May 5 2009, 4:16 pm **by Conor Clarke**

The Cato Institute Doesn't Understand Corporate Taxes

Since, as Ryan Donmoyer and others have reported, the business lobby is gearing up for a big fight over the president's proposed changes to the corporate tax, I am going to try to be somewhat diligent about tracking arguments for and against the proposal. ("This is going to be the biggest fight for the corporate community in the next two years," says one lobbyist.) And a post over at Cato's @Liberty blog does such a wonderful job of misrepresenting Obama's plan that I figure I will start there.

Daniel Griswold writes, contra the Obama plan:

> Of course, there is a perfectly good reason why we don't tax what U.S. companies earn and keep abroad: those companies are already paying taxes in the countries where their affiliates are located, and at the same rates that apply to multinationals from other countries competing in the same markets.
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> As I pointed out in a Cato Free Trade Bulletin in January, locating affiliates in foreign markets is now the chief way that U.S. companies reach new customers outside the United States. If we sock them with the relatively high U.S. corporate rate, U.S. companies will be less able to compete against German and Japanese multinationals in the same markets who need only pay the (almost always) lower corporate rate assessed by the host country.[...]

Much of the first paragraph has a kind of warm, true-ish quality. But unfortunately it has almost nothing to do with the Obama plan. *No one is proposing taxing what US companies earn and keep abroad!* The proposal Griswold has in mind is, I think, to halt companies from claiming tax *deductions* on investments they make abroad -- investments that, under the currently law, are deductible even if they generate profits that never feel the wrath of the IRS.

To the second paragraph: It is true that if US companies with affiliates abroad are paying the American corporate tax rate, they will be more of a disadvantage than they are under the current law. That's a truism: Their taxes are going up. But it's not necessarily the case that, say, Japanese multinationals are always going to be paying a lower rate than American multinationals.

My understanding is that corporate taxes in Japan are structured in a manner broadly similar to corporate taxes in the US: if a Japanese company earns profits abroad and repatriates them, they pay the Japanese rate, not the foreign rate. (Or, to be more specific: they pay the local rate, and then earn it back as a domestic tax credit.) And the top marginal Japanese rate is actually higher than the American rate.

Again: I think the American corporate tax rate is too high. And in a perfect world of optimal taxes we might want to do without it. But Obama's plan is short and doesn't take that long to read.