Is the Tax Code Driving Taxpayers from Wisconsin?

An Analysis of Wisconsin Taxes

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EXECUTIVE SUMMARY

The news for Wisconsin taxpayers has been quite positive lately. Governor Scott Walker and lawmakers have cut taxes three times in the past year, and since 2011, taxes have been cut by nearly $2 billion. In addition, the tax code has been simplified, eliminating 17 special interest tax credits and reducing the amount of income tax brackets from five to four.

While these recent events are great news for the hard-working taxpayers of the Badger State, this new report from the John K. MacIver Institute for Public Policy and the National Center for Policy Analysis (NCPA) shows there is more work to be done.

On average, Wisconsin loses $136 million a year in adjusted gross income (AGI) from residents moving to other states. That is equal to nearly $2.5 billion over the past two decades. Money leaving the state means less investment in local businesses, less revenue for state and local governments and less being spent on Wisconsin goods and services.

Wisconsin loses $136 million a year in adjusted gross income from residents moving to other states.

The state's burdensome tax climate may be to blame for money leaving the state at such an alarming rate. Our analysis compares state tax burdens across the country to see if it is advantageous to move from Wisconsin to a different state.

For example, Wisconsinites are moving to Florida for more than just the warm weather. Florida's taxpayers do not pay a state income tax, and the average property tax rate is almost half of Wisconsin's. That means over the period of a lifetime, taxpayers could stand to gain hundreds of thousands of dollars in AGI just by heading to the Sunshine State.

According to the NCPA's State Tax Calculator, the analysis tool used in this study, a 40-year-old married couple who owns a home and earns $75,000 a year would gain $223,735 over the rest of their lifetime if they moved to Florida from Wisconsin.

Southern states are not the only ones to hold a tax advantage over Wisconsin. That same couple would be better off in Iowa, Michigan and Minnesota. The only neighboring state that has a worse tax climate for this couple is Illinois.

While Wisconsinites can celebrate that the tax climate is better than our neighbors to the south, the Land of Lincoln's flat income tax of five percent is lower than most of Wisconsin's rates. However, Illinois' average sales tax rate is a staggering 8.16 percent compared to Wisconsin's 5.43 percent and property tax rates are similar between the two.

The State Tax Calculator shows us that a single 25-year-old earning $30,000 is better off in Wisconsin than Iowa, Illinois and Minnesota. But, as this taxpayer earns more and purchases a home, it is actually advantageous to move to Iowa or Minnesota.

Essentially, the state is penalizing taxpayers for being more successful.

With Wisconsin discouraging home ownership and higher income, it is no wonder that $136 million leaves the state every year. If Wisconsin wants to be a national competitor for new businesses, investment and job creation, it must keep reforming its tax code and reduce the overall tax burden.

Is the Tax Code Driving Taxpayers from Wisconsin?

People move from state to state for a variety of reasons, whether it is for business relocation, weather, retirement or family matters. According to IRS and Census data, Wisconsin has lost about $136 million annually in adjusted gross income (AGI) over the past 20 years because of residents moving to other states.[1] While the majority of Wisconsin's relocating citizens have moved to Florida, four other states — Arizona, Texas, Colorado and North Carolina — have also welcomed former residents of the Badger state. Could taxes be a factor in these relocations?

For residents concerned about the state's tax burden, is it enough to entice them to stay? The NCPA's State Tax Calculator (whynotmove.org) can be used to compare the tax burdens in Wisconsin to those of the five aforementioned states, as well as Wisconsin's neighboring states (Minnesota, Illinois, Iowa and Michigan).

About the NCPA's State Tax Calculator

The NCPA's State Tax Calculator is a first-of-its-kind tool to help people determine their tax burden by moving from one state to another. The State Tax Calculator is not a typical cost-of-living calculator. The software is based on a proprietary financial planning model developed by NCPA senior fellow Laurence Kotlikoff.

