

Fiscal Estimate - 2011 Session

Original
 Updated
 Corrected
 Supplemental

LRB Number 11-2616/1	Introduction Number AB-0381
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Description
 A sales and use tax exemption for items and services sold as part of a lump sum contract

Fiscal Effect

State:

<input type="checkbox"/> No State Fiscal Effect	<input type="checkbox"/> Indeterminate	<input type="checkbox"/> Increase Existing Revenues	<input checked="" type="checkbox"/> Increase Costs - May be possible to absorb within agency's budget
<input type="checkbox"/> Increase Existing Appropriations	<input type="checkbox"/> Decrease Existing Appropriations	<input checked="" type="checkbox"/> Decrease Existing Revenues	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No
<input type="checkbox"/> Create New Appropriations			<input type="checkbox"/> Decrease Costs

Local:

<input type="checkbox"/> No Local Government Costs	<input type="checkbox"/> Indeterminate	5. Types of Local Government Units Affected	
1. <input type="checkbox"/> Increase Costs	3. <input type="checkbox"/> Increase Revenue	<input type="checkbox"/> Towns	<input type="checkbox"/> Village
<input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory	<input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory	<input checked="" type="checkbox"/> Counties	<input checked="" type="checkbox"/> Others
2. <input type="checkbox"/> Decrease Costs	4. <input checked="" type="checkbox"/> Decrease Revenue	<input type="checkbox"/> School Districts	<input type="checkbox"/> WTCS Districts
<input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory	<input type="checkbox"/> Permissive <input checked="" type="checkbox"/> Mandatory		<u>Stadium Districts</u>

Fund Sources Affected	Affected Ch. 20 Appropriations
<input checked="" type="checkbox"/> GPR <input type="checkbox"/> FED <input type="checkbox"/> PRO <input type="checkbox"/> PRS <input type="checkbox"/> SEG <input type="checkbox"/> SEGS	

Agency/Prepared By DOR/ Robert Schmidt (608) 267-9892	Authorized Signature Paul Ziegler (608) 266-5773	Date 12/13/2011
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Fiscal Estimate Narratives

DOR 12/13/2011

LRB Number	11-2616/1	Introduction Number	AB-0381	Estimate Type	Original
Description A sales and use tax exemption for items and services sold as part of a lump sum contract					

Assumptions Used in Arriving at Fiscal Estimate

Under current law, contractors' charges for real property construction are not subject to sales or use tax, but contractors' purchases of building materials are taxable. In contrast, contractors' sales of personal property and taxable services (e.g., a stove and installation charges) may be taxable even if the sale is included within a real property construction contract. The current law treatment for the sale of tangible personal property and taxable services by contractors as part of a lump sum contract is dependent on the amount of taxable products sold to a customer and whether the contractor provides a list price for the taxable products to the customer. If a contractor includes taxable products that are minor in relation to a lump sum contract (less than 10% of the total contract) and no separate charge is made in any document provided to the customer, the cost to the contractor of the taxable products shall be used as the sales price subject to sales tax. If a separate charge is made for any of the taxable products, or the taxable products are more than 10% of the lump sum contract, the separate charge to the customer is subject to the sales tax.

The bill creates a sales and use taxes exemption for tangible personal property and taxable services that are sold as part of a lump sum contract, if the total of all such amounts is less than 10 percent of the total amount of the contract, and regardless of whether the amounts charged for labor and services are listed separately from the amount received for the tangible personal property. Under the proposal, a lump sum contract is a contract to perform real property construction activities and for which the contractor quotes the charge for labor, services of subcontractors, and materials as one price, including a contract for which the contractor subsequently itemizes the charges for labor, services of subcontractors, and materials as part of a schedule of values or similar document. The exemption would be effective on the first day of the 3rd month following publication.

While the intent of the bill may be narrower, the bill as written creates a sales and use tax exemption not only for a contractor's sales of personal property and taxable services to its customer, but also for any of the contractor's purchases of tangible personal property that are transferred to the customer as part of a lump sum contract, including building materials.

Under the bill, the maximum revenue loss would occur if contractors separate their charges into two contracts to take advantage of the tax exemption. Under such a scenario, the cost of labor and other nontaxable charges would be 90% of the value of the first contract and the remaining 10% would be construction materials and taxable services. A second contract would be the charge for the construction materials and taxable services not included in the first contract.

