



Legislative Fiscal Bureau

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TO: Members
Joint Committee on Finance

FROM: Bob Lang, Director

SUBJECT: Assembly Bill 757: Individual Income and Corporate Income and Franchise Taxes --
Food Processing Plant and Warehouse Investment Tax Credit

Assembly Bill 757, which would create a food processing plant and warehouse investment tax credit under the state individual income and corporate income and franchise taxes, was introduced on February 17, 2010, and referred to the Assembly Committee on Agriculture. The bill was recommended for passage by that committee by a vote of 11 to 0 on February 25, 2010.

CURRENT LAW

Under current law, capital assets used in a trade or business are usually depreciated. The deduction for depreciation allows taxpayers to recover, over a period of years, the cost of capital assets used in a trade or business or for the production of income. Because state depreciation provisions are referenced to the Internal Revenue Code (IRC) in effect on December 31, 2000, tangible depreciable property currently placed in service is generally subject to the federal Modified Accelerated Cost Recovery System (MACRS). Specifically, the cost of eligible property is recovered over a 3, 5, 7, 10, 15, 20, 27.5, 31.5, 39, or 50-year period depending upon the type of property involved. Depreciation methods are prescribed for each MACRS class. Generally, personal property is assigned to the three-year class, the five-year class, the seven-year class, or the 10-year class. Real property is assigned to the remaining classes based on the type of property involved. Property included in the three-year, five-year, seven-year, and ten-year classes is depreciated using the double declining balance method, switching to the straight-line method at a time which maximizes the depreciation allowance. Property in the 15-year and 20-year classes is depreciated using the 150% declining balance method, again switching to the straight-line method at a time which maximizes the depreciation allowance.

Under Section 179 of the IRC, a taxpayer may elect to treat all or a portion of the cost of

qualifying property, up to a limit, as an expense rather than as a capital expenditure. Such an expense or cost is deductible in the year in which the property is placed in service. Federal section 179 provisions enacted since 2003 have not have adopted for state income and franchise tax purposes for non-farm property. Rather, state taxpayers are generally subject to Section 179 IRC provisions that were in effect for tax years through 2002. As a result, under current Wisconsin law, a taxpayer may elect to deduct up to \$25,000 of the cost of qualifying property (except for property used in farming) in the year it is placed in service rather than taking depreciation deductions over a specified recovery period. In general, qualifying property is depreciable tangible personal property that is purchased for the active conduct of a trade or business. The maximum deductible amount of \$25,000 is reduced (but not below zero) by the amount by which the qualifying property placed in service during the taxable year exceeds \$200,000. In addition, the amount eligible to be expensed for a tax year may not exceed the taxable income of the taxpayer that is derived from the active conduct of a trade or a business for that year. Any amount that is not allowed as a deduction because of the taxable income limitation may be carried forward to succeeding years and deducted, subject to the total investment and taxable income limits. The \$25,000 expense limits also applies to vehicles weighing between 6,000 and 14,000 pounds.

Current state law is referenced to the Section 179 provisions included in the federal Tax Increase Prevention and Reconciliation Act of 2005, for property that is used in farming that is acquired and placed in service in tax years beginning on or after January 1, 2008, and used by a person who is actively engaged in farming. Under the Act, the maximum amount that could be expensed was \$100,000, and the investment limit was \$400,000. Both the maximum expense deduction and investment limit were indexed for inflation. Consequently, for state income and franchise tax purposes, for the 2009 state tax year, the maximum amount that can be expensed is \$120,000, and the investment limit is \$480,000, for eligible property used in farming.

The terms "farming" and "actively engaged in farming" are referenced to federal law. "Farming" means the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity including the raising, shearing, feeding, caring for, training, and management of animals. Trees, other than trees bearing fruit or nuts, are not treated as an agricultural or horticultural commodity.

"Actively engaged in farming" means that the individual or entity independently makes a significant contribution to a farming operation of: (a) capital, equipment, or land, or a combination of capital, equipment, or land; and (b) active personal labor or active personal management, or a combination of active personal labor and active personal management. In determining if the individual or entity is actively contributing a significant amount of active personal labor or active personal management, the following factors must be considered: (a) the types of crops and livestock produced by the farming operation; (b) the normal and customary farming practices of the area; and (c) the total amount of management and labor necessary for such a farming operation in the area. In order to be actively engaged in farming, the individual or entity must have: (a) a share of the profits or losses from the farming operation; and (b) contributions to the farming operation that are at risk.

SUMMARY OF BILL

AB 757 would create a refundable food processing plant and food warehouse investment tax credit under the state individual income and corporate income and franchise taxes, equal to 10% of the amount paid in the tax year by the claimant for food processing or food warehousing modernization or expansion. The credit could be claimed for tax years beginning after December 31, 2009, and before January 1, 2017. In order to claim a tax credit, a claimant would have to submit to the Department of Revenue (DOR) a copy of the Commerce certification of the claimant's eligibility and tax credit allocation.

