

Introduction

Spending in Wisconsin has increased significantly in recent years. Total state spending increased by 47 percent from 1995 to 2017, significantly faster than population growth over the same period. Notably, most spending growth occurred in the period preceding the Great Recession and has slowed in years since.

While other chapters will examine each major tax type in Wisconsin, this chapter provides a brief overview of the tax system and budget structure as a whole. It also examines the state's performance on our *State Business Tax Climate Index*, a measure of tax structure, both overall and on the *Index*'s constituent components (corporate, individual, sales, property, and unemployment insurance taxes).

The issue of tax competitiveness has to do with how tax revenue is generated; it is for lawmakers to determine how much is collected. In Wisconsin, individual income taxes and sales taxes generate approximately 72 percent of state tax collections. Many elements of the state's tax system, however, stand in the way of competitiveness. For example, the structure of the state's individual income tax ranks poorly compared to other states, and the state corporate income tax is levied at a relatively high rate.

Following the overview of Wisconsin's tax and budget structure, this reform book will explore the current tax code in the Badger State, highlighting uncompetitive policies and offering recommendations for improvement.

Recent Tax and Spending Policies

Wisconsin's inflation-adjusted expenditures increased from \$19.33 billion in 1995 to \$28.42 billion in 2017 (Figure 2a).²⁷ This was a 47 percent surge in inflation-adjusted expenditures, compared to 17 percent population growth and 39 percent inflation-adjusted revenue growth over the same period.²⁸ That said, much of the increase in spending occurred between 1995 and 2008; since that time, spending has slowed.

Wisconsin's largest expenditure is human relations and resources, chiefly comprised of Medicaid, Temporary Assistance for Needy Families (TANF), and state correctional costs. Spending in this category grew substantially following the Great Recession due to the federal American Recovery and Reinvestment Act (stimulus).²⁹ Education spending is the next largest category in Wisconsin, reaching a peak value of 31 percent of total state spending in 1998 but settling closer to 25 percent in recent years. The Badger State also remains one of the only states with a nearly fully-funded pension system for public sector employees.³⁰ See Figure 2b for a complete illustration of Wisconsin's expenditures from 1991 to 2017.

State of Wisconsin, Department of Administration, Comprehensive Annual Financial Reports: 2017, 2008, 2000.

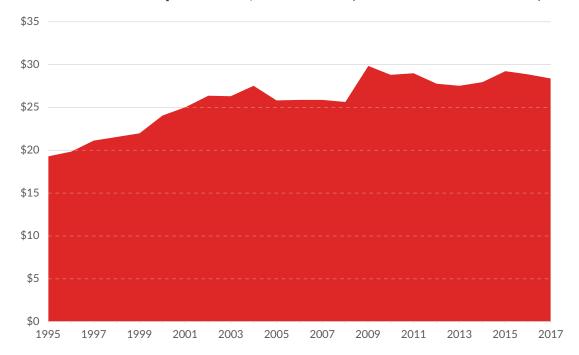
²⁸ U.S. Census Bureau. State Intercensal Datasets: Bureau of Labor Statistics. Consumer Price Indexes (All Urban Consumers).

²⁹ State of Wisconsin, Department of Administration, Comprehensive Annual Financial Reports: 2017, 2008, 2000.

³⁰ State of Wisconsin, Department of Employee Trust Funds, "WRS Active Lives Valuation & Gain/Loss Analysis," June 1, 2018.

Between 1995 and 2017, total state tax collections grew by 24.9 percent after adjusting for inflation.³¹ Similar to the growth in Wisconsin's expenditures, most of the state's tax collections growth occurred during the 1990s, increasing by 23.3 percent from 1995 to 2000 on an inflation-adjusted basis. From 2000 to 2017, inflation-adjusted state tax collections grew by just 1.3 percent. See Figure 2c for an illustration of Wisconsin's tax collections over the past two decades.

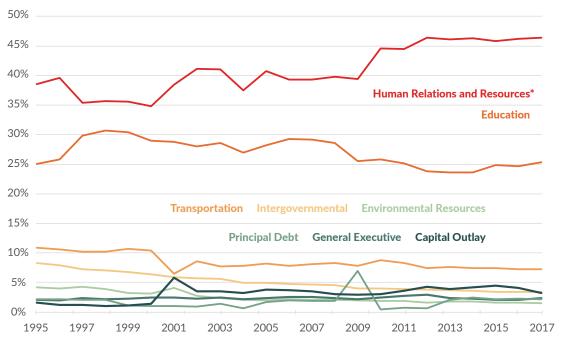
FIGURE 2a. Wisconsin Total Expenditures, 1995-2017 (Billions of 2017 Dollars)



 $Source: State\ of\ Wisconsin,\ Department\ of\ Administration;\ Comprehensive\ Annual\ Financial\ Reports:\ 2017,\ 2008,\ 2000.$

FIGURE 2b.

