Discussion of R. Avi-Yonah, *Reinventing the wheel*

Stuart Adam, Institute for Fiscal Studies

Oxford University Centre for Business Taxation 9th Annual Symposium

Saïd Business School, Oxford, 23 June 2015

The approach

- Draws on both legal and economic literatures
  - Plus an all-too-rare historical perspective
  - Combines theory, empirical evidence and institutional detail
- Considers different parts of the system and how they fit together
- Acknowledges political reality while still considering radical options
- Makes specific recommendations

➢ All thoroughly admirable!

The proposal

1. 28% top marginal rate of personal income tax
   – Applied to all income including dividends and capital gains

2. 28% rate of corporate income tax
   – Applied immediately to worldwide profits of US-headquartered firms
   – Accelerated depreciation and domestic manufacturing deduction ended

3. Classical approach to personal-corporate interaction
   – Double taxation of corporate-source income: no imputation credit or tax exemption/reduction for dividends

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1. Personal taxation

- Critique of optimal tax literature
  - Neither very low nor very high marginal rates at the top seem sensible
  - Labour supply, avoidance and migration all significant
- Some concerns with reading of the economic literature and evidence
  - e.g. significance of demogrants; evidence on tax avoidance

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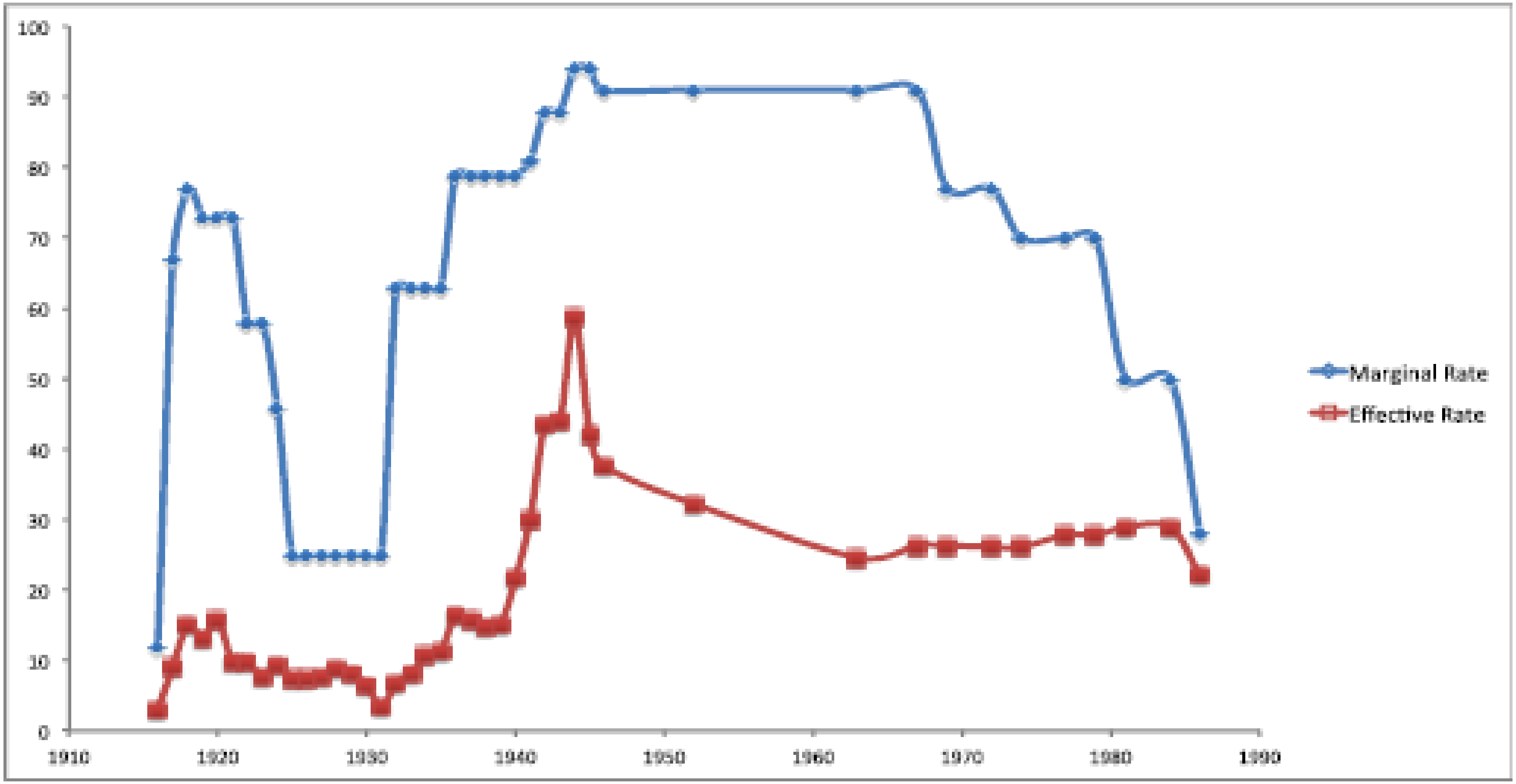
Evidence of avoidance among the top 1%?



Source: Brownlee, in Slemrod (ed), Does Atlas Shrug (2000).

1. Personal taxation

- Critique of optimal tax literature
  - Neither very low nor very high marginal rates at the top seem sensible
  - Labour supply, avoidance and migration all significant
- Some concerns with reading of the economic literature and evidence
  - e.g. significance of demogrants; evidence on tax avoidance
- Agree that 0% too low, 73% too high – but why 28%?
- Tax capital gains at 28%
  - No evidence that rate affects saving and investment
  - But (absent accruals taxation) keep low to minimise lock-in effects
  - Risk of conversion then necessitates low rate on ordinary income too
  - But again, why is 28% and exact alignment the right balance?
  - Key arguments missed: effects on work incentives; consistent treatment of all savings

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2. Corporate taxation

- Move to full worldwide taxation with no exemption or deferral
  - Well-known disadvantages avoided if rest of G20 follow suit
  - But would they? Lots of areas where others don't follow US. Still a good idea if they don't?

- 28% tax rate
  - Reduce from 35% as companies and profits mobile
  - Match top personal rate 'so that the choice between C-corporations and pass through entities is not distorted'
  - But avoiding distortions requires aligning *overall* rates, which this does not achieve – indeed paper argues against it…

3. Interaction of personal and corporate taxes

- Classical approach: tax at both levels with no ‘integration’
- ‘Standard’ distortions exaggerated
  - But distortion (and inequity) between corporate-taxed and personal-taxed forms still seems problematic to me
- Argues integration creates its own distortions when other countries classical
  - But not clear biases are the fault, or the problem, of the country choosing integration

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Summary

- Big, important questions and an admirably broad view of them
- Some arguments convincing; others less so
  - I still favour territoriality and personal/corporate integration
  - Can solve many problems by applying full rates to capital income but with allowances for amounts saved/invested
- Specific numerical recommendations demand numerical inputs
  - Why 28% rather than e.g. 23% or 33%?
  - ‘designed to be revenue neutral overall’ – but does it achieve that?
- Much depends on the politics / political economy
  - What might US politicians (and voters) actually be persuaded to adopt?
  - Would other countries follow a US lead to worldwide taxation?
  - If the 1986 settlement was good, why did it not last?

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