California's business tax burden no heavier than average

It's a common refrain whenever executives gather: California is tough on business, putting companies here at a competitive disadvantage.

It came up again this month during an economic outlook conference at the Citizens Business Bank Arena in Ontario, where a discussion on the real estate market detoured into gripes about how high taxes and fees make California a terrible place to do business, triggering hearty applause from the audience of local business leaders.

"Corporate taxes, fees to do business — they all add up," developer Robert J. Lowe, one of the panelists, explained later. "It encourages companies to relocate to other locations where taxes are lower."

But for all the bellyaching, at least one of the millstones on business — taxes — is not particularly heavy compared with other states, data show. What's more, the share of state taxes paid by corporations has been shrinking steadily over the years, shifting more of the load to individuals and smaller businesses.

California takes about 4.7% of what a business produces in taxes — which happens to be the national average. The government take is higher in Alaska (13.8%), New York (5.5%) and Florida (5.3%). Even Texas, known for rolling out the red carpet for business, pocketed more than California — 4.9%.

That's according to an annual study of the tax burdens in all 50 states by the Council on State Taxation, a business-friendly group led by senior executives of Chevron Corp., General Electric Co. and other major corporations.

"California is pretty middle-of-the-pack when it comes to business taxes," said Joseph R. Crosby, the organization's senior director of policy.

Although the state's corporate income tax rate — 8.84% — is among the higher in the nation, its bite is diminished by various tax credits and other measures that have been adopted over the years, including:

• One of the most generous research-and-development tax credits in the nation, allowing businesses to deduct 15% of the amount they increase their R&D funding over a base level. The national median is 6.5%, according to Yonghong Wu of the University of Illinois at Chicago.

• Proposition 13, the 1978 initiative that limits property tax increases to 1% a year until properties are sold, when they are reassessed at the market value. This has slowly shifted the property tax burden from businesses to homeowners, since commercial real estate changes hands less often than residential.

• No extraction tax for oil, making California unique among major oil-producing states. Last year, Louisiana got $$606 million in severance tax revenues and Texas received $$884 million.

• A system that assesses businesses at the same tax rate, whether they are Google Inc., which pulled in $$6.5 billion last year, or a small-time outfit that makes $$100,000 a year. Many states require bigger businesses to pay higher rates.

"A lot of the tax credits are given to larger business, and frankly, individuals and medium- and smaller-sized business have to pay higher tax rates," state Controller John Chiang said at a recent Milken Institute conference.

Big corporations, with their squadrons of lobbyists, public relations specialists and attorneys, have been most adept at winning tax breaks and then exploiting them to maximum advantage, critics say.

Hewlett-Packard Co., for example, was granted a $$13-million sales tax refund in 2005, a year it made $$2.5 billion in profit, even though HP had previously used tax credits to erase its income tax liability for the years covered by the sales tax refund.

"Corporations have the best minds in the legal profession working on this, and state and local governments are basically outgunned," said Jean Ross, executive director of the nonprofit California Budget Project.

The state's business tax structure has emerged as a major battlefield in the Nov. 2 election. Proposition 24, backed by public employee unions and the League of Women Voters, would repeal business tax changes approved by the Legislature in 2008 and 2009.

One of these changes, set to take effect Jan. 1, allows businesses to choose between two formulas to determine their income tax, which could mean millions of dollars in tax savings. For example, a California firm that makes $$10 million a year but has only 20% of its sales in California could pay 60% less in taxes with this new law, the state's nonpartisan Legislative Analyst's Office said.

Opponents, including the California Chamber of Commerce and the California Manufacturers and Technology Assn., contend that passage could lead to job losses.

"We have high taxes across the board: income taxes, business taxes, sales taxes on manufacturing equipment," said Scott Macdonald, a spokesman for the No on 24 campaign.

But business leaders aren't unanimously opposed to the measure.

Rob Kerth, president of the North Sacramento Chamber of Commerce, points out that the $$1.3 billion in tax breaks that would be undone by Proposition 24 would largely benefit big corporations — and provide nothing for the portable ice rink company he owns.

It's not lost on Kerth and others that the state is struggling through chronic budget shortfalls — forcing spending cuts to schools, healthcare, parks and other programs — at a time when many of California's biggest companies are minting money.

Just this month, Google reported $$2.2 billion in profit for the three months ended Sept. 30. Days later, Apple Inc. said it made $$4.3 billion in profit.

"It's further unbalancing the playing field," Kerth said. "It lets people out of paying their fair share and makes the rest of us pay more."

Business groups contend that the state should strive to keep taxes on business as low as possible, saying the less they pay in taxes, the more they can spend to hire people and create jobs.

"There's something wonderful and encouraging that you can have companies like Google and others who can still be making money during the worst economic downturn since the Depression," said Loren Kaye, president of the California Foundation for Commerce and Education.

But corporations now shoulder less of the state's tax burden than they did a generation ago, according to a Times analysis of state Franchise Tax Board data. The analysis found that corporations reporting net income paid 5.4% of their state income in taxes in 2008, the most recent year available, down from 9.7% in 1981.

The analysis looked at the amount of taxes assessed on all corporations in California in each year, and calculated it as a percentage of income corporations reported to the Franchise Tax Board that year.

The trend can also be seen in the share of state tax revenue collected from corporations versus individuals over time. Corporations contributed 16% of the state's general fund in 1977-78, but that's now down to 11%. Personal income taxes, meanwhile, have grown to 53% of general fund revenue, from 36% in 1977-78.

The decline in the share of corporate income taxes is partly explained by companies changing their structures to "S" corporations and limited liability corporations, said Justin Garosi of the Legislative Analyst's Office. But it's also a result of companies taking better advantage of the tax code to reduce what they pay.

"Companies can play games to try to shift their income around," he said.

Businesses have also benefited more from Proposition 13 than homeowners. A study in May by the California Tax Reform Assn. found that residential property owners provided 53% of the property tax revenue for Los Angeles County in 1975, but now shoulder 69% of the tax burden.

California businesses also get a big break from the state's research-and-development tax credit adopted in 1986. The credit allows companies that boost their R&D spending to claim a tax credit of 15% of that increase. If a company spends $$2 million more, for example, it gets a $$300,000 credit.

Chip maker Intel Corp. is able to generate an R&D tax credit of $$60 million a year, according to spokesman Chuck Mulloy. Some might argue Intel doesn't need the credit — it recently reported a third-quarter profit of $$3 billion — but Mulloy makes no apologies, saying it's "the only incentive tax left in California."

The credit was worth $$1.2 billion to companies operating in California in 2008, the most recent year for which data are available, state officials say. But the state does not require individual companies to disclose how much they received in that or other tax credits.

This summer the state Legislature approved AB 2666, which would have required the state to reveal what it awards publicly traded corporations in tax breaks.

"There are businesses that do pay their share, but it would seem that there are other businesses that don't," said Assemblywoman Nancy Skinner (D-Berkeley), the bill's sponsor. "How do we determine which without some kind of transparency?"

Opponents said that it would discourage business investment, and Gov. Arnold Schwarzenegger vetoed it.

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Story posted 2010.10.24 at 06:14 AM PDT