

ARTICLE

# Corporate Governance and Tax Avoidance: Evidence from Nigerian Quoted Food and Beverage Companies

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ABSTRACT

The study determine the effect of CEO duality on the effective tax rate of quoted foods and Beverage companies. *Ex-post facto* research design was adopted. A purposive sampling technique was applied in selecting nine (9) companies during the data collection process. Data were collected from annual reports and accounts of the sampled companies from 2013-2019. Data for the study analyzed using descriptive statistics and regression was used with aid of the e-view was at 95% confidence at five degrees of freedom (df). The result shows that CEO duality was significant and had a positive coefficient on tax planning of food and beverage companies in Nigeria. The study, therefore recommended that non-separation of CEO from Chairman of the Board may lead to higher levels of tax planning; and an opportunity for manager's rent extraction, because of their dominating role to ensure that adequate oversight roles are separated.

## 1. Introduction

Corporate governance refers to policies and procedures adopted by firms to achieve certain sets of objectives, corporate missions, and visions concerning different stakeholders<sup>[1]</sup>. Corporate governance enhances the means through which the objectives are set, and the means of executing those objectives and monitoring performance are ascertained<sup>[2]</sup>. It is directed at improving corporate behaviour and the reliability of accounting information provided to the stakeholders<sup>[3]</sup>. Corporate governance is a combination of company's management, board, shareholders, and other stakeholders<sup>[2]</sup>. According to<sup>[4]</sup>, corporate governance ascertain if the finance providers earn a

return on their investments.

Tax is a levy imposed on individual or legal entity by the Government or agent<sup>[5]</sup>. The government uses the proceeds from the tax to provide its legal functions, which include the provision of amenities and infrastructure, defense against external aggression, maintenance of law and order, regulate economy<sup>[5-6]</sup>. Corporate tax avoidance refers to the deliberate attempt to reduce the amount of taxes paid. Tax avoidance can be divided into acceptable (legal) tax avoidance and unacceptable (illegal) tax avoidance<sup>[7]</sup>.

Previously, manufacturing companies in Nigeria were required to prepare accounts using the Statement of

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Accounting Standards. However, following the recommendation of the Financial Reporting Council of Nigeria (FRCN), henceforth from 2012 all manufacturing companies complied with the provisions of the International Financial Reporting Standards in the preparation of financial statements. On January 15, 2019, the FRCN released the Nigerian Code of Corporate Governance ('the Code'), according to Sections 11(c) and 41(c) of the Financial Reporting Council of Nigeria Act, 2011. This formed part of the move to strengthen and institutionalize corporate governance best practices in Nigerian companies. The Code adopts an approach in designing the minimum standards of practice that all the firms should adhere to<sup>[8]</sup>.

Different stakeholders perceive such tax avoidance acts differently from its consequent implication. For instance, shareholders may prefer tax avoidance because it increases residual income and lowers the cost of debt<sup>[9]</sup>; whereas, the Government kick against tax avoidance because it lowers the amount of revenue available for developmental activities<sup>[10]</sup>. Negative consequences of tax avoidance include reputational damage and a decline in firm value<sup>[11]</sup>, which resulted to a lower in the return on investments of the shareholders<sup>[12]</sup>. Another issue is the question of if the firm enhances the economic well-being of the society<sup>[13]</sup>. Other consequences that may arise are related to political costs and marginal costs. High corporate tax avoidance leads to higher political costs<sup>[14]</sup>. Marginal costs are potential costs, such as penalties and fines imposed by the tax authorities<sup>[15]</sup>. Corporate tax avoidance is an outcome of policies/decisions taken by the leaders of a company<sup>[16]</sup>.

Within the Nigerian context, few studies are yet to address the efficiency with which the board and other sub-committees discharge their responsibilities. According to<sup>[17]</sup> board and committee activity may be measured by the frequency of meetings.

Prior studies have conducted research on this nature in several countries. The studies provide counterintuitive predictions on the link between governance and tax avoidance. While some reported a positive effect, others report a negative association. Such studies have mainly used proxies such as meeting frequency, board size, board independence, CEO duality, among others as proxies for good corporate governance. The study therefore, sought to analyze the effect of corporate governance on tax avoidance from a developing country perspective.

