

TAX CREDITS, EXEMPTIONS, AND PROFITABILITY: EVIDENCE FROM NIGERIA'S LISTED COMPANIES

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Abstract

This study examined the effect of tax credits and tax exempts on the operating profits of listed firms. It used the Dangote Group of Companies in Nigeria, as its population. Anchored on the Benefit theory of taxation, two objectives and hypotheses were formulated and tested. The researcher employed ex post facto research design and used panel data collected from annual financial reports of the sampled companies (Dangote Cement Plc and Dangote Sugar Refinery Plc), for 2013 to 2022. The data collected were analyzed using descriptive statistics, correlation and analyzed using panel regression technique. The study proxy firm characteristics using tax credits (TXCDT), and tax exempts (TXEMP) as predictor variables; while Operating profit (OPP) was used as measure of the dependent variable. Results revealed that tax credit had negative and insignificant effect on the companies' operating profits. It was also found that tax exempts had negative but significant effect on their operating profits. Accordingly, the study recommended that tax credits doesn't matter, since it does not significantly affect operating profits. Hence, companies should place less emphasis on tax credits. Finally, it was also recommended that companies should take steps to earn more tax-exempt incomes; since they affect operating profit of listed firms significantly and positively.

Keywords: Tax credits, Tax Exempts, Operating Profits, Dangote Cement Plc, Dangote Sugar Refinery Plc.

For the provision of public conveniences (both social and security); to create conditions for the economic well-being of the society.

More recently, some developing economies have devised another means of using taxation as a tool for projects funding. These are seen as part of public-private-partnership (PPP) arrangements. Under this scheme, companies are required to finance government projects; in return for exemptions from payment of income taxes (for an agreed amount and stated period of time). Accordingly, corporate bodies are encouraged to invest and develop infrastructure, in return for tax rebates. Being that companies are profit driven, the government in return compensates them with some tax rebates or incentives (in the form of credits, exemptions, or rate reductions) for a stated period of time.

In Nigeria, the Buhari administration adopted this strategy. This follows the signing of Executive Order 07 of 2019 on road infrastructure tax credit by the former President Muhammadu Buhari. Accordingly, tax credit certificates were issued to some companies to bank-roll the construction of certain roads on behalf of the government. In particular, the Federal Government of Nigeria (through the Federal Inland Revenue Service, FIRS) issued tax credit certificates to Dangote Cement Plc, for the construction of Apapa-Oworonshoki-Ojota road in

Lagos and the Lokoja-Obajana-Kabba road connecting Kogi and Kwara. Prior to that, tax credit certificate was issued to the company by the FIRS for the construction of LokojaObajana-Kabba road in 2019 totaling over N9.5 billion. Then FIRS Chairman (Mr Nami) was quoted by AriseTv to have said that government came to that reasoning so that they could encourage local investors to do investment in infrastructural development such as road construction on behalf of the government under an agreement with some due monitoring and approvals then some of the monies they would have accrued back to government as taxes, they would have paid. The former chairman further argued that it was for the interest of the government that other investor, business entrepreneurs, companies would take advantage of that key initiative so that Nigeria could develop faster than the government would have done alone.

Similarly, the NNPC Limited also had an agreement with the government to prioritize road infrastructure in return for a tax credits and exemptions totaling over N621 billion. The Managing Director, Mallam Mele Kyari, was quoted to say that the company planned to invest over one trillion naira for a similar purpose. According to him, the NNPC was expected to construct a total of 1,804.6 kilometers of roads at a total cost of over six hundred and twenty-one billion naira, in the first phase. Under the scheme, the road projects will be funded by NNPC and the equivalent amount deducted by the Federal Inland Revenue Service from the company's tax obligations.

The impact of these tax incentives (tax credits and exempts) on the operating profits of some selected companies in Nigeria is the reason for this study.

