

UNIVERSITY OF KWAZULU-NATAL

**The impact of Tax Planning and Corporate Governance on Firms'
Value in East Africa**

Alfred James Kimea

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**UNIVERSITY OF
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School of Accounting, Economics and Finance

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The impact of Tax Planning and Corporate Governance on Firms' Value in East Africa

By

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A Thesis Submitted in Fulfilment of the Requirements of Doctor of Philosophy

in Accounting

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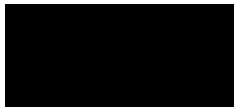
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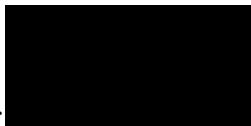


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Tax Planning, Corporate Governance and Firm Value in East Africa

Submitted in fulfilment of the requirements for the degree of
Doctor of Philosophy
in the Accounting at the University of KwaZulu-Natal.

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DEDICATION

I dedicate this thesis to my family, especially my late mother.

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In the Name of God, the merciful, the compassionate: *“All praise and thanks to the most Gracious and Merciful God.”* I am highly grateful to God for His blessings that continue to flow into my life and for giving me strength, patience, courage and ability to complete this work against all odds. Then, with great pleasure, I would like to acknowledge the sincere help and generous support made by many individuals during this long journey. Undertaking this PhD has been a truly life-changing experience for me, and it would not have been possible without the support and guidance that I received from many people. My deepest gratitude and heartfelt thanks go to my supervisor at the University of KwaZulu-Natal, Prof. Msizi Mkhize. I acknowledge the enormous intellectual help and encouragement you provided me.

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1. Kimea, A. and Mkhize, M. (2019). Institutional Investors, Corporate Governance and Firm Performance: Evidence from an Emerging Economy. *Biennial Conference of the Economic Society of South Africa*, 3 - 5 Sept 2019, Johannesburg

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ABSTRACT

The study investigated the impact of tax planning on the value of listed firms in East African countries (EACs). Further, it examined the moderating influence of corporate governance on the relationship between tax planning and firm value. The data collected involved 99 firms listed on the capital markets of three EACs: Tanzania, Kenya and Uganda. The study used unbalanced panel data reflecting twelve years from 2008 to 2019. The research had four separate objectives. Regarding the first objective, the empirical findings revealed the existence of tax planning activities amongst the firms listed in EACs. The results showed a gradual increase in the tax planning activities in EACs during the twelve years represented. The study's findings concerning the second objective showed that firm size, profitability, and age significantly influenced the level of tax planning in EACs. Moreover, these results suggested that large, more profitable, and older firms were less tax aggressive. Regarding corporate governance mechanisms, the findings were that large board size, an increase in directors' compensations and ownership concentration increased the tax planning aggressiveness of the firms. The results further demonstrated that specific institutional arrangements in a country, such as management quality, culture, regulations, ethics and auditing quality, significantly impacted the firms' tax planning activities. Regarding the third objective, the findings showed that tax planning negatively impacted firm value. Lastly, concerning the fourth objective, the results established that the strength of corporate governance had a significant moderating influence on the relationship between tax planning and firm value. The study concludes that firms that engage in better tax planning practices can generate higher firm value when good corporate governance systems are in place. The researcher recommends higher transparency in firms' tax-planning activities because they can potentially increase a firm's value. The study contributes to knowledge since there is a general dearth of published research studies that estimate the associations between tax planning, corporate governance and firm value in emerging economies. This thesis makes several recommendations from the study concerning tax planning activities to guide governments, managers, practitioners and shareholders of firms in emerging economies.

KEYWORDS: Tax planning; tax avoidance, corporate governance; agency theory; political cost theory; firm value; East Africa Countries

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CHAPTER ONE

INTRODUCTION AND OVERVIEW

1.0 Introduction

Firms are increasingly looking for ways to reduce costs and maintain profit for investment opportunities and increase their value. Tax planning, an important corporate strategy in today's business environment (Hanlon & Heitzman, 2010), is one of the ways to achieve these goals (Wahab & Shaipah, 2010). However, it takes up a great deal of a management's time and resources, as well as eroding a significant percentage of a firm's income. In this case, the question is whether corporate tax planning leads to an increase in firm value. The predominant assumption of shareholders is that it does because taxes represent a significant burden to firms. Therefore, tax planning, which lowers the corporate tax burden, is believed to increase firm value (Desai & Dharmapala, 2009a; Kirkpatrick & Radicic, 2020). Nevertheless, Desai and Dharmapala (2009a) contend that tax planning is not costless. Several costs and risks are associated with tax planning, which may include potential punishments from revenue authorities, such as penalties and fines. Apart from these, there are tax planning implementation costs, legal fees and reputation loss, which could harm firm value.

Similarly, agency theorists argue that due to agency costs resulting from shareholders-management relationships, management may not align tax-planning decisions with the interests of shareholders (Dyreng et al., 2010; Putra, Syah & Sriwedari, 2018). This is so because managers may have personal incentives to implement tax planning in ways that are different from what shareholders would prefer. Accordingly, Campbell et al. (2020) emphasise that tax planning is a complex and opaque activity that may create opportunities for managerial diversion of rents (a business arrangement to benefit management at the expense of shareholders) and could negatively affect shareholder value.

However, some empirical studies such as those of Desai et al. (2006), Hidayat and Yuliah (2018) and Nugroho and Agustia (2018) claim that the risks and costs of tax planning may be reduced by corporate governance. These studies maintain that corporate governance mechanisms of firms occupy an essential role in monitoring and shaping managerial behaviours. In the context of tax

planning, the implementation of favourable governance mechanisms may reduce the risk of misappropriation by managers, who would thus be more likely to engage in tax planning activities to enhance the wealth of their shareholders. This implies that the importance of tax planning depends on whether the benefits outweigh the costs. Moreover, the benefits depend on the strength of the firms' governance (Dyrenge et al., 2010).

However, there is a dearth of studies investigating the relationships between tax planning, corporate governance and firm value in emerging economies. Findings from studies (see Guenther, Matsunaga & Williams, 2016; Putra et al., 2018; Chen et al., 2019; Zolotoy et al., 2020) that examine the relationship between tax planning and firm value are divergent and inconclusive. In addition, they focus mainly on firms in particular countries, which make the generalisation of findings to emerging economies difficult and sometimes impossible. Therefore, the study described in this thesis not only investigated the impact of tax planning on firm value but also examined whether corporate governance moderates the relationship between tax planning and firm value by considering firms from three selected emerging market countries.

The rest of this chapter provides the background of the study; the statement of the problem; the context of the study; the research aim, objectives and questions; the justification and significance of the study; an overview of the research methodology; and the structure of the study.

1.1 Background of the Study

Owing to its impact and significance, corporate tax planning has recently attracted the attention of researchers, governments, the public and international bodies. Tax planning is defined as a strategic approach that firms undertake to reduce their tax liabilities by implementing a broad range of activities, mechanisms and methods, whilst staying within the bounds of what is legally acceptable (Chen et al., 2018; Francis, Neuman & Newton, 2019; Tang, 2019). The terms "tax planning", "tax avoidance", "tax aggressiveness" and "tax management" tend to be used interchangeably in the literature (Hanlon & Heitzman, 2010).

Tax planning activities by multinational companies (MNCs) have occupied headlines, particularly since the global financial crisis of 2008 when the conduct of the private sector came under increased scrutiny. For instance, companies such as Starbucks, HSBC, Google, Barclay's Bank and

Amazon have been accused on many occasions of corporate tax avoidance (Sikka, 2018). This suggests that corporate tax avoidance has damaging effects in nearly all countries, but the impact of tax avoidance on developing nations is most acute (Sikka, 2018). Sikka (2018) suggests that developing countries are severely affected by tax planning because they are most in need of predictable sources of tax revenue to invest in essential areas, such as healthcare, education and infrastructure. Indeed, since aggressive corporate tax practices prevent governments from accessing their major resources, they have received growing attention from policymakers and academics worldwide (Chen et al., 2010; Armstrong et al., 2019). For example, Cobham and Janský (2018) report that global revenue losses through tax planning activities are estimated to be \$500 billion annually. Similarly, Ogembo (2019) estimate global revenue losses through tax planning to be US\$650 billion annually. This shows that various governments, especially those in developing countries, are denied the needed resources for development and other activities.

Fuest, Hebous and Riedel (2013) in a related study observed that tax planning/avoidance has a disproportionately large effect on developing economies, where it is estimated that revenue loss is \$160 billion per year. The authors posit that the social and economic costs experienced by developing economies due to tax planning are exasperated by two principal factors. Firstly, in developing economies, tax revenue accounts for a greater share of state income than in advanced economies. Secondly, the affected governments generally lack the legislative and administrative resources to tackle the issue.” Likewise, Johannesen et al. (2016) posit that countries most affected by tax planning are developing nations, where it is estimated that around one-third of total revenue loss is due to tax planning. Johannesen et al. (2016) put forward possible reasons for the high concentration of tax avoidance in developing nations. Firstly, the authors suggest that developing countries are primarily dependent on revenue collection from informal sectors, and therefore lack the capacity to tax large companies, particularly multinational companies (MNCs). Secondly, the authors point out that developing nations lack sophisticated anti-avoidance rules. Pratama (2018) maintains that sophisticated anti-avoidance rules have reduced the problem, but such rules rarely exist in less developed nations. Lastly, weak governance, poor law enforcement and a lack of political accountability may facilitate tax avoidance in developing countries.

The empirical evidence suggests that, like most developing nations, EACs have also been significantly affected by tax avoidance activities over the past few years. For instance, a study by

Cobham and Janský (2018) revealed that in 2013, EACs lost US \$2.69 billion because of tax avoidance: Kenya lost US \$1.22 billion; Tanzania lost US \$0.86 billion; and Uganda lost US \$0.61 billion. These figures represent approximately three percent of the gross domestic product (GDP) for each country. The authors maintained that currently, tax avoidance in EACs is on the increase. For instance, Cobham and Janský (2018) report that in the past three years, the Court of Appeal of Kenya adjudicated 122 tax avoidance cases, 26 in 2018, 43 in 2017 and 53 in 2016. A similar situation exists in Uganda and Tanzania. The Tanzania Revenue Authority (TRA), for example, reported 21 decided cases of corporate tax avoidance in 2017 that were adjudicated by the Court of Appeal of Tanzania during the past ten years.

As taxation incurs high costs to firms and shareholders (Owen & Htun, 2018), managers take action to reduce their tax liabilities (Gaaya et al., 2017). Several studies support the claim that corporate taxpayers avoid taxes because of the significant costs of taxes to firms and shareholders (Hutchens et al., 2019; Steinmüller et al., 2019). Most governments worldwide, including EACs, levy corporate income tax at a rate ranging from 20% to 35%, with an average of 28.5% (Steinmüller et al., 2019). In other words, they take almost one-third of a firm's pre-tax profits, which discourages innovation and investment (Heitzman & Ogneva, 2019) because the large amount of money paid to governments in the form of corporate income taxes, property taxes and withholding taxes, for example, means that firms are unable to maintain or expand their operations.

Since taxes transfer a significant proportion of a firm's pre-tax earnings to the government, which reduces the after-tax distributable profits available to shareholders and affects firm value and growth (Chen et al., 2010), companies practise tax planning. Hanlon and Heitzman (2010) define tax planning as a firm's strategy to reduce its tax burden by shifting profits to lower-tax rates or to countries that do not levy corporate-tax (Cobham & Janský, 2018). Corporate tax planning has been the most common strategy followed by firms to maximise profits and is perceived as improving firm value, thus benefitting shareholders (Desai & Dharmapala, 2006). Desai and Dharmapala (2009b) and Armstrong et al. (2012) support this notion of tax planning benefitting shareholders, as it transfers resources from the state to them.

However, some empirical studies such as Salawu (2017), Hoseini et al. (2019) and Hutchens et al. (2019) have not provided conclusive evidence to prove that it is not worthwhile for companies to

invest in tax planning that might, in fact, affect firm value negatively, although the general consensus is that since corporate tax planning reduces the tax burden, it will lead to increase after-tax returns. There is a large body of literature that suggests that corporate tax planning is beneficial to firms and has a positive impact on their value. For instance, Hoseini et al. (2019) posit that because corporate tax planning reduces the amount of taxes transferred from firms to the government, which is perceived as a value-enhancing activity by shareholders. Correspondingly, Desai and Dharmapala (2009a) argue that shareholders perceive tax planning as the vehicle, which transfers resources from the state to shareholders. Likewise, Salawu (2017) finds a positive impact of tax planning on firm value and maintains that it creates value for shareholders in a strong, legal, institutional and corporate governance environment that protects investors from expropriation and self-seeking managers. In fact, Wilde and Wilson (2018) suggest that through tax planning, firms reduce the amount of taxes payable to the government, which increases net cash flows for further investments, debt obligations or distributing profits to investors. Therefore, it is generally expected that shareholders would prefer reduced tax liabilities, and thus firms exhibit tax aggressiveness.

From the preceding discussion, it is evident that tax-planning strategies reduce the tax burden and lead to a greater after-tax cash flow. However, it is associated with uncertain future outcomes, imposing high costs on firms (Hutchens et al., 2019). In fact, Guenther, Matsunaga, and Williams (2016) describe certain and uncertain tax planning strategies and their likely consequences. According to the authors, certain tax planning strategies, such as “tax treatment of capital expenditures”, is unlikely to be challenged by tax authorities. In contrast, uncertain tax planning strategies have highly uncertain future outcomes (for example, cross-border income shifting via intellectual property and transfer pricing schemes). Uncertain tax planning strategies are highly likely to be challenged by tax authorities. Thus, tax planning can impose additional costs if a firm is audited by revenue authorities. In this case, a firm can experience high costs because of an audit and may end up paying additional taxes, interest and penalties.

Armstrong et al. (2015) argue that if revenue authorities detect tax aggressiveness through an audit or an investigation, firms may be fined and receive penalties that may significantly affect them. Nevertheless, as argued by Hoopes et al. (2012), firms are still understandably eager to invest in tax planning to lower their taxes to benefit shareholders as the residual claimants. The authors advise firms to consider the costs stemming from tax aggressiveness, including the fines, interest,

and penalties that revenue authorities can charge for under-reporting. Chen et al. (2019) maintain that firms that engage in extensive tax planning are more likely to participate in the types of transactions and activities that could be affected by future tax policy moves. As a result, they are exposed to the uncertainty of tax policies, which can lead to higher systematic risks.

Huseynov et al. (2017) examined the risks and costs associated with tax planning and concluded that it is also associated with the loss of a firm's reputation. This is an essential factor to consider when deciding whether to implement tax planning or not (Graham et al., 2013), as tax aggressiveness can lead to the organisational legitimacy of a firm being questioned by the general public (Preuss, 2010). In fact, society expects legitimate firms to be socially responsible by paying taxes to the government, thereby contributing to the social and economic development of a country (Hoopes et al., 2018). Therefore, tax planning may threaten a firm value and existence.

Tax planning literature often discusses the problem of the role of managers, who pursue their self-interests under the guise of tax planning because of agency problems created by information asymmetry (Desai & Dharmapala, 2009a; Ayers et al., 2018; Wang et al., 2020). Various authors argue that tax planning is a risky investment and because of agency conflict, management may over- or under-invest what shareholders would prefer. In fact, Armstrong et al. (2015) suggest that agency costs associated with tax planning might offset the benefits of tax saving, thereby destroying firm value. The existence of agency costs in tax planning has been documented by several studies that provide empirical evidence that corporate tax aggressiveness negatively affects firm value (Hanlon & Slemrod, 2009; Kim et al., 2011; Putra et al., 2018; Zolotoy et al., 2020).

Desai and Dharmapala (2009a), who support the notion that tax planning may negatively affect firm value, propose the incorporation of the agency theory in analysing the relevance of tax planning. According to Desai et al. (2006), this theory posits that self-serving managers may use mechanisms involved in tax planning to conceal managerial rent extraction. On a similar note, Chen et al. (2019) report that the separation of a firm's ownership and control causes information asymmetry that enables management to engage in high levels of tax aggressiveness, of which shareholders may not approve. The above studies conclude that the overall effect of tax minimisation on firm value depends on whether the costs outweigh the tax-saving benefits. Moreover, Chen et al. (2010), Hidayat and Yuliah (2018) as well as Bhagiawan and Mikhlasin

(2020) maintain that the effect of tax avoidance on firm value depends on the ability of firm governance to control managerial actions.

Some studies acknowledge that good corporate governance is a way to monitor and control the actions of managers, which reduces the risks and costs associated with tax planning (Zemzem & Ftouhi, 2013; Filatotchev et al., 2018). According to Filatotchev et al. (2018), strong corporate governance ensures that managerial decisions related to tax planning are monitored and controlled so that they align with the interests of shareholders (Nugroho & Agustia, 2018). Likewise, agency problems related to tax planning can be mitigated by good corporate governance, which reduces the information gap between management and shareholders (Hidayat & Yuliah, 2018).

A few studies, however, question the influence of corporate governance on tax planning decisions (Wahab & Shaipah, 2010; Wahab & Holland, 2012). These studies hold that there is no significant contribution by corporate governance to mitigating costs and risks associated with tax planning. Despite the debate on the influence of corporate governance on the control and monitoring of managerial decisions related to tax planning, the predominant view is that strong corporate governance is required to oversee the managers' activities.

The above discussions of the results of previous studies show clearly that the relationship between tax planning and firm value is theoretically ambiguous and still a controversial issue in the literature. In addition, it is evident that the nature of the relationship might vary from country to country, depending on their tax regulations and enforcements. The strength of a country's legal institutions, such as capital markets authorities that regulate corporate governance may influence the relationship between tax planning and firm value. Unfortunately, the exact relationship in emerging economies, in particular, is yet to be explored, and the controversy is yet to be empirically examined. Given the importance of tax planning and corporate governance in creating shareholder value and the mixed results from previous studies, there is a pressing need to examine the impact of tax planning on firm value and further investigate whether the strength of a firm's corporate governance has a moderating influence on the relationship between tax planning and firm value in EACs.

1.2 Problem Statement

Tax represents a significant source of income to the governments of every country. Particularly, in developing countries, where finances are limited, governments have relied on corporate taxes to finance their development and social activities, which means that firms are deprived of resources for investment and growth, especially since retained profits represent the most direct source of capital (Aghion et al., 2016; Marian, 2018; Handayani, 2020). In developing countries such as the EACs, an average of 30% of a firm's profits are paid to the governments as tax.

Firms have adopted tax planning as a strategy to reduce the amount of taxes paid to governments, which many argue can allow firms to save a substantial amount of money. Desai and Dharmapala (2009a), Wahab and Holland (2012) as well as Saavedra (2013) and Zhang et al., 2017 provide evidence to show that tax planning increases firm value and is value relevant (Saavedra, 2013; Chen et al., 2019; Handayani, 2020). If successfully implemented, tax planning would transfers resources from the government to shareholders (Hanlon & Heitzman, 2010), and thus results in relatively low taxes payable to the government, as well as higher after-tax returns. A number of studies maintain that shareholders also hold the view that tax planning is value relevant (Desai & Dharmapala, 2009b; Zhang et al., 2017).

Counter evidence shows that tax planning is not only futile but also serves as a major drain on a firm's resources and its management's time. Firms pay large sums of money for tax planning, but the benefits may not warrant the resources spent. According to Cooper and Nguyen (2020), the view that corporate tax planning is a transfer of resources from the state to shareholders is simplistic, given the agency problems characterising shareholder and management relationships. The authors explain that the benefit of tax planning is not apparent because of implicit agency costs. Costs and risks, such as tax planning implementation costs, additional taxes, fines, and legal fees indicate that tax planning does not always increase firm value (Bauer et al., 2020). Moreover, tax planning is not only accompanied by substantial observable costs but also unobservable costs, such as the loss of firms' reputation, which might negatively affect them (Bayar et al., 2017; Shin & Woo, 2018). Authors such as Preuss (2010) and Garg et al. (2020) hold the view that firms that practise tax planning risk attracting negative publicity, which affects their image because it is a dereliction of social responsibility and indicates that they are not contributing to the development of a nation. Moreover, because of agency problems, there is a concern that managers of firms may

try to use tax planning for their self-interests instead of those of shareholders (Putra et al., 2018; Zolotoy et al., 2020).

The conundrum of whether tax planning has any significant impact on firm value, especially in EACs, has occasioned a renewed discussion among researchers and the management of firms. In fact, concerns have been raised about how to ensure that management does not engage in actions, which are detrimental to the interests of shareholders under the umbrella of tax planning. Another school of thought claims that firms can benefit from tax planning activities only if management actions are monitored by strong corporate governance that ensures a high level of control and transparency (Kiesewetter & Manthey, 2017). However, previous studies report that corporate governance does not influence managerial decisions about tax planning (Wahab & Shaipah, 2010; Wahab & Holland, 2012). In fact, there is a paucity of evidence that corporate governance moderates the relationship between tax planning and firm value.

To date, research has investigated tax planning and its effect on firm value in developed countries and markets, mainly the United Kingdom (UK) and the United States (US) (Desai et al., 2006; Hanlon & Slemrod, 2009; Hoopes et al., 2018; Slemrod, 2004; Wahab & Shaipah, 2010; Wahab & Holland, 2012). However, studies have not researched developing countries, particularly EACs, which need investigation (Ogembo, 2019; Steinmüller et al., 2019; Thomsen & Watrin, 2018). Because of cultural, social and economic differences, findings from studies of developed countries cannot be applied to developing countries. Thus, the lack of empirical studies of developing countries and the mixed results of prior studies indicate the need for the current study, which focused on emerging markets. This study investigates the relationship between tax planning and firm value and how corporate governance influences such a relationship.

1.3 Study Context

The research focussed on emerging economies by conducting a case study of EACs, where economic growth is soaring ahead of other regions on the continent (Albagoury & Anber, 2018). East Africa is leading the continent with a GDP growth estimated at above 6% in 2018, followed by North Africa at 4.9%, West Africa at 3.3%, Central Africa at 2.2%, and Southern Africa at 1.2% (Albagoury & Anber, 2018). East Africa's economic growth was estimated to remain robust at above 6% in 2019, thus encouraging multinational firms to invest and manufacture their

products in the region. The favourable economic growth of the region motivated the researcher to investigate its tax arena and establish whether strong corporate governance exists to protect the interests of individual investors, particularly local ones.

The East African Community (EAC) is a regional intergovernmental organisation of six partner states: the Republic of Burundi, Kenya, Rwanda, South Sudan, the Republic of Uganda and the United Republic of Tanzania. However, the study considered only three countries (Kenya, the United Republic of Tanzania and the Republic of Uganda) and pooled data from firms operating in these three EACs for the analysis for two reasons. Firstly, the capital markets of these three countries are regulated by the East African Securities Exchanges Association (EASEA), which was established in 2015 to develop sustainable capital markets and to integrate capital market activities in the region. The other three countries (Burundi, Rwanda and South Sudan) were not members of EASEA during the study period. Secondly, Tanzania, Kenya, and Uganda are former colonies of the UK and countries are based on English common law. Moreover, like other African countries, corporate governance in Tanzania, Kenya and Uganda are based on the principles of the Organisation for Economic Co-operation and Development (OECD), the South African King's Report, and the Commonwealth Association for Corporate Governance (CACG) (Wanyama et al., 2013; Waweru, 2018).

Rwanda, Burundi and Southern Sudan were not included in the study sample for various reasons. Firstly, South Sudan joined the EAC in 2016, while the study period was from 2008 to 2019. Secondly, South Sudan and Burundi do not have capital markets, and the sample comprised only firms listed on capital markets. Although Rwanda has a capital market, it was excluded because it is the youngest country in East Africa, and trading only began in 2011, while the study period started in 2008. In addition, Rwanda's capital market has only seven listed firms, four of which are cross-listed Kenyan firms whose stock was primarily traded on the Nairobi Securities Exchange (NSE).

1.3.1 East African Community (EAC)

As stated above, the EAC is a regional intergovernmental organisation of six partner states: the Republic of Burundi, Kenya, Rwanda, South Sudan, the United Republic of Tanzania and the Republic of Uganda, with its headquarters in Arusha, Tanzania. The EAC is home to 172 million

citizens, over 22% of which make up the urban population. With a land area of 2.5 million square kilometres and a combined GDP of US\$ 172 billion (East African Community Statistics for 2017), the EAC has great strategic and geopolitical significance as well as prospects for the renewal and reinvigoration of the region.

The EAC's activities are governed by its Treaty, which was ratified by their founding three partner states: Kenya, Tanzania, and Uganda on 30 November 1999 and came into effect on 7 July 2000. On June 18, 2007, the Republic of Rwanda and the Republic of Burundi ratified the Treaty, becoming full members of the EAC as of July 1. The Republic of South Sudan also joined the Treaty on April 15, 2016, and on August 15, 2016, it was admitted as a full member (Bizuneh et al., 2020).

The EAC is one of the world's fastest-growing regional economic blocs and it is expanding and extending cooperation among its member states in a number of crucial areas, including the political, economic, and social domains, for the benefit of all. The East African Customs Union is making encouraging strides, the Common Market was established in 2010, and the East African Monetary Union Protocol has been put into effect, all of which show that the regional integration process is currently well underway. The EAC's map is shown in Figure 1.1 below.



Figure 1.1: Map of East African Community (<https://www.mapstudio.co.za>)

1.3.2 Brief Overview of Individual East African Countries

1.3.2.1 Tanzania

Tanzania has experienced remarkable economic growth primarily based on its vast natural resources and tourism, with a GDP growth rate averaging 6%-7% per year from 2009 to 2017 (Magombeyi & Odhiambo, 2019). Moreover, economic growth is due to fiscal reforms, including reform of the customs service, value-added tax, donor assistance and political stability. Tanzania used fiscal stimulus measures and accessible monetary policies to lessen the impact of the global recession and, in general, benefited from low oil prices. Tanzania has largely completed its transition to a market economy, although the government retains a presence in telecommunications, banking, energy and mining.

The Tanzanian economy depends on agriculture, which accounts for slightly less than one-quarter of its GDP and employs about 65% of the workforce. However, gold production in recent years has increased to about 35% of exports (Albagoury & Anber, 2018). All land in Tanzania is owned by the government, which can lease land for up to 99 years. Proposed reforms to allow for land ownership, particularly foreign land ownership, remain unpopular.

Tanzania depends heavily on tax as a key source of government revenue. Over the past few years, the government has focused on raising revenue from a limited number of sources. Since 1988, Tanzania has been implementing fairly comprehensive tax reforms as part of widening economic reform programmes to bolster growth and achieve sustained macroeconomic stability (Kipilimba, 2017). Despite the initiatives of the government, it appears that its seemingly good plans have never successfully generated resources to meet its anticipated national targets.

The country has a relatively low tax to GDP ratio, which lies considerably below the average for Sub-Saharan Africa, and thus revenue derived from taxes has been meagre. Tanzania is the second largest loser of revenue in the East African region, and the revenue generated from its government's fiscal and monetary plans are still far below the actual revenue required to finance and achieve targets (Cobham & Janský, 2018). Tanzania has remained heavily aid-dependent and unable to invest faster in its development. Moreover, a large proportion of the budget still depends on unpredictable funds from development partners (Koch, 2017).

1.3.2 Kenya

Kenya is the economic, financial, and transport hub of East Africa. Kenya's real GDP growth has averaged over 5% for the last decade (Odhiambo, 2021). While Kenya has a growing entrepreneurial middle class and steady growth, its economic development has been impaired by weak governance and corruption (D'Arcy & Cornell 2016). Although reliable numbers are hard to find, unemployment and under-employment are excessively high and could be near 40% of the population (Caporale & Gil-Alana, 2018).

Agriculture remains the backbone of the Kenyan economy, contributing one-third of its GDP (Okungu & McIntyre 2019). About 75% of Kenya's population of roughly 48.5 million is employed, at least part-time, in the agricultural sector, including livestock and pastoral activities (Chepkwony et al., 2019). Over 75% of agricultural output is from small-scale, rain-fed farming or livestock production. Tourism plays a significant role in Kenya's economic development. Despite political turmoil throughout the second half of 2017, tourism was up by 20%, thus showing the strength of this sector (Sindiga, 2018; Njoya & Seetaram, 2018). However, inadequate infrastructure continues to hamper Kenya's efforts to improve its annual growth, which is needed to address poverty and unemployment (Blomkvist & Nilsson, 2017).

The government of Kenya has been introducing tax reforms since independence, intending to make the tax system more effective and generating more revenue (Bett & Yudah, 2017). Bett & Yudah (2017) maintain that despite these efforts, the tax system is still incompetent, and the government is still struggling with huge budget deficits. In fact, fiscal statistics reveal that tax revenue provides only about 60% of the government budget, leaving the government with a deficit of about 3,660 billion Kenyan Shillings (KES) or 37 billion US dollars (USD). This has forced the government to turn to borrow money from both domestic and external sources to bridge the deficit (Ngugi, 2016).

1.3.3 Uganda

There are abundant natural resources in Uganda, such as rich soils, consistent rainfall, sizable recoverable oil reserves, and modest amounts of copper, gold, and other minerals. About 72% of the workforce is employed in agriculture, making it one of the most significant economic sectors (Sridharan et al., 2019). Following the onset of conflict in South Sudan, the nation's export market experienced a severe decline, but it has recently recovered thanks in large part to record coffee harvests, which account for 16% of exports, and rising gold exports, which account for 10% of exports. The small industrial sector in Uganda is reliant on imported materials like heavy machinery and refined oil. Since 2016, as government spending and the public debt have increased, Uganda's economic development has slowed. Energy and road infrastructure investment make up the majority of Uganda's budget, and the nation mostly depends on donor assistance to promote agriculture's long-term growth and to enhance the health and education sectors. Concessional loans are used to fund the greatest infrastructure projects externally; however the costs are overstated (Mawejje & Mawejje, 2016). As a result, it is anticipated that the cost of servicing the debt incurred for these loans will increase.

In 2019, oil revenues and taxes were expected to become a larger source of government funding, as oil production was planned to start in the following three to 10 years (Mawejje, 2019). Uganda faces many economic challenges. Instability in South Sudan has led to a sharp increase in Sudanese refugees and disrupted Uganda's primary export market (as mentioned above). Additional economic risks include poor economic management, endemic corruption and the government's failure to invest adequately in health, education and economic opportunities for a burgeoning

young population. Uganda has one of the lowest electrification rates in Africa, as only 22% of Ugandans have access to electricity, dropping to 10% in rural areas.

Uganda has recorded impressive economic growth rates over the last two decades. However, despite the sustained period of growth, the tax effort measured by the tax-to-GDP ratio has stagnated to between 10 and 13% of the GDP over the same period (Maweje & Okumu, 2016). It is said that tax compliance in Uganda is low because of the negative perception of taxpayers of the quality of public services (Ali et al., 2013).

Tax planning is a concern in Uganda, where the media occasionally reports gross tax evasion and avoidance (Fredrick & Peter, 2019). While the government of Uganda has enacted amendments to its tax laws to close the loopholes used by multinational companies (MNCs) and individuals to evade or dodge taxes, the tax regime is still susceptible to tax planning, especially that of MNCs (Tusubira, 2018).

1.4 Aim of the Study

The main aim of the study was to investigate the impact of tax planning on the firm value of East African listed companies while examining the role of corporate governance as a moderating factor. This aim was realised by achieving the following four specific objectives.

1.4.1 Objectives of the Study

Objective One: To longitudinally investigate the tax planning schemes of firms in EACs

This objective was achieved through a descriptive statistics analysis, which provided empirical evidence of the existence of tax planning schemes in listed firms in EACs. This evidence will alert governments to these practices and form a base for the regulatory authorities to develop appropriate policies and regulations to ensure revenue collection and the protection of investors.

Objective Two: To examine the determinants of tax planning amongst the listed firms

This objective was achieved using the fixed effects (FE) regression model and the generalised least squares (GLS) technique. Shareholders and firm management will benefit by understanding why some firms successfully reduce their tax burden compared to other firms. This will inform management and investors about how to structure their financial affairs and to engineer their firms'

structure so that they can benefit from tax planning. However, governments and other regulators such as revenue authorities need to be informed about what motivates tax planning amongst firms to come up with sound policies for counteracting it.

Objective Three: To investigate the impact of tax planning on firm value in EACs

This objective was achieved using the generalised method of moments (GMM) to produce findings that will be useful to shareholders, regulators and policymakers because they will answer the ongoing question in the literature of whether tax planning is relevant to firms and shareholders value.

Objective Four: To examine the role of corporate governance mechanisms in moderating the relationship between tax planning and firm value

This objective aimed to use a GMM estimation technique to examine the power of corporate governance to moderate the relationship between tax planning and firm value. As highlighted in the literature, tax planning is associated with agency problems because managers may implement tax planning for their self-interests at the expense of shareholders. Thus, corporate governance is argued to have the ability to solve the agency problem and align the interests of shareholders to that of management in tax planning strategies.

1.5 Research Questions

The research questions for this study were as follows:

1. What is the tax planning schemes of listed firms in EACs?
2. What are the determinants of tax planning?
3. How does tax planning affect firm value?
4. To what extent does corporate governance moderate the relationship between tax planning and firm value?

1.6 Significance and Justification of the Study

The research findings, which investigated the value relevance of tax planning, are theoretically, methodologically and practically relevant. Moreover, they have contributed to the body of knowledge on this topic in several ways.

Firstly, because it was the first study of its kind to be conducted in the East African Community, the study has contributed to the existing debate on whether tax planning is relevant to firms and shareholders, as well as the discussion about the relationship between tax planning and firm value. Furthermore, shareholders may benefit from knowing how tax-planning activities may affect their companies' value.

Secondly, the empirical evidence in the literature indicated that firms worldwide have increasingly resorted to tax planning in recent years. Governments, particularly those of developing nations, lose substantial tax revenue, which negatively affects public service delivery. The findings of the current study are expected to help tax administrators who struggle to increase tax revenue collection in developing countries to identify what motivates the tax planning activities of listed firms, thereby being able to monitor and control them.

Thirdly, the revenue authorities and capital market authorities will benefit from the study because it provides evidence of the level of firms' compliance with the tax laws and corporate governance codes. In addition, the study provides evidence as to whether a firm's compliance with corporate governance principles and the strength of corporate governance lead to variations in the association between tax planning and firm value.

Fourthly, the study used a large cross-section of data about listed firms from three countries when considering the drivers of tax planning for a broad range of firms from various industries. In addition, the study used a large panel dataset in its investigation. To the best of the researcher's knowledge, no existing research in this area has focused on the value relevance of tax planning using firms from three different emerging market countries.

Fifthly, from a methodological perspective, the study contributes to knowledge using several econometric methods that have not been used in previous studies of the relevance of tax planning to firm value. Since the robustness of results largely depends on the quality of the empirical strategy used at various stages of the study, using different estimation methods was expected to

produce new evidence that encourages the extension of the borders of research in other areas of emerging markets. Specifically, the use of the dynamic system GMM enabled the study, to be different from several previous studies of emerging markets (Kohli & Mann, 2012).

1.7 Overview of the Research Methodology

The study adopted a quantitative research design to achieve its objectives. The research mainly used archival panel data from the financial and annual reports of selected firms. This secondary data was collected from company websites, stock markets, McGregor and Bloomberg databases. The final sample of this study consisted of 99 firms listed on the capital markets of three EACs (Tanzania, Kenya and Uganda) for 12 years from 2008 to 2019. The researcher expected 1089 annual reports; however, owing to missing data for some of the years of the firms, 1021 annual reports were obtained and analysed.

1.8 Structure of the Thesis

This thesis is organised into nine chapters. Figure 1.2 below illustrates the structure of the thesis.

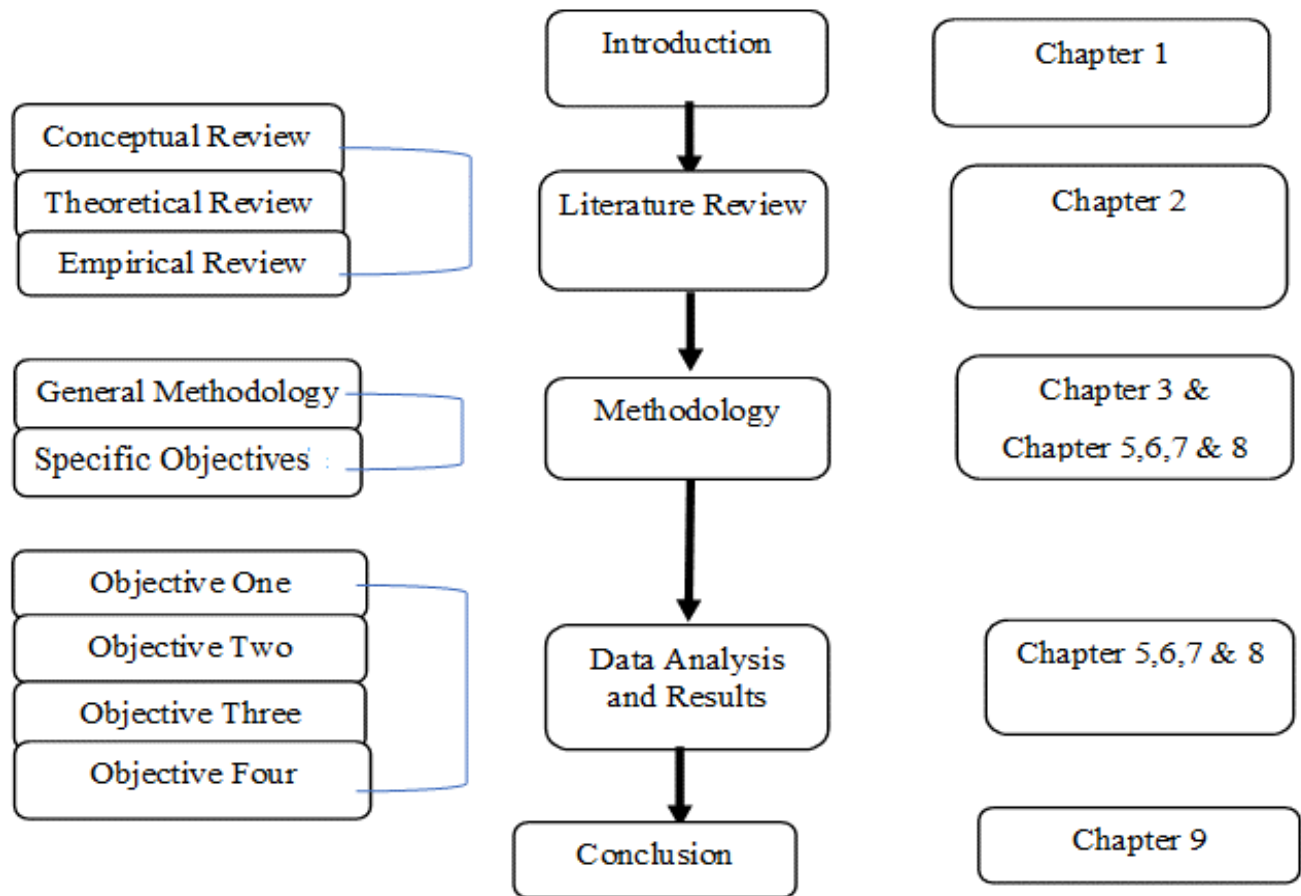


Figure 1.2: Structure of the Thesis

As presented in Figure 1.2, Chapter One was an introduction to the thesis and explained the background of the study; the statement of the problem; the aim and objectives; the significance of the research; the study’s contributions to the body of knowledge in the area of the research; and the structure of the thesis.

Chapter Two will discuss the main concepts used in the study. It will begin with a discussion of tax planning, its definition, objective, and costs and measurements. In addition, this chapter will discuss the concepts of corporate governance and firm value.

Chapter Three will review relevant theories that underpinned the study: the agency theory; the stakeholder theory; the political cost theory; the political power theory; and the resource dependence theory.

Chapter Four will explain the research methodology adopted to achieve the study objectives. The methodology used in a study is integral to the reliability of the findings and the study's validity. The chapter will explain the research design, research techniques, the research population, the sample and sample selection procedures, data types and sources, definitions of the variables, and estimation techniques.

Chapter Five will cover the presentation and discussion of the results of the study's first objective, which was to longitudinally investigate the tax planning schemes of listed firms in EACs.

Chapter Six will address the second study objective, which was to investigate the determinants of tax planning in EACs.

Chapter Seven will cover the third objective of the study, which was to examine the impact of tax planning on firm value in EACs.

Chapter Eight will address the fourth objective of the study, which was to investigate the moderating influence of corporate governance on the relationship between tax planning and firm value.

Chapter Nine will present the summary of the study and the major findings, the contributions of the research, recommendations for practice and policy, the limitations of the study and suggestions for future research.

The next chapter is the conceptual literature review. The chapter will provide definitions, explanations and discussions of the main concepts of the study: tax, tax planning, firm value, and corporate governance.

CHAPTER TWO

CONCEPTUAL REVIEW

2.0 Introduction

Chapter One was an introduction to the thesis and explained the background of the study, the statement of the problem, the aim and objectives, the significance of the research, the study's contributions to the body of knowledge and the structure of the thesis. This chapter provides definitions, explanations and discussions of the main concepts of the study: tax, tax planning, firm value, and corporate governance. Section 2.1 covers the concepts of taxation and tax planning, Section 2.2 deals with firm value and Section 2.3 addresses corporate governance.

2.1 Tax and Tax Planning

2.1.1 Tax

Tax can be defined differently, depending on whether the definition is made from an economic or legal perspective. Prichard (2015) defines tax as compulsory, unrequited payments to the general government. The Prichard (2015) describes taxes as unrequited payments because the benefits provided by the government to taxpayers are generally not in proportion to their payments. According to Duernecker and Herrendorf (2018) as well as Kiprotich (2016), tax is a fee levied by a government or regional administration from citizens and corporations on transactions, products or activities to finance government expenditure. Taxes provide revenue to cover the cost of administration and defence, as well as the provision of particular services by the state (Cobham & Janksky, 2018).

All the definitions make it clear that government is responsible for collecting the tax revenue owed to it. Therefore, taxation, which is the act of imposing taxes, involves the institutionalisation of state-controlled revenue collection, which can motivate citizens to hold the government accountable and facilitate collective bargaining between the ruler and the ruled (Boone & White, 2015). In other words, taxation is politically and economically significant in that it is one of the

most important ways that developing countries can mobilise their resources for sustainable development.

Tax supports the basic functions of an effective state, enabling it to raise the necessary resources to deliver essential services and create the context for economic growth. At the same time, it is a catalyst for governments to be more responsive and accountable to their citizens and for the expansion of state capacity (Cobham & Janksky, 2018). Historical, political science and economic research have led to the widely shared view that taxation offers opportunities for the improvement of accountable governance since tax-reliant governments are forced to bargain with their citizens and make policy concessions if they want to maintain tax compliance (Moore, 1966; North, 1990; Prichard, 2015).

According to the United Nations, achieving the Millennium Development Goals (MDGs) will require developing countries to raise at least 20% of their gross domestic product (GDP) in taxes (Kiprotich, 2016). This view is consistent with that of Burbidge (2016), who assert that taxation plays a central role in promoting sustainable development, offers an antidote to the dependence of developing countries on external concessional finance and provides the fiscal reliance and sustainability needed for economic growth. The emphasis here is that taxation strengthens the effective functioning of the state and reinforces the social contract between governments and citizens.

The taxation process helps build effective and accountable states, as reforms initiated by a tax administration may spread to other parts of the public sector (Hearson, 2018). Thus, strengthening the mobilisation of domestic resources is not only a question of raising revenue but also about designing a tax system that promotes inclusiveness, encourages good governance, responds to society's concerns over income and wealth inequalities and supports social justice (Burbidge, 2016). More fundamentally, the centrality of taxation in the exercise of state power means that more efficient, transparent and fairer tax systems, as well as less corrupt tax administrations, can spearhead improvement in broader governance issues (Prichard, 2015).

Despite the significant role of taxes, developing countries still face challenges in revenue collection. The bottleneck is that tax effort, which is the ratio of actual to potential tax revenues, in developing countries is meagre (Tusubira, 2018). Moreover, tax planning is documented as the

main challenge impeding revenue collection (Tusubira, 2018). However, countries face many other challenges to revenue collection, including weak tax administrations. Although a well-functioning tax administration is critical to mobilising domestic resources in developing countries, many administrations are staffed by poorly trained and low-paid officials; have structures that do not encourage an integrated approach to taxation, and do not strike the right balance between enforcement and taxpayer services. Therefore, the design of a tax system should consider the ability of its tax administration to manage it (Prichard, 2015). In addition, tax collection in developing nations is characterised by low tax morale, corruption and poor governance (Prichard, 2015). Empirical studies show a significant correlation between tax morale, which is the willingness to pay taxes, and tax compliance (Tusubira, 2018; Prichard, 2015).

High levels of corruption are strongly associated with low state revenue because corruption negatively affects tax morality, which like the term “tax morale” refers to willingness to pay taxes and distorts the tax structure. Studies in developing countries indicate that often more than half of the taxes that should be collected cannot be traced by government treasuries because of corruption and tax evasion (Fjeldstad & Tungodden, 2001). Additionally, poor governance, due to weak rule of law and political instability, reduces the revenue collection ability of a state. Therefore, the centrality of tax collection as an exercise of state power means that issues in tax collection may reflect poor governance. Marwejje and Okumu (2016) hold the view that developing nations are dominated by the hard-to-tax sector that includes small businesses, small farms and professionals. This challenge to revenue collection is exacerbated in countries where administrative capacity and incentives to comply are weak.

2.1.2 Brief History of Taxation

The history of taxation began thousands of years ago when ancient civilizations, including those of the Greeks, Romans and Egyptians, levied taxes to finance military operations and public services, as well as maintaining key strategic reserves (Hearson, 2018). In Europe, during the Middle Ages, tax was based on land and property ownership. However, income tax began to be levied in mediaeval towns on the earnings of artisans in proportion to that of property and landowners. Some mediaeval states also taxed income gained from renting land, official salaries and professional gains (Kiprotich, 2016). In 1799, the first general income tax in Europe was

imposed by William Pitt, the Prime Minister of England, during the Napoleonic wars (Passant, 2016). This included 10% tax on annual incomes over £200; between 1% and 10% tax on annual incomes between £60 and £200; and income below £60 was not taxed. In time, the tax came to be accepted as a vital resource for winning the war against Napoleon and a patriotic duty (Samson, 2002).

2.1.3 Taxation in Africa

Taxation in Africa started long before colonialism when kings and chiefs demanded that their subjects submit a portion of their harvest and/or livestock as a form of tax. Historical records show that many once powerful African empires or kingdoms had a tax system that supported them or enabled them to expand (Andersson & Lazuka, 2019). For instance, in southern Africa, the Zulu Empire's powerful king, Shaka Zulu, like all Zulu chiefs, demanded steadily increasing tributes or taxes from his subjects to command/operate a mighty army that subjugated neighbouring chiefdoms by confiscating livestock and other valuable products (Dincecco et al., 2019).

With the coming of colonialism, colonial masters introduced several tax laws to raise financial resources to run the colonial territories. In Northern Rhodesia, now called Zambia, the British South African Company (BSAC), established by a charter issued by Queen Victoria of the UK, introduced the hut tax in 1904 (Hanson, 1972). This tax was payable in money, labour, grain or stock and benefited the colonial authorities in various ways, including raising money and broadening the cash economy, which aided further development. Similarly, in the late 1890s, the German colonial administration introduced an annual head tax of three rupees on all adult males in Tanzania (formerly Tanganyika before its union with Zanzibar) (Shivji, 1979). This was the equivalent to more than a month's wages and was designed to force Africans out of the domestic economy to work for wages for the government and private German and South African settlers.

The British took over Tanganyika after World War I and continued German colonial policies regarding labour and taxes. To expand the tax revenue, the British introduced a tax system called the Hut and Poll Tax Ordinance in 1923. Officially, taxes were justified in terms of the need to recover the costs of the colonial public administration (Havnevik, 1993). However, the poll tax was also used to create regions for labour reserves and to flush out labour when it was most needed

by employers (Shivji, 1979). Thus, taxation is not new, and taxes have been in existence for a long time, although tax laws have changed with time.

Nowadays, taxes are no longer imposed solely for the purposes of the past and are used for social and economic development. They are a compulsory contribution by citizens to the state to enable it to discharge its social and economic responsibilities. Aghion et al. (2016) view state and tax as complementary, with one being unable to survive without the other. Other reasons for the imposition of taxes are outlined by Hanson (1972), including to check the consumption of commodities regarded as harmful if consumed to excess (which is why alcohol and, to some extent, tobacco are heavily taxed); to redistribute labour, for instance, to encourage it to move from employment in one industry to other types of industry; and to reduce income inequality.¹⁷

2.1.4 Tax Planning

Over the years, the tax burden experienced by business operations has been met by outcries from investors and led to companies constantly looking for strategies to reduce their taxes and rescue their businesses. Hanlon and Heitzman (2010) suggest that any business strategy that aims to reduce a firm's tax burden is tax planning. However, there are various strategies that firms can use to reduce the amount of taxes paid to the government. Rego (2003) points out that firms can reduce their tax burden by taking advantage of the differences in the corporate tax systems of various nations and shifting profits from countries with higher tax rates to those with lower ones, thus disconnecting these profits from the country where economic activity was generated. Such profit shifting can be achieved, for example, by manipulating transfer prices on intra-group transactions, strategically concentrating intangible assets (and the associated income) in low-tax countries or concentrating on internal and external debts (and thus interest payments) in high-tax countries. In addition, Nongwa (2014) argues that by profit shifting, firms can exploit mismatches between tax systems to reach situations of double non-taxation (for example, hybrid corporate entities that are not considered as a tax resident by any country) or double deduction (for example, expenses that are tax-deductible in two countries at the same time).¹⁸ Dyreng et al. (2017) suggest that tax planning can be done by domestic firms by exploiting the preferential tax treatment of certain activities or incomes.

According to Hanlon and Heitzman (2010), tax planning lacks a universal definition, although some studies describe it as a legal way of reducing tax expenses and using loopholes in the laws (Armstrong, Blouin, & Larcker, 2012; Minnick & Noga, 2010; Tang, 2016). Lim (2011) explains tax planning as a strategy that legally seeks to reduce a company's taxes in order to increase its performance and market value by using opportunities provided by tax legislation. Hanlon and Slemrod (2009) explain that tax planning aims at reducing explicit taxes (taxes levied by the government) per dollar of pre-tax accounting earnings. Desai and Dharmapala (2009a) define tax planning as a transfer of resources from the state to shareholders. These definitions suggest that tax planning can reduce a firm's tax burden, which is reflected in its effective tax rate (ETR) and includes tax deductions that are entirely legal, as well as those that occupy a grey area.

Desai and Dharmapala (2009a) argue that the concept of tax planning might have been wrongly defined because of a misunderstanding about the legality of the practice. The categorisation of legal tax planning as tax avoidance and illegal tax planning as tax evasion by scholars has been described as a simplistic conclusion because the legality of any tax behaviour cannot be easily determined (Lanis & Richardson, 2011). In fact, terms such as tax management, tax planning and tax aggressiveness have been used interchangeably in the literature to mean tax avoidance (Chen et al., 2010; Dyreng et al., 2008; Lanis & Richardson, 2011; Minnick & Noga, 2010). In light of the term tax avoidance, Pniowsky (2010) describes tax planning as the process of arranging financial affairs in order to defer, reduce or even eliminate the amount of tax payable to the government." However, tax planning generally involves strategies to reduce a firm's tax liabilities (Hanlon & Heitzman, 2010). Therefore, the study defined tax planning as activities that aim to reduce, postpone or avoid paying taxes.

2.1.5 Tax Planning Channels

Previous studies categorised two types of tax planning channels that firms use in tax management. The first channel of tax planning is to use the provisions within tax laws. A number of countries have tax provisions that allow firms to lower their overall tax burden if they change their behaviour in the desired way, for example, invest more in qualifying research and development (R&D) expenditure (Nongwa., 2014). Secondly, firms use the aggressive tax planning or tax aggressiveness channel, where firms, particularly MNCs that operate from more than one country,

exploit mismatches and loopholes in the international tax framework to reduce their overall tax burden (Cooper & Nguyen, 2020) and use a multitude of strategies to reduce their tax bills legally. In this context, aggressive tax planning is the excessive use of opportunities to reduce the corporate tax burden.

The boundaries of tax planning, aggressive tax planning and tax evasion are presented in brackets in Figure 2:1 below. The scope of the study included the use of tax provisions by firms to reduce the tax burden, which is clearly defined by policy makers. In addition, the tax aggressiveness of MNCs substantially reduces their tax burden and runs against the spirit of the law. However, the study excluded tax evasion (illegal measures to lower the tax burden).

