Nevada’s 2015 Proposal for Business License Fees

Analysis prepared for Las Vegas Global Economic Alliance

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Executive Summary

The proposal for a business license fee is to add a revenue-based assessment on businesses in Nevada. Our analysis shows a potential decrease in GSP of $14.6 million – a negligible impact for an economy the size of Nevada’s. The total change in demand for goods and services produced by Nevada businesses would be about 0.5% -- also relatively insignificant. The BLF would shift some of the tax burden on businesses to revenue and away from payroll, resulting in a small but positive impact on jobs in the state. There could also be a small impact on the growth of new business investment though this is harder to quantify. We demonstrate that common criticisms of “gross receipts taxes” and “corporate income taxes” are largely avoided in the proposed BLF. Yet, the BLF legislation should be carefully structured as a “fee” to avoid the many legal challenges and complications that otherwise can result for multi-state businesses. Once these accommodations are resolved, there will be minimal impact on economic development in Nevada from increasing the business license fee as proposed.

Introduction

On January 15, 2015, Nevada Governor Sandoval announced a proposal to generate additional state revenues with a business license fee (BLF). Details were released at the end of January for a structure using multiple tiers of company revenues and varying rates by industry. Although comparisons and calculations were made using the State of Texas tax collections, the proposed structure does not appear to parallel the Texas tax law. Indeed, Nevada may benefit from the experience gained in Texas while avoiding some of the pitfalls.

![Industrial Structure Comparison](image)

Source: Author’s calculation using data from the Bureau of Economic Analysis

The documents provided by the Governor’s office specifically and importantly state that it is the intention for the BLF to provide “a stable source of revenue for needed K-12 education programs.” The issue of funding for education in Nevada was driven to the forefront by the confluence of two events:
the poor performance of the state’s education system in national rankings and severe pressure on state finances resulting from the 2007-2009 Great Recession. Leading up to this, Nevada’s population growth, enrollment growth in public schools and intra-census population gains ranked near the top of all states (NEA 2013). Meanwhile, only Florida and Tennessee spend less per resident and only Arizona and Utah spend less per student on education. The burden of paying for education falls more heavily on local governments in Nevada than in 44 of the 50 states (U.S. Department of Education 2014).

Though Nevada ranks high in some rankings of “best places for business,” it scores low in others – in no small part due to failings in the education system. ¹ Ranking Nevada 29th in the nation in 2013, CNBC wrote that “the state’s education system remains among the worst in the country.” Improving education – which would improve the state’s human capital resources – could improve business investment in the future.

Our focus throughout this report will be the impact on business investment and jobs (economic development) in Nevada. We begin our analysis with a general discussion of business taxes. Next, we bring forward some important considerations for the drafting of legislation that have the potential to impact business activity and state revenues. We then present the heart of our analysis, where we make specific calculations for the general economy and for each of several industry clusters important to economic development in Nevada. Finally, we summarize the specific enhancements that could improve the efficacy and efficiency of the Business License Fee proposal.

**Business Taxes in General**

The total state and local tax burden on businesses in Nevada comes largely from taxes on business property and general sales taxes (Phillips, Cline, and Neubig 2008; Ernst & Young 2014). To maintain government services during and after the Great Recession, Nevada is one of just 10 states that raised revenues by at least 5% over prior year’s collections (Johnson, Collins and Singham 2010). This was accomplished in ways that directly impacted the cost of doing business in Nevada:

- Increasing the general sales tax (one of eight states) from 6.5% to 6.85%.
- Raising business payroll tax on larger companies while lowering it on smaller ones, generating $346 million in new revenue in the fiscal 2010-2011 biennium.
- Raising particularly large amounts of new revenues from “other” taxes and fees (one of three states). Nevada increased hotel taxes (raised $110 million), business license fees ($31 million) and the car rental tax.

