

**Tax Foundation's "Tax Policy Podcast"**  
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**Scott A. Hodge:** "Thank you for listening in. I'm Scott Hodge, president of the Tax Foundation. We're here to talk about the US corporate tax system; what's wrong with it, and how we can fix it. Many Americans would be shocked to learn that according to the most recent OECD figures the combined federal and state corporate income tax rate in the United States is now the second highest in the OECD at 39.3%. Ironically, while our rates are high, our corporate tax collections, in the US, are among the lowest in the OECD at just 2.1% of GDP. Here to discuss these issues is Glenn Hubbard, dean of the Columbia Business School and former chairman of the US council of economic advisors under President George Bush. Glenn is also a member of the Tax Foundation board of directors. Welcome, Glenn."

**R. Glenn Hubbard:** "Thank you."

**Hodge:** "Glenn, the US corporate tax system is coming under increased scrutiny. You recently hosted an all day conference on corporate taxes at the American Enterprise Institute with some of the leading business economists in the world. What can you tell us about the research that those economists presented there and what lawmakers can take away from this new research?"

**Hubbard:** "There's an increasingly important body of academic work that suggests that the corporate tax has much larger costs to our economy than we thought even ten or fifteen years ago. These big distortions come from the fact that in a global economy a high corporate tax in the US is a job killer and an investment killer and actually can lead to lower risk taking and innovation. It also leads to very high costs of compliance. All of these costs are borne by somebody. That somebody is us – either in terms of the prices of goods we buy, the wages we get, or the returns we get on our investments. I think economists are really focusing on the idea that we have got to cut the corporate tax rate in the US to be competitive."

**Hodge:** "Last year, President Bush appointed a blue ribbon panel of experts to look at fundamental tax reform. In the report they released in November, the panelists recommended reforming the corporate tax rate system, including lowering tax rates to thirty percent, full business expensing, and moving toward a territorial system. What were your thoughts on the President's proposals and do they go far enough to fully reform the federal tax system?"

**Hubbard:** "Well, I think they are the right steps and we can still go further. They're the right steps because they push toward what economists believe is the best tax system: a broad base and low rate. And it would push us toward a tax system that is more competitive. Moving toward expensing makes it easier to grow our capital stock which influences our wages and our productivity and a territorial tax system would make American companies more competitive for jobs abroad and that's good for jobs here as

well. Now, we could go further. I think there's a need to think more about the corporate tax rate, but everything that the President's tax reform panel put out is certainly worthy of consideration and I certainly hope that the President and the Congress will do something."

**Hodge:** "Many Americans are not aware that as a result of the Bush tax cuts the top individual tax rate and the top corporate tax rate are the same, now 35 percent. That's the first time in the history of the tax system that the individual and top corporate rate have been the same. When you were at the Treasury Department in the early 90s you helped develop a proposal to integrate the corporate and individual tax systems. Briefly, what can you tell us about integration? It's an interesting term and kind of an unusual term. And why is it so important for fundamental tax reform?"

**Hubbard:** "It's an odd term, Scott. The way I would explain it is under law before the Bush tax cuts, we were double taxing and in some cases triple taxing, or more, returns to savings. So you would work, earn money, save it but then be double taxed or maybe triple taxed on the returns. That strikes many people as unfair. It also strikes many economists as extremely costly: by raising the cost of capital for investment and by discouraging saving. All integration means is 'why don't we just tax all income once and only once?' So when President Bush pushed to try to eliminate dividend and capital gains taxes and got halfway, what he was trying to say is 'let's try to reduce the double taxation of corporate equity investments.' Many people view that tax cut as a big success for investment, for the stock market, and for our economy and jobs."

**Hodge:** "Fundamental tax reform is now moved to the backburner issue here in the United States but is clearly a front-burner issue across the globe. The OECD recently released a report on worldwide trends in fundamental tax reform and it shows that the rest of the world is clearly moving ahead and we're falling further and further behind. You know, as we try to move tax reform to the front, as a front-burner issue, are there countries that are doing it right? Are there countries that we can point lawmakers to and say 'that's what we should be doing?'"

**Hubbard:** "Well, that's a great question. I think some of the countries that are leading the way are in Eastern Europe, the so-called 'New Europe,' that are designing tax systems from scratch, and deciding, quite accurately and reasonably, that they don't want to tax capital or tax it as little as possible. But you know what's interesting, Scott, is that it's not just those economies. If you look at even continental European economies, like France, like Germany, you still see a trend in recent years toward cutting corporate taxes and replacing the tax burden with something else – even in those economies. The US is rapidly becoming the odd man out. And what that means for us as an economy in a very competitive global capital market is eventually capital will find us a bit less attractive."

**Hodge:** "You point to the tax system as a source of many of the problems facing our healthcare system today, especially the rising costs of care. I've heard the healthcare system likened to veterinary medicine where the patient really is cut out of the decision making process. The patient sits there while the people paying the bills, that being the

employers and the insurance companies, negotiate with the doctor over the quality and cost of the care. So it seems to me that it's really important that we do something to put patients themselves back in the driver's seats and make them part of the market process."

**Hubbard:** "Sure. I mean healthcare costs have become a competitive issue just like the issues surrounding the corporate tax. And part of the problem is that unlike the other five-sixths of our economy we have pursued public policies that perhaps unwittingly have made markets not work very well. There are a number of those policies that have had bad effects. The biggest probably is the tax code, where we try to encourage people to focus on getting healthcare only through employer-sponsored coverage that looks more like prepaid healthcare than it does insurance. The consequence of that is that people spend much more on insurance and on healthcare than they need to, depressing wages, and also leading to rising healthcare costs. Now, there are a couple of ways we can fix it. The best thing we could do, if this were a perfect world, is to pull the tax code out of this entirely, by which I mean, people would pay taxes on any imputed health insurance benefits they get from their employer putting it on the same footing as wages. If that happened people would rationally decide they want higher deductibles, higher co-pays, and take more money as wages. I'm not a politician. I think that's politically unlikely. An alternative that Cogan, Kessler, and I propose is going the other way, and making all forms of the purchase of health insurance and healthcare deductible. So whether your employer buys it, you buy it on your own, or you pay a provider directly on your own, the same tax treatment. Remember, in the US, five out of every six dollars that run through our healthcare system are paid by somebody other than the consumer. What other market works that way? We also don't have much information out there for consumers because frankly they don't have much incentive to ask for it under current policies. We can make this market work better. It'll lead to better patient centered medicine and lower healthcare costs."

**Hodge:** "Glenn, thanks for joining me today. I appreciate your insights on these very important issues."

**Hubbard:** "Thanks, my pleasure."

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