

# **CORPORATE GOVERNANCE CHARACTERISTICS DETERMINANTS OF TAX AVOIDANCE**

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**CHAPTER ONE**

**INTRODUCTION**

## **1.1 Background to the Study**

The issues of tax avoidance have been problems since the inception of tax legislations and are prevalent in every society where taxes are levied (Andreoni, Erard & Feinstein, 1998; Uadiale, Fagbemi & Ogunleye, 2010; Verboon & Dijke, 2007). This menace is even more prevalent

among corporate taxpayers given the magnitude of the company income taxes. The fact that taxes take away greater proportion of the firms' pre-tax earnings and subsequently reduce their distributable profits could be a reason for the endless war against corporate tax avoidance. While there are several anti-avoidance laws in almost every country, corporations around the world do employ expensive accountants to find increasing complicated ways of paying less taxes (Daily Mail, 2010). As such, Hundal (2011) argued that corporate tax avoidance seems to be the most challenging issue of our generation as it represents a serious loss of revenue to the governments of many developed and developing economies. Several studies have therefore been conducted to understand the determinants of tax avoidance among corporate taxpayers. These studies have examined several factors such as firm size and scale of international operations (Rego, 2003; Richardson & Lanis, 2007; Zimmerman, 1983), capital intensity, leverage (Noor, Mastuki & Bardai, 2008; Richardson & Lanis, 2007; Stickney & McGee, 1982), executives' roles and their compensations, industrial membership (Mahenthiran & Kasipillai, 2012; Shevlin & Porter, 1992), the legal form of organization (Tedds, 2006) and political connections (Adhikari, Derashid & Zhang, 2006) to understand the variations in firms' tax burdens across industry. However, the studies assume that firms make their tax reporting decisions with no agency consideration and influence from the board (i.e. given consideration to organizational legitimacy). They, therefore, provide little insight to the determinants of tax avoidance in a corporate setting where there is a segregation of ownership from control and legitimacy issues. Given this backdrop, Shackelford and Shevlin (2001) called for the investigation of ownership structure as likely determinant of corporate tax avoidance given its importance in the corporate setting. Afterward, Chen, Chen, Cheng and Shevlin (2010) and Landry, Deslandes, and Fortin (2013) documented negative relationships between family ownership and corporate tax

avoidance in US and Canada respectively. Also, government ownership has been established to be related to tax avoidance in varying directions (Adhikari et al., 2006; Chen, Mo and Zhou, 2013; Kim & Zhang, 2013; Law, Yuan, McIver & Burrow, 2012; Mahenthiran & Kasipilai, 2012; Wu, Rui & Wu, 2013; Zhang & Han, 2008). Similarly, Demirguc-Kunt & Huizinga (2001); Egger, Eggert & Winner (2010); Kinney and Lawrence (2000) and Law et al., (2012) have documented consistently positive relationship between foreign ownership and tax avoidance. On the other hand, various attributes of the board have been documented to impact corporate tax avoidance. For instance, Minnick and Noga (2010) found a negative significant relationship between board composition and corporate tax avoidance among S&P 500 firms. A similar negative relationship between the two variables was documented by Lanis and Richardson (2011) among Australian companies. Also, Vafeas (2010) found a negative relationship between board composition and corporate tax avoidance among Fortune 500 companies. However, Mahenthiran and Kasipilai (2012) found a significant negative but partial relationship between the two variables among Malaysian listed companies. These findings suggest the mitigating effect of the board on company's tax avoidance activities. While the studies so far have investigated the relationship between corporate tax avoidance and these various forms of corporate ownership, the joint effect of the three forms of ownership has not been investigated. It is a known fact that these forms of corporate ownership do overlap in the corporate environment given the public nature of these companies. It will therefore be worthwhile to investigate the joint effect of these forms of corporate ownership on corporate tax avoidance to better our understanding of the latter. In addition, the documented negative impact of board composition a measure of board independence on corporate tax avoidance suggests the potential intervening role of corporate governance on the relationship of corporate tax avoidance

with these forms of corporate ownership. Thus, investigating the interactive effect of corporate governance on such relationship will further enhance our understanding on the behaviours of the corporate taxpayers. Thus, this study is unique in proposing econometric models for investigating the joint effect of the three forms of corporate ownership on corporate tax avoidance with corporate governance's interaction.

## **1.2 Statement of Problem**

Extant literatures on corporate governance and characteristics and tax avoidance has yielded mix result. Hundal (2011) found that there is no significant association between effective corporate tax rates (ETRs), a measure of tax avoidance, and actual future tax payments. They questioned whether the effective corporate tax rate at a low level properly reflects the tax avoidance that entails risk. Dyreng (2019) provided that some firms can maintain high levels of tax avoidance (low effective corporate tax rates) for long periods. Additionally, Guenther (2018) showed that the relatively low effective corporate tax rate is more sustainable than the relatively high effective corporate tax rate. In addition, they presented evidence that there is no significant association between the effective corporate tax rate, a measure of tax avoidance, and the volatility of the effective corporate tax rate, which is a measure of tax risk. Corporate tax avoidance increases the possibility of incurring higher tax costs due to tax investigations and penalties from tax authorities in the future. It has also been discovered that companies lower their tax costs by avoiding them in a temporary way that cannot be used continuously in the future. Since such a temporary tax avoidance strategy cannot be maintained continuously, such tax avoidance entails more risk for companies. It is on this back drop that this research work seek to examine corporate governance characteristics, determinants of tax avoidance.

## **1.3 Research Questions**

The following research questions are raised to aid the study;

- i. What is the relationship between board size and tax avoidance in Nigeria quoted firms?
- ii. What is the relationship board gender diversity and tax avoidance in Nigeria quoted firms?
- iii. To what extent does board meeting affect tax avoidance in Nigeria quoted firms?

