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The Worst Tax

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Rank the following taxes from best to worst: individual income taxes; payroll taxes, corporate income taxes, sales or consumption taxes, and residential property taxes. The vast majority of economists would rank the corporate income tax as being worst and the sales tax and residential property tax as the best.

Unfortunately, the corporate income tax is often the favorite tax of fiscally irresponsible politicians because it is not easily seen. In fact, the corporate tax is paid by workers in lower wages and fewer new jobs, by consumers in higher prices and by savers and investors in lower rates of return. The Organization for Economic Cooperation and Development (OECD), based in Paris and not known for favoring lower taxes, published a new study last month, "Tax and Economic Growth," which provides more evidence that the corporate income tax interferes most (as compared with other taxes) with proper resource allocation, productivity growth, and economic efficiency.

Last week, the U.S. Government Accountability Office (GAO) released a study that showed 28 percent of large companies paid no corporate income tax in 2005 almost always because they had made no profit. Rather than thoughtfully considering whether the corporate income tax should be reduced or abolished, several bluster brains in the U.S. Congress used the report as an excuse to attack corporations. Sen. Byron Dorgan, North Dakota Democrat, who is a big supporter of agricultural subsidies to millionaire farmers and foolish corn ethanol mandates, which are neither cost-effective nor reduce total carbon emissions, demanded that big corporations pay "their fair share" of taxes. Mr. Dorgan, of course, ignored the fact that only people - again, workers, consumers, and/or savers and investors - pay taxes. He also did not explain how it is "fair" that U.S. companies are already more heavily taxed than their foreign competitors, even neighboring Canada.

Corporate and Individual Income Tax Rates

Country	Corporate Tax Rate	Individual Income Tax Rate
U.S.	39.25%	35-42%
Germany	30.18%	45%
U.K.	28.00%	40%
China	25.00%	45%
Russia	24.00%	13%

Singapore	18.00%	20%
Ireland	12.50%	41%
Bulgaria	10.00%	10%
UAE	00.00%	00%
Note: The above chart refers to maximum rates. The U.S. corporate rate reflects the federal rate of 35 percent plus the average of state rates. The U.S. individual rate varies considerably by state, from those with no state income tax to those with rates of more than 10 percent.		

The United States' corporate income tax rate now is more than 50 percent higher than the OECD members (major industrial countries) average.

Before the Reagan administration, the U.S. had a 50 percent corporate tax rate, and most other countries had similar high corporate tax rates. During the Reagan administration, the United States sharply reduced its corporate tax rate and other nations followed the lead.

As the benefits of corporate tax reduction quickly became obvious, most countries kept cutting their corporate rates. The Irish cut their rate to 12.5 percent and went from being the poor man of Europe to the second-richest on a per capita income basis. The formerly communist countries of Eastern and Central Europe are now in the process of besting the Irish, by going to low flat-rate systems on both personal and corporate income. As the accompanying chart shows, the Bulgarians are the most recent to join the flat-rate club with a 10 percent rate on both corporate and personal income.

There are a number of very high-growth countries, such as the United Arab Emirates (UAE), and financial centers, such as Cayman, that have no corporate or individual income tax at all. They rely primarily on sales or consumption taxes, property taxes and fees for government services. And for the most part they have done very well by their citizens.

Assume you are a businessperson who has just developed a greatly improved electric car battery that you expect to sell in most countries around the world. Would you set up your business in the United States, which has the highest corporate tax rates in the world?

What does it say about those U.S. politicians who rant about U.S. companies moving their businesses to other countries and U.S. citizens moving their capital elsewhere, when many of those same politicians oppose tax rate reductions and even advocate tax rate increases?

Corporate leaders have a fiduciary responsibility to their stockholders to maximize profits. If a country has tax and regulatory provisions that make its companies noncompetitive, the company has no choice but to move.

Businesses will continue to flee the United States, and new companies that intend to sell globally will be less likely to establish their companies in the U.S. as long as the U.S. is less globally attractive because of high tax rates and excessive regulatory costs.

The corporate tax should be abolished because it is the most destructive tax. In a typical year, it only produces about 10 percent of federal revenue. This static revenue loss would be quickly made up by the increase in shareholder dividends that should no longer have a tax preference (in the way that sole proprietorships, partnerships, and limited liability companies are now taxed), and through the additional productivity, international competitiveness and job growth that would result from abolition of the corporate income tax.

Sen. John McCain has said he wants to cut the corporate tax rate to 25 percent and not raise individual tax rates. Sen. Barack Obama has not yet proposed a reduction in corporate tax rates, and has proposed increasing the top marginal individual rates so that the United States would have some of the highest individual tax rates in the world.Given the above information, do you think the United States will gain more jobs and become more internationally competitive under Mr. McCain's or Mr. Obama's tax plan?

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