

**FISCAL ESTIMATE FORM**

**1999 Session**

- ORIGINAL     UPDATED  
 CORRECTED     SUPPLEMENTAL

LRB # 99-4588/3

INTRODUCTION # AB 852

Admin. Rule #

**Subject**

Create Sales and Use Tax Exemption for Digital Broadcasting Equipment

**Fiscal Effect**

- State:  No State Fiscal Effect  
 Check columns below only if bill makes a direct appropriation or affects a sum sufficient appropriation
- |  |  |  |
|--|--|--|
| <input type="checkbox"/> Increase Existing Appropriation | <input type="checkbox"/> Increase Existing Revenues            | <input type="checkbox"/> Increase Costs - May be Possible to Absorb Within Agency's Budget: <input type="checkbox"/> Yes <input type="checkbox"/> No |
| <input type="checkbox"/> Decrease Existing Appropriation | <input checked="" type="checkbox"/> Decrease Existing Revenues |  |
| <input type="checkbox"/> Create New Appropriation        |  |  |
- Decrease Costs

Local:  No Local Government Costs

- |  |   |  |
|--|---|--|
| 1. <input type="checkbox"/> Increase Costs<br><input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory | 3. <input type="checkbox"/> Increase Revenues<br><input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory                       | 5. Types of Local Governmental Units Affected:<br><input type="checkbox"/> Towns <input type="checkbox"/> Villages <input type="checkbox"/> Cities<br><input checked="" type="checkbox"/> Counties <input checked="" type="checkbox"/> Others <u>SWPBPD</u><br><input type="checkbox"/> School Districts <input type="checkbox"/> WTCS Districts |
| 2. <input type="checkbox"/> Decrease Costs<br><input type="checkbox"/> Permissive <input type="checkbox"/> Mandatory | 4. <input checked="" type="checkbox"/> Decrease Revenues<br><input type="checkbox"/> Permissive <input checked="" type="checkbox"/> Mandatory |  |

**Fund Sources Affected**

- GPR  FED  PRO  PRS  SEG  SEG-S

**Affected Ch. 20 Appropriations**

**Assumptions Used in Arriving at Fiscal Estimate:**

This proposal would create a sales and use tax exemption for digital-broadcasting equipment if purchased and used by a radio or television station. Currently, such items are considered tangible personal property and subject to the sales and use tax.

The Federal Communications Commission (FCC) has required that most television broadcasters convert to digital broadcasting by 2002. The FCC order will require new investment in digital transmission equipment by most of Wisconsin's 29 commercial TV stations that currently use analog equipment. The FCC has not yet mandated a switch to digital broadcasting for radio stations; therefore, the state's 250 commercial radio stations would not need to invest in digital broadcasting equipment in the near future.

As currently written, "digital broadcasting equipment" is not defined and could extend to all equipment used by broadcasters if indirectly part of the "digital" broadcast function of the TV or radio station. If so, the exemption may apply to all tangible personal property used in the production or transmission of digital broadcasts, such as office computers, ancillary broadcasting equipment, and other supplies used by the TV or radio station. The fiscal effect of such a broad exemption cannot be determined from available data. Nonetheless, the annual revenue loss associated with a more narrow interpretation of the proposal is also unknown because of considerable uncertainty regarding the conversion time frame and the potential expenditure required for digital broadcasting.

TV Transmission Equipment

Based on data from the National Association of Broadcasters (NAB), the average cost of digital transmission equipment will be about \$3 million per TV station. Under the proposal, there would be a

(continued on page two)

Long-Range Fiscal Implications:

Agency/Prepared by: (Name & Phone No.)	Authorized Signature/Telephone No.	Date
Wisconsin Department of Revenue John T. Stott, (608) 266-9706	Yeang-Eng Braun (608) 266-2700 <i>Yeang-Eng Braun</i>	3/16/00

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revenue loss of \$4.4 million ( $\$3 \text{ million} \times 29 \times .05$ ) over the next two years as Wisconsin TV stations switch to digital transmission equipment. There would also be an ongoing loss as replacement equipment is purchased.

