

Fair and Adequate Tax Policy

Modernizing state revenue policies to bolster community development

Background

While communities grow in certain areas, there is a real crisis in maintaining the high quality of public services that once characterized the state. Cuts in state shared revenue and a reduction in federal aid have created chronic financial crises at the city and county level. As communities work to build economic strength, the lack of fully effective public structures hinders the effort.

Unfortunately, too many people perceive the situation as a choice between higher property taxes or additional service cuts, a lose-lose proposition for everyone. This is actually a false choice that ignores the option of expanding state revenue. A broader tax base could ensure adequate funding for local communities and reduce reliance on the property tax. This requires state policy changes to modernize the tax structure so it can operate more effectively in a 21st century economy.

Defining modernization

The current tax structure was designed for a small farm and local factory era. It lacks capacity to capture needed revenues in a technically sophisticated economy with multi-national corporations whose armies of lawyers and accountants minimize costs and maximize profits. They have perfected numerous ploys to avoid paying taxes—especially corporate income taxes. Over 60% of the largest corporations doing business in the state pay no income tax at all because they move their profits from Wisconsin to paper subsidiaries in tax-free states like Nevada and Delaware. If these corporate giants would just pay their fair share for police, fire fighters, the courts and other vital services – our state would collect an additional half a billion dollars a year. Fortunately, some state leaders are looking to break the “cut-local-budgets” tradition by closing corporate tax loopholes that leak money from the state resource pool.

In addition, the current sales tax system was designed for a product economy, while we have become much more of a service economy with no sales tax on services. The World Wide Web was a fantasy when the state began collecting taxes, and we still have no ability to collect sales tax revenue on the massive expansion of Internet sales—an unfair penalty on local retailers who do collect sales tax.

In addition, the property tax system has failed to recognize the emergence of major forms of property that remain exempt from taxes. At one time hospitals generally served only poor. Like a homeless shelter today, these hospitals were, by definition, charitable organizations. Today, however, health care is a growth industry and many hospitals are enormous enterprises with lavish facilities and highly paid executives—indistinguishable from for-profit businesses. They remain, however, exempt from taxes while small businesses and homeowners cover the hospitals' share of public sector expenses. Also, some large housing facilities for more affluent seniors remain exempt from the property tax. An up-to-date tax system would expand revenue collection and better balance tax responsibilities.

Possible items for legislative agendas

I: Sales tax from Internet sales -- \$200,000,000+

There is virtually no sales tax revenue coming from purchases made on the Internet, despite the enormous growth in this retail sector. State estimates are that annual lost revenue is on the order of two hundred million dollars or more.

This is not unique to Wisconsin. But twenty-two states are doing something about it, by participating in the national Streamlined Sales Tax project. Once enough states have agreed on uniform definitions regarding sales taxes, Internet retailers will begin charging sales tax and sending the proceeds to the states.

Wisconsin has not joined the effort because the Assembly has refused to pass needed legislation. Joining the national Streamlined Sales Tax effort has the support of the Governor, the Senate and the Department of Revenue.

Collecting Internet sales tax would not only broaden the sales tax base and bring needed revenue to the state, but would also level the playing field for Wisconsin retailers. Local stores are at a price disadvantage to Internet retailers because online buyers can evade paying the sales tax.

II: Closing the Real Estate Investment Trust corporate tax loophole: \$100,000,000

The Real Estate Investment Trust (REIT) loophole is one among many tax-avoidance mechanisms available to corporations. The most well-known abuser in Wisconsin is Wal-Mart, which has confirmed using the technique for 82 of its 89 Wisconsin stores.

It involves a company having one subsidiary operating its Wisconsin facilities and a separate subsidiary (structured as a REIT) owning the facilities. The rent paid by the operating subsidiary to the REIT is so high as to wipe out profits. But the REIT is structured so its profits are tax-free.

The Department of Revenue has taken Wal-Mart to court, arguing that its use of this tactic in 1997, '98 and '99 enabled it to avoid tax on over \$104 million in profits. It is not known how many other firms use the technique, but many national retailers are known to use it in other states. Closing this loophole was included in Gov. Doyle's budget repair proposal.

III. Corporate Tax Disclosure

We know that over 60% of the largest corporations in Wisconsin pay no income tax and some use loopholes to move profits out of state – but information is limited. State law makes it difficult to find and share corporate tax facts. If we are going to plug unfair loopholes, we need to know where they are and how much they cost other taxpayers. Transparency is crucial so citizens see how tax responsibility is distributed.

The Corporate Tax Transparency Act would ensure that policymakers and the public had access to the corporate tax information necessary to decide if and what tax policy changes are actually needed to ensure a fair and adequate system. .

The Corporate Tax Transparency Act will require publicly held companies (less than 1% of all businesses) to disclose information on both income and taxes for the company and each of its subsidiaries. It will provide the bottom line information needed to discuss tax issues in an intelligent and businesslike manner. The Act was introduced by Senator Dave Hansen (SB367) but was not voted on in the 2008 session.