LRB-1561/1

STATE OF WISCONSIN

REPORT OF THE JOINT SURVEY COMMITTEE ON TAX EXEMPTIONS

2013 ASSEMBLY BILL 40

[Introduced by the Joint Committee on Finance at the request of Governor Scott Walker.]

2013 Assembly Bill 40 is the 2013-15 Executive Budget Bill ("bill") prepared by the Governor and introduced by the Joint Committee on Finance at the request of the Governor. The bill contains a number of provisions that affect existing statutes or create new statutes relating to the exemption of property or persons from state or local taxes. This report addresses those provisions.

General Nature and Fiscal Effect of Tax Exemption Provisions in 2013 Assembly Bill 40

Deferral for Capital Gains Reinvested in Qualified New Business Ventures

2013 Assembly Bill 40 would sunset the deferral of capital gains reinvested in qualified new business ventures, effective for taxable years beginning after December 31, 2013.

The Legislative Fiscal Bureau (LFB) indicates this modification would have a minimal fiscal effect.

Deferral for Capital Gains Reinvested in Qualified Wisconsin Businesses

For taxable years beginning after December 31, 2013, Assembly Bill 40 would modify the deferral of capital gains reinvested in qualified Wisconsin businesses by adopting a registration procedure performed by the Department of Revenue (DOR). Under current law, qualifying capital gains reinvestments are certified by the Wisconsin Economic Development Corporation (WEDC). The bill would also modify the conditions for becoming a qualified Wisconsin business. Under Assembly Bill 40, a business would be required to meet the following conditions in the year immediately preceding the date of its registration: (a) the business must have at least two full-time employees and at least 50% of the business' payroll compensation must be paid by the business in Wisconsin; and (b) at least 50% of the value of the business' real and tangible personal property that is owned or rented and used must be located in Wisconsin.

The LFB indicates these modifications would have a minimal fiscal effect.

Deferral for Capital Gains on Sale of Wisconsin Capital Asset

Assembly Bill 40 would modify the deferral of capital gains on the sale of a Wisconsin capital asset by adopting a registration procedure performed by DOR. Under current law, qualifying businesses are certified by WEDC.

The bill would also modify the conditions for qualifying for the deferral of capital gains. The current definition of Wisconsin capital asset would be repealed. Instead, under the bill, the qualifying capital gain would be derived from an investment in a qualified Wisconsin business, provided that in the year immediately preceding the date of the business' registration: (a) the business has at least two full-time employees and at least 50% of the business' payroll compensation is paid by the business in Wisconsin; and (b) at least 50% of the value of the business' real and tangible personal property that is owned or rented and used is located in Wisconsin. Also, the bill would repeal a current law provision that limits the amount of the exclusion to the lesser of the amount of the claimant's federal net capital gain or the amount of the claimant's qualifying gain. These changes would apply retroactively to tax years beginning after December 31, 2010.

The LFB indicates these modifications would have a minimal fiscal effect.

Higher Education Tuition Deduction

Under the bill, the income phase-out levels for the higher education tuition deduction would be indexed based on the percentage change in the Consumer Price Index for all urban consumers, U.S. city average, for August of the year preceding the tax year for which the claim is made, and the index for August 2011. The adjustment would first occur for tax year 2013.

The LFB estimates that the fiscal effect of this provision would be to decrease revenues $670,000 in 2013-14 and $1,530,000 in 2014-15.

Exclusion for Interest on Wisconsin Health and Educational Facilities Authority-Issued Debt

The bill would provide an income tax exclusion for interest income received on bonds or notes issued by the Wisconsin Health and Educational Facilities Authority (WHEFA). Generally, in order to qualify for the exclusion, the WHEFA bonds or notes must be issued to a person who is eligible to receive tax-exempt bonds or notes from another issuer for the same purpose as the bonds or notes issued by WHEFA. The LFB indicates that the administration estimates the fiscal effect of this provision to result in a minimal loss of state tax revenues.

Internal Revenue Code Update

Generally, under 2013 Assembly Bill 40, the state's income and franchise tax statutes would continue to reference the Internal Revenue Code (IRC) in effect as of December 31, 2010, with certain exceptions. However, the bill would adopt certain changes made to the IRC prior to December 31, 2010, but which have not yet been adopted by the state, as well as certain changes made to the IRC after December 31, 2010.