Statement of the Problem

Governments fund their activities in two ways. They can use the straight forward method of taxing and spending money which they generate. Alternatively, they can use tax expenditures. These are in the form of tax credits, exemptions, or rate reductions which give direct benefits to a category of taxpayers often as an incentive to take a particular action. The primary aim of these schemes is to encourage companies to invest, develop infrastructure, or set up in disadvantaged regions. In Nigeria for instance, participants in the Road Infrastructure Development and Refurbishment Investment Tax Scheme are entitled to recover the costs incurred by them in the construction or refurbishment of eligible roads as tax credits against income tax payable. In some other cases, the participants are also entitled to a single uplift, equivalent to the Central Bank of Nigeria (CBN) monetary policy rate plus 2% of the project costs. This uplift will not be taxable in the hands of the participants, but such tax credit can be carried forward to subsequent years until it is fully utilized. Again, the participants may be allowed to sell or transfer their tax credits to other companies, as a form of security or otherwise. These have been seen in the examples of Dangote Cement Plc, NNPC Limited and the Nigeria Liquefied Natural Gas Limited (NLNG), etc., who have been variously granted tax credits and exemptions by the government of Nigeria for embarking on road and other infrastructures on behalf of the government.

Studies have been carried out by various authors on the effects of tax incentives on the performance of companies. For example, Chukwumerije & Akinyomi (2011), Uwaume & Ordu (2014), Ohaka (2011), Gumo (2013), Ironkwe and Nnaji (2017) Timah and Chukwu (2021), etc. have all carried out studies on this subject matter. However, the studies so far carried out are still scanty, considering how weighty this subject matter is on the performances of businesses as well as economic growth. Hence, there is still more to explore, in the first place. Secondly, prior studies so far carried out on this subject area in Nigeria mainly employed survey research design, meaning that the data were sourced through the questionnaire and other primary data sources. That goes to show that there were chances that the results could have been prone to some level of manipulations, which could largely impair the reliability of the inferences and decisions taken based on such studies. All these constitute huge gaps in literature which this study intends to address. This study therefore attempts to close these identified gaps as well as to further expand the frontier of knowledge on the subject. Specifically, the study sought to use purely secondary data sources from the Dangote Cement Plc and Dangote Sugar Refinery Plc (specifically) from 2013 to 2022, to investigate the effect of tax credits and exempts on operational profits of companies in Nigeria. That formed the study's point of departure.

2 LITERATURE REVIEW

Concept of Tax Credits- Tax credit means a credit against, relief or remission for, or repayment of any tax. In Nigeria, government grants various tax incentives such as tax credits to companies to aid in the investment and development of certain infrastructures in the country. For example, participants in the Road Infrastructure Development and Refurbishment Investment Tax Scheme are entitled to recover the cost incurred by them in the construction or refurbishment of eligible roads as credit against CIT payable.

Concept of Tax-Exempt Incomes- Generally, incomes and profits can be exempted from tax. A tax exemption is an amount allowed by law as reduction of income or profit that would otherwise be taxed. The Black's Law Dictionary has defined the term to mean 'immunity from the obligation of paying taxes in whole or in part'. Nangih (2023) opined that tax-exempt refers to income or transactions that are free from tax at the federal, state, or local level.

Operating Profit After Tax-Operating profit is a measure of a company's profitability that looks at the profits made after tax has been paid. It matches all the company's expenses, which include operating and interest expenses, against its revenues. Profit after-tax is the earnings of a business after all income taxes have been deducted. This amount is the final, residual amount of profit generated by an organization. The profit after-tax figure is considered the best measure of the ability of an entity to generate a return, since it incorporates both operating income and income from other sources, such as interest income.

Theoretical Review

This study is guided by the Benefit theory of taxation. The benefit theory of taxation, according to Browning and Browning (1979) implies a specific method for distributing the tax burden; taxes should be allocated on the basis of benefits received from government expenditures. According to this theory, the state should levy taxes on individuals according to the benefit conferred on them. The more benefits a person derives from the activities of the state, the more he should pay to the government.