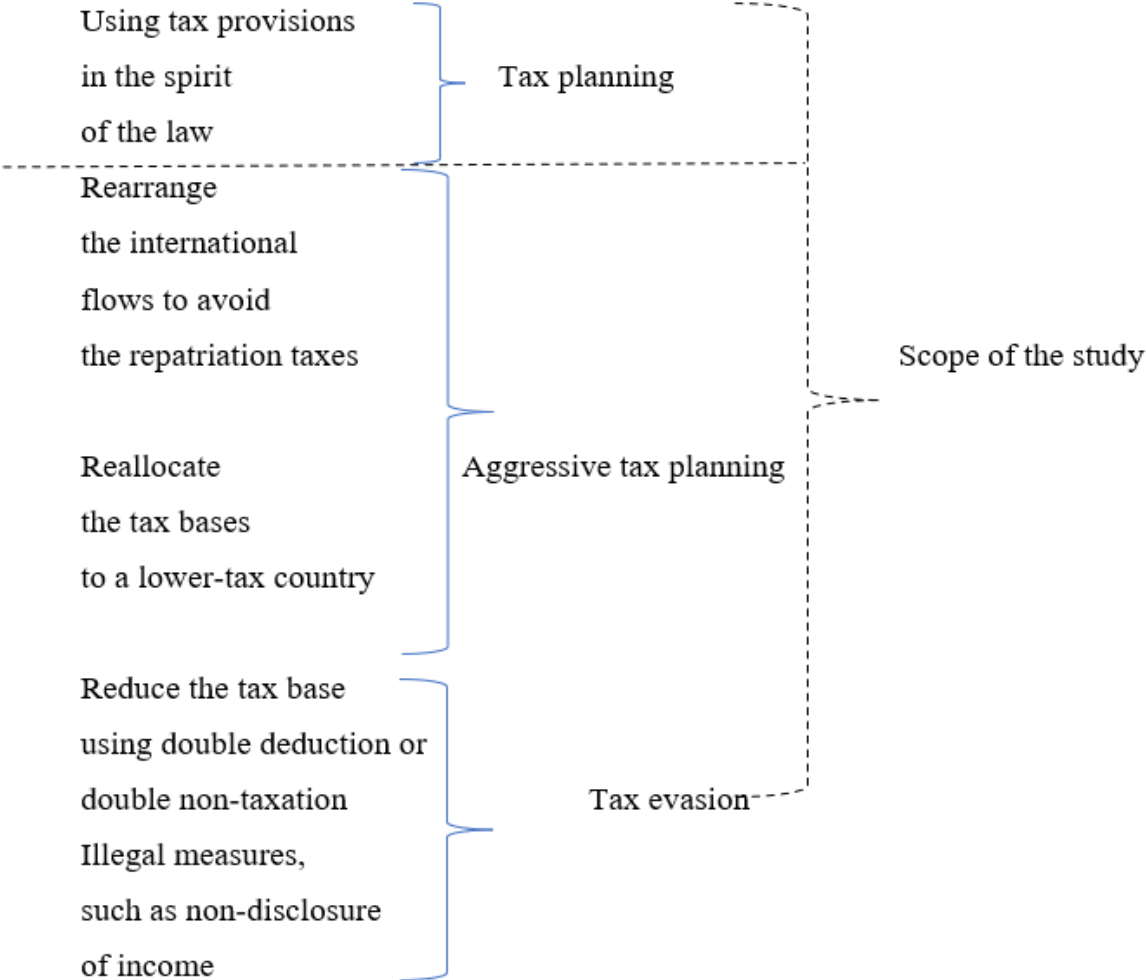


Figure 2.1: Boundaries of Tax Planning, Aggressive Tax Planning and Tax Evasion
Source: Researcher’s Characterisation

Nongwa (2014) highlighted the tax planning channels available in tax provisions for both local firms and MNCs. The first channel available for tax planning is income shifting. According to Nongwa, certain kinds of income (such as bonuses, dividends and year-end payments) can be shifted from one year to another to have the income fall where it will be taxed at lower rates. Secondly, there is the use of tax-deductible expenditures (Nongwa, 2014). A certain expense may be tax deductible if taxpayers meet specific requirements in the tax code, which reduces the amount of taxable income. On a similar note, taxpayers can use the shifting deductions as a tax planning technique. Certain deductible expenses can be paid in one year or the next to place them where the tax benefit will be greater.

Moreover, a taxpayer can use tax-deferring techniques, where taxpayers put business profits into certain investments or make pension plan contributions that allow them to defer the tax on some income to a future year. Apart from these tax planning channels and techniques, taxpayers may make tax-free investments that produce income, which is exempt from income tax laws. In addition, there are other tax planning channels available to a local firm, such as intracompany transactions between business group members, the usage of accelerated depreciation schemes, tax credit, and allowance for corporate equity (Dharmapala & Riedel, 2013; Dyreng et al., 2017).

There are tax-planning techniques, which are available for MNCs that have different ways to reduce their corporate tax burden by locating the profit generated in higher-tax rate countries in lower-tax rate countries. Thus, MNCs save on their tax bill because they can shift income from high-tax to low-tax jurisdictions, including tax havens (Dharmapala & Riedel, 2013; Dover, 2016). This may be especially true for MNCs that can arrange their cross-border transactions on intangible assets, which are by nature more difficult to value and can be more flexibly relocated across borders (Fuest et al., 2013). In a related study, Auerbach et al. (2017) argue that firms can shift profit from high to low tax jurisdictions by manipulating transfer prices of transactions between related companies and selecting a low transfer price range for profits transferred from high to low-tax jurisdictions.

Sorbe et al. (2017) posit that MNCs may manipulate the location of their debts to reduce corporate tax burden. Indeed, by locating debts in higher-tax rate countries, the interest payments of MNCs

will be deducted at a higher rate. According to Schindler et al. (2013), debt shifting plays “an essential role in the tax planning strategies of MNCs. Cross-country differences in corporate tax rates create opportunities for lending from low-tax countries to affiliates in high-tax countries or by locating external borrowing in high-tax countries. This debt shifting reduces a group’s tax bill without affecting its overall debt exposure and lessens the risk of bankruptcy. Interest payments are generally deductible from taxable income in most countries, which implies that locating debt in high-tax rate countries is a way for MNC groups to reduce their tax burden, as interest payments are deducted at a higher rate. Previous studies such as those of Schindler et al. (2013) and Buettner and Wamser (2013) confirm the reality of debt shifting, by showing that host-country taxes or international tax differentials have a positive and significant effect on internal debt. Debt shifting is more pervasive in developing countries, with the effect of taxes being twice as large as in developed economies (Fuest et al., 2013).

Johannesen (2014) claims that multinational corporations may employ hybrid instruments for tax planning, claims. According to the author, hybrid financial instruments are those that exhibit both debt and equity characteristics and may be categorized as either debt or equity depending on the jurisdiction. Tax professionals can design a class of transactions using hybrid instruments that receives different international tax treatment depending on the "deductibility, inclusion, timing, or character of payments made." According to Krahnal (2005), because different nations have different regulations defining debt and equity for tax purposes, it is possible for a hybrid financial instrument to be considered as debt in one jurisdiction and equity in another. By enabling businesses that invest abroad to combine tax-deductible interest expenses in the host country and tax-favourable dividend income in the home country may open up opportunities for tax avoidance. It may lead to a deduction for interest in the first nation and non-taxable income in the second (as the income is treated as a tax-exempt dividend).

Hybrid instruments may also be used as a tax planning strategy by MNCs. According to Ruchelman (2008), a corporation can be treated differently in two countries for tax purpose. For instance, a firm may not be considered a tax resident by any country (termed a stateless entity), and thus achieve double non-taxation of profit. Alternatively, an entity can be treated as a non-taxable entity, such as a partnership, which means that the partners are taxed instead of the entity

itself in one country whilst being a taxable entity in another. This can result in a tax deduction in the first country and a non-inclusion of income in the second country.

In addition, preferential tax treatment is another tax-planning channel (Ortiz, 2020; Yurko & Cheng, 2018). According to Ortiz (2020), MNCs may shift incomes to benefit from special tax treatment offered by particular countries. Tax laws provide special tax treatment to certain common types of investments in which companies might invest to benefit from these laws. Similarly, returns from investments in intellectual property (IP), financial services, stocks, mutual funds, land and real estate, for example, are taxed at a rate lower than that for individuals who meet specific requirements in some countries. Therefore, Yurko and Cheng (2018) argue that with sound tax and investment planning, these special benefits may produce a higher after-tax return on investments. Domestic firms can benefit from preferential tax treatment, but to a lesser extent than MNCs, since they cannot shift incomes across borders to enjoy these treatments on a larger scale (Ortiz, 2020).

Moving important intellectual property (IP) to low-tax affiliates strategically is another approach for MNCs to lower their overall tax burden (Ortiz, 2020). As a result, businesses can carry out their R&D in one nation while transferring patent ownership to another, where the ensuing income streams will be taxed at a lower rate. Determining the arm's length price for a company's intangible transactions is typically particularly challenging because there is frequently no comparable transfer of IP between unrelated parties, providing possibility for tax-induced manipulation of transfer pricing (see Desai et al., 2006). By showing a negative correlation between the level of corporate tax rate and the likelihood of patent application as well as the subsidiary's level of IP in one country, empirical evidence supports the claim that the location of valuable IP is systematically distorted toward low-tax locations (Hasegawa & Kiyota, 2017; Ortiz, 2020).

5.2.1 Tax Administrative Reforms and Level of Tax Planning

In order to boost the amount of tax income that goes toward GDP, governments, academics, economists, and international organizations have repeatedly emphasised the necessity for better tax administration. The advantages of better tax administration have mostly been felt by developed countries, and it appears that emerging ones will soon follow. The latter, however, continue to face obstacles like tax agency corruption, a lack of administrative resources, and tax evasion (Chen et

al., 2018). These problems and many others have contributed to insufficient tax revenue, which has negatively affected economic growth and development.

The International Monetary Fund (IMF) and the World Bank (WB) have consistently advised developing nations to increase their tax revenues to reduce the high poverty levels of their populations (Liu and Cao, 2007; Francis et al., 2019). During the past two decades, EACs have established revenue authorities (RAs) as a tax administrative reform to improve revenue collection. Prior to this reform, in the early 1990s, the administration of national taxes and duties was the responsibility of departments in the ministry of finance. However, the ministry of finance performed poorly in its responsibility of collecting taxes. This was because of (1) low staff morale and productivity due to low pay and a shortage of resources; (2) corruption; (3) ineffective tax collection methods; (4) weak management of revenue administration; and (5) a lack of a tax-paying culture because taxpayers viewed the tax system to be unfair (Soest, 2007; Soviana et al., 2020).

The argument for the RAs was that moving away from civil servants' terms and conditions of service and management practices would overcome many of these problems (Putra et al., 2018). With higher salaries, staff would not need to seek alternate sources of income and, coupled with stricter discipline, corruption would be less, whilst morale, productivity and revenue collection would improve. Similarly, by removing the basic tax administration functions from the traditional departments in the ministry of finance and granting the RAs a greater degree of autonomy to administer their internal systems, the expectation was that revenue collection would be enhanced; tax-related corruption and evasion would be reduced; and taxpayer services would be improved (Niu et al., 2019).

On 5 September 1991, Uganda established the Uganda Revenue Authority (URA), which was one of the first African RAs. Results were impressive in the early years, reflected by strong revenue growth in real terms that levelled off by the late 1990s (Hidayat & Yuliah, 2018). However, in a few years, many of the previous administration and taxpayer compliance problems gradually returned, including corruption and inefficiency. The URA had become a fragmented organisation with unclear accountabilities when a significant modernisation initiative was launched in late 2004 (Tarmidi, 2019). This reform strategy exploited the flexibility afforded by the RA model to appoint an entirely new management team and workforce, structurally reorganised by integrating tax

administration and begin streamlining and automating operations. Thus, the RA model has been the URA's vehicle to both success and failure over the past 15 years.

Acts of parliament authorised RAs in Kenya and Tanzania. The Kenya Revenue Authority (KRA) was established by Kenya Revenue Authority Act, Cap 469, which became effective on 1 July 1995, and the Tanzania Revenue Authority (TRA) was established by the Tanzania Revenue Authority Act 1995 (No. 11 of 1995), which came into effect 1 July 1996. According to Fjeldstad and Katera (2017), these RAs were responsible for collecting and assessing tax revenue as well as advising the government on policies concerning tax revenue.

The RAs were given semi-autonomy in that they were in charge of tax administration, while policies were left to the ministry of finance, which still had fiscal oversight over the RAs. This new arrangement was designed to ensure that the new body would concentrate solely on revenue collection. With this semi-autonomy, it was hoped that the RAs would operate according to business principles without political interference. Moreover, RA staff members were paid salaries that were above those of the civil service to attract and retain competent staff, as well as eliminating, or at least reducing, the corrupt practices that characterised most of the civil service (Soest, 2007).

2.2.2 Technological Reforms and Level of Tax Planning

EACs are amongst the developing countries that have adopted various technological reforms in their governance systems (Kim et al., 2018), which have transformed the economy by streamlining the flow of data and information. The RAs have taken advantage of the presence of the e-Government Agency (eGA) in the EACs, which is a dedicated agency established to oversee proper coordination of e-government initiatives in public institutions (Therkildsen, 2004; Barasa et al., 2017). This has facilitated the integration of the RAs' ICT systems with other public institutions to increase the scope of information sharing for taxation purposes. RAs in EACs have been using the High Availability Data Centre (HADC), which enables the RAs' data and applications to be moved to a platform that meets the requirements for security, availability and scalability (Eilu, 2018). The HADC is used for remote storage, processing and distributing of data. Moreover, it enhances the reliability of services delivery through the RAs' extensive use of ICT

that supports the provision of timely information for decision-making and the provision of convenient services to taxpayers (Murage et al., 2019).

Chatama (2013) found that ICT contributes significantly to tax collection in the large revenue department of the TRA because it processes tax returns in time, minimises operational costs and provides timely access to taxpayers' records. Therefore, Chatama (2013) maintains that tax authorities should focus on improving ICT infrastructure to ease tax collection mechanisms and boost government revenue.

One aspect of the ICT facilities in RAs that has received considerable attention is electronic tax filing (e-filing). The e-filing of tax returns is an essential application that automates tax-related processes to improve efficiency in collecting and assessing tax data. This makes e-filing one of the important government e-services that have advanced in most governments. Moreover, e-filing is one of the most crucial and advanced e-government services in most countries, as it allows taxpayers to assess their taxes conveniently and thus pay them. Because of e-filing, taxpayers can use tax software to send tax returns via the internet to tax authorities. Promoters of e-services in governments admit that electronic operations improve efficiency, promote transparency, reduce operating costs and minimise the need for taxpayers to use tax services (Bhuasiri, Zo, Lee & Ciganek, 2016).

Other e-filing benefits include efficiency in information searching, minimisation of processing errors, speedy filing of returns, fast and direct deposit of refunds, elimination of delays in tax filing and returns (Eilu, 2018). By using electronic services, tax-related processes, such as the assessment of taxpayers and payments are simplified. This indicates that e-filing improves tax filing services and thus reduces costs to both taxpayers and tax collecting organisations. Furthermore, e-filing increases tax compliance and achieves the objective of governments to ensure voluntary tax compliance.

2.3 Objectives and Benefits of Tax Planning

The objective of tax planning is to increase after-tax returns. According to Pniowsky (2010), tax optimisation mainly consists of minimising income tax to maximise after-tax returns. Bryant-Kutcher, Guenther and Jackson (2012) posit that the management of firms engages in tax planning

to reduce the tax burden and thus maximise the level of profits. Increasing after-tax returns can be attained if necessary, measures are taken when undertaking tax planning activities, as the process is complex and associated with tax and non-tax costs. According to Kirkpatrick and Radicic (2020), the minimisation of tax by means of tax planning contributes to tax and non-tax costs. Therefore, appropriate measures should be taken to ensure that optimal after-tax return is attained.

Salawu (2017) stipulates that effective tax planning uses skills and knowledge to minimise tax liabilities while ensuring that non-tax costs are minimised to ensure the increment of after-tax returns. Managers look for strategies to reduce their tax burden to maximise after-tax returns and enhance shareholder wealth (Wahab & Holland, 2012; Cooper & Nguyen, 2020). If successfully deployed, a tax planning strategy would transfer wealth from the state or government to shareholders. Therefore, it would result in relatively low payable taxes and a higher after-tax cash flow.

2.4 Constraints of Tax Planning

Firms that practise tax planning could end up facing numerous consequences (Scholes et al., 2009). Wilson (2009), Rego and Wilson (2012) as well as Wilde and Wilson (2018) maintain that tax planning may attract costs and risks that can be detrimental to firm value and reduce the net benefits received by shareholders. Moreover, explicit tax planning often affects various stakeholders, such as shareholders, managers and the government, and may incur non-tax costs, such as political costs and reputational penalties.

The consequences of tax avoidance can be direct or indirect (Hanlon & Heitzman, 2010). A direct consequence would be the choice to invest in a particular tax-favoured asset or accrue a tax-deductible expense. In addition, location decisions and other organisational choices could be predominantly based on tax motives. Direct tax planning costs are payments made to tax planners and legal consultancies (Jones & Rhoades-Catanach, 2004; Schreiber & Fuehrich, 2007; Armstrong et al., 2012).

The indirect effects of tax planning may be that it generally limits a firm's resources and funds available for alternative undertakings when tax-motivated investments are made. Therefore, firms

that practice tax planning are most likely to face significant indirect costs, such as expert fees; penalties and interests from revenue authorities; agency tariffs; and reputation costs.

Recently, promising research on the effects of tax avoidance on corporate decisions has been conducted. In the following paragraphs, these studies along with the fundamental works that laid the foundation for examining the potential consequences of tax avoidance will be reviewed.

Reputation Cost

A reputation cost is the various kinds of financial and other damage that an organisation or a firm suffers because of the loss of its reputation with investors, customers and others (Chalmers & Godfrey, 2004; Kim et al., 2020). Reputation cost may result in the loss of trust in a firm. Stakeholders believe that their firm is legally obligated to pay the tax due in any territory, in accordance with rules set by governments (Boone & White, 2015; Richardson, Taylor & Lanis, 2013). Tax planning activities may result in a negative perception amongst shareholders if it leads to the firm and management of a company losing their reputation (Jones & Bowrey, 2013). Furthermore, firms that consistently show lower taxable income, compared to other firms, raise suspicion amongst investors concerning the reliability of their financial statements (Doukakis, Siougle & Vrentzou, 2008; Hanlon & Heitzman, 2010). Hanlon and Slemrod (2009) maintain that tax-planning practices can also leave firms exposed to higher levels of political and regulatory risk. They argue that a company may be rejected by society as a punishment for its lack of citizenship when it becomes publicly revealed that the company dodges paying taxes.

Loretz and Moore (2009) argue that tax-planning decisions, similar to a firm's operational decisions, are made in a competitive environment. This implies that when tax payments made by the company deviate significantly from those of the peer group, reputational damage may occur. Loretz and Moore (2009) maintain that if they deviate too much from the behaviour of their peers, managers must balance the benefits of a reduced tax burden against the costs of a loss of reputation. However, management acts in bad faith when not paying its fair share of tax to the government, and thus, to some extent, may be showing bad faith towards shareholders as well (Frank, Lynch, & Rego, 2009; Hoopes et al., 2018).

A few studies including those of Wilson (2009), Bowen, Call and Rajgopal (2010), Graham et al. (2013) and Gallemore, Maydew and Thornock (2014) have examined the association between tax

planning and reputation cost. For instance, Hanlon and Slemrod (2009) shed light on the reputation cost borne by a company, once its tax avoidance actions are revealed to shareholders. They examined the market reaction to news of tax aggressiveness in terms of a firm's engagement in a tax shelter activity. Their results showed an overall negative effect of the news of involvement in tax shelter activity on stock prices. In contrast, Wilson (2009) finds that tax planning is associated with higher future stock returns and not reputation loss, as long as corporate governance is strong. At least for the firms in Wilson's (2009) study, the results showed that tax-planning activities create value for shareholders rather than significant reputational costs.

Gallemore, Maydew and Thornock (2014) advanced understanding about the potential reputational cost associated with explicit tax planning activities. In their attempt to explain the effect of tax planning, they provide evidence on the relationship between reputation cost and scrutiny of tax management (tax planning), but little evidence of reputation loss upon the revelation of a firm's tax planning activities. The authors extended their research design to investigate a broad array of dimensions of reputation cost, including the turnover of chief executive officers (CEOs), chief financial officers (CFOs) and auditors. The results indicated no significant turnover effects three years after news of the researched firms' tax planning, compared to a propensity-matched sample of control firms. Similarly, there appeared to be no significant effect of tax planning on the sales growth or the advertising expense of the concerned firms, indicating that customers were probably not too concerned about tax planning.

Bowen, Call and Rajgopal (2010) judged the public reputation of particular firms by consulting Fortune Magazine's lists "Best Companies to Work For" and "Most Admired Companies". There was no evidence for firms publicly identified as tax planners to be less likely to make it to the rankings when compared to the firms not involved in tax planning. Thus, these findings, taken together with the novel findings provided by Gallemore et al. (2014), suggest no public backlash.

Hence, the findings concerning the reputation cost of tax avoidance appear mixed (Graham et al., 2013; Hanlon & Slemrod, 2009). In a recent survey study, Graham et al. (2013) discussed the responses from close to 600 tax executives and showed that 69% of the respondents viewed reputation as necessary, which places this factor second amongst the factors explaining why firms do not engage in tax avoidance strategies. Hence, reputational concerns may be a relevant factor

restraining tax avoidance. While this survey-based evidence clearly circumvented some of the challenges of archival research by directly asking managers about their tax incentives, allowing for the identification of ex-ante reputation concerns, instead of studying ex-post market reactions, it naturally had its limitations. For instance, executives may not have responded truthfully, may have misunderstood the question (response bias), or might have been systematically different from non-respondents (sampling bias). More importantly, perhaps, when it comes to the triangulation of archival-based findings, researchers should bear in mind that the reputational costs perceived or anticipated by executives (firm insiders) may not necessarily exist or be equally valued by market participants.

Penalties and Interests

Nearly all tax systems have some form of interest and tax penalty regimes. Failure to comply with various provisions of tax laws requirements may attract penalties and interest in tax recovery (Mohdali, Isa, & Yusoff, 2014). Tax penalties and interests are imposed as a punishment to deter taxpayers from demonstrating non-compliant behaviour. Interest payable on any delinquent tax or underpayment of tax seeks to protect the present value of the tax amount to the government. In contrast, penalties intend to deter taxpayers from defaulting their tax obligations and to punish them if they do to achieve horizontal equity. Ortiz (2020) posits that, penalties are imposed on taxpayers who fail to meet their tax obligations to encourage them to file and pay their taxes voluntarily.

In a self-assessment tax system, taxpayers are required to estimate their income tax payable for the year of income. However, taxpayers are expected to show a high level of accuracy in their estimation. Failure to estimate tax within the allowed limits results in underestimation, which attracts interest. Moreover, taxpayers are charged interest for failing to pay tax. Any amount of tax imposed under any tax law that remains unpaid after due dates, as required by the respective tax law or regulation, attracts interest.

Divergence from tax laws may attract penalties, such as penalties for failure to keep, retain or maintain books, records and information; failure to file a tax return; and making false or misleading statements. Thus, if they are detected by revenue authorities, tax-planning strategies that exceed limits violate the spirit of tax laws may attract penalties and fines imposed by tax authorities (Chen

et al., 2010; Desai & Dharmapala, 2006). Moreover, Armstrong et al. (2015) argue that if tax aggressiveness is detected by revenue authorities through tax audits and investigations, firms will be subjected to additional tax payment, fines, interest and penalties, which should be considered.

Agency Cost

Agency costs are all costs borne by shareholders to encourage managers to maximise shareholder wealth rather than act in their self-interest (Maama & Mkhize, 2020). In poorly governed firms, the secrecy surrounding tax avoidance can be exploited to obscure rent extraction by managers, resulting in future negative abnormal returns (Desai et al., 2006). Furthermore, increased tax avoidance efforts may provide managers with opportunistic leeway to divert rents from shareholders. Based on the agency theory, Desai and Dharmapala's (2009b) study investigated the association between tax avoidance and firm value and found that tax avoidance does not significantly affect firm value. However, the study found cross-sectional variation in that association, depending on the level of institutional ownership of a firm. The findings indicated that for firms with high levels of institutional ownership (well-governed firms), there is a positive relationship, whilst for firms with low institutional ownership (poorly governed firms), there is no significant relationship. Viewing institutional ownership as an adequate proxy for governance quality, the researchers found that the results were in line with the agency theory in that they indicated a mitigating role of governance on agency problems related to tax avoidance that may reflect in firm value.

Kim et al. (2011) find a significant positive association between tax avoidance and the risk of a stock price crash at the firm level. Closely in line with the agency theory view of tax avoidance, the results of Desai et al.'s (2007) study suggested that tax avoidance facilitates opportunistic rent extraction, leading to the hoarding of bad news by managers. Ultimately, the accumulation of bad news over multiple periods may cause firms' stock price to drop as a certain threshold is crossed, and bad news emerges in the market. Moreover, the study confirmed the mitigating role of governance arrangements in this process. This finding suggests that in well-governed firms, for example, those with high levels of institutional ownership, the positive association between tax avoidance and the risk of a stock price crash is found to be lower than in firms with weak governance.

In a related study, Badertscher, Katz and Rego (2013) indirectly tested whether tax avoidance is partly value-destroying, meaning whether and to what extent it reduces the future profitability. The authors documented that current profitability components (margins, utilisations of assets and operating leverage) imply reduced future profitability for tax avoiders when compared to non-tax avoiders. Concerning the role of corporate governance, Badertscher et al. (2013) point out that their early-stage results somewhat contrast the findings of Blaylock (2016), who generally identifies a positive association with future performance, also amongst poorly governed firms. The findings indicate that the effect of tax planning on firm value might also prevail under the influence of control factors, which have previously been found to mitigate or further incentivise rent extraction, such as corporate governance structures, corporate life cycle stages, or the presence of foreign operations. According to the agency theory, tax savings may either be directed towards positive net present value investments or be extracted by opportunistically inclined managers.

2.5 Measurement of Tax Planning

The variables, which are central to research on the measurement of tax accounting and regularly occur as proxies for tax avoidance, are the effective tax rate (ETR) and book-tax difference (BTD) (Richardson et al., 2013). An ETR is the ratio of tax expense to pre-tax income. Thus, a low ETR is assumed to be reflective of low tax expense resulting from tax avoidance, which is indicated by a decrease in the numerator. However, inflation of book income (the amount of income corporations publicly report on their financial statements to shareholders) is indicated by an increase in the denominator, which may also result in a low ETR (Blaylock, 2016), where the term 'low' means lower than the statutory tax rate (STR). An ETR can easily be calculated from financial statement data, which likely explains why it is used by innumerable studies such as those conducted by Wahab and Holland (2012), Dyreng et al. (2008) as well as Minnick and Noga (2010). However, there is no consensus regarding the exact definitions of the numerator and denominator. Several variants of the ETR are established in the literature, which includes the accounting effective tax rate (AETR) (Phillips, 2003), the current effective tax rate, and the cash effective tax rate (CETR) (Dyreng et al., 2008).

Similar to the ETR, several variants of BTD are regularly used in the literature (Bryant-Kutcher et al., 2012), although the minimum consensus is that BTD refers to the difference between book

income and taxable income (Graham et al., 2013). BTD can be either positive, when book income exceeds taxable income, or negative when book income is less than taxable income (Lennox, Lisowsky & Pittman, 2013). As tax avoidance should result in increased book income and decreased taxable income, BTD is usually assumed to be positive. Most published studies rely on estimated BTD as the difference between book income and estimated taxable income (Graham et al., 2013).

The information used to compute tax planning is obtained from either tax returns or financial statements (Lee, Dobiyski & Minton, 2015). These two sources might give different information owing to divergence in the objectives between the financial accounting standards and tax accounting systems. For example, McGill and Outslay (2004) provide evidence for the divergence between the tax planning estimates using tax returns and those of financial statements. However, Graham and Mills (2008) argue that the two sets of the source of information are highly correlated. Moreover, although tax returns produce accurate information, they are highly confidential and not easily accessible. Therefore, the information from financial statements is the only publicly available source for estimating tax planning. Thus, the current study used information from the financial statements of firms, which was consistent with studies, such as those of McGill and Outslay (2004), Graham and Mills (2008), Dyreng et al. (2008), Bryant-Kutcher et al. (2012), Graham et al. (2013) as well as Lee, Dobiyski and Minton (2015).

According to Desai and Dharmapala (2009a), the main challenge of tax-planning research is the measurement of tax planning since companies have strong incentives to conceal their tax planning activities. For this reason, researchers have created several alternative metrics for tax planning, which could be used in estimating it. These proxy measures could be grouped into two: (i) tax proportions of business income; and (ii) the magnitude of the gap between accounting income and taxable income. The review of the measures and the studies that have employed them are as follows.

2.5.1 Book-Tax Deference (BTD)

Book-tax deference (BTD) is a measure of tax planning that focuses on the magnitude of the difference or gap between accounting income and taxable income (book-tax deference) (Minnick & Noga, 2010). It reflects the difference of taxable income from accounting income (Wahab &

Holland, 2012). Although the causes of the difference between accounting and taxable income are many and usually classified as permanent or temporary, the size of the gap is an indication of tax planning practices (Kim et al., 2011). The gap between accounting income and taxable income might be either due to the manipulation of earnings reported to the capital market or tax planning activities aimed at reducing the reported accounting income (or both).

Mills (1998), as well as Desai and Hines Jr (2002), posit that the difference between accounting and taxable income is due to corporate tax planning. Therefore, BTM is an indicator of tax planning activities. The BTM has recently received considerable attention from academics. It is defined as the difference between pre-tax book income and taxable income (Desai and Hines Jr, 2002). This measure is calculated as the difference between profit before tax and estimated taxable income (Wahab & Holland, 2012) and is operationalised as the difference between the book income reported by a firm to its shareholders and the capital market and the tax income reported to the revenue authorities.

2.5.2 Effective Tax Rate (ETR)

The second method to measure tax planning is the proportional amount of taxes to business income. This metric of tax planning is called the effective tax rate (ETR) measures. It is the average tax rate a corporation pays on its pre-tax profits. This is calculated by dividing a tax liability by pre-tax income (Hanlon & Heitzman, 2010) and measures aggressive tax planning through permanent book-tax differences. An example of such a tax planning activity is investments in tax havens with lower foreign tax rates. In fact, the ETR is a widely used measure of tax avoidance. It is utilised because it estimates the effectiveness of a company's tax planning activities (Phillips, 2003). While the ETR is considered generally as the ratio of tax liability to accounting income, several variants have been documented in the literature. For instance, an ETR is usually calculated as current income tax expenses divided by pre-tax accounting income (Phillips, 2003), thus measuring a firm's ability to reduce its income tax expenses so that the ratio between these and pre-tax accounting income is low, which would show a relatively heavy tax burden (Rego, 2003).

Tax avoidance influences ETRs in two ways. Firstly, it often generates book-tax differences that cause ETR variation because the numerator is based on taxable income, whereas the denominator

is based on financial accounting income. Tax-motivated transactions, such as foreign sales, tax-exempt income, tax credits and the deferral of income recognition, generally lower the ETR (Desai and Hines Jr, 2002). Secondly, firms often use their foreign operations to avoid paying income tax, and ETRs capture this form of tax avoidance (Dyreg et al., 2008). For instance, shifting income from a high-tax jurisdiction to a low-tax jurisdiction reduces a firm's ETR. Firms that avoid income tax by reducing their taxable income while maintaining their financial accounting income generally have lower ETRs, which suggests that ETRs are a suitable measure of tax avoidance (Rego, 2003). Therefore, the first tax avoidance measure is the cash effective tax rate (CETR), which is calculated as cash taxes paid divided by pre-tax accounting income. The second measure is the accounting effective tax rate AETR, which is computed as total tax expenses divided by pre-tax accounting income (Dyreg et al., 2008). The various variants of ETRs are discussed below.

2.5.3 Accounting Effective Tax Rate (AETR)

In the US context, the AETR is known as the generally accepted accounting principles effective tax rate (GAAP ETR) (Rego & Wilson, 2012). The AETR is the reported ETR as per financial statements and is computed as the total tax expenses divided by the accounting income before tax. Thus, it reflects the aggregate proportion of the accounting income payable as taxes and measures tax avoidance relative to accounting earnings. The literature argues that this measure is the most frequently used to capture tax aggressiveness (see Robinson et al., 2010; Armstrong et al., 2015; Dyreg et al., 2008; Rego & Wilson, 2012; Robinson, Xue & Zhang, 2012).

This measure was used by Chen et al. (2010) to identify tax aggressiveness in 1003 firms on S&P 1500 Composite Index and discover the relationship between tax planning and family ownership of firms. However, Dyreg et al. (2010) make adjustments for certain items when using the measure to identify tax planning and examine the influence of top executives on corporate tax planning. Similarly, Armstrong et al. (2012) used the AETR to measure tax planning when investigating the effect of tax directors' remuneration on firms' involvement in tax planning. Likewise, Huseynov and Klamm (2012) used the AETR in a study that examined the association between tax planning and corporate social responsibility (CSR) disclosure.

Although the AETR has been widely used to measure tax planning, it has certain limitations. Firstly, it can only capture non-conforming tax avoidance because it measures tax avoidance

relative to accounting earnings (Chen et al., 2010). Secondly, it might not also reflect the strategies for tax deferral because it uses aggregate tax expenses (Huseynov & Klamm 2012).

2.5.4 Current Effective Tax Rate

Slightly different from the AETR, the current effective tax rate is calculated as the current-year tax expense divided by the total accounting income before tax (Hope, Ma & Thomas, 2013). It reflects the tax deferral strategies of a firm by using the current income tax as against the total tax expense, hence its advantage over the AETR.

Given its merit, Hope et al. (2013) employed the current effective tax rate to measure tax avoidance while examining the association between corporate tax avoidance and geographical earnings disclosure practices of US multinationals. Similarly, Richardson et al. (2013) measured tax planning using the current effective tax rate in their study of the relationship between tax aggressiveness and CSR in 408 Australian companies.

Although the current effective tax rate reflects the deferral strategies of firms, it can only identify nonconforming tax avoidance (Richardson et al., 2013). In addition, both the AETR and the current effective tax rate are affected by year-to-year volatility, and they cannot reveal long-term tax avoidance.

2.5.5 Cash Effective Tax Rate (CETR)

A CETR reflects the amount of cash tax payments made by a firm in a given year (Davis, Guenther, Krull & Williams, 2015). A CETR is a relatively accurate measure of tax planning, as it is less prone to the error of including the reduction of tax expenses due to accounting practice requirements, which are not necessarily to be those of tax management (Davis et al., 2015; Minnick & Noga, 2010).

Some tax planning strategies cannot be reflected in a CETR and an AETR, such as deferred taxes (for example, accelerated depreciation for tax purposes), but are reflected in a CETR (Shin & Woo, 2018). In addition, the calculation of a CETR excludes the effect of special items, such as one-time charge-offs or impairments due to bad investments, whereas that of the AETR does not. Overall, given that prior literature prefers the CETR to the AETR and the CETR because of the

limitations of the latter, which may affect research results, the study used the CETR as a tax planning measure and variable.

A CETR has the benefit of detecting a broad range of tax planning activities that can have either certain or uncertain outcomes. Moreover, it is not affected by changes in accounting estimates, such as a valuation allowance or tax contingency reserve (Dyrenge et al., 2008). It is a variable of interest in most empirical research on corporate tax avoidance (Armstrong et al., 2015). Accordingly, a CETR is calculated as:

$$\text{CETR}_{it} = (\text{cash tax paid}_{it})/(\text{Pre-tax income}_{it}).$$

Table 2.1 below shows the summary of the tax planning measures used in previous studies.

Table 2.1 Measures of tax planning

S/N	Name of the Measures	Computation	References
1	Tax Book Difference	The difference between pre-tax book income and taxable income (YS–YT),	Wahab and Holland (2012), Chen et al. (2019), and Eddy and Angella (2020)
2	Accounting Effective Tax Rate	Total tax expense/Pre-tax income	Dyrenge et al. (2008), Minnick and Noga (2010) as well as Campbell et al. (2020)
3	Current Effective Tax Rate	Current-year tax expense/total accounting income before tax	Minnick and Noga (2010), Cen et al. (2020) and Soviana et al. (2020)
4	Cash effective tax rate	Cash taxes paid/Pre-tax income	Dyrenge et al. (2008), Minnick and Noga (2010) and Tang (2019)

Source: Author's Compilation

2.6 Action to Fight Corporate Tax Planning

In the fight against tax planning, OECD came up with the Inclusive Framework on Base Erosion and Profit Shifting (BEPS) plan. The BEPS action plan is a strategy used by multinational companies to avoid paying tax by exploiting the mismatches and gaps in the tax rules. Over 130 countries and jurisdictions collaborated to implement measures to tackle tax avoidance, improve the coherence of international tax rules, and ensure a more transparent tax environment (Tran &

Huynh, 2019). The 2015 BEPS action plan has 15 actions, covering strategies followed in aggressive tax-planning schemes. The implementation of the BEPS action plan was designed to be flexible due to its adoption by consensus (Dover, 2016; Johnson, 2017). Recommendations made in BEPS reports range from minimum standards to guidelines and include creating an instrument to modify the provision of tax treaties related to BEPS practices. In addition, putting BEPS actions into practice has included a growing number of countries beyond the OECD and G20 members and built cooperation between international organisations (Friedrich & Tepperova, 2020). The application of the BEPS action plan, which focussed on tax avoidance and its follow-up, involves issues that remain to be addressed and strategies that need to be implemented. Examples of these strategies are addressing the tax challenges of the digital economy; and building on the BEPS action report that outlined a calendar for providing an adaptation of international tax rules to the impact of digitalisation (Chand, 2016).

Based on several intermediary reports, the OECD/G20 Inclusive Framework on BEPS issued a work programme to develop a consensus-based solution to the tax challenges arising from the digitalisation of the economy. Endorsed in June 2019 by the G20, this programme outlines the steps for modernising international tax rules (Pun, 2017). An annex to this document outlines the different international fora and instruments relevant to BEPS actions and the countries or organisations that participate in and/or apply them.

Globalisation and the digitalisation of the economy have resulted in substantial changes in tax systems, leading to increased geographical tax mobility and concerns about a level playing field and fairness in global tax policy. Multinational companies operate as a unitary business (based on decisions taken at the ‘parent’ level) on a worldwide scale (as opposed to jurisdictions), and most related value chains are global (Schmidt, 2016; Popescu, 2020). Based on the understanding that no single tax rule on its own enables, or conversely can address, tax challenges, but that it is instead the interplay amongst different issues that makes it possible, an agreement on the necessity of a comprehensive package of measures was reached. The fight against harmful tax practices has been discussed since the late 1990s.

Table 2.2 and Figure 2.2 below summarise the BEPS action plan to eliminate or reduce the incidence of tax planning.

Table 2.2: The BEPS action plan

Action 1	Assessing how digitalisation could exacerbate BEPS issues and also raising broader tax challenges; issues cut across direct and indirect taxation and relate to taxing rights on income generated from cross-border activities and their allocation among tax jurisdictions; no special tax regime for the digital economy should be created (no ring-fencing)
Action 2	Neutralising the effects of hybrid mismatch arrangements (the fact that a situation is not treated in the same manner by two tax jurisdictions involved in the cross-border business); the action aims at eliminating the derived tax benefit, with the effect of neutralising a mismatch resulting in double non-taxation
Action 3	Designing effective rules on controlled foreign corporation (CFC) rules to address the risk that taxpayers with a controlling interest in a foreign low-taxed subsidiary can shift income to it and avoid taxation
Action 4	Limiting base erosion via interest deductions and other financial payments relates to excessive intra-group deductions and the differences in tax treatment of debt and equity
Action 5	Countering harmful tax practices more effectively, taking into account transparency; this is linked to the compulsory spontaneous automatic exchange and the review and monitoring of preferential intellectual property (IP) regimes according to the Nexus Approach (substantial activity); a minimum standard is developed
Action 6	Preventing treaty abuse so as to address treaty-shopping resulting in double non-taxation; the action provides for a minimum standard and for the introduction of anti-abuse rules in tax treaties (a specific one: limitations-on-benefits (LOB); and a general one: the principle purpose test'(PPT)
Action 7	Preventing the artificial avoidance of permanent establishment (PE) status; this addresses techniques used to avoid permanent establishment – and related taxation – irrespective of the place where the essential business activities of an enterprise are carried out in a country
Actions 8, 9 and 10	Ensuring that transfer-pricing outcomes are in line with value creation; they respectively cover intangibles; risks and capital; and other high-risk transactions. The actions provide for strengthened guidelines
Action 11	Methodologies to collect and analyse data
Action 12	Require taxpayers to disclose their aggressive tax-planning arrangements (mandatory disclosure) to enable countries to obtain information for counteracting such schemes

Action 13	Setting a minimum standard consisting of the provision of information to tax administrations regarding transfer-pricing documentation, including country-by-country reports (CBCR) for the global business operations of multinational enterprises with a total consolidated turnover of at least €750 million
Action 14	Making dispute-resolution mechanisms more effective – a minimum standard will ensure that administrative processes promote the prevention and timely resolution of disputes, with implementation in good faith within an average timeframe of 24 months
Action 15	Multilateral instrument to modify bilateral tax treaties so as to implement tax treaty measures developed in BEPS actions swiftly

Source: Chand (2016), Schmidt (2016), Johnson (2017) and Pun (2017)

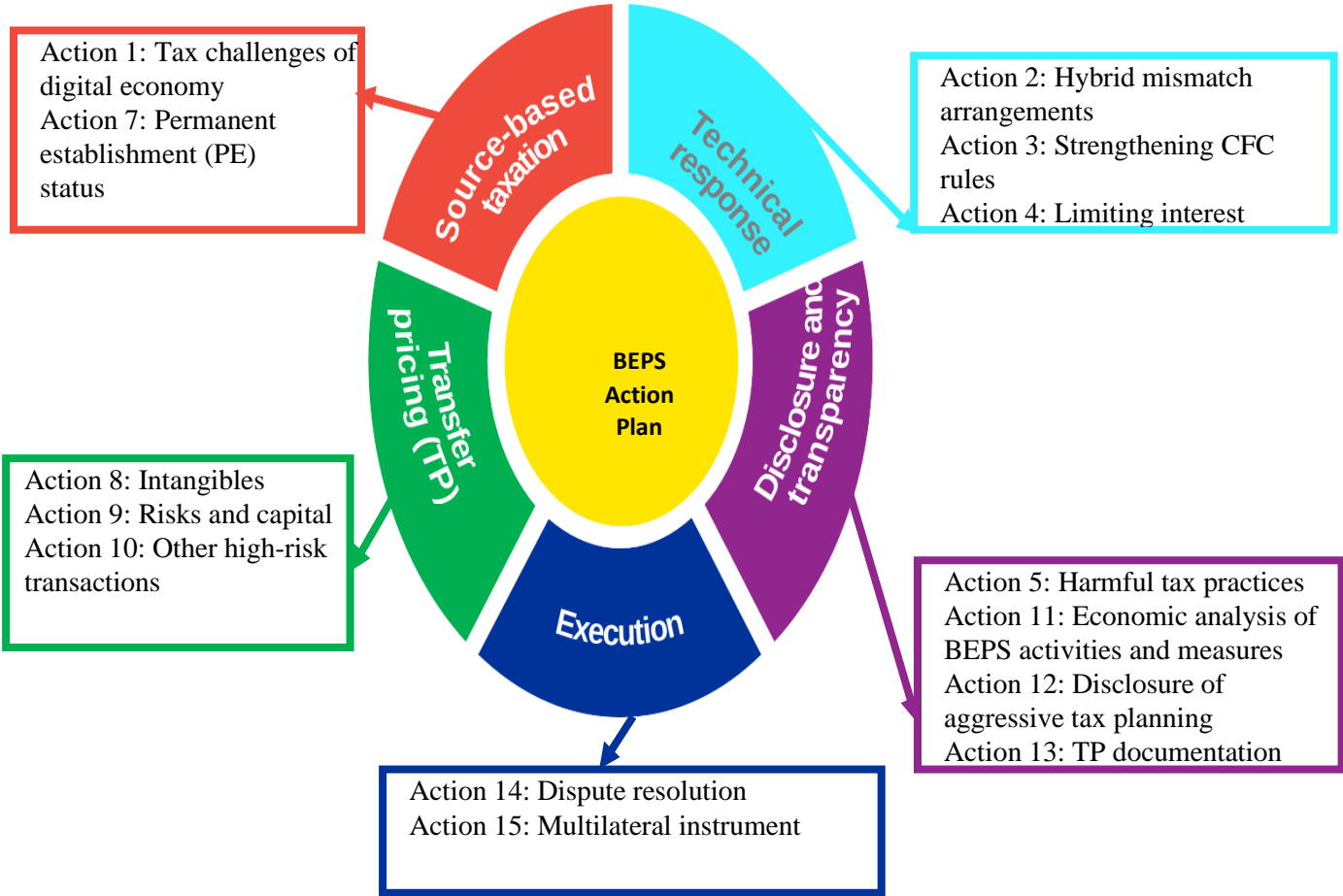


Figure 2.2: Snapshot of the OECD’s BEPS Action Plan (Bradbury, Hannapi & Moore, 2018)

Besides the OECD's BEPS action plans, the following are measures instituted to reduce the incidence of tax planning or avoidance.

2.6.1 Anti-Avoidance Regulations

Tax avoidance by MNCs has been at the top of the international tax policy agenda since the global financial crisis. The tight fiscal constraints in the aftermath of the crisis amplified long-standing concerns in many countries that large MNCs pay very low effective tax rates (Putra et al., 2018). Moreover, the revelation of aggressive avoidance schemes in the 2014 Lux leaks financial scandal and more recently the Paradise Papers reinforced public disquiet about the unfairness of the low effective taxation of some big MNCs (Niu et al., 2019). These concerns led to major new international initiatives to curb international tax avoidance, most notably the G20/OECD initiative described above (Johansson et al., 2017). They aimed to develop approaches that limit the opportunities for MNCs to shift profits artificially and thus enhance revenue mobilisation.

During the last few decades, countries have adopted various anti-avoidance regulations to mitigate tax avoidance by MNCs. These include, for example, the adoption of transfer pricing regulations, thin capitalisation rules, CFC rules and a general anti-avoidance rule (GAAR). These efforts have received considerable attention in light of the G20-OECD initiative on BEPS (Johansson et al., 2017). For instance, countries participating in the Inclusive Framework on BEPS commit to four minimum standards (for example, that of treaty abuse) and adhere to common approaches to adopt anti-avoidance legislation. EACs have also adopted an anti-tax-avoidance directive that requires its member states to implement a common set of rules to address tax avoidance.

The following section reviews the studies that have analysed the effectiveness of anti-avoidance rules in EACs.

2.6.2 Transfer Pricing Regulations

The principles of transfer pricing require that cross-border transactions between related firms should be valued at market price (the so-called *arm's-length principle*). When no comparable transaction exists, different valuation methods can be used, which can be based on cost plus a fixed mark-up or using economic models to split the relevant profit among entities, for example (Pun,

2017). Transfer pricing regulations offer guidance in the implementation of the arm's length principle. They often specify the methods that can be used to calculate transfer prices; determine documentation requirements; include various specific requirements in their application that are needed to support the transfer prices used; and set penalties if mispricing is detected or adequate documentation is not provided (Chand, 2016).

Their effectiveness in curbing international tax avoidance is supported in two concurrent studies, which show that the introduction and tightening of transfer pricing rules can diminish the tax sensitivity of corporate profits by 50%, although with much weaker effects for firms with many intangible assets or complex group structures (Beer & Loeprick, 2015). A later study shows that stricter regulations reduce reported profits of MNCs, possibly because of the combination of lower profit inflows into countries that are intermediate hubs for profit shifting and the higher compliance costs of MNCs (Saunders-Scott, 2013).

2.6.3 Thin Capitalisation Rules

Thin capitalisation rules and regulations limiting interest deductibility disallow the deduction of certain interest expenses when the debt-to-equity or the interest-to-earnings ratio of the debtor is considered excessive (Buettner et al., 2012). These rules apply either to total or related-party debt. Thin capitalisation rules deny interest deductibility above a certain threshold of either net interest payment (as a ratio of income) or net debt (as a ratio to equity) (Prastiwi & Ratnasari, 2019). The precise conditions of these rules vary between countries and over time. Empirical evidence suggests that, on average, well-designed thin capitalisation rules are effective in reducing debt shifting by multinationals (Blouin et al., 2014).

2.6.4 Controlled Foreign Company (CFC) Rules

CFC rules aim at eliminating the deferral of tax on certain income by using lower-tax foreign affiliates or the exemption on certain mobile foreign source income (Bandiyono & Murwanisari, 2019). CFC rules stipulate that the income of foreign subsidiaries be subject to domestic taxation without deferral if certain conditions are met. Thus, CFC rules expand the domestic taxation rights of territorial systems and limit the impact of deferral on worldwide systems. A recent study confirms this finding, by contrasting that the financial earnings of subsidiaries in 200 countries

just above and below the tax rate threshold; it reports a 20% difference in the level of reported profit owing to CFC rules (Ruf & Weichenrieder, 2012).

2.6.5 General Anti-Avoidance Rules (GAARs)

General anti-avoidance rules (GAARs) prohibit aggressive tax avoidance by denying tax benefits from a transaction that lacks economic substance, for instance (Baumann et al., 2020). A GAAR is typically designed to strike down lawful practices that are carried out in a manner that undermines the intention of the tax law, such as when a taxpayer has misused or abused that law (Prebble & Prebble, 2017). The authors maintain that most countries have introduced GAAR legislation or have equivalent rules or case law that states that if the primary purpose of an arrangement is to reduce tax, then the domestic tax authority can ignore it and remove any tax advantage obtained. Thus, any arrangements that confer a tax advantage should also have a demonstrable commercial purpose and be set up, at least in part, for reasons other than tax planning (Waerzeggers & Hillier, 2016).

2.7 Concept of Firm Value

A firm value is an economic measure reflecting the market value of a business (Marimuthu & Maama, 2021). The concept of firm value and its measurement is essential in corporate governance studies because it explains the variation in performance amongst firms. According to Simerly and Li (2000), measuring firm value has been a major challenge for scholars and practitioners. There are different aspects of firm value on which researchers can focus on their studies. The main focus has been on four drivers of value. The first three include the financial perspective (tracking financial performance); the customer perspective (tracking customer satisfaction, attitudes and market share goals); and the internal process perspective (tracking internal operational goals needed to meet customer objectives). The last is the learning and growth or innovation perspective (tracking intangible drivers for future success, such as human capital, organisational capital, training and informational systems) (Jabbour, Tao, Vanino & Zhang, 2019).

The financial performance perspective is the ultimate outcome measure for company success, and it is the most interesting aspect of firm value (Das & Goswami, 2019). Financial performance has been used to measure a firm's ability to achieve its economic goals. Various proxies have been

used to compute the financial aspect of a firm's performance. The literature has grouped these proxies into two major groups, the first group is accounting-based, and the second group is market-based (Assidi, Aliani, & Omri, 2016). According to Daily, Dalton and Cannella Jr (2003), accounting-based measures consider a company's current financial performance, whereas market-based measures consider investor perceptions of a company's potential performance. Different researchers have criticised each group. However, the literature recommends several accounting measurements instruments, namely, return on assets (ROA), and return on equity (ROE) and stock market valuation (Tobin's Q) (Assidi et al., 2016).

2.7.1 Accounting Measures of Firm Value

The most commonly used accounting-based measure is the return on assets (ROA), which various studies use (Farhat, 2014; King & Santor, 2008; Lin, Huang & Young, 2008). ROA sometimes referred to as return on investment, is an indicator of how profitable a company is or how efficient the management is in using assets to generate earnings. It is calculated as earnings after interest expenses and taxes divided by total assets. According to Farhat (2014), ROA is the most efficient measure of firm value and measures the relationship between tax benefits accorded by the revenue authority and corporate assets, which represent factors of the creation of value (Farhat, 2014). This ratio also represents a company's profitability levels from its business transactions (Assidi et al., 2016).

The second most used accounting measure of firm value is ROE, also known as return on net worth, which measures how much profit the company generates from the amount of the money invested by the investor (Farhat, 2014). The ROE focuses just on the equity component of the investment and specifies the earnings left over for equity investors after debt service costs have been factored into the equity invested in the asset (Tshipa, 2017). Similarly, ROE is the amount of net income calculated as a percentage of shareholders' equity, and it measures a corporation's profitability by revealing how much profit a company makes with the money that shareholders have invested (Elghuweel, 2015). Thus, a higher ratio indicates a higher return. The ROE is calculated by dividing a company's net income by the total shareholders' equity."

Other accounting measures include return on Sales (ROS), return on investment (ROI) and net profit margin (NPM). However, these accounting measures are the least used in the literature,

especially in studies related to tax planning and firm value. Researchers point out the advantages of using accounting-based measures in examining firm value. Generally, higher ROAs and ROEs denote the effective use of firm assets and equities by management when increasing the value of shareholders' wealth (Tshipa, 2017). Moreover, ROA and ROE are not affected by company size, and they provide an effective and easy solution for comparing companies (Farhat, 2014). Victor (2017) points out that ROA and ROE consider year-to-year fluctuations in implied business conditions better than a stock market rate of return. This is because a stock market rate of return reflects anticipated future changes that may hide the current fluctuations in business conditions.

However, the use of accounting-based measures has been criticised from different perspectives. Firstly, Ross, Westerfield and Jordan (2008) argue that accounting-based measures, such as ROA and ROE, are historical measures that are weak reflections of accurate future profits. Krivogorsky (2006) agrees that these measures are grounded in historical cost accounting and thus incapable of directly reflecting present business fluctuations in their valuations that the equity market rate of return does not indicate either. Secondly, Tayeh, Al-Jarrah and Tarhini (2015) argue that accounting-based measures are subject to changes and alterations in accounting methods, techniques and policies. Thirdly, Ross et al. (2008) hold the view that accounting-based measures ignore risk. Finally, according to Tayeh et al. (2015), accounting-based measures fail to reflect environmental and industry differences, such as employee and customer satisfaction. While accounting data is essential in corporate governance, accounting measures do not reflect all agency costs (Xian, Sun, & Zhang, 2015).

The accounting and reporting systems of a firm provide quantitative financial accounting data that consider its financial position and performance over a specified period. A firm's management provides financial statements that are subject to audit to prove that they are fairly presented according to general accounting principles and standards. Prowse (1992) observes that as stock market rates of returns are suspected of modifying conflicts between managers and shareholders, accounting measures examine the relationship between firm value and corporate governance. The role of accounting data in corporate governance mechanisms has been examined in previous studies (Farhat, 2014). However, accounting measures need to be carefully considered, as a study's results might be biased by using them. Accounting measures are normally established on historical

data, which could cause a lack of comparability, lead to distortions in firm valuation, and provide accounting valuation that may not be up to date.

