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Revenue Matters – 2008 Issue #1

Wisconsin Budget Project – WCCF
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1 WI REVENUE GROWTH HALTS IN SECOND FISCAL QUARTER

As recently as mid-December, the Dept. of Revenue said state tax collections seemed to be in good shape - based on revenue in the first quarter of fiscal year 2008. That has now changed significantly, after DOR said this week that tax collections turned down sharply in the second quarter and increased less than 1% over the first half of the fiscal year. You can find a Journal Sentinel article about the revenue slowdown at:

<http://www.jsonline.com/story/index.aspx?id=709620>

The implications of the downturn could be far more serious than the article suggests, particularly if a significant revenue reduction in FY 2008 causes a reduced base for growth in the second year of the current biennium. As the article points out, Wisconsin has virtually no Rainy Day Fund. Further complicating matters is the fact that the state has been trimming the budget for "state agency operations" every year, so additional cuts are going to be far more painful.

The Dept. of Revenue was painting a much rosier picture in December, when it released the report for the first quarter of FY 2008. A Dec. 11 DOR press release about that report

cites the following highlights:

- WI personal income rose 5.3% in 2006 and is expected to grow a healthy 5.2% in 2007.
- Revenue collections in the first quarter of Fiscal Year 2008 are on target with estimates, increasing 3.3% over last year to \$3.5 billion.
- Sales tax collections through October 2007 increased 4.2% over the same period last fiscal year.

You can find that quarterly report at:

<http://www.revenue.wi.gov/ra/0711/0711okma.html>

2. DOYLE PROPOSES MANY MORE CORPORATE TAX BREAKS

Over the last couple of weeks, Governor Doyle has announced several initiatives to spur economic development. We will probably hear more about all of these initiatives in the Governor's State of the State address Wednesday evening. Republican leaders were quick to applaud the Governor's tax breaks for businesses and vowed quick Assembly approval. However, as the Journal Sentinel reported, key Senate Democrats have been less enthusiastic --- expressing concerns about the price tag of the proposals, their cost-effectiveness relative to other possible uses of the funds, and the effects on the state's substantial structural deficit.

<http://www.jsonline.com/story/index.aspx?id=706249>

The following is an outline of three Doyle initiatives that would create numerous new corporate tax breaks. It includes links to press releases from his office about each of the three initiatives:

Next Generation Manufacturing Tax Credits - On Jan. 15, the Governor announced a plan "to propel Wisconsin manufacturers into the next generation by focusing on efficiency and lean manufacturing principles." The so-called Next Generation Manufacturing Plan "will target \$85 million in existing and new tax credits to leverage \$1.6 billion in private capital investment, creating 5,000 new jobs and training 4,000 workers for the jobs of tomorrow." The Jan. 15 press release adds that Doyle "will work with lawmakers to streamline five different economic developmental programs into one comprehensive, consolidated tax credit that is targeted to help Wisconsin manufacturers train workers, create jobs, and invest in the future."

http://www.wisgov.state.wi.us/journal_media_detail.asp?locid=19&prid=3102

Innovate Wisconsin Plan - On Jan. 8, the Governor announced a plan to increase the state's focus on research and development, which would include the following new tax breaks for businesses:

- *Providing new Innovate tax credits* - Companies that increase spending on research and development by 25% over their 3-year average will receive a \$1 tax credit for every \$1 spent above this threshold. The tax credit a company can claim through this initiative is capped at 50% of its tax liability.

-- *Sales tax exemption for research and development equipment* - The sales tax exemption that applies to machines and equipment used in manufacturing will be extended to cover equipment used in research and development.

-- *Property tax exemption* - The equipment used in research and development will also be exempt from property taxes.

http://www.wisgov.state.wi.us/journal_media_detail.asp?locid=19&prid=3081

Accelerate Wisconsin - The following are the key elements of a plan proposed by Doyle on Jan. 7 to attract investment and support new high tech start-up companies:

-- *Accelerate Grant and Loan Program* - The new program will double current funding for technology grants and loans and will direct \$5 million annually to provide seed money to start-up companies and small businesses and supply the matching funds required for federal research grant applications.

