Report 20-27
December 2020

Electronics and Information Technology Manufacturing Zone Program

Wisconsin Economic Development Corporation

STATE OF WISCONSIN

Legislative Audit Bureau

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Joe Chrisman
State Auditor

December 9, 2020

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Cowles and Representative Kerkman:

As required by s. 13.94 (1) (u), Wis. Stats., we evaluated the Wisconsin Economic Development Corporation's (WEDC's) process for verifying information submitted by recipients of Electronics and Information Technology Manufacturing Zone program tax credits, as well as whether WEDC adhered to statutory and contractual requirements when it verified the amount of program tax credits to award these recipients. This is the third of five statutorily required annual evaluations of these issues. Our last such evaluation was published as report 19-27 in December 2019.

In November 2017, WEDC executed a $2.85 billion tax credit contract with three corporations that are collectively referred to as "Foxconn" to create jobs and make capital investments over the 15-year period from January 2018 through December 2032.

We found that WEDC established written procedures that allowed it to award program tax credits for the wages paid to employees who did not perform services in Wisconsin. In this way, these written procedures did not comply with statutes or WEDC's contract. These procedures also indicated that WEDC will not award program tax credits for the wages paid to certain employees who performed services in Wisconsin. We recommend WEDC modify its written procedures.

In October 2020, WEDC indicated that Foxconn's activities and investments in Wisconsin to date were ineligible for program tax credits. As a result, WEDC did not award any program tax credits to Foxconn in 2020. It also did not award any program tax credits in prior years.

A response from WEDC's chief executive officer follows the Appendix.

Respectfully submitted,

Joe Chrisman
State Auditor

JC/DS/ss

Electronics and Information Technology Manufacturing Zone Program ▪

2017 Wisconsin Act 58, which was enacted in September 2017, created the Electronics and Information Technology Manufacturing Zone program. The Wisconsin Economic Development Corporation (WEDC) administers this program. Statutes allow WEDC to designate not more than one electronics and information technology manufacturing zone that shall remain in effect for no more than 15 years. Statutes stipulate that WEDC may award no more than $2.85 billion in tax credits under the program, including $1.5 billion for creating jobs and $1.35 billion for making capital investments. These tax credits are refundable, meaning that if a recipient's tax credits exceed its Wisconsin income tax liability, a recipient receives a payment from the Department of Revenue (DOR).

In November 2017, WEDC executed a $2.85 billion contract with Foxconn.

In November 2017, WEDC executed a $2.85 billion contract with three corporations that agreed to build a facility to fabricate thin-film transistor liquid-crystal displays, which are used in electronic appliances such as televisions and computer monitors. If these three corporations, which are collectively referred to as "Foxconn," create contractually specified jobs and make contractually specified capital investments, WEDC will award them up to $2.85 billion in program tax credits over the 15-year period of the contract and will inform DOR that they may claim these tax credits.

Beginning in 2018, statutes require the Legislative Audit Bureau to annually evaluate for five years:

- WEDC's process for verifying information that was submitted by recipients of program tax credits and that indicates the extent to which these recipients created contractually specified jobs and made contractually specified capital investments; and

- whether WEDC adhered to statutory and contractual requirements when it verified the amount of program tax credits to award recipients as a result of their efforts to create jobs and make capital investments.

In December 2019, we released report 19-27, which was our second statutorily required evaluation of these issues. To complete our third evaluation, we interviewed WEDC staff, examined WEDC's contract with Foxconn, and analyzed the policies and written procedures WEDC established to verify information submitted by recipients of program tax credits.

Contractual Provisions

WEDC's contract establishes minimum numbers of jobs that Foxconn must create in order to be awarded program tax credits for creating jobs in a given year. For example, to be awarded any tax credits for creating jobs in 2019, Foxconn needed to have 520 jobs filled by eligible employees as of December 31, 2019. Foxconn may be awarded program tax credits for creating jobs in each year of the 15-year contract, but it may be awarded them for making capital investments during only the seven-year period from 2019 through 2025. After Foxconn creates jobs or makes capital investments in a given year, WEDC determines the amount of program tax credits, if any, to award in subsequent years.

