Corporate Tax and Dividend Policy of Listed Conglomerate Companies in Nigeria

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Abstract: *This study investigates the effect of corporate income tax on dividend policy of listed conglomerate companies in Nigeria. Sample data were obtained from the Nigerian Stock Exchange (NSC) for a period of ten years from 2007 to 2016. Panel regression analysis was adopted to estimate the effect of corporate income tax on dividend policy. The result revealed a significant relationship between the two constructs. Effective income tax rate and firm size have negative and significant effect on dividend yield. Leverage have insignificant positive effect on dividend yield of listed conglomerate companies in Nigeria. It's therefore recommended that, sufficient clarification of some sections of tax laws specially section 19 needs to be made by tax authority and the national assembly, so that profits which have already been taxed and those that are specifically exempted from tax don't have to be taxed twice as this may amount to double tax and have a negative consequences on the company's decision to pay dividend.*

Keywords: Dividend Yield, Effective Income Tax Rate, Leverage

1. Introduction

Corporation tax is invariably an essential part of any tax system, predominantly for emerging economy like Nigeria where substitute revenue sources are thin. This is because corporation taxes are very progressive, they raise significant amounts of money for public services.Corporate tax is levied on the income of company and corporate dividend tax is levied on the amount of dividend declared, distributed or paid by the company. Brennan (1970), Masulis and Trueman (1988) have established that taxes affect corporate dividend policy.One of the ways is, it influences net income-after-tax of the company which determines the capacity of the company to pay dividends. Also, it may have implications for the net value received by the shareholders. In this sense, the structure and the rate of corporate tax play an important role in determining the dividend policy.

Nigerian tax rules subject corporate income to the corporate income tax (CIT) at the company level and then to the personal income tax when dividends are distributed. That is, if corporations do not distribute the profits as dividends, shareholders pay taxes on their capital gains when they sell shares. Therefore, corporate income is taxed twice. Nigerian companies are now liable to income tax at 60% if the new judgement of the Tax Appeal Tribunal on excess dividend tax is sustained (Oyedele, 2014). The corporate tax laws which was enacted by the government to serve as source generating income or revenue for the smooth-running of the state have over the years generated controversies because of the misinterpretation of the clauses by the judges in Nigeria. This is evidenced in a case where:

Tax Tribunal, in interpreting Section 19, held that dividends paid from retained earnings, where there is no taxable profit or taxable profit is less than the dividends, should be taxed at 30% regardless of whether the earnings had been taxed previously(Oyedele, 2014).

Financial analysts are eager to find out whether this issue of taxation may affect dividend policies in corporate business environment. If this holds true, then when government make changes in income tax policyeffect on corporate dividend policy should be anticipated (Wu, 1996). Consequently, companies may be discouraged from paying higher dividends.

Scholars such as Brennan (1970), Masulis and Trueman (1988), (Wu, 1996), Hu (2006) and LeRoy (2007) agree that corporate tax call for dividend policy change, However, Nigeria's conglomerate company's share in the Gross Domestic Product (GDP) is central to the growth of a nation's economy because it influencesindustrialization through national economic development prospects This motivatesresearcher to test the applicability of Brennan (1970) andMasulis and Trueman (1988)'s theory inconglomerate companies in Nigeria.However, despite decades of debate, no agreement has been reached on the relationship between corporate income tax and dividend policy in and around the globe. Empirical research on this topic will not only contribute to the establishment of a correct theoretical framework, but also will have policy implications on tax reforms. Therefore, the main objective of this study is to empirically examine the effect of corporate tax on dividend policy of listed conglomerate companies in Nigeria. The remaining parts of this paper are organized as follows. Section two reviews relevant existing literature and provides the theoretical framework of the study. Section three discusses the methodology of the study. Section four presents the results of the analyses and discussion while the last section concludes the study and presents recommendations.

2. Review of Related Literature

A review of literature on the relationship between corporate tax and dividend policy is an indication that the predictive ability of company income tax to influence dividend policy is relevant to all and sundry. There are two competing views on the corporate taxation and dividends. The traditional view argues that dividends are not only a way of distributing corporate profits to shareholders, but also have other utilities such as signaling profit to build up investors' confidence and satisfying investors' preference to have cash in their hands

rather than in the corporations. Therefore, corporations have the tendency to distribute the profits to shareholders despite the double taxation of dividends. However, the dividend tax increases the cost of profit signaling and decreases the rate of return of capital for corporate investors. Consequently, it increases the cost of capital and lowers overall investment level in the corporate sector. Others argue that for tax exemption for dividend income on the basis that taxation of dividend income will amount to double taxation. They claim that corporate profits are subject to corporate tax. Since dividends are paid out of profits, the personal income tax paid on dividend income amounts to a second tax on corporate profits.Previous empirical studies revealed significant association between corporate income tax and dividend policy are as follows.

