

The Truth of the Modern Recession, Root Causes and Reliable Solutions

A Not For Author Profit Book

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Free Trade Deficit Qualitative Tax Losses

9.7 Free Trade Deficit Related Tax Losses

We conclude this chapter by investigating the FMEA effect in Table 9.1, “loss of tax revenue” due to the free trade deficit. There are a number of reasons why we might expect tax losses from the free trade deficit. First we would like to mention that the explosion of the free trade deficit has become of the same order of magnitude as the national debt. In fact, the two show somewhat of a similar time series as displayed in Figure 9.2. This graph is simply the data from the U.S. government website listed in Table 9.11 for Columns 2 and 4. Figure 9.2 shows the trade deficit has exceeded the national debt in certain years. The trade deficit appears correlated, influencing the national debt, after 2001.

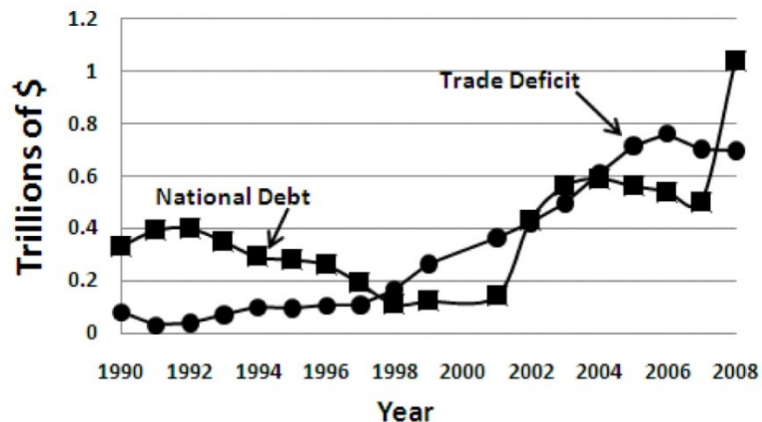


Figure 9.2 Comparison between trade deficit and national debt.

It is instructive to actually look at the mathematical correlation. Although we are making no claims as to how influential the trade deficit might be on U.S. tax losses, we will show that it is reason for concern. There are budgetary reasons why after the period from 1990 to 2001 the national debt increased from 2003 to 2008. In fact the main government expenses: defense and military, health & services and social security all increased by a total of 89% on average between these periods²¹⁹! Therefore, we are not claiming that the free trade deficit is the main reason for the increase in Figure 9.2, but our investigation will show there are serious tax revenue concerns.

The concern is a trade imbalance also provides tax consequences representing a combination of ways in which taxes are collected depending on the type of trade (import vs. export) for goods and services. As a simple example, the U.S. collects tax revenues on U.S. worker salaries for exported services compared to imported services for which no salary taxes are collected from foreign workers. This illustrates one simple difference in Trade Deficit Tax (TDT) consequences that can occur depending on the type of trade imbalance.

The U.S. Free Trade Deficit has accumulated to \$6.57 trillion dollars over the last 20 years and \$7.5 trillion since 1971. The National Debt now totals around \$12.1 trillion. In fact, from 1990 to 2007, the trade deficit totaled \$5.51 trillion, which was fairly close to the national debt in those years that totaled \$6.1 trillion. From a bird’s eye view, we see two very explosive amounts.

The question is then, are there excessive TDT losses due to the trade deficit, and is it effecting the national debt? Unfortunately, we will only be able to provide simple quantitative and qualitative information to demonstrate concern. First let’s look at some more qualitative reasons.

One basic concern of a trade deficit is that more money leaves the U.S. in trade than comes in, and can contribute to the national debt. Free trade advocates argue that such U.S. dollars must be

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reinvested back in the U.S., and while this is true, it leaves one unanswered question, what about related TDT loss consequences that have incurred in the trading transition? As well deficit reinvestments mean foreigners own more and more of the U.S. Here we provide simple examples of what we mean by trade transitions being associated with tax collection consequences from a U.S. trade deficit.

U.S. Import Related Tax Consequences:

- 1) Imports create decreases in federal tax revenues for various reasons, such as products made by non U.S. citizens who do not pay federal tax compared to products or services that would have created tax revenues if the products were not imported. Thus as U.S. made goods are replaced with foreign imports, so too are U.S. jobs and lost taxed wages in addition to unemployment benefits. Seemingly temporary, yet U.S. displaced workers occur frequently enough that the U.S. taxes burden is yearly (see Remark 9.9A estimate of \$77 billion). As well, foreign companies do not pay U.S. taxes compared to U.S. companies that would have paid taxes.
- 2) U.S. trade deficit enables foreigners to buy numerous American businesses and own more and more of the U.S. IRS data show that foreign-owned corporations doing business here typically pay far less in U.S. income taxes than do purely American firms with comparable sales and assets. This is because it's hard to determine how much of a corporation's worldwide earnings relate to its U.S. activities and therefore are subject to U.S. tax. There are many other tax issues that create serious tax problems.¹
- 3) Many U.S. CEOs outsource jobs creating service TDT losses, these "imported services" decrease potential tax revenues of the company's workforce compared to non outsourcing. This also creates higher unemployment. Unemployment causes more lost tax dollars due to U.S. government subsidies until workers can recover. Profits of U.S. companies abroad may end up abroad decreasing tax revenues.
- 4) Foreign profits from the trade deficit that are reinvested typically do not provide the tax revenue that U.S. citizen reinvestments may provide. For example, currently foreign reinvestments are considerable in U.S. government obligations for the U.S. national debt and now total about \$3 trillion. This provides tax liability as the U.S. has to pay interest on this money to foreigners. On the other hand, U.S. citizens pay taxes on many of their reinvestments when owning U.S. business and equities. Foreigners who reinvest in buying U.S. business also find ways to avoid U.S. taxes. Job outsourcing often occurs once a U.S. business is taken over.
- 5) There is a national debt, trade deficit cyclic effect (Sec. 9.3) when foreigners reinvest in U.S. treasuries, the interest obligation creates *negative* economic growth or jobs potential reducing taxes.

U.S. Export Related Tax Revenue:

- 6) Exports create federal tax revenue gains for various reasons (products more likely made by U.S. citizens who pay income tax, U.S. companies pay taxes on profits, we export services to foreign companies and these creates tax revenue through income tax, etc.)

These are basic examples, but serve to help in understanding the reasons for reliability economic concerns.

¹ www.ctj.org/hid_ent/part-2/part2-3.htm, "Tax breaks for multinational corporations"