This principle has been subjected to severe criticism on the following grounds: firstly, if the state maintains a certain connection between the benefits conferred and the benefits derived. It will be against the basic principle of the tax. The first is that, as we know, tax is compulsory contribution made to the public authorities to meet the expenses of the government and the provisions of general benefit. There is no direct quid *pro quo* in the case of a tax. Secondly, most of the expenditure incurred by the state is for the general benefit of its citizens. It is not possible to estimate the benefit enjoyed by a particular individual every year. On the other hand, one important advantage of the benefit principles is that it emphasizes the essential two-sidedness of government tax-expenditure decisions. If people do not receive benefits commensurate with their tax burden, then perhaps the expenditure should not be undertaken at all.

Review of Prior Studies

Several studies have been carried out both at the global as well as local levels to establish the impact of tax incentives on various indicators of a company's performance as well as investments. For instance, Omes and Maccarthy (2022) attempted to investigate the effect of tax incentives on financial performance of listed consumer goods firms in Nigeria. The study employed ex-post facto design. A sample of 21 consumer goods firms listed on the Nigerian Exchange Group were used as sample for the study. Data were sourced from their annual financial statements from 2009 to 2019. The results showed that investment allowance significantly and positively impacted profitability. It was also found that there existed positive and significant relationship between annual allowance and return on assets of the listed companies in Nigeria.

On their part, Chukwu and Timah (2021) investigated the influence of tax incentives on corporate earnings of quoted manufacturing companies in Nigeria. The study proxy tax incentives using annual allowance, investment allowance, and tax holiday; whereas earnings per share (EPS), was used as a measure of corporate earnings. The study also employed the companies' share capital as the moderating variable. Secondary data were sourced from their annual financial statements of 69 out of a total 89 listed companies, which formed the study sample. The data were analyzed using descriptive statistics and multiple regression, and the result showed that EPS is influenced by tax incentives.

Ironkwe and Nnaji (2017) carried out a study to empirically ascertain the extent to which tax incentives would enhance realization of core objectives of regulated microfinance business in Nigeria with a focus on Rivers State.

Primary data were collected from the shareholders, managers, key employees, customers and external auditors of 19 Microfinance Banks in Rivers State through questionnaire and participants observation. The questionnaire before they were administered to the respondents were subjected to validity and reliability tests. The data generated were analyzed using Spearman's Rank Correlation Coefficient while Z test statistics was used to test the formulated hypotheses. The findings showed that tax incentives had significant and positive effect on the performance of Microfinance Banks in Nigeria.

Uwuigbe, Uwuigbe, Adeyemo and Anowai (2016) examined the effect of tax incentives on the overall performance of manufacturing firms in Nigeria. The study specifically aimed at identifying how tax incentives impacted funds availability, productivity and growth rate of manufacturing firms. Primary data were collected through the questionnaire, which were distributed randomly to a 100 staff of the selected manufacturing industries. The data collected were tabulated and analyzed using regression analysis. The results revealed that tax incentives influenced the funds available for investment in the manufacturing industries. It was also revealed that tax incentives significantly increased the number of manufacturing industries in Nigeria.

3. METHODOLOGY

Ex post facto research design was utilized in this study. The population consists of all the manufacturing companies listed on the Nigeria Exchange Group. However, the study, purposively selected and used two companies from the Dangote Group with data on the variables as at 31st. December 2022, as samples. These were Dangote Cement Plc and Dangote Sugar Refinery Plc. Secondary data, were sourced from the annual financial reports of the sampled companies and summarized using descriptive statistics. Thereafter, the data was analyzed using the correlation and regression model based on Ordinary Least Square (OLS) and random effects model with the aid of Econometric Views. The decision rule for hypotheses formulated and test was that if the probability value is greater than the desired level of significance of 0.05; the researcher accepts the null and rejects the alternate hypothesis. If otherwise, the researcher accepts the alternative and rejects the null hypothesis.

