Corporate Tax Cut Required for Global Competitiveness, Cato Says

By: Stephanie Soong Johnston

September 21st, 2012

Lawmakers must reduce the statutory corporate tax rate and foster a more neutral tax base to remain globally competitive, according to a study released September 20 by the Cato Institute.

Lawmakers must reduce the statutory corporate tax rate and foster a more neutral tax base to remain globally competitive, according to a study released September 20 by the Cato Institute.

The report, written by Duanjie Chen and Jack Mintz from the University of Calgary's School of Public Policy, argues for a lower corporate tax rate with an updated list of corporate tax competitiveness rankings for 2012. The list ranks 90 countries based on their marginal effective tax rates (METRs), which take into account statutory rates, allowances, deductions and credits, and asset-based taxes and sales taxes on capital purchases. (For the full report, see Doc 2012-19663 .)

According to the study, whose preliminary findings were first presented at a joint Cato Institute and American Enterprise Institute event in May 2012 on Capitol Hill, the U.S. had the fourth highest METR on corporate investment at 35.6 percent, with Argentina, Chad, and Uzbekistan in first, second, and third place, respectively. (For prior coverage, see Doc 2012-11168 or 2012 TNT 101-7 .)

The U.S. METR is twice the average rate for the group of countries the authors analyzed. The high METR in addition to other factors, such as the high 35 percent statutory corporate tax rate and preferential corporate tax treatment, means the U.S. stands to lose big in the long run, according to the authors.

"This noncompetitive and nonneutral tax structure is harmful to growth, and it results in relatively low government revenues because the high rates induce businesses to shift their investments and profits abroad," Chen and Mintz wrote.

The authors cited as a as successful example the Canadian corporate tax reforms since 2000, which include a drastic federal statutory tax rate cut from 29.12 percent to 15 percent; a provincial tax rate decrease from 13.3 percent to 11.1 percent; and the elimination of special preferential treatment under the corporate income tax regime.

The Canadian government expected revenue losses, particularly in 2006-2007, but despite a cut in the corporate tax rate, it managed to maintain its corporate tax revenue. "I think it's remarkable that the revenues have stayed pretty constant despite the recession and despite the dramatic rate drop," Chris Edwards, director of tax policy studies at the Cato Institute, told Tax Analysts, adding that his research found that Canada did little to broaden the tax base.

Mintz and Chen recommended that Congress follow Canada's lead by reducing the federal statutory corporate tax rate by at least 10 percentage points and eliminating preferences to create a more neutral tax base. That would stimulate economic growth and without major long-term revenue losses, according to the report.

The authors advised state-level policymakers to make similar corporate tax rate cuts and to reform retail sales taxes and other levies that affect capital investment. Reducing the statutory corporate tax rate may have the added benefit of curbing profit shifting by companies like Google Inc., they said. (For related coverage, see Doc 2012-19683 .)

"Multinational companies, especially financial or services companies, seem to be able to get lower effective rates because it's easier to do profit shifting than a mainly domestic company like Wal-Mart," Edwards said. "And that's a key part of Mintz's argument -- he believes that the statutory rate is the driver for that kind of activity," he said.

"The problem always seemed to be that they wanted to make it revenue neutral, and as soon as you start doing that, you start talking about cutting back on things like R&D tax credits, which makes a lot of big corporations angry, and it's blocked," Edwards said. "So I think doing a revenue-neutral corporate tax cut, measured statically, is a wild goose chase. Whatever you cut back will be important to a lot of important companies and they are not going to get on board."