TV Production Equipment

TV stations would not need to switch to digital production until the majority of their viewers had access to digital broadcasts. The Wisconsin Broadcasting Association (WBA) and NAB estimate that the cost to upgrade to digital production equipment would be \$6 million for large TV stations and \$2.5 million for small stations. According to the WBA, there are 10 large and 8 small production TV stations in the state; therefore, total production equipment investment would be \$80 million [ $(\$6 \text{ million} \times 10) + (\$2.5 \text{ million} \times 8)$ ]. The potential revenue loss would be \$4 million ( $\$80 \text{ million} \times .05$ ). Again, there would be an unknown annual revenue loss as replacement digital production equipment is purchased.

Radio Broadcast Equipment

According to the 1997-98 Wisconsin Blue Book, 250 commercial radio stations currently operate in Wisconsin. WBA estimates that the cost of conversion to DAB will be about \$150,000 per station, resulting in potential digital broadcasting equipment investment of \$37.5 million ( $\$150,000 \times 250$ ). The revenue loss associated with the investment in digital radio broadcasting equipment would be \$1.9 million ( $\$37.5 \text{ million} \times .05$ ). It is unknown when such expenditures would occur, and there would be an ongoing annual sales tax revenue loss as digital equipment is replaced or purchased.

Local Fiscal Effect

County and stadium sales tax revenues would decline as TV and radio stations make investments in digital broadcasting equipment. Long-term local sales tax revenues would be reduced as digital equipment is replaced or purchased.

Summary of Fiscal Effect

One-time fiscal effect:\*

	State Fiscal Effect (\$m)	Local Fiscal Effect (\$)
TV Transmission	-4.4	-0.32
TV Production	-4.0	-0.32
Radio	-1.9	-0.11
Total	-10.3	-0.75

\*The actual year(s) in which the one-time revenue loss occurs depends on when the investment is undertaken. On-going reductions in state and local sales taxes will occur as equipment is replaced—these are not shown.

YEB 3/16/00

**FISCAL ESTIMATE WORKSHEET**

Detailed Estimate of Annual Fiscal Effect

**1999 Session**

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**INTRODUCTION # AB 852**

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**Subject**

Create Sales and Use Tax Exemption for Digital Broadcast Equipment

**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 State funds from:	
A. State Costs by Category	Increased Costs	Decreased Costs
State Operations - Salaries and Fringe	\$	\$ -
(FTE Position Changes)	( FTE)	(- FTE)
State Operations-Other Costs		-
Local Assistance		-
Aids to Individuals or Organizations		-
<b>TOTAL State Costs by Category</b>	<b>\$</b>	<b>\$ -</b>
B. State Costs by Source of Funds	Increased Costs	Decreased Costs
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	\$	\$ - See Text
GPR Earned		-
FED		-
PRO/PRS		-
SEG/SEG-S		-
<b>TOTAL State Revenues</b>	<b>\$</b>	<b>\$ - See Text</b>

**NET ANNUALIZED FISCAL IMPACT**

	<u>STATE</u>	<u>LOCAL</u>
NET CHANGE IN COSTS	\$ _____	\$ _____
NET CHANGE IN REVENUES	\$ See Text _____	\$ See Text _____

Agency/Prepared by: (Name & Phone No.)	Authorized Signature/Telephone No.	Date
Wisconsin Department of Revenue John T. Stott, (608) 266-9706	Yeang-Eng Braun (608) 266-2700 <i>Yeang Eng Braun</i>	3/16/00



## Legislative Fiscal Bureau

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December 15, 1999

**TO:** Representative Dean Kaufert  
Room 22 West, State Capitol

**FROM:** Faith Russell, Fiscal Analyst

**SUBJECT:** Sales Tax Exemption for Broadcasting Equipment

At your request, this memorandum provides information on the fiscal effect of providing a sales tax exemption for equipment used for digital broadcasting by television (TV) and radio stations in Wisconsin.

