MANAGEMENT ABILITY AS A DETERMINANT OF AGGRESSIVE CORPORATE TAX PLANNING PRACTICE OF LISTED MANUFACTURING COMPANIES IN NIGERIA

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Abstract

Recently, the alarming rate of increased in tax rate across the developing nations have becoming more worrisome. This issue has become major concern in Nigeria manufacturing, which has consequently resulted into poor corporate tax planning. In the light of this issue, this study investigates management ability as a determinant of aggressive corporate tax planning practice of listed manufacturing companies in Nigeria. The research design used in this study was ex-post facto; as of the date of the study, 39 companies that manufacture consumer and industrial goods were listed on the floor of the Nigerian Stock Exchange (Nigerian Stock Exchange Fact book, 2020). The study concentrated on 29 manufacturing companies for a period of twelve years, from 2013 to 2020. Therefore, the total number of observations was two hundred and thirty-two (232), which is the product of 29 manufacturing companies and eight years. Based on the study's findings, listed manufacturing companies in Nigeria have a positive and significant link between their corporate tax planning approach and management ability (Manab) variable (1, 232) = 2.4889, $\beta 1 = 0.1393$, $p = 0.0135$). At the significance level of 0.05, the probability value of 0.0135 is less than that. On this note, this study concludes that Managerial ability has significant positive impact on corporate tax planning strategy amongst listed manufacturing companies in Nigeria. Therefore, this study recommends that shareholders should place emphasis on the engagement of managers with higher-ability because they have capability to align corporate decisions with tax strategies and identify opportunity to increase the value of the company and maintain its sustainability.

Keyword: Management Ability, Corporate Tax Planning Cash Effective Tax Rate

Introduction

Amidst the worldwide financial crisis, managers and company owners are increasingly concerned about taxation, operating costs, companies' competitiveness, and firm survival. These factors can negatively impact a company's profitability, sustainability, and overall performance. Because of this, the tax burden is seen as a significant expense on the profitability of the company. These companies must develop corporate tax planning techniques in order to maintain their organization and grow its worth. Globally, corporate tax planning is understood to be an attempt, whether via legal or illicit means, to lower a company's taxable income. It entails ways of exploiting loopholes in the tax law in order to reduce companies' tax liabilities or anything that reduces companies' cash effective tax rate over a long time period. (Amrie, 2018).

Due of the deterrent effect of high tax rates, many companies, especially manufacturing corporations (MCs) at both developed and developing counties, are constantly looking for ways to lower their corporate income tax obligations. Any manufacturing companies that wants to successfully lower their tax liability needs to have management who have a strategic grasp of the many tax benefits found in each country's tax legislation. Pioneer status incentive, initiation rule, cessation rule, investment allowance, and roll-over loss relief are a few examples of these incentives. Others include business location or area of operation (free trade zone, rural area investment allowances), tax exemption benefits on interest on a loan granted by a foreign company, asset acquisition timing for claims of capital allowances, etc. (Ogundajo & Onakoya, 2016).

However, companies' long-standing use of strategic tax planning has put both industrialized and emerging economies' efforts to expand their infrastructure at risk. For example, in developed economies, unlawful tax planning continues to be the biggest compliance risk to the US tax system (Summer & Sarin, 2019). The US Treasury projects that there will be a yearly loss of tax income of about $10 billion, they claim that this is what has led to a significant threat to the United States. Likewise, the European Union is not exempt from this; it is estimated that tax planning costs the EU between 50 and 70 billion euros annually.

In the same vein, the anti-avoidance unit of Her Majesty's income and Customs in the United Kingdom calculated that tax evasions result in billions of pounds' worth of lost income annually (UK HMRC, 2016). When a result, the government incurs more costs when the authorities use risk classification evaluations to carry out tax investigations. This means that tax planning techniques raise the expense of tax compliance while also having a detrimental effect on government revenue. It has absurd effects on the economy and government treasury; it lowers the amount of public goods provided and addresses more broad social issues (UK HMRC, 2016).

