Washington Research Council

= Special Report =

July 1989

New Business Location in the Northwest

Overview and Introduction

The relationship between tax policy and economic development has been debated for years. Development enthusiasts lobby for more and greater tax incentives, claiming such breaks spur job growth. And tax reformers have suggested the current tax system impedes growth and development. Meanwhile, Washington has the fastest growing economy in the Northwest and one of the fastest growing in the nation. The public is justifiably confused and skeptical.

An earlier Research Council study, "Understanding Washington's Taxes," concluded that the present tax system is "fundamentally sound," but the Council lacked the data necessary to evaluate the impact of the tax structure on business development. Recently, supported by a grant from the Northwest Area Foundation, the Council conducted a business survey to learn more about one significant dimension of the relationship between tax policy and economic development.

Specifically, the purpose of the study was to determine the extent to which taxes affect a business's decision of where to locate in the Northwest. Businesses in Oregon, Washington and Idaho responded to a series of questions addressing the factors most important to them in their locational decision.

For small start–up businesses — the majority of our sample — taxes are relatively unimportant. More important is the personal residential preference of the business owner, followed by such traditional economic criteria as land, labor skills, domestic product markets and financing.

For larger businesses — those with 50 or more employees — taxes represent a greater concern. For these businesses, although still top on the list, residential preference declines in importance and economic considerations, including taxes, become more critical.

The study which follows describes the types of firms responding to the survey and discusses in more detail the locational characteristics they consider important. In addition case studies are presented of several different firms in the Northwest which either represent a common theme of survey responses or allow us to understand anomalies in a clearer light. These include the following:

- Dateline Technology, a Bellevue–based manufacturer of computer peripherals, located here because of the founder's strong preference for the quality of life of the area.
- Summation, a high–tech start–up which located in Woodinville in 1984, produces modular instrumentation equipment. It has grown from three employees initially to more than 85 people today. For Summation taxes are just another cost of doing business and did not enter into the firm's location decision.
- KJOS Systems Inc. is a computer distribution firm which relocated to Beaverton, Ore. from Santa Fe Springs, Calif. in 1987, after also considering Washington state. KJOS recently established an office in Bellevue, Wash.
- Heath Techna, a Kent–based plastic aerospace components manufacturer, plans to expand its operation to Bellingham. Its Bellingham facility will employ about 100 people initially.
- Seattle First National Bank moved and expanded its credit card operations to Spokane in 1988, after considering Seattle, Oregon and Nevada. An adequate pool of labor skills was the main reason for the move, but taxes were also a primary concern.

State Taxes Not Important to Most Location Decisions

State taxes are not a very important consideration in where to locate for most newly forming small businesses in the Northwest, according to the Washington Research Council survey. Not surprisingly, the key determinant in business location decisions is where the owner lives or wants to live.

Of the 644 businesses responding to the Research Council survey, 88 percent did not conduct a detailed review of state and local taxes in the process of deciding where to locate. Most of these were businesses with fewer than 50 employees. And most often — 85 percent — firms did not consider in their location decision states other than the one in which they located.

Of the 80 businesses responding which considered taxes "very important" only 29 percent (22 firms) reviewed them in detail. Firms in this smaller group are more likely to consider other states in their location decision and they typically have a larger start–up workforce and a greater level of initial capital investment. For these businesses, taxes are a more important consideration, however, the owner's residential preference was still on top by a significant margin.

906 S. Columbia, Suite 350 • Olympia, WA 98501 • (206) 357-6643

Characteristics of Respondents

Number of Firms Responding

Six hundred and forty–four (644) firms responded to the WRC survey: 315 from Washington, 209 from Oregon and 120 from Idaho, with about 68 percent locating after 1986.

Number of Relocations

Only 8 percent of the firms responding (52 firms) had relocated from other states or countries; the remainder were new businesses.

Number of Firms Considering Other States

Of the total number of firms responding only 95, or about 15 percent, had considered other states in their location decision. There was no significant difference between the states in this characteristic.

Respondents by Sector

There were some significant variations between the states in the industry of firms responding. As shown in Figure 1, the distribution of firms responding across industrial sectors in Washington and Oregon was generally similar, with about a 40–60 split between manufacturing and non–manufacturing activities. Idaho had heavier representation from the non–manufacturing sectors (79 percent).

Initial Capital Investment

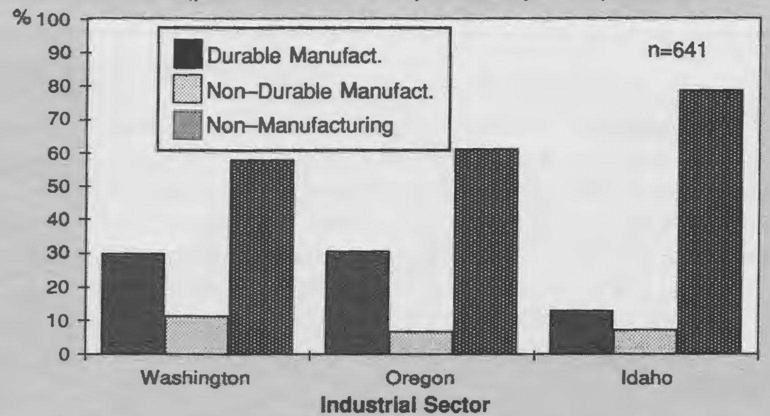
About 57 percent of the firms responding had initial capital investment of more than $50,000. Figure 2 illustrates the distribution of respondents by their level of capital investment. There was no significant variation between the three states in this characteristic.

Size of Workforce

More than 50 percent (309 firms) of the firms responding to the survey currently employed between five and 19 people. Their initial employment, however, was more often less than five employees. More than 85 percent of the firms employed less than 20 employees initially.