#### **1.4 Objectives of the Study.**

The broad objective is to examine corporate governance characteristics, determinants of tax avoidance. However, the specific objectives are to;

- i. Determine the relationship between board size and tax avoidance in Nigeria quoted conglomerates.
- ii. Ascertain the relationship between board gender diversity and tax avoidance in Nigeria quoted conglomerates.
- iii. To examine the extent to which board meeting affect tax avoidance in Nigeria quoted conglomerates.

#### **1.5 Statement of Hypothesis**

To proffer useful answer to the research questions and realize the study objectives, the following hypothesis stated in their null form will be tested.

##### **Hypothesis 1**

Board size has no significant relationship with tax avoidance in Nigeria quoted firms.

##### **Hypothesis 2**

Board gender diversity has no significant relationship with tax avoidance in Nigeria quoted firms.

### **Hypothesis 3**

Board meeting does not significantly affect tax avoidance in Nigeria quoted firms.

#### **1.6 Significance of the Study**

The study aims at equipping financial managers with applied knowledge for determining characteristics that affect some Nigeria listed firms' performance as a result of their financial control, planning and decision making. The study will also add to the body of knowledge in the finance discipline and form an foundation for other similar research work.

This study will serve as a source of reference in the future for academicians and scholars. The financial advisors can use the findings of the study to advice their clients on which companies to invest in other to meet their expectation.

#### **1.7 Scope of the Study**

This study examines corporate governance characteristics, determinants of tax avoidance.. The time frame will be six years i.e. from 2016 to 2020. The choice of five years i.e. from 2016 to 2020 period is premised on the availability of data and as a matter of interest to the researcher. The study is restricted to the listed conglomeration in Nigeria

#### **1.8 Limitation of the study**

The study certainly suffers from a number of limitations prominent among which include;

- i. One of the limitation of this study is the time frame to which the research work covers, the research covers a period of five years from 2016 to 2020 which is however too small to guarantee the reliability of the research.

- ii. Another limitation of the limitations of the study is that the research focuses on manufacturing firms which do not totally represent all companies listed in the Nigeria Exchange Group, extending this research to other sector of the economy would have improved the reliability of the research.
- iii. The depth to which information could have be gathered is limited for instance, it is inherit in human nature that some times what is being said is quite different from what is being done.
- iv. Sizable quality of information obtain from papers were in fragmentations and sometimes complex.

## **CHAPTER TWO**

### **REVIEW OF RELATED LITERATURE**

#### **2.1 Conceptual Framework**

##### **2.1.1 Corporate Governance**

Several authors have defined corporate governance from diverse perspectives; According to Yusoff (2018) this expropriation 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 account-ability (Effiong, 2018).

Corporate governance is the mechanisms aim at ensuring the fulfillment of corporate objectives Solomon (2004) stated that corporate governance is the process that allows directors and auditors to assume their obligations towards share-holders and company stakeholders”. 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” 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 firms management, shareholders and stakeholders”. Corporate governance is the system by which companies are directed and controlled (Ogbu, 2019): The Organization for Economic Co-operation and Development outlined five principles of corporate governance to include:

- i. The rights of shareholders
- ii. Equitable treatment of shareholders
- iii. The role of stakeholders
- iv. Disclosure and transparency
- v. The responsibility of the board.

Broadly, corporate governance mechanisms are sub-divided 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 (Hilton, 2017). Internal governance mechanisms include such as the board of directors, manager's compensation, audit committee, remuneration committee, and ownership structure, among others. The internal governance mechanisms are mainly associated with the structure, composition and, characteristics of the board of directors. The study by Jameson (2019) found a relationship between improved corporate governance and firm performance.

### **2.1.2 Board Size**

From the agency problem perspective, large boards are not recommended while small boards are preferred to improve performance (Lipton & Lorsch, 1992, Yermack, 1996). In these terms, Kim and Nofsinger (2007) argued that small boards are better than large ones as they avoid the free-rider problem that might appear among board members, meaning each board member may feel inclined to exert more effort than she/ he would have otherwise. The contrary view to the agency and resource-based perspective is that larger boards are associated with diversity in skills, business contact and experience (Haniffa & Hudaib, 2016). Similarly, larger boards secure access to critical resources such as finance and raw materials (Goodstein 1994). Regarding the board of directors size performance relationship, one of the main reliable empirical association is that board size is associated negatively with the performance of the firm (Hermalin & Weisback, (2003). Statistically, it has been found by Yermack (1996) that there is a significant negative association between the performance of an organization and the board size as calculated by

Tobin's Q by taking a sample of 452 huge U.S industrial companies for the period from 1984 to 1991. In the same research, it has also been have highly favorable standards for financial ratios.

### **2.1.3 Gender Diversity**

Gender diversity is part of the broader concept of board diversity (Milliken & Martins, 1996). The concept of board diversity suggests that boards should reflect the structure of the society and appropriately represent the gender, ethnicity and professional backgrounds. Boards are concerned with having right composition to provide diverse perspectives (Milliken & Martins, 1996; Biggins, 1999). Board diversity is supported on the ground of moral obligation to shareholders (Carver, 2002), stakeholders (Keasey, Thompson & Wright, 1997), corporate philanthropy (Coffey & Wong, 1998) and for commercial reasons (Mattis, 2000; Daily & Dalton, 2003). However, diversity should not only ensure equitable representation but also provide for an expression of broadening the principle of merit (Burton, 1991). Robinson and Dechant (1997) postulate that diversity promotes a better understanding of market place, increases creativity, produces more effective problem-solving and leadership and promotes effective global relationships.