¹ The Tax Foundation (2015) ranks Nevada the #3 state for doing business while Forbes (2014) ranks Nevada 34th. For another ranking example, see Ball State (2014).
It is important to recognize that these measures – along with any cost reductions – were not undertaken to expand government or increase education spending.\(^2\) They were done to balance spending with revenues. If all revenue from the general fund were allocated proportionally to the education fund, we estimate that the Modified Business Tax (MBT) contributes less than 5% of education funding.\(^3\)

**Effect on New Business Investment**

The impact of business tax changes on the economy can be measured as changes in business investment. These changes result from the tax raising the cost of capital (Verdugo 2006).\(^4\) The percentage change in investment as a ratio to the percentage change in the cost of investing is known as “elasticity.” A measure of elasticity with an absolute value less than 1 indicates that the percentage change in investment would be smaller than the percentage change in taxes (“inelastic”). Discouraging investment is a concern not only of economic development but because it could result in a decrease in state collections. When business investment is less responsive to changes in taxes, however, it is possible for total tax collections to rise even if total investment falls because the decrease in investment is proportionally smaller than the increase in taxes.

The importance of elasticity depends, to a large extent, on the definition of the market under analysis. The things that make Nevada unique are its source of advantage by comparison over other states – things like climate and natural resources. This definition is important because another determinant of the impact of taxes on business investment is the availability of alternatives (“substitutes”). For many operating businesses there are few alternatives to location in Nevada – casinos and mining are notable examples. Nevada has specific advantages in the leisure and hospitality industry. These industries are established to the point where firms locating in Nevada gain advantages in the availability of workers with a particular set of skills, the opportunity to interact with other firms in the same industry, and proximity to suppliers and customers who understand their business needs. These *external economies* serve to lower investment costs by increasing the size of the industry and can offset the potential negative effect of increasing business taxes.

**Effect on jobs**

There is a relatively small effect on jobs from taxes – the larger impact comes from general economic conditions. Even separating small businesses from large ones, job growth in Nevada did not fall with the implementation of the Modified Business Tax but it did react significantly to the 2001 and 2008 recessions.\(^5\) In the case of the BLF, the effect could be to reduce the weight (“apportionment”) on payroll (collected through the Modified Business Tax) by 4%. The result would be a small but positive impact on jobs (about 0.24%).\(^6\)

\(^2\) See the Fiscal Analysis Division Forecast for the Economic Forum for a comprehensive list of budget and spending changes in Nevada since the Great Recession.

\(^3\) After sales (51%), property (19%) and gaming taxes (15%), all other taxes collected by the state represent only 15% of budget revenue. The MBT was 12.3% of Total General Fund Revenues in Nevada FY2013 (Fiscal Analysis Division).

\(^4\) Business investment is typically measured as changes in five asset categories: machinery and equipment, buildings and facilities, land, transportation equipment, and other assets.

\(^5\) For details on this, see our 2014 Analysis on MBT. We also show that annual economic growth after the 2001 recession was not different between states that did and did not significantly raise taxes (CBPP.org, Table 1 in Johnson, Collins and Singham, 2010).

\(^6\) Goolsbee and Maydew (2000) demonstrate that these jobs tend to come in manufacturing, which includes part of two industry clusters being targeted by LVGEA (see table in appendix for a cross-walk of industries).
With these points in mind, we review some general criticisms of corporate income taxes (CIT) in the context of how the Governor’s proposal differs. The criticisms are applied to gross revenue taxes and margin taxes, too. We discuss each of these in the context of the proposed BLF before addressing the question of “tax pyramiding” which is levied specifically on gross receipts and margin taxes.

Important Considerations

Criticisms of Corporate Taxes

I. Collections are volatile and pro-cyclical
There has been a decades-long move towards businesses operating without the traditional C-corporation designation, resulting in a 30-year decline in CIT collections in the US. Federal CIT collections provide less than 10% of federal revenues. Gross revenue taxes avoid some of the volatility associated with taxes on net income by taxing total revenue, which fluctuates much less (Barbe 2013). The BLF proposal avoids these CIT problems by basing the fee on “most types of business receipts” with little exclusion and by extending the fee to all business forms. Similar to the structure used successfully in Delaware for more than 100 years, the BLF also has a minimum and maximum fee, which brackets the highs and lows of collections.

