% of the estimated GPR revenues for that fiscal year).

The Governor created a new personal income tax credit, "the tax relief fund tax credit". The credit would be a nonrefundable individual income tax credit for the purpose of returning moneys from the tax relief fund to taxpayers when the fund exceeds \$25,000,000. The credit is based on the number of dependents claimed on state income tax forms.

- ◆ State Spending Limits: The Governor's budget creates a statutory limit, first effective for the 2003-2005 fiscal biennium, on the percent by which year-to-year total appropriations from GPR can increase. The budget provides that for any biennial

budget period, the total amount appropriated (after certain enumerated exclusions) in that biennial period may not exceed the projected percentage increase in state personal income for the next two calendar years.

Tobacco Settlement Revenues

- ◆ **Tobacco Settlement Securitization:** According to the Legislative Fiscal Bureau, there are many ways the proposed transaction could be structured. Preliminary information indicates that the transaction could involve the following elements. Under this scenario, an estimated \$1.26 billion in bonds or other obligations would be issued by the Wisconsin Health and Educational Facilities Authority or by a nonstock, nonprofit corporation formed for that purpose. Bond proceeds would be deposited in a statutory segregated permanent endowment fund.

From the permanent endowment fund, \$350 million would be transferred to the general fund to provide increased revenue in the 2001-2003 biennium compared to current law. Under this scenario, bond proceeds would also be used to: (a) fund a debt service reserve of approximately \$137 million; (b) pay capitalized interest of \$188 million; (c) pay \$13 million of issuance costs; and (d) deposit \$570 million in the permanent endowment fund for long-term investment by the Investment Board.

Once bonds would be issued, debt payments to bondholders would be the first draw on the stream of tobacco settlement payments, while the state would retain a right to any revenues in excess of debt service required for the bond issue. Each year, once debt service payments on the bonds are paid, the remaining tobacco settlement revenue for that year would be transferred to the general fund. After the bonds would be paid off, all tobacco settlement revenue would flow through to the general fund.

Beginning in 2003-04, annual transfers would be made from the permanent endowment fund to the general fund. In general, these transfers would equal 8.5% of the balance in the fund, plus additional amounts from investments that could be designated by the Secretary of Administration.

- ◆ The Governor's budget affirms the state's participation in the tobacco settlement agreement and would specify that all payments received and to be received by the state under the tobacco settlement agreement would be property of the state, to be used as provided by law, including a sale, assignment, or transfer of the right to receive such payments. No political subdivision of the state, and no officer or agent of any political subdivision of the state, would be allowed to have or seek to maintain any claim related to the tobacco settlement agreement or any claim against any party that was released from liability by the state under the tobacco settlement agreement.

Kettl Commission Recommendations Contained in the Governor's Budget

- ◆ The municipal shared revenue reform initiative was included in the Governor's budget. Under the proposal, one-quarter of one cent of the state sales tax is to be

shared regionally as replacement to the current per capita payment. The Governor's budget also restructures the equalization component of municipal shared revenue to focus aid on basic services and creates an incentive to limit municipal expenditure growth.

- ◆ The Governor's budget requests the Joint Committee on Legislative Organization to review the Kettl Commission recommendations regarding state takeover of certain human service functions (including the child welfare system) and certain criminal justice functions.
 - WCA believes that full state funding of the court system could be accomplished during this biennium.
- ◆ The Governor's budget also requires counties to use shared revenue and mandate relief payments to first pay probation and parole hold costs, court expenditures and youth services costs not otherwise funded by state or federal aid or fees.
 - WCA opposes this provision.