2.7.2 Stock Market Measures of Firm Value

Other measures of firm value are stock market-based, which include Tobin's Q and the stock market rate of return. Tobin's Q, which is the ratio of a firm's market value to the replacement value of its assets, was introduced by Tobin (1967), and since its introduction, a number of studies have used this ratio as a measure of firm value (Farhat, 2014; Tobin, 1969; Tshipa, 2017). Tobin's Q measures firm value in terms of a company valuation. It is market capitalisation plus the total company debt divided by total assets (Weir, Laing, & McKnight, 2002). Kohl and Schaefer (2012) describe Tobin's Q as the current market value of the company divided by the replacement cost of the assets, which is measured by the book value of a firm's assets. In other words, Tobin's Q is the ratio of a firm's market value to its book value.

A firm's Tobin's Q is greater if it is more than 1, which implies that the firm is implementing a growth strategy, thus allowing investors to have a positive perception of the firm's growth opportunities (Otman, 2014). Moreover, a ratio greater than 1 indicates that the market value is higher than the recorded assets of a company. Hence, a higher Tobin's Q encourages companies to invest more capital, as the value of the company is more than the price they paid. In contrast, a ratio below one leads to investors having negative growth expectations and indicates that the firm should not reinvest in the same stock of assets. Perceiving a firm as a good or improving investment opportunity is an indicator of its sound corporate governance principles and structures (Evans & Loh, 2002).

The literature strongly favours the use of Tobin's Q as the primary measure of firm value. Its main benefit is that it reflects the value of intangible factors, such as management competence, growth opportunities and corporate governance, compared to other measures (Kohl & Schaefer, 2012). Consequently, a higher Q value indicates a more effective corporate governance and a more positive market perception of the company. However, a lower Q value suggests less effective corporate governance and greater managerial discretion (Weir et al., 2002).

In the current study, Tobin's Q is calculated as the book value of liabilities plus the market value of common equity divided by the book value of assets. Using the book value of assets rather than the replacement costs of assets is consistent with other studies (Garg et al., 2020). Research has also shown that the book value of assets is highly correlated with the replacement cost of capital (Elkinawy & Stater, 2011). This formulation of Tobin's Q was thought to be particularly appropriate for the current study because the firms in the sample raised funds through both equity and debt.

The foregoing discussion shows that various measures of firm value exist. However, Wei, Varela, D'Souza and Hassan (2003) argue that there has been no consensus on which firm value measures are appropriate. Thus, there is often no consensus on which performance measures should be employed (Farhat, 2014). Thus, a trade-off occurs between the advantages and disadvantages of market-based measures versus accounting measures. Eventually, in selecting measures of firm value, the suitability of measures concerning their environment and specified research objectives should be carefully considered (Garg et al., 2020).

As there is no consensus in the literature on the best measure of firm value, for the sake of the robustness of findings, it is better to use alternate measures (Farhat, 2014). Consistent with this view, Weir et al. (2002) state, "While Tobin's Q is the most common measure that has been used to date in modelling the relationship between ownership structure and corporate performance, it is important to test the robustness of reported results to the use of an alternate performance measure".

Therefore, understanding the different aspects of firm value measurement and choosing the most relevant measures are important for pursuing research objectives. Firm value measurements offer insights into appropriate measures for answering research questions. It should be noted that before selecting the measure to be used, a researcher should specify from which perspective the firm valuation is going to be based, that of insiders (management) or outsiders (shareholders). The two groups have different perceptions of firm value, as stipulated by Black, Jang and Kim (2006) who maintain that insiders and outsiders value a firm differently.

Previous literature sheds light on the profitability and value of a firm as measures (proxies) of firm performance. Key research has explained the relationship between corporate governance and firm value, along with more recent suggested amendments to this proxy. Generally, a considerable

number of recent studies on firm value and its relation to corporate governance practices have applied mainly accounting-based performance measures such as ROE and ROA, in addition to market-based measures such as Tobin's Q as proxies for firm value (Otman, 2014; Nugroho & Agustia, 2018; Khuong et al., 2020). In line with empirical studies from recent literature on firm performance, the current study used Tobin's Q to measure firm value. As the aim of the study was to examine the effect of tax planning on firm value, it implemented the measure that is widely used for listed companies.

Table 2.3 below provides a summary of the various measures of firm value and the way they are determined.

Table 2.3: Summary of measures of firm value

Category	Measure	Definition	References
Accounting-Based	ROA	Earnings after interest expenses and taxes (net income) divided by total assets	Farhat (2014), Zhang (2016), Assidi et al. (2016) and Victor (2017)
	ROE	Earnings after interest expenses and taxes (net income) divided by total equity	Krivogorsky (2006), Elghuweel (2015) and Tshipa (2017)
Market-Based	Tobin' Q	Book value of equity plus total liabilities divided by book value of total assets	Tshipa (2017), Nugroho and Agustia (2018), as well as <u>Khuong et al. (2020)</u>

2.8 Corporate Governance

The concept of corporate governance has become a concern due to financial scandals which caused the collapse of a large number of well-known companies such as Adelphia, Enron and WorldCom (Spanos, 2005; Kovermann & Velte, 2019). Corporate governance is the system of rules, practices and processes by which a company is directed and controlled (Maama et al., 2019). The collapse was occasioned by wrongdoings, incompetence and negligence on the part of the management, auditors and financial market operatives. These scandals, which shook the confidence and trust of investors, resulted in demands for improved corporate governance practices (Baydoun, Maguire, Ryan & Willett, 2013). For instance, the International Monetary Fund (IMF) required governance

improvements to be included in its debt relief program. Moreover, the OECD issued its Principles of Corporate Governance to assist both member and non-member countries to evaluate and improve their legal, institutional and regulatory frameworks for better corporate governance (Khanchel, 2007).

According to Adnan, Hay and Van Staden (2018), corporate governance is the manner in which power is exercised in the management of a company's resources for development. Bhagat and Bolton (2019) define corporate governance as the set of rules and practices regulating relationships among participants in a business enterprise and governing decision making within that enterprise. Shleifer and Vishny (1997) maintain that corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment. Dittmar, Mahrt-Smith and Servaes (2003), as well as Maama et al. (2019), hold that a firm's compliance with the principles of good corporate governance guarantees shareholder value by ensuring the proper utilisation of the firm's resources, which results in access to capital and improving investor confidence. Spanos (2005) points out that effective corporate governance is significant for economic growth, the reduction of risk to investors, attracting investment capital and improving the performance of companies. This suggests that corporate governance plays a vital role in monitoring different actors and harnessing planning procedures.

Corporate governance distributes rights and responsibilities amongst various company members, such as the board, managers, shareholders and other stakeholders. In addition, it ensures that rules and procedures for making decisions regarding corporate affairs are clear (Feleagă, Feleagă, Dragomi, & Bigioi, 2011) and is an internal mechanism for monitoring management. Good corporate governance is an effective tool for enhancing firm value and protecting shareholders' interests (Ghabayen, 2012; Adnan, Hay & van Staden, 2018). Ghabayen (2012) emphasises good corporate governance as providing a connection between a firm and its environment while securing the critical resource of shareholders and attracting new investors as well as capital funds.

Corporate governance has emerged as a critical topic in transition economies in recent years. Managers, directors and owners have understood the benefits of a good corporate governance structure (Kovermann & Velte, 2019).

2.8.1 Corporate Governance in East African Countries

Like other African countries, the corporate governance approaches of EACs heavily rely on OECD principles, the South African King's report and the Commonwealth Association for Corporate Governance pronouncements (Wanyama, Burton & Helliard, 2013; Mnzava, 2022). The following sections will discuss corporate governance in Kenya, Tanzania and Uganda. However, before this, the current section will discuss the structure of the East African Community, the legal system of the EACs and their capital market infrastructure.

The original East African Community comprised Kenya, Tanzania and Uganda. Currently, it has six member countries, namely Burundi, Kenya, Rwanda, South Sudan, Tanzania and Uganda. Most of these countries, particularly the original members (Kenya, Tanzania, and Uganda), are former colonies of the UK and are currently members of the Commonwealth. Therefore, most of the legal and judicial systems of these EACs are based on English common law.

Although the capital markets of the EACs are still developing, Kenya's capital market is relatively more developed. In fact, the 2015 Ibrahim Index of African Governance (IIAG) highlights Kenya's performance as amongst the top five improvers in governance since 2011. However, findings of the 2016 Doing Business revealed weaknesses in Kenya's regulatory framework for protecting shareholders' interests. This report places Kenya 115th amongst 189 countries and 17th amongst the 47 Sub-Saharan African countries with regard to the protection of minority interests and shareholders' governance. The institutional and legal frameworks of Uganda and Tanzania do not deviate too much from those of Kenya, which facilitate the regional integration of capital markets.

The subsequent sections discuss corporate governance in Kenya, Tanzania and Kenya.

2.8.2 Corporate Governance in Kenya

As Kenya is one of the most established capital markets in Africa, it has a relatively strong corporate governance structure (Waweru & Prot, 2018; Kariuki et al., 2021). Although both Kenyan laws and international standards guide corporate governance practice in Kenya, the revised Companies Act, 2009, which stipulates the basic structure and primary rules of running companies in Kenya, provides the main legal guidelines (Onware et al., 2020). Moreover, the Act establishes the positions of directors, duties and provisions for the protection of shareholders.

Waweru and Prot (2018) point out that prior to promulgating this Act, in 2000, Kenya produced and published her first national code, the Private Sector Corporate Governance Trust (PSCGT), which provides guidelines to be adopted voluntarily in terms of the *comply or explain* enforcement concept. The key recommendations of the PSCGT were that companies should establish audit committees composed of non-executive directors, improve the quality of financial reporting and extend the scope and duties of external auditors.

According to Barako (2007), the PSCGT contributed substantially to developing the guidelines for good corporate governance in public companies that were issued by the Capital Markets Authority (CMA) in 2002. All listed companies in Kenya, which meet the listing requirements provided and maintained by the Nairobi Stock Exchange (Waweru & Prot, 2018), are obligated to implement these guidelines that mainly concern boards of directors and the role of good corporate governance in maximising shareholder value and shareholder's rights (Waweru & Prot, 2018; Azegele et al., 2021). In addition, statutes dealing with professional bodies, such as those of lawyers, accountants and public secretaries, impact the standards of good corporate governance.

2.8.3 Corporate Governance in Tanzania

The concept of corporate governance in Tanzania is very much in its infancy stage. It receives little attention (Nyaki, 2013), which reflects a lack of awareness of its importance for economic development. However, the growth of the private sector in Tanzania requires sound corporate governance to ensure that the interests of investors are protected. Thus, various bodies, such as the Confederation of Tanzania Industries (CTI), the Tanzania Private Sector Foundation (TPSF), the Tanzania Chamber of Commerce and Industry and the Institute of Directors Tanzania (IoDT), are facilitating dialogue related to the business environment and corporate governance (Mnzava, 2022).

Corporate governance in Tanzania is regulated by legislation, such as the Capital Market and Securities Act, 1994, and the Companies Act, 2002. The enactment of the Tanzania Capital Market and Securities Act, 1994, established the Capital Market and Security Authority (CMSA) to regulate the capital market in Tanzania, promote the Tanzanian security market and establish a stock exchange. The Dar es Salaam Stock Exchange (DSE), which began operation in 1997 to regulate the activities of the listed companies in Tanzania, is the sole stock exchange in the country.

Companies seeking a listing on the stock exchange must comply with the CMSA Guidelines on Corporate Governance Practices by Public Listed Companies in Tanzania issued in 2002.

Nyaki (2013) suggests that the foundation of Tanzania's corporate governance practices is the Capital Market and Securities (CMS) Act, 1994 that regulates access to business, the conduct of business and disclosure by both investing companies and market operators. Likewise, the CMS Act ensures business stability and the protection of the interests of all investors. In addition, the Act ensures that businesses in Tanzania are conducted with a high level of transparency and integrity.

Matinde (2013) maintains that the Companies Act (CA), 2002, which came into effect in 2006, has provisions that regulate corporate governance. The CA Act introduced a modern shareholder-oriented legal framework, which includes the Anglo-Saxon (or Anglo-American) corporate governance model and regulates the statutory duties and the responsibilities of directors, as well as defining the responsibilities of boards of directors in Chapter VII. Based on the provisions of the Act, directors are required to protect the interests of shareholders and present their companies' annual reports at annual meetings with shareholders, thus allowing them to evaluate firm value and to make decisions regarding their investments in the companies.

Zhang et al. (2017) point out that the statutory rules of corporate behaviour are contained in company law, such as Tanzania's 2002 national code of corporate governance in 2002. The Guidelines on Corporate Governance Practices by Public Listed Companies in Tanzania emphasise the need for boards of directors to ensure that members comply with good governance practices, relevant laws and regulations and auditing and financial reporting standards. In 2008, the Bank of Tanzania (BOT) also issued guidelines for boards of directors of banks and financial institutions, stipulating their duties, responsibilities, composition, conduct and committees.

2.8.4 Corporate Governance in Uganda

Although similar to those of the other EACs, the corporate governance structure in Uganda is in its embryonic stage, unethical business behaviour, extensive corruption and several incidences of corporate scandals (for example, the collapse of the Greenland Bank) made the need for effective monitoring of business organisations and promoting best practices essential in Uganda (Musaali,

2010). Like other EAC markets, after embracing the Economic Recovery Programme (ERP) during the 1980s, Uganda aggressively adopted policies aimed at reducing the direct role of government in the economy and encouraging the participation of the private sector in transforming the economy (Otweyo, 2001; Marus et al., Lwanga & Basemera, 2021).

Corporate governance reforms in Uganda have gone through many steps. In 1993, the Government of Uganda enacted the Public Enterprises Reform and Divestiture (PERD) Statute to operationalise its PERD Statute of 1991 and Action Plan. The PERD of 1993 aimed to privatise more than 100 state-owned enterprises (SOEs) (Wanyama et al., 2013). In 1996, the CMA of Uganda was established following the enactment of the Capital Markets Authority Act, 2000 (revised). In exercising its powers, the CMA issued the Capital Markets Corporate Governance Guidelines, 2003. Section 2, Part I of the Guidelines, highlights that the CMA developed the guidelines as a minimum standard for good corporate governance in public companies and issuers of corporate debt in Uganda. The guidelines cover best practices related to board composition, the separation of the roles and responsibilities of the chairperson and the chief executive officer, the rights of shareholders and the roles of audit committees. Surprisingly, these guidelines are not mandatory, which means that they have a limited impact on the management of firms in Uganda (Nkuutu et al, 2020).

The Institute of Corporate Governance of Uganda (ICGU) was established in 1998, membership of which is open to both corporate bodies and individuals. In 2001, the ICGU published its Recommended Guidelines for Corporate Governance, which are also not mandatory but present a basic framework for corporate governance by indicating best practices related to boards of directors, shareholders, regulatory bodies, investors and other stakeholders (Musaali, 2010). However, the ICGU recommends that the Guidelines should be used by all corporate bodies in Uganda, regardless of their ownership or size, because both public and private sectors are equally affected by corruption; bad leadership; public mistrust; and a lack of transparency and integrity (Wanyama et al., 2013).

The listing requirements of the Uganda Securities Exchange direct firms to comply not only with the listing rules of the exchange but also with the laws (for example, the Companies Act) and requirements of various regulatory and supervisory authorities (for example, the CMA). However,

the Central Bank, through the Financial Institutions Act (FIA), 2004, made corporate governance regulations compulsory for all financial institutions. The FIA sets a minimum number of board members and requires all directors to be fit and proper persons. The Act establishes disclosure requirements, the establishment of audit committees, and duties of the internal and external auditor of the Central Bank, for example.

2.9 Chapter Summary

This chapter discussed the major concepts relevant to this study, namely tax, tax planning, firm value and corporate governance. The chapter defined tax and taxation as well as explaining their history and purpose. Furthermore, the chapter provided an overview of tax planning as well as explaining its objectives, constraints and channels. Moreover, how the global community has tried to reduce tax-planning practices was discussed.

The review of previously used measures of tax planning showed that many of the measures could identify tax planning activities. While there are other measures for tax planning, besides the ones reported, they are not widely used by researchers. It was, therefore, imperative to prove the viability of the measure used to identify tax planning in the current study. Hanlon and Heitzman (2010) postulate that information related to tax planning is not easily disclosed because it is done surreptitiously; therefore, all measures of corporate tax avoidance may be subject to error and have limitations.

Lastly, the chapter discussed firm value and corporate governance. The literature demonstrated that corporate governance is an important system that can control agency costs. The literature review showed that a considerable number of recent studies on firm value applied mainly accounting-based measures of firm value, such as ROE and ROA, in addition to market-based measures, such as Tobin's Q (Otman, 2014; Nugroho & Agustia, 2018; Khuong et al., 2020). In line with empirical studies from recent literature on firm performance, the current study used Tobin's Q as a proxy to measure firm value. As the aim of the study is to examine the effect of tax planning on firm value, the research implemented the measure that is widely used for listed companies, Tobin's Q, which is considered a proxy for market return in the study.

CHAPTER THREE

THEORETICAL LITERATURE REVIEW

3.1 Introduction

In Chapter One, this thesis introduced the research, while chapter two reviewed the major concepts of the study, namely tax planning, firm value and corporate governance. The present chapter provides the theoretical background of the study that aimed to provide a coherent explanation of observed or experienced phenomena (Gioia & Pitre, 1990). Thus, the researcher looked at theories about related phenomena to predict the outcome of the current related research agenda. Lewis and Grimes (1999) argue that in an empirical study, theories are important tools that researchers use to predict the association between variables. Therefore, the current study used theories and/or assumptions in developing the hypotheses to be tested to answer the study objectives. The study's assumptions, predictions and hypotheses development are based on five theories: the agency theory, the legitimacy and stakeholder theories, the political power theory, the political cost theory, and the resource dependence theory.

3.2 Agency Theory

According to Zemzem and Ftouhi (2013), historically, tax literature has not been able to differentiate between individual and corporate tax planning; thus, previous models of corporate tax planning have been based on individual taxpayer compliance. However, Chen and Chu (2005), Crocker and Slemrod (2005) as well as Slemrod (2004) distinguish corporate tax planning from individual tax compliance in the context of agency theory, which posits that in the corporate environment, a principal-agent relationship exists in that management (agent) runs a firm on behalf of shareholders (principles).

Although tax planning might be viewed as always being beneficial to a firm and its shareholders, the agency theory highlights the existence of agency cost (expenses due to a conflict of interests between principle and agent) in tax planning decisions. In other words, there is a separation between shareholder ownership and management control of firms, which are no longer in unison. This leads to information asymmetry between shareholders and management, whereby the former

has less information than the latter. Thus, tax-planning information is not made available to shareholders by management that aims to prevent its tax-planning activities from being detected by revenue authorities.

Desai and Dharmapala (2009a) posit that the opaqueness of tax planning leads to managerial rent diversion whereby a managers maximise their wealth at the expense of the firm and its shareholders. Rent diversion/rent seeking/rent extraction is creating wealth whereby a firm's management seeks to obtain financial gains through alteration/manipulation of the economic environment. Similarly, Jensen and Meckling (1976) maintain that because of conflict of interests between managers and shareholders, there is a high risk of management misusing a firm's resources through tax planning activities. The authors argue that the two conflicting parties have different objectives for wealth maximising.

Critics of agency theory note that control mechanisms based on agency theory are not only expensive but also economically ineffective because mechanisms protective of shareholders' interests may obstruct the implementation of strategic decisions, may limit collective actions, and may distort the market (Maama, 2020). Critics of agency theory further point out that many studies that draw from it concentrate on the effectiveness of various contract types that are intended to reduce moral hazard, and that they neglect the possibility of institutional influences on the nature and breadth of agency theory.

Despite these criticisms, agency cost emanating from agency theory may preclude the benefit of tax planning and may lead to a loss in shareholder value. Therefore, the theory supports the notion of corporate governance to mitigate agency costs incurred because of inappropriate tax planning decisions (Nugroho & Agustia, 2018). The current study used the agency theory to examine whether managers of firms use the separation of power and control between them and shareholders to pursue their own interests instead of those of shareholders.

3.3 Legitimacy and Stakeholder Theories

The interpretation of agency theory has been challenged by scholars who consider stakeholders' interests in a firm's operations rather than the relationship between management and shareholders. Some authors maintain that firms are managed to maximise shareholder value, as emphasised by

the agency theory, but the interests of other stakeholders are also important (Hill & Jones, 1992). Thus, according to theories related to corporate social responsibility (CSR), particularly the legitimacy and stakeholder theories, there is an implied social contract between the corporation and the society in which firms operate. Stakeholder theory maintains that a business is accountable to stakeholders with whom it has an interconnected relationship, whereas legitimacy theory is based on the idea that a social contract exists between business and society (Maama, 2020). They are different theories, but they both consider more than the management and shareholders of a firm, and therefore have been combined in this section of the thesis.

In this context, Preuss (2010) argues that tax payments to the government constitute an act of social responsibility. From this perspective, a firm exists beyond the relationship between management and shareholders (Waddock & Graves, 1997; Maama & Mkhize, 2020). Prior studies have established a link between CSR and tax planning, finding that more socially responsible firms are less tax avoidant (Huseynov & Klamm, 2012; Lanis & Richardson, 2011). In addition, Slemrod (2004) maintains that there are sufficient indications that the public considers the payment of taxes to the general community.

Legitimacy and stakeholder theories emphasise the issue of reputation risk. These theories suggest that firms should be lawful in fairness to the society and environment around them; otherwise, they cannot be sustainable. Richardson et al. (2013) and Maama (2020) posit that society expects firms to be legitimate in their operations. Thus, when making decisions, firms should consider the interests of all stakeholders. The legitimacy theory claims that tax planning might be legal and may potentially increase the after-tax return of the firms, but society may consider it unethical and irresponsible. Therefore, these theories postulate that firms should pay taxes to the government as contributions to the social and economic development of a country (Hoopes et al., 2018).

Despite appearing to gain acceptance, a stakeholder theory of the company is unpopular among many academics (Maama, 2020). Some claim that stakeholder theory lacks definition and cannot, therefore, be operationalized in a form that permits scientific investigation (Loke, Ismail & Hamid, 2016). Others believe that stakeholder theory does not provide any criteria for making decisions that would appropriately guide corporate governance. These authors claim that that stakeholder theory is hollow and presents an unreal picture of how businesses function.

The stakeholder theory assumes that a firm that practices tax planning will lose trust in the eyes of society and the environment in which it operates, which may disturb its operations and sustainability. For instance, Campbell and Helleloid (2016) point out that in 2012, Starbucks in the UK faced a public relations furore over its failure to pay British corporate income taxes. While the tax avoidance practices used by Starbucks were common among multinational companies, Starbucks had been very public in its commitment to being socially responsible and an upright organisation in the communities in which it operates by paying fair wages to employees and fair prices to coffee growers in developing countries. Thus, its critics found it easy to point out that not paying its fair share of taxes was inconsistent with the image Starbucks was portraying to consumers. This case poses questions about the strategic, legal, public relations and ethical implications of strategies for tax minimisation, especially when companies portray themselves as being responsible members of the communities in which they operate.

The foregoing discussion indicates that reputation risk is the most serious threat to a firm's existence. Therefore, these theories suggest that a firm's strategies to reduce or avoid its taxes may benefit shareholders but at the expense of society (Sikka, 2018), given that taxes are used, in part, for governmental infrastructure and social programmes. In summary, legitimacy and stakeholder theories indicate that firms should be less tax aggressive and seek to fulfil their implied social contract to gain trust and legitimacy (Preuss, 2010). Paying taxes is one of the most fundamental ways corporations can engage with broader society, as tax revenues are the lifeblood of a social contract (Visser et al., 2017).

The government, stakeholders and the international community urge companies to include tax payment as corporate social responsibility (Zeng, 2019), especially in light of the significant revenue loss through aggressive tax planning that governments experience, particularly in less-developed nations. Large multinational companies have been constantly accused of tax dodging (Visser et al., 2017). For example, in 2016, Google, Apple, Facebook, Starbucks, IKEA, Amazon, GAP and Microsoft were accused of aggressive tax planning strategies, resulting in governments experiencing a revenue loss of billions of dollars (Loke, Ismail & Hamid, 2016). While the authorities accused Google because of its double Irish, Dutch sandwich strategy (a complex tax avoidance scheme) to reduce its tax liabilities, Apple was under fire for its manipulation of subsidiaries in Ireland in the company's attempt to reduce its corporate tax liability (Barrera &

Bustamante, 2018). The public outcry about aggressive tax planning has become more apparent following the leak of Panama Papers, causing the media, NGOs and societies to demand more responsible corporate tax practices. Thus, both legitimacy and stakeholder theories can sufficiently be used to explain how a firm's tax planning activities may indirectly harm society. It is expected that firms could consider the particular needs of the community in which they operate before they engage in any tax planning activities.

3.4 Political Cost Theory

The political cost theory to which some studies refer as the positive accounting theory, has been used by previous accounting studies to explain why companies voluntarily become socially responsible and make voluntary disclosures (Belz et al., 2019). This theory assumes that firms will use various accounting methods to avoid attracting the attention of politicians who eye high profit industries. Following the study of Watts and Zimmerman (1978), several empirical studies have directly sought to provide evidence for the political cost hypothesis as an explanation for a firm's voluntary disclosures (Lemon & Cahan, 1997; Belz et al., 2019). Several related studies have also sought to use the political cost hypothesis to explain other types of voluntary disclosure, including value-added statements (Deegan & Rankin, 1996), disclosures by statutory authorities (Lim & McKinnon, 1993) and disclosures in pursuit of reporting excellence awards (Carroll, 1979).

The political cost hypothesis argues that firms may be reluctant to practise tax planning if they are seen as unpatriotic or irresponsible corporative citizens. There are instances where political costs have forced firms to alter choices, including not minimising taxes to the extent that they would wish to. For example, because of domestic political pressures, Stanley Works chose not to move their headquarters offshore, which would have resulted in a substantial tax saving. Chan et al. (2013), for instance, examined firm size (as a proxy for a firm's political cost) and its relationship with ETR and reported that firm size is positively associated with a firm's ETR. This is consistent with anecdotal evidence of larger firms investing in tax planning generating negative media attention (Hanlon & Slemrod, 2010; Sam & Zhang, 2019).

In addition, Belz et al. (2019) posit that larger firms face more government scrutiny. The higher visibility of larger firms causes them to become victims of greater regulatory actions from the government and vehicles for wealth transfers (Zimmerman, 1983). Thus, large firms endure higher

political costs because of their size. As taxes are one part of the total political costs borne by firms, the political cost theory claims that larger firms have higher ETRs (less tax aggressive). The relationship between firm size and political costs has been intensively debated in accounting research for several decades. Tehrani et al. (2011) maintain that the possibility of public policy and state action being directed at larger and more profitable firms is high. Madhani (2016) observes that large firms have a higher degree of public visibility and thus are more exposed to public and social pressure than smaller firms are. Boynton, Dobbins and Plesko (1992) indicate that larger firms are generally subject to closer surveillance from both financial markets and revenue authorities (Belz et al., 2019).

Watts and Zimmerman (1986) point out that the political cost theory can be subdivided into two main arguments. Firstly, larger firms are subject to more governmental regulations. Secondly, they are more prone to political and public pressure/scrutiny, which forces them to be socially responsible and adjust their actions and corporate behaviour to what their social environment expects. Several studies have been conducted in support of this argument (Graham, Hanlon, Shevlin & Shroff, 2013; Dyreng, Hoopes & Wilde, 2016). The political cost theory can be empirically examined by considering the relationship between taxes as a component of political cost and firm size. If larger firms indeed face systematically higher ETRs, compared to smaller firms, this would be consistent with the political cost theory (Sam & Zhang, 2019). Zimmerman (1983) empirically examines the size-ETR relationship and finds it to be positive. The author concludes that this finding is evidence for using firm size as a proxy for political cost.

3.5 Political Power Theory

The political power theory developed by Salamon and Siegfried (1977) stipulates that larger firms have economic and political power compared to small firms. Larger firms use their economic and political advantage to mitigate their tax burden. Large firms have the financial ability to pay tax experts to engage in aggressive tax planning and can manipulate the political process to their advantage (Wu, Wang, Luo & Gillis, 2012). Supporting this theory, Dyreng et al. (2008) argue that larger firms have relatively smaller effective tax rates than small firms. Rego and Wilson (2012) explain that economies of scale can significantly affect a firm's ability to reduce its tax burden.

Porcano's (1986) study supported this notion by finding that larger firms had smaller average ETRs in 1982 and 1983. Rego (2003) looked at 19,737 US corporations during a seven-year period from 1990 to 1997 and found that economies of scale can significantly affect a firm's ability to reduce its tax burden through tax planning. Derashid and Zhang (2003) found a negative relationship between firm size and ETRs in Malaysia, and Richardson and Lanis (2007) found a significant negative association between ETRs and firm size, using a sample of publicly listed Australian firms from 1997–2003.

However, a few studies did not find a significant relationship between firm size and tax planning as measured by ETR. Stickney and McGee (1982) examined the extent of the neutrality of the corporate income tax system by determining whether differences in average ETRs are due to systematic differences in firms due to firm size and other characteristics. They found that no significant relationship exists between ETR and firm size. As a control variable in Phillip's (2003) study, firm size did not have a significant relationship with ETRs. While the empirical evidence of the relationship between firm size and ETRs seems conflicting, Wilkie and Limberg (1990) along with Kern and Morris (1992) showed that differences can be attributed to the different time periods used in each study. Gupta and Newberry (1997) assert that inconsistent results suggest that firm-size effect could be sample-specific and not likely to exist over time in firms with longer histories.

Similarly, Wu et al. (2012) posits that large firms have greater political power than small firms do. Furthermore, the author suggests that large firms can use their resources and power to negotiate their tax burden or influence legislation in their favour (for example, through lobbying activities), resulting in lower ETRs for large firms compared to small firms. This study's results conformed to the finding of several previous studies (Gupta & Newberry, 1997).

3.6 The Resource Dependence Theory

In the tax-planning context, the resource dependence theory explains how the relationship between a firm and its environment, on the one hand, and other organisations, on the other, can be used in tax management (Delke, 2015). The theory postulates that organisations need resources to sustain their existence in the long term. Furthermore, it contends that firms can only obtain these resources

from their environment and that other organisations are interested in and competing for the same resources in this environment (Fink, Edelman, Hatten & James, 2006).

While having crucial resources, including skills, which will provide a competitive advantage, is essential in strategic management. According to Katila, Rosenberger and Eisenhardt (2008), companies usually remain inadequate in obtaining them and sustaining their flow, and therefore establish relationships with other organisations to meet their needs. Additionally, companies need to monitor continuously the opportunities and threats, which are created by the market dynamics and balances of power to ensure that the flow of resources is maintained. For this reason, they tend to increase the level of coordination and the control process (Mintzberg, Ghoshal, Lampel & Quinn, 2003). Therefore, they seek opportunities to decrease uncertainty and manage dependence by purposefully structuring their exchange relationships, establishing formal and semi-formal links with other businesses (Salam, Ali & Kan, 2017).

The resource dependence theory suggests that a larger number of directors on boards brings a wide range of knowledge and expertise from different fields, which add value to the board. Furthermore, the theory argues that an increased number of board members may lead to an increase in the resources available to the board and organisation because each director may have various connections with different industries. Thus, these directors bring fundamental skills and resources, which will provide the competitive advantage that is very important in tax management strategies. In other words, different directors have access to various resources and when the number of these directors is increased, resource availability will also increase, which in turn will increase the board's effectiveness in monitoring managerial tax management actions. This theory, therefore, hypothesises that an increase in the number of directors increases the ability of the firm to manage its taxes.

3.7 Chapter Summary

This chapter discussed the five theories that form the basis for the study: the agency theory, the legitimacy and stakeholder theories, the political power theory, the political cost theory, and the resource dependence theory. According to the literature, the agency theory highlights the existence of agency cost in tax planning, due to conflict between principle (shareholders) and agent (management). The separation between shareholder ownership and management control leads to information asymmetry between shareholders and management whereby information related to tax planning is not made available to shareholders to prevent the schemes to be detected by revenue authorities. The legitimacy and stakeholder theories articulated that firms are managed to maximise shareholder value, but the interests of other stakeholders are also important. Thus, these theories hold that tax payments to the government constitute an act of social responsibility, which indicates a link between CSR and tax planning. This suggests that more socially responsible firms are less tax avoidant because there are sufficient indications that the public considers the payment of taxes as a payment to the general community.

The political cost theory hypothesised that firms may be reluctant to manage their taxes if they will be seen as unpatriotic or as irresponsible corporations. The political power theory postulates that larger firms have economic and political power, compared to small firms, and therefore use their economic and political advantage to mitigate their tax burden. The resource dependence theory explains how the relationship between a firm and its environment, on the one hand, and other organisations, on the other, can be used in tax planning. The theory postulates that organisations with access to resources such as human resources can use that to their advantage to reduce their tax burdens and sustain their existence in the long term. The next chapter discusses the methodology adopted in the study.

CHAPTER FOUR

METHODOLOGY

4.1 Introduction

In the previous chapter, the thesis discussed the theoretical background of the study. Six theories that were used to develop hypotheses were discussed. This chapter discusses the methodology used in the study to provide answers to the research questions. It specifically discusses the research design, the research paradigm, data type, the data collection, the population, sample selection and model specification tests (diagnostic tests).

4.2 Research Design

The study was designed to examine tax planning and its impact on firm value. Moreover, the study aimed to understand how the strength of corporate governance moderates the relationship between tax planning and the value of listed firms in EACs. To achieve this aim, firstly, the study examined the trend and level of tax planning in EACs. Secondly, it investigated the determinants of tax planning in EACs. Thirdly, it investigated whether tax planning in listed companies in EACs improved firm value. Lastly, the study examined whether the strength of corporate governance moderates the relationship between tax planning and firm value.

To achieve the stated objectives, the study used a quantitative research design. Collis and Hussey (2009) posit that quantitative research collects information that yields statistical findings. Quantitative studies involve the measurement and analysis of causal relationships amongst variables of interest (Collis & Hussey, 2009). The quantitative research design was chosen because solving the research problem required collecting data that could be statistically analysed to understand the relationship between the variables discussed in the paragraph above.

The study used secondary data that, according to Creswell and Creswell (2017), are gathered for a purpose that differs from the one for which they were originally collected. Moreover, it is unnecessary to collect primary data if there are adequate secondary data to meet the research objectives. The choice for this research design is based on the fact that it makes the data gathered more reliable and less open to argument. In addition, secondary data was used for the study because

it is economical, saves efforts and expenses and helps to improve the understanding of the problem. It further provides a basis for comparison for the data that is collected by the researcher.

4.3 Research Paradigm

Management research studies are based on a research paradigm, which is based on methodological assumptions that guide researchers in adopting a method and generating new knowledge. A research paradigm is a framework that determines how research is conducted (Collis & Hussey, 2009). Although management research can adopt either positivism or interpretivism as a research paradigm (Becker et al., 2012), the study followed the positivism paradigm that is based on the assumption that only scientific (factual) knowledge is trustworthy and should be based on either exploratory or descriptive objective observations.

Researchers that adopt the positivism paradigm are independent of the study and do not consider participants' perceptions or emotions, for instance. The positivist paradigm is employed when quantitative data are considered in finding the causal relationship between variables (Becker et al., 2012). McMillan and Schumacher (2010) posit that positivism is applied when a study is based on theories that are used to formulate hypotheses to be tested statistically to provide factual conclusions. Thus, the study collected quantitative secondary data for statistical analysis.

4.4 Data Type

The study used panel data, which allowed the pooling of observations of successive cross-sectional data for twelve years. Panel data is a suitable dataset because of its short time series dimension, which provides results that are not affected by the deficiencies of pure time series or cross-sectional studies. Studies that employ panel data are based on a large number of observations. The benefit of using panel data is that it reduces collinearity among independent variables and also increases the degrees of freedom (Hsiao, 2014; Wooldridge, 2009), and thus the efficiency of the econometric estimation improves. Moreover, the heterogeneity of the individual variables of the firms could be controlled by using panel data (Wooldridge, 2009). The main advantage of panel data is that they solve the difficulties involved in interpreting regression coefficients in the framework of a cross-section or time series regression, as explained below.

In panel data research, a balanced panel is used whereby all participants that make up the sample are observed over the same period. However, in most practical applications, datasets are rarely balanced; thus, unbalanced panel or missing data is pervasive. For example, because of economic units electing to drop out of the sampling process, attrition arises. Another case is that individuals do not disappear from the panel, but certain variables are unobserved for at least some periods. Therefore, similar to previous studies (Tshipa, 2017; Tusubira, 2018; Wahab & Shaipah, 2010; Zhang, 2016), the current study used unbalanced panel data.

4.5 Data Collection

The dataset for the study involved categories of information, such as financial, taxation and corporate governance data. All the above data were archival, as companies were required to publish this information publicly in annual reports (audited annual reports and accounts). Therefore, the data sources were Bloomberg, McGregor, financial stock markets of the EACs and the websites of respective companies. The data on the collected variables of interest reflected a 12-year period, from 2008 to 2019.

In addition, the corporate governance practices of the firms were manually collected from the annual reports of the firms. The taxation data used to compute the proxy for tax planning could be obtained from either tax returns or financial statements of the selected firms. However, these two sources might give different information because of divergent objectives between the financial accounting standards and tax accounting systems. For example, Plesko (2007) provides evidence for the divergence between the tax planning estimates using tax returns and those of financial statements.

However, Graham and Mills (2008) argue that the two sets of information sources are highly correlated. Nevertheless, although tax returns produce accurate information, they are highly confidential and not easily accessible. Therefore, the data from financial statements is the only publicly available source for estimating tax planning. Thus, the study used data from the annual reports of firms. All the data used for the study were publicly available, hence no ethical issues arose from the data collection.

Table 5.1 below provides information on the various data used in the study and their sources.

Table 5:1 Data used and sources

	Data Used	Source of Data	Information Extracted
i	Financial Information	Bloomberg and MacGregor	Profit before taxes; profit after taxes; net profit, the market value of equity; book value of equity; capital expenditure; total assets, fixed assets; total equity; total debts; and long-term debt
ii	Taxation	Websites of Companies	Total tax expenses; cash tax paid
iii	Corporate Governance	Manual Extractions from Annual Reports	Number of board directors; executive directors; non-executive directors; number of directors with financial expertise; number of women on board; remuneration of directors; distribution of share ownership

Source: Researcher's Classification

4.6 Study Population

The population for this study was firms listed on the stock exchanges of EACs. This type of population is a finite population as there are a definite number of firms listed in EACs. The study targeted listed firms from all six countries of East Africa, including Burundi, Kenya, Rwanda, South Sudan, Tanzania and Uganda. In 2019, there were 212 companies listed on the stock exchanges of these countries. However, the study could access only companies from three countries, namely Kenya, Tanzania, and Uganda. The research covered a period of 12 years from 2008 to 2019.

4.7 Sample Selection

According to the author, a sample should be representative of the population. Creswell and Creswell (2017) give the criteria for sample size that should be based on (i) the study objective; (ii) the required level of the accuracy of the results; (iii) the level of detail in the proposed analysis; (iv) the availability of elements of the population; (v) the cost; (vi) time constraints; and (vii) the size of the population.

The sample selected for the study was based on the availability of data related to taxation, corporate governance and financial information of the companies. The firms with significant missing data for the period 2008 to 2019 were not selected. The firms included in the sample were those that had data for at least six years. This is consistent with previous studies that argued that including firms with at least six years of data has the potential to produce reliable results (Chan et al., 2013; Pshipa, 2017). The study collected data that covered a period of twelve years from 2008 to 2019. The year 2008 was chosen because the corporate governance code of all East African countries was effectively implemented in this year. The year 2019 was considered because it was the year of most currently available data. Table 5.2 below shows the countries with their listed companies and the number of firms from each country included in the study.

Table 5.2 Countries with the numbers of their listed companies

S/N	Country	Stock exchange (SE)	Number of listed companies	Year established	Firms included
1	Uganda	Uganda Securities Exchange	19	1997	16
2	Kenya	Nairobi Securities Exchange	64	1954	58
3	Tanzania	Dar es Salaam Stock Exchange	28	1998	25
Total			111		99

Source: Researcher's Classification

As stated earlier, data on Rwanda, Burundi, and Sudan were not accessible, and therefore these countries were excluded. The determination of the final sample size is provided in Table 5.3 below.

Table 5.3: Rationale for the final sample

Public traded companies in East Africa		111
Less the following	Firms with no data on stock market	(6)
	Firms not listed for at least four years during the period 2008-2017	(3)
	Firms with missing data of at least four years	(3)
	Final sample size	99

Source: Researcher's Classification

4.8 Model Specification Tests (Diagnostic Tests)

The study performed various diagnostic tests prior to the actual estimation of the study models. The literature suggests various diagnostic tests should be conducted to build up a reliable model that provides non-spurious results (Alkdai & Hanefah, 2012; Tshipa, 2017). Following this recommendation, the study performed several specification tests, such as the test for linearity; the test of normality; the test of autocorrelation; the test of multicollinearity; and the test of homoscedasticity, which are explained below. Thereafter, endogeneity is discussed.

4.8.1 Test of Linearity

Pedhazur and Schmelkin (2013) argue that before the actual estimation of the regression model, the study variables should be tested for linearity behaviour. The authors argue that the accuracy of the estimation of the multiple regression model is primarily affected by the linearity behaviour of independent and dependent variables. The study used linearity plots to test for the linearity behaviour of the variables involved in each study objective.

4.8.2 Test of Normality

Multiple regression assumes normal distributions of the variables involved in the model. The violation of this assumption may lead to estimation bias. The study used the skewness and kurtosis tests to analyse the possible data violation of the normality assumption. According to Tshipa (2017), normal distributed data should have kurtosis within a range of plus or minus 1.96, while plus or minus 3 for skewness.

4.8.3 Test of Autocorrelation

Habbash (2019) suggests that to obtain reliable and unbiased estimations, there should be little or no serial correlation (autocorrelation) in the regression model. Serial correlation occurs when the residuals are not independent of each other. Independent observations are assumed by most statistical procedures. The independence test for each of the predictor variables in this study was conducted using Durbin-Watson d statistics. Durbin-Watson is used to test autocorrelation, a situation whereby the independent variables repeat themselves or influence each other, and therefore cannot sufficiently predict the dependent variable.

Geniaux and Martinetti (2018) point out that the importance of testing autocorrelation is to show the distribution of disturbance (errors). It is always important to determine the presence of an autocorrelated disturbance term in a series before the least squares techniques for estimating a and b are developed. The Durbin-Watson statistics value ranges from 0 to 4. An ideal value of 2 indicates non-autocorrelation; a value closer to 0 indicates a positive autocorrelation; and a value closer to 4 indicates a negative autocorrelation (Geniaux and Martinetti, 2018). This means that coefficient values ranging from 1.5 to 2.5 show no presence of autocorrelation, while values ranging from 2.5 to 4 show a positive autocorrelation.

4.8.4 Test of Multicollinearity

Chen et al. (2019) propounds that multicollinearity occurs when two or more independent variables are highly correlated. The author posits that a problem with multicollinearity implies that the explanatory variables in the model being estimated are not precisely independent from one other. The existence of multicollinearity in the model may affect the estimation results (Huang, 2018).

These authors posit that regression analysis requires little or no presence of multicollinearity among the explanatory variables. The high positive correlation amongst independent variables might cause the parameters to switch signs, which may affect the R square (R^2). However, Geniaux and Martinetti (2018) argue that one explanatory variable can easily predict the estimations outcomes of other variables if the two variables are strongly correlated. Therefore, the presence of multicollinearity indicates that one variable can successfully predict the outcome of another variable.

Furthermore, Midi et al. (2010) suggest that including many dummy variables may accelerate the multicollinearity problem and lead to exact multicollinearity, where there is an exact linear relationship between two or more independent variables including the intercept. Following previous studies (Chen et al., 2019; Habbash, 2019; Huang, 2018; Tshipa, 2017), the study used the personal correlation matrix (PCM) to identify the existence of multicollinearity. Tshipa (2017) argues that in the PCM correlation between explanatory variables of 0.9 or more, the problem indicates the existence of multicollinearity. Additionally, the study used the variance inflation factor (VIF) to test the presence of multicollinearity.

4.8.5 Test of Homoscedasticity

Xu et al. (2014) posit that homoscedasticity is the situation in which the variance of errors is the same across all levels of the independent variables. When the variance of errors differs at different values of the independent variables, heteroscedasticity is indicated. According to Huang (2018), slight heteroscedasticity has little effect on significance tests. However, obvious heteroscedasticity can lead to a distortion of findings and weaken the analysis.

4.8.6 Endogeneity

The endogeneity occurs when the independent variable (X_i) is correlated with the error term (U_i). The Durbin Wu Hausman was used in this study to test the existence of endogeneity. Studies related to corporate governance and firm performance are prone to endogeneity (Wintoki et al., 2012). Endogeneity may exist because of omitted variables, measurement error and simultaneity (Minnick & Noga, 2010). The authors argue that the presence of endogeneity may cause biased estimations. Following previous studies, the study used both econometric and non-econometric

measures to mitigate possible endogeneity. Firstly, previous studies suggest using a panel data set as a way of minimising the problem of endogeneity (Minnick and Noga, 2010). Therefore, the study used a panel dataset. Moreover, Minnick and Noga (2010) point out that measurement error is one of the causes of endogeneity in a study (Wintoki et al., 2012). To mitigate this, the researcher took reasonable care in measuring the variables, which meant that there was no possibility for endogeneity due to measurement error.

Wintoki et al. (2012) suggest that the omitted variable may cause the problem of endogeneity. Thus, the study included several control variables to mitigate this problem. The reason why endogeneity is such a problem is that it violates one of the assumptions of multiple linear regression (MLR), termed the “Zero Conditional Mean”. If this expression is different from zero, the implications are that at least one of the independent variables is correlated with the disturbance term, which means that all the parameters estimated by OLS are biased (Wooldridge, 2009). This indicates the necessity to search for a more appropriate estimation method. However, the corporate finance literature suggests that in the presence of endogeneity, an appropriate econometric model, which deals with the problem of endogeneity, should be chosen. Thus, if endogeneity exists, the OLS results may be biased and inconsistent (Minnick & Noga, 2010). Following the study of Minnick and Noga (2010) as well as Wintoki et al. (2012), the generalised method of moment (GMM) is the appropriate model for solving the problem of endogeneity.

The dynamic GMM panel specifications, as developed by Arellano and Bond (1991), Arellano and Bover (1995) as well as Blundell and Bond (1998), can overcome the estimation problems introduced by unobservable heteroskedasticity, simultaneity and dynamic endogeneity, and produce unbiased and consistent estimates by employing valid internal instruments during estimation. Indeed, Wintoki et al. (2012) illustrate the technique using a reduced model of performance and board characteristics.

The emergence of GMM models in research, when using panel data, can resolve some of the unanswered questions raised in the recent literature on econometric techniques. The developed GMM model can be used for dynamic panel data. In dynamic panel data, the cause and effect relationship for an underlying phenomenon is generally dynamic over time. For example, it may

not be the current year's performance that is affecting sales, but rather that of the previous year that could be playing a significant role.

Dynamic panel data estimation techniques leverage the lags of the dependent variables as explanatory factors to capture this. In order to control the endogenous link, lagged values of the dependent variables are employed as instruments. Since they are taken from the current econometric model, these instruments are frequently referred to as "internal instruments" (Roodman, 2009). The GMM model, which is typically used for panel data, consistently produces accurate results in the presence of unobserved heterogeneity, simultaneity, and dynamic endogeneity (Wintoki et al. 2012).

According to historical studies (Schultz et al., 2010; Wintoki et al., 2012), two lags of the dependent variables are adequate to depict the dependent variable's persistence (for example, firm performance). By internally modifying the data, which is a statistical procedure wherein a variable's previous value is subtracted from its present value, the GMM model eliminates endogeneity (Roodman, 2009). This reduces the quantity of observations, and the internal transformation process improves the effectiveness of the GMM model (Wooldridge, 2009). Additionally, first difference transformation (one-step GMM) and second-order transformation (two-step GMM), two different types of transformation methods, can also be utilized as GMM estimators. The first-difference transformation (one-step GMM) does, however, have some restrictions. For instance, the first-difference transformation, which subtracts a variable's past value from its present value, may result in the loss of too many observations if a variable's most recent value is missing (Roodman, 2009). Arellano and Bover (1995) suggest using a second order transformation to prevent potential data loss caused by the internal transformation issue with the first stage GMM (two-step GMM).

4.9 Summary of Chapter

The chapter discussed the general research methodology used in the study to address the research questions and meet the study objectives. In this chapter, we described the research design, the research paradigm, the data type, the data collection, the population, the sample selection and model specification tests (diagnostic tests).

The population of the study comprised 11 listed firms in Kenya, Tanzania and Uganda as of December 2017. However, owing to the missing information of some of the firms (as detailed above), 99 companies were used for the study. The chapter explained that sources of data included Bloomberg; McGregor; financial stock markets of EACs and the websites of respective companies.

The subsequent chapters, Chapters Five, Six, Seven and Eight will cover the study's specific objectives. The first objective will be covered in Chapter Five, the second in Chapter Six, the third in Chapter Seven, while Chapter Eight will cover the fourth objective.

The next chapter, which is Chapter Five, will examine the tax-planning practices of listed firms in EACs. The chapter will examine the level and trend of their tax-planning practices. Furthermore, the chapter will investigate the responsiveness of tax-planning activities to the tax policy reforms (administrative and technological tax reforms) implemented by EACs during the period under study.

CHAPTER FIVE

TAX PLANNING SCHEMES OF FIRMS IN EAST AFRICA

5.1 Introduction

This chapter will cover the study's first objective, which was to investigate the tax planning schemes of firms in EACs. Like all businesses, these firms are increasingly finding ways to reduce cost, earn more profit for investment opportunities and increase their value. Amongst the strategies to achieve these objectives, tax planning represents a large part of management time and resources (Lee, 2020). This is because tax erodes a considerable percentage of a firm's income. Tax planning is, therefore, an essential corporate strategy in today's business environment (Hanlon & Heitzman, 2010; Heitzman & Ogneva, 2019). The question is, however, do firms effectively engage in corporate tax planning?

The predominant assumption of shareholders is that they do because taxes represent a significant burden to firms; therefore, tax planning that lowers corporate tax burden is believed to increase firm value (Jacob & Schutt, 2020; Kirkpatrick & Radicic, 2020). Nevertheless, Jacob and Schutt (2020) contend that tax planning is not costless. The authors maintain that there are several costs and risks associated with tax planning, which may include potential punishments, such as penalties and fines from revenue authorities. Apart from these, there are also tax planning implementation costs, legal fees and reputation loss, which could harm firm value.

Agency theorists argue that because of agency costs due to shareholders-management relationships, management may misuse tax-planning decisions (Graham et al., 2013; Maama & Mkhize, 2020; Putra, Syah & Sriwedari, 2018). This is because managers may have personal incentives to implement tax planning in ways that favour their self-interest and thus are different from what shareholders would prefer. Accordingly, Campbell et al. (2020) emphasise that tax planning is a complex and opaque activity that may create opportunities for managerial rent diversion and could negatively affect shareholder value.

Governments implement various strategies to enhance their tax collection capacities, particularly in developing nations (Armstrong et al., 2019). For instance, East African governments, like most

other developing nations, have implemented various tax policy reforms to boost their tax revenue (Kimea & Mkhize, 2021). The tax reforms, which have been instigated, include the establishment of revenue authorities, the establishment of large taxpayer departments and the digitalisation of the revenue collection. Apart from these reforms, information-sharing agreements amongst EACs, robust deterrence mechanisms and the education of taxpayers are other strategies that governments of EACs have implemented to increase tax revenue collection.

Despite the significant contribution of tax to the development of economies, it decreases a firm's resources and investment opportunities. As a result, owners would want to see their companies pay the minimum amount of tax possible. Hence, they employ competent managers to manage their businesses on their behalf. Moreover, these managers are entrusted with the firms' resources to create value for the shareholders using strategies such as tax planning, which plays a major role (Hanlon & Heitzman, 2010; Tang, 2019). Since tax represents an erosion of firm value, investors would like to see a downward trend in the effective tax rate, suggesting that they would prefer their firms to pay fewer taxes. However, governments strive to increase their revenue collection because taxes are the main source of funds for social and economic development. Therefore, they would like to see an upward trend in a company's effective tax rate.

The study examined the level and trend of the tax planning of listed firms in EACs and investigated the responsiveness of tax planning activities to the tax policy reforms (administrative and technological tax reforms) implemented by EACs during the period under study. The study adopted the effective tax rate as the measure of tax planning. Liu and Cao (2007) posit that the effective tax rate, which is used by many studies to measure tax planning, is also used to indicate the actual tax burden borne by the firms. Therefore, a higher effective tax rate suggests that firms are less tax aggressive. In contrast, firms with a lower effective tax rate are tax aggressive and thus engage more in tax planning and pay a lower amount of taxes.

The study used descriptive statistics to indicate the level and trend of tax planning trends, using both the CETR and the AETR. In addition, in meeting objective one, the study used the Wilcoxon signed ranked test (WSRT) to investigate whether there were significant changes in the effective tax rate over the years. The findings indicated the existence of tax planning activities in EACs. Furthermore, the study results showed that the tax planning activities of the firms decreased during

the period under study because of various tax policies reforms introduced by EACs to increase tax revenue.

5.2 Empirical Literature Review

The following section is an empirical literature review, which is a systematic examination of past empirical studies. In the case of the study, this involved finding how earlier studies investigated the level and trends of tax planning strategies.

Studies reveal that there is a high level of tax planning strategies used by complex group structures to minimise a firm's tax burden without violating tax laws, which may, in fact, be morally reprehensible or highly questionable (Lisowsky, 2010; Wilson, 2009). Moreover, newspapers report anecdotal evidence of extensive tax avoidance activities by MNCs almost daily (Hakim & Omri, 2015; Garside, 2016). In 2019, in the US, for instance, the statutory income tax rate was approximately 40%. However, a technology company with the third-largest market capitalisation had a tax rate of 2.4%, which indicated tax avoidance of 37.6% (Cooper & Nguyen, 2019). Based on these findings, a media-driven belief has emerged. The tax avoidance behaviour of (multinational) firms has increased over the last decade (Duhigg & Kocieniewski, 2012).