Foxconn is contractually required to annually report to WEDC by April 1 on the numbers of jobs it created and the capital investments it made in the prior year.

Foxconn is contractually required to annually report to WEDC by April 1 on the numbers of jobs it created and the capital investments it made in the prior year. Foxconn is also contractually required to hire and pay for a nationally recognized certified public accountant (CPA) firm to perform an attestation of the job creation and capital investment information that Foxconn reported to WEDC. WEDC's contract stipulates that this CPA firm must report to WEDC on the results of this attestation within 45 days after April 1. WEDC uses Foxconn's information and the CPA firm's report to determine the amounts of program tax credits to award.

Table 1 shows the contractually specified annual amounts of program tax credits that WEDC may award. If WEDC does not award all available tax credits in a given year, some or all of the unawarded tax credits may carry forward and be awarded in future years. All unawarded job creation tax credits carry forward, but

Foxconn must create a minimum number of jobs in order for unawarded capital investment tax credits to carry forward.

Table 1

Amounts of Program Tax Credits WEDC May Award Foxconn[1]
(in millions)

Calendar Year	Minimum Number of Jobs[2]	Job Creation	Capital Investment	Total
2018	260	$ 9.5	–	$ 9.5
2019	520	19.1	$ 192.9	212.0
2020	1,820	47.8	192.9	240.7
2021	3,640	84.0	192.9	276.9
2022	5,200	120.3	192.9	313.2
2023	7,150	120.6	192.9	313.5
2024	7,800	120.9	192.9	313.8
2025	8,450	121.1	192.9	314.0
2026	9,100	121.5	–	121.5
2027	10,400	121.7	–	121.7
2028	10,400	122.0	–	122.0
2029	10,400	122.3	–	122.3
2030	10,400	122.7	–	122.7
2031	10,400	123.0	–	123.0
2032	10,400	123.5	–	123.5
Total		**$1,500.0**	**$1,350.0**	**$2,850.0**

[1] Tax credits not awarded in a given year may carry forward and be awarded in future years. All unawarded job creation tax credits carry forward, but Foxconn must create a minimum number of jobs in order for unawarded capital investment tax credits to carry forward.

[2] Foxconn must create a minimum number of jobs in order to be awarded job creation tax credits in a given year.

Job Creation

Statutes and WEDC's contract require WEDC to award Foxconn program tax credits for creating jobs filled by employees paid at least $30,000 annually and offered retirement, health, and other benefits equivalent to such benefits offered to employees required to work at least 2,080 hours annually. Statutes and WEDC's contract stipulate that Foxconn is to be awarded program tax credits equal to 17.0 percent of the wages of such employees, but it cannot be awarded program tax credits for any wages exceeding $100,000.

Statutes and WEDC's contract require WEDC to award program tax credits for the wages paid to employees for services performed in Wisconsin.

Statutes and WEDC's contract require WEDC to award program tax credits for the wages paid to employees for services performed in Wisconsin. Section 238.396 (3s) (c), Wis. Stats., stipulates that WEDC may not certify Foxconn to claim program tax credits for services performed outside of Wisconsin. In addition, s. 71.28 (3wm) (b), Wis. Stats., requires WEDC to award program tax credits for a tax credit recipient's zone payroll, which is statutorily defined to be the wages paid to employees for services performed in Wisconsin. The texts of these statutory provisions are shown in the Appendix.

In report 19-27, we found that WEDC's October 2019 written procedures allowed WEDC to award program tax credits for the wages paid to employees for services not performed in Wisconsin. These procedures did not reference the zone payroll statutes defined in s. 71.28 (3wm), Wis. Stats., which requires WEDC to award program tax credits for the wages paid to employees for services performed in Wisconsin. Instead, these procedures referenced other statutory and administrative rule provisions that define a corporation's state payroll for income tax purposes to include all of the wages paid to certain individuals who perform a portion of their services outside of Wisconsin. As a result, we recommended that WEDC comply with statutes by modifying its written procedures to explicitly require it to award job creation tax credits under the program for only the wages paid to employees for services performed in Wisconsin.