Gender diversity in the boards is also supported by different theoretical perspectives. For example, agency theory is mainly concerned about independence of directors and a balance between executive and non-executive directors on boards. Representation from diverse groups will provide a balanced board so that no individual or small group of individuals can dominate the decision-making of the board (Hampel, 1998). Further, diversity also provides representation for different stakeholders of the firm for equity and fairness (Keasey et al., 1997). From resource dependency perspective, the board is a strategic resource, which provides a linkage to various

external resources (Ingley & Walt, 2001). This is facilitated by board diversity. Many scholars now believe that an increase in board diversity leads to better boards and governance on the ground that diversity allows boards to tap on broader talent pools for the role of directors (Pearce & Zahra, 1991; Burke, 1997; Daily, Certo & Dalton, 1999; Singh & Vinicombe, 2004).

#### **2.1.4 Board Meeting**

Board activity and meeting are key indicators for the effectiveness of the board of directors (Vafeas, 1999; Conger et al., 1998; Lipton & Lorsch, 1992). Even though the time devoted differs from one firm to another, Vafeas (1999) determines the different costs and benefits of board activity as measured by meetings. There are several costs that are associated with board meetings including managerial time, travel expenses, and directors' meeting fees. At the same time, there are other benefits pertinent to the board meeting such as more time for directors to confer, set strategy, and monitor management. Thus, devoting enough time is crucial to ensure that the benefits of regular board meeting outweigh its costs. However, there is continued emphasis on the utilisation of the time inside the board room (Conger et al., 1998). This is because optimising board meetings is critical to deliberate on outstanding issues thereby leading to better monitoring and performance (Carcello et al., 2002). Moreover, Lipton and Lorsch (1992) opine that by stating the frequency and duration of meetings contributes to their success and enhances board oversight activities. This is because having the appropriate and adequate team represents board diligence in carrying out its activities thereby accentuating its effectiveness. Empirically, Vafeas (1999) found that board meetings are statistically and significantly associated with the performance of the firms. On the other hand, Mangena and Taurigana (2008) showed positive association between activities of the board and firm performance. El Mehdi (2007) found that

board activities do not have a necessarily positive relation to firm performance. Overall, although the prior research is conflicting with regards to the impact of board meetings on performance, the majority of works tend to conclude that they do enhance the performance of firms. This is predominantly due to the fact that the performance of the boards relies on how they carry out their activities, which can be indicated by regular meetings. Therefore, in line with agency problem, we expect that more meetings are a signal of more discussion of the companies' operations. As such we propose:

### **2.1.5 Corporate Tax Avoidance**

Corporate tax avoidance (CTA) has no specific accepted definition in the literatures. This lack of universal definition follows the consequential tax effect of every business transaction aimed at increasing profit (Kadiri, 2018). According to (Martinez, 2017) 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, 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 Franca, (215) defined CTA as a strategy in reducing corporate tax liabilities. Chen (2017) opine that CTA refers to as a means of minimizing the company's tax accounting income. Saheed, (2018) sees tax avoidance as a strategy to reduce taxable income (e.g., tax shelters) at the other end. Derrick (2019) 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. Hilton (2017) 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. He 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 (Johnson, 2016). The benefits to the firm include such as higher cash flows and net income; while, to the shareholders, it implies higher residual income. The costs include negative consequences such as large penalties, negative publicity, political costs, or the firm labelled as a “poor corporate citizen”. Three conditions must exist for an individual or firm to engage in tax avoidance; incentive, access, and awareness. 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.

Obid (2014) 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. Raut (2018) identified the use of transfer pricing, royalty programs, off shore tax havens and structured transactions. Silva (2017) identified other methods such as debt allocation as well as sourcing rules for foreign tax credits.

### **2.1.6 Tax Avoidance**

Studies on the association between tax avoidance and tax risk mainly suggest that investment in tax avoidance increases corporate tax risk. Dyreng (2015) stated that tax avoidance is anything that reduces the firm’s taxes relative to its pre-tax income. Additionally, Hanlon and Heitzman (2018) stated that tax avoidance is thought of as a continuum of activities to reduce tax liability. It is difficult to maintain the tax avoidance strategy currently implemented by corporations in the

future. In addition, it shows that the low tax rate due to tax avoidance will be reversed to a high tax rate in the future because it is a temporary investment that invests in tax cost reduction, which is one of several investment alternatives that involve risk.

Hasan (2019) suggested that there is a significant positive association between the level of corporate tax avoidance and the corporate bank loan spread. Shevlin (2017) provided evidence that there is a significant negative association between the effective corporate tax rate and the cost of debt. Existing studies related to tax avoidance mainly analyzed the association between tax avoidance and corporate characteristics or the association between tax avoidance and tax risk. Kang and Ko (2017) stated that there is a significant negative relation between tax avoidance and corporate value by examining the role of corporate governance. In addition, Kang (2019) tested the effect of tax avoidance and tax risk according to a company's tax strategy on the cost of embedded capital. They provided that, for groups with high levels of tax avoidance, the cost of capital increases when the level of tax avoidance increases, and for groups with low levels of tax avoidance, the cost of capital decreases when the level of tax avoidance increases. Kim (2018) tested the effect of tax avoidance on the association between company reputation and the implied cost of capital in Korean companies from 2003 to 2016. Kim (2017) reported that a significant negative association between company reputation and implied cost of capital is not found in a group that was aggressive in tax avoidance

As described above, existing studies mainly suggest that investment in tax avoidance increases the tax risk of companies. Existing studies provide three main reasons why tax avoidance increases corporate tax risk. First, the reason is that the low tax rate due to corporate tax evasion increases the possibility of a tax investigation from the tax authorities and the possibility of paying higher tax expenses due to tax investigations and penalties from the tax authorities in the

future increases. In other words, the reduction of tax expenses due to tax avoidance entails additional corporate risk. Existing studies suggest the second reason is that corporations lower tax costs by avoiding taxes in a temporary way that can no longer be used in the future (Guenther, Matsunaga & Williams, 2019). Since the tax rate lowered by this tax strategy cannot be maintained continuously in the future, such tax avoidance entails more risk from the company's point of view. Third, existing studies argue that tax avoidance increases tax risk because a firm's low tax rate indicates that the firm is investing in a high-risk investment alternative. Finally, tax avoidance can incur agency costs and reduce corporate transparency, which can also bring uncertainty to a company's future cash flows.