The State Tax Calculator produces results based on the economic theory that households manage their finances so as to smooth out their discretionary spending over their lifetime. To make the calculator easy to use, there are also built-in assumptions about wages and investments.

- Wage/business income is the same in both states.
- Earnings during your working years will increase each year at the assumed rate of inflation of 3 percent.
- Any money invested in retirement accounts or regular savings accounts will grow at 4 percent per year.

Additionally, annual and lifetime results are based on the assumption that the individual or couple live to be 100-years-old, and that assets are spent down leaving nothing to pass on to heirs.

Wisconsin Income Taxes

2011 Personal Income Tax Brackets: Single/Head of Household		2014 Personal Income Tax Brackets: Single/Head of Household	
Income Amount	Tax Rate	Income Amount	Tax Rate
Up to $10,570	4.60 Percent	Up to $10,910	4.00 Percent
$10,571 to $21,130	6.15 Percent	$10,911 to $21,820	5.84 Percent
$21,131 to $158,500	6.50 Percent		
$158,501 to $232,600	6.75 Percent	$21,821 to $240,190	6.27 Percent
$232,601 and above	7.75 Percent	$240,191 and above	7.65 Percent

Results for the Top Five Destination States

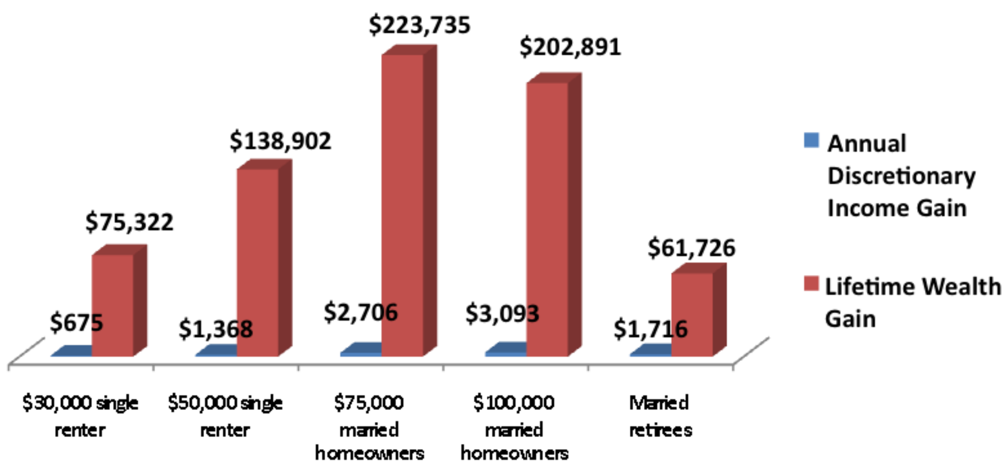
Florida, Arizona, Texas, Colorado and North Carolina

The majority of adjusted gross income lost annually by Wisconsin (about $2.3 billion) over the past 20 years has gone to Florida. It is easy to see why, particularly for those in their working years who move from Wisconsin to the Sunshine state [See Figure I]:

- A 25-year-old single renter earning $30,000 a year would have an additional $675 a year in discretionary income, and a gain in lifetime wealth of $75,322.
- A 30-year-old single renter earning $50,000 a year would have an additional $1,308 in discretionary income, and a gain in lifetime wealth of $132,778.
- A 40-year-old married, home-owning couple earning $75,000 a year would have an additional $2,706 in discretionary income, and a gain in lifetime wealth of $223,735.
- A 50-year-old married, home-owning couple earning $100,000 a year would have an additional $3,093 in discretionary income, and a gain in lifetime wealth of $202,891.

The primary reason for the gains in Florida is its absence of a state income tax. Also, Florida's median property tax rate is 0.97 percent, almost half of Wisconsin's rate (1.76 percent). Only Florida's state and local average sales tax rate is higher. In fact, of all nine states compared, Florida provides the largest income gain for Wisconsinites — with the exception of retirees. A 70-year-old married couple would gain an additional $1,716 in annual discretionary income, and $61,726 in lifetime wealth, but Arizona comes out slightly ahead.

