Iowa Fiscal Partnership

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Why does Iowa ignore its own pro-business tax climate?

By Peter Fisher

Every year thousands of new jobs are created in Iowa businesses that expand or build new plants, most without state incentives.

This point is frequently missed in commentary from Governor Terry Branstad's office. In Wednesday's story, "Bolkcom leads charge against Orascom deal," Branstad spokesman Tim Albrecht does it again — suggesting Iowa's "tax and regulatory environment" are not competitive, in particular with regard to property tax. He's wrong.

Such complaints about Iowa's business tax system are puzzling, because businesses get a really good deal here.

We go through this every so often. Now, in the wake of the Orascom giveaway, here they go again.

Business subsidy apologists find it convenient in political debate to cherry pick one feature of a complex tax structure and complain about it, ignoring the total picture. And they deliberately confuse Iowans about the real impact of Iowa's rates for both property taxes and corporate income taxes.

Look at Iowa's total business taxes. A recent study by Ernst and Young for the Council on State Taxation found Iowa's overall state and local taxes on business are lower than average, and that we were tied for 29th among the states — only 20 states had lower taxes. This includes corporate income, individual income, sales, and property taxes falling on businesses of all kinds.

For property taxes, the complaint has little merit because footloose companies are routinely provided large rebates and other incentives through tax increment financing that offset a major share of their property tax bill (as readers of this paper are well aware because of the Von Maur deal and others).

Iowa's corporate income tax is inaccurately criticized because Iowa's top rate is the nation's highest at 12 percent — though no company pays a rate that high on income, because of many adjustments they get to make.

Iowa actually claims very little from corporations through the income tax — in fact, from 2005 to 2009, only 10 states took a smaller share of private-sector output in corporate income taxes.

So, while we may not hear this too often from the governor, Iowa's effective tax rate on businesses makes our state highly competitive with our neighbors. It's Iowa's great secret, told not to residents, but surely whispered to business prospects.

Here's what's behind the secret.

• First, Iowa's corporate income tax applies only to profits from sales in Iowa. So, a company shipping computers or farm equipment or whatever across the border — or overseas — is taxed only on the tiny share of its profits from sales inside Iowa.

• Second, every corporation gets to deduct half of its federal taxes from business profits. Only four other states allow this perk, which reduces the effective rate dramatically even for firms that sell only within Iowa.

And that's not all. Iowa allows multistate companies to transfer profits out of the state — a loophole that Iowa lawmakers have refused to plug — lowering Iowa taxes further.

Research consistently has disproved the myth that tax rates have a big impact on decisions by companies on where to locate. More important are the availability and quality of the labor force, the proximity to materials and markets, transportation and other infrastructure, and the quality of life features, such as a strong educational system, to attract and retain a workforce.

Politicians can rant all they want about tax rates, but businesses with serious leaders have more on their minds. What message do we send them by holding K-12 funding stagnant and cutting back on higher-education funding? Let's turn our efforts to promoting the strengths that make Iowa a good place to live and to grow a business.

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For more information about Iowa business taxes, see this two-page backgrounder: http://www.iowafiscal.org/2011docs/110209-IFP-biztaxes-bgd.pdf