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EARNINGS MANAGEMENT AND TAX AVOIDANCE OF MULTINATIONAL MANUFACTURING COMPANIES LISTED ON NIGERIAN EXCHANGE GROUP

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ABSTRACT

The main objective of the study is to ascertain the effect of earnings management on tax avoidance of Multinational Manufacturing Companies in Nigeria. The study specifically ascertains the effect of discretionary accruals on effective tax rate and the book-tax differences of Multinational Manufacturing Companies. The study adopted the ex post facto research design. The final sample comprised of ten (10) multinational manufacturing Companies based on data availability during the study period, 2012-2024. The data were analyzed using the Panel Estimated Generalized Least Squares (EGLS) technique. The results revealed that discretionary accruals have a positive and significant effect on effective tax rate and on book-tax differences. In conclusion, the study submits that earnings management has a significant effect on tax avoidance of listed multinational manufacturing companies in Nigeria at 5% level of significance. The study recommended that the Federal Inland Revenue Service (FIRS) should enhance its capacity to detect and analyze accrual-based earnings manipulation by strengthening forensic tax audits and integrating accrual quality assessments into tax risk profiling tools; Financial Reporting Council of Nigeria (FRCN) should enforce stricter oversight on earnings management practices by promoting improved disclosure requirements and reviewing the consistency of firms' reported earnings with underlying economic activities.

Key words: *Book-Tax Differences, Discretionary Accruals, Earnings Management, Effective Tax Rate, Tax Avoidance.*

INTRODUCTION

The government of any country cannot operate without revenue. So, they impose mandatory levies on individuals and companies in the name of tax (Riri & Muhamad, 2024). Government impose taxes on citizens and businesses to raise revenue (Astri, Nera, & Cahyadi, 2023). Tax is the primary source of funding for the survival of the state and nation, but companies or individual taxpayers see them as a burden or expense that can reduce the company's net income (Alsaadi, 2020; Tabitha, Jullie, & Priscilia, 2023). On the company side, tax is a factor

that is considered a burden that affects the survival of the company. Meanwhile, on the tax authorities' side, tax is one of the sources of state revenue that is used for the benefit of the state and the prosperity of the people (Marlinda, Titisari & Masitoh, 2020). This situation creates a conflict of interest between the tax authorities and companies (Mukhtaruddin, Jerikho, & Umi, 2024). Companies, acting as agents, aim to reduce tax payments, while tax authorities, acting as the principal, seek the highest possible tax revenue from taxpayers (Olivia & Dwimulyani, 2019). The government wants substantial tax revenues, while companies want small tax payments (Tabitha, Jullie, & Priscilia, 2023). Therefore, due to differences in the interests of corporate taxpayers and tax authorities, management tend to look for ways to avoid compliance and minimize their tax payments (Diantari & Ulupui, 2016; Driya & Etty. 2023; Tabitha, Jullie, & Priscilia, 2023; Fitriani, & Nindah, 2022). One of the ways that companies can do this is by doing tax avoidance (Rani, Susetyo, & Fuadah, 2018). Tax avoidance is a legal effort made by companies to reduce tax obligations by exploiting loopholes in tax regulations (Drake, Lusch, & Stekelberg, 2019). Tax avoidance means paying as little tax as possible while still staying on the right side of the law (Vivek, 2025). Tax avoidance actions are carried out with the aim of reducing, avoiding, minimizing or lightening the tax burden (Marlinda, Titisari & Masitoh, 2020).

One of the tax avoidance methods used by companies is to control the level of company earnings (Kezia & Juniati, 2023). This attempt or act is referred to as earnings management (Zhang & Abraham, 2020). Earning management is the act of manipulating the company's earnings. It is the process of taking deliberate steps within the constraints of generally accepted accounting principles to bring about desired level of reported earnings (Swai, 2016). Earnings management can also be the systematic misrepresentation of the true income and assets of corporations or other organizations (Omoye & Eriki, 2014). Earnings management is often used to carry out tax avoidance, especially through accrual manipulation (Siska, Nursida & Astuti, 2024; Indriani & Ramli, 2024). Accruals are the most important earnings management instruments that are used by managers to fluctuate reported income. This is because they are components of earnings that are not reflected in current cash flows, and a great deal of managerial discretion goes into their construction (Bergstresser & Phillippon 2006). Managers use discretionary accruals to manipulate earnings because discretionary accruals can easily be exploited by managers, and also because they are derived from adoption of accounting practices that are outside the rules in the preparation and presentation of financial information to achieve a desired objective ((Zhang & Abraham, 2020; Apollos,

Jerry, & Olajumoke, 2019). Earnings management allows companies to organize financial statements to achieve certain goals, such as attracting investors or reducing the tax burden (Makkatul & Lucky, 2024). Through the use of earnings management, Companies report high accounting profits to shareholders as well as lower taxable income to the taxing authority so that the amount of tax burden borne by the company is low (Frank, Lynch, & Rego, 2009).

