

# **Business Taxes and Costs: A Cross-State Comparison 2003 Update**

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## **Executive Summary of Findings and Policy Recommendations**



Kansas Inc. and  
University of Kansas Policy Research Institute

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The complete report is available online from Kansas Inc.

**Kansas Inc.**  
**632 SW Van Buren, Suite 100**  
**Topeka, Kansas 66603**  
**785-296-1460**  
**<http://www.kansasinc.org>**  
**[ksinc@ink.org](mailto:ksinc@ink.org)**

Since 1987 and reaffirmed in 2001, a strategic goal for Kansas economic development has been to achieve tax and cost competitiveness within the region. In other words, a level of taxation that is neutral as a location and retention factor coupled with superior quality public services.

## **REPORT CONCLUSIONS**

- Within a region historically identified as including Kansas' chief competitors for economic growth (surrounding states) Kansas has achieved tax neutrality.
- Kansas also has a competitive business cost climate. Labor costs are in the mid-range for the region, industrial gas prices are well below the regional average, industrial electricity prices are approximately equal to the national average, and land costs are well below the national average.
- Given lower business costs and neutral taxation, Kansas has a competitive overall business tax and cost structure for both newly recruited (those able to take advantage of all economic development incentives) and existing firms. Different industries were analyzed ranging from capital-intensive manufacturing to research and development firms.
- The overall total measured costs of doing business in Kansas are average to below average for the region in every industry examined and for both mature firms as well as newly established or locating firms.
- While neither modeled nor examined specifically, given the competitiveness of Kansas in the immediate region and the region's general lower cost of living, it may be inferred that from a *total cost* of doing business, Kansas is positioned to compete nationally for business growth.

## **KANSAS INC. RECOMMENDATIONS**

1. The conclusions suggest that to insure ongoing competitiveness in the region currently *no major overhaul* is required of the tax system in Kansas. They do not suggest Kansas should sit back and be self-satisfied. Economic development for both retention and recruitment requires ongoing vigilance and imagination.
2. While no major tax changes are recommended, from a proactive standpoint policy-makers should take full advantage of information communicated by citizens and business owners participating in the seven regional Prosperity Summits. This statewide input has been incorporated in the Economic Revitalization Plan to address business needs and issues.
3. Competition has increasingly expanded outside the six-state region into national and global markets. Ongoing attention needs to focus on and be responsive to policy innovation in other states and the challenges communicated by the citizens and business community of Kansas.
4. Finally, Kansas Inc. asks leadership to *hold us accountable* in the future to monitor other states' tax and business policy developments. Kansas Inc. will then deliver an annual assessment of the state taxes and costs structure and present options that will insure ongoing competitiveness for economic growth.

Besides this monitoring and reporting function, Kansas Inc. will work to insure that the business cost structure is addressed from a proactive standpoint, so that the state will be seen as a "policy leader."

## REPORT SUMMARY

The levels of taxation and costs in a state are key factors for businesses making decisions to locate, relocate, or expand operations. At the same time, Kansas business leaders and economic development advocates have recognized the importance of quality public service and for adequate funding for the public sector.

The report focuses on the structure of state and local business taxes, tax incentives, and operational costs, from the point of view of the effects on economic development, and especially the location of potentially mobile firms. The study compares Kansas with five nearby states (Colorado, Iowa, Missouri, Nebraska and Oklahoma) and considers the following taxes and costs and their impact on business profits:

### **State and local taxes and tax-incentives**

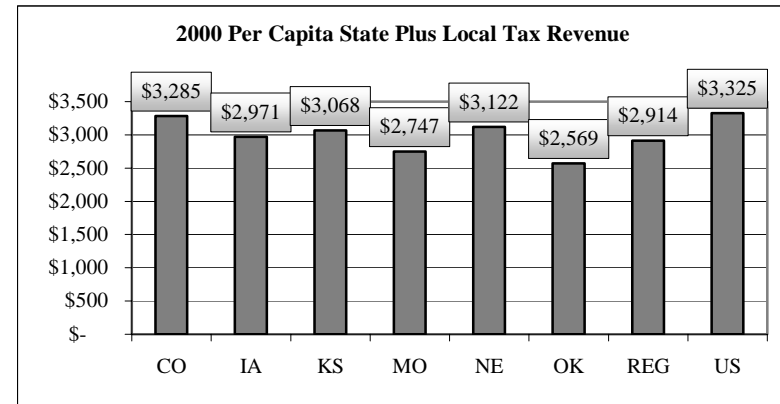
- Corporate income taxes
- Property taxes
  - Commercial/ industrial real estate
  - Business equipment and machinery
- Labor taxes
  - Unemployment insurance
  - Workers compensation
- Sales taxes
  - Capital expenditures
  - Business inputs
- Federal corporate income tax and offset

