THE BIDEN ADMINISTRATION'S PROPOSED GLOBAL MINIMUM TAX

Outsourcing America's Sovereignty and Undermining Its Economic Edge

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INTRODUCTION

The Biden administration has proposed raising taxes on U.S. firms to expand social safety net programs and impose its vision of economic "fairness," with the result being a European-style cradle-to-grave welfare state. The proponents of these policies claim that they will only raise taxes on corporations and the wealthy to ensure they pay their "fair share." However, both the historical precedent of broken tax promises and the mathematical reality that the proposed multi-trillion dollar spending plans vastly exceed the amount of money that can be extracted from just the top income-earners show the limits of such arguments. Moreover, the idea that C-suite executives will suddenly start cutting personal checks to pay their firm's corporate tax bill does not square with well-established economic evidence, which has found time and again that customers, workers, and the millions of Americans who have ownership stakes in companies through their retirement accounts also share considerably in the burden of corporate taxation (Baker, Sun, and Yannelis 2020; Suárez-Serrato and Zidar 2016; Auerbach 2006). By its very design, U.S. leadership in negotiating and crafting this Global Minimum Tax (GMT) is an admission that the domestic economic programs proposed alongside it put the U.S. economy at a strategic disadvantage, risking a flight of U.S. capital and innovation to foreign countries.

The Trump administration's 2017 Tax Cuts and Jobs Act (TCJA) provided significant tax relief to U.S. firms and the middle class, helping fuel the strongest economy in many years, leading to record high income gains for working Americans and record low poverty. This same focus on families and businesses undergirded the Trump administration's unprecedented economic response to the global pandemic, resulting in the quickest end to a recession in modern U.S. history (NBER Business Cycle Dating Committee). Unfortunately, the Biden administration's proposed tax increases—coupled with its ongoing destruction of work incentives and wasteful, inflationary spending—threaten to undermine the Trump administration's record economic recovery and also diminish longer-term U.S. economic prospects (Rachidi, 2021).

Among numerous current proposals to increase the tax burden on U.S. firms—and reverse, in part, the Trump administration's efforts to reduce that burden—is a multinational plan that in particular stands as an affront to the America First policy agenda. The Biden administration, in coordination with foreign governments, has proposed a GMT that will erode American sovereignty and undermine U.S. competitiveness. Rather than seeking to enhance America's ability to compete on the world stage, Treasury Secretary Yellen has instead emphasized governments "collaborating with one another" to prevent a "race to the bottom" and to put "an end to harmful tax competition." Whether it is businesses illegally colluding to prevent price decreases or governments "cooperating" to prevent tax cuts, the threat to peoples' pocketbooks is clear. The end result is a move away from America's heritage of free enterprise, national strength, and global competition toward a stultifying vision of European welfare state conformism.

THE GMT IS AN AFFRONT TO AMERICAN SOVEREIGNTY AND CORE CONSTITUTIONAL PRINCIPLES

The Biden administration's approach to the GMT negotiations is part of a worrying trend that erodes U.S. sovereignty and threatens American Constitutional traditions. The proper course for advancing a federal tax policy is not a mystery. The U.S. Constitution provides Congress the power "to lay and collect taxes, duties, imposts and excises" (U.S., 1787). The system is designed so that the Congress drafts legislation pertaining to taxation in consultation with the executive branch. Should a tax bill become law after congressional approval and the President's signature, the executive branch implements and ensures the law is upheld. This is the course of action followed in the passage and implementation of TCJA under the Trump administration, the most sweeping overhaul of the tax code in thirty years (CEA, 2021).

However, certain administrations are increasingly adopting a dangerous strategy of bypassing Congress by seeking agreements with foreign governments in order to create a false justification for advancing their unpopular domestic goals that require new legislation. For example, 63 percent of voters believe the Green New Deal would increase energy costs and reduce America's energy independence, and more people believe that it would destroy the U.S. economy than believe it would stop climate change (Rasmussen, 2021). Pursuing deeply unpopular policies without the approval of Congress is an implicit recognition that such policies are unlikely to otherwise become law. The Clinton administration pursued this approach with the Kyoto Protocols and the International Criminal Court. The Obama-Biden administration used this process with the Paris Agreement and the Iran Nuclear Deal. Now the Biden administration is trying the same exact strategy with the GMT.

