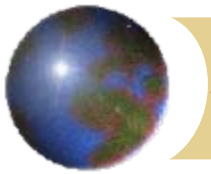


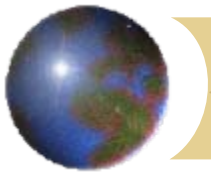
# *Why Competition Between Governments Is Desirable*

Vilnius, Lithuania, June 11, 2008



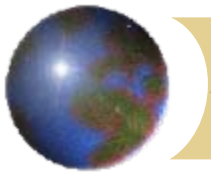
# *The Conditions for Prosperity*

- *Economic Freedom of the World* and the *Index of Economic Freedom* both tell similar stories.
- Rule of law, property rights, and honest courts are the foundation needed for a prosperous economy.
- Good policy – i.e., limited government – builds upon a good foundation by creating incentives for productive behavior.



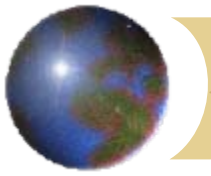
# *The Cost of Government*

- Taxation – How much the government takes from us and how they take it.
- Spending – How much the government spends and what they buy with the money.
- Regulation – The overall level of red tape and the degree of cost-benefit analysis.
- Monetary Policy – Is the currency a stable store of value or a political football?



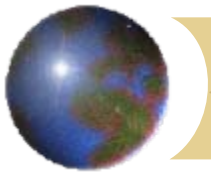
## *The “Public Choice” Challenge*

- “Public Choice” makes spending restraint a political challenge.
- Policy makers have an incentive to increase the size and cost of government.
- The burden of government has climbed in all nations.
- Though some nations have been successful with dramatic spending restraint – but only after first moving in the wrong direction.



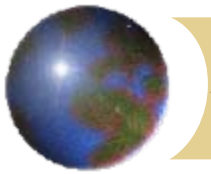
## *How to Convince Politicians?*

- Many lawmakers like bigger government, which means pressure for higher tax rates.
- Many lawmakers want high tax rates on the “rich” so other taxpayers more willingly accept higher tax rates on themselves.
- Many lawmakers want complicated tax systems since that means they have the ability to manipulate tax systems for the benefit of political supporters.



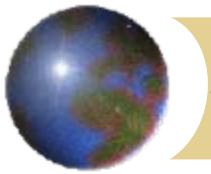
## *Jurisdictional Competition is Key*

- We won't win because people read our policy papers.
- Politicians generally do the right thing when other options are exhausted.
- Tax and regulatory competition is forcing pro-market reforms.
- Globalization is making it easier for the geese that lay golden eggs to escape oppression.

