

WASHINGTON REMAINS NEAR THE TOP IN BUSINESS TAX BURDEN

BRIEFLY

The Council on State Taxation recently released its sixth annual report comparing businesses tax burden across the 50 states. Washington ranks 14th highest among the states in the effective tax rate on business and 13th for business's share of state and local taxes.

Improvements in the state's ranking since 2002 largely reflect the business cycle rather than a fundamental change in the state's tax competitiveness.

The Council on State Taxation (COST) recently released its sixth annual report comparing businesses tax burden across the 50 states. The report, authored by Robert Cline, Tom Neubig, and Andrew Phillips of Ernst & Young LLP, is a nationwide analysis of business tax burdens in FY 2007, the peak of the business cycle. While they find that the ranking of Washington's business tax burden has improved modestly over the past 5 years, businesses in this state remain among the most highly taxed in the nation.

Where Washington Stands

Robert Cline and colleagues calculate that businesses paid \$14.9 billion in state and local taxes in Washington during FY 2007. Of this, \$7.3 billion was business and occupation tax and sales and use taxes on business purchases; \$3.2 billion was property tax; \$2.0 billion was excise and selective gross receipts taxes; \$1.5 billion was unemployment insurance tax; and \$0.9 billion was other taxes and license fees.

Figures 1a and 1b compare the composition of Washington's business taxes with the national averages.

Cline and colleagues define the effective tax rate on business as the ratio of state and local business taxes to private sector gross state product (GSP). They estimate that the effective tax rate on Washington businesses was 5.8 percent in FY 2007, up from 5.6 percent in FY 2002. Over this 5-year span, however, the average effective state and local tax rate across the country grew from 4.5 to 5.0 percent. As a result, Washington's ranking actually improved from 11th highest in FY 2002 to 14th highest FY 2007. (See Figure 2. In this competition, the further down the ranking list the better.) For FY 2007 effective tax rates ranged from a high of 11.6 percent in Alaska (largely taxes on petroleum) to a low of 3.5 percent in Delaware.

The percentage of state and local taxes paid by business varies significantly from state to state. For FY 2007, Cline and colleagues calculate, businesses paid 51.0 percent of Washington's total state and local taxes and ranked 13th highest among the states for business's tax share. The nationwide average business state and local tax share was 44.1 percent. Alaska was the state with the highest business tax share, 80.8 percent, while Maryland was lowest, 32.2 percent. In FY 2002 Washington's business tax share was 53.2 percent, which ranked 9th highest; the nationwide average was 43.4 percent that year.

Rankings Change Over the Business Cycle

Seemingly, the good news for Washington’s competitiveness is that while the state’s business taxes are high, they have not increased as fast as business taxes in other states, allowing Washington’s ranking to improve. However, as we explain below, our improved rankings largely reflect the business cycle rather than a fundamental improvement in the state’s tax competitiveness.

Over the last five years state and local taxes on business have grown faster than total state and local taxes. Cline and colleagues estimate that state and local tax payments by business grew 43.7 percent from \$401.8 billion FY 2002 to \$577.4 billion in FY 2007, an increase of 43.7 percent. Over the same period total state and local tax receipts increased by 41.4 percent, from \$926.1 million to \$1,309.4 billion. Businesses thus paid 45.8 percent of the increase in state and local taxes between 2002 and 2007. The share of state and local taxes paid by businesses rose from 43.4 percent to 44.1 percent.

Corporate income taxes and personal income taxes levied against non-corporate income account for nearly a quarter of the increase in business’s state and local taxes from FY 2002 to FY 2007.

State and local tax revenue in Washington grew from \$20.5 billion in FY 2002 to \$29.1 billion in FY 2007, an increase of 42.0 percent, slightly more than the national percentage growth. Over the period, state and local taxes paid by Washington businesses went from \$10.9 billion to \$14.9 billion, an increase of 36.2 percent. This percentage growth is lower than the percentage experienced in a number of other states.