WEDC's written procedures continued to allow WEDC to award program tax credits for the wages paid to employees for services not performed in Wisconsin.

In January 2020, WEDC revised its written procedures, which continued to allow it to award program tax credits for the wages paid to employees for services not performed in Wisconsin. We found that:

- WEDC's procedures did not require WEDC to award program tax credits for the wages paid to employees for services performed in Wisconsin, as is required by s. 71.28 (3wm) (b), Wis. Stats.; and

- WEDC's procedures referenced other statutory and administrative rule provisions that define a corporation's state payroll for income tax purposes to include all of the wages paid to certain individuals who perform a portion of their services outside of Wisconsin. Because of these references, WEDC may award program tax credits for all of the wages paid to certain Foxconn employees who performed services in Wisconsin for as little as five days in the prior year.

WEDC's written procedures indicated that WEDC will not award program tax credits for the wages paid to certain employees who performed services in Wisconsin.

We found that WEDC's written procedures indicated that WEDC will not award program tax credits for the wages paid to certain employees who performed services in Wisconsin. These procedures indicated that if employees were not residents of Wisconsin or contiguous states, Foxconn would not receive program tax credits for the wages paid to these employees, even if these employees performed services in Wisconsin. For example, if a resident of Indiana traveled to Wisconsin to perform services in the zone, these procedures indicated that WEDC would not award Foxconn any tax credits for the wages paid to this employee. In this way, WEDC's procedures did not comply with statutes.

We again recommend that WEDC comply with statutes by modifying its written procedures to explicitly require it to award program tax credits for only the wages paid to employees for services performed in Wisconsin. We also recommend that WEDC modify its written procedures to require it to award program tax credits for the wages paid to all employees for services performed in Wisconsin, regardless of the residency of these employees.

☑ Recommendation

We recommend the Wisconsin Economic Development Corporation:

- *comply with statutes by modifying its written procedures to explicitly require it to award job creation tax credits under the Electronics and Information Technology Manufacturing Zone program for only the wages paid to employees for services performed in Wisconsin;*

- *comply with statutes by modifying its written procedures to require it to award job creation tax credits under the Electronics and Information Technology Manufacturing Zone program for the wages paid to all employees for services performed in Wisconsin, regardless of the residency of these employees; and*

- *report to the Joint Legislative Audit Committee by March 1, 2021, on the status of its efforts to implement these recommendations.*

WEDC is contractually required to award program tax credits for job creation based on all of the wages up to $100,000 that Foxconn actually paid to eligible employees, including those who worked for only part of a given year. In report 19-27, we found that WEDC did not calculate program tax credits based on all of the wages up to $100,000 that Foxconn actually paid to employees who would have earned more than $100,000 if they had worked for the firm the entire year. As a result, we recommended that WEDC comply with its contract when calculating the amounts of wages eligible for program tax credits.

In January 2020, WEDC modified its written procedures to indicate that it will not calculate program tax credits based on all of the wages actually paid to certain employees.

In January 2020, WEDC modified its written procedures to indicate that it will not calculate program tax credits based on all of the wages up to $100,000 that Foxconn actually paid to employees who would have earned more than $100,000 if they had worked for the firm the entire year. Instead, these procedures indicated that WEDC will prorate the wages of such employees. For example, if an employee earned $80,000 over six months in a given year, these procedures indicated that WEDC would award program tax credits based on only $40,000 of that employee's wages. In this way, WEDC's procedures did not comply with the contract.

We recommend that WEDC modify its written procedures to require it to award job creation tax credits based on all of the wages up to $100,000 that were actually paid to eligible employees, including those who had worked for Foxconn for only part of a given year. Doing so will ensure that WEDC complies with its contract when verifying the amount of program tax credits to award Foxconn.

