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<https://doi.org/10.61796/jaide.v1i8.801>**THE EFFECT OF TAXATION ON THE ACTIVITY OF ENTERPRISES****Kudiyarov Kishibay Ramatullayevich**

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Abstract: This research examines the impact of taxation on the activities of enterprises. Theoretical and empirical approaches have been studied regarding the impact of taxation on the activities of enterprises. The issues of regulating the ratio of debt and private capital of enterprises by means of taxes are analyzed. As a result of the analysis, relevant conclusions were formed.

Keywords: business entities, taxation, tax rate, tax base, profit tax, VAT, property tax, debt interest, investment, employment.

This is an open-access article under the [CC-BY 4.0](https://creativecommons.org/licenses/by/4.0/) license**Introduction**

Effective taxation is one of the main important factors of the economic development of enterprises. Improving the tax system in modern conditions means ensuring the development of the priority directions of the economy and increasing the competitiveness of local producers by regulating the activities of enterprises through taxes. The functional features of taxation allow it to be used not only for fiscal purposes, but also to influence the conditions of production of goods and services. It is important to establish a single criterion for the optimal distribution of the level of taxation and to determine the optimal amount of taxes in relation to the income of enterprises. Applying different forms and methods of taxation if the paradigm of its fiscal orientation is changed to a regulation that takes into account changes in the investment and tax environment, which in turn allows the tax regulatory system to act as the most flexible way to attract additional resources to stimulate the activities of economic entities. Using a comprehensive approach and substantiating the set of existing instruments allows to activate the activities of enterprises taking into account the priorities of economic development (Eljurkaev, 2021).

Studying the impact of taxation on the investment activity of enterprises and the business environment is an urgent issue in both public finance and economic development. The impact of these taxes is important not only in the development of tax policy and the evaluation of its implementation results, but also in determining the priorities of economic growth (Barro 1991; DeLong and Summers 1991; Baumol, Litan and Schramm 2007). Consistent reduction of the tax burden, simplification of the taxation system, rapid development of enterprises' activities through taxes, and increase of investment attractiveness of enterprises are the most important conditions for improving taxation.

Today, ensuring optimal taxation of the activities of business entities is an important priority task of the tax policy. Despite the fiscal nature of taxes and mandatory fees, effective regulation of the activities of business entities by means of taxes means optimization of the tax system.

Literature review

Creating a business-friendly environment for entrepreneurs (including protection of private property rights, regulation, and low taxes) leads to increased entrepreneurial activity (Kreft and Sobel, 2005). A decrease in average effective tax rates in the taxation of business activities can lead to an increase in investment activity and an increase in the number of jobs and wages by having a positive effect on their financial stability (Carroll et al., 1998)

Ramsey's research is considered the foundation of the scientific literature on optimal taxation. Ramsey (1927) argued that effective taxation requires the introduction of a whole set of taxes, not just one tax. At the same time, it is also important in the taxation of interest income. Ramsey treats consumption and savings as two different goods and suggests that capital should be taxed at a much lower rate than income. Also, according to Chamley (1986), based on theories of optimal taxation of capital, tax policy development should avoid taxes that directly affect capital, including taxes on capital growth, dividends, and interest income. According to Andrew (2007), a flat rate tax on capital gains is not a distortion if capital expenditure is allowed to be deducted from the tax base of the purchasers of capital. However, even though this specification of the capital gains tax establishes a zero effective capital tax rate, the capital gains tax can generate significant revenue.

In classical corporate taxation, debt financing is generally preferred over private equity. This theoretical view made it possible to expand Modigliani-Miller's opinion about the insignificance of the capital structure, which implies that leverage does not affect the market value of the firm (Modigliani, Miller, 1958; Modigliani, Miller, 1963). When the corporate income tax is based on an initial uncertain supply, it is beneficial for debt financing because the interest payments shield the profits from taxes. This means 100 percent debt financing if there is no ability to cover the cost of the loan. However, the Modigliani-Miller theorem does not work in situations of high transaction costs, bankruptcy, agency conflicts, adverse selection, and so on. In the face of rising tax costs, having a company's optimal or target debt ratio and protection against a small change in leverage clearly offsets the additional costs of financial distress. In this case, the optimal debt ratio is determined by the company's profitability, asset risk classification, and corporate income tax rate. A level playing field for debt capital and private capital is required in reducing the discrimination between debt financing and equity financing in the corporate tax system.