## 2. Review of Related Literature

### 2.1 Corporate Governance

Several authors have defined corporate governance from diverse perspectives; According to<sup>[18]</sup>. This ex-

propriation acts include among others the diversion of profits/output; sale of assets or securities to other firms at below-market (fair) prices; employ unqualified family members in managerial positions; and/or over compensation packages. Corporate governance is concerned with enhancing corporate fairness, transparency, and accountability<sup>[19]</sup>.

Corporate governance is the mechanisms aim at ensuring the fulfillment of corporate objectives<sup>[20,21]</sup> stated that corporate governance is the process that allows directors and auditors to assume their obligations towards shareholders and company stakeholders".<sup>[22]</sup> corporate governance as the systems that checkmate both internal and external to activities of companies to ensure that companies discharge their accountability to their stakeholders".<sup>[23]</sup> documented that "corporate governance is a procedure, by which corporate resources allocated in a way to attract stakeholders wealth. According to<sup>[24]</sup>, it involves firm; management, shareholders and stakeholders". Corporate governance is the system by which companies are directed and controlled<sup>[25]</sup>. The Organization for Economic Co-operation and Development<sup>[26]</sup> outlined five principles of corporate governance to include:

- The rights of shareholders
- Equitable treatment of shareholders
- The role of stakeholders
- Disclosure and transparency
- The responsibility of the board.

Broadly, corporate governance mechanisms are subdivided into two: internal and external corporate governance mechanisms. The external governance mechanisms include such as the market for corporate control, the legal system, stock market, among others<sup>[27-28]</sup>. Internal governance mechanisms include such as the board of directors, manager's compensation, audit committee, remuneration committee, and ownership structure, among others<sup>[29-31]</sup>. The internal governance mechanisms are mainly associated with the structure, composition and, characteristics of the board of directors<sup>[32]</sup>. The study by<sup>[33]</sup> found a relationship between improved corporate governance and firm performance.

### 2.2 Corporate Tax Avoidance (CTA)

Corporate tax avoidance (CTA) has no specific accepted definition in the literature<sup>[12]</sup>. This lack of universal definition follows the consequential tax effect of every business transaction aimed at increasing profit<sup>[13]</sup>. According to<sup>[34]</sup> CTA involves "taking advantage of legitimate concessions and exemptions foreseen in the tax law; and, involves the process of organizing business operations so that tax obligations are optimized at their minimum

amount".<sup>[35]</sup> reported that tax aggressiveness is the different legal or illegal activities management engaged to reduce taxable income. Tax planning forms part of strategic decisions by the managers aimed at reducing explicit and implicit taxes.<sup>[36]</sup><sup>[13]</sup> defined CTA as a strategy in reducing corporate tax liabilities.

<sup>[37]</sup> opine that CTA refers to as a means of minimizing the company's tax accounting income".<sup>[12]</sup> sees tax avoidance as a strategy to reduce taxable income (e.g., tax shelters) at the other end.

<sup>[34]</sup> observed that generally, tax planning activities lead to a reduction in tax obligations. This however depends on the intensity and legality with which these practices are adopted.<sup>[38]</sup> stated that tax avoidance is the legal application of tax laws to one's selfish interest in order to minimize the taxable income within the law."<sup>[39]</sup> sees tax aggressiveness as an arrangement with the aim of avoiding tax.

Tax planning, avoidance or, aggressiveness has significant costs and benefits to a firm and its shareholders<sup>[40]</sup>. The benefits to the firm include such as higher cash flows and net income; while, to the shareholders, it implies higher residual income<sup>[41]</sup>. The costs include negative consequences such as large penalties, negative publicity<sup>[42]</sup>, political costs<sup>[14]</sup>, or the firm labelled as a "poor corporate citizen"<sup>[11]</sup>. Three conditions must exist for an individual or firm to engage in tax avoidance; incentive, access, and awareness<sup>[43]</sup>. Incentive implies that the perceived benefit must outweigh its costs. Access presupposes that the individual or firm has access to tax-minimizing strategies. Finally, the individual or firm is aware of the applicable tax laws that allow such opportunities available to avoid taxes.

<sup>[13]</sup> identified three classes of groups used in prior literature to measure tax avoidance. Which comprise of total book-tax gap; measures the proportional amount of taxes to business income and measures such discretionary.

There are several methods and/or schemes by which corporations engage in tax avoidance.<sup>[44]</sup> identified the use of transfer pricing, royalty programs, off shore tax havens and structured transactions.<sup>[45]</sup> identified other methods such as debt allocation as well as sourcing rules for foreign tax credits.

