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April 7, 2010

TO: Members
Joint Committee on Finance

FROM: Bob Lang, Director

SUBJECT: Assembly Bill 768: Department of Commerce -- Enterprise Zones

Assembly Bill 768 would allow Commerce to designate two additional enterprise zones. The bill was introduced on February 23, 2010, and referred to the Assembly Committee on Jobs, the Economy and Small Business. On March 2, 2010, AB 768 was recommended for passage by a vote of 10 to 0, and referred to the Joint Committee on Finance.

CURRENT LAW

Enterprise Zones. The enterprise zone program was created by 2005 Wisconsin Act 361. Under the enterprise zone program, the Department of Commerce is authorized to designate up to 10 areas in the state as enterprise zones. A zone designation cannot last more than 12 years. Eligible businesses that conduct operations in an enterprise zone that are certified by Commerce can claim the refundable enterprise zone tax credits.

In determining whether to designate an area as an enterprise zone, Commerce is required to consider all of the following:

a. Indicators of the area's economic need, including data regarding household income, average wages, the condition of property, housing values, population decline, job losses, infrastructure and energy support, the rate of business development, and the existing resources available to the area.

b. The effect of designation on other initiatives and programs to promote economic and community development in the area, including job creation and job training, and creating high-paying jobs.

Under 2009 Act 11, Commerce is required to specify whether an enterprise zone is in a tier I or tier II county or municipality, and to promulgate rules defining "tier I county or municipality" and "tier II county or municipality." The Department has to consider all of the following information when establishing the definitions: (1) unemployment rate; (2) percentage of families with incomes below the poverty line; (3) median family income; (4) median per capita income; and (5) other significant or irregular indicators of economic distress, such as a natural disaster or mass layoff. To the extent possible, Commerce must give preference in designating areas to those with the greatest economic need. The Department is in the process of promulgating these rules.

Commerce is required to certify a business as eligible for the enterprise zone jobs tax credit. The Department may certify for tax benefits any of the following:

a. A business that begins operations in an enterprise zone.

b. A business that relocates to an enterprise zone from outside the state, 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 outside the zone (as determined by Commerce).

c. A business that expands its operations in an enterprise zone, and increases its personnel by at least 10%, and enters into an agreement with Commerce to claim tax benefits only for years during which the business maintains the increased level of personnel. The business must offer compensation and benefits for the same type of work to its employees working in the enterprise zone that are at least as favorable as those offered to its employees working in Wisconsin but outside the zone (as determined by Commerce).

d. A business that expands its operations in an enterprise zone and that makes a capital investment in property located in the enterprise zone if the following apply: (1) the value of capital investment is equal to at least 10% of the business' gross revenues from business in the state in the preceding tax year; (2) the business enters into an agreement with Commerce to claim tax benefits only for years during which the business maintains the capital investment; and (3) the business offers compensation and benefits for the same type of work to its employees in the zone that are at least as favorable as those offered to employees working in Wisconsin, but outside the zone (as determined by Commerce).

e. A business that retains jobs in an enterprise zone, but only 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 was an original equipment manufacturer with a significant supply chain in Wisconsin [as determined by Commerce]; or (2) more than 500 full-time employees were employed by the business in the enterprise zone.

Commerce must notify the Department of Revenue (DOR) when it certifies a business to receive tax benefits and when it revokes certification. Commerce is required to revoke a firm's certification if the business does any of the following:

a. Supplies false or misleading information to obtain tax benefits.

b. Leaves the enterprise zone to conduct substantially the same business outside the zone.

c. Ceases operations in the zone and does not renew operation of the business or a similar business in the zone within 12 months.

Enterprise Zone Tax Credits. The enterprise zone program provides refundable tax credits that can be claimed under the state individual income and corporate income and franchise taxes for eligible expenses for increased employment, retaining employees, employee training, and capital investment.

Enterprise Zones Jobs Tax Credit. The enterprise zones jobs tax credit is a refundable tax credit and is provided under the state individual income and corporate income and franchise taxes to businesses that are certified by the Department of Commerce. The enterprise zones jobs tax credit is calculated as follows:

a. Determine the lesser of: (1) the number of full-time employees that are employed in an enterprise zone whose annual wages are greater than $20,000 in a tier I county or municipality or greater than $30,000 in a tier II county or municipality in the tax year, minus the number of full-time employees that are employed in the enterprise zone in the base year whose annual wages are greater than $20,000 in a tier I county or municipality or greater than $30,000 in a tier II county or municipality; or (2) the number of full-time employees in the state whose annual wages are greater than $20,000 in a tier I county or municipality or greater than $30,000 in a tier II county or municipality in the tax year minus the number of full-time employees in the state in the base year whose annual wages are greater than $20,000 in a tier I county or municipality or greater than $30,000 in a tier II county or municipality.

b. Determine the claimant's average zone payroll by dividing total wages for full-time employees in the zone whose annual wages are greater than $20,000 in a tier I county or municipality or greater than $30,000 in a tier II county or municipality and who the claimant employed in an enterprise zone for the tax year, by the number of employees whose annual wages are greater than $20,000 in a tier I county or municipality or greater than $30,000 in a tier II country or municipality and who the claimant employed in the enterprise zone in the tax year.

c. For employees in a tier I county or municipality subtract $20,000 from the average wage determined under " b," and for employees in a tier II county or municipality subtract $30,000 from the average wage determined under "b."

d. Multiply the amount determined under "c" (average wage in excess of $20,000 a year in a tier I county or municipality or in excess of $30,000 a year in a tier II county or municipality) by the number determined under "a" (net number of new employees hired in the zone).

e. Multiply the amount determined under "d" by a percentage determined by the Department of Commerce, not to exceed 7%.

