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ASSESSMENT OF THE IMPACT OF EFFECTIVE TAX RATES ON CAPITAL IN THE AGRICULTURAL SECTOR

ZHODNOTENIE VPLYVU EFEKTÍVNYCH DAŇOVÝCH SADZIEB NA KAPITÁL V POĽNOHOSPODÁRSKOM ODVETVÍ

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Abstract: *Effective tax rates reflect the real tax burden on enterprises under existing tax legislation. This study examines agricultural capital taxation through EATR and EMTR, using the Devereux–Griffith methodology adapted to Slovak conditions for 2004 and 2022. The analysis identifies the tax depreciation shield and post-tax economic rent, comparing them through the EATR–EMTR relationship across asset types. Results show that shorter-lived assets yield higher tax savings, debt financing offers a tax advantage (negative EMTR) and equity financing increases EMTR, especially for long-lived assets. The growing EATR–EMTR gap suggests declining tax neutrality of new investments.*

Keywords: effective tax rates, EATR, EMTR, tax depreciation shield, agricultural assets
JEL Classification: H25, H71, F38

Introduction

The agricultural sector is highly sensitive to changes in tax policies for several reasons. Tax adjustments directly influence the decision-making of agricultural enterprises, their investment capacity and the overall competitiveness of the sector. Agriculture is capital-intensive, while investments in technology, equipment and infrastructure requiring long-term returns. Changes in corporate tax rates or capital gains taxation can discourage such long-term investments. Since agricultural enterprises often operate with low profit margins, even small increases in the tax burden can significantly impact their viability. Additionally, they face competition from countries with more favorable tax regimes, which can influence the relocation of capital. Effective tax rates (ETR), which reflect the actual tax burden after exemptions and reliefs, play a crucial role in shaping investment decisions. If a country offers lower effective tax rates for agriculture compared to other sectors, it can stimulate higher investment activity in this field.

Given the sector's sensitivity to external factors such as seasonality and market volatility, it is essential to design well-targeted tax policies, including incentives, exemptions and reliefs,

that can mitigate risks, encourage investment and strengthen the long-term sustainability of the agricultural sector.

1 LITERATURE REVIEW

A market economy, capital mobility and corporate tax efficiency are closely interrelated concepts that currently exert significant pressure on both investors and policymakers when deciding on capital allocation. The globalization and digitalization of the economy have substantially increased the geographical mobility of taxes and capital, creating a competitive environment among national tax systems. This phenomenon raises concerns about the fairness, efficiency and sustainability of global tax policies. As noted by Devereux and Griffith (1998, 2003) and Egger and Raff (2015), an ideal tax system should be economically neutral, avoiding distortions in location decisions of the investors. Differences in corporate taxation across countries often reflect variations in social costs, depreciation policies or investment incentives. Therefore, recent research increasingly emphasizes effective tax rates (ETR), which more accurately capture the real tax burden of firms than nominal statutory tax rates (STR). This distinction was highlighted by Baker and McKenzie (1999) and Barrios et al. (2014), while newer studies, such as Ducept and Godar (2025), show that the decline in effective tax rates across the EU is primarily driven by changes in tax bases, not only by reductions in nominal rates. Similarly, Andrejovská and Glova (2025) analyze the influence of macroeconomic determinants on effective corporate taxation within Slovakia and the V4 region. Recent empirical works, including Beer, Klemm, and Matheson (2023) and Overesch and Wamser (2021), demonstrate that the gap between STR and ETR directly affects multinational firms' decisions regarding profit shifting and capital allocation. Further studies — such as McKenzie et al. (1997), Devereux, Griffith, and Klemm (2004), Kubátová et al. (2009), Šimková (2016) and more recent analyses by Cobham and Janský (2022) or OECD (2024) confirm that effective corporate tax rates significantly influence business behavior, including location choices, investment strategies and tax optimization practices. Additionally, research by Suzuki (2014) and Ducept & Godar (2025) explores the impact of tax holidays and investment incentives on effective tax rates in Asian and EU economies. They conclude that tax holidays may increase both EATR and EMTR under certain conditions due to variations in depreciation structures and capital contribution schemes. Smaller economies with lower effective tax rates tend to attract more foreign capital inflows, consistent with the tax competition theory proposed by Gordon (1986), Zodrow and Mieszkowski (1986) and later expanded by Bucovetsky (1991) and Wilson (1991) through the concept of asymmetric tax competition.