County Specific Items Contained in the Governor's Budget

- ◆ Community Aids: The Governor's budget decreases community aids to counties by \$1.2 million in each year of the biennium (the state did not fill the federal social services block grant cut).
 - County request: Ask the state to replace the federal funds as well as provide a 3% increase in each year of the biennium.
- ◆ Youth Aids: The Governor's budget provides no increase to counties in the youth aids or community intervention program appropriations. The Governor's budget increases the rates charged to counties for juveniles placed in the juvenile correctional institutions by 11% in the first year of the biennium and 3% in the second year of the biennium. Additionally, the Governor's budget also eliminates statutorily set assessments for care in a child caring institution, group home, foster home, or treatment foster home.
 - County request: Reduce the daily rate charged to counties for juveniles placed in JCI's. Oppose the elimination of statutorily set assessments for aftercare placements. Support increased funding for early intervention services by requiring the state to pay for 20% of all out-of-home placement costs and requiring counties to invest that savings in early intervention, community-based services.
- ◆ Shared Revenue/Mandate Relief: The Governor's budget provides no increases in the shared revenue or mandate relief accounts.
- ◆ Circuit Court Support Grants/Guardian ad Litem Reimbursements: The Governor's budget provides no increase in the circuit court support grant and guardian ad litem appropriations.

- ◆ **Intergovernmental Transfer Program:** The state of Wisconsin is changing the way it brings intergovernmental transfer program revenue to the state of Wisconsin (wire transfer program vs. certification of county losses). This change will bring additional IGT dollars to the state for the next two years. Changes in federal laws will mean less IGT revenue to the state in two years. The Governor's budget creates a medical assistance trust fund to hold IGT dollars to allow payments to be made to the nursing home industry following the federal law changes. Counties will receive an additional \$40 million in IGT revenues in each year of the biennium. An additional \$115 million will be placed in the nursing home formula.
 - **County request:** Support the creation and maintenance of the MA Trust Fund. Support the additional payments the county nursing homes and the rest of the nursing home industry.

- ◆ **Community Options Program:** The Governor's budget did not provide any additional COP slots to address the growing waiting lists for services in the community for the frail elderly and the developmentally disabled. Family Care implementation was also set back with no new funding for additional pilots.
 - **County request:** Support additional funding for the COP, CIP and Birth to Three programs.

- ◆ **Transportation:** The Governor's budget provides a 5.4% increase in General Transportation Aids in FY 2002 and an additional 0.7% increase in FY 2003. The Governor's budget also provides a 3.8% increase in FY 02 and a 4.2% increase in FY 03 in the Local Road Improvement Program. Counties received no increase in the CHIP-D program. The Governor's budget provides no increases in the combined Local Bridge Improvement Program and the Transportation Facility Improvement Assistance Program.
 - **County request:** Seek 5% annual increases in the GTA and LRIP programs, as well as the CHIP-D, Local Bridge and STP-Urban and STP-Rural programs.

- ◆ **Recycling:** The Governor's budget drastically reduces the amount of money allocated for grants to responsible units. The Governor's budget allocates \$14 million in SEG in FY 02 and \$13.5 million in FY 03. This represents a \$21.3 million cut.

SUMMARY - Department of Employee Trust Funds 2001-2003 Biennial Budget – Governor's Recommendations

I. Direct Service Staffing

Critical Customer Service Improvement – Provide funding and permanent position authority to meet the needs of a growing population of active, inactive and retired participants. The resources will enable the Department to process benefit applications and pay benefits to all eligible participants under the WRS within reasonable customer service response standards. Additional resources allow the Department's service response time to decrease, on average, from 12 weeks to 3 weeks and provide services, generally, at the median level of other comparable public retirement systems.

Requested: \$635,400 SEG in the first year and \$577,900 SEG in the second year and 13.0 FTE permanent positions.

Governor's Recommendation: \$376,400 SEG in the first year and \$311,400 SEG in the second year and 8.0 FTE permanent positions.

* **Customer Service Call Center** – Continue support of the Customer Service Call Center which provides critical telephony services to our members. Enhanced technology and permanent positions will enable the Department to meet a goal of answering 205,000 calls each year. Furthermore, if projections are accurate, the Call Center will meet its target of answering 80-85% of the inquiries within one minute 90% of the time in the first year and answering 85-90% of the inquiries within one minute 90% of the time in the second year. The Call Center includes an enhanced interactive voice response (IVR) system with Internet access, hardware and software capable of routing calls including the ability to select a staff person to answer questions, helpdesk and knowledge based software for call tracking and on-line information to aid call center staff.