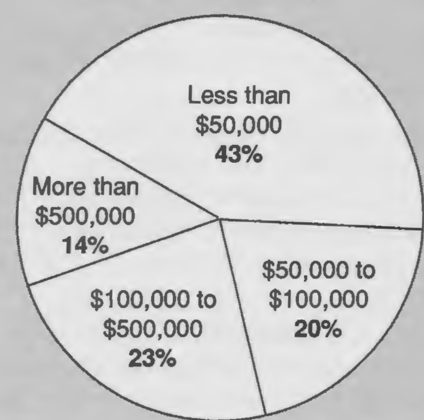
As Figure 3 illustrates, employment after the first year of business saw some growth in number of employees. The percentage of firms with 20 or more employees grew from 11 percent initially, to 18 percent after one year, and to 28 percent currently. More than 44 percent of the firms anticipated employment of 20 or more people in three to five years.

Figure 1
Industrial Distribution
(percent of total responses by state)



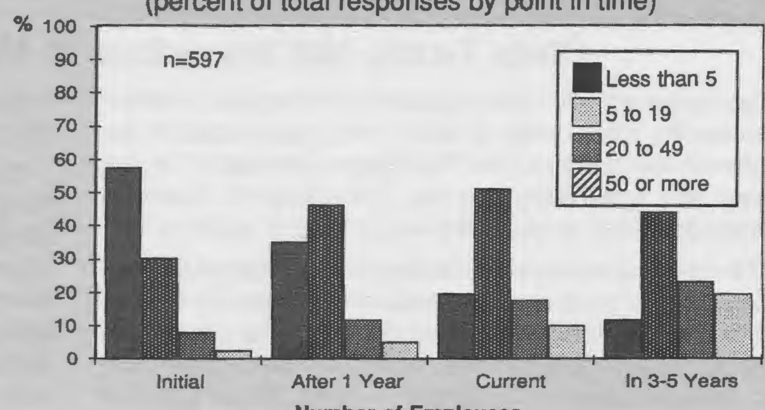
Source: Business Location Survey, Washington Research Council, 1989.

Figure 2
Initial Capital Investment
(percent of total)



Source: Business Location Survey, Washington Research Council, 1989.

Figure 3
Firm Size
(percent of total responses by point in time)



Source: Business Location Survey, Washington Research Council, 1989.

These data strongly suggest that tax policy plays a limited role in economic development efforts in the Northwest.

Owner Residence is Key to Location

In developing the survey instrument we wanted to understand the importance of different factors during three broad stages of decision making. These were: 1) initial impressions which led businesses to consider the Northwest; 2) the factors businesses reviewed in detail; and, 3) the factors which were critical to the final decision.

As shown in Figure 4, owner's residence was by far the most critical factor in recent firm locations in the Northwest (more than one response was allowed to this question). More than 70 percent of the survey respondents initially considered the Northwest as a business location because it was where the firm's owner lived or wanted to live. About 68 percent of survey respondents identified place of owners' residence to be a deciding factor in the firm's location.

Residential preference diminishes in importance for larger businesses. Only 53 percent of the firms (33 firms) with 50 or more employees said the owner's residential preference was a deciding factor. For these firms, economic factors become more important. Sixteen percent of the larger firms (10 firms) indicated that state and local taxes were a deciding factor, compared with less than 7 percent of the firms (35 firms) employing fewer than 50 employees.

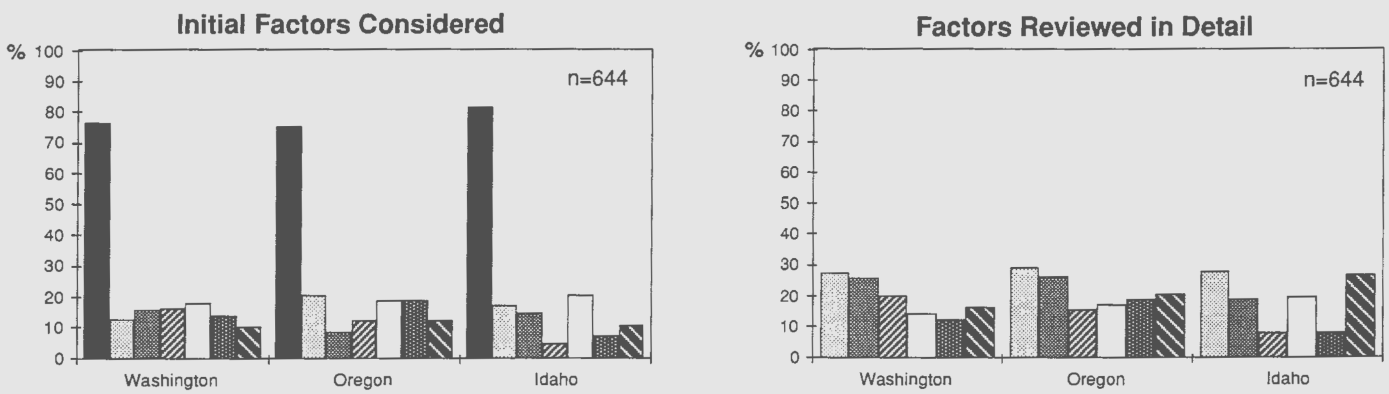
After Residence, Economic Theory Prevails

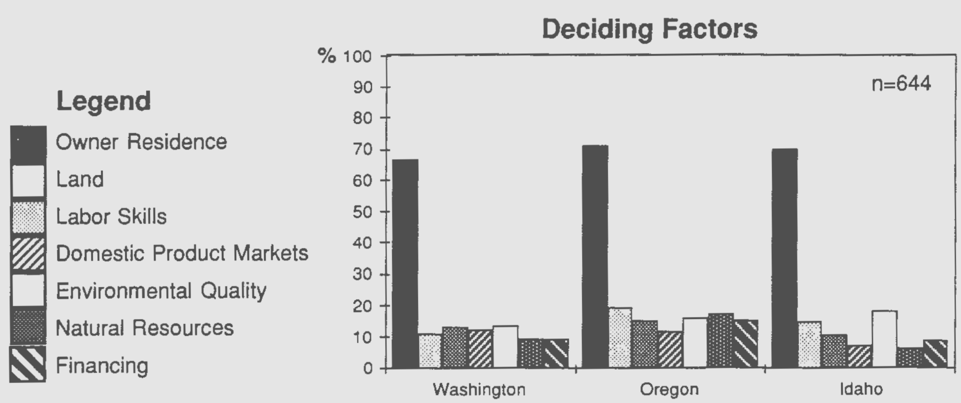
After place of owner residence, the important factors in firms' location decisions clustered in three successive tiers. In the first tier of importance, factors were selected by between 10 and 20 percent of the firms responding to the survey. These normally included land, labor skills, environmental quality, domestic product markets, natural resources, and financing and are shown in the accompanying graphs. Factors falling in the second tier of importance commanded about 5 to 10 percent of the firms responding and factors in the third tier less than 5 percent.