### 2.3 CEO Duality

<sup>[46]</sup> stated that a measure of board independence is whether the CEO also serves as the board chairman. The separation of CEO from Board chairman ensures adequate monitoring and checkmating the activities of management<sup>[24]</sup>. The non-separation of the two functions presents an obstacle and leads to managerial entrenchment<sup>[47]</sup>.

Non-separation of the two roles decreases the effectiveness of the board in monitoring management<sup>[48]</sup>; and, its ability to control managers effectively<sup>[49]</sup>. The empirical literature documents mixed findings on the association between CEO duality and firm performance.

<sup>[50]</sup> found a significant negative association between duality and disclosure. On the contrary,<sup>[51]</sup> found an insignificant relationship between duality and disclosure.<sup>[52]</sup> reported a positive association between board independence and audit fees. However, the positive association was only present in firms without CEO duality; suggestive of the fact that CEO duality constraints board independence.

### 2.4 Empirical Studies

Quite a number of researchers have conducted a study on corporate governance and tax avoidance; the study of<sup>[53]</sup> ascertained the effect of corporate board characteristics and tax aggressiveness of Nigerian manufacturing firms. Sample of forty-nine (49) manufacturing firms was used. Data were obtained from annual financial statements for the years 2011 to 2016. The data were analyzed using the fixed effect panel regression model. The results showed that board size and board independence exert a significant negative effect on tax aggressiveness; while, board gender had an insignificant negative effect.<sup>[54]</sup> examined the effect of corporate governance, tax avoidance, and financial constraints'. The sample comprised of over thirty-five thousand (35,000) firm-year observations from 1990 to 2015. They employed two-stage least squares (2SLS) analysis to validate the hypothesis. The results showed that for firms with strong governance, tax avoidance had a negative impact on financial constraints. However, in weak governance, tax avoidance is associated with greater financial constraints and a greater likelihood of financial distress.<sup>[55]</sup> ascertained the Demographic characteristics of the board of directors' structure and tax avoidance from Tehran Stock Exchange. The study relied on secondary data; between the periods 2012 to 2016. The hypothesis was tested using panel regression models. The results showed that the presence of women on corporate boards reduces corporate tax avoidance; also, firms with larger board sizes were associated with more tax avoidance.<sup>[56]</sup> conducted a study titled 'Corporate tax and financial performance of listed Nigerian consumer goods'. The sample comprised of sixteen consumer goods firms quoted on the NSE. The data were analyzed using multiple regression analysis. The results showed an insignificant negative relationship between corporate tax and ROA. However, age and risk had a positive non-significant relationship with ROA; while, size showed a positive significant relationship with ROA.<sup>[57]</sup> investigated corporate tax avoid-

ance of listed firms in Nigeria'. The sample comprised of nineteen (19) listed firms drawn from the list of NSE 30 firms on the Nigeria Stock Exchange. The data were obtained from annual accounts and were analyzed using descriptive statistics. The results showed that there exists variation across firms in the average long-run cash ETR. [4], undertook a study titled 'Tax Avoidance and Corporate Governance. The sample comprised four hundred and ninety five (495) firms in the Standard and Poor's 500 firms. The study covered the period from 2007 to 2015. The study relied on secondary data from Compustat and Institutional Shareholders Services (ISS). The hypothesis was validated using the fixed effects model. The results showed that board independence had a significant negative effect on tax avoidance; while, CEO duality had a negative insignificant effect on tax avoidance. [58], conducted a study whether corporate governance affect earnings management on tax aggressiveness?' The study employed secondary data from annual report and accounts from the official website of the companies and the IDX website. The results showed that good corporate governance moderates the influence of earnings management toward the tax aggressiveness. [59], studied the impact of governance mechanisms on tax aggressiveness: Empirical evidence from Tunisian context'. The sample comprised thirty-nine (39) firms listed on the Tunisian Stock Exchange. The data were analyzed using multiple regression techniques. The results showed that board size had negative non-significant effect on tax aggressiveness. Diversity, managerial ownership, firm size, and debt had a positive significant effect. The variable of audit quality had a positive non-significant effect; while, ownership concentration had a negative significant effect. [60] conducted a study titled 'The quality of reported earnings and the monitoring role of the board: Evidence from small and medium companies'. The study employed secondary data from the Johannesburg Stock Exchange and data from McGregor BFA. They used regression to examine the relationship. The study finds no evidence that boards and non-executive directors of SMEs adopt conservative accounting practices that will result in

