U.S. Corporate Taxes Now 50 Percent Higher than OECD Average

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Amid rising concerns about the state of the U.S. economy, new data compiled by economists at the OECD shows that for the 17th consecutive year the average rate of corporate taxes in non-U.S. countries fell while the U.S. corporate tax rate stayed the same. As a result, the overall U.S. corporate tax rate is now 50 percent higher than the OECD average.

Combined with another new OECD study that calls the corporate income tax the most harmful type of tax for economic growth, the implications for U.S. policy are clear. The long-term prospects of the U.S. economy are at risk as long as our corporate tax rate remains out of step with the rest of the world.

The U.S. continues to have the second-highest combined federal-state corporate tax rate among industrialized countries at 39.3 percent. Only Japan has a higher overall corporate tax rate at 39.5 percent. By contrast, the average corporate tax rate among OECD countries has fallen a full percentage point in the past year, from 27.6 percent to 26.6 percent. Ireland's 12.5 percent corporate tax rate remains the lowest among OECD nations.

The OECD data shows that nine of the 30 OECD member nations have lower corporate tax rates in 2008 than in 2007, including Canada, Germany, New Zealand, Spain, the United Kingdom, Italy, Switzerland, the Czech Republic and Iceland. Germany made the biggest change, cutting its corporate rate 8.7 percentage points from 38.9 percent to 30.18 percent. As a result, Germany fell from having the third-highest overall rate to seventh-highest. France now imposes the third-highest rate of 34.4 percent.

Italy had the second-largest rate cut, lowering its rate 5.5 percentage points, from 33 percent to 27.5 percent. As a result, Italy dropped in the rankings from seventh-highest to fifteenth-highest. Canada, meanwhile, dropped from fourth- to fifth-highest after cutting its overall corporate rate from 36 percent to 33.5 percent.

The new OECD rankings are only the latest indication of the wave of corporate tax cutting that is sweeping the globe. According to the World Bank's *Doing Business 2008*, 20 non-OECD countries cut their corporate income taxes in 2007.[1] These corporate rate changes include:

- Bulgaria, from15 percent to 10 percent
- Turkey, from 30 percent to 20 percent
- South Africa, from 12.5 percent to 10 percent
- Columbia, from 35 percent to 34 percent
- Israel, from 31 percent to 29 percent
- Malaysia, from 28 percent to 27 percent

This year, Asian countries have been very aggressive on the tax front. China's new 25 percent corporate tax rate, down from 33 percent, went into effect in January. Meanwhile, the Korean government has announced that it will cut its corporate rate from 25 percent to 22 percent, Taiwan is considering cutting its 25 percent corporate rate to 17.5 percent, and Hong Kong will cut its rate from 17.5 percent to 16.5 percent. In response to these developments, a Japanese advisory panel has called upon the government to cut Japan's corporate tax rate to remain competitive and avoid discouraging foreign investment.[2]

The empirical evidence from the new OECD study suggests that "investment is adversely affected by corporate taxation through the user cost of capital," meaning the after-tax return on investment. Looking at the firm level, OECD economists found that the effect of corporate taxes is strongest on industries that are older and more profitable because of their larger tax bases. Younger and smaller firms (*i.e.* start-ups) are less affected because they are less profitable.

