
STATE TAX INCENTIVES FOR ECONOMIC DEVELOPMENT IN WISCONSIN

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INTRODUCTION

Wisconsin offers a number of tax incentives for corporations and other businesses to locate or expand their operations within the state. This paper summarizes the major taxes imposed on businesses operating in the state and the tax incentives available to them.

Tax incentives available to businesses include exemptions, credits, and other special corporate tax treatment. In addition, the state has designated certain areas as development or enterprise zones and local governments have created tax incremental finance (TIF) districts. Businesses locating or expanding operations within the designated zones are eligible to claim tax credits. Businesses locating operations within a TIF district benefit from infrastructure financed by tax increments. The paper also discusses Wisconsin's preferential treatment of capital gains and other special tax treatments.

Currently there are 33 credits available for corporations to claim against the corporate income and franchise tax, as well as four other specific tax treatments for Wisconsin corporations that include deductions, exemptions, single-sales apportionment, and pass-through business organization. Businesses also may qualify for one of four property tax exemptions, and businesses expanding in Wisconsin may also be able to take advantage of one of three different types of tax incremental financing districts. A business may also qualify for one of seven general sales and use tax exemptions in addition to targeted exemptions for specific industries. Finally, individual taxpayers who own or invest in a Wisconsin business may be eligible to claim one or more of the 29 business income tax credits that are available to individuals or one of four different types of special treatments of capital gains.

CORPORATE INCOME AND FRANCHISE TAX

A. Description

Corporations doing business in Wisconsin are subject to either an income or a franchise tax. The corporate income tax is a tax on the net income of corporations doing business in the state. The corporate franchise tax is a tax on the privilege of doing business in the state. The distinction between the two taxes is subtle, relating primarily to the restrictions under federal law on the types of income that states can tax with an income tax (e.g., interest from U.S. obligations). Corporate net income is used as the measure or base for the franchise tax and both taxes are imposed at a rate of 7.9%. The 7.9% flat rate has not been changed since 1981, except for a 10% surtax during the 1982 and 1983 tax years.

Corporate tax collections in state fiscal year (FY) 2010 were \$834.5 million, or 6.9% of total general purpose revenue (GPR) taxes of \$12.1 billion.

Computation of net income is federalized; that is, based primarily on the Internal Revenue Code (IRC). The starting point for computing Wisconsin net income is federal gross income, subject to certain modifications. Conformity to the IRC is not automatic in Wisconsin but rather requires adoption by statute of each federal law change. Wisconsin applies federal regulations, rules, and court cases interpreting the IRC, when applicable, in determining the proper treatment of an item. In general, for purposes of computing amortization and depreciation, Wisconsin follows IRC as of December 31, 2000; thus, Wisconsin does not allow the more recent bonus depreciation and expensing allowed under federal law.

For tax years beginning on or after January 1, 2009, corporate groups with common ownership are required to file a combined tax return. Income and deduction items, with inter-company transactions removed, are summed for all of members to arrive at the group's income that is apportioned to each member based on the member's sales in Wisconsin.¹

Corporations that conduct business in more than one state must apportion their net income among the states with jurisdiction to tax the income. For most types of corporations, the numerator of the factor is comprised of sales in Wisconsin, while the denominator is total sales without regard to location. For members of corporate groups that are required to file a combined report, each member determines its sales both within Wisconsin as well as total sales. Sales between members of the same corporate group are disregarded. The total sales for each member are summed to derive a common denominator for the sales factor for all members. Total group income is apportioned to each member based on the member's Wisconsin sales as a share of total group sales everywhere. Members with no sales in Wisconsin will have no apportionable income that is taxable to Wisconsin.

Wisconsin provides for differential tax treatment of business income depending on the form of organization under which a business operates. Wisconsin law permits the formation of Subchapter S corporations and limited liability companies (LLCs)². Both of these entities combine the benefits of limited liability offered to corporations, with the ability to pass-through income to the individual owners. Thus, these entities generally pay no tax at the entity level. Instead, income is passed through to the individual shareholders or members, who pay tax on the income at the lower individual income tax rates. (The individual income

¹ More information on Wisconsin's combined reporting law can be found at <http://www.revenue.wi.gov/combrept/index.html>.

² Limited liability companies can choose to be treated as a corporation (paying tax at the entity level) or as a partnership or subchapter S corporation (passing through income or losses) for tax purposes.

tax rates range from 4.6% to 7.75%, compared to the 7.9% corporate income tax rate.) This flow-through aspect of income also avoids the double taxation of C-corporation dividends that occurs when profits are first taxed at the corporate level and then again at the individual level when profits are distributed as dividends to individual shareholders. (See the discussion below of pass-through entities in the section entitled "Other Special Tax Treatments")

In tax year 2008 there were approximately 113,000 corporate returns filed. Of these, approximately 64,000, or 56.6%, were subchapter S corporation returns. The remaining approximately 49,000 were returns filed by C-corporations or LLCs that choose to be treated as corporations for tax purposes, and thus pay tax at the entity level.

For state fiscal years before fiscal year 2012, Wisconsin also imposed a recycling surcharge on all non-farm businesses with gross receipts exceeding \$4 million at a rate of 3% on gross tax liability of corporations and 0.2% of net business income for non-corporate business entities. The maximum surcharge is \$9,800 and the minimum is \$25. The surcharge does not apply to exempt entities not required to file an income tax return. Revenues from the recycling surcharge are deposited in the segregated recycling fund and used to fund local government recycling and solid waste management programs and private business efforts to develop recycled products or markets related to these products. The recycling surcharge generated \$49.8 million in revenue in FY 2010.

Beginning in state fiscal year 2012, the recycling surcharge is renamed the economic development surcharge. All provisions of the surcharge remain the same, except that the revenues are deposited in a segregated economic development fund and are used to fund economic development programs of the Wisconsin Economic Development Corporation (WEDC).

B. Credits

A credit is an amount subtracted directly from the taxpayer's Wisconsin gross tax liability (i.e., the amount determined by applying the Wisconsin tax rate to Wisconsin taxable income) to determine Wisconsin net tax liability. Generally, business credits are nonrefundable, that is, they are used only to reduce the amount of tax otherwise due. If the amount of nonrefundable credits exceeds the claimant's tax liability for the year, the unused credit amounts can be carried over to future tax years (generally up to 15 years) to be used to offset tax liabilities in those years. An increasing number of business credits are refundable, in that the amount of credit in excess of tax otherwise due is refunded to the taxpayer.

Where available, data are provided on the amount of credit available, used and carried over. Unless otherwise noted, the analysis of the credits is based on the 2008 tax year returns of C-corporations. This data does not include credits claimed by S-corporation shareholders and non-corporate business entities, unless otherwise stated.

As used in this section, "available credit" includes new credit claims for the 2008 tax year plus the amount of any credit that was claimed in prior years but was not used to offset tax liability in those years. "Used credit" is the amount of this available credit actually applied in the 2008 tax year to offset tax liability. "Carryover credit" is the remaining available credit that is not used in the 2008 tax year and that will be available to offset tax liability in future years. Thus, "available credit" less "used credit" equals "carryover credit." A description of the current credits is provided below.

The credits generally fall into five general categories: research credits, zone-based credits, credits for economic development, industry-specific credits, and agricultural credits.

1. Research Credits

To encourage corporations to carry on research and development (R&D) activities in the state, five tax credits are available: a credit for R&D-related non-capital expenditures, a credit for investments in R&D facilities, an engine research credit, an energy efficient products research credit and a super research credit. The credits are only available to corporations.

Research Expenditure Credit. A nonrefundable research expenditure credit for non-capital expenditures related to research activities conducted in Wisconsin is available to corporations. The credit applies only to research expenditures that are undertaken to discover information that is technological in nature and intended to be useful in the development of a new or improved business component. Expenses must be incurred in connection with research conducted in Wisconsin in order to qualify for the credit.

The credit is patterned after the federal research credit and is equal to 5% of the excess of qualified research expenses for the current year over a base period amount. Qualifying expenditures are defined by reference to the rules established under Section 41 of the IRC. The "base period amount" is calculated in the same manner as that for the federal credit, except that the gross receipts used in computing the state credit are from sales attributable to Wisconsin (other than throwback sales) for purposes of apportionment. Qualified research expenses cover in-house expenses for the taxpayer's own research (wages, supplies, and computer use charges) and 65% of amounts paid or incurred for qualified research done by a person other than an employee of the taxpayer. Unused amounts of the credit can be carried forward for up to 15 years.

In tax year 2008, 308 C-corporations had \$96.6 million of credit available. Of these corporations, 133 used \$11.7 million of credits to offset tax liability, leaving \$84.9 million of credit available for use in future years.