Furthermore, Guenther (2019) presented the volatility of effective corporate tax rates as a measure of corporate risk and verified the association between tax strategy and corporate risk. However, Guenther (2019) found no evidence that, contrary to expectations, there is a significant association between corporate tax avoidance and corporate risk.

Dyreng (2014) argued that low effective corporate tax rates are not related to corporate risk because low effective corporate tax rates indicate the company's ability to invest in tax-preferred investments, such as municipal funds, that are free from IRS restrictions or legal problems. In other words, it is the concept that the current low effective corporate tax rate due to the corporate tax avoidance strategy will not be reversed to a higher tax rate in the future, nor will it increase the uncertainty of the actual future tax amount. In other words, companies can establish a sustainable tax avoidance strategy according to their environment or characteristics. They argue that, for this reason, a low effective corporate tax rate does not represent a risky investment, nor does it increase uncertainty about an entity's future cash flows. This study analyzed whether there is an association between the effective corporate tax rate, a measure of tax avoidance, and

the volatility of the effective corporate tax rate, which is a measure of tax risk, for Korean companies as well.

### **2.1.7 Non-debt Tax Shields**

The effective tax rate has been used as a possible determinant of the capital structure choice. According to Modigliani and Miller (1958), if interest payments on debt are tax-deductible, firms with positive taxable income have an incentive to issue more debt. That is, the main incentive for borrowing is to take advantage of interest tax shields. Accordingly, in the framework of the trade-off theory, one hypothesizes a negative relationship between leverage and non-debt tax shields. DeAngelo and Masulis (1980) argue that the marginal corporate savings from an additional unit of debt decreases with increasing non-debt tax shields. This is because of the likelihood of bankruptcy increases with leverage. The empirical evidence is mixed. According to Graham (2000), the tax shield accounts on average to 4.3% of the firm value when both corporate and personal taxes are considered. In this study, dividend is included as a supplementary indicator of firm liquidity.

## **2.2 Theoretical Framework**

### **2.2.1 The Hoffman's Tax Planning Theory**

This theory was propounded by Hoffmann in 1961. According to Hoffmann (1961) taxation, mostly are based on business or accounting concepts, thus a firm can modify such activities towards the attainment of reduction in tax liability. Hoffmann identified some ambiguity and loopholes in tax laws due to unclear intentions of the legislators and concluded that successful tax schemes work with the legal concepts and precise wording of the statute and

complying with these concepts very precisely as it relates to individual firm tends to be advantageous to firms in form of tax savings.

Tax planning activity theories introduce concepts and principles that are typically applicable to tax practitioners. Tax planning could not be continued for long except if the activities of tax planning are “flexible”, meaning of a continuity of the strategies (Hoffman, 1961). This is particularly applicable to the cases of tax planning strategies that depend on tax regulation ambiguities and loopholes. Thus, tax planning strategies must be time-oriented and proportionate in the logic that “consistency requires that the past limit the present and the future but the present must be further circumscribed in the light of the taxpayer’s future requirements” (Hoffman, 1961).

### **2.2.2 The Agency Theory**

This theory was propounded by Steven Ross and Barry Mitnick (1970). The agency view of tax avoidance on the other hand emphasized on the inability of the tax savings through tax planning strategies to transform into enhancement of after tax return due to agency problem of managerial opportunism or resource diversion. Desai and Dharmapala (2017) opined that complex tax avoidance transactions can provide management with the tools, masks, and justifications for opportunistic managerial behaviours, such as earnings manipulations, related party transactions, and other resource-diverting activities thus, tax savings may not actually result to increase on firms’ after tax rate of return. Salamon and Siegfried (1977) asserted that larger firms have economic and political power advantage over the small firms. Larger firms effectively utilizes their economic and political power to lessen their tax liability being able to engage in aggressive tax planning due to their broad resources and also, he’s of the opinion that large firms are opportunistic in manipulating the political principles for the enhancement their

after tax returns. These theories are relevant to this study, a firm which maximizes the loopholes in the corporate tax laws and which maintain an optimal gearing thus having tax shield on the deductible interest tends to lessen its tax burden and increases its after tax returns (Hoffman's theory). From the agency point of view, a firm might utilized all the strategies in reducing its tax burden but the savings not transformed into corporate financial benefit due to agency problem. The agency view theory is of the assertion that managers with their personal interest in conflict with the global interest of the entity might divert such savings to other investment for personal gains.

### **2.2.3 The Political Cost Theory**

Lastly, the political cost theory was propounded by Zimmerman (1978). The theory holds that larger firms tends to be more matured and possesses expansive resources thus have the capacity of engaging professionals in the formulations and implementations of their corporate strategies with tax liability inclusive.