The maximum aggregate amount of tax credits that could be claimed by a taxpayer would be \$200,000, and a credit could not be claimed for expenses that were deducted as trade or business expenses. If two or more persons owned and operated a food processing plant or food warehouse, each person could claim a tax credit in proportion to his or her ownership interest, except that the aggregate amount of credits claimed by all the persons who owned and operated the food processing operation could not exceed the \$200,000 aggregate tax credit limit. (The \$200,000 aggregate tax credit limit would apply to partnerships, limited liability companies [LLCs], and tax-option corporations [S-corporations].) If the allowable credit claim exceeded the taxes otherwise due on the claimant's income, the amount of credit claim that was not used to offset tax due would be certified by DOR to the Department of Administration for payment by check, share draft, or other draft from a GPR sum sufficient appropriation that would be created under the bill. The total amount of tax credits that could be claimed would be limited to \$600,000 for fiscal year 2009-10 and \$700,000 for subsequent fiscal years.

Partnerships, LLCs, or tax-option corporations could not directly claim the tax credit, but eligibility for, and the amount of the credit that could be claimed, would be based on the entity's payment of eligible expenses, subject to the \$200,000 limit on the total amount of tax credits that a taxpayer could claim. A partnership, LLC, or tax-option corporation would be required to compute the amount of the credit that each of its partners, members, or shareholders could claim and provide that information to them. Partners, members, and shareholders could claim the credit in proportion to their ownership interest.

The Department of Commerce would be required to certify taxpayers as eligible for the food processing plant and food warehouse investment tax credit. Once Commerce certified a taxpayer as eligible for the tax credit, it would determine the amount of credits that a taxpayer could claim, and allocate those credits to the taxpayer. Commerce would be required to inform DOR of every taxpayer that was certified, and of the amount of credits allocated to the taxpayer. Commerce, in consultation with DOR, would be also required to promulgate rules to administer the certification and allocation process. DOR would administer the tax credit, and current law provisions related to change of ownership and timely claims would apply to the food processing plant and food warehouse investment tax credit.

“Food processing plant or food warehouse modernization or expansion” would mean

constructing, improving, or acquiring buildings or facilities, or acquiring equipment, for food processing or food warehousing, including the following, if used exclusively for food processing or food warehousing and if acquired and placed in service in this state during taxable years that begin after December 31, 2009, and before January 1, 2017:

- a. Food intake, handling, storage, and warehouse facilities.
- b. Building additions.
- c. Upgrades to utilities, including water, electric, heat, refrigeration, freezing, and waste facilities.
- d. Installing energy savings equipment or equipment that converts waste to energy.
- e. Food or raw material intake and storage equipment.
- f. Processing and manufacturing equipment, including vats, cookers, freezers, pipes, motors, pumps, and valves.
- g. Packaging and handling equipment, including cleaning, sealing, bagging, boxing, labeling, conveying, and product movement equipment.
- h. Warehouse equipment, including storage racks and loading and unloading equipment.
- i. Waste treatment and waste management equipment, including tanks, blowers, separators, dryers, digesters, and equipment to produce energy, fuel, or industrial products.
- j. Computer software or hardware for managing the claimant's food processing or food warehousing operation, including software and hardware related to logistics, inventory management, production plant controls, and temperature monitoring controls.

"Food processing plant" would be defined as any place where food processing was conducted. However, it would not include establishments subject to the state retail food establishment law or state lodging and food protection permits. In addition, state licensed dairy plants and meat establishments would be excluded. "Food warehouse" would mean a warehouse used for the storage of food, including a cold-storage warehouse, frozen-food warehouse, and frozen-food locker plant. The definition of "food warehouse" would not include certain facilities specified under state law, including: (a) a grain or raw agricultural commodity storage warehouse; (b) retail food establishment, restaurant or other similar establishment; (c) licensed dairy-plant or meat establishment warehouses; (d) a licensed milk distributor warehouse; and (e) consumer owned or operated facilities.

"Used exclusively" would mean used to the exclusion of all other uses, except for use not

exceeding 5% of total use.

FISCAL EFFECT

Based on information from the 2006 Annual Census of Manufacturers, compiled by the U.S. Census Bureau, it is estimated that the food processing plant and food warehouse investment tax credit would increase state GPR expenditures by \$700,000 in 2010-11 through 2016-17. The credit would increase expenditures because it is refundable.

[As noted above, under the bill, the aggregate amount of credits that could be claimed by all taxpayers would be limited to \$600,000 in 2009-10 and \$700,000 in 2010-11 and subsequent fiscal years. However, the credit could not be claimed until tax year 2010, and credits for that tax year would be paid in fiscal year 2010-11. Therefore, the \$600,000 limit in 2009-10 would not apply.]

On January 27, 2010, this office issued a memorandum regarding the status of the state's general fund. At that time, the gross balance of the general fund, as of June 30, 2011, was estimated at \$55.7 million, or \$9.3 million below the \$65.0 million balance required under s. 20.003(4) of the state statutes. As a result, an amendment would be needed to include a notwithstanding clause relative to s. 20.003(4).

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