II. Conformity to Federal tax system creates problems
Changes in federal tax rules can reduce state collections without the states taking any action. Following the recession in the early 2000’s, many states began the process of decoupling from the Internal Revenue Code because legislation like the Job Creation and Workers Assistance Act of 2002 reduced Federal corporate tax payments – which resulted in lower collections in the states (Bruce 2011). In addition to making state collections volatile, this also makes state CIT revenue difficult to predict. The BLF legislation would do well to remain silent on using the federal interpretation of rules when calculating payments. One complaint levied in Texas about the structure of their franchise or margin tax is that it did not allow taxpayers to amend state returns after an IRS audit and/or an adjustment to a federal tax obligation.

III. Nexus relies on unresolved court cases
Many state rules rely on an economic “nexus” to establish the basis for collecting taxes from out of state (“foreign”) businesses. The nexus is an economic presence like having license agreements with affiliates or making efforts to generate sales (versus having a physical presence in the state). It also seeks to create combined reporting requirements, so that all related entities must file together. This captures income from spun-off operating segments or other affiliates. Some state courts have agreed that such economic contacts are sufficient to create the required nexus for taxes (other than sales and use taxes

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7 For a more detailed discussion on this point, see our section Critique of Corporate Income Tax in the MBT AB514 analysis. Our focus here is on responding to criticisms of the BLF as a corporate income tax, which it is not.
which require a physical presence). However, the Supreme Court of the United States has not reviewed any of these cases. It could remain for the State of Nevada to pursue collections in the courts.\textsuperscript{8}

The BLF proposal suggests a requirement for combined reporting to calculate the fee obligation. This might reduce the number of small businesses in the state if some are folded back into corporate structures (i.e., where they were created to avoid taxes) (Bruce and Deskins 2006). Bruce and Deskins research also finds that some states with combined reporting rules tend to have more small business activity, possibly due to a leveling of the tax playing field between larger multi-state corporations and smaller single-state firms.\textsuperscript{9} However, this outcome is only in comparison to states that already had an existing CIT and moved to combined reporting.

\textit{IV. Putting all the tax weight on corporate income is a poor substitute for correcting the tax system}

Adding the BLF could be thought of as an apportionment strategy, where the MBT is on calculated based on payroll, businesses pay some sales tax, some property tax, etc. Taxable activities are increasingly mobile – increasing the weight on revenue might effectively reduce taxes for firms that only do business in-state. For the average state, reducing the payroll weight from one-third to one-quarter increased manufacturing employment around 1.1%, concentrated in durable goods manufacturing and with larger effects in the long-run.\textsuperscript{10} As we discussed above (“Effect on Jobs”), the BLF serves to shift the balance for Nevada businesses.

Some researchers argue that fees structured like the BLF will tax revenue that is not subject to sales tax and therefore is a form of consumption tax (Shanske 2013). This is because it includes corporate revenue derived from the sale of services and intangibles, which are not taxed in Nevada. The impact of shifting the weight from consumption (sales) to revenue has not been directly examined in statistical studies we examined.

\textbf{Fee versus Tax}

The Multistate Tax Commission (MTC) Compact defines an income tax as collections "... measured by an amount arrived at by deducting expenses from gross income" where the deductions are not "specifically and directly related to particular transactions." Successful legal defenses have been mounted for state revenue schemes to be defined as fees when they are "fairly related to services provided by the State" (Wright 2011). Washington’s Business and Occupation Tax, for example, was held to be a “privilege” tax specifically related to the ability of businesses to exploit local markets – that is, the fee is paid for the privilege of doing business in the state and “computed using a broad measure of market access rationally related to enjoyment of the privilege” (Wright 2011). Courts in New Jersey similarly found that

\textsuperscript{8} See Trimbath (2014) under our report on Internet Sales Taxes for a more detailed discussion of nexus.