Tran and Yu (2018) suggest that large firms can afford better tax planning activities and are better able to 'influence political processes in their favour'. Richardson and Lanis (2018) are predisposed to the latter view pointing to a 'political power hypothesis' that they attribute to Siegfried (2019) an unpublished PhD thesis. Within a US context, Salamon and Siegfried (1977) explore this notion further, conceding the point that few would deny that 'big business' has resources to influence government but that it is not clear how successful big business is in pursuing its agenda at a policy level. They appear to find a large effect – a one per cent increase in size leads to a 0.08 per cent increase in the book tax income gap (they use the term tax-avoidance rate) (Salamon & Siegfried ,1977). Results such as that would suggest that government could increase corporate tax revenue by closing the so-called book-tax income gap.

Of course, if the result is simply driven by larger companies having better tax planning resources, then closing the book-tax income gap may not lead to an increase in revenue.

By contrast, Zimmerman (2018) suggests a ‘political cost hypothesis’ to explain a positive relationship between size and effective tax rates. His argument being that larger firms would be subject to greater scrutiny from the taxation authorities leading to higher effective rates of taxation. It is important to be clear what Zimmerman is arguing. He is not suggesting a monotonic relationship between size and effective tax rates – he is clear that the positive relationship exists only for the very largest companies. His other result contrary to much of the literature is that measures of effective tax rates calculated from financial accounting data are similar to estimates of effective tax rates calculated from US Internal Revenue Service data. He finds that financial statement data provide unbiased estimates of effective tax rates (Zimmerman,2018).

Based on these theories, effective tax rate (ETR), tax savings (TS) and firm’s size (SIZE) are selected as the explanatory variables for the study.

## **2.3 Empirical Review**

### **2.3.1 Board Size and Tax Avoidance**

This is considered to be a crucial characteristic of the board structure. Large board could provide the diversity that would help companies to secure critical resource and reduce environment uncertainties. (Pfeiffer, 1987, Pearce & Zahra, 1992, Goodstein, 1994). But, as Yermack (1996) said, coordination, communication and decision making problem increasingly impede company performance when the number of director increase. Thus as an extra member is included in the

board, a potential trade-off exist between diversity and coordination. Jensen (1993) appears to support Lipton and Lorsch (1992) who recommend a number of board members between seven and eight. However, board size recommendation tends to be industry- specific, since Adam and Mehran (2003) indicate that bank holding companies have board size significantly larger than those of manufacturing firms.

A review of the empirical evidence on the impact of board size on tax avoidance shows mixed results. Deheane (2018) find that board size is positively related to tax avoidance. However, the results of Haniffa (2016) are inconclusive. Using a market return measure of performance, their result suggest that a large board is seen as less effective in monitoring performance, but when accounting returns are used, large boards seems to provide the firms with the diversity in contacts, experience and expertise needed to enhance performance. Yermack (1996) finds an inverse relationship between board size and tax avoidance. In addition, financial ratios related to profitability and operating efficiency also appear to decline as board size grows. Finally, Connelly and Limpaphayom (2004) find that board size does not have any relation with tax avoidance

According to Robinson, Sikes and Weaver (2020), when the tax department of a firm is treated as a profit centre, it will pay lesser amount of taxes. This therefore means that tax managers are compensated for tax avoidance. In a study done by Ayers, Laplante and Schwab (2017) titled “Does Tax Deferral Enhance Firm Value? It was observed that tax deferral (tax savings) is positively related with future performance of a firm.

In a study done by Kawor and Kportorgbi (2014) on the Effect of Tax Planning and tax avoidance on Firm Performance: Evidence from Listed Firms in Ghana, the authors used 22 non-financial

companies listed on the Ghana Stock Exchange over a twelve year period from 2000. They used the longitudinal correlative design. It was observed that, the effect of tax planning savings on firm's performance is germane for all stakeholders in the evolving security markets like the Ghana Stock Exchange. Also, it was established that, each possible relationship has a special impact on the players. A positive relationship means a win-win situation for the management as well as for the shareholders (Kawor & Kportorgbi, 2017). A negative relationship between tax planning savings, tax avoidance and firm performance (firm value) exist when tax planning benefits (tax savings) goes into the pockets of managers. This negative relationship could be as a result of the existence on agency problem, where managers would pursue tax planning for their personal gains at the expense of the shareholders' welfare (Kawor & Kportorgbi, 2017).

### **2.3.2 Gender Diversity and Tax Avoidance**

Liu, Wei, and Xie (2014), by utilizing a panel of more than 2,000 Chinese recorded organizations from 1999 to 2011, found that gender diversity affects organization performance thus have an impact on tax avoidance. Specifically, male officials show more grounded positive impact on organization value than female free executives. Hence, they presumed that the requirement for ladies on corporation boards is something other than for the checking part. Moreover, they found that boards with at least three female executives show more grounded positive effect on organization value than those with two or less female directors. This finding was like the investigation of Reguera-Alvarado et al. (2015); they found that an expansion in the number ladies on the board decidedly influenced the firm value of 125 publicly quoted organizations on the Madrid Stock Exchange over the time of 2005 to 2009.

Ekadah and Josphat (2010), Considered gender diversity and tax avoidance. The reason for the paper was to examine the impact of board gender diversity on tax avoidance in Kenyan banks for the period 1998-2009. Stepwise regression analysis was utilized to break down the impact of board diversity on tax avoidance. It was discovered that boards of business banks in Kenya are male-ruled. By and large, out of a common board size of 8 individuals, just 1 is a female chief. At long last, this investigation finds that board diversity has no impact on tax avoidance in Kenya.