-- *Capital Gains Re-Investment Initiative* - This new initiative will increase investment in new WI businesses by allowing individuals a limited 100% capital gains exclusion of up to \$10 million for long-term capital gains reinvested in qualifying WI businesses.

-- *Accelerating Capital Investment to New Start-ups* - To increase flexibility for entrepreneurs seeking tax-creditable investment, the Governor proposes to raise the current cap of \$1 million in tax-creditable angel investment per business to \$4 million.

-- *Accelerate Wisconsin Tax Credit* - In the budget, Governor Doyle increased the total amount of angel investor and venture capital tax credits available to businesses. By 2015, the total amount of Accelerate Wisconsin tax credits will reach \$100 million, leveraging a minimum of \$400 million in private investment.

http://www.wisgov.state.wi.us/journal_media_detail_print.asp?prid=3078&locid=19

3 SENATOR HANSEN INTRODUCES CORPORATE TAX DISCLOSURE BILL

On Dec. 19, Senator Dave Hansen (D - Green Bay) introduced the Corporate Tax Accountability Act, which would require public companies doing business in Wisconsin to submit publicly accessible annual disclosures of their income and all items that can be used to reduce their Wisconsin tax liability. The bill is SB 367 and is in the Senate Committee on Tax Fairness and Family Prosperity.

Hansen cited a report issued by the Institute for Wisconsin's Future (IWF), which concluded that Wisconsin lost \$643 million last year because "corporate tax leakage." and a statewide effort to gather public comments regarding the state's tax structure. Hansen said the intent of SB 367 is "to get the information we need to have a well-informed debate over the current tax structure and the fairness or lack thereof of our current tax system and to make certain our policies are fostering competition and providing a level playing field for all Wisconsin businesses." You can find his press release at:

<http://www.wispolitics.com/1006/071219hansen.pdf>

More than 99% of businesses in the state would not be affected by the proposed bill because they don't have publicly traded stock. Speaking at the Dec. 19 press conference on the bill, Dr. Jack Norman, the Research Director at IWF, contrasted the corporate

responsibility of WI companies such as Harley-Davidson and Sentry Insurance, which pay their full share of state income taxes, with firms such as Microsoft, Merck and Pepsi that have billions in profit nationally but pay no corporate income taxes in WI.

A story about the bill can be found in the Dec. 19 Journal Sentinel at:

<http://www.jsonline.com/story/index.aspx?id=698240>

An op ed column by Karen Royster, the Exec. Director of IWF, can be found at:

<http://www.jsonline.com/story/index.aspx?id=703227>

You can find the bill, SB 367, at:

<http://www.legis.state.wi.us/2007/data/SB-367.pdf>

4. NEW SENATE COMMITTEE BEGINS EXAMINING TAX FAIRNESS -- NEXT MTG. JAN. 30

Late last year, the WI Senate created a new committee, the Senate Committee on Tax Fairness and Family Prosperity, which is being chaired by Senator Bob Jauch (D-Poplar). The committee's next (2nd) meeting will be on Wednesday, Jan. 30, at 10:00 AM in Room 411 South of the State Capitol. Michael Mazerov, a Senior Fellow with the Center on Budget and Policy Priorities in Washington D.C., will present his research on national trends in corporate strategies to minimize their state income taxes.

The committee held its first public hearing on January 10, 2008, to discuss the status of Wisconsin's tax system, including its lack of fairness and equity. In his opening remarks, Chairman Jauch said: "This committee has an opportunity to push for a greater effort to evaluate and reform our tax system so that fairness and progressivity-two hallmarks of Wisconsin-might be restored.". The only witness at the hearing was Department of Revenue (DOR) Secretary Roger Ervin, who discussed the 2004 DOR Tax Incidence Study.

