General Fund Taxes

Income and Franchise Taxes

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June, 2019 Joint Committee on Finance Paper #315

Create the Family and Individual Reinvestment Credit and Sunset the Working Families Credit (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 134, #1 and Page 143, #16]

CURRENT LAW

Under the individual income tax, Wisconsin taxable income is multiplied by the applicable tax rates to arrive at gross tax liability. Wisconsin provides a number of tax credits that may be subtracted from gross tax liability. Most individual income tax credits are not refundable, meaning that the credit can be used to reduce net tax liability to zero, but the amount of the credit cannot exceed tax liability. The state statues specify the order in which tax credits are claimed.

The working families tax credit may be claimed by taxpayers with Wisconsin adjusted gross income (AGI) below $10,000 ($19,000 if married joint). For claimants with AGI below $9,000 ($18,000 if married joint), the credit is equal to their net tax liability. The credit phases out over the next $1,000 in income until eliminated when Wisconsin AGI exceeds $10,000 ($19,000 if married joint).

GOVERNOR

Create a nonrefundable individual income tax credit beginning in tax year 2019 called the family and individual reinvestment credit, with the credit equal to a minimum dollar amount or a percentage of the claimant's net tax liability, subject to phaseout based on the claimant's Wisconsin AGI and filing status. Set the credit equal to the greater of 10% of the claimant's net tax liability, defined as the claimant's income tax liability prior to the application of the nonrefundable credit for taxes paid to other states, or (a) $100 if the claimant's filing status is single or head-of-household and the claimant's AGI is less than $80,000; (b) $50 if the claimant's filing status is married joint and the combined AGI of the claimant and the claimant's spouse is less than $125,000; and (c) $25 if the claimant's filing status is married separate and the claimant's AGI is less than $62,500. If the claimant's AGI, or combined AGI in the case of married joint filers, exceeds the preceding income thresholds but is less than $100,000 for single or head-of-household filers, $150,000 for married joint filers, and $75,000 for married separate filers, set the credit equal to the claimant's net tax liability multiplied by a percentage calculated as follows: (a) subtract the applicable income threshold from the claimant's AGI, or combined AGI in the case of married joint filers; (b) divide the difference by $20,000 if the claimant's filing status is single or head-of-household, $25,000 if the claimant's filing status is married joint, or $12,500 if the claimant's filing status is married separate; (c) subtract that fraction from 1.0; and (d) multiply that fraction by 10%. Under this structure, the 10% credit would phase down between $80,000 and $100,000 for single and head-of-household filers, $125,000 and $150,000 for married joint filers, and $62,500 and $75,000 for married separate filers, and the credit would phase out at the higher income thresholds for each filer type. Limit the credit to claims filed within four years of the unextended due date for which the tax return was due. Prohibit part-year residents and nonresidents from claiming the credit, and allow only one credit per household per year, except permit married separate filers to each claim the credit, as provided above, and permit married persons living apart and treated as single under the Internal Revenue Code (IRC) to claim the credit as if a single or head-of-household claimant. Define household as a claimant and an individual related to the claimant as husband or wife. Prohibit individuals who may be claimed as a dependent on a return of another taxpayer from claiming the credit. Authorize the Department of Revenue (DOR) to administer the credit under standard general statutory provisions related to the income tax. Decrease individual income tax collections by an estimated $421,550,000 in 2019-20 and $412,050,000 in 2020-21 and in each year thereafter.

Sunset the nonrefundable working families tax credit, effective in tax year 2019. The Department of Administration (DOA) indicates that the sunset would increase individual income tax collections by an estimated $50,000 annually. An additional amount of credits would be offset by credits claimed under the proposed family and individual reinvestment credit.

DISCUSSION POINTS

1. The family and individual reinvestment credit embodies Governor Evers' promise during the 2018 gubernatorial election to provide middle income tax relief by reducing taxes by 10% for families with incomes below $150,000 and for other tax filers with incomes below $100,000. DOA's Budget in Brief makes the case for targeting relief in this fashion by noting that "Wisconsin's middle-income filers are comparatively the most-heavily taxed income group in the state when comparing income tax burdens across states for different income levels."

2. DOA cites an April, 2017, report by the Minnesota Center for Fiscal Excellence, entitled Comparison of Individual Income Tax Burdens by State, 2017 Edition. Using tax year 2014 provisions in each of the 42 states with a state individual income tax, the report calculates the tax burdens for households at multiple income levels by filing status using a model maintained by the National Bureau of Economic Research. The report ranks each state's tax burden for each income category, with low rankings indicating a relatively high tax burden and high rankings indicating a

relatively low tax burden. The Budget in Brief includes only Wisconsin's rankings for married joint filers and excludes the ranking for the report's highest married joint income category ($1.0 million). Table 1 displays the report's rankings for each of its income categories, for both married joint and single filers. Note that the report employs different income categories for married joint and single filers. The table's highest tax rankings occur for married joint filers with an income of $100,000 (10) and for single filers with incomes of both $50,000 and $75,000 (12), thereby supporting the Budget in Brief finding of Wisconsin's middle-income filers being the most heavily taxed income group, in relative terms.

TABLE 1

Wisconsin Individual Income Tax Rankings for Married Joint and Single Filers at Various Income Categories, Tax Year 2014

Income	Wisconsin 42-State Ranking	
Category	Married Joint	Single
$10,000	--	19
20,000	32	30
35,000	30	19
50,000	22	12
75,000	13	12
100,000	10	13
150,000	14	17
250,000	16	17
500,000	16	--
1,000,000	11	--

Source: Minnesota Center for Fiscal Excellence, Comparison of Individual Income Tax Burdens by State, 2017 Edition, April 2017.

3. Another way to analyze the Minnesota report's data is to compare the Wisconsin tax burdens by income category to the average, unweighted tax burdens for the 42 states with an income tax. Table 2 displays this comparison. For example, the Wisconsin tax burden for taxpayers with an income of $20,000 is below the 42-state average by 48% for married joint filers and 26% for single filers. Further, the Wisconsin tax burden for married joint filers is at or below the 42-state average for income categories of $50,000 or less, but increases to 16% above the average for the $75,000 income category. For single filers, the Wisconsin tax burden is only 3% above the 42-state average for filers with income of $35,000 and is below the average for filers with incomes or $10,000 and $20,000. However, the Wisconsin tax burden exceeds the 42-state average by 12% at the $50,000 income level. Under the Governor's proposal, taxpayers at these income levels would qualify for maximum credits of 10%, but the credit percentage would begin to phase out when income exceeds $125,000 for married joint filers and $80,000 for single filers.

TABLE 2

Wisconsin Individual Income Tax Burdens, 42-State Average Tax Burdens, and Difference Between Wisconsin and Average as a Percentage of the Average for Married Joint and Single Filers at Various Income Categories, Tax Year 2014

Income	Wisconsin Tax Burden		42-State Average Tax Burden		Wisconsin Percentage Above or Below Average	
Category	Married Joint	Single	Married Joint	Single	Married Joint	Single
$10,000	--	$0	--	$41	--	-100%
20,000	-$601	371	-$407	503	-48%	-26
35,000	-45	1,293	268	1,251	-117	3
50,000	1,175	2,295	1,225	2,051	-4	12
75,000	2,984	3,634	2,577	3,277	16	11
100,000	4,122	4,989	3,575	4,534	15	10
150,000	7,130	7,720	6,301	7,125	13	8
250,000	12,481	12,943	11,523	11,921	8	9
500,000	28,877	--	26,149	--	10	--
1,000,000	66,532	--	58,064	--	15	--

Source: Minnesota Center for Fiscal Excellence, Comparison of Individual Income Tax Burdens by State, 2017 Edition, April 2017.

4. Under the credit's phaseout mechanism, a credit rate of 10% would extend to the net tax liability of taxpayers with incomes, at or below, the initial income threshold for the phaseout, and a credit rate of 0% would extend to the net tax liability of taxpayers with incomes above the second income threshold. The credit percentage would decrease based on the difference between the taxpayer's income and the "spread" between the two income thresholds for the taxpayer's filing type. Table 3 demonstrates how the percentage would phase out based on examples of taxpayers with different income levels.

TABLE 3

Credit Percentage Phaseout Based on Different Income Levels and Filing Types

Credit Rate	Single Income	Married Joint Income	Married Separate Income
10%	$80,000	$125,000	$62,500
8	84,000	130,000	65,000
6	88,000	135,000	67,500
4	92,000	140,000	70,000
2	96,000	145,000	72,500
0	100,000	150,000	75,000

5. Attachment 1 reports the estimated distribution of the proposed credit's claimants for tax

year 2019. It displays distributional information for married joint filers, other filers, and the two groups combined. For tax year 2019, the average credit is estimated at $216. Because married joint filers have average net tax liabilities that are higher than other filer types, the average credit for married joint filers ($305) would be higher than the average credit for other filer types ($156). Because the credit would equal 10% of net tax liabilities and net tax liabilities increase with income, average credit amounts also increase with AGI. However, average credit amounts decline after AGI exceeds the initial phaseout thresholds, and no credits are available to tax filers with AGI exceeding maximum income thresholds. Reflecting the targeted design of the credit, Attachment 1 indicates that the credit would deliver a tax reduction to more than 90% of the filers with AGI between $30,000 and $100,000, even though the credit would provide a tax reduction to only 60.3% of all tax filers. Taxpayers with Wisconsin AGI between $30,000 and $125,000 would receive 82.1% of the estimated tax decrease and would comprise 70.7% of the taxpayers with a tax decrease. The tax year 2019 reduction in state tax collections of $409.1 million that is reflected in Attachment 1 would increase to an estimated $412.0 million in tax year 2020.

6. Attachment 1 reflects minimum credit amounts of $100 for single and married joint claimants and $50 for married separate filers, provided their AGI is below the initial income threshold for their filing type. This is consistent with DOA's Budget in Brief, although the bill specifies minimum credit amounts of $50 for married joint filers and $25 for married separate filers. DOA has submitted an errata requesting the higher minimum credit amounts. This paper assumes the bill would be modified by adopting the DOA errata, if the Committee votes to retain the proposed credit in the bill. In addition, the bill indicates that the income of a married joint claimant would be summed with the income of the claimant's spouse for purposes of comparing the claimant's income to the income thresholds. Currently, married joint filers already combine their income when preparing their return. The DOA errata also requests that the bill be modified by deleting references to summing the income of the claimant and spouse and substituting references to the married couple's AGI.

7. Adopting the family and individual reinvestment credit would add another calculation to the state's individual income tax forms. While sunsetting the working families credit would remove a tax form calculation, the new credit would be claimed by a far larger number of taxpayers than currently claim the working families credit. Since the 2013 legislative session, the Legislature has adopted a number of provisions seeking to simplify the calculation of individual income taxes, including reducing the number of rates and brackets, sunsetting under-used tax credits, and federalizing the state's treatment of changes to the Internal Revenue Code. If the Legislature's policy goal is to target $400 million annually in tax relief to taxpayers with middle to lower levels of AGI, other alternatives could be considered that modify existing tax provisions.

8. Earlier this session, the Legislature voted to expand the sliding scale standard deduction. The sliding scale standard deduction targets tax relief to low and middle income taxpayers by providing a deduction to income that phases out as AGI increases. For tax year 2019, a maximum deduction of $20,110 is extended to married joint filers with Wisconsin AGI less than $22,599. Single and head-of-household filers with AGI less than $15,659 receive a maximum deduction of $10,860 and $14,030, respectively. As AGI increases, each of the deduction amounts phases down, until it equals $0 when AGI exceeds $124,279 for married joint filers and $106,160 for single and head-of-household filers. The deduction phaseouts are based on statutory percentages for each filing type,

except the percentage for head-of-household filers changes to the percentage for single filers when AGI reaches a certain level. The deduction and income phaseout amounts for married separate filers are set equal to 47.5% of the amounts for married joint filers.

9. As an alternative to the proposed family and individual reinvestment credit, the sliding scale standard deduction could be expanded to provide approximately $400 million in annual tax relief to roughly the same taxpayers eligible for the family and individual reinvestment credit. Table 4 compares the parameters for the tax year 2019 deduction under current law and an expanded deduction. Under this alternative (Alternative 2), the maximum deduction and initial phaseout income levels are increased by 23%. The phaseout percentages were decreased by 10% for married and head-of-household filers and increased by 10% for single filers, thereby reducing the gap between single and other filers.

TABLE 4

Sliding Scale Standard Deduction Factors Under Current Law and Alternative Proposal, Tax Year 2019

	Single	Head-of-Household*	Married Joint	Married Separate
Current Law				
Maximum Deduction	$10,860	$14,030	$20,110	$9,550
Initial Income Phaseout Level	15,659	15,659	22,599	10,729
Phaseout Percentage	12.000%	22.515%	19.778%	19.778%
Maximum Income Level	106,160	106,160	124,279	59,016

*The calculation for head-of-household filers equals that for single filers when AGI exceeds $45,807.

	Single	Head-of-Household*	Married Joint	Married Separate
Alternative Proposal				
Maximum Deduction	$13,360	$17,260	$24,730	$11,750
Initial Income Phaseout Level	19,259	19,259	27,799	13,199
Phaseout Percentage	13.200%	22.264%	17.800%	17.800%
Maximum Income Level	120,472	120,472	166,733	79,211

*The calculation for head-of-household filers equals that for single filers when AGI exceeds $74,470.

10. Attachment 2 displays the estimated distribution of taxpayers with a tax decrease under this alternative for tax year 2019. Just over two million taxpayers would receive a tax decrease, or 64.4% of all tax filers. Among these taxpayers, an average tax decrease of $200 is estimated, with married joint filers receiving an average decrease that is more than twice the average for other filers ($286 versus $139). The average tax decrease by Wisconsin AGI category would increase until peaking at $70,000 to $90,000 for married joint filers and $30,000 to $50,000 for other filer types. These income ranges are slightly below the midpoint of the proposed income phaseout ranges for each filer type. Taxpayers with Wisconsin AGI between $30,000 and $125,000 would receive 83.4% of the estimated tax decrease and would comprise 68.8% of the taxpayers with a tax decrease. The tax year 2019 reduction in state tax collections of $404.5 million that is reflected in Attachment 2 would increase to an estimated $415.8 million in tax year 2020.

11. Another income tax reduction mechanism that could be employed would be an across-the-board reduction in individual income tax rates. The Legislature chose this approach in 2013 for the conversion of general sales and use tax proceeds from remote sellers into an income tax decrease and re-affirmed this mechanism late last year in its enactment of 2017 Wisconsin Act 368. A 4% reduction in each of the four marginal tax rates would reduce individual income tax collections by an estimated $398.9 million in tax year 2019 and $423.7 million in tax year 2020 (Alternative 3), roughly equivalent to the two-year decreases resulting from the other alternatives presented in this paper. The income brackets for each marginal rate would remain unchanged, resulting in the following rate and bracket structure:

TABLE 5

Rate and Bracket Structure Under Current Law and a 4% Tax Rate Reduction
Tax Year 2019

Marginal Tax Rates		Single and	Married	Married
Current Law	Alternative	Head-of-Household	Joint	Separate
4.00%	3.84%	$0 to $11,760	$0 to $15,680	$0 to $7,840
5.84	5.61	11,760 to 23,520	15,680 to 31,360	7,840 to 15,680
6.27	6.03	23,520 to 258,950	31,360 to 345,270	15,680 to 172,630
7.65	7.35	258,950 and over	345,270 and over	172,630 and over

12. The estimated tax year 2019 distribution of taxpayers with a tax decrease under a 4% across-the-board tax rate reduction is displayed in Attachment 3. Almost 2.3 million taxpayers would receive a tax decrease, or 72.5% of all tax filers. Among these taxpayers, an average tax decrease of $175 is estimated, with married joint filers receiving an average decrease that is triple the average for other filers ($280 versus $91). This occurs because married joint filers, relative to other filers, have higher average incomes ($108,602 versus $33,841), which subjects them to higher marginal tax rates and results in higher average tax liabilities ($6,131 versus $1,995). For the same reason, the average tax change would increase with income, except in two Wisconsin AGI categories. For each AGI category, the share of the tax decrease would be roughly proportional to those taxpayers' share of net tax liability -- taxpayers with Wisconsin AGI over $100,000 incur 66.6% of total net income tax liabilities and would receive 66.5% of the estimated tax decrease.

13. Background information submitted by DOA on the Governor's proposal packaged the creation of the family and individual reinvestment credit with sunsetting the working families credit. None of the three attachments display the effects of sunsetting the working families credit, but that action would reduce the fiscal effect of each alternative by an estimated $50,000 annually.

14. In tax year 1999, 166,478 claimants used $25.1 million in working families credits to eliminate or reduce their individual income tax liability. Since then, the number of claimants and amount of used credits have dropped dramatically, and the amount of used working families credits has fluctuated from year to year. In tax year 2016, 259 filers used credits totaling only $76,692, and only 307 claimants used credits totaling $106,878 in tax year 2017. The reason for the reduction in claimants and credits is the expansion of the sliding scale standard deduction, which eliminates

individual income tax liabilities for most taxpayers otherwise eligible for the credit. Despite the expansion of the sliding scale standard deduction, several hundred claimants use about $100,000 in credits each tax year, and the nature of these claimants' tax circumstances has been somewhat of a mystery.

15. Department of Revenue distributional information relating to the combined effects of creating the family and individual reinvestment credit and sunsetting the working families credit reveals that about 200 taxpayers each year with incomes between $5,000 and $20,000 would experience tax increases under the combined proposals.

16. Nonresidents are not eligible to claim the working families credit, but Wisconsin residents who are married to nonresidents may claim the credit using special rules. These taxpayers pay state taxes using Form 1NPR for nonresidents and part-year residents, which requires them to calculate their sliding scale standard deduction using their federal AGI (combined income of both spouses). While the Wisconsin spouse may have a low Wisconsin AGI, the couple's federal AGI may result in a sliding scale standard deduction that is not sufficient to offset the couple's Wisconsin income tax liability. Nonetheless, the Wisconsin spouse may be eligible to claim the working families credit based on his or her Wisconsin AGI. Thus, the 200 or so taxpayers with a tax increase are Wisconsin residents married to nonresidents whose federal AGI exceeds the Wisconsin spouse's Wisconsin AGI. Their sliding scale standard deduction is not sufficient to eliminate their Wisconsin state tax, and the Wisconsin spouse qualifies for the working families credit due to a low Wisconsin AGI. A DOR review of the affected claimants in the tax year 2019 simulation reveals that their average federal AGI equaled over $90,000, while their Wisconsin AGI averaged less than $9,300. The DOR simulation is based on actual tax returns filed for tax year 2017.

17. Converting tax year estimates to fiscal year estimates often results in one-time fiscal effects due to timing differences between tax years and fiscal years. Frequently, the one-time effects materialize as larger amounts in the initial fiscal year than in subsequent fiscal years. While the preceding discussion points report amounts on a tax year basis, the following alternatives are reported on a fiscal year basis.

18. The one-time effects for the family and individual reinvestment credit and the sliding scale standard deduction are both about $12.5 million, but the one-time effect of the across-the-board tax rate reduction is estimated at $63.6 million. Under the first two alternatives, the tax relief is targeted to low and middle income taxpayers who rely on wage withholding for the majority of their tax payments. However, a small number of taxpayers would either adjust their withholding or lower their estimated payments, causing part of their tax year 2020 reduction to be reflected in 2019-20 tax collections. The across-the-board tax rate reduction would affect a larger number of taxpayers, including taxpayers who have nonwage income. Those taxpayers make estimated quarterly tax payments, which would likely be adjusted to reflect the lower tax rates and result in the one-time fiscal effect. By lowering the tax rate reduction of the across-the-board tax rate decrease (Alternative 3), the fiscal effect could be set at a level comparable to the other two alternatives. However, taxpayers would experience a smaller overall tax reduction on a tax year basis.

19. None of the alternatives assume the tax reduction would be accompanied by a withholding table change. As a result, each alternative would be expected to increase the state's deficit

under generally accepted accounting principles (GAAP). A withholding table change could be required as a component of each alternative, but a higher fiscal effect would result.

ALTERNATIVES

1. Approve the Governor's proposal to create a nonrefundable individual income tax credit beginning in tax year 2019 called the family and individual reinvestment credit, with the credit equal to a minimum dollar amount or a percentage of the claimant's net tax liability, subject to phaseout based on the claimant's Wisconsin AGI and filing status. Modify the credit's minimum dollar amounts to be set at $100, instead of $50, for married joint filers, and $50, instead of $25, for married separate filers and substitute "married couple's adjusted gross income" for references in the bill to "the sum of the claimant's adjusted gross income and his or her spouse's adjusted gross income" with regard to married joint filers. Decrease individual income tax collections by an estimated $421,550,000 in 2019-20 and $412,050,000 in 2020-21 and in each year thereafter.

ALT 1	**Change to**	
	Base	**Bill**
GPR-Tax	- $833,600,000	$0

2. Delete the Governor's proposed credit, and instead, expand the sliding scale standard deduction beginning in tax year 2019. For single filers, set the maximum deduction at $13,360, the initial income phaseout level at $19,260, and the phaseout percentage at 13.2%. For head-of-household filers, set the maximum deduction at $17,260, the initial income phaseout level at $19,260, and the phaseout percentage at 22.264%, but specify that the deduction be calculated as if the claimant is a single filer when the claimant's Wisconsin AGI results in a deduction equal to the standard deduction for a single individual with the same AGI. For married joint filers, set the maximum deduction at $24,730, the initial income phaseout level at $27,800, and the phaseout percentage at 17.8%. For married separate filers, set the maximum deduction at $11,750, the initial income phaseout level $13,200, and the phaseout percentage at 17.8%. Extend these changes to individuals who may be claimed as a dependent, based on the individual's filing status. Decrease individual income tax collections by an estimated $417,000,000 in 2019-20 and $416,100,000 in 2020-21.

ALT 2	**Change to**	
	Base	**Bill**
GPR-Tax-	- $833,100,000	$500,000

3. Delete the Governor's proposal, and instead, reduce each of the four marginal tax rates under current law by 4%. Set the rate for the first bracket at 3.84%, for the second tax bracket at 5.61%, for the third tax bracket at 6.03%, and for the fourth tax bracket at 7.35%, beginning in tax year 2019. Decrease individual income tax collections by an estimated $462,500,000 in 2019-20 and $427,700,000 in 2020-21.

ALT 3	Change to Base	Bill
GPR-Tax	- $890,200,000	- $56,600,000

4. Approve the Governor's recommendation to sunset the nonrefundable working families tax credit, effective in tax year 2019. Increase individual income tax collections by an estimated $50,000 annually. This alternative can be adopted in addition to another alternative.

ALT 4	Change to Base	Bill
GPR-Tax	$100,000	$0

5. Take no action.

ALT 5	Change to Base	Bill
GPR-Tax	$0	$833,500,000

Prepared by: Rick Olin
Attachments

ATTACHMENT 1

Estimated Distribution of Taxpayers Claiming the Family and Individual Reinvestment Credit, Tax Year 2019

All Filers

Wisconsin Adjusted Gross Income	Taxpayers Receiving the Proposed Tax Credit: Count	% of Count	Amount of Tax Credit	% of Credit	Average Credit	Count of All Returns	% of All Returns in AGI Class
Under $5,000	15,150	0.8%	-$731,960	0.2%	-$48	472,390	3.2%
5,000 to 10,000	8,820	0.5	-591,760	0.1	-67	220,080	4.0
10,000 to 15,000	61,800	3.3	-3,767,230	0.9	-61	188,590	32.8
15,000 to 20,000	102,590	5.4	-8,899,850	2.2	-87	173,680	59.1
20,000 to 25,000	132,710	7.0	-12,698,250	3.1	-96	171,290	77.5
25,000 to 30,000	143,440	7.6	-13,846,390	3.4	-97	169,640	84.6
30,000 to 40,000	296,620	15.7	-33,144,120	8.1	-112	316,190	93.8
40,000 to 50,000	245,290	12.9	-38,449,560	9.4	-157	255,800	95.9
50,000 to 60,000	189,570	10.0	-39,936,920	9.8	-211	197,050	96.2
60,000 to 70,000	151,010	8.0	-40,170,920	9.8	-266	156,370	96.6
70,000 to 80,000	121,710	6.4	-39,193,210	9.6	-322	126,060	96.5
80,000 to 90,000	104,040	5.5	-36,692,930	9.0	-353	107,750	96.6
90,000 to 100,000	89,350	4.7	-32,287,000	7.9	-361	92,090	97.0
100,000 to 125,000	141,530	7.5	-75,965,550	18.6	-537	172,630	82.0
125,000 to 150,000	90,620	4.8	-32,748,970	8.0	-361	104,860	86.4
150,000 to 200,000	0	0.0	0	0.0	N.A.	100,950	0.0
200,000 to 250,000	0	0.0	0	0.0	N.A.	41,960	0.0
250,000 to 300,000	0	0.0	0	0.0	N.A.	21,080	0.0
300,000 to 500,000	0	0.0	0	0.0	N.A.	30,220	0.0
500,000 to 1,000,000	0	0.0	0	0.0	N.A.	15,660	0.0
1,000,000 and over	0	0.0	0	0.0	N.A.	7,640	0.0
Total	1,894,250	100.0%	-$409,124,620	100.0%	-$216	3,141,990	60.3%

Married Joint Filers

Wisconsin Adjusted Gross Income	Taxpayers Receiving the Proposed Tax Credit: Count	% of Count	Amount of Tax Credit	% of Credit	Average Credit	Count of All Returns	% of All Returns in AGI Class
Under $5,000	80	< 0.1%	-$4,190	< 0.1%	-$52	84,230	0.1%
5,000 to 10,000	70	< 0.1	-6,260	< 0.1	-89	30,080	0.2
10,000 to 15,000	80	< 0.1	-7,290	< 0.1	-91	30,520	0.3
15,000 to 20,000	120	< 0.1	-10,730	< 0.1	-89	28,470	0.4
20,000 to 25,000	2,670	0.4	-153,800	0.1	-58	30,470	8.8
25,000 to 30,000	15,810	2.1	-1,108,260	0.5	-70	35,870	44.1
30,000 to 40,000	67,820	8.9	-6,629,370	2.9	-98	78,980	85.9
40,000 to 50,000	73,230	9.7	-7,978,220	3.4	-109	78,760	93.0
50,000 to 60,000	73,900	9.7	-11,852,330	5.1	-160	78,200	94.5
60,000 to 70,000	75,530	10.0	-17,113,520	7.4	-227	78,870	95.8
70,000 to 80,000	74,690	9.8	-21,958,030	9.5	-294	77,320	96.6
80,000 to 90,000	73,360	9.7	-26,541,690	11.5	-362	75,530	97.1
90,000 to 100,000	69,040	9.1	-29,636,650	12.8	-429	70,670	97.7
100,000 to 125,000	141,530	18.7	-75,965,550	32.8	-537	144,390	98.0
125,000 to 150,000	90,620	11.9	-32,748,970	14.1	-361	92,490	98.0
150,000 to 200,000	0	0.0	0	0.0	N.A.	90,420	0.0
200,000 to 250,000	0	0.0	0	0.0	N.A.	37,480	0.0
250,000 to 300,000	0	0.0	0	0.0	N.A.	18,670	0.0
300,000 to 500,000	0	0.0	0	0.0	N.A.	26,490	0.0
500,000 to 1,000,000	0	0.0	0	0.0	N.A.	13,610	0.0
1,000,000 and over	0	0.0	0	0.0	N.A.	6,360	0.0
Total	758,550	100.0%	-$231,714,860	100.0%	-$305	1,207,880	62.8%

Other Filers

Wisconsin Adjusted Gross Income	Taxpayers Receiving the Proposed Tax Credit: Count	% of Count	Amount of Tax Credit	% of Credit	Average Credit	Count of All Returns	% of All Returns in AGI Class
Under $5,000	15,070	1.3%	-$727,770	0.4%	-$48	388,160	3.9%
5,000 to 10,000	8,750	0.8	-585,500	0.3	-67	190,000	4.6
10,000 to 15,000	61,720	5.4	-3,759,940	2.1	-61	158,070	39.0
15,000 to 20,000	102,470	9.0	-8,889,120	5.0	-87	145,210	70.6
20,000 to 25,000	130,040	11.5	-12,544,450	7.1	-96	140,820	92.3
25,000 to 30,000	127,630	11.2	-12,738,130	7.2	-100	133,770	95.4
30,000 to 40,000	228,800	20.1	-26,514,750	14.9	-116	237,210	96.5
40,000 to 50,000	172,060	15.2	-30,471,340	17.2	-177	177,040	97.2
50,000 to 60,000	115,670	10.2	-28,084,590	15.8	-243	118,850	97.3
60,000 to 70,000	75,480	6.6	-23,057,400	13.0	-305	77,500	97.4
70,000 to 80,000	47,020	4.1	-17,235,180	9.7	-367	48,750	96.5
80,000 to 90,000	30,680	2.7	-10,151,240	5.7	-331	32,220	95.2
90,000 to 100,000	20,310	1.8	-2,650,350	1.5	-130	21,410	94.9
100,000 to 125,000	0	0.0	0	0.0	N.A.	28,240	0.0
125,000 to 150,000	0	0.0	0	0.0	N.A.	12,380	0.0
150,000 to 200,000	0	0.0	0	0.0	N.A.	10,530	0.0
200,000 to 250,000	0	0.0	0	0.0	N.A.	4,480	0.0
250,000 to 300,000	0	0.0	0	0.0	N.A.	2,400	0.0
300,000 to 500,000	0	0.0	0	0.0	N.A.	3,740	0.0
500,000 to 1,000,000	0	0.0	0	0.0	N.A.	2,050	0.0
1,000,000 and over	0	0.0	0	0.0	N.A.	1,280	0.0
Total	1,135,700	100.0%	-$177,409,760	100.0%	-$156	1,934,110	58.7%

- An estimated 1,894,250, or 60.3%, of all filers in 2019 would receive the family and individual reinvestment tax credit. A slightly higher percentage of married joint filers (62.8%) would receive the credit, than other filers (58.7%).

- The credit is estimated to decrease individual income tax collections by $409.1 million in tax year 2019. Married joint filers would receive an estimated 56.6% of the decrease but represent only 40.0% of the total claimants. Other taxpayers would receive 43.4% of the estimated decrease but represent 60.0% of the estimated number of claimants.

- The average tax credit is estimated at $216 in tax year 2019. The average credit is estimated to be higher for married joint claimants ($305) than for other claimants ($156).

- Generally, the average credit by Wisconsin AGI category would increase until reaching the phaseout range of $125,000 to $150,000 for married joint filers and $80,000 to $100,000 for single filers. Married separate filers are included with single filers and have a lower income phaseout range, but represent a small percentage of total filers (about 1%).

- Over 90% of all filers with a Wisconsin AGI between $30,000 and $100,000 would receive a tax credit. Tax filers not receiving the credit would include those with no tax liability, filers whose income is above the AGI phase out threshold, part-year residents, nonresidents, and individuals claimed as a single dependent on the return of another taxpayer claiming the credit.

Based on a simulation of tax year 2019 by the Wisconsin Department of Revenue.

ATTACHMENT 2

Estimated Distribution of Taxpayers Under Alternative to Expand the Sliding Scale Standard Deduction, Tax Year 2019

All Filers

Wisconsin Adjusted Gross Income	Taxpayers Receiving a Tax Decrease: Count	% of Count	Amount of Tax Decrease	% of Decrease	Average Decrease	Count of All Returns	% of All Returns in AGI Class
Under $5,000	16,950	0.8%	-$199,770	< 0.1%	-$12	472,390	3.6%
5,000 to 10,000	14,160	0.7	-457,490	0.1	-32	220,080	6.4
10,000 to 15,000	69,260	3.4	-3,250,850	0.8	-47	188,590	36.7
15,000 to 20,000	110,770	5.5	-9,483,060	2.3	-86	173,680	63.8
20,000 to 25,000	139,970	6.9	-16,898,270	4.2	-121	171,290	81.7
25,000 to 30,000	149,640	7.4	-24,248,670	6.0	-162	169,640	88.2
30,000 to 40,000	306,500	15.1	-58,606,910	14.5	-191	316,190	96.9
40,000 to 50,000	251,990	12.4	-57,216,870	14.1	-227	255,800	98.5
50,000 to 60,000	194,490	9.6	-47,179,070	11.7	-243	197,050	98.7
60,000 to 70,000	154,320	7.6	-39,931,070	9.9	-259	156,370	98.7
70,000 to 80,000	124,300	6.1	-34,628,810	8.6	-279	126,070	98.6
80,000 to 90,000	105,520	5.2	-31,421,610	7.8	-298	107,750	97.9
90,000 to 100,000	90,390	4.5	-27,032,010	6.7	-299	92,080	98.2
100,000 to 125,000	165,960	8.2	-41,444,890	10.2	-250	172,630	96.1
125,000 to 150,000	91,180	4.5	-11,421,720	2.8	-125	104,870	86.9
150,000 to 200,000	38,890	1.9	-1,028,280	0.3	-26	100,950	38.5
200,000 to 250,000	20	< 0.1	-2,490	< 0.1	-125	41,960	0.0
250,000 to 300,000	0	0.0	0	0.0	N.A.	21,070	0.0
300,000 to 500,000	0	0.0	0	0.0	N.A.	30,230	0.0
500,000 to 1,000,000	0	0.0	0	0.0	N.A.	15,660	0.0
1,000,000 and over	0	0.0	0	0.0	N.A.	7,640	0.0
Total	2,024,310	100.0%	-$404,451,840	100.0%	-$200	3,141,990	64.4%

Married Joint Filers

Wisconsin Adjusted Gross Income	Taxpayers Receiving a Tax Decrease: Count	% of Count	Amount of Tax Decrease	% of Decrease	Average Decrease	Count of All Returns	% of All Returns in AGI Class
Under $5,000	6,230	0.7%	-$73,310	< 0.1%	-$12	84,230	7.4%
5,000 to 10,000	4,050	0.5	-137,050	0.1	-34	30,080	13.5
10,000 to 15,000	3,170	0.4	-185,970	0.1	-59	30,520	10.4
15,000 to 20,000	2,720	0.3	-229,150	0.1	-84	28,470	9.6
20,000 to 25,000	5,020	0.6	-431,690	0.2	-86	30,470	16.5
25,000 to 30,000	17,910	2.1	-1,936,410	0.8	-108	35,870	49.9
30,000 to 40,000	72,070	8.6	-16,097,450	6.7	-223	78,980	91.3
40,000 to 50,000	76,680	9.2	-25,535,910	10.7	-333	78,760	97.4
50,000 to 60,000	76,740	9.2	-28,147,440	11.8	-367	78,200	98.1
60,000 to 70,000	77,660	9.3	-29,523,120	12.3	-380	78,870	98.5
70,000 to 80,000	76,240	9.1	-29,484,680	12.3	-387	77,320	98.6
80,000 to 90,000	74,540	8.9	-28,708,790	12.0	-385	75,530	98.7
90,000 to 100,000	69,910	8.4	-25,607,020	10.7	-366	70,670	98.9
100,000 to 125,000	142,760	17.1	-40,537,680	17.0	-284	144,390	98.9
125,000 to 150,000	91,180	10.9	-11,421,720	4.8	-125	92,490	98.6
150,000 to 200,000	38,890	4.7	-1,028,280	0.4	-26	90,420	43.0
200,000 to 250,000	20	< 0.1	-2,490	< 0.1	-125	37,480	0.1
250,000 to 300,000	0	0.0	0	0.0	N.A.	18,670	0.0
300,000 to 500,000	0	0.0	0	0.0	N.A.	26,490	0.0
500,000 to 1,000,000	0	0.0	0	0.0	N.A.	13,610	0.0
1,000,000 and over	0	0.0	0	0.0	N.A.	6,360	0.0
Total	835,790	100.0%	-$239,088,160	100.0%	-$286	1,207,880	69.2%

Other Filers

Wisconsin Adjusted Gross Income	Taxpayers Receiving a Tax Decrease: Count	% of Count	Amount of Tax Decrease	% of Decrease	Average Decrease	Count of All Returns	% of All Returns in AGI Class
Under $5,000	10,720	0.9%	-$126,460	0.1%	-$12	388,160	2.8%
5,000 to 10,000	10,110	0.9	-320,440	0.2	-32	190,000	5.3
10,000 to 15,000	66,090	5.6	-3,064,880	1.9	-46	158,070	41.8
15,000 to 20,000	108,050	9.1	-9,253,910	5.6	-86	145,210	74.4
20,000 to 25,000	134,950	11.4	-16,466,580	10.0	-122	140,820	95.8
25,000 to 30,000	131,730	11.1	-22,312,260	13.5	-169	133,770	98.5
30,000 to 40,000	234,430	19.7	-42,509,460	25.7	-181	237,210	98.8
40,000 to 50,000	175,310	14.8	-31,680,960	19.2	-181	177,040	99.0
50,000 to 60,000	117,750	9.9	-19,031,630	11.5	-162	118,850	99.1
60,000 to 70,000	76,660	6.5	-10,407,950	6.3	-136	77,500	98.9
70,000 to 80,000	48,060	4.0	-5,144,130	3.1	-107	48,750	98.6
80,000 to 90,000	30,980	2.6	-2,712,820	1.6	-88	32,220	96.2
90,000 to 100,000	20,480	1.7	-1,424,990	0.9	-70	21,410	95.7
100,000 to 125,000	23,200	2.0	-907,210	0.5	-39	28,240	82.2
125,000 to 150,000	0	0.0	0	0.0	N.A.	12,380	0.0
150,000 to 200,000	0	0.0	0	0.0	N.A.	10,530	0.0
200,000 to 250,000	0	0.0	0	0.0	N.A.	4,480	0.0
250,000 to 300,000	0	0.0	0	0.0	N.A.	2,400	0.0
300,000 to 500,000	0	0.0	0	0.0	N.A.	3,740	0.0
500,000 to 1,000,000	0	0.0	0	0.0	N.A.	2,050	0.0
1,000,000 and over	0	0.0	0	0.0	N.A.	1,280	0.0
Total	1,188,520	100.0%	-$165,363,680	100.0%	-$139	1,934,110	61.5%

- An estimated 2,024,310, or 64.4%, of all filers in 2019 would receive a tax decrease under an expanded sliding scale standard deduction. A higher percentage of married filers (69.2%) would receive a tax decrease, than other filers (61.5%).