European-based researchers' confirmation on gender diversity, tax avoidance and firm performance gives off an impression of being blended. Rose (2007) utilized a specimen of Danish firms recorded on the Copenhagen Stock Exchange amid 1998-2001, and found that female board portrayal had no effect on firm performance. Smith et al. (2006) in a board information investigation of 2,500 of the greatest Danish firms found that the offer of ladies among top administrators and on boards of directors had a tendency to have an altogether beneficial outcome on firm performance, controlling for firm attributes, and in addition for the heading of causality. Besides, their outcomes uncovered that the Positive performance impacts were for the most part represented by female administrators with university intuition, and were likewise identified with female board individuals chosen by the staff. Randoy, Thomsen and Oxelheim (2006) explored the impact of board diversity on corporation value, analyzing an example of the biggest organizations from Denmark, Norway and Sweden, and found no huge gender diversity impact. Bohren and Strom (2007), considering a specimen of Norwegian recorded non-financial firms, appear to be the main analysts who found an altogether negative relationship between board gender diversity and firm value.

### **2.3.2 Board Meeting and Tax Avoidance**

According to Jaiswal and Banerjee (2012) more number of meetings would facilitate more vigilant monitoring by the board in a company's affairs and thus would be associated with better firm's performance and thus reduce earnings management.

Kinjo (2018) states that the greater the number of meetings, the more effective the board monitoring function. Companies that have fewer board meetings than necessary, have their firms' value decreased. Hills (2015) finds evidence that board of directors that meet frequently are more likely to reduce the level of tax. Previous studies show that a board that meets frequently is likely to monitor the board activities in order to reduce tax more effectively (Xie, et al. 2015; Vafeas 2018). Zhou and Chen (2004) suggest that board activity is an important dimension of board operation and effective board should meet regularly to stay on top of accounting and control related matters. Hence, board meetings among others are an important mechanism of corporate governance.

Quite a number of researchers have conducted a study on corporate governance and tax avoidance; the study of Nwoje, (2018) 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.

Gabi and Dabor (2019) 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 2018. 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. Ogundele and Alabi (2017), 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. Fakorede (2016), 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. Enoma (2017), investigated corporate tax avoidance 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

## **2.4 Summary of the Review**

The issues of tax avoidance have been problems since the inception of tax legislations and are prevalent in every society where taxes are levied (Andreoni, Erard & Feinstein, 1998; Uadiale, Fagbemi & Ogunleye, 2010; Verboon & Dijke, 2007). This menace is even more prevalent

among corporate taxpayers given the magnitude of the company income taxes. The fact that taxes take away greater proportion of the firms' pre-tax earnings and subsequently reduce their distributable profits could be a reason for the endless war against corporate tax avoidance. While there are several anti-avoidance laws in almost every country, corporations around the world do employ expensive accountants to find increasing complicated ways of paying less taxes (Daily Mail, 2010). As such, Hundal (2011) argued that corporate tax avoidance seems to be the most challenging issue of our generation as it represents a serious loss of revenue to the governments of many developed and developing economies. Several studies have therefore been conducted to understand the determinants of tax avoidance among corporate taxpayers. These studies have examined several factors such as firm size and scale of international operations (Rego, 2003; Richardson & Lanis, 2007; Zimmerman, 1983), capital intensity, leverage (Noor, Mastuki & Bardai, 2008; Richardson & Lanis, 2007; Stickney & McGee, 1982), executives' roles and their compensations, industrial membership (Mahenthiran & Kasipillai, 2012; Shevlin & Porter, 1992), the legal form of organization (Tedds, 2006) and political connections (Adhikari, Derashid & Zhang, 2006) to understand the variations in firms' tax burdens across industry. However, the studies assume that firms make their tax reporting decisions with no agency consideration and influence from the board (i.e. given consideration to organizational legitimacy).

## **CHAPTER THREE**

### **RESEARCH METHODOLOGY**

#### **3.1 Research Design**

The correlational research design is adopted for this study based on positivist approach. A correlation research design is used to describe the statistical relationship between two or more variables. It is most appropriate for this study because it allows for testing of expected relationships between audit quality proxies and earnings management practices of listed conglomerates in Nigeria and the making of predictions regarding such relationships.

#### **3.2 Population of the Study**

The population of the research comprises of all the conglomerates listed on the Nigerian Exchange Group (NGX) as at 31st December, 2021.

#### **3.3 Sample and Sampling Technique**

The sample size for the study is 10 quoted conglomerates firms in the Nigeria Exchange Group. A two point filter was used to arrive at the sample of the study. Firstly, the company must be listed on the NSE and have the required data for the study period of 2016 - 2020. Year 2016 was chosen as the beginning of the study period because the economic meltdown that rocked the world during this time (Nigeria inclusive) provided opportunity for Nigerian companies to manipulate reported earnings to present impressive performance (Bello & Yero, 2020). Similarly, year 2021 was chosen as the end of the study period to ensure the availability of published financial statements for the sampled companies.

#### **3.4 Sources of Data Collection**

The data for this study were obtained from secondary source. Secondary data were extracted from the published annual reports and accounts of the companies and the NSG fact book

for the relevant years.

### 3.5 Method of Data Analysis

The study adopted the Ordinary Least Square (OLS) multiple regression technique. Descriptive statistics was used to compute summary statistics for both the dependent and independent variables of the study. The use of descriptive statistics is important because it summarizes and enhances understanding of the data collected for analysis in a study. Before using multiple regression analysis to analyze the data for the study some robustness tests were carried out to enhance the reliability of findings.

### 3.6 Model Specification

. The model is expressed as follows:

$$\text{NDTS}_{it} = \beta_0 + \beta_1 \text{BSIZ}_{it} + \beta_2 \text{BGDV}_{it} + \beta_3 \text{BDMT}_{it} + \varepsilon_{it} \text{-----} \mathbf{3.1}$$

Where:

NDTS = Non Debt Tax Shield (A proxy for tax Avoidance)

BSIZ = Board Size

BGDV = Board Gender Diversity

BDMT = Board Meeting

$\beta_0$  = constant of the model

$\beta_1 - \beta_6$  = coefficients of the study  
model  $\varepsilon$  = error term

## CHAPTER FOUR

### DATA PRESENTATION, ANALYSIS AND DISCUSSION OF FINDINGS

#### 4.1 Presentation and Analysis of Data

Table 4.1 presents the summary of the descriptive statistics for the dependent and independent variables for fifty (50) observations. It shows that tax avoidance has a mean value of about 3.9086 and a standard deviation of about 2.9708. The maximum value of the variable is 12.3054 while the minimum is 0.4251. The maximum values for all other variables are 12,15 and 10 while the minimum for all the variables are 1.