\textsuperscript{9} The U.S. Small Business Administration distinguishes “small- and medium-sized business” from “entrepreneurial activity.” The later may be a substitute for unemployment, is more likely to be discouraged by higher personal income tax rates, estate/inheritance/gift taxes and lower sales tax (which can act like substitutes for business income taxes in the funding of state services) (Bruce and Gurley 2005; Bruce and Deskins 2006). On the other hand, higher CIT rates discourage small business activity by removing the incentive to incorporate – with the result being an increase in entrepreneurial activity (basically, individuals filing Schedule C). There is no consensus on the balance between the two (Wheeler 2006).

\textsuperscript{10} For more on this point, see Gamage & Shanske (2011), Goolsbee and Maydoo (2000), Robinson and Slemrod (2010). This point is also covered in Trimbath (2014).
the Delaware Franchise Tax is “not, strictly speaking, a tax at all” but a charge for the privilege of existing under Delaware’s corporate laws (Geisenberg 2012).\footnote{Delaware’s corporate law is a significant source of market power, which “allows its tax revenue to far exceed marginal costs” of administration (Barzuza 2010). This is an example of an economic externality that impacts statistical analyses of tax changes in the state. Corporations are more likely to incorporate in Delaware over corporate governance issues than the cost of taxes.}

On the other hand, California’s gross receipts fee on LLCs was successfully challenged because it was assessed as “a graduated fee based on California-sourced gross receipts.” The plaintiff also argued that the fee was a tax because the money went to the general fund and was not “segregated in a special fund for a specified purpose” (Wright 2011, page 9).

According to discussions in Wright (2011) the resolution of this issue will depend, at least in part, on wording in the legislation. Even then, courts in the other states may interpret this as a tax (not deductible for their income tax purposes) or a business fee (deductible for income tax purposes). Nevada would be well-advised to include wording in legislation emphasizing that the fee is to be “paid voluntarily in exchange for a specific benefit conferred or a privilege granted” (i.e., doing business in the state).\footnote{This is not to say that simply calling a collection a “fee” is enough to avoid litigation. Wright (2011) offers examples where payments to Texas, Ohio and Michigan are considered fees in some states and taxes in others.} Furthermore, legislators should consider specifying that collections will be held aside for education funding. This wording would leave Nevada open to a legal challenge only if the fees paid exceeded the “reasonable cost” of providing education, a condition that is unlikely to occur in Nevada under the current circumstances. The link between education and employment is fairly straight-forward.

**Pyramiding**

The Tax Foundation (TF, 2014) is strictly opposed to gross receipts taxes due to perceived economic distortions resulting from the imposition of taxes on multiple levels of production. The resulting addition of a revenue-based tax from the top down builds a sort of “pyramid” of taxes that, if passed on to end users, raises consumer costs. In the classic example of a loaf of bread the tax is paid by the wheat farmer, the miller that grinds the flour, the baker who combines the ingredients, etc., etc. This closed-economy theory is increasingly less applicable in today’s global economy. Using the bread example, agriculture and food production combined represent less than 1% of Nevada’s private economy. Although bread and bakery products are an important food manufacturing output in most counties, wheat is not among the top 5 commodities produced in Nevada (Nevada Department of Agriculture and Nevada Farm Bureau Federation).\footnote{Wheat is grown in Nevada for livestock feed and as a rotational crop under irrigation in addition to being sold as grain.} In other words, some pyramiding already takes place in Nevada because other states are taxing inputs used by Nevada businesses.

The taxation of inputs to final goods and services can cause firms to substitute less-heavily taxed inputs even if those inputs function less efficiently than the higher-taxed item. Sales taxes, for example, avoid this complication because the tax is paid by the consumer of the final good – so it does not influence production decisions. This, of course, assumes an ideal world: producers always make efficient production decisions; there are no exceptions/exemptions to sales taxes; etc. Yet even under ideal conditions, a sales tax would have to be 78% higher than a gross receipts tax to generate the same revenue for the state (Barbe 2013).