Requested: \$663,200 SEG (\$357,000 SEG one-time) in the first year and \$367,600 in the second year and 6.5 FTE permanent positions.

Governor's Recommendation: \$308,000 SEG in the first year and \$314,000 SEG in the second year (includes funding for ongoing software enhancements and DOA information technology charges) and 2.0 FTE permanent positions and 4.5 FTE two-year project positions.

* **Ombudsperson Services** – Reduce the growing backlog of health insurance complaints, meet the workload demands of anticipated complaint increases and enable quality assurance initiatives to be implemented by the Department. An

any appeal taking into account relevant factors such as the cost of litigation, likelihood of success of appeal and actuarial impact on the fund.

Requested: \$1.0 million SEG in a new biennial appropriation; \$28,600 SEG in the first year and \$38,100 in the second year and 1.0 FTE four-year project position.

Governor's Recommendation: \$301,700 SEG in the first year and \$423,000 SEG in the second year to reduce the Department's appeals backlog over a six-year period. Recommendation includes funding to contract with the Division of Hearings and Appeals, provide court reporter services, contract for additional hearing examiner services to implement an expedited case process, and obtain outside legal counsel for appeal representation and for specialized tax services.

Approved statutory language: (1) authorizing the Department Secretary equity authority to resolve certain appeals, and (2) granting the governing boards the authority to settle a dispute of an appeal taking into account relevant factors such as the cost of litigation, likelihood of success of appeal and actuarial impact on the fund.

IV. Other

Electronic Document Management – Contract for services to meet increased annual workload of processing and imaging daily mail due to the growing participant population. Resources will allow the Records Management Section to meet 24-48 hour document turnaround standards to users and provide a quality assurance function.

Requested: \$167,200 SEG in the first year and \$199,900 in the second year.

Governor's Recommendation: Item not approved.

Business Resumption Planning Contract Services – Contract with a vendor to purchase three computer servers and store the servers off-site at the Department of Administration as part of the Department's business resumption plan. The back-up server capacity is necessary in the event a natural or man-made disaster either destroys the facility or makes it inaccessible to management and staff to perform critical business functions within 2 to 3 days of a disaster.

Requested: \$22,500 SEG in the first year and \$36,300 SEG in the second year.

Governor's Recommendation: Item not approved.



**" DEMONSTRATING GOD'S WISDOM
TO THE POWERS AND PRINCIPALITIES..."**

Eph. 3:10

MICAH

HOSEA

RIC

CUSH

***WISDOM PRESENTATION TO THE
STATE BUDGET HEARING***

Tuesday, April 10th, 2001

Kenosha, WI

PROGRAM

Press Conference

9:30am

Opening Prayer

WISDOM's Position

Q & A

Closing Statements

HEARING PRESENTATION

11 AM-1 PM

WISDOM's Position by The Rev. Mark Jaramillo

Community Learning Centers by Karen Kinsman

AODA Presentation by Connie Molbeck

School Funding Presentation by Lydia McCoy

Student Perspective by Charles Helm

During the Hearing we will have a meeting with Senator Brian Burke.
Packets are going to be provided to the media and all the members of the Joint
Finance Committee.

Several People will be delegated to stay at the Hearing until 5 pm so that we get
informed of other funding issues that were addressed.

2000 Domanik Dr., Racine, WI
262-633-8346 Fax 262-633-8351

I am the Reverend Mark Jaramillo, vice president of the faith based social justice organization known as CUSH in Kenosha. This morning I officially speak for 90 congregations, of 14 religious denominations, from throughout southeastern Wisconsin, known as the organization of "Wisdom." an organization made up of CUSH Congregations United to serve Humanity, MICAHA Milwaukee Inner city Congregations allied for Hope, HOSEA Hope Offered thru Shared Ecumenical Action in South Milwaukee, and RIC Racine interfaith Coalition.