For tax avoidance in Nigerian quoted firms, mean value was 0.7878 and standard deviation of 0.4091. The corresponding values for the others are: board size, 7.86 and 1.8071 respectively; board meeting, 4.82 and 1.9240 respectively. The p-values of the skewness and kurtosis statistics show that nearly in all the cases the data are judged to be normally distributed at 5% level of significance.

**Table 4.1 Descriptive Statistics**

| Variable    | Obs | Mean    | Std. Dev. | Min   | Max     | Pr(Kurtosis) | Pr(Skewness) | Prob>chi2 |
|-------------|-----|---------|-----------|-------|---------|--------------|--------------|-----------|
| <b>BDSZ</b> | 50  | 7.86    | 1.807129  | 5     | 12      | 0.0293       | 0.3842       | 0.0700    |
| <b>BDMT</b> | 50  | 4.82    | 1.923963  | 2     | 15      | 0.0000       | 0.0000       | 0.0000    |
| <b>BDDV</b> | 50  | 1.02    | 2.453569  | 0     | 10      | 0.0000       | 0.0000       | 0.0000    |
| <b>TXAV</b> | 50  | 3.90863 | 2.970799  | .4251 | 12.3054 | 0.3217       | 0.0036       | 0.0165    |

Source: Researcher's Computation Using STATA

**Table 4.2 : Correlation Matrix**

|             | <b>BDSZ</b> | <b>BDMT</b> | <b>BDDV</b> | <b>TXAV</b> |
|-------------|-------------|-------------|-------------|-------------|
| <b>BDSZ</b> | 1.0000      |             |             |             |
| <b>BDMT</b> | 0.3389      | 1.0000      |             |             |
| <b>BDDV</b> | 0.4195      | 0.0051      | 1.0000      |             |
| <b>TXAV</b> | 0.0364      | -0.3013     | 0.0152      | 1.0000      |

Source: Researcher's Computation Using STATA

Table 4.2 shows that there are mixed correlations between the various variables used in the study. The table shows negative correlation between tax avoidance and board gender diversity while tax avoidance and the other variables are positively correlated. The table shows that no two of the explanatory variables are perfectly correlated or nearly so. Thus, the problem of multicollinearity is absent in this model.

## **4.2 Testing of Hypothesis**

### ***Test Statistic***

The statistical tool used in testing the stated hypotheses is the regression test procedure which uses the individual significance test (t-test) and the overall significance test (chi-squared-test). The goodness of fit of the model is tested using the coefficient of determination. The estimation of these statistics is done using the STATA computer software.

### ***Significance Level***

The level of significance adopted in this study in testing the stated hypotheses of this study is 5%. This level is usually considered adequate for studies in management and other behavioural sciences.

### ***Decision Rule***

The critical p-value used in these tests is 0.05. Thus, the researcher accepts a given alternative hypothesis as being accepted if calculated p-value is less than or equal to 0.05, otherwise the researcher accepts the null hypothesis that there is no significant effect.

| <b>Variable</b>           | <b>OLS<br/>Regression</b> | <b>ROBUST<br/>Regression</b> |
|---------------------------|---------------------------|------------------------------|
| <b>BDSZ</b>               | .3043(0.260)              | -0.10296(0.684)              |
| <b>BDMT</b>               | -.5668(0.010)             | -0.33433(0.005)              |
| <b>BDDV</b>               | -.0733(0.692)             | 0.14869(0.00)                |
| _cons                     | 4.298(0.035)              | 1.8365(0.004)                |
| F-Stat                    | 2.00(0.0070)              | 1.37(0.0026)                 |
| N                         | 50                        | 50                           |
| <b>VIF</b>                | 1.27                      |                              |
| <b>Heteroscedasticity</b> | 4.01(0.0451)              |                              |
| <b>R-Squared</b>          | 0.1154                    |                              |
| <b>Adj R-Squared</b>      | 0.0577                    |                              |

Table 4.3 shows that the explanatory variable does not account for much of the systematic variations in the dependent variable.

The VIF test (1.27) shows that there is the absence on multi-colinearity and so there is no need to drop any variable. Also, the heteroscedasticity is 4.01 with p-value of 0.0451, showing that there is a significant heteroscedasticity problem and thus necessitating a robust regression.

The table shows very moderate value of R-squared of 0.1154. This small value of the R-squared statistic suggests that there are many other variables in explaining changes in the dependent variable. For the model, the p-value of the F statistic (0.0026) shows that the model overall is suitable for estimating the stated model.

### ***Hypothesis 1***

**H<sub>0</sub>:** Board size has no significant effect on tax avoidance in Nigerian quoted firms.

**H<sub>1</sub>:** Board size has a significant effect on tax avoidance in Nigerian quoted firms

### *Computation*

The test statistic is computed by STATA software and the results are as shown in Table 4.3.

**Table 4.3: Regression Results on Board Size and Tax Avoidance**

| Variable | Coefficient | p-value |
|----------|-------------|---------|
| BDSZ     | -0.10297    | 0.684   |

Source: Extracted from STATA Computations

### *Decision*

With a coefficient of -0.10297 the results indicate that board size negatively impacts tax avoidance, while the probability value of 0.689 indicates that the positive impact is not significant. This leads to the rejection of the alternate hypothesis, thus acceptance of the null hypothesis that board size has no significant impact on tax avoidance in Nigerian quoted firms, though the impact is positive.