the asymmetric timeliness of earnings. [61], evaluated the impact of the board of directors' structure on tax avoidance in the companies listed in Tehran Stock Exchange. They employed a binary logistic regression. Results showed that board non-executive members and board change ratio had a non-significant effect on tax aggressive policy. However, CEO duality had a significant effect on tax aggressive policy. [62], studied the effects of the board of directors' characteristics on tax aggressiveness'. The sample comprised seventy three (73) companies listed on the SBF 120 index, France. The study employed multiple regressions to analyze the data. The results showed that board size negatively affects effective tax rate; board independence has a negative non-significant; board diversity has a positive significant effect on effective tax rate; and, CEO duality has a negative non-significant effect on effective tax rate. [53], ascertained the effect of the board of director composition on corporate tax aggressiveness'. They employed logit regression to validate the hypothesis. The results proved that higher rate of external members on the board of directors lower the likelihood of tax aggressiveness.

### 3. Methodology

An *ex post facto* research design was employed. This type of design is a systematic empirical inquiry, in which the researcher has no direct control of the variables in case of manipulation.

The population of this study covered twelve (12) Foods and Beverages in Nigeria. A purposive sampling technique was used. A total of three (3) out of the twelve (12) companies were inevitably excluded during the data collection process due to unavailability of data.

#### 3.1 Methods of Data Analysis

Descriptive statistics and regression analysis were used to test the relationship between the independent variable (CEO Duality) and the dependent variable (corporate tax avoidance). This was done with aids of the e-view version

**Table 1.** Description of variables

**Dependent Variable**

CTA<sub>it</sub> = Proxied as the Effective Tax Rate. This is the proportion of the profit before tax is paid as tax. It is computed as tax paid divided by profit before tax. The Statutory Tax Rate is the official corporate tax rate; which presently in Nigeria is 30% of the assessable profit.

**Independent Variable**

CEODU<sub>it</sub> = Takes the value of 1 if CEO and the chairperson positions are held by the same individual, 0 otherwise in the period (t)

**Control Variables**

Size<sub>it</sub> = Measured as the natural logarithm of total assets in the period (t)



9 was at 95% confidence at five degree of freedom (df).

**Decision Rule**

The alternative hypotheses is to be accepted if the p-value is less or equal than the alpha and to be rejected the if the p-value is greater than alpha at 5% significance level.

**Model Specification**

$$ETR_{(i,t)} = \alpha + CEODU_{(i,t)} + Size_{(i,t)} + \mu$$

Where:

ETR<sub>(i,t)</sub> = Effective tax rate of firm i at time t

CEODU<sub>(i,t)</sub> = CEO Duality of firm i at time t

SIZE<sub>(i,t)</sub> = Firm size of firm i at time t

μ = Error term (stochastic term)

**Description of variables**

The table below presents the description of the variables included in the model

**4. Data Analysis and Result**

The panel data obtained from the annual reports and accounts of the sampled firms from 2013 to 2019.

**4.1 Descriptive Statistics**

**Table 2.** Descriptive statistics of independent (corporate governance) variables

	ETR	CEODUALITY	AVERAGE_ASSET
Mean	9.401361	0.761905	1.38E+11
Median	9.000000	1.000000	8.05E+10
Maximum	17.00000	1.000000	7.45E+11
Minimum	0.000000	0.000000	0.000000
Std. Dev.	3.259674	0.427374	1.68E+11
Skewness	0.218983	1.229837	1.627434
Kurtosis	2.988632	2.512500	4.808414
Jarque-Bera	1.175654	38.51189	84.92026
Probability	0.555533	0.000000	0.000000
Observations	9	9	9

Source: E-Views 9.

The Table 2 (shown above), presents the mean (average) for each of the independent variables, median, their minimum, maximum, standard deviation, Kurtosis, Skewness, and the Jarque-Bera statistic (and associated p-value). The variable CEO Duality had an average value of 0.761

(76.2% of the entire observations recorded a value of one, i.e., CEO and Chairman of the Board are the same person; while 23.8% of the entire observation recorded a value of zero). CEO duality is positively skewed. The kurtosis values for CEO duality had values less than 3; they can be considered *platykurtic* relative to the normal. The Jarque-Bera statistic showed that CEO duality had p values>.05. The control variable firm size showed p values of the Jarque Bera statistic all less than .05; this is an indication of non-normality of the variable.

