EFFECT OF CORPORATE TAX ON SUSTAINABLE FINANCIAL PERFORMANCE OF LISTED FIRMS IN NIGERIA

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ABSTRACT
The study examined the effect of corporate tax on the sustainable financial performance of listed firms in Nigeria, specifically the listed manufacturing firms. The study employed ex post facto research design using data from 10 listed manufacturing firms. The data span across 5 years ranging from 2013-2017 and were analyzed using simple linear regression. Findings from the study revealed that corporate tax payment has no significant effect on the return on equity of firms. Further findings revealed a positive and significant effect of corporate tax payment on the debt to equity ratio of the listed firms. Hence, based on the results obtained from this study it is recommended that Investors in the manufacturing sector should use their tax pay-out policy as a tool for financing decision as it greatly affects the firm's debt to equity ratio (Capital combination) decision making. Also, they should encourage the prompt payment of tax as it has no significant effect on their returns but in turn, increases the market value of the firms.

Keywords: Corporate tax, Return on Equity, Debt to Equity Ratio.

INTRODUCTION

There are numerous literatures on the issue of corporate tax as a fundamental determinant of doing business and how it influences the sustainable performance of organizations. This is of great interest to policymakers and business executives, as many well-established researches look into corporate tax and its effects on firm performance. Gatsi, Gadzo and Kportorgbi (2013) assert that the manufacturing sector of any economy is regarded as an essential sector to the growth of the economy as it contributes to the growth of the economy which is mirrored in job creation and increased tax contribution to the nation. The study carried out by Junaidu and Hauwa (2018) also, confirmed that Nigeria has turned to tax administration for revenue generation owing to the depletion of oil prices from 2014. The liberalization of the Nigerian economy thru a range of home grown policies, and World Bank policy

prescriptions over the last four years have modified the structure of the manufacturing sector in Nigeria in a manner that is a challenge for current policymakers and business executives; specifically, how -these businesses are taxed (Junaidu & Hauwa, 2018).

The major issue facing corporate managers in the manufacturing sector is the inconsistency of corporate tax policies (Bauer, Kourouxous & Krenn, 2018). The question is, whether it is the high corporate tax rates that determine poor sustainable performance of firms in the manufacturing sector or poor corporate tax planning carried out by the management of the firms in the presence of various tax incentives. Whatever the case, researchers such as Abiola, James and Asiweh (2012); Adams (2012) and Abiahu and Amahalu (2017) have argued that, taxation plays a role in the growth of corporate organizations. This is as a result of effective tax policies, which apart from generating revenue for the government, serve other purposes like investment attraction. Effective tax policies also serve as a means of protecting emerging firms in the manufacturing sector, as well as creates an incentive for investors to invest in certain areas of the economy (Aloys, George & Thomas, 2015). A tax policy defines the cost structure of firms as it is factored into pricing (Beigi, Rafat & Panah, 2013). Governments, over the years, have made pronouncements and policies that are supposed to create tax incentives for businesses. Fortunately, most of the provisions are to help manufacturing companies to withstand adverse external issues that will impede the growth of the firm (Junaidu & Hauwa, 2018).

Schwellnus and Arnold (2008) examined the effects of corporate income taxes on two of the main drivers of growth; profitability and investment of firms in European OECD-member countries. They found out that corporate income taxes reduce investment through an increase in the user's cost of capital while Junaidu and Hauwa (2018) carried out a study on corporate tax and performance of listed manufacturing firms in Nigeria and found out that corporate tax rate has no significant effect on the performance of the listed firms. This may be partly explained by the negative profitability effects of corporate income taxes if there is an increase in the corporate tax rate without commensurate tax incentives and benefits to the firm. That been the case, this study will examine the effect of corporate tax on the sustainable financial performance of manufacturing companies in Nigeria to see if result now conforms with that of previous studies. In light of this, the study main objective is to examine the effect of corporate tax on sustainable performance of listed firms in Nigeria but its specific objectives are to determine the effect of corporate income tax on the return on equity of listed firms in Nigeria; and examine the effect of corporate income tax on debt to equity ratio of listed firms in Nigeria.