Research Facilities Credit. A research facilities credit applies to capital investments to construct and equip new research facilities or expand existing facilities located in Wisconsin. The credit is equal to 5% of the amount of qualified investments in tangible, depreciable property that is not replacement property. The rules relating to the credit are similar to the rules for the research expenditures credit. The credit is nonrefundable and unused amounts of credit may be carried forward and offset against tax liability over the next 15 years.

In tax year 2008, 53 C-corporations had \$11.7 million of available research facilities credit. Seventeen corporations used \$963,000 of credit to offset tax liability, leaving \$10.8 million of credit available for use in future years.

Engine Research Credits. For tax years beginning after June 30, 2007, credits equal to 10% of qualified research and 10% of qualified facility expenses related to designing internal combustion engines and related substitutes such as fuel cells and electric and hybrid drives are available. The credits are also available for research related to designing vehicles powered by such engines and for research on improving production processes for such engines and vehicles. Expenses under the engine research credits

are not eligible for the regular research expenditure and research facilities credits. Unused credits may be carried forward for fifteen years.

In tax year 2008, there was \$6.2 million in engine research expense credits available. Of that amount, \$5.2 million was used to offset taxes, leaving a balance of \$1.0 million to be carried forward to offset taxes in future tax years.

Energy Efficient Products Research Credits. For tax years beginning after June 30, 2007, credits equal to 10% of qualified research and 10% of qualified facility expenses related to design and manufacturing of energy efficient lighting systems, building automation and control systems, or automotive batteries for use in hybrid-electric vehicles, that reduce the demand for natural gas or electricity or improve the efficiency of its use are available. Expenses under the energy efficient products research credits are not eligible for the regular research expenditure and research facilities credits. Unused credits may be carried forward for fifteen years.

Super Research and Development Credit. A credit is available for tax years beginning on or after January 1, 2011, for corporations that increase their research expenditures. The credit is equal to the amount of qualified research expenses for research conducted in Wisconsin in a tax year that exceeds 1.25 times the average annual amount of qualified research expenses in the corporation's previous three tax years. Unused credit amounts may be carried forward up to five years to offset future tax liabilities. "Qualified research expenses" are as defined under Section 41 of the IRC, and the research must be done in this state. Expenses for claims under the regular research expenditure credit also qualify for the super research credit as long as they exceed 1.25 times the preceding three-year average.

2. Zone-Based Credits

Prior to the passage of 2009 Act 2, Wisconsin had seven zone-based programs to encourage economic development in certain areas of the state: the Development Zone, Airport Development Zone, Agricultural Development Zone, Enterprise Development Zone, Technology Zone, Development Opportunity Zone, and the Enterprise Zone Jobs credit programs. Act 2 repealed the Development Zone, Airport Development Zone, Agricultural Development Zone, Technology Zone, and Enterprise Development Zone programs and replaced them with a single Economic Development Credit (see the discussion below of the Economic Development Credit), but left in place the Development Opportunity Zone and Enterprise Zone Jobs credits.

Development Opportunity Zone Credit. Under the Development Opportunity Zone program, businesses conducting economic activities in a zone may claim nonrefundable development opportunity zone credits allocated to them by the WEDC. Nine zones with a total of \$44.4 million in tax credits have been authorized. Of those, six zones have expired. A zone in Janesville and one in Kenosha were authorized in 2009 Act 28 with a total credit available of \$5 million each over a five-year period. In addition, 2011 Act 37 authorized an additional zone for the City of Beloit, also for a total credit amount of \$5 million over the life of the zone. For all three of these new zones, if the original \$5 million is allocated within five years, the zones can be extended for an additional five

years with an additional \$5 million each. The designation for the new zones will be effective for 60 months from the date of designation.³

Businesses locating or expanding their operations within the development opportunity zones are eligible to claim a job creation credit based on the number of new, full-time positions created; an environmental remediation credit that equals up to 50% of eligible environmental remediation costs; and an investment credit equal to 2.5% of the purchase of depreciable tangible personal property (or 1.75% of the price if the property has been expensed under section 179 of the IRC).

A capital investment credit is also available for certain businesses located in the new Kenosha, Janesville, and Beloit zones equal to 3% of qualified purchases of depreciable tangible personal property and amounts expended to acquire, construct, rehabilitate or remodel qualified real property.

Enterprise Zone Jobs Credit. A refundable enterprise zone jobs credit is available for certified businesses located in a designated enterprise zone. The WEDC may certify for tax benefits a business that begins operations in an enterprise zone if the business offers compensation and benefits to its employees working in the zone for the same type of work that are at least as favorable as those offered to its employees working outside the zone. The WEDC may also certify a business that expands operations in an enterprise zone, if the business will increase its personnel by at least 10% or the business makes a capital investment in property located in the enterprise zone equal to at least 10% of the business' gross revenues in the preceding tax year attributable to business activities in Wisconsin. Finally, the WEDC may certify a business that retains existing jobs in an enterprise zone if the business makes a significant capital investment in property located in the zone, and at least one of the following applies: (1) the business is an original equipment manufacturer with a significant supply chain in Wisconsin, as determined by the WEDC; or (2) more than 500 full-time employees are employed by the business in the enterprise zone

The WEDC is authorized to designate no more than 20 enterprise zones, with three of the zones being areas comprising political subdivisions whose population totals less than 5,000 and at least two areas comprising political subdivisions whose population is greater than 5,000 but less than 30,000. A designation may be in effect for no more than 12 years. In determining whether to designate an area as an enterprise zone, the WEDC must consider indicators of the area's economic need, infrastructure and energy support, the rate of business development, existing resources available to the area, and the effect of designation on other initiatives and programs to promote economic and community development in the area, such as job training and the creation of high-paying jobs.

The credit has five components:

- 1) A credit based on changes in the claimant's zone payroll over a base year, up to 7% of the base change. Eligible wages are those paid to new employees whose annual wages are greater than \$20,000 but not more than \$100,000 in a Tier I county or

³ The Janesville zone was designated in March, 2010, and the Kenosha zone was designated in March, 2011. The Beloit zone will be designated as of August 2, 2011, the effective date of 2011 Act 37.

municipality, or greater than \$30,000 but not more than \$100,000 in a Tier II county or municipality.⁴ Credit claims would be limited to 12 consecutive years.

- 2) An additional credit based on up to 7% of wages paid to existing zone employees. Eligible wages are those paid to employees whose annual wages are greater than \$20,000 but not more than \$100,000 in a Tier I county or municipality, or greater than \$30,000 but not more than \$100,000 in a Tier II county or municipality. The total number of employees would have to be equal to or greater than the number of employees in the base year. Credit claims would be limited to five consecutive years.
- 3) A credit based on the amount paid for training to upgrade the job-related skills of full-time employees who work in the enterprise zone;
- 4) A credit of up to 10% of significant capital expenditures in the zone.
- 5) For taxable years beginning after December 31, 2009, a credit equal 1% of the amount the claimant paid in the taxable year for goods or services from Wisconsin vendors, not including capital expenditures for which the credit is claimed.

To date, nine enterprise zones with a total tax credit amount of \$264.8 million have been designated.

3. Credits for Economic Development

Economic Development Credit. For tax years beginning after December 31, 2008, an economic development tax credit is available that replaces five zone-based credits. The nonrefundable credit may be claimed against the corporate income and franchise tax or against the insurance premiums tax. The amount of credit available is limited to \$103.2 million, which is the amount of available credit that had not been allocated by the WEDC in the five zone-based programs that this credit replaces, plus an additional \$25 million added by 2011 Act 4.

Under the program, a business may apply to the WEDC for certification to claim tax benefits. The WEDC may certify a business that conducts or intends to conduct at least one eligible activity. The eligible activities include:

- Creating and maintaining, for a period of time established by the WEDC, full-time jobs in addition to any existing full-time jobs provided by the person.
- Making a significant investment in new equipment, machinery, real property, or depreciable personal property.
- Making significant investments in the training or reeducation of employees for the purpose of improving the productivity or competitiveness of the business.

⁴ The provisions of 2009 Act 11 require the Department of Commerce to promulgate rules defining a Tier I and Tier II county. As of this writing, the rules have not been issued. Act 11 requires Commerce to consider the following in defining Tier I and Tier II: unemployment rate, percentage of families with incomes below the poverty line, median family income, median per capita income, and other significant or irregular indicators of economic distress, such as a natural disaster or mass layoff.

- Locating or retaining a corporate headquarters in Wisconsin, or retaining employees holding full-time jobs in Wisconsin.