Model Specification

Based on the study objectives, the basic model proposed for the study to specify the relationship is presented below:

$$OPP = f(Txcdt, Txemp), \dots \dots \dots 1$$

From the above functional relationship, the econometric model will be specified below:

$$OPPit = a_0 + a_1 Txcdtit + a_2 Txempit \dots \dots \dots 2$$

Where; OPPit = Operating Profit;

Txcdt = Tax Credits;

Txemp = Tax Exempt Incomes

a_0 = Constant term a_1, a_2 = Coefficient attached to explanatory variables. i = company; t = time period; u = Stochastic error term

4. DATA ANALYSIS AND DISCUSSION OF FINDINGS Descriptive Statistics

Descriptive statistics provide information concerning the basic characteristics of the data, such as the mean, standard deviation, skewedness, kurtosis and normality, etc. They also enable the comparative assessment of the variables under study. The result of the descriptive statistic is shown in table 4.1.

Table 4.1: Descriptive Statistics

	TXCDT	TXEMP	OPP
Mean	38519.45	167618.4	145354.1
Median	15959.50	55292.50	98602.00
Maximum	342069.0	889498.0	402857.0
Minimum	0.000000	0.000000	12171.00
Std. Dev.	75150.76	233763.8	143830.4
Skewness	3.501796	1.746548	0.685292
Kurtosis	14.78029	5.466992	1.991422
Jarque-Bera	156.5214	15.23981	2.413110
Probability	0.000000	0.000491	0.299226
Sum	770389.0	3352367.	2907081.
Sum Sq. Dev.	1.07E+11	1.04E+12	3.93E+11
Observations	20	20	20

Source: Author's Computation using EViews

The results in Table 4.1 indicate that TXCDT and TXEMP have mean values of N38.5m and N167.7m, while OPP have mean values of N145.4m. The standard deviations show that TXCDT and TXEMP are more widely dispersed from the mean than OPP. The Skewness and Kurtosis statistics also indicate that TXCDT and TXEMP are more skewed and peaked than OPP, which suggests that they are abnormally distributed. Lastly, the Jarque-Bera statistics also revealed that TXCDT and TXEMP have probability values that are less than 0.05, while that of OPP is greater than 0.05, indicating that TXCDT and TXEMP are abnormally distributed while OPP is normally distributed.

Correlation Statistics

The correlation statistics is meant to ascertain whether or not there are associations between the variables employed. It also provides information about the likelihood or unlikelihood of multi co-linearity in the variables captured in the research model. The result of the correlational statistics is presented in Table 4.2 below.

Table 4.2 Correlation Matrix

	TXCDT	TXEMP	OPP
TXCDT	1.000000		
TXEMP	0.075197	1.000000	
OPP	-0.376503	-0.500073	1.000000

Source: Author's Computation using EViews

The result in Table 4.2 indicates a correlation coefficient of 0.075 between TXCDT and TXEMP, which implies that the variables are positively associated. Both variables have negative associations with OPP. The negative association implies that increase in tax credit as well as tax exempts will lead to a reduction in operating profit after tax. Specifically, it means that 1% increase in tax credit will reduce operating profit after tax by about 38% while a 1% increase in tax exempts will reduce operating profit after tax by about 50%. More so, the correlation coefficient of 0.075 between TXCDT and TXEMP suggests an unlikelihood of multi co-linearity between the variables in the research model.

Multiple Regression

The multiple regression is employed to ascertain the possible effects of the independent variables on the dependent variables. The result is shown in Table 4.3.