From the reviewed literatures, (and to the best of our knowledge), the effect of earnings management on tax avoidance using book-tax differences (BTDs) of firms in the manufacturing sector has not been sufficiently examined in Nigeria. So, there is need for further research to examine its connection with earnings management. Again the fiscal year of this study was extended to 2024 contrary to prior studies in Nigeria whose financial period ended in 2023. This created a gap in literature which this study filled. The study is therefore set out to tackle the issues raised above in order to ascertain the effect of earnings management on tax avoidance of Listed Multinational Manufacturing Companies in Nigeria.

Objectives

The main objective of the study is to ascertain the effect of earnings management on tax avoidance of Listed Multinational Manufacturing Companies in Nigeria. The specific objectives of the study are to:

1. ascertain the effect of discretionary accruals on effective tax rate of Listed Multinational Manufacturing Companies in Nigeria.
2. examine the effect of discretionary accruals on book-tax differences of Listed Multinational Manufacturing Companies in Nigeria.

LITERATURE REVIEW

Earnings Management

Earnings management is altering a company's earnings to make financial statements appear better than the real reports (Abraham, Zhang, Joseph, Agyemang & Ofori, 2021). Earnings management (EM) was described by Swai (2016) as the process of taking deliberate steps within the constraints of generally accepted accounting principles to bring about desired level of reported earnings. According to Ali, Butt, and Tariq (2011), earnings management refers to the use of accounting knowledge to influence the reported figures, while remaining within the jurisdiction of accounting rules and laws, so that instead of showing the actual performance or position of the company, they show or reflect what the management wants to

tell the stakeholders. The practice is commonly used by managers to accomplish their individual and corporate goals (Cohen & Zarowin, 2010; Roychowdhury, 2006; Zang, 2012; Omar, Rahman, Danbatta & sulaiman, 2014).

Tax Avoidance

There is no universally accepted definition of corporate tax avoidance in the literature (Annuar, Salihu, & Obid, 2014; Hanlon & Heitzman, 2010). Terms such as "Tax Planning", "Aggressive Tax Planning" and "Abusive Tax Planning" are common in the literature. According to Andre and Murtanto (2024) another term that is often used to express tax avoidance is aggressive tax planning. Tax avoidance is a deliberate effort by the company to minimize the tax to be paid and increase the company's cash flow (Siboro & Santoso, 2021). According to Bianca and Einde (2024) tax avoidance refers to companies' efforts to avoid paying as much tax as possible by taking advantage of loopholes in applicable tax regulations. The main goal of practicing tax avoidance is to minimize one's tax liability (Driya & Etty, 2023). For the purpose of this study, effective tax rate (ETR) and book-tax differences (BTD) are used as measures of tax avoidance.

H_{o1}: *Discretionary accruals has no significant effect on effective tax rate of Listed Multinational Manufacturing Companies in Nigeria.*

H_{o2}: *Discretionary accruals have no significant effect on book-tax differences of Listed Multinational Manufacturing Companies in Nigeria.*

Theoretical Review

Agency Theory

The separation between owners and managers creates an agency relationship (Olotu, Salawu, Adegbie, & Akinwunmi, 2019). According to Ireland, Hoskisson and Hitt (2011) an agency relationship exists when one or more persons (the principal or principals) hire another person or persons (the agent or agents) as decision-making specialists to perform a service.

Agency theory explains how the behavior of related parties in companies that have different interests can cause conflicts of interest (Sahara, 2022). On the company side, tax is a factor that is considered a burden that affects the survival of the company. Meanwhile, on the tax authorities' side, tax is one of the sources of state revenue that is used for the benefit of the state and the prosperity of the people (Marlinda, Titisari & Masitoh, 2020). The government (principal) wants large tax revenues, while companies (agents) want to pay taxes to a

minimum (Aulia & Purwasih, 2022). This situation creates a conflict of interest between the tax authorities and companies (Mukhtaruddin, Jerikho, & Umi, 2024). The theory therefore explains that the motivation for minimizing tax payments by companies through the practice of earnings management is rooted in the conflict of interest between managers and the government.