State and local taxes normally clustered in the bottom of the second tier. Their importance to location paled in comparison to owner residence and the first tier locations considerations.

...improving the existing business climate through attention to the first tier concerns of business will be a more effective, long–term strategy ...

Figure 4
Factors in Locational Decision
(percent of total responses by state)





Note: Top responses shown as percent of total survey responses. Owner Residence was not a listed choice for factors reviewed in detail. Respondents could select more than one factor for each question.

Source: Business Location Survey, Washington Research Council, 1989.

The overriding consideration in deciding where to locate is personal: firms locate where the owner lives or wants to live.

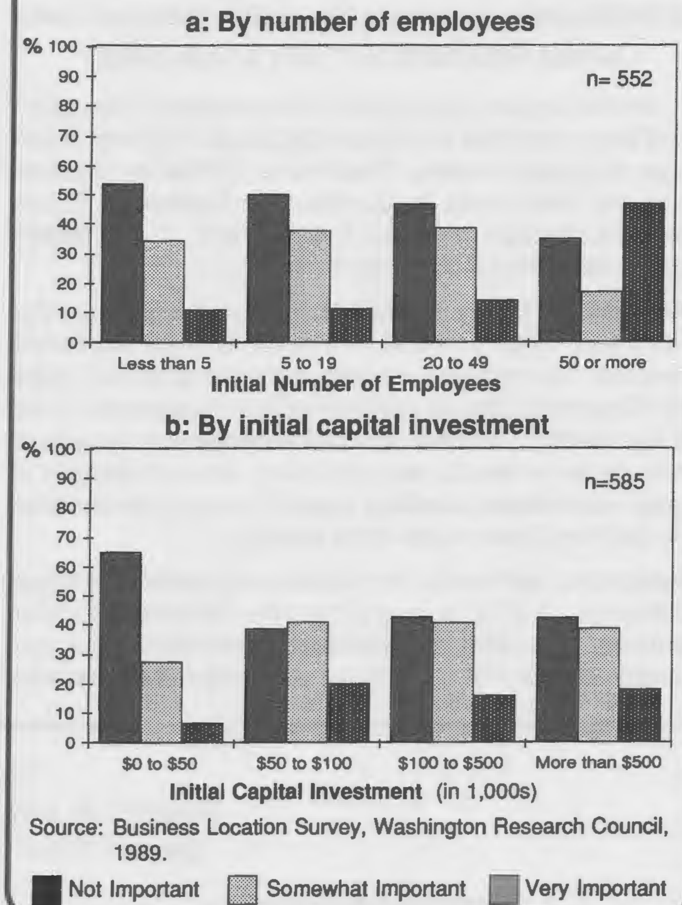
In Washington and Oregon taxes were an important deciding factor to about 5 or 6 percent of the firms responding. Taxes were consistently more important to respondents from Idaho, representing about 16 percent of the firms responding and ranking more closely with factors in the first tier of importance to firms in that state.

Taxes More Important for Larger Firms

Although more than 85 percent of the firm's responding to the survey were not concerned about taxes when deciding where to locate, about 11 percent (71 firms) indicated that they reviewed taxes in detail. This corresponds to the 14 percent (80 firms) that characterized taxes as "very important" to their location decision. The small initial size of most new businesses likely contributed to this result. Survey responses indicate that larger firms (both in number of employees and level of capital investment) cared more about taxes than smaller ones. For example, as illustrated in Figure 5a, taxes were "very important" to about 11 percent of the firms with less than 50 employees. This compares with about 47 percent of the firms with 50 or more employees, which felt taxes were "very important."

Similarly, taxes were very important to about 18 to 20 percent of the firms with capital investment exceeding about $50,000. As shown in Figure 5b, beyond the $50,000 level of investment the importance of taxes does not change much.

Figure 5
Importance of Taxes to Location
(percent of respondents)



Source: Business Location Survey, Washington Research Council, 1989.

Spotlight 1: Dateline Technology

Jack VanderWeerd is a start–up manager in the high–tech field. He was founder and president of Dateline Technology, a Bellevue–based manufacturer of peripheral products for Wang computer systems. Dateline was sold to ADC Corporation in 1987. VanderWeerd has since started Macron, Inc. with plans to enter the CD–ROM publishing market.

For high–tech businesses "location is immaterial. Well developed systems of transportation and communication allow access to partnerships and customers all over the world."

— Jack VanderWeerd , Dateline Technology

According to VanderWeerd, "there are a number of other states in the country with more favorable business climates." But he quickly adds, "I am personally involved in this (location) decision and I want to live in the Puget Sound area." As a result, taxation and the overall business climate fall well down on his list of locational priorities.

Items which did turn his decision were quality of life and access to first–rate higher educational facilities and the engineers they produce. VanderWeerd believes that for high–tech businesses "location is immaterial. Well developed systems of transportation and communication allow access to partnerships and customers all over the world."

On the issue of taxes he said "Assuming the success of my venture, the lack of an income tax in the state of Washington is an incentive for me to remain here." As a venture becomes more and more successful, income increases. It is at this point that he benefits from Washington's tax structure.

