

Tax Incentives and the States

CSG West

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About the Tax Foundation

- 77 years of informing smarter tax policy at the federal, state, and local levels
- Tax systems that are simple, neutral, transparent, stable, and pro-growth
- *Facts & Figures* booklet
- *Tax Freedom Day*
- *State-Local Tax Burdens*
- *State Business Tax Climate Index*
- *Location Matters*

Defining Incentives

- Inherent(?) state advantages
 - Network Effects (e.g., Silicon Valley, Wall Street, DC Lobbyists)
 - Tourism/Weather, Labor Costs, Education, Transportation (airline hubs, ports, highways), Prestige, Access to Markets
- Regulatory & Legal Environment
 - Clear, consistent rules & scope of licensing and regulations
 - Turnaround (e.g., Delaware filing response within 24 hours)
- Tax Structure
 - Not having a major tax (e.g., Alaska income & sales tax, Texas income tax, Oregon sales tax)
 - Having all the major taxes but keeping them low and simple (Indiana & Utah)
 - High taxes but good structure (e.g., NY corp income tax reform, sales tax on business inputs)
 - Apportionment formulas, combined reporting, throwout/throwback
- Broadly-Available Incentives (e.g., new jobs credit)
- Industry- or Geography-Specific Incentives (e.g., Tax Free NY, R&D credits, film credits)
- Company-Specific Incentive Packages

Perspective

Tax policy is powerful but can't change everything. Some broader trends affecting economic growth include

- Demographic shifts
- Knowledge-intensity of activities
- Shortened product & industry cycles
- Fragmentation of production
- Economic interdependence

(Kenneth Poole, Center for Regional Economic Competitiveness)

Status Quo

- Ubiquitous
 - Jobs credits (42 states + DC)
 - R&D credits (41 states)
 - Investment credits (40 states)
 - Film credits (39 states + DC)
- High-profile
 - Tax Free NY television ads
 - Governor Perry visits and radio ads
 - Boeing (Washington, Missouri, South Carolina, Texas)
 - Northrup Grumman headquarters (Maryland, DC, Virginia)
 - Michigan (pre-2009 tax reform)
 - North Carolina (pre-2013 tax reform)
 - Rhode Island (pre-2014 tax reform)
- Cost is ~\$8-\$10b/yr in economic development spend plus perhaps \$10b-\$50b on tax expenditures

State Business Tax Climate Index

- *How* (not *how much*)
- Ranking of status quo (as of July 1) and roadmap for improving
- Overall rank and five component ranks
 - Individual Income, Corporate Income, Sales, Unemployment, and Property/Wealth
- Widely cited and used by media, policymakers, and other indices
- Downloaded 500,000 times a year
- Survey of academics, policymakers, and media named it 21st best think tank policy report in the world for 2013

Location Matters

- Corporate Headquarters
 - New: Nebraska (1.4%) to Pennsylvania (30.7%)
 - Mature: Wyoming (8.3%) to Pennsylvania (28.0%)
- R&D Facility
 - New: Louisiana (-10.5%) to Pennsylvania (33.5%)
- Retail
 - New: South Dakota (17.4%) to Iowa (49.7%)
- Distribution Center
 - New: Ohio (18.3%) to Kansas (65.4%)
- Capital-Intensive Manufacturer
 - New: Louisiana (1.0%) to Maryland (31.9%)

Do They Work?

- Hard to know
 - Comparing what happened with what would have happened
 - Everyone encouraged to say that the incentive did it (recipient, ED office, legislators)
 - Incentives promote activity (ribbon-cutting) and saying yes, not measuring and targeting outcomes
 - Focus is on lowering costs, not creating competitive advantage (e.g., FL shift to VisitFL)
 - Evaluations usually ignore opportunity costs and diminishing returns
 - Incentives often not connected to addressing overall shortcomings (e.g., DC retail)

Effective Tax Expenditure Reports

- Most are ineffective evaluation tools
- Some states don't do them at all
- Many do not distinguish between tax structure, social policy incentives, and business incentives
- Some report projections but never update them, or don't report multiyear
- Some exclude major taxes
- Some include only statutory exemptions and miss structural exclusions
- Few include number of recipients
- Few state goals of incentive or measures
- Few include impacts on local governments

Questions to Ask

- What is the problem we are trying to solve?
- What will we create with this incentive?
- Does this incentive create a competitive advantage?
- How will we measure the impact?
- Who is in charge of collecting data and reporting it?
- How does this incentive fit into the larger mix?
- If we had to appropriate budget dollars for this incentive package, would we spend it?
- How much is too much?

Additional Reading

- “Evidence Counts” (Pew Center on the States 2012)
 - Set goals for each incentive, use data to analyze incentives’ economic impact, review all major incentives, build evaluation into budget process
- “Avoiding Blank Checks” (Pew Center on the States 2012)
 - Importance of estimating costs & capping total incentive amount
- “Promoting State Budget Accountability through Tax Expenditure Reporting” (CBPP 2009, 2011)
 - Reviews status quo of tax expenditure reports, highlighting good practices
- “Location Matters” (Tax Foundation 2012, forthcoming 2014)
 - Business tax costs by firm type and compares effect of incentives

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