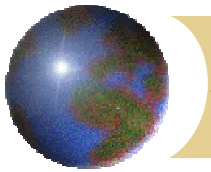


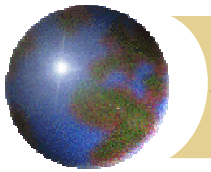
# *Should Governments Compete or Collude?*

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



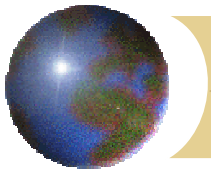
## *What is Tax Harmonization?*

- ✿ 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.



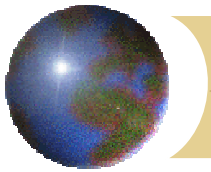
# *What is Tax Competition?*

- ❖ 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.



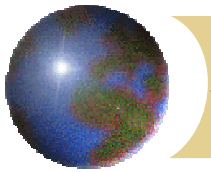
## *Three Real-World Examples*

- 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.



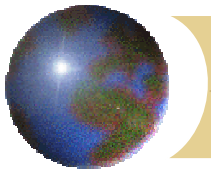
# *If Tax Reform is Good, then Tax Competition Should be Celebrated*

- ✚ 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.



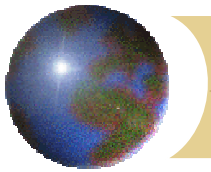
# *Competitive Harmonization*

- ❖ 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.



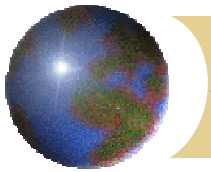
# *What About Tax Evasion? One Good Answer, One Bad Answer*

- ❖ 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.