In Europe, studies show that firms cannot reduce their tax rates to minimal levels in contrast to US counterparts (Boffey, 2017; Garside, 2016). A study conducted by Boffey (2017) investigated tax avoidance behaviours of firms from 12 European countries over time. The results indicated that firms in EU countries, such as France and Germany, practised tax planning. However, in contrast to the results of observations for the US, the findings showed that the gap between the STR and the ETR significantly decreased over time for EU firms. This finding suggested that tax avoidance in EU firms might have, on average, decreased over time. This decline in tax planning activities was the result of efforts made by European countries. The European Commission, for instance, prompted by France and Germany, was seeking ways to collect a greater amount of tax from companies that exploited their lack of physical offices in a country to book their profits in low-tax states.

Taxing tech companies has been on the agenda of an EU leaders' summit devoted to the digital economy. A study found that Amazon's corporation tax bill in the UK was 11 times smaller than

British bookstores. In Ireland between 2003 and 2014, the European Commission found that Apple had lowered its effective corporate tax rate from 1% to just 0.005% (Barrera & Bustamante, 2018). Counting all unpaid taxes over this period, plus interest, the agency ordered Apple to pay \$14.3 billion in back taxes to the Irish government. France was pushing a proposal to tax technology companies on turnover rather than a conventional corporation tax on profits (Faulhaber, 2019).

In Kenya, Ouma (2019) reported that the level of tax planning responded negatively to each of the tax reforms. According to Cobham and Janský (2018), on average, Kenya was losing around \$1.22 billion annually due to tax planning, which was approximately 3% of their GDP. However, Ouma's (2019) findings showed a gradual decrease in tax planning activities over the last decade. Furthermore, the author argues that government effectiveness, together with other tax policy reforms aiming to control corruption, promoted revenue generation.

Most prior studies focused on trends in tax avoidance, particularly studies on ETRs, have been cross-sectional. Some studies have also investigated inter-temporal changes, but that was not their primary focus (Dyreng, Hanlon & Maydew, 2008; Hoopes, Mescall & Pittman, 2012; Armstrong et al., 2012). More closely related to the current study are the findings of Dai et al. (2007) as well as Dyreng, Hanlon, Maydew and Thornock (2017). Dai et al. (2007) examined the trend of tax planning measured by ETRs, worldwide and found evidence of their decline over time in many countries. They examined firms in 82 countries from 2005 to 2009 and found evidence that the average ETR of US firms was high relative to that of firms in other countries but declined over the sample period.

By dividing their US sample into multinational and domestic firms, Dyreng et al. (2017) investigated the trend of tax planning measured by CETRs over the previous 25 years. They reported that Cash ETRs decreased significantly over the sample period, including a cumulative decline of approximately 5.0% points from 32% (in 1988) to approximately 27% (in 2012) and an average reduction in the CETR of 0.4% per year over the sample period. This significant economic trend resulted in a \$109 billion decrease in taxes paid in 2012, relative to the amount that would have been paid had no decrease in ETRs occurred.

The contributions of this chapter are twofold. Firstly, it extends the initial findings of Dyreng et al. (2017), which elucidate trends in tax planning by explaining the variations in CETRs of US

firms over 25 years (1988–2012), but not the trends in tax planning outside the US. Therefore, the current study attempted to contribute to the overall understanding of international taxes by examining the tax planning trends of EACs. Secondly, this chapter adds to the findings of Markle and Shackelford (2012), who found that ETRs fell during their sample period and that there were only minor differences between the rates of purely domestic firms and those of MNCs. However, Markle and Shackelford's (2012) study did not consider potential changes in STRs over time. Furthermore, previous studies failed to test whether changes in firms' tax planning were statistically different over time. The current study fills this gap in the literature by employing the WSRT to examine the significance of changes in the tax planning activities of firms in EACs.

5.3 Objective One of the Study

The study's first objective was to examine the level and trend of tax planning activities of firms in EACs. This objective was achieved through a descriptive statistics analysis, which provided empirical evidence of tax planning practices in EACs. The evidence might alert governments to the presence of tax planning in listed firms in EACs. This might assist governments and regulatory authorities in developing appropriate policies and regulations that will ensure revenue collection and the protection of investors.

5.4 Methodology

5.4.1 Data Collection

In achieving its "first objective, the study used a sample of listed firms in EACs, comprising Kenya, Tanzania, and Uganda. The data used in attaining this objective were the tax expenses of firms and other taxation information. All this information was archival, as companies were required to publish information through their annual reports (audited annual reports and accounts). The taxation data were obtained from the financial statements of the firms. The financial statements were obtained from the financial stock markets and the annual reports from the websites of companies. Annual reports are widely used firms documents because they are audited and widely distributed to shareholders (Maama, 2020; Mensah et al., 2017). The data were collected on the variables of interest for 12 years, from 2008 to 2019. The year 2008 reflected the year when all EACs adopted their code of corporate governance, while 2019 reflected the most currently

available data. Ninety-nine firms were included in the study. Consequently, 1089 annual reports were targeted. However, some annual reports were not available, resulting in a shortage of 68 annual reports. As a result, 1021 annual reports were used for the study.

The information used to compute the proxy for tax planning were obtained either from tax returns or financial statements (Lee et al., 2015), although these two sources might have given different information due to the divergence in the objectives between the financial accounting standards and tax accounting systems. In fact, McGill and Outslay (2004) and Plesko (2007) provide evidence for divergences between the tax planning estimates using tax returns and those using financial statements. However, Graham and Mills (2008) argue that the two sets of the source of information are highly correlated. Nonetheless, tax returns produce accurate data, but they are highly confidential and not easily accessible. Therefore, the data from the firms' financial statements were the only publicly available source for estimating tax planning. Thus, this study used information from the firms' financial statements.

5.4.2 Variables Definition and Measurement

There is no agreement amongst scholars about what constitutes tax planning (Hanlon & Heitzman, 2010). The term “tax planning” is comprehensive and involves various activities, which might be legal or illegal. Prior studies do not rely on a single measure of tax avoidance because every measure has its limitations. Following the most recent studies (Chen et al., 2010; Armstrong et al., 2012; Lennox et al., 2013; Dyreng, Hanlon, Maydew & Thornock, 2016), the study used more than one measure of tax planning. Due to the weaknesses of the measures of the tax planning, the use of more than one measure ensured the capture of a broad range of activities that are symptomatic of tax planning (Hanlon & Heitzman, 2010; Lisowsky et al., 2013).

Firstly, the study used ETR to measure tax planning, which is computed as tax expense divided by a firm's pre-tax accounting income (Hanlon & Heitzman, 2010). Therefore, the ETR measures the ability of a company to minimise tax liabilities (which are indicative of the relative tax burden of a firm) so that they are less than its pre-tax accounting income. Firms with lower ETRs are said to be more tax aggressive compared with firms with higher ETRs. ETR can be categorised into CETR and AETR, both of which the study used to measure tax planning.

CETR is computed as the ratio of cash taxes paid to pre-tax accounting income (Dyreng et al., 2008; Chen et al., 2010). However, AETR is computed as the ratio of total tax expense to pre-tax accounting income (Chen et al., 2010; McGuire et al., 2012). The strengths and weaknesses of these two tax avoidance proxies should be considered when interpreting results. One advantage of ETRs is that they can be computed for each jurisdiction. However, the rules underlying both the numerator and denominator can vary across countries and across time.

5.4.3 Data Analysis Method

The study employed descriptive statistics together with the WSRT to analyse the results.

Descriptive statistics, such as the variables' mean were used to represent the trend and level of tax planning activities of firms in EACs. In addition, the WSRT was used to check whether there was any significant change in the trend and level of tax planning activities of the firms. Thus, the trend and level of the firms' tax planning practices were analysed based on a moving average score for every year to demonstrate whether there was any variation in the tax planning trend and level. In addition, the p-values were obtained from the WSRT to explain whether there were significant changes in the tax planning across the years.

5.5 Results and Discussion

5.5.1 The Level and Trend of Tax Planning in East Africa

This section presents the results of the investigation of the tax planning schemes of firms listed in EACs. The study used both the CETR and the AETR as tax planning measures. Furthermore, the study further used a line graph to demonstrate whether the tax planning activities of the firms increased, decreased or remained constant over the twelve years. The line graph also depicts the firms' tax savings, which is the difference between the AETR and the CETR; moreover, it provides an accurate measure of the actual benefit emanating from tax planning activity. Moreover, a WSRT was used to examine whether the difference in the tax-planning activities of the firms changed significantly over the years. Figure 5.1 presents the result of the level and trend of tax planning activities by the firms in EACs. Table 5.1 below shows the WSRT results indicating the changes in the tax planning activities of the firms over the years.

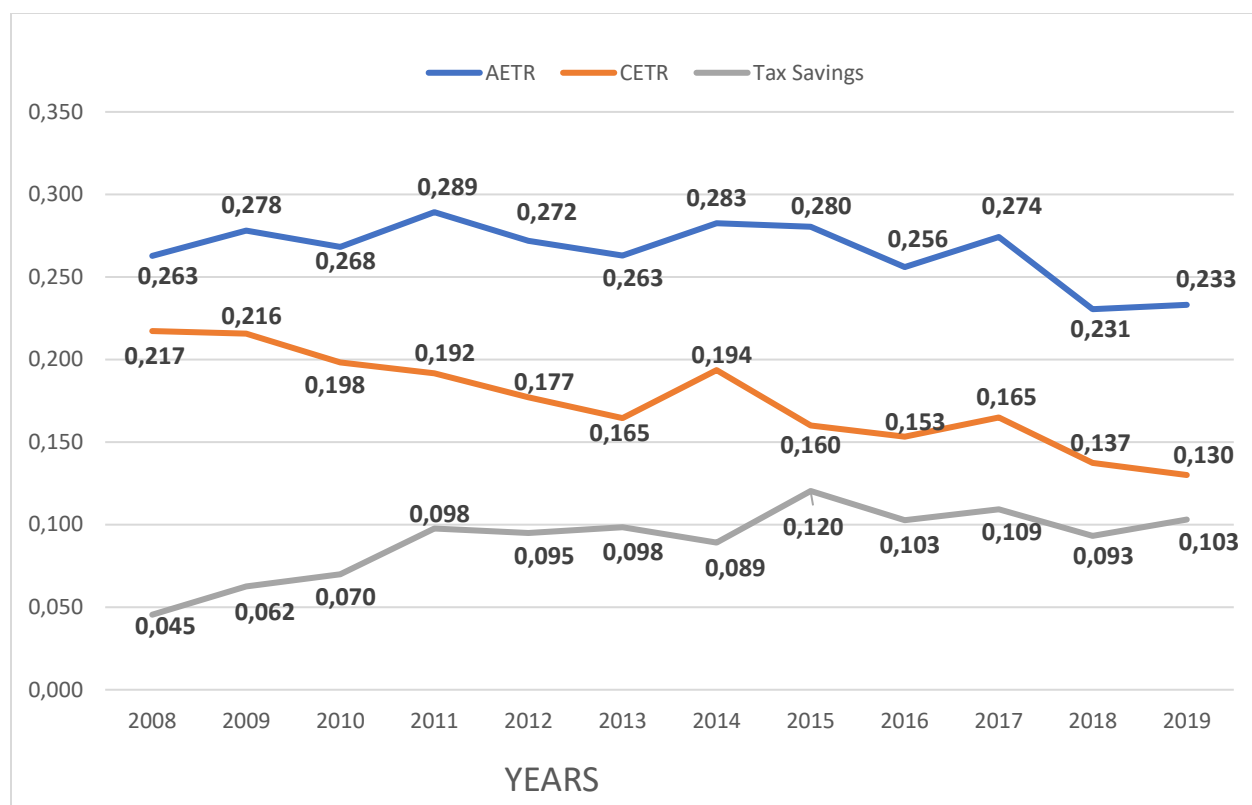


Figure 5.1: Tax Planning Trend (2008 – 2019)

Source: Author's Calculation

Table 5.1: Wilcoxon signed-rank test results

Years	Cash Effective Tax Rate (CETR)		Accounting Effective Tax Rate (AETR)	
	Z-Value	Asymp. Sig. (2-tailed)	Z-Value	Asymp. Sig. (2-tailed)
2008-2009	-0.393b	0.694	-1.579b	0.114
2009-2010	-2.292c	0.022	-1.412b	0.158
2010-2011	-2.656b	0.008	-0.652c	0.514
2011-2012	-1.158c	0.247	-1.364c	0.173
2012-2013	-2.161b	0.031	-1.358c	0.174
2013-2014	-0.426c	0.67	-0.485b	0.627
2014-2015	-2.163c	0.031	-1.426b	0.154
2015-2016	-0.025b	0.98	-0.508c	0.611
2016-2017	-1.364c	0.173	-1.347b	0.178
2017-2018	-3.016b	0.003	-1.158c	0.247
2018-2019	-1.646c	0.108	-2.121b	0.034

Source: Author's Calculation

The results revealed a gradual increase in tax planning activities in EACs over the 11-year period. This was demonstrated by both measures of tax planning. Both ETRs slightly increased during the 11 years, which indicated an increase in tax planning activities. The descriptive statistics results in Figure 5.1 above show that the mean value of the CETR in 2008 was 21.7%, whilst the AETR was 26.3%. The results indicated that, on average, listed firms in EACs paid almost one-quarter of their pre-tax earnings to the governments as taxes. Furthermore, both tax planning measurements showed that there were tax-planning activities in EACs. The STRs for the three EACs (Kenya, Tanzania and Uganda) were 30% over the study period. Therefore, the CETR and the AETR of 21.7% and 26.3%, respectively, revealed that there were tax-planning activities in EACs. An interesting observation is that the companies saved about 8.3% and 3.7% of their CETR and AETR, respectively. These savings represent the difference between the AETR and the CETR, which accurately measures the actual benefit emanating from tax-planning activity. Figure 5.1 shows that in 2008, they already paid less tax (4.5%) than what they were required to pay, which emphasised that they began to be engaged in tax planning in the same year.

The evidence showed that the CETR and the AETR were 21.6% and 27.8%, respectively, in 2009. This suggests an increment in the AETR and a decrease in the CETR. This result indicated that the firms' tax liabilities affecting their profits marginally increased in 2009; however, the percentage of tax paid decreased. Once again, an average tax savings of 8.4% and 2.2% was recorded by the firms, given that the average tax rate in these countries is 30%. The WSRT results showed that although there were changes in both the CETR and the AETR, they were statistically insignificant. In 2010, the CETR and the AETR of the firms decreased to 19.8% and 26.87%, respectively. These results indicated the tax savings of listed firms in EACs. The AETRs indicated that, on average, the firms saved 3.2% of pre-tax earnings paid to the government in 2010. However, in the same year, the tax savings of the firms concerning CETR was 10.2%, which was far more than that of the AETR. Figure 5.1 below shows that the difference between the CETR and AETR was 7.0%, which indicated further tax planning activity. The WSRT showed that the change in the tax planning activities of the firms was statistically significant for AETR ($p < 0.05$) and statistically insignificant for CETR ($p > 0.05$).

In 2011, the tax planning activity of the firms decreased, as indicated by the AETR (28.8%), and the tax savings decreased to 1.1%. However, the tax savings with respect to the CETR increased to 10.8%. Once again, the level of change was statistically significant for the AETR ($p = 0.008$), as opposed to the CETR ($p = 0.514$).

In 2012, the CETR of the firms decreased to 17.7%, which resulted in a tax savings of 12.3%. Again, the AETR in 2012 was 27.2%, which resulted in a tax savings of 2.8%. This result suggested that the firms increased their tax planning activities. However, the WSRT result showed that the increment level in the firms' tax planning was statistically insignificant ($p > 0.05$) for both methods.

Similarly, the firms increased their tax planning activities in 2013, evidenced by the decline in the CETR and the AETR of 16.5% and 26.3%, respectively. This resulted in tax savings for the CETR (13.5%) and the AETR (3.7%), which suggested that the firms increased their tax planning activities in 2013. The WSRT results indicated that the change in the AETR in 2014 was statistically significant ($p = 0.031$), whilst the change in the AETR was statistically insignificant ($p = 0.17$).

The results demonstrated that in 2014, the AETR and CETR increased to 28.3% and 19.4%, respectively. This showed that the firms' tax planning activity in 2014 was less. Nonetheless, the tax savings for AETR and CETR were 1.7% and 10.6%, respectively. However, the WSRT results showed that the level of increment in the tax planning activities for both methods were statistically insignificant ($p > 0.05$).

Both tax planning measures indicated the existence of tax planning activities in EACs in 2015. In fact, tax savings related to the CETR (16.0%) and the AETR (28.0%) increased in 2015 to 14.0% and 2.0% respectively. It can be ascertained from Table 5.1 that the level of increment was statistically significant for the AETR ($p < 0.05$) and statistically insignificant for the CETR ($p > 0.05$).

The firms increased their tax planning activities in 2016, demonstrated by the decline in the CETR and the AETR of 16.3% and 25.6%, respectively. In addition, the AETR and CETR tax savings in 2016 were 4.4% and 14.7%, respectively. The substantial increase in the tax savings of the firms in 2016 suggests that the firms were not happy with their tax savings in the previous year and thus

put in place policies and strategies that decreased their tax burdens. Despite the increment in the tax planning activities by the firms in 2016, the WSRT results showed that the level of increment was statistically insignificant ($p > 0.05$) for both methods.

Surprisingly, the tax savings for both methods of measuring tax planning decreased in 2017, suggesting that the tax planning activity of the firms were ineffective in that year. The results showed that the CETR for 2017 was 16.5%, whilst the AETR for the same year was 27.4%. Figure 5.1 indicates that the CETR tax savings of the firms in 2017 decreased to 13.5% whilst that of the AETR decreased to 2.6%, although the levels of decline were statistically insignificant ($p > 0.05$) in both methods.

The firms marginally increased their tax planning activities in 2018, evidenced by a decrease in the CETR and AETR to 13.7% and 23.1%, respectively. These tax rates represented a tax savings of 16.3% and 6.9% for CETR and AETR, respectively. The WSRT results showed that the increment of the CETR was statistically significant ($p = 0.03$), as opposed to that of the AETR ($p = 0.247$).

In 2019, the CETR of the firms was 13.0%, as opposed to the AETR of 23.3%. This resulted in a tax savings of 17.0% and 6.7% for CETR and AETR, respectively. Once again, the difference between the tax liability and the tax paid by the firms was 10.3%. This represented significant tax savings in 2019, which was a testament to tax planning amongst the firms. These results demonstrated that the increments in the tax savings in 2019 for CETR was statistically significant ($p = 0.034$) whilst that of the AETR was not ($p = 0.108$).

The results showed an increasing trend in the tax planning of firms in EACs, which indicates that they aggressively deployed means to reduce their tax liabilities and demonstrates that the governments in the EACs failed to institute pragmatic measures that would minimise tax planning or tax avoidance. Moreover, the results suggested that the tax policy reforms established by the various governments did not achieve their desired objective of reducing tax planning, which confirms the findings of Ouma's (2019) study that revealed that the firms' level of tax planning was not reduced by tax reforms.

The East African governments implemented various tax policy reforms in 2012 to boost their tax revenue. These tax reforms included the establishment of revenue authorities, the establishment of

large taxpayer departments and the digitalisation of revenue collection. Apart from these, the EACs agreed to share information to reduce tax avoidance and evasion. It must be admitted that the objective of these tax policies was not solely to minimise tax planning; however, since corporate tax represents a significant component of tax income, it was expected that such policies would curb the incidence of tax planning.

The possible reason for the inability of the tax reforms and policies to reduce the level of tax planning conducted by firms is that the companies may have developed strategies to improve their tax planning. The reforms may have motivated the firms to engage the services of professional and expert tax consultants to assist them in their planning. One point to note is that if the governments in EACs cannot use tax reforms to reduce tax planning, they should enact laws that would severely punish firms and their management that engage in tax evasion and thus deter them from aggressively engaging in tax planning.

Such measures have worked in Europe; for instance, the European Commission punished Apple for lowering its effective corporate tax rate from 1% to just 0.005% (Barrera & Bustamante, 2018). This view is consistent with those of Hanlon and Heitzman (2010) as well as Tang (2019), who explain that owners and shareholders employ competent individuals to help them to reduce their burden and increase their value.

The results showed that managers were more concerned about increasing the financial performance of the firms and the value of their shareholders' investment, at the expense of the firms' image in the eyes of the public, which views paying the required tax as responsible. Moreover, these results suggested that the firms in EACs were not concerned about the possible loss of reputation and that their tax planning activities cannot be explained in terms of the legitimacy theory. In fact, the agency theory can be used to explain these activities because the managers of the firms used tax planning as a tool to prove to shareholders that they work to pursue their interests. This view is plausible because tax represents an erosion of firm value, and investors would like to see a downward trend in the ETR, which would indicate their firms are paying less tax than what they would otherwise be paying.

The results confirmed the findings of previous studies, such as those of Drucker (2010) as well as Duhigg and Koscienski (2012), which found that the tax planning of firms in the US increased

over the years. However, the results contradict the findings of Boffey (2017) and Garside (2016) that demonstrated that firms in Europe were unable to use tax planning to reduce their tax burden significantly.

5.6 Conclusion and Recommendations

Owing to the importance of taxes in social and economic development, EACs made a greater effort to increase tax revenue, which excessively increased the tax burden for taxpayers. To counter this action, taxpayers in EACs devised ways to reduce taxes legally through tax planning. Based on this, the study examined the level and trend of tax planning of listed firms in EACs and concluded that they practised tax planning, although there was a gradual decrease in the level and trend during the 11 years that were the focus of the study. However, the level of decline was not statistically significant.

EACs are eager to become middle-income countries by 2025 or, at the latest, 2030. However, the tax planning practices of big MNCs may impede government efforts to collect domestic revenue to meet their developments goals. Although the study's results showed a decrease in the trend of tax planning, the researcher recommends that tax authorities should implement additional tax enforcement mechanisms to eliminate the tax planning problem.

The study proved that firms in EACs practised tax planning during the period under study. However, the factors that influence this were not addressed in the current chapter that explained how the study investigated the factors that influenced the tax planning activities of firms in EACs.

CHAPTER SIX

DETERMINANTS OF TAX PLANNING

6.1 Introduction

The previous chapter explained the study's examination of the level and trend of tax planning in EACs and the research findings, which indicated that tax planning activities were carried out by firms in EACs and that there was a gradual increase in these activities during the period examined. Nonetheless, the study did not clearly reveal determinants (factors) that may affect tax planning in these countries. Factors, such as firm characteristics and corporate governance variables, have been associated with variations in the level of tax planning; however, their influence remains equivocal. This shortcoming meant a lack of clarity about tax planning activities in EACs. Consequently, the study investigated the factors that influence the tax planning activities of firms in the EACs. This part of the study is explained in this chapter.

Following the involvements of several MNCs in aggressive tax planning, the issue of tax planning has attracted attention among academics, political bodies, investors and the public at large (Huseynov et al., 2017; Lee et al., 2015). For instance, recent evidence about tax planning in companies, such as Starbucks, Apple and Facebook (Davis et al., 2015), and the unforgettable scandals involving firms, such as Enron and WorldCom (McGill & Outslay, 2004), have shown that tax planning has become more aggressive, which is notable in today's businesses around the globe. Supporting this claim, Ogembo (2019) showed that tax planning/avoidance worldwide had reached \$650 billion per year as of 2018. Nevertheless, some companies promptly pay a substantial amount of taxes annually.

Empirical findings indicate substantial differences in the amounts of taxes that firms pay (Thomsen & Watrin, 2018). The variation in the level of tax payment of firms has been evidenced in empirical studies (Jingga & Lina, 2017; Richardson et al., 2016) that showed that different companies pay different amounts of corporate income taxes (Chen et al., 2019; Dyreng et al., 2008). This means that some companies seem to reduce their corporate income taxes successfully compared to their counterparts in the same economy or industry. In addition, Thomsen and Watrin (2018) showed that some companies pay very little taxes compared to other companies in the same country.

Thomsen and Watrin (2018) noted that while more than half of the companies paid an ETR ranging from 30% to 40%, other companies paid as low as 20%.

This considerable variation in corporate tax avoidance amongst firms has raised concerns among academics, researchers and policymakers. The central question of debate is, therefore, why do some companies aggressively reduce their taxes, whereas others pay substantial amounts of taxes with an ETR that is equal to or above the statutory tax rate? This variation may be associated with the tax planning opportunities presented by loopholes in tax laws (Dyreng et al., 2016).

Nevertheless, while some companies have successfully utilised these tax-planning opportunities, others have remained tax compliant (Dyreng et al., 2016). As tax planning reduces the amount of tax revenue that firms transfer to governments, thereby increasing after-tax return (Austin & Wilson, 2017), it may enhance firm value and increase distributable amounts to shareholders, who can be expected to support the strategy (Rego & Wilson, 2012). However, as the rationale behind the non-adoption of tax planning opportunities by various companies has remained unanswered, it should be empirically investigated.

Therefore, the study sought to understand what contributes to variations in the ETRs of firms. As stated above, several factors have been identified as influencing the trend and level of tax planning, such as firm characteristics (size, profitability, leverage, capital intensity, age and asset tangibility, for example) and corporate governance characteristics (Atwood et al., 2012; Jingga & Lina, 2017; Ribeiro, 2015). However, the results of previous studies using these factors conflict with one another, leading to incomplete information on why and how some companies avoid taxes compared to their contemporaries. Moreover, an essential piece of information missing in the tax planning literature is whether a country's institutional arrangements influence the tax planning activities of firms operating in it. This means that the literature still does not fully understand the factors that may support tax avoidance among firms.

Payne and Raiborn (2018) argue that studies investigating the determinants of tax planning focus on developed nations, thus sidelining developing countries. Although prior studies are useful in understanding the determinants of tax planning yet, there is a lack of consensus amongst them. Moreover, they offer little insight into why some firms in developing countries engage in more tax

planning activities than others (Kerr et al., 2016). A possible determinant of corporate tax avoidance that has not been fully explored is mainly considered in this study.

It is against this background that the study investigated the determinants of tax planning in the East African context, and thus contributed to the existing literature on the topic by showing whether country-specific institutional factors, such as management quality, the quality of financial reporting, auditing quality, the quality of regulations, ethics and culture influence tax planning. This is a complete departure from the literature, which has concentrated chiefly on firm and corporate governance variables.

The rest of this chapter is organised into the following sections: Section 6.2 (literature review); Section 6.3 (research methodology); Section 6.4 (results and discussion); and Section 6.5 (conclusion and recommendations).

6.2 Objective of the Study

The second objective of the study was to investigate the determinants of tax planning in EACs, and thus explore why some firms appear to be more efficient in reducing their tax burden than others. Shareholders and firm management would benefit by understanding why some firms successfully reduce their tax burden compared to other firms. The findings of the study concerning Objective Two, which will be explained in this chapter, might guide management and investors on how to structure their financial affairs and engineer the structure of their firms so that they can benefit from tax planning. In addition, governments and other regulators (for example, revenue authorities) might be informed on what motivates firms to practise tax planning, which would help policy formulation.

6.2.1 Sub-objectives

The following sub-objectives were formulated to help achieve Objective Two of the study.

1. To examine firm-specific determinants of tax planning in firms in EACs.
2. To explore corporate governance determinants of the tax planning practices of firms in EACs.
3. To investigate the country-specific determinants of tax planning among firms in EACs.

6.3 Determinants of Tax Planning in Firms

6.3.1 Firm-Specific Determinants

Some studies have investigated the influence of firm-specific characteristics on corporate tax planning. For instance, firm attributes, such as firm size, profitability, leverage, capital intensity, and the age of firms have been constantly investigated to examine their influence on the trend and level of tax planning (Ribeiro, 2015; Wahab & Holland, 2012). Studies on the specific characteristics of firms have documented conflicting results on the relationship between these specific characteristics and corporate tax planning. The mixed results might be due to different methods of measuring tax planning, different research timespans and the estimation techniques used in analysing the data (Minnick & Noga, 2010). The study included the firm-specific characteristics discussed below in its investigation of the determinants of tax planning. These firm characteristics are size, profitability, leverage, capital intensity and age.

6.3.1.1 Firm Size

The influence of firm size on tax management has been extensively researched in the literature, with studies using two competing views in their arguments based on the political power theory and the political cost theory. The political power theory maintains that larger firms pay lower taxes because they have substantial resources (such as financial capacity and manpower), which capacitate them to hire competent tax planners to organise their financial affairs for optimal tax saving. Owing to their power, larger firms have political connections with high-level government officials, which allow them to manipulate political processes and minimise their taxes (Wu et al., 2016). This view argues that political power possessed by larger firms allows them to negotiate with revenue authorities about their tax position. Kraft's (2014) study confirms this view by documenting that the larger firms are more tax aggressive than smaller firms.

Previous studies have documented a positive association between tax planning and firm size (increased firm size equates to increased tax aggressiveness, which they explain by way of the political power theory) (Hanlon & Heitzman, 2010; Hoi et al., 2013; Rego, 2003). These studies suggest that large firms have enough resources to manage their taxes, which is not the case with smaller companies. Similar findings emanated from Richardson and Lanis's (2007) study investigating the determinants of tax planning in listed firms in Australia between 1997 and 2003.

Using ordinary least squares (OLS) as an estimation technique, the authors found that larger firms have a smaller ETR than smaller firms. In addition, their study concluded that larger companies appear to possess superior economic and political power compared to smaller firms and they are also able to reduce their tax burden.

A number of studies base their arguments on political cost theory, which was developed by Jensen and Meckling (1976). This theory proposes that large size companies are subjected to political pressure, which limits them from practising aggressive tax planning. According to this theory, firms may opt not to avoid taxes to protect their reputation and thus lessen their level of tax management to avoid being seen as unpatriotic corporations that do not pay their fair share of taxes to support the social and economic wellbeing of the country.

Studies that have found that the size of a firm is negatively associated with tax planning have explained their result in terms of the political cost theory. In other words, large-sized firms are less tax aggressive compared to small-sized firms. Zimmerman (1983) finds that companies that are relatively large have higher ETRs. Additionally, the literature suggests that as the size of a firm increases and become more visible, it attracts the government's attention and thus is closely monitored to meet revenue collection targets (Kraft, 2014). Therefore, successful businesses are subjected to stringent scrutiny, are less tax aggressive (Halioui et al., 2016) and transfer more wealth to the government. According to Halioui et al. (2016), larger and more prosperous firms become more exposed to strict government regulations (Lestari, 2010; Parisi, 2016).

Jingga and Lina (2017) also hold the view that governments and other regulatory authorities closely supervise and investigate larger firms, as opposed to smaller firms. Larger firms represent the interests of the public, who are shareholders, and those to whom the corporations offer employment opportunities. They also pay a substantial amount of taxes to governments. Therefore, their strategic role makes it logical that they are subjected to many regulations because any wrongdoings could affect the interests of the public. The literature argues that this close supervision limits tax avoidance in larger firms. Thus, large firms endure higher political costs because of their size, as found by Irianto et al. (2017), who conducted a study to determine the firm attributes that affect tax avoidance practices. The study found a positive link between firm size and tax avoidance that was explained by the political cost theory.

However, several studies have suggested that firm size does not significantly influence tax planning (Phillips, 2003). Wu et al. (2016) conclude that firm size has no significant influence on tax planning. Wang (2003) also investigated the impact of firms' size on tax planning in two different periods, before 1997 and after 1998, using data from China. The study found a positive relationship between firm size and tax planning in the data before 1997, while the data after 1998 showed that the size of a firm does not have a significant influence on tax planning. This suggests that time is a factor that must also be considered in such studies.

Askenberg and Isaksson (2018) conducted a study to investigate the relationship between two proxies (revenue and total assets) of firm size and the ETR. Generally, this study showed that large firms are most likely to avoid more taxes compared to small firms, which is consistent with the political power theory. Surprisingly, when revenue was used as a measure of firm size, the results showed a positive relationship, in line with the political cost theory. According to Askenberg and Isaksson (2018), the relationship between a firm's size and tax planning is amongst the most interesting research topics, owing to its inconsistent results in previous studies, and thus is recommended for further research.

Studies based on the political power theory argue that large firms are more tax aggressive compared to small firms. However, other studies believe that small firms have an advantage in tax planning over large firms because of the political cost theory. To the best of the researcher's knowledge, studies that have investigated the influence of firm size on tax aggressiveness are limited in developing nations, and those that are available provide mixed results. Thus, the researcher was motivated to investigate the influence of firm size on tax planning in the East African context and formulated the following hypothesis:

Hypothesis One (H₁): Firm size positively and significantly influences the effective tax rate

6.3.1.2 Profitability

According to the political cost theory, profitability influences tax planning (Fernández et al., 2019; Jingga & Lina, 2017). This theory holds that large and more profitable firms are more exposed to government regulations than smaller firms are. This limits their tax management, and thus they pay their taxes according to the law to avoid reputation loss. Furthermore, Fernández et al. (2019) suggest that more profitable firms have higher corporate ETRs and are less tax aggressive than

less profitable firms. However, the findings of Derashid and Zhang (2003) reveal that profitable firms have lower ETRs and are more tax aggressive than less profitable firms. Thus, the findings of the studies support the political power theory that presumes that profitable firms have resources, such as financial and competitive human resources and tax planning instruments at their disposal, which allow them to minimise their tax burden.

The current study included the firm profitability variable as a possible determinant of the level of tax planning in EACs. ROA, which was used as a proxy for firm profitability, is defined as the ratio of pre-tax income to total assets. ROA has been used in previous tax planning studies, such as those conducted by Armstrong et al. (2012) and Kraft (2014). Based on the explanation above, this study formulated the following hypothesis:

Hypothesis (H₂): Profitability has a positive influence on the effective tax rate.

6.3.1.3 Leverage

Leverage is the ratio of debt finance to equity finance (Swingly & Sukartha, 2015). Firms can use the debt from external sources as an alternative to equity finance from the shareholders. Therefore, leverage is simply described as the debt-to-equity ratio. Debt finance results in interest expenses that the firm has to pay to debt owners. The interest on debt finance is a tax-deductible expense in most countries. As a result, firms with more debt finance than equity finance will have a smaller net profit compared with those firms with more equity finance than debt finance. This argument is logical since the cost of equity (dividend) is not a tax-deductible expenditure, while the cost of debt finance (interest expenses) is an allowable expenditure when computing taxable income (Parisi, 2016).

According to Parisi (2016), a firm's decisions about capital structure affect its ETR. This study argues that tax laws exhibit differential treatment of capital structure (debt and equity). Consequently, Richardson and Lanis (2007) suggest that firms use finance decisions as a tax planning decision to reduce their tax burden. The results of this study indicate that the leverage ratio significantly and positively affects tax aggressiveness. In line with the argument that companies use debt as a tax planning strategy, Ozkan and Ozkan (2004) posits that firms with higher tax liabilities may choose to acquire more loans to get tax deductions.

Swingly and Sukartha (2015) investigated the determinants of tax avoidance in Indonesia, using a sample of 41 manufacturing firms listed on the Indonesia Stock Exchange (IDX) between 2011 and 2013. The results of this study indicated that leverage has a positive effect on aggressive tax planning. In this context, Arora and Sharma (2016) suggest that a high leverage ratio lowers the ETR. This means that firms with high leverage ratios are more tax aggressive. This study maintains that companies deliberately use debt finance to reduce their tax burden.

Irianto et al. (2017) argue that leverage does not influence the level of tax planning. The authors investigated the factors that affect a firm's tax planning, including size, leverage, profitability and capital intensity. Amongst other results, this study found that the leverage ratio does not significantly influence tax planning. Similarly, Primordia (2015) claims that leverage does not have any effect on the level of a firm's tax planning.

In conclusion, previous studies about the influence of leverage on tax planning document mixed empirical results. A few studies revealed a near consensus that high debt financing results in low ETRs, although other studies found that leverage does not significantly affect the level of tax planning. However, the current study expected that firms with high leverage ratios might have a lower ETR. Therefore, based on the above discussion, the current study proposed the following hypothesis:

Hypothesis (H₃): There is a negative and significant relationship between leverage and the effective tax rate.

6.3.1.4 Capital Intensity

The capital intensity ratio measures a firm's investment in capital assets (fixed assets), according to Ribeiro (2015), who argues that firms invest in fixed assets as a tax planning strategy, although they may depreciate over time. Several studies have investigated the influence of capital intensity on tax planning (Parisi, 2016; Ribeiro, 2015; Richardson & Lanis, 2007). These studies show that capital intensity significantly influences the ETR. Richardson and Lanis (2007) maintain that there is a negative and significant relationship between capital intensity and ETR and that corporate taxpayers are permitted to write off the cost of a fixed asset (depreciable asset) in a shorter period than the asset's economic life. Therefore, companies that are relatively more capital intensive are likely to have a lower ETR.

However, Irianto et al. (2017) claim that capital intensity does not significantly influence tax avoidance. Therefore, due to the mixed results from previous studies relating to capital expenditure, the current study included this variable as a possible factors that influence tax planning in EACs. Hence, the researcher formulated the following hypotheses:

Hypothesis (H₄): Capital intensity has a negative impact on the effective tax rate.

6.3.1.5 Age of Company

Age is the length of the period that a company's stock has been traded in the securities market (Maama et al., 2019). The relationship between the length of time that firms trade on the capital market and their involvement in tax planning has been debated in the literature. Some studies argue that firms that have been longer in the capital market are under pressure to maintain their performance and to meet future performance expectations, which leads to them engaging in aggressive tax planning activities. Supporting this claim, Lanis and Richardson (2011) present evidence to show that older firms are more tax aggressive compared to the new firms in the public capital market. However, Halioui et al. (2016), Irianto et al. (2017) as well as Askenberg and Isaksson (2018) use political cost theory to connect firm age and tax planning. They avow that older firms with well-established businesses are prone to reputational risk and choose not to practise tax planning that may harm their reputation. Therefore, the current study predicted that older firms are less tax aggressive with the following hypothesis:

Hypothesis Five (H₅): Age is positively associated with the effective tax rate.

This section contributes to the unresolved debate in the literature about the influence of firm-specific characteristics on tax planning. Specifically, the above discussion focused on the influence of firm size, profitability (ROE), leverage (capital structure), capital intensity (asset mix) and age on tax planning. For each characteristic, previous studies reveal three streams of findings as shown below:

1. Studies that find a positive link between a firm's characteristics and the effective tax rate
2. Studies that document a negative relationship between a firm's characteristics and the effective tax rate
3. Studies that establish that there is no effect

Five theory-based study hypotheses (H₁ – H₅) on the relationship between firm-specific characteristics and the level of tax planning (ETR) were developed. Table 6.1 below presents the summary of these five hypotheses together with their expected or predicted signs.

Table 6.1: Summary of the hypotheses for the relationship between firm-specific characteristics and the effective tax rate

Hypotheses	Tested relationships	Predicted Sign
H ₁	Firm size and effective tax rate	+
H ₂	Profitability (ROA) and effective tax rate	+
H ₃	Leverage and effective tax rate	-
H ₄	Capital intensity and effective tax rate	-
H ₅	Age and effective tax rate	+

Source: Compiled by the researcher from the literature review

6.3.2 Corporate Governance Determinants

Studies that have explored the relationship between corporate governance and tax aggressiveness (Hanlon & Heitzman, 2010; Hidayat & Yuliah, 2018; Nugroho & Agustia, 2018) have had mixed findings. For example, Hanlon and Heitzman (2010) reviewed tax studies, which had been conducted during 10 years and found that the relationship is ambiguous. Furthermore, Hanlon and Heitzman (2010) argue that most of the studies had been based on agency theory and that a firm's attitude towards tax management largely depends on the level of corporate governance. Several previous studies have found that corporate governance significantly influences tax management. As tax management is the key element of firm performance, it is one of the essential corporate strategies. Therefore, management efforts to lower corporate taxes payable to governments are valuable to firms and shareholders.

Tax management increases the after-tax returns distributable to shareholders and retained earnings for further corporate expansion. However, Hidayat and Yuliah (2018) argue that managers may have bad intentions when managing taxes and may engage in tax planning activities that appear to lower tax for the benefit of companies and shareholders but, in fact, indirectly do so for their self-interests. Desai and Dharmapala (2006) posit that tax management may heavily cost shareholders

because managers can easily mask their self-interested activities using tax planning. Therefore, good corporate governance is recommended for monitoring and controlling managerial decisions related to tax planning to ensure that they are aligned with the interests of shareholders. The literature suggests that if there is strong corporate governance in place, management will not have the incentive to misuse tax planning (Kovermann & Velte, 2019; Bhagiawan & Mukhlisin, 2020). Several studies have investigated the impact of corporate governance structure on tax planning (Hidayat & Yuliah, 2018; Nugroho & Agustia, 2018; Kovermann & Velte, 2019; Bhagiawan & Mukhlisin, 2020). Despite the findings of these studies, the relationship between corporate governance and tax planning is still unclear. Besides this challenge, the attention of these studies has been directed towards developed countries, which have reliable legal systems, leaving out developing countries with different legal, economic, political, cultural and social arrangements. The lack of focus on the importance of corporate tax management and corporate governance in developing countries, as well as the mixed results from other studies, indicates a gap that the current study sought to fill by examining the effect of corporate governance on tax planning in EACs. Therefore, the study investigated whether the following components of corporate governance affect tax planning: board size, board independence, gender diversity, managerial incentives, ownership concentration, and institutional investors.

6.3.2.1 Board Size

Board size, which is the number of members contained in the board of directors, can influence the efficiency of the board of directors to reduce the agency problem to improve performance (Bhagat & Bolton, 2008). As a result of its relevance in decision-making, several studies have investigated the effect of board size on a firm's performance (Minnick & Noga, 2010; Sikka, 2010). Sikka (2018) argues that board composition has attracted the interest of many researchers due to its importance to firms. Most of the studies about the size of a board and its impact on tax planning base their argument on three corporate governance theories: agency, resource dependence and stewardship theories. The agency and resource dependence theories support a large-sized board. However, the stewardship theory supports a small-sized board.

Agency theorists argue that a board of directors represents and protects the interests of shareholders and other stakeholders in the companies through close monitoring of a manager's performance and

controlling his/her activities (Crocker & Slemrod, 2005; Nugroho & Agustia, 2018). Therefore, the theory argues that managerial action will be more monitored and controlled when enough directors are acting on behalf of shareholders. In this context, firms with larger board sizes are more effective in monitoring. The resource dependence theory also posits that a larger number of directors on boards bring a wide range of knowledge and expertise from different fields that may add value to the board. A large number of board members may increase the resources of the board and organisation.

The resource dependence theory also assumes that each director has access to specific resources or resources, which are helpful to the board (Crocker & Slemrod, 2005). Therefore, a large board of directors adds valuable resources needed for board effectiveness. The concept is based on the view that firms with a larger board benefit from the varied experiences, expertise and professional skills of their members. Members who are skilled professionals can advise firms on strategic decisions about business issues. The theory maintains that firms with larger boards pool a number of opinions that could enhance board debates and enrich decision-making. Moreover, a board with many members is more diversified in terms of nationality, race, gender and experience, which are expected to increase the board's effectiveness (Fink et al., 2006). Based on the agency and resource dependence theories, it is clear that firms with larger board sizes would be more effective in monitoring and controlling managerial actions. Therefore, management would not be motivated to practise aggressive tax planning, hence a negative relationship between board size and tax planning.

Contrary to the aforementioned, some studies support a small board size (Belz et al., 2019; Bhagat & Bolton, 2019; Koverman & Velte, 2019). These studies suggest that small board size is more efficient in monitoring and controlling. These studies outline the following points to support arguments in favour of small board size. Firstly, they believe that a small board size eases communication among board members; secondly, a small board size increases the speed of decision-making in an emergency; thirdly, small board size has enough time to discuss issues and provide express opinions. In addition, it is easy to organise a meeting for a small board. These studies, which support a small-sized board of directors, use two theories to buttress their claims: the stewardship and agency theories. According to the stewardship theory, management is seen as the steward and custodian of the assets of an organisation. Shareholders entrust management with

the firm's assets and are expected to act responsibly without being closely supervised. Therefore, there is no need for many board members to monitor and supervise management. Thus, the theory supports a board with a small number of members. Based on this theory, tax planning is expected to associate positively with board size.

Various studies have used the agency theory to support the argument of a small board size (Putra et al., 2018; Zolotoy et al., 2020). According to these studies, a large number of board members may lead to communication problems amongst board members. This may lead to a decrease in the board's effectiveness in controlling and monitoring management. In addition, a board's inability to control management may increase the agency problem. Therefore, these studies suggest that board size may be positively linked to corporate tax aggressiveness.

Minnick and Noga (2010) used the system GMM estimation technique to investigate the association between tax aggressiveness and corporate governance. This study showed that there is a positive association between board size and the ETR, which indicates that firms with a larger board of directors are less tax aggressive compared with firms with smaller board sizes. However, Hoseini et al. (2019) suggest that firms with larger board sizes are more tax aggressive compared to those with small board sizes. Similarly, Minnick and Noga (2010) investigated the influence of board characteristics on tax management and found a positive relationship between board size and the level of tax planning. Salawu (2017) investigated the influence of corporate governance on tax avoidance in Nigeria. Using the generalised method of moments (GMM) estimating technique, the study revealed a positive association between board size and ETR and concluded that firms with a large board size are less tax avoidance compared with firms with small board size.

The discussion above revealed the lack of consensus amongst researchers on the influence of board size on tax planning, especially in developing economies. Therefore, the current study added to the existing literature on the relationship between board size and tax planning in the context of EACs by proposing the following hypothesis:

Hypothesis (H₆): There is a negative and significant relationship between board size and the effective tax rate

6.3.2.2 Board Independence

Independent directors can be described as the members of a firm's board of directors who are not part of a firm's management (Li et al., 2016) represent and protect the interests of shareholders. Habbash (2019) argues that the collapse of large, well-known corporations worldwide during the late 1900s and early 2000s was facilitated by the wrongdoing of their management. As a result, the Sarbanes-Oxley Act (2002) requires the corporate governance structure to have a board that includes outside independent directors. The Act requires the inclusion of non-executive directors who are independent of the organisation's management because they are objective and thus more efficient in monitoring management actions.

To understand the importance of independent directors in board effectiveness, several previous studies have investigated its role in monitoring managerial activities. For instance, the studies of Habbash (2019) as well as Zemzem and Ftouhi (2013), reveal that the effectiveness of corporate governance of firms improves with an increase in the proportion of independent directors. Furthermore, these studies suggest that the ratio of independent directors has an impact on corporate performance. McCahery et al. (2016) suggest that a board of directors should include outside directors to represent shareholders and protect their interests. The codes of corporate governance of EACs, for instance, allow shareholders who have a certain percentage of ownership to select independent directors to represent them on the board to protect their interests. Empirical studies provide evidence that non-executive directors representing shareholders or groups of shareholders on the board of directors effectively monitor managerial actions (Ozkan & Ozkan, 2004). Ozkan & Ozkan's (2004) study maintains that independent non-executive directors are appointed specifically to protect the interests of shareholders and suggests that a higher percentage of independent directors on the board would ensure that managerial decision-making and the protection of the interest of shareholders would improve.

Although previous studies have emphasised the competence of a board with independent directors, few have referred to its relevance to tax management. Minnick and Noga (2010) suggest that prior studies brush aside the influence of board composition on the tax avoidance activities of firms and focus on the association between a board's independence (due to having independent directors) and tax planning. Minnick and Noga (2010) explain that independent directors have diverse knowledge and experiences related to the operation of firms, including tax management and the

risk involved, which can be helpful for tax management. However, Minnick and Noga's (2010) study fails to establish a link between board independence and tax management.

Empirical evidence reported in Lanis and Richardson (2011) suggests that the increase of non-executive directors enhances the effectiveness of board monitoring. The study further suggests that firms with an effective board of directors are less likely to engage in corporate fraud. Furthermore, the management of a firm with an effective board has little incentive to engage in unethical behaviour, including misuse of tax management for rent diversion (Fich & Shivdasani, 2007).

To emphasise the link between fraudulent behaviour in firms and the composition of the board of directors, Beasley (1996) conducted a study to understand the difference between the board composition of firms that had experienced fraud and that of firms that had not. The study concluded that the board composition of these corporations differed in that the firms that had experienced an incidence of fraud had a lower proportion of independent directors compared with firms who had not. Furthermore, the study explained that fraudulent actions might be prevented by increasing the number of independent directors on a board.

Huang et al. (2018b) argue that the interests of shareholders may easily be ignored if executive directors (inside directors) dominate the board because it is difficult for the majority of directors to review and judge their managerial actions. Therefore, a high proportion of independent directors are suggested in order to hold the management responsible for their actions. Wahab and Holland (2012) posit that agency costs can be effectively reduced in firms with boards that have a higher proportion of independent (outside) directors who possess professional knowledge and industrial experience. Florackis (2008) brings a different view of board composition and argues that outside directors have less knowledge about the organisation compared with inside directors. Furthermore, Florackis (2008) explains that even though independent directors are required to protect the interests of shareholders, the importance of inside directors should not be undermined.

Lanis and Richardson (2018) investigated the association between outside directors and aggressive tax planning. Their empirical evidence reports a negative association between the number of outside directors and corporate tax aggressiveness; moreover, it suggests that an increased number of outside directors on a board would increase the level of protection of the interests of

shareholders and other stockholders. Thus the organisation would become more socially responsible. Therefore, if a corporate firm is socially responsible, it will be less tax aggressive.

In an earlier study, Lanis & Richardson (2011) maintained that firms are likely to be less tax aggressive if their boards have a high proportion of non-executive directors. Lanis and Richardson (2011) provide empirical evidence that companies with a relatively higher proportion of outside directors are less tax aggressive. Their study suggests that companies with boards that have a higher percentage of independent directors are more concerned with the welfare of their shareholders. Consequently, it can be concluded that outside non-executive directors are deliberately appointed to balance boards and managerial decisions in protecting the interests of majority shareholders. Nevertheless, Minnick and Noga (2010) fail to establish the significant influence of board independence on tax planning. Conversely, McClure et al. (2018) and Richardson, Taylor and Lanis (2016) provide evidence that firms with a higher proportion of independent directors are associated with more tax aggressiveness.

Apparently, the influence of independent directors on tax planning has attracted several studies, but the concept is still unclear in the literature. The lack of consensus on the association between board independence and tax planning indicates the need for further investigation. Based on the findings of the previous studies discussed above, the current study predicted that a board of directors possesses sufficient power to influence a firm's tax management. This study also presumes that the presence of outside directors on a board reduces the agency problem; thus, the interests of shareholders become more protected. Therefore, it is believed that the higher the percentage of outside director participation, the better the managerial actions relating to tax planning will be, and consequently the firm will be less tax aggressive. Following the above discussion, the following hypothesis was formulated:

Hypothesis (H₇): Board independence positively influences the effective tax rate.

6.3.2.3 Gender Diversity

The representation of women on boards of directors and their role in their effectiveness have recently become one of the most litigious issues in research related to corporate governance and tax management (Lanis et al., 2017). Because of agency problems that make management take

important, risky decisions, such as those about tax management, on behalf of the shareholders, a strong board of directors is crucial for overseeing managerial decisions.

Previous studies focus on the effect of board composition on firm outcomes, such as performance, and quality of financial reporting, while neglecting the relevance of the board diversity to board effectiveness. Empirical evidence suggests that the effectiveness of a board of directors is associated with personal attributes, such as the skills and qualities of directors. In addition, demographic attributes such as nationality, ethnicity, age and gender are important. It is suggested that a strong board of directors should contain executives who have appropriate personal values and attitudes as well as ethics (Mohammad & Zakzouk, 2018). The literature argues that the personal values of executives significantly affect their decision-making (Lanis et al., 2017; Richardson et al., 2016). Additionally, the attitude, beliefs and cognitive functioning of directors systematically vary with demographic characteristics such as gender (Hoseini et al., 2019).

Gender diversity in terms of female representatives makes the board of directors much stronger (Lanis et al., 2017; Richardson et al., 2016). Female directors play a significant role in shaping the board of directors to be more effective in discharging its role (Lanis & Richardson, 2011). Lanis and Richardson's (2011) study holds that compared to male directors, female directors are more willing to hold management accountable for poor performance. Furthermore, the study maintains that attendance at board meetings of female directors is better than that of male directors. Consequently, the presence of women on boards has a positive impact on the participation of male directors. Lanis and Richardson's (2011) study concludes that a higher proportion of female executives and directors greatly impacts the quality of decision-making (Lanis et al., 2017).

According to Richardson et al. (2013), firms that do not use the potential of women in their boards of directors are at great risk of poor firm performance because they fail to take advantage of the social capital and intellectual abilities of women. Several studies suggest that females are more ethical than males are; therefore, females on a board can significantly influence it to make ethical decisions in the shareholders' interests (Hoseini et al., 2019). This suggests that compared to men, female directors are more willing to devote their time to address the important issues facing organisations and are more trustworthy than men are. Therefore, they are less likely to make a decision that will infringe on shareholders' interests. Boussaidi and Hamed (2015) used a sample

of Tunisian listed firms to examine the influence of board composition measured by gender diversity on tax avoidance from 2006 to 2012. The study showed that firms with female directors on their boards are less tax aggressive. In a similar study, Hoseini et al. (2019) examined the association between the demographic distribution of the board and tax planning. The results suggested that female representation on a board of directors reduces corporate tax planning.

In another study, Francis et al. (2014) investigated the influence of gender diversity of chief financial officers (CFO) on firm tax aggressiveness. The study found that female chief financial officers are less associated with aggressive corporate tax planning than male chief financial officers. The authors suggest that gender diversity is a significant factor in determining corporate tax aggressiveness. Richardson et al. (2013) employed the ordinary least squares (OLS) estimation technique to investigate the association between woman directors and tax planning in the US. Using a sample of 418 listed firms from 2006 to 2009, the study found that female directors are less involved in aggressive tax planning.

A similar result was found by Lanis et al. (2017), whose study examined whether gender diversity influences tax aggressiveness in the US. They found that gender diversity has a negative and statistically significant association with corporate tax planning. Based on their findings, they concluded that if there is at least one female on a firms' board of directors, there is likely to be less tax aggressiveness. Richardson et al. (2016) also found a negative association between women on boards and tax aggressiveness. These studies suggest that the inclusion of female directors on a firm's board promotes efficiency in monitoring corporate boards. Moreover, Lanis and Richardson (2011) claims that female directors on board is like that of external auditors, which can reduce aggressive tax planning.