The abolition or limitation of tax deductions for interest on debt financing will lead to an increase in the capital of the banking sector and a decrease in the volume of debt financing (Abdullaev, 2020). In particular, in the conducted studies, it was determined that the advantages of taxation on debt financing in the corporate tax system have an impact on the occurrence of financial crises as a result of encouraging the attraction of debt funds (DeNicolo G., Gamba A. & Lucchetta M., 2012; Modigliani, Miller, 1963; de Mooij & Keen., 2016). Tax-induced corporate debt exposure leads to excessive borrowing for companies and reduces their resilience potential in times of financial stress. Economists have also argued that the bias towards debt over private capital destabilizes the economy, especially the financial sector (Admati et al., 2013; de Mooij, Keen and Orihara, 2013). From a microeconomic point of view, the standard theory of optimal taxation assumes that intermediate goods and services should not be taxed (these distortions in production processes are more costly than taxation of the final product). If we take into account the financial intermediation activities of banks, in particular, the sale of financial products to businesses and individuals, the loss of efficiency as a result of the disparity in taxation depends on who actually bears the tax burden.

Indirect taxes (VAT, excise tax) are included in the price of goods (works, services) and are paid by final consumers. Theoretically, indirect taxes exclude the possibility of encroachment on the interests of producers and sellers, because their source of payment is the income of final consumers. However, in some cases, the producer or seller can become the payer of indirect taxes, then the source of their payment becomes profit, and a certain amount of indirect taxes part takes on the characteristics of direct taxation (Zaripova, 2014). For these reasons, it is important to assess whether business entities actually bear the burden of taxes they pay from their activities, and if not, to which categories of customers they can shift them. In particular, as a result of exemption of goods and services from

VAT, the input VAT leads to an increase in the value of goods and services and a violation of the essence of taxation.

According to economists, the property tax is part of the investor's cost of capital and affects investment behavior along with the income tax. The introduction of new taxes or an increase in the level of existing property taxes leads to a decrease in the demand for capital goods, thereby disincentivizing the process of investment. An increase in the tax burden on property can lead to a refusal to reinvest profits to modernize existing facilities, their obsolescence, withdrawal of capital due to long-term depreciation payments, and reduced activity (Koroleva, 2023). Also, as a result of empirical analysis, it was determined that the provision of tax credits from property tax can lead to an increase in employment (Leonard et al., 2020), while a high level of the average effective tax rate on property tax can lead to a decrease in the volume of investment (Church, 1981; Hayashi, Hynes, 2020).

Methods

Scientific abstraction, analysis and synthesis, induction and deduction, expert assessment, descriptive statistics, comparative analysis, scientific approach to theoretical and empirical studies were used in the research work

Result and Discussion

Based on research, you can say that debt can increase the value of a company, because the availability of tax deductions creates advantages in using large amounts of debt capital. It can be seen that the availability of tax deductions for interest on debts reduces taxable income. But if the debtor company has a high level of risk, the debtor company bears only the economic risk, while the debtor company records the equity risk relative to the level of debt. Of course, in order to limit excessive leveraged financing and reduce the negative effects of interest tax deductions, several countries have developed "interest deduction limitation rules" or "anti-capitalization rules". These rules determine how much of the interest you pay on corporate debt is deductible for tax purposes.

In the tax legislation, when determining the taxable profit, it is possible to directly limit the amount of the rate calculated on the interest amounts that should be included in the expenses. There are two approaches to this. In the first, it is envisaged that the maximum possible interest rate will be set in the legislation. In the second case, according to the tax legislation, the interest rate applied to each transaction is derived from the conditions that can be compared (Abdullaev, 2020). In addition, there are restrictions on tax deductions for interest when the ratio of debt capital to private capital exceeds a certain level. For example, in Japan, as a general rule, interest on debt obligations to a foreign subsidiary is not deductible when calculating corporate income tax when the corresponding amount of debt exceeds three times the proportion of the corporation's equity (Langedijk et al., 2015). In the Netherlands, there are restrictions on interest expenses if they exceed interest income.

