As Congressional Democrats Push A Corporate Tax Hike, New Study Finds Repeal Would Boost Economy

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Speaker Nancy Pelosi (Calif.-D) and her new Democratic majority in the U.S. House of Representatives have already made clear they would like to raise the federal corporate tax rate, which was cut from 35% to 21% last year with passage of the Tax Cuts and Jobs Act (TCJA).

Meanwhile, there is new evidence out showing the economic harm caused by corporate taxation and benefits that would come from reducing corporate tax rates to zero. A new report by the Civitas Institute, a Raleigh, N.C.-based non-profit, found that eliminating North Carolina's state corporate income tax, already the lowest in the nation among the 48 states that impose a corporate or gross receipts tax on businesses, would increase worker salaries by an average of $1,500 and create more than 43,000 jobs over the next decade.

"Research shows that the state corporate income tax is the most harmful of all taxes to a state's economic growth," said Civitas President and CEO Donald Bryson. "North Carolina can take its positive economic momentum to the next level by eliminating this job-killing tax."

As recently as a half decade ago, North Carolina had one of the worst state business tax climates in the country. After North Carolina lawmakers enacted their landmark tax reform package 2013, which was improved upon with further rate reduction in 2015 and 2017, the state's business tax climate improved from being ranked as the nation's 44th best business tax climate (or, put another way, the seventh worst), according to the non-partisan Tax Foundation's annual State Business Tax Climate Index, to 12th place.

By eliminating the state corporate tax entirely, according to the new Civitas report, the state would further improve to having the fifth best state business tax climate in the U.S.

"North Carolina would not only be among the five best tax climates for business, but we could greatly curb the practice of state politicians picking winners and losers in our economy and apply a more fair tax code to hardworking North Carolinians," added Bryson.

Advocates for repealing corporate income taxes point out that they cause a great deal of economic pain for little revenue gain. According to the most recent Census data, state corporate income taxes generate only 5.3% of total state tax collections.

"Corporate income taxes represent a small and shrinking share of state revenue, the product of a long-term trend away from C corporations as a business entity and ever-narrowing bases due to the accumulation of tax preferences," writes Jared Walczak, an economist at the Tax Foundation.

“Although few states have repealed their corporate income taxes,” adds Walczak, “their volatility, narrowing bases, economic impacts, and modest contribution to state revenues have all contributed to states’ decisions to reduce reliance on the tax.”

This new Civitas report comes on the heels of non-partisan federal government scorekeepers’ decision to acknowledge, for the first time ever, that corporate taxes are borne in part by workers.

The Congressional Joint Committee on Taxation (JCT) announced in a 2013 study that, moving forward, the JCT would be reporting the effect that corporate taxes and corporate tax changes have on both labor and capital. JCT models had assumed that the burden of corporate taxes was borne entirely by the owners of capital (stocks, bonds, mutual funds, IRAs and so on) prior to that change five years ago.

In addition to that move by the JCT, the Congressional Budget Office and Treasury Department have made similar model adjustments in recent years to account for the share of corporate taxes borne by workers. It is a noteworthy achievement that by the end of the Obama administration, key non-partisan scorekeepers had all begun, for the first time, to formally recognize that corporate taxes are paid for, in part, by labor in the form of lower pay for workers, fewer benefits, and fewer job opportunities.

While the Tax Cuts and Jobs Act made it so the U.S. is no longer home to the highest corporate tax rate in the developed world, the U.S.’s corporate tax regime is now just barely internationally competitive when factoring in state corporate income taxes, which put the combined average federal-state corporate tax rate in the U.S. at 27% post tax reform.

“That is still higher than the 24% average of the OECD countries in 2018, according to KPMG,” writes Chris Edwards, the Cato Institute’s director of tax policy studies. "The global average rate per KPMG is also 24%."

“On corporate taxes," Edwards points out, "America is still a high-rate country.”

While further reduction in the federal corporate income tax rate will not happen for at least the next two years, given the makeup of Congress, governors and state lawmakers can still take action to reduce, phase out, or repeal their corporate levies like North Carolina and a number of other states have done in recent years. When it comes to opportunities for further corporate tax relief, at least for the foreseeable future, all the action will be in the states.