The WEDC may authorize additional tax benefits for certified claimants if the claimant conducts at least one eligible activity in an area designated by the WEDC as economically distressed, or if the claimant creates, retains, or trains members of certain targeted groups.⁵

Unused tax credit amounts may be carried forward up to fifteen years to offset future tax income and franchise tax liabilities.

Jobs Tax Credit. 2009 Act 28 created a refundable Jobs Tax Credit for tax years beginning after December 31, 2009. In order to claim the credit, a business would have to be certified by the WEDC, which may certify a business, for up to ten years. The WEDC may award jobs credits equal to 10% of wages of an employee who is paid at least \$20,000 in a Tier I county or municipality, and at least \$30,000 in a Tier II county or municipality.⁶ The maximum credit for wages is \$10,000 per employee. The WEDC may also award tax credits for costs incurred by the business to undertake training activities.

The WEDC may allocate up to \$5 million in jobs tax credits in a calendar year, except that the maximum total amount that may be awarded in the period from January 1, 2010 through June 30, 2013 is \$14.5 million. The \$14.5 million limit does not apply to amounts transferred from the angel investment credit or the early stage seed investment credit (see below). Amounts claimed in taxable years beginning after December 31, 2009 and before January 1, 2012 are to be paid in taxable years beginning after December 31, 2011.

Early Stage Seed Investment Credit. Effective for taxable years beginning after 2004, an early stage seed investment credit is available equal to 25% of investments paid to a fund manager that invests the funds in qualified new business ventures that are certified by the WEDC. The credit may be claimed against the income and franchise tax as well as against the insurance premiums tax. The maximum annual amount that may be claimed by all claimants is \$6.0 million for calendar years beginning before January 1, 2010, and \$8.0 million for calendar year 2010. For calendar years beginning on or after January 1, 2011, the maximum annual amount is increased to \$20.5 million for all claimants, plus an additional \$250,000 per year for investments in nanotechnology businesses. If the investment is held for less than three years, any previously claimed credits must be repaid to the Department of Revenue. In addition, if the investor has

⁵ “Member of a targeted group” means a person who resides in an area designated by the federal government as an economic revitalization area, a person who is employed in an unsubsidized job but meets the eligibility requirements for a Wisconsin Works employment position, a person who is employed in a trial job, as defined in s. 49.141 (1) (n), or in a real work, real pay project position under s. 49.147 (3m), a person who is eligible for child care assistance, a person who is a vocational rehabilitation referral, an economically disadvantaged youth, an economically disadvantaged veteran, a supplemental security income recipient, a general assistance recipient, an economically disadvantaged ex-convict, a dislocated worker, as defined in 29 USC 2801 (9), or a food stamp recipient, if the person has been certified in the manner under 26 USC 51 (d) (13) (A) by a designated local agency, as defined in 26 USC 51 (d) (12).

⁶ As of this writing, the rules defining a Tier I and Tier II county have not been promulgated. See the criteria the Department of Commerce must use in creating the definitions in footnote 4 under the Enterprise Zones Jobs Credit.

invested in the business prior to the business being certified as a qualified new business venture, investments after certification by this investor are not eligible for credit.

For tax years beginning on or after January 1, 2009, unused credits may be transferred from the original claimant to another entity. The transferor will be required to obtain prior authorization from the fund manager, and the fund manager would be required to notify the Department of Revenue and the WEDC.

To be qualified to receive investments that are eligible for the credit, a qualified new business venture must have its headquarters in the state, have less than 100 employees, at least 51% of whom are employed in the state, and have been in business for not more than seven consecutive years. A qualified new business venture must also be engaged in one of the following: manufacturing, biotechnology, nanotechnology, communications, agriculture, or clean energy creation or storage technology, processing or assembling products, including medical devices, pharmaceuticals, computer software, computer hardware, semiconductors, any other innovative technology products, or other products that are produced using manufacturing methods that are enabled by applying proprietary technology, services that are enabled by applying proprietary technology, , pre-commercialization activity related to proprietary technology that includes conducting research, developing a new product or business process, or developing a service that is principally reliant on applying proprietary technology.

The business may not be primarily engaged in real estate development, insurance, banking, lending, lobbying, political consulting, professional services provided by attorneys, accountants, business consultants, physicians, or health care consultants, wholesale or retail trade, leisure, hospitality, transportation, or construction, except construction of power production plants that derive energy from a renewable resource.

In tax year 2008, 238 individual filers had \$2.1 million of available credit. Of this amount, 214 individuals used \$1.5 million to offset tax liability, leaving \$600,000 to be used to offset tax liability in future years.

Supplement to the Federal Historic Rehabilitation Credit. A nonrefundable credit is available to encourage the rehabilitation of historic buildings in Wisconsin.⁷ This supplement to the federal historic rehabilitation credit can be claimed only for projects that are eligible for the federal credit. The state supplemental credit is equal to 5% of qualified rehabilitation expenditures, as defined under Section 48 (g) of the IRC, to substantially rehabilitate certified historic buildings for use in a trade or business. The credit is patterned after the federal 20% credit for commercial rehabilitation of historic buildings. The rehabilitation work must meet historic preservation standards and the expenditures must exceed the taxpayer's adjusted basis in the building. Unused amounts of the credit can be carried forward for up to 15 years. The credit applies only to property located in Wisconsin.

Taxpayers must reduce their Wisconsin adjusted basis in the building by the amount of the credit claimed. The reduced basis will result in lower depreciation deductions.

⁷ The credit applies to rehabilitation projects begun after December 31, 1988, and for rehabilitated property placed in service after June 30, 1989.

In tax year 2008, approximately \$3.0 million of credit was available to 23 C-corporation taxpayers. In addition, 69 individual filers had \$470,000 in available credit. Of this amount, \$320,000 was used by 62 individuals.

Water Consumption Credit. A non-refundable credit is available for taxable years that begin after December 31, 2009 and before January 1, 2020 for claimants who are an industrial customer of a municipal water utility that is located in a federal renewal community zone in this state, and whose average annual water consumption from that utility for a 24-month period exceeds 100 million cubic feet. The credit is calculated by subtracting the claimant's water usage costs in taxable year 2009 from the claimant's water usage costs in the taxable year and multiplying by 0.5. The maximum amount that a claimant may claim in a taxable year is \$300,000.

Post-Secondary Education Credit. For taxable years beginning on or after January 1, 2010, a credit is available for businesses that pay tuition for their employees at a qualified post-secondary institution if the individual was eligible for a grant from the Federal Pell Grant Program and is a resident of this state. A qualified post-secondary institution is defined as a University of Wisconsin System institution, a technical college system institution, a regionally-accredited four-year non-profit college or university having its regional headquarters and principal place of business in this state, or a school approved by the Educational Approval Board if the delivery of education occurs in this state. The credit is equal 25% of the tuition paid, or 30% if the individual is enrolled in a course of instruction that relates to a worker shortage in this state as determined by the local Workforce Development Board. The claimant shall claim the credit for the taxable year in which the individual graduates for costs incurred or paid for all taxable years. A claimant may not claim the credit for tuition amounts paid or incurred for a family member unless the family member was employed an average of 20 hours per week at the claimant's business in the one-year period commencing participation in the education program, and if the family member is enrolled in a course of instruction that substantially relates to the claimant's business.

Relocation Credit. For taxable years beginning after December 31, 2010, a nonrefundable credit is available for businesses that relocate to this state from another state or country. The credit is equal to the net Wisconsin tax liability of the businesses after taking into account all other allowable credits, deductions, and exclusions, and can be claimed for two taxable years beginning with the year in which the business relocates to Wisconsin. To be eligible for the credit the claimant must not have done business in this state in the any of the two preceding taxable years. Unused credit amounts may not be carried forward.

4. Industry-Specific Credits

Manufacturing Investment Credit. The manufacturer's sales tax credit was repealed for tax years beginning after December 31, 2005. For tax years beginning on or after January 1, 2008, firms that had more than \$25,000 of unused manufacturer's sales tax credit as of December 31, 2005 may claim a new nonrefundable manufacturing investment credit equal to the total unused manufacturers' sales tax credit carryforwards held before the credit was repealed.⁸ The unused credit must be amortized equally over 15 years. Unused credits can be carried forward for 15 years. Companies are allowed

⁸ Firms that had less than \$25,000 in manufacturer's sales tax credit carryforwards as of December 31, 2005 were allowed to claim 50% of the amount in tax year 2006 and 50% in tax year 2007.

to take the credit beginning in 2008 only if they were certified by the Department of Commerce to have met one of the following criteria:

- Retention of 100% of the full-time (at least 35 hours per week) jobs employed by the company as of December 23, 2003.
- Average annual investment since January 1, 2003 equal to 2% of total book value of the company's depreciable assets in Wisconsin-based plants/facilities or \$5 million.