- An expanded sliding scale standard deduction is estimated to decrease individual income tax collections by $404.5 million in tax year 2019. Married joint filers would receive an estimated 59.1% of the decrease but represent only 41.3% of all taxpayers with a tax decrease. Other taxpayers would receive 40.9% of the estimated decrease but represent 58.7% of the taxpayers with a tax decrease.

- The average tax decrease is estimated at $200 in tax year 2019. The average decrease is estimated to be higher for married joint filers ($286) than for other filers ($139).

- The average tax decrease by Wisconsin AGI category would increase until peaking at $70,000 to $90,000 for married joint filers and $30,000 to $60,000 for other filer types. These income ranges are slightly below the midpoint of the income phaseout ranges for each filer type.

- Over 90% of all filers with a Wisconsin AGI between $30,000 and $125,000 would receive a tax decrease. Tax filers not receiving a decrease would include those with no tax liability and filers whose income is above the income phaseout thresholds.

Based on a simulation of tax year 2019 by the Wisconsin Department of Revenue.

ATTACHMENT 3

Estimated Distribution of Taxpayers Under Across-the-Board Tax Rate Reduction Alternative, Tax Year 2019

All Filers

	Taxpayers Receiving a Tax Decrease						
Wisconsin Adjusted Gross Income	Count	% of Count	Amount of Tax Decrease	% of Decrease	Average Decrease	Count of All Returns	% of All Returns in AGI Class
Under $5,000	37,150	1.6%	-$149,920	< 0.1%	-$4	472,390	7.9%
5,000 to 10,000	26,420	1.2	-263,860	0.1	-10	220,080	12.0
10,000 to 15,000	70,980	3.1	-497,700	0.1	-7	188,590	37.6
15,000 to 20,000	114,340	5.0	-1,348,890	0.3	-12	173,680	65.8
20,000 to 25,000	142,600	6.3	-2,768,090	0.7	-19	171,290	83.3
25,000 to 30,000	151,720	6.7	-4,445,630	1.1	-29	169,640	89.4
30,000 to 40,000	309,670	13.6	-13,998,090	3.5	-45	316,190	97.9
40,000 to 50,000	254,330	11.2	-17,820,360	4.5	-70	255,800	99.4
50,000 to 60,000	196,290	8.6	-18,684,340	4.7	-95	197,050	99.6
60,000 to 70,000	155,910	6.8	-18,725,590	4.7	-120	156,370	99.7
70,000 to 80,000	125,760	5.5	-18,301,940	4.6	-146	126,070	99.8
80,000 to 90,000	107,540	4.7	-18,475,290	4.6	-172	107,750	99.8
90,000 to 100,000	91,970	4.0	-18,264,850	4.6	-199	92,080	99.9
100,000 to 125,000	172,420	7.6	-42,144,120	10.6	-244	172,630	99.9
125,000 to 150,000	104,770	4.6	-32,252,650	8.1	-308	104,870	99.9
150,000 to 200,000	100,810	4.4	-39,389,190	9.9	-391	100,950	99.9
200,000 to 250,000	41,840	1.8	-21,355,220	5.4	-510	41,960	99.7
250,000 to 300,000	21,000	0.9	-13,271,690	3.3	-632	21,070	99.7
300,000 to 500,000	29,830	1.3	-27,132,660	6.8	-910	30,230	98.7
500,000 to 1,000,000	15,520	0.7	-27,467,980	6.9	-1,770	15,660	99.1
1,000,000 and over	7,470	0.3	-62,148,010	15.6	-8,320	7,640	97.8
Total	2,278,340	100.0%	-$398,906,070	100.0%	-$175	3,141,990	72.5%

Married Joint Filers

	Taxpayers Receiving a Tax Decrease						
Wisconsin Adjusted Gross Income	Count	% of Count	Amount of Tax Decrease	% of Decrease	Average Decrease	Count of All Returns	% of All Returns in AGI Class
Under $5,000	12,180	1.2%	-$63,650	< 0.1%	-$5	84,230	14.5%
5,000 to 10,000	6,910	0.7	-102,220	< 0.1	-15	30,080	23.0
10,000 to 15,000	5,040	0.5	-123,440	< 0.1	-24	30,520	16.5
15,000 to 20,000	4,070	0.4	-137,190	< 0.1	-34	28,470	14.3
20,000 to 25,000	6,020	0.6	-168,610	0.1	-28	30,470	19.8
25,000 to 30,000	18,890	1.9	-358,720	0.1	-19	35,870	52.7
30,000 to 40,000	73,670	7.3	-2,152,810	0.8	-29	78,980	93.3
40,000 to 50,000	77,960	7.7	-4,220,570	1.5	-54	78,760	99.0
50,000 to 60,000	77,760	7.7	-6,363,240	2.2	-82	78,200	99.4
60,000 to 70,000	78,590	7.8	-8,643,590	3.0	-110	78,870	99.6
70,000 to 80,000	77,100	7.6	-10,665,600	3.8	-138	77,320	99.7
80,000 to 90,000	75,380	7.4	-12,571,140	4.4	-167	75,530	99.8
90,000 to 100,000	70,590	7.0	-13,776,390	4.9	-195	70,670	99.9
100,000 to 125,000	144,250	14.2	-35,083,050	12.4	-243	144,390	99.9
125,000 to 150,000	92,420	9.1	-28,410,400	10.0	-307	92,490	99.9
150,000 to 200,000	90,330	8.9	-35,248,870	12.4	-390	90,420	99.9
200,000 to 250,000	37,420	3.7	-19,063,590	6.7	-509	37,480	99.8
250,000 to 300,000	18,640	1.8	-11,740,610	4.1	-630	18,670	99.8
300,000 to 500,000	26,170	2.6	-23,643,590	8.3	-903	26,490	98.8
500,000 to 1,000,000	13,520	1.3	-23,875,940	8.4	-1,766	13,610	99.3
1,000,000 and over	6,250	0.6	-46,997,660	16.6	-7,520	6,360	98.3
Total	1,013,160	100.0%	-$283,410,880	100.0%	-$280	1,207,880	83.9%

Other Filers

	Taxpayers Receiving a Tax Decrease						
Wisconsin Adjusted Gross Income	Count	% of Count	Amount of Tax Decrease	% of Decrease	Average Decrease	Count of All Returns	% of All Returns in AGI Class
Under $5,000	24,970	2.0%	-$86,270	0.1%	-$3	388,160	6.4%
5,000 to 10,000	19,510	1.5	-161,640	0.1	-8	190,000	10.3
10,000 to 15,000	65,940	5.2	-374,260	0.3	-6	158,070	41.7
15,000 to 20,000	110,270	8.7	-1,211,700	1.0	-11	145,210	75.9
20,000 to 25,000	136,580	10.8	-2,599,480	2.3	-19	140,820	97.0
25,000 to 30,000	132,830	10.5	-4,086,910	3.5	-31	133,770	99.3
30,000 to 40,000	236,000	18.7	-11,845,280	10.3	-50	237,210	99.5
40,000 to 50,000	176,370	13.9	-13,599,790	11.8	-77	177,040	99.6
50,000 to 60,000	118,530	9.4	-12,321,100	10.7	-104	118,850	99.7
60,000 to 70,000	77,320	6.1	-10,082,000	8.7	-130	77,500	99.8
70,000 to 80,000	48,660	3.8	-7,636,340	6.6	-157	48,750	99.8
80,000 to 90,000	32,160	2.5	-5,904,150	5.1	-184	32,220	99.8
90,000 to 100,000	21,380	1.7	-4,488,460	3.9	-210	21,410	99.9
100,000 to 125,000	28,170	2.2	-7,061,070	6.1	-251	28,240	99.8
125,000 to 150,000	12,350	1.0	-3,842,250	3.3	-311	12,380	99.8
150,000 to 200,000	10,480	0.8	-4,140,320	3.6	-395	10,530	99.5
200,000 to 250,000	4,420	0.3	-2,291,630	2.0	-518	4,480	98.7
250,000 to 300,000	2,360	0.2	-1,531,080	1.3	-649	2,400	98.3
300,000 to 500,000	3,660	0.3	-3,489,070	3.0	-953	3,740	97.9
500,000 to 1,000,000	2,000	0.2	-3,592,040	3.1	-1,796	2,050	97.6
1,000,000 and over	1,220	0.1	-15,150,350	13.1	-12,418	1,280	95.3
Total	1,265,180	100.0%	-$115,495,190	100.0%	-$91	1,934,110	65.4%

- An estimated 2,278,340, or 72.5%, of all filers in 2019 would receive a tax decrease under an across-the-board tax rate reduction. A higher percentage of married filers (83.9%) would receive a tax decrease, than other filers (65.4%).

- An across-the-board tax rate reduction is estimated to decrease individual income tax collections by $398.9 million in tax year 2019. Married joint filers would receive an estimated 71.0% of the decrease but represent only 44.5% of all taxpayers with a tax decrease. Other taxpayers would receive 29.0% of the estimated decrease but represent 55.5% of the taxpayers with a tax decrease.

- The average tax decrease is estimated at $175 in tax year 2019. The average decrease is estimated to be higher for married joint filers ($280) than for other filers ($91).

- The average tax change would increase with Wisconsin AGI. The relationship between share of tax decrease and share of net taxes paid is proportional. Taxpayers with Wisconsin below $100,000 would receive 33.5% of the tax decrease, and their share of net tax equals 33.4%. Taxpayers with Wisconsin AGI above $100,000 would receive 66.5% of the tax decrease, and their share of net taxes equals 66.6%.

- Over 95% of all filers with a Wisconsin AGI above $30,000 would receive a tax decrease. Tax filers not receiving a decrease would include those with no tax liability.

Based on a simulation of tax year 2019 by the Wisconsin Department of Revenue.

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June, 2019 Joint Committee on Finance Paper #316

Internal Revenue Code Update
(General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 136, #4]

CURRENT LAW

State individual income tax and corporate income/franchise tax provisions are generally referenced to definitions under federal law. With limited exceptions, changes to federal law take effect for state purposes only after action by the Legislature. Generally, the Legislature reviews the previous year's federal law changes each year to update state references to the Internal Revenue Code (IRC). Under current law, state tax references generally refer to IRC provisions enacted as of December 31, 2017.

GOVERNOR

Update references to the IRC under the individual and corporate income/franchise taxes. For tax years beginning after December 31, 2013, and before January 1, 2017, create provisions adopting selected IRC provisions in P.L. 115-141, the Consolidated Appropriations Act of 2018, which made technical corrections to the Protecting Americans from Tax Hikes Act of 2015 (P.L. 114-113) and the Surface Transportation and Veterans Health Care Choice Improvement Act of 2015 (P.L. 114-41). In addition, adopt P.L. 115-141 provisions making technical corrections to the American Jobs Creation Act of 2004 (P.L. 108-357) for purposes of the IRC definition in the 2013 Wisconsin Statutes for tax years beginning after December 31, 2003, and before January 1, 2005. Limit the current law definition of the IRC for tax years beginning after December 31, 2017 to apply only to tax years beginning before January 1, 2019, but specify that selected provisions of the Disaster Tax Relief and Airport Airway Extension Act of 2017 (P.L. 115-63) and the Tax Cuts and Jobs Act of 2017 (P.L. 115-97) first apply for Wisconsin purposes for tax years beginning after December 31, 2017, rather than at the same time as for federal purposes. For tax years beginning after December 31, 2018, create provisions adopting IRC provisions in effect as of

December 31, 2018, with exceptions. Specify that the provisions of federal public laws that directly or indirectly affect the IRC apply for state tax purposes at the same time as for federal tax purposes, with exceptions, and specify that the definition of the IRC does not include amendments to the IRC enacted after December 31, 2018. Repeal obsolete provisions pertaining to tax years beginning after December 31, 2004, and before January 1, 2006. The Department of Administration (DOA) has submitted an errata seeking a technical modification to the bill to achieve this affect.

Increase individual income and corporate income/franchise taxes by an estimated $187,850,000 in 2019-20, $174,450,000 in 2020-21, $250,675,000 in 2021-22, and $224,625,000 in 2022-23. Most of the fiscal effect is attributable to provisions in the Tax Cuts and Jobs Act of 2017, which results in tax increases estimated at $189,650,000 in 2019-20, $175,350,000 in 2020-21, $251,575,000 in 2021-22, and $225,525,000 in 2022-23, due to seven provisions not previously adopted in 2017 Wisconsin Act 231: (a) loss limitation for taxpayers other than corporations; (b) amortization of research and experimental expenditures; (c) accounting rules for accrual method taxpayers; (d) limitation on the deduction for business interest; (e) limitation on the deduction for entertainment, amusement, and recreation expenses; (f) limitation on the deduction of Federal Deposit Insurance Corporation premiums; and (g) modification of the limitation on the deduction for highly paid individuals. The remainder of the fiscal effect is attributable to provisions in the Bipartisan Budget Act of 2018 that would reduce general fund tax revenues by an estimated $1,800,000 in 2019-20 and $900,000 in 2020-21 and thereafter.

DISCUSSION POINTS

1. State references to federal law generally provide greater simplicity for taxpayers in preparing returns and reduce the administrative burden and cost for both taxpayers and the Department of Revenue (DOR) in assuring compliance with tax laws. The IRC references are used to determine which items of income are subject to taxation prior to specific state modifications. The state uses separate tax rates and brackets and separate provisions regarding standard deductions, personal exemptions, itemized deductions, and tax credits.

2. During the last legislative session, the Legislature adopted IRC provisions in effect as of December 31, 2017, although certain IRC provisions were excluded from the adoption. Since then, three federal laws have been enacted that affect the IRC. These include the Bipartisan Budget Act of 2018 (P.L. 115-123), the Consolidated Appropriations Act of 2018 (P.L. 115-141), and the John S. McCain National Defense Authorization Act for Fiscal Year 2019 (P.L. 115-232). Enacted in 2018, the three acts were federal spending measures pertaining to federal fiscal years 2018 and 2019. These acts also included an assortment of federal tax provisions.

3. The Department of Revenue reports that adopting the provisions in the John S. McCain National Defense Authorization Act would not affect state tax collections. The two other acts included technical provisions relating to preceding tax years. The Consolidated Appropriations Act made technical corrections to IRC provisions that had been enacted in 2015. Wisconsin had previously adopted the 2015 provisions, so the bill would adopt the technical corrections and extend the corrections to tax years 2014, 2015, and 2016. Two provisions that had expired were extended by the

Bipartisan Budget Act through tax year 2017, and the bill would adopt these provisions retroactively for tax year 2017. The preceding provisions are technical in nature and would not have a fiscal effect.

4. Since 2000, a number of federal tax provisions have been enacted and renewed on a temporary basis. Over 30 of these provisions expired at the end of 2016 and were not renewed during 2017. The Bipartisan Budget Act (BBA) extended these provisions for one to four years, with the extension retroactive to tax year 2017. Several of the provisions were adjustments to income, but these provisions expired at the end of one year (2017). Many of the other expiring provisions relate to federal tax credits, which are not tied to state tax provisions. Other provisions in the federal act relate to tax relief for hurricane and California wildfire victims or to federal excise taxes. For these reasons, federalizing most of the provisions in the BBA would not affect state tax collections.

5. Nonetheless, there are two provisions in the BBA that would result in a state fiscal effect if adopted by the state. Because some provisions would apply retroactively to tax year 2018, these provisions have a larger tax effect in 2019-20 than in 2020-21. These provisions are estimated to decrease income and franchise tax collections by an estimated $2,150,000 in 2019-20 and $1,500,000 in 2020-21:

Qualified Opportunity Zones. Federal law allows states to designate certain low-income census tracts as qualified opportunity zones, and taxpayers may exclude certain capital gains from their taxable income if the gain is reinvested in a qualified opportunity zone within 180 days. The BBA designates each low-income census tract in Puerto Rico as a qualified opportunity zone. Because a limited number of Wisconsin taxpayers are likely to make a qualifying investment, a minimal effect on state revenues is estimated, reducing individual income tax collections by $1,250,000 in 2019-20 and $900,000 in 2020-21 and annually thereafter.

Contract Employees Serving in a Combat Zone. The BBA allows contractors or employees of contractors supporting the U.S. Armed Forces in designated combat zones to exclude their foreign earned income for tax purposes even if the individual has an abode in the United States. Adopting this provision would reduce individual income tax collections by an estimated $900,000 in 2019-20 and $600,000 in 2020-21 and annually thereafter.

6. A third provision of the BBA directs the IRS to modify existing regulations related to hardship distributions from retirement plans by generally relaxing certain restrictions on taking a hardship distribution. Because contributions to retirement plans are generally made on a pre-tax basis, except for ROTHs, withdrawals are subject to tax. Wisconsin taxpayers making IRS-permitted hardship withdrawals from retirement plans are likely to do so regardless of whether Wisconsin adopts this provision. DOA indicates that this provision would increase individual income tax collections by an estimated $600,000 in 2019-20 and $600,000 in 2020-21 and annually thereafter. Because Wisconsin will receive these additional revenues even if the provision is not adopted, this paper does not assign a fiscal effect to this provision. Further, the revenues related to the provision have been incorporated into this office's May, 2019, revenue estimates.

7. A fourth provision under the BBA extends the energy efficient commercial building deduction for one year and would result in an estimated $400,000 decrease in corporate income/franchise tax collections in 2019-20. This provision is extended under Section 179 of the IRC.

Its adoption by the Legislature is unnecessary because Wisconsin automatically adopts Section 179 changes under an existing statutory provision [s. 71.98(4)]. If the Committee wants to adopt the technical provisions of the Bipartisan Budget Act but exclude the two preceding items (qualified opportunity zones and contract employees serving in a combat zone) from the IRC update due to their fiscal effect, the Committee could adopt Alternative 2.

8. Adopting the Consolidated Appropriations Act is not expected to result in a state fiscal effect because the Act's IRC changes consist of technical corrections to the federal Tax Cuts and Jobs Act of 2017 (P.L. 115-97). Wisconsin adopted many of the Tax Cuts and Jobs Act changes in 2018 when it enacted 2017 Wisconsin Act 231, which also adopted some provisions from the Disaster Tax Relief and Airport Airway Extension Act of 2017 (P.L. 115-63). However, Act 231 did not adopt certain provisions in the Tax Cuts and Jobs Act. The bill would adopt seven provisions from the Tax Cuts and Jobs Act (the Act) that were excluded from Act 231. Each of these provisions is described below.

9. Loss Limitation for Pass-Through Taxpayers. Under the individual income tax, taxpayers may deduct business losses from their regular income, subject to certain limitations. For example, passive losses and excess farm losses cannot be deducted in the year incurred, but can be carried forward. For tax years 2018 through 2025, the Act limits the amount of business losses by not allowing excess business losses to be deducted. The Act defines excess business loss as the taxpayer's aggregate deductions for business purposes that exceed the sum of the taxpayer's gross income or gain plus $500,000 for married joint filers or $250,000 for other types of filers. Excess business losses may be carried forward and claimed under net operating loss provisions, as amended by the Act. Also for tax years 2018 through 2025, the limitation relating to excess farm losses does not apply. Excess farm losses comprise losses occurring in the same year that certain farm subsidies are received, provided the farm is not a C corporation. For purposes of calculating adjusted gross income, the excess business loss limitation created by the Act applies after passive loss rules. Adopting this provision beginning in tax year 2019 would increase state individual income tax collections by an estimated $70,400,000 in 2019-20, $66,300,000 in 2020-21, $61,650,000 in 2021-22, and $47,700,000 in 2022-23.

10. Amortization of Research Expenses. Most business expenses associated with the development or creation of an asset that has a useful life beyond the current year must be capitalized and depreciated over the useful life of the asset. However, researchers can elect to immediately deduct reasonable research or experimentation expenditures associated with the development or creation of a business asset. Researchers also may elect to amortize such expenditures over a five-year or 10-year period, rather than capitalize such expenditures under uniform capitalization rules. The Act requires research and experimental expenditures to be capitalized and amortized ratably over a five-year period. Expenditures attributable to research conducted outside of the United States must be capitalized and amortized ratably over a period of 15 years. The election to immediately expense such costs was repealed. The Act also expands the definition of research or experimental expenditures to include expenditures for software development, as well as depreciation and depletion allowances for property other than land that is depreciated or depleted in connection with research or experimentation. This provision takes effect in taxable years beginning after December 31, 2021. Because this provision was enacted with a delayed effective date, state adoption of this provision would not affect state tax revenues in the 2019-21 biennium. However, adoption of this provision

would increase state tax revenues by an estimated $76,850,000 in 2021-22 and $83,175,000 in 2022-23.

11. Accounting Rules for Accrual Method Taxpayers. Gross income is generally taxable in the tax year in which the money, property, or service is received, with exceptions to permit deferral of gross income related to advance payments. The Act requires an accrual method taxpayer to recognize income no later than the taxable year in which such income is taken into account as revenue in an applicable financial statement, with an exception for taxpayers without an applicable or other specified financial statement. The Act codifies the current deferral method of accounting for advance payments for goods, services, and other specified items to allow accrual method taxpayers to elect to defer the inclusion of income associated with advance receipt if such income is also deferred for financial statement purposes. The Act also repeals special rules that apply to the accrual of interest for original issue discount debt instruments (other than mortgage servicing contracts) that have an applicable financial statement, and the change in accounting for such debt instruments must be taken into account ratably over six taxable years. State adoption of this provision beginning in tax year 2019 would increase tax revenues by an estimated $10,450,000 in 2019-20, $7,925,000 in 2020-21, $5,350,000 in 2021-22, and $2,775,000 in 2022-23.

12. Limitation on Deduction for Interest. Under state and federal law, interest paid or accrued by a business was generally deductible from taxable income prior to tax year 2018, with certain limitations. However, deductible interest on indebtedness allocable to property held for investment was generally limited to net investment income for the taxable year, provided interest exceeded 2% of AGI. Investment interest that could not be deducted could be carried forward to the following year. A deduction could be disallowed for disqualified interest paid involving related parties or to a taxable real estate investment trust subsidiary if the payor's debt-to-equity ratio exceeded 1.5 to 1.0 and the payor's net interest expense exceeded 50% of AGI.

In general, the deduction for business interest is limited under the Act to the sum of: (a) business interest income; (b) 30% of the taxpayer's adjusted taxable income (ATI); and (c) floor plan financing interest of the taxpayer for the taxable year. Business interest income means any interest paid or accrued on indebtedness allocable to a trade or business, but does not include investment interest or investment income. ATI means taxable income of the taxpayer computed without regard to any: (1) item of income, gain, deduction, or loss not properly allocable to the trade or business; (2) business interest or interest income; (3) net operating loss deduction; and (4) the 20% deduction for certain pass-through income. Wages are not included in ATI. For tax years 2018 through 2021, ATI is computed without regard to deductions allowable for depreciation, amortization, or depletion. Floor plan financing interest includes any interest on indebtedness used to finance any self-propelled vehicles (such as on the floor of a car dealership) and is not subject to the deduction limitation, but not on indebtedness used to finance construction machinery and equipment.

Any deduction disallowed as a result of the limit for business interest may be carried forward indefinitely for use in future years. The deduction limit for partnerships and S corporations is computed at the entity level, and special rules apply, generally to prevent double counting of the deduction limit at the entity-level and at the partner or shareholder level. The following entities are exempt from the deduction limit: (a) taxpayers with average gross receipts of less than $25 million over the prior three taxable years; (b) certain regulated public utilities; (c) most businesses engaged in real property development, construction, rental, leasing, or brokerage activities; and (d) farming businesses, as well as certain agricultural or horticultural cooperatives. A farming business that claims this exemption must use straight line depreciation for property that has a recovery period of ten years or more. Adopting this provision beginning in tax year 2019 at the state level would increase state tax revenues by an estimated $87,000,000 in 2019-20, $83,500,000 in 2020-21, $89,900,000 in 2021-22, and $78,225,000 in 2022-23.

13. Limitation on Employers Deduction for Entertainment, Amusement, and Recreation Expenses. Deductions are not allowed for expenses related to activities that are considered entertainment, amusement, or recreation, or expenses for a facility (like aircraft) used for such purpose. However, prior to 2018, taxpayers could deduct certain expenses equal to: (a) 50% of entertainment expenses that are directly related to a taxpayer's active trade or business; and (b) 50% of food and beverages provided to employees. The Act repeals the deduction allowed under "a." Under state and federal de minimis fringe benefit provisions prior to the Act, food and beverages provided to employees through an eating facility operated by the employer that is located on or near the employer's business premises and that meets certain requirements could be deducted by the employer. The Act limits the deduction to food and beverages provided for the convenience of the employer and reduces the deductible amount to 50% for amounts incurred and paid after December 31, 2017. However, for amounts paid or incurred after December 31, 2025, such expenses cannot be deducted. It is estimated that state adoption of these provisions would increase tax revenues by an estimated $10,050,000 in 2019-20, $8,225,000 in 2020-21, $8,350,000 in 2021-22, and $6,375,000 in 2022-23.

14. Limitation on FDIC Premium Deduction. Under the Act, beginning in tax year 2018, bank and financial institution payments of Federal Deposit Insurance Corporation (FDIC) premiums are no longer deductible if paid or incurred by a taxpayer with total consolidated assets of $50 billion or more. For taxpayers with such assets of less than $10 billion, FDIC premiums are 100% deductible. For taxpayers with such assets of between $10 billion and $50 billion, the applicable percentage of the deduction is prorated over that range (for example, if the taxpayer has $20 billion of such assets, 25% of FDIC premiums are taxable). State adoption of this provision beginning in tax year 2019 would increase tax revenues by an estimated $7,250,000 in 2019-20, $5,800,000 in 2020-21, $5,875,000 in 2021-22, and $4,575,000 in 2022-23.

15. Limitation on Deduction for Highly Paid Individuals. Salaries, wages, and other forms of remuneration to officers of a business are deductible. However, deductible compensation expenses in the case of a "publicly held corporation" are limited to no more than $1 million per year for each "covered employee." A covered employee generally means the principal executive officer and the three most highly compensated officers as of the last day of the tax year (four covered employees). Certain types of remuneration are not included when calculating the deduction limit. The Act generally expands applicability of the $1 million deduction limit by:

a. Expanding the definition of a publicly held corporation to include all domestic publicly traded corporations, including large private C corporations or S corporations that are not publicly traded;

b. Including remuneration paid on a commission basis and performance-based compensation;

c. Expanding the definition of a covered employee to also include the principal financial officer, in addition to the principal executive officer and the three most highly compensated officers (five covered employees);

d. Including any individual that holds the position of principal executive officer or principal financial officer at any time during the taxable year; and

e. Requiring that an individual who is a covered employee, beginning in tax year 2017, remains a covered employee subject to the $1 million deduction limit with respect to compensation otherwise deductible in subsequent years, including years in which the individual is no longer employed by the corporation and in years after the employee has died.

As a result, the number of covered employees under the Act may exceed five, and deferred compensation paid to a covered employee, or the beneficiary of a covered employee, is subject to the $1 million deduction limit. A transition rule applies that grandfathers written binding contracts in effect on November 2, 2017. However, a contract is considered a new contract if it is renewed or if there has been a material modification to its terms. State adoption of this provision beginning in tax year 2019 would increase tax revenues by an estimated $4,500,000 in 2019-20, $3,600,000 in 2020-21, $3,600,000 in 2021-22, and $2,700,000 in 2022-23.

16. The preceding provisions related to the Tax Cuts and Jobs Act would increase individual and corporate income/franchise tax collections by an estimated $189,650,000 in 2019-20, $175,350,000 in 2020-21, $251,575,000 in 2021-22, and $225,525,000 in 2022-23. If the Committee agrees with the 2017 Legislature's decision to exclude these provisions from state tax provisions, the Committee could remove them from the proposal, either selectively or en masse (Alternative 3). Excluding all seven items from the definition of the Internal Revenue Code would decrease state income and franchise tax collections by an estimated $365,000,000 in the biennium, relative to the bill. Relative to current law, removing the items from the bill would not affect state income and franchise tax collections.

17. The fiscal effects of the individual IRC provisions identified in the preceding descriptions sum to lower totals in both years than the amounts reported by DOA. As a result, adopting all of the provisions identified in this paper would increase state tax collections by an estimated $361,350,000 in the 2019-21 biennium, or $950,000 less than the $362,300,000 amount originally estimated.

18. On May 1, 2019, DOA submitted an errata seeking a technical modification to the IRC provisions. Under current law, the IRC definition excludes a federal provision requiring estimated tax payments for insurance companies. The bill's creation of the IRC definition for tax years beginning after December 31, 2018, would continue that exclusion. However, the IRC provision was repealed by the Tax Cuts and Jobs Act. The technical modification would delete the bill's references to the repealed IRC provision and would not have a fiscal effect.

ALTERNATIVES

1. Approve the Governor's recommendation to update state income and franchise tax references to the Internal Revenue Code, including the technical modification submitted by DOA. Reestimate increased general fund tax revenues of $187,500,000 in 2019-20 and $173,850,000 in 2020-21 under the bill.

ALT 1	Change to Base	Change to Bill
GPR-Tax	$361,350,000	-$950,000

2. Approve the Governor's recommendation to update state income and franchise tax references to the Internal Revenue Code, including the technical modification submitted by DOA, except exclude sections in the Bipartisan Budget Act of 2018 (P.L. 115-123) related to qualified opportunity zones (section 41115) and civilians serving in a combat zone (section 41116). The retirement plan provisions related to hardships (sections 41113 and 41114) would be adopted since those provisions have no fiscal effect. Relative to the bill, this alternative would increase state tax collections by an estimated $1,800,000 in 2019-20 and $900,000 in 2020-21. The Tax Cuts and Jobs Act changes described in this paper would be adopted, increasing income and franchise tax collections by an estimated $365,000,000 in the biennium, reflected as Change to Base.

ALT 2	Change to Base	Change to Bill
GPR-Tax	$365,000,000	$2,700,000

3. Approve the Governor's recommendation to update state income and franchise tax references to the Internal Revenue Code, including the technical modification submitted by DOA, except exclude the following sections in the Tax Cuts and Jobs Act of 2017 (P.L. 115-97). Relative to the bill, excluding all of the sections would decrease state tax collections by an estimated $190,000,000 in 2019-20 and $175,950,000 in 2020-21. The Bipartisan Budget Act changes described in this paper would be adopted, decreasing income and franchise tax collections by an estimated $3,650,000 in the biennium, reflected as Change to Base. Exclude the following sections of P.L. 115-97 from the definition of the Internal Revenue Code under the state income and franchise tax (GPR-Tax change to bill):

a. Section 11012, relating to loss limitation for pass-through taxpayers (-$136,700,000);

b. Section 13206, relating to amortization of research expenses ($0);

c. Section 13221, relating to accounting rules for accrual method taxpayers (-$18,375,000);

d. Section 13301, relating to limitation on the deduction for interest (-$170,500,000);

e. Section 13304 (a), (b), and (d), relating to limitation on the deduction for entertainment, amusement, and recreation expenses (-$18,275,000);

f. Section 13531, relating to limitation on FDIC premium deduction (-$13,050,000); and

g. Section 13601, relating to the limitation on the deduction for highly paid individuals (-$8,100,000).