### **Non-tax costs**

- Measure cost variations: wage rates, electricity and gas rates and real estate
- Costs assumed constant: cost of capital (except taxes), materials, transportation to market, and intermediate products

## TAX COMPARISONS

Per capita tax collections are one indicator of the level of taxation. The states in this region fall into two groups with respect to tax collections. The higher taxed states in this region (Colorado, Nebraska, Kansas, and Iowa) collected revenue ranging from about \$2,970 to \$3,300 per capita, while the lower taxed states (Missouri and Oklahoma) collected less than \$2,750 (see chart).



Overall, Kansas tax collections amounted \$3,068 per capita, which was higher than the regional average of \$2,914, but almost 8% lower than the U.S. average of \$3,325.

The overall level of taxation can balance out the effect of specific high and low taxes. Oklahoma at \$2,589 collects the lowest per capita tax revenue in the region. However, if an analysis considered only the maximum state and local sales tax rate, at 10.5%, Oklahoma could be labeled the least tax friendly state.

A similar example where Kansas is concerned is with property taxes. Relative to the region Kansas is one of the higher taxing states. However, the mix of other tax levels places Kansas at or near the average for the region, diminishing the impact of property taxes on total state and local per capita tax revenue.

## NON-TAX COST COMPARISONS

<b>Location</b>	<b><u>2001</u> Average annual wages</b>	<b><u>2003</u> Commercial electricity rates (cents per kwh)</b>	<b><u>2003</u> Industrial electricity rates (cents per kwh)</b>	<b><u>2003</u> Construc- tion cost index</b>	<b><u>2003</u> Weighted average land (price per sq foot)</b>
<b>Colorado</b>	\$37,894	6.4	4.9	0.93	3.00
<b>Iowa</b>	\$28,007	6.7	4.2	0.89	1.11
<b>Kansas</b>	\$30,161	6.5	4.7	0.86	2.00
<b>Missouri</b>	\$32,208	5.9	4.4	0.97	3.00
<b>Nebraska</b>	\$28,145	5.6	4.1	0.87	2.11
<b>Oklahoma</b>	\$27,187	6.8	4.8	0.82	n/a
<b>U.S.</b>	\$35,862	8.1	4.9	1.00	4.06

Taxes are only one of the cost factors that influence a firm's decision to stay or to locate. Non-tax business costs can have an even greater impact on business profits than taxes. Direct and indirect labor costs represent in nearly every industry the majority of costs for a business.

The table above shows that in general; Kansas offers a competitive business cost climate. Labor costs are in the mid-range for the region and are much lower than the nation. Kansas has one of the lowest construction costs for the region and is well below the national average. Land costs throughout the region are well below the national average.

## HOW COMPETITIVE IS KANSAS?

Accounting for the total costs of doing business (taxes, labor land, etc.) in each state in the region, a simulation model was created. For example: profits for newly located Kansas firms in high-capital intensive manufacturing, profits would be about 4.8% higher than the region's average profit level. Colorado has the lowest modeled profits, 17.5% below the regional average. Iowa has the highest profits, 10.4% above the regional average.

It is important to note that being a lower cost and higher profit state does not necessarily translate into higher growth rates. From 1993 to 2002, Colorado the state with the highest taxes and costs had private employment increases of 32.8%. Missouri frequently represented as a low cost state that Kansas competes directly with had private employment growth of just over 12%. Kansas had private sector employment growth of 20.2% greater than both the nation and the other states in the region.

## A MESSAGE FROM KANSAS INC.

This study looks at the overall taxes and costs of conducting business in each state in the region for a selected group of attractive industries. Kansas has, for now, neutralized the issue of overall taxation as a location factor. It does not address specific tax issues that could make individual companies or industries more competitive, and improve the competitiveness of Kansas.

Specific industries could benefit from changes to the tax structures that impact them at disproportionately higher levels (i.e. sales taxes on custom software). Although Kansas is at or near the average for overall levels of taxation in the region, this does not suggest a "do nothing" strategy. Other states continue to respond to competitive challenges and Kansas must do so as well. In addition to the monitoring recommendation, Kansas Inc. will focus ongoing research efforts on reviewing property taxes and corporate income taxes.

**Average vs. Excellent:** Importantly, the desire to be average in terms of our overall tax structure should not be viewed as the desire to be average in economic development and job creation. Kansas has a rich history of innovation and entrepreneurial spirit that needs to be continued and supported.