Wisconsin Expenditures by Source as a Percent of Total, 1995-2017

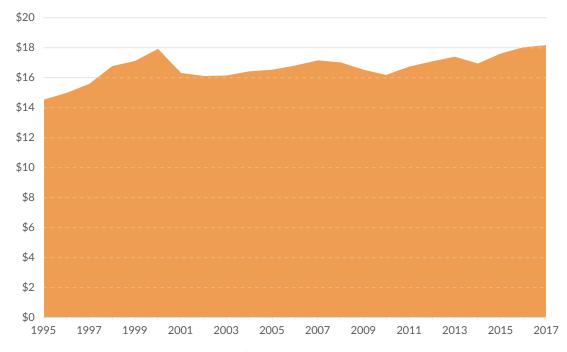


Note: The Human Relations and Resources category is composed mainly of Medicaid, Temporary Assistance for Needy Families (TANF), and state correctional costs.

Source: State of Wisconsin, Comprehensive Annual Financial Reports: 2017, 2008, 2000.

FIGURE 2c.

Wisconsin Total Tax Collections, 1995-2017 (Billions of 2017 Dollars)



Source: U.S. Census Bureau, 2016 Annual Survey of State Tax Collections.

Wisconsin's Budget Makeup

The individual income tax and sales tax are Wisconsin's largest sources of tax revenue, comprising 43 percent and 29 percent of total state tax collections, respectively. Selective sales taxes, chiefly made up of alcohol, tobacco, fuel, and utility taxes, also comprise a significant portion of the state's revenue. Property taxes, which are almost exclusively a local levy, are only a small component of state-level tax collections. Figure 2d shows the percentage of total state tax collections attributable to each of the major taxes between 1995 and 2017. Figure 2e highlights Wisconsin's state and local tax collections between 1995 and 2016, which shows a heavy reliance on property taxes for revenue at the local level.

While taxes are the largest source of revenue for the state, Wisconsin also relies on federal funding. Following the Great Recession, the state saw a significant uptick in federal funding from the American Reinvestment Recovery Act of 2009 (see Figure 2f).³³ As a result of the recession, both individual and corporate income tax revenue decreased between 2008 and 2010, which boosted the state's reliance on federal aid. Since 2010, however, federal funding as a percentage of Wisconsin's total revenue has steadily declined and is on a trajectory to reach prerecession levels.

Figure 2g compares year-over-year changes in revenue collections for three of Wisconsin's revenue streams—individual income, sales, and corporate income—since 1994.³⁴ The volatility of the corporate income tax is immediately apparent. While all taxes can be volatile, corporate income taxes are especially so.

FIGURE 2d.

Wisconsin State Tax Collections as a Percent of Total, 1995-2017



^{*} Note: The Selective Sales Taxes category includes alcohol, tobacco, fuel, and utility taxes. Source: U.S. Census Bureau, Annual Surveys of State Tax Collections.

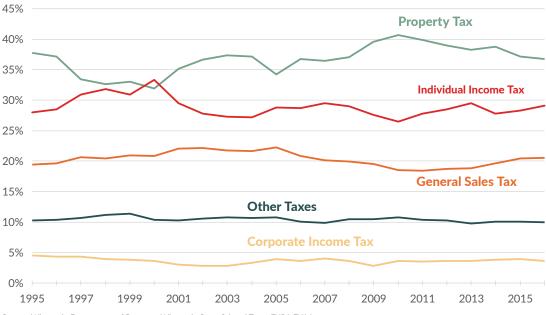
³² U.S. Census Bureau, "2016 State & Local Government Finance Historical Datasets and Tables," https://www.census.gov/data/datasets/2016/econ/local/public-use-datasets.html.

State of Wisconsin, Comprehensive Annual Financial Reports: 2017, 2008, 2000.

³⁴ U.S. Census Bureau, Annual Surveys of State Tax Collections.

FIGURE 2e.

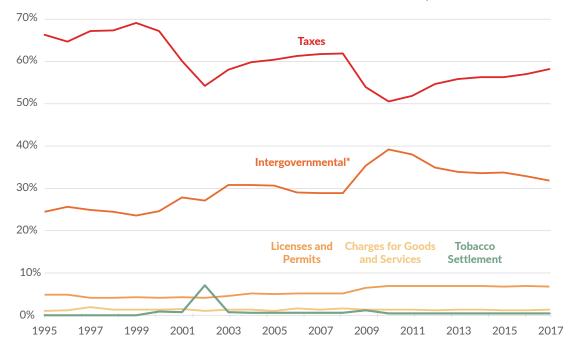
Sources of Wisconsin State & Local Tax Collections as Percent of Total, 1995-2016



Source: Wisconsin Department of Revenue, Wisconsin State & Local Taxes FY86-FY16.