Odia and Ogiedu (2013) examine the relationship among profit, dividend and taxes of the nineteen banks quoted in the Nigerian Stock Exchange for the period of ten years from 2000 to 2009. The study employ OLS as the method of statistical estimation and find that profitability is a major determinant of the dividend policy as there is significant relationship between dividend and profitability; and taxes have negative and insignificant impact on the dividend policy of the banks. Similarly, Samuel and Inyada (2010) study the relationship between corporate income tax and dividend policy of firms quoted in the Nigerian stock exchange for the period of and find a significant relationship between corporate income tax and dividend policy of financial institutions in Nigeria and conclude that a change in corporate income tax rate will significantly affect dividend policy of financial institutions in Nigeria.Pooled OLS regression model neglects the cross sections and time series nature of data. And no evidence of robustness test conducted to validate the results the regression.Hamid, Hanif, Saif-Ul-Malook andWasimullah (2012) found a significant correlation between taxes and the dividend income of banks and conclude that the tax rates is an important determinant of the dividend policies of the banking sector.

On his part, Hu (2006) study the impact of dividend taxation on investment and the impact of corporate income tax exemption on non-profit organizations activity of USA for the period of ten years 1990 to 1999. The study use panel data regression analysis and find that the coefficients of the average CIT rate are positive and significant, suggesting that CIT exemption does have a positive impact on non-profit hospitals market share. But have impact on profit making firms. However, biasness is noticed in the selection of data average. The study did not make use of accounting ratios in the transformation of data rather it log of data relating to earnings and equity use in order to downsize their Scales and normalize them. This may have negative impact on the finding and of course, the generalization.

Furthermore, Jatmiko (2015) determines the effect of tax rate and dividend policy on the stock price of listed Indonesian companies for the period of fifteen years 2001 to 2014. The study adopt Path analysis statistical measurement and find that the tax rate and dividend policy had an effect on the stock price, the tax rate had a positive effect on the stock price, the dividend policy had a positive effect on the

stock price and the tax rate had a positive effect on the dividend policy. The method of data analysis used in the study isn't a common tool and there was no explanation as to its use and its importance in the study. Uwuigbe and Olusegun (2013) also find that there is a significant positive relationship between the company income tax andthe dividend payout of the sampled firms in Nigeria. The study basically modeled the effects of company income tax on the dividend policy of firms listed in the Nigeria stock exchange for the period of five years 2006 to 2010. A total of 40 listed firms in the Nigerian stockexchange market were selected for the study judgmental sampling technique and regression analysis method was used. Their study conclude that a changein corporate income tax rate will significantly affect the dividend policies of the sampled firmoperating in Nigeria.The sample size cut across different sectors, but there was no test or explanation on the analysis of variances and there was no sectorial analysis done, this may render a generalized conclusion unreliable.

On the contrary, Dragota, Dragota,Tatu and Tatu (2009) find no significant correlation between the dividend policy and the corporate tax burden. They analyze dividend payout by Romanian companies listed on the Bucharest Stock Exchange in connection with the changes in corporate taxes for the period of eight years 1998 to 2006. Using panel regression analysis, they suggest that dividend payout reacted when the regulations related to the tax treatment of incomes were changed. They argue that if the tax burden on corporate gross incomes is increasing, the companies' management can follow two reasons in deciding the dividend payout. That is, to allocate more for investments, or to increase the dividend ratio. Each of these decisions can be argued based on corporate finance principles depending on the management objectives. However, the reported values for corporate income tax burden, gross income, dividend payment, total assets, market capitalization and total debts were transformed in logarithmic values in order to normalize the data series and after that, they were expressed as logarithmic differences equivalent to the growth rate of the variable. Also, Chetty and Saez (2010) reveal corporate income taxation have significant positive impact on dividend policy. They state that corporate income tax may therefore be a more efficient way to generate revenue than dividend taxation, challenging existing intuitions based on neoclassical models. They develop a simple agency model in which managers and shareholders have conflicting interests to explain the evidence.

