



Iowa Taxes: Blue Bunny and Booze

by David Hogberg

As if the Iowa tax code isn't complicated enough (for instance, see *IOWA ECONOMIC SCORECARD*, April 2004), the state government made it even more complicated this year. The Iowa Legislature opened up a new tax loophole for business, while the Iowa Alcoholic Beverages Division has started taxing vodka at different rates.

The business loophole was precipitated by the announcement of Iowa-based Wells Dairy Company (the maker of Blue Bunny Ice Cream) that it was looking for a new corporate headquarters and was considering a move to tax-friendlier Nebraska or South Dakota. Well, no Legislature wants to be known as the one that "lost the Blue Bunny," so what was to be done? First, the Grow Iowa Values Fund came through with some corporate welfare, to the tune of about \$2.6 million. Second, Iowa's Legislators passed and Governor Vilsack signed what amounts to a new tax loophole in the Iowa Tax Code.

According to Senate File 2290,

An eligible business or supporting business may claim a corporate tax credit in an amount equal to the taxes paid by a third-party developer . . . for gas, electricity, water, or sewer utility services, goods, wares, or merchandise, or on services rendered, furnished, or performed to or for a contractor or subcontractor and used in fulfillment of a written contract relating to the construction or equipping of a facility with the economic development area of the eligible business or supporting business.¹

Although it seems confusing, it's not when you keep in mind that Wells Dairy wants a tax break to build a new corporate headquarters. Basically, what the new law states is that if a business wants to pay a developer to build it a new facility, it can lower its corporate tax burden by an amount equal to any sales taxes or utilities taxes incurred by the *developer*. For example, if Wells Dairy pays ACME Construction to build it a new corporate headquarters, Wells Dairy can then write off on its corporate income tax return any sales tax that ACME Construction pays on the materials used for construction.

While it is certainly a good idea to lower the tax burden on businesses in Iowa, this is not the optimum way to do it. First, this sort of tax loophole also means that businesses will have to spend more money on accountants and tax attorneys to exploit the tax loophole, money that won't be spent on new investment. Second, this loophole will probably only be used by businesses that are large enough to actually have corporate headquarters. Thus, if you own a small business, you are out of luck.

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However, if you like to drink pricey vodka, it is your lucky day. According to the *Des Moines Register*, on March 1 of this year the state began “using a sliding scale for liquor excise taxes. The effect will be to lower the tax rate on high-priced vodkas while increasing the rate on cheap vodkas.”² Apparently, this is part of Governor Tom Vilsack’s new effort to reinvent government, in that it gives the Iowa Alcoholics Beverage Division more leeway in deciding how to tax booze. Exactly which spirit-producing company benefits from this isn’t quite clear (does Absolut have a lobbyist in Des Moines?), but the thinking behind the tax change is quite interesting: “Iowa is not trying to stand tax policy on its head, said Lynn Walding, administrator of the Alcoholic Beverages Division. The goal is to raise revenue by selling more of the pricey vodka.”³

Permit me to explain the thinking behind Mr. Walding’s remark: If you tax something more, you get less of it: if you tax something less, you get more of it. That’s the basic logic behind cutting taxes. If this logic works so well for people who like to drink screwdrivers, perhaps someone should ask the Vilsack Administration why it doesn’t apply to other folks, say, those who pay income taxes?

Indeed, what Iowa needs is not new tax loopholes or different rates on vodka, but tax reform that helps most if not all of Iowa’s taxpayers. The State Legislature and the Governor need to stop using the tax code to please every special interest in Des Moines and instead reform Iowa’s tax structure so that it is conducive to economic growth in Iowa.

A great place to start would be with the personal and corporate income tax system in Iowa. Both are complicated, highly progressive, with high top marginal rates — all of the things in a tax system that are inimical to robust economic growth. Cutting income taxes and at the same time replacing them with a simple flat tax would be the best thing Iowa could do to ensure strong economic growth in the future.

Let’s see if the State Legislature and the Governor can come through in the next legislative session.

ENDNOTES:

¹Senate File 2290, <<http://coolice.legis.state.us/legislation/enrolled/SF2290.html>> (June 9, 2004).

²David Elbert, “Vodka Drinker Set to Taste New Tax Plan,” *Des Moines Register*, February 18, 2004, <<http://desmoinesregister.com/business/stories/c2122222/23564069.html>> (July 19, 2004).

³Ibid.

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