However, Zemzem and Ftouhi (2013) suggest that the presence of female directors on board does not significantly influence tax planning. Their study used a sample of 300 listed firms in the US and 19 years of data. The study found that female opinion, experience and knowledge do not have any impact on reducing the tax burden. Furthermore, the study showed that men are more predominant in tax management and seem to have more knowledge and expertise in tax minimisation. Similarly, Oyenike et al. (2016) found that gender diversity has no significant influence on the tax planning and tax aggressiveness of the listed firms in Nigeria. Furthermore,

Aliani and Zarai (2012) suggest that a higher proportion of female board of directors has an insignificant influence on tax planning.

The extant literature on board gender diversity has concluded that females on corporate boards can reduce tax aggressiveness and increase firm value. On this basis, the ability of a board of directors to minimise aggressive tax behaviour can be potentially increased when a female is present on the board. Nevertheless, empirical studies have proposed contradictory ideas in this regard. Some studies have revealed that gender diversity in a firm's board influences tax planning, some have concluded differently, and other studies have reported no relationship. An alternative view on how gender diversity in boards influences tax behaviour suggests that female directors are better at controlling and monitoring the actions and reports of management through better board attendance, as well as sitting on audit, nominating and corporate governance committees, which may limit avenue for rent extraction.

A substantial number of studies have examined whether the involvement of women in boards can lead to improved corporate governance and company results, risk portfolio and financial reporting. However, there is a dearth of research that addresses the influence of board gender diversity on aggressive tax behaviour and the extent of tax planning activities in emerging economies, which indicated an opportunity for the current study. Consequently, the study hypothesised the presence of a woman on a board of directors reduces the likelihood of corporate tax aggressiveness. Based on the above discussions, this study hypothesised the following:

Hypothesis Eight (H₈): There is a negative relationship between gender diversity and the effective tax rate.

6.3.2.4 Managerial Incentives

A board of directors performs significant duties in a corporation, such as overseeing various policy decisions, including those for tax management. Owing to the significant role of a board of directors and the decisions that it makes on behalf of shareholders at various corporate levels, it seems reasonable to compensate them with incentives. Seidman and Stomberg (2017) argue that firms use compensation paid to management and board members to align the managers' interest to those of shareholders. Given the significant burden of corporate income taxes and the desire of every firm to minimise tax costs, management has compelling reasons to reduce tax payments (Cobham

& Janský, 2018). However, evidence from the literature reveals that not all firms engage in tax planning, and the level of tax aggressiveness varies amongst firms that practice it (Fernández et al., 2019; Hoopes et al., 2012; Richardson & Lanis, 2007).

Recent empirical evidence shows that the variation of tax avoidance may be attributed to the confidence of the chief executive officers (CEOs) of firms and their attitude to tax management. However, the study of Dyreng et al. (2010) posits that to influence their attitude toward taxes, CEOs and managers should be incentivised. Dyreng et al. (2010) provide evidence that top management and CEOs, motivated by incentives have a significant effect on tax planning measured by ETR. Slemrod (2004) suggests that because tax avoidance is hidden and risky, shareholders should provide incentives to managers to motivate them.

The literature suggests that well-motivated managers can focus on corporate tax strategies to reduce the corporate total tax burden significantly (Graham et al., 2014). Rego and Wilson (2012) argue that tax-planning strategies are associated with high risk and can lead to severe costs for managers and firms. Thus, incentives are used to motivate managers to engage in risky corporate tax planning that can benefit shareholders and firms. This has led to researchers, regulators and shareholders becoming motivated to understand better how managerial incentives influence tax planning (Armstrong et al., 2012; Gaertner, 2014).

Several studies have shown that managers of firms are motivated by incentives and compensation to engage in tax management (Armstrong et al., 2012; Phillips, 2003; Robinson et al., 2010). These studies show an association between firm success in tax management and managerial incentives, particularly after-tax incentives. Armstrong et al. (2015) point out that tax planning is a risky investment decision in which outcomes might negatively or positively affect the firm. Due to existing agency problems, management may ignore the risk of tax planning and engage in more or less corporate tax avoidance for their interests rather than those of shareholders. Management may engage in tax planning because it may facilitate their rent extraction, even though it might negatively affect shareholders value. Fernández et al. (2019) argue that executives are compensated for aligning the interests of management with those of shareholders.

Xian et al. (2015) find that compensation increases tax avoidance, as it is an effective tool for deterring harmful managerial practices while promoting the desired behaviour. Huang et al.

(2018a) examined the influence of corporate compensation policies on the tax aggressiveness of firms in an emerging market, where executive compensation is primarily in cash form. This study was based on a hand-collected dataset of 958 firm-year observations of Chinese listed firms from 2006 to 2012. Using system GMM estimation, the study found that firms paying higher executive cash compensation are associated with lower tax aggressiveness. This relationship also holds for the excess cash compensation measures that control executive shareholding, firm profitability, size, growth opportunity and board independence.

According to Philips (2003), managerial incentives based on after-tax performance are associated with a firm's tax cost reduction. Philips recommends that firms should employ an after-tax incentive to motivate managers to engage in profitable tax planning strategies. Minnick and Noga (2010) find that managerial incentives given to CEOs, directors and managers are negatively related to tax avoidance. Their results support the use of managerial incentives as a tax-planning tool. However, Desai and Dharmapala (2006) suggest that compensations reduce tax avoidance. This study concludes that managerial incentives align the interests of shareholders and managers, and therefore reduce opportunistic behaviours.

Rego and Wilson (2010) investigated the influence of various corporate governance mechanisms on tax planning and found that managerial incentives significantly determine the level of tax avoidance. In the same vein, Rego and Wilson (2012) investigated board compensation in terms of shares and stock options on tax avoidance and found a positive relationship between compensation and corporate tax avoidance. They argue that since incentives paid to the management are performance induced, the board will want to use opportunities within its reach to avoid paying tax so that the wealth of the company can be enhanced.

The foregoing discussion demonstrated that the influence of managerial incentives on corporate tax planning remains unclear, although it has been investigated by several studies, with mixed results and a lack of consensus. Thus, the current study sought to contribute to the literature by investigating the phenomenon to reconcile the mixed evidence. Based on the above literature review; the study developed the following hypothesis:

Hypothesis Nine (H₉): Managerial incentives negatively impact on the effective tax rate.

6.3.2.5 Ownership Concentration

The separation of firm ownership and control is prevalent in public companies with many shareholders. If a company has a dispersed ownership structure, where every investor owns a small portion of the shares, the power to control and monitor is minimal because of cost implications (Huseynov et al., 2017). However, ownership concentration (few shareholders with a significant number of shares) in a company strengthens the power and influence of shareholders to control and monitor the firm's management.

Shareholders with a small number of shares do not have an incentive to monitor the firm's management. However, owning a substantial shareholding is an incentive to monitor and control management. Because shareholders bear the costs of monitoring management entirely, large shareholders (ownership concentration) will justify their involvement. Through ownership concentration, management is well controlled and monitored, which reduces the agency problem (Ozkan & Ozkan, 2004). In firms with higher ownership concentration, the controlling shareholders have enough power to influence management decisions, including tax management strategies to benefit both the firm and all shareholders.

However, the literature argues that although ownership concentration reduces the agency problem between shareholders and the management of firms, it causes an agency problem between large and small shareholders (Chen et al., 2010; Khurana & Moser, 2012). Because large shareholders have power and are actively involved in monitoring a firm, they can easily access private information that can be used for their self-interests at the expense of small shareholders. The controlling shareholders may encourage management to engage in aggressive tax planning for their interests, which small shareholders would not accept (Shleifer & Vishny, 1997).

Khan et al. (2016) suggest that shareholders with concentrated ownership have the power and incentive to influence managers to minimise the ETR to increase their after-tax earnings. Chen et al.'s (2010) study revealed a positive association between ownership concentration and aggressive tax planning. This comparative study used two types of firm ownership: (i) family-owned firms (ownership concentration); and (ii) non-family-owned firms (non-concentrated ownership). The authors posited that family-owned firms (ownership concentration) could benefit from cash

savings from tax planning and thus have the incentive to influence management to implement tax planning. However, these family firms might be concerned about the negative consequences of aggressive tax planning, such as reputation loss, price discounts and penalties from revenue authorities. Therefore, the results showed that family-owned firms (with higher ownership concentration) are less tax aggressive than non-family firms.

The above discussion shows that ownership concentration may either affect tax planning negatively or positively. Studies, which document a positive relationship between ownership concentration and tax planning, claim that controlling shareholders have the incentive to incentivise managers to engage in aggressive tax planning to increase after-tax cash saving. These studies maintain that owing to the monitoring of management action, firms with higher ownership concentration are likely to succeed in reducing the tax burden while minimising non-tax costs related to tax planning (Desai & Dharmapala, 2009a; Huseynov et al., 2017; Khan et al., 2016).

However, other studies claim that firms with higher ownership concentration are less tax aggressive (Badertscher et al., 2013; Chen et al., 2010; Khurana & Moser, 2012). Although these studies agree that controlling shareholders have the incentive to control and monitor management, they suggest that, in fact, shareholders influence management to reduce the level of tax aggressiveness because of potential risks and costs associated with tax planning. Thus, the evidence indicates that the effects of ownership concentration on tax planning are still somewhat ambiguous.

The lack of consensus in the literature provides a gap to be filled, which led the study to hypothesise the following:

Hypothesis Ten (H10): Ownership concentration has a negative and significant relationship with the effective tax rate

6.3.2.6 Institutional Investors

Institutional ownership is considered an essential mechanism that influences the corporate governance of firms (Boone & White, 2015). An institutional investor is a company or organization that invests money on behalf of other people. Mutual funds, pensions, and insurance companies are examples (Maama et al., 2019). Boone & White (2015) maintain that institutional

ownership increases a firm's transparency and positively influences information disclosure. Firms with a higher proportion of shares held by institutional investors increase their information disclosures in response to institutional investors' demand (Bird & Karolyi, 2016). Some studies provide evidence that firms with a higher percentage of institutional investors have well-developed information systems, as the institutional investors play a significant role in monitoring and disciplining managerial opportunism (Gillan & Starks, 2003, Wu et al., 2016; Zhang, 2016). The presence of institutional investors improves firm performance, as they have the ability and incentive to monitor the performance of managers. Evidence of the active monitoring roles of institutional investors in a firm's management has been well reported by some studies (Schmidt & Fahlenbrach, 2017; Velury & Jenkins, 2006; Wu et al., 2016; Zhang, 2016).

Khurana and Moser (2012) maintain that, institutional investors play an important role in monitoring and controlling firm management. These authors suggest that the influence of institutional investors on management decisions depends greatly on the size and type of their investments. Where institutional investors hold a substantial number of shares of the companies, there is a high possibility that they will own them for many years. Therefore, institutional investors are very active in monitoring managerial performance and actions. However, institutional investors are less involved in monitoring when they have a short-term investment or an insignificant number of shares. In this case, they are less active because they can liquidate quickly or sell their shares in response to unfavourable performance.

Salehi et al. (2012) opine that the influence of institutional investors on management decisions depends on the type of institutional investor that the authors classify as active or passive. Active institutional investors, who have representatives on a firm's board of directors, have a greater influence than passive investors. They have the power to play an active role in influencing the board and controlling management decisions (Mashayekhi & Bazaz, 2008). Mashayekhi and Bazaz (2008) maintain that institutional investors are willing to influence a firm's decisions and use their power, which is due to high ownership concentration, to serve their own ends, at the expense of small shareholders

Studies investigate the influence of institutional investors on tax management decisions with divergent results. For, instance Moore (2012) examined the influence of institutional investors on

the variability of tax avoidance and found a negative relationship between institutional investors and tax avoidance. In contrast, Khurana and Moser (2012) documented that firms that have a higher proportion of shares held by active institutional investors are more tax aggressive compared to those with few no active institutional investors. The differences in the findings of these studies may be attributable to the types of institutional investors. Institutional investors who have short-term investments are said to encourage the management of firms to concentrate on short-term market performance strategies that are likely to increase short-term profits, including tax avoidance (Bushee, 1998; Maama et al., 2019).

However, institutional investors with long-term investments may be concerned about the future wellbeing of firms. These institutional investors are more active in monitoring management to avoid managerial decisions that may have current and future impacts on their firms, including aggressive tax planning (Khurana & Moser, 2013). Thus, firms with a higher proportion of long-term institutional investors are less tax aggressive. Khurana and Moser (2013) also provide evidence of a negative association between tax planning and long-term institutional investors (pension funds and banks, for example), which are typically more risk-averse. Khurana and Moser's (2013) results contradict the findings of most recent empirical studies, such as those of Huseynov et al. (2017) and Chen et al. (2019), who found that an increase in the percentage of institutional investors leads to a rise in an aggressive tax planning.

However, Schmidt and Fahlenbrach (2017) argue that the relationship between institutional investors and tax avoidance is ambiguous and may go in either direction. The authors argue that the domination of long-term institutional investors provides active monitoring to ensure maximum long-term firm value by restricting tax aggressiveness. However, domination by short-term institutional investors, who focus on short-term firm performance, may influence managers to be more tax aggressive to maximise after-tax cash flow and boost short-term earnings.

The lack of consensus on the influence of institutional investors on tax planning led the study to conduct its own investigation in the context of the listed firms in EACs and to formulate the following hypothesis:

Hypothesis Eleven (H₁₁): There is a positive and significant relationship between institutional investors and the effective tax rate

Section 6.3.2 above discussed the unresolved debate in the literature on the influence of corporate governance on the trend and level of tax planning in terms of the variables of board size, board independence, gender diversity, managerial incentives, ownership concentration and institutional investors on the level of tax planning. For each of these corporate governance variables, previous studies showed that there are three streams of findings:

1. Studies that find a positive link between particular firms' corporate governance and effective tax rate
2. Studies that document a negative relationship
3. Studies that establish no relationship

From the discussion, six testable hypotheses (denoted by H₆ – H₁₁) were formulated on the relationship between the corporate governance variables and the level of tax planning (ETR). Table 6.2 below presents the summary of the five hypotheses together with their predicted signs.

Table 6.2: Summary of the hypotheses for the relationship between corporate governance and the effective tax rate

Hypotheses	Tested relationships	Predicted Sign
H ₆	Board size and level of tax planning	-
H ₇	Board independence and level of tax planning	+
H ₈	Gender diversity and level of tax planning	+
H ₉	Managerial incentives and level of tax planning	-
H ₁₀	Ownership concentration and level of tax planning	-
H ₁₁	Institutional investors and level of tax planning	+

Source: Compiled by the author from a literature review

6.3.3 Country-Specific Determinants

The majority of corporate tax planning studies, such as those of Richardson and Lanis (2007), Parisi (2016), Irianto et al. (2017), Huseynov et al. (2017), Schmidt and Fahlenbrach (2017), Khan et al. (2016), Askenberg and Isaksson (2018), Chen et al. (2019) as well as Ermasova, Haumann and Burke (2021) concentrate on firm-specific variables as determinants of tax planning activities.

However, the specific features of a country can also influence the tax planning of its firms. In this section, specific characteristics of a country that can influence tax planning are discussed: management quality, culture, regulatory quality, financial reporting quality, ethics and audit quality.

6.3.3.1 Management Quality and Tax Planning

Research, such as that of Dyreng et al. (2010) and Koester et al. (2017), investigates the impact of the quality of management (managerial ability) on the tax planning strategies of firms. Demerjian et al. (2013) explain that management is expected to have a high standard of knowledge and understanding of the operating environment of firms, which will result in a reduction of the taxes paid because such managers can align a firm's decisions with tax strategies. This would make them able to identify and utilise tax-planning opportunities due to their superior understanding of the operating environment of their firms. For instance, Koester et al. (2017) maintain that the timing, classification and location of research and development (R&D) activities have significant ramifications for tax reduction. This suggests that highly qualified managers would be able to use R&D activities to reduce the tax burdens of their firms. Another reason for a possible relationship between the quality of management and tax planning is that top-quality managers can set objectives that emphasise cost minimisation (Dyreng et al., 2010). Even though all managers aim to reduce costs, managers with a high level of experience, expertise and skills are more likely to attain substantial cost savings, which can positively affect their tax savings. Therefore, it is anticipated that the shrewdness of managers in managing resources would result in cost reduction through tax avoidance strategies.

However, there are conceptual explanations of how management quality may not be related to tax planning. *Ceteris paribus*, all good managers should manage firms so that they would pay the lowest possible tax. However, the skills needed to manage a firm may differ from the specialised training and expertise required to find and implement tax planning strategies. Another explanation for a possible nonlinearity between good-quality management and tax planning is that management may be concentrated on the primary business operations of the firms; hence, the implication of their decisions on tax would not be their major concern. There are some conceptual reasons to

suggest why management quality may not result in high tax planning activities. *Ceteris paribus*, all managers may wish to pay the least amount of taxes that are legally tolerable for a given income. However, managers may have dissimilar opportunities to achieve a lower tax rate. This may be caused by factors such as industry affiliation, research and development activities and location decisions (Koester et al., 2017). In addition, evidence indicates that compensation paid to management affects their tax planning activities (Rego & Wilson, 2012; Gaertner, 2014). According to Koester et al. (2017), where compensation motives and firm characteristics drive the variations in tax planning, there is little or nothing that managers, even top-quality ones, can do to reduce the tax burden of companies.

The preceding discussion indicates that good-quality management will have the ability and skills to manage a firm's resources effectively and reduce its tax burden. Based on the argument advanced in this section, the following hypothesis was developed:

H₁₂: Management quality increases a firm's tax planning activities

6.3.3.2 Culture and Tax Planning

The literature predicts that culture plays a crucial role in explaining the tax planning activities of firms in a particular country (Richardson, 2008; Brink & Porcano, 2017; Ermasova, Haumann & Burke, 2021). The current study predicted that the culture of a country would influence the tax planning activities of its firms. In this context, culture is measured by Hofstede's (2011) uncertainty avoidance cultural dimension. Hofstede (2011) defined uncertainty avoidance as the degree to which a group of individuals feels threatened by uncertainty and unknown or unstructured conditions. In the context of an organisation, uncertainty avoidance is characterised as the extent to which a firm as a whole and its agents handle their inability to predict the future correctly and to be fully ready for it because of unclear circumstances or free and amorphous situations (Minkov & Cabelkova, 2015). It is possible to relate culture to the tax planning activities of firms because a country with a strong uncertainty avoidance culture upholds unyielding codes of beliefs and attitudes and is intolerant of heretical behaviour and views. This attitude can limit the ability of a firm and its staff to embrace the concept of tax planning because they would consider such practice as unethical and unacceptable, which may land them in trouble. This view

held by the firm would force it to organise its operations according to the prescripts of the law and regulations, hence less tax planning activities.

The foregoing argument is consistent with that of Gallego-Alvarez and Ortas (2017), who contend that firms and individuals in societies with a high level of uncertainty avoidance mainly accept and follow rigid codes. Moreover, they are inclined to embrace many rules and norms, making them less disposed to innovation and change. This indicates that firms operating in countries demonstrating high uncertainty avoidance will be less prone to tax planning. Studies provide evidence that a country's culture influences a firm's tax planning activities.

For instance, Richardson (2008) demonstrates that higher uncertainty avoidance results in higher tax planning activities in firms. In a related study, Brink and Porcano (2017) reveal that a firm's tax planning is influenced by culture. A study in the US and Germany by Ermasova et al. (2021) find that culture significantly predicts tax planning activities in firms in these countries. Based on their results, the authors suggest that policymakers should factor cultural variables in the design and implementation of tax administration as well as in understanding the increasing amount of tax evasions. The literature discussed above resulted in the formulation of the following hypothesis.

Hypothesis Thirteen (H₁₃): Culture (uncertainty avoidance) reduces a firm's tax planning activities

6.3.3.3 Regulatory Quality and Tax Planning

In a country with a good-quality regulatory regime, tax authorities may have unrestricted access to the financial records of a firm and its worldwide business transactions. This will serve as a deterrent to firms engaging in tax planning strategies. In addition, access to sensitive information may expose firms to litigation risk, which they would wish to avoid. In this context, firms operating in countries with a good-quality regulatory regime will avoid tax planning strategies because they may be disputed by regulatory authorities, which may give rise to litigation. Furthermore, a strong regulatory environment enables investors and creditors to enforce their rights, and non-compliant firms are likely to face liquidation or take-over in such an environment. This would deter management from engaging in tax planning activities that may receive greater scrutiny. However, in the absence of a detection mechanism, firms will take advantage of the flexibilities in regulations, laws and standards and will engage in aggressive tax planning.

This view is in accord with those of Bushman and Piotroski (2006), who found that firms in countries with strong regulatory systems reflect bad news in earnings faster than firms in countries with weak regulatory systems. However, it is conceptually possible that firms operating in countries with strong investor protection would pay a lower tax. This position is possible because firms operating in a country with a robust regulatory system would adopt more aggressive accounting policies and estimates in financial reporting than those of firms operating in countries with weaker regulation regimes. The literature discussed above led to the study formulating the following hypothesis:

Hypothesis Thirteen (H₁₄): Strong regulatory quality in a country reduces its tax planning activities.

6.3.3.4 Financial Reporting Quality and Tax Planning

A good-quality financial reporting system in a country increases transparency and accountability in corporate management (Overesch & Wolff, 2018). This suggests that in a good-quality financial reporting regime, firms would not have the opportunity to engage in tax planning. Moreover, good-quality financial reporting would suggest that firms provide additional, reliable and relevant information. Tax authorities can use additional information to spot inconsistencies in income, expenses, profit and tax expenses. This is particularly true for firms that engage in international transactions. Authors such as Wang (2011), Kerr (2019) and Stiglingh, Smit and Smit (2020) provide evidence to show that corporate transparency emanating from good-quality financial reporting results in fewer tax planning activities.

One important reason to relate financial reporting quality to tax planning is that detailed and accurate disclosures can prevent managers from engaging in tax planning, especially if they anticipate scrutiny from the public, which may come with a significant risk to firms, especially that of reputation. Tax irregularities may increase reputational, regulatory and litigation costs. In other words, engaging in tax planning strategies can lead to the danger of being detected and suffering from the loss of a firm's reputation and that of its management.

However, other studies, such as those of Freedman (2018) as well as Balakrishnan et al. (2019), show that quality financial reporting increases the tax planning activities of firms because managers use transparency to mitigate tax-planning problems. Freedman (2018) contends that

excessive information and transparency may obscure the business operations of firms. This suggests that firms can employ financial reporting and transparency as a smokescreen to disguise their activities and revenue, with the specific aim of paying less tax. Nonetheless, the weight of the preceding discussion appears to favour the position that good-quality financial reporting would result in less tax planning activities by firms. The literature discussed above led the study to formulate the following hypothesis.

Hypothesis Fifteen (H₁₅): Quality financial reporting reduces firms' tax planning activities.

6.3.3.5 Ethics and Tax Planning

The relationship between ethical values and the tax planning strategies of firms has received considerable attention in recent times. As a result, taxation has been included in the discipline of business ethics (Scarpa & Signori, 2020). According to Scarpa and Signori (2020), tax laws are imperfect; hence, firms will always find a loophole in them to avoid paying taxes. In this context, ethics would help firms to self-regulate their tax planning behaviour. Firms with high ethical values would want to avoid damaging public information and engaging in tax planning activities, especially in contentious transactions. Zeng (2019) agrees that a responsible citizen in a country is tax compliant, and tax avoidance is considered contradictory to ethical corporate citizenship.

Lanis and Richardson (2011) view that highly ethical firms are less likely to be involved in tax planning activities because tax avoidance is a risky activity and leads to high costs, including reputational damage and government/public scrutiny. Ethics can prevent firms from engaging in tax planning activities, especially when negative information can damage a firm's image. Indeed, firms can reduce reputational risks by reducing or avoiding tax planning activities. Henderson and Kaplan (2005) provide evidence that ethics influence the tax compliance behaviour of firms. The implication of this evidence is that unethical firms typically have considerable tax benefits, indicating that ethical values reduce tax planning. Similarly, ethics are negatively related to tax planning, which suggests that ethics reduce the tax avoidance activities of firms. Based on the strength of the argument favouring a negative relationship between ethics and tax planning, the study provided the following hypothesis:

Hypothesis Sixteen (H₁₆): The ethics of a country decrease the tax planning activities of its firms.

6.3.3.6 Audit Quality

Owing to their unique role and relationship with firms, auditors influence a firms' tax planning activities, which has been a subject of discussion among academics and practitioners. The majority of the arguments appear to favour the view that good-quality audits decrease the tax liabilities of firms. Several reasons have been provided to support this position. Firstly, auditors can provide additional services, such as tax planning advice to firms. In this case, top-quality auditors would be able to develop comprehensive and effective tax strategies for their clients because they would have accumulated substantial knowledge about the operations, systems and internal processes of their clients' firms and gained access to broad financial information (Chyz et al., 2017).

Anecdotal evidence indicates that good-quality audit firms rely on the inside information of their clients to provide the best tax audit service (Yuniarwati et al., 2017; Chyz et al., 2017). In addition, Cripe and McAllister (2009) assert that firms engage the services of audit firms who have extensive knowledge about their clients' tax structure and can bring tax savings as well as efficiency to their business. This suggests that firms that hire top-quality auditors would save tax costs by paying less tax.

Another reason that a good-quality audit increases a firm's tax planning activities is that audit firms can draw on broad tax-specific knowledge because they offer tax services to a broad array of clients (Chyz et al., 2017). The specialised knowledge of auditors would enable them to provide quality tax services to their clients when they are called to do so. In addition, Klassen et al. (2015) opine that for audit firms to provide tax services, they must incessantly invest in modern audit and accounting technologies. This would eventually help their clients through a tax reduction. In addition to the number of clients they may serve, audit firms may have modern tax technologies, which may be deployed to the benefit of their clients to reduce their tax liabilities. Moreover, firms may lack such technologies, expertise and skills. This view is supported by Dai et al. (2007), who provide evidence to suggest that it would take many years for firms to develop tax and business expertise similar to those possessed by auditors who have performed their services for decades. Because they have provided tax services for a long time, auditors may also have broad global

exposure that they can use to benefit their clients (Dai et al., 2007; Yuniarwati et al., 2017). This would enable top-quality audit firms to employ effective tax-planning strategies to favour their clients since such strategies mostly encompass the international and departmental transfer of resources, funds and other assets. The literature discussed above suggests that audit quality would reduce a firm's effective tax rate. In this context, the study proposed the following hypothesis:

Hypothesis Seventeen (H₁₇): Audit quality decreases the tax-planning activities of firms.

Section 6.3.3 above discussed the possible relationships between country-specific determinants and the tax-planning activities of firms operating in particular. The discussion specifically focused on how a firm's tax-planning activities can be influenced by the following: management quality, culture, regulatory quality, financial reporting quality, ethics and audit quality. Based on the discussion, six different hypotheses were developed, which are summarised in Table 6.3 below.

Table 6.3: Summary of the hypotheses for the relationship between country-specific determinants and tax planning

Hypotheses	Tested relationships	Predicted Sign
H ₁₂	Management quality and level of tax planning	-
H ₁₃	Culture and level of tax planning	+
H ₁₄	Regulatory quality and level of tax planning	+
H ₁₅	Financial reporting quality and level of tax planning	+
H ₁₆	Ethics and level of tax planning	+
H ₁₇	Audit quality and the level of tax planning	-

Source: Compiled by the author from a literature review

6.4 Methodology

6.4.1 Data and Data Source

The study used a sample of listed firms from EACs comprising Kenya, Tanzania and Uganda. The dataset included financial, taxation and corporate governance information. This information was archival, as companies were required to publish it publicly through their annual reports (audited annual reports and accounts). Consequently, the data on corporate governance practices,

financial information and taxation of firms were obtained from Bloomberg, McGregor, financial stock markets and particular company websites. Data were collected on the variables of interest for an 12-year period, from 2008 to 2019. The starting date 2008 reflected the year when the EACs adopted their code of corporate governance, while the cut-off date, 2019, reflected the most currently available data. Although 1089 annual reports were targeted, those of some firms were not available, resulting in a shortage of 68 annual reports. As a result, 1021 annual reports were used for the study.

The corporate governance variables were collected manually from the annual reports, whilst the data on financial information and taxation were obtained from the above-mentioned databases in the form of three financial statements: statements of comprehensive income, statements of financial position and statements of cash flows.

6. 4.2 Definition and Measurement of Variables

6.4.2.1 Dependent Variable

The study used tax planning measured by the effective tax rate (ETR) as the dependent variable. Following recent studies (Armstrong et al., 2012; Chen et al., 2010; Dyreng et al., 2016; Lennox et al., 2013), This study used a cash effective tax rate (CETR), together with an accounting effective tax rate (AETR), to measure tax planning. The use of more than one measure helps to capture the broad range of activities that are symptomatic of tax planning. In addition, the use of multiple measures improves the robustness of the results.

An ETR is computed as the tax expense divided by a firm's pre-tax accounting income (Hanlon & Heitzman, 2010). Therefore, an ETR measures the ability of a company to minimise its tax, compared with its pre-tax accounting income, and is an indication of its tax burden relative to other firms. Firms with lower ETRs are said to be more tax aggressive compared to the firms with higher ETRs tax rates. CETR is computed as cash taxes paid divided by pre-tax accounting income (Dyreng et al., 2008; Chen et al., 2010), while AETR is computed as total tax expense divided by pre-tax accounting income (Chen et al., 2010; McGuire et al., 2012).

6.4.2.2 Independent Variables

Firm-Specific Characteristics

To examine the influence of firm-specific characteristics on tax planning, the study used five firm-specific factors: size, profitability, financing decisions, investments decision and age.

Size: To investigate the influence of size on a firm's tax planning, the study used the variable of firm size (SIZE), which was computed as the natural logarithm of total assets. This variable is largely used in previous papers related to tax planning (Armstrong et al., 2012).

Profitability: Following Armstrong et al. (2012) and Kraft (2014), the study included the profitability of a firm as another possible factor affecting its level of tax planning. A firm's profitability is commonly argued to have the explanatory power of its ETR. The study measured profitability using ROA, which is the ratio of pre-tax income to total assets, as used in Armstrong et al. (2012).

Financing Decisions: To evaluate the influence of financing decisions on the level of tax planning, the study included leverage, which was the ratio of long-term debt to shareholder equity, as computed by Chen et al. (2010). Chen et al. (2010) and Armstrong et al. (2012) are some of the authors who used leverage in their studies.

Investment Decisions: To investigate the influence of investment decisions on the level of tax planning, the study used capital intensity to represent the asset mix of the firms, which was the ratio of fixed assets to total assets. Asset mix has been used to investigate its power on tax planning variation (Gupta & Newberry, 1997; Derashid & Zhang, 2003; Richardson & Lanis, 2007; Minick & Noga, 2010).

Age: In addition, the study included the variable of age to investigate the influence of a firm's experience in business on its level of tax planning. The age variable was measured as the number of years a corporation's stock had been traded on the stock market (Maama et al., 2019).

Corporate Governance variables

The second group of hypotheses discussed in Section 6.3.2 was developed to test the influence of a firm's corporate governance mechanisms on tax planning. The discussion in the literature review revealed that the strength of a firm's corporate governance could influence its tax management

decisions. The study included variables related to board composition structure (board size, board independence and gender diversity), ownership structure (ownership concentration and institutional investors), and board compensation (managerial incentives).

Board Size: The variable used to represent the board of directors and its composition structure was board size (BOS), which was measured by the number of board members, as used by Wahab and Holland (2012). The dimension of the board of directors is a variable extensively used in the literature (Yermack, 1996; Eisenberg et al., 1998; Minick and Noga, 2010; Lanis and Richardson, 2011; Wahab and Holland, 2012).

Board Independence: Alongside the board size, the study used the variable of board independence (BOI), representing the ratio of the total number of non-executive directors to the total number of directors as computed in Lanis and Richardson (2011). Board independence was expected to influence decisions, which may affect a firm's ETRs. Therefore, the study included in the investigation several non-executive board members to capture their effect on tax planning.

Gender Diversity: The investigation of the influence of board composition as an element of corporate governance on tax planning included the variable of gender diversity (GDV). This variable was measured as the percentage of female directors on the board. Measurement of the composition of boards of directors has previously been used (Florackis 2008; Lanis & Richardson, 2011; Wahab & Holland, 2012).

Ownership Concentration and Institutional Investors: A firm's ownership structure was proxied by ownership concentration (OWN) and institutional investors (INV). This approach followed studies in the literature, such as those of Schmidt and Fahlenbrach (2017), Zhang et al. (2017) and Zhang (2016). The OWN variable was measured by the total number of shares held by shareholders with more than 5% shares (Wilde & Wilson, 2018). The INV variable was measured by the number of shares held by institutional investors (Zhang et al., 2017; Zhang, 2016).

Managerial Incentives: The last corporate governance variable was the board of directors' compensation structure represented by managerial incentives (MIV). This variable was measured by the logarithm of the remuneration paid to the board of directors (Armstrong et al., 2015; Huang et al., 2018a; Seidman & Stomberg, 2017).

All the corporate governance variables were measured on a yearly basis. Even though some studies consider these variables to be constant for more than one year, the study computed all variables year by year to obtain more precise and rigorous estimations.

Country-Specific Variables

The country-specific variables were sourced from the database of the World Economic Forum (WEF). The operationalisation of the variables and their measurements are explained below.

Management Quality: In the study, the management quality variable (MQ) measured the extent to which a country relied on professionals in senior management positions and ranged from 1 to 7, where 1 represented usually hiring relatives or friends without regard to merit, and 7 denoted hiring mostly professional managers chosen for merit and qualifications. This data was sourced from the WEF database.

Culture: The national cultural dimension was adopted from Hofstede's Values Survey Modules (VSM), and it was measured by the level of uncertainty avoidance. Uncertainty avoidance is the degree to which a group of individuals feels threatened by uncertainty, unknown or unstructured conditions (Hofstede, 2011). The culture variable (Culture) was sourced from Hofstede's uncertainty avoidance index, which ranges from 1 to 100, where 1 represents a country with low uncertainty avoidance, and 100 denotes a country with high uncertainty avoidance.

Regulatory Quality: Regulatory quality (RQ) indicated the strength of regulators to ensure the stability of the financial market. Moreover, it measured the strength of the legal rights of investors. The measurement ranged from 1 to 7, where 1 implied that a regulator's ability to ensure a stable financial market was weak for country i in year t , and 7 indicated that a regulator's ability to ensure stability in the financial market was strong for country i in year t . The data for the calculations were obtained from the World Economic Forum database.

Financial Reporting Quality: Financial reporting quality (FRQ) was measured based on Tang et al.'s (2016) model that they developed as a country-level measure. The authors employed six elements of accounting and auditing quality to determine the indicators of national FRQ, namely loss avoidance ratio (LAR), profit decline avoidance ratio (PDAR), qualified audit opinion ratio (QAOR), accruals ratio (AR) (in other words, scaled accruals), non-Big4 auditor ratio (NBAR)

and audit-fee ratio (AFR), (in other words, scaled audit fee). Given the values of the six indicators per capital market per year, an overall quality index method was adopted (Kurtzman, Yago & Phumiwasana, 2004; Kurtzman & Yago, 2007, 2008) to determine the FRQ for the sample markets.

The following are the steps followed to determine the FRQ for a capital market. Firstly, the study ranked capital markets based on the values of the six individual FRQ indicators calculated. Apart from AFR, these indicators related negatively to FRQ. Next, for each indicator out of the first five (apart from the AFR), the market with the lowest (highest for AFR) indicator value was given a score of 100, and the scores of other markets were calculated as a percentage of the top score. Next, the scores for each indicator were equally weighted and aggregated to calculate the yearly FRQI for each capital market (in other words, FRQI = the arithmetic average of the scores of six indicators). The index increased in reporting quality. Finally, the average of FRQ determined a market's overall FRQ and rank, which reflected the number of total markets of the sample, were indexed above it.

Ethics: In the study, the ethics variable (Ethics) measured the level of corporate ethics in interacting with public officials, politicians and other firms. It ranged from 1 to 7 where 1 signified extremely poor (among the worst in the world) for country i in year t , and 7 represented excellent (among the best in the world) for country i in year t . The ethics data were obtained from the database of the World Economic Forum.

Audit Quality: In the study, the audit quality variable (AQ) represented the strength of the auditing standards of a country regarding financial performance and ranged from 1 to 7, where 1 signified extremely weak, for country i in year t , and 7 signified extremely strong, for country i in year t . This data was obtained from the World Economic Forum database.

Table 6.3 below summarises the definitions, the acronyms and the expected signs of all the variables discussed in this section.

Table 6.3 Measurement of Variables

Variables	Symbol	Expected Sign	Operationalisation
Dependent Variables			
Cash effective tax rate	CETR	N/A	Cash taxes paid divided by pre-tax income
Accounting effective tax rate	AETR	N/A	Total tax expense divided by pre-tax earnings
Independent variables (Firms' specific characteristics)			
Firm size	SIZE	+	SIZE, which is computed as the natural logarithm of total assets
Return on assets	ROA	+	This study measures the profitability using return on assets as the ratio of pre-tax income and total assets
Leverage	LEV	-	Leverage is the ratio between long term debt and shareholders' equity
Capital Intensity	CTN	-	Determined as fixed assets over total assets
Age of the firm	AGE	-	Measured as the number of years that a firm's stock has been traded on the stock market
Independent variables (Corporate Governance variables)			
Board size	BOS	-	Measured by the total number of directors on the corporate board
Board Independence	BOI	+	Percentage of non-executive directors to number of directors
Gender diversity	GDV	+	Measured in terms of the percentage of women on the board
Managerial incentives	MIV	-	Measured as the log of the total remuneration paid to executive
Ownership concentration	OWN	-	Measured by the total number of the shares held by shareholders who own 5% or more of shares in the firm
Institutional investors	INV	+	Percentage of shares held by substantial institutional shareholders

Independent variables (Country-specific variables)			
Quality Management	QM	-	Measured by the strength of regulators to ensure the stability of the financial market (according to a range from 1 to 7)
Culture	Culture	+	Adopted from Hofstede's Values Survey Modules (VSM); measured by the level of uncertainty avoidance (according to a range from 1 to 100)
Regulatory Quality	RQ	+	Measured by the strength of regulators to ensure the stability of the financial market (according to a range from 1 to 7)
Financial Reporting Quality	FRQ	+	Measured based on Tang et al.'s (2016) model
Ethics	Ethics	+	Measured by the level of corporate ethics of companies in interacting with public officials, politicians and other firms (according to a range from 1 to 7)
Audit Quality	AQ	-	Measured by the strength of the auditing standards of a country for financial performance (according to a range from 1 to 7)

Source: Author's Compilation

6.4.3 Model Specification and Estimation Method

The study used a panel data estimating technique, which is also referred to as longitudinal or cross-sectional time-series data. With this type of data, the individual behaviours of entities are observed across time (Jaba, Robu & Balan, 2017). These entities could be states, companies, individuals, or countries, for example. Jaba et al. (2017). One significant advantage of panel data is that it can control for individual heterogeneity and allow identifying and measuring effects that are not detectable using other data models (Khan et al., 2018). In addition, it has the benefit of reducing collinearity and allowing more degrees of freedom while being more efficient. In this sense, a panel data structure controls for unobservable effects in cross-section and time dimensions. Panel data also allows for the inclusion of variables at different levels of analysis (for example, students, schools, districts and states) suitable for multilevel or hierarchical modelling. With panel data, the most commonly estimated models are fixed effects models and random-effects models.

6.4.3.1 Fixed Effects

The fixed-effects (FE) model is used in areas where a study analyses the impact of variables that vary over time (Jaba et al., 2017). This suggests that the FE model explores the relationship between predictor and outcome variables within an entity (country, person, company). According to Asteriou and Hall (2015), the FE estimation technique is employed where each entity has characteristics that may or may not influence the predictor variables. For instance, being a male or female could influence the opinion of a specific issue, the political system of a particular country could affect trade or GDP, or the business practices of a company may influence its stock price. When using the FE model, authors assume that something within the individual may influence or bias the predictor or outcome variables. Thus, there is a need to control for this. This is the rationale behind the assumption of the correlation between an entity's error term and predictor variables.

The FE model removes the effect of time-invariant characteristics to assess the net effect of the predictors on the outcome variable. Another important assumption of the FE model is that time-invariant characteristics are unique to the individual and should not be correlated with other individual features (Wong & Tang, 2018). Since each entity is different, the entity's error term and the constant (which captures individual characteristics) should not be correlated with others. Nevertheless, if the error terms are related, then the FE model is not suitable since inferences may not be correct, and there is a need to model that relationship (probably using random effects); this is the primary rationale for the Hausman test.

The FE can control for omitted variables bias as long as these variables are time-invariant. The use of the FE model has been largely supported in the literature because of its ability to produce a consistent estimator. Consistent estimation means that the values around various sample means are differenced (Blundell, Bond & Windmeijer, 2001). The FE model also controls for the effect of time-invariant differences between the individuals. The equation for the FE model is as follows:

$Y_{it} = \beta_1 X_{it} + \alpha_i + \mu_{it}$	(i)
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Where α_i ($i= 1, \dots, n$) is an unknown intercept for each entity. Y_{it} is the dependent variable where i = entity and t = time. X_{it} represents a vector of independent variables (it contains covariates that are not time constant). β_1 denotes the coefficients for independent variables and α_i is the

unobserved individual-level effect fixed over time (fixed effect). It could also incorporate a fixed effect for time; λ_t . μ_{it} is the error term.

6.4.3.2 Random Effect

The rationale behind the random-effects (RE) model is that, unlike the fixed effects model, the variation across entities is assumed to be random and uncorrelated with the predictor or independent variables included in the model (Castro & Arino, 2016). According to Green (2008), the crucial distinction between fixed and random effects is whether the unobserved individual effect embodies elements that are correlated with the regressors in the model, not whether these effects are stochastic or not. An advantage of the RE model is that a study can include time-invariant variables (Khan et al., 2018). In the FE model, these variables are absorbed by the intercept.

The RE model assumes that the entity's error term is not correlated with the predictors, which allows for time-invariant variables to play a role as explanatory variables. In the RE model, researchers need to specify the individual characteristics that may or may not influence the predictor variables. The problem with this is that some variables may not be available, leading to omitted variable bias in the model. The RE model allows the generalisation of inferences beyond the sample used in the model. The random-effects model is stated as follows:

$Y_{it} = \beta X_{it} + \alpha + \varepsilon_{it} + \mu_{it}$	(ii)
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6.4.3.3 Selection of the Fixed Effects or Random Effects Model

In deciding whether to select the estimation technique of the fixed effects or random effects model, a Hausman test is run whereby the null hypothesis is that the preferred model is random effects versus fixed effects (Torres-Reyna, 2007). The Hausman test basically tests whether unique errors μ_{it} are correlated with the regressors; the null hypothesis is that they are not. The null hypothesis is rejected when the probability of the Hausman test is significant ($p < 0.05$). Thus, a fixed effects model is adopted. However, the null hypothesis cannot be rejected when the

probability of the Hausman test is insignificant ($p > 0.05$); hence, a random effects model is considered.

6.4.3.4 Model Specifications

To test the first set of hypotheses about the influence of a firm's specific characteristics on the level of tax planning, the study presented two regression models. These two models only differed in the dependent variables, CETR and AETR. These models were our initial point of investigation. The first two regressions models were as follows:

$$CETR_{it} = \beta_0 + \beta_1 SIZE_{it} + \beta_2 ROA_{it} + \beta_3 LEV_{it} + \beta_4 CNT_{it} + \beta_5 AGE_{it} + \mathcal{E}_{it} \quad (1)$$

$$AETR_{it} = \beta_0 + \beta_1 SIZE_{it} + \beta_2 ROA_{it} + \beta_3 LEV_{it} + \beta_4 CNT_{it} + \beta_5 AGE_{it} + \mathcal{E}_{it} \quad (2)$$

Where

CETR	Cash effective tax rate	AGE	years of existence of the firms
AETR	Accounting effective tax rate	β_0	constant of the equation
SIZE	Size of the firms at a time	β_1 to β_5	Coefficients of the variables
ROA	Return on assets	\mathcal{E}_{it}	the stochastic error term
LEV	leverage	<i>i</i>	Firms
CNT	Capital intensity	<i>t</i>	Time (the year 2007 to 2018)

Next, the study tested the second phase of the hypotheses that investigated whether corporate governance mechanisms influence the level of tax planning. Therefore, the study extended equations 1 and 2 to include corporate governance variables in the regressions. These variables were related to board composition structure, ownership structure and board compensation structure. This second set of equations was as follows:

$$CETR_{it} = \beta_0 + \beta_1 BOS_{it} + \beta_2 BOI_{it} + \beta_3 GDV_{it} + \beta_4 MIV_{it} + \beta_5 OWN_{it} + \beta_6 INV_{it} + \mathcal{E}_{it} \quad (3)$$

$$AETR_{it} = \beta_0 + \beta_1 BOS_{it} + \beta_2 BOI_{it} + \beta_3 GDV_{it} + \beta_4 MIV_{it} + \beta_5 OWN_{it} + \beta_6 INV_{it} + \mathcal{E}_{it} \quad (4)$$

Where:

CETR	<i>Cash effective tax rate</i>	INV	<i>Institutional Investors</i>
AETR	<i>Accounting effective tax rate</i>	β_0	<i>Constant of the equation</i>
BOS	<i>Board Size</i>	β_1 to β_5	<i>Coefficients of the variables</i>
BOI	<i>Board Independence</i>	ϵ_{it}	<i>The stochastic error term</i>
GDV	<i>Gender Diversity</i>	<i>i</i>	<i>Firms</i>
MIV	<i>Managerial Incentives</i>	<i>t</i>	<i>Time (the year 2007 to 2018)</i>
OWN	<i>Ownership Concentration</i>		

Following previous studies, such as those of Parisi (2016), Irianto et al. (2017), Huseynov et al. (2017), Schmidt and Fahlenbrach (2017), Askenberg and Isaksson (2018), Chen et al. (2019) as well as Ermasova, Haumann and Burke (2021), the study developed models 5 and 6 to examine the country-specific determinants of tax planning in EACs. Here, the study investigated whether institutional factors that are specific to a particular country significantly influence the tax planning of that country.

$$CETR_{it} = \beta_0 + \beta_1 QM_{it} + \beta_2 Culture_{it} + \beta_3 RQ_{it} + \beta_4 FRQ_{it} + \beta_5 Ethics_{it} + \beta_6 AQ_{it} + \epsilon_{it} \dots \quad (5)$$

$$AETR_{it} = \beta_0 + \beta_1 QM_{it} + \beta_2 Culture_{it} + \beta_3 RQ_{it} + \beta_4 FRQ_{it} + \beta_5 Ethics_{it} + \beta_6 AQ_{it} + \epsilon_{it} \dots \quad (6)$$

Where:

CETR	<i>Cash effective tax rate</i>	AQ	<i>Audit quality</i>
AETR	<i>Accounting effective tax rate</i>	β_0	<i>Constant of the equation</i>
QM	<i>Management quality</i>	β_1 to β_5	<i>Coefficients of the variables</i>
Culture	<i>Culture of a country</i>	ϵ_{it}	<i>The stochastic error term</i>
RQ	<i>Regulatory quality</i>	<i>i</i>	<i>Firms</i>
FRQ	<i>Managerial incentives</i>	<i>t</i>	<i>Time (the year 2007 to 2018)</i>
Ethics	<i>Ethics</i>		

The following section presents the results from the statistical analysis of the factors that influenced the tax planning practices of firms in EACs.

6.5 Results and Discussion

This section presents the results of the variables that influenced the tax-planning practices of firms in EACs. This section is organised into three main sections. The first section presents and discusses the results of the statistical analysis of the firms-specific variables that influenced the firms' tax planning activities, whilst the second section presents and discusses the results of the statistical analysis of the corporate governance variables that influenced the tax planning of the firms. Lastly, the results of the statistical analysis of the country-specific variables that affected tax planning are presented and discussed in Section 3.

6.5.1 Hausman Tests

After establishing that the panel data estimation models were appropriate techniques in Section 6.5.3 above, the study explored the type of panel data estimation model to be adopted (either an FE or an RE model). The Hausman test was used to decide whether FE or RE was the appropriate technique in equations 1 to 6. The results of the Hausman tests are reported in Table 6.5 below. The results showed that the first two equations, which analysed the relationship between firm-specific characteristics and tax planning using CETR (Model 1) and AETR (Model 2), each obtained a $p < 0.05$. These results were significant. Therefore, H_0 was rejected in the research models, implying that the models had to be estimated using the fixed effect estimation method.

Investigating the association of corporate governance and tax planning using CETR (Model 3) and AETR (Model 4), the results were ($p = 0.1321$) and ($p = 0.0752$), respectively. In addition, the p-values in models 5 and 6 were more than 0.05, indicating that the results were insignificant. The results in Models 3 to 6 suggested that the results were insignificant, and thus the null hypothesis of the presence of time-specific variations in the models was not rejected. As a result, a generalised least squares (GLS) random effects model was to be used for Models 3, 4, 5 and 6 in the estimation.

Table 6.5: Hausman Tests

	Model	Measure	Chi-Sq. Stats	Chi-Sq. d.f.	Prob.	Results
Firms-Specific Variables	1	CETR	47.3226	6	0.0000	H0-Rejeted
	2	AETR	41.1343	13	0.0001	H0-Rejeted
Corporate Governance Variables	3	CETR	18.7178	13	0.1321	H0-Accepted
	4	AETR	15.8113	8	0.0752	H0-Accepted
Country-Specific Variables	5	CETR	17.392	9	0.0838	H0-Accepted
	6	AETR	28.175	11	0.1037	H0-Accepted

Source: Author's Computation

6.5.2 Firm-Specific Factors that Influence Tax Planning

6.5.2.1 Descriptive Statistics

The summary of the descriptive statistics for the variables is presented in Table 6.6. This table displays the summary of the descriptive statistics of both dependent variables (CETR and AETR) and independent variables, including firm-specific characteristics (SIZE, ROA, LEV, CNT and AGE) from 2008 to 2019.

Table 6.6: Descriptive Statistics

	Obs.	Mean	Median	Max.	Min.	SD	Skewness	Kurtosis	Jarque-Bera
AETR	1021	0.263	0.289	0.30	0.000	0.139	0.928	8.351	121.56
CETR	1021	0.195	0.191	0.30	0.000	0.107	0.895	4.356	176.36
SIZE (\$m)	1021	48.67	48.69	203.85	13.59	27.01	-0.097	2.432	12.565
ROA	1021	0.086	0.057	0.692	-0.557	0.151	-0.0296	6.897	53.199
LEV	1021	0.578	0.606	0.995	0.007	0.252	-0.265	1.674	71.254
CNT	1021	0.599	0.635	0.983	0.009	0.212	-0.635	2.806	57.840
AGE	1021	27.000	26.000	67.000	14.0000	12.947	0.687	2.718	68.814
CETR	Cash effective tax rate			ROA	Return on assets		CNT	Capital intensity	
AETR	Accounting effective tax rate			LEV	Leverage		AGE	Years of existence of the firms	
SIZE	Size of the firms at time								

Source: Author's Computation

For the dependent variables, the results showed that the mean value of the accounting effective tax rate (AETR) was 0.263 (26.3%) while that of the tax effective tax rate (CETR) was 0.195 (19.5%). This showed that, on average, the tax liabilities of the firms in the EACs represented 26.3%. However, the firms paid 19.5% as tax, suggesting tax-planning activities. This is because the statutory tax rate for all three EACs (Kenya, Tanzania, and Uganda) had been 30% over the past 12. Therefore, the mean value of less than 30% indicated the presence of tax planning in EACs. The standard deviation (SD) of AETR and CETR were 0.139 and 0.107, respectively. This suggested a small degree of dispersion of AETR and CETR amongst the firms in the EACs.

Furthermore, the mean value of firm-specific variables, such as firm size, return on assets (ROA), leverage, capital intensity and age were 48.67, 0.086, 0.578, 0.599 and 19.992, respectively. The average firm size of 48.67 indicated that the average total assets of the firms amounted to \$48.67 million, with maximum and minimum values of \$13.59 million and \$203.85 million, respectively. This showed that the firms in the EACs had relatively large assets. A standard deviation of 27.01, suggested wide variations amongst the asset size of the firms. In addition, the average ROA of 0.086 indicated that the average ROA of the firms was 8.6%, suggesting that they were profitable, albeit small. In addition, the results showed that the average leverage of the firms was 0.578. This showed that, on average, the debt of firms in EACs represented 57.8%. This result suggested that the firms were not highly geared. Concerning the capital intensity of the firms, the mean value was 0.599. This suggests that the percentage of fixed assets to total assets of the firms was relatively low.

Data are normally distributed if they have bell-shaped probability density (Hansen, 2017). Therefore, data with bell-shaped probability are within the standard kurtosis of plus or minus 3 and standard skewness of plus or minus 1.96 (Haniffa, 2006). The descriptive statistics presented in Table 6.6 above showed that most of the variables used in the estimation model did not meet the assumption of normality. However, results indicated that all variables met the standard skewness assumption with a value less than 1.96, but most did not meet the kurtosis assumption. For instance, only SIZE, LEV, CNT and AGE had a kurtosis of less than 3. This result suggested that the ordinary least square (OLS) model was not an appropriate estimation technique. As a result, the study used FE and RE, which is suggested to be a more sophisticated technique that could offer more robust results than the OLS estimation technique (Tshipa, 2017).

6.5.2.2 Multicollinearity Tests

The Pearson correlation matrix, together with the variance inflation factor (VIF), were performed to check the possibility of multicollinearity amongst the independent variables used in the model. Table 6.7 below provides the results of the Pearson correlations matrix and VIF. The results of the VIF and correlation matrix showed that all variables were far from being highly correlated. The estimation indicated that the VIF of all variables was less than two, which was far from the threshold of 10, which is suggested by literature (Menard, 2002). These outcomes suggested that no variables used in this analysis suffered from multicollinearity. Similarly, the correlation matrix results suggested no strong correlation among the variables used in the analysis. All the correlation coefficients were less than 0.5, suggesting that the variables were not highly correlated. These results showed that the use of these variables in the regression would not produce any spurious results.

