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June 11, 2019

Senator Darling, Co-Chair
Representative Nygren, Co-Chair
2019 Joint Committee on Finance
Wisconsin State Legislature

Re: Concerns with A.B. 56 & S.B. 59 – Wisconsin’s 2019 Budget Bills

Dear Co-Chair Sen. Darling, Co-Chair Nygren, and Members of the 2019 Joint Committee on Finance:

On behalf of the Council On State Taxation (COST), I am submitting this written testimony to oppose the application of Internal Revenue Code (IRC) Sec. 163(j) to Wisconsin’s income tax. Additionally, COST recommends changes to A.B. 56 & S.B. 59 marketplace provider provisions. Further, COST recommends the allowance of a Wisconsin dividend received deduction when a foreign subsidiary elects to be taxed as a corporation (federal “check the box” rule).

About COST

COST is a nonprofit trade association based in Washington, DC. COST was formed in 1969 as an advisory committee to the Council of State Chambers of Commerce and today has an independent membership of approximately 550 major corporations engaged in interstate and international business. COST’s objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities. COST has a significant number of members that own property, have employees, and otherwise have significant operations in Wisconsin.

Opposition to Imposing Interest Expense Limitation under IRC Sec. 163(j)

In March 2018, COST, through its affiliated State Tax Research Institute (STRI), issued a study entitled *The Impact of Federal Tax Reform on State Corporate Income Taxes*.¹ The study, conducted by Ernst & Young LLP, determined that state tax conformity with federal tax reform would result in an average state corporate income tax base increase of 12 percent over the 10-year period between 2018 through 2027. The study concludes that Wisconsin would experience an approximately 9 percent increase in its corporate income tax base if it conformed to the TCJA. This increase is averaged over the next 10 years, and the estimated corporate tax base increase for each year varies depending on the timing of the various federal changes.

The federal provision with the largest impact on the Wisconsin corporate income tax is the 30% limitation on net interest expense deductions under the revised IRC Sec. 163(j). This limitation on business interest expenses would expand the Wisconsin corporate income tax base by an average

¹ See *The Impact of Federal Tax Reform on State Corporate Income Taxes*, by Ernst & Young LLP for the State Tax Research Institute, March 2018, available at: <http://cost.org/globalassets/cost/state-taxresources-pdf-pages/cost-studies-articles-reports/the-impact-of-federal-tax-reform-on-state-corporate-income-taxes.pdf>.

of approximately 7.25% over the next ten years. This corporate base broadener at the federal level funded, in part, the substantial reduction in federal corporate tax rates to make the U.S. more competitive internationally. These rate reductions, of course, do not flow through to the states, and therefore Wisconsin conformity would result in a substantial corporate income tax increase. At the federal level, the net interest expense deduction was linked with IRC Sec. 168(k), which allows immediate expensing, and the primary reason for the interest expense limitation under IRC Sec. 163(j) was to discourage excessive debt financing of assets subject immediate expensing under IRC Sec. 168(k). Last year, this Legislature decoupled from IRC 168(k) to not allow immediate expensing for Wisconsin income tax purposes,² so no sound policy reason exists for Wisconsin to remain coupled with IRC 163(j). Doing so would simply result in a baseless tax increase on businesses.

The state-specific outcomes are arbitrary and inconsistent with the goals of federal tax reform. For example, the IRC Sec. 163(j) provisions limit interest expense across the board, for both intercompany and third-party borrowing, and thus impact all borrowing by Wisconsin taxpayers for both business operations and investment/expansion. This result would harm Wisconsin’s competitiveness, especially in light of decisions by states in 2018 to decouple from these provisions (see, *e.g.*, Connecticut, Georgia, Indiana, South Carolina, and Tennessee). Wisconsin recognized the benefits of decoupling just last year by wisely determining not to incorporate the TCJA’s changes to IRC Sec. 163(j) when it passed Act 231.

Lastly, applying the interest expense limitation in Wisconsin would also significantly increase the complexity of corporate tax compliance, as much remains to be determined, both at the federal level and by the Wisconsin Department of Revenue, on how to implement this provision. It is uncertain how the interest expense limitation will be computed and reflected in federal consolidated return filings, and commensurately how to determine if, and in what amount, the limitation applies at the state filing level.

Recommended Changes to Marketplace Provider Proposal

Attached to this testimony are comments COST submitted last week regarding recommendations to improve the proposed marketplace provider provisions in A.B. 251. These comments also apply to A.B. 56 and S.B. 59. Importantly, the definition of “marketplace provider” should be modified to prevent a person that merely advertises products, without actually facilitating a sale, from being included. Also, some transactions are subject to other fees and taxes associated with the sale (such as 911 charges for certain telecommunication services) which certain marketplace sellers have sophisticated systems to accurately collect along with the State’s sales or use tax. Thus, an exception (*e.g.*, waiver provision) should exist to enable those marketplace sellers to continue collecting and remitting the tax. Lastly, some other administrative issues should be addressed, such as ensuring marketplace providers have the same rights and duties as other sellers.

