KPMG Private Enterprise

A delicate balancing act between economic impact and taxation

Achieving sustainable growth in private companies

KPMG International

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In 2022, KPMG Private Enterprise Tax published a reported titled "Carving a new path: How private companies can contribute to future economic stability". It strongly suggested that supporting the resilience, adaptability, innovation and long-term focus of privately owned companies is in everyone's best interest.

That priority has not changed. If anything, it is even more relevant today as governments across the world are looking for ways to raise money to reduce their post-pandemic debt and address the decline in tax revenues that are resulting from an economic slowdown.

It continues to be our view that businesses are able to respond more productively to measures that support the growth, resilience, adaptability, innovation and long-term focus of private companies, than they are to tax increases.

As KPMG Private Enterprise Tax professionals, there are several reasons why we consider this to be a more sustainable option.

Economic opportunities beyond taxation

Every citizen and organization has an obligation to pay their fair share of taxes. And, to a certain extent, it's understandable that raising taxes may be governments' default position when the need for a global economic revival is looming.

The need and urgency for governments to act is understood. But what's also understood is how important it is to achieve the right balance between a mix of taxation changes and incentives.

This is especially the case in areas where private companies have proven to be the economic drivers and sources of growth in their countries.

Should governments, therefore, target their efforts toward more tax *incentives*, for example, to stimulate growth versus introducing tax rate *increases*? Or can — and should they — do both?

Finding the right balance for sustainable growth

Equilibrium entails tax-positive fiscal policies that encourage and incentivize private companies to increase their business activity — with less reliance on corporate and personal tax increases for achieving that goal.

In many jurisdictions, privately owned businesses are long-term engines of growth, and they actually have the potential to generate ***new tax revenues*** through the jobs they create the suppliers they support and the economic contributions they make to their communities. Throughout the pandemic, most of these companies behaved responsibly by making use of government support — where necessary — and combining that support with their own resources to protect their employees, customers, suppliers and local communities.

With a sustained long-term outlook and a reputation for operating responsibly, many private companies are also investing in the future by leading the ESG agenda.

Are we creating an unequal burden?

Despite their economic, environmental and social contributions, there is a legitimate concern that private companies and their owners may be required to carry an unequal burden in helping to close the gap between the financial safety net that governments provided during the pandemic and the costs of reconstruction going forward.

The concern is that private companies may become entangled in a web of increased corporate taxes, a rise in succession and inheritance taxes and the introduction of new personal wealth taxes. It's our view that achieving the right balance will be critical for sustaining the long-term economic and societal impact of these companies.

Businesses contribute more effectively to the economy when they are incentivized to make capital expenditure investments that spur economic growth and recovery, along with appropriate tax policies that don't act as a disincentive to growth.

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The upside and downside of incentives for private companies

While government subsidies, tax credits and other incentives may be welcomed, they can have unintended knock-on effects. Private companies operating in a global economic environment are facing an entirely new set of opportunities as well as challenges.

There have been questions, for example, regarding how the new clean energy tax credits in the US will be treated in terms of the OECD 15 percent global minimum corporate tax rate agreement. The concern is that these 'green' tax credits may reduce a company's US tax liability to less than 15 percent, and multinational companies that invest in the US could, therefore, be taxed by other countries to reach that 15 percent level.

As well, these incentives reward companies for building equipment nationally or for sourcing components and critical minerals from the US or from countries where the US has a free-trade agreement. In response, the EU is working on its own green subsidy proposals, and there are concerns that companies may begin to play governments against each other.

A world view on the evolving tax landscape

In our previous report, we emphasized the importance of encouraging entrepreneurship, introducing workplace advances, accelerating environmental and societal improvements and removing barriers to entry in certain industries. These are not tax changes.

The question remains, though, of how much money Governments need to raise in order to finance their operations. And companies will need to recalculate their paths in light of their governments' fiscal requirements, potential corporate and personal tax changes, as well as other obligations and concerns, such as BEPS, the Global Minimum Tax, decarbonization targets, and urgent Environmental Social and Governance (ESG) priorities.

Each of these matters is accompanied by new regulations and additional compliance and reporting requirements. Achieving measurable ESG progress, for example, requires companies to collect the right data and to be transparent and consistent in reporting it. There were calls for greater tax transparency and public disclosure long before the surge in sustainability metrics. But there is no question that these calls are becoming louder. And with heightened pressure from stakeholders and regulators for consistent, transparent reporting in every aspect of their business, companies will be expected to provide evidence that they are not only meeting the regulatory requirements, but also complying with their own tax policies.

The need for consistent and transparent reporting across most aspects of their operations will now be essential.

Getting the balance right

Private companies are accustomed to preparing for new challenges such as these, while also seeking out fresh opportunities. Many have already undertaken a thorough review of their business models and supply chain operations, which were directly affected by the pandemic. Now, it will also be important to review their affairs in light of potential legislative changes that are currently evolving and the impact that these may have on their businesses, their families and themselves.

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We believe that promoting the benefits of patient and responsible capital and its deployment has never been so important. Entrepreneurial, privately owned businesses make important contributions to employment growth *and* the economic prosperity that generates its own increased tax contributions, In contrast, increased taxation may have the countereffect of inhibiting entrepreneurial ambitions and slowing the economic growth that governments are striving to achieve.

Planning begins now

No one can predict the actions that governments in different countries and jurisdictions may take in order to move their economies in a positive direction. It's unlikely that these will be short- or even medium-term decisions. At a minimum, it's best to be prepared for the transparent and consistent reporting that will likely be required in all aspects of your business.

The world is moving at pace. And as the regulatory environment continues to evolve in jurisdictions across the world, we'll provide regular updates on the KPMG Private Enterprise Tax website as the proposed changes arise along with a perspective on the implications of these changes for private companies and their owners.

In the meantime, we welcome your views on these and other tax- and reporting-related issues that may be important for you and other private companies to consider and prepare for. We encourage you to contact us at privateenterprise@kpmg.com or your local KPMG Private Enterprise Tax professional to share your views and keep the dialogue open on these evolving changes.

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