At the local level, taxes do make a difference to him. Given the choice between Bellevue (which has a B&O tax) and Redmond (which does not), VanderWeerd said he will probably choose the low–tax community. Adding again, "I live and work in Washington because its where I want to be."

Sales Tax Preferred by Most Businesses

The relative unimportance of taxes to most locational decisions does not indicate, however, that businesses do not hold strong opinions about taxes and the extent to which they impede profitability.

Businesses responding to the survey were asked to indicate the taxes they considered to be "best," "worst," "best tax to raise" and "best tax to eliminate from consideration for adoption or increase" for their business. Respondents were given the opportunity to explain their responses and several representative quotes are highlighted throughout this report.

> ***"All taxes other than end consumer-purchase taxes retard savings and penalize business ... "***
>
> ***— an Oregon wine producer***

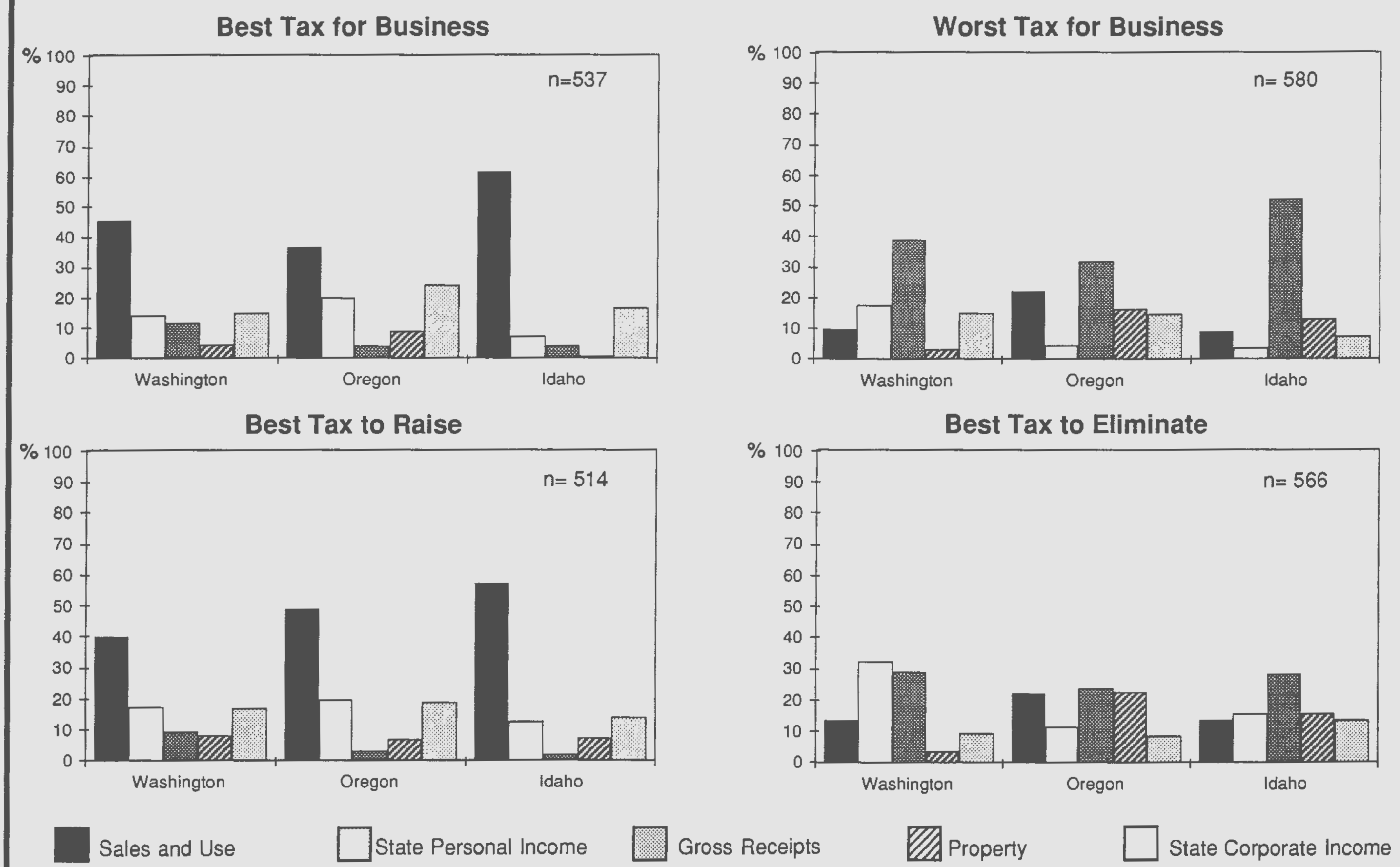
There was no significant variation by state in how businesses felt about different taxes. As shown in Figure 6, the bulk of respondents in each state liked the sales and use tax best. Even in Oregon, which has no sales tax, there was still a healthy margin of preference for sales and use taxes. In Washington 46 percent of the businesses indicated their preference for the sales and use tax, with the personal income, corporate income and gross receipts taxes being preferred by 12 to 15 percent of the respondents. Even so, a Washington print shop owner spoke for many of the smaller group when he said: "I feel funding the state on sales tax alone is unfair to business and unstable to government. The personal income tax adds stability to state (government) income even during recession."

When asked about the best tax to raise if taxes must be raised substantially, businesses predictably demonstrated a similar preference for the sales and use tax, although Washington and Idaho seemed to like it a little less, and Oregon a little more, than they had in concept.

An Idaho trucking company owner felt the sales and use tax "spreads tax burden out evenly." An Oregon wine producer felt more strongly: "All taxes other than end consumer–purchase taxes retard savings and penalize business...."

The picture changed somewhat when asked which taxes were worst for business. Again, however, businesses in the three states agreed. The gross receipts tax was considered

Figure 6
Preferences for Selected Taxes
(percent of total responses by state)



Note: Combinations and other responses are not shown. Source: Business Location Survey, Washington Research Council, 1989.

Spotlight 2: Summation Inc.