### **Current Law - Sales Tax**

Under current law, the Wisconsin 5% general sales tax is imposed on the gross receipts from the sale and rental of tangible personal property and selected services. However, an exemption from the sales tax is provided for the sale and repair of machinery and equipment, including safety attachments, used exclusively and directly by a manufacturer in manufacturing tangible personal property. For purposes of this exemption, "manufacturing" is defined as the production by machinery of a new article with a different form, use and name from existing materials by a process popularly regarded as manufacturing.

Under current law, TV and radio stations are not classified as manufacturers for sales tax purposes and broadcasts are not considered to be tangible personal products. Therefore, machinery and equipment used in broadcasting are not eligible for the sales tax exemption for manufacturing machinery and equipment.

### **Digital Broadcasting**

Most commercial TV stations will be required to begin digital broadcasting by May, 2002, as a result of an order by the Federal Communications Commission (FCC) implementing digital television (DTV). Once stations have started digital broadcasting, they will be required to broadcast simultaneously in digital and analog (the current format) formats until 2006, after which

it is expected that the analog format will no longer be used. Digital radio broadcasting, referred to as digital audio broadcasting (DAB), has not yet been mandated by the FCC. However, industry sources anticipate that DAB will follow shortly after DTV. The conversion to digital broadcasting will require capital expenditures on the part of both TV and radio stations.

For the conversion to DTV, TV stations are required to have the capacity to pass through digital broadcasts by the May, 2002, deadline. The next step will be to produce digital broadcasts, rather than simply to pass them through. According to industry sources, TV stations will have to have the ability to produce some types of broadcasts by 2008. The cost of converting to DTV will vary by station and the level of production capability for which the station will be configured.

Industry estimates vary as to the average cost of implementing DTV. The National Association of Broadcasters has estimated that individual stations will spend \$8 to \$12 million for a full conversion. Another local source projects an average cost for Wisconsin TV stations of \$6.5 million for full conversion to DTV. A Madison station that has begun to implement DTV estimates that its total costs for full conversion will be \$5.6 million. The Wisconsin Broadcasters Association (WBA) anticipates that initial outlays may be as much as \$3 million to \$6 million for TV stations to purchase digital transmitting equipment and another \$3 million to \$6 million for production equipment.

Industry estimates also vary as to the number of TV stations that will implement production facilities for DTV and the time frame for associated expenditures. WBA estimates that 70% of Wisconsin stations will implement full production facilities and that the conversions will not be complete until sometime in 2006. Another industry source maintains that all stations will have to implement full production facilities in order to compete and that most will finish implementation by May, 2002.

The cost and timing of radio conversion to DAB are even less certain than for DTV, as the conversion has not yet been mandated. WBA has estimated costs of \$75,000 to \$200,000 per station. The costs per station are also expected to vary depending on whether the station is an AM or FM station.

### **Fiscal Effect of Sales Tax Exemption**

The estimates provided below are based on projections of average costs and timing of costs provided by the Vice-President of Equipment for the Journal Broadcast Group, who is also an engineer for a Wisconsin TV station. The estimate of the number of commercial TV and radio stations in Wisconsin was compiled by WBA, based on the Broadcasting and Cable Yearbook 1999.

#### **Television**

The estimate of the fiscal impact of providing an exemption from the sales tax for equipment used by commercial TV stations in Wisconsin for broadcasting in digital format assumes the following: (a) there are 31 commercial TV stations in the state; (b) all TV stations will

implement DTV at a level to include both pass-through and production capabilities; (c) capital costs to convert to DTV will average \$6.5 million per station; (d) all stations will complete the conversion by the end of calendar year 2002; and (e) once a station has converted to DTV, digital maintenance costs will average \$100,000 annually.