So why is the Biden administration bothering with an international agreement that itself cannot create legal obligations beyond the executive's existing authority? Most likely, the Biden administration hopes to conclude an international agreement on the GMT and then lobby Congress to pass harmful tax hikes on the basis that there is international consensus for such action. The Biden administration will likely argue that the United States must satisfy its international obligations, when in fact the United States has no such obligations because the Biden administration's GMT agreement does not have the force of domestic law in the absence of congressional action (Miller & Chevalier, 2021). This scheme undermines congressional authority and threatens U.S. sovereignty. Tax policy best serves Americans when it is designed and debated by Americans' elected representatives.

If the Biden administration is permitted to move forward with the GMT, it will set a harmful precedent that will likely expose American citizens to policies that are designed to benefit the interests of international actors rather than American taxpayers. Political agreement on the GMT will be followed by an immensely complex exercise to develop the technical rules that would need to accompany a GMT. This process – convened through the Organisation for Economic Co-operation and Development (OECD) – will likely reflect the interests of OECD bureaucrats and foreign governments more than the interests of American taxpayers. If the Biden administration is permitted to set the precedent of changing U.S. law in order to comply with a potential GMT, it will increase the likelihood that future OECD recommendations and agreements are adopted into U.S. law under the same process. If history is any guide, once this tax precedent is established, it is likely there will be more international agreements that liberals try to use to raise taxes and advance their progressive agenda.

THE GMT FACILITATES THE BIDEN ADMINISTRATION'S PLANS FOR DAMAGING DOMESTIC TAX HIKES ON AMERICAN WORKERS AND COMPANIES

Proponents of the GMT suggest that the central goal of the policy regime is to address the erosion of the tax base and the shifting of profits by multinational corporations to lower tax jurisdictions (OECD, 2020). In their attempt to arrest what they claim is a "race to the bottom" (White House, 2021), however, these proponents often implicitly admit to the uncompetitive nature of domestic tax policy. It is not a coincidence that the Biden administration's spearheading of the GMT abroad coincides with its push domestically to raise the statutory U.S. corporate income tax rate from 21 percent to 28 percent (Treasury, 2021). This coordinated timing serves as a tacit admission of the damaging effects of such corporate tax hikes. These fears are well-founded. Raising the domestic tax rate on corporate income would incentivize U.S. firms to shift investment abroad. Prior to the passage of TCJA, an increasingly uncompetitive corporate tax rate relative to the average in other advanced economies led to the share of foreign earnings that U.S.-based multinational corporations invested abroad nearly doubling between 1990 and 2016 (CEA, 2017; CEA, 2018). Especially now, as the U.S. economy emerges from the sharp pandemic-related economic contraction, strong domestic investment will be necessary to support long-lasting, non-inflationary economic growth. To counter the negative effects of domestic tax hikes, the Biden administration's push to simultaneously raise the tax rate on the foreign earnings of U.S. firms serves as an effort to confront and partially offset the incentive to shift investment abroad resulting from the proposed higher domestic corporate tax rate. This tacit admission of the uncompetitive nature of the Biden administration's tax proposals is further supported by their own economic projections—assuming the implementation of these, among other, policies. Forecasting historically low growth over the next decade, it is clear that the Biden administration does not believe their proposed tax policies will lead to the more robust growth rates of the pre-pandemic era.

By Its Own Admission, There Is Little Upside to the Biden Administration's Fiscal Policies

Just weeks before the Biden administration secured the G7 endorsement of its GMT proposal, it released yet another admission that its proposed policies should not be expected to deliver strong long-run economic growth. Despite promising trillions of dollars in new spending and tax hikes, the Biden administration in its Fiscal Year (FY) 2022 budget, and subsequent mid-session review, forecasts that its policies will fail to significantly improve economic growth (OMB, 2021a, OMB 2021b). In fact, the administration's FY 2022 budget forecast of average economic growth in the long-run—assuming implementation of most of the policy proposals so far announced—is among the lowest projections from the past five decades. Nearly every administration's budget proposals include a set of economic assumptions that underpin its forecasts. These assumptions are policy inclusive, that is, they presuppose that the policies proposed by the administration in the budget will in fact be implemented. As a result, closely examining these economic assumptions offers insight into how the administration believes its own policies will affect economic growth and the labor market in addition to debt and deficits.

