THE
NATIONAL LAW REVIEW

Wisconsin Enacts Discriminatory Exit Charge for Businesses Moving out of State

Article By
Mark Nebergall
Stephen P. Kranz
McDermott Will & Emery
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Friday, June 28, 2019

On June 24, 2019, Wisconsin Governor Tony Evers (D), signed into law AB 10, entitled "2019 Wisconsin Act 7." This Act either bars a deduction for, or requires that amounts deducted be added back to, Wisconsin taxable income "for moving expenses" deducted on federal income tax returns if the expenses are associated with a move of a business either out of the state or out of the country. This requirement would not apply to expenses incurred by a taxpayer in moving a business to a different location within the state of Wisconsin. The provisions apply regardless of the form of ownership of a business, either as a sole proprietorship, a corporation, or a pass through entity such as a partnership, limited liability corporation or subchapter S corporation.

Under federal tax law, a taxpayer generally may deduct the costs associated with moving its business operations from one location to another as ordinary and necessary business expenses. The Wisconsin income tax "piggybacks" on federal taxable income for purposes of determining the state income tax. Under the provision, a taxpayer would have to add back to its Wisconsin taxable income any expenses associated with a move that had been deducted on the federal return.

The fiscal note accompanying the bill notes no data exists that would permit an estimate of how much revenue the measure would raise, but anticipates the amount would not be large. The fiscal note provides an example of a business that spent $500,000 in moving either out of the state or out of the country. Assuming an apportionment factor of 14.7% (the average for all Wisconsin businesses in 2016), it would pay an additional $5,807 in income tax. If 100 similar businesses moved out of the state, the revenue increase to the state (or cost to business in increased income taxes) would be $580,700.

The low revenue score for the measure suggests the purpose is political rather than revenue raising. Indeed, Governor Evers, in his Twitter feed, stated "I signed AB 10 into law to make sure businesses don't get an unfair tax advantage for moving their business out of Wisconsin." Governor Evers was backed by the head of the Wisconsin chapter of the AFL-CIO, who praised him for calling out the "unjust practice of rewarding companies with tax breaks for moving jobs out of WI."

Discriminatory?

The Act blatantly discriminates against interstate and international commerce and is unconstitutional under the Commerce Clause of the US Constitution, which grants to Congress the power to regulate commerce with foreign nations, and among the several states. The Supreme Court has long held the Commerce Clause "prohibits state laws that unduly restrict interstate commerce" and "prevents States from adopting protectionist measures.[1] In addition, the Court has held that "a State "may not tax a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the State." *See Armco Inc. v. Hardesty*, 467 U. S. 638, 642 (1984).

In evaluating state taxes under the Commerce Clause, the Courts look to the four-part test enunciated in *Complete Auto Transit, Inc. v. Brady*, which asks whether a "tax is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State." 430 U.S. 274 (1977). Because the Act would impose a higher tax burden on a business moving from Wisconsin to another state or country than it would impose on a business moving from one location in the state to another, it discriminates against interstate commerce and would fail the "does not discriminate against interstate commerce" prong of the *Complete Auto* four-part test.

The Act also likely infringes on the constitutional right of free travel between the states (Art. IV, Sec. 2). The right of a citizen of one state to pass through, or to reside in any other state has long been recognized as a right protected by various provisions of the Constitution. One line of cases grounds the right in the Privileges and Immunities Clause.[2] Another line of cases rests on the Privileges and Immunities Clause of the Fourteenth Amendment.[3] Other cases find the right in the Commerce Clause.[4] To the extent the Act restricts travel outside the United States, it might infringe the Due Process Clause of the Fifth Amendment.[5] Whatever the source of the right to travel, the placement by a state of a tax on the right of egress of a citizen from a state is abhorrent and likely unconstitutional.

What can be done about it?