Not too long ago, I received a tear filled phone call from a person in distress. We'll call her Mary. All Mary could get out on the phone was the statement "I need someone to help me." Without hesitation, I sped to where she was uncertain of what I would find. Upon entering her home I found myself faced with a woman who had been beaten so badly that her eyes were swollen shut and her lips busted wide open. All Mary could say, was "I can't take it anymore." Never had I felt such a horrific sensation of pain and hopelessness in the pit of my stomach than I experienced that day, until I read this Thompson/McCallum's Budget. And I am here to say today that we "We can't take it anymore." This budget is a direct assault to the body and soul of every person here in Wisconsin, bloodying the hopes of people who want to have a decent life for themselves and for their children. We at "Wisdom" are outraged at the abuse this budget will deliver to the people of Wisconsin and therefore it cannot be passed as it is now.

Our schools are being forced to make dramatic cuts in many key and vital areas, leading to increased class sizes, cutbacks in music and art programs, loss of paraprofessional staff, and more. Districts throughout the state are suffering as revenue limits cannot keep pace with the real cost of education. This must stop. Each education dollar lost in this budget, means we lose essential programs. Among the programs at risk are the CLC after schools programs, offering tutoring and classes in creativity, and the SAGE program, where smaller classrooms allow children to receive the individual attention they need and deserve. Adequate funding of these and similar programs is essential for our children's intellectual, personal and emotional development. Without proper funding for education: what lies ahead? A bleak future of children, abused through the lack of an opportunity for decent education, creating a whole generation of children who have been stunted in their development. So I say, we cannot support this abusive budget that will at the very least produce generations that are not prepared to lead the future of our communities.

There is also the issue of community aid. Funds for programs that will help build healthy foundations within our neighborhoods are being lost due to funds that have been frozen, or even worse, cut. Cuts have been made to our mentoring programs handicapping many children in discovering their true potential. Cuts have been made to programs that provide decent care for the elderly and the disabled depriving them the most basic of human freedoms: the right to live with dignity. Programs such as these, are being cut, are being crushed and discarded

in order to make room for more prisons.

For the past two-years General Public Revenue has increased the Corrections funding by 13.9%, where the rest of the state government has only received an increase of 6.3%. There have been three new prisons; one new "secure detention facility," and two expansions on existing facilities. But, don't be fooled into thinking that this is a great effort to help create a better prison system. Since 1989 the corrections budget has grown 11.5% per year, yet there has been no increase in prison health-care staffing, except to service new prisons. Further proof of the systems failure is their denial to fund testing for hepatitis C in prisons, taking away the basic human need to live in a healthy environment. Accountability for crimes is appropriate, but destroying the human spirit is not.

I ask you now, do not simply invest in prisons as a place to put children who did not have an opportunity for a life giving education, but invest in the children themselves. For when there is a deadly disease in our midst, we do not start by building cemeteries, we look for the cures.

As our elected servants, I ask you to look at yourselves and your values and ask yourselves, how much you believe in providing the basic necessities for the future of all of the people of Wisconsin, both young and old. For Mary, who I initially started this speech with, it took a complete restructuring of her life to remove the abuse. That is what we at "Wisdom" are calling upon you, as our elected servants, to do with this budget. Restructure the budget so that our education, our communities and our prisons, may work to create a stronger and greater community. Restructure the budget so that the blatant abuse to human life that is this Thompson/McCallum's Budget will not be allowed to strike the people of Wisconsin.

"Wisdom" believes that the Thompson/McCallum budget

is an attack on the people of Wisconsin.

We at "Wisdom" are willing to help you create a just budget.

Today we call on all of you to create a budget that will provide support

for the programs and the education that will help keep Wisconsin alive and well.

Thank you

WISDOM, Inc.
2000 Domanik Dr.
Racine, WI 53404

Budget Hearing April 10, 2001

My name is Karen Kinsman and I am a member of the Executive board of CUSH, a faith-based, social-action group. CUSH stands for Congregations United to Serve Humanity. We are part of a collaboration of four South Eastern Wisconsin faith-based groups that make up "Wisdom". We are, MICAH , HOSEA , RIC , and CUSH .