These changes include: limiting the amount of contributions to flexible spending arrangements for medical expenses, to $2,500 annually, indexed for inflation; eliminating a deduction for employers who receive Medicare Part D retiree drug subsidy payments; increasing the threshold for the deduction for unreimbursed medical expenses from 7.5% of adjusted gross income (AGI) to 10% of AGI, but retaining the 7.5% threshold for individuals who are 65 years of age or over; increasing the penalty on distributions from health savings accounts that are not used for qualified medical expenses from 10% to 20% of the disbursed amount; and certain other changes.

The LFB indicates that the administration estimates the net fiscal effect of these provisions to be an increase of individual and corporate income and franchise tax collections by $15,500,000 in 2013-14 and $18,200,000 in 2014-15.

Sales and Use Tax Exemption for Lump Sum Contracts

2013 Assembly Bill 40 would create a sales and use tax exemption for certain lump sum contracts, defined to mean a contract to perform real property construction activities and to provide taxable goods or services and for which the contractor quotes the charge for labor, services of subcontractors, and the taxable items as one price, including a contract for which the contractor itemizes such charges as part of the schedule of values or similar document.

Under the bill, taxable items would be exempt if they constitute 10% or less of the total of the lump sum contract. Instead, for lump sum contracts with entities subject to sales and use tax, contractors would be the consumer of the taxable items and would pay sales tax on the purchase price of the items.

The LFB indicates that the administration estimates the provisions would reduce general fund revenues by $460,000 in 2013-14 and by $580,000 in 2014-15, as a result, generally, of sales and use tax being paid on the contractors' purchase price, rather than the contractors' final sales prices, including mark-up.

Sales and Use Tax Exemption for Qualified Research in Biotech and Manufacturing

2013 Assembly Bill 40 would make certain definitional changes relating to the existing sales and use tax exemption for qualified research in biotech and manufacturing, as well as the existing sales and use tax exemption relating to machinery and equipment used to raise animals for use in such qualified research. Generally, the changes relate to purchases by entities that are members of combined groups for purposes of combined reporting.

The modifications to these exemptions would be retroactive to sales made on or after January 1, 2012. The LFB indicates that the administration estimates the changes would have a minimal impact on sales and use tax revenues.

Sales and Use Tax Exemption for Veterinary Services

Under current law, certain items and property are exempt from the sales and use tax if used or consumed in the business of custom farming services. 2013 Assembly Bill 40 would define "custom farming services" to include services performed by a veterinarian to animals that are farm livestock or work stock.

The LFB indicates that the administration estimates this provision would codify current practices and would not have an impact on sales and use tax revenues.

Sales and Use Tax Exemption for Property Provided With Services

2013 Assembly Bill 40 would clarify that the sales and use tax exemption for products provided free of charge with the purchase of another product does not apply to products provided free of charge with the purchase of taxable services. Following 2011 Wisconsin Act 32, sellers were no longer required to pay use tax on products provided free of charge with the purchase of other products. The bill would clarify that this exemption does not extend to products provided free of charge with the purchase of taxable services, codifying current DOR practices.

The LFB indicates that DOR estimates this provision would maintain $5.2 million or more in sales and use tax revenues relating to the continued enforcement of current department practices.

Sales and Use Tax Exemption for Printing Services for Promotional and Direct Mail

Current law provides a sales and use tax exemption for promotional and direct mail. 2013 Assembly Bill 40 would exempt services related to printing of promotional and direct mail, effective July 1, 2013. The LFB indicates that the administration estimates the exemption would have a minimal impact on sales and use tax revenues.

Property Tax Exemption for Biogas Energy Systems

The bill would exempt biogas energy systems from property taxation, including equipment used to generate biogas and to store biomass or biogas, as well as structures used to shelter or operate such equipment. The administration estimates that the exemption would result in an aggregate statewide property tax shift of $516,000 to $1,032,000, as well as a reduction of state forestry tax revenues of $4,250 to $8,500.

Legality Involved

There are no questions of legality regarding the provisions of the bill described in this report.

Public Policy Involved

The bill is good public policy.

06/12/13 ***JOINT SURVEY COMMITTEE ON TAX EXEMPTIONS***