Empirical Review

Ketut, Thom, and Harry (2023) examined the effect of earning management and fixed asset intensity on tax management with management compensation as intervening variable in Indonesia. The data source used in this study is secondary data in the form of published company financial reports. The population of the study consisted of 76 primary consumer goods manufacturing companies listed on the Indonesia Stock Exchange (IDX) for the 2017-2021 period. Purposive sampling technique was used to determine a sample of 64 companies or 120 research sample data. The analytical method used in this study is the panel data linear regression method. The results show that partially earnings management has a significant effect on tax management, but asset intensity still has no effect on management tax. And simultaneously earnings management and fixed asset intensity affect tax management. Management compensation can mediate the effect of earnings management on tax management, but management compensation cannot mediate the effect of fixed asset intensity on tax management.

Delgado, Elena, Roberto, Manuel, and Antonio (2023) examined tax avoidance and earnings management: a neural network approach for the largest European economies. The sample size comprised largest five (5) European Union economies by using artifcial neural network regressions. Compustat data was analyzed for Germany, the United Kingdom, France, Italy, and Spain for the 2006–2015 period, focusing on discretionary accruals. Tax avoidance was measured by efective tax rate (ETR) and book-tax diferences (BTD). The results indicate the presence of nonlinear patterns and a positive, statistically signifcant relationship between discretionary accruals and both ETR indicators implying that when companies resort to earnings management, a larger taxable income and thus higher ETR and lesser tax avoidance would ensue.

Karjalainen, Kasanen, Kinnunen, and Niskanen (2023) analyzed the relationship between tax avoidance and earnings management in Finland. A panel data on all Finnish dividend-paying

SMEs companies spanning the period 2006 to 2010 was used in the study. Pooled ordinary least square (OLS) was adopted for the study. The results of the study indicate that tax avoidance represented by cash effective tax rate was positively significant with discretionary accrual (DACC) which is a proxy for earnings management. This means that tax avoidance is negatively related to earnings management and so managers' opportunistic behavior in reporting of financial and taxable income is reduced.

Ndum (2022) examined the effect of corporate tax avoidance on earnings management in Nigerian deposit money banks. Ex-Post Facto research design was adopted for the study. The study was based on a sample of nine (9) deposit money banks with international authorization out of the twenty-two (22) banks Listed on the Nigerian Stock Exchange from 2010-2020. The hypothesis was tested with Ordinary Least Square with aid of E-view 9.0 to arrive at a logical conclusion. The study revealed that amortization has significant effect on Earnings Management of deposit money banks in Nigeria. Based on the findings, the researcher recommended that bank management should be aware of the fundamentals of amortization in order to determine how it affects their business and how they might benefit from expense deductions.

Yeye, and Egbunike (2021) examine the effect of discretionary accruals on corporate tax avoidance of Multinational Corporations (MNCs) in Nigeria. Ex post facto research design was adopted for the study. The sample of the study was fifty (50) Multinational Corporations (MNCs). Data for the study were analysed using multiple linear regression techniques. Tax avoidance was proxied by book-tax differences and effective tax rate. The results showed a negative non- significant effect of discretionary accruals on book-tax differences, and a positive non-significant effect of discretionary accruals on the effective tax rate. The study concludes that the accruals quality is related to tax avoidance via transfer price manipulation of MNCs in Nigeria. Based on this, it is recommended that the FIRS should equip its personnel through effective training to effectively deal with intra-firm trade by MNCs.

MATERIALS AND METHOD

The *ex post facto* research design was adopted in this study. Secondary data, precisely annual reports and accounts of Multinational manufacturing companies listed on the Nigeria Exchange Group for the period 2012–2024 were solely deployed. Information from the financial statements were obtained in respect of the following variables: Discretionary

accruals (DA); Effective tax rate (ETR); Book-tax differences; Leverage (LEV), Firm size (FS); Firm age (FA). The population of this study consists of eleven (11) listed Multinational manufacturing Companies on the Nigeria Exchange (NGX) Group as at the end of 2024 financial year. Ten (10) Multinational manufacturing companies were sampled using purposive sampling technique, based on availability of data needed for the study. The study employed both descriptive and inferential statistical techniques to analyse the data. Descriptive statistic comprises measures such as the mean, median, standard deviation, minimum, and maximum values, Skewness, Kurtosis statistics. The hypotheses were tested using panel estimated generalised least squares. It was used to predict the value of a variable based on the value of the other variables. Multiple regression was used to validate the hypotheses. The modified Jones model, as proposed by Dechow, Sloan, and Sweeney (1995) was used to identify earnings management by calculating discretionary accruals as a proxy for earnings management.