☑ Recommendation

We recommend the Wisconsin Economic Development Corporation:

- *comply with its contract by modifying its written procedures to require it to award job creation tax credits under the Electronics and Information Technology Manufacturing Zone program for all wages up to $100,000 that were actually paid to eligible employees, including those who had worked for only part of a given year; and*

- *report to the Joint Legislative Audit Committee by March 1, 2021, on the status of its efforts to implement this recommendation.*

In April 2020, Foxconn reported its 2019 payroll information, which included 688 employees and indicated that all of them performed their services in Wisconsin. WEDC reviewed this information and estimated that as of December 31, 2019, Foxconn had created 281 jobs for which Foxconn may have been eligible to receive program tax credits, if these jobs had been related to the construction and operation of a facility that complied with the contractual terms. WEDC indicated that it did not completely verify this information because it concluded that Foxconn had not started to build such a facility.

WEDC followed its written procedures when it completed its partial verification of the payroll information that Foxconn provided in April 2020.

We found that WEDC followed its written procedures when it completed its partial verification of the payroll information that Foxconn reported in April 2020. For example, WEDC's determination that Foxconn had created 281 jobs included only those jobs filled by residents of Wisconsin or contiguous states. WEDC's determination excluded 18 jobs filled by residents of other states, even though some of these individuals may have performed services in Wisconsin. In addition, WEDC prorated the wages of 66 employees who would have earned more than $100,000 if they had worked for Foxconn for all of 2019. In these ways, WEDC's partial verification did not comply with statutes and the contract.

In report 19-27, we found that WEDC did not approve in writing the procedures that the CPA firm used to perform an attestation of the job creation and capital investment information that Foxconn reported to WEDC in April 2019. We recommended that WEDC not award any program tax credits unless it approves in writing the procedures used by the CPA firm.

In our current audit, we found that WEDC complied with our recommendation by approving in writing the procedures the CPA firm used to perform an attestation of the job creation and capital investment information that Foxconn reported to WEDC in April 2020. The CPA firm based its attestation, in part, on its review of information for a sample of 93 employees listed in Foxconn's information and its survey of these employees, 76 of whom responded.

The CPA firm identified concerns with the information Foxconn reported to WEDC in April 2020.

In its July 2020 report to WEDC, the CPA firm identified concerns with the information Foxconn reported to WEDC in April 2020, including:

- 25 of the 93 employees (26.9 percent) did not use their Foxconn-provided badges to enter Foxconn facilities during at least five days in 2019;

- 10 employees who responded to the CPA firm's survey indicated they were residents of Wisconsin or contiguous states but did not perform all of their services in Wisconsin, including 1 employee who indicated no services were performed in Wisconsin; and

- 2 employees who responded to the CPA firm's survey indicated they were employed by a firm other than the three contractually specified firms eligible for program tax credits.

The CPA firm's July 2020 report further demonstrates the need for WEDC to modify its written procedures to ensure that it complies with statutes and its contract by awarding program tax credits for the wages paid to employees for services performed in Wisconsin. Some of these employees may be residents of states other than Wisconsin or contiguous states.

Capital Investments

Statutes and WEDC's contract allow WEDC to award Foxconn program tax credits for making capital investments.

Statutes and WEDC's contract allow WEDC to award Foxconn program tax credits for making capital investments from 2019 through 2025 if WEDC determines that Foxconn made a significant capital investment in the zone, which is contractually defined to be Foxconn's business facilities within specified geographic boundaries in Racine County. These tax credits must not exceed 15.0 percent of Foxconn's capital investments. WEDC's contract indicates that Foxconn will make up to $10.0 billion in capital investments to complete the facility. As we noted in report 18-18, which was our first statutorily required evaluation of these issues, Foxconn may be awarded all $1.35 billion in program tax credits for capital investment if it makes at least $9.0 billion in capital investments.