2 METHODOLOGY AND DATA COLLECTION

The topic of capital investment taxation has been a central focus of economic research since the mid-twentieth century. Pioneering studies by Jorgenson (1963) and Hall & Jorgenson (1967) first examined the impact of corporate income taxation on the cost of capital. Later, researchers such as Jorgenson & Yun (1991), Jorgenson (1992), and King & Fullerton (1984) expanded the early models by incorporating various forms of corporate and non-corporate taxation, as well as different sources of financing and asset types. This led to the development of key indicators used to assess both the location and scale of capital investments. The first of these is the Effective Average Tax Rate (EATR), which determines the location decision (i.e., country choice) of an investment, while the second, the Effective Marginal Tax Rate (EMTR), measures the extent of investment undertaken within a given country. In this paper, the methodology for calculating EATR and EMTR was adapted to the conditions of the Slovak Republic, focusing on both agricultural and non-agricultural sectors of the national economy. The EATR is defined as the ratio of the present discounted value of taxes to the present

discounted value of pre-tax profits from the project (investment). The indicator takes the following form:

$$EATR = \frac{\frac{R^* - R}{p}}{\frac{}{(1+r)^t}} \quad (1)$$

Where R* is the economic rent generated by the project in the absence of taxation. It represents the difference between the required pre-tax rate of return and the real interest rate on an alternative investment. To obtain the present value of the project's profit, it is necessary to discount it using the real interest rate.

$$R^* = \frac{p-r}{1+r} \quad (2)$$

The effective marginal tax rate (EMTR) expresses the tax burden on a hypothetical marginal investment. It is defined as the ratio of the difference between the pre-tax rate of return on the marginal investment p~ and the post-tax rate of return s to the pre-tax rate of return on the marginal investment p~. It is given by the following form:

$$EMTR = \frac{p^{\sim} - s}{p^{\sim}} \quad (3)$$

The value p~ represents the actual pre-tax rate of return required to achieve zero economic rent after taxation, where the capital cost is the initial investment. The variable s denotes the actual post-tax rate of return for the shareholder.

The present discounted value of depreciation – A, also referred as the tax shield, was calculated based on the following relationship:

$$A = \tau \emptyset \left\{ \left(\frac{1}{1+\rho}\right) + \left(\frac{1}{1+\rho}\right)^2 + \cdots + \left(\frac{1}{1+\rho}\right)^T \right\}, \quad (4)$$

where ρ denotes the shareholder's discount rate. Since personal income taxation is not considered in this model, the shareholder's discount rate is equal to the nominal interest rate i, the value which was determined based on Fisher's equation:

$$i = (1 + r)(1 + \pi) - 1 = (1 + 0{,}05)(1 + 0{,}02) - 1 = 0{,}071 = 7{,}1\ \% \quad (5)$$

It follows that $\rho = i = 7{,}1\ \%$.

By rearranging the previous equations, we can derive the relationship between EATR and EMTR. This relationship is used when we decide whether to undertake a specific investment, as it evaluates the interaction between the location and the scale of the investment. After adjustment, the relationship between the marginal and average effective tax rates takes the following form:

$$EATR = \frac{p^{\sim}}{p}\, EMTR + \frac{p - p^{\sim}}{p}\tau \quad (6)$$

where τ represents the statutory corporate tax rate.
This relationship is essential when an investor is deciding between several mutually exclusive locations or types of investment within a given country.

