The "Border Tax Problem”

- Residents of a high-tax jurisdiction may buy goods in neighboring low-tax jurisdictions in order to avoid paying the higher tax charged in their own jurisdiction
- This is illegal tax evasion not legal tax avoidance because there is a ‘use tax’ liability on goods brought into Washington, but is is often not collected on consumer goods.

The Border Tax Problem for Washington

- Is likely to be serious with a state sales tax rate of 6.5% and local tax rates ranging from 0.5% to 2.3% while
- Oregon has no sales tax and
- Idaho's state sales tax rate is only 5% (with local sales taxes up to 2%)

Four Aspects of the Border Tax Problem

- Loss of sales tax revenue, estimated at $22 million for the state
  - (1% of total sales tax collections in 1989) and $4.7 million for local governments (8% of local sales taxes in border counties)

- Loss of business and employment in the border counties

Four Aspects of the Border Tax Problem

- Inequity of border area residents being able to evade their "fair share" of state taxes

- Tax evasion by Washington residents gives Oregon retailers an unfair advantage over Washington retailers.

A Previous Attempt to Deal With Washington's Border Tax Problem

- A February 1983 increase in the state sales tax rate from 5.4% to 6.5%, left tax rate at 5.4% in four designated "border counties" in the Portland-Vancouver area
- In November 1984, the Washington State Supreme Court ruled that the lower tax rate in border counties violated article 11 of the state constitution, requiring uniform state taxes

A Previous Proposal to Deal With Washington's Border Tax Problem

- Alleviating the border tax problem was one rationale for governor's committee (1989) proposal to reduce the state sales tax rate to 3.75% and introduce a personal income tax to replace revenues lost by the cut in the sales tax

Is This Only a Problem in the Portland-vancouver Area?

- An argument might be made that Portland-Vancouver is special because shopping and a neighboring low-tax county is more attractive if that county offers the diversity of retail stores found only in metropolitan areas, but this question can only be answered by empirical analysis

Empirical Estimates

- Elasticity of taxable retail sales per capita with respect to the price (including sales tax) in the county relative to the price in the neighboring low-tax county
- -5.876 in the Portland-Vancouver MSA (Clark & Skamania counties)
- -3.2131 in all other border counties (except Columbia & Garfield)

Source: John H. Beck, "The border tax problem in metropolitan and nonmetropolitan areas of Washington," Western Tax Review 10 (winter 1992): 15-35, using 1984-1988 data.

Another Estimate of the Elasticity of Retail Sales

Allowing for long-run effects of past differences in tax rates on the pattern of retail sales

- -1.825 in the short run
- -2.443 in the long run

Source: Lorrie Jo Brown, "The effects of tax rate differences on retail trade in Washington border counties," in Washington state excise tax noncompliance study (1990), using data from 1975 to 1987.

Estimated Increase in Retail Sales

From Elimination of Tax Differential*

County	Total taxable retail sector sales in 1988	Gain estimated by Beck
Asotin	$31,422,903	$1,964,003
Benton	$387,726,715	$101,426,591
Clark	$645,477,579	$339,099,454
Columbia	$6,113,109	0
Cowlitz	$309,373,970	$75,127,027

*i.e., if Oregon and Idaho imposed tax rates equal to Washington's

Estimated Increase in Retail Sales

From Elimination of Tax Differential*

County	Total taxable retail sector sales in 1988	Gain estimated by Beck
Garfield	$5,146,769	0
Klickitat	$20,936,179	$5,084,051
Pacific	$44,544,559	$12,158,014
Pend Oreille	$11,914,508	$744,684
Skamania	$7,226,902	$3,528,110

*i.e., if Oregon and Idaho imposed tax rates equal to Washington's

Estimated Increase in Retail Sales

From Elimination of Tax Differential*

County	Total taxable retail sector sales in 1988	Gain estimated by Beck
Spokane	$1,526,466,432	$119,885,569
Wahkiakum	$3,771,810	$986,679
Walla Walla	$137,171,110	$35,452,501
Whitman	$78,801,876	$5,977,511
TOTAL (14 counties)	$3,216,094,421	$701,434,193

*i.e., if Oregon and Idaho imposed tax rates equal to Washington's

The Border Tax Problem With The Cigarette Tax

- Evasion occurs through purchases of cigarettes in neighboring states with lower tax rates, on some Indian reservations, and through the Internet and mail order.

- I-773 raised the tax by 60 cents per pack. Increased evasion is likely.

Previous Estimate Of Revenue Loss From Cigarette Tax Evasion

WA State Untaxed Cigarettes and Losses
FY 1992 through FY 2001

	Estimated Retail Price	Cigarette Tax/pack	Untaxed Packs (millions)	Untaxed Packs per capita	Revenue Loss* (millions)
2001	$3.52	$0.825	94.8	20.2	$107.2
2000	3.13	0.825	96.7	21.3	105.4
1999	2.91	0.825	107.2	23.2	114.9
1998	2.60	0.825	114.8	24.9	120.0
1997	2.40	0.825	116.8	25.7	120.1
1996	2.35	0.815	108.7	24.8	110.2
1995	2.10	0.565	78.3	19.7	58.1
1994	2.10	0.540	75.2	19.6	54.0
1993	2.00	0.340	52.8	15.6	26.9
1992	2.00	0.340	23.1	10.0	11.8

*State and Local

Source: Washington State DOR ~ Research Division. (September 2001).

Conclusions

- Differing sales tax rates or no sales tax in border areas result in:
  - Significant loss of state and local sales tax revenue in border areas.
  - Loss of business and employment in the border areas
  - Increased evasion

Conclusions

- Border areas are very sensitive to any changes in tax rates.

- Constitution requires uniform state taxes. Supreme court overturned attempted solution to border problem--lower tax rates in border areas.