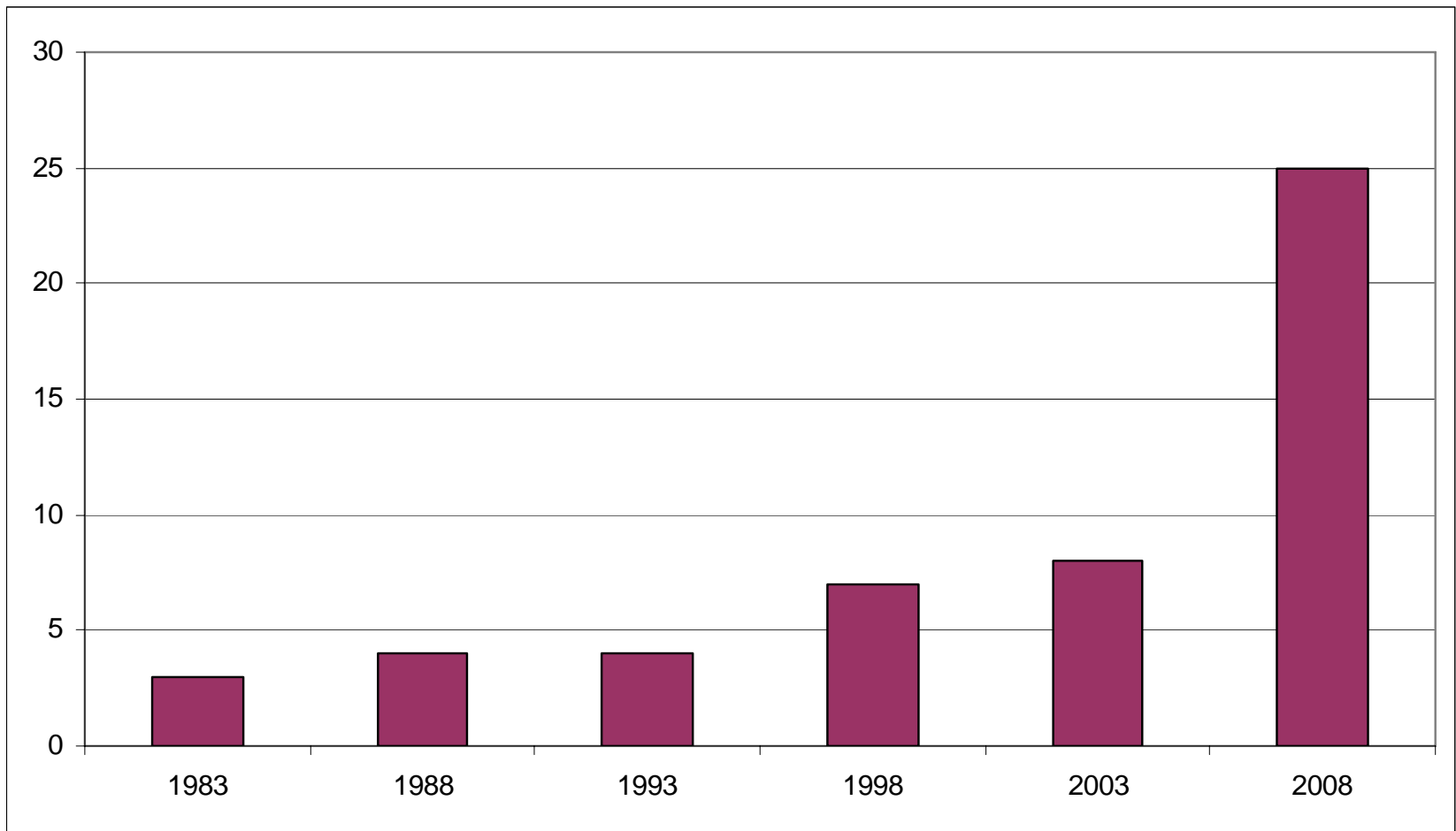


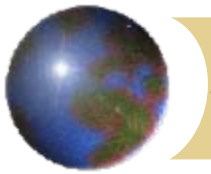
## *World is Moving the Right Direction*

- More than 20 nations with flat tax systems.
- More than 30 nations with some form of personal retirement accounts.
- Several nations substantially reducing the burden of government spending.
- Around the globe, we are seeing lower tax rates and less double taxation of saving and investment.