Led by start–up manager, James Bloomer, Summation Inc. began business on May 5, 1984. The original business plan was prepared by E.I. du Pont de Nemours of Wilmington, Del. and involved a concept of modular instrumentation — taking various electronic measurement functions and putting them into a single unit.

Bloomer's first task was to decide where to locate the firm. He considered three general locations, including Boston, Northern California and the Pacific Northwest. First and foremost, Summation needed to be in an area where skilled technical personnel, primarily design engineers, could be recruited. Because of Bloomer's knowledge of the Seattle–Bellevue–Everett area labor market, he decided on a location in Woodinville.

"Cash is all important, without it you have to sell more and more of your company just to keep it running."

— James Bloomer, Summation Inc.

Starting with three employees and a capital investment of $1.5 million, Summation grew to more than 50 employees after one year and currently employs more than 85 people.

Conceptually, Bloomer perceives the corporate income tax to be best for his type of business, because he carried a loss for so long. He is quick to add, however, that, "the B&O was never a problem." In the first two years of operation he had no sales and, therefore, no B&O. In the third year, with sales of $2.4 million, his B&O liability totalled about $11,600.

Taxes are just another cost of doing business, according to Bloomer. However, to the extent that they reduce cash they are painful. "Cash is all important," says Bloomer, "without it you have to sell more and more of your company just to keep it running." In this regard he expressed more concern for Washington's sales tax on capital. With about $2 million in capital equipment, he had to raise enough additional capital to cover the 8.1 percent sales tax—about $160,000. "This is painful to a young company," said Bloomer. In order to avoid having to pay all of it up front, he leased as many things as feasible, including land, building and much of his equipment.

the worst tax for 39 percent of the businesses in Washington, 32 percent in Oregon, and 52 percent in Idaho. A Washington household mover summarized the problem with gross receipts taxes best: "We take in a lot of money and put out almost as much in business expenses." However, Larry Kring of Heath Techna (see Spotlight 4) further noted that "the problems with the B&O's effect on unprofitable start–ups has theoretical basis, but the rates are so 'miniscule' that the importance of the point is moot."

When asked which tax should be eliminated from consideration, either for increase or for adoption, business responses changed again. In Washington the personal income tax drew 33 percent of the responses; the gross receipts received 29 percent. In Oregon the sales, gross receipts and property taxes drew similar votes of disapproval. And in Idaho, although gross receipts stayed on top, taxes seemed to be disliked in near equal proportions. Interestingly, the best tax to eliminate from consideration for each state was the tax or taxes not currently being levied.

Table 1

Non–Agricultural Wage and Salary Employment by Industry

1987

	Washington			Oregon			Idaho		
	Number	Percent of total	Percent Change from '78	Number	Percent of total	Percent Change from '78	Number	Percent of total	Percent Change from '78
Total Employment	1,935.5	—	30.3%	1,152.3	—	14.2%	348.5	—	5.3%
Manufacturing	338.6	17.5	18.9	214.3	18.6	(2.2)	58.0	16.6	0.0
Durable	241.0	12.5	19.5	155.9	13.5	(5.6)	29.4	8.4	(9.3)
Non–Durable	97.6	5.0	17.4	58.4	5.1	8.1	28.6	8.2	11.3
Non–Manufacturing	1,596.9	82.5	33.0	938.0	81.4	18.7	290.5	83.4	6.4
TCU	101.5	5.2	21.1	60.5	5.3	6.3	18.6	5.3	(4.6)
FIRE	109.8	5.7	31.8	73.6	6.4	14.6	19.4	5.6	(7.2)
Trade	475.2	24.6	32.8	291.3	25.3	18.6	87.0	25.0	5.8
Services	444.3	23.0	63.0	260.6	22.6	48.5	72.0	20.7	26.3
Others	466.1	24.1	15.5	252.0	21.9	1.2	93.5	26.8	0.0

Source: Washington State Employment Security Department; Oregon Employment Division; Idaho Department of Employment.

Spotlight 3: KJOS Systems Inc.

KJOS Systems Inc. distributes computers and computer peripherals to wholesalers and larger end users. In 1987, it moved to Beaverton, Ore. from Santa Fe Springs, Calif.

From an initial work force of two employees and a capital investment of less than $25,000, the firm has grown to 18 employees and recently opened an additional facility in Bellevue, Wash. KJOS expects to employ 50 or more people in three to five years.

"No tax is 'best,' as far as I'm concerned... they're just another cost of doing business."

— John W. Kjos, KJOS Systems

In deciding where to relocate, John W. Kjos considered both Washington and Oregon. The primary reason the Northwest was considered was that it is where he wants to live: Kjos was raised in Seattle and went to school in Oregon. Labor skills and environmental quality were high on his list of secondary considerations in looking to the Northwest and finally deciding to locate in Oregon.

Kjos reviewed in detail the availability of land, labor skills, environmental quality and financing. The final decision to locate in Oregon turned on the availability of a specific facility in Beaverton.

State and local taxes were not reviewed in detail, nor were they deciding factors in his final decision. "No tax is 'best,' as far as I'm concerned" said Kjos, "... they're just another cost of doing business."

And, as he would with any other business expense, he tries to manage his taxes. "I buy office equipment in Oregon (with no sales tax) and lease to my Washington company (which would otherwise pay sales tax in Washington)," Kjos said. Although he pays sales tax on the monthly capital lease amount, Kjos says he is able to avoid the immediate out-of-pocket expense, which he would otherwise have to pay by purchasing in Washington and paying 8.1 percent sales tax on the purchase price.

Spotlight 4: Heath Techna Aerospace Company

Heath Techna Aerospace Company builds plastic aerospace components which are distributed to several airplane manufacturers as well as airline companies. The firm located in Kent, Wash. in the 1950s and is in the process of building a second plant in Bellingham.

The Kent plant employs about 1,400 people currently and the Bellingham facility will employ about 100 people — 50 new employees and 50 transfers from the Kent plant. Employment at Bellingham is expected to increase by about 100 people a year over the next five years, according to company president, Larry Kring. The Bellingham expansion requires an initial capital investment of $16 million. That means more than $12 million in state and local sales taxes.

