Ask the Experts: Should Corporations Pay Less than Consumers?

Get ready to take some notes because WalletHub is taking you back to school! More specifically, we turned to some of the foremost experts in the fields of accounting and tax law in search of insights into the country's current corporate tax system as well as potential fixes to it. You can check out the questions we posed as well as their responses below.

1. Is the U.S. leaving money on the table with the current corporate tax structure?
2. What would you change about the way U.S. corporations are taxed?
3. Do you consider tax-inversion deals to be unpatriotic?
4. What should the relationship be between corporate and consumer taxes?

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Is the U.S. leaving money on the table with the current corporate tax structure?

There are a number of things that are globally uncompetitive about U.S. corporate income tax rates. Firstly, the U.S. has a double tax system whereby the profits earned by a company are taxed, and then they are taxed again in the hands of shareholders. It is really an internationally uncompetitive tax system. There are a number of ways to minimize double tax, and in the USA many CPAs/tax advisors have businesses established as a S corporation or use LLCs which are taxed as partnerships/sole proprietorships. However, this is not an option for U.S. public companies, as they must be C corporations. Remember, the majority of income taxes (federal and state) are paid by individuals.

Secondly, the U.S. taxes U.S. corporations on a worldwide basis, unlike other countries that tax on a territorial basis, such that corporations based in those countries only pay tax on earnings made in that country. Other countries have a participation exemption such that dividends and capital gains earned by those corporation are not subject to corporate income taxes.

Thirdly, the U.S. has the highest corporate income tax of any OECD country, when you combine federal and state income taxes. If you compare corporate tax rates for OECD countries from 1999 to 2015, you will see the majority have reduced their rates, but the U.S. has remained the same. The US is no longer globally competitive in relation to corporate income tax rates. Corporate income taxes are a significant cost for any global business, let alone for U.S. MNCs trying to compete on the global stage.

Many people in Congress seem to think that lowering the corporate income tax rate will lower tax receipts, but firstly more income taxes are collected from individuals, and secondly, I do not think consideration is paid to the encouragement a lower corporate income tax rate could play in encouraging more investment into the USA, such there would be more businesses operating in the USA, with more people employed and more income taxes paid by those employed in the new businesses. You only need to look at the UK economy to see what lowering the corporate income tax rates has done for the economy. The UK employment rate has been increasing and they have had positive growth. You can also look what happened to the German economy between 1999 and 2009; the corporate tax rate lowered and Germany has a very strong economy. I provide U.S. tax advice to many businesses who are looking to commence operations in the USA and then expand into Central and South America, and I advise them not to use the USA as a holding company to expand into Central and South America due to the U.S. corporate income tax rate and the structure of taxing U.S. corporations on a worldwide basis.

So, in summary, for all of the above reasons I believe the U.S. is leaving money on the table with the current corporate tax structure.

What would you change about the way U.S. corporations are taxed?

If you are going to leave at the U.S. corporate income tax at the highest of any OECD country, then adopt an exemption system for foreign earnings. We already have complex international tax rules to discourage shifting income offshore for easily shifted profits – the subpart F rules were introduced in 1962 to discourage such behavior. However, I believe in competition, and if a country has the highest corporate tax rate (this is the combination of federal and state income taxes) then perhaps consideration should be given to make the rates globally competitive. If we have free trade agreements to given to make the rates globally competitive. If we have free trade agreements to encourage global movement of business, then businesses are going to consider where tax rates are globally competitive.

As noted above, I provide U.S. tax advice to many businesses who are looking to commence operations in the USA and then expand into Central and South America, and I advise them not to use the USA as a holding company to expand into Central and South America due to the U.S. corporate income tax rate. In addition, the USA has very few tax treaties in South America. So well as exempting foreign earnings (derived from non-subpart F income activities), I would also develop a better tax treaty network with countries in South America.

Do you consider tax inversion deals to be unpatriotic?

If you believe the role of management is to provide the highest EPS to shareholders, in a legal and ethical manner, then lowering the overall ETR (effective tax rate) should be like lowering any other cost to the business. So if the corporation is operating in a high cost environment, responsible management would seek a lower cost environment. It is sad to see the flight of business from the USA, but understandable when it costs 39% of earnings before tax and in fact I am surprised more lawyers are not lining up to sue management of companies that choose to remain in the USA for not maximizing profits to shareholders. Remember, inversions do not stop corporations paying U.S. taxes on business in the USA; it just means they do not pay profits on earnings outside the USA (broad statement), and when dividends come back to the ultimate U.S. shareholders, U.S. income tax is paid as the U.S. has a double taxation system – one corporate level of taxes, and another at the shareholder level.

So I do not consider tax inversion deals unpatriotic, and believe if the U.S. corporate tax system stays at the high rate of 39% (federal and state), and U.S. companies cannot invert, then non-US MNCs will buy those companies as they can afford to purchase the shares, as the on-going operations will have a lower ETR and thus lower EPS.

What should the relationship be between corporate and consumer taxes?

As you may be aware, there is no uniformity as sales taxes are imposed at the state, county and city levels and the exemptions and application and rates all differ. The cost to business is very expensive to maintain the necessary systems to capture, charge, register, remit, etc. Ultimately, consumer taxes should be paid by the consumers in a way that is easily understood and administered – some of the necessary characteristics for an efficient tax system. The USA is one of the few developed tax systems without a VAT/GST – however, it should be uniform and easy for everyone to understand. Interesting enough, most U.S. businesses can obtain refunds of EU VAT, except in Italy.

The Italian tax system only allows the VAT refund for a non-Italian business if the country where the business operates allows for VAT refunds. As the USA does not allow for VAT refunds, U.S. businesses incur Italian VAT when sourcing from businesses in Italy. I will

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