Clarity Needed Wisconsin’s Dividend Received Deduction Law

Wisconsin follows the federal “check the box” rules under U.S. Treasury Regulation Sec. 301-7701. That regulation allows a business entity, such as a partnership, regardless of its legal structure to be taxed as if it was a corporation for federal income tax purposes. However, recently, the Wisconsin Department of Revenue has not been following a provision (adopted in Wis. Stat. s. 71.26(3)(j)) for a business claiming a dividend received deduction from a foreign subsidiary which makes a valid “check the box” election. Wisconsin Manufacturing & Commerce (WMC) submitted legislative language to this Committee on May 20 this year to address this issue.³ COST supports WMC’s efforts to provide clarifying language in this area and encourages this Committee to address this issue to curtail future litigation on this issue.

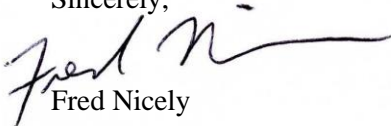
² See Act 231 (A.B. 259).

³ WMC’s letter is available at: https://www.wmc.org/wp-content/uploads/DRD_5-20.pdf.

Summary

COST appreciates the opportunity to provide this Committee with comments regarding the State's budget bills, A.B. 56 and S.B. 59. Please contact me if you have any additional questions. COST is willing to work with all interested parties to address the issues raised in this letter.

Sincerely,



Fred Nicely

cc: COST Board of Directors
Douglas L. Lindholm, COST President & Executive Director

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June 6, 2019

Representative Macco, Chair
Representative Wittke, Vice-Chair
Assembly Committee on Ways and Means
Wisconsin State Legislature

Re: Recommended Changes to Marketplace Provider Provisions in A.B. 251

Dear Chair Macco, Vice-Chair Wittke, and Members of the Committee on Ways and Means:

On behalf of the Council On State Taxation (COST), I am submitting this testimony to recommend changes to the marketplace facilitator provisions in A.B. 251. While we are continuing to work with our members to ensure marketplace laws operate as intended to enhance the states' collection of sales and use taxes via remote sales and marketplace provider laws, COST recommends the following changes to prevent unintended problems with the enforcement of marketplace provisions contained in A.B. 251. Addressed in more detail below, COST recommends improvements to the definition of a marketplace provider and the inclusion of broader exceptions allowing certain marketplace sellers to continue collecting and remitting the tax to the Wisconsin Department of Revenue. COST further recommends that services subject to additional taxes and fees or have simultaneous use at multiple locations should be excluded from the marketplace provider provisions.

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Definition of Marketplace Facilitator and Need for Exceptions

COST suggest some clarification to the proposed definition of a marketplace provider to ensure a person that is merely advertising products or assisting in the payment process, without actually facilitating a sale to a purchaser, is excluded from the definition. The provision also fails to address certain marketplace sellers that have already developed and implemented sophisticated sales and use tax collection systems that more accurately collect Wisconsin state and local sales and use taxes (along with other taxes and fees on the same transaction such as certain telecommunication fees such as 911 charges) than a marketplace provider could. To address this issue, COST recommends incorporating the following language into Wisconsin law to address definitions of "marketplace provider" and "marketplace seller" and to clearly allow certain transactions to be excluded:

- A. "Marketplace provider" means a person who facilitates a retail sale by a marketplace seller by:
1. Listing or advertising for sale by the marketplace seller in any forum, tangible personal property [limited to enumerated services and/or digital goods] that are subject to tax under this [chapter]; and
 2. Collecting payment from the customer and transmitting that payment to the marketplace seller, either directly or indirectly, through agreements or arrangements with third parties, regardless of whether the marketplace provider receives compensation or other consideration in exchange for its services.
- B. "Marketplace seller" means a seller that makes retail sales through any physical or electronic marketplace operated by a marketplace provider.
- C. Marketplace provider transactions do not include:
1. Transactions where a marketplace provider provides advertising services, including listing products for sale, so long as the internet advertising service platform or forum did not engage directly or indirectly through one or more affiliated persons in the activities described in Subsection A.2. In addition, Subsection A.2 does not apply to transactions where a person is appointed by a marketplace provider or marketplace seller to handle various forms of payments, such as processing credit cards and debit cards, and the person's principal activity with respect to the transactions is facilitating the payment between the purchaser and the marketplace provider or seller.
 2. Transactions for rooms, lodgings, or accommodations described in [cite code section] and transactions for motor vehicle rentals described in [cite code section] if the provider of such rooms, lodgings, accommodations, or motor vehicle rentals is a [registered seller] under [cite code section(s)].
 3. All transactions of a marketplace seller where a waiver is approved provided the following requirements are met:
 - a. The marketplace provider submits a waiver application to the tax commissioner;
 - b. Both the marketplace provider and the marketplace seller subject to the waiver agree that the marketplace seller will collect and remit all applicable taxes and fees and the marketplace provider collects the applicable tax registration numbers from the marketplace seller;
 - c. The marketplace seller who agrees to collect and remit all applicable taxes and fees provides evidence to the marketplace provider that it is registered under [cite code section]; and
 - d. The department approves the waiver application. The department has the authority to promulgate regulations for applying, processing a waiver for approval, and the denial of a waiver.