According to a press release from Jauch's office, he "complimented the DOR and Secretary Ervin for their efforts to use existing law to require 184 banks to repay \$43 million in legitimate taxes they were sheltering from the state. The northern lawmaker also recognized the efforts of the Department to force the WalMart corporation to remit more than \$17 million they owe the state after hiding their actual earnings."

"These 184 banks and WalMart are employing a strategy of questionable legality in order to avoid paying their fair share of Wisconsin taxes," Jauch said. "Our failure to place equity and fairness at the forefront has resulted in a system that has become decidedly unfair and unequal-particularly to those at the lower end of the economic ladder. Frankly, long before now we should have been able to find ways to target relief appropriately and maintain progressivity. With the help of this committee, we still might," Jauch concluded.

You can find the press release at
<http://www.wispolitics.com/index.iml?Article=115325>

A link to a video of the entire Jan. 10 committee hearing can be found on Jauch's website at:
<http://www.legis.state.wi.us/senate/sen25/news/>.

5. THE STATE'S ESTATE TAX ENDS; WILL IT EVER RETURN ?

Wisconsin faces a substantial structural deficit in the next biennium, and one of the factors contributing to that is the elimination of the state's estate tax, which ended - at least for a few years - on January 1, 2008. If current state and federal law is not amended, the tax will return in 2011, but the probability of that does not seem to be high. The estate tax has generally brought in about \$100 million per year, though that amount grew to \$121 million in fiscal year 2007. The fiscal impact of the hiatus of the estate tax won't be fully felt for another year or two, because it takes a while to collect the taxes on estates of WI residents who died in previous years.

Prior to this year, the WI estate tax applied to the estates of about 2% of state residents - individuals with estates worth more than \$675,000 and couples with estates of over \$1.35 million. It is expiring because of a federal law enacted in 2001 that effectively negated most state estate taxes, by repealing - until 2011 - a federal tax credit that had allowed state estate taxes (up to the level in Wisconsin) to offset that much of the federal estate tax. That federal law had essentially allowed states to share in the federal tax, by "picking up" the amount of the credit, without increasing the total tax liability. The 2001 federal change phased out the credit, thereby phasing out the states' so-called "pick-up taxes" on estates. Wisconsin quickly responded in the 2001-03 budget bill by decoupling its estate tax from federal law. However, the compromise amendment included in that budget bill put a Dec. 31, 2007, sunset date on the revised estate tax.

Although the state's interim estate tax has expired, WI statutes still provide for an estate tax that equals the federal credit. Since there is no federal credit until 2011, Wisconsin no longer has an estate tax. Legislation introduced in the state Assembly would permanently repeal the state estate, retroactive to January 1, 2007. That would ensure the state estate tax does not return in 2011 and would also cost the state at least \$100 million in the current biennium, which makes it unlikely that the bill will be enacted. But even assuming no state action is taken, future Congressional action could extend or make permanent the repeal of the federal credit, thereby preventing a revival of the WI estate tax.

Articles about the "slumbering" of the estate tax appeared in both the Journal Sentinel (Dec. 16) and the State Journal (Dec. 8):
<http://www.jsonline.com/story/index.aspx?id=696945>
<http://www.madison.com/wsj/topstories/index.php?ntid=261087>

The changes in federal law didn't merely repeal state "pick-up" taxes on estates. They also phase out the federal estate tax, with it going away entirely in 2010. However, to keep the price tag of estate tax cuts within the limits Congress set for the total long-term cost of the tax cuts enacted in 2001, Congress had to write the law to say that in 2001 the tax would return to the 2001 level - although everyone anticipated that subsequent Congressional action would extend the tax cuts. Over the last few years a debate has raged in Congress about whether to permanently repeal the federal estate tax or to revise it by setting a higher exemption and a lower tax rate. Although Congress seemed to be close a year or two ago to having enough votes for permanent repeal, that no longer appears to be the case.

An article in OMB Watch in November examines the federal debate and Warren Buffet's vocal opposition to repeal.