FIGURE 2f.

Sources of Wisconsin Revenue as Percent of Total, 1995-2017



Note: Per the U.S. Census Bureau, Intergovernmental expenditures include federal grants and aid, reimbursements for state activities, and revenue received but transmitted through the state to local governments. For more, see U.S Census Bureau, "Government Finance and Employment Classification Manual".

Source: State of Wisconsin, Comprehensive Annual Financial Reports: 2017, 2008, 2000.

FIGURE 2g. Wisconsin Tax Collection Volatility, 1994-2017



Dollar amounts were adjusted for inflation and expressed in 2017 dollars prior to calculating percentage changes using the Consumer Price Index for All Urban Consumers (CPI-U) from the Bureau of Labor Statistics.

Source: U.S. Census Bureau, State & Local Government Finance.

Measures of State Tax Competitiveness

Tax reform can deliver several positive outcomes; for example, it can improve the budgeting process, making budgeting easier and more consistent, and it can reduce compliance costs for individuals and businesses. Most importantly, though, tax reform can improve a state's competitiveness.

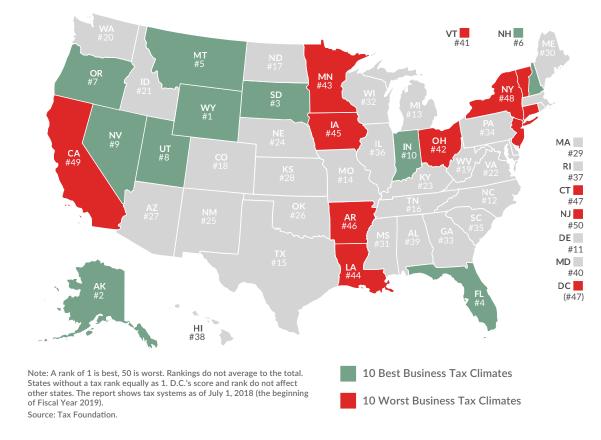
While how much is paid in taxes each year is an important consideration for competitiveness, it is also important to consider *how* those taxes are paid. Taxes vary significantly, with certain levies being more harmful to growth or creating significant compliance costs.

Each year, the Tax Foundation produces the *State Business Tax Climate Index* to enable business leaders, state policymakers, and taxpayers to gauge how these structural elements compare. The *Index* examines more than 100 variables in individual income tax, corporate income tax, sales tax, unemployment insurance tax, and property tax categories to produce a ranking from these many complex considerations.

In the most recent 2019 edition (Figure 2h), which gauges states as of July 1, 2018, those with the most competitive tax systems are Wyoming, Alaska, South Dakota, Florida, Montana, New Hampshire, Oregon, Utah, Nevada, and Indiana. The states with the least competitive tax systems are New Jersey, California, New York, Connecticut, Arkansas, Iowa, Louisiana, Minnesota, Ohio, and Vermont.

FIGURE 2h.

2019 State Business Tax Climate Index



Wisconsin's overall tax structure ranks 32nd among states, leaving much to be desired. The worst performing major tax in the state's system is the individual income tax, which ranks 39th in the country, chiefly due to its high top marginal rate of 7.65 percent. Wisconsin's unemployment insurance tax also ranks poorly (41st), due to its high rates and overly complex structure.

TABLE 2A.

Wisconsin Component Rankings in the 2019 State Business Tax Climate Index

Component	Rank
Overall Rank	32
Corporate Taxes	35
Individual Taxes	39
Sales Taxes	8
Property Taxes	21
Unemployment Insurance Taxes	41

Another component that contributes to Wisconsin's poor *Index* rankings is the top statutory corporate income tax rate of 7.9 percent. Though lower than neighboring Illinois's rate, Wisconsin's corporate rate remains among the highest nationally. Wisconsin's overall corporate income tax structure ranks 35th on the *Index*.

Fundamental tax reform provides an opportunity to improve these shortcomings so Wisconsin can collect the revenue necessary for government services while maintaining a competitive position that allows the state to attract new businesses and individuals.

Throughout this book, we use the *State Tax Business Climate Index* to show how Wisconsin currently compares to its neighbors in terms of competitiveness in each of the major tax types: individual, corporate, sales, property, and unemployment insurance taxes. We also use the *Index* to show how different reform options would improve Wisconsin's *Index* rankings from where they stand under the existing tax code.