ALT 3	**Change to**	
	Base	**Bill**
GPR-Tax	-$3,650,000	- $365,950,000

4. Take no action (the Change to Bill reflects reversing DOA's original fiscal effect).

ALT 4	**Change to**	
	Base	**Bill**
GPR-Tax	$0	- $362,300,000

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June, 2019 | Joint Committee on Finance | Paper #317

Earned Income Tax Credit -- Current Law Sum Sufficient Reestimate (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 137, #6]

CURRENT LAW

The earned income tax credit (EITC) is offered at both the federal and state levels as a means of providing assistance to lower-income workers. The state EITC is calculated as a percentage of the federal credit. The state, therefore, uses federal definitions and eligibility requirements for purposes of the EITC, except that the state does not provide a credit to individuals without children. Both the federal and state credits are refundable -- if the credit exceeds the amount of tax due, a check is issued for the difference.

The credit is calculated based on family size, filing status, and the amount of earned income (although the credit can also be affected by adjusted gross income). Individuals without earned income are not eligible for the credit. The income limits and maximum federal credit amounts are adjusted annually for changes in inflation.

The state EITC is funded with a combination of GPR and federal temporary assistance for needy families (TANF) funding transferred from the Department of Children and Families. The GPR portion is provided through a sum sufficient appropriation and covers the balance of the cost of the credit.

Base funding for the credit is $100,600,000 ($30,900,000 GPR and $69,700,000 TANF).

GOVERNOR

Decrease the estimated cost of the program by $1,600,000 in 2019-20 and $200,000 in 2020-21. The cost of the credit under current law is reestimated at $99,000,000 in 2019-20 and $100,400,000 in 2020-21.

MODIFICATION

Reestimate the total amount of credit payments at $95,700,000 in 2019-20 and $97,400,000 in 2020-21, decreases of $4,900,000 in 2019-20 and $3,200,000 in 2020-21, relative to the base level. Relative to the amounts in the bill, the reestimates reflect reductions of $3,300,000 in 2019-20 and $3,000,000 in 2020-21. These decreases equate to GPR expenditure reductions. Estimate the amount of the GPR appropriation at $26,000,000 in 2019-20 and $27,700,000 in 2020-21 to reflect this reestimate. The TANF funding for the credit would remain unchanged relative to base level funding at $69,700,000 annually.

Explanation: The modification reflects a reduction in the estimated total cost of the credit compared to the bill, based on more recent claims data for the current year. The total cost of the credit in 2018-19 is now estimated at $95,200,000, compared to the base level of $100,600,000 and the November reestimate of $98,700,000. On a year-to-year basis, the reestimates reflect estimated increases in total credit funding of 0.5% in 2019-20 and 1.8% in 2020-21.

	Change to	
	Base	**Bill**
GPR	- $8,100,000	- $6,300,000

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June, 2019 Joint Committee on Finance Paper #318

Homestead Tax Credit -- Current Law Reestimate (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 138, #7]

CURRENT LAW

The homestead tax credit is a refundable income tax credit based on a formula that takes into account a tax filer's household income and property tax or rent paid during a tax year. To qualify for the credit, a claimant must be at least 18 years or older, must own or rent his or her residence, and must have household income under the maximum income level of $24,680. Claimants do not need to have a tax liability or income in order to receive the credit, although claimants must have earned income unless the claimant, or the claimant's spouse, is at least 62 years of age or disabled. For purposes of calculating the credit, household income is adjusted downward by $500 for each dependent to account for family size.

For claimants with income of $8,060 or less, a credit is equal to 80% of property taxes or rent constituting property taxes up to a maximum of $1,460 in property taxes or rent. Rent constituting property taxes is 25% of rent if payment for heat is not included in rent and 20% of rent if payment for heat is included. The maximum credit is $1,168.

The credit is phased out for claimants with household income between $8,060 and $24,680, at which point the credit equals zero. For claimants with less than $1,460 in allowable rent or property taxes, the credit is reduced at lower income levels. The credit formula can be expressed as a mathematical equation for individuals with income between $8,060 and $24,680 as follows:

Homestead Credit = 80% x [Property Taxes - 8.785% x (Household Income - $8,060)]

In 2017-18, homestead tax credit claims totaled $83,465,017. Because the credit is refundable, it is reflected as a GPR expenditure.

GOVERNOR

Decrease funding by $6,000,000 in 2019-20 and $7,500,000 in 2020-21 for the sum sufficient appropriation to reflect anticipated costs of the current law credit in the biennium. With these adjustments, estimated total funding for the credit would decrease from an adjusted base level of $84,900,000 to $78,900,000 in 2019-20 and $77,400,000 in 2020-21. The homestead tax credit appropriation was reestimated by the Department of Administration at $80,600,000 for 2018-19 in November, 2018, which is lower than the adjusted base level.

MODIFICATION

From the Governor's proposed funding level, decrease funding by $7,700,000 in 2019-20 and $6,900,000 in 2020-21 to reflect reduced expenditures. Reestimate the sum sufficient appropriation for the credit under current law provisions at $71,200,000 in 2019-20 and $70,500,000 in 2020-21.

Explanation: The downward revision in the credit amounts is due to a lower base year (2018-19) reestimate. Since January, credit claims in each month have been more than 10% below the amounts claimed in the same month last year, and the year-to-date total is 14.4% below the corresponding total through April, 2018. In the last three years, more than 86% of the fiscal year total has been claimed by the end of April. Based on these factors, total credits for 2018-19 are now estimated at $72.0 million, 13.7% below the actual total for 2017-18. The eligibility modification included in 2017 Act 59 requiring claimants to have earned income, unless disabled or 62 or over, is believed to be partially responsible for the year-to-year reduction, as are a growing economy and the absence of indexing for the credit's formula factors. These latter factors result in total credits continuing to decrease in the coming biennium, but at reduced rates, estimated at 1.1% in 2019-20 and 1.0% in 2020-21.

	Change to	
	Base	**Bill**
GPR	-$28,100,000	-$14,600,000

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June, 2019 Joint Committee on Finance Paper #319

Individual Income Tax Rate Reduction Based on Sales Taxes from Out-of-State Retailers (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 139, #9]

CURRENT LAW

State law establishes four tax brackets and assigns a marginal tax rate to each bracket. The brackets vary by filing status, and each tax bracket spans a range of taxable income. Each marginal tax rate applies only to income that falls within the corresponding bracket, and a taxpayer's gross tax is the cumulative total tax from each applicable bracket. The tax brackets are indexed annually for changes in inflation, and for tax year 2019, the following rates and brackets apply:

	Income Brackets by Filing Status		
Tax Rate	Single and Head-of-Household	Married Joint	Married Separate
4.00%	$0 to $11,760	$0 to $15,680	$0 to $7,840
5.84	11,760 to 23,520	15,680 to 31,360	7,840 to 15,680
6.27	23,520 to 258,950	31,360 to 345,270	15,680 to 172,630
7.65	258,950 or over	345,270 or over	172,630 or over

For tax year 2019, the preceding rates will be proportionally reduced, so that the lower amount of individual income tax collections will be offset by the additional amount of state sales and use taxes realized from imposing the state sales and use tax on certain remote sellers during the 12-month period between October 1, 2018, and September 30, 2019. Procedures for determining the rate reductions were enacted as part of 2013 Wisconsin Act 20 and modified by 2017 Wisconsin Act 368, so that the Department of Revenue (DOR) determines the amount of sales and use tax reported by out-of-state retailers and the proportional tax rate reductions under the individual income tax and reports those determinations to the Governor, the Secretary of the

Department of Administration (DOA), the Joint Committee on Finance, and the Legislative Audit Bureau (LAB). If the LAB's review of the determinations results in a different calculation of tax rates, the Joint Committee on Finance is required to determine which tax rates apply.

GOVERNOR

Modify the current law provision that requires a reduction in individual income tax rates in tax year 2019 to offset the additional sales and use tax collected from out-of-state retailers during the 12-month period from October 1, 2018, to September 30, 2019, by requiring the rate reduction be made to the lowest individual income tax rate (currently 4.0%), rather than to all four tax rates in proportion to the share of gross tax attributable to each of the four tax brackets established under current law.

DISCUSSION POINTS

1. In 2013, the Wisconsin Legislature recognized the possibility that the U.S. Congress may enact legislation expanding states' ability to require out-of-state sellers to collect and remit sales and use taxes on remote sales to individuals in their state. In response, the Legislature included a provision in 2013 Wisconsin Act 20, the 2013-15 biennial budget act, specifying that any resulting sales and use tax collected on such sales to Wisconsin residents be used first to eliminate the alternative minimum tax (AMT) and then to further reduce income tax rates in proportion to the share of gross tax attributable to each of the tax brackets in effect. The Act charged DOR with determining how much additional sales and use tax was collected from remote sales during the first 12 months following the date on which the state began collecting the tax.

2. On two occasions, the Legislature has modified the Act 20 provision, and in each instance, the Legislature retained the requirement that the rate reductions be in proportion to the share of gross tax attributable to each tax bracket. In 2017 Wisconsin Act 59, the 2017-19 biennial budget, the Legislature adopted a provision eliminating the state AMT, effective in tax year 2019. The AMT reference in the Act 20 provision was removed, and the proportional reduction in income tax rates became the sole use of the sales tax proceeds from remote sales. In the following year, 2017 Wisconsin Act 368 modified the Act 20 provision to accelerate the tax year that the tax rate reductions take effect and to provide additional oversight of DOR's rate reduction calculations, including a role for the Legislature. The Act 368 changes were prompted by the 2018 U.S. Supreme Court decision, *South Dakota v. Wayfair, Inc.*, rather than an act of Congress, allowing states to require out-of-state sellers lacking a physical presence in the state to collect tax on remote sales, so long as the state tax meets certain other requirements. Act 368 specified that the decision triggered the income tax rate reductions.

3. While the Legislature has affirmed its use of proportional tax rate reductions for the sales tax proceeds from remote sales on these occasions, the Legislature has also recently adopted a more targeted tax rate reduction. A year after the Legislature adopted the original requirement that sales tax from remote sales be used to proportionally reduce individual income tax rates, the Legislature enacted an individual income tax rate reduction. In 2013 Wisconsin Act 145, the Legislature adopted

a provision reducing the marginal tax rate that applies to income that falls within the bottom income tax bracket from 4.4% to 4.0%, effective in tax year 2014. The Act did not make changes to the marginal tax rates for the other three income tax brackets.

4. DOR has estimated that $61.0 million will be available to reduce tax rates in tax year 2019 based on the amount of sales tax collected from remote sellers at the time the biennial budget bill was introduced. Table 1 reports the tax year 2019 tax rate structure for the tax rates that are currently in effect, the estimated tax rates under the Governor's proposal to limit the rate reduction to the bottom tax bracket (bottom bracket), and the estimated tax rates under a reduction in proportion to each bracket's share of gross tax (across-the-board).

TABLE 1

Individual Income Tax Rates Currently in Effect and Estimated Tax Rates Under Two Rate Reduction Alternatives

	Income Tax Rates Currently in Effect	Alternative Tax Rate Reductions Bottom Bracket	Across-the-Board
Bottom Bracket	4.00%	3.78%	3.98%
Second Bracket	5.84	5.84	5.81
Third Bracket	6.27	6.27	6.23
Top Bracket	7.65	7.65	7.61

5. Attachment 1 reports the estimated distribution of taxpayers and net tax by Wisconsin adjusted gross income (AGI) for tax year 2019 under the tax rates currently in effect, before the tax reduction based on the amount of sales tax collected from remote sellers. For tax year 2019, the total amount of net tax is estimated to decrease by $61.0 million, or 0.7%, from $8,779.3 million to $8,718.3 million. Similar attachments were not prepared for the two alternatives because the amount of the tax reduction is not large enough to appreciably change the distribution of taxpayer count or amount of net tax. However, there are some low-income taxpayers who currently have a tax liability, but who would no longer have a tax liability under each alternative. Because there would be fewer taxpayers with a net tax under the alternative that reduces the rate for the bottom bracket, than under the alternative that reduces rates across-the-board, a higher average net tax results under the reduction to the bottom bracket ($3,809), than under the across-the-board alternative ($3,800), even though each alternative would reduce taxes by $61.0 million.

6. Attachment 2 reports the estimated distribution by Wisconsin AGI of taxpayers and tax change among taxpayers with a tax decrease in tax year 2019 under the two tax rate reduction alternatives. Over 95% of all taxpayers with a tax liability and over 70% of all tax filers would experience a tax decrease under each alternative, and no taxpayers would experience a tax increase. The number of taxpayers experiencing a tax decrease is estimated at 2,273,210 under the bottom bracket alternative and at 2,215,020 under the across-the-board alternative. Compared to the bottom bracket alternative, more than 58,000 taxpayers would not experience a tax decrease under the across-the-board alternative. These taxpayers have lower AGIs and their taxable income falls entirely in the

bottom bracket. The estimated change to the 4.0% rate under the across-the-board alternative is so small as to result in no tax change for these taxpayers. Taxpayers with no tax change are likely to be single dependent, nonresident, and part-year resident filers.

7. The distribution of taxpayers with a tax decrease is similar under the two alternatives. While the tax decrease distribution under the bottom bracket alternative is comparable to the taxpayer distributions, the tax decrease distribution under the across-the-board alternative is more heavily weighted towards taxpayers in higher AGI categories. To illustrate, taxpayers with AGI between $20,000 and $70,000 would comprise just over 50% of the taxpayers with a tax decrease, and those taxpayers would receive just over 50% of the tax decrease under the bottom bracket alternative. However, taxpayers in that AGI range would receive only 18% of the tax decrease under the across-the-board alternative. The tax decrease distribution under that alternative mirrors the distribution of net tax, as displayed in Attachment 1.

8. Under the rate and bracket structure currently in effect, taxpayers with AGI under $100,000 represent 78.5% of taxpayers with a net tax and pay 33.5% of the net tax, and taxpayers with AGI over $100,000 represent 21.5% of the taxpayers with a net tax and pay 66.5% of the net tax. These amounts are displayed in Table 2.

TABLE 2

Distribution of Taxpayers and Net Tax Under Tax Rates Currently in Effect for Taxpayers with AGI Under $100,000 and Over $100,000, Tax Year 2019

	Taxpayers		Net Tax	
AGI Group	Count	Percentage	$ (Million)	Percentage
Under $100,000	1,802,150	78.5%	$2,940.0	33.5%
Over $100,000	493,680	21.5	5,839.3	66.5
Total	2,295,830	100.0%	$8,779.3	100.0%

9. Under the bottom bracket alternative, taxpayers with an AGI below $100,000 represent 78.3% of the taxpayers with a tax decrease, and they would receive 73.3% of the estimated tax decrease. Taxpayers with AGI over $100,000 represent 21.7% of the taxpayers with a tax decrease, and they would receive 26.7% of the estimated tax decrease. Under the across-the-board alternative, taxpayers with an AGI below $100,000 represent 77.7% of the taxpayers with a tax decrease, and they would receive 32.3% of the estimated tax decrease. Taxpayers with AGI over $100,000 represent 22.3% of the taxpayers with a tax decrease, and they would receive 67.7% of the estimated tax decrease. These amounts are displayed in Table 3.

TABLE 3

Distribution of Taxpayers with a Net Tax and a Tax Decrease for Taxpayers with AGI Under $100,000 and Over $100,000 Under Two Tax Rate Reduction Alternatives, Tax Year 2019

	Bottom Bracket		Across-the-Board	
AGI Group	Percent of Taxpayers	Percent of Tax Decrease	Percent of Taxpayers	Percent of Tax Decrease
Under $100,000	78.3%	73.3%	77.7%	32.3%
Over $100,000	21.7	26.7	22.3	67.7
Total	100.0%	100.0%	100.0%	100.0%

10. Under the bottom bracket alternative, taxpayers with AGI below $100,000 would receive an average tax decrease of $25, equal to 1.5% of their current tax liability. Taxpayers with AGI above $100,000 would receive an average tax decrease of $33, equal to 0.3% of their current net tax liability. Under the across-the-board alternative, taxpayers with AGI below $100,000 would receive an average tax decrease of $11, and taxpayers with AGI over $100,000 would receive an average tax decrease of $84. The across-the-board alternative would result in a tax decrease equal to 0.7% of each group's current tax. For all taxpayers with a tax decrease, a $61.0 million tax decrease would produce an average tax decrease of $27 under the bottom bracket alternative and $28 under the across-the-board alternative. As a percentage of current tax, the decrease would average 0.7% under each alternative. These amounts are displayed in Table 4.

TABLE 4

Estimated Average Tax Decrease and Percentage Tax Decrease for Taxpayers with a Net Tax and with AGI Under $100,000 and Over $100,000 Under Two Tax Rate Reduction Alternatives, Tax Year 2019

	Bottom Bracket		Across-the-Board	
AGI Group	Average Tax Decrease	Percentage Tax Decrease	Average Tax Decrease	Percentage Tax Decrease
Under $100,000	$25	1.5%	$11	0.7%
Over $100,000	33	0.3	84	0.7
All Taxpayers with a Decrease	$27	0.7%	$28	0.7%

11. At the time 2017 Wisconsin Act 368 was enacted, the amended Act 20 provision was expected to reduce tax rates on an ongoing basis beginning in tax year 2019. Reductions of $60 million were incorporated into the amount of individual income tax collections estimated for 2019-20 and 2020-21 that were reported by this office in its January 30, 2019 revenue estimates, and those amounts were used by the administration to prepare the biennial budget. However, the amended statute reads,

"the new tax rates take effect for the taxable year ending on December 31, 2019" and that the tax rates "apply to the taxable year ending on December 31, 2019." After reviewing the language of Act 368, DOR has indicated that it interprets the law to mean the income tax rate reduction applies to tax year 2019 only. On May 1, 2019, DOA submitted an errata seeking to clarify that the tax rate reduction is ongoing.

12. If the Committee wants the tax rate reduction to apply only in tax year 2019, it could not adopt the errata and either adopt the Governor's proposal to limit the tax rate reduction to the tax rate for the bottom income bracket (Alternative 1) or retain the current law provision reducing each of the four tax rates on an across-the-board basis (Alternative 2).

13. If the Committee believes the Legislature intended the tax rate reduction to be ongoing, rather than apply only in tax year 2019, the Committee could modify the bill to amend the tax rate reduction statute to accomplish this purpose. Because this office reflected the DOR determination in its May, 2019, revenue reestimates, this modification would have the effect of reducing individual income tax collections by over $60 million in 2020-21. However, making the tax rate reduction ongoing would result in a somewhat different fiscal effect, depending on whether the Committee adopts the Governor's proposed tax rate reduction or retains the tax rate reduction under current law. If the Committee modifies the Governor's proposal to limit the tax rate reduction to the tax rate for the bottom income bracket, a 2020-21 tax decrease estimated at $63.2 million would result (Alternative 3). If the Committee modifies the across-the-board tax rate reduction authorized under current law, a 2020-21 tax decrease estimated at $64.7 million would result (Alternative 4).

14. The estimated tax decrease presented in the preceding alternatives totals about $60 million annually. This amount represents a relatively minor change to the state's individual income tax, which totals about $9 billion. Instead of using the sales tax proceeds to reduce individual income tax rates, the Legislature could use it to enhance another budget initiative, such as the proposed family and individual reinvestment credit or the proposed child and dependent care credit. If the Legislature wants to pursue more fundamental income tax reform, the tax revenues from this proposal could be combined with revenues associated with other budget provisions, such as those just mentioned, and used to address the marriage penalty, reduce the income range for the third tax bracket, or increase the personal exemption level to adjust tax liabilities in relation to family size. Alternative #5 would repeal the income tax rate reduction requirement, as created by 2013 Act 20 and modified by 2017 Act 368, thereby making the sales tax proceeds from remote sellers available for other uses. This alternative would increase individual income tax collections by an estimated $61.0 million in tax year 2019 and in fiscal year 2019-20.

ALTERNATIVES

1. Approve the Governor's proposal to modify the current law provision that requires a reduction in individual income tax rates in tax year 2019 to offset the additional sales and use tax collected from out-of-state retailers during the 12-month period from October 1, 2018, to September 30, 2019, by requiring the rate reduction be made only to the lowest individual income tax rate (currently 4.0%). This alternative would not include the errata submitted by DOA to clarify that the tax rate reduction is ongoing.

2. Take no action and retain the current law requirement for an across-the-board reduction in individual income tax rates in tax year 2019.

3. Modify the Governor's proposal to limit the tax rate reduction to the rate for the lowest individual income tax bracket by extending the tax rate determined for tax year 2019 to succeeding tax years. Decrease individual income tax collections in 2020-21 by an estimated $63,200,000.

ALT 3	**Change to**	
	Base	**Bill**
GPR-Tax	-$63,200,000	-$63,200,000

4. Modify the current law provision that requires an across-the-board reduction in individual income tax rates by extending the tax rates determined for tax year 2019 to succeeding tax years. Decrease individual income tax collections in 2020-21 by an estimated $64,700,000.

ALT 4	**Change to**	
	Base	**Bill**
GPR-Tax	- $64,700,000	- $64,700,000

5. Delete the Governor's recommendation and repeal the current law requirement to reduce individual income tax rates based on the amount of sales tax collected from remote sellers. Increase individual income tax collections under the bill by an estimated $61,000,000 in 2019-20.

ALT 5	**Change to**	
	Base	**Bill**
GPR-Tax	$61,000,000	$61,000,000

Prepared by: Rick Olin
Attachments

ATTACHMENT 1

Estimated Distribution of Taxpayers and Net Tax Under Current Tax Rate Schedule Prior to Reduction Related to the Sales Tax Collected from Remote Sellers, Tax Year 2019

Wisconsin Adjusted Gross Income	Count	Percent of Count	Amount of Net Tax	Percent of Net Tax	Average Net Tax	Count of All Returns	% of Returns with Net Tax
Under $5,000	43,300	1.9%	$3,661,620	< 0.1%	$85	472,390	9.2%
5,000 to 10,000	28,050	1.2	6,387,500	0.1	228	220,080	12.7
10,000 to 15,000	77,860	3.4	11,894,980	0.1	153	188,590	41.3
15,000 to 20,000	115,740	5.0	27,707,260	0.3	239	173,680	66.6
20,000 to 25,000	143,140	6.2	54,284,430	0.6	379	171,290	83.6
25,000 to 30,000	152,380	6.6	91,763,370	1.0	602	169,640	89.8
30,000 to 40,000	309,860	13.5	297,265,620	3.4	959	316,190	98.0
40,000 to 50,000	254,340	11.1	392,107,250	4.5	1,542	255,800	99.4
50,000 to 60,000	196,290	8.5	415,271,980	4.7	2,116	197,050	99.6
60,000 to 70,000	155,910	6.8	416,618,200	4.7	2,672	156,370	99.7
70,000 to 80,000	125,760	5.5	406,504,820	4.6	3,232	126,060	99.8
80,000 to 90,000	107,550	4.7	410,624,430	4.7	3,818	107,750	99.8
90,000 to 100,000	91,970	4.0	405,928,910	4.6	4,414	92,090	99.9
100,000 to 125,000	172,420	7.5	931,082,470	10.6	5,400	172,630	99.9
125,000 to 150,000	104,770	4.6	713,679,370	8.1	6,812	104,860	99.9
150,000 to 200,000	100,810	4.4	887,056,330	10.1	8,799	100,950	99.9
200,000 to 250,000	41,850	1.8	491,227,990	5.6	11,738	41,960	99.7
250,000 to 300,000	21,000	0.9	309,767,870	3.5	14,751	21,080	99.6
300,000 to 500,000	29,840	1.3	639,697,160	7.3	21,438	30,220	98.7
500,000 to 1,000,000	15,520	0.7	639,469,730	7.3	41,203	15,660	99.1
1,000,000 and over	7,470	0.3	1,227,264,440	14.0	164,292	7,640	97.8
Total	2,295,830	100.0%	$8,779,265,730	100.0%	$3,824	3,141,980	73.1%

- Under the current rate and bracket structure, an estimated 2.3 million taxpayers will incur net tax liabilities estimated at $8,779.3 million in tax year 2019. An average tax of $3,824 is estimated.

- Taxpayers with AGI under $100,000 comprise 78.5% of the taxpayers and pay 33.5% of the net taxes. Their average tax equals $1,631. Taxpayers with AGI over $100,000 comprise 21.5% of the taxpayers and pay 66.5% of the net taxes. Their average net tax equals $11,828.

Based on a simulation of tax year 2019 by the Wisconsin Department of Revenue.

ATTACHMENT 2

Distribution of Taxpayers and Tax Change Among Taxpayers with a Tax Decrease Under Tax Rate Reduction Alternatives, Tax Year 2019

Wisconsin Adjusted Gross Income	Taxpayers with a Tax Decrease Under Tax Rate Reduction Alternatives: Bottom Bracket		Across-the-Board		Amount of Tax Decrease Under Tax Rate Reduction Alternatives: Bottom Bracket		Across-the-Board		Average and Percentage Tax Decrease Under Tax Rate Reduction Alternatives: Bottom Bracket		Across-the-Board	
Under $5,000	30,170	1.3%	18,160	0.8%	-$82,660	0.1%	-$20,370	< 0.1%	-$3	-2.3%	-$1	-0.6%
5,000 to 10,000	25,320	1.1	20,750	0.9	-147,290	0.2	-37,160	0.1	-6	-2.3	-2	-0.6
10,000 to 15,000	73,580	3.2	35,770	1.6	-413,000	0.7	-66,050	0.1	-6	-3.5	-2	-0.6
15,000 to 20,000	115,050	5.1	111,420	5.0	-1,522,580	2.5	-182,210	0.3	-13	-5.5	-2	-0.7
20,000 to 25,000	142,700	6.3	141,340	6.4	-3,161,980	5.2	-351,590	0.6	-22	-5.8	-2	-0.6
25,000 to 30,000	152,200	6.7	152,220	6.9	-3,659,490	6.0	-579,570	0.9	-24	-4.0	-4	-0.6
30,000 to 40,000	309,590	13.6	309,860	14.0	-8,191,180	13.4	-1,868,480	3.1	-26	-2.8	-6	-0.6
40,000 to 50,000	254,170	11.2	254,340	11.5	-7,096,360	11.6	-2,522,040	4.1	-28	-1.8	-10	-0.6
50,000 to 60,000	196,180	8.6	196,290	8.9	-5,636,780	9.2	-2,742,410	4.5	-29	-1.4	-14	-0.7
60,000 to 70,000	155,820	6.9	155,910	7.0	-4,633,920	7.6	-2,817,740	4.6	-30	-1.1	-18	-0.7
70,000 to 80,000	125,700	5.5	125,760	5.7	-3,862,620	6.3	-2,798,920	4.6	-31	-1.0	-22	-0.7
80,000 to 90,000	107,500	4.7	107,550	4.9	-3,390,130	5.6	-2,858,250	4.7	-32	-0.8	-27	-0.7
90,000 to 100,000	91,930	4.0	91,970	4.2	-2,957,750	4.8	-2,852,050	4.7	-32	-0.7	-31	-0.7
100,000 to 125,000	172,340	7.6	172,420	7.8	-5,655,030	9.3	-6,660,030	10.9	-33	-0.6	-39	-0.7
125,000 to 150,000	104,710	4.6	104,770	4.7	-3,478,270	5.7	-5,151,920	8.4	-33	-0.5	-49	-0.7
150,000 to 200,000	100,750	4.4	100,810	4.6	-3,353,130	5.5	-6,363,210	10.4	-33	-0.4	-63	-0.7
200,000 to 250,000	41,810	1.8	41,850	1.9	-1,387,140	2.3	-3,484,450	5.7	-33	-0.3	-83	-0.7
250,000 to 300,000	20,970	0.9	21,000	0.9	-693,550	1.1	-2,175,990	3.6	-33	-0.2	-104	-0.7
300,000 to 500,000	29,790	1.3	29,840	1.3	-978,080	1.6	-4,334,950	7.1	-33	-0.2	-145	-0.7
500,000 to 1,000,000	15,490	0.7	15,520	0.7	-504,100	0.8	-4,121,440	6.8	-33	-0.1	-266	-0.6
1,000,000 and over	7,440	0.3	7,470	0.3	-236,250	0.4	-9,059,420	14.8	-32	> -0.1	-1,213	-0.7
Total	2,273,210	100.0%	2,215,020	100.0%	-$61,041,290	100.0%	-$61,048,250	100.0%	-$27	-0.7%	-$28	-0.7%

- The number of taxpayers experiencing a tax decrease is estimated at 2,273,210 under the alternative to reduce the rate for the bottom tax bracket and at 2,215,020 under the alternative to reduce rates across-the-board. The difference is concentrated among taxpayers with lower AGIs whose income is entirely taxed in the bottom tax bracket. The estimated change to the 4.0% rate under the across-the-board alternative is so small as to result in a tax change of less than $1. The rest of the difference is due to taxpayers filing nonresident and part-year resident returns. Over 95% of all taxpayers with a tax liability and over 70% of all tax filers would experience a tax decrease under each of the two alternatives.

- The total tax decrease is estimated at $61.0 million and would result in an average tax decrease of $27 under the alternative lowering the rate for the bottom bracket and $28 under the alternative lowering the rates on an across-the-board basis, with the number of taxpayers receiving a tax decrease responsible for the difference. The average tax decrease is estimated at 0.7% under each alternative.

Based on a simulation of tax year 2019 by the Department of Revenue.

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June, 2019 Joint Committee on Finance Paper #320

Child and Dependent Care Tax Credit
(General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 139, #11]

CURRENT LAW

Expenses related to child and dependent care are deductible from income for state tax purposes. The deduction equals up to $3,000 for one qualified individual and up to $6,000 for more than one qualified individual. The deduction was phased in over a four-year period starting in tax year 2011, and increased each year until reaching the current amounts in 2014. The deduction is based on the expenses claimed for purposes of the federal child and dependent care credit and must be deducted for the same taxable year as the year to which the claim for the federal credit relates.

Federal law provides an individual income tax credit for child and dependent care expenses that are paid for the purpose of enabling a taxpayer to be gainfully employed. The maximum amount of expenses that can be claimed for the federal credit is $3,000 if the claimant has one qualifying child or dependent and $6,000 if the claimant has more than one qualifying child and/or dependent. In addition to the $3,000/$6,000 limit, the amount of eligible expenses cannot exceed the claimant's earned income or the earned income of the claimant's spouse if a married joint filer. The credit is calculated as a percentage of eligible expenses, with the percentage ranging from 35% to 20%, depending on the claimant's federal adjusted gross income (AGI).

Eligible claims for the federal credit must satisfy a number of tests, including a qualifying person test. Under the federal provisions, a qualifying person includes: (a) the claimant's qualifying child, who is the claimant's dependent and who was under the age of 13 when the care was provided; (b) the claimant's spouse who was physically or mentally not able to care for himself or herself and lived with the claimant for more than half the year; and (c) a person who was physically or mentally not able to care for himself or herself, lived with the claimant for more than half the year, and, with certain exceptions, was the claimant's dependent.

The following federal tests must also be met to claim the child and dependent care credit: (a) with an exception related to being a student, the individual claiming the credit (and the individual's spouse, if married) must have earned income during the year; (b) the child and dependent care expenses must be being paid so that the individual claiming the credit (and the individual's spouse, if married) can work or look for work; (c) the payments for the child and dependent care must be made to someone who cannot be claimed as a dependent of the individual claiming the credit or the individual's spouse; (d) in general, the claimant's filing status must be single, head-of-household, qualifying widow(er) with dependent child, or married filing jointly; and (e) the care provider must be identified on the claimant's tax return. In addition, if a claimant excludes or deducts dependent care benefits provided by a dependent care benefit plan, the total amount excluded or deducted under such a plan must be less than the dollar limit for qualifying expenses under the credit.

GOVERNOR

Create a nonrefundable individual income tax credit for household and dependent care expenses, beginning with tax year 2020. Set the credit equal to 50% of the amount of the federal household and dependent care expenses credit, authorized under the Internal Revenue Code (IRC), that is claimed by a taxpayer on his or her federal income tax return for the same tax year. Limit the credit to claims filed within four years of the unextended due date for which the tax return was due. Prohibit claims for a period of less than 12 months, except by reason of the taxpayer's death, and prohibit part-year residents and nonresidents from claiming the credit. Require couples who are married at the end of a tax year to claim the credit as married joint filers for that tax year, except permit married persons living apart and treated as single under the IRC to claim the credit as if a single or head-of-household claimant. Authorize DOR to administer the credit under general statutory provisions related to the income tax. Sunset the current law deduction for household and dependent care expenses beginning in tax year 2020. Decrease individual income tax collections by an estimated $9,900,000 in 2020-21.

DISCUSSION POINTS

1. Federal law has provided a child and dependent care tax credit since 1976, while the state's child and dependent care deduction took effect in 2011. As a matter of tax policy, some experts generally prefer tax credits over deductions to income. Deductions treat taxpayers differently depending on the taxpayer's income and tax bracket. For example, a $2,000 deduction to AGI would provide an $80 tax reduction to a taxpayer whose taxable income falls entirely within the state's 4% tax bracket and a $153 tax reduction to a taxpayer whose last dollar of income is subject to the state's 7.65% marginal tax rate. Based on the same $2,000 expense, a 6% tax credit would result in a $120 tax reduction regardless of the taxpayer's income, thereby providing more uniform treatment to taxpayers. As a policy distinction, some tax experts object to refundable tax credits, but the credit proposed by the Governor would be nonrefundable.

2. Each of the state's largest nonrefundable tax credits is based on a single credit rate -- 12% for the property tax/rent credit, 5% for the itemized deduction credit, and 3% for the married

couple credit. While the proposed credit would be calculated using a single credit rate of 50%, the state credit would be based on the federal child and dependent care credit which uses 16 separate credit rates, which phase down from 35% for claimants whose federal AGI is below $15,000 to 20% for claimants whose federal AGI is over $43,000. Based on $6,000 in eligible expenses, the maximum state credit would equal $1,050 for a claimant with federal AGI of $15,000 or less and $600 for a claimant with federal AGI of more than $43,000. As a result of the sliding scale in the federal credit rate, a lower-income taxpayer with the same eligible child or dependent care expenses as a higher-income taxpayer would receive a larger state credit under the credit structure proposed in the bill.

3. The proposed credit would reduce individual income tax collections by an estimated $28.9 million in tax year 2020. Because the proposal would sunset the current law deduction for child and dependent care expenses, which already reduces taxes by an estimated $19.0 million, the net effect of the proposed credit would be to reduce individual income tax collections by an estimated $9.9 million in tax year 2020.