The economic assumptions in the mid-session review of the FY 2022 budget proposal include projections for growth from calendar year 2021 through 2031. Under the Trump administration, real GDP growth exceeded 2.0 percent in each year of the 2017-19 period before the pandemic-recession of 2020. While growth averaged 2.5 percent over the 2017-19 period, the Biden administration is forecasting average growth of 2.3 percent over the 2022-2031 period. Although 2021 falls within the forecast window, pandemic base effects and policies of the Trump administration—namely the unprecedented fiscal support in the Coronavirus Aid, Relief, and Economic Security (CARES) Act rescue package and the record vaccine development and deployment facilitated by Operation Warp Speed—make its inclusion in the average growth forecast not reflective of the Biden administration's expectations for growth after its budget is implemented. To the extent the administration believes its proposed policies—including the trillions of dollars in spending proposed in the American Jobs Plan and American Families Plan—will have a growth effect, the effect is extremely short-lived. Following its forecast of real GDP growth of 7.1 and 3.3 percent, respectively, in 2021 and 2022, the Biden administration expects growth to fall to 2.2 percent in 2023 and 1.8 percent in 2024. To put 1.8 percent growth in perspective, this would be the lowest growth rate in any non-recession calendar year since 2012, when the country was experiencing the weakest economic recovery in its history (CEA, 2021).

Finally, the Biden administration's own forecasts may not fully account for inflationary pressures—at least in the short term—that will weigh on its real growth projections. Thus far in 2021, the inflation rate—as measured by the headline Consumer Price Index (CPI)—is 6.6 percent at an annual rate over the first eight months of the year. Meanwhile, the administration forecasts a CPI inflation rate for 2021 of 4.8 percent. To achieve that low of a rate, month-over-month CPI inflation for the remainder of the year would have to be roughly flat, an unlikely scenario. Higher consumer price inflation experienced thus far will bleed into overall inflation as measured by the GDP chained price index, which is the index used to adjust nominal GDP to real GDP. As a result, the administration's forecast for real GDP growth of 7.1 percent in 2021 may be revised down in future forecasts as higher-than-projected inflation partially erodes nominal gains. Were inflation to persist, so too would the inflationary erosion of the Biden administration's real GDP growth forecasts. In short, even by the Biden administration's own projections, the upside potential of its trillions of dollars in spending and taxes is quite low; meanwhile, families and businesses are left dealing with considerable uncertainty and downside risk about their economic prospects.

False Rhetoric from the Biden Administration on International Comparisons of Corporate Taxation

In defense of their proposals to raise the tax burden on corporations, proponents have cited the United States' relatively low ranking amongst OECD economies when measuring corporate income tax revenues relative to the size of the economy (Treasury, 2021). Measuring corporate income revenue as a percent of GDP, however, dismisses the importance of the noncorporate sector—a burgeoning and critical sector in the United States, especially relative to other advanced economies. Pomerleau and Schneider (2021) find through their analysis that the U.S. position on such a ranking changes substantially after accounting for the large noncorporate—or pass-through—business sector in the United States and the collection of revenues from that large sector. The authors adjust for the large U.S. pass-through sector in addition to adjusting for cross-country variation in depreciation—which affects the net income measured in the rankings of corporate income as a share of GDP. Prior to these adjustments, the United States ranks at the bottom among 30 OECD economies and far below the OECD average. After these necessary adjustments in measuring business revenues as a share of GDP, the United States ranks 12 out of 30 OECD economies, and above the OECD average (Pomerleau & Schneider, 2021). What is more, post-adjustment, by implementing the Biden administration's proposed tax policies, the U.S. ranking would rise from 12 to 4, making the business tax burden in the United States among the highest of all advanced economies.

TAX COMPETITION IS HEALTHY FOR THE U.S. ECONOMY AND IMPROVES THE LIVES OF AMERICAN WORKERS & FAMILIES

The case for a GMT rests on profoundly shaky ground and is based more on alarmist rhetoric about a "race to the bottom" than on anything resembling reality. In fact, the term is a misnomer (Wildasin, 2021) based largely on misleading extrapolations from unrealistic, non-dynamic, and purely qualitative theories of tax competition. Moreover, even these conceptual concerns about a "race to the bottom" are borne out of a selective and incomplete reading of the theoretical economics research. A more complete assessment of the theoretical landscape underscores many potential benefits from tax competition. Empirical studies raise even more doubts about "harmonization" efforts such as a global minimum tax aimed at stifling tax competition.