"I wanted our firm to be part of the community and to share in the responsibilities...I didn't want the community to feel that it had to buy us, in order to get us to locate."

— Larry Kring, Heath Techna

Asked how he felt about taxes, Kring said he had no strong feelings about any one tax. Taxes were not especially important in his location decision. And he didn't seek any special tax treatment — "I wanted our firm to be part of the community and to share in the responsibilities...I didn't want the community to feel that it had to buy us, in order to get us to locate."

Heath Techna also considered Yakima, Chehalis, and the Longview–Kelso area for its new plant. Important considerations included driving distance from the Kent plant, size of the available labor pool, and "quality of life." The plastics research capability at Western Washington University was especially attractive — many of Heath's employees have graduated from Western's program. However, according to Kring, a talented and trained workforce was difficult to maintain in the Kent area with other companies competing heavily for similar skills.

A quick review was done of taxes, to assure that there were no "show stoppers," like any local sewer or water districts anticipating skyrocketing rates. But the values of people in the Bellingham area became an important factor in the final analysis. There was a commitment to and pride in the community which was very evident, Kring said.

An Idaho real estate broker was representative of the vehemence of many respondents with regard to taxes. He said, "Why can't government be accountable like business. I want all of them (taxes) cut back!" In Washington the personal income tax was the tax to eliminate from consideration. For a specialty wood products manufacturer, the personal income tax "is the most oppressive type of tax that can be levied. The state should cut back on social programs."

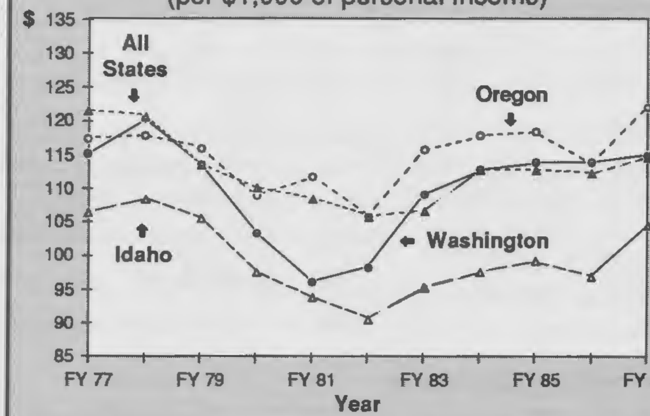
Comparison of Economic and Tax Structure

The Northwest states have demonstrated substantial differences in economic activity and prosperity over the last 10 years. Since 1978, for example, Washington's non-agricultural wage and salary employment has increased 30 percent. Comparable growth in Idaho was 5 percent over this period. Oregon was in the middle with a 14 percent increase.

While Washington has been experiencing an economic boom in recent years, led by Boeing commercial airplane orders, Oregon has been much slower in its economic recovery and Idaho only began climbing out of the recession in the last couple of years.

With a 1988 workforce of about 348,500 people, Idaho has the smallest economy of the three Northwest states. Over the 10–year period shown in Table 1 the decline in durable goods manufacturing and growth in non–durable manufacturing resulted in no change in Idaho's total manufacturing employment. Actual losses occurred in Transportation, Communications and Utilities (TCU) and Finance, Insurance and Real Estate (FIRE). Shrinking employment in mining and other manufacturing sectors, together with drought–related contractions in agriculture since 1986, have coupled with deregulation of major portions of TCU and FIRE to explain most of the declines in these secondary employing sectors. Since the recession of the early 1980s growth in Idaho has concentrated primarily in the manufacturing and services sectors.

Figure 7
State and Local Tax Burden
(per $1,000 of personal Income)



Source: How Washington Compares, Washington Research Council, 1989.

In Oregon the forest products industry, although replacing employees at a fairly rapid rate since its decline in the early 1980s, has not yet regained its 1978 level. With a total of 1,152,300 people employed in non–agricultural sectors, Oregon has the largest concentration of its workforce in manufacturing (about 19 percent) of the three states, most of which is directly related to forest products. Over the last decade, employment in durable goods manufacturing declined by about 6 percent, while economic growth in the balance of Oregon's economy has been moderate, with services (48 percent), trade (19 percent), and FIRE (15 percent) leading the way.

Spotlight 5: Seattle First National Bank, Credit Card Operations

In September of 1988 Seattle First National Bank (Seafirst) decided to move its credit card operations from Seattle to Spokane, Wash. Services include the approval, issuance, and servicing of credit card accounts.

Like Heath Techna, the decision was driven by problems Seafirst was having with attracting and retaining a high quality workforce in the Puget Sound area. And according to Seafirst spokesman, Milt Fitch, Seattle's B&O tax was a contributing factor to the decision to change locations.