### *Hypothesis II*

H<sub>0</sub> : Board gender diversity has no significant effect on tax avoidance in Nigerian quoted firms.

H<sub>1</sub> : Board gender diversity has a significant effect on tax avoidance in Nigerian quoted firms.

### *Computation*

The test statistic is computed by STATA software and the results are as shown in Table 4.4.

**Table 4.4: Regression Results on Board Gender Diversity and Firm Performance.**

| Variable | Coefficient | p-value |
|----------|-------------|---------|
| BDDV     | 0.1487      | 0.005   |

Source: Extracted from STATA Computations

***Decision***

With a coefficient of 0.1487 the results indicate that board gender diversity positively impacts tax avoidance in Nigerian quoted firms, while the probability value of 0.005 indicates that the positive impact is significant. This leads to the acceptance of the alternate hypothesis, thus the rejection of the null hypothesis. The researcher accepts that board gender diversity significantly impacts tax avoidance, and that such effect is positive.

***Hypothesis III***

H<sub>0</sub>: Board meeting has no significant effect on tax avoidance in Nigerian quoted firms.

H<sub>1</sub>: Board meeting has a significant effect on tax avoidance in Nigerian quoted firms.

***Computation***

The test statistic is computed by STATA software and the results are as shown in Table 4.6.

**Table 4.6: Regression Results on Local Community Disclosure and Firm Performance**

| Variable | Coefficient | p-value |
|----------|-------------|---------|
| BDMT     | -0.3343     | 0.007   |

Source: Extracted from STATA Computations

***Decision***

With a coefficient of -0.3343 the results indicate that board meeting negatively impacts tax avoidance in Nigerian quoted firms while the probability value of 0.007 indicates that the negative impact is not significant because it is more than 0.05. This leads to the rejection of the alternate hypothesis, thus accepting the null hypothesis. The researcher accepts that board meeting does not significantly affect tax avoidance in Nigerian quoted firms.

#### **4.4 Discussion of Findings**

This study examined corporate governance characteristics, determinants of tax avoidance.

The results indicate that almost all the variables are significantly normally distributed at 5% level of significance. The correlation matrix indicates the variables have mixed relationships. The results also indicate the absence of multi-collinearity.

Essentially, the findings of the study are: with a coefficient of -0.10297 the results indicate that board size negatively impacts tax avoidance, while the probability value of 0.689 indicates that the positive impact is not significant. This leads to the rejection of the alternate hypothesis, thus acceptance of the null hypothesis that board size has no significant impact on tax avoidance in Nigerian quoted firms, though the impact is negative. The result is consistent with the findings of Deheane (2018) and Robinson et al. (2018), but was not consistent with the findings of Haniffa (2016), Limpaphyayom (2004), Ayers et al. (2017) and Kawor and Kporgbi (2017). This inconclusiveness may have resulted from the existence of varying degrees of institutional backdrops.

Similarly, with a coefficient of 0.1487 the results indicate that board gender diversity positively impacts tax avoidance in Nigerian quoted firms, while the probability value of 0.005 indicates that the positive impact is significant. This leads to the acceptance of the alternate hypothesis, thus the rejection of the null hypothesis. The researcher accepts that board gender diversity

significantly impacts tax avoidance, and that such effect is positive. The result agrees with the findings of Liu et al. (2014), Pratama (2017), Reguera-Alvarado et al. (2015), Ekadah and Josphat (2010) but not consistent with the findings of Rose (2007) and Randoy et al (2007).

And, with a coefficient of -1.163 the results indicate that board meeting negatively impacts tax avoidance in Nigerian quoted firms while the probability value of 0.463 indicates that the positive impact is not significant because it is more than 0.05. This leads to the rejection of the alternate hypothesis, thus accepting the null hypothesis. The researcher accepts that board meeting does not significantly affect tax avoidance in Nigerian quoted firms. The result agrees with the findings of Nwoje (2018), Gabi and Dabor (2019), Kinjo (2018) and Hills (2015), but not consistent with the finding of Enoma (2017). This might have been as a result of using different industrial sectors.

## **CHAPTER FIVE**

### **SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS**

#### **5.1 Summary of findings**

This study examined corporate governance characteristics, determinants of tax avoidance. Based on the test conducted and the analysis of the results, the study made the following findings.

- i. Board size has no significant relationship with tax avoidance in Nigeria quoted conglomerates.
- ii. Board gender diversity has a significant relationship with tax avoidance in Nigeria quoted conglomerates.
- iii. Board meeting does not significantly affect tax avoidance in Nigeria quoted conglomerates.

#### **5.2 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. Studies on the relation between existing tax avoidance and corporate governance mainly suggest that a high level of tax avoidance increases the tax risk of a company. Previous studies have shown that corporate tax evasion increases the likelihood of corporate tax audits, increases the likelihood of paying higher tax costs

due to tax audits and penalties from tax authorities, and is a temporary method that corporations cannot use continuously in the future.

### **5.3 Recommendations**

Based on the findings from this study and the conclusion reached, the study offers the following recommendations:

- i. It is therefore recommended that the board Size should not be too large, specifically, maximum of nine (9) members. This would assist in facilitating quick decision in relation to fraud.
- ii. The presence of female directors on board should be encouraged since it has a positive relationship with the performance of firm though the relationship is insignificant. The result is justified based on the fact that women are more ethical than men.
- iii. The study recommends that regular board meeting so as to address issues relating to tax avoidance and how to improve the overall organizational efficiency.

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