Figure I. Discretionary Income Gain Moving from Wisconsin to Florida



Source: Author's calculations using the NCPA State Tax Calculator.

Do any of the top five destination states make Wisconsinites worse off? In most cases, no. But there are a few exceptions [See Table I]:

- A 25-year-old renter earning $30,000 a year would be worse off in North Carolina, losing $248 in annual discretionary income and a $27,644 in lifetime wealth.
- A 30-year-old renter earning $50,000 a year would fare worse in North Carolina, losing about $286 in annual discretionary income and $29,079 in lifetime wealth.
- A 70-year-old married retired couple moving to Texas would lose $790 a year in annual discretionary income and $28,402 in lifetime wealth.

North Carolina's income tax rates begin at very low income thresholds, which could explain the loss for the 25-year-old and 30-year-old renters. For the 70-year-old retirees, the burden of property and sales taxes in Texas (a state with no income tax) outweigh the income tax burden in Wisconsin.

Wisconsin's Income Tax

There have been a number of changes to Wisconsin's tax code recently. For personal income taxes, Wisconsinites faced five income brackets in 2011. Taxpayers paid rates ranging from 4.6 percent for income earned up to $10,570 to 7.75 percent for earnings over $232,600. The brackets have now been simplified to four with the bottom rate starting at 4 percent for income up to $10,910 and the top rate at 7.65 percent for income over $240,190.[2] Rate reductions have been applied to all categories of taxpayers, including married couples filing jointly or separately, with only slight variations in withholding tables between groups. Income tax rate reductions enacted since 2011 are expected to save taxpayers over $416 million in the 2014-15 fiscal year.[3]

Of the four states that border Wisconsin, two have flat income taxes, Illinois and Michigan, and two have progressive income tax systems, Iowa and Minnesota. The highest income rate is found in Minnesota, where state lawmakers recently approved a new tax bracket with a rate of 9.85 percent for individuals making over $152,540 and married couples making over $254,241. In Illinois and Michigan, all taxpayers, regardless of income, pay a flat rate of 5 percent and 4.25 percent respectively.

Table I. Lifetime Gain (Loss) to Taxpayers Moving from Wisconsin to Top Five States[14]

State	25-year-old single renter: $30K annual income	30-year-old single renter; $50K annual income	40-year-old married homeowners; $75K annual income	50-year-old married homeowners; $100K annual income	70-year-old married homeowners; retired
Florida	$75,322	$132,778	$223,735	$202,891	$61,726
Arizona	$19,608	$41,122	$166,029	$163,532	$65,679
Colorado	$4,143	$20,991	$170,252	$174,782	$85,221
Texas	$67,001	$117,187	$62,050	$43,204	($28,402)
North Carolina	($27,644)	($29,079)	$98,075	$105.686	$52,077

Table II. Lifetime Gain (Loss) to Taxpayers Moving from Wisconsin to Neighboring States[15]

State	25-year-old single renter: $30K annual income	30-year-old single renter; $50K annual income	40-year-old married homeowners; $75K annual income	50-year-old married homeowners; $100K annual income	70-year-old married homeowners; retired
Minnesota	($12,657)	($31,114)	$50,497	$38,914	$2,672
Illinois	($34,759)	($24,040)	($55,612)	($36,586)	($21,216)
Iowa	($33,850)	($50,221)	$8,720	$19,587	$35
Michigan	$714	$29,874	$18,095	$19,948	$11,417

Comparing Wisconsin to Neighboring States

In all fairness, states such as Florida and Arizona offer amenities besides lower taxes that make it difficult for Wisconsin to compete, such as warmer weather. Climate is a major factor, especially for retirees to consider when moving. So how does Wisconsin fare compared to its immediate Midwestern neighbors?