Table 1: Indication and description of the variables used in the calculation of the effective tax rate

Indication	Variable name	Indication	Variable name
A	Depreciation tax shield	e	effective property tax rate - SK 0,35%

π	Inflation rate of 2 %,	v	Inventory depreciation valuation: Predetermined inventory cost: (mostly in agriculture),
δ	accounting depreciation rate determined according to ZEW for capital	$\emptyset$	tax depreciation for intangible and tangible assets (SK Act No. 595/2003 Coll. on Income Tax).
r	a real rate of return of 5% on an alternative investment	γ	shareholder tax discrimination
τ	statutory corporate tax rate (21%)	p	profit before tax
ρ	shareholder discount rate	$\tilde{p}$	return on investment before tax
i	nominal interest rate	R^*	present discounted value of the untaxed economic rent received

Source: Own processing

Table 2: Input assets in the agricultural and non-agricultural sectors in the Slovak Republic

Assets	Accounting write-off ZEW- $\boldsymbol{\delta}$	Calculated lifespan	Tax write-off in the SR - (∅)
Intangible assets	15,35% = 0,1535	max. 5 years	100/5 = 20%
Industrial buildings	3,1% = 0,031	40 years	100/40 = 2,5%
Agricultural buildings	3,1% = 0,031	20 years	100/20 = 5%
Machinery, equipment and devices	17,5% = 0,175	6 years	100/6 = 16,6%
Machinery for agriculture and forestry	17,5% = 0,175	4 years	100/4 = 25%
Basic herd and draft animals	17,5% = 0,175	4 years	100/4 = 25%
Permanent crop growing units	4,5% = 0,45	12 years	100/12 = 8,33%

Source: Own processing

Table 1 lists the designation and name of the quantities entering the EATR and EMTR calculations, and Table 2 lists the input assets in the agricultural and non-agricultural sectors in the Slovak Republic.

The aim of the paper is to identify and analyze the tax depreciation shield, which measures the level of tax savings from capital investments and the post-tax economic rent of the project, expressing the financial benefit adjusted for taxation. Subsequently, the calculated tax depreciation shield and post-tax economic rent are compared in the EATR ↔ EMTR relationship across asset categories.

1.1 Tax shield

It represents the present discounted value of depreciation, where depreciation expenses are deducted from taxable income. In cases where accelerated depreciation is available, it is important to consider its use. Accelerated depreciation allows the use of higher asset

depreciation in the early years as a taxable expense to reduce the tax base from which legal entities pay taxes.

Table 3: Tax savings in %

Assets	Values			
	Tax depreciation rate	Accounting depreciation rate	Depreciation tax shield (A)	
			2004	2022
Intangible assets	20%	15,3%	15,54	20,60
Agricultural buildings	5%	3,1%	9,99	13,25
Machinery for agriculture and forestry	25%	17,5%	16,05	21,29
Basic herd and draft animals	25%	17,5%	16,05	21,29
Permanent crop growing units	8,33%	4,5%	12,50	16,58
Land	-	-	-	-

Source: Own processing

The development of the tax depreciation shield in Table 3 reflects the extent to which a company can reduce its tax liability through tax depreciation, therefore lowering its effective tax burden. The highest tax depreciation shield is recorded for agricultural and forestry machinery and for breeding herds and draft animals at 21.29%. This is due to the faster depreciation of these assets and a relatively higher percentage of tax deductibility, which positively affects cash flow of the company and the attractiveness of investments in these assets. Overall, it can be stated that the tax advantage of individual assets has slightly increased over the observed period.

1.2 Effective Average Tax Rate (EATR)

The values of the project's economic rent in Table 4 represent the additional profit of a company that exceeds the minimum required return on capital. These values are relatively higher for debt financing, which results from more favorable tax conditions (e.g., interest deductibility), creating a more advantageous environment for the profitability of debt-financed investments. The lowest post-tax economic rent was recorded for agricultural and forestry machinery and breeding herds and draft animals (0.0621 and 0.0796 in 2022), indicating a greater negative impact of taxation on the attractiveness of investments in these types of assets.

Table 4: Economic rent of the project with taxation and EATR in %

Assets	Economic rent of the project with taxation (R)				EATR (in %)			
	Retained earnings		Debt		Retained earnings		Debt	
	2004	2022	2004	2022	2004	2022	2004	2022
Intangible assets	0,0666	0,06768	0,0792	0,0852	40,06	49,951	41,32	51,55
Agricultural buildings	0,0874	0,09528	0,1000	0,0112	29,14	36,674	30,40	37,48
Machinery for agriculture and forestry	0,0630	0,06216	0,0756	0,0079	41,95	52,613	43,21	54,22

Basic herd and draft animals	0,0630	0,06216	0,0756	0,0079	41,95	52,613	43,21	54,22
Permanent crop growing units	0,0826	0,08892	0,0952	0,0106	31,66	39,732	32,92	41,33
Land	0,1033	0,11088	0,1159	0,0134	20,79	26,158	22,05	27,77
Supplies for agriculture	0,0996	0,0924	0,1122	0,0128	22,73	29,161	24,00	30,77

Source: Own processing

The EATR indicator reflects the overall average tax burden on investments, with a higher value indicating a greater tax load. In 2022, the least favorable investments in terms of EATR were breeding herds and draft animals and agricultural and forestry machinery (52.61% and 54.22%).

