

Corporations Should Pay Higher Taxes?

It Just Ain't So!

The May 18 *Washington Post* article “Why Companies Pay Less” is less remarkable for what it says than for who is saying it. Its author is not Ralph Nader or Robert McIntyre of Citizens for Tax Justice. It is Steven Rattner, a well-known investment banker and a founder of the Quadrangle Group, a large private investment firm. Since it is unlikely that Rattner does not realize that his argument—that corporations are not paying their fair share of taxes—is based on a false premise—that corporations *pay* taxes—I can only conclude that he is being deliberately misleading.

In his article, Rattner reports sadly, “Over the past 50 years, the share of tax revenue coming to the federal government from business has collapsed. . . . In fiscal 2003 corporate taxes represented just 7.4 percent of federal revenue, down from 32 percent in 1952. . . . Corporate taxes as a percentage of our gross domestic product dropped to 1.2 percent in 2003, compared with as high as 6 percent in the early 1950s.”

In a defensive tone he denies that favoring tougher enforcement of the tax and the closing of “loopholes” is “populist or anti-business or redistributionist.” All he wants is what any tax system should aim for: “to distribute the burden fairly.”

The corporate income tax has always been the darling of the socialist left. For this group, whose true goal is to transfer increasing amounts of revenue from private to government control, it may be the perfect tax. It gives these self-proclaimed champions of the downtrodden a way to tax the very constituency they claim to represent, while leading that constituency to believe the tax is being imposed on its “oppressors.” Indeed,

corporate taxes are the most dishonest taxes used by any level of government.

It is curious that Rattner would call for a fair distribution of the tax burden on corporations, because as Rattner clearly must know, corporations *pay no taxes*. They appear to pay taxes, but as Henry Hazlitt would remind us, we need to look past appearances to see the true effects of economic policies.

Corporations pay no taxes not because of the litany of loopholes and special breaks that Rattner lists in his article or because of “the . . . sophistication of large multinational corporations in . . . shifting profits to countries with lower tax rates.” It is because corporations *can't* pay taxes. All taxes, corporate or otherwise, must come out of some real human being's pocket.

All this is well known and not at all controversial. Yet Rattner does not even hint at the possibility that the true burden of the corporate tax may be borne by exactly those taxpayers he is presumably championing in his article. The unstated implication of Rattner's argument is that customers of corporations are paying too little for their products; employees of corporations are being paid too much for their work; and shareholders, even retirees and those putting a few dollars a month into IRAs and 401ks, are getting too much in return for their investments.

But even if corporate taxes were transparent to those who pay (in which case they probably wouldn't exist), they would still violate every important principle of sound tax analysis. Again, this is a point that Rattner cannot credibly claim to misunderstand. While there is no such thing as an efficient tax, some forms of taxation clearly do more economic damage than others.

A basic principle of taxation is that the tax system should seek to minimize the extent to which some market decisions are favored over others. This means that income should be taxed only once.

Double, Triple Taxation

But the corporate income tax introduces double and in some cases triple taxation into the system. A worker at Wal-Mart pays personal income tax on a salary that has already been reduced by the corporate income tax.

Wal-Mart's customers are taxed at least twice. Their purchasing power is reduced when they pay tax on their income. Then it is further reduced when the corporate tax raises the prices they pay at the cash register.

A shareholder in the company faces triple taxation. First, when any income is taxed, the tax by definition reduces the potential income stream—interest, dividends, and capital gains—that the income can generate. Second, dividends and capital gains are

reduced further by the corporate income tax. And third, when dividends and capital gains are finally earned, they are taxed as part of the investor's personal income.

Corporate taxes are hidden and fraudulent. The people who pay them do not know they pay them, and thus such taxes help mask the actual cost of government. If it is true that companies are finding ways to avoid these taxes and less revenue is being generated, then we should cheer those companies on. Ultimately corporate taxes should be abolished. Lovers of big government have no better friend than a tax that everyone thinks someone else pays.

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Instead of What?

All subsidy measures, all schemes to redistribute income or to force Peter to support Paul, are one-eyed as well as shortsighted.

They get their immediate appeal by focusing attention on the alleged needs of some particular group of intended beneficiaries. But the inevitable victims—those who are going to be asked to pay for the new handout in increased taxes (which directly or indirectly means almost everybody else)—are left out of account.

Only one-half of the problem has been seen. The cost of the proposed solution has been overlooked.

The vast majority of would-be social reformers think of the “cost” of something as simply its money cost; and they persistently underrate or dismiss even this because they think of money as something that can be turned out at will by a government printing press. But when economists talk of cost in the broader sense they mean whatever alternate opportunity must be forgone in order to produce the thing that is made. Everything we make, and everything we do, must be at such a cost. For every alleged benefit that the politicians confer upon us, they must necessarily deprive us of something else.

I have not raised here the political and moral issue involved when governments extend and pervert their powers to expropriate part of the earnings of Peter to turn them over as a handout to Paul, or force both to “buy” something with their earnings quite different from what either would have bought of his own free will. But even if we put aside this basic issue, the next time the politicians offer us some alleged economic gift, let us at least ask them the question: Instead of what?

—Henry Hazlitt, *The Freeman*, March 1976