4. Attachment 1 reports the estimated distribution of taxpayers with a tax decrease under the proposed credit for tax year 2020. An estimated 110,950 taxpayers, or 3.5% of all tax filers, would experience a tax decrease. The average tax reduction would equal $90. Due to the sliding rate scale employed by the federal credit, the highest average tax decrease would result for taxpayers with AGI in the $25,000 to $30,000 range ($148), although taxpayers with AGI over $100,000 would receive a larger average tax reduction ($91) than taxpayers with AGI under $100,000 ($88). This is most likely the result of those claimants having a higher number of eligible children and/or higher average child care costs. Taxpayers with AGI of less than $100,000 represent 49.6% of the taxpayers with a tax reduction, and they would receive 48.6% of the total tax decrease. Taxpayers with AGI over $100,000 would receive 51.4% of the estimated tax decrease and represent 50.4% of the taxpayers with a tax decrease. The small percentage of filers receiving a tax decrease (3.5%) is due to the credit being limited to taxpayers with children who are under 13 years of age and in daycare or taxpayers with a spouse or dependent with certain disabilities.

5. Biennially, this office reviews the income tax provisions in each state with an individual income tax. For tax year 2017, this review reveals that three states, including Wisconsin, offered a deduction for child and dependent care expenses based on the federal definition of eligible expenses. Idaho's deduction was structured similarly to Wisconsin's deduction, while Massachusetts offered a higher limitation on deductible expenses -- up to $4,800 for one child and $9,600 for two or more children.

6. A tax credit for child and dependent care expenses was offered in 21 states in tax year 2017. Generally, these states' credits are calculated either as a percentage of the federal credit or as a percentage of eligible federal expenses, although there is considerable variation in the percentages employed. A number of states employ multiple percentages. In at least four states, the state credit can equal the federal credit below certain income levels, with California employing an income threshold of $100,000. The New York credit uses the same credit percentages as the federal credit, and also employs a multiplier that can exceed 1.0 for lower income claimants, so the state credit can exceed the federal credit. Also, New York authorizes higher limitations on eligible expenses for claimants with three ($7,500), four ($8,500), or five or more ($9,000) eligible dependents.

7. Child and dependent care tax credits are refundable in nine of the 21 states, including Nebraska, where the credit is refundable for claimants with incomes at or below $29,000 and nonrefundable for claimants with incomes above $29,000. Making the proposed credit refundable would increase the cost of the credit by an additional $4.1 million in 2020-21, and the average tax reduction would be about $25 higher than under a nonrefundable credit. Also, there would be almost 11,000 more claimants. Generally, these are filers with no net tax liability under current law.

8. Attachment 2 reports the estimated distribution of taxpayers with a tax decrease under a refundable child and dependent care tax credit for tax year 2020. An estimated 121,693 taxpayers, or 3.8% of all tax filers, would experience a tax decrease. The average tax reduction would equal $115. The combination of a refundable credit and the sliding rate scale employed by the federal credit would result in an average tax decrease of more than $300 for claimants with AGI of less than $15,000. Further, claimants with AGI of less than $100,000 would receive a larger average credit ($134) than claimants with AGI over $100,000 ($93). Claimants with AGI of less than $100,000 represent 54.5% of the claimants with a tax reduction, and they would receive 63.3% of the total tax decrease. Claimants with AGI over $100,000 would receive 36.7% of the estimated tax decrease and represent 45.5% of the claimants with a tax decrease. As under the proposal in the bill, the small percentage of filers receiving a tax decrease (3.8%) is due to the credit being limited to taxpayers with children who are under 13 years of age and in child care or taxpayers with a spouse or dependent with certain disabilities.

9. Among the alternatives presented in this paper, a refundable child and dependent care tax credit is presented as Alternative 2. Because the state budget system records refundable tax credits as state expenditures, rather than a reduction in tax collections, this alternative would be reflected as an increase in GPR expenditures estimated at $33.0 million in 2020-21. Because the proposal would sunset the child and dependent care deduction offered under current law, this alternative would increase tax collections by an estimated $19.0 million in 2020-21 compared to current law. Since it would also replace the proposed nonrefundable tax credit, it would increase individual income taxes by an estimated $28.9 million compared to the bill.

10. Under the two preceding alternatives, the child and dependent care credit would be limited to between 110,950 and 121,693 taxpayers with employment-related child and dependent care expenses. As noted, these claimants would comprise only 3.5% or 3.8% of all tax filers. The proposed credit would not be available to families in which the caregiver refrains from seeking employment in order to provide care for a child or dependent or to families with children who are 13 years of age or older. One way to broaden the scope of the credit would be to extend the credit to all filers with children or dependents.

11. A separate federal tax credit, called the child tax credit, may be claimed by individuals with children under 17 years of age, provided the taxpayer can claim the children as dependents. The credit equals $2,000 per child and phases out for claimants with incomes above $400,000 for married joint filers and $200,000 for other filer types. The credit consists of both nonrefundable and refundable components. A nonrefundable credit of $500 is also provided for each of the claimant's other dependents, such as children 17 years of age or older and other relatives of the taxpayer.

12. There are approximately 1.5 million dependents claimed by Wisconsin taxpayers, which

implies about $3.0 billion in federal child tax credits are claimed by Wisconsin filers. Because converting the child and dependent care deduction to a credit has a fiscal effect of $9.9 million, a state child tax credit at that funding level would equal about 0.3% of the initial federal credit (prior to its division between nonrefundable and refundable) or about $6 per dependent. Taxpayers may regard such a small credit as more of a nuisance to calculate than as a tax benefit. Another reason to not base a state credit on the federal child tax credit is that the federal credit, as described above, was expanded on a temporary basis for tax years 2018 through 2025 by the Tax Cuts and Jobs Act of 2017. The expansion of the credit was tied to the Act's elimination of personal exemptions for the same time period.

13. Under Wisconsin's individual income tax, a $700 personal exemption is provided for each taxpayer and taxpayer's spouse, as well as for each individual claimed as a dependent. An additional $250 exemption is provided for each taxpayer who has reached the age of 65 before the end of the tax year. By eliminating the personal exemption for dependents, estimated at $57.6 million, and combining the tax savings with the $9.9 million related to the proposed tax credit in the bill, a nonrefundable state child tax credit of $50 per dependent could be provided, beginning in tax year 2020 (Alternative 3). Total claims for credits are estimated at $78.6 million, but if the credit would be nonrefundable, only $67.7 million in claims would be used. The personal exemption for filers and their spouses, and the additional personal exemption for persons 65 years of age or older would not be eliminated since that would cause individuals without children to experience a tax increase. Also, a credit of $50 per dependent would not employ an income phaseout, like the federal credit. Incorporating an income phaseout would result in a higher per child credit rate, but would also cause some taxpayers to experience a tax increase. This alternative would retain the current law child and dependent care expense deduction.

14. A credit structured in this way would be claimed by an estimated 757,800 filers, resulting in a reduction in individual income tax collections estimated at $67.7 million in tax year 2020. This overstates the effect of this alternative by not considering the loss of the personal exemption for dependents. Attachment 3 displays the net effect of the alternative by combining the tax effects of claiming the credit with the loss of the personal exemption for dependents. An estimated 716,500 taxpayers, or 22.6% of all tax filers, would experience tax decreases totaling $10.3 million. The average tax reduction would equal $14. Claimants with AGI of less than $100,000 would receive a larger average decrease ($15) than claimants with AGI over $100,000 ($12). Claimants with AGI of less than $100,000 represent 65.5% of the taxpayers with a tax reduction, and they would receive 70.5% of the total tax decrease. Claimants with AGI over $100,000 would receive 29.5% of the estimated tax decrease and represent 34.5% of the taxpayers with a tax decrease.

15. The cost of the credit would be reduced by an estimated $157,000 due to about 26,000 taxpayers who would experience a tax increase, equaling $6 on average. For these taxpayers, the tax reduction resulting from the $700 personal exemption exceeds the tax reduction resulting from a $50 tax credit. These would be taxpayers who are subject to the state's 7.65% marginal tax rate, the top tax bracket, since a tax benefit of $50 represents only 7.14% of a $700 reduction in income. With the offset provided by this tax increase, the net effect of this alternative would be to reduce individual income tax collections by $200,000 more than the creation of the tax credit for child and dependent care expenses and the sunset of the related deduction that is proposed in the bill. Under this alternative

(Alternative 3), the current law child and dependent care expense deduction would be retained.

ALTERNATIVES

1. Approve the Governor's recommendation to create a nonrefundable individual income tax credit for household and dependent care expenses, beginning in tax year 2020. Set the credit equal to 50% of the amount of the federal household and dependent care expenses credit, authorized under the IRC, that is claimed by a taxpayer on his or her federal income tax return for the same tax year. Sunset the current law deduction for household and dependent care expenses beginning in tax year 2020. Decrease individual income tax collections by an estimated $9,900,000 in 2020-21.

ALT 1	**Change to**	
	Base	**Bill**
GPR-Tax	- $9,900,000	$0

2. Modify the Governor's recommendation to create a nonrefundable individual income tax credit for household and dependent care expenses, beginning in tax year 2020, by making the proposed credit refundable. Set the credit equal to 50% of the amount of the federal household and dependent care expenses credit, authorized under the IRC, that is claimed by a taxpayer on his or her federal income tax return for the same tax year. Sunset the current law deduction for household and dependent care expenses beginning in tax year 2020. Estimate the cost of the credit at $33,000,000 GPR in 2020-21. Increase individual income tax collections in 2020-21 by an estimated $19,000,000 compared to current law to reflect the sunset of the current law deduction and by $28,900,000 compared to the bill to reflect the elimination of the proposed nonrefundable credit.

ALT 2	**Change to**	
	Base	**Bill**
GPR-Tax	$19,000,000	$28,900,000
GPR	33,000,000	33,000,000

3. Take no action on the Governor's recommendation. Instead, create a nonrefundable child and dependent tax credit and sunset the $700 personal exemption for dependents under the individual income tax beginning in tax year 2020. Set the credit equal to $50 per qualifying dependent, for each dependent who the claimant supports during the tax year and who may be claimed as a dependent on the claimant's state individual income tax return. Limit the credit to claims filed within four years of the unextended due date for which the tax return was due. Prohibit claims for a period of less than 12 months, except by reason of the taxpayer's death. Require couples who are married at the end of a tax year to claim the credit as married joint filers for that tax year, except permit married persons living apart and treated as single under the IRC to claim the credit as if a single or head-of-household claimant. Require claimants to comply with identification requirements under the IRC for receiving the federal child tax credit. Authorize DOR to administer the credit under general statutory provisions related to the income tax. Decrease individual income tax collections by an estimated $10,100,000

compared to current law and by $200,000, compared to the bill.

ALT 3	Change to	
	Base	**Bill**
GPR-Tax	- $10,100,000	- $200,000

4. Take no action.

ALT 4	Change to	
	Base	**Bill**
GPR-Tax	$0	$9,900,000

Prepared by: Rick Olin
Attachments

ATTACHMENT 1

Distribution of Taxpayers Under Proposal to Replace the Child and Dependent Care Deduction with a Nonrefundable Tax Credit, Tax Year 2020

Wisconsin Adjusted Gross Income	Taxpayers Receiving a Tax Decrease: Count	Percent of Count	Amount of Tax Decrease	Percent of Decrease	Average Decrease	Count of All Returns	% of All Returns in AGI Class
Under $5,000	0	0.0%	$0	0.0%	$0	470,540	0.0%
5,000 to 10,000	0	0.0	0	0.0	0	212,390	0.0
10,000 to 15,000	110	0.1	-5,270	0.1	-48	184,210	0.1
15,000 to 20,000	940	0.8	-98,250	1.0	-105	166,810	0.6
20,000 to 25,000	2,940	2.6	-422,074	4.2	-144	167,290	1.8
25,000 to 30,000	3,840	3.5	-569,396	5.7	-148	165,390	2.3
30,000 to 40,000	7,820	7.0	-875,330	8.8	-112	315,400	2.5
40,000 to 50,000	6,280	5.7	-461,570	4.6	-73	260,350	2.4
50,000 to 60,000	5,830	5.3	-383,910	3.9	-66	201,340	2.9
60,000 to 70,000	6,000	5.4	-412,810	4.1	-69	161,740	3.7
70,000 to 80,000	6,570	5.9	-456,750	4.6	-70	126,930	5.2
80,000 to 90,000	7,150	6.4	-535,630	5.4	-75	108,430	6.6
90,000 to 100,000	7,510	6.8	-615,780	6.2	-82	93,510	8.0
100,000 to 125,000	17,800	16.0	-1,586,310	15.9	-89	178,310	10.0
125,000 to 150,000	13,020	11.7	-1,274,700	12.8	-98	113,470	11.5
150,000 to 200,000	13,060	11.8	-1,226,450	12.3	-94	110,470	11.8
200,000 to 250,000	5,520	5.0	-505,420	5.1	-92	47,440	11.6
250,000 to 300,000	2,440	2.2	-226,090	2.3	-93	23,600	10.3
300,000 to 500,000	2,830	2.6	-216,420	2.2	-76	33,310	8.5
500,000 to 1,000,000	1,030	0.9	-67,360	0.7	-65	17,250	6.0
1,000,000 and over	260	0.2	-16,870	0.2	-65	8,430	3.1
Total	110,950	100.0%	-$9,956,390	100.0%	-$90	3,166,610	3.5%

- An estimated 110,950, or 3.5%, of all tax filers in 2020 would receive a tax decrease under the proposal.
- The total tax decrease is estimated at $10.0 million in tax year 2020.
- For all taxpayers with a tax reduction, the average tax decrease in 2020 would be $90.
- Taxpayers with Wisconsin AGI of less than $100,000 represent 49.6% of the taxpayers with a tax reduction, and they would receive 48.6% of the reduction. Their tax decrease would average $88. Taxpayers with Wisconsin AGI of more than $100,000 represent 50.4% of the taxpayers with a tax reduction, and they would receive 51.4% of the reduction. Their tax decrease would average $91.
- Taxfilers without a tax decrease would include those without an eligible dependent, those with no tax liability under current law, and those who are nonresidents or part-year residents.

Based on a simulation of tax year 2020 by the Wisconsin Department of Revenue.

ATTACHMENT 2

Distribution of Taxpayers Under Proposal to Replace the Child and Dependent Care Deduction with a Refundable Tax Credit, Tax Year 2020

	Taxpayers Receiving a Tax Decrease					Count	% of All
Wisconsin Adjusted Gross Income	Count	Percent of Count	Amount of Tax Decrease	Percent of Decrease	Average Decrease	of All Returns	Returns in AGI Class
Under $5,000	1,696	1.4%	-$514,387	3.7%	-$303	470,540	0.4%
5,000 to 10,000	2,181	1.8	-685,831	4.9	-314	212,390	1.0
10,000 to 15,000	3,321	2.7	-1,011,973	7.2	-305	184,210	1.8
15,000 to 20,000	3,659	3.0	-1,093,257	7.8	-299	166,810	2.2
20,000 to 25,000	4,182	3.4	-978,508	7.0	-234	167,290	2.5
25,000 to 30,000	4,314	3.5	-736,927	5.3	-171	165,390	2.6
30,000 to 40,000	8,060	6.6	-966,640	6.9	-120	315,400	2.6
40,000 to 50,000	6,230	5.1	-467,550	3.3	-75	260,350	2.4
50,000 to 60,000	5,770	4.7	-390,340	2.8	-68	201,340	2.9
60,000 to 70,000	5,940	4.9	-417,090	3.0	-70	161,740	3.7
70,000 to 80,000	6,490	5.3	-462,640	3.3	-71	126,930	5.1
80,000 to 90,000	7,080	5.8	-538,880	3.8	-76	108,430	6.5
90,000 to 100,000	7,420	6.1	-619,360	4.4	-83	93,510	7.9
100,000 to 125,000	17,620	14.5	-1,591,620	11.3	-90	178,310	9.9
125,000 to 150,000	12,870	10.6	-1,277,390	9.1	-99	113,470	11.3
150,000 to 200,000	12,900	10.6	-1,230,490	8.8	-95	110,470	11.7
200,000 to 250,000	5,440	4.5	-507,140	3.6	-93	47,440	11.5
250,000 to 300,000	2,410	2.0	-228,100	1.6	-95	23,600	10.2
300,000 to 500,000	2,820	2.3	-225,320	1.6	-80	33,310	8.5
500,000 to 1,000,000	1,020	0.8	-68,210	0.5	-67	17,250	5.9
1,000,000 and over	270	0.2	-17,710	0.1	-66	8,430	3.2
Total	121,693	100.0%	-$14,029,363	100.0%	-$115	3,166,610	3.8%

- An estimated 121,693, or 3.8%, of all tax filers in 2020 would receive a tax decrease under the proposal.
- The total tax decrease is estimated at $14.0 million in tax year 2020.
- For all taxpayers with a tax reduction, the average tax decrease in 2020 would be $115.
- Taxpayers with Wisconsin AGI of less than $100,000 represent 54.5% of the taxpayers with a tax reduction, and they would receive 63.3% of the reduction. Their tax decrease would average $134. Taxpayers with Wisconsin AGI of more than $100,000 represent 45.5% of the taxpayers with a tax reduction, and they would receive 36.7% of the reduction. Their tax decrease would average $93.
- Taxfilers without a tax decrease would include those without an eligible dependent and those who are nonresidents or part-year residents.

Based on a simulation of tax year 2020 by the Wisconsin Department of Revenue.

ATTACHMENT 3

Distribution of Taxpayers Under Proposal to Replace the Personal Exemption for Dependents with a Nonrefundable Child Tax Credit, Tax Year 2020

	Taxpayers Receiving a Tax Decrease					Count	% of All
Wisconsin Adjusted Gross Income	Count	Percent of Count	Amount of Tax Decrease	Percent of Decrease	Average Decrease	of All Returns	Returns in AGI Class
Under $5,000	2,230	0.3%	-$4,460	< 0.1%	-$2	470,550	0.5%
5,000 to 10,000	2,820	0.4	-11,490	0.1	-4	212,390	1.3
10,000 to 15,000	4,560	0.6	-57,750	0.6	-13	184,220	2.5
15,000 to 20,000	15,050	2.1	-385,450	3.7	-26	166,800	9.0
20,000 to 25,000	30,070	4.2	-909,980	8.8	-30	167,290	18.0
25,000 to 30,000	36,810	5.1	-708,270	6.9	-19	165,390	22.3
30,000 to 40,000	78,680	11.0	-1,467,550	14.2	-19	315,400	24.9
40,000 to 50,000	67,470	9.4	-967,470	9.4	-14	260,350	25.9
50,000 to 60,000	55,430	7.7	-664,590	6.5	-12	201,330	27.5
60,000 to 70,000	49,820	7.0	-590,390	5.7	-12	161,740	30.8
70,000 to 80,000	44,780	6.2	-528,840	5.1	-12	126,930	35.3
80,000 to 90,000	42,330	5.9	-500,610	4.9	-12	108,430	39.0
90,000 to 100,000	39,100	5.5	-464,680	4.5	-12	93,510	41.8
100,000 to 125,000	82,920	11.6	-996,400	9.7	-12	178,310	46.5
125,000 to 150,000	59,010	8.2	-720,840	7.0	-12	113,480	52.0
150,000 to 200,000	60,020	8.4	-746,020	7.2	-12	110,470	54.3
200,000 to 250,000	25,880	3.6	-326,010	3.2	-13	47,440	54.6
250,000 to 300,000	12,310	1.7	-157,930	1.5	-13	23,600	52.2
300,000 to 500,000	7,210	1.0	-94,290	0.9	-13	33,320	21.6
500,000 to 1,000,000	--	--	--	--	--	17,250	--
1,000,000 and over	--	--	--	--	--	8,430	--
Total	716,500	100.0%	-$10,303,020	100.0%	-$14	3,166,630	22.6%

- An estimated 716,500, or 22.6%, of all tax filers in 2020 would receive a tax decrease under the proposal.
- The total tax decrease is estimated at $10.3 million in tax year 2020.
- For all taxpayers with a tax reduction, the average tax decrease in 2020 would be $14.
- Taxpayers with Wisconsin AGI of less than $100,000 represent 65.5% of the taxpayers with a tax reduction, and they would receive 70.5% of the reduction. Their tax decrease would average $15. Taxpayers with Wisconsin AGI of more than $100,000 represent 34.5% of the taxpayers with a tax reduction, and they would receive 29.5% of the reduction. Their tax decrease would average $12.
- Taxfilers without a tax decrease would include those without an eligible dependent, those with no tax liability under current law, and those with a tax increase. Although not shown above, about 26,000 taxpayers would experience tax increases totaling an estimated $157,330, or $6 on average.

Based on a simulation of tax year 2020 by the Wisconsin Department of Revenue.

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June, 2019 Joint Committee on Finance Paper #321

Medical Care Insurance Deduction for Self-Employed Persons (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 140, #12]

CURRENT LAW

Under both federal and state law, self-employed persons are entitled to deduct 100% of amounts paid for health insurance for themselves, their spouse, and their dependents to the extent that such premiums do not exceed net earnings from self-employment.

GOVERNOR

Modify the limitation on the deduction under the individual income tax that self-employed persons may claim for medical care insurance for themselves, their spouse, and their dependents. Beginning in tax year 2020, sunset the current law provisions that limit the deduction for all persons to the person's aggregate net earnings from a trade or business that are subject to Wisconsin tax and, instead, limit the deduction to the person's aggregate wages, salary, tips, unearned income, and net earnings from a trade or business that are subject to Wisconsin tax.

Beginning in tax year 2020, sunset the current law provisions that prorate the deduction for nonresidents and part-year residents based on the percentage of the person's net trade or business earnings that are subject to Wisconsin tax relative to the person's total net trade or business earnings and, instead, prorate the deduction based on the percentage of the person's wages, salary, tips, unearned income, and net trade or business earnings that are subject to Wisconsin tax relative to the person's wages, salary, tips, unearned income, and total net trade or business earnings. Relative to the proration, specify for married persons filing separately that “wages, salary, tips, unearned income, and net earnings from a trade or business" means the separate wages, salary, tips, unearned income, and net earnings from a trade or business of each spouse, and specify for married persons filing jointly that “wages, salary, tips, unearned income, and net earnings from a trade or business" means the total wages, salary, tips, unearned income, and net earnings from a trade or business of both spouses.

Repeal obsolete provisions regarding medical care insurance deductions that were sunset in prior tax years (originally, these provisions were sunset, rather than repealed, to allow taxpayers to file amended returns). Remove cross-references to repealed medical care insurance deductions under the itemized deduction credit. Reduce individual income tax collections by an estimated $9,500,000 in 2020-21. The reduction is estimated at $9,100,000 annually in subsequent years.

DISCUSSION POINTS

1. Federal adjusted gross income (AGI) is the starting point for calculating Wisconsin individual income taxes. When determining Wisconsin AGI, differences between the federal and state definitions of income become adjustments to federal AGI. Under both federal and state law, self-employed persons are entitled to deduct 100% of amounts paid for health insurance for themselves, their spouse, and their dependents, to the extent that such premiums do not exceed net earnings from self-employment.

2. Because Wisconsin has adopted the federal definition of income in most instances, Wisconsin does not generally authorize deductions for expenses which are the subject of federal deductions unless there is a difference between the state and federal treatments. For federal tax purposes, insurance plans of self-employed individuals must be established under the business, although if the individual is in a partnership or is more than a 2% stakeholder in a S corporation, the policy can be either in the name of the individual or the business. In the latter case, either the individual or the business may pay the premiums. However, if the individual pays the premiums, the business must reimburse the individual and report the premiums as guaranteed payments in the case of partnerships or as wages in the case of S corporations. The Wisconsin deduction is not limited in the preceding ways and simply allows self-employed individuals to deduct amounts paid for medical care insurance. Self-employed individuals claiming the state deduction must reduce the amount claimed for state tax purposes by the amount claimed under the federal deduction.

3. Both the federal and state deductions limit the amount that a self-employed individual may deduct to the net earnings or net profits from the business. For federal purposes, the net profit from the business must be reduced by amounts deducted as payments to a SEP, SIMPLE, or other retirement plan authorized for use by small businesses, but this reduction is not required for Wisconsin tax purposes. The Governor's proposal would lessen the limitation on the state individual income tax deduction for health insurance payments made by self-employed persons by allowing the deduction to offset most types of other income subject to the state individual income tax.

4. Self-employed individuals who are under the age of 65 may purchase nongroup health insurance through one of the marketplaces established under the Affordable Care Act or through an organization outside those marketplaces. For 2018, the Congressional Budget Office (CBO) estimates that 244 million noninstitutionalized civilians under the age of 65 in the United States had health insurance, including 15 million individuals with nongroup health insurance coverage (6%). Almost two-thirds of the insured population had employment-based health insurance. Employer spending on

employer-sponsored health insurance premiums is not subject to tax. The employer contribution is not considered taxable income of the employee and is a deductible business receipt of the employer. Further, any portion of the premium that is the responsibility of the employee may be paid with pre-tax income if the employer has established a "cafeteria plan" under Section 125 of the Internal Revenue Code. The National Bureau of Economic Research reports that such plans are available to 80% of the employees with an employer-sponsored health plan.

5. Three additional deductions are allowed under the Wisconsin state income tax for health insurance premium payments. These deductions extend to payments by individuals: (a) who are employees not covered by employer-provided medical insurance; (b) who have no employer and no self-employment income; and (c) who have insurance through their employment but their employer does not pay the entire premium. These deductions are authorized without limitation, except for reasonable limitations, such as not allowing the same expense to be deducted more than once and not allowing expenses that were not paid by the claimant.

6. DOA's Budget in Brief, 2019-21 notes that the proposed modification is intended to "help self-employed individuals better afford health insurance." It goes on to state that the proposed modification would be particularly helpful to individuals who are starting a small business and working another job as the business becomes established.

7. In a 2018 report on federal subsidies for health insurance coverage, the CBO estimated that 29 million, or 11.3%, of all noninstitutionalized civilians under the age of 65 were uninsured. Data on health insurance status by employer firm size is included in the U.S. Census Bureau's Current Population Survey and reports that, among the 17 million employed individuals between the ages of 18 and 64 who were uninsured, 55.8% were employed at firms with fewer than 25 employees, and workers at these firms were more than two and a half times as likely to be uninsured as workers employed at larger firms.

8. A nonemployer business is a business that has no paid employees. The U.S. Small Business Administration (SBA) reports that nonemployer businesses comprise 80% of all businesses, and income from some other source is the primary income for over 60% of the owners of nonemployer businesses. While the SBA classifies any business with fewer than 500 employees as a small business, almost 90% of small business startups have one to four employees in their first year. Only 78.5% of small businesses survive their first year, with the survival rate dropping to 67.2% at two years, 59.4% at three years, 53.3% at four years, and 48.2% at five years. At the end of ten years, only 33.5% of small business startups are still operating. Despite these survival rates, the small business startup rate has exceeded the small business exit rate over the 11-year period between 2004 and 2014, except for the three years coinciding with the recession from 2007 to 2009. Between 2000 and 2017, small businesses accounted for 66% of the country's net new jobs.

9. The SBA indicates that 57% of new businesses utilize the owner's personal savings as startup capital and 17% use other forms of self-financing, including personal credit cards, home equity loans, and other personal assets. Bank loans and business loans provide startup capital to 10% of new businesses, and over 20% of new businesses begin with no startup capital. These are largely nonemployer firms. Over 43% of employer firms used over $25,000 in startup capital, compared to only 12% of nonemployer firms. New business' use of self-financing may demonstrate that they have

not yet generated the earnings needed to finance the business venture, nor might they have the taxable business earnings to fully deduct the cost of health insurance with only those earnings.

10. If the Committee believes the state limitation on the deduction for medical care insurance for self-employed persons should be lessened sooner, the Governor's proposal could be modified to take effect in tax year 2019 (Alternative 2). This action would have the effect of reducing state individual income tax collections by an additional $9.1 million compared to the bill. The estimated reduction would equal $9,500,000 in 2019-20 and $9,100,000 in 2020-21. The ongoing reduction is less than in the initial year due to a one-time effect. If the Committee does not believe the limitation should be lessened, it may want to retain that part of the Governor's proposal that repeals obsolete provisions regarding medical care deductions that were sunset in prior tax years (Alternative 3).

ALTERNATIVES

1. Approve the Governor's proposal to modify the limitation on the deduction under the individual income tax that self-employed persons may claim for medical care insurance for themselves, their spouse, and their dependents, beginning in tax year 2020. Repeal obsolete provisions regarding medical care insurance deductions that were sunset in prior tax years. Remove cross-references to repealed medical care insurance deductions under the itemized deduction credit. Reduce individual income tax collections by an estimated $9,500,000 in 2020-21.

ALT 1	**Change to**	
	Base	**Bill**
GPR-Tax	-$9,500,000	$0

2. Modify the Governor's proposal to modify the limitation on the deduction under the individual income tax that self-employed persons may claim for medical care insurance by making the modification effective beginning in tax year 2019. Reduce individual income tax collections by an estimated $9,500,000 in 2019-20 and by $9,100,000 in 2020-21. Compared to the bill, this alternative reduces tax collections by an additional $9,100,000.

ALT 2	**Change to**	
	Base	**Bill**
GPR-Tax	-$18,600,000	- $9,100,000

3. Delete the Governor's proposal to modify the limitation on the deduction under the individual income tax that self-employed persons may claim for medical care insurance, beginning in tax year 2020. However, retain those parts of the proposal repealing obsolete provisions regarding medical care insurance deductions that were sunset in prior tax years and removing cross-references to repealed medical care insurance deductions under the itemized deduction credit. Compared to current law, there would be no change in individual income tax collections. Compared to the bill, individual income tax collections would be higher by an estimated $9,500,000 in 2020-21.

ALT 3	Change to	
	Base	Bill
GPR-Tax	$0	$9,500,000

4. Take no action.

ALT 4	Change to	
	Base	Bill
GPR-Tax	$0	$9,500,000

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June, 2019 | Joint Committee on Finance | Paper #322

Net Operating Loss Carrybacks
(General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 140, #13]

CURRENT LAW

Under the individual income tax, taxpayers may carry back net operating losses for two tax years and may carry forward net operating losses for up to 20 years.

GOVERNOR

Repeal current law provisions under the individual income tax that allow net operating losses to be carried back for two tax years as an adjustment to federal adjusted gross income (AGI), beginning in tax year 2019. Increase individual income tax collections by an estimated $2,000,000 in 2019-20, $4,100,000 in 2020-21, and $2,000,000 in 2021-22 and 2022-23.

DISCUSSION POINTS

1. Generally, a net operating loss (NOL) results when a taxpayer's business deductions exceed the taxpayer's gross income. A NOL deduction for a tax year may not exceed the amount of the taxpayer's taxable income. However, the taxpayer may carry back or carry forward the amount of the unused deduction to other tax years offsetting taxable income in those years. Under the state individual income tax, the carryback period is two years, and the carryforward period is 20 years. NOL carrybacks are claimed on a separate tax form and typically require the taxpayer to file an amended return.

2. Several reasons exist to allow businesses to carry NOLs into different tax years. Accounting for losses in a single tax year may not accurately reflect a business's overall profitability.

For example, many businesses, such as new businesses and capital intensive industries, are subject to wide fluctuations in earnings year over year, especially when expanding into new products and services. In addition, income for a single business may differ year-to-year for various reasons, such as the business cycle, natural disasters, or energy price fluctuations, and not allowing otherwise deductible expenses to be used in a different tax year may overweigh the importance of profitable years compared to years having losses. Carrying a loss to another tax year can reduce the impact the income tax may have on investment decisions and provide fairer tax treatment across different types of businesses over a multi-year period.

3. Wisconsin adopted its individual income tax treatment of NOLs in 2013 Wisconsin Act 20 in order to mirror federal NOL treatment. However, Wisconsin's NOL treatment no longer mirrors federal NOL treatment due to changes made in the federal Tax Cuts and Jobs Act (P.L. 115-97), adopted in 2017. The federal Act eliminated the carryback allowance in most instances for NOLs occurring in tax years ending after 2017. Also, the federal Act eliminated the 20-year carryforward limitation, thereby allowing NOLs arising after 2017 to be carried forward indefinitely. The federal Act limits the amount of a carryforward NOL that may be deducted in a tax year to 80% of taxable income.

4. One reason not to adopt the federal carryforward treatment is that businesses experiencing large losses in a given year would experience a tax increase, compared to current law, if the business were limited in the amount of NOL it could use to offset taxable income in each year. Conversely, the number of years over which NOLs can be claimed is unlimited, and could extend well beyond the normal business cycle. In addition, Wisconsin cannot fully federalize its treatment of NOLs because Wisconsin taxable income has adjustments to the federal definition of income, which may result in differing loss amounts. Taxpayers with operations in Wisconsin and in another state may have different losses for federal tax purposes than for Wisconsin tax purposes.

5. Eliminating the two-year carryback under the individual income tax would make the tax treatment of business losses comparable to treatment under the corporate income/franchise tax. Under the state corporate income/franchise tax, a net business loss may be carried forward and used to offset income for the following 20 years. State law does not allow net business losses to be carried back under the corporate income/franchise tax.

6. Another reason to eliminate the two-year carryback of NOLs is administrative simplicity. To claim a NOL carryback, taxpayers must file a separate tax form, Form X-NOL. Because the NOL carryback may affect the taxpayer's adjustments to income or tax credits claimed in the carryback year, taxpayers may be required to file amended returns for the affected years.

7. NOL carrybacks generally result in the Department of Revenue issuing refunds to taxpayers, thereby allowing taxpayers to procure refunds they would not otherwise be able to claim in the current year. As a result, eliminating NOL carrybacks would delay taxpayers realizing a tax benefit. However, because taxpayers with business income generally make estimated tax payments, taxpayers with NOLs can adjust their estimated payments to realize the benefit of the NOL carryforward.

8. The Committee could find that allowing losses to be carried forward adequately

addresses the policy rationales listed above and that it is unnecessary and administratively burdensome to allow taxpayers to carry back losses into previous tax years (Alternative 1). By not allowing taxpayers to realize refunds in the current year, this provision would increase individual income tax collections by an estimated $2,000,000 in 2019-20, $4,100,000 in 2020-21, and $2,000,000 in 2021-22 and 2022-23. This provision would not affect current law provisions that allow taxpayers to carry forward net operating losses for up to 20 years. As a result, individual income tax collections would be reduced in future years, as NOLs that could no longer be carried back, instead, would be carried forward. Over time, the revenue gain due to the elimination of loss carrybacks would be offset by the revenue loss due to larger amounts of loss carry forwards.

9. However, carrybacks are more valuable than carryforwards due to the time value of money. Generally, the value of a NOL carryforward should be discounted to account for the uncertainty of when (or if) a business would have taxable income to be offset in the future. By contrast, a carryback may be taken immediately. Allowing net operating losses to be carried back into previous tax years can also provide relief for businesses in periods in which taxable income in current and future years is likely to decrease or decline entirely into a loss, such as a recession or a natural disaster.

