Understanding the Cost and Impact of Corporate Tax Subsidies

A Four-Part Series on Economic Development Incentives in Illinois

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Series Summary

Business subsidies play a prominent role in economic development policy at both the state and local levels in Illinois, yet these policies continue to lack the strict scrutiny they deserve. A new research series by the Illinois Economic Policy Institute (ILEPI) finds that billions of dollars in state and local tax subsidies for private businesses have heavily favored a handful of companies, have largely supported high-income and white communities, and are outperformed by investments in education and infrastructure.

Economic development subsides should create jobs, increase wages, and promote positive economic growth; yet these goals do not consistently prevail. In light of recent deals awarded in Wisconsin and Indiana – $3 billion to Foxconn and $7 million to Carrier, respectively – it is worthwhile to understand the historical context of Illinois' own programs and how excessive deals can even harm the state's economy. Furthermore, given Illinois' current budget situation, after a protracted two-year dispute and ongoing funding woes, taxpayers have the right to know whether their money is being spent effectively. The General Assembly made tough decisions to finally pass a budget, and it is in the taxpayers' best interests to carefully consider the benefits of economic development subsidies and ensure their money is supporting worthwhile programs.

Subsidizing the Few

The use of subsidies in the State of Illinois came about as a method to lure companies away from other states and promote a positive image of Illinois. However, officials must carefully consider the benefits of these deals, particularly "megadeals," which are economic development packages made up of multiple incentives that total more than $50 million.

- Since 1985, state and local governments have doled out at least $5 billion in economic development subsidies (not adjusted for inflation).
- Sears, Mitsubishi, and Motorola received more than $900 million, or 17 percent of total state and local subsidies, from taxpayers. All three companies have since laid off workers, with Mitsubishi now closed.
- While these three deals exemplify the most egregious form of publicly-funded subsidization, Illinois' business subsidy practice has been widespread and costly for many years.

Playing Favorites

Economic inequality in Illinois has reached levels not experienced in decades, with the ratio of the top one percent to the median worker increasing by 173 percent. The evaluation of subsidies in the context of their geographic distribution and demographics illustrates whether they are helping those residents who are most in need.

- State subsidies are disproportionately located in municipalities that have poverty rates *below* the state's average and are majority white – 77 percent of subsidies have gone to municipalities with a smaller share of minorities than the state average.
- Southern Chicago and Cook County have noticeably higher poverty and unemployment rates, yet only 80 state subsidies were issued to locations there, while just over 130 and 120 state subsidies were issued to locations in DuPage and Lake Counties, respectively.
- The north side of Chicago has received over 1,600 local subsidies, while the south side has received fewer than 500 local subsidies.

Preferable Alternatives

Most basically, economic development subsidies have the potential to negatively impact the economy if they come at the expense of other productive public goods. Whereas business subsidies generally accrue to the richest households and have little "trickle-down" effect on the middle class, broad-based investments in infrastructure and in people improve connectivity, increase worker skill levels, spur innovation, and boost consumer demand.

- While business subsidies have created 1,700 jobs per year, the same level of investment in infrastructure would have created 3,900 jobs in Illinois every year.
- Similarly, the same level of investment in education would have created between 3,400 jobs (higher education) and 6,100 jobs (K-12 education) in Illinois every year.
- Doubling the state's Earned Income Tax Credit match to 20 percent would have created or saved over 2,500 jobs per year, about 800 more than through business subsidies.
- If state and local governments in Illinois had saved the money used for business subsidies to help balance public budgets, Illinois could have lessened its current financial woes and potentially avoided as many credit rating downgrades, which have cost taxpayers and reduced investor confidence.

Quality Investments

If governments are to continue using subsidies as an economic development strategy, measures must be implemented to ensure companies are creating quality, good-paying jobs that will not only benefit the state in the long run, but also help those truly in need.

- While Illinois has made positive steps towards making economic development subsidies accountable – including the Corporate Accountability for Tax Expenditures Act of 2003 and other minimal stipulations for certain programs – these measures are not sufficient.
- A variety of measures are employed across Illinois' five major economic development subsidy programs, but they are inconsistent and often apply to only specific types of projects; policymakers must consider the inclusion of job quality and enforcement standards in all economic development subsidy programs.
- Most importantly, the state needs to create and implement an economic development strategy that requires careful consideration and evaluation before any subsidy deal is made.

Illinois' business subsidy practice – in the name of job creation and retention – has been widespread and costly for decades. The state continues to consider large subsidy deals despite proof that they have not succeeded in the past; currently it is competing against 11 other states for a Mazda and Toyota manufacturing plant. Consequently, Illinois' economic development policy deserves strict scrutiny to ensure investments by taxpayers truly benefit the state's residents.

As stated by the Federal Reserve Bank of Minneapolis, "while states spend billions of dollars competing with one another to retain and attract businesses, they struggle to provide such public goods as schools and libraries, police and fire protection, and the roads, bridges and parks that are critical to the success and economic competitiveness of any community." Alongside vital investments in education and infrastructure, arguments can be made for certain small-scale subsidies and those that aid low-income and high unemployment areas. But it is crucial to ensure that receipt of these subsidies are tied to clear economic outcomes and consistent enforcement measures. Absent these provisions, taxpayers would be right to question whether these investments are really aiding the local communities they are supposed to benefit.