Furthermore, LeRoy (2007) study the effects of dividend and capital gains taxes on optimal dividend payout policy are analyzed in the context of a one-good model (so that capital consists of stored units of the consumption good). The after-tax discount factor is assumed to adjust to taxes to bring about equality between the discounted value of the firm's after-tax dividend stream under the optimal dividend policy and the number of units of capital the firm is operating. A standard result that the Miller-Modigliani dividend irrelevance proposition applies in the presence of taxes if dividend tax rate equals capital gains tax rate (and if capital gains are taxed as they accrue) is demonstrated. The analysis is extended to deal with unequal tax rates. The two major results are allocating retained earnings to share

repurchases has the same tax implications as allocating retained earnings to new investments and either of these will be optimal if and only if the tax rate on company income are high. Janis and Stacescu (2014) find significant positive effect of corporate taxes on dividend policy of Norwegian companies. The Norwegian tax reform in 2006 increased as dividend tax rate rise from 0% to 28% for individuals, but not for companies. They find that an average payout ratio drops from 41% before this shock to 16% afterwards. Operating companies with higher potential agency conflicts pay higher dividends and are more often owned by holding companies. This evidence suggests that taxes strongly reduce dividends that tax costs are actively traded off against agency costs, and that indirect ownership may allow for a dividend policy that reduces agency costs at minimal tax costs. Similarly, Jacob, Michaely and Alstadsaeter (2014) study taxation and dividend policy. Their study finds that taxation has a first order impact on payout policy. However, the impact of taxation on dividend policy becomes insignificant as the number of owners increases. Bank (2006) suggest that corporate income tax design has important implications for predictions about the future of dividend policy.

Bushra and Mirza (2015) identify the significant determinants of firms' dividend policy across different sectors in Pakistan. Using data on 75 companies listed on the KSE, 100 index for the period 2005 to 2010 was examined. They find that profitable firms tend to give higher dividends than loss-making firms. Firm size has a negative relationship with the dividend payout ratio and dividend yield, indicating that, the larger the firm, the more likely it is to retain cash to pay off its liabilities. Growth in sales is positively related to dividend yield, whereby an increase in sales leads to higher profitability and higher dividend payments. Finally, the market-to-book ratio is negative and highly significant: firms with better growth opportunities rely on internal financing more than on generating external funds.

3. Methodology

Descriptive research design is used for this study. The population of this study covers the six conglomerate companies listed on the Nigerian stock exchange as at 31st December, 2007 up till 2016. Census sampling method was adopted base on the availability of data. This study is quantitative in nature and it's based on secondary source which is generally collected from publicly listed conglomerate companies. Therefore, the data obtained from these sources relate to dependent and explanatory variables.

The dependent variable is dividend policy proxy by dividend yield. The use of the dependent variables in this study is informed by the study of Ying (2011), Uwuigbe and Olusegun 2013; Salawudeen (2015). The explanatory variables of this study include the independent and control variables. The study use effect income tax rate as independent variable as informed by Uwuigbeand Olusegun (2013); Ikin and Tran (2013). Review of literature on corporate income tax and dividend policy led to the decision to include some variables believed to influence dividend policy as control variables in the model to test the main hypotheses. These variables are leverage and firm size. This

is informed by previous studies such as Uwuigbe and Olusegun 2013;Salawudeen (2015).

Table 3.1: Variables and their Measurements

Variables	Abbreviation	Description
Dependent Variables		
Dividend Yield	DY	Dividend yield is measured by dividend per share divided by market price per share at the end of the year.Uwuigbe and Olusegun 2013;Salawudeen (2015); Abdulrahman and Salawudeen (2017).
Independent Variables		
Effective Income Tax Rate	EITR	Income tax expenses divided income earned before tax as used by Uwuigbe and Olusegun (2013); Ikin and Tran (2013).
Control Variables		
Leverage	LEV	Leverage is measured by total debt divided by total assets as used by Salawudeen (2015)
Firm size	FS	Firm Size is measured by the natural log of total assets as used by Uwuigbe and Olusegun 2013;Salawudeen (2015)

Panel Regression Analysis
Panel data regression analysis is used to determine the variability of dependent variables (dividend yield) as a result of changes in any of explanatory variables (effective income tax rate, Leverage, and Firms Size). Panel regression technique of data analysis is used to estimate the effect of explanatory variables on dependent variable due to the longitudinal nature of the data. Hence, the model that follow was adopted as informed by Ikin and Tran (2013); Uwuigbe and Olusegun (2013);Salawudeen (2015); Abdulrahman and Salawudeen (2017).

Model Specification
$DY = \alpha_0 + \beta_1 itEITR + \lambda_2 itLEV + \lambda_3 itFS + \mu_{it}$
Where:
DY   Dividend Yield for firm i in period t,
EITR   Effective Income Tax Rate for firm i in period t,
LEV   Leverage for firm i in period t,
FS   Firm size for firm i in period t,
α_0 Constant or Intercept.
$\beta_1...n$ is the regression model coefficients of the independent variables
λ is the parameters of the control variables
μit is the random error of firm i in period t,
t   Time dimension of the Variables
i   represents firms under consideration

4. Results and Discussions

This section presents the results of the regression and discussion of major findings. It begins with descriptive statistics, correlation matrix and regression analysis of the study.

