Tax Incidence and Tax Avoidance

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ABSTRACT

Economists broadly agree that the economic burden of corporate taxes is not entirely borne by shareholders, but also borne in part by workers or consumers. We theoretically examine corporate tax avoidance in a setting where shareholders do not bear the entire economic burden of the corporate tax. We show that the relation between corporate tax avoidance and the share of the tax burden borne by shareholders is ambiguous, but we derive several testable predictions and their conditions. Using empirical analyses, we find that firms whose shareholders bear less of the economic burden of corporate income taxes engage in less tax avoidance than other firms, and that the results are strongest under conditions predicted by our model. Our findings suggest that maximizing after-tax profits might entail less tax avoidance if shareholders do not entirely bear the economic burden of the corporate tax.

Keywords: Tax avoidance, tax burden, tax incidence

JEL classification: H20, H25