Many people of Wisconsin are upset by the new state budget. It is widely believed that this budget is Governor Thompson's. If this is so, we think it is time to shred this old budget and have Governor Scott McCullum start again—this time with a budget that *cares* about our children!

CUSH found an interest in Lincoln and Washington Middle School's 21st century Community Learning Centers, or CLCs about a year ago. Within the time covered by the Wisconsin 2001-2003 biennial budget cycle, funding for 74 CLCs, will expire. Of these 74 CLCs, 19 sites are in Milwaukee, seven are in Franklin, two are in Kenosha and six are in Racine. Eleven CLCs in Milwaukee, one in Racine and two in Kenosha will lose funding this June.

The CLCs have proven effective by providing safe alternatives to drugs, gangs and other destructive activities. These vital programs are in danger of being cut because the federal grants will soon expire.

Why Do We Need CLCs?

- They provide a safe place for children and youth to go after school.

- And improve student achievement in math, reading and other subjects. Better school attendance, and graduation rates.
- CLCs help reduce juvenile crime rates, and help to prevent victimization during high crime hours between 2-8pm, creating safer neighborhoods.
- Adults in the neighborhood may be able to learn English as a Second Language or beginning computer skills at local CLCs.
- And increase the use of school facilities to make them a vital part of the neighborhood while school is not in session.

So what is the Solution?

The cost to sustain the operation of the 74 CLCs for two years is \$11 million. WISDOM calls upon the state legislature and the Governor to use funds from outside the regular 2001-2003 Education budget. In addition to this, a bipartisan taskforce that includes Education, Religious, Business and Community leaders should be established to design a plan that permanently funds current and future Wisconsin CLCs. Finally, WISDOM calls upon the federal legislators to support Congressman Tom Barrett's legislation HR 419, which extends funding for CLCs from three to five years.

In a tight budget, we are currently investing in ballparks, museums, historical societies, and prisons while squeezing the life and future out of our public schools. We must establish our priorities, and find the money to support the CLCs and our communities.

FOR IMMEDIATE RELEASE!!!!

Contact: Karen Kinsman (262) 657-6588

IT'S OUR MONEY \$\$\$\$\$\$
Join WISDOM and our affiliates
CUSH, RIC, HOSEA, and MICAH

FOR A PRESS CONFERENCE

Tuesday, April 10, 2001

9:30 a.m.

UW- Parkside Union Theatre
Legislative Joint Finance Committee
Public Hearing on the State Budget

We will send a message that we will not tolerate
Governor (Thompson) McCallum's budget proposal that
increase spending by millions of dollars for prisons and
stadiums, as it fails to fund needed programs for schools, drug
treatment, youth programs and help for the needy.

It's our tax \$\$\$
CUSH, RIC, MICAH, HOSEA and WISDOM will demand
that our elected officials introduce a responsible budget for
Wisconsin!!

Sponsored by:



" DEMONSTRATING GOD'S WISDOM
TO THE POWERS AND PRINCIPALITIES... "

MICAH
414-449-0805

HOSEA
414-486-1718

WISDOM
262-633-8346

RIC
262-635-9532

CUSH
262-564-8223



**" DEMONSTRATING GOD'S WISDOM
TO THE POWERS AND PRINCIPALITIES..."**

Eph. 3:10

MICAH

HOSEA

RIC

CUSH

WISDOM Calls for Reform of School Funding

As members of WISDOM (an organization comprised of 90 congregations, of 14 religious denominations, from throughout southeastern Wisconsin), we are saddened and angered by the crisis of funding for our public schools. Just a few of the many alarming facts are:

- Milwaukee Public Schools needed to make \$32 million in budget cuts in the 2000-01 school year, and projects a need to cut a similar amount in 2001-02.
- Racine schools have had to cut \$23 million from their budgets since 1994, and anticipate a further \$3 million shortfall for 2001-02
- In 1999, students and parents in New Berlin protested cuts in technology education, business and social studies classes made necessary by cap-imposed budget shortfalls