LITERATURE REVIEW

Concept of Corporate Tax

The concept of corporate tax has different dimensions from a conceptual standpoint (Graham, 2003). This research looks at two-dimensional approach. The first dimension considers corporate taxpayers, which is about the evaluation of how this

tax affects the income of firms whilst carrying out production activities; while the second dimension considers corporate tax based totally on its influence on the way firms are financed. The first and second dimensions of corporate tax go hand in hand in influencing the company's preference for a financing decision which is centered on the company's sustainable performance (Graham, 2003). Whatever choice of capital the firm decides, it is quintessential to note that the firm will incur a cost represented by dividends, in case of financing it business activities from its own resources, or interest, if they chose to finance the business through borrowed funds (Modigliani & Miller, 1963). In respect to this puzzle, the management's decision on the choice of capital will need to take into consideration tax issues (corporate tax planning) and the effect it has on sustainable financial performance of the firm.

According to Albertazzi and Gambacorta (2006), corporate tax are taxes levied against the income earned by firms during the course of doing business in a given tax period. Corporate taxes are majorly applied to firms making earnings after expenses are deducted from sales. Myles, (2007) and Lederman (2002) are of the view that tax incentives and advantages such as limited liability to incorporation, which add value to firms' serve as a foundation for corporate tax as well. Firms are taxed because they in many instances, earn some pure economic profits, profits that are more than the return to capital employed. Many authors have defined corporate tax in quite a number of ways, however this study strive to look at the definition made by Myles, (2007); Onourah and Chigbu (2013); Abiahu and Amahalu (2017); Rohoya, Nor'Azam and Bardai (2010) and Musgrave and Musgrave (2004). While Onourah and Chigbu (2013); Rohoya, Nor'Azam and Bardai (2010); Musgrave and Musgrave (2004) and Abiahu and Amahalu (2017) defined corporate tax as the statutory transfer or payment made from non-public individuals, institutions or groups to the government, Myers (2007) asserted that corporate tax is a firm activity other than tax payment, which is about taking benefit of tax incentives for funding decisions. Also, Deloitte (2017) posits that the National Tax Policy of Nigeria in 2012 regarded taxation as basically the process of collecting taxes within Nigeria and as a deliberate effort towards entrenching a strong and efficient tax system in Nigeria. This study will be tailored on the premise of these literature definitions and conceptualization of corporate tax discussed by matching the definition of corporate tax payment and tax incentives which give rise to tax netting.

What Give Rise to Tax Netting

In accounting theory, there is no doubt about the importance of tax adjustment when making tax plans, the purpose of which is to correct the influence of due income tax on the financial performance of firms (Citron, 2014). As stated in Ogundajo and Onakoya (2016) the concept and content of tax adjustment have a certain history, development and experience in Nigeria but it cannot be said that in its practical application, it is a self-evident and seamless part of the current financial report and plans of a firm. Ogundayo and Onakoya (2016) in their work further stated that even though tax adjustment via deferred tax calculation appeared in Nigerian firms accounting reports for the first time in the early1990s, it became more widely known

to the public accounting audience when Nigeria keyed into the use of financial reporting standard propagated by the International Accounting Standard Board (IASB). Since that time, all accounting entities that are obliged to draw up financial statements in compliance with the International Financial Reporting Standards (IFRS) also have to make proper adjustment in their tax liability taking into consideration tax exemptions, allowances and various tax incentives. This was the dawn of accounting methodology for tax netting in Nigeria, as tax accounting practice eliminates distortions of accounting profit or loss due to the impact of different tax conditions for the inclusion of accounting for the various tax exemptions into the tax burden of firms.

