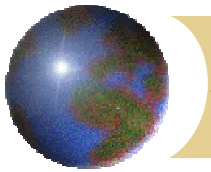


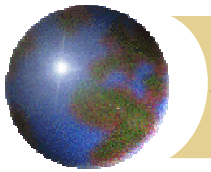
Should Governments Compete or Collude?

**Tax Competition: A Liberalizing
Force in the Global Economy**



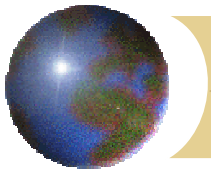
What is Tax Harmonization?

- ✿ Tax harmonization exists when taxpayers incur similar tax rates regardless of where they work, shop, save, or invest.
- ✿ Tax harmonization can be explicit (rate-setting) or implicit (information-sharing), but the impact is similar since taxpayers are unable to benefit from lower tax rates in other jurisdictions.
- ✿ Proponents argue that harmonization reduces distortions caused by differential tax rates.



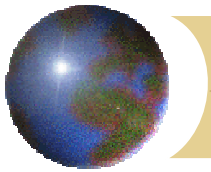
What is Tax Competition?

- ❖ Tax competition exists when jobs, capital, and entrepreneurial talent are able to escape high-tax jurisdictions.
- ❖ This puts pressure on politicians to lower tax rates and reduce tax burden on capital.
- ❖ Proponents argue that tax competition is a “race to the top” by encouraging pro-growth tax policy.
- ❖ Competition may reduce size of government.



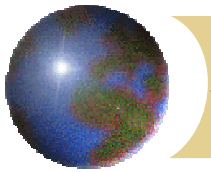
Three Real-World Examples

- Nations all around the world had to lower tax rates in response to the Thatcher and Reagan rate reductions.
- Western European nations have been reducing corporate tax rates in response to Ireland's 12.5 % rate.
- Led by the Baltic nations and Russia, governments in Eastern Europe are implementing tax reform.



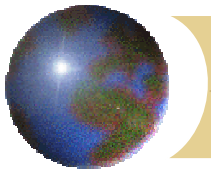
If Tax Reform is Good, then Tax Competition Should be Celebrated

- ✚ A growth-maximizing tax system will have low rates and tax economic activity only one time.
- ✚ But organized interest groups often pressure governments to impose high tax rates and create tax biases against capital.
- ✚ Tax competition creates an offsetting pressure, thus encouraging governments to implement pro-growth tax policy.



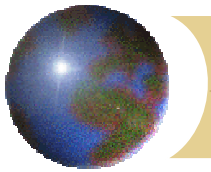
Competitive Harmonization

- ❖ Supporters of harmonization are correct in noting that tax rate differences may cause inefficient allocation of resources.
- ❖ Opponents of harmonization are correct in noting that an “OPEC for politicians” will facilitate higher tax rates and destructive treatment of capital.
- ❖ Tax competition is the best of all worlds since it will drive down tax rates and theoretically cause tax systems to converge.



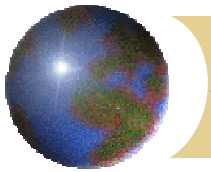
What About Tax Evasion? One Good Answer, One Bad Answer

- ❖ Tax evasion is not to be condoned, at least if a government is honest and tax rates are reasonable.
- ❖ The real issue is how to reduce tax evasion: Reforming the tax system or creating a global tax cartel.
- ❖ Tax reform works, increasing taxable income both because of faster growth and better reporting.
- ❖ A global network of tax police may improve reporting, but surely will reduce the tax base.



Other Issues are Important

- ⊕ OECD and EU tax harmonization schemes have implications in non-tax fields.
- ⊕ National sovereignty.
- ⊕ Human rights.
- ⊕ Constitutional freedoms.
- ⊕ The money-laundering red herring.
- ⊕ US self-interest.



Concluding Thoughts

- ❖ Proponents say harmonization does not mean higher tax rates, but French and Germans are biggest advocates.
- ❖ We are told that national differences in tax rates will cause profound differences in behavior, but the same people also tell us that lower tax rates have no impact on behavior.
- ❖ Adam Smith is right.