According to the 2007 Economic Census, the total value of construction work in Wisconsin was \$28.158 billion in 2007, and the cost of materials, components, and supplies totaled \$9.099 billion. The value of construction work less the value of materials, components, and supplies was \$19.059 billion in 2007. IHS Global insight currently forecasts that US construction will decrease 33.5% from 2007 to 2012. Assuming Wisconsin construction decreases by the same percentage, 2012 construction expenditures, excluding materials, are estimated at \$12.674 billion. Assuming \$12.674 billion represents 90% of the sum of the first contracts, the remaining 10% would be \$1.408 billion of taxable construction materials, components, and supplies. The remaining taxable materials and services would be placed on a second contract, and would exceed the 10% threshold that would allow for the exemption.

Revenue Impact: Assuming contractors segment their contracts as described above, it is estimated that state sales and use tax collections will decrease by up to \$70.4 million (5% x \$1.408 billion). County and stadium district sales taxes were 8.2% of state sales tax revenues in FY11. Assuming this percentage does not change, county and stadium district sales taxes would decrease by about \$5.8 million per year under the bill.

If, however, the bill is amended to only apply to a contractor's sales of taxable products to its customers (and thereby no longer provide an exemption for building materials consumed in real property construction), the

bill would have a much smaller fiscal effect. Assuming the amendment clarifies that contractors are deemed the consumer of taxable products that are sold as part of a lump sum contract, the fiscal effect of such an amended bill would be narrowed to the tax difference on the markup on contractor's sales of tangible personal property and taxable services. According to the 2007 Economic Census, the total value of retail trade by construction businesses in Wisconsin was \$68.2 million in 2007. IHS Global insight currently forecasts that US construction will decrease 33.5% from 2007 to 2012. Assuming that Wisconsin retail trade by construction businesses decreases by the same amount, 2012 retail sales by construction businesses are estimated at \$45.3 million. Assuming that contractors' markup on taxable products is 20%, sales of taxable products to Wisconsin contractors for resale will be \$37.8 million ($\$45.3 \text{ million} \div 120\%$) in 2012, resulting in a markup amount of \$7.5 million ($\$45.3 \text{ million} - \37.8 million).

Under such an amended bill, it is estimated that state sales and use tax collections would decrease by up to \$380,000 ($5\% \times \7.5 million) depending on the extent to which contractors currently make a separate charge for taxable products sold as part of a lump sum contract. County and stadium district sales taxes were 8.2% of state sales tax revenues in FY11. Assuming this percentage does not change, county and stadium district sales taxes would decrease by about \$30,000 per year under the bill.

Long-Range Fiscal Implications

Fiscal Estimate Worksheet - 2011 Session

Detailed Estimate of Annual Fiscal Effect

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Description A sales and use tax exemption for items and services sold as part of a lump sum contract			
I. One-time Costs or Revenue Impacts for State and/or Local Government (do not include in annualized fiscal effect):			
II. Annualized Costs:		Annualized Fiscal Impact on funds from:	
		Increased Costs	Decreased Costs
A. State Costs by Category			
State Operations - Salaries and Fringes	\$		\$
(FTE Position Changes)			
State Operations - Other Costs			
Local Assistance			
Aids to Individuals or Organizations			
TOTAL State Costs by Category	\$		\$
B. State Costs by Source of Funds			
GPR			
FED			
PRO/PRS			
SEG/SEG-S			
III. State Revenues - Complete this only when proposal will increase or decrease state revenues (e.g., tax increase, decrease in license fee, etc.)			
		Increased Rev	Decreased Rev
GPR Taxes	\$		\$-70,400,000
GPR Earned			
FED			
PRO/PRS			
SEG/SEG-S			
TOTAL State Revenues	\$		\$-70,400,000
NET ANNUALIZED FISCAL IMPACT			
		<u>State</u>	<u>Local</u>
NET CHANGE IN COSTS	\$		\$
NET CHANGE IN REVENUE		\$-70,400,000	-\$5,800,000
Agency/Prepared By		Authorized Signature	Date
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