In Nigerian companies, various reward packages, particularly in the manufacturing sector, are offered to managers who can guarantee the companies' survival by lowering operating expenses and tax obligations. When these managers successfully utilize their technical expertise and skill set to take advantage of every tax planning opportunity, including tax avoidance tactics, they become increasingly adept at producing financial gains from regular operations. Conversely, a manager who lacks relevant knowledge and certification in tax affairs is likely to create a subpar tax planning strategy for the organization. Several enterprises in the country have collapsed as a result of this.

In of view of foregoing problems, various emphasized have been discussed in literature as to different determinant of tax planning strategies. However, to the best of the researcher's knowledge, company tax planning strategy and managerial ability are still mostly undiscovered. In summary, there has been a dearth of study expressly addressing the companies' characteristics, corporate tax planning, financial difficulty, and managerial ability of Nigerian listed manufacturing enterprises. Research evidences on tax planning in Nigeria has majorly focused on either of tax planning and firm value (Nwaobia, 2016), tax planning and financial performance (Fagbemi, Olaniyi & Ogundipe, 2019; Ogundajo & Onakoya, 2016), corporate governance and tax planning (Salawu & Adedeji, 2017), corporate effective tax rate and firm performance (Inua, 2018). On this note, this study examined management ability as a determinant of aggressive corporate tax planning practice of listed manufacturing companies in Nigeria.

Literature Review

Conceptual Review

Koester, Shevlin and Wangerin (2017) use the terms "tax planning", "tax avoidance", "tax management", "tax aggressiveness" simultaneously to define tax strategy and defined "tax sheltering" as a particularly aggressive form of tax planning. In conclusion, the authors stated that further research may increase the likelihood of an accepted definition, even though they acknowledged that the lack of a single, clear definition of tax planning hinders the development of more effective measures Koester Shevlin and Wangerin (2017). Contrarily, Ching, Gerab and Toste (2017) conceptualized that tax planning includes tax avoidance or tax aggressiveness that are legal, or that may fall into gray area, as well as activities that are illegal. Tax aggression does not always mean that the company has engaged in unethical behavior. For the purpose of achieving the objective of this study, this study conceptualized tax planning as the cash taxes paid divided by pre-tax income prior to exceptional items.

In the light of managerial ability, Demerjian, Lev, Lewis and McVay (2013) defined managerial ability as the ability of the manager to efficiently marshal the firm's resources. Managerial ability is further viewed by Hambrick and Mason (2014) as well as Jakada and Aliyu (2015)as the integrated skills of the entire top management. All these studies are contend that because the measure can be used with large panel data sets due to its utilization of a variable stated in financial statements, it is appropriate for research on business effective tax planning. Ching, Gerab and Toste (2017) defined managerial ability as efficiency of manager as well as the degree of management's efficiency to utilize a firm's resources (tangible and intangible) in generating revenue. Stated differently, the definition and assessment of managerial ability in their work concentrated on the capacity of firms to generate revenue (output) through the estimation of total firm efficiency (TFE). This suggests that efficient firms are able to produce more revenue from a given set of inputs (assets). However, the estimated total firm efficiency is influenced by the manager and firm-specific characteristics, so data envelope analysis (DEA) was used to regress TFE on firm characteristics and convert it into managerial ability. Therefore, this study define managerial ability, as a firm-specific attribute, is crucial in determining a company's financial performance, especially when it area of tax.

Theoretical Review

Various theories such as agency theory, stakeholder theory and Upper Echelon's Theory (UET) on company managerial ability and efficient tax planning have been put forth. In the light of this, Hambrick and Manson (1984) were the first proponents of Upper Echelon's Theory (UET). The theory was developed on the tenet that the knowledge, experiences, and skill of individuals holding significant leadership positions within an organization directly affect organizational outcomes. The authors presented a model in which managers respond to situations that arise in the context of organizational life and make strategic decisions based on the distinctive qualities that these people possess. It is claimed that these people's decisions have a direct impact on the functioning of the organization. To balance these "upper echelons'" effects on organizational performance Hambrick and Mason (1984) argued that focus should be directed towards those data readily observable reflecting individual characteristics with respect to the educational, professional, and social backgrounds of prominent managers in organizational contexts. The upper echelons assume that organizations are reflections of their top managers (Martin, 2011).