The theoretical economic scholarship on tax competition largely emerged out of a construct called the Zodrow, Mieszkowski, and Wilson (ZMW) model (Keen and Konrad, 2013). In this framework, countries compete for a fixed pie of global capital by setting their own tax rates on capital income. If one country in isolation were to lower its capital tax, capital would shift there from other locations. However, other countries can respond in kind to prevent such movement in capital from occurring. In this zero-sum analysis, the result is tax rates that are too low and an under-provision of public goods without a net increase in private investment. Some have used this result to raise the specter of a "race to the bottom" and to justify implementing a global minimum tax, but there are numerous flaws to making such an inference and using such a loaded rhetorical image.

To start with, such an analysis does not take into account the sensitivity of *total* global capital formation to the tax burden imposed on it. In addition, the theoretical framework abstracts in important ways from the practical reality of how international capital taxation actually occurs, for example, by assuming that all countries have source-based tax schemes (as opposed to residence or destination-based schemes) and by ignoring important real-world factors that impede capital mobility and allow other factors to influence investment location decisions (Feldstein and Horioka, 1980).

Of course, it is important to recognize that there is ample evidence showing the importance of taxes for the location of investment and the evolution of an economy's capital stock (Hines, 1996; Devereux and Griffith, 1998; Bond and Xing, 2015). Still, the theoretical case undergirding "race to the bottom" fears is tenuous. For example, agglomeration economies—which are the benefits that accrue to people and firms as a result of clustering near each other to share knowledge, talent, and supply chains—can greatly offset the theoretical forces described above (Brulhart, Jametti and Schmidheiny, 2012; Baldwin and Krugman, 2002). In addition, there is significant evidence that the United States is a global leader in setting tax policy, which violates one of the core assumptions in the basic ZMW model and those that have followed from it. For example, after the 1986 U.S. tax reform, many OECD countries in the 1980s and 1990s pursued similar rate-cutting and base-broadening reforms (Altshuler and Goodspeed, 2015). While some may point to this historical sequence of events as evidence in favor of harmful tax competition, it is important to reiterate that the theoretical basis for showing such harms implicitly assumes that the U.S. is just one of many countries on the world stage rather than a leading economic superpower that can set the tone for what other countries do. Taking into account the more realistic scenario of U.S. leadership can overturn the theory behind a "race to the bottom" and suggests the adoption of a global minimum tax will be harmful. In other words, the choice of assumptions matters in any analysis, and thus one cannot determine confidently that tax competition is bad in the first place (Keen and Konrad, 2013). To the contrary, others have put forward compelling arguments in favor of tax competition.

Before turning to those arguments, it is worth assessing the empirical evidence. Whichever assumptions or theory one finds most compelling from a conceptual standpoint, there is little evidence that "race to the bottom" dynamics have emerged in reality that would justify tax harmonization policies. For one thing, a meta-analysis of the research examining the impact of international integration fails to find a robust negative link between globalization and capital taxation (Adam, Kammas, and Lagou, 2013). Even in the EU, where tax competition between member countries is likely to be strongest, there is no indication that a race to the bottom has unfolded (Boss, 1999). Moreover, even if it were occurring, it does not follow that tax harmonization efforts would improve economic welfare for all participating countries (Gordon and Hines, 2002). One key issue that arises is the likely existence of countries outside of any coalition of countries participating in tax harmonization. As long as there are players on the outside of any global tax agreement, even the optimistic welfare gains from coordination are extremely small (Sorensen, 2004). In a larger-scale analysis that quantifies many of the possible benefits of tax coordination while abstracting from some of those associated with tax competition, the result is strikingly small quantitative gains from harmonization efforts.

To summarize the above results, even if one believes in the idea of a "race to the bottom" and ignores the benefits of tax competition, the best-case scenario for capital tax harmonization efforts is a negligible gain in global economic welfare, with some countries on the losing side. One reason for these small effects is that corporations account for only a slice of the economy, and international differences would persist for taxes on households (Sorensen, 2004). This fact raises the ominous prospect that a global minimum tax on corporations would be just the beginning, only to be followed by subsequent efforts to cede national sovereignty over other areas of the tax code and pave the way for much broader-based tax increases.