Table 4.1: Descriptive Statistics of corporate income tax and dividend policy

Variable	Obs	Mean	Std. Dev.	Min	Max	Skewness	Kurtosis
DY	60	0.3474	0.2894	0.0113	0.9971	0.0055	0.2499
EITR	60	0.2581	0.1534	-0.2659	0.6220	0.7467	0.0130
LEV	60	0.3124	0.5650	0.0111	4.4353	0.0000	0.0000
FS	60	23.8977	1.4405	21.3427	45.4326	0.8704	0.3847

Source: Generated by the researcher, using Stata (Version 13).

Table 4.1 presents the descriptive statistics of all the variables used in this study and it shows the mean, standard deviation, minimum and maximum values of sampled conglomerates companies. The table unveils some moderately small figures in standard deviation which was necessitated by the nature and size of data obtained and used. All variables employed in this study are closely spread out as can be seen from their close margins between their mean and standard deviations' figures. Likewise, their minimum and maximum figures. Also positive mean values of the dependent variable indicate an upward change in its value.

The analysis of the table divulges that, the dividend yield ratio has the average of 0.347 indicating that, each N1.00 of corporate income tax in conglomerates companies generates about 0.35K of dividend yield ratio. This indicates the possibility of management of conglomerates not paying dividend if income tax were to be increased and this may portray the company in a bad light.The standard deviation of 0.32 indicates that there is no significant variation in dividend yield between the sampled companies during the study period. Effective income tax rate shows an average of 0.258 which means every 1% income tax rate can generate 26% increase in dividend yield of sampled firm. The standard deviation of 0.153 indicates that there is no significant variation in effective income tax rate of sampled companies during the study period with a minimum effective income tax rate of 27% and maximum effective income tax rate of 62%. Leverage shows an average of 0.312 this means that N1 worth of leverage can generates 31k dividend yield ratio which indicates that a more levered firm may have less dividend yield. Firm size shows an average of N23.9m. This means each N1m worth of assets in conglomerates companies generates about N23.89K of dividend yield ratio.This is necessitated by the size of the firms as large firms have the capability to high dividend yield than smaller firms. However, all the variables under study are positively skewed means that more results were obtained in the lower values, this happens because the right side of the axis has the peak of the histogram. The kurtosis of the variables in the study exhibits the characteristics of a platykurtic curve shape. In that the peak of the curves are less peaked than the normal curve.

Table 4.2: Correlation Matric of corporate income tax and dividend policy

Variables	DY	EITR	LEV	FS	VIF
DY	1.0000				
EITR	-0.3057	1.0000			1.09
LEV	0.5067	0.0959	1.0000		1.03
FS	-0.3342	0.0242	-0.0475	1.0000	1.02

Source: Generated by the researcher using Stata (Version 13).

Table 4.2 shows the results of the spearman rank correlation between the dependent variable (DY) and explanatory variables (EITR, LEV and FS). The relationship between DY and DY is perfect. EITR has weak and negative relationship with the dependent variable DY. There is fair and positive relationship between LEV and DY. Also, FS shows a weak and negativeassociation with DY of the sampled firms. However, EITR has weak and positive association with LEV while EITR weak and positive relationship with FS. Again, FS and LEV are negatively related and weak.

Robustness Check

Root MSE: root mean squared error shows a value of 0.25. This indicate that the model is fit. The study also indicates no present of multicollinearity in the independent variable with a Variance Inflation Factor (VIF) mean of 1.01 which is less than 10 which is the bench mark, this result provides evidence of the absence of collinearity (see table 4.2). This shows that the explanatory variable in this are not interrelated. Heteroscedasticity test was further conducted to ascertain the variability of error term being constant or not. This study shows presence of heteroscedasticity in the data set which implies that the error term is not constant with significant p-value of 0.0197, to correct this heteroscedasticity robust standard error test was conduct (see table 4.3). Normality test of the residual was conducted to check the behavior of the error term. The test shows insignificance with probanility valve of 0.9546. Linearity test was conducted to check the relationships between the variable, it does provide a good testing for linearity. Normality of residuals was also carried out Normality test of the error term is an assumption of the regression model (OLS) which ensure that the validity of all tests (p, t and F) residuals behave normal. However, the study predict error term (e) by running sktest e and result reveal an insignificant p-value at 0.9546 which means that the standard error are normally distributed (see table 4.3). Thus panel regression analysis was adopted for the study and the model indicates a good fit.This study conduct a Hausman specification test to choose between fixed effect and random effect regression. This is to check the trade-off between the efficiency of random effect and the consistency of fixed effect. This study reveals that random effects model is more efficient than the fixed effects with the p-value of 0.2256 and hence, the fixed effect are rejected in favour of the random effect model. Then Breusch and Pagan Lagrangian multiplier test for random effects (xttest0) was conducted to choose between OLS and RE. OLS was chosen in favor of RE after preliminary test of its assumption. The robustness test is carried out in order to ensure the validity of all statistical inferences for this study and to check any outliers among the regression standardized residuals.