In the light of these arguments, this study anchored on the prediction of Upper Echelon's Theory

after critically reviewing the theories to the study, this study is anchored on the Upper Echelon's Theory. The theory highlights the significance of the top management team as the ultimate decision-making body within an organization and highlights the fact that the ability and sound knowledge of individual executive managers are what really matter when it comes to making actual decisions within an organization. Therefore, managers with greater ability offer better tax planning strategies that can lower corporate income tax liabilities, demonstrate cost minimization, increase short-term working capital, lower the effective tax rate of the company over an extended period of time, improve the performance of the firm, and increase market shares, all of which will benefit the company's owners by creating wealth.

Empirical Review

Empirically, a number of research questions, including those that examined at executive compensation, corporate governance, and the economic effects of corporate ownership most importantly, managerial firm to firm performance and investment decisions, and executive ability or talent quantification in developed countries are fundamental to these studies. Previous study has demonstrated that proxies such as business size, past anomalous control performance, salary, tenure, media mentions, education, or manager fixed effects are used by researchers to estimate management aptitude. Researchers have also recently used data envelopment analysis (DEA) to infer management skill.

Demerjian, Lev and McVay (2012) studied on quantifying managerial ability: a new measure and validity test. The study included a sample of 78 CEOs from US companies that had switched, and it used manager fixed effects as the explanatory power to describe managerial skill. After adjusting for company fixed effects, the results of the Data Envelopment Vector Analysis showed that manager fixed effects are statistically significant in explaining managerial ability. Furthermore, the outcome shows that managerial skill measures impact business efficiency in contrast to firm fixed effects, which are weaker but still have more explanatory power. Another study by Demerjian et al. (2012) was carried out in the US using a sample of 2,229 enterprises that had a CEO transition during the study period. Correlation approaches for managerial aptitude and proxy MA with CEO departure announcements were employed in the study. The findings indicate that the departure of CEOs with poor ability is linked to positive stock price reactions, whereas the departure of CEOs with strong ability is linked to negative stock price reactions.

Again, Demerjian *et al.,* (2013) carried out another research by obtaining data from the following sources: the 2009 annual Compustat file (for financial statement data), the Morningstar database (to track traditional managers across firms, with coverage from 1999 to 2009), the Execuomp database (for executive compensation and tenure to track managers across firms), the Centre for Research in Security Prices (CRSP) file (for returns data), and Audit Analytics (to obtain the 8-K fillings dates of CEO turnover announcements, with coverage from 2000 to 2009). Optimization and OLS regression techniques were used to produce a final sample of 177,134 because many of the variables were missing in the Composted before 1980. The study's samples include all firm-year observations from 1980 to 2009 cutting across large firms in the US with the necessary data to calculate the firm efficiency measure. The findings show that managerial skill is positively correlated with performance at the CEO's new appointments and negatively correlated with price reactions to announcements of CEO change. It also shows an economically meaningful link with manager fixed effects.

Aganyo (2014) conducted a research on corporate tax planning and its effects on firm value for companies listed on Nairobi Stock Exchange. Given that the aim of the study was to investigate the impact of tax evasion on financial performance among listed manufacturing companies in Nairobi, the research methodology was casual predictive. All of the firms listed on the Nairobi Securities Exchange made up the study's population, and for the five years between 2009 and 2013, 20 companies with complete data were selected using a secondary method of data collecting on the variables of interest. Thus, the study concluded that tax planning influences the performance of listed companies in Kenya. The results also showed that firm age had a negative but significant effect on firm value; firm size had a positive and significant effect on firm value; leverage had a negative and significant effect on firm performance; and firm age had a positive but insignificant effect on firm value.