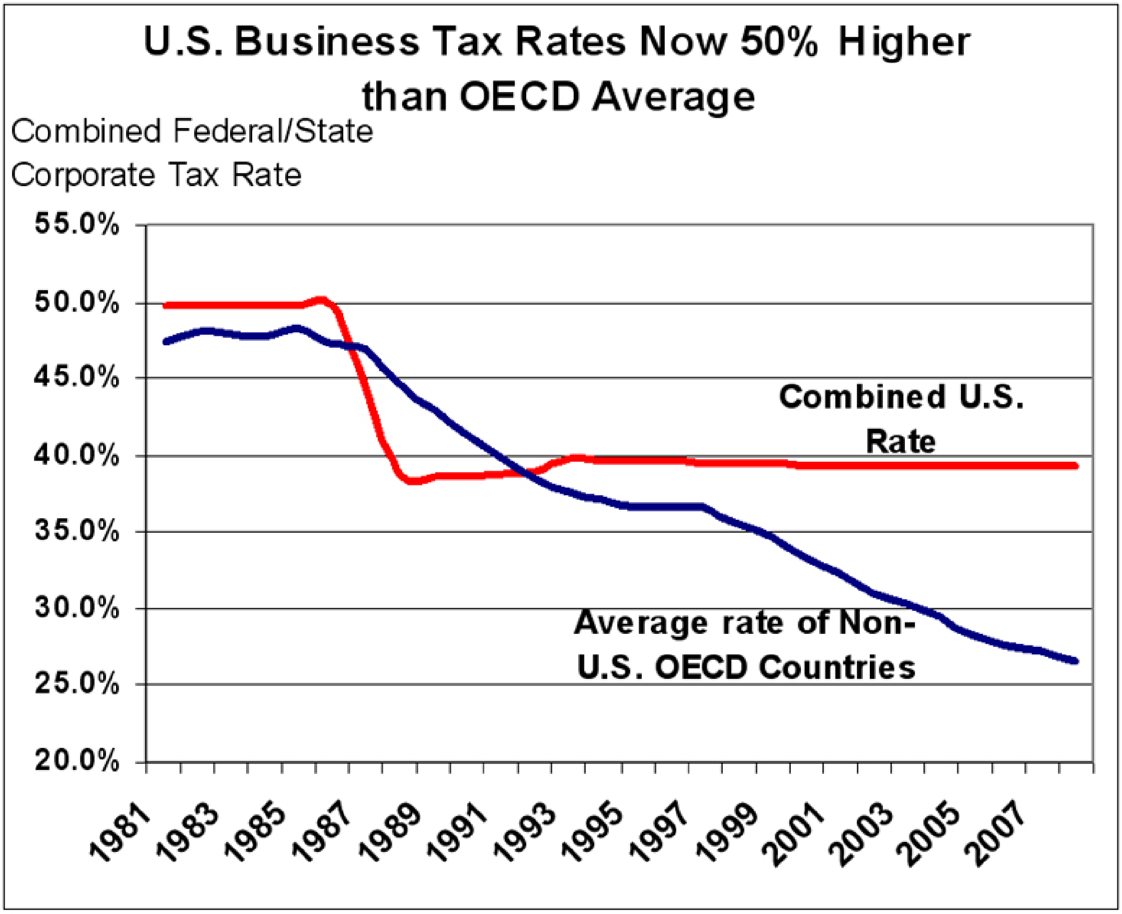
The OECD study also found that statutory corporate tax rates have a negative effect on firms that are in the "process of catching up with the productivity performance of the best practice firms." This suggests that "lowering statutory corporate tax rates can lead to particularly large productivity gains in firms that are dynamic and profitable, *i.e.* those that can make the largest contribution to GDP growth."[3]

The main recommendation of the study is that if countries want to enhance their economic growth they would do well to move away from income taxes—especially corporate income taxes—toward less distortive taxes such as consumption-based taxes. The key to creating a growth-oriented corporate income tax system is to impose a reasonably low tax rate with few exemptions.

The release of these two OECD studies could not have come at a better time for the current political debate over how to move the U.S. economy forward. A U.S. corporate tax rate 50 percent higher than the OECD average should be a wake-up call to Washington, especially when combined with the empirical evidence that corporate taxes are the most harmful tax on economic growth. The question remains for the presidential candidates, What is your plan to restore American competitiveness?

Table 1
OECD Nations Continue Cutting Corporate Tax Rates While U.S. Stands Still
Statutory Rates, Federal Plus Provincial/State, 2007 and 2008

Rank	Country	Combined Corporate Income Tax Rate 2008	Combined Corporate Income Tax Rate 2007	Change from 2007 to 2008
1	**Japan**	39.54	39.54	0.0
2	**United States**	39.25	39.26	0.0
3	**France**	34.43	34.43	0.0
4	**Belgium**	33.99	33.99	0.0
5	**Canada**	33.50	36.12	-2.6
6	**Luxembourg**	30.38	30.38	0.0
7	**Germany**	30.18	38.9	-8.7
8	**Australia**	30.00	30.0	0.0
9	**New Zealand**	30.00	33.0	-3.0
10	**Spain**	30.00	32.5	-2.5
11	**Mexico**	28.00	28.0	0.0
12	**Norway**	28.00	28.0	0.0
13	**Sweden**	28.00	28.0	0.0
14	**United Kingdom**	28.00	30.0	-2.0
15	**Italy**	27.50	33.0	-5.5
16	**Korea**	27.50	27.5	0.0
17	**Portugal**	26.50	26.5	0.0
18	**Finland**	26.00	26.0	0.0
19	**Netherlands**	25.50	25.5	0.0
20	**Austria**	25.00	25.0	0.0
21	**Denmark**	25.00	25.0	0.0
22	**Greece**	25.00	25.0	0.0
23	**Switzerland**	21.17	21.32	-0.1
24	**Czech Republic**	21.00	24.0	-3.0
25	**Hungary**	20.00	20.0	0.0
26	**Turkey**	20.00	20.0	0.0
27	**Poland**	19.00	19.0	0.0
28	**Slovak Republic**	19.00	19.0	0.0
29	**Iceland**	15.00	18.0	-3.0
30	**Ireland**	12.50	12.5	0.0
	OECD Average	26.6	27.6	-1.0



Notes

1. *Doing Business 2008*, The International Bank for Reconstruction and Development/The World Bank, 2007

2. Yoko "Nishikawa, Japan tax overhaul key for corporate tax cut: LDP," Reuters, July 2, 2008
http://www.reuters.com/article/JapanInvestment08/idUSTFD00295620080702

3. "Tax and Economic Growth," Economics Department Working Paper No. 620, July 11, 2008. Organization for Economic Cooperation and Development. P. 9.
http://www.olis.oecd.org/olis/2008doc.nsf/LinkTo/NT00003502/$FILE/JT03248896.PDF

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