Model Specification

$ETR_{(i,t)} = \alpha_0 + \beta_1 DA_{(i,t)} + \beta_2 Leverage_{(i,t)} + \beta_3 FS_{(i,t)} + \beta_4 FA_{(i,t)} + \mu$…….. Eqn 1.

$BTD_{(i,t)} = \alpha_0 + \beta_1 DA_{(i,t)} + \beta_2 Leverage_{(i,t)} + \beta_3 FS_{(i,t)} + \beta_4 FA_{(i,t)} + \mu$…… Eqn 2.

Where:

$ETR_{(i,t)}$ = Effective Tax Rate of firm í at time t

$DA_{(i,t)}$ = Discretionary Accruals of firm í at time t

$BTD_{(i,t)}$ = Book-tax differences of firm í at time t

α_O = Constant

$\beta_1 - \beta_4$ = Coefficients of the regression

$Leverage_{(i,t)}$ = Leverage of firm í at time t

$FS_{(i,t)}$ = Firm Size of firm í at time t

$FA_{(i,t)}$ = Firm Age of firm í at time t

μ = Error term

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RESULT AND DISCUSSIONS

Test of Hypotheses

Hypothesis One

H_{o1}: Discretionary accruals has no significant effect on effective tax rate of Listed Multinational Manufacturing Companies in Nigeria.

H_{i1}: Discretionary accruals has significant effect on effective tax rate of Listed Multinational Manufacturing Companies in Nigeria.

Table 1; Panel estimated generalised least squares testing the effect of DA on ETR

Dependent Variable: ETR
Method: Panel EGLS (Cross-section SUR)
Date: 06/25/25 Time: 16:18
Sample: 2012 2024
Periods included: 13
Cross-sections included: 10
Total panel (balanced) observations: 130
Linear estimation after one-step weighting matrix

Variable	Coefficient	Std. Error	t-Statistic	Prob.
DA	0.199935	0.034989	5.714156	0.0000
LEV	-0.007133	0.000673	-10.59747	0.0000
FS	-0.083344	0.006384	-13.05491	0.0000
AGE	-0.003687	0.000545	-6.760675	0.0000
C	1.013936	0.057562	17.61463	0.0000

	Weighted Statistics		
R-squared	0.765492	Mean dependent var	3.608189
Adjusted R-squared	0.757988	S.D. dependent var	5.707194
S.E. of regression	1.001182	Sum squared resid	125.2958
F-statistic	102.0076	Durbin-Watson stat	1.758126
Prob(F-statistic)	0.000000		

Source: Eviews 10 Output (2025)

Table 1 evaluates the effect of discretionary accruals (DA) on effective tax rate (ETR). The overall model is statistically valid as indicated by the F-statistic probability of 0.0000, which means the explanatory variables jointly have a statistically significant effect on ETR at the 5% level. The adjusted R-squared of 0.7580 implies that approximately 76% of the variation in ETR among listed multinational manufacturing companies in Nigeria is explained by the model. The Durbin-Watson statistic (1.76) falls within the acceptable range, indicating no serious autocorrelation in the residuals. The constant term (1.0139, p = 0.0000) is positive and significant, implying that when all predictors are zero, the baseline ETR would be 101.39%, a theoretical value likely reflecting the fixed effects of omitted firm-specific attributes.

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The coefficient of Discretionary Accruals (DA) is 0.1999 (p = 0.0000). This means that for every unit increase in DA, the effective tax rate increases by approximately 20%, all else being equal. The effect is statistically significant at the 5% level. This suggests that when multinational manufacturing firms engage in greater earnings management using discretionary accruals, their tax burden increases, possibly due to tax authorities detecting and adjusting such accrual manipulations. Other control variables—leverage (LEV), firm size (FS), and firm age (AGE)—all have negative and significant effects on ETR, implying that more indebted, larger, or older firms tend to have lower effective tax rates, potentially due to tax planning advantages or experience.