A total of 175 taxpayers were certified by the Department of Commerce to receive total tax credits of \$149.4 million to be amortized over 15 years.

Film Production Credits. For tax years beginning after December 31, 2008, two refundable credits related to expenditures for film production in this state are available. The credits include:

- A film production services income and franchise tax credit. The credit is equal to 25% of the salary, wages, or labor-related contract payments paid by the claimant in the taxable year to individuals, including actors, who were residents of this state at the time that they were paid and who worked on an accredited production in this state, not including the salary, wages, or contract payments paid to any individual who was paid more than \$250,000. In addition, a credit equal to 25% of the production expenditures paid in the taxable year is available. "Production expenditures" means any expenditures that are incurred in this state and directly used to produce an accredited production, including expenditures for set construction and operation, wardrobes, make-up, photography, sound recording/mixing, lighting, editing, film processing, special/visual effects, renting or leasing facilities, equipment or motor vehicles, food, lodging, and any other similar expenditure as determined by the Department of Tourism. "Production expenditures" do not include salary, wages, or labor-related contract payments.
- A film production company investment credit. A claimant may claim a credit against income and franchise taxes an amount equal to 15% of the purchase price of depreciable, tangible personal property, if the purchase is sourced to this state. In addition, a claimant may claim 15% of the amount expended to acquire, construct, rehabilitate, remodel, or repair real property, if the production company exclusively produces accredited productions.

To be certified, the production company must apply to the Department of Tourism and pay an application fee equal to 2% of the claimant's budgeted production expenditures or \$5,000, whichever is less. Total film production services and investment credits are limited to \$500,000 in a fiscal year for all claimants.

Credit for Insurance Security Fund Assessments. Chapter 646, Wisconsin Statutes, provides a credit against state taxes, including the corporate income and franchise tax, for certain assessments levied on insurance companies by the Wisconsin Insurance Security Fund. The fund is designed to protect policyholders in cases where their insurance company has failed and is in the process of liquidation. Where the available assets and reserves of failed insurers are inadequate to meet claims, the fund may assess insurance companies doing business in the state, with some exceptions (e.g., fraternal benefit societies). Such assessments are eligible for a 100% tax credit if they cannot be recovered through higher premiums. This can occur if premiums are fixed for

a particular line of business. The tax credit is nonrefundable and must be claimed in equal installments over a five-year period, beginning with the year following the one in which the assessment is made.

Health Insurance Risk-Sharing Plan (HIRSP) Assessments Credit. An income and franchise tax credit and a license fee credit are available for insurers that pay assessments for HIRSP. HIRSP offers health insurance to Wisconsin residents who either are unable to find adequate health insurance coverage in the private market due to their medical conditions or who have lost their employer-sponsored group health insurance. Applicants are required to meet HIRSP eligibility criteria to qualify. The credit is equal to a percentage of the amount of assessments paid by the insurer that taxable year under the HIRSP. The Department of Revenue, in consultation with the Office of the Commissioner of Insurance, determines the credit percentage for each year so the annual cost the credit is approximately \$5 million. The amount of the credit for all insurers cannot exceed \$5 million per year.

Biodiesel Production Credit. For tax years beginning on or after January 1, 2012, and before January 1, 2015, a nonrefundable credit is available that is equal to 10 cents per gallon for biodiesel fuel produced in Wisconsin for producers that produce at least 2.5 million gallons of biodiesel fuel per year. The maximum credit that a claimant may claim in a taxable year is \$1 million.

Ethanol and Biodiesel Pump Credit. An ethanol and biodiesel fuel pump tax credit is available for tax years beginning after December 31, 2007 and before January 1, 2018. The credit is equal to 25% of the amount paid in a tax year to install or retrofit pumps located in Wisconsin that dispense motor fuel consisting of at least 85% ethanol or at least 20% biodiesel fuel or pumps that allow the end user to choose the percentage of gasoline replacement renewable fuel or diesel replacement renewable fuel. The maximum tax credit for a tax year cannot exceed \$5,000 for each service station that claims a credit for an installed or retrofitted pump. Unused credit amounts may be carried forward up to 15 years to offset future tax liabilities.

In tax year 2008, 16 individual taxpayers claimed \$47,000 in credit. Of that amount, taxpayers used \$6,900 in credit, carrying forward the balance of \$40,100 to future years.

Electronic Medical Records Credit. For tax years beginning after December 31, 2011, a nonrefundable tax credit is available equal to 50% of the amount paid by a health care provider in a tax year for information technology hardware or software that is used to maintain medical records in an electronic form. Tax credits not entirely used to offset income and franchise taxes can be carried forward up to 15 years to offset future tax liabilities. The maximum total amount of electronic medical records tax credits that can be claimed in a tax year is \$10 million and is allocated to claimants by the Department of Revenue. The Department of Revenue also certifies health care providers as eligible to claim the electronic medical records tax credit.

Community Rehabilitation Program Credit. A community rehabilitation program tax credit that equals 5% of the amount the claimant pays in a tax year to a community rehabilitation program to perform work for the claimant's business is available for tax years beginning on or after July 1, 2011. The maximum tax credit that can be claimed is \$25,000 for each community rehabilitation program that the claimant enters into a contract with, and unused credit amounts can be carried forward up to 15 years to offset future tax liabilities. In order to claim a credit, the claimant is required to submit with the

claimant's tax return verification that the claimant has entered into a contract with a community rehabilitation program and that the program has received payment from the claimant for work provided by the program.

Food Processing Plant and Food Warehouse Investment Credit. For taxable years beginning after December 31, 2009 and before January 1, 2017 a refundable credit is available for investments in modernization or expansion of food processing plants and food warehouses. "Food processing plant or food warehouse modernization or expansion" is defined as constructing, improving, or acquiring buildings or facilities, or acquiring equipment if used exclusively for food processing or food warehousing and if acquired and placed in service in this state during taxable years that begin after December 31, 2009, and before January 1, 2017.

The maximum aggregate amount of credits that may be claimed by a claimant is \$200,000 for all tax years. Claimants must be certified by the Department of Agriculture, Trade, and Consumer Protection (DATCP) as eligible for the credit, and the claimant must include a copy of the certification with the tax return when the credit is claimed. DATCP allocates credits among claimants. The maximum amount that may be allocated is \$1.0 million in fiscal year 2010, \$1.2 million in fiscal year 2011, and \$700,000 in fiscal years 2012 through 2017.

Woody Biomass Harvesting and Processing Equipment Credit. A refundable woody biomass harvesting and processing tax credit equal to 10% of the amount the claimant paid in the tax year for equipment that is used primarily to harvest or process woody biomass that is used for fuel or as a component of fuel is available for taxable years beginning after December 31, 2009, and before January 1, 2016. "Woody biomass" is defined as trees and woody plants, including limbs, tops, needles, leaves, and other woody parts, grown in a forest or woodland or on agricultural land.

Claimants must be certified by DATCP as eligible to receive the credit, and DATCP allocates credits among claimants. The maximum amount of credit that may be allocated in a year is \$900,000, and the maximum aggregate amount of credits that a claimant may claim for all tax years is \$100,000.

Qualified Production Activities Credit. For taxable years beginning after December 31, 2012, 2011 Act 32 created a non-refundable Qualified Production Activities Credit. The credit would equal a specified percentage of the claimant's qualified production activities income, as defined under the Internal Revenue Code, that is derived from property assessed as manufacturing or agricultural property in Wisconsin, as defined under state property tax law. Under the corporate income and franchise tax and for insurance companies, the credit would be the lesser of a specified percentage of the claimant's:

- qualified production activities income, as defined under the federal Internal Revenue Code, derived from manufacturing or agricultural property, in Wisconsin, as defined under state property tax law;
- income apportioned to Wisconsin for state corporate income and franchise tax purposes; or
- income determined as taxable under state combined reporting provisions.

The specified tax credit percentages are as follows:

- 1.875% for tax years beginning after December 31, 2012, and before January 1, 2014;
- 3.75% for tax years beginning after December 31, 2013, and before January 1, 2015;
- 5.526% for tax years beginning after January 31, 2014, and before January 1, 2016; and
- 7.5% for tax years beginning after December 31, 2015.

Unused tax credit amounts may be carried forward up to 15 years to offset future tax liabilities.