10. Last year, this office reviewed the treatment of losses among states with a corporate income/franchise tax. For tax year 2018, eight states allowed losses to be carried back for two years, and one state allowed a three-year carryback. The remaining 35 states and the District of Columbia did not allow NOL carrybacks, including Wisconsin. If the Committee were to amend the bill to, instead, allow losses to be carried back for corporate filers, Wisconsin would be one of ten states to allow loss carrybacks.

11. The Committee could find it beneficial to align the treatment of losses under state law for both the individual income tax and the corporate income/franchise tax by providing for the carryback of losses for two tax years under the corporate income/franchise tax beginning in tax year 2019 (Alternative 2). As discussed, the principal effect of allowing a loss to be carried back is not to increase the overall amount of deductions, but rather to change the timing of when they are claimed. The fiscal effect would be from shifting deductions from future years for use as an immediate tax refund. It is estimated that Alternative 2 would reduce tax revenues by $107,600,000 GPR-Tax and $636,000 SEG-REV in 2019-20 and $69,100,000 GPR-Tax and $409,000 SEG-REV in 2020-21. The loss of tax revenue would decrease to $51,500,000 GPR-Tax and $305,000 SEG-REV in 2021-22 and the annual fiscal effect would continue to decrease thereafter. The segregated revenue is the economic development surcharge imposed upon C corporations and tax-option (S) corporations, the proceeds of which are deposited into the economic development fund and pay for the programs and operations of the Wisconsin Economic Development Corporation (WEDC).

12. However, Alternative 2 would further distance state law from the treatment of losses under federal law.

13. Under current law, the primary source of WEDC's funding is from the segregated economic development fund. In addition, WEDC receives a sum sufficient GPR appropriation that is capped at $16,512,500, annually. If the Committee chose to adopt Alternative 2, estimated expenditures from WEDC's SEG appropriation would decrease by $636,000 in 2019-20 and $409,000 in 2020-21. Estimated GPR expenditures would increase by the same amount.

ALTERNATIVES

1. Approve the Governor's recommendation to repeal current law provisions under the individual income tax that allow net operating losses to be carried back for two tax years as an adjustment to federal AGI, beginning in tax year 2019. Compared to current law, this provision would increase individual income tax collections by an estimated $2,000,000 in 2019-20 and $4,100,000 in 2020-21.

ALT 1	Change to Base	Change to Bill
GPR-Tax	$6,100,000	$0

2. Instead of the Governor's recommendation, modify current law to allow claimants under the corporate income/franchise tax to carryback net business losses for two tax years, beginning in tax year 2019. Compared to current law, reduce estimated corporate income/franchise tax collections by $107,600,000 in 2019-20 and $69,100,000 in 2020-21. Reduce estimated economic development surcharge revenues by $636,000 SEG-REV in 2019-20 and $409,000 SEG-REV in 2020-21. Reduce estimated expenditures in WEDC's SEG appropriation from the economic development fund for operations and programs by $636,000 in 2019-20 and $409,000 in 2020-21, and increase estimated expenditures in WEDC's sum sufficient GPR appropriation for operations and programs by the same amount.

ALT 2	Change to Base	Change to Bill
General Fund Taxes		
GPR-Tax	- $176,700,000	- $182,800,000
SEG-REV	-1,045,000	-1,045,000
WEDC		
GPR	$1,045,000	$1,045,000
SEG	-1,045,000	-1,045,000

3. Take no action.

ALT 2	Change to Base	Change to Bill
GPR-Tax	$0	- $6,100,000

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June, 2019 Joint Committee on Finance Paper #323

First-Time Home Buyer Savings Accounts
(General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 141, #14]

CURRENT LAW

There are several steps required to calculate state income tax liability for tax year 2019. They include: (a) determining Wisconsin adjusted gross income (AGI); (b) subtracting the state standard deduction and personal exemptions to arrive at Wisconsin taxable income; (c) applying the state's tax rate and bracket schedule to determine gross tax amount; and (d) subtracting any applicable state tax credits. Under the first step, Wisconsin AGI is determined by making adjustments to federal AGI, which reflect differences between the state and federal tax codes. These adjustments can be expressed either as additions to or subtractions from federal AGI.

GOVERNOR

Create a program administered by the Department of Revenue (DOR) allowing an individual to become an account holder by creating an account, either individually or jointly with his or her spouse, to pay or reimburse the eligible costs of a first-time home buyer. Require the accounts to be created at any financial institution, defined as any bank, trust company, savings institution, savings bank, savings and loan association, industrial loan association, consumer finance company, credit union, or any benefit association, insurance company, safe deposit company, money market mutual fund, or similar entity authorized to do business in Wisconsin. Specify that eligible costs mean the down payment and allowable closing costs, defined as disbursements listed in a settlement statement for the purchase of a single-family residence in Wisconsin by an account owner or beneficiary. Limit the program to individuals who reside in Wisconsin and have not owned or purchased, either individually or jointly, a single-family residence, defined as a residence intended for the occupation by a single family unit that is owned and occupied by a beneficiary as his or her principal residence, including a manufactured home, residential trailer, mobile home, condominium unit, or cooperative, during the 36 month period prior to the purchase of a single-family residence that is located in Wisconsin.

When an account is created, require the account holder to designate a single account beneficiary who is a first-time home buyer and who may be the account holder. Allow the account holder to change the beneficiary at any time. Allow individuals to jointly own accounts with their spouses. Provide that an individual may be the account holder of more than one account, but prohibit the account holder from having more than one account that designates the same beneficiary. Permit an individual to be the beneficiary of more than one account. Limit account contributions to cash and marketable securities and allow persons other than account holders to contribute to accounts.

Authorize account holders to withdraw funds from accounts to pay eligible costs for the benefit of the beneficiary or to reimburse the beneficiary for eligible costs that the beneficiary incurred and paid. Prohibit account holders from using account funds to pay any expenses incurred by the account holder in administering the account, but permit financial institutions to deduct service fees from accounts. Require account holders each year to submit the following information related to the account to DOR on forms prepared by the Department with the account holder's income tax return: (a) a list of account transactions during the tax year, including the account's beginning and ending balances; (b) the 1099 form issued by the financial institution relating to the account; and (c) a list of eligible costs, and other costs, for which account funds were withdrawn during the tax year. Authorize account holders to withdraw and transfer funds to a different financial institution without incurring a withdrawal penalty or affecting the account holder's Wisconsin AGI if the transfer occurs immediately and the funds are deposited in a first-time home buyer savings account at that institution. Require account holders to dissolve an account not later than 120 months (10 years) after its creation, and require financial institutions to distribute any proceeds in dissolved accounts to the account holder. Require proceeds be distributed to the account holder's estate if the account holder dies while funds remain in the account.

Create the following adjustments to federal AGI when calculating Wisconsin AGI under the state individual income tax. Require account holders to increase their AGI to include any distribution of proceeds from a dissolved account, and require account holders' estates to increase the AGI of the estate to include any distribution to an account holder's estate after the death of an account holder. In addition, require account holders to increase their AGI to reflect any amount withdrawn from an account for any reason other than payment or reimbursement of eligible costs, unless the withdrawal is the result of a transfer to an account at a different financial institution, as described above, or unless the disbursement is pursuant to a filing for bankruptcy protection. Impose a penalty of 10% on the amounts added to federal AGI under the preceding provisions. Authorize account holders to subtract from federal AGI the amount of any deposits into their accounts, as well as any interest, dividends, or other gain accruing in the account if the interest, dividends, or other gain is redeposited into the account. Limit the subtraction for each account holder to $5,000 per year, or $10,000 if the account holder is a married joint filer, for each account to which the account holder makes a deposit. Limit the total amount subtracted to $50,000 of deposits per account for each beneficiary.

For federal tax purposes, no deduction for contributions would be allowed and the interest earnings accruing to accounts would be subject to tax. Since the accounts would be taxable on the "front end," no federal tax would be imposed at the time of withdrawal. Nor would withdrawals trigger a state tax, provided the proceeds would be used for eligible costs.

Require DOR to prepare and distribute any forms that an account holder is required to submit and any other forms that the Department believes are necessary to administer the program and the program's adjustments to income, as described above. In addition, require DOR to prepare and distribute informational materials to financial institutions and potential home buyers. Finally, require DOR to impose a penalty on withdrawals from accounts that are additions to income, as described above, and direct the Department to administer the penalty as it assesses, levies, and collects income and franchise taxes.

The preceding provisions would apply beginning in tax year 2020. Reduce individual income tax collections by an estimated $4,100,000 in 2020-21. The reduction is estimated at $6,200,000 in 2021-22 and $7,500,000 in 2022-23.

DISCUSSION POINTS

1. According to the Wisconsin Realtors Association, at least nine states have first-time home buyer savings accounts, including Iowa and Minnesota. While the programs differ from state to state, state tax benefits are a feature of each state's program. The Budget in Brief indicates that the Governor's proposal is intended to address concerns regarding housing affordability by providing "an incentive for prospective homeowners to build savings for a down payment and eligible closing costs" for the purchase of a first home.

2. Concerns about housing affordability have been prompted by a decline in the home ownership rate, defined as the number of owner-occupied housing units as a percentage of total occupied housing units. The U.S. home ownership rate peaked in 2004 at 69.0%, the same year that Wisconsin's rate peaked at 73.3%. After 2004, both rates declined over a multi-year period, with Wisconsin's home ownership rate reaching its nadir in 2015 at 66.6%, one year before the U.S. rate reached 63.4% in 2016. Since then, the U.S. home ownership rate has risen one percentage point to 64.4% in 2018, but has been outpaced by the Wisconsin rate, which improved to 67.9%, albeit over three years instead of two. Table 1 reports the change in the two rates since 1985.

TABLE 1

Homeownership Rate, U.S. and Wisconsin:
1985 - 2018

Year	U.S.	Wisconsin
1985	63.9%	63.8%
1990	63.9	68.3
1995	64.7	67.5
2000	67.4	71.8
2005	68.9	71.1
2010	66.9	71.0
2015	63.7	66.6
2018	64.4	67.9

Source: U.S. Census Bureau, Current Population Survey/Housing Vacancy Survey.

3. The 2004 peak in the homeownership rate was attributable, in part, to the housing bubble, and the bursting of the bubble precipitated the worst national economic downturn since the Great Depression. Although the housing market's recovery from the 2007-2009 recession has been slow, it could be argued that homeownership rates have returned to their natural levels. The 2018 home ownership rates for the U.S. and Wisconsin are comparable to the rates that occurred between 1985 and 1995, and a 2016 report in the housing Market Perspectives series of the Federal Reserve Bank of St. Louis notes, "Prior to the 1990s, the homeownership rate had fluctuated for three decades in a narrow band between 63 and 66 percent. This still might be the range to expect in the future."

4. To protect against a similar economic downturn in the future, a variety of safeguards have been implemented, including many affecting residential lending practices. These include more rigorous verification of borrowers' income and assets, oversight of credit rating agencies, lower loan to value ratios for home mortgages, regulations related to real estate appraisals, and fewer subprime mortgages. In addition, the Federal Reserve performs stress tests on banks and imposes capital reserve requirements based on a bank's loan portfolio. While intended to enhance the nation's economic security, the additional regulation has had some negative effects, such as hampering community banks' ability to be responsive to their community's needs and the inability of non-traditional borrowers to secure loans.

5. The safeguards implemented after the recession may disproportionately impact first-time home buyers. A proxy for this group could be individuals who are 35 years of age or younger because most individuals who become homeowners do so before they reach middle age. The homeownership data maintained by the U.S. Census Bureau includes data on homeownership rates by age category. Table 2 reports home ownership rates by age category for the nation as a whole between 1985 and 2018. During this period, the homeownership rate decreased for each of the age groups displayed, except for homeowners in the 65 years and over group. Between 2005 and 2018, the homeownership rate decreased for each of the age groups, as well as for the nation as a whole. The decrease for the under 35 age group (-15.8%) was greater than for any other age group and more

than twice the rate of decrease for the nation as a whole (-6.5%). Since 2015, the homeownership rate has increased for the under 35 and the 35 to 44 age groups, while remaining stable for the other age groups.

TABLE 2

Homeownership Rates by Age of Homeowner, United States: 1985 to 2018

Year	Under 35	35 to 44	45 to 54	55 to 64	65 and Over
1985	39.9%	68.1%	75.9%	79.5%	74.8%
1990	38.5	66.3	75.2	79.3	76.3
1995	38.6	65.2	75.2	79.5	78.1
2000	40.8	67.9	76.5	80.3	80.4
2005	43.0	69.3	76.6	81.2	80.6
2010	39.1	65.0	73.5	79.0	80.5
2015	35.0	58.5	70.0	75.4	78.9
2018	36.2	60.1	70.1	75.4	78.5
Change					
2005 to 2018	-15.8%	-13.3%	-8.5%	-7.1%	-2.6%
2010 to 2018	-7.4	-7.5	-4.6	-4.6	-2.5
2015 to 2018	3.4	2.7	0.1	0.0	-0.5

6. Some of the decrease in homeownership rates may relate to housing affordability, which can be gauged by comparing the change in per capita income, as determined by the U.S. Department of Commerce, Bureau of Economic Analysis (BEA), to the house price index, as determined by the Federal Housing Finance Authority (FHFA). The index measures average price changes in repeat sales or refinancings on the same properties, based on properties whose mortgages have been purchased or secured by Fannie Mae (Federal National Mortgage Association) or Freddie Mac (Federal Home Loan Mortgage Corporation). Both the BEA and FHFA maintain data specific to Wisconsin. For the 23-year period between 1995 and 2018, the average per capita income in Wisconsin has grown slightly faster than Wisconsin housing values, and the two rates of change between 2010 and 2018 are almost identical. However since 2015 when Wisconsin's homeownership rate reached its post-recession low point, the average rate of growth in Wisconsin's house price index (6.3%) is more than double the rate of growth in Wisconsin's per capita personal income (2.9%), indicating that Wisconsin housing has become less affordable over this period. These data are displayed in Table 3.

TABLE 3

Average Rate of Change in Wisconsin Per Capita Personal Income and Wisconsin House Price Index for Select Periods Ending in 2018

Period Beginning	Per Capita Personal Income	House Price Index
1995 (23-yr. avg.)	3.5%	3.0%
2000 (18-yr. avg.)	3.0	2.6
2005 (13-yr. avg.)	3.0	1.3
2010 (8-yr. avg.)	3.4	3.3
2015 (3-yr. avg.)	2.9	6.3

7. One reason to provide assistance to first-time homebuyers is due to their importance to the residential real estate market. Without buyers for entry-level homes, owners of those homes are unable to "move up" in the market. The National Association of Realtors has conducted a survey of homebuyers since 1981 and reports that first-time homebuyers have historically comprised nearly 40% of the purchases of homes to be used as the buyer's primary residence. In 2015, sales to first-time homebuyers equaled 32% of sales, the second lowest percentage in the survey's history. The percentage of sales to first-time buyers climbed to 35% in 2016, but has declined in each of the two subsequent years, totaling only 33% in 2018.

8. Recent increases in home appreciation rates and higher loan-to-value requirements since the recession have combined to make the down payment a constraint for many first-time homebuyers. Other contributing factors, such as "burdensome student loans and rising rents," as noted in a 2015 Urban Institute report, "A Closer Look at the Data on First-Time Homebuyers," also make saving for a down payment more difficult. Based on an examination of debt levels of young adults between the ages of 24 and 32 from 2005 to 2014, a U.S. Federal Reserve System report concludes that 20% of the decrease in the young adult homeownership rate is due to student loan debt. The report indicates that the average real per capita student loan debt doubled between 2005 and 2014.

9. The proposed first-time homebuyer accounts would help prospective buyers overcome these obstacles and accumulate a down payment. It would allow individuals seeking to enter the housing market to establish a first-time home buyer account at a financial institution and make contributions to the account which would be deductible for state tax purposes. Also, account earnings would not be subject to state tax. Contributions would be limited to no more than $5,000 per year for each account holder, or $10,000 if the account holder is a married joint filer. Under these adjustments, account holders would be prohibited from subtracting more than $50,000 per account. Accounts would be permitted to exist for up to ten years after their creation.

10. Because contributions would not be deductible for federal tax purposes and account earnings would be subject to federal tax, the two state tax treatments would occur as subtractions to federal AGI on state tax forms. Also, disbursements from dissolved accounts and amounts withdrawn from accounts for any reason other than for the payment or reimbursement of eligible costs would be

reported on state tax forms as additions to federal AGI. The proposed state tax treatments are estimated to decrease individual income tax collections by $4.1 million in 2020-21. This assumes that over 8,000 tax filers would claim deductions averaging $7,850 and totaling $66.0 million in tax year 2020. The tax benefit per file would average $492. As more prospective buyers open accounts and make deductible contributions, the statewide tax decrease is estimated to increase to $6.2 million in 2021-22 and $7.5 million in 2022-23.

11. If the Committee prefers a smaller state tax reduction, lower contribution limits could be specified. For example, if the annual contribution limits were set at $3,750 and $7,500 for married joint filers, a 2020-21 decrease in individual income tax collections estimated at $3.1 million would result, $1.0 million less than under the Governor's proposal. If the contribution limits were set at $2,500 and $5,000, a 2020-21 decrease in individual income tax collections estimated at $2.1 million would result, $2.0 less than under the Governor's proposal. The estimated average tax benefit would decrease from $492 under the Governor to $369 and $246, respectively under these alternatives. These alternatives are presented as Alternatives 2.a. and 2.b.

12. Another option would be to remove the deduction for account contributions and limit the state tax benefit to the exclusion for account earnings. Under this option, accounts would operate similarly to Roth IRA and 401k plans, but without the federal tax benefits. An argument against this approach is that one of the barriers that first-time homebuyers face is difficulty saving for a down payment. Consequently, the deduction for contributions under the Governor's proposal address this issue. Nonetheless, if the Committee prefers a Roth-styled approach for first-time homebuyer accounts, the deduction for contributions could be removed, increasing individual income tax collections by an estimated $4.1 million relative to the bill. This is presented as Alternative 3.

13. The proposal's fiscal effect indicates that a larger decrease in state tax collections in the 2021-23 biennium than in the 2019-21 biennium. The program is not likely to be fully phased-in for five to ten years, when the number of newly created accounts is offset by the number of dissolved accounts. If the Committee is concerned about the potential long-term impact of the proposal, the $50,000 limitation on tax-preferred deposits could be reduced. An account with a $50,000 balance could provide a 20% down payment on a home with a $250,000 selling price. This is considerably higher than the 2018 median sales price of $184,000 reported by the Wisconsin Realtors Association (WRA). However, home prices vary considerably based on location, and WRA reports that 2018 median sale prices ranged from $155,000 for 18 counties in northern Wisconsin to $226,500 for the 12 counties in south central Wisconsin.

14. A 20% down payment is a goal for many buyers because a down payment at that level eliminates the requirement for private mortgage insurance (PMI), which protects the lender against foreclosure. PMI premiums typically increase a homeowner's mortgage payment by $30 to $70 per month for every $100,000 borrowed. If a buyer is willing to incur that cost, conventional mortgages are available in the private sector with down payments of less than 20%. In addition, a 3.5% down payment is available to an eligible buyer under the Federal Housing Authority (FHA) mortgage program. Alternative 4 would lower the proposed limitation on tax-preferred deposits from $50,000 to $30,000, although the Committee could set the limit at another level. Adopting this alternative would not immediately affect the proposal's fiscal estimate, but would reduce the proposal's fiscal

effect in future years.

ALTERNATIVES

1. Approve the Governor's proposal to create a first-time homebuyer savings account program, beginning in tax year 2020. Reduce individual income tax collections by an estimated $4,100,000 in 2020-21.

ALT 1	Change to Base	Bill
GPR-Tax	- $4,100,000	$0

2. Modify the Governor's proposal to create a first-time home buyer savings account program. Based on the amount deposited in an account, reduce the limit on the annual amount that an account holder may subtract from federal AGI from $5,000, or $10,000 in the case of a joint filer, to either: (a) $3,750, or $7,500 in the case of a joint filer; or (b) $2,500, or $5,000 in the case of a joint filer. Relative to current law, reduce individual income tax collections in 2020-21 by an estimated $3,100,000 under (a) or $2,100,000 under (b). Relative to the bill, increase individual income tax collections by an estimated $1,000,000 under (a) or $2,000,000 under (b).

ALT 2	Change to Base	Bill
a. GPR-Tax	- $3,100,000	$1,000,000
b. GPR-Tax	- 2,100,000	2,000,000

3. Modify the Governor's proposal to create a first-time home buyer savings account program by eliminating the proposed individual income tax subtraction from federal AGI based on the amount that an account holder deposits in a first-time home buyer savings account. The proposed subtraction for interest, dividends, or other gain that accrues and is redeposited to an account would be retained. Modify the proposed addition to federal AGI to apply only to the withdrawal of amounts subject to the remaining subtraction. Increase individual income tax collections in 2020-21 by an estimated $4,100,000, relative to the bill.

ALT 3	Change to Base	Bill
GPR-Tax	$0	$4,100,000

4. Modify the Governor's proposal to create a first-time home buyer savings account program by reducing the limitation on the total amount that may be subtracted from federal AGI from not more than a total of $50,000 of deposits to a total of not more than $30,000 of deposits. This

alternative could be adopted with any of the preceding alternatives, without changing the reported fiscal effect.

5. Take no action. Relative to the bill, increase individual income tax collections in 2020-21 by an estimated $4,100,000.

ALT 5	**Change to**	
	Base	**Bill**
GPR-Tax	$0	$4,100,000

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June, 2019 Joint Committee on Finance Paper #324

Illinois-Wisconsin Reciprocity -- Current Law Sum Sufficient Reestimate (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 143, #17]

CURRENT LAW

Under state individual income tax provisions, income may be taxed on the basis of where it is earned or on the basis of the taxpayer's legal residence. Wisconsin, like most other states with an individual income tax, provides a credit for taxes paid to another state while the taxpayer was a Wisconsin resident in order to prevent double taxation of the same income. In addition, reciprocity agreements may be entered into between two states to reduce the filing requirements of persons who live in one state and work in another state. Under such agreements, the taxpayer is only required to file a return and pay taxes on income from personal services in the state of legal residence. Wisconsin currently has income tax reciprocity agreements with four states: Illinois, Indiana, Kentucky, and Michigan.

The reciprocity agreement with Illinois requires a compensation payment when the net foregone tax revenues of one state exceed those of the other state. Historically, Wisconsin has made a payment to Illinois under the agreement because there are more Wisconsin residents who work in Illinois than Illinois residents who work in Wisconsin. The most recent payment was made in December, 2018, and totaled $93.1 million.

GOVERNOR

Increase the estimated payment by $5,078,000 in 2019-20 and $8,760,000 in 2020-21 under the Illinois-Wisconsin individual income tax reciprocity agreement. Compared to the base funding level of $92,987,000, payments are estimated at $98,065,000 in 2019-20 and $101,747,000 in 2020-21.

MODIFICATION

Reestimate Wisconsin's payments under the Illinois-Wisconsin income tax reciprocity agreement at $102,800,000 in 2019-20 and $102,900,000 in 2020-21. These amounts represent increases of $4,735,000 in 2019-20 and $1,153,000 in 2020-21, relative the amounts in the bill. Compared to the base, the reestimate would increase the payment by $9,813,000 GPR in 2019-20 and $9,913,000 GPR in 2020-21.

Explanation: The reestimates are based on Wisconsin's projected individual income tax collections reported in a memorandum to the Cochairs of the Joint Committee on Finance from this office on May 15, 2019, and Illinois' personal income tax collections reported in the "Revised FY 2020 Revenue Estimate and FY 2019 Revenue Update," released by the Illinois Commission on Government Forecasting and Accountability in May, 2019. The payment amounts represent increases of 10.4% in 2019-20, relative to the actual 2018-19 payment amount, and 0.1% in 2020-21, relative to the 2019-20 reestimate. For the first year's payment, the rate of growth in individual income tax collections is expected to be higher in Illinois than in Wisconsin. However, for the second year's payment, the rate of growth in individual income tax collections is expected to be higher in Wisconsin than in Illinois.

	Change to	
	Base	**Bill**
GPR	$19,726,000	$5,888,000

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June, 2019 Joint Committee on Finance Paper #325

Refundable Research Tax Credit
(General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 147, #28; and Page 148, #29]

CURRENT LAW

A tax credit is an amount that is subtracted from the gross income tax liability of the taxpayer in a given year, resulting in a dollar-for-dollar reduction in gross tax liability. In general, businesses may be eligible to claim a business tax credit when preparing and filing the required individual and corporate income/franchise tax forms with the Department of Revenue (DOR).

If a nonrefundable credit exceeds tax liability, any amounts claimed that cannot be used to offset tax liability are identified so that the taxpayer can carry the unused amount forward for use in a future tax year. In general, unused tax credits may be carried forward for up to 15 years. Conversely, if the credit is refundable and the amount of the credit exceeds the claimant's tax liability, the state issues a check for the excess amount or the claimant may apply the credit against the next year's tax liability. Nonrefundable credits are counted as revenue reductions in the state's accounting system. Refundable credits are paid from appropriations and counted as state expenditures.

The state provides research tax credits to businesses equal to a percentage of the increase in a business's qualified research expenses, as defined under the Internal Revenue Code (IRC), for research conducted in Wisconsin. This includes expenses for wages, supplies, and renting or sharing computers owned and operated by another person. In general, qualifying expenses are non-capital, and thus, do not include spending for buildings and equipment. The credits can be claimed against the individual income tax and the corporate income/franchise tax. For most businesses, the credit equals 5.75% of the amount by which the claimant's qualified research expenses for the taxable year exceed 50% of the average qualified research expenses for the three taxable years immediately preceding the tax year in which the claimant claims the credit. If the taxpayer had no qualified research expenses in any of the three preceding tax years, the credit is equal to 2.875% of the claimant's qualified research expenses for that tax year.

For businesses that engage in certain types of research activities, the same calculation of the credit applies, but the credit percentages are equal to 11.5% (rather than 5.75%) and 5.75% (rather than 2.875%). The higher percentages apply to: (a) designing internal combustion engines (including substitute products such as fuel cell, electric, and hybrid drives) for certain vehicles; and (b) designing and manufacturing energy efficient lighting systems, building automation and control systems, or automotive batteries for use in certain hybrid-electric vehicles.

For taxable years beginning prior to January 1, 2018, the credits were 100% nonrefundable and any unused portion of the credit could be carried forward to offset future tax liabilities for up to 15 years. Pursuant to 2017 Act 59, for taxable years beginning on or after January 1, 2018, the amount of the credit is calculated in the same manner; however, up to 10% of the amount may be claimed as a refundable credit. The refundable portion of the research tax credit is equal to the lesser of 10% of the tax credit claimed in the current year or the credit remaining after subtracting the amount of credit used in the current year to offset the tax owed. Any unused portion of the nonrefundable tax credit may be carried forward for up to 15 years. Unused credits that were carried forward from taxable years beginning prior to January 1, 2018, remain nonrefundable.

GOVERNOR

Modify the partially refundable research tax credit (including the engine and energy efficiency credits), as computed under current law, to increase the refundable portion from up to 10% of the credit amount to up to 20% of the credit amount. The administration estimates that the change would increase expenditures on refundable research tax credits by $2,250,000 in 2020-21 and $9,000,000 in 2021-22 and annually thereafter. The provision would first apply to new research credit claims beginning in tax year 2020. Together with the cost to continue the refundable portion of the research tax credit under current law, total funding provided under the bill would be $7,500,000 in 2019-20 and $11,250,000 in 2020-21. The cost of the refundable portion of the credit is estimated to increase to $18,000,000 in 2021-22 and annually thereafter.

Further, the bill would specify that claimants under the electronics and information technology manufacturing (EITM) zone tax credit program would not be eligible to receive the refundable portion of the research tax credit. The nonrefundable portion of the research tax credit could still be claimed.

DISCUSSION POINTS

Purpose of the Research Tax Credit

1. Technological innovation is an important driver of economic growth and has wide social benefits. Long-run economic growth and improved living standards are driven by the accumulation of knowledge-based factors of production, such as human capital, learning-by-doing, research and development (R&D), and innovation.

2. A number of economists have found that, on average, the social returns to R&D investment exceed the private returns from such investments. For example, John C. Williams and Charles I. Jones, found that the optimal R&D investment is at least twice the actual investment, and possible higher. *Measuring the Social Return to R&D*, Quarterly Journal of Economics, vol. 113, no. 4 at 1119-1135 (Nov 1998).

3. The excess in the social returns to R&D investments compared to the private returns is an external benefit of R&D (spillover effect). Positive externalities or spillovers include reducing the costs of other firms' innovative activities by creating technological knowledge and showing the dead ends in research. In addition, an important part of innovative output is creating new and improved products and services at lower prices.

4. Private sector investment in R&D is likely to fall short of its overall economic and social benefit because a firm will not invest in a project if it knows that it cannot appropriate the potential revenues from that investment. Investment in R&D, and knowledge in general, are not fully appropriable, because once produced, at least part of the research can be obtained at no cost. Once invented, an idea can be imitated by others, although patent protection and delays in the dissemination of new ideas enable the innovator to appropriate a share of revenues from the new idea. If some portion of revenues from the investment is appropriable, the firm will invest only to the level where revenues are sufficient to make the investment profitable. In this case, the firm's investment is based on its private rate of return, which is lower than the social rate of return.

5. Tax credits for qualified research are intended to incent the private sector to increase R&D investments by lowering the after-tax cost of R&D. This is meant to correct for the market's failure to reward firms for the spillover effects that would result from their increased investment. Further, compared to other states, the state research credit may induce researchers to conduct their activities in Wisconsin instead of another location.

Use of Nonrefundable Research Credit

6. As noted, for tax years beginning prior to January 1, 2018, the research tax credit was 100% nonrefundable. It is estimated that a significant amount of the nonrefundable research tax credit went unused each year because the claimants' taxable income was exceeded by the available tax benefits earned.

7. Based on aggregate statistics provided by DOR through tax year 2013 (the most recent year for which they are available) and preliminary tax return data for tax years 2014 and 2015, the amount of research credits claimed under the corporate income/franchise tax grew significantly since tax year 2009. Research credit claims, including credit carryforwards, totaled $129.8 million in tax year 2009, but increased to $451.4 million in tax year 2015 (248% growth over six years). For comparison, the amount of credits used under the corporate income/franchise tax increased from $8.3 million in 2009 to $25.8 million in 2015 (213% growth). Because credit claims grew by more than use of the credit, the overall balance of unused credits grew from $121.6 million in 2009 to $426.1 million in 2015 (250% growth).

8. It is estimated that unused research credits continued to grow to $614.4 million under

the corporate income/franchise tax after tax year 2017.

9. The research credit was not available under the individual income tax until tax year 2013. However, DOR's aggregate statistics through tax year 2017 for the individual income tax shows a similar pattern. The amount of credits claimed increased from $10.7 million in 2013 to $34.0 million in 2017 (219% growth over four years), whereas use of the credits grew from $8.7 million in 2013 to $19.2 million in 2017 (growth of 121%). The balance of unused credits in tax year 2017 was $14.8 million for individual filers.

10. Overall, approximately two-thirds of the amount of new research tax credit claims between tax years 2010 and 2017 were not actually used by taxpayers during that time period. It is estimated that claimants used the research tax credit in the amount of $245.3 million to reduce their tax liability from tax year 2010 through tax year 2017. For comparison, unused, carried-forward credits grew by $507.6 million over that period.

Proposals to Change the Refundable Portion of the Research Tax Credit

11. Because a significant portion of the research tax credit went unused each year, it is likely that the incentive provided by the research tax credit to invest in additional qualified research expenses was significantly reduced.

12. If a firm has no taxable income after accounting for tax benefits, it cannot use a nonrefundable credit in that tax year. If the firm cannot use the credit, additional nonrefundable credits provide no incentive to invest in additional R&D expenses. This is especially the case if the unused credit amount is expected to be carried forward indefinitely.

13. For example, new and expanding firms that heavily invest in R&D may lack profit in the short term because their start-up and expansion costs exceed their revenues. Such firms are not able to rely on the nonrefundable portion of the credit unless and until they realize taxable income in a future tax year.

14. As another example, businesses are more likely to have operating losses during and after a recession. During such times, businesses may be unable to use the research credit simply because they have no profit. Further, as discussed in LFB Paper #322, net operating losses may be carried forward for up to 20 years. Due to the depth of the 2008-09 recession and slow recovery period, some firms carried forward significant losses between tax year 2009 through tax year 2017. The accumulation of unused research tax credit may be partially the result of the use of net operating losses.

15. Due to the time value of money, the value of credits carried forward is discounted to account for the uncertainty of when (or if) the claimant will have taxable income to be offset in the future. Thus, assuming that firms eventually do use the credits they claim, these firms will ultimately realize a reduced value compared to when the credit was initially claimed.

16. Pursuant to Act 59, the research tax credit is partially refundable beginning in tax year 2018. As noted, the refundable portion of the research tax credit is equal to the lesser of 10% of the

tax credit claimed in the current tax year or the credit remaining after subtracting the amount of credit used in the current tax year to offset the tax owed.

17. Even accounting for the recent changes to the research tax credit, it is anticipated that the majority of the credit will not be used in the current tax year. Under current law, based on the above information and including previously unused credits that have carried forward, it is estimated that individual and corporate tax filers will claim $792.4 million in research tax credits in tax year 2019, of which only $48.0 million will be used as nonrefundable tax credits and $9.0 million used as refundable credits.

18. Under current law, if the current trends in claiming and using the research credit were to continue, the amount of unused credit is expected to increase to $879.1 million in tax year 2021.

19. The bill would provide $2,250,000 GPR in 2020-21 to expand the refundable portion of the research tax credit from up to 10% of the credit amount to up to 20% of the credit amount for taxable years beginning after December 31, 2019 (Alternative A1). It is estimated that expenditures would increase to $9,000,000 GPR in 2021-22 and annually thereafter.

20. In the Department of Administration's Budget in Brief, the administration indicates that expansion of the refundable portion of the credit will provide a meaningful incentive for R&D investment by Wisconsin businesses to improve their competitiveness and help develop new products. Further, the administration indicates that the credit is meant to aid start-up companies that do not have tax liability to offset with the nonrefundable portion of the credit.

21. Alternatively, in order to reduce the cost of the proposed expansion, the Committee could expand the credit to up to 15% of the credit amount as opposed to 20% (Alternative A2). It is estimated that expenditures would increase compared to current law by $1,125,000 GPR in 2020-21 and by $4,500,000 GPR in 2021-22 and annually thereafter.

22. On the other hand, the Committee could take no action on the Governor's proposal and instead maintain the refundable portion of the credit at its current amount for two reasons. (Alternative A4).