<http://www.ombwatch.org/article/articleview/4089/>

6. SHOULD A FEDERAL STIMULUS PACKAGE HELP LOW-INCOME FAMILIES?

With rapidly growing evidence that the nation is on the verge of a recession, lawmakers have quickly decided that a substantial economic stimulus package should be enacted. Democratic leaders in Congress and key Republicans, including the President, agree that rapid action is needed, and they seem to be on about the same page in terms of the amount of funding they are willing to commit to the effort (about \$150 billion). There also seems to be fairly wide agreement that a stimulus bill should not be subject to pay-as-you-go budget rules that would require raising taxes to offset the cost of tax rebates or other provisions. However, there are significant disagreements on the form of the economic stimulus - between Republicans and Democrats and to a lesser extent among legislators of the same party.

Most lawmakers seem to concur that a significant component of the stimulus plan should be tax rebates for families and individuals. However, Republicans, unlike Democrats, do not want to approve refundable credits that would reach low income taxpayers. Democrats argue that it is fair to include lower income households because they pay payroll and other taxes, they need assistance, and they will spend more of their refunds - thereby providing a more effective economic stimulus. An article in the Jan. 20 NY Times looks at the debate over refundable credits.

http://www.nytimes.com/2008/01/20/washington/20rebate.html?_r=1&hp&oref=slogin

That article explains the implications of non-refundable credits: "For practical purposes, analysts estimate, a family of four with an income of \$24,000 would receive no government payments at all, and families with incomes below \$40,000 would at most receive partial rebates. But a household with an income of \$100,000 or more could get back \$1,600." It goes on to quote an Rep. Paul Ryan (R - WI) who defends the notion that the rebates should be just for people "who pay taxes." Under the President's proposal, estimated 30 million working households would get no rebate and another 19 million would get less than the maximum.

Many Democrats have suggested that the stimulus package shouldn't be limited to tax rebates or corporate tax relief, but should include increased spending that will get into the economy more quickly. There has been a wide range of suggestions, including things such as extended unemployment benefits, increased food stamps and fuel assistance, more construction spending, and increased state aid for programs like Medicaid. A report issued on Jan. 15 by the nonpartisan Congressional Budget Office (CBO) says:

"The most effective types of fiscal stimulus (delivered either through tax cuts or increased spending on transfer payments) are those that direct money to people who are most likely to quickly spend the bulk of any additional funds provided to them."

http://www.cbo.gov/ftpdocs/89xx/doc8916/01-15-Econ_Stimulus.pdf

Members of the conservative Republican Study Committee are touting a proposal that focuses on tax breaks for businesses. "Job growth - not increased government spending - is the key to addressing the slowdown in investment due to the housing crisis," said Rep. Eric Cantor of Virginia, the House Republican Chief Deputy Whip. Some Republicans have also endorsed extending the tax cuts that are set to expire in 2010. A recent report by the Center on Budget and Policy Priorities (CBPP) responds to that idea:

"Extending the 2001 and 2003 tax cuts would have virtually no stimulus effect, since it would not put a dollar in anyone's pocket until 2011. Meanwhile, it would substantially worsen the nation's budget outlook, likely damaging the economy in the long run and possibly even depressing investment in the short run if it caused long-term interest rates to rise."

You can find that report at: <http://www.cbpp.org/1-15-08tax.pdf>

A more recent CBPP report about unintended consequences of the business tax breaks can be found under item #9, below.

7. A REPORT CARD WITH SOME GOOD FISCAL NEWS FOR WISCONSIN

A study of public sector retirement benefits by The Pew Charitable Trusts' Center on the States has some very encouraging news for Wisconsin. It gave our state high marks for fiscal responsibility with respect to the financing of its pension and non-pension obligations to public sector retirees. The report found:

-- By 2006, only five states - Florida, New York, North Carolina, Oregon and Wisconsin - had pension funding ratios at a 100 percent or greater level. (Actually WI was at 99.6%, but that still put us in the top 5 and compares to a national average of just 82%.)