5. Agricultural Credits

Dairy and Livestock Farm Investment Credit. A nonrefundable credit is available for 10% of expenses to modernize or expand a dairy or livestock farm. Dairy animals include heifers raised as replacement dairy animals. Livestock includes cattle (not including dairy animals), swine, poultry including farm-raised pheasants but not including other farm raised game birds or ratites, fish that are raised in aquaculture facilities, sheep, and goats. The aggregate amount of credit that a taxpayer may claim is \$75,000 for expenses to construct, improve, and acquire buildings or facilities and equipment, for dairy animal housing, confinement, feeding, milk production, and waste management, except that no more than \$50,000 may be based on expenses that are incurred prior to May 27, 2010. The credit may be claimed for dairy farm modernization or expansion for taxable years that begin after December 31, 2003, and before January 1, 2017. The credit may be claimed for livestock farm modernization or expansion for taxable years beginning after December 31, 2005 and before January 1, 2017.

In tax year 2008, \$7.3 million of credit was available to 455 C-corporation taxpayers. Of this amount, \$905,000 was used by 222 corporations and \$6.4 million was carried forward for use in future tax years. In addition, 10,379 individual filers had \$72.4 million in available credit. Of this amount, \$14.0 million was used by 7,235 individuals and \$58.4 million was carried forward for use in future tax years.

*Farmland Preservation Credit.*⁹ Corporations are eligible for Farmland Preservation Credits and must meet basically the same requirements as individual taxpayers. Income for corporations is defined as the sum of net corporate income, any business loss carry forward allowed under section 71.26 (4), Wis. Stats., and the household income of each corporate shareholder including the income of spouse, dependents, and other members of the household. Corporations must include in their household income farm depreciation in excess of \$25,000, all nonfarm depreciation and nonfarm business losses. The credit is refundable.

The credit is available for tax years through 2009, although the credit may still be claimed for tax years after 2009 for preservation agreements entered into before July 1, 2009. For tax years 2010 and after, the Farmland Preservation Credit and the Farmland

⁹ For more information on the Farmland Preservation Credit, see Publication 503, "Wisconsin Farmland Preservation Credit," available at <http://www.revenue.wi.gov/pubs/pb503.pdf>

Tax Relief Credit have been replaced with a single program called the Farmland Preservation Credit, 2010 and Beyond (see below).

In tax year 2008, 256 C-corporation taxpayers claimed \$206,000 in refundable farmland preservation credit. In addition, 16,982 individual filers claimed \$11.6 million in credit.

Farmland Preservation Credit, 2010 and Beyond. Beginning in tax year 2010, a refundable per-acre farmland preservation credit is available under which a claimant may claim as a credit against income taxes an amount calculated by multiplying the claimant's qualifying acres by one of the following amounts:

- \$10 if the qualifying acres are located in a farmland preservation zoning district and are also subject to a farmland preservation agreement that is entered into after the budget's effective date;
- \$7.50 if the qualifying acres are located in a farmland preservation zoning district but are not subject to a farmland preservation agreement that is entered into after the budget's effective date; or
- \$5 if the qualifying acres are subject to a farmland preservation agreement that is entered into after the budget's effective date but are not located in a farmland preservation zoning district.

Dairy Manufacturing Facility Investment Credit. For tax years beginning after December 31, 2006 and before January 1, 2015, a refundable credit is available based on expenses incurred for modernization or expansion of a dairy manufacturing facility in this state. The maximum annual amount of credit that may be allocated to all claimants is \$700,000. The maximum aggregate amount a claimant may claim is \$200,000 for each of its dairy manufacturing facilities. "Dairy manufacturing modernization or expansion" is defined as constructing, improving, or acquiring buildings or facilities, or acquiring equipment, for dairy manufacturing, including the following, if used exclusively for dairy manufacturing.

DATCP must certify dairy manufacturer's as eligible for the credit. In the event that the total dollar amount of applications for the credit exceeds the annual limit, DATCP will allocate the credit on a pro-rata basis to the applicants.

For tax year 2008, 25 dairy manufacturing facilities were certified to receive a total of \$700,000 in credit.

Dairy Cooperative Manufacturing Facility Investment Credit. For tax years beginning after December 31, 2008 and before January 1, 2017, a refundable credit is available to dairy cooperatives based on expenses incurred for modernization or expansion of the cooperative's dairy manufacturing facility in this state. The maximum amount of credit that may be allocated to all cooperatives is \$600,000 in FY 2010 and \$700,000 in FY 2011 through FY 2017. The maximum aggregate amount a single cooperative may claim for all years is \$200,000 for each of its manufacturing facilities. The dairy cooperative would apply to the DATCP for the credit but may not claim the credit. Instead, the cooperative passes the credit through to its members.

The definition of "dairy manufacturing facility" and other terms are the same as for the dairy manufacturing facility credit outlined above.

Meat Processing Facility Investment Credit. 2009 Act 2 created a refundable meat processing facility investment tax credit equal to 10% of the amount the claimant paid in the tax year for meat processing modernization or expansion related to the claimant's meat processing operation. The tax credit can be claimed for tax years beginning after December 31, 2008 and before January 1, 2017. The maximum aggregate amount of meat processing facility investment tax credits that can be claimed by a claimant in all years is \$200,000. The total amount of tax credits that can be claimed is limited to \$300,000 in fiscal year 2010 and \$700,000 in fiscal years 2011 and thereafter.

"Meat processing modernization or expansion" is defined as constructing, improving, or acquiring buildings or facilities or acquiring equipment for meat processing if acquired and placed in service in this state during taxable years that begin after December 31, 2008, and before January 1, 2017.

DATCP must certify meat processors as eligible for the credit. In the event that the total dollar amount of applications for the credit exceeds the annual limit, DATCP will allocate the credit on a pro-rata basis to the applicants.

Beginning Farmer and Farm Asset Credit. Available for tax years beginning after December 31, 2010, the refundable beginning farmer tax credit would equal the amount paid by the beginning farmer to enroll in a financial management program in the year to which the claim related. An individual is a beginning farmer if they have:

- a net worth of less than \$200,000,
- farmed for fewer than ten years out of the preceding 15 years,
- entered into a lease for a term of at least three years with an established farmer for the use of the established farmer's agricultural assets by the beginning farmer, and
- used the leased agricultural assets for farming.

The credit may be claimed on one-time basis, and the maximum credit that may be claimed would be \$500.

The farm asset owner tax credit would equal 15% of the lease amount received by an established farmer in the year to which the claim related. "Lease amount" is defined as the amount of the cash payment paid by a beginning farmer to an established farmer each year for leasing the established farmer's agricultural assets. The credit may only be claimed for the first three years of any lease of the established farmer's assets to a beginning farmer. The credit is refundable.

C. Other Special Tax Treatments

Wisconsin offers additional tax incentives in the form of deductions, exemptions, apportionment provisions, and organizational form of entity.

1. *Deduction for Corporate Dividends Received.* A deduction is allowed for 100% of dividends received from subsidiaries in which the parent company owns at least 70% of the voting stock. The deduction is also allowed for dividends received by one member of a combined group that are paid by another member of the same combined group if the

dividends are paid out of the earnings and profit reported on the combined return. The ownership threshold for membership in a combined group is at least 50% of the voting stock.

The rationale for the deduction is that corporations are required to treat their investment income, including dividends, as business income subject to the multistate apportionment formula. In the case of dividends received from unitary subsidiaries, the transactions do not constitute the realization of income but merely the transfer of funds among branches of a unitary business entity. The deduction, it is argued, provides the same treatment as that for similar transfers of funds among unincorporated divisions, which are not taxed.

2. *Deduction for Job Creation.* For taxable years beginning on or after January 1, 2011, employers may take a deduction equal to the increase in the number of full-time equivalent employees during the taxable year multiplied by \$4,000 if gross receipts in the taxable year are \$5 million or less, or by \$2,000 if gross receipts in the taxable year are greater than \$5 million.
3. *Apportionment Formula.* Corporations that conduct business in more than one state must apportion their net income among the states with jurisdiction to tax the income. For taxable years 2007 and before, the Wisconsin portion of taxable income for businesses that operated in multiple states was determined by using a formula that had three factors – sales, payroll, and property. For tax years 2008 and after, a single sales factor formula is used, with the numerator being Wisconsin sales and the denominator being total companywide sales.

The change to a single sales factor did not affect equally all corporations with income apportionable to Wisconsin. Individual companies could have had a tax increase or a tax decrease depending on the organization of their business compared to prior law. A multi-state company based in Wisconsin (and therefore having a larger share of its total property and payroll in the state) with relatively greater sales outside Wisconsin benefits from a single sales factor formula. For example, a company with 80% of its property and 60% of its payroll attributed to Wisconsin and in-state sales of 20% would apportion 45% of its income to Wisconsin under the double-weighted sales factor formula $((80\% + 60\% + 20\% + 20\%) / 4 = 45\%)$. If income were apportioned with a single sales factor formula, the company would apportion 20% of its income to Wisconsin.