Sustainable Financial Performance of Firms

Sustainable Performance of a firm is viewed as the annual proportion of increase in the financial overall performance that is consistent with a defined financial policy of the company (Gatsi, Gadzo & Kportorgbi, 2013). Such performance standards consist of targeted debt to equity ratio, dividend payout ratio, profit margin and return on owner equity. Girish, Harsh and Nidhi (2014) asserts that the concept of sustainable performance presents a precise financial performance framework which is based totally on statistical long-term assessments. It gives an orientation framework for the firm's precise mid- to long-term performance target as well. According to Girish, Harsh and Nidhi (2014), the sustainable performance framework assumes a number of concepts. Some of the concepts ensure that the profit margin of firms remains stable, the percentage of assets and income remains consistent and the firm keeps its current capital structure as well. This is aimed at keeping the company in operation with foresight for meeting up with the accounting going concern principle.

In the fast-changing economic and competitive environment, achieving sustainable growth is no easy task, especially in the present highly complex global environment (Ilaboya, Izevbekhai & Ohiokhu, 2016). Customer attitude, for instance, has changed considerably over the last few decades. They are more discriminative in terms of prices of product which compels the firm to attract customers by adding more values to the products and by offering innovative services than mere regulation of their tax plans in the guise of high prices on the product (Lucaman, 2012). Similarly, competition is keen in almost all the industries, which has been behind unprecedented breakdowns in the barriers that formerly separated them, therefore, companies must look forward to identifying their competitive advantages and their strategic choices in the search for creating sustainable growth (Mucai, Kinya, Noor & James, 2014).

The Expectancy Theory of Tax

This study is anchored on the expectancy theory of Tax. According to Adam (1776), everytax proposal must pass the test of practicality and that must be the only consideration government authority should consider in choosing a tax policy. This theory which focuses on the cannon of economy explains the economic,

effectiveness and efficiency of tax collection instrument. According to Adam (1776), Taxation is seen to provide a powerful set of policy tools to the authorities and such tools should be effectively used for remedying economic and social ills of the society such as income inequalities, regional disparities, and unemployment.

Effective administration of corporate tax in Nigeria can be used as a tool to offset the economic challenges currently facing the Nigerian economy (Chigbu, Eze & Ebimobowei, 2011). Scholars such as Teraoui and Kaddour (2012) carried out a study and found out that good corporate administration fosters investment increase in the country which in turns brings about more employment. While the study of Beigi et al (2013) asserts that the effective administration of tax system increases the revenue base of a country which as a result fosters development and growth of the economy.

Resource-Based View Theory

Pearce and Robinson (2011) define the resource-based view as a method of analyzing and identifying a firm's strategic advantages based on examining its distinct combination of assets, skills, capabilities and intangibles as an organization. This theory views the firm-specificfactors and their effect on performance. Grant (1991) views the firm as a bundle of resources which are combined to create organizational capabilities which it can use to earn above average profitability and in turn settle its tax obligation. Firms develop competencies from these resources and when they are well developed, these become the source of the firm's sustainable financial performance.

Review of Empirical Literature

Ţâţu (2006) analyzed the impact of corporate tax on the profitability of an entity and examined how the deductible expenses and the tax rate reflect on this indicator. Starting from the premise that profitability is the difference between total revenues and expenses and developing this formula in the presence of taxation, it was found that the size of this indicator activates the income volume, the number of expenses, the share of non-deductible expenses in total and the tax rate in the same time. Different hypotheses were tested, based on the relationship between total income and expenses, the conclusions being the following: profitability of an enterprise is influenced by corporate tax through the weight of non-deductible expenses in total.

In the study of Gatsi, Gadzo, and Kportorgbi (2013) on the effect of corporate income tax on the financial performance of manufacturing firms in Ghana, it was revealed that there is a significant negative relationship between corporate income tax and financial performance. It also disclosed that firms' size, age of the firm and growth of the firm show a significant positive relationship with financial performance.

Assidi, Aliani, and Omri (2016); and Pitulice, Stefanescu, Minzu, Popa, and Niculescu (2016) carried out studies on the effect of corporate income tax on profitability of firms in Tunisian and Romania respectively. Using simple regression, they discovered that corporate income tax is statistically significant determinant of

firm profitability a reduction of effective tax rate leads to a significant increase of firm profitability.

