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Who Pays Corporate Taxes?

Virginia has a car tax. Does the car pay the tax? In most political jurisdictions, there's a property tax. Does property pay the tax? You say: "Williams, that's lunacy. Neither a car nor property pays taxes. Only flesh-and-blood people pay taxes!" What about a corporation? As it turns out, a corporation is an artificial creation of the legal system and, as such, a legal fiction. A corporation is not a person and therefore cannot pay taxes. When tax is levied on a corporation, who pays it?

There's an entire subject area in economics, known as tax incidence, that investigates who bears the burden of a tax. It turns out that the burden of a tax is not necessarily borne by the party or entity upon whom it is levied. For example, if a sales tax is levied on a cigarette retailer, the retailer does not bear the full burden of the tax. Part of it will be shifted forward to customers in the form of higher product prices. The exact amount of the shifting depends upon market supply and demand conditions.

What about raising taxes on corporations as a means to get them to pay their "rightful share of government"? If a tax is levied on a corporation and if it is to survive, it will have one of several responses or some combination thereof. One response is to raise the price of its product, so customers share part of the burden. Another response is to lower dividends, so shareholders share a part of the burden. And a considerable portion of reduced dividend burden falls on ordinary non-rich people. According to the Tax Foundation, 19 percent of federal tax returns report dividend income but 42 percent of taxpayers older than 65 report dividend income. Therefore, it is people, not some legal fiction called a corporation, who bear the burden of the tax. Because corporations have these responses to the imposition of a tax, they are merely government tax collectors.

The largest burden of corporate taxes is borne by workers. We discover that by asking a simple question, such as: Which workers on a road construction project earn the higher pay, those employed moving dirt with shovels and wheelbarrows or those doing the same atop giant earthmovers? You'd guess the guys operating the earthmovers, but why? It's not because they're unionized or because construction contractors have a fondness for earthmover operators. It's because those workers have more capital (tools) to work with and are thereby more productive. Higher productivity translates into higher wages.

Tax policies that raise the cost of capital formation — such as capital gains taxes, low depreciation allowances and corporate taxes — reduce capital formation. As a result, workers have less capital, lower productivity and lower wage growth. In 1980, Joseph Stiglitz, now a Nobel laureate, said that workers share the highest corporate tax burden in the form of lower wages. A number of economic studies, including that of the Congressional Budget Office, show that workers bear anywhere from 45 to 75 percent of the corporate tax burden. Adding to the burden is the fact that capital has the kind of mobility that labor doesn't. Corporate capital can flee to other countries easily, but workers cannot.

Politicians and leftist elite get away with corporate tax demagoguery because economists haven't done well in making our subject understandable to ordinary people, not to mention that we have derelict news media people with little understanding.

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