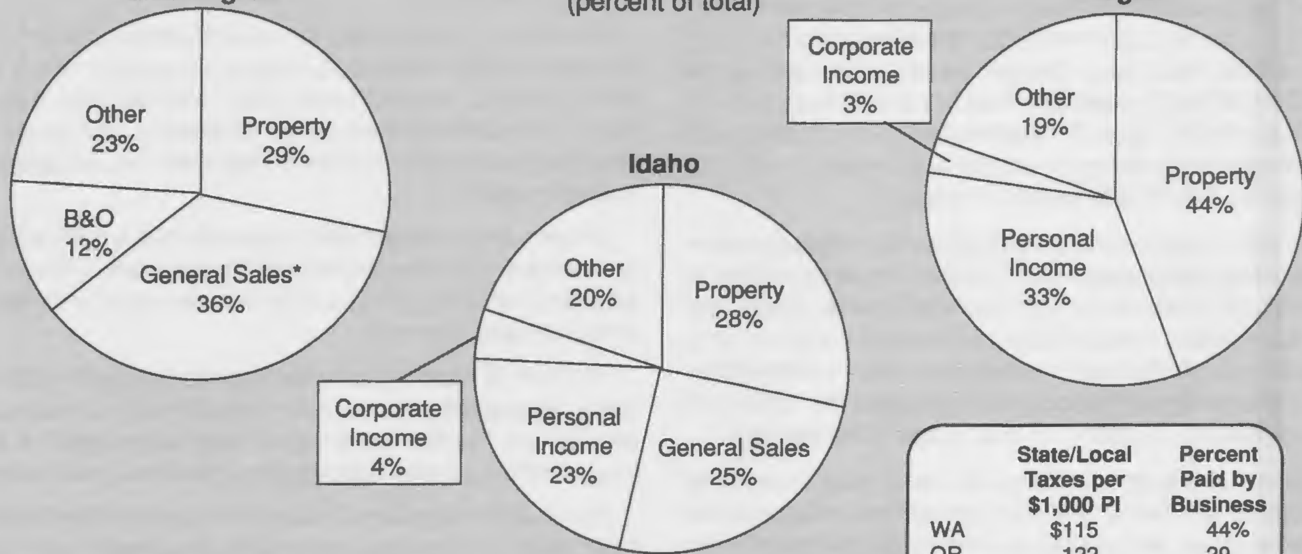
Sites in Seattle, Spokane, Nevada and Oregon were considered. Nevada, which was considered because of its credit card legislation which was designed to attract banks, lacked the stable workforce Seafirst was seeking. Oregon locations were forecast to be growing toward a tight labor market similar to the current situation in Seattle.

In Spokane, Seafirst found the stable workforce it was looking for with an economy which was not expected to boom in the short or long term. And Spokane did not yet have a city B&O tax. Fireman's Fund Insurance and Old National Bank, both financial institutions, had recently moved out of the Spokane area, leaving behind a trained and highly motivated workforce.

In making its decision Seafirst reviewed in detail land, environmental quality, labor skills, the presence of a major university, domestic product markets, transportation linkages, education and training resources, communication services and state and local taxes. And, although other states offered preferable taxing structures and freedom from usury laws, according to Fitch, Seafirst chose the Spokane location because it found an excellent, permanent facility that offered a better work environment, as well as enabled Seafirst to keep the business in its home state.

The move required an initial capital investment of about $6.5 million and the Spokane facility is expected to employ about 350 people, 75 of whom will relocate from Seattle. Seafirst expects growth of about 20 employees per year over the next three to five years.

Figure 8
State and Local Taxes
Fiscal Year 1987
(percent of total)



	State/Local Taxes per $1,000 PI	Percent Paid by Business
WA	$115	44%
OR	122	29
ID	105	33

Sources: Governmental Finances, U.S. Bureau of the Census, 1988. Economic and Revenue Forecast, Revenue Forecast Council, June 1989. Local Government Comparative Statistics, Washington State Auditor's Office, 1989. Interstate Comparison of Business Taxes: State and Local Taxes with an Initial Burden of Business, Jim McIntire, 1988.

In Washington, even in the period from 1978 to 1983 when the economy slowed down substantially, only one sector — durable goods manufacturing — reported employment losses. These losses were related primarily to employment declines in the wood products industry in the early 1980s, which was responding to the effects of general economic recession concurrent with its own industry restructuring.

With fairly brisk recovery since the early 1980s, manufacturing growth over the 10–year period in Washington totalled almost 19 percent and the trade and FIRE sectors grew about 32 percent. The fastest growth sector for Washington, however, was services, which grew 63 percent from 1978 to 1988.

Until the last 12 to 18 months, most of this recovery was felt only in the central Puget Sound area. Outside of the Seattle–Everett–Tacoma area Washington's economy was still stagnant. In these other areas employment fell further, stayed down longer, and has been slower to increase even after turning the corner toward recovery.

The economic climate for our survey of new businesses in the Northwest, then, was generally one of health and optimism for all three states. Boeing continues to break its own records. The wood products industry has completed its restructuring and is again experiencing healthy employment and profits in all three states. And, although Idaho and the balance of Washington outside the Puget Sound area have not yet experienced their full share of economic prosperity, there are positive indications of near–term developments for them, as well.

High on the list are the Boeing and Seafirst expansions to the Spokane area, with a promise of more than 600 new employees to be hired from that labor force. Key Technology has located in Walla Walla with 40 new jobs anticipated. Heath Techna has expanded to Bellingham. And there are others. But probably most promising for Washington is the recognition on the part of resident businesses throughout the Puget Sound area that growth and expansion need to be spread around the state in order to utilize more efficiently the economic resources available throughout the region.

Transportation infrastructure, labor skills, and land availability are among those resources which are reaching maximum capacities in some areas, like central Puget Sound, while remaining plentiful in others.

In Idaho new firms, like Spears, Inc., which manufactures plastic pipe and created about 400 new jobs in Jerome, as well as expansions, like Truss Choice, have added new life to the economy. Agriculture is doing well, due to drought conditions in the Midwest, which have driven up farm prices. Plywood production is at record levels and mining has resumed its prominence in the overall economy. Unemployment is down and state government has revenue surpluses totalling more than 7 percent of its general fund state budget.

State and Local Tax Burden on Business

Businesses in Washington pay a higher share of state and local taxes than businesses in the other two Northwest states. Of a 1987 tax burden of $115 for every $1,000 of state personal income ($1,000 PI), about $50 per $1,000 PI (44 percent of $115) is paid by business initially in Washington.

According to *How Washington Compares*, published annually by the Washington Research Council, these data compare with state and local taxes in Oregon of $122 per $1,000 PI and $105 per $1,000 PI in Idaho. Washington ranked 20th in tax burden, nationally, Oregon ranked 11th, and Idaho ranked 37th of the 50 states and the District of Columbia in FY 87. As illustrated in Figure 7, Washington's overall tax burden has been steadily growing since it hit a 15–year low in FY 81 of $96 per $1,000 PI and a rank of 41st.