Consider our representative households again [See Table II]:

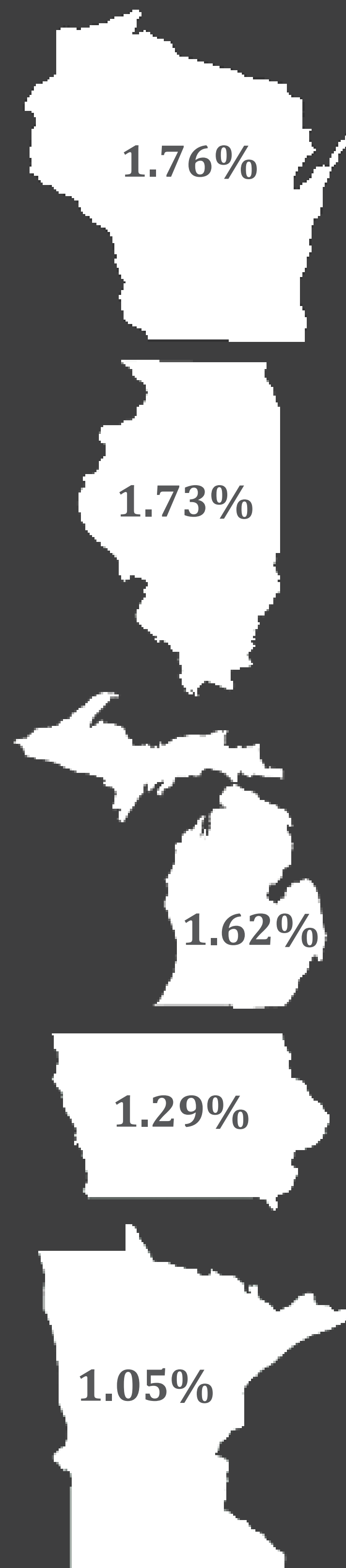
- A 25-year-old renter earning $30,000 a year would fare worse in Minnesota, Illinois and Iowa, losing annual discretionary income ranging from $113 to $311 a year, for a loss in lifetime wealth of $12,657 to $34,759.
- A 30-year-old renter earning $50,000 a year would also fare worse in Minnesota, Illinois and Iowa, losing annual discretionary income ranging from $237 to $495 a year, for a loss in lifetime wealth of $24,040 to $50,221.
- In Michigan, however, both renters would gain in annual discretionary income and lifetime wealth, compared to Wisconsin.
- Conversely, 40-year-old married homeowners earning $75,000 a year would do better in neighboring states — except for Illinois, where their annual discretionary income loss would equal $685, for a loss in lifetime wealth of $56,612.
- A 50-year-old married, home-owning couple earning $100,000 a year will also do better in neighboring states, with the exception of Illinois, where they would lose $558 in annual discretionary income and lifetime wealth of $36,586.
- As with their younger counterparts, the 70-year-old retirees would do better in neighboring states except for Illinois, where they would lose $590 in annual discretionary income and $21,216 in lifetime wealth.

Why are taxes in neighboring states advantageous for homeowner households?

Minnesota. Minnesota has higher marginal income tax rates than Wisconsin, ranging from 5.35 percent to 9.85 percent, but Minnesota's median property tax rate is lower. Thus, while a renter would fare worse in Minnesota thanks to the higher income tax, homeowners would fare better because of Minnesota's lower property tax rate.

Michigan. Michigan's state income tax rate is a flat 4.25 percent, benefiting singles earning more than $11,000 and couples earning more than $15,000 (in which case marginal tax rates increase in Wisconsin). However, Michigan's and Wisconsin's sales and property tax rates are comparable.

Midwest Property Tax Rates[4]



Iowa. Iowa has nine different marginal tax rates that begin after a $1,900 personal exemption for single filers and $4,670 for married filers. Their rates, ranging from 0.36 percent to 8.98 percent, hurt lower income individuals. But higher-income homeowners still fare better in Iowa becuase of its lower median property tax rate of 1.29 percent.