Payroll Tax Credit. An additional refundable tax can be claimed, under the state individual income and corporate income and franchise taxes, for an amount equal to the percentage up to 7%, as determined by Commerce, of the claimant's zone payroll paid in the tax year to full-time employees who were employed in the enterprise zone in the tax year and whose annual wages were greater than $20,000 in a tier I county or municipality, or greater than $30,000 in a tier II county or municipality, not including the wages paid to employees that are used to claim the enterprise zone jobs credit. The total number of employees has to equal or be greater than the number of employees in the base year. Credit claims are limited to five consecutive years.

Job Retention. A refundable tax credit can be claimed, under the state individual income and corporate income and franchise taxes, for job retention, if the business makes a significant capital investment and is an original equipment manufacturer or has more than 500 full-time employees in an enterprise zone.

Training Component. The claimant may claim a supplemental, refundable credit, under the state individual income and corporate income and franchise taxes, equal to the amount paid in the tax year to upgrade or improve the job-related skills of any of the claimant's full-time employees, to train any of the claimant's full-time employees on the job-related use of new technologies, or to provide job-related training to any full-time employee whose employment with the claimant represents the employee's first full-time job. The training must be provided to employees who work in the enterprise zone

Significant Capital Expenditures. A refundable tax credit is provided, under the state individual income and corporate income and franchise taxes, equal to an amount determined by the Department of Commerce, but not exceeding 10% of the claimant's significant capital expenditures in the enterprise zone. Commerce must determine that the business investment is a significant capital expenditure, and allocate the tax benefits over the remaining life of the zone.

As noted, the credits are refundable. Therefore, if the amount of credit exceeds the claimant's income or franchise tax liability, the state issues a check to the claimant for the difference.

Partnerships, limited liability companies (LLCs), and tax option corporations may not claim a tax credit, but eligibility for, and the amount of credit is determined based on the economic activity of the entity. The partnership, LLC, or tax-option corporation must compute the amount of credit that may be claimed by each partner, member, or shareholder and provide that information to them. Partners, members of LLCs, and shareholders of tax-option corporations may claim the tax credit in proportion to their ownership interest.

The Department of Commerce is required to determine the maximum amount of tax credits that a certified business can claim and notify DOR of the amount. Commerce is also required to verify information submitted to it that is related to the enterprise zone tax credits. Claimants are required to include, with their tax returns, a copy of the certification for tax benefits and verification of expenses from Commerce. Businesses may not claim enterprise zone tax credits to the extent the basis for the credit is the basis for another tax credit claimed by the business.

Commerce may require a business to repay any tax benefits the business claims for a year in which the business failed to maintain employment or capital investment levels required by the certification agreement.

"Base year" means the tax year beginning during the calendar year prior to the calendar year in which the enterprise zone in which the claimant is located takes effect. "Claimant" means a person who is certified by Commerce to claim enterprise zone tax benefits and who files a claim for an enterprise zone tax credit. In general, "full-time employee" means an individual who is employed in a regular, non-seasonal job and who, as a condition of employment, is required to work at least 2,080 hours per year, including paid leave and holidays. Commerce can specify, by rule, circumstances under which it can grant exceptions to the requirement that a full-time employee means an individual who, as a condition of employment, is required to work at least 2,080 hours a year. However, under no circumstances, would a full-time employee mean an individual who, as a condition of employment, was required to work less than 37.5 hours per week. "State payroll" means the amount of payroll apportioned to this state under the income and franchise tax apportionment rules for multi-state businesses. "Zone payroll" is defined as wages paid to full-time employees for services performed in the enterprise zone. "Zone payroll" does not include the amount of compensation paid to any individual that exceeds $100,000. The definition of "wages" is referenced to federal Internal Revenue Code to mean all remuneration for employment, including the cash value of all remuneration (including benefits paid in a medium other than cash, with specified exceptions, such as payments to certain trusts or annuitant plans).

SUMMARY OF BILL

Assembly Bill 768 would increase, from 10 to 12, the number of enterprise zones that could be designated by the Department of Commerce.

FISCAL EFFECT

Under current law a total of 10 enterprise zones can be designated. Two enterprise zone projects have been contracted, a few projects have been identified as likely, but not yet contracted, and other projects are in discussion. The process of identifying, negotiating tax benefits, and designating a project varies, and is dependent upon each individual project considered. It is difficult to determine if all 10 authorized enterprise zone designations will be made during the 2009-11 biennium. In addition, the timing of enterprise zone tax credits claims also varies for each individual project. For example the contract with Uline, Inc. was completed in May, 2009, but the company will not start hiring at its new facility until 2010.

Based on experience with the enterprise zone program to date, it is estimated that authorizing an additional two enterprise zones would have a minimal fiscal effect in 2010-11. However, state GPR expenditures would be increased by an estimated $2.0 million in fiscal year 2011-12, and by $7.6 million in 2012-13, and annually thereafter for the life of the zone. There would be an increase in GPR expenditures, rather than a reduction in state tax revenues, because the enterprise zone tax credits are refundable.

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