There is empirical evidence that pyramiding is much less pervasive in reality than the theory would suggest. Barbe (2013) calculates the input requirements for selected industries as the percent of final

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\footnote{Wheat is grown in Nevada for livestock feed and as a rotational crop under irrigation in addition to being sold as grain.}
costs. We aligned the industries in Barbe’s research with those provided in the BLF proposal. Our focus in the final analysis of this report will be on the industry clusters identified by LVGEA’s *Comprehensive Economic Development Strategy* (TIP 2013). Because each of these lists is slightly different, we provide a cross-walk between the three as an appendix, and we indicate the designations in the tables. In the table below, we see that the industries with the highest share of intermediate inputs have some of the lowest rates in the BLF proposal. They also represent relatively low shares of Nevada’s economy – providing support for our point about reliance on inter-state commerce.\(^{14}\)

<table>
<thead>
<tr>
<th>Industry</th>
<th>Inputs</th>
<th>CEDS Cluster Impacted</th>
<th>Rate</th>
<th>Share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing</td>
<td>61%</td>
<td>Gaming Tourism and Entertainment, Defense and UAV</td>
<td>12</td>
<td>6</td>
</tr>
<tr>
<td>Mining support</td>
<td>59%</td>
<td>Mining</td>
<td>13</td>
<td>13</td>
</tr>
<tr>
<td>Transportation and warehousing</td>
<td>56%</td>
<td>Logistics &amp; Operations</td>
<td>6</td>
<td>7</td>
</tr>
<tr>
<td>Mining-Oil and Gas</td>
<td>52%</td>
<td>Mining</td>
<td>1</td>
<td>14</td>
</tr>
<tr>
<td>Mining, except oil and gas</td>
<td>47%</td>
<td>Mining</td>
<td>14</td>
<td>2</td>
</tr>
<tr>
<td>Retail trade</td>
<td>45%</td>
<td>Retail Trade</td>
<td>9</td>
<td>3</td>
</tr>
<tr>
<td>Information</td>
<td>44%</td>
<td>Business IT Ecosystems</td>
<td>2</td>
<td>12</td>
</tr>
<tr>
<td>Wholesale trade</td>
<td>44%</td>
<td>Logistics &amp; Operations</td>
<td>11</td>
<td>8</td>
</tr>
<tr>
<td>Accommodation and food services</td>
<td>36%</td>
<td>Gaming Tourism and Entertainment</td>
<td>4</td>
<td>1</td>
</tr>
<tr>
<td>Arts, entertainment, and recreation</td>
<td>33%</td>
<td>Gaming Tourism and Entertainment</td>
<td>3</td>
<td>10</td>
</tr>
<tr>
<td>Technical Services</td>
<td>33%</td>
<td>Business IT Ecosystems, Gaming Tourism and Entertainment</td>
<td>7</td>
<td>9</td>
</tr>
<tr>
<td>Management of companies and enterprises</td>
<td>32%</td>
<td>Business IT Ecosystems, Gaming Tourism and Entertainment</td>
<td>8</td>
<td>11</td>
</tr>
<tr>
<td>Finance and insurance</td>
<td>30%</td>
<td>Banking and Financial Services</td>
<td>10</td>
<td>5</td>
</tr>
<tr>
<td>Health care and social assistance</td>
<td>29%</td>
<td>Health Care and Social assistance</td>
<td>5</td>
<td>4</td>
</tr>
</tbody>
</table>

Table only includes industries contained in the CEDS Clusters; industries not shown have slightly higher average cost of inputs and slightly lower average tax rates. Inputs expressed as a percent of final costs; Rate rank based on BLF proposal; Share rank based on industry share of private GSP.

**Impact on Economic Development**

Generally, business investment is impacted by the willingness of companies to invest in Nevada. For the general economy, we refer back to our discussion of “elasticity” in an earlier section and summarize that statistic here. For individual industries, we demonstrated above that the impact of pyramiding may be minimized under the industry rates proposed in the BLF. Below we calculate the potential change in demand for products where prices may be affected through costs passed on to consumers. We can relate this to a potential decrease in output.