Based on the assumptions described above, it is estimated that a sales tax exemption for television equipment needed for digital broadcasting would result in a decrease in general fund tax collections of \$2.7 million in 2000-01, assuming an effective date of July 1, 2000. It is estimated that sales tax reductions as a result of the exemption would be \$3.3 million in 2001-02, \$2.0 million in 2002-03, and then begin to decrease until reaching a baseline of \$360,000 annually beginning in 2007-08. All estimates are provided in 2000-01 dollars.

Because the optional county sales tax is "piggy-backed" on the state sales tax, it is estimated that an exemption from the sales tax for equipment used for digital broadcasts would reduce county tax collections by \$270,000 in 2000-01. Currently, 53 of the 72 counties in Wisconsin impose the county sales tax.

As described above, projections vary as to the timing, the level and the cost of making the conversion to DTV. The fiscal effect of the exemption could be larger or smaller than the estimate provided if actual experience differs from the assumptions used to make the estimate. For example, if not all stations implement full production capabilities, as this estimate assumes, the cost per station to convert to DTV could be lower than the \$6.5 million used in the fiscal estimate. On the other hand, based on the maximum cost of \$12 million per station for full conversion projected by both WBA and the National Association of Broadcasters, the average cost could be higher than the \$6.5 million used in the estimate. In addition, if stations do not fully implement DTV by May, 2002, the time frame used in the estimate, the impact would be to shift some of the reduction in sales tax collections from the exemption into subsequent years.

## **Radio**

The estimate of the fiscal effect of providing an exemption from the sales tax for equipment for digital broadcast used by commercial radio stations in Wisconsin assumes the following: (a) there are 260 commercial radio stations in the state; (b) there are currently capital and maintenance costs for digital equipment that average \$23,000 per station and this will be the ongoing cost even after conversion to DAB; (c) capital costs to convert to DAB will average \$174,200 per station; and (d) stations will make the conversion in calendar years 2002 and 2003.

Based on these assumptions, it is estimated that a sales tax exemption for equipment for digital radio broadcasting would result in a decrease in general fund tax collections of \$270,000 in 2000-01, assuming an effective date of July 1, 2001. In addition, county tax collections would decrease by an estimated \$27,000 in 2000-01.

The estimate of the fiscal effect in 2000-01 of a sales tax exemption for digital radio broadcast equipment is based on the current capital and maintenance costs for digital equipment described under (b) above. In addition to this ongoing effect, it is estimated that state sales tax

collections in 2001-02, 2002-03 and 2003-04 would be reduced by an average of \$710,000 per year as a result of the conversion to DAB. The fiscal effect in individual years would vary from this amount depending on the timing of the conversion.

### **Analog Broadcasting Equipment**

Because the FCC order requires television stations to continue broadcasting in the current analog format until 2006, the broadcast industry would incur equipment and repair costs needed to maintain analog broadcasting functions as well. The Department of Revenue has indicated that it could be administratively difficult to provide a sales tax exemption for digital equipment only. Some equipment is necessary for broadcasting in either format. In addition, while the term "digital broadcast equipment" has been used, the equipment needed to broadcast digitally is not always digital equipment. For example, in many cases, new towers will be needed in order to broadcast digitally. However, the same towers could be used for analog broadcasts. It would have to be clear whether this type of equipment, that could be used for either analog or digital broadcasts, would be eligible for a "digital broadcast equipment" sales tax exemption. Because the distinction between types of equipment would not always be clear, it could be difficult to enforce a limitation of the sales tax exemption to broadcast equipment for digital broadcasting. If a sales tax exemption for broadcast equipment were to be extended to analog as well as digital equipment, state sales tax collections for 2000-01 would be further reduced by an estimated \$800,000, assuming an effective date of July 1, 2000 (\$600,000 for equipment for TV stations and \$200,000 for equipment for radio stations).

I hope this information is useful. Please let me know if you have additional questions.

FR/dls