Challenging the provision through a traditional tax dispute is a problematic and likely lengthy process. A taxpayer seeking to litigate the issue of the constitutionality of the provision could claim deductions (or fail to add them back to its Wisconsin taxable income) and wait to see if the moving expense issue is challenged on audit and then work the issue through the typical administrative review process and through the courts. However, as noted above, the financial impact of the moving expense issue on a taxpayer's liability likely is minimal. There would not be enough money in the issue to justify the challenge. The same would be true if a taxpayer were to not claim a deduction or add the moving expenses back to income and then file a claim for refund. The juice would not likely be worth the squeeze.

Another possible avenue of attack on the constitutionality of the Act would be through a declaratory judgment action. Wisconsin has adopted the Uniform Declaratory Judgments Act.[6] Under this procedure, one would not have to wait for the usual administrative tax dispute process to play out. A taxpayer could bring an action asking that a court enter a declaration that the Act is unconstitutional on a number of grounds. Such a decision would be precedential and available for use by other taxpayers in challenging the denial of deductions or refusal to add moving expense back to Wisconsin taxable income. But, once again, the juice likely is not worth the squeeze as the costs of litigation likely would exceed the amount of any deduction for tax refund.

One other possible angle of attack would be for a trade association representing business interests to bring such a declaratory judgment action on behalf of its members. In Wisconsin, it appears associations have standing to bring declaratory judgment actions on behalf of their members.[7] For instance, a trade association representing business located in Wisconsin could allege that the constitutional rights of its member companies is being chilled by the infringement on such members rights to freedom of travel between the states by the Act's imposition of higher taxes on business that move out of state as compared to Wisconsin businesses who move to a different location in the state. The Act also works immediate harm on Wisconsin businesses because it discriminates against interstate commerce by virtue of more favorable taxes on those who move from one location in Wisconsin to another as compared to those who chose to move to another state or country. Making a showing of standing by a business trade association with members in Wisconsin should not be a problem.

Where does it stop?

Wisconsin is the first state to pull a political stunt like enacting a tax on exiting businesses, but if Wisconsin is not stopped in its tracks, its unconstitutional approach is likely to proliferate and mutate. Wisconsin started with a small item like moving expenses. Other states are sure to scour their, and the federal, tax codes for other deductions or tax benefits to tweak so they don't apply to businesses moving out of the state that will hurt more than moving expenses. A better approach for Wisconsin would be for it to review its corporate income tax policies to make sure they are pro-job and pro-growth. Then perhaps no one would move out...

Special thanks to Marisa Poncia in our DC office for contributing to this piece.

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[1] See *Philadelphia v. New Jersey*, 437 U. S. 617, 623–624 (1978), *Willson v. Black Bird Creek Marsh Co.,* 2 Pet. 245, 252 (1829), *New Energy Co. of Ind. v. Limbach*, 486 U. S. 269, 273 (1988), *Comptroller of Treasury of Md. v. Wynne,*575 U. S. ___ (2015), *Tennessee Wine and Spirits Ass. V. Thomas*, _ U.S. _ (June 26, 2019) (slip op. p. 6).

[2] See e.g., *Corfield v. Coryell*, 6 F. Cas. 546, 550 (C.C.E.D.Pa. 1823), *Paul v. Virginia*, 8 Wall. 168, 180 (1869), and *Ward v. Maryland*, 12 Wall. 418, 430 (1871).

[3] *Edwards v. California*, 314 U.S. 160, 181, 183-185 (1941) (Douglas and Jackson, JJ., concurring), and *Twining v. New Jersey,* 211 U.S. 78, 97 (1908).

[4] *Edwards v. California, supra*, and the *Passenger Cases*, 7 How. 283 (1849)

[5] *Kent v. Dulles*, 357 U.S. 116, 125 (1958), *Aptheker v. Secretary of State*, 378 U.S. 500, 505-506 (1964); *Zemel v. Rusk*, 381 U.S. 1, 14 (1965),

[6] Wisc. St. Sec. 806.04.

[7] *Wisconsin's Environmental Decade, Inc., v. Public Service Commission of Wisconsin,* 69 Wis. 2d 1

230 N.W.2d 243 (1975), *Metropolitan Builders Association f Greater Milwaukee, v. Village of Germantown,* 282 Wis. 2d 458, 2005 WI App 103, 698 N.W.2d 301(2005).