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New KPMG International Location Study: U.S. Is Falling Behind; Taxes Are a Major Fault

By Scott A. Hodge

The image of the United States as a competitive place to do business was dealt another blow with the recent release of KPMG's "2010 Competitive Alternatives," the firm's guide to international business location.¹ Of the ten countries ranked by several criteria – including labor costs, facility costs, transportation costs, and tax costs – the U.S. ranked 8th, ahead of only Germany and Japan.

What should alarm federal and state lawmakers in the U.S. is that our border nations, Mexico and Canada, ranked first and second best respectively with the lowest overall cost of doing business of the ten nations surveyed. Mexico, which was the only emerging country included in the study, was determined to be the most cost-effective place to do business in large measure because of its low labor and facilities costs. Canada's main advantage comes from the pro-business tax policies it has enacted over the past decade at both the federal and provincial levels. Since 2000, Canada's combined corporate tax rate (federal and provincial) has fallen from 43 percent to 31 percent.

The Canadian government's stated goal is to have the lowest statutory corporate tax rate among the major G-7 countries. Indeed, the government's 2010 budget would lower the federal corporate rate from 18 percent to 16.5 percent as a first step toward lowering the rate to 15 percent by 2012.² This will bring the combined rate down to roughly 26 percent. However, that rate could fall further if the provinces continue to cut their rates. For example, Ontario recently announced a three-year plan to cut its corporate income tax from 14 percent to 10 percent.

The KPMG study not only compares the business-cost competitiveness of the ten countries but also ranks 112 cities in those countries, including 15 in Canada and 60 in the U.S. Considering every factor, the most cost-effective city was Monterrey, Mexico, while Montreal was the top-rated Canadian city and Tampa the top-ranked American city.

On the tax side, KPMG considers corporate income taxes, capital taxes, sales taxes, property taxes and local business taxes. Table 1 compares corporate income taxes for selected cities across the

¹ Report downloaded on April 7, 2010, from <http://www.competitivealternatives.com/default.aspx>.

² Jeffrey Hodgson, "Canada Keeps Corporate Tax Cuts in Place, Targets," Reuters, March 4, 2010.

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ten countries. Two U.S. cities are included to illustrate the importance of state and local taxes. Businesses in Baltimore pay Maryland's corporate income tax while businesses in Las Vegas benefit from Nevada's zero rate.

Table 1 Comparing Statutory and Effective Corporate Tax Rates in Selected Cities 2010						
Country	City	Corporate Income Tax				Effective Income Tax Rate*
		Federal	Regional	Local	Combined Income Tax Rate	
U.S. †	Baltimore	34.00%	8.25%	-	39.45%	28.07%
U.S. †	Las Vegas	34.00%	-	-	34.00%	26.98%
Canada	Toronto	18.00%	14.00%	-	32.00%	17.91%
Mexico	Monterrey	30.00%	-	-	30.00%	27.32%
France	Lyon	33.33%	-	-	33.33%	19.30%
Germany	Frankfurt	15.83%	-	16.10%	31.93%	30.51%
Italy	Milan	27.50%	4.82%	-	32.19%	35.01%
Netherlands	Amsterdam	25.50%	-	-	25.50%	14.85%
U.K.	Manchester	28.00%	-	-	28.00%	22.83%
Australia	Melbourne	30.00%	-	-	30.00%	16.32%
Japan	Osaka	30.00%	10.07%	6.15%	43.20%	40.10%
* Average of 17 firm types. † The top statutory U.S. federal rate is 35 percent. The 34 percent rate shown in the table is an average that accounts for smaller firms that are not hit by the top rate. Source: KPMG						

Comparing the combined federal-regional income tax rate of these sample cities, neither Baltimore nor Las Vegas fares very well. Only Osaka, Japan, levies a higher statutory rate. Companies in Las Vegas face a combined statutory rate of 34 percent while those in Baltimore face a rate of 39.45 percent. Companies in Osaka face the highest combined rate of 43.20 percent while those in Amsterdam face the lowest rate of 25.50 percent.

However, for all companies, the “list price” statutory corporate tax rate is not the final tax rate they end up paying. KPMG also calculated the “effective” tax rate firms would pay after factoring in the various credits and deductions that each country has in their corporate tax code. The last column in this table indicates the effective tax rate for each location based upon the average of the effective rates paid by 17 different firm types within three major industries – manufacturing, corporate and IT services, and research and development (R&D).

By this measure of average effective tax rates for many industries, Baltimore and Las Vegas fare slightly better. With the advantage of Nevada's lack of a corporate income tax, Las Vegas creeps into the middle of the pack, while Baltimore improves from 2nd highest to 4th highest. What tends to bring down the average effective tax rate for many U.S. industries is the deduction for domestic manufacturing (which has the effect of lowering the statutory rate from 35 percent to roughly 32 percent for manufacturers, or from 34 percent to 31 percent if the firm has less than \$10 million in taxable income), the U.S.'s more generous depreciation schedules for capital purchases, and the credit for research and experimentation (R&E credit). Table 2 gives a more comprehensive list of cities.

