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America: An Expensive Place to Do Business

Government regulation and a complicated tax code have made American companies less competitive in the global economy.

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Presidential candidate John Kerry recently made headlines by comparing corporate CEOs who move production overseas to the most hated traitor in U.S. history, Benedict Arnold. Mr. Kerry has placed at the center of his economic plan a carrot-and-stick approach to stop American companies from outsourcing labor to foreign countries. Mr. Kerry's approach would end "the unpatriotic practice of U.S. corporations moving offshore simply to avoid paying their fair share of our nation's tax burden." What Mr. Kerry fails to understand is that companies are not moving jobs overseas because they are unpatriotic; companies are moving jobs overseas because big government is making America too expensive a place to do business.

In December of 2003, the National Association of Manufacturers released a report by economist Jeremy A. Leonard that cited how external, non-production costs are reducing investment, reducing innovation, and are a barrier to job creation. The study compares the competitiveness of U.S. manufacturers with those in our nine largest trading partners and finds, "Domestically imposed costs—by omission or commission of federal, state, and local governments—are damaging manufacturing more than any foreign competitor and adding at least 22.4 percent to the cost of doing business" in the United States. According to Mr. Leonard, "absent these extra costs, the United States would compete on an even playing field" with our nine largest trading partners. The costs of government mandates and taxes place U.S. manufacturers at a significant disadvantage compared to competitors in our nine largest trading partners.

The manufacturing sector has been aggressive in its attempt to remain competitive. Since 1990, the manufacturing sector has increased productivity by 54 percent. The productivity gains of the 1990s were the highest of any previous post-World War II expansion. During the economic boom of the 1990s, manufacturing accounted for 22 percent of the economic growth and increased its share of total value added in the U.S. economy. Despite these gains, U.S. export penetration has decline from 12 percent in 1998 to 10.7 percent in 2002 and 2.8 million manufacturing jobs have been lost in the last 39 months.

What are the external costs that have been so burdensome to U.S. manufacturers? Jeremy Leonard writes, "The largest burden comes from high corporate tax rates and employee benefits, with small but substantial burdens cause by litigation costs and regulatory compliance." When federal and state corporate taxes are combined, the corporate tax burden is 40 percent, making it the second highest among our nine major trading partners. The high tax burden discourages foreign businesses from setting up operations in the United States and encourages U.S. companies to migrate production to more friendly tax jurisdictions. Leonard estimates the U.S. corporate tax burden reduces the cost competitiveness of U.S. manufacturers by 5.6 percent.

In a competitive global economy, the United States cannot continue to ignore the mounting costs

of doing business at home. Other countries are liberalizing their economies, providing a more business-friendly environment. Ireland is a perfect example of a tax-friendly country. The government reduced its corporate tax rate from 16 percent to 12.5 percent in 2003, well below the EU average rate of 30 percent and lower than the 35 percent federal rate in the United States. The corporate friendly environment in Ireland has been a boon to foreign direct investment. Despite accounting for only 1 percent of the European market, Ireland receives one-third of all U.S. investment in Europe. The three largest industries to invest in Ireland are engineering, computer, and software companies, three industries making the most noise about outsourcing in the United States. Rather than attempting to regulate how and where firms do business, a simpler solution would be to lower corporate tax burdens, which would keep American businesses from locating facilities elsewhere and save U.S. jobs.

Another excessive external cost hurting manufactures is litigation. Leonard estimates tort litigation reduces U.S. manufacturers' competitiveness by more than 3.2 percent. Tillinghast-Towers Perrin, an independent consulting firm, reported the total cost from tort litigation in 2002 was $233 billion. This is a shocking 2.23 percent of the entire Gross National Product. Companies often pass this bill to consumers in the form of higher prices and reduced services, costing the average American $809 a year. Foreign competitors are able to offer lower prices than American companies because trial lawyers continue to exploit the legal system for personal gain. Class action lawsuits and rampant punitive damage claims have imposed significant costs on business in the United States. Tort reform is needed to help American companies become more competitive and save American jobs.

A third excessive external cost hurting manufacturers is the cost of compliance with excessive environmental mandates. Leonard estimates pollution abatement expenditures alone reduces U.S. cost competitiveness by at least 3.5 percent. The United States is one of the "greenest" countries in the world and yet some politicians want to adopt Kyoto-Protocol like regulations which will hamper economic growth while providing little or no environmental benefits. Instead of forcing American companies to adopt one-size-fits-all regulatory mandates to alleviate environmental concerns, companies should be given the flexibility to use market forces to meet environmental standards. A more market-oriented approach to environmental issues would reduce compliance costs and make U.S. companies more competitive while improving environmental quality.

In all, the "...total compliance burden of environmental, economic, workplace, and tax compliance on the economy is in the order of $550 billion..." The additional regulatory costs act as a hidden tax to consumers and increase costs to producers, making them less competitive in the world market. If politicians want to get serious about U.S. jobs and allow U.S. companies to operate on a level playing field with their competitors, they must make it less expensive to conduct business here. Simplifying the complicated tax code while reducing tax rates, instituting tort reform, and reducing regulatory costs faced by U.S. companies will promote economic growth and protect American jobs far better than any scheme to artificially control how American companies do business in the global marketplace.

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