Table 6.7: Pearson correlation matrix together with the Variance Inflation Factor (VIF)

	CETR	AETR	SIZE	ROA	LEV	CNT	AGE	VIF
CETR	1.000							1.39
AETR	.893***	1.000						1.92
SIZE	.155	.064	1.000					1.06
ROA	.241**	.203**	-.104	1.000				1.29
LEV	.096	.022**	.068	-.422*	1.000			1.62
CNT	-.269*	-.156	.097**	-.189	.013*	1.000		1.83
AGE	-.047	.015	-.004	-.065	-.104**	.119	1.000	1.47
CETR	Cash effective tax rate		ROA	Return on assets	CNT	Capital intensity		
AETR	Accounting effective tax rate		LEV	Leverage	AGE	Years of existence of the firms		
SIZE	Size of the firms at time							

Source: Author's Computation

6.5.2.3 Regression Results of the Impact of Firm-Specific Characteristics on Tax Planning

This section presents the results and discussion of the influence of firm-specific characteristics on the level of tax planning. Table 6.8 below presents the regression results of Models 1 and 2, which analysed the impact of the firms' specific characteristics on tax planning, using the cash effective tax rate (Model 1) and the accounting effective tax rate (Model 2).

Table 6.8: Regression Results: The Influence of Firm-Specific factors on Tax Planning

Variable	Model 1	Model 2
Size	1.1668*** (7.486)	0.0674** (2.0705)
Return on Assets	0.1493*** (4.662)	0.3754*** (3.2989)
Leverage	0.0499 (0.542)	0.1286 (1.496)
Capital intensity	-0.0716 (-1.028)	-0.0528 (-0.756)
Age	0.4012*** (3.382)	1.1703*** (7.701)
C	-0.3901** (-2.322)	-1.6225*** (-2.679)
R-squared	0.5525	0.5576
Adjusted R-squared	0.4436	0.4502
F-statistic	5.0725	5.1927
Prob(F-statistic)	0.0000	0.0000
Prob. of Hausman test	0.0000	0.0000
Durbin-Watson stat	2.2554	2.2785

Source: Author's Computation

Note: *** = Significance at 0.01; ** = at 0.05 and * = at 0.1, and * = at 0.1,

Table 6.9: Summary of Hypotheses and Results of the Association between Firm-Specific Characteristics and Tax Planning

Independent Variable	Hypothesis Number	Tested relationships	Results		Model	Conclusion	Significance level	Relevant theory
			M1	M2				
Firm size	H1	Firm size and level of tax planning	Accepted	Rejected	M1a	Firm size has a positive and significant association with the cash effective tax rate (CETR)	(V ⁺ , p<0.1)	The positive relationship supports the political cost theory
			Accepted	Rejected	MIib	Firm size has an insignificant influence on the accounting effective tax rate (AETR)	(V ⁺ , p<0.1)	No impact association rejects the political power and the political cost theory
Return on assets	H2	ROA and level of tax planning	Accepted	Accepted	M1a	ROA has a positive influence on the CETR	(V ⁺ , p<0.1)	The positive relationship supports the political cost theory
			Accepted	Accepted	MIib	ROA has a positive influence on the AETR	(V ⁺ , p<0.1)	The positive relationship supports the political cost theory
Leverage	H3	Leverage and level of tax planning	Rejected	Rejected	M1a	Leverage has no significant influence on the CETR	(V ⁺ , p<0.1)	No impact association rejects the agency theory and the stakeholder theory
			Rejected	Rejected	MIib	Leverage has no significant influence on AETR	(V ⁺ , p<0.1)	No impact association rejects the agency theory and stakeholder's theory
Capital intensity	H4	Capital intensity and level of tax planning	Rejected	Rejected	M1a	Capital intensity has insignificant influence on the CETR	(V ⁺ , p<0.1)	No impact association rejects the political power and the political cost theory
			Rejected	Rejected	MIib	Capital intensity has an insignificant influence on the AETR	(V ⁺ , p<0.1)	No impact association rejects the political power and the political cost theory
Age	H5	Age and level of tax planning	Accepted	Accepted	M1a	Age has a positive and statistically significant influence on the CETR	(V ⁺ , p<0.1)	The positive relationship supports the political cost theory
			Accepted	Accepted	MIib	Age has a positive and statistically significant influence on the AETR	(V ⁺ , p<0.1)	The positive relationship supports the political cost theory

Source: Author's Computation

Note

	Significant
	Insignificant

- M1 Is Model 1** This model uses cash effective tax rate (CETR) as the proxy for tax planning
- M2 Is Model 2** This model uses accounting effective tax rate (AETR) as a proxy for tax planning

The study analysed the influence of firm-specific characteristics on the firms' level of tax aggressiveness in Model 1 and Model 2, using the fixed effects model. Model 1 and Model 2 included different tax planning measures as dependent variables and firm-specific characteristics as independent variables. Table 6.8 above exhibits the estimation results for Models 1 and 2. As explained above, the two models had the same independent variables, and the only difference was the measure of the dependent variable, which was the tax planning variable. Model 1 used CETR, which was the main measure of tax planning of the study, while Model 2 used the accounting effective tax rate (AETR) as the alternative measure of tax planning. The cash effective tax rate was expected to be a more reliable measure of tax planning because the literature shows that it can control for the effects of tax reductions through other factors, which are not necessarily tax-planning activities (Zimmerman, 1983). Therefore, our discussion is based chiefly on Model 1, although Model 2 is also discussed to support Model 1's results.

The hypotheses were tested by examining whether the explanatory variables (the five firm-specific characteristics) were statistically significant at 1% and 5% levels to predict the level of tax-planning variation. Hypothesis One (H_1) predicted a significant positive relationship between firm size and level of tax planning, measured by CETR and accounting effective tax rate (AETR). The results in Table 6.8 above showed that the size of the firms (SIZE) has a significant positive association with CETR ($p < 0.01$) and AETR ($p < 0.05$). This finding supported H_1 that firm size influences the level of tax planning. This finding suggested that large companies report higher effective tax rates, that is, a low level of tax planning than small firms, which implies that larger firms do not engage in tax planning activities as much as smaller firms. This finding also suggested that an increase in the size of a firm would result in a decrease in its tax planning activities.

A possible explanation of these results is that large firms are exposed to effective and efficient scrutiny by various regulatory agencies, stakeholders and, particularly, the tax authority. They would have little or no chance to minimise tax expenses aggressively. Another explanation is that larger firms are concerned about their reputation and would like to protect it, hence their decision not to engage in tax planning activities. In other words, the community may view big firms that pay less tax as socially irresponsible, which damages their reputation.

This explanation is consistent with the legitimacy theory, which explains that firms may want the public to perceive them as responsible, which may force them to pay higher taxes and will enhance

their public image and acceptance. The results also supported the political cost theory, which postulates that big companies prevent a negative reputation by avoiding aggressive tax planning. Moreover, the results conformed with findings of several other studies, such as those of Askenberg and Isaksson (2018), Kraft (2014), Minnick and Noga (2010), Rego (2003), Ribeiro (2015) and Zimmerman (1983). These studies found that an increase in a firm's size increases the ETR (less tax avoidance).

Hypothesis Two (H_2) predicted that a firm's profitability measured by ROA has a significant and positive relationship with the ETR. This hypothesis postulated that more profitable firms report higher ETRs (less tax planning) than less profitable firms. The results in Table 6.8 above showed that ROA has a positive and statistically significant association with CETR well below ($p < 0.01$) and AETR at the level of ($p < 0.05$), which is consistent with H_2 . This finding affirmed that more profitable firms are less tax aggressive than those that are less profitable. The results were not surprising because it is expected that tax rates are progressive according to income. Therefore, profitable firms are expected to pay more taxes than the less profitable ones.

Similarly, these results suggested that profitable firms have higher earnings that would allow them to pay their taxes. In addition, these results were consistent with political cost theory, suggesting that large and more profitable firms are exposed to government regulations that reduce their chance of tax avoidance. The finding of a positive relationship between ETRs and ROE was consistent with that of Richardson and Lanis (2007), Minick and Noga (2010) and Armstrong et al. (2012). However, these results contradicted the conclusions of Derashid and Zhang (2003) as well as Kraft (2014), who documented a negative association between effective tax rates and firm profitability. With this finding, the study accepted the second hypothesis that there is an association between tax planning and ROA.

Hypothesis Three (H_3) envisaged a negative and statistically significant relationship between leverage and level of tax planning. This hypothesis predicted that firms with a high leverage ratio have a low ETR (more tax aggressive). As anticipated, the results in Table 6.8 above showed that leverage has a positive but statistically insignificant association with CETR and AETR ($p > 0.1$). This was inconsistent with H_3 , which predicted a positive and statistically significant relationship between leverage and ETR. The study predicted a negative association between ETR and leverage because a higher leverage ratio implies that a firm uses more debts than equity as its tax-planning

strategies. Leverage reduces taxable income because the use of debts accumulates interests, which are tax-deductible expenses. Contrary to the expectation of the study that there is a negative relationship between leverage and ETR, the analysis revealed a positive and statistically insignificant association. These findings aligned with Minnick and Noga (2010) as well as Taylor and Richardson (2013). Thus, the research showed that managers might view debt as a burden for a company (Gitman, 2006; Godfrey et al., 2013), and therefore they choose to remove it, rather than use it as a tax avoidance tool.

Hypothesis Four (H₄) predicted a negative and significant relationship between capital intensity and the ETR. It suggested that firms with a high capital intensity ratio have a lower ETR than firms with a low capital intensity ratio. The results from Models 1 and 2 showed that capital intensity has a negative and insignificant relationship with CETR and AETR (i.e. $p > 0.1$). These results indicated that firms with high capital intensity (more fixed assets) have a lower effective tax rate. Furthermore, the results confirmed H₄. This finding was accepted because firms with higher capital intensity exhibit a lower ETR due to the deductibility of depreciation and amortisation expenses. Big investments in physical assets, for example, tend to use higher values of depreciation expense to reduce their assessable income, and therefore pay lower income tax expenses. This evidence was in line with the findings of other studies (Gupta & Newberry, 1997; Richardson & Lanis, 2007). However, the insignificant results might have been because firms in emerging economies are relatively incapable financially of having massive investments in physical assets.

Hypothesis Five (H₅) envisaged a positive relationship between age and tax planning (EETR). This hypothesis predicted that older firms have a higher ETR (less tax aggressive) than new firms. Table 6.8 above shows that age is positive and statistically significant with CETR ($p < 0.01$) and AETR at ($P < 0.05$). This result was consistent with H₅, which predicted a positive relationship between age and the ETR in EACs. This finding indicated that older firms are less tax aggressive than new firms. One might expect that the old firms with experiences and connections have the advantage to reduce taxes. However, this result confirmed the political cost theory that older and big companies may be under close government monitoring, which could limit their possibilities of averting tax. These results showed that the older firms in EACs tried to be good citizens by paying their fair taxes to the government. These firms likely tried to avoid reputation loss due to their long history of good reputations and goodwill. The high involvement in tax planning by the more recently listed

firms might have been facilitated by pressure from the firms' owners and stakeholders to compel management to meet earning expectations.

Furthermore, the adequacy of the independent variables in explaining the dependent variables was tested. The general results showed that, in Models 1 and 2 that examined the influence of firm-specific characteristics on tax planning, all variables had an influence, except leverage and capital intensity. Moreover, the results indicated that the models were robust and justified by the high coefficients of R^2 and adjusted R^2 . The results show that R^2 was 55.24% for Model 1 and 55.56% for Model 2. This meant that the two models showed that firm-specific characteristics could explain about 55% variations in the level of tax planning. This result showed that the findings related to the first regression were more robust concerning the influence of firms' characteristics on the ETR tax rate. On the whole, the finding of the estimations indicated that the firm-specific characteristics influence the level of corporate tax planning measured by the ETR.

6.5.3 Influence of Corporate Governance on Tax Planning

This section presents the results and discussions of the influence of corporate governance on the level of tax planning. The regression results of Models 3 and 4 presented in Table 6.10 below analysed the influence of corporate governance on tax planning using the CETR (Model 3) and the AETR (Model 4).

6.5.3.1 Descriptive Statistics

Table 6.10 below presents the descriptive statistics of the variables used for the estimation.

Table 6.10: Descriptive Statistics

	Obs.	Mean	Median	Max.	Min.	SD	Skewness	Kurtosis	Jarque-Bera	
AETR	1021	0.263	0.289	0.30	0.000	0.139	0.928	1.351	121.56	
CETR	1021	0.195	0.191	0.30	0.000	0.107	0.895	1.356	176.36	
BOS	1021	8.522	8.000	14.000	5.000	1.666	1.119	1.995	209.547	
BOI	1021	0.877	0.857	1.857	0.000	0.189	0.664	1.507	140.94	
GDV	1021	0.244	0.250	0.600	0.000	0.134	-0.253	1.224	29.976	
MIV	986	1.3163	1.2927	1.8245	0.6487	1.653	-0.1827	1.958	35.269	
OWN	972	8.0128	37.414	95.00	17.110	9.936	0.781	1.013	346.503	
INV	1008	66.092	64.249	95.825	1.850	15.673	-0.0791	1.376	5.816	
CETR	Cash effective tax rate			BOS	Board size		MIV	Managerial incentives		
AETR	Accounting effective tax rate			BOI	Board independence		OWN	Ownership concentration		
VIF	Variance inflation factor			GDV	Gender diversity		INV	Institutional investors		

Source: Author's Computation

The results showed that the mean value of the accounting effective tax rate (AETR) was 0.263 (26.3%), while that of the CETR was 0.195 (19.5%). These results suggested that, on average, the firms' tax liabilities represented 26.3% of their profit. However, the CETR of 0.195 indicated that the firms paid 19.5% as tax, suggesting tax-planning activities. The CETR of 19.5% represented a significant tax planning activity because the statutory tax rate (STR) for all three EACs (Kenya, Tanzania and Uganda) had been 30% over the previous 11 years. Hence, the mean value of less than 30% indicated tax planning activities in EACs. Furthermore, the standard deviation (SD) of AETR and CETR were 0.139 and 0.107, respectively, indicating a small degree of dispersion of AETR and CETR amongst the firms in the EACs.

Regarding corporate governance variables, the board size (BOS) obtained a mean value of 8.522, suggesting that the average size of the board of directors was 8.5. In addition, the mean value of board independence (BOI) was 0.877, which suggested that about 87.7% of the board of directors of the firms in EACs were independent directors. This result highlighted that the firms' board of directors enjoyed a significant degree of autonomy from management. The results further showed that the mean value of the GDV variable was 0.244, indicating that about a quarter (24.4%) of the

board of directors were females. This result showed a greater level of diversity in the board, given that female representation on the board had been insignificant over the years.

Concerning the managerial incentive variable (MIV), the mean value was 1.3163, with maximum and minimum values of \$1.8245 and \$0.6487, respectively. The average mean for ownership concentration (OWN) was 38.01%. This result suggests that, on average, 38.01% of the shares in the EACs firms were owned by individuals who held not less than 5% of the shares/ownership of the firms. The results further showed that the INV variable obtained a mean of 66.09%. This indicated that institutional investors owned about 66.09% of the shares of firms in EACs. It was therefore expected that they would have exercised supervision and control over the management of the firms; hence, there would have been minimal rent extraction and unethical business activities.

The results further exhibited an attribute of normally distributed data because most of the variables used in the estimation model met the standard skewness assumption with a value less than 1.96. In addition, the kurtosis of all the variables was less than 2.0, which suggested that they met the assumptions of kurtosis. For instance, only SIZE, LEV, CNT and AGE had a kurtosis of less than three. As a result, the study used FE and RE, which is suggested to be a more sophisticated technique that could offer more robust results than the OLS estimating technique (Tshipa, 2017).

6.5.3.2 Multicollinearity Tests

The Pearson correlation matrix, together with the variance inflation factor (VIF), was performed to check the possibility of multicollinearity among the independent variables used in the model. Table 6.11 below provides the results of the Pearson correlations matrix and VIF. The results of the VIF and correlation matrix showed that all variables are far from being highly correlated. Our estimation showed that the VIF of all variables was less than two (2), which was far from the threshold of 10, suggested by literature (Menard, 2002). These outcomes suggested that no variables used in this analysis suffer from multicollinearity. Similarly, the correlation matrix results suggested no strong correlation amongst the variables used in the analysis. All the correlation coefficients were less than 0.5, suggesting that the variables were not highly correlated. These results showed that the use of these variables in the regression would not produce any spurious results.

Table 6.11: Correlation Matrix

	CETR	AETR	BOS	BOI	GDV	MIV	OWN	INV	VIF
CETR	1.000								3.82
AETR	.893***	1.000							1.55
BOS	.083*	.018	1.000						2.92
BOI	.149*	.071	.372**	1.000					3.08
GDV	.004	.092	.036	-.286***	1.000				5.72
MIV	.035**	.058*	-.097	-.087	-.257**	1.000			3.67
OWN	-.017***	-.014**	.081*	.043	-.408	-.089*	1.000		4.89
INV	-.061***	.052*	.217	-.091	.339**	.024	-.072	1.000	1.62
CETR	Cash effective tax rate		BOI	Board independence		OWN	Ownership concentration		
AETR	Accounting effective tax rate		GDV	Gender diversity		INV	Institutional investors		
BOS	Board size		MIV	Managerial incentives					

Source: Author's Computation**6.5.3.3 Regression Results**

This section presents and discusses the influence of corporate governance on the level of tax planning of firms in EACs. Table 6.12 below presents the regression results of Models 3 and 4, which analysed the influence of corporate governance on tax planning using the CETR (Model 3) and AETR (Model 4).

Table 6.12: Regression Results of Tax Planning and Corporate Governance Variables

Variable	Model 3 (CETR)	Model 4 (AETR)
Board Size	-0.01819** (-1.984)	-0.0205** (-1.986)
Board Independence	0.1975*** (6.881)	0.0029** (1.973)
Gender Diversity	0.2139** (1.975)	0.023*** (3.719)
Managerial Incentives	-1.9061** (-2.34)	-0.0519 (-0.724)
Institutional Investors	0.0031** (2.051)	0.0525** (2.074)
Ownership Concentration	-0.0694** (-2.064)	-0.2316*** (-2.949)
C	-1.0242 (-1.559)	1.2793** (2.128)
R-squared	0.579	0.5483
Adjusted R-squared	0.4602	0.4317
F-statistic	4.8591	4.7006
Prob(F-statistic)	0.0000	0.0000
Prob. of Hausman Test	0.1321	0.0452
Durbin-Watson Stat	2.3051	2.3051

Source: Author's Computation

Note: *** = Significance at 0.01; **= Significance at 0.05 and * = Significance at 0.1, and * = at 0.1

Table 6.13 Summary of Hypotheses and Results on the Association between Corporate Governance and Tax Planning

Independent Variable	N/S	Tested relationships	Results		Model	Conclusion	Level of significance	Relevant theory
			M1	M2				
Board size	H ₆	Board size and level of tax planning	Accepted	Accepted	M1a	Board size has a negative and significant association with the cash effective tax rate (CETR)	(V ⁻ , p<0.1)	The negative relationship supports the agency theory, the stakeholder theory and the resource dependence theory
			Accepted	Accepted	MI Ib	Board size has a negative and significant association with the accounting effective tax rate (AETR)	(V ⁻ , p<0.1)	The negative relationship supports the agency theory, the stakeholder theory and the resource dependence theory
Board Independence	H ₇	Board Independence and level of tax planning	Accepted	Accepted	M1a	Board independence has a positive influence on the CETR	(V ⁺ , p<0.1)	The positive relationship supports agency theory and the stakeholder theory
			Accepted	Accepted	MI Ib	Board independence has a positive influence on the AETR	(V ⁺ , p<0.01)	The positive relationship supports the agency theory and the stakeholder theory
Gender diversity	H ₈	Gender diversity and level of tax planning	Rejected	Rejected	M1a	Gender diversity has a positive influence on the CETR	(V ⁺ , p<0.1)	The positive relationship supports the agency theory and the stakeholder theory
			Rejected	Rejected	MI Ib	Gender diversity has a positive influence on the AETR	(V ⁺ , p<0.01)	The positive relationship supports the agency theory and the stakeholder theory
Managerial incentives	H ₉	Board compensation and level of tax planning	Rejected	Rejected	M1a	Board compensation has a negative influence on the CETR	(V ⁻ , p<0.05)	The negative relationship rejects the agency theory
			Rejected	Rejected	MI Ib	Board compensation has a negative and insignificant influence on the AETR	(V ⁻ , p>0.1)	No impact association rejects the agency theory
Institutional investors	H ₉	Institutional investors and level of tax planning	Accepted	Accepted	M1a	Institutional investors have a positive and significant association with the CETR	(V ⁺ , p<0.05)	The positive relationship supports agency theory, political cost theory, and stakeholder theory
			Accepted	Accepted	MI Ib	Institutional investors have a positive and significant association with the AETR	(V ⁺ , p<0.1)	The positive relationship supports the agency theory, the political cost theory, and the stakeholder theory
Ownership concentration	H ₁₁	Ownership concentration and level of tax planning	Accepted	Accepted	M1a	Ownership concentration has a negative and significant association with the CETR	(V ⁻ , p<0.05)	The negative relationship rejects the agency theory and supports political power theory
			Accepted	Accepted	MI Ib	Ownership concentration has negative and significant association with the AETR	(V ⁻ , p<0.1)	The negative relationship rejects the agency theory and supports the political power theory

Note

	Significant
	Insignificant

M1 is Model 1

M2 is Model 2

This model uses the cash effective tax rate (CETR) as the proxy for tax planning

This model uses the accounting effective tax rate (AETR) as a proxy for tax planning

In the preceding section, the study analysed and discussed the influence of firm-specific characteristics on tax management. The empirical findings revealed that particular firm-specific characteristics affect the level of corporate tax planning. Along with firm-specific characteristics, the results revealed that aspects of a firm's corporate governance contribute to the variation in the level of corporate tax planning. The management of tax issues is relevant as they have significant effects on companies' shareholders, firm value and cash flows. Thus, the board of directors of the firms is expected to use corporate governance mechanisms to influence the tax behaviour of firms in the best interests of shareholders.

This section describes the investigation of the influence of corporate governance mechanisms on tax planning using the generalised least squared (GLS) estimation technique. Two models were used in the analysis: the first was Model 3, which used the CETR (dependent variable) to measure tax planning. The second was Model 4, which used the AETR (dependent variable) to measure tax planning. Both models had the same independent variables (corporate governance variables).

Hypothesis Six (H₆) predicted a negative and significant relationship between board size and the ETR. In other words, companies with a larger board size have a lower ETR (more tax aggressive) than firms with small board size. Table 6.10 provides the results for Models 3 and 4. Model 3 results showed that the relationship between board size and ETR is negative (-0.0182) and significant at ($p < 0.05$). Similarly, Model 4 showed that firm size is negative (-0.0205) and significant at ($p < 0.05$). Thus, the results showed that board size has a negative and significant relationship with the ETR and indicated that firms with a larger board size are more tax aggressive than firms with smaller board size. The literature does not establish or agree on the optimal size for a board; therefore, the study could not conclude which size is suitable. However, the estimation results clearly provided evidence that firms with relatively larger boards pay lower taxes (more aggressive) compared with firms with smaller board sizes. This result was consistent with the resource dependence theory, which maintains that a large number of board members would mean that a great deal of expertise and experience is available to a firm, which might increase its ability to reduce its tax burden and provide tax avoidance benefits to managers, firms and shareholders. Mainly, when there is an after-tax incentives base, board members may be motivated to engage in tax avoidance to reduce tax costs, which will increase after-tax earnings to boost their incentives. Therefore, it is logical that a larger board of directors could increase the tax avoidance strategy of firms.

Hypothesis Seven (H₇) predicted that board independence has a significant and positive relationship with the effective tax rate. This hypothesis postulated that firms with a board of directors with a higher ratio of non-executives have a high ETR (less tax aggressive) than firms with boards of directors with a small proportion of non-executive directors. The results of both models showed that board independence has a positive and significant influence on the level of the ETR. However, the results showed independent directors could influence more CETR than the accounting effective tax rate. This could be seen in the significance level of the two models estimated, where Model 3 (CETR) board independence was significant at 1% ($p < 0.01$), while the result of Model 4 (AETR) was significant at 5% ($p < 0.05$).

These results supported H₇ that firms with a higher ratio of non-executive directors (board dependence) on the board of directors have a high effective tax rate (less tax aggressive) than firms with a lower proportion of non-executive directors (less board independence). The possible explanation for this result is that non-executive members of a board of directors can provide independent and pragmatic advice, direction and policies to management, which might reduce a firm's tax burden. In addition, these board members might prevent management from engaging in activities that may not lead to a long-term maximisation of shareholders health. The study results implied that firms with a higher proportion of outside directors on the board have a high ETR, and therefore they are less tax aggressive.

These results were expected because the presence of outside directors who are independent of the management of a firm improves the monitoring of management actions. If the tax planning is not in the interests of shareholders, independent directors protect the interests of shareholders by limiting the level of tax planning and possible rent extraction. The finding of the study agreed with several studies (Lanis & Richardson, 2011; Minnick & Noga, 2010), which also suggested that independent directors are essential monitors of management. A board of directors with a higher percentage of outside members can effectively monitor a manager's tax management decisions to reduce agency problems. Furthermore, the finding suggested that independent directors have skills, expertise and experience, which can be used to protect the interests of shareholders more actively against managerial opportunism. Consequently, these results are similar to the finding of Armstrong et al. (2015), who found that a board with a higher percentage of outside directors reduces disagreement between shareholders and managers about the level of tax planning in which firms should engage.

In other words, it alleviates under- and/or over-investment in corporate tax planning, which is a major symptom of unresolved agency problems in tax planning.

Hypothesis Eight (H₈) expected a negative and significant relationship between managerial incentives and the ETRs. This hypothesis predicted that firms that provide more managerial incentives have a low ETR (more tax aggressive) than those with fewer managerial incentives. As anticipated, the results shown in Table 6.10 revealed that managerial incentives have a negative and statistically significant relationship with CETR ($p < 0.05$) but one that is statistically insignificant with AETR ($p > 0.1$). These results suggested that managerial incentives influence cash tax paid more than they influence reported tax expenses. These results were consistent with H₈, which predicted a negative relationship between managerial incentives and ETR and indicated that firms that pay more to their directors have a lower ETR. This was not surprising, given that compensation is paid after-tax; therefore, CEOs are motivated to reduce tax costs to increase their compensation. The logic is straightforward: if managers are compensated on an after-tax basis, they have a much stronger incentive to reduce tax expenses. Therefore, managerial incentives are provided to managers to encourage them to invest more in aggressive tax avoidance activities. These results were consistent with several previous findings (Minnick & Noga, 2010; Armstrong et al., 2012, 2015; Rego & Wilson, 2012).

In addition, the literature suggests that compensation paid to executives is aimed at aligning the interests of the executives with that of shareholders in tax management. Thus, it is accepted that compensation motivates executives to exert more effort in reducing tax costs, which will benefit themselves (managers), firms and shareholders. This finding confirmed Desai and Dharmapala's (2006) study, which concluded that incentive compensation helps to align the interests of managers and shareholders, thereby reducing opportunistic behaviours. Therefore, Desai and Dharmapala's (2006) study concluded that remuneration is the best corporate governance tool to encourage tax management in companies. The results of the current study also confirmed the views of Rego and Wilson (2012), who argue that incentives are paid to encourage managers to make greater efforts to engage in tax-planning activities that can increase firm value by reducing tax liability and increasing cash flow.

Hypothesis Nine (H₉) expected that the gender diversity of the board would have a positive relationship with the ETR. This suggests that firms with many female representatives on their board

of directors would have a higher ETR (less tax aggressive) compared to firms with few female board representatives. The results indicated that tax planning is significantly different for firms with different gender diversity on their boards of directors. The results in Table 6.10 showed that gender diversity had a positive coefficient (0.2139), and it was significant at 0.05 with CETR. In contrast, Model 4 showed a positive (0.0230) and significant ($p < 0.01$) influence of gender diversity on AETR. These results suggested that firms with a large number of female directors on their board of directors have a high ETR (less tax aggressive) than firms with a less diversified board of directors. These results provided evidence that firms that have diversified their board of directors in terms of gender are less involved in tax planning activities.

These results supported the stakeholder theory, which postulates that the presence of female directors increases the monitoring role of corporate governance. According to this theory, an increasing number of female directors increases a board's effectiveness and helps firms to make more informed and accountable decisions, taking into account their responsibility to the society in which they operate. Essentially, it can be expected that female directors help firms to remember their social responsibility to pay their fair share of taxes for social wellbeing. The results supported the agency theory, which maintains that a firm's management always seeks to maximise its interests at the expense of shareholders.

According to the theory, to achieve this, managers create an information gap between themselves and shareholders when making decisions, including those about tax management strategies. Managers accomplish this by showing their tax avoidance behaviour and portraying their concerns about shareholders' interests. Accordingly, the current study concluded that the presence of a female on a firm's boards could contain the selfish and opportunistic behaviour of managers and uncover their false claim to be avoiding paying taxes to maximise shareholders' interests, for example. This leads to better monitoring and hence reduces the gap between shareholders and firms. The study results conformed to those conducted earlier (Boussaidi & Hamed, 2015; Francis et al., 2014; Hoseini et al., 2019; Lanis et al., 2017; Richardson et al., 2013).

Hypothesis Ten (H_{10}) predicted that ownership concentration has a negative and significant link with tax planning. This means that firms with more ownership concentration have a lower ETR (more tax aggressive) than those with less ownership concentration. The results indicated that ownership concentration was negative (-0.0694) and significant at 5% ($p < 0.05$). It had a negative

relationship with the level of CETR in Model 3. In addition, the results of Model 4 showed that ownership concentration was negative (-0.2316) and significantly influenced the ETR at 1% ($p < 0.01$). This result indicated that firms with more concentrated ownership engage in more tax planning activities and those with less concentrated ownership are less tax aggressive.

This result was acceptable because the ownership concentration of firms indicates domination by large shareholders who would have sufficient incentives to exercise control and power over the managerial process, including tax management activities. As a result, ownership concentration aligns management and shareholders' interests, which makes management act in the interests of shareholders. Additionally, in a well-governed firm, shareholders can encourage tax-planning activities, as they can be sure that management has a limited chance to extract rent. The current study's finding was similar to the findings of other studies (Gaaya et al., 2017; Liu & Lu, 2007; Slemrod, 2004; Chen & Chu, 2005; Crocker & Slemrod 2005; Hanlon & Heitzman, 2010). Moreover, these results were supported by the political power theory, which suggests that large shareholders in listed firms have ties with the government through political connections, which can be utilised to help them to obtain government-related resources and support such as tax benefits (Zeng, 2019; Wu et al., 2012).

Hypothesis Eleven (H_{11}) anticipated a positive and significant relationship between institutional investors and ETRs, suggesting that firms with more institutional investors have a higher ETR (less tax aggressive) than firms with fewer institutional investors. The results showed that institutional investors have a positive (0.0031) and significant ($p < 0.05$) influence on the CETR. Moreover, the results of Model 4 indicated that institutional investors have a positive (0.0525) and significant ($p < 0.1$) relationship with AETR. These results implied that firms with a higher percentage of shares owned by institutional investors are less involved in tax planning. These results were consistent with the studies of Moore (2012) and Khurana as well as Moser (2013) and might have been associated with a decrease in information asymmetry between managers and shareholders due to the presence of institutional investors.

Similarly, these results were consistent with the view that in developing nations, institutional investors owning shares in listed firms are government organisations such as pension funds. This allows the government to have indirect control and influence on the listed firms. Government control can reduce the incentives of companies to manage taxes aggressively because they are

under pressure to pursue political objectives of protecting government revenue. In contrast, firms with fewer institutional investors are assumed to have less government control. Therefore, managers of a firm that is not government-controlled may exploit complex tax-planning strategies to reduce tax expenses for their own and shareholders' benefits (Chan et al., 2013).

The adequacy of the independent variables in both models explaining the dependent variables was tested. The results showed that the models were robust, which was evident in the values of the evaluation coefficients, R^2 and adjusted- R^2 . Specifically, the results of Model 3 showed that R^2 and adjusted R^2 were 0.5795 and 0.4603, respectively, while their F-statistic counterpart was recorded as 4.859102, which was highly significant ($p=0.000$). This result suggested that this model had an acceptable predictive power. Model 4 offered good predictive power, which showed that R^2 and adjusted- R^2 were 0.54830 and 0.431659, respectively, while the F-statistic was 4.700581, which was highly significant ($p = 0.000$).

6.5.4 Influence of Country-Specific Characteristics on firms' Tax Planning

This section presents the results and discussions of the influence of country-specific variables on the level of tax planning. The regression results of Models 5 and 6 presented in Table 6.14 showed the impact of country-specific variables on tax planning using the CETR (Model 5) and AETR (Model 6). Table 6.14 presents the descriptive statistics of the variables used for the estimation.

Table 6.14: Descriptive statistics

	Obs.	Mean	Median	Max.	Min.	SD	Skewness	Kurtosis	Jarque-Bera	
AETR	1021	0.263	0.289	0.30	0.000	0.139	0.928	1.351	121.56	
CETR	1021	0.195	0.191	0.30	0.000	0.107	0.895	1.356	176.36	
QM	952	4.73	4.82	5.00	3.00	0.337	1.326	2.963	138.81	
Culture	987	51.98	52.78	61.27	48.21	4.682	0.692	2.281	61.27	
RQ	981	3.29	3.03	4.00	3.00	0.729	1.027	1.835	78.63	
FRQ	946	1.023	1.18	1.83	0.76	0.862	1.003	2.836	151.16	
Ethics	975	3.16	3.29	6.00	3.00	2.728	0.897	1.926	83.57	
AQ	913	3.84	3.63	5.00	3.00	1.626	1.281	2.207	134.01	
CETR	Cash effective tax rate			Culture	Culture			Ethics	Ethics	
AETR	Accounting effective tax rate			RQ	Regulatory quality			AQ	Audit quality	
QM	Management quality			FRQ	Financial reporting quality					

Source: Author's Computation

Table 6.14 above presents the descriptive statistics of the variables used to estimate the relationship between tax planning and country-specific variables. The results demonstrated that the mean value of the AETR was 0.263 (26.3%) while that of the CETR was 0.195 (19.5%). These results suggested that, on average, the tax liabilities of the firms in the EACs represented 26.3%. However, the firms paid 19.5% as tax, suggesting tax-planning activities because the statutory tax rate for all three EACs (Kenya, Tanzania, and Uganda) had been 30% over the previous 11 years. Therefore, the mean value of less than 30% indicated the presence of tax planning in EACs. The standard deviation (SD) of the AETR and the CETR were 0.139 and 0.107, respectively. This suggested a small degree of dispersion of AETR and CETR among the firms in the EACs.

The results indicated that the mean value of the management quality (QM) variable was 4.73 and ranged from 3.00 to 5.00. This result demonstrated that most of the firms in East Africa employed good-quality management. The mean value of the culture variable was 51.98. This demonstrated that the level of collectiveness among the EACs was high. Furthermore, the standard deviation of 4.682 showed a low level of disparity in cultural dimensions amongst the EACs. Concerning the regulatory quality (RQ) variable, the mean score was 3.29, with a minimum score of 3.00 and a maximum score of 4.00, which were far from the full score of 7.00. This result suggested that there was a low-level regulatory system that protected the various shareholders in EACs. In addition, the SD of the RQ was 0.729, which showed that there was a small variance amongst the regulatory systems of the EACs.

Furthermore, the average score of the financial reporting quality (FRQ) of firms in EACs was 1.023, with minimum and maximum values of 0.76 and 1.83, respectively. The ethics variable ranged from 3.00 to 6.00, with a mean value of 3.16. As the maximum possible score was 7.00, this result demonstrated a low ethical standard amongst firms in East Africa. Furthermore, the results showed that the mean score of the audit quality (AQ) variable was 3.63. This result implied that the firms in East Africa had a relatively high level of audit quality. The results also indicated that the data used for the analysis was normally distributed because all the variables met the standard skewness assumption with a value less than 1.96. In addition, the kurtosis of all the variables was less than 3. This result suggested that FE and RE could offer robust results.

6.5.4.1 Multicollinearity Tests

Table 6.14 presents the results of the Pearson correlations matrix and the VIF. The VIF and the correlation matrix results revealed all the variables were not highly correlated. The results demonstrated that the VIF of all the variables was less than five (5), which was far from the threshold of 10 suggested by literature (Menard, 2002). These outcomes suggested that all no variables used in this analysis suffered from multicollinearity. Similarly, the correlation matrix results suggested no strong correlation among the variables used in the analysis. All the correlation coefficients were less than 0.5, suggesting that the variables were not highly correlated. These results showed that the use of these variables in the regression would not produce any spurious results.

Table 6.14: Correlation Matrix

	CETR	AETR	QM	Culture	RQ	FRQ	Ethics	AQ	VIF
CETR	1.000								4.07
AETR	.893***	1.000							2.83
QM	.015	-.094	1.000						2.19
Culture	.083*	.158*	-.128**	1.000					1.55
RQ	-.385**	-.097	.085	.037	1.000				4.20
FRQ	-.133***	-.013***	.172	.035**	-.105	1.000			3.97
Ethics	.182	.391	-.393**	-.486	.097*	.042*	1.000		1.29
AQ	-.029*	.243	.375	.104	.179	.142	.083	1.000	3.82
CETR	Cash effective tax rate		QM	Management quality		Culture	Culture		
AETR	Accounting effective tax rate		RQ	Regulatory quality		Ethics	Ethics		
VIF	Variance inflation factor		FRQ	Financial reporting quality		AQ	Audit quality		

Source: Author's Computation

6.5.4.2 Regression Results

This section presents the results of the relationships between country institutional characteristics and tax-planning activities of listed firms in East Africa. The results are presented according to two main models. Model 1 measured tax planning based on the CETR, whilst Model 2 used the accounting effective tax rate to measure tax planning (AETR). The results are presented in Table 6.15.

Table 6.15: Regression Results of Tax Planning and Corporate Governance Variables

Variable	Model 1 (CETR)	Model 2 (AETR)
Management Quality	-0.1967*** (-2.962)	-0.0162** (-2.027)
Culture	0.0372** (1.993)	0.0815** (2.191)
Regulatory Quality	0.1628** (2.058)	0.0922** (1.973)
Financial Reporting Quality	0.0626* (1.842)	0.0836 (1.283)
Ethics	0.2833** (2.096)	0.0927*** (3.784)
Audit Quality	-0.1537** (-2.018)	-0.2903* (-1.815)
C	-2.2735*** (-4.753)	-1.9364*** (-3.187)
R-squared	0.7293	0.7528
Adjusted R-squared	0.6846	0.6927
F-statistic	5.1926	4.6375
Prob(F-statistic)	0.0000	0.0000
Prob. of Hausman test	0.0032	0.0032
Durbin-Watson stat	2.3774	2.3774

Source: Author's Computation

Note: *** = Significance at 0.01; **= Significance at 0.05 and * = Significance at 0.1, and * = at 0.1

Table 6.16 Summary of Hypotheses and Results on the Association between Corporate Governance and Tax Planning

Independent Variable	N/S	Tested relationships	Results		Conclusion	Level of significance	Relevant theory
			M1	M2			
Management Quality	H ₆	Management quality and level of tax planning	Accepted	Accepted	Management quality has a negative and significant association with the cash effective tax rate (CETR)	(V ⁻ , p<0.01)	The negative relationship supports the agency theory, the institutional theory and the resource dependence theory
			Accepted	Accepted	Management quality has a negative and significant association with the accounting effective tax rate (AETR)	(V ⁻ , p<0.05)	The negative relationship supports the agency theory, the institutional theory and the resource dependence theory
Culture	H ₇	Culture and level of tax planning	Accepted	Accepted	Culture has a positive and significant influence on the CETR	(V ⁺ , p<0.05)	The positive relationship supports the institutional theory
			Accepted	Accepted	Culture has a positive and significant influence on the AETR	(V ⁺ , p<0.05)	The positive relationship supports the institutional theory
Regulatory Quality	H ₈	Regulatory quality and level of tax planning	Rejected	Rejected	Regulatory quality has a positive and significant influence on the CETR	(V ⁺ , p<0.05)	The positive relationship supports the institutional theory
			Rejected	Rejected	Regulatory quality has a positive and significant influence on the AETR	(V ⁺ , p<0.05)	The positive relationship supports the institutional theory
Financial Reporting Quality	H ₉	Financial reporting quality and level of tax planning	Rejected	Rejected	Financial reporting quality has a positive influence on the CETR	(V ⁺ , p<0.1)	The negative relationship rejects the institutional theory
			Rejected	Rejected	Financial reporting quality has a positive and insignificant influence on the AETR	(V ⁺ , p>0.1)	No significant association rejects the institutional theory
Ethics	H ₉	Ethics and the level of tax planning	Accepted	Accepted	Ethics has a positive and significant association with the CETR	(V ⁺ , p<0.05)	The positive relationship supports the political cost theory and the institutional theory
			Accepted	Accepted	Ethics has positive and significant with the AETR	(V ⁺ , p<0.01)	The positive relationship supports the political cost theory and the institutional theory
Audit Quality	H ₁₁	Audit quality and level of tax planning	Accepted	Accepted	Audit quality has a negative and significant association with the CETR	(V ⁻ , p<0.05)	The negative relationship supports the agency theory and the institutional theory
			Accepted	Accepted	Audit quality has negative and significant association with the AETR	(V ⁻ , p<0.1)	The negative relationship rejects the agency theory and the institutional theory

Note

	Significant
	Insignificant

M1 is Model 1 This model uses CETR as a proxy for tax planning
M2 is Model 2 This model uses AETR as a proxy for tax planning

Table 6.15 above presents the results of the impact of country-specific characteristics on the tax planning activities of firms listed in EACs. Interestingly, the results revealed a wide range of significant relationships between tax planning and country-specific characteristics. The estimates demonstrated that management quality has a negative and significant ($p < 0.05$) relationship with the CETR. This indicates a low CETR, which is an indication of tax planning activities in firms. This inverse relationship suggests that an increase in management quality would result in a decrease in CETR. This result implied that tax planning increases in countries that depend on good-quality management for senior management positions than those that do not. This relationship is possible because top-quality managers can align a firm's decisions with tax strategies. This would make them able to identify and utilise tax-planning opportunities because of their superior understanding of the operating environment of their firms. For instance, timing, classification as well as research and development (R&D) activities have significant ramifications for tax reduction. In particular, good-quality managers would be able to use R&D activities to reduce the tax burdens of their firms.

Another reason for this result is that good-quality managers can set objectives that emphasise cost minimisation, which is consistent with the views of Dyreng et al. (2010). It is agreed that all managers aim to reduce cost; however, managers with a high level of experience, expertise and skills are more likely to attain substantial cost savings. These cost savings can positively affect their tax savings. Therefore, it is not surprising that a manager's shrewdness in managing resources well would result in cost reduction through tax avoidance strategies.

Moreover, tax planning is a product of a meticulous and well-designed strategy put in place by management. Thus, professional and experienced managers would be able to develop sound strategies as well as guiding business operations and tax planning activities. Consequently, this would result in firms paying less tax. Another reason for this result is that good-quality management may have the skills, expertise and experience of supervising and overseeing different business units over time; hence, they can draw on their expertise to reduce their tax liabilities. This result confirms the findings of earlier studies, such as those of Dyreng et al. (2010) as well as Koester et al. (2017), who reported a negative relationship between managerial quality and tax planning of firms.

The study predicted that a country's culture would have a positive relationship with the CETR. In other words, if the CETR of the firms is high, the indication is that tax-planning activities are not taking place in firms. Confirming our expectations, the results showed that the estimate for culture was positive and significant at 5%. This result indicated that firms in countries with rigid and strict norms and regulations are less likely to engage in tax planning activities. This result is reasonable because individuals living in a country with a strong uncertainty avoidance culture uphold unyielding codes of beliefs and attitudes as well as being intolerant about heretical behaviour and views. This attitude limits the ability of the firms and their staff to embrace the concept of tax planning because they would consider such practices as unethical and unacceptable, which may land them in trouble.

This view would force firms to organise their operations according to the prescripts of the law and regulations, hence less tax planning activities. This position is consistent with Gallego-Alvarez and Ortas (2017), who contend that firms and individuals in societies with a high level of uncertainty avoidance mainly accept and follow rigid codes and are inclined to embrace many rules and norms, which makes them less disposed to innovation and change. This view highlights that firms operating in high uncertainty avoidance countries will be less prone to tax planning.

The finding is consistent with the stakeholder theory, which holds that responsible firms establish culture, standards and norms to guarantee certainty and stability in their operations. By this logic, Kim and Kim (2009) explain that public relations practitioners might interpret the responsible actions of firms as a means to ensure the success of both firms and society. Evidence provided by the current study supported the findings of earlier studies, such as those of Richardson (2008), who provided evidence to demonstrate that higher uncertainty avoidance results in higher tax planning activities by firms. Brink and Porcano's (2017) study also lends support to this finding when they showed that the culture of countries influences the tax planning of their firms. Although the current study was conducted in developing countries, it is consistent with the findings of studies conducted in developed countries. For instance, Ermasova et al. (2021) found that culture is a significant predictor of tax planning activities of firms in the USA and Germany.

The study investigated whether the quality of regulations in a country influences the tax planning activities of its firms. Apriori, the study expected a positive relationship between these variables.

Affirming the study's apriori prediction, the results showed that regulatory quality positively correlates with the CETR. This meant that the CETR was high, which indicated that tax planning was not taking place. The results further demonstrated that the positive relationship between regulatory quality and tax planning was significant at 5%. The results implied that firms operating in countries with strong regulatory regimes would engage in less tax planning. This result was plausible because governments typically use regulations to expose firms to additional transparency. In addition, there may be harsher punishments for management who engage in activities that are contrary to the standards, policies and laws of a country.

This result emphasises that in the absence of a detection mechanism, firms will take advantage of loopholes in regulations, laws and standards and will engage in aggressive tax planning. In this context, they will be afraid to engage in aggressive tax avoidance practices. Exposure to additional transparency restricts firms from engaging in overt tax planning activities. This view is supported by Overesch and Wolff (2018), who explained that firms that operate in countries with a high level of transparency increase their tax levels.

In other words, enforced transparency decreases the tax planning activities of firms, and the regulatory framework is powerful enough to prevent firms from engaging in tax planning activities. This finding was not surprising because it affirmed the findings of previous studies. Such studies, including that of Bushman and Piotroski (2006), showed that firms in countries with strong regulatory systems discover tax non-compliance faster than firms in countries with weak regulatory systems.

The study hypothesised a negative relationship between financial reporting quality and CETR, which would mean that a low CETR would indicate tax planning. However, the financial reporting quality variable's coefficient was positive and statistically insignificant ($p > 0.05$). This result implied that financial reporting quality had a lesser influence in explaining their tax planning practices. This result shed light on the relationship between the financial reporting quality of a country and the tax planning activities of its firms. Moreover, this result was conceivable in many ways. For example, investors are not directly involved in the regular management of firms. Therefore, financial reporting is the medium through which firms demonstrate accountability to their shareholders. Because of this separation of power, countries establish sound systems to ensure

robust and accurate financial reporting. In this context, it is logical that firms operating in countries with good-quality financial reporting and investor protection would force management to embrace proper accounting and tax practices. In addition, countries with a more robust accounting system may have systems that prevent management from engaging in practices that are not in accordance with the prescribed policies and standards.

Moreover, good-quality financial reporting provides additional, reliable and relevant information to tax authorities, who would use it to identify inconsistencies in income, expenses and profit. Another key reason for this result is that detailed and accurate disclosures can prevent managers from engaging in tax planning, especially if they anticipate scrutiny from the public because it would come with a significant risk to the firms, especially reputation risk. In this context, engaging in aggressive tax avoidance strategies can lead to the danger of being detected, and the firm together with its management may suffer from reputational damage.

The findings of the study agreed with those of previous authors, such as Wang (2011), Kerr (2019) and Stiglingh, Smit and Smit (2020), whose evidence showed that corporate transparency emanating from quality financial reporting results in less tax planning activities by firms. However, this finding contradicts the findings of Freedman (2018) as well as Balakrishnan et al. (2019), who showed that quality financial reporting increased the tax planning activities of firms because managers claimed to be transparent to mitigate tax-planning problems but, in fact, were engaged in covert practices.

Turning to the effects of ethics on the tax planning activities of the firms, the results of the study showed that the coefficient for the ethics variable was positive and statistically significant at 5%. This result indicated that the ethical behaviour exhibited by firms in EACs significantly influenced their tax planning activities. This result was consistent with the prediction of the study that strong corporate ethics in a firm would result in a reduction in its tax planning activities. Since tax laws are imperfect, firms would always find a loophole in them to avoid paying taxes. In this context, ethics would help firms to self-regulate their tax planning behaviour. Firms that hold high ethical values would want to avoid negative public information and would avoid tax planning activities, especially in contentious transactions.

Zeng (2019) agrees that responsible citizens would not avoid the payment of tax, which is also

considered contradictory to ethical corporate citizenship. Moreover, Lanis and Richardson (2011) hold the view that highly ethical firms are less likely to be involved in tax planning activities because tax avoidance is risky and leads to high costs for firms, including reputational damage and government/public scrutiny. Ethics can prevent firms from engaging in tax planning activities, especially when negative information can damage a firm's image. Indeed, firms can handle reputational threats by reducing or avoiding tax planning activities. Henderson and Kaplan (2005) provided evidence that ethics influence the tax compliance behaviour of firms. This suggests that unethical firms usually have large tax benefits, indicating that high ethical values reduce tax planning.

The study further hypothesised a negative relationship between audit quality and the CETR of firms in EACs. The study results confirmed this prediction by demonstrating a negative and significant ($p < 0.05$) relationship between auditor quality and CETR, which indicated that an improvement in firms' audit quality in the EACs increased their tax planning. This result was reasonable because auditors can provide extra tax-related services, such as tax planning advice to firms to reduce their tax liabilities. Good-quality auditors would be able to develop comprehensive and effective tax strategies for their clients because they have accumulated substantial knowledge about the operations, systems and internal processes of their clients, as well as gaining access to comprehensive financial information. Moreover, firms can engage the services of audit firms that have extensive knowledge about the tax structure of their clients, which would lead to substantial tax savings.

Another reason that good-quality auditing increases firms' tax planning activities is that audit firms can draw on extensive tax-specific knowledge because they offer tax services to a wide array of clients, thus enabling them to provide tax services to their clients when they are asked to do so. The number of clients of good-quality auditors may force them to invest in human resources and technologies to help them render quality services to their clients, leading to a tax reduction. Another critical point is that individual firms may lack the expertise and technologies to reduce their tax burdens. This view is supported by Dai et al. (2007), who provided evidence that it would take many years for firms to develop tax and business expertise similar to those possessed by auditors who have performed their services for decades. In addition, this result was not surprising because recent studies, such as those of Chyz et al. (2017), Klassen et al. (2015), Dai et al. (2007)

as well as Yuniarwati et al. (2017) show that firms that engage the services of good-quality auditors benefit from their efficiency, which reduces their tax burden.

The abovementioned results were consistent with the views of the institutional theory, which espouses that the role of institutions, law and regulations on the behaviour of firms through coercive and normative isomorphism may influence their tax planning activities. In other words, in a jurisdiction with quality laws, institutions, and enforcement systems or strict investor protection regimes, firms are more exposed to high risk of litigation and cost. Consequently, to mitigate such risk, the firm will not employ tax-planning strategies to reduce their tax burden. Therefore, country-specific characteristics of an institutional nature such as management/financial reporting/ regulatory quality, ethics and culture significantly influence the tax planning activities of its firms.

6.6 Conclusion and Recommendations

Tax management is an essential agenda item for managers when making strategic corporate decisions because it contributes significantly to cash savings, which benefit both firms and shareholders. For a government, tax collection is the main source of revenue to finance its operations. Tax planning activities reduce a substantial amount of taxes that governments could collect for the economic and social development of countries. For this reason, governments, policymakers and other stakeholders are keen to understand the factors affecting the level of tax planning.

The identification of these factors could assist government revenue authorities in finding solutions to the tax-planning problem. For shareholders, tax planning can facilitate the elimination of rent-seeking behaviour that maximises the wealth of managers at the expense of shareholders, which is possible owing to the opaque nature of tax planning. Understanding the factors that influence the tax planning activities of firms has gained considerable attention among management, shareholders, policymakers and researchers. This justifies the importance of the study's examination of the determinants of tax planning in selected emerging economies.

Following the approach used by Richardson and Lanis (2007) as well as Kraft (2014), the study investigated the influence of firm-specific characteristics on tax planning measured by the ETRs.

The study results showed that smaller firms are more tax aggressive compared with larger firms, which is consistent with the political cost theory. This finding may alert policymakers and regulatory authorities (for example, revenue authorities) that small firms are most likely to avoid paying taxes compared with larger firms. This might be associated with fewer regulations and enforcements imposed on this category of business.

Furthermore, the results revealed that profitable firms are less tax aggressive. This result confirmed the view that profitable firms have enough earnings to pay their taxes and thus are less tax aggressive. Given this, the researcher recommends that emerging economies should revisit their policies to make their economies more conducive in order to attract profitable investments. Moreover, the evidence showed that older firms are less involved in tax avoidance. This is possible because old firms are affected by political pressure to pay fair taxes to avoid reputation loss. However, results of the examination of leverage and capital intensity found no influence on the level of tax planning.

Regarding the corporate governance variables, the study results provided evidence that board size positively affects corporate tax avoidance. However, there is no consensus in the empirical studies on the optimal level of board size, but Goodstein et al. (1994) suggest that a small board is more effective. This researcher recommends that listed firms in EACs should balance their board size to avoid too many directors on the board, as a large board size can reduce the speed and response of a company in times of crisis because of the multitude of decision-making perspectives. The study also documented a significant and positive relationship between board independence and the CETR, which is inconsistent with the agency and stakeholder theories. Therefore, the researcher recommends that regulatory authorities should enforce a minimum number of independent directors on boards, as their presence on the board makes the firm less tax aggressive. This is necessary as the presence of independent directors ensure the independence of the board.