This result can be explained by the possibility that aggressive accrual practices trigger scrutiny from tax authorities, leading to adjustments that nullify tax benefits and, in turn, increase tax liabilities. It also indicates that such manipulations are more focused on meeting financial reporting objectives (like inflating income) than minimizing taxable income, which ultimately results in higher tax expense relative to pre-tax earnings.

Hypothesis Two

H_{o2}: Discretionary accruals have no significant effect on book-tax differences of Listed Multinational Manufacturing Companies in Nigeria.

H_{i2}: Discretionary accruals have significant effect on book-tax differences of Listed Multinational Manufacturing Companies in Nigeria.

Table 2 Panel estimated generalised least squares testing the effect of DA on BTD

Dependent Variable: BTD
Method: Panel EGLS (Cross-section SUR)
Date: 06/25/25 Time: 16:19
Sample: 2012 2024
Periods included: 13
Cross-sections included: 10
Total panel (balanced) observations: 130
Linear estimation after one-step weighting matrix

Variable	Coefficient	Std. Error	t-Statistic	Prob.
DA	0.077153	0.009301	8.294974	0.0000
LEV	0.002648	4.48E-05	59.09697	0.0000
FS	0.028751	0.002589	11.10425	0.0000
AGE	-0.001351	0.000122	-11.08422	0.0000
C	-0.119032	0.021392	-5.564355	0.0000

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Weighted Statistics

R-squared	0.974054	Mean dependent var	-0.456427
Adjusted R-squared	0.973224	S.D. dependent var	8.120617
S.E. of regression	1.006191	Sum squared resid	126.5526
F-statistic	1173.179	Durbin-Watson stat	1.818249
Prob(F-statistic)	0.000000		

Source: Eviews 10 Output (2025)

Table 2 tests the effect of discretionary accruals (DA) on book-tax differences (BTD). The model is statistically valid with a p-value of the F-statistic at 0.0000, and the adjusted R-squared of 0.9732 indicates that over 97% of the variability in BTD is explained by the model—a very high explanatory power. The Durbin-Watson stat (1.82) confirms minimal autocorrelation. The intercept is negative (-0.1190, p = 0.0000), indicating that when all predictors are zero, the BTD would be slightly negative, reflecting a small tax excess over book income. Discretionary accruals have a positive coefficient of 0.0772 (p = 0.0000), suggesting that a one-unit increase in earnings management increases BTD by approximately 7.7%. This implies that firms engaging more in accrual-based earnings management are likely to report higher discrepancies between book and tax income, supporting the notion that DA is a mechanism for tax avoidance through income shifting. All control variables also have significant effects: leverage and firm size increase BTD, while firm age reduces it.

When firms manipulate earnings through discretionary accruals, they are essentially creating artificial differences between what is reported to shareholders (book income) and what is declared to tax authorities (taxable income). This practice results in widened book-tax gaps, which may be indicative of tax avoidance strategies or aggressive earnings smoothing that leads to inflated accounting income while minimizing taxable income.

CONCLUSION AND RECOMMENDATIONS

This study assessed the effect of earnings management on tax avoidance of Listed Multinational Manufacturing Companies in Nigeria. The study obtained data from annual reports, account and publications from the Nigerian Exchange Group for the Multinational manufacturing Companies that operated during 2012-2024. In addition, the correlation of specific earnings management such as discretionary accrual and dependent variable measures such as effective tax rate and book-tax differences were assessed. To determine the relationship that exists amongst the variables and the effect thereof, pearson correlation coefficient and panel estimated generalised least squares were employed. This study revealed that discretionary accruals have a positive and significant effect on effective tax rate and on

book-tax differences. In conclusion, the study submits that earnings management has a significant effect on tax avoidance of Listed Multinational Manufacturing Companies in Nigeria at 5% level of significance.

Based on the study findings, the following were recommended:

a. Federal Inland Revenue Service (FIRS) should enhance its capacity to detect and analyze accrual-based earnings manipulation by strengthening forensic tax audits and integrating accrual quality assessments into tax risk profiling tools.
b. Financial Reporting Council of Nigeria (FRCN) should enforce stricter oversight on earnings management practices by promoting improved disclosure requirements and reviewing the consistency of firms' reported earnings with underlying economic activities.

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