This rule aims to reduce the tax benefits of debt financing by limiting the tax deductions for related interest expenses. Thus, anti-capitalization rules limit the tax deduction of interest from the tax base when the ratio of debt capital to private equity exceeds the specified ratio. According to the results of the conducted empirical analysis, such rules are more effective for the reduction of debt capital, differentiation in taxation and control measures of domestic debt obligations. In a broad sense, based on the approach of the countries to the rules against lack of capitalization, they are divided into three categories: countries without any rules against lack of capitalization; countries where special rules do not apply; countries where there are rules against a lack of specific capitalization.

In the scientific literature, in order to reduce the tax discrimination in the taxation of corporate profits through equity and debt financing, two approaches are proposed as a solution: the Comprehensive Business Income Tax (CBIT) and the tax deduction for corporate private capital (Allowance for Corporate Equity–ASE). Allowance for Corporate Equity–ASE can reduce systemic risk by influencing the capital structure and reducing the risk of default. Allowance for Corporate

Equity–ASE was proposed as a solution. ASE can reduce systemic risk by influencing the capital structure and reducing the risk of default. Also, a number of features specific to ASE can be cited:

- prevents neutrality between debt and equity financing and repeals provisions against undercapitalization;
- neutrality with respect to the marginal investment solution, that is, the presence of a discount on the return of interest and capital to a normal amount of income;
- Eliminates investment imbalances that arise due to differences between economic depreciation and tax depreciation.

In particular, an increase in the amount of accelerated depreciation for tax purposes will lead to a decrease in the book value of assets in tax calculations and reduce payments for capital in the next year (Abdullaev, 2020).

In particular, the limitation of tax advantages in relation to debt financing in the corporate tax system has a positive effect on the private capital ratio of banks, and the implementation of tax incentives for private capital increases the private capital ratio in the sample by approximately 13.5% on average. Second, the impact of changes in the tax regime is related to the increase of capital, not through the reduction of activity. Third, the level of capitalization reduces risks (Schepens, 2016).

Globally, differences in corporate tax rates across countries mean that the impact on pre-tax profits is very high. For this reason, the competition in the field of international corporate tax, in turn, leads to decreasing trends in tax rates (Fig. 1). Lowering the rate of corporate profit tax has a positive effect on the financial results of business entities, which leads to an increase in the financial stability of business entities and investment activity of the country. economic growth is ensured.