Otwani, Simiyu, and Makokha, (2017) investigated the effect of corporate income tax on financial performance of the companies listed on the Nairobi Securities Exchange in Kenya. They used a mixed research design. They found out that there is a positive relationship between corporate income tax and financial performance of listed companies on the Nairobi Stock Exchange in Kenya.

Abiahu and Amahalu (2017) examined the effect of taxation on the dividend policy of banks in Nigeria from 2006-2015, using the Pearson coefficient of correlation, and Ordinary Least Square (OLS) regression analysis. Their study reveals a negative significant relationship between tax and dividend policy. Also, it was discovered that tax has a statistically significant effect on dividend policy.

Junaidu and Hauwa (2018) assessed the effect of company income tax on the financial performance of listed consumer goods companies in Nigeria from 2006-2016 using regression analysis. They found out that there is an insignificant negative relationship between corporate tax and financial performance using the return on assets as a measure.

Ohrn (2018) in his study estimated the investment, financing, and payout responses to variation in a firm's effective corporate income tax rate in the United States. He exploits quasi-experimental variation created by the Domestic Production Activities Deduction, and a corporate tax expenditure created in 2005. His findings showed that a percentage point reduction in tax rates increases investment by 4.7 percent of installed capital, increases pay outs by 0.3 percent of sales, and decreases debt by 5.3 percent of total assets. These estimates suggest that lower corporate tax rates and faster accelerated depreciation each stimulate a similar increase in investment, per dollar in lost revenue.

Findings from the study of Chen, Ge, Louis and Zolotoy (2019) on stock liquidity and corporate tax avoidance shows firms with higher stock liquidity engaging less in extreme tax avoidance. According to Chen et al., (2019), "the effect of stock liquidity on tax avoidance is economically meaningful and robust across alternative measures of tax avoidance and stock liquidity. Their findings also hold after controlling for potential endogenous effects". They further document that the effect of stock liquidity on tax avoidance is amplified for firms with high proportions of activist shareholders and attenuated for firms with high levels of stock price informativeness.

Mohammad and Ahmed (2019) examined the effect of corporate income tax rate on investment decisions of listed deposit money banks in Nigeria. Using descriptive research design and panel data generated from annual reports and accounts of the

sampled banks covering the periods of 2014 to 2018, the study employed Ordinary Least Square (OLS) regression to analyse the data of their study. Findings of their study indicated that after tax cash flow is the major factor that affect investment decisions of listed deposit money banks in Nigeria. Whereas depreciation tax shield and interest tax shield had insignificant effect on investment decisions of listed deposit money banks in Nigeria and corporate tax rate has no effect on investment decisions of listed deposit money banks in Nigeria as the company income tax rate of 30% has been constant over decades.

Vržina and Dimitrijević (2020) analyzed the financial performance of agricultural companies and corporate income tax as key determinants of financial performance. They analyzed the corporate income tax burden of agricultural companies in Vojvodina, as well as its impact on company profitability. They carried out r simple descriptive statistics test which showed that effective corporate income tax rates (ETRs) in agricultural companies are significantly lower than the statutory corporate income tax rate. Their result further revealed that, nearly 69% of observations have both a current effective tax rate and cash effective tax rate of 0%, which indicates that agriculture is an industry with an exceptionally low corporate income tax burden. They further used Panel regression which showed that agricultural companies with lower effective tax rates are more profitable than companies with higher effective tax rate. Results of the analysis are not sensitive to changes in corporate income tax burden and profitability proxies.

METHODOLOGY

This study adopts ex post facto research design and employed Simple Linear regression using Ordinary Least Square (OLS) method in analysing the data collected from the annual financial statement of 10 listed manufacturing firms on the Nigerian stock exchange market from 2013-2017.