Amrie (2018) study examined the relationship between managerial ability and tax aggressiveness of listed manufacturing companies in the Indonesia Stock Exchange (ISE) with a particular focus on variables affecting the tax aggressiveness of those companies. To measure the variables, the author employed the dynamic panel system of linear regression method (LRM) estimate. For a period of five years (2011-2015), a sample of thirty-six manufacturing firms were selected from among the 144 manufacturing companies listed on ISE, which made up the study's population of non-financial Indonesian firms. DEA was used to quantify managerial ability, and the results indicated that tax aggressiveness was significantly positively impacted by managing ability. As a result, tax aggression increases with managerial skill. That is, a manager with higher ability has a greater grasp of the resources and workings of the business, which helps the business somewhat by reducing cash outflow and freeing it up for other internal investment projects. A skilled manager may better oversee the effectiveness of a business's resources, which encourages the business to continue operating, comply, or refrain from fulfilling its tax requirements (Amrie, 2018).The author came to the conclusion that managerial skill positively affects tax aggression, particularly when there are plenty of opportunities to engage in tax aggression.

Ogundajo and Onakoya (2016) examined the influence of tax planning on financial performance of manufacturing firms quoted on the Nigerian Stock Exchange. Ten companies were chosen as study samples using a judgmental sampling technique, based on the premise that the selected samples represented approximately 40% of the study population, which is above the general threshold of 30% (Kawor & Kportorgbi, 2014; Ogundajo & Onakoya, 2016). The study's population consisted of twenty-eight (28) companies listed under the consumers' goods sector. The study found that Nigerian companies have not made full use of aggressive tax planning strategies such thin capitalization, tax law incentives, and other advantages of loopholes in Nigerian tax legislation. The study suggested that, given the complexity and dynamics of Nigerian tax laws, manufacturing companies in the country incorporate tax planning into their strategic financial planning, hire tax experts, and make effective use of all available tax planning strategies to further impact financial performance.

Adegbie, Akintoye and Alu (2019) examined managerial efficiency and corporate financial performance of quoted Nigerian firms. Panel regression analysis was used to examine the information gathered from the audited reports of ninety (90) companies listed on the Nigerian Stock Exchange that were selected as a sample for the years 2008 to 2017. The study's findings indicate that managerial effectiveness raises ROA, however the coefficient of determination indicates that the primary model's ability to explain changes in ROA is less strong.

Methodology

This study used the extant annual reports of listed manufacturing enterprises in Nigeria as well as other pertinent documents in a systematic disaggregated method and descriptive ex-post facto research design. This study encompasses all companies that are listed on the Nigerian Stock Exchange (NSE) floor that manufacture consumer and industrial goods as of December 31, 2020. As of that date, 39 companies were listed on the Nigerian Stock Exchange floor (Nigerian Stock Exchange Fact book, 2020).The purposive sampling method was adopted due to the availability of data, active trading, and continuous listing of the firms over the study period, and after carefully removing 10 companies with incomplete data. The study focused on 29 manufacturing companies for twelve years spanning from 2013-2020, making the total number of observations to be two hundred and thirty-two (232). That is 29 manufacturing companies multiply by eight years.

However, ordinary least square (OLS) regression techniques were used to analyze the objective of this study. Prior to the inferential statistics, Firm efficiency was ascertained, and a normality test was carried out to verify the accuracy of the data gathered using Jaque-Bera, skewness, and kurtosis. In addition, additional preliminary analysis was carried out, which included the Heteroskedacity test using the Breusch-Godfrey serial correlation, Breusch-Pagan Godfrey, and Ramsey Reset tests, and the multi-collinearity test using the variance inflation factor (VIF). These checks were performed to make sure that the multiple regression analysis's underlying assumptions are not broken by the data that was used. To determine whether the hypotheses should be accepted or rejected, the Eviews and SPSS software packages were utilized at a significance level of 5%. The model of Amrie (2018) was adapted in order to achieve the objectives of the study and it was modified as follows:

$$TaxP_{it} = \beta_0 + \beta Manab_{it} + + \beta_7 roa_{it} + \varepsilon_{it}$$

Where;

TaxP = Tax Planning Strategy proxy with Cash Effective Tax Rates (CETR);