\(^{14}\) The top 5 industries for share of intermediate inputs have an average rank of 9.2 for proposed BLF rates and 8.4 for share of Nevada’s economy.
General

Economists generally agree that higher state and local taxes reduce business activity with an elasticity of about -0.3 (e.g., Bartik 1989 and Ladd 1998). Total taxes paid by businesses in Nevada were about $6.2 billion in 2013 (Ernst & Young 2014). Raising tax collections by $219 million would be a 3.6% increase in total. Therefore, Nevada could expect a 1.1% decline in the growth of business investment after the BLF is implemented. In comparison to recent growth, this would result only in a slowing of growth rather than a net reduction in economic development. For example MBT revenues grew 4.6% in 2013; since the tax rate was constant that means salaries and/or employment grew – reasonable indications of growing business investment in the state.

It could be argued – assuming the additional revenue is spent wisely to improve education in the state – that any short run decline in business activity would be offset by increased growth in the future as a result of improved human capital. It is worth noting that questions were raised during debate over the “Education Initiative” for a margin tax in 2014 that the draft legislation did not guarantee that the money would only be spent on education. Opponents identified prior instances in Nevada where additional revenue assigned to education funding resulted in a deduction from the State’s general funding obligation with no change to the total expenditure on education. We return to this later but point it out here to highlight the risk that businesses may not believe that improvements in education are coming unless this issue is addressed in draft legislation for the proposed BLF.

Industry Specific Impacts

We calculated the industry economic development impact as the potential change in economic growth that would result from the imposition of the BLF at the proposed rates following the results in Barbe (2013). Barbe made several calculations that we find useful. Examining a gross receipts tax of 1%, Barbe calculated the per industry potential increase in prices and the resulting decrease in demand. Using these results, we calculated the potential decrease in gross state product (GSP), a measure parallel to firm business revenue, though not identical.

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15 The plan is to raise $188 million in FY ‘16 and $250 million in FY ‘17. For ease of calculation, we use the average over two years of $219 million per year.
16 To be clear, private gross state product grew by 3.9% last year. See our earlier discussion under “Effect on New Business Investment” for specifics on our use of the term here.
17 As noted in the State of Nevada General Fund Projection Model, revenues after exclusions will be larger than gross state product “because Gross State Product is a value added concept and total revenue is a sales and income concept,” the latter being more like the calculation in an accounting statement whereas gross state product is a survey-based estimate of economic activity.
Our analysis shows a total potential decrease in Nevada GSP of $14.6 million in the year the BLF is implemented – a negligible difference for a state the size of Nevada. Total demand for goods and services produced by Nevada business could fall by about 0.5% – also relatively insignificant – as a result of price increases that occur when business costs rise. Starting with the CEDS Cluster industries, we added the remaining statistically identifiable industries to the table below. Using methodology in Barbe (2013), we determine the potential decrease in industry contribution to GSP using the tax rate and the impact on demand, which is generated from price impacts (where business taxes are passed-on to consumers in the form of higher prices, resulting in lower demand). Note that the decrease in GSP is sometimes smaller for industries with larger output, supporting the idea that the BLF proposed rates have been adjusted to account for differing industry cost structures.
Note on Small Businesses
The MBT currently provides for an exemption for businesses with a minimum payroll below $85,000/quarter. These businesses are currently paying only the $200 business license fee and so would recognize a higher percentage change in their cost for doing business in Nevada under the proposed BLF. Using industry level data for Nevada available from the Small Business Administration, we estimate that more than 60,000 businesses are currently paying the business license fee but not the MBT. We also assume that these businesses are too small to be property owners. Excluding the MBT and property taxes removes 47% of the average business taxes in Nevada. That would make the proposed tax burden increase a substantially higher percentage for these firms. Although it is difficult to be exact, we can get a rough idea by doubling the percentage increase from our earlier estimate to an approximate 7% increase in tax payments for small firms. That could mean a 2% decline in small business investment in Nevada. However, the BLF rates are structured in a way that would provide for most of these enterprises to only realize the increase from $200 to $400. While the increase in the specific fee is 100%, the increase is relatively minor in relation to the overall state and local business tax burden in Nevada for small- and medium-sized enterprises.