In April 2020, Foxconn reported information to WEDC on the capital investments it had made through December 2019. After reviewing this information, WEDC estimated that Foxconn had made $202.4 million in capital investments for which Foxconn may have been eligible to receive program tax credits, if these capital investments had been related to constructing a facility that complied with the contract. However, WEDC indicated that it did not completely verify information associated with these capital investments because it concluded that Foxconn had not started to build such a facility. As a result, WEDC did not award Foxconn any program tax credits for capital investment.

In report 19-27, we found that the information Foxconn reported to WEDC in April 2019 did not specify whether capital investments were made in the zone. WEDC's contract indicates that WEDC is to award Foxconn tax credits for machinery and equipment installed and used in the zone, as well as for land and buildings that are in the zone and needed to complete the project. We recommended that WEDC award program tax credits for only capital investments made in the zone. In our current audit, we found that the information Foxconn reported to WEDC in April 2020 specified that the capital investments were made in the zone.

Future Reporting

A total of $28.6 million in job creation tax credits will carry forward and may be awarded in future years.

WEDC's contract specifies that any job creation program tax credits that WEDC does not award to Foxconn in a given year will carry forward and may be awarded in future years. Because WEDC did not award Foxconn any of the $9.5 million it could have awarded in 2018 or any of the $19.1 million it could have awarded in 2019, all $28.6 million of these tax credits will carry forward to future years. However, the contract specifies that Foxconn may be awarded no more than $19.1 million of these tax credits in 2021.

None of the $192.9 million in capital investment tax credits that Foxconn could have been awarded in 2020 will carry forward to future years.

WEDC's contract required Foxconn to create 520 jobs filled by eligible employees and make approximately $1.286 billion in capital investments through December 2019 in order to be awarded all $192.9 million in tax credits for making capital investments. The contract specifies that if Foxconn created fewer than 520 jobs filled by eligible employees, Foxconn would not be awarded all $192.9 million in tax credits, and the unawarded capital investment tax credits would not carry forward to future years. For example, if Foxconn had created 390 jobs (75.0 percent of the 520 jobs) filled by eligible employees, it would have been awarded no more than $144.7 million (75.0 percent of $192.9 million) for making capital investments. The remaining $48.2 million of capital investment tax credits would not carry forward to future years. Because WEDC determined that Foxconn did not create any jobs filled by eligible employees, none of the $192.9 million in capital investment tax credits that Foxconn could have been awarded in 2020 will carry forward to future years.

WEDC may award Foxconn up to $259.8 million in program tax credits for creating jobs and making capital investments through 2020.

As shown in Table 2, WEDC may award Foxconn up to $259.8 million in program tax credits for creating jobs and making capital investments through 2020. WEDC would award such tax credits in 2021. To be awarded any job creation tax credits, Foxconn must create at least 1,820 jobs filled by eligible employees as of December 31, 2020. To be awarded any of the $19.1 million in program tax credits that were carried forward and available to be earned in 2020, Foxconn must create at least 5,200 jobs filled by eligible employees as of December 31, 2020.

Table 2

Amounts of Program Tax Credits WEDC May Award Foxconn[1]
(in millions)

Calendar Year	Minimum Number of Jobs[2]	Job Creation	Carryforward for Job Creation	Capital Investment	Carryforward for Capital Investment	Total
2018	260	$ 9.5	–	–	–	–
2019	520	19.1	$ 9.5	$192.9	–	–
2020	1,820	47.8	19.1[3]	192.9	$0	$259.8

[1] Tax credits not awarded in a given year may carry forward and be awarded in future years. All unawarded job creation tax credits carry forward, but Foxconn must create a minimum number of jobs in order for unawarded capital investment tax credits to carry forward.

[2] Foxconn must create a minimum number of jobs in order to be awarded job creation tax credits in a given year.

[3] Because Foxconn did not create at least 260 jobs filled by eligible employees in 2018 or 520 jobs filled by eligible employees in 2019, $28.6 million in program tax credits will carry forward, including $19.1 million that Foxconn may earn in 2020.