Model Specification:

$ROE_{ft} = \alpha + \beta_1 COT_{ft} + U_{ft}$
$DER_{ft} = \alpha + \beta_1 COT_{ft} + U_{ft}$
COT (Reported Corporate Tax paid of the firms at a time)
ROE = Return on Equity (Net Income divide by Total Equity of the firms at the time)
DER = Debt to Equity Ratio (Total Debt divide by Total Equity of the firms at the time)
U = Error term
FT= Firm time
β_1 = Beta coefficient

Decision Criteria: Accept the null hypothesis if the calculated significant value is greater than the accepted significant value of 0.05.

Hypotheses:

Ho_1: Corporate income tax has no significant effect on return of equity of listed firms in Nigeria

Ho_2: Corporate income tax has no significant effect on debt to equity ratio of listed firms in Nigeria

RESULT ANALYSIS AND DISCUSSION

Descriptive Statistics

The table below shows the descriptive statistics of our sample make up.

Table 1: **Descriptive Statistics Table**

Descriptive Statistics						
	N	Minimum	Maximum	Mean		Std. Deviation
	Statistic	Statistic	Statistic	Statistic	Std. Error	Statistic
COT	50	.02	.90	.3465	.03022	.21368
ROE	50	.01	1.28	.2406	.03793	.26819
DER	50	.07	4.38	1.3966	.14541	1.02818
Valid N (listwise)	50					

Source: SPSS V.20

The mean value of COT (the proxy for Corporate Tax rate of the firms) is 0.03022, while its standard deviation value is 0.21368. The maximum value of COT is 0.90 while the minimum value is 0.02. The mean value for the Return on Equity (ROE) is 0.2406 while its standard deviation is 0.26819. The maximum value of ROE is 1.28 while its minimum value is 0.01. Lastly, the mean value of Debt to Equity Ratio (DER) is 1.3966 while its standard deviation value is 1.02818. The maximum value of DER is 4.38 while its minimum value is 0.07 showing that some of the firms held a bit higher DER capital than others.

The various levels of deviation values in the firms' COT, ROE and DER shows the level of fluctuations and variations in the manufacturing sector corporate tax rate, return on equity and debt to equity ratio financing. Also, the minimum and maximum values represent the lowest and highest values of COT, ROE and DER recorded by the firms under review.

Model Summary

The table below reveals the direction of association of the variables of study for both models. To further validate the non-porosity of the data set and results, the study used

the Dublin Watson (DW), Variance Inflation Factor (VIF) and Tolerance Statistics to test for auto-correlation & Multi-collinearity of the data. Considering other tests of multicollinearity in the table below; the VIF and Tolerance Level all stood at 1.000 respectively while the Dublin Watson statistic lies between 0.817-0.983. According to Gujarati and Sangeetha (2007), values of VIF that exceed 10, tolerance level values that are below 0.1 and Dublin Watson values above 2.00 are often regarded as indicating multicollinearity and autocorrelation, which is not the case in this study. This substantiates the validity of the study model & data set .

Table 2: Model Summary Result

	Model 1: COT*ROE	Model 2: COT*DER
R	0.183	0.365
R^2	0.034	0.133
R Adjusted	0.013	0.115
R^2 Change	0.034	0.133
F Change	1.668	7.364
Sig. F Change	0.203	0.009
DW	0.817	0.983
VIF	1.000	1.000
Tolerance	1.000	1.000
Constant	0.320	0.789
Standard Beta	-0.183	0.365
T- Stat	-1.291	2.714
P-Value	0.203	0.009

Source: Authors' Compilation from SPSS Output

The above results in table 2 show that there exists a weak but positive relationship between COT as a proxy for corporate tax rate and variables of sustainable performance (ROE, DER) at 18.3% R-value in the first model (Table 2) and 36.5% R-value in the second model which explains that the model is fit.

Also, the R^2 values for both models stood at 0.034 (Model 1) and 0.133 (Model 2) respectively. The R^2 otherwise known as the coefficient of determination shows the percentage of the total variation of the dependent variable (ROE, DER) that can be explained by the independent or explanatory variable COT. Thus, the R^2 value of 0.034 and 0.133 for model 1 and 2 indicates that 3.4% and 13.3% of the variation in the sustainable performance (ROE and DER) of listed manufacturing firms can be explained by a variation in COT (Corporate Tax Rate) while the remaining 96.6% and 86.7% in model 1 and 2 (i.e. 100-R^2) could be accounted by other variables not included in these models.