Of particular concern for small businesses will be the cost of compliance. It is important that the process of calculating the BLF obligation be simple and straight-forward. One complication that is immediately plain is presenting the fee tables based on annual revenue but requiring payments quarterly. Also, new small businesses may run at a net loss until they are established. This could be managed by having some exception for companies in their first five years of operation or for businesses not producing revenue in excess of expenses. While a big business may already have an accounting department or engage the services of an outside accountant, this may not be the case for small businesses.

According to the BLF proposal, there are at least five lines that will need to be deducted from “total revenue.” The MBT has only one (health care coverage expenses). After arriving at the taxable base, the MBT form asks if the result is greater or less than $85,000 for the quarter, then applies the rate. For the BLF, the business will need to cross reference their industry and their calculated base amount in a table. The MBT is presented as a form and also as a spreadsheet that will do the necessary calculations after entering only a few numbers. If it is possible to present a calculating spreadsheet for the BLF, it would make the process easier.

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18 SBA reports information on 60,919 employer-firms in Nevada. To find the number of firms with payrolls under $85,000 per quarter, we divide the annual payroll by 4 and then count the number of businesses across firm sizes. We found 41,084 with fewer than 20 employees (the smallest category in the SBA data) with payrolls below the minimum. Another 16,553 business with payrolls below the minimum are mostly in retail trade (e.g., gas stations, clothing and sporting goods stores). There are 173 motion picture and sound recording industry firms that would be exempt for small payrolls, but these are already excluded under Nevada’s definition of “business.” We do not know at this time if it is the intention of the governor’s proposal to retain this exclusion in the BLF.
19 Author’s calculation using data from E&Y 2014.
20 Contrast this to statements in Tax Foundation analyses (e.g., Henchman 2011) that more than 18,000 businesses that were paying the corporate income tax in Texas reported no liability under the Texas margin tax. The minimum and maximum brackets – similar to the strategy used in Delaware – appear to avoid this problem in the Nevada proposal.
Conclusion

Three theories justify taxing corporate revenue: 1) It is a convenient way to collect taxes from shareholders for undisbursed corporate profits; 2) It ensures that businesses pay for benefits provided by the state; and 3) It can improve corporate governance by imposing a cost on income not distributed as dividends. In this last view, corporate taxes may be seen as a way to reduce the power of corporate management by reducing the economic resources at their disposal (Avi-Yonah 2004). The increase on the BLF also could be seen as reducing the weight on payroll taxes in Nevada. The BLF roughly shifts 4% of tax weight to revenue. The resulting decrease in tax weight on payroll could have a 0.24% positive impact on employment. In addition, the tax weight shift from the BLF might effectively reduce taxes for firms that only do business in-state (Cline and Neubig 2007, Rork and Wheeler 2008). States spend millions of dollars every year to defend tax laws.21 On the other hand, the states may reasonably charge fees for services provided to end users.

We urge the legislature to consider wording for a set-aside to address the over-arching questions of funding for education. The Coalition to Defeat the Margin Tax Initiative raised concerns during debate of the 2014 “Education Initiative” that “under the state constitution, the legislature would have complete authority to divert funds ... to things other than education.” That draft legislation had a section directing the Department of Taxation to deposit all proceeds directly to the State Distributive School Account for apportionment among the school districts and charter schools according to the State Distributive School Account. Nevada legislators might consider doing something similar to the job development fund established in Rhode Island or New York’s Metropolitan Commuter Transportation Mobility Tax. Legislative methodology with a set-aside could be used to designate Nevada’s collections for spending only on education. The argument for raising education financing money through a business fee rests on the connections of education with employment (businesses need skilled employees) and income (prosperous consumers have more disposable income for purchases from Nevada businesses). These connections could make a fee easily defensible.