-- At the end of fiscal year 2006, just six states - Arizona, North Dakota, Ohio, Oregon, Utah and Wisconsin - were on track to have fully funded their non-pension obligations [primarily health care] during the next 30 years.

Here's a story about the report from Stateline.org:

<http://www.stateline.org/live/details/story?contentId=265697>

Here's the link to the WI fact sheet:

http://www.pewtrusts.org/uploadedFiles/wwwpewtrustsorg/Fact_Sheets/State_policy/FINAL_Wisconsin.pdf

8. REVENUE ISSUES IN THE NEWS

-- "States often don't go after taxes owed on Internet cigarette sales" - Dec. 26, Assoc. Press/Appleton Post Crescent - "Wisconsin and other states either don't know who is buying cigarettes over the Internet and not paying state taxes, or they know and don't go after the culprits. Some states make high-profile attempts to collect taxes owed on cigarette sales. But even when they do, many Web sites skirt the law by operating overseas or on American Indian reservations where state laws are largely unenforceable. Tracking down who bought what, and determining how much they owe, is a loophole that anti-smoking advocates and others want to see closed."

<http://www.postcrescent.com/apps/pbcs.dll/article?AID=/20071226/APC0101/712260577/1979>

-- "Out of state, out of fine; Wisconsin's failure to join pact lets non-resident drivers defy tickets" - Dec. 3, Journal Sentinel - "Out-of-state drivers are skipping out on millions of dollars in traffic fines and forfeitures because Wisconsin has failed to join an interstate compact that keeps track of driving records in the United States, officials say. Twice in the last four years, including in May, the Wisconsin Legislature has failed to approve having the state join the national Driver License Agreement."

<http://www.jsonline.com/story/index.aspx?id=692292>

-- "State offices must prune budgets; Doyle hopes to avoid layoffs in \$100 million trim"

-
Dec. 24, Journal Sentinel - "State government agencies must return \$100 million in unspent funds on June 30 - an edict that has them not filling hundreds of jobs, reorganizing and preparing for possible layoffs. Gov. Jim Doyle says he hopes state agencies can avoid layoffs as they figure out how to comply with the order to contribute to \$100 million in forced savings, which was part of the budget he signed in October."

<http://www.jsonline.com/story/index.aspx?id=699744>

-- "More state offices may close to cut costs" - Dec. 24, State Journal - "Department of Administration Secretary Michael Morgan said the state is looking at ways it can be more efficient and save money for taxpayers. As part of the two-year state budget approved in October, state agencies must find \$200 million in savings to keep the budget balanced. ...The state Department of Revenue said this week it is planning to close 19 offices by May 2010. In April, the Department of Tourism also will not reopen two offices to serve travelers, in Genoa City and Prairie du Chien, that were closed for the winter."

<http://www.madison.com/wsj/home/local/index.php?ntid=263735&ntpid=2>

9. READING ROOM

-- "Bonus Depreciation and "Expensing Would Cost States Billions of Dollars" - The Center on Budget that proposals to let businesses deduct expenses or depreciation more rapidly could cost states billions. Fortunately, Wisconsin is among the minority of states that have decoupled from federal law and would not be affected.

<http://www.cbpp.org/1-22-08sfp.pdf>

-- Wisconsin Comprehensive Annual Financial Report for FY 2007 - The State's annual financial report for the year ending June 30, 2007, is now available online at the URL below. Bound copies are available upon request from Mary Sommerfield at 608-266-2291 or mary.sommerfield@wisconsin.gov.

ftp://doafp04.doa.state.wi.us/doadocs/2007CAFR_Linked.pdf

9. JOIN AND SUPPORT WCCF!

WCCF relies on the generosity of its supporters to fund much of the work we do. By making a contribution, you can help us sustain our efforts to ensure that Wisconsin has the revenue necessary for strong state and local programs serving children and families.

You can donate online at: <http://www.wccf.org/support.php>