Conclusion

U.S. lawmakers who are worried about the economy's slow recovery and weak job growth should take special note of KPMG's latest international competitiveness study that ranks the U.S. only 8th best out of the ten countries surveyed for their cost-effectiveness for business. Of the 26 cost components that KPMG measured, many – such as labor costs, access to markets, and suitable land sites – are largely beyond the control of policymakers. Some components – such as crime rates, schools and universities, and the cost of housing – are not factors that can be improved quickly with policy changes.

However, tax policy is a factor that federal and state lawmakers can change immediately and that can have dramatic short-term and long-term benefits. Cutting the federal corporate tax rate would immediately improve U.S. competitiveness while setting the stage for long-term economic growth.

Table 2
Comparing Statutory and Effective Corporate Tax Rates in Selected Cities
2010

Country	City	Corporate Income Tax				Effective Income Tax Rate*
		Federal	Regional	Local	Combined Income Tax Rate	
Netherlands	Amsterdam	25.50%	-	-	25.50%	14.85%
Netherlands	Brabant Stad	25.50%	-	-	25.50%	14.92%
Netherlands	The Hague	25.50%	-	-	25.50%	14.79%
Netherlands	Utrecht	25.50%	-	-	25.50%	14.84%
Canada	Edmonton	18.00%	10.00%	-	28.00%	15.65%
U.K.	Manchester	28.00%	-	-	28.00%	22.83%
U.K.	London	28.00%	-	-	28.00%	18.51%
Canada	Prince George	18.00%	10.50%	-	28.50%	17.15%
Canada	Vancouver	18.00%	10.50%	-	28.50%	17.15%
Canada	Montreal	18.00%	11.90%	-	29.90%	12.39%
Canada	Quebec City	18.00%	11.90%	-	29.90%	12.25%
Canada	Sherbrooke	18.00%	11.90%	-	29.90%	11.77%
Australia	Melbourne	30.00%	-	-	30.00%	16.32%
Australia	Adelaide	30.00%	-	-	30.00%	16.12%
Australia	Brisbane	30.00%	-	-	30.00%	15.67%
Australia	Sidney	30.00%	-	-	30.00%	13.31%
Canada	Fredericton	18.00%	12.00%	-	30.00%	10.46%
Canada	Moncton	18.00%	12.00%	-	30.00%	10.86%
Canada	Saskatoon	18.00%	12.00%	-	30.00%	13.01%
Canada	Winnipeg	18.00%	12.00%	-	30.00%	16.00%
Mexico	Monterrey	30.00%	-	-	30.00%	27.32%
Mexico	Mexico City	30.00%	-	-	30.00%	27.29%
Germany	Berlin	15.83%	-	14.35%	30.18%	28.67%
Germany	Frankfurt	15.83%	-	16.10%	31.93%	30.51%
Canada	Toronto	18.00%	14.00%	-	32.00%	17.91%
Canada	St. Catherines-Niagara	18.00%	14.00%	-	32.00%	18.31%
Canada	St. John's	18.00%	14.00%	-	32.00%	9.62%