Washington ranks 32nd in the percentage increase between FY 2002 and FY 2007 in total state and local government tax revenues, and ranks 43rd for the percent increase in business tax revenues collected during the same period. Nevertheless the proportion of additional state and local revenue contributed by businesses in Washington was identical to the nationwide proportion, 45.8 percent.

The greater business tax revenue growth in other states vis-à-vis Washington is largely the result of income taxes. Nationally, state and local revenue from the economically sensitive income taxes on business income nearly doubled from FY 2002 to FY 2007, as the economy moved from the trough of the business cycle to the peak. Washington, of course, has neither a corporate nor a personal income tax. Nationally, business taxes other than income taxes increased 37.5 percent over the five-year period, nearly the same increase Washington experienced in business taxes overall.

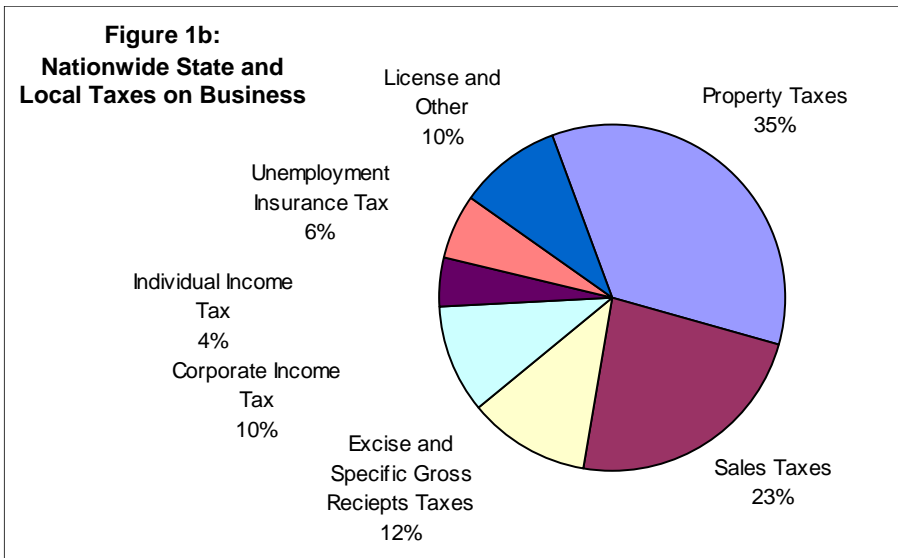
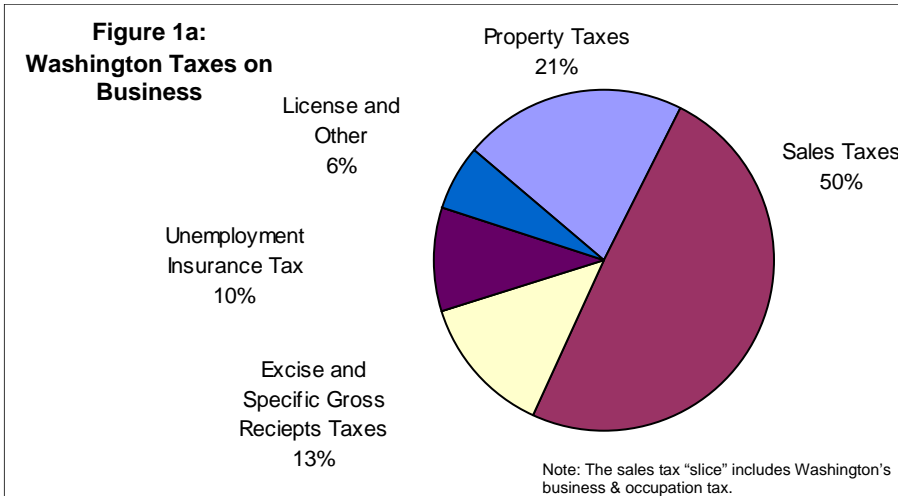


Figure 2: State and Local Business Taxes as Shares of Private Sector GSP and Total Taxes, FY 2007