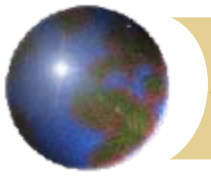
# *Number of Flat Tax Jurisdictions*



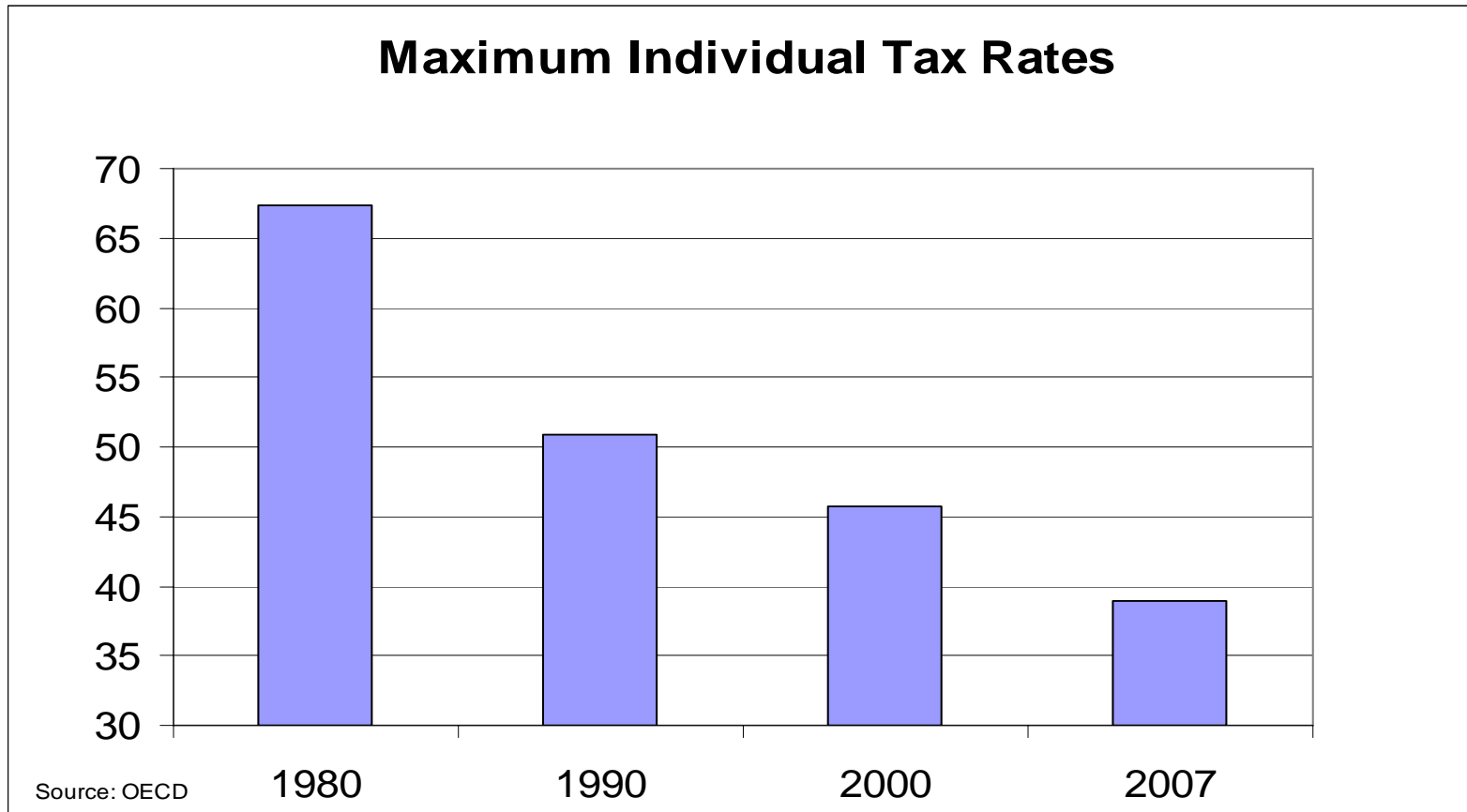


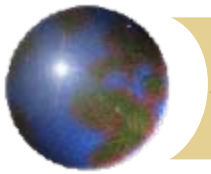
## *Tax Rates Also Have Dropped*

- Since 1980, initially spurred by the Thatcher/Reagan personal income tax rate reductions, top income tax rates have dropped by an average of more than 25 percentage points in developed nations.
- Similarly, the average corporate tax rate in OECD nations today is more than 20 percentage points lower today than in 1980, though Ireland probably deserves credit for sparking the shift to lower rates.



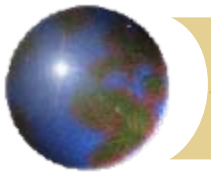
# *Global Progress on Tax Rates*





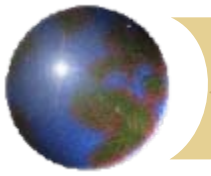
## *Falling Corporate Tax Rates*

- Average corporate tax rate in 1980 = 48 percent.
- Average corporate tax rate in 1990 = 42 percent.
- Average corporate tax rate in 2000 = 34 percent.
- Average corporate tax rate today = 28 percent.
- America is now an outlier on corporate tax.