The results revealed that managerial incentives appear to be a significant determinant of tax avoidance activity. Overall, the researcher suggests that equity risk incentives induce managers to undertake risky tax strategies in an effort to increase their compensation and thus the value of their options portfolios. The study found that ownership concentration negatively influences the CETR. The findings suggested that large shareholders in firms with highly concentrated ownership might

have sufficient incentive to exercise control and power over the managerial process, including their tax-saving activities about which they are concerned.

Based on the findings of the study, gender diversity has a significant positive association with the CETR of listed firms in EACs. This result has important policy implications concerning board gender diversity and tax aggressiveness, an issue that has attracted a great deal of public, political, and government attention. The results might help to support recent initiatives by the security markets in EACs, which relate good corporate governance practices to a reduction in tax aggressiveness and various non-profit making organisations to promote and encourage firms to increase female representation on the board of directors.

Furthermore, the study findings showed that the presence of institutional investors reduces a firm's level of tax planning. This situation might be due to the monitoring role of such investors or that they are subservient to rules and regulations. Consequently, this finding suggested that the presence of institutional investors protects the interests of outside investors. This indicates that further steps need to be taken to encourage institutional investment in listed firms in EACs.

The findings further demonstrated that specific institutional arrangements in a country influence the level of tax planning of its firms. The evidence showed that management quality, regulatory quality, auditing quality, finance reporting quality, culture and ethics influence the level of tax-planning activities of firms.

Thus, the study contributed to existing literature that explores the determinants of tax planning in emerging markets. The findings provided a better understanding of tax planning in listed firms in EACs by investigating the effect of firm-specific characteristics, corporate governance mechanisms and country-specific determinants on the ETRs of these firms, which indicated the level of tax planning in firms in EACs.

CHAPTER SEVEN

IMPACT OF TAX PLANNING ON FIRM VALUE

7.1 Introduction

The previous chapter described the study's examination of the various factors that may have an impact on the level of corporate tax planning in EACs and explained the evidence of why some firms are more successful in reducing their tax burden through tax planning compared to other companies. The chapter reported the study's conclusion that those factors impact the ETR of firms in EACs, which indicated their level of tax planning. However, the relevance of tax planning to firms and shareholders is still unclear in the literature. Therefore, this chapter describes the empirical study's contribution to the literature by investigating the impact of tax planning on firm value in EACs.

Over the years, businesses have been complaining of the adverse effect of corporate income tax, as it represents a significant cost to them and shareholders. This is so because governments around the world charge business corporate income tax at a rate that ranges from 20% to 35%, the global average of which is 28.5% (Steinmüller et al., 2019). The average corporate income tax rate in EACs is 30%. Steinmüller et al. (2019) argue that governments take almost more than one-third share of the firms' pre-tax profits. Given this significant tax cost to firms and their shareholders, firms implement tax planning to reduce their tax costs. As a result, most of the developing nations, including EACs, have significantly engaged in tax avoidance activities over the past few years. For instance, Cobham and Janský (2018) report that in 2013, owing to tax avoidance, EACs lost \$2.69 billion, with Kenya losing US \$1.22 billion, Tanzania losing \$0.86 billion and Uganda losing \$0.61 billion, which is approximately 3% of the GDP for each country.

The literature suggests that tax avoidance in EACs is on the increase. For instance, from 2016 to 2018, the Kenya Court of Appeal reported 122 tax avoidance cases: 26 in 2018, 43 in 2017 and 53 in 2016 (Kenya National Council for Law Reporting, 2019). The situation is similar in Uganda and Tanzania. The Tanzania Revenue Authority (TRA), for example, reported 21 decided cases from the Tanzania Court of appeal that related to corporate tax avoidance during the previous twelve years (Tanzania Revenue Authority Report, 2019). This showed that firms in EACs had

been actively engaging in tax planning activities. Meanwhile, firms involved in these legal cases may have suffered from reputation loss and customer apathy.

An important question is whether it is worthwhile for companies to use their resources to invest in tax planning. At first sight, it is tempting to contend that it may affect firm value positively because corporate tax planning reduces the tax burden and leads to an increase after-tax return. This view is plausible because corporate tax planning has long been perceived as a value-enhancing activity by shareholders. For instance, Hoseini et al. (2019) posit that because corporate tax planning reduces tax payable, it is perceived as a value-enhancing activity by shareholders.

Similarly, Desai and Dharmapala (2009a) argue that shareholders perceive tax planning as a vehicle for transferring resources from the state to shareholders. In a related study, Wilde and Wilson (2018) maintain that through tax planning, firms reduce the amount of taxes payable to the government, which increases net cash flows for further investments, meeting their debt obligations, or increasing the amount distributable to investors. It is generally expected that shareholders would prefer reduced tax liabilities, and thus firms exhibit tax aggressiveness because evidence shows that tax planning enhances the firm value (Nugroho & Agustia, 2018; Tang, 2019; Heitzman & Ogneva, 2019, Kirkpatrick & Radicic, 2020; Khuong et al., 2020; Rezki et al., 2020; Handayani, 2020).

However, aggressive tax planning engenders significant risks for firms, especially in the absence of effective corporate governance mechanisms that can mitigate managerial rent extraction masked by tax avoidance activities (Armstrong et al., 2015; Desai et al., 2006). Hutchens et al. (2019) posit that although tax-planning strategies reduce the tax burden and lead to greater after-tax cash flows, they are associated with ambivalent future outcomes, which can lead to significant costs to the firms. Thus, tax planning can cause additional costs if a firm is audited by revenue authorities, as the firm will have to pay more taxes, interest and penalties in compliance with the audit. Similarly, Armstrong et al. (2015) argue that if tax aggressive is detected, subsequent payment of taxes and penalties must be considered. In this case, Chen et al. (2019) posit that firms that engage in intensive tax planning are more likely to participate in the types of transactions and activities, which could be affected by changes in future tax policy. As a result, they would be exposed to the uncertainty of tax policies, leading to higher systematic risks. This indicates that tax avoidance can

involve unusual transactions that are costly to implement, given the complexities in the application of tax law and understanding company costs, such as those associated with internal staff tax; external service provider tax; and coordination with other functional units within the firm. Empirical studies, such as those of Chalmers and Godfrey (2004), Wahab and Shaipah (2010), Wahab and Holland (2012), Bauer et al. (2020), Garg et al. (2020) and Kim et al. (2020) argue that tax planning is costly and risky, which may negatively affect firm value.

The above discussion of the results of prior studies shows clearly that the relevance of tax planning to a firm value of the firms is still a controversial issue in the literature. Thus, the relationship between tax planning and firm value is empirically and theoretically ambiguous. From the findings of these previous studies, it appears that there are two separate views of the relationship between tax planning and firm value. In addition, these studies indicate that the nature of the relationship between tax planning and firm value might vary from country to country, depending on the nature of tax regulations and enforcements. Again, the strength of a country's legal institutions (for example, the capital market and revenue authorities) that regulate corporate governance may influence the relationship between tax planning and firm value. Unfortunately, the relationship in emerging economies is yet to be explored, and the conundrum and controversy of the direction of the association is yet to be empirically examined.

Therefore, the study described in this chapter investigated the impact of tax planning on firm value in EACs. This will contribute to the growing literature on the nexus between tax planning and firm performance in developing nations. The study results will lead to policy recommendations to the regulatory authorities (revenue and capital market authorities in EACs) on how to handle tax planning so that both governments and shareholders benefit from business operations. The rest of this chapter is organised into sections as follows: Section 7.2 is the review of previous related studies; Section 7.3 discusses the methodology adopted in this study; Section 7.4 presents the results and the discussion and Section 7.5 presents the recommendations and conclusion of the study.

7.2 Aims and Objectives of the Study

The aim of this chapter was to investigate the impact of tax planning on firm value in EACs. This was achieved by using the generalized method of moments (GMM). The findings of this investigation are predicted to be useful to shareholders, regulators and policymakers because they contribute to the ongoing debate in the literature of the relevance of tax planning to firm and shareholder value in developing countries. The specific objectives of the study were as follows.

1. To investigate the impact of tax planning on firm value in EACs
2. To examine the relationship between tax planning and the profitability of firms in EACs

7.3 Literature Review

7.3.1 Empirical Literature Review

The relevance of tax planning to firm and shareholder value of the firms and shareholders has been a subject of debate over the years. The argument about whether tax planning actually benefits investors and increases firm value still attracts considerable attention from many scholars (Graham et al., 2013; Kim, McGuire, Savoy & Wilson, 2018; O'Malley, 2018; Pniowsky, 2010; Powers, Robinson & Stomberg, 2016; Robinson et al., 2012; Sani & Madaki, 2016; Wahab & Shaipah, 2010; Wahab & Holland, 2012; Wilde & Wilson, 2018). The literature provides two competing views. The first view is the traditional view, which considers tax planning as a beneficial activity, as it transfers worth from the government to shareholders, while the second view is the agency cost perspective of tax planning, which views tax planning as an activity management use for their benefits at the expense of the owners.

The traditional view believes that tax planning is beneficial to firms and shareholders. Studies under this perspective suggest that tax planning acts as value-enhancing activity, reducing the amount of tax costs payable to the government. A large body of literature acknowledges that the straightforward benefit of tax planning is a reduction in the overall corporate tax burden, which increases after-tax returns (O'Malley, 2018; Salawu, 2017; Sani & Madaki, 2016; Wahab & Shaipah, 2010; Wahab & Holland, 2012; Wilde & Wilson, 2018).

Scholes et al. (2009) provide evidence that companies can keep their taxable liabilities low and increase after-tax return through corporate tax planning. The authors explain that tax planning is

one of the most effective business strategies firms use to attain performance goals. The literature supports the view that firms can reduce their effective taxes to less than 20% using tax planning (Dyreng et al., 2008). Some literature holds that tax planning maximises after-tax returns that can be reinvested and/or distributed to shareholders as dividends (Scholes et al., 2009). This view is reasonable because, traditionally, shareholders perceive tax planning as a value-enhancing activity and approve of management's engagement in tax planning activity, as they expect an increase in after-tax return (Desai & Dharmapala, 2009a).

Consequently, there is a number of previous studies that support the perspective that tax planning is a value-enhancing activity (Salawu, 2017; Tang, 2016; Wang, 2011; Zhang et al., 2017). These studies find a positive relationship between tax planning and firm value, suggesting that an increase in tax planning would increase in firm value. For instance, the results of Graham and Tucker's (2006) study showed that tax planning was a value-enhancing activity and that shareholders viewed it as such. Furthermore, Chen et al. (2010) suggest that shareholders positively value tax planning and they support the management of their firms when it engages in tax planning because it is relevant to firm value.

A study conducted by Desai et al. (2007) in Russia found that when revenue authorities increased tax enforcement for companies in 2000, the market values of these firms interestingly increased. The findings of this study showed that strong government enforcement to combat tax aggressiveness increased shareholders value. This indicated that tax planning had been a distractive vehicle for firm value and served as evidence that the interests of shareholders were more aligned with the government's interests than with those of managers.

This argument is supported by Desai and Dharmapala (2006), who maintain that there is a complementary relationship between managerial diversion and tax sheltering, emphasising the corporate governance role in monitoring and preventing such activities. Rego and Wilson's (2012) evidence showed that where a firm has weak governance, corporate tax planning could be detrimental to firm value due to managerial resource diversions. Their results imply that in firms with poor corporate governance, tax aggressiveness may significantly engender managers' rent extraction and reduce shareholder value.

Wahab and Holland (2012) investigated the influence of tax planning on firm value in the UK. The study found a negative relationship between the intensity of tax planning and firm value, regardless of corporate governance mechanisms, meaning that investors do not appreciate tax avoidance activities. In the same vein, the study of Sani and Madaki (2016) reported a negative relationship between tax planning and firm value. These authors provided evidence to show that corporate governance does not influence managerial decisions that relate to tax planning.

Similar to the studies discussed above, Assidi et al. (2016) conducted a study in Tunisia to examine the influence of tax planning on firm value. The results of this study showed a negative relationship between corporate tax planning and firm value. This indicates that the minimisation of the tax rate has a direct negative impact on a firm's profitability. Meanwhile, a positive relationship was documented by the study of Desai and Hines Jr (2002). This study investigated the association between the tax planning behaviour of a firm and its performance. The results of this study showed that firm performance is positively associated with tax aggressiveness.

In a related study, Chen et al. (2014) adjusted the methodology used by Desai and Dharmapala (2009a) in the USA to investigate this issue in China. They found that tax-planning strategies are inversely related to firm value. The fixed effects regression model was employed in their data analysis. The study used the ETR and tax savings ratio measures as independent variables. Tobin's Q ratio was also used as a dependent variable. Their results established a negative relationship between tax planning and firm value, which suggested that as tax aggressiveness increases, the value of firms decreases. Furthermore, this study concluded that the negative impact of tax planning on the firm value is because "tax avoidance behaviour increases agency costs".

Similarly, Ftouhi, Ayed and Zemzem (2015) find that tax planning has a negative effect on firm value, which conforms to the agency cost theory. Tang (2016) also reports that tax planning enhances firm value, as there is a positive relationship between firm value and tax planning. Zhang et al. (2017) argue that a firm's tax-planning practice has the potential to increase its value. However, they suggest that firms should strengthen their governance and monitoring for the benefits to accrue to shareholders.

Salawu (2017) examined the influence of governance structure on tax planning and firm value in non-financial quoted companies in Nigeria between 2004 and 2014. A sample of 50 companies

out of 151 non-financial quoted companies that covered 10 sectors was purposively selected on a stratified random sampling basis. The data used in the analysis were collected from the audited financial statements of the selected non-financial quoted companies in Nigeria and the Nigeria Stock Exchange Factbook and analysed using the generalised method of moments (GMM). The findings showed a positive and significant relationship between ETRs and firm value (Tobin'Q). Hanlon and Slemrod (2009) investigated how the market reacts to news that firms engage in tax planning (tax sheltering). The finding of this study showed that the market reacted negatively to tax planning news. However, this negative reaction was more pronounced in firms with poor corporate governance.

Other studies express different views on the subject of the relationship between tax planning and firm value. For instance, Lestari and Wardhani (2015), using a dataset from Indonesia from 2010 to 2014, held that tax planning was positively associated with a firm value in Indonesia. Similarly, Wang (2011) found that tax planning is a value-enhancing activity to firms. These studies found a positive relationship between tax planning and firm value.

Zhang et al. (2017) examined the impact of corporate tax avoidance on firms' financial performance. The authors selected China as a case study because it had a unique experience of reform. The results from structural equation modelling (SEM) showed a significant negative direct relationship between tax avoidance and market value. The findings indicated that the opaque nature of China's stock market creates opportunities for managers to use tax avoidance as an instrument for engaging in rent seeking activities, which hurts shareholder value. The results implied that tax avoidance could be a value-adding activity. However, to enjoy its advantages, firms need to strengthen their internal supervision and management capability.

From the foregoing discussion, it can be claimed that tax planning is important to shareholders, as it results in a reduction of the tax cost that significantly burdens them and their firms (Chen et al., 2010). However, shareholders may not always support tax-planning activities because of potential costs and risks. This shows that shareholders have different views of corporate tax planning activities practised by firm management. Shareholders who consider taxes as a significant burden to their firms are in favour of tax planning, as it transfers wealth from the state to shareholders. Indeed, successful tax planning can reduce the tax burden, and firms pay fewer taxes

than they would otherwise pay. In contrast, some shareholders react negatively to news that their companies engage in tax planning because of the costs and risks associated with it (Slemrod, 2005; Chen et al., 2010).

The above discussion shows that the literature has documented mixed results relating to the relationship between tax planning and firm value. Although a few studies found no association (Desai & Dharmapala, 2006; Desai & Dharmapala, 2009a; Kawor & Kportorgbi, 2014) most of the studies provided evidence that relationships exist. Some found a negative relationship (Chen et al., 2014; Kiesewetter & Manthey, 2017; Wang, 2011; Wahab & Shaipah, 2010; Sani & Madaki, 2016; Wahab & Holland, 2012). Other studies, such as those of Desai and Hines Jr (2002), Chen et al. (2010), Desai and Dharmapala (2009b), Tang (2016), Lestari and Wardhani (2015) as well as Zhang et al. (2017), documented a positive association. These conflicting results suggest that the debate on the relationship between tax planning and firm value continues. Moreover, these results have not yet been documented in a broader setting. Thus, from the above mixed results, it is evident that the relationship between firm value and tax planning remains unsolved, as there is no consensus among previous researchers. Therefore, to fill the gap, the current study intended to examine the association between firm value and tax planning in EACs.

7.3.2 Theoretical Background

Researchers use knowledge of the theory about past phenomena to predict the outcome of current related research. Lewis and Grimes (1999) argue that in an empirical study, a theory is an important tool that researchers use to predict the association between variables. Therefore, the current study used the agency theory, (which describes management (agent) as serving the interests of shareholders (principles), to develop the hypothesis to be tested when meeting the study's objectives. According to Zemzem and Ftouhi (2013), historically, tax literature has not differentiated between individual and corporate tax aggressiveness. Thus, previous models of corporate tax planning/aggressiveness have been based on individual taxpayer compliance. However, studies by Chen and Chu (2005), Crocker and Slemrod (2005) as well as Slemrod (2004) make an attempt to distinguish corporate tax aggressiveness from individual tax compliance in the context of the agency theory. However, the agency theory is more applicable to the corporate environment, where there is a principal-agent relationship whereby management (agent) runs a

firm on behalf of shareholders (principle). In this context, it may appear that tax planning is always beneficial to firms and shareholders.

However, the agency theory highlights agency costs (principle-agent problem) in tax planning decisions. This is due to the separation between the ownership and management (control) of firms, which causes information asymmetry between them. However, the situation is more pronounced in tax planning, where the information related to tax management is not made available to shareholders to prevent it from being detected by revenue authorities. Desai and Dharmapala (2009b) maintain that the opaqueness of tax planning leads to managerial opportunism in maximising the manager's wealth at the expense of the firm and shareholders.

Jensen and Meckling (1976) also suggest that the risk of management misusing a firm's resources under the tax-planning umbrella is related to a conflict of interest on the part of managers and shareholders. The authors argue that the two conflicting parties have different wealth maximising objectives. According to this theory, the agency cost may exceed the benefit of tax planning and may lead to a loss in shareholder value. Therefore, the theory suggests the use of corporate governance, which can mitigate the agency problem concerning tax planning decisions (Nugroho & Agustia, 2018). Based on this theory and the empirical literature, the study developed the following hypotheses.

H7₁: Tax planning has a positive impact on firm value in EACs

H7₂: There is a positive relationship between tax planning and the profitability of firms in EACs.

7.4 Methodology

7.4.1 Model Specification

Studies that examine the variables that influence firm value employ the Ohlson (1995) model. Consequently, the current study employed the value relevance model developed by Ohlson (1995) to examine the impact of tax planning on firm value. The original value relevance model pioneered by Ohlson (1995) is provided in equation (7.1).

$$MV_{it} = \beta_0 + \beta_1 BV_{it-1} + \beta_2 EPS_{it} + \epsilon_{it} \quad (7.1)$$

Where MV_{it} is the average market value of shares in the first quarter after the publication of the annual reports; BV_{it-1} is the lagged book value of shares of the firms; EPS_{it} is the earnings per share of the firms at time t ; and ϵ_{it} is the random error term. Previous studies have modified Ohlson's model to estimate the impact of tax planning on the firm value by including the tax planning and firm value variables into the Ohlson equation (Wahab & Shaipah, 2010; Wahab & Holland, 2012; Yee, Sapiei, & Abdullah, 2018). Therefore, the current study adopted the modified version of the Ohlson model by following the studies of Wahab and Shaipah (2010) as well as Wahab and Holland (2012), where firm value was the function of tax planning and other explanatory variables as indicated in Equation (7.2) below.

$$FV = \int (TP, SIZE, ROA, LEV, CNT, AGE) \quad (7.2)$$

The implicit transformation of equation (1) was represented in Equations 3 and 4 such that

$$Q_{it} = (\beta_0 + \beta_1 CETR_{it} + \beta_2 SIZE_{it} + \beta_3 ROA_{it} + \beta_4 LEV_{it} + \beta_5 CTN_{it} + \beta_6 AGE_{it} + \epsilon_{it}) \quad (7.3)$$

$$Q_{it} = (\beta_0 + \beta_1 AETR_{it} + \beta_2 SIZE_{it} + \beta_3 ROA_{it} + \beta_4 LEV_{it} + \beta_5 CTN_{it} + \beta_6 AGE_{it} + \epsilon_{it}) \quad (7.4)$$

In order to build a dynamic model into the equation, the lag of dependent variables was introduced into the right-hand side of the equations as follows.

$$Q_{it} = (\beta_0 + \beta_1 Q_{it-1} + \beta_2 CETR_{it} + \beta_3 SIZE_{it} + \beta_4 ROA_{it} + \beta_5 LEV_{it} + \beta_6 CTN_{it} + \beta_7 AGE_{it} + \epsilon_{it}) \quad (7.5)$$

$$Q_{it} = (\beta_0 + \beta_1 Q_{it-1} + \beta_2 AETR_{it} + \beta_3 SIZE_{it} + \beta_4 ROA_{it} + \beta_5 LEV_{it} + \beta_6 CTN_{it} + \beta_7 AGE_{it} + \epsilon_{it}) \quad (7.6)$$

Where Q_{it} is Tobin's Q , a measure of firm value, $CETR_{it}$ denoted cash effective tax rate, $AETR_{it}$ represented accounting effective tax rate, $SIZE_{it}$ is the size of firms, AGE_{it} was the years of existence, ROA_{it} represented return on assets, LEV_{it} denoted a firm's leverage, CNT_{it} was the capital intensity. Lastly, β_0 was the constant of the equation, β_1 to β_7 were the coefficients of the variables, and ϵ_{it} was the stochastic error term at time 't'.

7.4.2 Estimation techniques

The study employed a panel regression model to estimate the impact of tax planning on firm value. Wilfred and Mbonigaba (2018) posit that panel data models can be categorised into either static or dynamic models. The authors argue that dynamic panel models have been identified as a technique to improve the performance of the estimators in panel data analysis. The literature suggests that a lack of consensus of the results of previous studies that investigated the association between tax planning and firm value may be attributed to the insufficient estimation methods used in previous studies. French and Popovici (2011) propound that to avoid bias or erratic results, the selected estimator must have the statistical econometric power to estimate the model in an equation. Wintoki et al. (2012) suggest that studies related to firm valuation (performance), corporate governance and tax-related issues are greatly affected by the problem of endogeneity. Because of endogeneity problems, the use of the ordinary least squares (OLS) method, which researchers in this field commonly use, could lead to spurious results. This is because the ordinary least squares method does not consider time-invariant unobservable individual effects and endogeneity.

Given the limitations of previous estimation techniques, the current study employed the dynamic modelling estimation framework, as shown in the equations with one-year lag of dependent variables to account for the endogeneity problem. Wilfred and Mbonigaba (2018) suggested that business researchers should use more sophisticated methods to improve the estimated results. The author suggested various estimation methods, such as the fixed effects method (FE), two stage least square method (2SLS), the generalised least squares and the generalised method of moment (GMM). Therefore, in order to account for the dynamic nature of firm valuation and to control for the endogeneity problem, GMM was adopted to estimate the impact of tax planning on firm value.

7.4.3 Data and Data Source

The study used a sample of firms listed on the Kenya, Tanzania and Uganda stock exchange. The dataset for the study included financial information and taxation data. This information was archival in nature, as companies were required to publish information publicly in annual reports (audited annual reports and accounts). Therefore, data were sourced from Bloomberg, McGregor, financial stock markets and respective company's websites. The data were collected on the

variables of interest for an 12-year period, from 2008 to 2019. The base year is 2008 because it was the year when all EACs adopted their code of corporate governance, while 2018 provided the most current data that was available.

7.4.4 Variables Selection and Measurement

To achieve the objectives of the study which investigated the impact of tax planning on firm value, the firm value measured by Tobin's Q (dependent variable) was regressed against the tax planning (main independent variable) and other control variables. For robust results, the study used two measures of tax planning: cash effective tax rate (CETR) and accounting effective tax rate (AETR). After the following paragraph, the chapter discusses the various variables used for the estimation.

TOBIN'S Q: The study measured firm value using the Tobin's Q ratio, which was developed by Tobin (1969) and has been extensively used in the literature to measure firm value. Bhagat and Bolton (2013) argue that Tobin's Q is the market-based measure of firm value, which is widely used in accounting, finance and corporate governance studies. Tobin's Q is highly utilised owing to its ability to reflect management performance (Bhagat & Black, 2002). They explain that a high Tobin's Q suggests that managers have added value to the assets employed. Similarly, the use of Tobin's Q in studies on the value implications of corporate tax planning has become standard since 1985, when Demetz and Lehn (1985) used it in their study (Desai & Dharmapala, 2009a). Following the study of Desai and Dharmapala (2009b), the study computed Tobin's Q as the ratio of the market firm value to the total book value of assets. The market value is calculated as the book value of assets minus the book value of equity plus the market value of equity. This method of computing Tobin's Q was also used by Bhagat and Bolton (2013), Gompers, Ishii and Metrick (2003), Haniffa and Hudaib (2006) as well as Villalonga and Amit (2006).

Tax Planning: The independent variable of interest was tax planning. The study used the ETR to measure tax planning. ETR is calculated by dividing a tax liability by pre-tax income (Hanlon & Heitzman, 2010). It is defined as the ratio of total tax expense to pre-tax income expressed as a percentage. The study used ETR for two important reasons. Firstly, recent empirical tax research has found that the ETR can indicate the level of tax planning (Armstrong et al., 2012; Tarmidi, 2019; Vrzina, 2018; Vacca et al., 2020). Secondly, ETR is a proxy measure of tax planning frequently used by many academic researchers (Dyreng et al., 2008; Robinson et al., 2010;

Zemzem and Ftouhi, 2013b; Niu et al., 2019; Soviana et al., 2020; Campbell et al., 2020). This study uses two types of ETR to have more robust study results.

This study uses the CETR together with the AETR to measure tax planning. The CETR reflects the cash amount that firms pay in a given year. Chen et al. (2019) posit that the CETR is an accurate measure of tax planning, and it is less prone to the error of including the reduction of tax expenses due to accounting practices requirements, which are not necessarily those of tax management. Similarly, Badertscher et al. (2013) argue that the CETR can capture a wide range of tax planning compared to other measures. Thus, in line with the computation of Chen et al. (2010), the CETR is calculated by dividing tax paid by income before taxes.

The study also uses AETR as the alternative measure of tax planning in the regression equation. The literature suggests that AETR is the tax planning measure that mostly reflects the firms' tax management activities. In addition, it is the most common method used by shareholders to evaluate the level of a firm's tax aggressiveness (Rego, 2003; Armstrong et al., 2012; Graham et al., 2013). Therefore, following the studies of Armstrong et al. (2012), Cheng et al. (2012), Dyreng et al. (2010) and Francis et al. (2019), the study computed the AETR as the ratio of a firm's total tax expenses to corporate pre-tax income.

The study included various control variables in line with the study of Dyreng et al. (2008), Rego and Wilson (2012), Tang (2019) as well as Kirkpatrick and Radicic (2020). These control variables are explained below.

Control Variables: Firm size (SIZE) was included in the regression equation to control for the influence of the size of firms on tax management capability (political power). Large firms are argued to have resources that allow them to benefit from tax planning, compared to small firms (Wu et al., 2012). The authors observe that large firms have the resources for engaging competent tax planners, which smaller firms cannot afford. Similarly, Wu et al. (2012) suggest that larger firms have the political power to influence government systems through negotiation with tax authorities or lobbying, which allows them to enjoy tax benefits.

SIZE was computed as the log of the total assets of the firms (Dyreng et al., 2008; Handayani, 2020). The study also included firm age (AGE) to control for firm experience in tax management.

AGE was computed as the number of years from firm registration on the stock market to 2018, which was the last year covered by the study. Firm tax aggressiveness is likely to be influenced by the desire for firm profit. To control for influence of profit on tax planning, the study included return on assets (ROA), which is measured as the ratio of pre-tax income to total assets (Richardson et al., 2013).

Minnick and Noga (2010) suggest that leverage (LEV) can be used as a mechanism to reduce taxes. The authors point out that debt can also influence the tax avoidance behaviour of a company. Similarly, Badertscher et al. (2013) find that leverage positively affects tax avoidance, implying that a firm's capital structure can significantly affect its tax management. Following the example of Hanlon and Heitzman (2010) and Minnick and Noga (2010), the study included leverage, which is measured as the ratio of a firms' debt to its total assets.

To control for accelerated depreciation expenses in tax planning, the study included capital intensity (CTN), measured as the ratio of fixed assets to total assets. Wu et al. (2012) argue that investment in fixed assets may lower a firm's ETR because of the higher depreciation expenses of fixed assets. A year dummy variable was also included in the study to control for differences in corporate tax aggressive activities that could exist over the 2008–2018 sample years (Chen et al., 2014).

7.5 Results and Discussion

7.5.1 The Panel Unit Root Results

The data analysis and the interpretation of the study results are presented in this section. Before data analysis, the study began by understanding the nature of the variables that were used to see if they fitted the data estimation technique adopted. This was achieved by testing the stationarity of the study variables (unit root test). Chen et al. (2014) contend that to ensure the fitness of the variables in dynamic panel data models, stationarity tests must be performed. The problem of non-stationarity, which has been more pronounced in time-series data, is also confirmed in panel data, particularly panel data where the number of units (N) is greater than time series (T) (Arellano, 2003).

Consequently, the study performed a unit root test to examine the order of the integration of all study variables. Omolade (2014) argues that the Im Pesaran and Shin (IPS) unit root test, together with the augmented Dickey-Fuller (ADF)-Fisher Chi square unit root test are the most established and appropriate unit root tests for panel data. Therefore, the study used these to test the stationarity properties of the variables. Table 7.1 below presents the results of these tests.

Table 7.1: Unit Root Tests

IM, PESARAN AND SHIN W-STAT			ADF - FISHER CHI-SQUARE	
	t-statistics (P-Value)	Order of integration	t-statistics (P-Value)	Order of integration
Q	-632.220(0.0000)	I(1)	252.953(0.0000)	I(1)
CETR	-88.5936(0.0000)	I(0)	213.855(0.0072)	I(0)
AETR	-4.16323(0.0000)	I(0)	265.598(0.0000)	I(0)
SIZE	-3.60059(0.0002)	I(1)	238.145(0.0000)	I(1)
ROA	-5.82484(0.0000)	I(1)	304.881(0.0000)	I(1)
LEV	-6.21184(0.0000)	I(1)	217.470(0.0045)	I(0)
CTN	-5.57296(0.0000)	I(1)	298.964(0.0000)	I(1)
AGE	-236.856(0.0000)	I(0)	492.10(0.0000)	I(0)

Source: Author's Computation

Table 7.1 above presents the results of the unit root test. The results showed that all the variables were integrated either at level I(0) or at order one I(1). The results further showed that none of variables is integrated at order two I(2). This result implied that there was no spurious result amongst the variables as they were all stationary (no unit root) and statistically significant at 1%.

Therefore, the study proceeded with the data analyses, the results of which are presented in Table 7.2 below.

Table 7.2: Summary of Descriptive Statistics

	Obs.	Mean	Median	Max.	Min.	SD	Skewness	Kurtosis	Jarque-Bera	
Q	1021	1.87	1.74	2.20	0.73	1.354	0.738	2.847	63.14	
CETR	1021	0.220	0.223	0.999	0.000	0.181	0.895	4.356	176.36	
AETR	1021	0.263	0.289	1.000	0.000	0.139	0.928	8.351	121.56	
SIZE (\$m)	1021	48.67	48.69	203.85	13.59	27.01	-0.097	2.432	12.565	
ROA	1021	0.086	0.057	0.692	-0.557	0.151	-0.0296	6.897	53.199	
LEV	1021	0.578	0.606	0.995	0.007	0.252	-0.265	1.674	71.254	
CNT	1021	0.599	0.635	0.983	0.009	0.212	-0.635	2.806	57.840	
AGE	1021	19.992	16.000	67.000	1.0000	12.947	0.687	2.718	68.814	
<i>CETR</i>	<i>Cash effective tax rate</i>		<i>ROA</i>	<i>Return on assets</i>			<i>CNT</i>	<i>Capital intensity</i>		
<i>AETR</i>	<i>Accounting effective tax rate</i>		<i>AGE</i>	<i>Years of existence of the firms</i>			<i>BOS</i>	<i>Board size</i>		
<i>SIZE</i>	<i>Size of the firms at time</i>		<i>LEV</i>	<i>Leverage</i>						

Source: Author's Computation

The study's results as presented in Table 7.2 indicated that the value of Tobin's Q in EACs had increased over the years, which indicated good investment prospects. Generally, the results showed that the mean value of Tobin's Q for the previous twelve years was (1.87). This result implied that there were viable investments for the firms listed on the EACs' securities market. The overall Tobin's Q mean of this study was consistent with previous studies such as that of Gathara et al. (2019) conducted in EACs. Furthermore, the results showed that the mean value of CETR and AETR were 22.34% and 26.4%, respectively.

The results showed that the mean value of ROA was 9.0%. Furthermore, the descriptive statistics indicated that the minimum value of ROA was -55.74%, while the maximum value was 69.26%. The results further showed a decreasing trend in ROA over the previous twelve years. In 2008, the ROA was 13.27, although this value decreased to 3% in 2018. The results suggested the overall mean value of ROA for listed firms in the EACs listed firms was 10%. The study results showed that the mean value of the firm size was 18.64, with a minimum value of 13.59781 and a maximum

of 23.84672. The results indicated the mean value of capital intensity as 58.98%. This result suggested that more than half of the firm assets were fixed assets.

7.5.2 Pearson's Correlations

To confirm that none of the variables in the model suffered from a problem of multicollinearity, the study conducted a Pearson's correlation analysis. The correlation matrix results presented in Table 7.3 below suggested no multicollinearity problem amongst the variables included in the analysis. The correlation matrix results presented in Table 7.3 below suggested a weak correlation amongst the variables included in the analysis. The results indicated that the maximum correlation coefficient was less than 0.5, emphasising a weak correlation amongst the independent variables.

Generally, the variables were not highly correlated, which implied that multicollinearity was not an issue. However, results of interest were the correlations between tax planning and Tobin's Q of the firms, which were -0.0522 and -0.0357 for the CETR and the AETR, respectively. The correlations among the three variables are interesting, as evidence has shown negative associations between tax planning and firm value.

The above Pearson's correlation results were consistent with the VIF results, which indicated that the variables did not suffer from multicollinearity problems, as all VIF values were below two. These results compared favourably with the threshold value of 10 set by Salmeron, Garcia and Garcia (2018) and Thomson et al. (2017). The correlation results are presented in Table 7.3 below.

Table 7.3: Correlation Matrix

	Q	CETR	AETR	SIZE	ROA	LEV	CTN	AGE	VIF
Q	1.0000								1.32
CETR	-0.0522	1.0000							1.27
AETR	-0.0357	0.3327***	1.0000						1.16
SIZE	-0.304***	0.1697***	0.0843**	1.0000					1.45
ROA	0.2128***	0.2297***	0.2030***	-0.082	1.0000				1.40
LEV	-0.095***	0.0877**	0.0189	0.4986	-0.402***	1.0000			1.71
CTN	-0.0400	-0.260***	-0.162***	0.1008	-0.188***	-0.0003	1.0000		1.16
AGE	-0.0215	0.0165	0.0478	0.0817	-0.0603*	-0.0876**	0.1493***	1.000	1.07

Source: Author's Computation

7.5.3 Gmm Specifications Test

The study employed dynamic panel data models using the system generalised method of moment (SYS-GMM) estimator. Similar to studies conducted by Omolade (2014), Wilfred and Mbonigaba (2018) as well as Maama (2020), the study used SYS-GMM with the orthogonality option. The orthogonality conditions that existed between the lagged values of the dependent variable and the disturbance term were due to the use of an additional instrument in the model. The GMM with the orthogonality option was a modified version of the GMM designed by Blundell and Bond (1998). Omolade (2014) argues that the strict exogeneity assumption is more relaxed under this option. The author posits that this option of the system GMM provides more consistent and efficient results.

Roodman (2009) posits that a crucial assumption for the validity of the GMM is that the instruments are exogenous. Omolade (2014) maintains that model estimations, using the GMM, commonly suffer from over-identification and serial correlation. Hayakawa (2013) argues that the over-identification problem is associated with the GMM finite sample behaviour, which is affected by several conditions together with the strength of identification. Sargan/Hansen is the common test for the over-identification problem of the GMM estimation of the model.

The exogeneity assumption in the study was that a firm's historical performance and characteristics are exogenous with respect to tax planning. Therefore, the study carried out rigorous tests of the validity of the orthogonality assumptions, as well as the strength of the instruments that is implied by these assumptions. Arellano and Bond (1991) suggest some key tests of these assumptions. The first test is the test for the exogeneity of the instruments by performing a Hansen test of over-identifying restrictions. The Hansen test has a null hypothesis that the instruments as a group are exogenous (Arellano & Bond, 1991). The study used two tests for the validity of instruments, the Hansen J test and the Sargan test of over-identification. These two tests each have a null hypothesis that the over-identification restriction of the instruments used in the model is valid. Second, the models have to meet the "rule of thumb" that the number of instruments does not exceed the number of panels (groups).

Table 7.4 below presents the results of the Sargan test of over-identification. The Sargan test has the null hypothesis of the joint validity of the instruments identifications. The results in Table 7.4

below showed that in all the models, the null hypothesis (H₀) was rejected. These results implied that in all study models, over-identifying restrictions were invalid. Furthermore, these results indicated that the number of instruments used in the GMM models did not have any adverse effect on the study's outcomes.

Table 7.4: Sargan Test of Over-Identifying Restrictions

CASH EFFECTIVE TAX RATE		ACCOUNTING EFFECTIVE TAX RATE	
chi2	Prob> chi2	Chi2	Prob> chi2
chi2(66) = 581.29	0.000	chi2(66) = 591.30	0.000

Source: Author's Computation

The literature asserts that dynamic panel data estimators, especially the GMM, are affected by autocorrelation or serial correlation problems. Autocorrelations limit the efficiency of generalised methods of moment estimators (Hayakaya, 2013). The biggest concern was whether the study had included enough lags to control for the dynamic aspects of the empirical relationship. If it had, then any historical value of firm performance beyond those lags was a potentially valid instrument since it would be exogenous to current performance. The Arellano-Bond test for serial correlation uses AR(1) and AR(2), which are the most popular tests for serial correction. Arellano and Bover (1995) suggest that failure to reject the null hypothesis of no second-order serial correlation AR(2) implies that the original error term is serially uncorrelated and that the moment conditions are correctly specified.

Table 7.5 below provides the results of the Arellano-Bond test for serial correlation. The null hypothesis (H₀) of the test is that there is no serial correlation. The p-value of all results of the models presented in Table 7.5 below suggested that the null hypothesis of no second-order serial correlation AR(2) could not be rejected. This was evidenced by the p-value of the second-order autocorrelation (AR(2) in all the models, which were higher than 5% (0.05). These results led the study to conclude that serial correlation was not an issue in the GMM models, and thus the estimations were consistent and efficient.

Table 7.5: Arellano-Bond Test for Serial Correlation

CASH EFFECTIVE TAX RATE				ACCOUNTING EFFECTIVE TAX RATE			
AR(1)		AR(2)		AR(1)		AR(2)	
z	Prob>z	z	Prob>z	z	Prob>z	z	Prob>z
-2.25	0.025	0.97	0.331	-2.27	0.023	1.01	0.311

Source: Author's Computation

7.5.4 Regression Results and Discussion

This section presents the regression results of the models' estimations of the association between tax planning and firm value in EACs. The dependent variable used was Tobin's Q, while the main independent variable of interest was tax planning measured by CETR and AETR as alternative measures of tax planning. The models also included firm-specific characteristics as control variables, comprising firm size (SIZE), return on assets (ROA), leverage (LEV), capital intensity (CNT) and age (AGE). This section presents two different sets of results. In the first set, the study used CETR as the main independent variable, while the second results use AETR as the robustness check.

7.5.5 The Association between Cash Effective Tax Rate and Firm Value

Table 7.6 below provides the estimation results of Model 7.5, which estimated the relationship between tax planning measured by CETR and firm value (Tobin's Q). The result demonstrates that there is an association between tax planning and firm value. Specifically, the results demonstrated that tax planning is negatively and statistically significantly associated with firm value. With a coefficient of -1.5974, the results suggested that the tax-planning rate influences firm value up to 158%, provided that other variables are held constant. In addition, this result was significant at 1%. This regression result confirmed the correlation analyses provided in Table 7.3 above, where the results showed that the correlation between ETR and Tobin's Q was negative. These results were consistent with those of Desai and Hines (2002), Wang (2010) and Chen et al. (2010). These studies found that tax planning activities are negative and significantly related to firm value. The results indicated that firms that are less tax aggressive have more firm value compared with those that are more tax aggressive.

Table 7.6: Regression Results of the Association between Tax Planning and Firm Value Using (CETR) as the Measure of Tax Planning

Variable	Coefficient	Std. Error	t-Statistic	Prob.
Tobin's Q_{L-1}	0.8150629	.0588495	13.85	0.000
CETR	-1.577111	.5616577	-2.81	0.006
Firm size	0.2934734	.1321223	2.22	0.029
Return on assets	1.638947	.7521859	2.18	0.032
Leverage	-0.6175472	.2470544	-2.50	0.014
Capital intensity	-0.2264239	.7312138	-3.10	0.003
Age of the firm	0.0028459	.0124439	0.23	0.820
Constant	7.454657	2.774336	2.69	0.009
Wald chi2(7) = 148.95		Prob> chi2 = 0.0000		

Source: Author's Computation

Table 7.6 above displays the system GMM results. From the outcome, these results showed that all the variables under investigation, except for age, exhibited a significant relationship with firm value. Moreover, the results showed that tax planning has a negative impact on the value of a firm. This means that firms that engage in tax planning contribute to the decrease of firm value. Here, the coefficient of -1.577 indicated that a 1% increase in tax planning would cause a firm value to decrease by 158% when the other variables remain unchanged. The regression result was consistent with the findings of Bryant-Kutcher et al. (2011), MacNaughton and Mawani (1997), Nanik and Ratna (2015), as well as Desai and Dharmapala (2006), who report a negative relationship between Tobin's Q and tax planning.

The negative relationship is further explained by the concept of information asymmetry between the resource owners and the management of the organisation. Information asymmetry causes management to pursue its selfish interests when engaging in tax planning, which leads to a negative relationship between the ETR and firm value. However, the extant literature reports a positive relationship (Derashid & Zhang, 2003; Gupta & Newberry, 1997; Richardson & Lanis 2007; Minnick & Noga, 2010; Rego, 2003).

This result was expected and was in accordance with the theoretical foundation of the study. The implication of this negative relationship between tax planning and firm value is that because of agency problems; tax planning may become a shield for managers' rent-seeking behaviour, thus making the costs of tax planning outweigh the gains it brings, which eventually leads to a negative effect on firm value. Similarly, this result reflected reality because when governance is inadequate, agency costs, together with other tax and non-tax costs related to tax planning, outweigh the benefits of tax planning and lead to shareholders' value distraction. This result revealed that costs, such as fees paid to tax experts in EACs, time and the effort of employees involved in resolving audit issues with tax authorities, were significant.

Moreover, this result established that fines, penalties and interest, which revenue authorities charge listed firms in EACs when tax aggressiveness is discovered, were significant enough to affect firm value. Likewise, this result showed that investors and other stakeholders in EACs punished firms that were not socially responsible and did not pay their fair share of tax. To clarify, this result indicated that firms in EACs suffered reputational costs when aggressive tax avoidance became public knowledge and negatively affected firm value. This result confirmed the findings of the studies of Chen et al. (2010), Desai and Hines Jr (2002), Tang (2016), Xin-hua, Qian and Mengting (2015) and Zhang et al. (2017), who demonstrated that tax planning results in a decrease in the value of firms.

The capital intensity variable also exhibited a significant and negative relationship with firm value. The result indicated that a 1% increase in capital intensity caused firm value to decrease by 23%. The finding of the negative effect of capital intensity on firm value (measured by Tobin's Q), implicitly supported the literature finding that capital intensity increases a firm's risk. This result was similar to prior studies such as that of Lee (2010). The relationship between leverage and firm value was also significant and negative, whereby a 1% increase in leverage resulted in a 62% decrease of firm value, which supported previous studies suggesting that higher debt results in low return for equity shareholders (Chadha & Sharma, 2015). Firm size and ROA had a direct relationship with firm value. The results indicated that a unit increase in firm size caused firm value to increase by 29%, suggesting that firms with larger assets have a higher propensity to increase their value. Moreover, the results revealed that a 1% increase in ROA caused the firm

value to increase by 164%. This result indicates that an increase in firms' ROA will cause an increase in their value.

7.5.6 Regression Results of the Association between Tax Planning and Firm Value Using (AETR) as the Measure of Tax Planning

The literature argues that the cash effective tax rate is a more reliable measure of tax planning. Nonetheless, the study conducted a further analysis using the accounting effective tax rate to check the robustness check of the study's inferences. The regression results of the association between AETR and firm value (Tobin's Q) are presented in Table 7.7 below. These results confirmed the study's inferences from the previous estimation model. It was clearly shown that there was consistency in the results of the different measures of tax planning. All the coefficients' signs were the same for the two measures of tax planning. They both showed that tax planning is negatively associated with firm value. Both models were statistically significant, with CETR at 1% while AETR at 5%.

Table 7.7: Regression Results of the Association between Tax Planning and Firm Value Using (AETR) as the Measure of Tax Planning

Variable	Coefficient	Std. Error	t-Statistic	Prob.
Tobin's QL-1	0.8381471	.0536175	15.63	0.000
AETR	-1.186147	.4507903	-2.63	0.010
Firm size	-0.2359849	.1029168	-2.29	0.024
Return on assets	1.662178	.8222253	2.02	0.046
Leverage	0.6299227	.2355588	2.67	0.009
Capital intensity	-2.07376	.652828	-3.18	0.002
Age of the firm	0.0010806	.0097693	0.11	0.912
Constant	6.068046	2.179508	2.78	0.007
Wald chi2(7) = 143.79		Prob> chi2 = 0.0000		

Source: Author's Computation

7.5.7 Inferences and Comparison with Previous Empirical Studies

The study results suggested that the aggressive tax-planning practices by the listed firms in EAC were associated with the reduction of firm value. Generally, this was not a surprising result because it was consistent with the agency theory of tax planning, which postulates that the complexity of tax planning would provide a shield to self-serving managers to mask their actions and exploit wealth during tax-saving activities. In this context, tax-planning activities would not enhance firm value. The direct effect of tax planning would be to increase the possibility of rent diversion in the agency framework. Wahab and Shaipah (2010) suggest that the negative result can be that tax-planning activities are associated with the moral hazard behaviour of managers. Additionally, a negative relationship between tax planning and the firm value indicates that tax planning incurs costs and risks that might offset tax-saving benefits. The result suggested that news about a firm's involvement in tax planning would warn investors about its lack of transparency when publishing its financial information, causing them to lose interest and confidence, which could negatively affect its market value.

The results of the study contributed to the literature in the context of EACs. This was in response to the call made by Weisbach (2002) to investigate the “under-tax management sheltering puzzle”, which is “why some corporations do not engage in tax planning more extensively”. Perhaps, shareholders disapprove of tax planning, regardless of the after-tax cash saving, because approval could create an avenue for managerial rent diversion. Similar to that of Desai and Darampala (2009), the study result did not validate the simplistic presumption that tax planning represents the transfer of value (resources) from state to shareholders. Instead, the patterns in the data were more consistent with the agency theory perspective on corporate tax avoidance, suggesting that increasing tax planning activity is associated with costs and risks that harm shareholder value (Blaylock, 2016; Lennox et al., 2013; Seidman & Stomberg, 2017).

7.6 Conclusion and Recommendations

As discussed in the empirical literature review, there is an unabated debate amongst researchers and practitioners about whether corporate tax planning improves firm value. Traditionally tax planning is viewed as a firm value-enhancing activity since it reduces tax expenses and increases after-tax profit. However, recent researchers provide empirical evidence that corporate tax

planning does not necessarily translate into value maximisation, as value-enhancing tax planning is argued to depend on the strength of a firm's corporate governance. In light of the continuing debate, the study examined the relevance of tax planning to firm value in EACs by investigating the relationship between tax planning and firm value. The study used the system GMM in the data analysis, and the results showed a negative and statistically significant association between tax planning and firm value. These results suggested that a firm's investments in tax planning activities do not create value for shareholders.

The study's findings contributed to the literature by providing empirical evidence of the association between tax planning and firm value in developing countries, thus clarifying the ambiguity and contradictory evidence of previous studies of the relationship between these two important concepts in accounting and tax planning research. However, the evidence of the study suggested that the results of tax studies might depend on the differences in the tax and governance regulations of particular countries and economies. This indicates that tax-planning researchers, particularly those in developing nations, should consider practical and policy differences before generalising the findings in the literature to other countries.

The study has policy implications for the government and other regulatory authorities involved in taxation, financial reporting and corporate governance. The findings could be used for regulation and enforcement purposes. The study results revealed that listed firms engaged in tax planning in EACs, which are eager to become middle-income countries by 2025 or 2030 at the latest. However, tax planning in large multinational companies might impede the efforts of governments to collect sufficient domestic revenue to meet their developmental goals. Since the justice and effectiveness of tax systems have been challenged by the recent tax scandals of high-profile companies, such as Google, Apple, Starbucks and Amazon, the OECD and G20 countries have stepped up their efforts to combat certain widespread tax-avoidance practices, commonly known as base erosion and profit shifting (Johansson et al., 2017).

Therefore, the researcher recommends that EACs and other developing countries use the initiatives of the OECD and G20 to strengthen their tax systems, realise their development objectives and strive to attain the Sustainable Development Goals. Adequate tax capacity is vital to the development of these countries since a well-functioning tax system allows them to chart their

futures, pay for essential services, such as education and healthcare, and build the trust of their citizens. Indeed, tax capacity is a fundamental development issue.

Evidence of a negative impact of tax planning on firm value suggests that tax planning is not beneficial to firms. Therefore, with strong tax enforcement mechanisms, firms may reduce their tax planning for fear of being penalised. Thus, the researcher recommends that EACs governments, through their tax revenue authorities, implement additional tax enforcement mechanisms to reduce tax avoidance activities. In addition, the negative relationship between tax avoidance and firm value suggests that the associated tax/non-tax costs and risks serve as a deterrent to tax planning.

The adverse effects of tax planning on firm value found in this study imply that tax planning has double effects: it reduces the value of firms at the micro level while reducing government revenue at the macro level. Therefore, the researcher recommends that firms institute robust tax-planning practices that will reduce their effective tax liabilities, and thus improve their overall value. Firms that engage in better tax planning practices are likely to increase their firm value.

As shareholders may negatively perceive management's tax planning practices because of information asymmetry, the researcher recommends that company managers be more transparent and inform them about tax planning strategies and decisions that have the potential to increase firm value.

CHAPTER EIGHT

CORPORATE GOVERNANCE, TAX PLANNING AND FIRM VALUE

8.1 Introduction

This chapter describes the examination of the moderating influence of corporate governance on the association between tax planning and firm value. The study attempted to resolve the existing debate in the literature about the association between corporate governance, tax planning and firm value. The previous chapter described the study's investigation of the impact of tax planning on firm value. The findings showed that tax planning has a negative impact on firm value. The results confirmed that tax reduction through tax planning is associated with potential costs and risks. Thus, tax planning may accumulate both tax and non-tax costs, especially those associated with agency problems. Extensive tax planning may be associated with increased opportunities for rent extraction by a firm's manager. For example, studies, such as that of Desai and Dharmapala (2006), explain that tax planning and managerial rent extraction are complementary in that, an increase in tax planning creates information asymmetry, which facilitates opportunities for the diversion of corporate resources by managers for personal benefits. This may result in tax planning having a negative effect on firm value (Lee & Swenson, 2012).

However, Slemrod (2004) suggests an existing link between corporate governance mechanisms and the relationship between tax planning and firm value. For instance, Slemrod's (2004) study claims that managerial incentives can influence firm managers to engage in tax avoidance to create shareholder value. Thus, corporate governance can affect the relationship between tax planning and firm value. In addition, internal corporate governance mechanisms, such as board independence, are considered as the main vehicle of control of management. Therefore, corporate governance becomes a key mechanism for monitoring the behaviour of managers.

Previous studies identified a number of relationships involving corporate governance. Without a doubt, the link between corporate governance and tax risk is one of the most important. However, so far, the extant literature has not explored the potentially important effect of corporate governance mechanisms on the relationship between corporate tax planning and firm value in an emerging economies context. Therefore, the current study aimed to fill this gap in the literature by

analysing whether the impact of tax planning on firm value depends on the strength of corporate governance.

This chapter provides empirical evidence of the role of corporate governance in moderating the association between tax planning and firm value. The study used a sample of listed firms in EACs for the twelve years from 2008 to 2019. The study analysed the panel data using a robust version of the system GMM designed by Roodman (2009). The study results suggested that the strength of corporate governance has a significant moderating influence on the relationship between tax planning and firm value.

8.2 Background Information

The concept of corporate governance has become a concern because of financial scandals that caused the collapse of a large number of well-known companies, such as Adelphia, Enron and WorldCom (Dibra, 2016). The collapse was facilitated by wrongdoings on the part of management, auditors and financial market operatives. These scandals shook the confidence and trust of investors (Connelly et al., 2016). Moreover, they resulted in demands for improved corporate governance practices because, in the absence of corporate governance, managers can act in their self-interest, rather than in the interests of investors, and cause information asymmetry between themselves and shareholders (Gillan & Starks, 2003). Management can use various investment strategies that may seem beneficial to shareholders, but, in fact, some may work for their self-interest.