These data, however, do not fully reflect the relative burden of taxes felt by businesses in each of the Northwest states. In his *Interstate Comparison of Business Taxes: State and Local Taxes with an Initial Burden of Business*, Jim McIntire, in association with the Institute for Public Policy and Management at University of Washington, estimated the state and local business tax burdens for each state in the country.

According to McIntire, state and local governments in Washington have the highest initial tax burden on businesses of the three states, with almost 44 percent of total taxes being paid by business and a national ranking of 8th. Businesses in Idaho paid about 33 percent of state and local taxes, ranking 29th. Oregon firms were lowest with a business tax burden of 29 percent and a rank of 44th. As a share of state personal income, that means businesses in Washington pay about $50 per $1,000 PI, compared to about $35 per $1,000 PI in Oregon and Idaho.

As shown in Figure 8, the three Northwest states are about as diverse in their state and local tax structures as any three states can be. Washington's state and local tax structure does not include income taxes, personal or corporate and, therefore, relies more heavily on sales and excise taxes than the other states.

Oregon, on the other hand, does not have a retail sales tax and relies more on its property and income taxes. Idaho uses a full array of taxing options, with a tax structure more like that of the national average.

The bulk of Washington's taxes on business, in addition to B&O and property taxes, are collected through the sales and use tax on capital construction and equipment — a tax treatment unusual to Washington and a few other states.

The diverse structure of taxes from state to state make the Northwest a particularly appropriate geographic area within which to test the importance of state and local taxes to business location.

Methodology

This report is based on information obtained through a survey of businesses recently locating to the Pacific Northwest — Washington, Oregon and Idaho. With the help of state employment offices in Washington and Oregon, and Dunn's Market Services for Idaho, confidential random samples of newly locating businesses were drawn and surveys were mailed to more than 3,200 businesses in the three–state area.

Samples were stratified in order to receive adequate responses from three broad employing sectors — durable goods manufacturing, non–durable goods and non–manufacturing. And, although we intended to survey only firms locating after 1986, due to problems in the data bases, about 200 (one–third) responses were from businesses locating prior to 1986. We learned from this group of older businesses that the considerations important to location 10 or 20 years ago are not significantly different to those considerations important today — issues affecting business locations are not transitory. For this reason all 644 responses were retained and used in this analysis.

The survey was mailed to each firm twice. Each mailing included a cover letter and postage–paid return envelope. The survey was directed toward the business owner or chief executive officer.

Of the 3,227 surveys mailed, 644 completed surveys were returned to the Research Council — a response rate of 20 percent. The returns by state were as follows:

State	Surveys Mailed	Surveys Returned	Response Rate
Idaho	608	120	20%
Oregon	1,119	209	19
Washington	1,500	315	21

The surveys specifically identified the state to which they were mailed. In addition to descriptive questions about each firm, the survey explored three levels of decision–making relating to their locational decision — initial factors causing firms to consider the Northwest, factors reviewed in detail, and factors upon which the final decision turned.

Because the focus of the study was the role taxes play in the decision, several questions were asked directly — the importance of taxes in the decision, whether a special review of taxes was done as part of the decision making process, the taxes which were best and worst for the business, the best tax to raise and the tax one would most like to see eliminated.

Statistical analysis of the survey was done using a personal computer version of Statistical Package for the Social Sciences (SPSS) by the Washington Research Council. For additional information on the survey methodology, questionnaire design or survey results, please call or write the Research Council.

Conclusion: Taxes Unimportant to Most NW Business Locations

Taxes are rarely considered by entrepreneurs as they make their initial decision to do business in the Northwest.

The vast majority (about 88 percent) of firms responding to a recent survey of the three Northwest states located their businesses without the assistance of any detailed review of the tax impacts of their location decision. And 86 percent indicated that taxes were either not important at all or only somewhat important to their decision.

Most important to the majority of firms was where the owner of the firm lived or wanted to live. Owner residence was a deciding factor for more than two–thirds of the businesses responding. After owner residence, a first tier of deciding factors, ranging from about 10 to 20 percent of firms responding, included land, labor skills, domestic product markets, environmental quality, natural resources and financing.

In Washington and Oregon taxes fell to the bottom of a second tier of importance as a deciding factor. About 5 to 6 percent of the businesses responding from these two states indicated taxes to be a deciding factor, along with transportation linkages and power. Idaho businesses appeared to be more sensitive to taxes, normally placing them in the first tier of importance as a deciding factor.

Taxes were more important to larger firms. Those firms indicating taxes to be "very important" increased from about 11 percent of firms with initial employment of less than 50 employees to 47 percent for firms with 50 or more employees. Similarly, about 7 percent of the firms with capital investment of less than $50,000 said taxes were very important to their decision, compared to about 20 percent of the firms with capital investment exceeding $50,000.

There was no significant variation between states about how businesses felt about different taxes. Sales taxes were the preferred taxes to raise by more than 40 percent of firms responding in the three states. When asked which tax they would most like to see eliminated, businesses in each state indicated they would most like to eliminate from discussion those taxes not currently being assessed — in Washington the personal income tax; in Oregon the sales and gross receipts taxes; and, in Idaho the gross receipts tax.

These data strongly suggest that tax policy plays a limited role in economic development efforts in the state of Washington and the Northwest. Most of our new businesses are coming from within the state, and do not consider tax policy to be a determining factor in where they locate. The overriding consideration is more personal: firms locate where the owner of the firm lives or wants to live.

Taxes, however, are a business expense. And as they would with any business expense, entrepreneurs try to assure they are receiving their money's worth from their tax dollar. As an entrepreneur's investment grows so does the interest in and ability to give greater attention to all of the costs of doing business, including taxes.

But, taxes do not motivate most location decisions. Chasing smokestacks, or even the latest high–tech manufacturer, for location in Washington is not the most productive focus for state and local economic development efforts. Data from this study indicate that improving the existing business climate through attention to the first tier concerns of Washington's existing businesses will be a more effective long–term strategy for enhancing the state's economic prosperity.

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