The adjusted R^2 of 0.013 and 0.115 in model 1&2 above indicates that if the entire population is considered for this study, this result will deviate from it by only 0.021 (i.e. 0.034 – 0.013) in model 1 and 0.018 (i.e. 0.133 – 0.115) in model 2. This result

shows that there is a deviation of the sample examined from the total population by 2.1% and 1.8% in model 1 and 2 respectively. There are up to 50 listed manufacturing firms on the Nigerian Stock Market of which 10 were considered, using only those whose complete set of financials are available for the time frame of the study. The level of deviation for both models in this study of the samples from the population is below 5% which further validates the results of the models specified and serves as a pointer to the fact that the manufacturing sector is wholly represented at more than 95% degree of confidence intervals.

Furthermore, to determine the directional relationship between COT (Corporate Tax Rate) and sustainable performance variables (ROE & DER) shows that when Corporate Tax Rate (COT) is held stationary, the sustainable performance (ROE & DER) variables in both models are estimated at 0.320 and 0.789 in model 1 and 2 respectively. This simply implies that when COT is held constant, there will be an increase in ROE and DER of manufacturing firms up to the tune of 0.320 and 0.789 units in model 1 and 2 respectively occasioned by factors not incorporated in this study. Thus, a unit increase in COT will lead to a decrease in the ROE (Model 1) of firms by 18.3% while, a unit increase in COT will lead to an increase in DER (Model 2) by 36.5%.

Discussion of Results

Given the result obtained above from the models formulated which are in line with the stated specific objectives; to examine the effect of corporate tax rate on return on equity (0.203) and to determine the effect of corporate tax rate on debt to equity ratio (0.009) of listed manufacturing firms in Nigeria.

Ho_1: Corporate income tax has no significant effect on return of equity of listed firms in Nigeria

The findings from the first specific objective revealed that corporate tax rate has no significant (P-value: 0.203) effect on return on equity of the firms. This finding is in line with that of Junaidu and Hauwa (2018) who carried out a study to ascertain the effect of company income tax on the financial performance of listed consumer goods companies in Nigeria from 2006-2016 using regression analysis. In their study, they found out that there is an insignificant negative relationship between corporate tax and financial performance of the firm. The result of the first specific object is also in line with the a-priori expectation that corporate income tax is expected to reduce the return on equity of the firms as shown in the result which denotes a negative relationship between COT and ROE.

Ho_2: Corporate income tax has no significant effect on debt to equity ratio of listed firms in Nigeria

In the second specific objective, findings revealed that corporate tax rate positively and significantly (P-value: 0.009) affects the debt to equity ratio of the listed manufacturing firms in Nigeria. The choice of the firm's capital combination is greatly affected by the tax rate as most managers go for more debt financing to shield against tax. This assertion is in line with that of Modigliani and Miller (1963) who opined that firms' capital structure decisions are influenced by corporate income tax. Also, this notion is supported by the trade-off theory as postulated by Meyers (2001) who asserts that, firms will owe to a certain debt level where tax shields from extra debt will equate the cost of financial distress. The result of the second specific object is also in line with the a-priori expectation that corporate income tax is expected to increase the debt to equity ratio (Leverage) of the firms as shown in the result which denotes a positive relationship between COT and DER; this is made possible by the firms' managers decision to use more leverage as a shield against corporate income tax.

CONCLUSION AND RECOMMENDATIONS

From the findings of this study, it is concluded that corporate tax payout does not significantly affect the return on equity of firms but has a positive and significant effect on debt to equity ratio of the listed manufacturing firm in Nigeria.

As a result, it is recommended that investors in the manufacturing sector should use their tax payout policy as a tool for financing decision as it greatly affects the firm's debt to equity ratio combination decision making. Also, they should encourage the prompt payment of tax as it has no significant effect on their returns but by paying it will increase the market value of their firms.

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