At the other extreme, a non-Wisconsin corporation with 1% of its property and 0.5% of its payroll in Wisconsin and Wisconsin sales of 2% would have a Wisconsin apportionment factor of 1.38% under the present double-weighted sales formula. This company would apportion 2% of its income to the state under the single sales factor formula. While the difference between 2% and 1.38% may not appear to be overly significant, when applied to the apportionable income of a large multi-state or multinational corporation, the difference in Wisconsin corporate tax liability can be substantial.

For most types of corporations, the numerator of the factor is comprised of sales in Wisconsin, while the denominator is total sales without regard to location. For members of corporate groups that are required to file a combined report, each member determines its sales both within Wisconsin as well as total sales. Sales between members of the same corporate group are disregarded. The total sales for each member are summed to derive a common denominator for the sales factor for all members. Total group income

is apportioned to each member based on the member's Wisconsin sales as a share of total group sales everywhere. Members with no sales in Wisconsin will have no apportionable income that is taxable to Wisconsin.

Like most states, Wisconsin uses special apportionment formulas for certain industries. The following table shows the special industry factors used in the apportionment formula. Each factor measures the share of Wisconsin activity to total activity, e.g., Wisconsin payroll to total payroll. In each case where multiple factors are listed, the apportionment percentage for the specific industry is the arithmetic average of the factors listed.

TABLE 1 SPECIAL INDUSTRY APPORTIONMENT FACTORS	
Industry	Factors
Interstate Pipeline Companies	Three equally-weighted factors - property, payroll, and traffic units
Interstate Financial Institutions	Single receipts factor
Interstate Telecommunications Companies	Three equally-weighted factors - property, payroll, and sales
Insurance Companies	Single premiums factor
Interstate Air Carriers	Three equally-weighted factors - revenue tons, originating revenues, and arrivals and departures
Interstate Motor Carriers	Two equally-weighted factors - gross receipts and ton miles of carriage
Interstate Railroads, Sleeping Car Companies, Car Line Companies	Two equally-weighted factors - gross receipts and revenue ton miles
Interstate Broker-Dealers, Investment Advisers, Investment Companies, and Underwriters	Single receipts factor

In calculating the sales factor under the multi-state apportionment formula, taxpayers are required to treat certain "throwback" sales as being the equivalent of Wisconsin sales. Throwback sales are shipments to the federal government or to customers located in states where the seller is not subject to tax due to the nexus standards defined by federal law (P.L. 86-272) and further clarified by the Wisconsin Administrative Code.

Under nexus standards, a corporation must have some type of operations in a state in the form of property or employees before its income can be taxed by that state. A corporation cannot be taxed by a state in which it does not have nexus. The purpose of the throwback rule is to ensure that 100% of a multi-jurisdictional corporation's income is apportioned to states with jurisdiction to tax it (it does not matter if the state actually imposes a corporate income tax). In the absence of a throwback rule, sales to destinations where the seller does not have nexus would not be included in the numerator of the sales factor of any state. This would result in a company paying tax on less than its entire income.

4. *Exemption for Activities of Out-Of-State Publishers and Certain Other Foreign Corporations.* Certain foreign corporations are exempt from the state nexus guidelines and, therefore, are not required to file a Wisconsin tax return. In particular, out-of-state publishing companies that contract with Wisconsin printing firms for the printing, storage and distribution of books, magazines, and other publications are exempt from income and franchise tax. As a result, foreign publishers, often with no payroll, plant or

equipment in Wisconsin, are not liable for Wisconsin tax simply because they purchase raw materials and store inventory on the premises of in-state printers. This exemption removes a disincentive for the publishers to do business with in-state printers.

In addition, the temporary storage of inventory on the premises of Wisconsin firms when the intent is to distribute all of the goods outside the state does not create nexus for the out-of state firms.

5. *Pass-Through Entities.* Wisconsin provides for differential tax treatment of business income depending on the form of organization under which a business operates. Business income of S-corporations, partnerships and limited liability companies that choose to be treated as partnerships is reported and taxed on the individual income tax returns of the owners (shareholders, partners or members) of the business.

Wisconsin law permits the formation of Subchapter S corporations and limited liability companies. Both of these entities combine the benefits of limited liability offered to corporations, with pass-through of income to the individual owners. Thus, these entities generally pay no tax at the entity level. Instead, income is passed through to the individual shareholders or members, who pay tax on the income at the lower individual income tax rates. (The individual income tax rates range from 4.6% to 7.75%, compared to the 7.9% corporate income tax rate.) This flow-through aspect of income also avoids the double taxation of C-corporation dividends that occurs when profits are first taxed at the corporate level and then again at the individual level when profits are distributed as dividends to individual shareholders.

- a. *Subchapter S Corporations*¹⁰. Wisconsin has federalized its treatment of Subchapter S corporations. Subchapter S, or "tax-option" corporations, elect to have their income exempted from the corporate income tax. The net profit or loss of these companies, with certain exceptions, is instead attributed to stockholders on a prorated basis and taxed under the individual income tax. Interest income on debt issued by federal, state, and municipal governments is taxable at the entity level. In addition, S corporations with more than \$4 million in gross receipts are also subject to the economic development surcharge. Finally, S corporations are subject to a tax on certain built-in gains (gains on sale of assets held at the time of conversion to an S corporation).

Typically, "tax-option" corporations are small businesses with fairly simple capital structures. The IRC restricts the number of shareholders to a maximum of 100. It also imposes a number of other limitations, such as the amount of passive investment income that can be earned and the types of stock that can be issued.

Tax liability is determined as of the end of each stockholder's tax year and must be paid regardless of whether or not the corporate income has been distributed. A major impact of exempting S-corporation income at the entity level is that capital gains realized by the S corporation qualify for the state net capital gain exclusion for individuals when the gains are passed through to the shareholders. Up until tax year

¹⁰ For more information on Wisconsin tax treatment of Subchapter S corporations, see Publication 102, "Wisconsin Tax Treatment of Tax-Option (S) Corporations and Their Shareholders," available at <http://www.revenue.wi.gov/pubs/pb102.pdf>.

2009, this exclusion was 60% for long term gains; 2009 Act 28 reduced the exclusion to 30%.¹¹

- b. *Limited Liability Companies (LLCs)*¹². Owners (called members) of limited liability companies (LLCs) are taxed on the flow-through income of the company at lower individual income tax rates rather than at the higher corporate rate if the LLC elects to be treated for tax purposes as a partnership or S-corporation. LLCs allow for greater flexibility than S-corporations in the way they can be structured. For example, while S-corporations allow only individuals to be owners, LLC members can include corporations, partnerships, foreign entities, trusts, and charitable organizations as well as individuals. An LLC can have an unlimited number of members as owners and profits and losses can be more freely allocated among the members.

An LLC may be classified for federal income tax purposes as a partnership, a corporation, a subchapter S corporation, or as an entity disregarded as a separate entity from its owner. If an LLC is classified as a partnership for federal income tax purposes, it is treated as a partnership for Wisconsin purposes. An LLC classified as a corporation for federal income tax purposes is treated as a corporation by Wisconsin. An LLC disregarded as a separate entity for federal income tax purposes is also disregarded as a separate entity for Wisconsin income tax purposes.

- c. *Partnerships*. A partnership is an association of two or more persons to carry on as co-owners a trade or business for profit. The term “partnership” includes a limited partnership, registered limited liability partnership, syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and is not, within the meaning of the Wisconsin income tax law, a corporation, trust, estate, or sole proprietorship.

As with S corporations and LLCs that elect to be treated as partnerships for tax purposes, income and losses generated by the partnership are passed through to the partners and will be reported on the partner's individual returns. Partnerships with over \$4 million in gross receipts are subject to the economic development surcharge.

¹¹ Long-term capital gains of farm assets retain the 60% exclusion. Farm assets include farm livestock, farm real property, farm depreciable property or farm equipment.

¹² For more information on Wisconsin tax treatment of limited liability companies, see Publication 119, "Limited Liability Companies," available at <http://www.revenue.wi.gov/pubs/pb119.pdf>.

PROPERTY TAX

A. Description

All real and tangible personal property is subject to taxation unless expressly exempt. Except for farmland, agricultural forest, and undeveloped land, real property is assessed at full market value, i.e., the full value ordinarily obtained at private sale, and personal property is assessed at true cash value. Classes of real property include residential, commercial, manufacturing, agricultural, agricultural forest, undeveloped, productive forest land, and other (defined as farm buildings and improvements to land). Intangible property is not subject to the property tax.