Schools have been forced to make dramatic cuts in many areas, leading to increased class sizes, cutbacks in music and art programs, loss of paraprofessional staff, and more. Districts throughout the state are suffering as revenue limits cannot keep pace with the real cost of education. Simply, the system is not working. **A new system must be devised to guarantee adequate, equitable access to resources for children in every district in the state.**

Even as we work toward a just long-term solution to the crisis of education funding, some steps must be taken immediately to prevent catastrophic budget shortfalls in 2001-02. There are many viable proposals for this. We offer a few:

1. Fund Special Education at 64%

Costs for Special Education have risen dramatically, as the level of state reimbursement has remained static. The State of Wisconsin must return to providing 64% of the cost of Special Education, to ensure adequate services to our most vulnerable children, without taking resources away from other educational programs. This must be provided outside of the spending limits.

2. Include 3 and 4 year-olds in student count

The state should include all three and four year-olds as full-time equivalent students for purposes of aid and revenue caps. Positive early learning experiences pave the way for future success.

3. The 1% Solution

Local school boards must be given the authority to exceed the state-imposed revenue limits by at least 1% without the need to call for a referendum.

4. Create Exemptions for Security and Building Maintenance

Our schools must not be asked to choose between safety and quality education.

Our Governor and our State legislature must act immediately, before the crisis worsens. Our children's education cannot endure another round of budget cuts. We call upon our legislators to demonstrate leadership and courage and to act responsibly toward our next generation of leaders and taxpayers.

WISDOM Calls for 21st Century Community Learning Centers Funding

History: The 21st Century Community Learning Centers (CLC) is a 3-year federal grant to public schools to operate after school programs. The CLCs provide expanded learning opportunities, social service, cultural and recreational activities outside of the regular school hours in a safe, supervised and drug free environment.

Within the time covered by the Wisconsin 2001-2003 biennial budget cycle funding for 74 CLCs, which serve 26,177 youth and adults, will expire. Of these 74 CLCs, 19 sites are in Milwaukee, 7 are in Franklin, 2 are in Kenosha and 6 are in Racine. 11 of the CLC's in Milwaukee, 1 in Racine and 2 in Kenosha will lose their funding in June 2001.

The CLCs have proven very effective in serving the needs of our youth by providing safe alternatives to drugs, gangs and other high risk or destructive activities. These vital programs, which must be preserved, are in danger of being cut because the federal grants will soon expire.

Benefits: National studies and surveys point consistently to the benefits and success of CLC programs for youth and the larger community. CLCs provide a safe, supervised and positive environment for youth. CLCs are a vital community asset, which we must preserve as:

50% of all juvenile crime is committed between the hours of 2-8pm on workdays. (Dept. of Justice)

Students in after school programs exhibit fewer behavioral problems, better ability to handle conflicts and improved self-confidence. (Safe and Smart: Making the Afterschool Hours Work for Kids, U.S. Dept. of Education and U.S. Dept. of Justice, 1998)

Students who spend no time in extracurricular activities are 49% more likely to have used drugs and 37% more likely to become teen parents than those students who spend one to four hours per week in extracurricular activities. (Adolescent Time Use, Risky Behavior and Outcomes: An Analysis of National Data, U.S. Dept. of Health and Human Services, 1995)

Students in after school programs show better achievement in math reading and other subjects. (Child Development 65, 1994: 440-456, Posner and Vandell)

Solution: The cost to sustain the operation of the 74 CLCs for two years is \$11million, therefore:

WISDOM calls upon the state legislature and the Governor to appropriate \$11million from the 2001-2003 state budget to fund the 74 CLCs.

WISDOM calls upon the state legislature and the Governor to appropriate these funds from outside the regular 2001-2003 education budget.

WISDOM calls upon the state legislature and Governor to establish a bipartisan taskforce that includes Education, Religious, Business and Community leaders to design a plan that permanently funds current and future Wisconsin CLCs.

