Policy Brief

Corporate Tax Planning, Governance Mechanisms, and Economic Growth in West Africa

PUBLISHED

BY

RESEARCH AND STATISTICS DEPARTMENT (RSD)

Introduction

Corporate tax planning plays a vital role in financial performance, governance, and economic growth but faces increasing scrutiny from governments, regulators, and the public. This Policy Brief analyses findings on the following research:

- The Relationship between Corporate Tax Planning and Financial Performance in Nigeria Consumer Goods Firms,
- The Impact of Governance Mechanisms on Tax Planning in Nigeria, and
- The Role of Institutional Quality in Shaping Company Income Tax and Economic Growth in West Africa.

Using data from Nigerian and West African firms, these studies employed Structural Equation Modelling (SEM), Generalized Least Squares (GLS) Regression, Dynamic Panel, Auto Regressive Distributed Lag (ARDL) models to analyse key economic indicators such as GDP, institutional quality, trade openness, inflation, interest rates, exchange rates, and tax effort ratio.

Key Findings

1. Corporate Tax Planning and Financial Performance:

- Book Tax Difference (BTD) positively influences Return on Assets (ROA), suggesting firms managing BTD effectively can enhance profitability.
- Effective Tax Rate (ETR) has a statistically insignificant but positive impact on ROA, indicating that tax rate alone does not drive firm performance.
- Earnings management strengthens the positive relationship between BTD and ROA but negatively affects the link between ETR and ROA, revealing risks associated with aggressive tax planning.

2. Governance Mechanisms and Corporate Tax Planning:

- Board independence, board gender diversity, and audit firm size significantly reduce corporate tax planning in Nigeria firms.
- Stronger governance frameworks improve transparency and reduce tax avoidance practices.

Key Findings Con

3. **Institutional Quality and Economic Growth in West Africa**:
   - Institutional quality plays a crucial role in determining the effectiveness of company tax policies in enhancing economic growth.
   - Economic factors such as inflation, interest rates, trade openness, and exchange rates significantly influence economic growth.

Policy Recommendations:

1. **Strategic Tax Planning for Firms:** Firms should leverage available BTD opportunities to enhance financial performance while ensuring compliance with regulatory standards.
2. **Strengthening Governance Mechanisms**: Nigerian regulatory authorities should increase minimum requirements for board independence and gender diversity to enhance corporate accountability.
3. **Enhancing Institutional Quality for Economic Growth:** Governments should strengthen governance, transparency, and regulatory frameworks to improve tax policy effectiveness. Policymakers should design tax policies that consider the broader economic environment, maximizing their impact on economic growth.
4. **Monitoring Economic Indicators**: Continuous assessment of macroeconomic indicators is necessary in developing an effective fiscal policy which would assist regulatory agencies in creating a more conducive investment climate.
5. **Capacity Building and Compliance Measures:** Governments should implement policies to attract foreign investment by improving institutional quality and economic stability.

You can access these research papers on the FJTS Website and the FJTS Vol 4.