Warnings that Nevada’s “ability to attract investment and capital depends greatly on its favorable tax climate” (Henchman 2011) ignore the state’s sources of comparative advantage in things like climate and natural resources or external economies in tourism, gaming and entertainment. For the same reasons that most banks want to locate in New York City, many businesses will make a decision to locate in Nevada that is not wholly dependent on the cost of fees and taxes. With minor modifications, the proposed changes to Nevada’s business license fee appear to have the potential to achieve the objectives of equity, stability and simplicity.

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21 The State of Nevada Department of Taxation appears 34 times in the Nevada Supreme Court case listings as a respondent, nearly twice as often as appellant. [Online database: searched February 13, 2015]
References


Geisenberger, Rick (2012). The Delaware Corporation Franchise Tax, 30 Delaware Lawyer 18 (Fall).


### Appendix: Cross-walk of industries in BLF proposal with CEDS Clusters and data sources

<table>
<thead>
<tr>
<th>CEDS Cluster</th>
<th>BLF Proposal</th>
<th>Primary Data Sources</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Gaming Tourism and Entertainment</strong></td>
<td>Accommodation; Food Services (including restaurants)</td>
<td>Accommodation and food services</td>
</tr>
<tr>
<td>na</td>
<td>Agriculture</td>
<td>Agriculture, forestry, fishing, and hunting</td>
</tr>
<tr>
<td><strong>Gaming Tourism and Entertainment</strong></td>
<td>Arts, entertainment, and recreation</td>
<td>Arts, entertainment, and recreation</td>
</tr>
<tr>
<td>na</td>
<td>Construction</td>
<td>Construction</td>
</tr>
<tr>
<td>na</td>
<td>Educational services</td>
<td>Educational services</td>
</tr>
<tr>
<td>Finance and insurance</td>
<td>Financial services</td>
<td>Finance and insurance</td>
</tr>
<tr>
<td><strong>Health Care and Social assistance</strong></td>
<td>Health Services</td>
<td>Health care and social assistance</td>
</tr>
<tr>
<td>Business IT Ecosystems</td>
<td>Publishing, Software, Data Processing; Telecommunications</td>
<td>Information</td>
</tr>
<tr>
<td><strong>Gaming Tourism and Entertainment; Business IT Ecosystems</strong></td>
<td>Management of companies</td>
<td>Management of companies and enterprises</td>
</tr>
<tr>
<td><strong>Gaming Tourism and Entertainment; Defense and UAV</strong></td>
<td>Manufacturing</td>
<td>Manufacturing</td>
</tr>
<tr>
<td>Mining</td>
<td>Mining</td>
<td>Mining support</td>
</tr>
<tr>
<td>Mining</td>
<td>Mining</td>
<td>Mining, except oil and gas</td>
</tr>
<tr>
<td>Mining</td>
<td>Other Services</td>
<td>Other services, except government</td>
</tr>
<tr>
<td>na</td>
<td>Real estate</td>
<td>Real estate</td>
</tr>
<tr>
<td>na</td>
<td>Retail Trade</td>
<td>Retail trade</td>
</tr>
<tr>
<td><strong>Gaming Tourism and Entertainment; Business IT Ecosystems</strong></td>
<td>Professional Services: Administrative and Support Services</td>
<td>Technical Services</td>
</tr>
<tr>
<td><strong>Logistics &amp; Operations</strong></td>
<td>Air Transportation; Truck Transportation; Rail Transportation; Other Transportation; Warehousing and Storage</td>
<td>Transportation and warehousing</td>
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<tr>
<td>na</td>
<td>Utilities</td>
<td>Utilities</td>
</tr>
<tr>
<td>na</td>
<td>Waste management services</td>
<td>Waste management and remediation services</td>
</tr>
<tr>
<td><strong>Logistics &amp; Operations</strong></td>
<td>Wholesale Trade</td>
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</tr>
<tr>
<td>na</td>
<td>Unclassified</td>
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<tr>
<td>na</td>
<td>Non-Employer Companies</td>
<td>na</td>
</tr>
<tr>
<td>na</td>
<td>Foreign Filers</td>
<td>na</td>
</tr>
</tbody>
</table>

*Italics in CEDS column are sectors proposed for development focus in LVGEA strategy (TIP 2013).*