23. First, the research tax credit is not targeted to any specific type of claimant or research activity. Any business having qualified research expenditures may claim it, regardless of the size or age of the business. Further, the credit is not targeted to certain areas of research that are directed to developing new products in Wisconsin or that are otherwise more likely to generate social or economic value. For example, the credit makes no difference between investments in applied research as opposed to more basic research, even though the latter is much less likely to produce immediate economic returns (and hence businesses are less likely to engage in). As a result, the stated goals of the administration may not be served by increasing the refundable portion of the credit amount.

24. If the Committee seeks to target investment into new start-up firms that conduct research in Wisconsin, it could, instead, provide funding for other tax credit programs or for economic development programs administrated by the Wisconsin Economic Development Corporation (WEDC), such as technology development loans or grants for companies that conduct research

activities in Wisconsin.

25. Second, because approximately two-thirds of the amount of credits claimed over the previous eight tax years has not yet been used, it is likely the case that many claimants would continue to claim more credits than they can use against their taxable income in future years. If that trend continued, the great majority of the expanded refundable portion of the credit would be paid to current claimants, rather than to induce additional research activities. As discussed, the total credit amount is computed based on qualified expenditures in the current year compared to the average expenditures in the three previous years. Thus, claimants may continue to earn credits for approximately half of their research spending simply by maintaining their current R&D expenditures. It follows that many claimants would be able to claim the full refund for 20% of the credit amount without actually increasing their current planned investments into R&D.

26. Finally, the Committee could sunset the refundable portion of the research tax credit beginning in tax year 2020 (Alternative A3). Based on survey data from the National Science Foundation's Business R&D and Innovation Survey for 2016, private sector expenditures for R&D research in Wisconsin were $4,387 million in 2016. Among the 50 states and the District of Columbia, Wisconsin private sector research expenses were 15th highest on a per capita basis. It could be argued the research credits available under current law were already incentivizing private companies to conduct research in Wisconsin, compared to other states, even before enactment of the 10% refundable credit.

27. In the U.S. economy, where barriers to the free flow of information across state borders is essentially nonexistent, encouraging firms to locate R&D in a particular state might not result in economic benefits that are easily confined to the state. *See* Bronwyn H. Hall and Marta Wosinska, *California R&D Tax Credit: Description, History, and Economic Analysis,* Report to the California Council on Science and Technology (1999). Thus, even assuming that the state credit efficiently induces additional investment in the state over and above the level induced by the federal credit, the benefits may not accrue solely in, or at all in, Wisconsin. For example, the intellectual property created due to research activities in Wisconsin may generate income taxable in other states where a firm may locate its factory or headquarters.

28. Further, the efficiency of the credit and to what extent state tax credits for R&D actually cause private sector firms to increase and/or relocate their R&D activities, remains a matter of controversy in economic literature. For example, one study suggests that credits increase in-state R&D investment, but almost exclusively from attracting investment from other states as opposed to causing an overall national increase. Wilson, D. J. *Beggar Thy Neighbor? The In-State, Out-of-State, and Aggregate Effects of R&D Tax Credits*. Review of Economics and Statistics, 91(2), 431–436 (2009). Other surveys of research have found a $1 to $1 increase in R&D expenses from subsidies. Bronwyn H. Hall and John van Reenen, *How Effective Are Fiscal Incentives for R&D? A Review of the Evidence*, working paper 7098 Cambridge, MA: National Bureau of Economic Research (April 1999); *see also* Bronwyn H. Hall and John Van Reenan, *How Effective are Fiscal Incentives for R&D? A Review of the Evidence* (2000).

29. Given that taxpayers in aggregate currently claim more research tax credits than they can use, the Committee could reasonably conclude that it is unnecessary to provide further tax benefits

to companies without taxable income in Wisconsin in the form of refundable credits. It is estimated that sunsetting the refundable portion of the research credit beginning in tax year 2020 would reduce expenditures for credit claims by $2,250,000 in 2020-21 and by $9,000,000 in 2021-22 and annually thereafter.

30. Further, sunsetting the refundable portion of the credit would reduce expenditures in the 2021-23 biennium by an estimated $36,000,000 GPR compared to the bill.

Eligibility for Refundable Research Tax Credit

31. Qualified research expenses eligible for the state research tax credit include in-house and contract research expenses for research conducted in Wisconsin. This includes wages and supplies used in the conduct of qualified research. Under the IRC, qualified research means research expenditures that may be treated as expenses which are undertaken for the purpose of discovering information which: (a) is technological in nature; (b) is intended to be useful in the development of a new or improved business component of the taxpayer; and (c) constitutes elements of a process of experimentation relating to a new or improved function, performance, reliability, or quality.

32. Under current law, in-house research expenses do not include compensation used in computing credits under the development zone program.

33. The bill would prohibit claimants under the EITM zone tax credit program from claiming the refundable portion of the research tax credit (Alternative B1). The nonrefundable portion of the research tax credit could still be claimed.

34. Businesses eligible for credits under the EITM zone tax credit program have already been certified by WEDC to earn up to $2.85 billion in tax credits based on their qualifying for payroll and capital expenditures. This may include wages paid to researchers employed by the claimants that either perform services inside the EITM zone, or perform services outside the zone while in the state for the benefit of the operations within the zone.

35. Given the significant tax incentives already available under the EITM zone program, the administration indicates that providing additional tax incentives for potentially the same expenditures under the refundable research tax credit, such as the wages of researchers, would be unnecessary.

36. However, the Governor's proposal would still permit EITM zone claimants to use the same expenditures under the EITM zone program to claim the nonrefundable portion of the research tax credit. The administration's concern regarding the refundable research tax credit could also apply to the nonrefundable research tax credit.

37. Thus, the Committee could instead modify current law to define qualified research expenses as not including compensation used in computing credits under the EITM zone program (Alternative B2). Under this alternative, EITM zone claimants would be treated similar to claimants under the development zone tax credit program, such that they could not use either the refundable portion or the nonrefundable portion of the research tax credit for wage amounts claimed under the EITM zone tax credit program. Under this alternative, EITM zone claimants would be able to claim

both the refundable and nonrefundable portions of the research tax credit to the extent that their qualified research expenses are not claimed under the EITM zone program.

38. Finally, the Committee could decide that the administration's concerns regarding EITM zone claimants claiming tax credits for the same research expenditures apply to claimants under the enterprise zone and business development tax credit programs, which both award significant refundable credits for wages paid to eligible full-time employees. For example, based on DOR tax return information, it is estimated that had the refundable portion of the research tax credit been available in tax year 2017, at least 27 individuals filers and 15 corporate filers could have claimed both the refundable portion of the research tax credit and either the enterprise zone tax credit or the business development tax credit. Based on data provided by DOR, none of these claimants would have had a net tax liability and the refundable portion of the research tax credit, had it existed at the time, would have been fully refunded. As a result, prohibiting such claimants from claiming research credits for wage amounts used to claim the enterprise zone credit or the business development credit could reduce GPR expenditures and/or increase general fund tax revenues.

39. The Committee could modify the bill to also prohibit claimants of enterprise zone and business development tax credits from claiming the refundable portion of the research tax credit (Alternative B3). This would prevent claimants from claiming refundable tax benefits for the same research expenditure. However, because tax return data for tax year 2018 is not yet available (the first year in which refundable research tax credit is available), the amount of claims that would be prohibited is unknown.

40. Alternatively, similar to Alternative B2, the Committee could instead modify current law to define qualified research expenses as not including the compensation used in computing credits under the business development, EITM zone, and enterprise zone tax credit programs (Alternative B4). Such claimants could claim both the refundable and nonrefundable portions of the credit to the extent that their qualified research expenses are not claimed under these other programs.

ALTERNATIVES

A. Proposal to Increase Refundable Research Credit

1. Approve the Governor's recommendation to expand the refundable portion of the research tax credit from up to 10% to up to 20% of the claimed amount. Increase estimated expenditures related to refundable research credit claims by $2,250,000 GPR in 2020-21.

ALT A1	**Change to**	
	Base	**Bill**
GPR	$2,250,000	$0

2. Approve the Governor's recommendation to expand the refundable portion of the research tax credit, but with the modification to expand the refundable portion from up to 10% to up to 15% of the claimed amount. Increase estimated expenditures related to refundable research credit

claims by $1,125,000 GPR in 2020-21.

ALT A2	Change to Base	Change to Bill
GPR	$1,125,000	- $1,125,000

3. Take no action on the Governor's proposal. Instead, repeal the refundable portion of the research tax credit effective for tax years beginning on January 1, 2020. Reduce estimated expenditures related to refundable research credit claims relative to the bill by $4,500,000 GPR in 2020-21. Relative to current law, estimate reduced expenditures of $2,250,000 GPR in 2020-21.

ALT A3	Change to Base	Change to Bill
GPR	- $2,250,000	- $4,500,000

4. Take no action.

ALT A4	Change to Base	Change to Bill
GPR	$0	- $2,250,000

B. Eligibility for Refundable Research Tax Credit

1. Adopt the Governor's proposal and specify that claimants under the EITM zone tax credit program would not be eligible to receive the refundable portion of the research tax credit. The nonrefundable portion of the research tax credit could still be claimed.

2. Specify that for purposes of both the refundable and nonrefundable portions of the research tax credit that qualified research expenses do not include compensation used in computing credits under the EITM zone program.

3. Adopt Alternative B1, with the modification to specify that claimants under the enterprise zone and business development tax credit programs would also not be eligible to receive the refundable portion of the research tax credit. The nonrefundable portion of the research tax credit could still be claimed.

4. Adopt Alternative B2, with the modification to specify that qualified research expenses do not include compensation used in computing credits under the enterprise zone and business development tax credit programs.

5. Take no action.

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June, 2019 | Joint Committee on Finance | Paper #326

WEDC Tax Credits and Other Economic Development Awards and Reporting Requirements (General Fund Taxes -- Income and Franchise Tax)

[LFB 2019-21 Budget Summary: Page 145, #22; Page 146, #25; and Page 454, #13]

CURRENT LAW

The Wisconsin Economic Development Corporation (WEDC) is a public-private entity created under state law as the state's lead authority in promoting economic development. The WEDC Board of Directors (Board) is required to: (a) develop and implement economic programs to provide business support, expertise, and financial assistance to companies that are investing and creating jobs in Wisconsin; and (b) support new business startups, expansion, and growth in the state. WEDC's economic development programs offer a number of tax credits, loans, grants, and technical assistance programs to eligible Wisconsin companies.

WEDC is responsible for certifying and verifying eligible claimants under certain tax credit programs, including the business development tax credit and enterprise zones tax credit programs, which are described below. WEDC will generally enter into a contract with a business to create or retain jobs or to make a capital investment in the state for which the business may claim the awarded tax credits. Pursuant to the terms of the contract, a business may receive a verification letter from WEDC upon completion of the Wisconsin investment to claim the credits from the Department of Revenue (DOR).

Enterprise Zone Tax Credit. The enterprise zone tax credit program provides refundable tax credits that can be claimed for eligible expenses for increased employment, retaining employees, employee training, capital investment, and purchases from Wisconsin vendors. A zone designation cannot last more than 12 years. WEDC is responsible for designating enterprise zones, certifying businesses as eligible to receive credits, allocating and verifying tax credits, and performing other general administrative functions related to the enterprise zone program.

The enterprise zone tax credit for job creation can be claimed for a percentage of the increase in wages resulting from creating full-time jobs in the zone. Specifically, the credit is an amount equal to a percentage (up to 7% as determined by WEDC) multiplied by: (a) the number of the claimant's new full-time employees; and (b) the creditable wage amount. New full-time employees are equal to the number of employees in the zone in the taxable year minus the number of employees in the base year (or, if the difference is smaller, the new employees in the state minus base year employees in the state). The creditable wage amount is the average zone payroll minus the average eligible wage amount. The average zone payroll is the total wages of full-time employees employed in the zone whose wages exceed the average eligible wage threshold in the taxable year, excluding wages in excess of $100,000, divided by the number of these full-time employees employed in the zone in the taxable year. The average eligible wage amount is currently $22,620 for Tier 1 and $30,000 for Tier 2 counties and municipalities. Counties and municipalities are designated as Tier 1 or Tier 2 by WEDC, based on certain economic indicators.

The enterprise zone tax credit for job retention can be claimed for an amount equal to the percentage, up to 7% as determined by WEDC, of the claimant's zone payroll (excluding wage amounts that are over $100,000) paid in the tax year to full-time employees who were employed in the enterprise zone in the tax year and whose annual wages were greater than the eligible wage amount (described above). Wages paid to employees that are used to claim the enterprise zone job creation credit cannot be used to claim the job retention credit. In general, the total number of employees must be equal to or greater than the number of employees in the base year.

Business Development Tax Credit. The refundable business development tax credit can be claimed equal to a portion of certain expenses for increased employment, retaining employees, employee training, capital investment, and corporate headquarters location or retention in Wisconsin. WEDC is responsible for certifying businesses as eligible to receive credits, verifying eligible activities to claim credits from DOR, and performing other general administrative activities related to the business development tax credit program.

In order to be certified to receive any of the business development tax credits, a person must operate or intend to operate a business in this state and enter into a contract with WEDC. Certifications can remain in effect for up to 10 years. A certified business is eligible to receive tax benefits if, in each year the business claims the credit, it increases net employment in Wisconsin above the level during the year before the person was certified, as determined by WEDC under its policies and procedures. Certified businesses can earn a business development tax credit for up to 10% of the amount of wages paid to an eligible employee (full-time job) in a tax year. If the employee is employed in a full-time job at the claimant's business in an "economically distressed area," as determined by WEDC, an additional credit may be awarded for up to 5% of such wages. Further, under WEDC's policies and procedures, a certified business can earn corporate headquarters credits for up to 10% of the annual wages of eligible positions created or retained in connection with a corporate headquarters location or retention in Wisconsin.

GOVERNOR

Specify that a recipient of a WEDC grant, loan, or tax credit may not use the grant, loan, or tax credit to reduce net employment in this state or relocate jobs outside this state.

Further, require recipients of a grant, loan, or tax credit to report to WEDC each full-time job in this state that the recipient eliminates or relocates outside this state within seven business days after the job is eliminated or relocated and describe in detail the circumstances of that job elimination or relocation. The bill would specify that, if extenuating circumstances make it impossible for the recipient to submit the report within seven business days, the recipient may submit the report within 30 days after the full-time job is eliminated or relocated.

DISCUSSION POINTS

1. The Governor's recommended changes are intended to increase accountability and transparency by recipients of state funded grants, loans, and tax credits under WEDC's economic development programs and to prevent recipients of state support from relocating jobs outside the state As stated in the administration's Budget in Brief, "economic development awards should only be used to enhance economic opportunity in Wisconsin."

2. For example, in its May, 2019, audit of WEDC programs (Report 19-6), the Legislative Audit Bureau (LAB) conducted a review of 10 of WEDC's tax credit contracts. In relevant part, LAB found that WEDC "awarded $462,000 in tax credits for creating jobs to one recipient that created 66 jobs in the first two years of [the] contract but then lost 83 jobs in the third year, for a net loss of 17 jobs." The recipient was contractually required to maintain all existing and newly created jobs over the 60 consecutive months of the contract. As of February, 2019, WEDC had not revoked the $462,000 in tax credits, even though the contract ended in October, 2017.

3. Report 19-6 also indicated that WEDC did not consistently comply with statutes and its contracts because it "awarded tax credits to recipients that created or retained jobs filled by individuals who did not perform services in Wisconsin or were non-Wisconsin residents."

4. The Joint Committee on Finance could approve the Governor's recommendation and prohibit WEDC economic development award recipients from using those awards to reduce net employment in Wisconsin or to relocate jobs outside the state (Alternative 1). Under this alternative, recipients would be required to report to WEDC each full-time job in this state that the recipient eliminates or relocates and describe in detail the circumstances of that job elimination or relocation for further consideration by WEDC's Board.

5. Further, based on the concerns raised in Report 19-6, the Committee could also modify the bill to clarify that: (a) business development tax credits may not be awarded for jobs filled by individuals performing services outside of Wisconsin; and (b) WEDC may not certify a business to claim tax benefits under the enterprise zone program for services performed outside this state (Alternative 2).

6. In Report 19-6, LAB noted that the statutes related to the business development tax credit program do not specifically require services to be performed in Wisconsin. Current law states only that WEDC may award business development tax credits for wages paid to an "eligible employee,"

which is defined as a person employed in a full-time job by a person certified for the credit. Thus, WEDC stated in its response to Report 19-6 that it may award business development tax credits to recipients for creating or retaining jobs filled by individuals who perform services outside of Wisconsin.

7. Examples of such situations may include employees paid by businesses located within Wisconsin, but who are physically located outside the state due to various reasons such as business travel by a salesmen, being embedded within a customer worksite, or working remotely from a residence outside the state.

8. Report 19-6 found that WEDC's Board approved policies for the business development tax credit program that allow WEDC to award tax credits to recipients based on the wages of employees that do not perform services in Wisconsin. For example, according to Report 19-6, WEDC awarded a recipient a total of $5,500 in business development tax credits in April, 2018, for one job filled by an individual in Texas and another job filled by an individual in Arizona.

9. LAB identified that the Legislature could modify the statutes relating to the business development tax credit program to require WEDC to award program tax credits to recipients for creating or retaining jobs filled only by individuals performing services in Wisconsin.

10. Further, Report 19-6 found that WEDC's written procedures for the enterprise zone tax credit program allow WEDC to award tax credits for "any employee that does not live in Wisconsin and is designated as 'remote,' 'working at home,' or 'sales'" as long as these employees are paid out of a location within an enterprise zone. For example, in September 2018, WEDC determined that a recipient had created 967 jobs, including 261 jobs filled by individuals who lived in 36 states not contiguous with Wisconsin. Based on its written procedures, WEDC awarded this recipient $61,100 in job creation tax credits for these 261 jobs. LAB questioned whether these individuals actually performed services in the enterprise zone, as required by statutes and WEDC's contract.

11. WEDC may certify a business for enterprise zone tax credits for creating or retaining jobs, which, as described above, are based on zone payroll, which include eligible wages of full-time employees employed in the enterprise zone. "Full-time employee" means an individual who is employed in a regular, nonseasonal job and who, as a condition of employment, is required to work at least 2,080 hours per year, including paid leave and holidays. "Zone payroll" means the amount of state payroll that is attributable to wages paid to full-time employees for services that are performed in an enterprise zone. "State payroll" means the amount of payroll apportioned to this state.

12. LAB recommended in Report 19-6 that WEDC comply with current law by modifying its written enterprise zone tax credit program procedures to require it to award tax credits only for the wages of employees who perform services in an enterprise zone.

13. However, WEDC indicates that its written policies and procedures for the enterprise zone tax credit program comply with current law. WEDC states that enterprise zone tax credits are calculated based on Wisconsin payroll reported on corporate income/franchise tax forms, which is determined using a six-factor, statutory payroll factor test which DOR previously used to apportion employee compensation to Wisconsin or to another state under corporate income/franchise tax

apportionment statutes under prior law. According to WEDC, under this test, the services performed by employees who physically reside in other states may be fairly apportioned to Wisconsin, and hence may also fairly qualify as being performed in the zone for purposes of the enterprise zone tax credit program.

14. WEDC indicates that a similar analysis does not apply to the electronics and information technology manufacturing (EITM) zone tax credit program because the statutes explicitly state that WEDC "may not certify a business to claim tax benefits. . . for services performed outside this state." This explicit restriction is absent from the statutes related to the enterprise zone program.

15. Alternative 2 would treat the credits for job creation and retention under the enterprise zone and business development programs similar to the treatment of payroll credits under the EITM zone program.

16. Based on LAB's findings and Report 19-6, the Committee could conclude that providing refundable tax credit incentives for applicants to create and retain jobs for services that are performed outside the state runs counter to the purpose of the business development and enterprise zone tax credit programs. As stated in WEDC's program guidelines, the goal of the business development tax credit is to incent new and expanding businesses in the state of Wisconsin and the goal of the enterprise zone tax credit is to incent projects involving expansion of existing Wisconsin businesses or relocation of major business operations from other states to Wisconsin. Awarding tax credits for jobs created outside the state advances neither goal.

17. Finally, the Committee could find that it is unnecessary to modify current law because WEDC's Board already has the statutory authority necessary to properly administrate the business development and enterprise zone tax credit programs and to determine when such credits are properly available (Alternative 3).

ALTERNATIVES

1. Approve the Governor's recommended modifications regarding notifications requirements for job elimination and relocation under WEDC's grant, loan, and tax credit programs.

2. Adopt Alternative 1, but with a modification to clarify that: (a) business development tax credits may not be awarded for jobs filled by individuals performing services outside of Wisconsin; and (b) WEDC may not certify a business to claim tax benefits under the enterprise zone program for services performed outside this state.

3. Take no action.

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June, 2019 Joint Committee on Finance Paper #327

Enterprise Zone Tax Credit Program Sum Sufficient Reestimate and Oversight of Tax Credit Programs (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 145, #22; and Page 452, #6]

CURRENT LAW

The enterprise zone tax credit program provides refundable tax credits that can be claimed against the individual income tax and the corporate income/franchise tax for eligible expenses for increased employment, retaining employees, employee training, capital investment, and purchases from Wisconsin vendors. The Wisconsin Economic Development Corporation (WEDC) is responsible for designating enterprise zones, certifying taxpayers, allocating and verifying tax credits, and performing other general administrative functions related to the enterprise zone program. Under the state's accounting system, refundable enterprise zone tax credit claims are paid from a sum sufficient GPR appropriation.

Pursuant to 2017 Act 369, there is no specific limit on the number of enterprise zones which WEDC may designate. Instead, each designation is subject to approval by the Joint Committee on Finance under a 14-day passive review process. WEDC is required to notify the Committee, in writing, of its intent to designate a new enterprise zone. The notice must describe the new zone and the purpose for which WEDC proposes to designate the new zone. Each enterprise zone may exist for up to 12 years.

GOVERNOR

The bill would decrease funding by $4,000,000 GPR in 2019-20 and by $17,600,000 GPR in 2020-21 for the sum sufficient appropriation for refundable enterprise zone tax credits to reestimate anticipated claims during the biennium. With the adjustments, estimated total funding would decrease from base funding of $68,300,000 to $64,300,000 in 2019-20 and to $50,700,000 in 2020-21.

Further, the bill would require that each contract WEDC executes with a taxpayer under which the taxpayer may be eligible to claim tax benefits in excess of $5,000,000 during the term of the contract include an obligation that the taxpayer promptly notify WEDC of: (a) each material change to a project subject to the contract; and (b) all effects of each material change on the contract's performance goals or requirements, including job retention, creation, or training and capital expenditures, and any effect on the timing of the taxpayer's achievement of the performance goals or requirements. WEDC would be required to notify the Committee of any material change for which WEDC receives notice and, for any contract under which a taxpayer may be eligible to claim tax benefits in excess of $5,000,000 during the term of the contract, of any material change due to an amendment to the contract. These requirements would first apply to contracts entered into, modified, or renewed on the effective date of the bill.

DISCUSSION POINTS

Enterprise Zone Tax Credit Sum Sufficient Reestimate

1. Table 1 provides information regarding the current 28 enterprise zone tax credit awards that have, through May 1, 2019, been contracted by WEDC and the former Department of Commerce, including the year in which each contract was executed, the number of years over which each business can earn the credits, and the amount of credits that have been verified by WEDC/Commerce as eligible to be claimed with the Department of Revenue (DOR). Table 1 shows that the duration of enterprise zone designations has been for between four and 12 years, with an average duration of eight years per zone.

2. As shown in Table 1, contracts have ranged from $65.0 million over a 12-year period for Mercury Marine to $3.0 million over a four-year period for Saputo Cheese USA. WEDC/Commerce has entered into contracts to award up to $708.1 million in enterprise zone tax credits from 2009 through 2029. To date, WEDC has verified $298.7 million of this amount is eligible to be claimed as tax credits with DOR based upon the performance of the certified businesses.

TABLE 1

Enterprise Zone Awards Contracted by WEDC (Millions)

Certified Business	Contracted Amount of Credits	Year Awarded	Years Over which Credits Have Been Allocated	Credits Verified to Date
Mercury Marine	$65.0	2010	2010-2021	$51.3
Kohl's Corporation	62.5	2012	2012-2021	39.1
Quad Graphics, Inc.	61.7	2010	2010-2020	44.5
Green Bay Packaging Inc - Mill Division	60.0	2018	2018-2029	6.6
Komatsu Mining Corporation	59.5	2018	2017-2028	0.0
Oshkosh Corporation	55.0	2010	2009-2020	33.2
Fincantieri Marine Group LLC	42.0	2011	2010-2021	23.5
Kimberly-Clark Corporation	28.0	2018	2019-2023	0.0
Milwaukee Electric Tool Corporation	26.0	2016	2016-2022	7.4
Direct Supply, Inc.	22.5	2016	2017-2023	0.0
Haribo of America Manufacturing LLC	21.0	2017	2017-2028	1.3
Kwik Trip, Inc	21.0	2017	2017-2021	6.5
U.S. Venture, Inc.	20.0	2017	2017-2023	0.4
Uline, Inc.	18.6	2010	2010-2018	16.0
DRS Power & Control Technologies, Inc.	18.5	2018	2018-2025	0.0
Amazon.com	17.8	2014	2015-2018	5.2
InSinkErator	15.5	2012	2012-2019	15.1
Plexus Corp.	15.0	2011	2011-2018	12.6
Northstar Medical Technologies, LLC	14.0	2013	2014-2024	3.4
Generac Power Systems Inc	10.0	2017	2017-2021	1.9
Johnsonville Sausage, LLC	10.0	2017	2017-2021	3.4
Exact Sciences Corporation	9.0	2015	2014-2020	4.3
Weather Shield Mfg., Inc.	8.0	2013	2013-2019	6.5
ATI Ladish LLC	7.0	2018	2018-2024	1.8
Brakebush Brothers, Inc.	6.5	2017	2017-2022	1.4
Dollar General Corporation	5.5	2014	2013-2018	5.4
Trane US Inc.	5.5	2016	2016-2020	4.9
Saputo Cheese USA	3.0	2017	2016-2019	2.9
Total	$708.1			$298.7

3. In 2016, 2017, and 2018, WEDC awarded contracts in the amount of $54.0 million, $91.5 million, and $173.0 million, respectively.

4. Attachment 1 provides additional detail regarding how WEDC/Commerce has allocated enterprise zone credit awards. The year in which WEDC has allocated the largest amount of enterprise zone tax credits is 2019, for which $102.1 million is allocated to businesses to be earned. Annual allocations of tax credit awards for individual companies range from $19,000 for Saputo Cheese USA in 2018 to $29.3 million for Komatsu Mining Corporation in 2023.

5. The cost estimate used under the bill for the enterprise zone sum sufficient GPR appropriation was based on projections of credit claims under contracts between WEDC and participating businesses through October, 2018. Since that time, WEDC entered into three new contracts which allocated $106.0 million over a twelve-year period, including $3.5 million in 2018

and $14.7 million in 2019. In addition, two contracts were amended to increase awarded amounts by $21.5 million, including $9.5 million allocated in 2019.

6. Based upon more recent information described above, it is estimated that enterprise zone tax credits relative to the bill will be $31,000,000 GPR higher in 2020-21 (Alternative 1). The reestimate reflects projections of credit claims for major economic development projects for which WEDC has, to date, contracted tax credit awards including recent contract amendments. With the adjustments, estimated total funding would decrease from base funding of $68,300,000 to $64,300,000 in 2019-20 and increase to $81,700,000 in 2020-21.

Committee Oversight of Enterprise Zone Designations

7. Typically, WEDC will certify a business as eligible via a contract that specifies a maximum amount of tax benefits that may be earned by the business by successfully completing specified goals for job creation, job retention, capital investment, employee training, and/or Wisconsin supply chain investment. The contract will delineate the amount that can be earned in each year of the contract, for a period of up to 12 years. According to WEDC, each zone has a unique eligible earning period and the length of a specific contract is dependent on the terms of each contract and each business's unique plan for investment and job growth under that project.

8. The total amount awarded and when that amount may be earned may change one or more times over the duration of a zone based on amended contracts between the certified business and WEDC. Attachment 2 shows all contract amendments for active enterprise zones. According to WEDC, there have been 34 amendments in total for currently active zones. These 34 contract amendments have increased the aggregate enterprise zone awards by $68,500,000 and increased the aggregate duration of zones by 165 months for seven zones.

9. As shown in Attachment 2, a contract may be substantially altered and the amount of tax benefits significantly increased after the Committee has reviewed and approved a proposed enterprise zone. For example, despite changes under 2017 Act 369 which require Committee approval of enterprise zone designations, WEDC amended a contract with Fincantieri Marine Group LLC on December 17, 2018, which increased the overall award of enterprise zone tax credits by $14.0 million and with Amazon.com on April 25, 2019, that increased the total award by $7.5 million.

10. The bill would require WEDC to notify the Committee of any material change due to an amendment to a contract under which a taxpayer may be eligible to claim tax benefits in excess of $5,000,000 (Alternative 2). The requirements would first apply to contracts entered into, modified, or renewed on the effective date of the bill.

11. However, as noted, current law does not require WEDC to seek approval from the Committee for a contract amendment for any of the currently open enterprise zone contracts shown in Table 1. Further, because the enterprise zone tax credit program is funded via a sum sufficient GPR appropriation, current law does not limit the amount of tax benefits that can be added via contract amendment.

12. In addition to the Governor's proposed notification requirements, the Committee could

also require approval by the Committee, under a 14-day passive review process, of any amendment to a contract which would change the total amount of tax credits awarded under a contract or would alter the allocation schedule for when such tax credits could be earned (Alternative 3). Under this alternative, WEDC would be prohibited from executing an amendment to a contract under which a certified business may be eligible to claim tax benefits in excess of $5,000,000 during the term of the contract if the amendment would alter the amount awarded or the allocation schedule of the award, unless approved by the Committee under a 14-day passive review process. WEDC would be required to notify the Committee, in writing, of its intent to amend such a contract. The notice would need to describe the recipient and the purpose for which WEDC proposes to amend the amount awarded or scheduled to be awarded. These requirements would first apply to contracts entered into, modified, or renewed on the effective date of the bill.

13. Alternatives 2 and 3 would apply to the amendment of contracts under any of the tax credit programs administered by WEDC. This includes the enterprise zone tax credit program and the electronics and information technology manufacturing (EITM) zone tax credit program.

14. Finally, because current law already provides for certain EITM zone audit and verification requirements, including an annual evaluation by the Legislative Audit Bureau, the Committee could adopt Alternative 3 with the modification that the provisions would not apply to the EITM zone tax credit program (Alternative 4).

ALTERNATIVES

1. *Enterprise Zone Tax Credit Program Sum Sufficient Reestimate.* Modify the Governor's recommended funding for the enterprise zone tax credit program sum sufficient appropriation to provide an additional $31,000,000 GPR in 2020-21. With the adjustments, estimated total funding would decrease from base funding of $68,300,000 to $64,300,000 in 2019-20 and increase to $81,700,000 in 2020-21.

ALT 1	**Change to**	
	Base	**Bill**
GPR	$9,400,000	$31,000,000

2. *Governor's Proposed Disclosure of Contracts and Material Changes to Contracts or Projects*. Adopt Alternative 1 and adopt the Governor's proposed notification and reporting requirements for WEDC contracts under which a taxpayer may be eligible to claim tax benefits in excess of $5,000,000.

ALT 2	**Change to**	
	Base	**Bill**
GPR	$9,400,000	$31,000,000

3. *Committee Review of Tax Credit Contract Amendments.* Adopt Alternatives 1 and 2 and also modify the Governor's recommendations to prohibit WEDC from executing an amendment to a contract under which a certified business may be eligible to claim tax benefits in excess of $5,000,000 during the term of the contract if the amendment would alter the amount awarded or the allocation schedule of the award unless approved by the Committee under a 14-day passive review process. Specify that WEDC is required to notify the Committee, in writing, of its intent to amend such a contract. The notice must describe the recipient and the purpose for which WEDC proposes to amend the amount awarded or scheduled to be awarded. These requirements would first apply to contracts entered into, modified, or renewed on the effective date of the bill.

ALT 3	**Change to Base**	**Change to Bill**
GPR	$9,400,000	$31,000,000

4. *Committee Review of Tax Credit Contract Amendments Except for Electronics and Information Technology Manufacturing Zone.* Adopt Alternatives 1, 2, and 3 but with the modification that the provisions under Alternatives 2 and 3 would not apply to the EITM zone tax credit program.