Table 4.3 Multiple Regression

Dependent Variable: OPP

Method: Panel Least Squares

Sample: 2013 2022

Periods included: 10

Variable	Coefficient	Std. Error	t-Statistic	Prob.
TXCDT	-0.652305	0.362266	-1.800624	0.0895
TXEMP	-0.291916	0.116951	-2.496053	0.0231
C	219411.0	36421.47	6.024222	0.0000

R-squared	0.365579	Mean dependent var	145354.1
Adjusted R-squared	0.290941	S.D. dependent var	143830.4
S.E. of regression	121113.4	Akaike info criterion	26.38432
Sum squared resid	2.49E+11	Schwarz criterion	26.53368
Log likelihood	-260.8432	Hannan-Quinn criter.	26.41348
F-statistic	4.898037	Durbin-Watson stat	1.674166
Prob(F-statistic)	0.020903		

Source: Author's Computation using EViews

In Table 4.3, adjusted R-squared, which is the coefficient of determination or measure of good fit of the model, tests the explanatory power of the independent variables in the OPP Model. Accordingly, Table 4.3 reveals that the independent variables determine 29% of the variations in the operating profit of the sampled firms. By implication, it means that about 29% of the changes in operating profit (the dependent variable) were caused by the independent variables in our model, leaving the remaining 61%, which would be accounted for other variables outside the model as captured by the error term.

The F-statistics which measures the overall significance of the explanatory parameters in the model, and illustrates the appropriateness of the model used for the analysis while the probability value means the model is statistically significant and valid in explaining the outcome of the dependent variable. From the above result in the Model, the F-statistic and probability value of 4.898 and 0.021 reveal that the model has a high goodness of fit. We therefore accept the alternative hypothesis and state that there is a significant relationship between the variables. This means that the parameter estimates are statistically significant in explaining the relationship in the dependent variable. On the other hand, the coefficient and the t-statistics helps in measuring the individual statistical significance of the parameters in the model from the result report. The result as shown on the table 4.3. The t-statistics also reveal that both TXCDT and TXEMP have negative effects on OPP but only TXEMP is significant at 5%.

Discussion of Findings

The regression results presented revealed that tax credit had an insignificant negative effect on both the operating profits of the two firms. Given the t-statistics of -1.800624 with a probability value of 0.089, it implies that an increase in tax credit will cause a reduction in the operating profit, which is contrary to the apriori expectation. However, the result was not significant, as the P-value was greater than 0.05. This may be probably due to the challenging operating environment of business firms in the country, given the recessionary economic trend in the country, especially since 2015. This result was contrary to the results of Ironkwe and Nnaji (2017) who found that

tax incentives had significant and positive relationship with the business performance of Microfinance Banks in Nigeria. The study was also in contrast with the findings of Omesi and Maccarthy (2022)

In the same vein, tax exempt was found to have a significant but negative effect on the operating profit firms in the Dangote Group. The results in Table 4.5 revealed t-statistics of -2.496053 as well as probability value of 0.0231. These results imply that an increase in tax exempt is likely to result in a decrease in operating profit, which is contrary to the a priori expectation. The probable reason for this may also be due to the challenging operating environment of business firms in the country, as previously stated. The above result also is contrary to the findings was not in agreement with the findings of Chukwu and Timah (2021)

5 CONCLUSION AND RECOMMENDATIONS

This study undertaken to determine the extent to which tax exempts and tax credits affect operating profits of Dangote Sugar Plc and Dangote Cement Plc. The study also utilizes panel data collected from the annual financial reports of the two companies from 2013 to 2022. These were analyzed using panel regression technique. The major findings made from the study were: (i) tax credit had negative and insignificant effect on operating profit and (ii) tax exempt had negative but significant effect on operating profits.

The findings of this study lead to the following conclusions; (i) Tax credit is not like to influence operating profits, since the effect is insignificant and (ii) Tax exempts are also likely to have significant effect on operating profits since the p-value is less than 0.05 but the relationship is negative. It was therefore recommended that; (i) Tax credits are doesn't matter much since it does not significantly affect operating profits. So, companies should place less emphasis on tax credits and (ii) companies should take steps to earn more tax-exempt incomes since they affect operating profit of listed firms.

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