Cutting the Corporate Tax Can Help Workers. Really.

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Is cutting the corporate tax rate merely a sop to the wealthy, as a report recently published by the Institute for Policy Studies alleges? It's an important question, since a corporate rate cut is a prominent feature of every tax reform proposal currently on the table.

Those who share this perspective allege it is straightforward: the corporate income tax is a tax on wealthy owners of capital and reducing it would be wildly regressive and do little to boost the economy. The IPS study looks at 92 large U.S. corporations post-great-recession—when there was no change in the corporate tax rate—and concludes that, since their hiring over that period wasn't that high, lower taxes won't do all that much for hiring overall, and any tax savings will just be given to shareholders or CEO salaries.

However, I beg to differ, as do lots of other economists. Taxing capital income (which is what the corporate income tax does) is a costly way to generate revenue for the government, in terms of the forgone economic growth (companies can't hire or expand or invest with any money sent to the government), and it's not nearly as progressive a tax as the detractors of the current tax reform efforts allege.

Economics tells us that the person who writes the check to the government is not necessarily the person who bears the burden of the tax, and this holds for the corporate income tax as well. Labor bears a portion of this tax: the corporate income tax reduces the returns to investment so firms invest less, which means workers have less equipment to work with. As a result, they are less productive, which reduces wages as well as employment.

Other countries have figured out the economic cost of a high corporate income tax and have been reducing their corporate tax rates at a rapid pace: from 2000-2012 the countries that are members of the Organization of Economic Cooperation and Development cut corporate tax rates fully 85 times. Most of these were not offset by tax revenue increases elsewhere, either.

The economists Mihir Desai, James Hines and Fritz Foley estimate that workers bear well over 50 percent of the corporate tax burden; A study done by the Congressional Budget Office estimated that the proportion is more than 70 percent. If either proportion is anywhere close to reality then it is indisputable that the corporate income tax hurts working Americans.

A recent study that I did with Andrew Hanson, an economist at Marquette University, found support for that conclusion. We looked at a bevy of research that examined the relationship between the corporate tax rate, wages, and employment. Based on this research we concluded that reducing the corporate tax rate to the vicinity of 20 percent (Paul Ryan and Congress would like to get it into the low-to-mid 20s) from the current 35%—which is currently the highest

among the 35 members of the Organization for Economic Development—would boost wages in the long run by 15 percent to 20 percent and employment from 10 percent to 15 percent.

The Nobel Laureate Robert Lucas once remarked that getting rid of the tax on corporate profits and other capital income was the closest thing to a free lunch he had ever seen in economics. While such a radical change is not on the table, we do have an opportunity to dramatically alter a poor environment for U.S. businesses by cutting the corporate income tax. Doing so would benefit American workers as much as anyone.

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