ALT 4	**Change to Base**	**Change to Bill**
GPR	$9,400,000	$31,000,000

Prepared by: John D. Gentry
Attachments

ATTACHMENT 1

Allocation Schedule for Earning Enterprise Zone Tax Credits
(As of May 1, 2019)

Certified Business	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Amazon.com						$1,655,500	$3,046,500	$535,000	$560,000	$585,000	$7,105,000
ATI Ladish LLC										1,750,000	2,275,000
Brakebush Brothers, Inc.									5,370,500	346,000	320,000
Direct Supply, Inc.									2,770,000	3,090,000	3,435,000
Dollar General Corporation								434,531	4,846,816	128,653	50,000
DRS Power & Control Technologies, Inc.										65,000	2,420,000
Exact Sciences Corporation						200,000	900,000	1,300,000	1,900,000	1,600,000	1,600,000
Fincantieri Marine Group LLC		$948,000	$2,138,000	$4,650,000	$4,966,000	3,192,000	2,506,000	2,562,000	2,531,000	2,461,000	5,046,000
Generac Power Systems Inc.									2,281,000	2,488,000	2,293,000
Green Bay Packaging Inc. - Mill Division										11,100,000	26,400,000
Haribo of America Manufacturing LLC									1,310,377		4,143,123
InSinkErator						6,785,954	3,535,568	2,667,979	2,069,000	441,500	
Johnsonville Sausage, LLC									3,797,660	1,586,000	1,718,000
Kimberly-Clark Corporation											8,500,000
Kohl's Corporation				583,000	1,414,000	6,818,600	9,506,586	9,896,728	10,187,086	6,026,000	3,068,000
Komatsu Mining Corporation									3,400,000	3,500,000	3,750,000
Kwik Trip, Inc.									6,501,000	3,686,000	4,838,000
Mercury Marine		7,662,000	10,741,000	10,014,000	7,766,000	7,552,000	2,490,000	2,526,000	2,562,000	3,099,000	3,491,000
Milwaukee Electric Tool Corporation								2,979,432	4,465,568	4,110,000	4,260,000
Northstar Medical Technologies, LLC			19,374	28,904	135,456	142,376	1,088,900	359,951	902,322	1,508,717	2,464,000
Oshkosh Corporation	$2,496,457	8,470,543	4,812,000	4,511,000	4,176,000	2,244,000	2,408,000	4,064,000	3,792,000	5,926,000	5,100,000
Plexus Corp.				1,014,250	3,641,000	2,316,750	2,029,750	1,860,250	1,752,250	1,373,250	1,012,500
Quad Graphics, Inc.		4,937,000	6,421,000	6,800,000	5,519,000	5,508,000	4,005,000	5,630,000	5,658,000	5,698,000	5,742,000
Saputo Cheese USA								1,000,000	1,863,000	19,000	118,000
Trane US Inc.					891,000	1,910,000	749,000	722,000	668,000	560,000	
U.S. Venture, Inc.									8,157,800	2,148,000	2,207,000
Uline, Inc.		1,006,048	1,785,000	2,022,000	2,074,000	2,124,000	2,736,952	2,230,000	2,285,000	2,337,000	
Weather Shield Mfg., Inc.					1,186,605	1,272,605	1,317,605	1,360,605	1,360,605	732,000	769,975
Total	$2,496,457	$23,023,591	$25,916,374	$29,623,154	$31,769,061	$41,721,785	$36,319,861	$40,128,476	$80,990,984	$66,364,120	$102,125,598

Source: Wisconsin Economic Development Corporation

ATTACHMENT 1 (Continued)

Allocation Schedule for Earning Enterprise Zone Tax Credits
(As of May 1, 2019)

Certified Business	2020	2021	2022	2023	2024	2025	2026	2027	2028	2029	Grand Total
Amazon.com	$815,000	$852,000	$882,000	$882,000	$882,000						$17,800,000
ATI Ladish LLC	1,925,000	350,000	350,000	175,000	175,000						7,000,000
Brakebush Brothers, Inc.		320,000	143,500								6,500,000
Direct Supply, Inc.	3,810,000	4,225,000	2,330,000	2,840,000							22,500,000
Dollar General Corporation	40,000										5,500,000
DRS Power & Control Technologies, Inc.	3,570,000	3,920,000	2,995,000	3,020,000	1,500,000	$1,010,000					18,500,000
Exact Sciences Corporation	1,500,000										9,000,000
Fincantieri Marine Group LLC	5,346,000	5,654,000									42,000,000
Generac Power Systems Inc	1,502,000	1,436,000									10,000,000
Green Bay Packaging Inc - Mill Division	11,450,000	6,500,000	1,550,000	350,000	400,000	450,000	$450,000	$450,000	$450,000	$450,000	60,000,000
Haribo of America Manufacturing LLC	6,033,250	5,798,250	865,000	700,000	575,000	700,000	475,000	200,000	200,000		21,000,000
InSinkErator											15,500,000
Johnsonville Sausage, LLC	1,659,000	1,239,340									10,000,000
Kimberly-Clark Corporation	5,800,000	4,900,000	4,400,000	4,400,000							28,000,000
Kohl's Corporation	7,343,000	7,657,000									62,500,000
Komatsu Mining Corporation	4,450,000	3,900,000	1,500,000	29,300,000	1,600,000	1,600,000	1,800,000	2,200,000	2,500,000		59,500,000
Kwik Trip, Inc	3,779,000	2,196,000									21,000,000
Mercury Marine	3,529,000	3,568,000									65,000,000
Milwaukee Electric Tool Corporation	4,185,000	3,000,000	3,000,000								26,000,000
Northstar Medical Technologies, LLC	2,750,000	2,765,000	1,835,000								14,000,000
Oshkosh Corporation	7,000,000										55,000,000
Plexus Corp.											15,000,000
Quad Graphics, Inc.	5,782,000										61,700,000
Saputo Cheese USA											3,000,000
Trane US Inc.											5,500,000
U.S. Venture, Inc.	2,283,000	2,371,000	1,871,000	962,200							20,000,000
Uline, Inc.											18,600,000
Weather Shield Mfg., Inc.											8,000,000
Total	$84,551,250	$60,651,590	$21,721,500	$42,629,200	$5,132,000	$3,760,000	$2,725,000	$2,850,000	$3,150,000	$450,000	$708,100,000

Source: Wisconsin Economic Development Corporation

ATTACHMENT 2

Enterprise Zone Tax Credit Contract Amendments
(Through May 1, 2019)

Certified Business	Amendment Contract Date	Initial Award Amount	Amended Award Amount	Increased Award	Initial Zone Duration (Months)	Amended Zone Duration (Months)	Duration Change
Uline, Inc.	9/19/2017	$18,600,000	$18,600,000	-	108	108	0
Oshkosh Corporation	3/31/2016	35,000,000	47,000,000	$12,000,000	120	141	21
Oshkosh Corporation	6/22/2017	47,000,000	47,000,000	-	141	141	0
Oshkosh Corporation	6/6/2018	47,000,000	55,000,000	8,000,000	141	141	0
Mercury Marine	9/25/2017	65,000,000	65,000,000	-	144	144	0
Northstar Medical Radioisotopes, LLC	11/20/2015	14,000,000	14,000,000	-	60	96	36
Northstar Medical Radioisotopes, LLC	10/3/2016	14,000,000	14,000,000	-	96	96	0
Northstar Medical Radioisotopes, LLC	1/2/2019	14,000,000	14,000,000	-	96	144	48
Quad/Graphics, Inc.	10/27/2010	46,000,000	61,700,000	15,700,000	132	132	0
Quad/Graphics, Inc.	12/20/2017	61,700,000	61,700,000	-	132	132	0
Fincantieri Marine Group LLC	5/14/2014	28,000,000	28,000,000	-	108	120	12
Fincantieri Marine Group LLC	12/14/2016	28,000,000	28,000,000	-	120	120	0
Fincantieri Marine Group LLC	12/17/2018	28,000,000	42,000,000	14,000,000	120	144	24
Plexus Corp.	7/13/2017	15,000,000	15,000,000	-	84	84	0
Kohl's Corporation	3/20/2019	62,500,000	62,500,000	-	144	144	0
Weather Shield Mfg., Inc.	12/10/2015	8,000,000	8,000,000	-	84	84	0
Weather Shield Mfg., Inc.	4/5/2017	8,000,000	8,000,000	-	84	84	0
Amazon.com	3/18/2014	7,000,000	10,300,000	3,300,000	132	132	0
Amazon.com	9/18/2015	10,300,000	10,300,000	-	132	132	0
Amazon.com	2/13/2017	10,300,000	10,300,000	-	132	132	0
Amazon.com	4/25/2019	10,300,000	17,800,000	7,500,000	132	132	0
InSinkErator	4/11/2017	15,500,000	15,500,000	-	60	60	0
Exact Sciences Corporation	2/11/2016	9,000,000	9,000,000	-	78	78	0
Exact Sciences Corporation	11/8/2016	9,000,000	9,000,000	-	78	78	0
Trane US Inc.	3/31/2015	5,500,000	5,500,000	-	60	72	12
Trane US Inc.	3/28/2017	5,500,000	5,500,000	-	72	72	0
Dollar General Corporation	11/10/2017	5,500,000	5,500,000	-	52	52	0
Milwaukee Electric Tool Corporation	5/10/2018	18,000,000	26,000,000	8,000,000	72	84	12
Milwaukee Electric Tool Corporation	11/15/2018	26,000,000	26,000,000	-	84	84	0
Direct Supply, Inc.	10/23/2017	22,500,000	22,500,000	-	84	84	0
Johnsonville Sausage, LLC	7/12/2018	10,000,000	10,000,000	-	60	60	0
Saputo Cheese USA	5/23/2018	3,000,000	3,000,000	-	36	36	0
U.S. Venture, Inc.	12/19/2017	20,000,000	20,000,000	-	84	84	0
Haribo of America Manufacturing LLC	12/6/2018	21,000,000	21,000,000	-	138	138	0
Total		$748,200,000	$816,700,000	$68,500,000			165

Source: Wisconsin Economic Development Corporation

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June, 2019 | Joint Committee on Finance | Paper #328

Business Development Tax Credit Sum Sufficient Reestimate (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 146, #25]

CURRENT LAW

The refundable business development tax credit can be claimed against the individual income tax and the corporate income/franchise tax equal to a portion of eligible expenses for increased employment, retaining employees, employee training, capital investment, and corporate headquarters location or retention in Wisconsin. The Wisconsin Economic Development Corporation (WEDC) is responsible for certifying businesses as eligible to receive credits, verifying eligible activities to claim credits from the Department of Revenue (DOR), and performing other general administrative activities related to the business development tax credit program. It is estimated that expenditures related to tax credit claims in 2018-19 will be $13,400,000.

GOVERNOR

The bill would increase funding by $2,000,000 in 2019-20 and by $2,300,000 in 2020-21 for the sum sufficient GPR appropriation for business development tax credits to reestimate anticipated claims during the biennium. With the adjustments, estimated total funding would increase from base funding of $16,100,000 to $18,100,000 in 2019-20 and to $18,400,000 in 2020-21.

MODIFICATION

Increase funding for the business development credit appropriation by $600,000 in 2019-20 and $1,700,000 in 2020-21. With the adjustments, estimated total funding would increase from base funding of $16,100,000 to $18,700,000 in 2019-20 and to $20,100,000 in 2020-21.

Explanation: The reestimate is based on more recent information from WEDC regarding awards, allocations, and verifications to-date of business development tax credits and more recent information on claims of such tax credits with DOR. This modification would more accurately reflect the amount of business development tax credits estimated to be claimed for the 2019-21 biennium.

		Change to
	Base	**Bill**
GPR	$6,600,000	$2,300,000

Prepared by: John D. Gentry

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June, 2019 Joint Committee on Finance Paper #329

Business Development Tax Credit Program (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 147, #26]

CURRENT LAW

The refundable business development tax credit can be claimed against the individual income tax and the corporate income/franchise tax equal to a portion of eligible expenses for increased employment, retaining employees, employee training, capital investment, and corporate headquarters location or retention in Wisconsin. The Wisconsin Economic Development Corporation (WEDC) is responsible for certifying businesses as eligible to receive credits, verifying eligible activities to claim credits from the Department of Revenue (DOR), and performing other general administrative activities related to the business development tax credit program.

In order to be certified to receive any of the business development tax credits, a person must operate or intend to operate a business in this state and enter into a contract with WEDC. Certifications can remain in effect for up to 10 years. A certified business is eligible to receive tax benefits if, in each year the business claims the credit, it increases net employment in Wisconsin above the level during the year before the person was certified, as determined by WEDC under its policies and procedures. There is no limit on the number of businesses that may be certified as eligible to receive business development tax credits.

State law permits WEDC to allocate up to $22 million in business development tax credits annually. Any unused allocation can be carried forward to future tax years. WEDC may request the Joint Committee on Finance for an increase of up to $10 million annually for the amount of business development credits that may be allocated.

Under the credit for capital investment, WEDC can certify businesses to earn a credit for up to 3% of the business's personal property investment and for up to 5% of a new real property investment that is made in a capital investment project of $1 million or more. For projects involving a capital investment of less than $1 million, the investment must be equal to at least $10,000 per eligible employee employed in the project for the business to be eligible to receive a capital investment credit.

The business development credit was created under 2015 Wisconsin Act 55, which consolidated aspects of the nonrefundable economic development credit and the refundable jobs credit. Act 55 sunset the jobs and economic development credits for taxable years beginning after December 31, 2015, and the business development credit took effect for taxable years beginning in 2016.

GOVERNOR

Authorize WEDC, for a project that satisfies the current law requirements under the business development tax credit program to earn the 5% capital investment credit for a real property investment, to award an additional tax credit in an amount equal to up to 5% of the person's real property investment in a capital investment project if the investment is made for purposes of energy efficiency or the generation of energy from renewable resources. Thus, the combined total credit would be 10% of the real property investment in that capital investment project.

Further, WEDC would be required to include in any contract for the award of such tax benefits a requirement that the recipient provide documentation to WEDC verifying all expenditures and showing the energy efficiency or renewable energy impacts of those expenditures.

DISCUSSION POINTS

Energy Efficiency and Generation of Renewable Energy

1. The bill would authorize WEDC to enter into contracts to award tax credits for energy efficiency and renewable power generation investment as part of the business development tax credit program. As noted, the combined total credit would be up to 10% of the real property investment in that capital investment project.

2. However, the bill does not include a provision that creates such a tax credit under the income or franchise tax statutes.

3. On May 1, 2019, the Department of Administration (DOA) submitted an errata seeking a modification to the bill in order to create such provisions and to properly reflect the intent of the Governor. The administration indicates that the credit was meant to apply to personal property investments, including business equipment and supplies. As amended, the credit would be available for: (a) up to 5% of the amount of a person's real property investment made for purposes of energy efficiency or the generation of energy from renewable resources; and (b) up to 5% of the amount of a person's personal property investment made for purposes of energy efficiency or the generation of

energy from renewable resources. Thus, the combined total credit under the business development tax credit program would be up to 10% of the portion of real property investment and up to 8% of the portion of personal property investment. However, the proposed credit would only be available for the portion of the investment that pertains to energy efficiency or renewable energy generation.

4. The Committee could choose to approve the Governor's recommendation to create tax credits for energy efficiency and the generation of energy from renewable resources under the business development tax credit program, as amended by the errata, for the following reasons (Alternative A1).

5. Tax incentives can support environmental and economic development policy goals and correct market failures that undervalue energy efficiency and renewable energy. For example, electricity and gas prices may not adequately account for the negative externalities associated with energy production, such as pollution and greenhouse gas emission. Thus, although a business can reduce its energy costs by investing in energy efficiency and renewable power generation on an ongoing basis, energy prices may not adequately account for the true cost of energy production and the societal savings from making such "up-front" investments. Providing refundable credits for energy efficiency and clean energy generation would increase the incentives for businesses to invest.

6. The tax incentives provided under the bill would leverage private construction spending to deliver energy efficiency and renewable energy generation. The eligible businesses are already venturing to undertake a capital investment project, and thus, a small investment through the 5% tax benefit may ultimately have an outsized impact. Further, the tax benefits may have a spillover effect that influences other persons to pursue such investments without claiming a tax benefit, such as by increasing the size of the market for, and increasing awareness of, energy efficiency and renewable energy generation projects.

7. On the other hand, the Committee could decide to take no action on the proposal for the following reasons (Alternative A3). First, businesses already have a long-term financial incentive to reduce their energy costs. As a result, tax incentives for energy efficiency and renewable energy generation may award a portion of the tax benefits to businesses that were already going to make some or all of such investments. Awarding tax credits to such businesses would not improve the overall energy efficiency or renewal energy generation in the state.

8. Second, WEDC is not an environmental protection agency and generally does not develop its rules and procedures based on environmental impacts or studies. The bill would not provide any standards or guidance for WEDC to determine what sorts of projects should qualify for the tax incentive or what policy goals the incentive should seek to achieve. The Committee could reasonably conclude that WEDC lacks the expertise needed to develop the policies and procedures to administrate or assess the effectiveness of the program under the bill.

9. Finally, fluctuations in energy prices may provide clearer incentives than the tax benefits provided under the bill. Generally, businesses will tend to be more sensitive to energy costs when they are higher and less so when they are lower. Thus, energy price fluctuations may become the incentive to increase usage of the proposed tax credit. The Committee could reasonably conclude that the program cost is vulnerable to unpredictable swings in energy prices that would undermine its

usefulness in incenting businesses to undertake energy efficiency and renewable power generation projects.

Fiscal Effect of the Governor's Proposal and Maximum Allocation of Credits

10. The bill would not provide any additional funding for the Governor's proposed credit, and DOA did not provide an estimated cost. However, the creation of a new tax credit for real and personal property investment related to energy efficiency and generation of renewable energy under the business development program would cause WEDC to certify persons to claim tax benefits for which they previously would not have qualified. Thus, the fiscal effect of the credit, and alternatives to increase the funding available for it, are discussed below.

11. As discussed in LFB Paper #328, it is estimated that the amounts that will be claimed for business development tax credits that are available under current law are $18,700,000 in 2018-19 and $20,100,000 in 2020-21.

12. Based upon information supplied by WEDC regarding the allocation of business development credits for capital investment, data from the U.S. Census Bureau on capital investment, and industry data on investment into energy efficiency and renewable power generation, it is estimated that WEDC would allocate approximately $2,000,000 annually in credits for energy efficiency and generation of renewable energy under the business development tax credit program.

13. Assuming that the amounts allocated in 2019-20 would not be claimed at DOR until 2020-21, the estimated fiscal effect of the governor's proposal, as amended by the technical errata, is $2,000,000 in 2020-21. Because WEDC would need time to establish policies and procedures for the new credit and additional time to review applications to certify applicants, and because applicants would need to finish their capital investment projects before WEDC could review and verify the amounts to be claimed at DOR, claimants are unlikely to claim the new credit during the first year of the biennium.

14. As discussed above, current law limits the amount of credits WEDC may allocate to $22.0 million each year, unless a requested increase is approved by the Committee. If less than that maximum amount is allocated, the shortfall carries forward to be allocated in a future year.

15. Assuming that WEDC allocates an additional $2,000,000 annually for the estimated fiscal effect of the energy efficiency and renewable power generation credit as discussed above, and allocates a similar amount of tax credits under current law, as discussed below, WEDC would likely allocate approximately $22,000,000 each year. Therefore, in addition to providing increased funding in 2020-21 for the proposed credit, the Committee could also increase the allocation limit to $24,000,000 annually, beginning in 2020, to account for the increase in tax benefits allocated under the proposed energy efficiency and renewable power generation credit (Alternative A2). This provision is not estimated to increase the cost of the Governor's proposed credit, because, as discussed below, WEDC is currently not allocating up to the limit under current law. However, it would provide WEDC with statutory authority to allocate more business development tax credits in future years.

16. On the other hand, the Committee could find that it is unnecessary to increase the

allocation limit because WEDC has not allocated the maximum amount of business development credits allowed under current law over the past few years.

17. Table 1 shows the business development tax credit amounts WEDC allocated by contract year compared to its statutory limit on allocations. The ending balance corresponds to the amounts carried forward to be allocated in contracts executed in a future year. If additional credits are needed, WEDC may ask the Committee to provide an additional amount up to a total of $10,000,000 in any year.

TABLE 1

Business Development Tax Credits Allocated Under Contracts by Calendar Year (as of May 1, 2019)

	2016	2017	2018	2019
Opening Balance	$0	$2,494,000	$1,549,200	$3,769,200
Limit	25,000,000*	22,000,000	22,000,000	22,000,000
Tax Credits Contracted	22,506,000	22,944,800	19,780,000	2,650,000
Ending balance	$2,494,000	$1,549,200	$3,769,200**	

* In 2016, the limit on contracting tax credits was $17,000,000. The Committee approved an increase of $8,000,000 in its June, 2016, meeting.
** WEDC indicates that additional contracts may be finalized which certify recipients for tax credits based upon payroll and activities conducted in 2018.

18. As shown in Table 1, WEDC can allocate up to $25.8 million in credits in 2019. Thus, it is likely that WEDC would be able to allocate additional tax credits without increasing the limit under current law during the 2019-21 biennium. Further, if needed, WEDC could request the Committee to increase the limit by up to another $10,000,000 in each year. Thus, the Committee could choose to retain the current limit of $22,000,000.

Allocation and Reporting of Business Development Tax Credits

19. Because the maximum amount of business development tax credits WEDC may allocate each year may change, the maximum amount that may be claimed by recipients at DOR will also vary from year to year. Thus, the flexibility provided under current law for WEDC to allocate tax benefits also makes it more difficult to predict the amounts that will be claimed under the program in a given year.

20. The Committee could require WEDC to identify the amount of unallocated tax credits carried forward into the current fiscal year as part of its annual report to the Legislature (Alternative B1). Under current law, WEDC must submit an annual report to the Legislature on January 1 regarding the economic development projects that the Board intends to develop and implement during

the current fiscal year. [Under a separate provision of the bill, this report would be submitted on October 1 instead.] Current law does not specifically require WEDC to identify the amount of unallocated business development tax credits that have carried forward for allocation in a future year as part of that report. Providing such a requirement would clarify the amount of tax credits available to be allocated and inform the Legislature of the funding likely to be required in the current and subsequent fiscal years.

21. Finally, in order to provide for more oversight of the program, the Committee could instead sunset the provision which allows unallocated amounts to carry forward after December 31, 2019 (Alternative B2). In the event WEDC required additional authority to allocate credits, WEDC would retain the ability to request that the Committee increase the limit by up to $10,000,000 in any given year. While this alternative is not expected to lower estimated expenditures under the bill, this would provide for more certainty over the maximum cost of the program because Committee approval would be required for WEDC to allocate more than the limit in any given year.

ALTERNATIVES

A. Tax Credits for Energy Efficiency and Generation of Renewable Energy

1. Approve the Governor's recommendation to create a 5% tax credit for energy efficiency and renewable energy generation as part of the business development tax credit for capital investment and increase funding for the business development credit appropriation by $2,000,000 GPR in 2020-21. Amend the bill to reflect the Governor's intent to create the credit in the appropriate sections of the individual income and corporate income/franchise tax statutes. In addition, specify that the additional credit be available for up to 5% of the amount of a person's real property investment and personal property investment made for purposes of energy efficiency or the generation of energy from renewable resources.

ALT A1	Change to Base	Change to Bill
GPR	$2,000,000	$2,000,000

2. Adopt Alternative A1, but modify the bill to increase the limit for allocations of business development tax credits from $22,000,000 annually to $24,000,000 annually, beginning in 2020.

ALT A2	Change to Base	Change to Bill
GPR	$2,000,000	$2,000,000

3. Take no action.

B. Allocation and Reporting of Business Development Tax Credits

1. Modify the bill to require WEDC to identify the amount of unallocated tax credits carried forward into the current fiscal year as part of its annual report to the Legislature on its economic development programs.

2. Modify the bill to prohibit unused allocations for business development tax credits from carrying over to be allocated in a future year after December 31, 2019.

3. Maintain current law with respect to the allocation and reporting of business development tax credits.

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June, 2019 Joint Committee on Finance Paper #330

Limit the State Supplement to the Federal Historic Rehabilitation Tax Credit (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 149, #32]

CURRENT LAW

Federal law provides a 20% tax credit for qualified rehabilitation expenditures (as defined under the Internal Revenue Code) for certified historic structures. A nonrefundable state supplement to the federal historic rehabilitation tax credit (historic tax credit) of 20% is a supplement to, and must be claimed at the same time as, the federal credit. The state credit of 20% along with the federal credit of 20% yields a total credit for qualified rehabilitation expenditures of 40%.

A "certified historic structure" is a building that is listed in the National Register of Historic Places or that is determined to be historic and will be listed in the National Register. For the state credit, qualified rehabilitation expenditures are eligible if the rehabilitated structure is located in this state and the cost of the qualified rehabilitation expenditures is at least $50,000. Also, the Wisconsin adjusted basis of the building must be reduced by the amount of the credit awarded.

For taxable years beginning after December 31, 2013, no person may claim the state credit without being certified by the Wisconsin Economic Development Corporation (WEDC). WEDC may certify a business if it determines that the claimant is conducting an eligible activity. Under changes made in 2017 Acts 59 and 280, the amount of historic credits that WEDC can certify persons to receive is no more than $3,500,000 for all rehabilitation projects undertaken on the same parcel, beginning with certifications on or after July 1, 2018. Generally, WEDC provides a three-year period during which businesses may earn historic credits (difference between the date of contract award with WEDC and the final date to earn the historic tax credit award). Certain large multi-phase projects can earn credits over a six-year period.

Unused credit amounts can be carried forward up to 15 years to offset future tax liabilities. As an alternative to carrying forward unused credits, a claimant, including a nonprofit entity, may sell or otherwise transfer a historic tax credit to another person.

In order to claim the credit from the Department of Revenue (DOR), a claimant must include with their tax return a copy of the certification by WEDC. The claimant must provide WEDC with evidence that the rehabilitation was recommended by the state historic preservation officer for approval by the U.S. Secretary of the Interior prior to beginning the physical work of construction, or destruction in preparation for construction, and that the rehabilitation was approved by the state historic preservation officer. The claimant must include evidence that the taxpayer had obtained written certification from the state historic preservation officer regarding the historical significance of the property and the proposed preservation or rehabilitation plan and expenditures.

It is estimated that state general fund tax revenues will be reduced by claims of the state supplement to the federal historic rehabilitation tax credit by $75.8 million in 2018-19, $56.8 million in 2019-20, and $54.5 million in 2020-21.

GOVERNOR

Sunset the current law limit for the state supplement to the federal historic rehabilitation tax credit as of June 30, 2019, and replace it with a new limit such that WEDC would not be able to certify anyone to claim more than a total of $3,500,000, for any project, regardless of the number of parcels on which the project is undertaken, beginning July 1, 2019.

DISCUSSION POINTS

1. The current limit on the state supplement to the federal historic rehabilitation tax credit was enacted under Acts 59 and 280 to control the rising costs of the credit.

2. Prior to tax year 2013, state law allowed only a credit for 5% of qualified expenditures on certified historic structures. Pursuant to 2013 Act 20, the credit increased for tax year 2013 from 5% of qualified expenditures on certified historic structures to 10%. The credit was again increased in tax year 2014 from 10% of qualified expenditures on certified historic structures to 20% under 2013 Act 62. Act 62 also required WEDC to certify claimants, among other changes.

3. In tax year 2013, 110 persons claimed $4.8 million in credits from DOR. For comparison, the following table shows the amounts of historic tax credits WEDC contracted to certify persons in each year through May 1, 2019. Attachment 1 lists the WEDC contract recipients. As shown in Attachment 1, prior to July 1, 2018, WEDC entered into contracts to certify 28 projects in excess of $3.5 million. Those 28 awards averaged $6.4 million per contract and totaled of $179.7 million (57% of the overall amount awarded).

WEDC Historic Tax Credit Contracts
(As of May 1, 2019)

Year	Amount	Contracts
2014	$21,896,308	24
2015	65,703,091	40
2016	67,269,061	36
2017	83,434,505	47
2018	84,382,577	32
2019	142,000	2
Total	$322,827,542	181

4. Under changes made in 2017 Acts 59 and 280, the amount of historic credits that WEDC can certify persons to receive is no more than $3.5 million for all rehabilitation projects undertaken on the same parcel, beginning with certifications on or after July 1, 2018. This limits overall revenue reduction under the program by limiting tax credit awards on large projects. Further, the provision prevents a business from circumventing the limit by applying for the certification of subsequent projects on the same parcel.

5. Prior to the effect of the limit, from January, 2018, through June, 2018, WEDC contracted with 26 businesses to certify a total of $77.1 million. After the limit went into effect, from July, 2018, through December, 2018, WEDC contracted with six businesses to certify a total of $7.3 million in historic tax credits. WEDC contracted with two businesses to certify a total of $0.1 million in 2019 through April.

6. Based on the above certification information from WEDC, the amount of credits certified by WEDC reduced significantly after the initial applicability of the limit enacted under Acts 59 and 280. For this reason, the Joint Committee on Finance could find that it is unnecessary to change the limitation under current law (Alternative 3).

7. On the other hand, the current limit may not be as effective as it appears. The amount certified in 2017 and 2018 may have been inflated, and the amount certified in 2019 artificially reduced, by an unknown amount because both state and federal law provided incentives for developers to commence projects prior to July, 2018, which might otherwise have been undertaken at a later date. In addition to the $3,500,000 limit under state law commencing on July 1, 2018, certain provisions of the federal Tax Cuts and Jobs Act (TCJA) reduced the economic value of historic rehabilitation tax credits after June 20, 2018 (due to a certain transition rule under which prior federal law would apply for projects commenced prior to that date). The TCJA requires taxpayers take the 20% credit ratably over five years instead of in the year they placed the building into service, thereby reducing the present value of the nonrefundable credit. Further, the TCJA limited the ability of certain multinational companies to claim the credit, which effectively eliminated all value of the credit for these entities (which may otherwise have been interested in purchasing the credit from a developer). These factors do not apply to projects commenced prior to June 20, 2018.

8. The bill would sunset the current limit for the state supplement to the federal historic rehabilitation tax credit (which prohibits WEDC from certifying a claimant for more than $3,500,000

for all rehabilitation projects undertaken on the same parcel of tax credits), and, as of July 1, 2019, replace it with a new limit such that WEDC would not be able to certify anyone to claim more than a total of $3,500,000, for any project, regardless of the number of parcels on which the project is undertaken.

9. This provision is intended to prevent a developer from qualifying for multiple state tax credits by developing multiple parcels of land in a single project. In such cases, current law may effectively provide for a higher limit for a large historic structure simply because it spans across multiple parcels.

10. The Committee could approve the Governor's proposed modification to prevent applicants from circumventing the limit on certifications and to provide for the same treatment of historic rehabilitation projects regardless of the number of parcels they span (Alternative 1).

11. On the other hand, because the current limitation would be sunset, it is possible that the changes under the bill could potentially allow WEDC to certify applicants to receive more than $3,500,000 in state tax credits for multiple projects on a single parcel of land. For example, the same developer could undertake subsequent projects on the same historic structure by rehabilitating different floors at different times.

12. Alternatively, in order to more effectively limit the use of historic rehabilitation tax credits for larger projects, the Committee could decide to retain limits on both the basis of a single parcel and a single project (Alternative 2). This would prohibit WEDC from certifying more than $3,500,000 of tax credits for any single project on multiple parcels or multiple projects on a single parcel. As a result, an applicant could not circumvent the intent of the limit by undertaking subsequent projects on the same parcel or a single project on multiple parcels.

ALTERNATIVES

1. Approve the Governor's recommendation to sunset the limitation under current law restricting WEDC from certifying persons to receive no more than $3,500,000 for all rehabilitation projects undertaken on the same parcel as of July 1, 2019, and replace it with a $3,500,000 limit per project.

2. Modify the Governor's recommendation to retain the limitation under current law restricting WEDC from certifying persons to receive no more than $3,500,000 for all rehabilitation projects undertaken on the same parcel. Beginning with certifications on or after July 1, 2019, WEDC would be able to certify persons to receive no more than $3,500,000 for any project, regardless of the number of parcels on which the project is undertaken, and in no event could WEDC certify persons to receive more than $3,500,000 for all rehabilitation projects undertaken on the same parcel.

3. Take no action. The limitation under current law restricting WEDC from certifying persons to receive no more than $3,500,000 for all rehabilitation projects undertaken on the same parcel would be retained.

