Essay on taxation

Business, Company

The current economic problems facing United States requires formation of policies that are meant to improve the economic situations in this region. Each proposed tax reform should be analyzed accordingly to ensure that it affects the economy of United States positively. Each tax reform should be such that it supports the aims of taxation. It should be such that it facilitates fair distribution of resources and allocates resources accordingly. One of the areas where tax reforms have been proposed is in corporate tax reforms. The proposal is that the corporate tax should be lowered from 35 percent to 25 percent (Sullivan, 2011).

Corporations that are large enough are required to pay a tax rate of 35 percent on their total incomes. This is the only tax that these corporations are required to pay considering that, no interest is paid on capital gains of the corporations and the dividends that are distributed to the shareholders. Corporate tax is a federal tax considering that it is imposed by the federal government. This tax is applied to all organizations that are classified as corporations. Both international and domestic corporations are required to pay this tax as long as they operate within the boundaries of United States. It is important to note that some companies as not taxed because they are not classified as corporations. Some companies are sometimes subjected to withholding corporate tax. This offers a benefit to such corporations. Companies that are required to pay corporate tax are required to file a return for purposes of taxation every year. They are required to choose their tax year, which may not be the same as their financial year. However, the tax year should have 12 months.

Research has shown that reduction in tax rates is likely to facilitate economic growth. Reduced corporate tax rate means that the required rate of return after taxation will be low. With the current rate, the required rate of return is very high and this means that many of the projects proposed by companies fail to be implemented. As a result, many viable projects are abandoned as long as the required rate of return is greater than actual rate of return after corporate taxation. If the corporate tax is lowered, the required rate of return would decrease and many projects that are proposed by various companies would be implemented. Implementing these projects means that the output in the economy increases. In order to implement this project, laborers are required. This means that lowering the corporate tax rates would create employment opportunities for many people hence the problem of unemployment would have been solved (Sullivan, 2011).

The increase in the investment of companies with lowered corporate tax rate would mean that companies increase their capital stock and the levels of technology in their organizations. Increased technology improves the efficiency of workers and hence their salaries are increased. There are many benefits associated with increased wages to employees. In the first place, the income tax collected by the government increases. Another advantage is that people are able to save and then invest their savings. This trend causes a cycle that facilitates economic growth (Agrawal, 2008).

If tax is lowered to this level, many international companies will find it beneficial to invest in the United States. Many foreign companies will invest their assets in the United States. This means that the output in the economy increases due to this policy. Employment opportunities also increase with the increased foreign investment in the United States. Increase in the total output in the United States mean that the total gross domestic product of the United States also increases.

The graph below shows the relationship between lower corporate taxes and freign direct investment.

Lowering the corporate tax rate will help in correcting distortion in the financial markets. With the current tax rates, many companies are biased in seeking their capital investment. Many of these companies prefer debt financing. This is because interest rate is a deductible expense for purpose of tax. This therefore creates a tax shield for the companies that finance their investments through debts. This tax reform is important in that it helps to reduce distortions in the economy. With the lower interest rate, resources will be appropriately allocated. This is because those preferring debt financing will experience a higher tax burden. As a result, companies will be indifferent in choosing the method of financing. This means that the resources available in the organization will have to be allocated in the best way possible.

If the tax reform were accepted, the results would be that corporations would be neutral on whether to issue debts or equity in order to finance their activities. The decisions to borrow loans would be based on economic reasons. The decisions will no aim at avoiding tax. Firms will therefore consider the benefits of borrowing and its costs. It means that corporations will borrow debts when it is extremely necessary to do so. In addition, the management of the borrowed funds will be an important issue. The companies will have to manage the funds they borrow effectively considering that the debts do not benefit them a lot. The increase in efficiency of managing funds will lead to better performance of United States corporations and this is advantageous to the United States economy (Shaviro, 2009).

The objections to this proposal are that many companies will rush to borrow huge long-term loans currently so that they can continue to benefit from the current tax shield. This unnecessary borrowing would lead to mismanagement of funds and many companies will face difficulties in repaying their loans. However, measures can be taken to prevent this problem. It can be stated that any company that borrows funds from the time this proposal is presented to the congress should not be covered by the previous tax rate (Agrawal, 2008). However, allowance can be given to companies that borrow loans during the period through good faith. Otherwise, if the proposal starts its operations from the time it is enacted, then the trend will be that companies will borrow long term loans before its enactment. In this regard, the objection is not very important if the expected problem is addressed at early stages.

Lowering the tax rate is likely to increase the total profits of the organizations. If the profits are high, then it means that shareholders receive higher dividends. This adds to their household income. With increased income, people are able to save for their investment. Their living standards are also increased since they have a wider choice with increase in income. High profits also have the effects of increasing the stock prices. This will encourage the shareholders to invest more of their funds in order to receive capital gains. Increased value of United States assets is important in facilitating economic growth of the region (Shaviro, 2009).

Another objection on corporate tax cut is that the total tax revenue to the government is likely to decrease. This is only true in the short-term. However, the long-term effects of the proposal show that the total tax collected by the government will increase. As it has been seen, more companies will be encouraged to invest in United States. Additional companies in the United States mean that more revenues will be collected from these companies. More people are employed and therefore income tax increases. The projects being implemented by companies due to lowered corporate tax increase hence profitability of the companies increase. Increased profits mean that the government gets more profits. In this regard, the opposition is not reasonable enough to make the proposal to be rejected.

References.

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