Table 5: Effective marginal tax rate in %

Assets	Effective marginal tax rate in %			
	Retained earnings		Debt	
	2004	2022	2004	2022
Intangible assets	10,49	15,24	-26,48	-34,75
Agricultural buildings	18,45	24,55	-11,15	-15,26
Machinery for agriculture and forestry	12,56	17,66	-22,38	-29,52
Basic herd and draft animals	12,56	17,66	-22,38	-29,52
Permanent crop growing units	16,10	21,81	-15,55	-20,83
Land	22,19	28,93	-4,31	-6,64
Supplies for agriculture	24,97	32,52	0,62	0,20

Source: Own processing

EMTR (Table 5) recorded significant changes between 2004 and 2022, varying according to the method of financing (retained earnings and debt) as well as the type of asset. When financed through retained earnings, the highest EMTR in 2022 was observed for agricultural inventories (32.52%). Conversely, the lowest, and thus most favorable rate in 2022 was for intangible assets (15.24%), indicating their relative tax advantage.

When considering debt financing, the EMTR values are negative, representing a substantial tax benefit. In 2022, intangible assets showed the most advantageous rate (-34.75%), while the least favorable under debt financing were agricultural inventories (0.20%).

Table 6: Relationship between EATR and EMTR in %

Assets	EATR ↔EMTR (v %)			
	Retained earnings		Debt	
	2004	2022	2004	2022
Intangible assets	16,62	22,62	20,48	26,64
Agricultural buildings	18,83	23,31	17,24	22,99
Machinery for agriculture and forestry	17,16	22,64	19,69	26,06
Basic herd and draft animals	17,16	22,64	19,69	26,06
Permanent crop growing units	18,14	22,58	18,25	24,26
Land	20,03	26,43	15,48	20,79
Supplies for agriculture	20,99	27,70	14,06	18,84

Source: Own processing

The difference between the effective average tax rates and marginal tax rates (EATR ↔ EMTR) shown in Table 6 generally increased between 2004 and 2022, applying to both retained earnings and debt financing. For intangible assets, the gap between EATR and EMTR grew by 2.23% under retained earnings financing, while under debt financing, the largest difference was observed for agricultural and forestry machinery and breeding herds and draft animals, reaching 5.48%. This indicates that investments in these types of assets have become less tax-neutral compared to the past. Based on the data in Table 7, effective tax rates (EATR and EMTR) differ significantly depending on the financing method (retained earnings vs. debt) and the type of assets. The highest tax savings were recorded for agricultural and forestry machinery (21.29%), while the lowest were found for standard buildings (6.92%). This shows that tax advantages are considerably greater for assets with shorter depreciation periods. The effective average tax rate (EATR) is the lowest under retained earnings financing for inventories (21.94%) and agricultural inventories (24.72%), whereas the highest values are for agricultural and forestry machinery (45.09%) and industrial machinery and equipment (44.73%). Under debt financing, EATR values are slightly higher (by about 1–1.5 percentage points). The effective marginal tax rate (EMTR) shows substantial variation depending on the financing method. Under retained earnings, the lowest EMTR values occur for assets with short depreciation periods, particularly agricultural and forestry machinery (13.65%), indicating their tax efficiency.

