Kerry Just Doesn't Get It

[Thinking Outside the Boxe wrote this article in response to Senator John Kerry's guest column, "A two-part solution to an illogical corporate tax regime," in *The Financial Times* on July 22, 2005. For Senator Kerry's complete article, visit *The Financial Times* website at www.ft.com.]

John Kerry's interesting article ("A two-part solution to an illogical corporate tax regime," July 22, 2005) makes several legitimate points regarding the need for corporate tax reform in the United States. However, his rationale that the "right kind of tax policy" will prevent companies from moving jobs overseas is severely flawed and shows once again how he truly fails to grasp the dynamics of the situation.

To be sure, Senator Kerry is right in arguing for corporate tax reform that lowers the tax rate across the board and provides incentives, such as tax credits, for businesses that create new jobs domestically. As he rightly points out, corporate taxes are up to one third lower in foreign countries, giving companies an incentive to reinvest profits made in foreign countries back into those economies. Given this competitive disadvantage from a significantly higher tax burden in the US, it is not surprising that companies choose to reinvest profits overseas. Legitimate tax reform should be structured so that companies are indifferent when faced with a decision between reinvesting profits in foreign countries and repatriating those profits to the US. In addition, the corporate tax loopholes such as offshore tax havens and tax shelters, which may cost up to $40 billion per year in lost tax revenues, should be closed so that those tax revenues could be used to fund any reduction in the corporate tax rate in the US to a more competitive level.

In justifying the need for corporate tax reform, Senator Kerry claims that "companies have a tax advantage to move jobs overseas." This continues claims he made during the 2004 presidential campaign that tax loopholes have "American workers actually subsidizing the loss of their own job" (Third Bush-Kerry debate in Tempe, Arizona on October 13, 2004). In the Democratic 2004 primary debate in Greenville, South Carolina on January 29, 2004, Kerry indicated that "we need a president who's going to close the loopholes of these corporation that have a reward to take the jobs overseas."

Herein, Senator Kerry fails to understand that companies move jobs overseas due to the much lower labour costs in countries such as

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China, India, and Mexico. Hourly compensation costs for production workers in manufacturing range from roughly $22 in the United States to over $30 in Germany (according to the US Department of Labour, Bureau of Labour Statistics). Hourly compensation costs in Mexico are less than $2.50 and may be as low as $1 in China and India. Companies that move production to the low wage countries have a competitive advantage, which enables them to produce products more efficiently and at a lower cost to consumers. Those companies that do not seek competitive advantages will lose market share to competitors and will likely suffer financially. The trend towards outsourcing illustrates the basic economic principle of comparative advantage—a country should produce what it is most efficient at producing and then trade with other countries that produce goods where they have a competitive advantage. As such, each country should benefit economically through trade.

It should be clear, then, that tax policy is not the underlying motivation for outsourcing jobs to low wage countries. Furthermore, reforming corporate tax policies will not change the wage differential between the US and other countries and will not prompt companies to bring jobs back from overseas. Likewise, tax reform will not prevent companies from outsourcing to lower wage countries in order to remain competitive in this age of globalization. Effective tax reform may promote job creation domestically in industries where the US maintains a competitive advantage, such as technology, and in small businesses that are one of the engines of economic growth. Tax reform should also be viewed as the right step in helping US companies become more competitive in the global economy by simplifying a convoluted tax regime.

However, in order for the United States to remain competitive, our country must make the necessary investments in education and job training that provide the best workforce for producing the "revolutionary technologies and products of tomorrow." Only by ensuring that the United States is at the forefront of change and that our workforce is highly educated and ready for the challenges of tomorrow will we be able to attract businesses and remain competitive in the global economy.

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