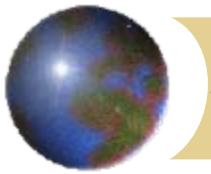
# *The Role of the European Union*

- The European Union is both good and bad for government competition.
- On the plus side, competition between governments is enhanced by free trade among nations and the “four freedoms.”
- On the minus side, there is too much economic policy between decided by Brussels, and this means one-size-fits-all policies.



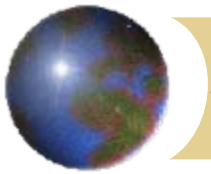
## *Nobel Laureates: Gary Becker*

- The world's leading economists strongly favor tax competition.
- Gary Becker: "...competition among nations tends to produce a race to the top rather than to the bottom by limiting the ability of powerful and voracious groups and politicians in each nation to impose their will at the expense of the interests of the vast majority of their populations."



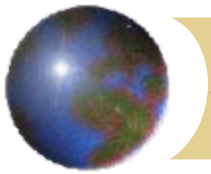
## *Buchanan and Friedman*

- James Buchanan: "...tax competition among separate units...is an objective to be sought in its own right."
- Milton Friedman: "Competition among national governments in the public services they provide and in the taxes they impose is every bit as productive as competition among individuals or enterprises in the goods and services they offer for sale and the prices at which they offer them."



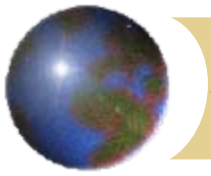
## *Vernon Smith*

- “[Tax competition] is a very good thing. ...Competition in all forms of government policy is important. That is really the great strength of globalization ...tending to force change on the part of the countries that have higher tax and also regulatory and other policies than some of the more innovative countries. ...The way to get revenue is doing all you can to encourage growth and wealth creation and then that gives you more income to tax at the lower rate down the road.”



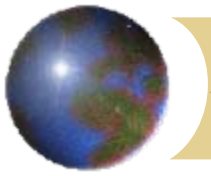
## *Edward Prescott*

- “With apologies to Adam Smith, it’s fair to say that politicians of like mind seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise taxes. This is why international bureaucracies should not be allowed to create tax cartels, which benefit governments at the expense of the people.”



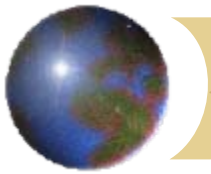
## *Edmund Phelps*

- “[I]t’s kind of a shame that there seems to be developing a kind of tendency for Western Europe to envelope Eastern Europe and require of Eastern Europe that they adopt the same economic institutions and regulations and everything. ...We want to have some role models... If all these countries to the East are brought in and homogenized with the Western European members then that opportunity will be lost.



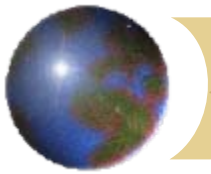
## *What Does Adam Smith Say?*

- An inquisition into every man's private circumstances, and an inquisition which, in order to accommodate the tax to them, watched over all the fluctuations of his fortunes, would be a source of such continual and endless vexation as no people could support.... The proprietor of stock is properly a citizen of the world, and is not necessarily attached to any particular country. He would be apt to abandon the country in which he was exposed to a vexatious inquisition, in order to be assessed to a burdensome tax, and would remove his stock to some other country where he could...



## *Adam Smith... Continued*

- ...either carry on his business, or enjoy his fortune more at his ease. By removing his stock he would put an end to all the industry which it had maintained in the country which he left. Stock cultivates land; stock employs labour. A tax which tended to drive away stock from any particular country would so far tend to dry up every source of revenue both to the sovereign and to the society. Not only the profits of stock, but the rent of land and the wages of labour would necessarily be more or less diminished by its removal. —Adam Smith, *An Inquiry into the Nature & Causes of the Wealth of Nations*, 1776.



## *Conclusion*

- Competition between governments is both theoretically and empirically desirable.
- Global governance sounds nice in theory, but it is counterproductive.
- One-size-fits-all means an “OPEC for politicians”.
- European Union is good and bad.
- Lithuania should aggressively compete with market-friendly policies.