4. All the transactions of a marketplace seller shall be subject to a waiver without the pre-approval of the department where the conditions in Subsections C.3.a through C.3.c are met and the marketplace seller is able to certify the following:
 - a. It has annual U.S. gross sales over \$1 billion, including the gross sales of any related entities; and,
 - b. The seller or a related entity is publicly traded on at least one major stock exchange.

This waiver shall be valid at the time the marketplace provider submits the waiver application to the department that includes the information required to be certified in this Subsection.

For all transactions excluded under Subsection C, the tax levied under [cite code section], including [list other applicable taxes/fees directly imposed on consumer from a transaction, *e.g.*, environmental fee for paint, tire fee, 911 charges, etc.], shall be the responsibility of the marketplace seller and the seller must collect and remit such taxes. The marketplace provider is not responsible for collecting and remitting the taxes on such transactions and shall be relieved of liability for any taxes or associated penalties and interest that qualify for exclusion under this section.

D. Nothing in this section shall allow the department to collect the tax owed more than once.

The above language would clarify which transactions a marketplace provider and seller must collect tax on. Importantly, it also allows marketplace sellers with sophisticated sales and use tax collection and remittance systems already in place to continue collecting those taxes and other associated taxes and fees that apply to their transactions. This will also help marketplace providers with insufficient systems to allow marketplace sellers to continue to collect and remit their own additional taxes and fees.

Recommended Improvements to Other Marketplace Provider Provisions

The class action provision contained in s. 77.523(7) should also be clarified to include marketplace sellers. As presently written, it is inequitably limited to marketplace providers. Audit liability relief for marketplace sellers should also extend to the additional taxes and fees. And, to clarify that marketplace providers have the same standing as other sellers in Wisconsin, COST recommends revising the language in A.B. 251 to specifically address providers' rights to claim credits, deductions, and other adjustments to the sales price in the same manner as other sellers, including vendor compensation and the administration of exemptions and refunds.¹

COST also recommends removing the last sentence in s. 77.523(2), which would hold marketplace providers and sellers jointly liable if a marketplace provider fails to notify a marketplace seller it will be collecting and remitting the tax. While there is no problem with requiring notification, it is inequitable to

¹ Fortunately, bad debt is addressed in A.B. 251 under s. 77.585(1g). COST recommends using the following language to more broadly apply all rights and duties a seller has in Wisconsin to marketplace providers: "A marketplace provider shall be entitled to any credits, deductions, or adjustments to sales price provided to a marketplace seller, in addition to any such adjustments provided directly by the marketplace provider. This section pertains to, but is not limited to, adjustments such as bad debt deductions, discounts, coupons, rebates, etc. In addition, a marketplace provider shall be entitled to any [seller/vendor] compensation available to other sellers. A marketplace provider has the same rights and duties as a marketplace seller, including the handling of refunds, and maintenance and acceptance of certificates from purchasers claiming a transaction is not taxable."

"

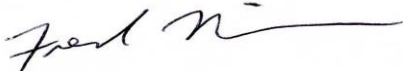
impose joint liability on marketplace sellers that otherwise know the marketplace provider is required to collect and remit that tax. Finally, COST recommends s. 77.523(4) be clarified to address errors from insufficient or incorrect information² and that the liability relief in s. 77.523(4) should be independent of s. 77.523(3) and not phased out under s. 77.523(5). A marketplace provider that makes reasonable attempts to ascertain information from a marketplace seller should always be allowed liability relief, with the marketplace seller and purchaser remaining liable for the tax on such a sale.

Summary

COST appreciates the opportunity to provide this Committee with comments and suggested changes to improve A.B. 251's proposed marketplace provider provisions. The recommended changes to the definition of marketplace provider and related provisions requiring providers to collect and remit Wisconsin's state and local sales and use taxes will facilitate compliance and mitigate potential legal issues with the proposed law.

Please contact me if you have any additional questions. COST is willing to work with all interested parties to address A.B. 251's marketplace provider provisions.

Sincerely,



Fred Nicely

cc: COST Board of Directors
Douglas L. Lindholm, COST President & Executive Director

² The following language is recommended: A marketplace provider shall be relieved of liability under this [section] for failure to collect and remit sales or use tax on sales facilitated for marketplace sellers, excluding related entities as defined in [cite code section], when the marketplace provider demonstrates to the satisfaction of the department that the provider relied on insufficient or incorrect information from the marketplace seller that was necessary to determine taxability or proper sourcing of a transaction. A marketplace seller is not relieved of liability under this subsection for transactions for which it provides insufficient or incorrect information provided the marketplace provider demonstrates a reasonable attempt to obtain the information from the marketplace seller.