Corporate Taxation and the Distribution of Income

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ABSTRACT

Corporate income taxation affects income distribution both by changing relative returns to capital and labor and by reducing the size of the corporate sector of the economy. A smaller corporate sector entails a larger non-corporate sector, rewarding small business entrepreneurs who compete with corporations. Due to the undiversified riskiness of non-corporate business activity, its expansion contributes to income dispersion and thereby increases ex post income inequality. This effect can be so large that higher levels of corporate taxation are associated with greater after-tax income inequality, despite any associated reductions in after-tax returns to capital.

JEL Classifications: H22, H25, D31.