Except for manufacturing, telecommunication, and utility properties, valuation is made by the municipal assessor. Property is assessed on the value as of January 1. Manufacturing, telephone, and utility properties are assessed by the Department of Revenue. Manufacturers annually submit, on or before March 1, self-reporting forms of the original installed costs of all property owned that is still in operation. The Department of Revenue conducts field appraisals of each parcel once every five years.

Property tax incentives include specific exemptions and special tax districts.

B. Exemptions

1. *Machinery and Equipment Used in Manufacturing.* Machinery and equipment used in manufacturing is exempt from property taxes – the exemption greatly reduces the property tax burden on manufacturers. There are approximately 11,000 manufacturers in the state. For the 2010/11 property tax year, \$1.50 billion of manufacturing machinery and equipment was taxable. Assuming that 10% of all manufacturing machinery and equipment is taxable, approximately \$13.5 billion of machinery and equipment is currently exempt from tax. Based on this assumption, the exemption resulted in an estimated tax shift of \$290 million from owners of manufacturing machinery and equipment to other property owners.
2. *Merchants' and Manufacturers' Inventories.* Inventories of manufacturers and merchants are fully exempt from personal property taxes. A tax on inventories is viewed as inequitable because businesses differ in their annual inventory cycle, making a fixed date of assessment a poor measure of average inventory levels. In addition, taxing inventories penalizes businesses for storing products in Wisconsin.
3. *Waste Treatment Facilities.* Certain facilities used to treat wastes are exempt from general property taxation. A waste treatment facility is property (land, improvements, and machinery) used for the treatment of industrial waste materials, including particulates, gas, solids, liquids, and other superfluous products. Qualifying facilities must remove, alter or store waste materials. The exemption is available to utilities, manufacturers, and commercial businesses. The Department estimates that approximately \$2.8 billion of manufacturing and commercial waste treatment property is exempted. An estimate of the amount of utility waste treatment property that is exempted is not available.
4. *Computer Equipment.* Wisconsin provides property tax exemptions for certain computer equipment. Exempt from tax are: mainframe computers, minicomputers, personal computers, networked personal computers, servers, terminals, monitors, disk drives,

electronic peripheral equipment, tape drives, printers, basic operational programs, systems software, prewritten software, fax machines and cash registers. The exemption does not apply to copiers, custom software, equipment embedded with computerized components or telephone systems. Special payments are made to affected local municipalities to compensate for the lost tax base. For the 2010/11 property tax year, approximately \$3.49 billion in computer equipment was exempted, and computer aid payments totaled \$82.0 million.

C. Tax Incremental Finance Districts

Wisconsin allows the use of tax incremental finance (TIF) districts and environmental remediation TIFs as development tools for cities, villages and, for limited projects, towns and counties. The purpose of TIF is to encourage economic development that would not occur without some assistance. A municipality may form a tax incremental district, or TID, for purposes specified by statute. These purposes, as well as other statutory requirements and restrictions, vary by type of municipality and are discussed below.

A review board made up of representatives from the overlying taxing jurisdictions and a public member must approve the creation of the district and the district's project plan, and must assert that the development would not occur without the TIF district. This board may request DOR review of objective facts regarding a proposed TID – the description of boundaries, the finding that the TID satisfies territorial limits, and the finding that the proposed TID is blighted, in need of rehabilitation or suited for industrial or mixed use.

When a TIF district is created, the current value in the district is set as its "base value." Improvements and development that occur after the district's creation lead to increases in its value over the base value, referred to as "increment value." The property taxes levied by all taxing jurisdictions (i.e., the municipality, county, school district, and technical college) on the increase in the district's value are used to pay the public improvements needed for the development to occur.

In this way, the cost of providing the infrastructure for the district is not incurred solely by the municipality, but is shared among all taxing jurisdictions. Typical public improvements in a district include land acquisition, sewer and storm water construction, and street improvements. Property owners in the district pay the same amount of property taxes as they would outside a TIF district; however, the taxes paid on the value increases go directly to paying for the public improvements made within the district. The tax on the base value continues to go to the taxing jurisdictions that levy the tax. After a TIF district terminates, the taxes paid by the property owners within the district, both on the base value and on the increment value, are shared by all taxing jurisdictions.

1. *TIF for Cities and Villages.* Cities and villages that create a TID must declare the type of district created: "blighted," "rehabilitation or conservation," "industrial" or "mixed-use." The declaration is based on the type of real property that makes up at least 50% of the area in the district or which of the four types is predominant in the district. Each type of TID must meet specific requirements for its designation and adhere to defined project expenditure and maximum life periods.

A city or village may create a TID as long as the equalized value of the proposed TID, plus the increments of all existing TIDs in the municipality, do not exceed 12% of a municipality's total value. The 12% test does not apply if, simultaneously, a new TID is created and territory of equal or greater value is subtracted from an existing TID. In

addition, annexed land may not be included in a TID until three years after its annexation, unless there is a border agreement or tax payment to the town by the annexing municipality. A municipality may amend a TID project plan up to four times after its creation.

Counties with no cities or villages may create a TID if the town board in which the proposed TID is located adopts a resolution approving the creation of the district. A town may use city powers to create a TID if the town has entered into a cooperative plan with a city or village for annexation of the town or part of a town in a future. The annexing city or village must approve the creation of the town TID.

As of June 1, 2011, there were 1,053 city and village TIF districts in existence.

2. *Town TIF.* In addition to the town TIDs allowed through cooperative plans, as noted above, beginning on October 1, 2004, towns can create TIDs for limited projects that fall within the following North American Classification System (NAICS) codes:
 - Agricultural: crop production (111), agricultural production (112), support activities for agriculture (1151) or animal production (1152), and refrigerated farm product warehousing and storage (493120).
 - Forestry: forestry and logging (113) and support activities for forestry (1153).
 - Manufacturing: animal slaughtering (3116), wood product manufacturing (321), paper manufacturing (322), and ethyl alcohol manufacturing (325193).
 - Tourism: recreational and vacation camps (721214), recreational vehicle parks and campgrounds (721211), racetracks (711212), dairy product stores included in 445299, and public golf courses included in 71391. (Classification 445299 includes more than dairy product stores and 71391 includes more than public golf courses.)

Limited residential development, including sleeping quarters for employees, is permitted in town TIDs, though hotels and general residential development are specifically prohibited. Also, retail development is permitted only for products that are produced as a result of an agricultural or forestry project. Town TIDs also are subject to many of the provisions that apply for TIDs in cities and villages.

As of June 1, 2011, there were three town TIDs in existence.

3. *Environmental Remediation TIF.* Since 1997, cities, villages, towns, and counties have the authority to create environmental remediation tax incremental financing (ER TIF) districts to recover the costs of remediation of environmental pollution. The funding mechanism is the same as other TIF districts; however, there are several differences between the two financing tools.

Project expenditures for ER TIF districts are limited to costs associated with environmental remediation, such as professional services associated with the investigation, containment, removal, and monitoring of contaminants. Expenditures in an ER TIF district may be incurred prior to the creation of the district.

As of June 1, 2011, there were 18 ER TIF districts in existence.

SALES AND USE TAX

A. Description

Wisconsin imposes a 5% tax on the sale or use of tangible personal property that is not specifically exempted from the tax and on selected services that are explicitly listed as subject to tax. Taxable services include hotel or other temporary lodging, admissions, certain telecommunications and telephone answering services, laundry and dry cleaning, photographic services, parking, repair and other services to tangible personal property, certain printing and production services, cable television services, and landscaping services.¹³

Counties may impose a 0.5% local sales and use tax on the same tax base as the state sales tax. As of January 1, 2011, 62 of the state's 72 counties impose the additional tax. A 0.5% professional football stadium district sales and use tax is imposed only in Brown County. Proceeds of this tax are used to finance renovation of Lambeau Field in Green Bay. A 0.1% professional baseball park district sales and use tax is imposed in five counties (Milwaukee, Ozaukee, Racine, Washington, and Waukesha). Proceeds of this tax are used to finance a new baseball park for the Milwaukee Brewers.

B. Exemptions

The following exemptions from the sales and use tax apply to a wide number of industries. In addition, Wisconsin provides exemptions targeted at specific industries, including meat packing, printing, newspapers, logging, and motion pictures.

1. *Manufacturing Machinery and Equipment.* Wisconsin allows a comprehensive sales and use tax exemption for purchases of machinery and equipment used directly and exclusively in a manufacturing process. Manufacturing is defined as the production of a new item of tangible personal property using machinery. The new article must be of a different form or have a different use or name than the material from which it was created. Machinery and equipment used in activities such as the storage or delivery of finished products or research and development are not exempt. In FY10, the sales and use tax exemption for manufacturing machinery and equipment reduced sales and use taxes by an estimated \$\$191 million for the approximately 10,000 manufacturers in the state.
2. *Manufacturers' Materials.* Wisconsin exempts from sales and use tax tangible personal property that becomes an ingredient or component part of an item of tangible personal property. Wisconsin also exempts sales of tangible personal property that is consumed or loses its identity in the process of manufacturing tangible personal property.
3. *Fuel and Electricity Used in Manufacturing.* Beginning January 1, 2006, fuel and electricity used in manufacturing is exempt from sales tax. This exemption replaced the income and franchise tax credit for sales and use taxes paid for fuel and electricity used in manufacturing. In FY10, this exemption is estimated to have reduced sales and use taxes by \$\$87 million.