Table 4.3: Result OLS and GLS

Variables	OLS			GLS (Random-Effects)		
	Coeff.	T	t>/t/	Coeff	Z	t>/z/
Constant	2.1119	3.9	0	2.5187	-2.54	0.005
EITR	-0.8103	-3.83	0	-0.5438	0.61	0.011
LEV	0.5703	0.99	0.325	0.0329	-2.29	0.541
SIZE	-0.06583	-2.93	0.005	-0.0854	2.82	0.022
R2	0.3011			R2 Within ----- 0.1714		
Adj. R2	0.2636			Between ----- 0.2782		
Hettest	0.0197			Overall ----- 0.2009		
Sktest	0.9446					
Probability	0.0002			Probability ----- 0.0004		

Source: Generated by the researcher, using Stata (Version 13).

Table 4.3 the coefficient of determinations, R-square of 0.3011 indicates that the variables considered in the model accounts for 30.11% changes in dividend yield, while the remaining 69.89% of the changes are as a result of other variables not addressed by this study. The general level of significance of 0.0002 indicates that, the result is highly significant.

The result of both OLS and GLS(Random-Effects) shows that there is significance negative effect of effective income tax rate on dividend yield at 1%.This result suggest that an increase in corporate income tax decreases dividend yield as sampled companies. While Firm Size shows a significant negative effect on dividend yield at 1% level of significance. This result also suggest that an increase in assets of firms can lead to decrease in dividend yield, as more financial resources will be channeled towards purchases of more assets for the company. However, Leverage has positive but insignificant relationship dividend yield of the sampled conglomerates companies in Nigeria. This suggests that whether a company is levered or not, does not affect the dividend yield.

Effective income tax rate shows an inverse relationship with dividend yield. This indicates that an increase in effective income tax rate cause about 1% decrease in dividend yield of the sample conglomerate companies in Nigeria. This result is in line with Brennan (1970), Masulis and Trueman (1988) and Wu (1996) who stipulated that taxes affect corporate dividend policy. Also, the result of Uwuigbe and Olusegun (2013); Odia and Agiedu (2010) who found positive significant relationship between the two construct. Therefore, the study fails to reject the null hypothesis that corporate income tax has no significant effect on dividend policy of sampled conglomerate company in Nigeria. This result implies that an attempt to increase the income tax rate of the sampled firms can cause a dividend yield cut by the companies.Thus, changes in corporate dividend policywould be anticipated when government changes its income tax policy. Leverage showsinsignificant effect on dividend yieldwhich means that leverage does not explain changes in dividend yield of listed conglomerate companies in Nigeria. This implies that whether the companies are levered or not does not affect dividend yield. Firm size also indicates a significant negative relationship with dividend yield of sampled conglomerate companies. Indicating that, increase in assets of sampled conglomerate can lead to decrease in dividend yield, as more financial resources will be channeled towards purchases of more assets for the company. Also, the larger the firm, the more likely it is to retain cash to pay off its liabilities or for expansion purposes. This result is in line with the result of Bushra and Mirza (2015).

5. Conclusion and Recommendation

This study concludes that effective income tax rate have significant effect on dividend yield, thuscorporate income tax can be significant determinant of dividend policy making in sampled companies in Nigeria. This implies an increase in corporate income tax decreases dividend yield as such each increase in effective income tax rate cause about 1% decrease in dividend yield in conglomerate companies in Nigeria. Also, firm size have significance effect on dividend yield which suggest that increase in assets of sampled conglomerate can lead to decrease in dividend yield, as more financial resources will be channeled towards purchases of more assets for the company. However, Leverage have insignificant effect on dividend yield which means leverage does not determine changes in dividend yield of listed conglomerate companies in Nigeria.

It's therefore recommended that, sufficient clarification of some sections of tax laws specially section 19 needs to be madeby tax authorityand the national assembly, so that profits which have already been taxed and those that are specifically exempted from tax don't have to be re-taxedas this may amount to double tax and have a negative consequences on the company's decision to pay dividend.

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