The case against a global minimum tax extends beyond simply pointing to meager or nonexistent gains from harmonization. Indeed, there is a robust case to be made in favor of tax competition and fiscal federalism broadly. To begin with, tax competition can act as a safeguard against big government colluding with lobbyists to raise taxes on the population (Sorensen, 2004; Brulhart and Jametti, 2019). Moreover, governments do not set taxes in isolation. Instead, they offer taxes and services as a bundle, which mitigates against unbridled race-to-the-bottom dynamics, given that any reduction in tax revenues must eventually be accompanied by cuts to public services (Agrawal, Hoyt, and Wilson, 2020). Thus, competition between governments creates the incentive to offer a good "bang for the buck" by reducing waste and inefficiencies rather than an incentive to always look for ways to cut taxes and core services. Another benefit of tax competition relates to its ability to help countries (and jurisdictions within a country) identify better tax systems and learn from the experiences of others (Boss, 1999).

In fact, it is relatively straightforward to make both the theoretical and empirical case for fiscal federalism with an analogy to competition in the private sector. In this analogy—which is articulated through formal economic modeling by researchers—governments compete with each other to attract capital and labor, and the "invisible hand" can act to guide decisions at the individual jurisdiction level to produce efficient outcomes at a larger scale without any race to the bottom (Oates, 1999). This work is in many ways an extension of the

Tiebout hypothesis—a concept first introduced by Charles Tiebout in 1956 which postulates that governments orient their policy bundles to efficiently serve the interests of their constituents, who in turn sort themselves into communities where the policy mix is most amenable to their varied preferences. In this case, the Tiebout hypothesis would be applied to the relationship between the international governing consensus and individual nations. More recent research provides support for the Tiebout hypothesis involving competition at the nation-state level acting in part through competition for labor (Razin and Sadka, 2011). Not only does such competition avoid detrimental "race to the bottom" dynamics, but it can enhance economic growth by increasing the incentive to save, leading to greater investment in human capital (Brueckner, 2006).

As the above evidence indicates, tax competition can be a powerful tool to restrain government excess and promote economic growth. Conversely, in addition to the obvious stripping of national sovereignty, tax harmonization via a GMT at its best could only hope to offer minuscule and speculative theoretical gains or, more likely, to act as a tool to empower bureaucrats, ossify bad tax policy by limiting policy experimentation, and limit the scope for pro-growth tax reforms that have proven successful in the past, such as TCJA in the United States. Foregoing such reforms would be a shame, as there is considerable evidence that federal corporate tax policy that reduces investment costs can lead to higher total employment and earnings in the labor market (Garrett, Ohrn, and Suarez Serrato, 2019). The United States would not be the only loser under a GMT arrangement. After all, the cutting of Ireland's business tax to as low as 12.5 percent in 2003—where it remains today—accompanied by fiscal reforms that shrunk public sector consumption contributed significantly to the Irish Miracle that saw Ireland, over the course of 1980 to the early 2000s, close an economic output gap of nearly 50 percent per adult between Ireland and the United States (Klein and Ventura, 2020). Which country will be denied the opportunity to go through its own growth miracle as a result of a GMT suppressing tax policy innovation?

CONCLUSION

The GMT sought by the Biden administration falls far short of putting the American people first. It corrodes our country's sovereignty and skirts around the role of the people's representatives in legislating domestic tax policy. At the same time, it weakens the ability to transform the American economy into a powerhouse of innovation and growth that is necessary to confront the future. U.S. leadership in pursuing this GMT is an admission that the domestic economic programs proposed alongside it put the U.S. economy at a strategic disadvantage, risking a flight of U.S. capital and innovation to foreign countries. While proponents of the GMT claim it arrests a so-called "race to the bottom," in reality it sets its sights on the lowest common denominator and attempts to drag all countries down to that uncompetitive, growth-killing economic state. The United States should always set its sights high, put American workers and family first, and avoid the failed globalist pursuits of the past. The GMT, if enacted, will be another example in this long line of failures.

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