Table 7: Comparison of EATR and EMTR for capital in agricultural and other sectors

Indicator	Financing method	Buildings (40 years)	Agricultural buildings (20 years)	Machines, devices and equipment (6 years)	Machinery for agriculture and forestry (4 years)	Stocks	Agricultural stocks
Tax savings	-	6,92	13,25	16,56	21,29	-	-
EATR (v%)	Retained earnings	29,50	31,18	44,73	45,09	21,94	24,72
	Debt	30,90	32,58	46,13	46,49	23,34	26,12
EMTR (v %)	Retained earnings	19,45	15,72	14,88	13,65	27,11	34,83
	Debt	-14,75	-22,47	-24,27	-26,89	0,17	0,10
EATR ↔ EMTR (v %)	Retained earnings	20,51	19,43	19,20	18,87	23,09	26,31
	Debt	19,65	21,31	21,66	22,16	15,70	10,78

Source: Own processing

When financed through debt, the EMTR values are negative, indicating a very high tax advantage of debt financing. The most negative EMTR is observed for agricultural and forestry machinery (-26.89%), while inventories show an EMTR close to zero (0.17%). The differences between EATR and EMTR reflect the extent of deviation between the average and marginal tax rates. The largest difference under retained earnings financing occurs for agricultural inventories (26.31%), while under debt financing, the highest difference is found for agricultural and forestry machinery (22.16%). It can therefore be concluded that debt financing provides significantly more favorable effective marginal tax rates, especially for assets with shorter depreciation periods. Assets with a short depreciation life (e.g., agricultural machinery)

are the most tax-advantageous due to their high tax savings and low EMTR. In contrast, long-lived assets (e.g., buildings) face a higher effective tax burden, which may discourage investment in such assets. If an investment is financed through retained earnings, non-agricultural sectors may appear more attractive because they have lower effective average tax rates (EATR). Conversely, investments in agricultural inventories are the least favorable, as they bear the highest tax burden. Overall, investing in agriculture is most beneficial when financed by debt and particularly in machinery investments, while non-agricultural investments tend to be more advantageous under retained earnings financing. As noted by Devereux (2007); Bayer (2012); Barrios (2014); and Devereux et al. (2003), differences in tax rates have a decisive influence on investment location. Both the effective average and marginal tax rates, along with the legal tax base, are key determinants shaping investors' decisions on where and how much to invest. In developed countries with high capital income, various tax reliefs, incentives, and holidays can lead not only to higher EMTR but also to increases in EATR. Šimková (2016), in her analysis of EATR construction under Slovak conditions, highlights that setting the appropriate tax rate is a complex process of compromise, on one hand, the state aims to maximize tax revenues, as they represent a key income source for the national budget, while on the other hand, entrepreneurs and consumers view taxes as a necessary burden.

CONCLUSION

The results of the analysis demonstrated that the agricultural sector in the Slovak Republic exhibits a high sensitivity to changes in tax policy, primarily due to its capital intensity, low profit margins, and the high degree of risk associated with seasonality and external factors. Empirical findings reveal significant differences in effective tax rates across asset types and financing methods. Debt-financed investments are markedly tax-advantaged, with effective marginal tax rates (EMTR) often taking on negative values. The highest tax savings and lowest effective tax burden are observed for assets with shorter depreciation periods, particularly agricultural and forestry machinery. In contrast, long-lived assets, such as agricultural buildings, show higher effective average tax rates (EATR), which may reduce incentives for their renewal and modernization.

From the perspective of tax neutrality, the gap between EATR and EMTR increased during the observed period, indicating a growing distortion of investment decisions due to tax policy. This highlights the need for a targeted optimization of the tax system in agriculture, ensuring a balance between fiscal interests and the economic sustainability of enterprises.

For economic policymakers, the results suggest the need to consider the specificities of the agricultural sector when setting tax incentives, depreciation rules and reliefs. The introduction of effective investment incentives and the maintenance of favorable tax conditions can support higher levels of capital investment, innovation and technological modernization, thereby strengthening the competitiveness and long-term sustainability of Slovak agriculture.

The difference between EATR and EMTR widened between 2004–2022, reflecting reduced tax neutrality and a stronger impact of tax policy on investment choices. The largest disparities were recorded for agricultural inventories (26.31%) and agricultural and forestry machinery (22.16%). The results indicate that, from a tax optimization standpoint, the most advantageous investments are those in short-lived assets financed through debt, while buildings and long-term assets are less attractive due to their higher effective tax burden. To preserve the competitiveness and sustainability of agriculture, it is essential that tax policy reflects these differences and promotes investments in modernization and technological advancement of the sector.

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