A new study finds companies that are more aggressive in their tax planning tend to do a worse job of managing their workforce. Specifically, these companies were more likely to be "underemployed," meaning they hadn't hired enough staff to operate efficiently.

"Aggressive tax planning means a company will have more cash on hand, so it should be able to invest more in its workforce," says Nathan Goldman, co-author of a paper on the work and an assistant professor of accounting at North Carolina State University. "We wanted to know if this was actually playing out in the real world. As it turns out, companies that engage in aggressive tax planning are actually doing a worse job of hiring to meet their workforce needs," Goldman says.

Here's why.

Aggressive tax planning requires companies to embrace a certain amount of uncertainty. For example, there's always the possibility a company will be audited and have to pay more in taxes and fines than it anticipated. Similarly, there are indirect risks, such as facing public relations or political challenges as a result of paying too little in taxes.

"Our study strongly suggests that the risks and uncertainties associated with aggressive tax planning make firms more cautious about engaging in long-term investments, such as hiring," Goldman says.
These findings were strongest among firms that took on greater tax risk, higher labor costs and weaker corporate governance. Companies with "weaker corporate governance" are subject to less institutional oversight, and garner less attention from external analysts, than their peers.

"Ultimately, the take-away message for business leaders is that they need to think about whether aggressive tax strategies ultimately benefit the company," Goldman says. "If those tax strategies mean a company is not investing efficiently in its workforce, that could hurt the company's bottom line. Basically, is the labor inefficiency costing the company more than it saved in taxes?"

The paper, "Aggressive Tax Planning and Labor Investments," is published in the Journal of Accounting, Auditing & Finance. First author of the paper is Simone Traini of the Norwegian School of Economics. The paper was co-authored by Christina Lewellen, an assistant professor of accounting at NC State.

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