Manab = Total managerial ability with variables definitions as stated below

β_0 = Intercept or constant of the coefficient;

$\beta_1 - \beta_7$ = Coefficient of Explanatory Variables;

Measure of Variables

Type of Variable	Variables Name	Measurement	Sources
Dependent *CETRs*	Cash Effective Tax Rate	This is Measured as tax paid divided by pre-tax book income before in period *t*, proxy for Corporate Effective Tax Planning Strategy	Amrie (2018) Ruhs & Østerås (2019)
Independent MASCORE	Managerial Ability	Managerial Ability score (Total Firm Efficiency) developed by Demerjian *et al.*, (2012)	Ruhs & Østerås (2019), Adegbie *et al.,* (2019), Compustat Global

Analysis of Result

To verify that the data collected was normal, a preliminary test was carried out before the hypothesis was tested. The correlation matrix test, the variance inflation factors (VIF) test of multi-collinearity, the Breusch-Godfrey test for serial correlation LM, the Breusch-Pagan-Godfrey serial heteroskedacity test, and the Ramsey Reset test for misspecification test are some of the preliminary tests that were conducted. For instance, the result of correlation LM using Breusch-Godfrey reveals the results of the correlation analysis as one of the basic assumptions of regression. The aforementioned result indicates that the independent and dependent variables of the study have a linear relationship. This is supported by the fact that the variable's coefficient of correlation with itself was 1.00, indicating perfect correlation. There was a positive and negative association seen in every variable. For example, Manab and TAXP (0.1145), furthermore, the Table revealed that the correlation was moderate and were within the recommended threshold of 0.8 (Aifuwa & Embele, 2019; Stundenmund, 2014). This observation led to a suspicion that the model might have problems with multicollinearity. The variance inflation factor test was carried out to look at the possibility of multicollinearity problems in the model and variables examined further.

Inferential Sta Result: Ordinary Least Square:

Variables	Predicted Sign	Model *Coefficient (t-Statistics)*	***Prob.***
Constant	Nil	0.2267 (1.6933)	0.0918
Managerial Ability	+	0.1393 (2.4889)	0.0135

Source: Author's 2020

Discussion of Findings

The study discovered that the corporate tax planning approach of Nigerian listed manufacturing companies is significantly positively impacted by management skill. This supported the claim made by agency and upper echelon theories, which hold that the knowledge, skills, and experiences of people holding important leadership positions inside an organization directly affect its outcomes (Hambrick & Mansion, 1984). The elites believe that companies are mirror images of their senior leadership (Martin, 2011). According to agency theory, managers act as the principals' (shareholders') representatives and, as such, must show more sustainability and efficiency in the business as well as better tax methods that lower the likelihood of being discovered by tax authorities.

Therefore, the effectiveness with which a corporation can manage its resources as a manager has a significant impact on how well it can carry out its operational activities. Three main explanations were offered by Koester et al. (2016) for the connection between business tax planning tactics and managerial skills. First, a manager with greater skill comprehends the surroundings of the organization better. Second, managers are viewed as "a tone at the top" when it comes to generating cost savings and accomplishing the goals of the business. Third, because tax payments were viewed as a "lost fund," they do not directly benefit the organization. Consequently, higher-ability managers may find the corporation tax planning technique to be a desirable alternative in the context of a cost-effective framework.

Conclusion and Recommendations

The study indicated that managerial ability has a considerable favorable impact on corporate tax planning approach among listed manufacturing companies in Nigeria, based on the empirical results of the hypotheses investigated in the result above. This notifies shareholders that, in the years under review, managers with higher ability levels at listed manufacturing companies in Nigeria demonstrated higher levels of management efficiency, which enhanced the performance and sustainability of the manufacturing companies through better tax planning techniques. In line with the findings of this study, which recommends that managers with greater ability are better able to implement the appropriate tax planning strategy, this study advises shareholders to prioritize the involvement of managers with higher ability, as they are better able to align companies decisions with tax strategies and spot opportunities to boost the company's value and sustain its sustainability.

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