**4.2 Test of Hypothesis**

H<sub>1</sub>: There is a significant effect of CEO duality on effective tax rate of quoted food and beverage companies in Nigeria.

**Table 3.** Ordinary Least Square (OLS) analysis between ETR and CEODU

Dependent Variable: ETR				
Method: Panel Least Squares				
Date: 10/02/20 Time: 09:04				
Sample: 2013 2019				
Included: observations: 7				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-4.84E-17	3.96E-17	-1.223676	0.2882
CEODU	1.000000	2.88E-16	3.47E+15	0.0000
SIZE	0.000000	4.49E-22	0.000000	1.0000
R-squared	0.438092	Mean dependent var		1.000000
Adjusted R-squared	0.418327	S.D. dependent var		0.000000
S.E. of regression	2.72E-16	Akaike info criterion		11.70756
Sum squared resid	2.96E-31.	Schwarz criterion		1.000000
Log likelihood	-874.0671	Hannan-Quinn criter.		11.74018
F-statistic	7.548921	Durbin-Watson stat		0.411106
Prob(F-statistic)	0.000037			

Source: E-Views 9.0 Panel Regression Output, 2020.

Table 3 shoes an adjusted R<sup>2</sup> value of 0.42. The adjusted R<sup>2</sup>, which represents the coefficient of multiple determinations imply that 42% of the total variation in

the dependent variable (ETR) of the sampled companies in Nigeria is jointly explained by the explanatory variables (CEODU and SIZE). The adjusted  $R^2$  of 42% did not constitute a problem to the study because the F- statistics value of 7.548921 with an associated  $\text{Prob.} > F = 0.0000$  indicates that the model is fit to explain the relationship expressed in the study model. The value of adjusted  $R^2$  of 42% also shows that 58 % of the variation in the dependent variable is explained by other factors not captured in the study model. This suggests that apart from CEO-DU and SIZE there are other factors that mitigate ETR of quoted companies in Nigeria. The results shows that CEODU has a positive and significant relationship with ETR measured with a beta coefficient ( $\beta_1$ ) and t- value of 1.000000 and 3.47 respectively and p- value of 0.000 which is statistically significant at 5% level.

### 4.3 Decision

Based on the empirical evidence that suggests that there is a significant effect of CEO duality on effective tax rate of quoted food and beverage companies in Nigeria at 5% level of significance, thus, the alternative hypothesis of the study is accepted.

### 4.4 Discussion of Findings

All the corporate governance variables were insignificant. Studies have shown that low ETR rates imply that a firm engages in tax planning more aggressively; while, higher ETR rates may imply a more conservative approach to tax planning.

The corporate governance variable of CEO duality was significant; CEO duality had a negative coefficient. The sign of the coefficient of CEO duality is consistent with the study by <sup>[61]</sup> in Iran using binary logistic regression showed that CEO duality had a significant effect on tax aggressiveness.

However, the study by <sup>[4]</sup> on firms drawn from S & P 500 which documented a negative insignificant effect of CEO duality on tax avoidance. <sup>[32]</sup> showed that tax evasion were significantly lower in firms where board chairman is also the CEO. Also, <sup>[62]</sup> reported a negative non-significant effect of CEO duality on effective tax rate.

The control variables firm size is not significant. However, <sup>[16]</sup> in Indonesia reported a insignificant positive effect of firm size and audit quality on tax avoidance. <sup>[59]</sup> in Tunisia, reported a significant positive effect of firm size.

## 5. Conclusion

This study assesses the relationship between corporate governance and corporate tax avoidance. The study there-

fore, expands the scope of prior research by estimating the relationship. This study found that CEO duality impact positively on effective tax rate (ETR), and this was statistically significant. The control variable, firm size showed statistical insignificance at 5% level. It imply that to improve the value of the firm, the owners of the firm would prefer to reduce their taxable income. Besides, they desired to plan diligently for the company. The study therefore, recommended that non-separation of CEO from Chairman of the Board may lead to higher levels of tax planning; and an opportunity for manager's rent extraction, because of their dominating role in order to ensure that adequate oversight roles are separated.

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