

Corporate income taxes and entrepreneurship

The type, quality, and quantity of entrepreneurship are influenced significantly by corporate income taxes—though only slightly

Keywords: entrepreneurship, self-employment, start-ups, business taxes, corporate income taxes

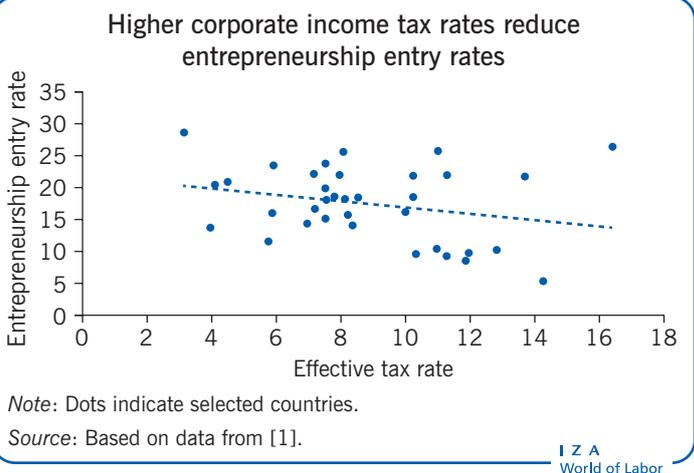
ELEVATOR PITCH

Corporate income taxation influences the quantity and type of entrepreneurship, which in turn affects economic development. Empirical evidence shows that higher corporate income tax rates reduce business density and entrepreneurship entry rates and increase the capital size of new firms. The progressivity of tax rates increases entrepreneurship entry rates, whereas highly complex tax codes reduce them. Policymakers should understand the effects and underlying mechanisms that determine how corporate income taxation influences entrepreneurship in order to provide a favorable business environment.

KEY FINDINGS

Pros

- + Corporate income tax rates have a statistically and economically significant influence on entrepreneurship.
- + The relationship between corporate income taxes and entrepreneurship is stronger than the relationship between other taxes and entrepreneurship.
- + High effective corporate income tax rates increase the capital size of new firms, thereby enhancing their chances of survivability (“entry barrier effect”).
- + High levels of corporate income tax progressivity increase entrepreneurship entry rates (“tax progressivity effect”).



Cons

- High statutory and high effective corporate income tax rates reduce business density and entrepreneurship entry rates (“tax level effect”).
- Reductions in the corporate income tax rate may only affect entrepreneurship rates below a certain threshold tax level.
- Corporate income tax rate reductions are more effective at promoting entrepreneurship in countries with higher quality accounting standards.
- Highly complex corporate income tax codes reduce entrepreneurship entry rates (“tax code complexity effect”).
- High corporate income tax rates increase the size of the informal sector.

AUTHOR’S MAIN MESSAGE

Empirical evidence shows that corporate income taxation has a significant, albeit small, influence on the quantity and type of entrepreneurship. In addition to the corporate income tax level, tax progressivity and tax code complexity exhibit effects on entrepreneurship activity. As such, tax policy impacts a country’s overall business profile. Policymakers must understand the nuances of how corporate taxation can affect entrepreneurship in their country, and must consider contextual factors such as the quality of accounting systems and investors’ risk profiles before determining tax policy. For policymakers in countries with low-quality accounting standards, this suggests that lowering taxes to increase entrepreneurship rates should be accompanied with an effort to improve the quality of accounting standards.