WISDOM calls upon the federal legislators to support Congressman Tom Barrett's legislation HR 419, which extends funding for CLC from three to five years.

WISDOM is a collaboration of four congregation-based organizations: MICAH (Milwaukee), HOSEA (southern Milwaukee County), RIC (Racine) and CUSH (Kenosha). For more information, call (414) 449-0805 or (262) 633-8346, fax (262) 633-8351, or e-mail WISDOM00@milwpc.com.



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Eph. 3:10

MICAH

HOSEA

RIC

CUSH

ALCOHOL & OTHER DRUG ADDICTIONS (AODA)

Through the process of issue selection by the WISDOM Core Team Congress, the second issue that WISDOM has chosen to move forward from the local level and into a regional campaign is Alcohol and Other Drug Addictions (AODA). Over the past several years Racine Interfaith Coalition (RIC) and MICAH have sought ways to address AODA problems in their individual territories.

- In 1998 RIC supported funding for intensive treatment program for inmates of the Racine County Jail.
- RIC was successful in reducing the concentration of liquor establishments that attracted crime and other drug-related activities.
- In 1996, MICAH was successful in stopping the reduction of funds for AODA treatment in the Milwaukee County budget and through the pray-in the funding is being restored.
- In 1999, MICAH was successful in securing 10 million dollars in the state budget for AODA treatment in Milwaukee County.

AODA issues continue to be a major concern in the hearts and minds of our constituency. AODA treatment and related recovery programs are often the last stop for many people in their efforts to re-enter society. The people most affected by this problem are the poor, uninsured, and low-income residents of our communities, due to the unjust negligence and injustice of our socio-economic system. Due to lack of funding, there are not enough treatment facilities, and existing programs are limited. As a result, we continue to face:

- Extensive waiting lists for treatment
- Decreased number of available beds
- Lack of a comprehensive strategy and facilities to deal with families
- Increase in the number of drug-related crimes and arrests and ultimately an increase in the ever-growing prison population thus criminalizing drug addiction.
- The loss of productive lives and countless other negative effects that continue to trap thousands in a cycle of hopelessness and despair.

The leaders of WISDOM believe that AODA funding will continue to be of concern, until society changes the way we view victims of AODA. We believe that alcohol and other drug addictions are an illness and should be treated as such. We know that AODA activities are directly related to criminal activities and to the rise in prison populations. Treatment that is accessible and comprehensive is far more cost effective than the conventional approaches to dealing with victims of AODA. The absence of treatment often puts people on to crime, incarceration, and the outer fringes of our societies.

With this in mind, WISDOM will direct the AODA campaign to address the following:

- Reduction of the prison population by creating opportunities for treatment rather than incarceration. Many AODA suffers commit crimes, often non-violent in nature, to support their addiction or to gain access to inmate treatment programs. Remanding non-violent offenders to treatment will reduce not only the prison population but save the state millions of dollars.
- Making AODA treatment available to all those in need. Effective AODA treatment is needed to rebuild a life of stability after being trapped in the cycle of addiction.

The immediate goal of the WISDOM AODA Regional Task-force is to secure state funding to address AODA treatment for residents of the entire state. The state has proposed in its 2001-2002 budget not to award 10 million to Milwaukee County but to provide the 10 million to the entire state. **THIS IS UNACCEPTABLE.** If funding is to be expanded to the entire state then the funding will have to be increased as well.

WISDOM DEMANDS!

- \$20 million dollars to be included in the state budget for AODA treatment for the entire state of Wisconsin.

My name is Connie Molbeck. I am chair of the Sacred Ground campaign of Racine Interfaith Coalition (RIC), which is attempting to establish a drug free zone in the space between 6 of our congregations. I am also a veteran teacher of 32 years.

When I read the details of this budget, I find myself asking some questions:

What vested interest do legislators have in increasing our prison population? What benefits are you getting from the fastest growing industry and employer in the state?

Prison spending has grown 11.5% a year each year since 1989, a phenomenal rate of growth, esp. during a period when funding for education, AODA, and many human services has been curtailed.