State	Billions of \$	% of GSP	Rank (%GSP)	Share of Total Taxes	Rank (Share)
Alaska	3.9	11.6%	1	80.8	1
Wyoming	2.4	9.3%	2	73.5	2
Maine	3.1	7.6%	3	48.5	18
North Dakota	1.7	7.4%	4	60.9	4
West Virginia	3.3	7.2%	5	53.1	9
Vermont	1.4	6.8%	6	47.2	20
Montana	1.8	6.5%	7	51.8	10
Louisiana	11.2	6.5%	8	60.8	5
New York	58.6	6.4%	9	42.4	31
Mississippi	4.4	6.3%	10	48.8	16
New Mexico	4.0	6.3%	10	54.4	8
Kansas	5.8	6.1%	12	48.5	18
Rhode Island	2.4	6.1%	13	46.4	23
Oklahoma	6.6	5.8%	14	49.8	14
Washington	14.9	5.8%	14	51.0	13
South Dakota	1.6	5.5%	16	61.9	3
Hawaii	2.4	5.4%	17	37.6	44
Nebraska	3.5	5.4%	17	46.8	21
New Hampshire	2.8	5.4%	17	55.2	7
Arizona	10.4	5.1%	20	48.7	17
Illinois	27.3	5.1%	20	46.8	21
Michigan	17.3	5.1%	20	43.7	29
Pennsylvania	23.4	5.1%	20	42.0	32
Kentucky	6.2	5.0%	24	44.9	27
Texas	48.0	5.0%	24	60.3	6
Wisconsin	10.1	5.0%	24	40.1	39
South Carolina	6.2	5.0%	24	43.4	30
Florida	30.8	4.9%	28	46.2	24
Nevada	5.2	4.9%	28	49.1	15
New Jersey	20.2	4.9%	28	37.0	45
Iowa	5.3	4.8%	31	45.8	25
California	72.9	4.7%	32	41.4	34
Alabama	6.2	4.6%	33	45.2	26
Arkansas	3.7	4.6%	33	38.7	43
Idaho	2.0	4.6%	33	39.7	40
Minnesota	10.0	4.6%	33	40.4	37
Tennessee	9.8	4.6%	33	51.2	12
Massachusetts	13.8	4.5%	38	39.2	41
Ohio	18.7	4.5%	38	41.1	36
Missouri	8.6	4.3%	40	41.3	35
Utah	3.6	4.3%	40	39.1	42
Colorado	8.6	4.2%	42	44.6	28
Georgia	13.9	4.2%	42	41.6	33
Maryland	9.0	4.2%	42	32.2	50
Connecticut	7.4	4.0%	45	34.0	49
Indiana	8.9	4.0%	45	40.2	38
Virginia	12.3	4.0%	45	36.6	47
North Carolina	12.6	3.9%	48	36.9	46
Oregon	5.0	3.8%	49	35.9	48
Delaware	1.9	3.5%	50	51.6	11
Dist. Of Columbia	2.2	3.8%		45.1	
United States	577.4	5.0%		44.1	

As the economy cools, corporate income tax receipts are now falling in a number of states. The Rockefeller Institute reports that for the six months July–December 2007 (the first 6 months of FY 2008) overall state corporate income tax receipts were down 9.2 percent, year-over-year (Dadayan 2008). When COST calculates business tax burdens for FY 2008, Washington is likely to move back up in the rankings.

References

- Dadayan, Lucy and Robert B. Ward. 2008. State Tax Revenue Weakens Still Further, While Costs Rise Sharply. *State Revenue Report Number 71*. Nelson A. Rockefeller Institute of Government, State University of New York, Albany. March.
- Phillips, Andrew, Robert Cline and Thomas Neubig. 2008. Total State and Local Business Taxes: 50-State Estimates for Fiscal Year 2007. Prepared by Ernst & Young LLP's Quantitative Economics and Statistics Practice for the Council on State Taxation. April.