¹³ More information can be found in Department of Revenue sales tax publications, available at <http://www.revenue.wi.gov/html/taxpubs.html#sales>

4. *Pollution Abatement, Waste Treatment, and Recycling Equipment.* Wisconsin exempts from sales and use tax pollution abatement equipment and waste treatment facilities. Also exempted are replacement parts, chemicals and supplies used for pollution abatement or waste treatment.
5. *Trucks, Tractors, and Buses sold to Common or Contract Carriers.* Sales of trucks, truck tractors, buses, trailers and semi-trailers and accessories, parts and supplies sold to common or contract carriers are exempt from sales tax. This exemption applies to urban mass transportation, bus and trucking companies, and other contract carriers. This exemption is estimated to have reduced sales and use taxes by \$27million in FY10.
6. *Alternative Energy.* 2007 Wisconsin Act 20 (the 2007-09 budget bill) created new exemptions for products whose power source is wind, solar, or gas generated from the anaerobic digestion of animal manure or other agricultural waste products. Act 20 also created an exemption for the electricity produced by the products listed above. The new exemptions become effective July 1, 2011. It is estimated that the new exemptions will reduce sales and use tax revenues by \$1.3 million annually.
7. *Biotechnology and Manufacturing Research.* 2009 Wisconsin Act 28 (the 2009-2011 budget bill) created new exemptions from the sales and use tax for purchases of machinery and equipment and tangible personal property used exclusively and directly in, or consumed in, qualified research in manufacturing or biotechnology. New exemptions were also created for machines, equipment, and tangible personal property used exclusively and directly in raising animals sold to a biotechnology business, a public or private institution of higher education, or a governmental unit for exclusive use in qualified research. The new exemptions become effective January 1, 2012. It is estimated that the new exemptions will reduce sales and use tax revenues by \$13 million annually.

INDIVIDUAL INCOME TAX

A. Description

Wisconsin imposes an individual income tax on a tax base that, to a large extent, conforms to the federal personal income tax base. There are, however, several important exceptions. Although Wisconsin law is based largely on federal law, the Legislature must actively adopt federal law changes in order for them to apply for Wisconsin tax purposes.

The starting point for determining Wisconsin taxable income is federal adjusted gross income (FAGI), subject to certain modifications and adjustments to account for differences in Wisconsin and federal law. From that base, the standard deduction and personal exemptions are subtracted to arrive at taxable income. Tax rates are then applied to determine gross tax liability, from which certain credits are then deducted.

The tax rates are shown in the following table. For all tax years beginning after 2001, all personal income tax brackets are indexed each year based on the consumer price index.

**TABLE 2
TAX RATES AND BRACKETS, 2011**

Single	Married, Joint	Married, Separate	Marginal Tax Rates
\$0 - \$10,180	\$0 - \$13,580	\$0 - \$6,790	4.60%
\$10,181 - \$20,360	\$13,581 - \$27,150	\$6,791 - \$13,580	6.15%
\$20,361 - \$152,740	\$27,151 - \$203,650	\$13,581 - \$101,820	6.50%
\$152,741 - \$224,210	\$203,651 - \$298,940	\$101,821 - \$149,470	6.75%
\$224,211 +	\$298,941 +	\$149,471 +	7.75%

If the personal income tax imposed for Wisconsin tax purposes, not considering certain credits, is less than the Wisconsin alternative minimum tax, the Wisconsin alternative minimum tax is imposed. Approximately 0.2 percent of individual filers paid Wisconsin alternative minimum tax in 2009.

Wisconsin offers tax benefits to individual taxpayers to encourage investment in the state that include special tax treatments for capital gains.

B. Capital Gains Treatments

1. *Exclusion for Long-Term Capital Gains.* Wisconsin allows individual taxpayers to exclude 30% of the net capital gain on non-farm assets held more than one year and 60% of the net capital gain on farm assets held more than one year. This exclusion is intended to encourage capital investment. The amount of the exclusion is also not included in the tax base for the state alternative minimum tax.
2. *Special Capital Gains Treatment for Wisconsin Small Businesses.* An exclusion is provided for 100% of the capital gains from the sale of stock in eligible Wisconsin small businesses that is held for five or more years. This exemption first applies to the gain on the sale of stock acquired on or after January 1, 1986. Qualified small business stock is defined as shares issued by a corporation that:
 - Has at least 50% of its payroll and property in Wisconsin;

- Has no more than 500 employees;
- Derives no more than 25% of its gross receipts from rents, interest, dividends, and sales of intangible investment assets combined;
- Has not previously issued stock that is traded on any of the major stock exchanges;
- Has not liquidated or reorganized for purposes of qualifying for this exemption.

There are a limited number of investments qualifying for the exclusion, and the tax benefit it provides is believed to be minimal.

3. *Capital Gains Exclusion for Intergenerational Transfers of Farming and Business Assets.* Wisconsin excludes from income all capital gains from intergenerational transfers of farming and business assets that are held more than one year and are sold or otherwise disposed of to persons related to the seller within the third degree of kinship. The exclusion applies to a limited number of transfers each year.
4. *Income Tax Deferral for Capital Gains Reinvested in New Business Ventures.* Beginning in 2011, Wisconsin allows an income tax deduction for the full amount of the net capital gain, up to \$10 million, on assets held more than one year if the gain is reinvested in a qualified new business venture. The investor's basis in the new investment is reduced by the amount of the subtraction. Qualified new business ventures are determined and certified by the WEDC.
5. *Income Tax Deferral for Capital Gain Reinvested in Wisconsin Businesses.* Beginning in 2011, Wisconsin allows an income tax deduction for the full amount of the net capital gain on assets held more than one year if the gain is reinvested in a qualified Wisconsin business. The investor's basis in the new investment is reduced by the amount of the subtraction. Qualified Wisconsin businesses are determined and certified by the WEDC and must have at least 50% of its payroll and property in Wisconsin.
6. *Capital Gain Exclusion for Wisconsin Businesses.* Beginning with assets purchased in 2011, Wisconsin allows individual taxpayers to exclude the net capital gain on Wisconsin assets held more than five years. A Wisconsin asset is defined as real or tangible property located in the state and used in a Wisconsin business or stock or other ownership interest in a Wisconsin business. Qualified Wisconsin businesses are determined according to certain restrictions and certified by the WEDC and must have at least 50% of its payroll and property in the state.

C. Credits and Deductions

With the exception of the research credits, all of the business credits described above in the Corporate Income and Franchise Tax section are available to individual filers.¹⁴ Typical individual filers who claim these credits would be sole proprietors or owners of pass-through entities.

¹⁴ In the case of the business relocation credit, individuals are instead eligible for a comparable deduction, which is described later in this section.

In addition, individuals who invest in qualified new business ventures may claim the Angel Investment Credit. The angel investment tax credit is equal to 25% of the claimant's bona fide angel investment made directly in a qualified new business venture in a tax year. Similar to the Early Stage Seed Investment Credit described in the Corporate Income and Franchise Tax section above, the qualified new business venture must be certified by the WEDC. In addition, the angel investor must have the investment verified by the WEDC to claim the credit. Unused credit amounts can be carried forward up to 15 years to offset future tax liabilities. The maximum aggregate amount of angel investment tax credits that may be claimed for a tax year is \$5.5 million for tax years before December 31, 2010, and \$18.0 million, plus an additional \$250,000 for tax credits claimed for investments in nanotechnology businesses, for tax years beginning after December 31, 2010. The maximum total amount of tax credits that can be claimed for all tax years is \$47.5 million.

In tax year 2009, 528 individuals had \$5.6 million in Angel Investment credits available. Of that amount, 469 individuals used \$3.8 million to offset tax liability, leaving \$1.8 million available to be used to offset tax liability in future years.

Starting in 2011, individuals who relocate a business to Wisconsin from another state or country are allowed a full exemption of the qualifying business income for two taxable years beginning with the year in which the business relocates. In order to qualify for the exemption, the business must move either 51 percent or more of the workforce payroll of the business or at least \$200,000 of wages. Furthermore, the person may not have done business in Wisconsin during the prior two taxable years.