Since the average prisoner reads at a 3rd grade reading level, it would appear that the revenue caps on public education would be for the explicit purpose of increasing the failure rate in public schools, and therefore filling up your fancy new prisons.

And we all know... at least those of us on THIS side of the table know... that drug related crimes account for the the biggest increase in prison population. Besides drug possession and sales, we know many burglaries and robberies, violent deaths, traffic fatalities, as well as homelessness, and broken families are the result of addiction.

It would seem logical, then to fund the drug problem at its root cause: addiction. But this government is not that logical. Last year, Milwaukee had \$10 million for drug and alcohol treatment, far below what was needed.

This year, that 10 million will be spread statewide, cutting many successful Milwaukee programs.. WISDOM is asking this legislature for \$20 million for AODA. This would maintain Milwaukee's current level of funding, and allow \$10 million more for other communities such as Racine and Kenosha to initiate programs.

Treatment facilities for the uninsured and under insured have long waiting lines. While people wait, jobs are lost, families are destroyed, and crimes are committed. Many people who work full time have no health insurance to cover treatment.

The cost of an average treatment program is far below cost of incarceration, therefore investing in treatment would save taxpayer money, and create useful citizens rather than convinced felons.

Who is benefiting from the phenomenal increase in prison spending? It is certainly not US the taxpayers. It is most certainly not the children whose public school programs have been cut to pay for it. It is obviously not the prisoners themselves.

It must therefore be the governor and legislators. because, If no one is better off, why would we have this phenomenal growth in prison spending at the expense of the very programs which could keep people out of prison? It just doesn't make any sense.

TESTIMONY FOR JOINT FINANCE COMMITTEE HEARING
April 10, 2001
University of Wisconsin, Parkside

Good morning. My name is Lydia McCoy. I am a member of the Education Committee of WISDOM. WISDOM is an organization made up of 92 congregations, of 14 different religious denominations, from throughout southeastern Wisconsin.

I am here today to speak to you about the matter of school funding. As you know, our public schools are in terrible trouble. The system is very unfair. When spending caps were imposed, they guaranteed that some districts would have much more money to spend on their students than others. Now, the spending caps are slowly eating away at public schools everywhere.

The most serious issue of education funding has to do with Special Education. The state has consistently allowed its share of funding for special needs kids to drop and drop. So, a much larger share of the burden is falling to local school districts. We have to spend more and more on special education at exactly the same time you tell us we can't spend more money. The state has been so irresponsible in this area that it is a miracle that our public schools function at all.

At a community meeting we sponsored last summer, the mother of a special needs child actually came to apologize to the other parents. She knew that the school had to cut programs for other children so that her child could be served. That's what this funding system has done! You have turned people against each other as they fight over who will be hurt the most by the deficits created by the state spending caps.

Last May, when the Milwaukee School Board met to decide on the budget with a \$32 million deficit created by the state funding formula, I watched a very sad scene. I watched programs for teen moms pitted against art classes, and I watched both of them pitted against programs for children with special needs. I cannot believe that our state government really wants budgets to be balanced by making the most vulnerable of our people have to fight each other.

In the last budget, the state did one very good thing for schools. You increased the size of the SAGE program, which is a wonderful program that shows real, positive results. Now, Governor McCallum wants to cut THAT back, too. Please don't let him.

WISDOM, like a lot of other groups, has given you a position paper, in which we outline some of our biggest concerns. The best thing you can do right now is to agree to meet your 63% obligation for the cost of Special Education. And, don't take it from another part of the education budget.

How are you going to pay for it? I'm not sure. It's too late to tell you that you shouldn't have been in such a hurry to give money away last year when you had it. Maybe we can live with less new prisons for the next two years. Maybe the Historical Society can wait. Maybe taxpayers would be willing to pay a little more in order to have excellent schools again – school referendums just won in some very conservative districts.

We, members of WISDOM, look to you to show leadership and to show that you have your priorities in order. It sounds like you are going to have to practically start from scratch with this budget. START with public schools.