

CITY OF LOS ANGELES
INTER-DEPARTMENTAL CORRESPONDENCE

0220-04582-0008

Date: April 18, 2012

To: Jobs & Business Development Committee

From: Miguel A. Santana, City Administrative Officer *Dik*

Subject: OFFICE OF ECONOMIC ANALYSIS - FOLLOW-UP REQUEST FOR INFORMATION FROM BLUE SKY CONSULTING GROUP

During a March 28, 2012 meeting, the Jobs & Business Development Committee requested the Blue Sky Consulting Group (Blue Sky) to provide additional information regarding the economic impact of the City's previous actions to reduce business taxes over the past several years. Blue Sky conducted this review using both published economic research and the Regional Economic Models, Inc. (REMI) model. A response prepared by Blue Sky is attached.

Blue Sky reports that applying the results of the economic research to the \$135 million in previously-enacted tax relief increases economic output in the City by \$645 million, results in the creation of approximately 5,200 new jobs and provides approximately \$8.6 million in revenue to the City. Further, applying the results from the REMI model increases economic output in the City by \$280 million, results in the creation of approximately 2,100 new jobs and provides approximately \$3.7 million in revenue to the City.

MAS:KDU:02120115c

Attachment

Date: 4/18/12
Submitted in JBD Committee
Council File No: 09-1914-SB
Item No.: 1
Deputy: CAO



MEMORANDUM

To: City of Los Angeles Office of Economic Analysis
From: Matthew Newman and Shawn Blosser, Blue Sky Consulting Group
Date: April 17, 2012
Re: Impact of Previous Business Tax Cuts

This memo was prepared in response to a request for additional information made by the Jobs and Business Development Committee on March 28, 2012. Specifically, council members inquired about the economic impact of the City's previous actions to reduce business taxes over the past several years.

According to a November 7, 2011 report prepared by the CAO and the CLA, in FY 2010-11, the City provided more than \$135 million in business tax relief. This tax relief included wholesale and manufacturing relief dating back to 1994-95, new and small business relief from 2001 and 2007, and general tax rate reductions for all businesses implemented between 2006 and 2009, as well as a series of other actions during this time period.

In order to estimate the likely economic impact of this tax relief, we applied the estimation methodologies developed previously by the Blue Sky Consulting Group to estimate the likely impact of the complete elimination of the City's business tax, as proposed by the BTAC.¹ Specifically, we estimated the impact of the previously enacted tax relief by applying the results of published economic research on the responsiveness of local economies to tax cuts as well as by using the REMI model.

According to the most recent published meta-analysis (i.e., a review and synthesis of the published research), a 10 percent reduction in state and local business taxes would lead to a 2 percent increase in economic activity (i.e. an elasticity of economic output with respect to state and local taxes of -0.2).² Applying this result to the \$135 million in previously enacted tax relief suggests that a tax reduction of this magnitude will increase annual economic output in the City by \$645 million and result in the creation of nearly 5,200 new jobs in the City.^{3,4} Looking at just the impact of the 2006 to 2009 rate

¹ For a complete explanation of the methodologies developed, see our March 22, 2012 report, "Economic and Fiscal Effects of Eliminating the Los Angeles Business Tax."

² Wasylenko, Michael, "Taxation and Economic Development: The State of the Economic Literature," *New England Economic Review* (March/April 1997): 37-52. Wasylenko reported an average elasticity of -.2 among the studies he reviewed.

³ We note that the full impact of the most recently enacted tax reductions may not yet have been fully felt in the City's economy. The results presented above reflect the full impact, once the economy has had sufficient time to adjust to the changes.

⁴ By applying the results from the published research, we estimate that this increase in economic output is associated with an increase in other, non-business tax revenues of about \$8.6 million annually, for a net fiscal impact of \$126.4 million.

reductions, this analysis suggests that these across the board rate reductions are associated with an annual increase in economic output of about \$325 million and the creation of more than 2,600 new jobs in the City.⁵

We also modeled the impact of these previously enacted tax cuts using the REMI model. Applying the results from the REMI model suggests that a \$135 million tax reduction will increase economic output by just over \$280 million and create about 2,100 new jobs.⁶ Looking at just the impact of the 2006 to 2009 rate reductions, this analysis suggests that these tax reductions will increase economic output by about \$160 million annually and create just over 1,200 new jobs.

⁵ Note that these results reflect the economic impact once the tax relief has had its full effect, which can take several years or more. Because some of the tax relief measures are relatively recent, their full impact may not yet have been felt.

⁶ Using the REMI methodology, we estimate that this increase in economic output is associated with an increase in other, non-business tax revenues of about \$3.7 million annually, for a net fiscal impact of \$131.3 million.