Italy	Milan	27.50%	4.82%	-	32.19%	35.01%
Italy	Rome	27.50%	4.82%	-	32.19%	35.01%
France	Lyon	33.33%	-	-	33.33%	19.30%
France	Paris	33.33%	-	-	33.33%	14.85%
Canada	Charlottetown	18.00%	16.00%	-	34.00%	19.36%
Canada	Halifax	18.00%	16.00%	-	34.00%	18.47%
U.S. [†]	Las Vegas	34.00%	-	-	34.00%	26.98%
U.S. [†]	Cheyenne	34.00%	-	-	34.00%	28.20%
U.S. [†]	Seattle	34.00%	-	-	34.00%	26.49%
U.S. [†]	Sioux Falls	34.00%	-	-	34.00%	28.00%
U.S. [†]	Spokane	34.00%	-	-	34.00%	27.23%
U.S. [†]	Dallas-Fort Worth	34.00%	1.00%	-	34.66%	27.87%
U.S. [†]	Houston	34.00%	1.00%	-	34.66%	27.74%
U.S. [†]	McAllen	34.00%	1.00%	-	34.66%	26.68%
U.S. [†]	Youngstown	34.00%	-	1.00%	34.66%	28.63%
U.S. [†]	Montgomery	34.00%	6.50%	-	36.08%	28.20%
U.S. [†]	Shreveport	34.00%	8.00%	-	36.56%	27.50%
U.S. [†]	Denver	34.00%	4.63%	-	37.06%	28.82%
U.S. [†]	St. Louis	34.00%	6.25%	-	37.06%	30.47%
U.S. [†]	Greenville-Spartanburg	34.00%	5.00%	-	37.30%	28.39%
U.S. [†]	Jackson	34.00%	5.00%	-	37.30%	29.50%
U.S. [†]	Salt Lake City	34.00%	5.00%	-	37.30%	29.38%
U.S. [†]	Atlanta	34.00%	6.00%	-	37.60%	27.74%
U.S. [†]	Miami	34.00%	5.50%	-	37.63%	29.59%
U.S. [†]	Tampa	34.00%	5.50%	-	37.63%	29.95%
U.S. [†]	Honolulu	34.00%	6.40%	-	37.81%	37.80%
U.S. [†]	Metro DC Virginia	34.00%	6.00%	-	37.96%	28.94%
U.S. [†]	Oklahoma City	34.00%	6.00%	-	37.96%	30.14%
U.S. [†]	Detroit	34.00%	6.04%	-	37.99%	26.92%
U.S. [†]	Fargo	34.00%	6.50%	-	38.29%	31.14%
U.S. [†]	Little Rock	34.00%	6.50%	-	38.29%	30.12%
U.S. [†]	Nashville	34.00%	6.50%	-	38.29%	29.78%
U.S. [†]	Saginaw	34.00%	6.04%	0.50%	38.32%	27.39%
U.S. [†]	Albuquerque	34.00%	7.60%	-	38.44%	30.33%
U.S. [†]	Billings	34.00%	6.75%	-	38.46%	31.50%
U.S. [†]	Omaha	34.00%	7.81%	-	38.54%	26.78%
U.S. [†]	Raleigh	34.00%	6.90%	-	38.55%	29.60%
U.S. [†]	Phoenix	34.00%	6.97%	-	38.60%	27.72%
U.S. [†]	Wichita	34.00%	7.00%	-	38.62%	31.00%
U.S. [†]	Buffalo	34.00%	7.10%	-	38.69%	28.80%
U.S. [†]	New York City	34.00%	7.10%	-	38.69%	26.96%
U.S. [†]	Chicago	34.00%	7.18%	-	38.74%	30.19%
U.S. [†]	Hartford	34.00%	7.50%	-	38.95%	28.27%
U.S. [†]	Boise	34.00%	7.60%	-	39.02%	30.68%
U.S. [†]	Milwaukee	34.00%	7.90%	-	39.21%	29.21%
U.S. [†]	Baltimore	34.00%	8.25%	-	39.45%	28.07%
U.S. [†]	Burlington	34.00%	8.50%	-	39.61%	29.17%
U.S. [†]	Charleston	34.00%	8.50%	-	39.61%	28.79%

U.S. [†]	Indianapolis	34.00%	8.50%	-	39.61%	32.10%
U.S. [†]	Manchester	34.00%	8.50%	-	39.61%	32.35%
U.S. [†]	Wilmington	34.00%	8.70%	-	39.74%	30.62%
U.S. [†]	Boston	34.00%	8.75%	-	39.78%	29.61%
U.S. [†]	Lexington	34.00%	6.00%	2.75%	39.78%	31.22%
U.S. [†]	Los Angeles	34.00%	8.84%	-	39.83%	30.94%
U.S. [†]	Riverside-San Bernadino	34.00%	8.84%	-	39.83%	31.74%
U.S. [†]	San Diego	34.00%	8.84%	-	39.83%	31.31%
U.S. [†]	San Francisco	34.00%	8.84%	-	39.83%	30.07%
U.S. [†]	Cedar Rapids	34.00%	12.00%	-	39.88%	27.06%
U.S. [†]	Bangor	34.00%	8.93%	-	39.89%	31.64%
U.S. [†]	Providence	34.00%	9.00%	-	39.94%	28.66%
U.S. [†]	Trenton	34.00%	9.00%	-	39.94%	28.69%
U.S. [†]	Anchorage	34.00%	9.40%	-	40.20%	40.90%
U.S. [†]	Minneapolis	34.00%	9.80%	-	40.47%	27.15%
U.S. [†]	Harrisburg	34.00%	9.99%	-	40.59%	30.64%
U.S. [†]	Philadelphia	34.00%	9.99%	-	40.59%	29.95%
U.S. [†]	Portland	34.00%	6.60%	3.65%	40.77%	33.12%
Japan	Osaka	30.00%	10.07%	6.15%	43.20%	40.10%
Japan	Tokyo	30.00%	10.07%	6.21%	43.26%	43.10%

* Average of 17 firm types.

† The top statutory U.S. federal rate is 35 percent. The 34 percent rate shown in the table is an average that accounts for smaller firms that are not hit by the top rate.

Source: KPMG