Illinois. Illinois is the only neighboring state that Wisconsin beats hands down in terms of tax advantage. While Illinois' flat 5 percent income tax seems like a bargain, the personal exemption for both single and married filers is only $2,100 and the state and local average sales tax is 8.16 percent, much higher than Wisconsin's 5.43 percent.

Wisconsin's Property and Sales Taxes

Wisconsin's property taxes have been historically high and are consistently ranked in the top ten in the nation.[5] Average property taxes for a median-valued home increased every year from 2003-2010 according to estimates from Wisconsin's non-partisan Legislative Fiscal Bureau.[6] The average rate of increase was 2.57 percent per year during that time period with a high of 4.6 percent in 2004.

Data used in this study shows Wisconsin has the fifth highest median property tax rate in the nation at 1.76 percent. Only New Jersey, New Hampshire, Texas, and Nebraska come in with higher rates.[7] Two Midwest states join Wisconsin in the top ten. Illinois, at a rate of 1.73 percent, ranks sixth and Michigan, at a rate of 1.62 percent, ranks eighth. Iowa ranks fourteenth at 1.29 percent, and Minnesota is nineteenth at 1.05 percent.

Wisconsin has taken steps in the last few years to lessen the property tax burden. In fact, property taxes have come down each year since 2011 with an average rate decrease of 1.18 percent, including an estimated 3.42 percent decrease for 2014. Wisconsin's property taxes were actually higher in 2010 than in 2014, according to the Fiscal Bureau. Recent decreases have been driven by property tax relief measures enacted in the 2013-2014 legislative session totaling $535.7 million.[8] Of that total, $100 million came in the form of local aid to K-12 school districts, and $406 million was thanks to changes in the way Wisconsin's technical colleges are funded. The remaining $29.7 million came from an increase in the state's lottery tax credit. Property tax relief enacted since 2011 is expected to save the average Wisconsin homeowner around $133 a year.[9]

Taken together, the Legislative Fiscal Bureau estimates that tax policy changes since 2011 will save taxpayers $2 billion by the end of 2015. Those changes will save the average married taxpayer and homeowner $813 over the same period.[10]

The state sales tax in Wisconsin remains unchanged at 5 percent, where it has been since 1982. There are numerous exemptions to the sales tax, such as different kinds of equipment and machinery that benefit businesses or farms, as well as food and energy for households.[11] Most counties have a higher sales tax rate, however, because of the option for counties to implement their own sales tax of 0.5 percent. Six counties also have a small sales tax for stadium districts to help fund professional sports facilities. Local option sales tax policies bring the average sales tax rate in Wisconsin to 5.43 percent[12], but 63 out of 72 counties pay 5.5 percent or higher.[13]

Wisconsin's average state and local sales tax rate is lower than rates in each of its four border states [See Table III]. Illinois has the highest in the region at 8.16 percent, then Minnesota at 7.19 percent, Iowa at 6.78 percent, and Michigan at 6 percent.

Conclusion

Wisconsin has made some strides in reducing and simplifying its tax burden. Although lower- and middle-income residents, particularly non-homeowners do quite well in Wisconsin compared to its neighbors, higher-income earners and wealthy earners have a tax advantage by moving to another state. This should be of concern to the state's policymakers who have the potential to lose the residents who pay the most taxes. Wisconsin has the potential to lose billions of dollars a year to other states as people move to reduce their tax burden.

