

## **Pollina Corporate Real Estate, Inc.**

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### **U.S. is number one...with the highest corporate income tax rate in the world!**

Corporate tax rate is considered one of the most important site selection factors for one simple reason: it has become a significant part of the debate by companies relative to whether to stay in the United States or move offshore. If the economic development communities, states, and federal government do not provide companies with corporate tax assistance, among other incentives, then companies have little choice than to look for a new community, state, or country that will provide such assistance. In today's global competition, companies are struggling to find every advantage they can to stay profitable.

Not only is the U.S. encouraging companies to move offshore by the way we have structured our tax code, but we are trying to tax them at home to the point that they must move offshore. The Tax Foundation released a study in November 2005 that showed that the U.S. now has the highest overall corporate income tax rate (39.4 percent combined federal and sub-federal) of all countries in the Organization for Economic Cooperation and Development (OECD). Japan at 39.0 percent and Germany at 38.9 percent are ranked second and third with the average for all OECD countries being 29.2 percent. The federal rate would need to be reduced to 25 percent, which when coupled with state rates would then approach the OECD average.

The Pollina Corporate Top 10 Pro-Business States Study finds that, in spite of a 3.7 percent growth in Gross Domestic Product for 2005, many Americans are still unemployed and a growing number are underemployed. Off-shoring of the nation's high-tech and manufacturing jobs is continuing at a rate that is growing in intensity, and yet the federal government and many state governments continue to offer little or no assistance to business to promote job growth.

Today, if a job is relocated out of a state, it is more likely to be moved offshore than to another state. To understand the importance of each state's economic development efforts one needs a clear understanding of the nation's economic situation and how it ties into international economics. In the 21st Century, if communities do not have a clear understanding of how their economy relates to their state and in turn their state's relationship to the national economy and the international economic system, their economic development efforts are proceeding with at least one eye closed.

Current economic-development trends are not promising for the U.S. Today, manufacturing jobs in the U.S. continue a rapid exodus offshore, and professional, scientific, technical service and corporate management jobs are leaving the U.S. at a rate that is higher than the nation's population growth. Certainly these trends are not in

keeping with a nation that would like to consider itself a technological leader. There are some bright spots, represented by those states that really understand the national and especially the international competition. These states are making the effort to keep their existing jobs and to attract new employers. We are beginning to see, albeit at a slow rate, a spreading of efforts by enlightened state political leaders.

There are three principal reasons driving the off shoring trend. First, an increasing share of work can be digitized or conducted by telephone in places like Bangalore, India, making these locations functionally as close as the office next door. Second, wages in low-cost developing nations are on an average 20 percent of U.S. wages. Third, many low-wage, low-cost nations, such as China and India, have developed the infrastructure, educational systems, skilled workforce and business climate to make themselves attractive to the U.S. and other countries' multinational corporations. While other nations are making themselves more attractive places to do business, the U.S. has behaved like many of its states – either standing still, allowing others to pass them by, or in the worst case, making themselves less attractive.

The differential in wages is the primary, but not the only reason U.S. and Western European corporations choose to move their operations to Asia, Latin America or Central and Eastern Europe. While these foreign governments are not without fault, and there are issues in some countries of political and economic instability and corruption, relocation or off shoring may make better economic sense for some U.S. companies than dealing with governments that regulate virtually every aspect of business; especially if there is a wide differential in wages. It is not just federal agencies, but also state and local governments, that place hurdles in the path of economic development. These hurdles often take the form of additional taxes (i.e. real estate, income, inventory, sales, and unitary taxes). Add to these taxes development fees, tap on fees, and permitting fees and you can see why companies are placing corporate income taxes as a highly critical site selection factor.

In spite of five years of tax cutting legislation, corporate income taxes have remained unchanged. While the U.S. has stagnated, there has been a world-wide wave of corporate income tax reduction that is still underway. How can we expect to keep our existing employers, much less attract new employers or expect companies to choose the U.S. for expansion of existing facilities, when we have chosen to tax them higher than any other nation? Other nations understand this most basic economic concept and have taken the necessary steps to be more competitive. Yet we have not reduced corporate taxes in 20 years.

In summary, while businesses are leaving the US in record numbers, for those companies that choose to grow within the US, state corporate income tax rates are very important in the site selection process. State business tax rates can vary wildly between zero and as much as 9.99%. This is not an insignificant amount of additional cost over and above the Federal corporate income tax to be born by a corporation. Provided that a company is not bound to a certain geographic area of the US for other economic reasons, a company expanding in the US will consider the additional annual costs imparted by the state corporate income tax rate. Therefore, to remain competitive, states must either reduce the corporate income tax rate or offer other incentives to equalize

their competitive disadvantage as compared to states with low or zero corporate income tax rates.

**Sources:**

1. Tax Foundation – 2005 The State Business Tax Climate Index
2. Pollina Corporate Top 10 Pro-Business States for 2006

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