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Biden and Yellen's Nutty Corporate Tax Rate Plan

by Richard W. Rahn

ADMINISTRATION PROPOSES RAISING RATES, PROVING THEY'RE NOT AS SMART AS TRUMP ECONOMIC TEAM

In 2020, a great global pandemic descended upon the Earth. It not only affected people's bodies, leading to death in many of the elderly, but also caused the global political class to lose a non-negligible number of IQ points.

The open question is: "Is their new stupidity a permanent or temporary condition?" Silly talk leads to silly policies. Where, at one time, it was known that if the government printed too much money without real backing or productivity growth, the currency would lose its value — that simple fact has been forgotten by those who make such decisions.

There was a time when most educated or naturally astute people knew that if tax rates were disproportionately high in one place, people and their money would flee to lower tax rate environments. That simple fact has eluded the Democrats who control New York, to the great benefit of Florida. At one time, most people understood that government tended not to spend money as carefully as they did themselves and, as a result, it was necessary to restrain the growth in government spending.

Every competent economist knows that there is some tax rate for each type of tax where the tax becomes counterproductive and causes a loss in revenue and economic well-being. There is considerable honest (and some dishonest) debate of where the revenue and welfare-maximizing point is for each tax. About four decades ago, the noted economist Art Laffer did a simple drawing of a parabolic curve as way of enabling members of the political class to understand that ever-increasing tax rates do not mean ever-increasing tax revenue. Unfortunately, this age-old concept has escaped the brains of many who comment on or implement taxes.

There exists a series of letters between Thomas Jefferson and the famous French economist J.B. Say in which they discuss the question as to what tariff rate (a tariff is a tax on imports) maximizes tax revenue. They both clearly understood that if the rate were too high, it would either cut off trade and/or lead to smuggling, which would result in less revenue to the government.

Those who study the economics of taxation learn that a tax that falls on consumption (what one takes out of the economy) is usually far less damaging than a tax that falls largely on labor or capital (what one puts into the economy).

Thus, most tax economists oppose the corporate income tax, because it is a tax that falls largely on labor (in the form of lower wages and benefits) and perhaps a small amount on capital. Recognizing this fact and the fact that high corporate tax rates make their companies less internationally competitive, in recent decades many countries (including the U.S.) have reduced their corporate tax rate – and some all the way down to zero.

In order to prove their ignorance, some politicians have demanded that the corporate tax be increased because "it is not fair" that some companies in some countries pay a lower tax than others. If they were not so dim, they would understand that only people pay taxes and that the corporate tax is a tax on a particular legal form of business — corporations — that is actually paid mainly by the workers.

The corporate tax is a double tax being paid on the profits at the company level, and then the owners being taxed once again on their dividends or capital gains. High corporate tax rates incentivize businesses to move their legal homes to lower-tax jurisdictions or to recast themselves as limited liability companies, partnerships or sole proprietors, where they are taxed only once.

Pre-2016, the U.S. ended up with the highest corporate tax rate among the major industrialized companies. The U.S. burden was approximately three times Ireland's, so you may recall there was much in the press about the many American companies that were being domiciled in Ireland for tax reasons. The Trump tax rate cuts in 2018 re-established U.S. tax competitiveness, and many companies came back to America. The Biden administration has proposed raising the corporate tax rate, which proves they are not as smart as the Trump economic team.

So, once again, the U.S. will have the highest business taxes in the world (when state and local taxes are included). Janet Yellen, the new secretary of the Treasury and former head of the Federal Reserve, wanting to prove that she is not the dimmest economist in Washington, has just proposed a minimum global corporate income tax for the express purpose of discouraging U.S. companies from once again leaving the country. High business tax countries like France, Japan and Italy think it is a splendid idea. Lower business tax countries like Sweden, the U.K. and Ireland quite correctly think it is bonkers.

To briefly recap, the Biden folks think it is a good idea to not only increase one of the worst forms of taxation, but then try to get the other countries of the world to also adopt the same nutty policy. This, of course, will lead to endless pressures to increase the corporate tax rate, as tax competition is being destroyed, thereby ensuring lower wages, fewer jobs and less economic growth everywhere. Oh, how splendid.

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