Supporting Information and Citations

Table III. Midwest Sales Tax Rates[16]

	Illinois	Minnesota	Iowa	Michigan	Wisconsin
Sales Tax Rate	***8.16%***	***7.19%***	***6.78%***	***6.00%***	***5.43%***

[1] "IRS Tax Migration," How Money Walks; www.howmoneywalks.com

[2] Rates and withholding amounts apply to singles and head of household; "Tax Rates," Wisconsin Department of Revenue; http://www.revenue.wi.gov/faqs/pcs/taxrates.html

[3] "Tax Law Changes Since 2011," Wisconsin Legislative Fiscal Bureau; http://legis.wisconsin.gov/lfb/publications/Miscellaneous/Documents/2014_04_30_Tax%20Law%20Changes.pdf

[4] "Property Taxes by State," Tax-Rates.org; http://www.tax-rates.org/taxtables/property-tax-by-state

[5] "State and Local Government Tax and Revenue Rankings, Years 2004-2011," Wisconsin Department of Revenue; http://www.revenue.wi.gov/report/t.html

[6] "Levy Limit for Counties and Municipalities (Shared Revenue and Tax Relief -- Property Taxation), Wisconsin Legislative Fiscal Bureau, May 2005; http://legis.wisconsin.gov/lfb/publications/budget/2005-07-Budget/Documents/Budget%20Papers/685.pdf, May 2013; http://legis.wisconsin.gov/lfb/publications/budget/2013-15%20Budget/Documents/Budget%20Papers/605.pdf, Property Tax Bill Estimates Under January 2014 Special Session Proposal, January 2014; http://legis.wisconsin.gov/lfb/publications/Miscellaneous/Documents/2014_01_28%20Property%20Tax%20Estimates%20Jan%202014%20SS.pdf

[7] "Property Taxes by State," Tax-Rates.org; http://www.tax-rates.org/taxtables/property-tax-by-state

[8] "Tax Law Changes Since January 2011," Wisconsin Legislative Fiscal Bureau; http://legis.wisconsin.gov/lfb/publications/Miscellaneous/Documents/2014_04_30_Tax%20Law%20Changes.pdf

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[10] Calculation by the John K. MacIver Institute for Public Policy, "Distributional Impacts of Individual Income Tax Proposal," Wisconsin Legislative Fiscal Bureau; http://legis.wisconsin.gov/lfb/publications/budget/2013-15%20Budget/Documents/2013_06_05_WILeg%20Tax.pdf, "Scott Walker Announces $100 Million in Property Tax Cuts," Wisconsin State Journal; http://host.madison.com/news/local/govt-and-politics/scott-walker-announces-million-in-property-tax-cuts/article_87bf2bce-3f67-5b9d-b8a7-ccc577e7cc0c.html, "Distributional Information on Proposed Individual Income Tax Rate Reduction," Wisconsin Legislative Fiscal Bureau; http://legis.wisconsin.gov/lfb/publications/Miscellaneous/Documents/2014_01_28%20Distributional%20Information%20on%20Individual%20Income%20Tax%20Rate%20Reduction%20Jan%202014%20SS.pdf, "Property Tax Bill Estimates Under January 2014 Special Session Proposal," Wisconsin Legislative Fiscal Bureau; http://legis.wisconsin.gov/lfb/publications/Miscellaneous/Documents/2014_01_28%20Property%20Tax%20Estimates%20Jan%202014%20SS.pdf, "Revised Withholding Tables Now Available," Wisconsin Department of Revenue; http://www.revenue.wi.gov/news/2014/20140129_01.pdf

[11] "Sales and Use Tax (Informational Paper #6)," Wisconsin Legislative Fiscal Bureau; http://legis.wisconsin.gov/lfb/publications/Informational-Papers/Documents/2013/6_Sales%20and%20Use%20Tax.pdf

[12] "State and Local Sales Tax Rates in 2014," Tax Foundation; http://taxfoundation.org/article/state-and-local-sales-tax-rates-2014

[13] "Sales Tax Rate Chart," Wisconsin Department of Revenue; http://www.revenue.wi.gov/faqs/pcs/taxrates.html

[14] Calculation by Pamela Villarreal, NCPA State Tax Calculator; http://www.whynotmove.org/

[15] Calculation by Pamela Villarreal, NCPA State Tax Calculator; http://www.whynotmove.org/

[16] "State and Local Sales Tax Rates in 2014," Tax Foundation; http://taxfoundation.org/article/state-and-local-sales-tax-rates-2014