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| **Title** | Country size and corporate tax rate: Rationale and empirics |
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| **Abstract** | This paper investigates whether the differences in corporate tax rates set by countries can be explained, in part, by the size of national home markets. We set up a simple model in which multinational firms within an industry choose where to invest, given the levels of corporation tax rates in each location. This model yields predictions with respect to the influences of the relative size of countries on the differences in corporate tax rates that should arise in equilibrium. We then test these predictions using data from 27 European Union member-states for the period 1981-2005. Consistent with our model, we find that large countries set higher corporate tax rates than their smaller competitors for FDI. Our rationale for the existence of this effect, the market access, withstands the test of alternative explanations. |
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| **Keywords** | country size, corporate tax rate, foreign direct investment, tax competition |
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