WEDC's November 2017 contract with Foxconn remains in effect. However, WEDC indicated that it attempted to work with Foxconn to develop a new contract that it believed would align with Foxconn's plans for developing a manufacturing facility in Wisconsin. If a new contract were executed in the future, the contractual terms and conditions pertaining to how WEDC may verify the amount of program tax credits to award could change. Our next statutorily required annual evaluation will be performed in 2021.

■ ■ ■ ■

Appendix ■

Appendix

Statutory Requirements for Awarding Program Tax Credits

Statutes indicate how WEDC is required to award program tax credits. Statutes refer to WEDC as "the corporation" and a tax credit recipient as a "claimant."

Section 238.396 (3s) (c), Wis. Stats., states that "The corporation may not certify a business to claim tax benefits under ss. 71.07 (3wm) (b) and 71.28 (3wm) (b) for services performed outside this state."

Sections 71.07 (3wm) (b) and 71.28 (3wm) (b), Wis. Stats., require WEDC to award program tax credits based on the "zone payroll" of a tax credit recipient. Sections 71.07 (3wm) (a) 6. and 71.28 (3wm) (a) 6., Wis. Stats., define zone payroll as "the amount of state payroll that is attributable to wages paid by the claimant to full-time employees for services that are performed in the zone or that are performed outside the zone, but within the state, and for the benefit of the operations within the zone, as determined by the Wisconsin Economic Development Corporation."

Response ■

December 7, 2020

Mr. Joseph Chrisman
State Auditor
Legislative Audit Bureau
22 E. Mifflin Street, Suite 500
Madison, WI 53703

Dear Mr. Chrisman:

Thank you for the opportunity to respond to the Legislative Audit Bureau's (LAB) evaluation of the Wisconsin Economic Development Corporation's (WEDC) process for verifying information submitted by claimants SIO International Wisconsin, Inc., FEWI Development Corporation, and AFE, Inc. (collectively referred to as "Foxconn") under the Electronics and Information Technology Manufacturing Zone (EITMZ) tax credit program.

Enacted in September 2017, Wisconsin Act 58 created the EITMZ and provided statutory guidelines for WEDC's contract with Foxconn. WEDC signed a contract with Foxconn on November 10, 2017, setting forth the terms, conditions, and requirements related to Foxconn's construction of a Generation 10.5 TFT-LCD Fabrication Facility within the EITMZ. WEDC created Program Guidelines for the EITMZ program, which were approved by WEDC's Board of Directors in November 2017. WEDC also created internal procedures to address the verification process specific to the EITMZ program, which were revised in response to LAB's 18-18 and 19-27 reports.

Act 58 requires LAB to annually evaluate WEDC's process for verifying information submitted by Foxconn until 2022. This report represents LAB's review of statutory and contractual requirements of tax credit verifications for the EITMZ program. Foxconn has not qualified for or earned any tax credits to date.

<u>LAB's Recommendations</u>

In its prior EITMZ report (LAB's 19-27 report), LAB identified four recommendations. We are pleased that the current report recognizes that WEDC has remedied the following two prior recommendations that:

- WEDC not issue tax credits if the Agreed Upon Procedures (AUP) report has not been accepted by WEDC, and
- when capital expenditure information is collected, it includes the location of the capital expenditure.

WEDC has been actively pursuing practical remedies for the remaining two recommendations:

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- WEDC award job creation tax credits only for wages paid for services performed in the EITMZ and not exclude wages for services performed in the EITMZ, regardless of the residency of the employees; and
- Align procedures with the contract and award job creation tax credits for all wages up to $100,000 that were actually paid to eligible employees including those who had worked for only part of a given year.

WEDC will continue to pursue practical remedies for these matters which may occur via contract amendment and/or changes and modifications to WEDC procedures. As Foxconn has not qualified for or earned any tax credits to date, WEDC has not awarded any EITMZ tax credits contrary to either the statute or the contract. Pursuant to your recommendation, WEDC will report its progress on these remedies to the Joint Legislative Audit Committee on March 1, 2021.

Sincerely,

Melissa L. Hughes
Secretary and CEO