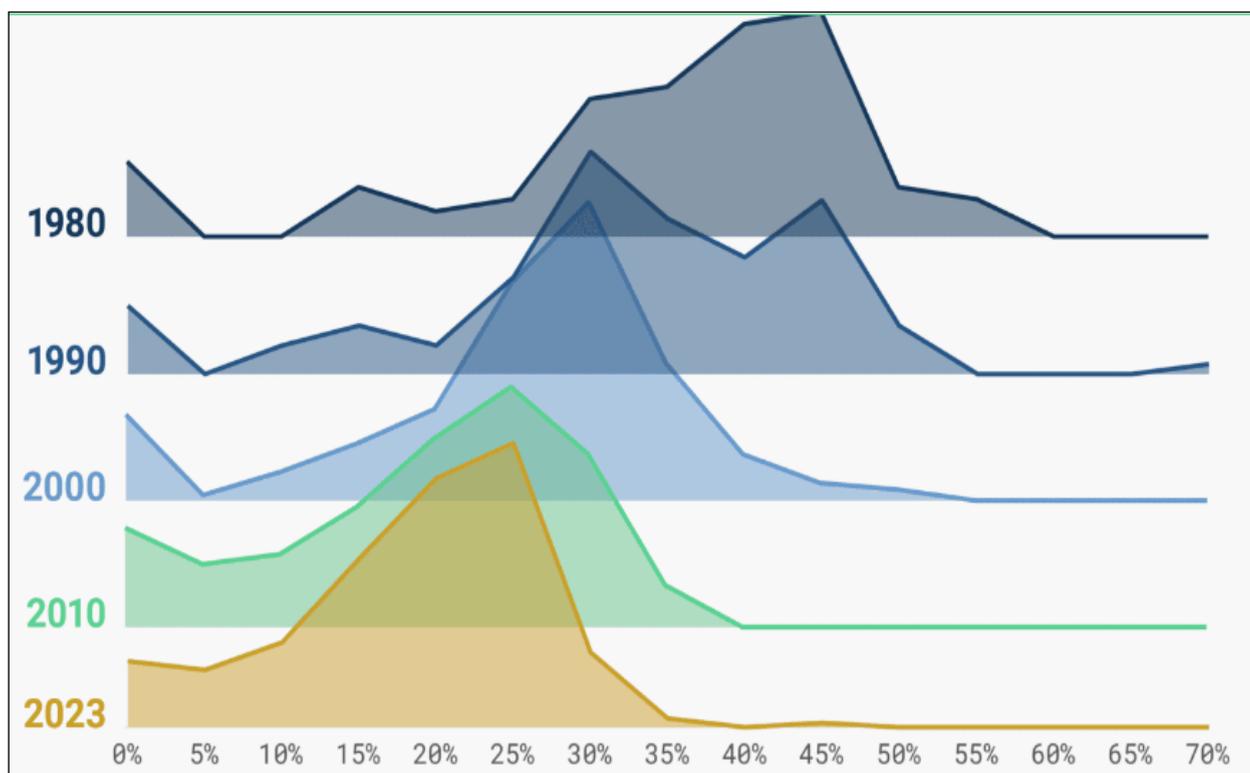


Fig 1. Trends in statutory maximum tax rates around the world (Tax Foundation, 2023).

VAT is an indirect tax on the added value created at each stage of production. The use of VAT in the tax system of different countries shows its tax efficiency based on a number of features: coverage of a wide tax base, including transactions related to the sale of goods and services, transfer and sale of property rights, transfer of property for exchange for other goods, free property - transfer of property, lease of property, provision of inventory on the basis of loan agreements, etc.; provides

automatic indexation of budget incomes depending on the level of inflation, because when determining VAT on sales of taxable goods by the seller to the buyer, the taxable base includes the value of material resources and other costs incurred by the producer; receiving the product at each stage of delivery to the consumer and characterized by a short reporting period, ensures the uniformity of budget revenue receipts; due to the fact that it is relatively neutral for the payer due to its transformation into the final consumer, as a result of pricing and inclusion in the sales price, it reduces their desire to avoid payment (Kononchuk, 2018).

According to Mirrlees (2011), the exemption of financial services from VAT is contrary to the principle of taxation, as it makes it impossible for financial institutions to recover the input VAT, leading to a disruption of the chain. This is a clear violation of the nature of taxation, and the tax exemption turns VAT into a direct tax on production. The financial consequences of the VAT exemption are described by comparing the performance indicators of two economic entities: the economic entity exempted from paying VAT; Business entity paying VAT at the rate of 20% (Table 1).

Indicators	When exempted from paying VAT	When VAT is applied at the rate of 20%
1 Net sales proceeds	1000	1000
2 VAT on sales	-	200
3 Production costs are exclusive of VAT	472	472
4 The purchase price of the product is exclusive of VAT	200	200
5 VAT included in costs	40	-
6 Deductible VAT amount	-	40
7 Taxable profit (line 1–line 3–line 4–line 5)	288	328
8 Profit tax (7 lines x20/100)*	57,6	65,6
9 Net profit (line 7-line 8)	230,4	262,4
10 Profitability (9 lines/1 line x 100)	23	26,2
11 Tax burden (8 lines – 6 lines)/1 line x 100)	5,8	2,6

Source: prepared by the author based on conditional numbers.

As can be seen from the table, taxpayers who are exempted from paying VAT have a lower net profit compared to VAT payers, and the level of tax burden is higher compared to net income, *ceteris paribus*.

Conclusion

The taxation system should be considered not only from the point of view of increasing "fiscal" budget revenues, but also as an instrument for increasing the stability of enterprises and regulating their activities related to high level of risks. Allowance for Corporate Equity–ASE allows companies to make tax deductions at conditional interest rates on their capital. Ideally, these rules should make companies indifferent to the choice between private equity and debt financing. Improving the taxation of enterprises will reduce the tax discrimination between debt and equity financing, and the provision of tax incentives that encourage private capital will lead to an increase in the level of capitalization. Profit tax affects the development of business entities, investment volume. In particular, as a result of exemption of goods and services from VAT, the input VAT leads to an increase in the value of goods and services and a violation of the essence of taxation. A high level of the average effective tax rate on property tax can lead to a decrease in the volume of investment

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