Prepared by: John D. Gentry
Attachment

ATTACHMENT

WEDC Historic Tax Credit Contracts
(as of May 1, 2019)

Contract Date	Certified Business	Location	Amount	Project End Date
3/25/2014	Longfellow Historic, LLC	Madison	$1,543,000	8/31/2014
3/27/2014	Julie M. Halsne	Mayville	13,600	3/3/2017
4/2/2014	Lehmkuhl Enterprises LLC	Racine	12,493	7/31/2017
4/9/2014	Stephen Green	Waukesha	26,000	8/31/2018
4/9/2014	West II Building Corporation	Ashland	14,100	9/30/2015
4/25/2014	1818 MLK Drive LLC	Milwaukee	262,119	8/31/2014
6/23/2014	207 East Michigan Street, LLC	Milwaukee	240,000	9/30/2015
6/23/2014	Mitchell Street Group LLC	Milwaukee	422,918	8/22/2016
7/17/2014	Housing Authority of Oshkosh	Oshkosh	1,500,000	1/31/2016
7/29/2014	Pritzlaff Redevelopment LLC	Milwaukee	4,131,600	12/31/2018
7/29/2014	Beam House Apartments LLC	Milwaukee	2,200,000	6/15/2019
8/8/2014	New Orpheum, LLC	Madison	600,000	10/14/2019
8/14/2014	407 N Grand Partnership	Waukesha	18,000	9/30/2015
9/3/2014	Paper Box Lofts Limited Partnership	Milwaukee	2,700,000	12/31/2014
9/9/2014	Mo Street Development LLC	Milwaukee	4,360,000	8/31/2015
9/16/2014	Beilke, LLC	De Pere	13,000	7/31/2014
9/19/2014	Pance LLC	La Crosse	60,000	12/31/2017
9/19/2014	Doerflinger's Second Century, Inc.	Madison	70,000	7/31/2014
10/22/2014	Ringling Theatre Holding, Inc.	Baraboo	670,183	9/30/2017
11/12/2014	Iron Block Building Partners LLC	Milwaukee	1,900,000	8/1/2015
11/14/2014	Karen Baggot	Mauston	15,000	9/30/2019
11/18/2014	O'Kroley/646 LLC	Madison	10,000	9/29/2019
11/20/2014	Railway Exchange Building LLP	Milwaukee	331,942	9/29/2019
12/10/2014	Eau Claire Limited Partnership	Eau Claire	782,353	12/31/2015
1/20/2015	Bob's Bitchin' BBQ LLC	Dodgeville	141,992	12/31/2016
1/20/2015	HB Callahan Block	La Crosse	36,000	10/31/2016
1/23/2015	Historic Third Ward Development LLC	Milwaukee	1,300,000	5/16/2017
1/23/2015	Milwaukee Fortress LLC	Milwaukee	9,146,810	12/15/2019
2/16/2015	Elementary Apartments LLC	Schofield	784,210	12/31/2015
2/16/2015	Steensland/Bethel LLC	Madison	249,273	12/30/2015
2/18/2015	Florida Lofts LLC	Milwaukee	4,414,818	6/30/2015
2/26/2015	Divall Nichols Station Associates A Wisconsin Limi	Madison	1,018,211	11/30/2020
2/26/2015	James and Suzanne Holton	Milwaukee	63,600	10/31/2016
3/3/2015	Ross Acquisition, LLC	Kaukauna	4,387,659	9/15/2015
3/3/2015	Grand Kakalin, LLC	La Crosse	1,407,200	9/10/2017
3/10/2015	Historic Lincoln School, LLC	Shawano	556,106	9/23/2016
3/19/2015	Holy Name Heights, LLC	Madison	3,721,615	6/1/2016
4/2/2015	BrewCity Redevelopment Group, LLC	Milwaukee	580,000	4/7/2019
4/22/2015	Artist Lofts, LLC	Milwaukee	1,690,680	6/30/2016
4/22/2015	225 East Michigan Street LLC	Manitowoc	2,541,531	8/31/2017

Contract Date	Certified Business	Location	Amount	Project End Date
4/27/2015	Toho Properties LLC	La Crosse	$406,200	10/31/2014
4/27/2015	The Wedding Tree	Green Bay	140,000	12/30/2017
5/4/2015	Judge Jason Downer House LLC	Sauk City	268,185	12/31/2016
5/4/2015	FOLR, LLC	Milwaukee	193,772	3/15/2015
5/7/2015	RLR Properties of La Crosse, LLC	La Crosse	31,800	12/31/2015
5/28/2015	2430 Lake LLC	Milwaukee	42,915	2/1/2014
6/2/2015	Blue Ribbon Suites LLC	Milwaukee	7,728,462	7/31/2016
6/30/2015	Discovery Properties, LLC	Oshkosh	664,451	4/1/2017
7/9/2015	531 N. Main, LLC	Oshkosh	339,279	8/31/2015
7/10/2015	Impact Seven, Inc.	Rice Lake	421,213	3/31/2018
8/4/2015	Twekenberg 237 LLC	Madison	15,830	10/17/2014
8/18/2015	S.C. Johnson & Son, Inc.	Racine	500,000	12/31/2016
8/24/2015	Welford Sanders Lofts LLC	Milwaukee	3,956,893	9/30/2018
8/31/2015	Varin/Library Park II LLC	Kenosha	1,994,000	3/31/2019
9/14/2015	Global Water Center II LLC	Milwaukee	1,700,000	6/30/2019
9/18/2015	Carriage Works Real Estate, LLC	Janesville	94,380	12/31/2017
9/23/2015	Milwaukee Pabst Holdings LLC	Milwaukee	7,637,098	12/31/2019
9/28/2015	Greene Bros' Holdings, Inc	Janesville	721,024	4/30/2016
9/29/2015	605 Erie Avenue, LLC	Madison	54,742	12/31/2015
9/29/2015	Roosevelt School Apartments, LLC	Sheboygan	1,200,000	12/30/2017
9/29/2015	144 Langdon Street Historic LLC	La Crosse	409,800	3/31/2016
11/5/2015	Cream City Properties LLC	Milwaukee	68,110	12/31/2018
11/13/2015	2219 Lofts Limited Partnership	La Crosse	957,232	12/31/2018
12/22/2015	Greater Green Bay YMCA	Green Bay	4,118,000	12/31/2021
1/3/2016	Washington School Apartments, LLC	Sheboygan	1,600,000	12/31/2018
1/7/2016	LMN Investment Properties, LLC	Platteville	117,939	10/31/2018
2/3/2016	Lorenzen Holdings LLC	Green Bay	600,000	12/31/2018
2/4/2016	Watertown Main Street Holdings, LLC	Watertown	500,000	12/31/2020
2/9/2016	Button Block Holdings LLC	Milwaukee	3,505,049	11/1/2017
2/12/2016	Shoe Factory Lofts - Milwaukee LLC	Milwaukee	1,780,000	12/31/2018
2/12/2016	611 W National Avenue Milwaukee LLC	Milwaukee	1,251,768	7/14/2018
4/4/2016	Blue Ribbon Management LLC	Milwaukee	680,129	12/31/2018
4/13/2016	Schusters Redevelopment LLC	Milwaukee	12,725,662	12/31/2021
4/14/2016	Mitchell on Water LLC	Milwaukee	1,355,189	12/31/2020
5/2/2016	Germania Real Estate Venture II LLC	Milwaukee	3,512,347	2/28/2018
5/2/2016	Haymarket Lofts LP	Milwaukee	2,719,202	4/30/2018
6/2/2016	RLR Properties of La Crosse, LLC	La Crosse	40,000	12/31/2016
6/13/2016	Mitchell Street Apartments LLC	Milwaukee	3,260,000	12/12/2018
6/22/2016	Batavian Building, LLC.	La Crosse	340,000	2/3/2021
7/8/2016	Doerflinger's Second Century, Inc.	La Crosse	83,227	6/30/2016
7/19/2016	Kenosha Heritage House LLC	Kenosha	2,215,912	12/31/2017
8/1/2016	Barclay Historic LLC	Milwaukee	4,620,000	6/29/2021
8/8/2016	Woolen Mills Lofts-Appleton, LLC.	Watertown	2,160,000	12/31/2016
8/8/2016	Schempf Building, LLC	Appleton	307,801	7/1/2021
8/16/2016	DBGreen, LLC	Stevens Point	245,000	10/20/2018

Contract Date	Certified Business	Location	Amount	Project End Date
8/22/2016	Union Bank & Trust Company	Evansville	$240,400	5/11/2019
8/31/2016	336 N Milwaukee St LLC	Milwaukee	1,640,000	12/31/2018
9/12/2016	207 East Michigan Street, LLC	Milwaukee	440,000	5/15/2021
9/14/2016	RP Nutrients Inc.	East Troy	292,000	12/31/2019
9/27/2016	Insight Industries, LLC	Platteville	60,000	4/24/2019
11/9/2016	Historic Garfield Apartments LLC	Milwaukee	1,289,055	10/30/2019
11/28/2016	240 Algoma Blvd, LLC	Oshkosh	526,636	11/30/2016
11/28/2016	Donna Schultz - 41 S. Broad St. Bayfield	Bayfield	30,000	10/25/2018
12/1/2016	15th and North Apartments LLC	Milwaukee	1,579,318	2/28/2019
12/15/2016	213 2nd St LLC	Milwaukee	120,000	9/28/2019
12/15/2016	JJAWC, LLC	La Crosse	9,425,566	11/30/2021
12/19/2016	Waite Rug Housing, LLC	Superior	3,327,974	3/31/2019
12/19/2016	Empire Block, LLC	Oshkosh	1,228,887	11/24/2019
12/21/2016	Parish School Apartments, LLC	Fond du Lac	1,650,000	1/31/2018
12/28/2016	Lawler School Lofts, LLC	Prairie du Chien	1,800,000	1/14/2020
1/10/2017	Peperoni Cannoli, LLC	Milwaukee	76,000	6/30/2017
1/12/2017	Henry L. Doane	Madison	80,000	10/1/2018
1/12/2017	Tenney, LLC	Madison	423,000	11/30/2021
1/17/2017	Garver Feed Mill LLC	Madison	2,400,000	5/1/2018
2/6/2017	Circa on Seventh, LLC	Racine	89,611	9/15/2019
2/9/2017	State and West, LLC	La Crosse	153,010	3/31/2018
2/15/2017	Wiegand Investments 2711 LLC	Milwaukee	4,088,927	10/31/2022
2/27/2017	Historic Berlin School Apartments, LLC	Fond du Lac	1,441,286	10/20/2018
2/27/2017	Exchange at 104, LP	Berlin	1,785,233	5/1/2018
4/3/2017	Wiegand Investments 2711 LLC	Milwaukee	6,135,399	9/11/2022
4/4/2017	Beloit Powerhouse, LLC	Beloit	7,500,938	7/31/2020
4/11/2017	St. Anthony's Apartments LLC	Milwaukee	2,525,538	12/31/2018
4/17/2017	Atrium Lofts Limited Partnership	Wausau	1,191,192	6/30/2018
5/1/2017	Daniel Kessenich	Madison	50,000	4/1/2019
5/8/2017	VMC Lofts, LLC	Kenosha	3,382,662	3/21/2020
5/9/2017	LearnEMC, LLC	Stoughton	46,359	1/26/2023
5/10/2017	Fifth Street School LLC	Milwaukee	1,739,758	12/31/2018
5/26/2017	K.L.C. Properties, LLC	La Crosse	383,600	12/31/2017
5/26/2017	Sartori Company	Plymouth	1,300,000	10/19/2022
6/5/2017	National Soldiers Home Residences I LLC	Milwaukee	7,018,580	9/1/2023
6/6/2017	Ambassador Suites LLC	Milwaukee	4,836,172	4/11/2023
6/6/2017	Cecelia Building LLC	Milwaukee	2,418,086	5/31/2022
6/7/2017	Cecelia Annex LLC	Milwaukee	1,813,229	5/31/2022
6/12/2017	214 Florida LLC	Milwaukee	3,940,737	3/29/2020
6/12/2017	Hotel Retlaw, LLC	Fond du Lac	4,600,000	5/30/2019
6/12/2017	Mt. Horeb Opera House, LLP	Mount Horeb	61,600	3/20/2023
6/12/2017	National Soldiers Home Residences II LLC	Milwaukee	1,136,000	9/1/2023
6/12/2017	National Soldiers Home Residences III LLC	Milwaukee	592,000	9/1/2023
6/15/2017	Quantum Leap, LLC	Platteville	25,000	9/30/2017
6/19/2017	101 West Main LLC	Waukesha	1,495,000	8/15/2018

Contract Date	Certified Business	Location	Amount	Project End Date
6/19/2017	Driver Opera House Restoration, Inc.	Darlington	$265,368	6/25/2018
6/20/2017	AAL Community Center, LLC	Milwaukee	1,210,533	7/31/2020
6/21/2017	Century Building Milwaukee LLC	Oshkosh	2,190,000	12/1/2018
6/23/2017	Haggero's Mall LLC	Waupaca	2,476,500	9/1/2022
6/23/2017	Danes Hall of Waupaca, LLC	Milwaukee	220,000	4/17/2020
6/23/2017	Docks Building LLC	Milwaukee	2,700,000	3/28/2023
6/23/2017	Matthews Building LLC	Milwaukee	1,324,894	5/31/2022
6/26/2017	219 MKE LLC	Milwaukee	43,200	12/31/2018
6/26/2017	Whitney School Development, LLC	Milwaukee	1,300,000	10/1/2018
6/26/2017	1037 West McKinley Avenue LLC	Green Bay	1,240,000	7/15/2018
6/27/2017	Doneff's Shuette Building	Menomonee Falls	1,820,822	12/31/2018
6/27/2017	National Block, LLC	Milwaukee	1,244,228	3/15/2020
6/27/2017	Appleton 175 LLC	Manitowoc	257,600	5/30/2018
6/27/2017	Coakley Brothers Company	Milwaukee	1,700,000	12/31/2018
6/29/2017	Luther Memorial Evangelical Lutheran Church, INC.	Madison	880,000	11/30/2017
6/29/2017	North Waite Plaza, LLC	Oshkosh	892,584	7/1/2019
10/23/2017	331 South 3rd Street LLC	Milwaukee	939,859	3/1/2019
1/8/2018	D&L Baumhardt, LLC	Fond du Lac	117,422	6/30/2019
1/29/2018	Winston Holdings, LLC	Madison	34,060	8/1/2020
2/13/2018	405 Washington Ave, LLC	Oshkosh	944,703	9/1/2018
2/13/2018	Cedar Hill Multi-Family Properties, LLC	La Crosse	117,150	12/13/2020
2/19/2018	Kleuter Building LLC	Madison	3,480,000	9/13/2020
3/19/2018	Dale Berg	La Crosse	460,981	11/7/2020
4/10/2018	Carroll University, Inc.	Waukesha	2,240,278	12/26/2020
4/19/2018	TNSH Landlord LLC	Milwaukee	11,085,600	6/22/2023
4/23/2018	John M. Evans Hall, LLC	Evansville	53,240	11/14/2022
4/26/2018	Governors Mansion LLC	Madison	256,674	11/28/2020
4/30/2018	Sheboygan County Economic Development Foundation	Plymouth	300,000	10/30/2019
5/2/2018	CB Teweles Redevelopment LLC	Milwaukee	6,721,087	2/12/2023
5/4/2018	Barton School Apartments, LLC	West Bend	1,100,000	3/15/2023
5/11/2018	Candise Street Lofts, LLC	Jefferson	1,800,000	2/27/2023
5/25/2018	Live Here LLC	Madison	23,923	12/6/2020
6/4/2018	758 North Broadway, LLC	Milwaukee	9,480,000	3/12/2023
6/6/2018	Friar House Flats, LLC	Green Bay	1,280,000	3/20/2023
6/6/2018	Platform II Wisconsin LLC	Milwaukee	643,200	3/23/2021
6/10/2018	304 North Adams Green Bay LLC	Green Bay	8,855,879	1/20/2020
6/11/2018	Community Within The Corridor Limited Partnership	Milwaukee	12,400,000	1/31/2023
6/14/2018	Badger State Lofts, LP	Sheboygan	5,638,570	3/12/2023
6/19/2018	David V. & Leigh Mollenhoff (Joint Filers)	Madison	13,392	2/20/2017
6/19/2018	Zuelke Building, LLC	Appleton	3,400,000	2/12/2023
6/21/2018	600 North Broadway LLC	Milwaukee	287,151	3/18/2023
6/21/2018	Gold Medal Lofts, LLC	Racine	3,074,141	2/14/2023
6/30/2018	507 South 2nd Street Development, LLC	Milwaukee	3,298,000	3/11/2023
9/13/2018	Hotel Metro LLC	Milwaukee	1,064,000	2/23/2021
9/20/2018	McKinley School Apartments, LLC	Milwaukee	2,112,004	11/30/2023

Contract Date	Certified Business	Location	Amount	Project End Date
9/26/2018	107 King St LLC	Madison	$65,412	3/26/2021
11/8/2018	833 West Wisconsin Avenue, LLC	Milwaukee	1,400,000	6/6/2021
12/14/2018	William J. Sodemann	Janesville	22,253	12/8/2019
12/19/2018	GenCap Delavan 73, LLC	Delavan	2,613,457	9/19/2021
2/13/2019	Kono Properties LLC	Baraboo	42,000	6/18/2021
4/14/2019	Lazy Meadows Homes LLC	Marshfield	100,000	3/5/2021

Source: Wisconsin Economic Development Corporation.

Legislative Fiscal Bureau
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June, 2019 | Joint Committee on Finance | Paper #331

Administration of WEDC-Certified Business Tax Credits (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2019-21 Budget Summary: Page 137, #5; Page 145, #22; Page 146, #25; Page 147, #26; and Page 149, #34]

CURRENT LAW

In general, businesses may be eligible to claim a tax credit when preparing and filing the required individual income and corporate income/franchise tax forms with Department of Revenue (DOR). A tax credit is an amount that is subtracted from the gross income tax liability of a taxpayer in a given tax year.

If a nonrefundable credit exceeds tax liability, any amounts claimed that cannot be used to offset tax liability are identified so that the taxpayer can carry the unused amount forward for use in a future tax year. Taxpayers claim a refundable credit to reduce taxes otherwise due and/or to receive a check for the amount of the credit in excess of the claimant's tax liability in that year. Alternatively, a business may choose to apply any excess refundable tax credit as a payment towards its tax liability in the next year.

Nonrefundable credits are counted as revenue reductions in the state's accounting system. Refundable credits are paid from appropriations and counted as state expenditures from the general fund.

Pass-through entities (partnerships, limited liability companies (LLCs), and tax-option (S) corporations) may not claim the credits directly, but the eligibility for, and the amount of, the credit are based on their eligible activities. Pass-through entities must compute the amount of credit that each of their owners may claim and provide that information to each of them. Partners of a partnership, members of LLCs, and shareholders of S corporations may claim the credit in proportion to their ownership interest.

Some business tax credits are jointly administered by DOR and the Wisconsin Economic Development Corporation (WEDC). WEDC is responsible for certifying and verifying eligible claimants under the following tax credit programs: (a) business development; (b) enterprise zones; (c) electronics and information technology manufacturing (EITM) zone; (d) development opportunity zone; (e) historic preservation; and (f) early stage seed and angel investment. Claimants are required to include, with their tax returns, a copy of the certification for tax benefits and verification of expenses from WEDC.

Business development credits may be awarded throughout the state. EITM zone credits may be awarded only to businesses that conduct operations in one specific geographical zone designated by WEDC. Similar to the EITM zone program, WEDC may award enterprise zone credits for businesses that conduct operations in specific geographic zone areas designated by WEDC.

In practice, WEDC has designated enterprise zone credits on the basis of specific economic development projects performed by individual companies, rather than to multiple companies located in a geographic area. Pursuant to 2017 Act 369, there is no specific limit on the number of enterprise zones which WEDC may designate. Instead, each designation is subject to approval by the Committee under a 14-day passive review process. When designating an enterprise zone, WEDC must consider the economic need of the area and the effect on other initiatives and programs to promote economic and community development in the surrounding area. WEDC is required to certify at least three enterprise zones in a political subdivision with populations of fewer than 5,000, and two enterprise zones in political subdivisions with populations between 5,000 and 30,000.

For all tax credits administered by WEDC, DOR must track the amount of credits that have been claimed or used to offset tax liability and the amount of all available unused credits. WEDC is required to provide certain information to DOR by the last day of the first month of each calendar quarter for each of the credits that the two agencies jointly administer, including any credits transferred to another claimant.

In general, when certifying a recipient for a tax credit, WEDC must require the recipient to sign a contract which sets out a compliance schedule of anticipated actions and reporting requirements. WEDC must independently verify, from a sample of tax credits, the accuracy of the information required to be reported. WEDC must revoke a certification for tax benefits if the recipient submits false or misleading information. Further, specific requirements regarding revocation apply for certain tax credit programs.

WEDC may require tax credit repayment clauses in its contracts for not meeting contract obligations or when revoking a certification. For example, WEDC must require recipients to repay tax benefits for failing to maintain contracted levels of employment or capital expenditures under its tax credit programs. WEDC may recover EITM zone credits that are revoked or otherwise invalid from a partnership, limited liability company, or tax-option corporation or from the individual partner, member, or shareholder. However, current law does not specify to which state agency recovered credits must be repaid for other tax credits.

Pursuant to Wis. Stat. § 20.906, agencies generally must deposit funds received on behalf of the state within one week into the state treasury, which is administrated by the Department of Administration (DOA). However, WEDC is created as an "authority" under state law, rather than an "agency."

GOVERNOR

The bill would require that, no later than seven days after WEDC receives a repayment of tax credits, WEDC must remit the full amount of that payment to the Secretary of DOA for deposit in the general fund. According to the administration, the provision is intended to conform to an issue highlighted by the Legislative Audit Bureau (LAB) as part of its May, 2017, report (Report 17-9) for legislative consideration.

Further, the bill would provide estimated funding of $18,100,000 GPR in 2019-20 and $18,400,000 GPR in 2020-21 for the business development credit, $211,954,900 GPR in 2020-21 for the EITM zone credit, and $64,300,000 GPR in 2019-20 and $50,700,000 GPR in 2020-21 for the enterprise zone tax credit.

LFB Papers #327 and #329 address budget related issues regarding the business development tax credit and enterprise zone tax credit, respectively. The estimated funding level for the enterprise zone tax credit is revised higher in 2020-21 to $81,700,000 GPR under LFB Paper #327 and the estimated funding level for the business development tax credit is revised higher in 2019-20 to $18,700,000 and in 2020-21 to $20,100,000 under LFB Paper #328.

DISCUSSION POINTS

1. As noted, WEDC has extensive administrative responsibilities over certain business tax credits. This paper presents alternatives to clarify the administrative responsibilities for paying tax credits to, and recovering revoked credits from, businesses certified under economic development programs by WEDC. This paper also presents an alternative to codify WEDC's current practice of designating enterprise zones based on individual businesses rather than geographic location.

Recovery of WEDC-Administered Refundable Tax Credits

2. If tax credit recipients do not perform the terms of their contracts with WEDC, they may be required to repay the amount of tax credits previously claimed. Typically, in an event of default, the contract would allow for either WEDC or DOR (but not both) to recover 100% of the tax credits verified by WEDC and claimed by the recipient from DOR plus certain penalties, interests, and fees.

3. LAB Report 17-9 found that tax credit recipients repaid $5.3 million to WEDC from July, 2016, through November, 2016. However, WEDC indicated to LAB on March 16, 2017, that it had not yet deposited the $5.3 million with DOA. Instead, WEDC indicated that it had a verbal agreement with DOA, under which it could retain the funds unless, and until, DOA requested their return. Seven days later, WEDC deposited $5.3 million with DOA.

4. As stated in Report 17-9, state law generally requires agencies to deposit at DOA within

one week any funds received on behalf of the State. However, Report 17-9 indicated that because WEDC is not a state agency, current law does not specify how frequently WEDC is required to deposit tax credits with DOA. Report 17-9 recommended that current law be modified to require WEDC to deposit all tax credits repaid to it with DOA within one week.

5. The Committee could adopt the Governor's recommendation in order to clarify that WEDC may not retain repayments of tax credits recovered pursuant to its contracts with certified businesses (Alternative A1). This alternative would require WEDC to return all recovered state funds to DOA, rather than potentially allowing WEDC to retain and expend those monies as part of its economic development programs.

6. Alternatively, the Committee could take no action on the Governor's recommendation and instead modify the bill to require that all repayment of tax credits be directed to DOR rather than to WEDC (Alternative A2). Under this alternative, WEDC could not actually obtain the repayment of tax credits under its contracts, and would instead remit to DOR the amounts that must be repaid. DOR would ultimately receive the payment and remit the funds to DOA.

7. Although WEDC may know the amount of tax credits it verifies a recipient to claim and the amount that are revoked, nonrefundable and refundable tax credits are actually claimed at DOR. Thus, it is DOR, and not WEDC, which has direct knowledge of the amounts each year that have been actually paid to claimants or used to offset tax. Current law provides DOR authority to recover tax amounts due and owing.

8. Any nonrefundable credit claimed at DOR that is used to offset tax reduces state general fund tax revenues. If a claimant did not have sufficient tax liability to use the full amount of a revoked credit, DOR would know the used credit amount that must be repaid, whereas WEDC would not have such information. Any refundable credit claimed in excess of tax owed that is disbursed to a claimant is a state expenditure paid out of the general fund. In either case, expenditures or reduced revenues related to a tax credit claim are not attributed to WEDC's appropriations or revenues and are authorized by DOR. As such, the Committee could conclude that DOR is better suited to recover such funds.

9. Finally, the Committee could elect both Alternatives A1 and A2 (Alternative A3). This would clarify current law so that DOR is the proper party for repayment, but in the event that WEDC does receive a repayment of a tax credit, WEDC would be required to remit it to DOA within a week.

Payment of WEDC-Administered Refundable Business Tax Credits

10. Most state tax deductions and credits do not require prior approval from a state agency; all eligible persons may claim the tax benefits. In contrast, the credits discussed in this paper are awarded at WEDC's discretion, subject to statutory requirements, and are very similar to grants paid directly by the certifying agency.

11. The business development credit, enterprise zone credit, and EITM zone credit are refundable. Similar to grants awarded by state agencies, refundable tax credits are not affected by a claimant's tax liability and are recorded as state expenditures. According to DOR, in tax year 2016, claims for WEDC-certified refundable credits totaled $45.0 million. Of this amount, $8.2 million

(18%) was used to offset the claimants' tax liability and $36.8 million (82%) was refunded to the claimants.

12. The business development credit, enterprise zone credit, and EITM zone tax credits may be claimed if pass-through entities conduct eligible economic activities in the state. However, unlike grants awarded by state agencies, the credits are not directly claimed by the business entity that conducted the eligible activities. Instead, the credits are passed through to the individual owners of the entity and claimed on their individual income tax returns. This is also the case for S corporations, LLCs, and partnerships electing to be taxed at the entity level under the provisions of 2017 Act 368.

13. Often, owners of pass-through entities are other pass-through entities, which, in turn, may be owned by still other pass-through entities. This makes it difficult to ascertain whether individual credit claims are valid without further review of multiple pass-through entities' tax returns. Also, with this arrangement, the tax benefits only indirectly assist the business entity that received certification from WEDC and conducted the eligible activities.

14. Furthermore, after a business is certified for tax benefits by WEDC, several years may pass before WEDC verifies that the business has completed the required activities, and additional time may elapse before the credit is actually claimed on a tax return. When claimed, DOR will not be directly aware of that claimant's performance under its contract with WEDC.

15. In fiscal year 2017-18, WEDC entered into contracts to award refundable tax credits totaling $2,970.1 million, which can be earned and claimed over the next several years, including: (a) $2,850.0 million in EITM zone credits; (b) $104.5 million in enterprise zone credits; and (c) $15.6 million in business development credits.

16. Under current law, funding for these tax credits does not appear in WEDC's appropriation schedule even though WEDC is responsible for nearly all aspects of awarding the credits. Instead, the costs of the EITM zone credit, enterprise zone credit, and the business development credit appear in separate GPR appropriations under "Shared Revenue and Tax Relief" in the schedule of appropriations. The value of these credits exceeds $96 million in 2018-19. Further, as amended by the sum sufficient reestimates described above, the bill would provide funding of $396.8 million during the 2019-21 biennium for these credits. This is far larger than WEDC's base funding level for its operations and other economic development programs ($41,550,700 all funds annually). Appropriations under "Shared Revenue and Tax Relief" are primarily aids to counties and municipalities and are not related to tax credits for businesses. It would be more appropriate to place these credits under WEDC.

17. The budgetary impact of WEDC's activities would be more transparent if the existing tax credit appropriations were transferred to, and paid to businesses by, WEDC (Alternative B1). Under this alternative, the Committee could retain the current business development, EITM zone, and enterprise zone tax credits, but require WEDC to pay credit claims directly to the business entity that is eligible for the credit rather than requiring that claims be filed with DOR. Payments would be made to eligible C corporations, pass-through entities, and sole proprietors from GPR appropriations for these tax credits using policies and procedures developed by the WEDC Board. The main advantage of this approach is that WEDC would make a single payment to eligible pass-through entities rather than having multiple individual owners file relatively small credit claims with DOR. This would

reduce the potential for fraudulent claims and significantly decrease paperwork and processing requirements for these credits. It would also enhance transparency and accountability for these programs and provide the applicable financial benefits directly to the business entity that conducted the eligible activities.

18. Under the Governor's proposal discussed above, any tax credits recovered by WEDC would be required to be paid to DOA within seven days. WEDC would not be permitted to retain any funds for use in its programs or operations. Likewise, alternatives A2 and A3 would also prohibit WEDC from retaining recovered tax credits, as they would be recovered by DOR.

19. Alternatively, the Committee could choose to only eliminate the current provisions regarding pass-through entities and, instead, require eligible pass-through entities to file credit claims with DOR and require credit payments to be made directly to the pass-through entity (Alternative B2). As with the preceding option, this alternative would reduce the potential for fraudulent claims and reduce paperwork and processing requirements for these credits. It would also provide the financial benefits directly to the business entity that conducted the eligible activities.

20. A potential drawback of having pass-through entities claim the credit is that individual owners of such entities would no longer be able to reduce their estimated tax payments in anticipation of receiving the credit. Thus, the Committee could choose to maintain current law (Alternative B3).

Enterprise Zone Designations by WEDC

21. State law provides little guidance as to what geographic area should comprise an enterprise zone. WEDC states that certain businesses have been awarded enterprise zone credits for economic development projects in non-contiguous geographic areas throughout the state. Further, under the current statutory construction, as long as so approved by the Committee, state law does not prohibit an enterprise zone that could encompass the entire state for an unlimited number of businesses to receive enterprise zone credits.

22. As discussed above, in practice, enterprise zone credits have been awarded on the basis of specific economic development projects performed by individual companies, rather than to multiple companies located in a geographic area.

23. The Committee could choose to statutorily codify WEDC's current practice of certifying businesses as eligible to receive the credits, rather than certifying businesses in a geographically designated zone for the credits by eliminating the term "zones" under the enterprise zone program and replacing it with "projects" (Alternative C1). Under this alternative, WEDC could certify, with the Committee's approval, businesses as eligible to receive enterprise zone tax credits for economic development projects performed by certified businesses in the state. The criteria for whether a business could be certified by WEDC to receive the credits would be the same as under current law.

ALTERNATIVES

A. Recovery of WEDC-Administered Tax Credits

1. Approve the Governor's recommendation and require WEDC to remit the full amount

of any repayment of tax credits it receives to the Secretary of DOA for deposit in the state general fund within seven days of their receipt.

2. Take no action on the Governor's recommendation. Instead, clarify current law to require that all repayments of tax credits administrated by WEDC be paid directly to DOR.

3. Adopt Alternative 1, but with the modification to require in WEDC's tax credit contracts that all repayments of tax credits administrated by WEDC be paid directly to DOR.

4. Take no action.

B. Payment of WEDC-Administered Tax Credits

1. Maintain the current EITM zone, enterprise zone, and business development tax credits, but transfer the existing GPR appropriations for these programs to WEDC and require that credit claims be filed with, and paid by, WEDC using policies and procedures developed by the WEDC Board. Provide under WEDC's appropriations, rather than under the title "Shared Revenue and Tax Relief," $83,000,000 GPR in 2019-20 and $313,754,900 GPR in 2020-21 for the transferred sum sufficient tax credit appropriations. Specify that this provision would first apply to credit claims filed on September 1, 2019. In addition, require credits earned by pass-through entities to be claimed by, and paid to, the business entity instead of the individual owners of the business, effective with credits earned by pass-through entities on January 1, 2020. This would include pass-through entities electing to pay tax at the entity level pursuant to 2017 Act 368. For credits earned on or after that date, prohibit partners of a partnership, members of LLCs, and shareholders of S corporations from claiming the credits individually. Specify that credits have been revoked or that are otherwise invalid may be recovered from either the pass-through entity or the individual owners of the entity. [The funding amounts identified above are equal to the sum of the appropriations under the bill for the business development, enterprise zones, and EITM zone tax credits with revised amounts described under LFB Papers #327 and #328.]

2. Effective with credits earned by pass-through entities in taxable years beginning on January 1, 2020, eliminate the current provisions of the refundable business development tax credit, EITM zone tax credit, and enterprise zone tax credit regarding pass-through entities. Instead, require eligible pass-through entities to file claims for these credits with DOR and require that credit payments be made directly to the pass-through entity. This would include pass-through entities electing to pay tax at the entity level pursuant to 2017 Act 368. Prohibit partners of a partnership, members of LLCs, and shareholders of S corporations from claiming the credits individually. Specify that credits have been revoked or that are otherwise invalid may be recovered from either the pass-through entity or the individual owners of the entity.

3. Maintain current law.

C. Enterprise Zone Designation by Project

1. Amend the enterprise zone tax credit statutes so that rather than designating specific

geographic zones, WEDC could certify, with the Committee's approval, businesses as eligible to receive enterprise zone tax credits for economic development projects undertaken by those businesses in Wisconsin. The criteria for whether a business could be certified by WEDC to receive the credits would be the same as under current law.

2. Maintain current law.

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June, 2019 Joint Committee on Finance Paper #332

Repeal Obsolete Refundable Credits and Appropriations (General Fund Taxes -- Income and Franchise Taxes)

CURRENT LAW

The following refundable income and franchise tax credits were sunset for new claims beginning in tax year 2014: (a) dairy manufacturing facility investment; (b) dairy manufacturing facility investment for dairy cooperatives; (c) food processing plant and food warehouse investment; (d) beginning farmer and farm asset owner; (e) film production company investment; and (f) film production services. The refundable woody biomass harvesting and processing investment credit was sunset for new claims beginning in tax year 2015. For refundable credits, if the amount of credit exceeds the claimant's tax liability, the state issues a check for the excess amount or the claimant may apply the credit against the next year's tax liability. Refundable credits are paid from appropriations and counted as expenditures in the state's accounting system. Current law provides a sum sufficient GPR appropriation to pay credit claims for each of the credits shown above, and base funding of $0 is provided for each appropriation. These credits were sunset under 2013 Wisconsin Act 20.

An annual GPR appropriation was provided to make payments to Illinois of not more than $5,500,000 for tax year 1998 and not more than $8,250,000 for tax year 1999, the first two years in which the Department of Revenue (DOR) made income tax reciprocity payments to Illinois. Base funding of $0 is provided for this appropriation.

GOVERNOR

Maintain base funding of $0 in 2019-20 and 2020-21 for each of the current law appropriations listed above. Retain current statutes.

DISCUSSION POINTS

1. Refundable tax credit appropriations and associated statutes are generally sunset, rather

than repealed, to allow eligible claimants to claim the credit when timely filing a return or an amended return. For example, if an individual filer was eligible to claim the film production services credit, which sunset after tax year 2013, the individual is generally required to file a tax return and claim the credit by April 15, 2014. However, taxpayers may file an amended return to claim the credit for up to four years beyond the unextended due date of the tax year. As a result, an eligible claimant could file an amended return to claim the credit until April 15, 2018 (state fiscal year 2017-18).

2. Corporate filers may have a tax year that does not align with a calendar year, and certain filers may timely file a return on the 15th day of the fifth month beginning after the corporation's tax year. Under the example above, a taxpayer with a tax year beginning on December 1, 2013, could file an amended return to claim the film production services credit until April 15, 2019 (2018-19). The Committee could choose to repeal the six refundable business tax credit appropriations and associated statutory language that sunset after tax year 2013 on the effective date of the bill without affecting any claimant eligible to file an amended return to claim those credits.

3. For the woody biomass harvesting and processing investment credit, which sunset after tax year 2014, taxpayers can file amended returns to claim the credit until April 15, 2020 (2019-20). The Committee could choose to repeal this credit and associated statutory language beginning on July 1, 2020, without affecting any claimant eligible to claim the credit.

4. As noted, an annual GPR appropriation was created under 1997 Wisconsin Act 63 for DOR to make income tax reciprocity payments to Illinois for tax years 1998 and 1999. Wisconsin made payments from this appropriation of $5.5 million in 1998-99 and $8.25 million in 1999-00. No payments have been made from this appropriation since 1999-00. The Committee could choose to repeal this appropriation and associated statutes on the effective date of the bill without affecting the current Illinois-Wisconsin reciprocity agreement described in LFB Paper #324, as payments to Illinois are made from a separate appropriation.

5. According to the Legislative Reference Bureau, if the Committee chose to repeal these eight obsolete appropriations and associated statutory language, the number of printed pages of the statutes would be reduced by approximately 19 pages.

ALTERNATIVES

1. Repeal the following appropriations and associated statutory language on the effective date of the bill: (a) Illinois income tax reciprocity, 1998 and 1999; (b) dairy manufacturing facility investment credit; (c) dairy manufacturing facility investment credit; dairy cooperatives; (d) food processing plant and food warehouse investment credit; (e) beginning farmer and farm asset owner credit; (f) film production company investment credit; and (g) film production services credit. Repeal the woody biomass harvesting and processing credit appropriation and associated statutory language on July 1, 2020.

2. Take no action.

Prepared by: Sean Moran

GENERAL FUND TAXES

Income and Franchise Taxes

LFB Summary Items for Which No Issue Paper Has Been Prepared

Item #	Title
15	Exclusion for Interest on Certain WHEFA Bonds and Notes
18	Veterans and Surviving Spouses Property Tax Credit
19	Interest on Overpayment of Taxes
20	Repayment Credit
24	Jobs Tax Credit Sum Sufficient Reestimate
27	Refundable Research Tax Credit Sum Sufficient Reestimate
31	Addition for Low-Income Housing Tax Credit
33	Sunset the State Supplement to the Federal Tax Credit for Nonhistoric Qualified Rehabilitated Buildings
35	Tax Law Change Interaction Effects

LFB Summary Item Addressed in Separate Legislation

Item #	Title
30	Deduction for Business Expenses for Moving Out-of-State (Enrolled AB 10)

LFB Summary Items Removed From Budget Consideration

Item #	Title
2	Limitation on Exclusion for Nonfarm Capital Gains
3	Manufacturing and Agriculture Credit Limitation
6 (part)	Earned Income Tax Credit (Except Current Law Reestimate)
8	Homestead Tax Credit -- Modifications to Formula Factors and Indexing
10	Sunset Private School Tuition Deduction
21	Broadcaster Apportionment Modifications
23	Enterprise Zone Tax Credit Program