Studies, such as those of Martinez and Ramalho (2014) as well as Landry et al. (2013), suggest that tax planning may seem beneficial to firms and shareholders but, in most cases, is used for rent extraction. Fortunately, corporate governance mechanisms can restrict the self-interested decisions of managers (Aldaas et al., 2019). Authors suggest that corporate governance, which is described as a system that influences the direction and control of a corporation, builds trust, integrity and transparency. According to McCahery et al. (2016), a firm's compliance with principles of good corporate governance guarantees shareholder value by ensuring the proper utilisation of the firm's resources, which improves investor confidence. Spanos (2005) points out that effective corporate governance ensures economic growth and reduces risks for investors. Moreover, it attracts investment capital and improves the performance of companies. The key feature of corporate

governance is that it distributes rights and responsibilities amongst various participants in a company, such as the board, managers, shareholders and other stakeholders (Yermack, 2017). Similarly, corporate governance ensures that rules and procedures for making decisions about corporate affairs are clear (Steckler & Clark, 2019).

Over the years, firms have extensively engaged in aggressive tax planning, which reduces tax payments and generally increases after-tax returns to investors. However, tax laws and regulations are very complex, and there is close supervision by revenue authorities. Gribnau and Jallai (2019) posit that, managers of companies reduce the possible scrutiny by revenue authorities by obscuring the underlying intent of tax avoidance transactions and reducing the level of tax-related disclosures. Both revenue authorities, capital market authorities and national accounting reporting boards require disclosure of tax-related information in financial statements.

However, the amount of detail required and reported is rather limited; therefore, firms may not provide sensitive tax information as required. Thus, it is difficult for outside investors to judge the underlying purpose of tax avoidance and the degree of complementarity between tax avoidance and diversion of rents. The agency theory view of tax avoidance suggests that tax avoidance creates a shield for managerial opportunistic behaviour. Agency theory treats the company as a contract according to which shareholders (principals) engage managers (agent) to perform services on their behalf, and commonly principals delegate decision-making authority to the agent (Jensen & Meckling, 1976; Wu, Zhao & Tang, 2014). In this agency relationship, a misalignment of interests between shareholders and managers is created by separating ownership and control (Fama & Jensen, 1983; Maama & Mkhize, 2020). Thus, the agency problem (also known as the principal-agent problem) arises, which has become a pervasive phenomenon in modern corporations across the globe.

Corporate governance is essentially viewed as a mechanism in the agency relationship to mitigate the agent's self-serving behaviour (Eisenhardt, 1989; Bar-Yosef & Prencipe, 2013). Corporate governance has been playing an important role in monitoring different actors and harnessing tax-planning procedures. However, its performance in developing nations has been questioned and disputed. Moreover, how corporate governance can rehabilitate informational efficiency and mitigate the agency problem is still debated. The tax literature that incorporates the issue of

corporate governance, such as the studies of Desai and Dharmapala (2006), Hanlon and Slemrod (2009), Lanis and Richardson (2011) as well as Chen et al. (2010), has shown that corporate governance mechanisms can minimise tax aggressiveness. In fact, shareholders assess the effectiveness of corporate governance practices in monitoring managerial decisions related to tax affairs (Desai and Dharmapala, 2009b). However, there is a dearth of published research on corporate governance and tax planning in developing nations. Most studies of corporate governance concentrate on a suitable regulatory framework for introducing the principles of corporate governance. Consequently, attention is paid to legal practices, information disclosure and principles of ethical control. However, little attention is given to the relation between corporate governance and tax management.

To the researcher's knowledge, there is no published research that investigates the role of corporate governance in monitoring the relationship between tax planning and firm value in EACs. Together with the mixed results of previous studies, this was a further motivation to carry out the study, which investigated the moderating effect of the strength of corporate governance on the relationship between tax planning and firm value. The study was essential, given the importance of tax planning, corporate governance and firm value.

This chapter is organised as follows: Section 8.2 presents the literature review; Section 8.3 discusses the methodology; Section 8.4 presents the results and the discussion; Section 8.4 covers the conclusion and recommendations.

8.3 Aim and Objectives of the Study

As highlighted in the literature, tax planning is associated with agency problems because managers may implement tax planning for their self-interests at the expense of shareholders. Thus, corporate governance is argued to have the ability to reduce the agency problem and align the interests of shareholders to that of management in tax planning strategies. In view of this claim, the study examined the ability of corporate governance to moderate the relationship between tax planning and firm value. Specifically, the study evaluated how the corporate governance mechanisms of firms influence the relationship between tax planning and firm value.

8.4 Review of Previous Studies

The agency theory framework of the association between tax planning and firm value developed by Desai et al. (2006) predicts that tax planning can reduce firm value. The authors posit that a lack of transparency in tax planning provides firm managers with a screen to hide their self-serving actions. A survey conducted by Henderson (2005) showed that managers are reluctant to disclose information related to tax management to shareholders for fear of revenue authority scrutiny. This lack of awareness on the part of shareholders can lead to information asymmetry between managers and shareholders and create a moral hazard. This provides an opportunity for rent diversion to managers of the firms. It is believed that managers who are aggressive concerning tax planning may also be aggressive in their financial reporting decisions (Frank et al., 2009). For example, within the same accounting period, they attempt to manage accounting profit upwards while simultaneously managing taxable income downwards.

Against this setting, it is relevant to consider the role of corporate governance mechanisms in protecting the interests of shareholders when management is engaged in tax planning (Desai et al., 2006). A large body of research has investigated the role of corporate governance in monitoring managerial actions (Filatotchev et al., 2018; Habbash, 2019; Yee et al., 2018). These studies argue that the strategic decisions of companies rely on the conduct of corporate governance. Additionally, Yermack (2017), as well as Filatotchev et al. (2018), suggest that when shareholders evaluate management tax-planning strategies and decisions, they consider the role that corporate governance has played in monitoring them.

The importance of corporate governance in moderating tax planning is also highlighted by Owens (2008), who argues that good corporate governance leads to transparent and good-quality management, which precludes any conflict of interest between shareholders and management. Thus, corporate governance aligns the interests of shareholders with those of managers, which enhances the quality of financial reporting (Habbash, 2019). When corporate governance provision is strong, accounting profit understatement is impossible, and tax planning provides no diversionary benefit. Desai et al. (2009a) provide empirical evidence that corporate governance moderates the relationship between tax planning and firm value and that tax planning benefits shareholders only when the level of corporate governance is strong. Similarly, Wilson (2009) and

Hanlon and Slemrod (2009) provide evidence that tax planning ensures firm value only when corporate governance is strong.

Thus, firms with different governance structures may practise various types of tax management (Abdul-Wahab et al., 2017) because corporate governance may discourage managers from engaging in opportunistic behaviour and excessive tax risk-taking. As taxation may interact with various governance mechanisms, it can affect firm value. If shareholders and managers diverge on a tax planning strategy, corporate governance may have an impact on the final decision that is taken. Hence, if corporate governance is poor, tax planning will be associated with decreased firm value. In the same context, Desai and Dharmapala (2009a) argue that when information asymmetry between managers and shareholders occurs, managers are motivated to act in their interests resulting in a negative relationship between tax planning and firm value. Based on a sample of UK listed firms from 2005 to 2007, Abdul-Wahab and Holland (2012) report a negative relationship between tax planning and firm value.

Wang (2011) suggests that corporate governance plays a vital role in moderating the negative effects of corporate tax aggressiveness on shareholder value. The author argues that corporate transparency brought about by strong corporate governance facilitates monitoring and thus constrains managerial opportunistic behaviour. Chung (2019) argues that poor corporate governance leads to corporate opacity, which will provide a layer of protection for insider rent extraction, facilitating related party asset transfers, excessive perquisite consumption or outright theft of earnings. The author maintains that the effect of agency problems engendered by tax avoidance is more severe in firms with poor corporate governance. However, the author suggests that stronger governance facilitates firm transparency.

Beyer et al. (2010) point out that while the opacity created by tax aggressiveness provides more opportunities for managers to engage in insider trading, more robust monitoring can reduce the information advantage of managers. Corporate opacity exacerbates the hidden costs associated with tax aggressiveness (Chung, 2019). The agency theory view of tax avoidance suggests a negative relationship between tax aggressiveness and firm value as corporate opacity increases. Strong corporate governance alleviates potential agency problems underlying tax aggressiveness. Thus, the value-enhancing view of tax planning is more pronounced in well-governed firms. The

study conducted by Chen et al. (2010) argued that corporate governance, which is represented by ownership structure, moderates the relationship between tax planning and firm value. Chen et al.'s (2010) study, which investigated whether family firms are more aggressive compared with non-family firms, found that family firms are less tax aggressive and have a higher value. This implied that family firms are governed effectively and less subjected to agency problems, as control and management rest on one hand. The authors posit that family owners are willing to forgo the tax-saving benefits of tax planning to avoid tax and non-tax costs associated with it, such as potential price discounts and rent-seeking, which is masked by tax avoidance activities, potential penalties and reputation damage.

Hanlon and Heitzman (2010) maintain that based on the agency theory, managers will engage in tax avoidance to achieve maximum utility by engineering the firm's financial performance. Increased monitoring by governance and incentives will reduce the bad practices, and therefore reduce the adverse effects of tax avoidance. Spanos (2005) points out that effective corporate governance ensures economic growth, the reduction of risks for investors; moreover, it attracts investment capital and improves the performance of companies. In the context of tax planning research, understanding the link between corporate governance and tax planning explains the difference in the economic strength of owners (principles) and the management (agent) of firms.

The interaction between corporate governance and tax planning determines whether management is allowed to pursue its self-interests in tax planning activities in a complex and obfuscated process (Desai & Dharampara, 2008) due to information asymmetry between owners and management caused by agency problems. In this scenario, which involves decisions and choices related to the adoption of tax planning practices, it is up to the owners to limit their losses. Typically, these measures involve the implementation of a monitoring system. The principal mechanism, which a company can use to protect the owners' interests from the selfish actions of managers and protect minority shareholders from the actions of controlling shareholders, is corporate governance. Therefore, shareholders prefer corporate governance mechanisms in ensuring that tax-planning decisions are consistent with their interests. In this light, corporate governance mechanisms could be considered as moderating factors of tax planning decisions.

Desai and Dharmapala (2009b) argue that the impact of corporate tax planning on firm value depends on the strength of firm governance. They showed that tax planning significantly impacted firm value with well-governed firms. Likewise, Koester (2011) investigated the influence of various corporate governance structures on moderating the association between tax planning and firm value. Results suggested that tax planning has a moderating influence on the relationship. The study argued that tax planning positively impacts firm value only when the company is well-governed. However, Wahab and Holland's (2012) study suggested that the strength of corporate governance does not influence the relationship between tax planning and firm value. The study posited that regardless of corporate governance mechanisms, there is a negative relationship between the intensity of tax planning and a firm's value.

The discussion above clearly shows that corporate income taxes represent a significant business cost and reduce a firm's after-tax returns, which encourages firms to practice tax planning to save the company. However, intensive tax planning is associated with other significant costs and risks, which might harm firm value. Nevertheless, if the interests of the managers who are engaged in tax planning are appropriately aligned with those of shareholders, they will practise effective tax management to increase after-tax firm value. Furthermore, the above discussion of the literature points out that the complexity of tax rules and proprietary information about a firm's tax position makes it difficult for outside investors to gauge the key driving forces of its tax avoidance. Prior research suggests that corporate governance allows outside investors to monitor managerial opportunistic behaviour better (Maama et al., 2019). Additionally, the managers of well-governed firms are more likely to engage in tax avoidance to enhance after-tax firm value and less likely to use abusive tax avoidance to mask rent extraction. Hence, the current study predicted that the strength of corporate governance influences the relationship between tax planning and firm value:

Hypothesis Twelve (H₁₂): The strength of corporate governance influences the relationship between tax planning and firm value.

8.5 Methodology

This section discusses the methods used to analyse the link between corporate governance, tax planning and firm value, using selected variables.

8.5.3 Data and Data Source

This study used a sample of all listed firms in Kenya, Tanzania and Uganda. The dataset for this study included financial, corporate governance and taxation data. These data were archival, as companies were required to publish information publicly in annual reports (audited annual reports and accounts). Therefore, all the data sources were Bloomberg, McGregor, financial stock markets and respective company websites. The data on the variables were collected from sources that covered 12 years, from 2008 to 2019. The year 2008 was when all EACs had adopted their code of corporate governance, while 2019 was the year when the most data were available at the time of the study.

8.5.1 Model Specification

The focus of the investigation was to achieve the fourth objective of the study, which was to establish the moderating effect of the strength of corporate governance on the impact of tax planning on firm value. The investigation was the final stage of the data analysis and followed the analysis of the data gathered to achieve the third objective of the study, which was to investigate the impact of tax planning on firm value, as explained in Chapter 7. The data analysis described in Chapter 7 used the model specification developed by Ohlson (1995). To examine whether the strength of firm corporate governance has moderating effects on the relationships between tax planning and firm value, the study included the interactive variables of tax planning and corporate governance.

Following the study of Wahab (2010), we provide Models 8.1 to 8.4 below to estimate the moderating role of corporate governance in the relationship between tax planning and firm value. Models 8.1 and 8.3 estimate the moderating effect of the individual corporate governance variables on the relationship between tax planning and firm value. On the other hand, models 8.2 and 8.4 estimate the relative influence of each of the elements of corporate governance on the relationship between tax planning and firm value.

$$Q_{it} = \beta_0 + \beta_1 Q_{t-1} + \beta_2 CETR_{it} + \beta_3 SIZE_{it} + \beta_4 ROA_{it} + \beta_5 LEV_{it} + \beta_6 CTN_{it} + \beta_7 AGE_{it} + \beta_8 BOS_{it} + \beta_9 BOI_{it} + \beta_{10} GDV_{it} + \beta_{11} MIV_{it} + \beta_{12} OWC_{it} + \beta_{13} INV_{it} + \beta_{14} CGV * CETR_{it} + \epsilon_{it} \quad 8.1$$

$$Q_{it} = \beta_0 + \beta_1 Q_{t-1} + \beta_2 CETR_{it} + \beta_3 SIZE_{it} + \beta_4 ROA_{it} + \beta_5 LEV_{it} + \beta_6 CTN_{it} + \beta_7 AGE_{it} + \beta_8 BOS_{it} + \beta_9 BOI_{it} + \beta_{10} GDV_{it} + \beta_{11} MIV_{it} + \beta_{12} OWC_{it} + \beta_{13} INV_{it} + \beta_{14} BOS * AETR_{it} + \beta_{15} BOI * AETR_{it} + \beta_{16} GDV * AETR_{it} + \beta_{17} MIV * AETR_{it} + \beta_{18} OWC * AETR_{it} + \beta_{19} INV * AETR_{it} + \epsilon_{it} \quad 8.2$$

$$Q_{it} = \beta_0 + \beta_1 Q_{t-1} + \beta_2 AETR_{it} + \beta_3 SIZE_{it} + \beta_4 ROA_{it} + \beta_5 LEV_{it} + \beta_6 CTN_{it} + \beta_7 AGE_{it} + \beta_8 BOS_{it} + \beta_9 BOI_{it} + \beta_{10} GDV_{it} + \beta_{11} MIV_{it} + \beta_{12} OWC_{it} + \beta_{13} INV_{it} + \beta_{14} CGV * CETR_{it} + \epsilon_{it} \quad 8.3$$

$$Q_{it} = \beta_0 + \beta_1 Q_{t-1} + \beta_2 AETR_{it} + \beta_3 SIZE_{it} + \beta_4 ROA_{it} + \beta_5 LEV_{it} + \beta_6 CTN_{it} + \beta_7 AGE_{it} + \beta_8 BOS_{it} + \beta_9 BOI_{it} + \beta_{10} GDV_{it} + \beta_{11} MIV_{it} + \beta_{12} OWC_{it} + \beta_{13} INV_{it} + \beta_{14} BOS * AETR_{it} + \beta_{15} BOI * AETR_{it} + \beta_{16} GDV * AETR_{it} + \beta_{17} MIV * AETR_{it} + \beta_{18} OWC * AETR_{it} + \beta_{19} INV * AETR_{it} + \epsilon_{it} \quad 8.4$$

Where Q_{it} is Tobin's Q, a measure of firm value, $CETR_{it}$ denoted cash effective tax rate, $AETR_{it}$ represented accounting effective tax rate, $SIZE_{it}$ is the size of firms, AGE_{it} was the years of existence, ROA_{it} represented return on assets, LEV_{it} denoted a firm's leverage, CNT_{it} was the capital intensity, CGV_{it} denoted the individual corporate governance variables. Lastly, β_0 was the constant of the equation, β_1 to β_7 were the coefficients of the variables, and ϵ_{it} was the stochastic error term at time 't'.

The above two models were estimated using the GMM. This was an appropriate model for the investigation since the variables included did not follow a normal distribution. In addition, the GMM estimations were not affected by heteroskedasticity and autocorrelation, which are common problems when using panel data.

8.6 Definition of Variables

8.6.1 Dependent Variable

The dependent variable of this study was firm value. The study used Tobin's Q to proxy the firm value, which was measured as market capitalisation over the total assets. This measure was used in previous tax studies, such as those of Wang (2011), Dey (2008) and Dhaliwal et al. (2011), which examined agency problems, tax planning and firm value. Tobin's Q is the most appropriate measure of firm value, compared to accounting returns (Inger, 2013). Tobin's Q is less affected by accounting policies and minimises distortions from tax laws and policy. This measure is mainly used because it reflects the total value of the firm together with debt (Iwamoto, 1992). Furthermore, this measure of firm value is appropriate for evaluating the value relevance of tax avoidance when there are agency costs.

8.6.2 Independent Variables

Tax Planning: This study used CETR, together with AETR, to measure tax planning. CETR was computed as cash taxes paid divided by pre-tax accounting income (Dyreng et al. 2008; Chen et al. 2010), while AETR was calculated as total tax expense divided by pre-tax accounting income (Chen et al. 2010; McGuire et al. 2012). The justification for selecting these two measures of tax planning is described in Chapter 2, Section 2.1.3.

Board Size: This variable was measured as the number of board members on the board of directors (Minnick & Noga, 2010). The size of a board reflects its effectiveness on its control of firm management (Lanis & Richardson, 2011).

Board Independence: Board independence was measured as the proportion of independent directors on a board.

Gender Diversity: In this study, gender diversity was measured as the percentage of female members on a board (Bear, Rahman, & Post, 2010; Nguyen & Faff, 2007).

Ownership Concentration: This variable was measured by the total number of shares held by shareholders who had more than 5% of the shares (Wilde & Wilson, 2018).

Institutional Investors: This was measured by the number of shares held by institutional investors (Schmidt & Fahlenbrach, 2017; Zhang et al., 2017; Zhang, 2016).

Managerial Incentives: This variable was measured by the natural logarithm of the remuneration paid to the board of directors (Huang et al., 2018a; Seidman & Stomberg, 2017).

8.3.2.3. Control Variables

This investigation included several control variables, such as firm size, ROA, leverage, capital intensity and age.

Firm Size: Prior studies provide two different views about the influence of firm size on tax planning. The first viewpoint suggests that larger firms have higher ETRs due to political costs (Zimmerman, 1983). The second view suggests that larger firms have smaller ETRs. This view holds that larger firms have financial resources that empower them to invest in tax management, political lobbying and negotiation with revenue authorities (Rego, 2003).

Return on Assets: ROA was integrated into the study to monitor the operational performance of the company (Gupta & Newberry, 1997). This variable was measured as the ratio of pretax profit to total assets. This ratio is the most used to establish accounting-based performance as a proxy for firm performance. It is important to improve firm performance and create strategies, techniques and tools that are appropriate and adapted to a company. Firm performance is considered an indicator of the success of a company. As a result, it is a reference for investors in their investment decision-making.

Leverage: The study included leverage as a control variable in line with Parisi (2016), who suggests that a firm's decisions about its capital structure affect its ETR. This study argues that tax laws provide the differential treatment of capital structure (debt and equity). Consequently, Richardson and Lanis (2007) suggest that firms use finance decisions as a tax planning decision to reduce their tax burden.

Capital Intensity: The capital intensity was included in this investigation to control the influence of a firm's investment into fixed assets on tax planning in line with previous studies (Parisi, 2016; Ribeiro, 2015; Richardson & Lanis, 2007). These studies showed that capital intensity significantly influences the ETR.

Age: The study included the age variable in supporting the claim that the age of a firm influences tax aggressiveness (Lanis & Richardson, 2011). Age was measured as the length of the period that

the company's stock had been traded in the security market. Table 8.1 below summarises the variables used in the models.

Table 8.1 Variables and Definitions

Variable		Definition	Reference
Firm Value	Tobin's Q	The market value/Total assets	Chen et al. (2019)
Tax Planning	CETR	Total tax expense/Pre-tax income	Minnick and Noga (2010)
Tax Planning	AETR	Cash taxes paid/Pre-tax income	Armstrong et al. (2012)
Board Size	BOS	Total number of directors on a board	Badertscher et al. (2013)
Board Independence	BOI	Proportion of independent directors on a board	Minnick and Noga (2010)
Gender Diversity	GDV	Proportion of female directors on a board	Minnick and Noga (2010)
Managerial Incentives	MIV	Total salary paid to executive directors	Badertscher et al. (2013)
Institutional Ownership	OWN	Number of the shares held by shareholders who own 5% or more of shares in a firm	Richardson et al. (2013)
Institutional Investors	INV	Percentage of shares held by institutional shareholders	Richardson et al. (2013)
Firm Size	SIZE	Total assets of a firm	Wu et al. (2012)
Firm Age	AGE	Years of existence of a firm	Richardson et al. (2013)
Return on Assets	ROA	Ratio of pre-tax income to total assets	Richardson et al. (2013)
Leverage	LEV	Total debt to total equity	Minnick and Noga (2010)
Capital Intensity	CTN	Ratio of fixed assets to total assets	Wu et al. (2012)

Source: Compiled by the author from the Literature Review

8.7 Results and Discussion

8.7.1 Descriptive Analysis

Table 8.2 below presents the summary of the descriptive statistics provided by the data analysis. The results of the descriptive statistics showed that firm value (the mean value of Tobin's Q) and the tax planning variables (CETR & AETR) were all closer to the minimum than the maximum. For, instance the mean value for Tobin's Q, which was the measure of firm value, was 1.94, with a minimum of 0.99 and a maximum of 11.97. A value of Tobin's Q of 1 or more indicated a positive investment opportunity. Therefore, these results showed that there were positive investment opportunities in EACs. The good performance of the listed firms in EACs was revealed

by the ROA, where the mean value of ROA was 9% with a minimum of -55% and a maximum of 69%.

Furthermore, the results showed that, on average, the CETR was 22% while AETR was 26%. The results also showed that the ETR decreased from 2007 to 2018. This result may be explained by non-compliance to the country's tax rules due to weak tax enforcement and regulations in developing nations, which led to a decrease in the ETR (Lee & Swenson, 2012). This result is confirmed by Atwood et al. (2012), who show that companies engage in aggressive tax planning when there is weak tax enforcement. Therefore, non-compliance with rules tends to decrease the ETR.

4.7.2 Multicollinearity Test

To check for multicollinearity amongst the variables, a correlation analysis was performed. The results presented in Table 8.3 below suggested a low correlation amongst the variables included in the analysis. All correlation coefficients were less than 0.5, suggesting that the variables were not highly correlated. According to Hair et al. (2009), multicollinearity exists if the correlation between two variables is above 0.90. Based on the results, it can be stated that no serious correlation problem existed. Confirming this claim, the variance inflation factors showed no problem of multicollinearity among the variables.

Table 8.2: Descriptive Data

	TOBIN'S	CETR	AETR	SIZE	ROA	LEV	CNT	AGE	BOS	BOI	GDV	MIV	OWN	INV
Mean	1.938775	0.220368	0.262774	48.66807	0.086717	0.578663	0.599589	19.99285	8.522673	0.877657	0.244057	11.16350	38.01248	66.09234
Median	0.992324	0.223894	0.288890	48.69526	0.057416	0.606048	0.635589	16.00000	8.000000	0.857143	0.250000	11.27068	37.41416	64.24937
Maximum	11.97096	0.999589	1.000000	203.8467	0.692599	0.994606	0.983331	67.00000	14.00000	1.857143	0.600000	15.82592	95.00000	95.82588
Minimum	0.038647	0.000000	0.000000	13.59781	-0.557430	0.007069	0.009266	1.000000	5.000000	0.000000	0.000000	5.874931	7.110992	10.85048
Std. Dev.	2.567060	0.180722	0.139250	27.00186	0.150671	0.252177	0.212412	12.94720	1.666691	0.189727	0.134605	1.653536	9.936766	15.67331
Skewness	2.663166	0.895199	0.928298	-0.096538	-0.029613	-0.264811	-0.635798	0.687209	1.119222	0.664080	-0.253425	-0.182799	0.781930	-0.079138
Kurtosis	9.292717	4.356246	8.351258	2.432420	6.897653	1.674190	2.806082	2.718153	3.995357	4.507535	2.224365	3.958046	9.013629	3.376199
Jarque-Bera	2376.051	176.3624	1121.565	12.56493	531.1992	71.25460	57.84065	68.81408	209.5478	140.9472	29.97620	35.26950	1346.503	5.816308
Probability	0.000000	0.000000	0.000000	0.001869	0.000000	0.000000	0.000000	0.000000	0.000000	0.000000	0.000000	0.000000	0.000000	0.054576
Sum	1626.633	184.8888	220.4670	15662.51	72.75552	485.4980	503.0550	16774.00	7142.000	735.4762	204.5199	8986.617	31816.44	55385.38
Observations	1021	1021	1021	936	1021	1021	947	1021	1021	1021	1021	1021	1021	1021

Source: Computed by the author

Table 8.3: Correlation Matrix

	TOBIN'S	CETR	AETR	SIZE	ROA	LEV	CNT	AGE	BOS	BOI	GDV	MIV	OWN	INV
TOBIN'S	1.000000													
CETR	0.081538	1.000000												
AETR	0.065754	0.318062	1.000000											
SIZE	-0.270259	0.155020	0.063609	1.000000										
ROA	0.255659	0.240258	0.203041	-0.103450	1.000000									
LEV	-0.081365	0.096077	0.022387	0.506782	-0.421724	1.000000								
CNT	-0.050274	-0.269892	-0.155916	0.096980	-0.189838	0.012791	1.000000							
AGE	0.017954	-0.047290	0.014888	-0.004111	-0.064840	-0.103842	0.118604	1.000000						
BOS	-0.046845	0.060489	0.051566	0.113046	-0.090749	0.213346	0.023665	-0.069690	1.000000					
BOI	-0.012535	-0.017450	-0.014221	0.080727	-0.045935	-0.039898	0.089781	0.083751	-0.205261	1.000000				
GDV	0.112854	-0.027399	-0.004097	-0.018893	-0.081661	0.051524	0.081111	0.085336	-0.155924	0.318781	1.000000			
MIV	0.103681	0.149557	0.078138	0.387635	0.116849	0.239574	-0.160313	-0.350178	0.060856	-0.180386	-0.069373	1.000000		
OWN	0.050558	0.004388	0.057995	0.038808	0.047771	0.013522	0.044528	-0.091357	-0.273417	-0.029863	0.154422	0.179944	1.000000	
INV	-0.043477	0.012765	0.079016	-0.099896	0.178644	-0.250614	0.028111	0.115460	-0.318362	0.038758	0.104745	-0.081288	0.397873	1.000000

*** = $p < 0.01$; ** = $P < 0.05$ and * = $p < 0.10$

Source: Computed by the author

8.8 Regression Results

This section presents the regression results of the models' estimations of the relationship between tax planning, firm value and corporate governance in EACs. The study's objective was to investigate the moderating influence of the strength of corporate governance on the relationship between tax planning and firm value. The previous chapter described how the study investigated the impact of tax planning on firm value. Consistent with the agency theory, the study found that tax planning affects firm value negatively and significantly (at 1%). Thus, this chapter explains how the study examined the influence of the strength of corporate governance on the association between tax planning and firm value. The results are reported in Table 8.4 and Table 8.5 below.

To examine the role of the strength of corporate governance, the model that was used to examine the relationship between tax planning and firm value was extended by incorporating six interactive or moderating variables. These variables comprised BOS*CETR, BOI*CETR, GDV*CETR, MIV*CETR, OWN*CETR and INV*CETR in the first model which used the cash effective tax rate as the measure of tax planning. In addition, the six interactive or moderating variables were included in the second model, which used the accounting effective tax rate as the measure of tax planning. These interactive variables included BOS*AETR, BOI*AETR, GDV*AETR, MIV*AETR, OWN*AETR and INV*AETR. These interactive variables were included to examine whether the relationship between tax planning and firm value is contingent upon the strength of corporate governance. Prior studies suggest that the association between firm tax planning and firm value may vary owing to the strength of corporate governance (Desai & Wahab, 2010).

Table 8.4 and Table 8.5 below present the results of the analysis of the data to find whether corporate governance has a moderating effect on the association between tax planning and firm value. The general results of the influence of corporate governance are shown in Column "d" of Tables 8.4 and 8.5 below. The model included the complete set of six interactive variables. The results revealed that the previous finding of a significant negative relationship between firm value and tax planning no longer holds. With good corporate governance, tax planning has a positive and significant impact on firm value. Therefore, similar to the findings of Desai and Dharmapala (2009b), this result supported the view that the strength of corporate governance moderates the relationship between tax planning and firm value. The results showed that tax planning is

positively and statistically associated with firm value at 1%. The result supported the study's *a priori* that the strength of corporate governance has a moderating effect on the association between tax planning and firm value. These findings suggested that the strength of corporate governance has a significant influence on the value relevance of tax planning.

These results highlighted the monitoring role of strong corporate governance, the presence of which would lead to the transparency of tax management strategies and thus limit managerial opportunistic behaviour. Furthermore, the results suggested that corporate governance in EACs could oversee managerial decision-making regarding tax planning strategies to ensure that the level and form of tax planning would enhance the value of firms. In addition, the results demonstrated that the strength of corporate governance amongst firms in EACs could alleviate the potential agency problems underlying tax aggressiveness. In this context, corporate governance mechanisms in firms in EACs could play a greater role in protecting the interests of shareholders in the event of managers engaging in tax planning. The implication of these results was that the interests of shareholders and management could be aligned by corporate governance in EACs, which would ensure management's efficient use of firm resources when engaging in tax planning for the benefit of shareholders.

The study findings contradicted those of Wahab and Holland (2012) as well as Goergen and Renneboog (1998), who found that the strength of corporate governance has an insignificant monitoring effect on tax planning. However, the study results were in consonance with the findings of other studies (Desai & Dharmapala, 2009; Wilson, 2009; Hanlon & Slemrod 2009), which found that corporate governance monitoring mechanisms significantly moderated the impact of corporate tax avoidance on the wellbeing of shareholders. The essence of such monitoring is to ensure that managers effectively utilise cash tax savings from corporate tax avoidance practices for value-enhancing activities.

The findings aligned with the agency theory of corporate tax planning, which asserts that without adequate monitoring, managers could be involved in suboptimal decisions. Furthermore, the results suggested that the separation of ownership from management highlights the necessity for strong corporate governance, which was consistent with the views of Sultana, Singh and Rahman (2019), who suggest that to mitigate the risk of corporate financial failure and enhance the

confidence of the public, effective functioning of corporate governance is needed. Furthermore, the results confirmed the findings of earlier studies, such as those of Soliman and Elslam (2012), as well as Al-Dhamari and Chandren (2018), who found that corporate governance could enhance the relationship between tax planning and firm value.

The results presented in Column “a” of Tables 8.4 and 8.5 below revealed the moderating influence of board size. The results showed that board size has a negative and statistically significant effect on the relationship between tax planning and firm value at ($P < 0.001$), in the case of the models that used the cash effective tax rate (BOS*CETR), and at ($p < 0.1$), in the case of the models that used the accounting effective tax rate (BOS*AETR). This result suggested that board size is a moderating factor and strengthens the negative relationship between tax planning and firm value. Moreover, the result supported the claim that the larger the board size, the greater the asymmetry of information, which increases opportunities for managers to extract rent through tax planning. This implies that a large board size lessens the board's effectiveness in overseeing a manager's tax-planning activities. This might be caused by a lack of coordination in a large board (Putri & Chariri, 2016), which is a reasonable argument because a larger board is associated with complicated communication and decision-making processes (Florackis, 2008).

Regarding the moderating effect of board independence on the relationship between tax planning and firm value, the results showed that the estimated coefficients of BOI*CETR and BOI*AETR were both positive and significant at 1% and 5% level, respectively. These results suggested that increasing one independent director on a board would positively affect the relationship between tax planning and firm value. Furthermore, these results implied that additional independent members on a board would increase firm value, as the ETR would go up (less tax planning).

Similar to the results of Al-Musali and Ismail's (2014) study, the results showed that additional independent members might decrease the costs and risks associated with tax planning, which may affect firm value (principled tax planning would lead to an increase in firm value). The moderating role played by board independence can be explained by the fact that a board of directors is made up mostly non-executive directors, and thus can work independently and effectively to ensure quality decisions regarding the level and type of tax planning strategies that are followed, and thus increase firm value.

The gender diversity variable was made to interact with the tax planning variables (GDV*CETR and GDV*AETR) to investigate its influence on the relationship between tax planning and firm value. The study results showed that the coefficient on the interaction term was positive and significant at the 5% level. This result demonstrated that the relationship between tax planning and firm value is positively moderated by female board representation. The slope of the coefficients indicated that female board representation could trigger an increase in firm value. Therefore, female representation on boards may decrease the costs and risks associated with tax planning, which may change its effect on firm value. However, the results failed to establish the moderating influence of managerial incentives on the relationship between tax planning and firm value. Consistent with those of Wahab's (2010) study, the results suggested that the effect of managerial incentives on the relationship between tax planning and firm value is not significant.

Additionally, the study investigated the moderating influence of ownership concentration on the relationship between tax planning and firm value. The results confirmed the study's hypothesis that firms with a higher percentage of large shareholders (ownership concentration) suffer less agency problems than those with dispersed ownership (Shleifer & Vishny, 1986). This position could be attributed to the large shareholders' capacity to assert monitoring prowess over their agents (management) unlike a company with fragmented shareholders. Large shareholders could be instrumental in monitoring the actions of managers and insider shareholders, thus minimising the free-rider problem often found when atomistic shareholding exists (Grinstein & Michaely, 2005).

In this case, the cost of monitoring can best be borne by large shareholders, who are more motivated and capacitated than small shareholders. This monitoring helps in mitigating non-value creation or the suboptimal behaviour of managers. Regarding the moderating influence of ownership concentration, the results in Table 8.4 and Table 8.5 below, Column "e", found that it positively and significantly influences the relationship between tax planning and firm value. Both OWN*CETR and OWN*AETR were positive and significant at 1%.

The results of the moderating influence of institutional investors on the relationship between tax planning and firm value are presented in Column "f" of Table 8.4 and Table 8.5 below. The study results found a positive and significant influence on both variables, with INV*CETR at 10% and

INV*AETR at 5%. Thus, institutional investors significantly moderate the relationship between tax planning and firm value because, as large shareholders, they are active in monitoring managerial performance and actions. The evidence adduced from the analysis demonstrated that the monitoring presence of large shareholders improves the impact of corporate tax planning on listed firms. Although shareholders might not effectively monitor and control a firm's decision to engage in tax avoidance, they have to ensure that its cash tax savings are channelled appropriately in the interests of shareholders. However, the results contradicted the results of previous studies, such as those of Hart (1995), Goergen and Renneboorg (2001) as well as Wahab (2010), which suggested that large shareholders (institutional investors or shareholders with concentration ownership) would pursue their interests at the expense of other shareholders because of their ability to access insider information.

Table 8.4: Regression Results of the Association between Tax Planning, Firm Value and Tax Planning (CETR)

Tobin's Q	A	b	c	d	e	f	g. Full Model
Tobin's Q_{t-1}	0.60(12.5)***	0.54(14)***	0.57(12.06)***	0.56(10.75)***	0.50(10.34)***	.56(10.88)***	0.605(25.54)***
CETR	2.48(0.88)	-10.63(-3.65)***	0.002(0.1)	6.70(1.95)*	-9.06(-3.26)***	-4.23(-1.85)*	20.99(2.84)***
SIZE	-1.21 (-6.89)***	-1.33(-8.90)***	-1.30(-7.18)***	-1.31(-7.79)***	-1.42(-8.30)***	-1.33(-7.82)***	-1.12(-12.39)***
ROA	2.50(3.19)***	3.07(3.67)***	2.07(2.97)***	2.43(3.10)***	3.90(4.47)***	2.46(3.64)***	1.76(2.07)**
LEV	5.21(6.35)***	4.18(6.19)***	4.45(4.82)***	4.02(4.11)***	5.55(4.89)***	4.87(5.88)***	2.71(2.89)***
CNT	-1.93(-2.30)**	-2.76(-3.25)***	-2.99(-3.05)***	-2.86(-3.12)***	-1.81(-1.73)*	-2.35(-2.65)**	-3.11(-4.13)***
AGE	0.06 (1.94)*	0.03(0.97)	0.052(1.34)	0.043(1.11)	0.08(0.02)	0.032(0.89)	024(0.11)
BOS	0.20(1.82)*	0.22(3.56)***	0.17(2.50)**	0.19(3.18)***	0.22(3.15)***	0.191(3.05)***	0.10(1.31)
BOI	2.0(2.70)***	0.62(0.79)	2.15(3.08)***	2.58(3.42)***	3.38(4.88)***	2.71(3.86)***	.061(0.07)
WOB	-1.042(-1.32)	-1.28(-1.71)*	-0.71(-0.74)	-1.02(-1.23)	-2.0(-2.33)**	-1.59(-1.94)*	1.51(1.54)
COP	.41(3.73)***	0.41(4.65)***	0.39(4.28)***	.54(4.67)***	.519(4.11)***	0.536(5.38)***	0.45(4.58)***
OWN	-0.07(-0.31)	0.011(0.67)	-0.012(-0.80)	-0.005(-0.32)	-0.044(-1.83)*	0.0017(0.09)	-.027(-1.36)
INV	0.039 (2.97)***	0.04(3.65)***	0.05(3.56)***	0.050(4.11)***	0.050(3.11)***	0.026(1.46)	.027(1.60)
BOS*CETR	-0.30(-2.89)***						-.091(-0.29)
BOI*CETR		11.74(3.21)***					12.41(3.29)***
GDV*CETR			0.85(2.39)				7.394(2.03)**
MIV*CETR				0.63(1.03)			-0.612(-1.53)
OWN*CETR					0.22(3.32)***		.128(1.97)*
INV*CETR						0.060(1.92)*	016(1.12)
Constant	10.02(3.36)***	2.92 (4.44)***	12.92(4.08)***	11.25(3.93)***	13.70(4.31)***	12.50(3.85)***	14.76(5.55)***
Observations	719	719	719	719	719	719	719
No of firms	91	91	91	91	91	91	91
AR(1)	0.025	0.010	0.027	0.022	0.017	0.19	0.004
AR(2)	0.265	0.206	0.298	0.290	0.239	0.278	0.219
Sargan	0.000	0.000	0.000	0.000	0.000	0.000	0.000
Hansen test	0.769	0.637	0.822	0.750	0.678	0.642	0.608

Source: Author's Computation

Note: *** = Significance at 0.01; ** = at 0.05 and * = at 0.1, and * = at 0.1,

Table 8.5: Regression Results of the Association between Tax Planning, Firm Value and Tax Planning (AETR)

Tobin's Q	A	b	c	d	e	f	g. Full Model
Tobin's Q _{t-1}	0.58(11.82)	.56(11.49)***	.532(9.91)***	0.558(1.86)***	0.554(11.05)***	0.566(10.96)***	0.6047729(22.28)***
AETR	-0.048(-0.18)	-0.061(-0.21)	-0.217(-0.86)	-0.061(-0.21)	-0.120(-0.43)	-0.124(-0.39)	4.852911(6.09)***
SIZE	-1.26(-7.22)***	-1.24(-6.95)***	-1.48(-7.93)***	-1.32(-7.56)***	-1.35(-7.94)***	-1.350(-7.49)***	7.183626(-1.59)
ROA	2.13(2.71)***	2.308(2.68)***	1.417(1.64)	1.99(2.55)**	2.00(4.29)***	2.357(2.83)***	2.646865(3.60)***
LEV	4.644(4.82)***	4.55(4.55)***	4.032(3.66)***	4.53(4.41)***	4.41(4.29)***	5.35(4.85)***	-1.207995(-11.50)***
CNT	-2.14(-2.39)**	-1.646(-1.91)*	-2.86(-3.25)***	-2.12(-2.34)**	-2.31(-2.52)**	-2.139(-2.32)**	-2.427925(-4.00)***
AGE	0.062(1.65)	0.072(1.95)*	0.067(1.68)*	0.068(1.78)*	0.054(1.44)	0.057(1.55)	0.0354626(2.18)**
BOS	0.097(1.43)	0.128(1.85)*	0.180(2.65)***	0.168(2.46)**	0.160(2.34)**	0.161(2.39)**	0.1732106(2.12)**
BOI	1.83(2.51)**	0.920(1.21)	2.17(3.06)***	2.013(2.78)***	2.19(3.17)***	2.066(2.79)***	0.025163(0.03)
WOB	-1.228(-1.65)	-1.452(-1.92)*	-3.61(-3.17)***	-1.42(-1.91)	-1.34(-1.86)*	-1.48(-1.94)	-1.737868(-1.69)*
COP	0.497(4.83)***	0.514(4.77)***	0.490(4.16)***	0.479(4.55)***	0.495(4.74)***	0.548(5.06)***	0.4540877(5.90)***
OWN	-0.009(-0.50)	-0.0105(-0.55)	-0.017(-0.84)	0.646(-0.35)	-2.70(-1.32)	-0.0168(-0.83)	0.0146163(0.64)
INV	0.044(3.45)***	0.035(2.60)**	0.049(3.50)***	0.045(3.50)***	0.050(3.89)***	0.0420(3.09)***	-0.0033108(-0.24)
BOS*AETR	-0.222(-1.72)*						-.1996212(-0.62)
BOI*AETR		2.52(2.58)**					6.602084(2.21)**
GDV*AETR			10.301(3.95)***				2.387688(0.73)
MIV*AETR				0.159(1.34)			-0.0546107(-1.53)
OWN*AETR					0.047(2.71)***		-0.0844594(-1.44)
INV*AETR	10.84(3.95)***					0.0265(2.07)**	0.1189578(2.52)***
Constant	719	8.84(2.15)***	15.308(4.68)***	12.01(4.30)***	11.01(3.30)***	11.77(4.12)***	14.42(7.4)***
Observations	91	719	719	719	719	719	719
No of firms	0.020	91	91	91	91	91	91
AR(1)	0.277	0.020	0.019	0.012	0.018	0.020	0.014
AR(2)	0.000	0.268	0.286	0.283	0.249	0.261	0.317
Sargan	0.707	0.000	0.000	0.000	0.000	0.0000	0.000
Hansen test	.222(2.42)**	0.743	0.768	0.682	0.737	0.685	0.523

Source: Author's Computation

Note: *** = Significance at 0.01; ** = at 0.05 and * = at 0.1, and * = at 0.1,

Although the literature shows that CETR is a reliable measure of tax planning, the study conducted a further analysis using AETR as the alternative measure of tax planning to check the robustness check of the inferences. The regression results of the association between tax planning, firm value (Tobin's Q) and tax planning (AETR) are presented in Table 8.5 above. These results confirmed the inferences from the previous estimation model that used CETR, indicating the consistency of the different measures of tax planning. All the signs of the coefficients were the same for the two measures of tax planning that showed that tax planning has a positive impact on firm value when corporate governance is incorporated.

8.9 Conclusion and Recommendations

The debate on the impact of tax planning on firm value and how corporate governance moderates this relationship has been of interest to policymakers and researchers, particularly in the EACs that are trying to create a worthwhile investment environment for business, on the one hand, and to enable governments to collect enough revenue, on the other. As a result, the study examined the impact of tax planning on firm value and the role of corporate governance in moderating this relationship. The evidence showed that tax planning has a negative influence firm value. The results implied that corporate governance moderates the relationship between tax planning and the value of firms and that good corporate governance, in fact, improves it. This revelation suggests that firms must have strong corporate governance if they want to reap the full benefit of tax planning. The study predicted and confirmed that the agency problem would be lessened with governance control, and tax avoidance activities would represent a transfer of value from the government to shareholders, thereby increasing firm value.

With strong corporate governance, the agency problem would be minimised, and the interests of shareholders and managers would be aligned. Strong corporate governance would monitor tax avoidance decisions and ensure that tax avoidance activities lead to firm value. In poorly governed firms, tax planning is likely associated with costs and risks, such as managerial rent extraction and penalties/interests charged by revenue authorities, which may negatively affect firm value. However, tax planning could enhance firm profitability if corporate governance ensures expertise and professionalism on the part of managers and monitors their decisions for tax avoidance to achieve its aim of value maximisation.

The findings of this study, which were generally consistent with those of Desai and Dharmapala (2009) and Wang (2011), contribute to the literature in two ways. Firstly, they demonstrated that shareholders are positively affected by tax planning activities in well-governed firms. Secondly, they provide evidence of the significant effect of corporate governance on the association between tax planning and firm value. The results indicated that board independence, gender diversity, ownership concentration and institutional investors have a significant and positive effect on the relationship between tax planning and firm value. The results were consistent with the agency theory on tax planning, which claims that information asymmetry, generally associated with tax planning, can result in moral hazard or fear of moral hazard. Board size was found to have a negative and significant association with the relationship between tax planning and firm value, while managerial incentives were found not to have a significant moderating influence on the association between tax planning and firm value.

The study had some interesting results, which opens up opportunities for other researchers. Several caveats to this study can be overcome by further research. Firstly, future studies can extend the sample period. Secondly, the study could be extended by taking into account other variables, such as the disciplinary role of each controlling shareholder in determining a tax strategy, and therefore firm value. Finally, the findings have policy implications for academics, government officials and company managers regarding the disclosure of tax expenses, the reconciliation of ETRs and corporate governance.

This researcher recommends effective monitoring of managers using various corporate governance mechanisms within a framework of sound corporate governance policy in EACs. The study found that corporate tax planning might be a value-enhancing practice, which leads to tax savings, thereby improving the liquidity, profitability, expected growth and tangibility of a firm. However, it should be implemented with caution to make it less aggressive and excessive. Moreover, shareholders should monitor managers to ensure that tax savings are channelled in value-enhancing directions and discourage tax aggressiveness, leading to negative consequences, thus depleting the returns due to shareholders.

CHAPTER NINE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

9.1 Introduction

This chapter presents the summary of the study and the major findings, the contributions of the research, recommendations for practice and policy, the limitations of the study, and suggestions for future research. The chapter begins with a summary that gives an overview of the entire study. The chapter proceeds with the summary of key findings, then a section on the many contributions of the study, followed by sections on recommendations for practice and policy, limitations, possible areas for further research and some concluding remarks.

9.2 Summary of the Study

The main aim of the study was to investigate the impact of tax planning on the firm value of East African listed companies while taking into consideration the role of corporate governance as a moderating factor. To achieve this aim, the study examined the level and trend of tax planning in EACs, the determinants of tax planning, the impact of corporate tax planning on firm value, and the role of corporate governance mechanisms in moderating the relationship between tax planning and firm value.

Chapter One of the thesis covered the introduction, the background to the study, the statement of the problem, the study context, the main aim of the study, the specific objectives, the research questions, and the significance and justification of the study. Chapter Two covered the conceptual literature review. This chapter provided a thorough discussion of the main concepts used in the study: tax planning, firm value and corporate governance.

Chapter Three laid the theoretical foundation for the study by expounding the theories that underpinned the development of the study hypotheses. This chapter discussed and contextualised the following theories: the agency theory, the legitimacy theory, the stakeholder theory, the political power theory, the political cost theory, the stewardship theory and the resource dependence theory.

Chapter Four of this thesis discussed the methodology adopted by this study. This chapter described the research design used by this study to achieve its objectives, the study population, the sample and sample selection procedures, the data and data sources, definitions of the variables, and the estimation techniques.

Chapter Five was the first to cover the empirical research that began with the examination of the level and trend of tax planning in EACs over 11 years. For many years, governments and other stakeholders have been complaining that companies are practising aggressive tax planning that leads to the loss of tax revenue, which could be used for public wellbeing and the provision of public goods. In light of this complaint, the study aimed to establish if firms in EACs were engaged in tax planning. Additionally, the study investigated the response of tax planning activities to tax policy reforms (administrative and technological tax reforms) implemented by EACs during the period under study.

The study adopted the ETR as the measure of tax planning, which according to Liu and Cao (2007), is also used by many studies to indicate the tax burden borne by the firms. Higher ETRs suggest that firms are less tax aggressive, while lower ETRs indicate more tax aggressiveness and fewer taxes being paid. The study used descriptive statistics to demonstrate the level and trend of tax planning using both the CETR and AFTR as tax planning measures.

Chapter Six described the study's examination of the determinants of tax planning. The study explored the motivation behind tax-planning activities carried out by firms in EAC to explain why some companies aggressively reduce their taxes, whilst others pay taxes with an ETR, which is equal to or above the statutory tax rate. The study used fixed effects (FE) and generalised least squares (GLS) as estimation techniques to examine the influence of firm-specific characteristics, corporate governance and country-specific variables on tax planning.

Chapter Seven explained the study's investigation of the impact of tax planning on firm value. As taxes form a significant cost to a business, which is expected to pay one-third of its earnings in tax, the use of corporate tax planning to reduce tax has become one of the most important business strategies. However, tax planning is associated with costs and risks, which may negatively affect firm value instead. Therefore, shareholders, firm management, government and other stakeholders are keen to understand the value relevance of tax planning. Therefore, the study examined the

value relevance of tax planning using the two-stage system generalised method of moments with robust orthogonality.

Chapter Eight explained how the study investigated the moderating influence of corporate governance on the association between tax planning and firm value. This investigation was based on the argument that the strength of corporate governance could influence the association. The study used the two-stage system generalised method of moments with robust orthogonality in this data analysis.

9.3 Key Findings and Discussion

The preceding section provided the summary of the study that achieved the four study objectives as described in Chapters Five to Eight. In achieving its objectives, the study provided empirical results that significantly add to the body of knowledge on tax planning, for example. The discussion below presents a summary of the key findings of the study based on its stated objectives.

9.3.1 The Level and Trend of Tax Planning

To achieve its first objective, the study used descriptive statistics to describe the results of the analysis of the tax planning schemes in EACs. The findings indicated the existence of tax planning activities in EACs. Furthermore, the study results showed that the trend and level of tax planning had been increasing over the previous 11 years, despite various tax policy reforms implemented by the EACs to increase tax revenue. This result indicated that more efforts needed to be done by the EACs to strengthen their revenue collection capacity. More anti-avoidance techniques required to be implemented to curb the tax avoidance practices. However, the results revealed that, on average, firms in EACs could have CETR savings from tax planning amounting to 7.66% and 3.6% AETR savings. These results indicated that the listed firms in EACs could benefit from tax savings through tax planning if they could manage the tax costs and risks associated with it.

9.3.2 Determinants of Tax Planning

Thomsen and Watrin's (2018) study suggested that firms pay significantly different amounts of taxes, and this variation in the level of tax payment has been evidenced in empirical studies (Jingga & Lina, 2017; Richardson, Wang, & Zhang, 2016). These studies have shown that different companies pay different amounts of corporate income taxes (Chen, Ge, Louis, & Zolotoy, 2019;

Dyreng, Hanlon, & Maydew, 2008) and suggest that some companies seem to be successful in reducing their corporate income taxes, compared with their counterparts in the same economy or industry. In addition, Thomsen and Watrin (2018) showed that some companies pay very little taxes when compared with other companies in the same country.

This considerable variation in the level of corporate tax avoidance among firms has perplexed academics, researchers and policymakers. The question that has become a central focus in the debate is, therefore, why do some companies aggressively reduce their taxes, whereas other companies pay substantial amounts of taxes, with an ETR equal or above the statutory tax rate? This question sets the tone for Objective Two of the study that involved investigating the determinants of tax planning in EAC. Essentially, this objective sought to understand what contributes to the variations in the EFTs of firms. The summary of the key findings of chapter two is provided below.

The study results showed that smaller firms are more tax aggressive compared with larger firms, which is consistent with the political cost theory. This result should alert policymakers and regulatory authorities (for example, revenue authorities) that small firms are most likely to avoid taxes compared to larger firms. Furthermore, the results revealed that profitable firms are less tax aggressive. This result confirmed the view that profitable firms have enough earnings to pay their taxes and thus are less tax aggressive. Given this, the study recommended that emerging economies should revisit their policies to make their economies more conducive to attract profitable investments. Moreover, the evidence showed that older firms are less involved in tax avoidance. This is possible because these firms are affected by political pressure to pay fair taxes to avoid reputation loss. However, the results of the investigation of leverage and capital intensity found no influence on the level of tax planning.

Regarding the corporate governance variables, the evidence showed that board size positively affects tax planning. The study also documented a significant and negative relationship between board independence and tax planning, which is inconsistent with the agency and stakeholder theories. The results further revealed that managerial incentives appear to be a significant determinant of tax planning activity. Overall, the study suggested that equity risk incentives induce managers to undertake risky tax strategies to increase their compensation and thus the value of their options portfolios. The study further found that ownership concentration negatively affects

the ETR. Based on the study's findings, gender diversity had a significant negative association with the tax aggressiveness of listed firms in EACs.

Furthermore, the evidence showed that the presence of institutional investors reduces firms' level of tax planning. This situation might be due to the monitoring role of such investors, or these investors are subservient to rules and regulations. Consequently, this result suggested that the presence of institutional investors protects the interests of outside investors. The findings further demonstrated that specific institutional arrangements in a country influence the tax planning of its firms. For instance, the evidence showed that management quality, culture, regulatory quality, ethics and auditing quality in a country has a significant impact on the tax planning activities of firms.

9.3.3 Tax Planning and Firm Value

Chapter Seven investigated the impact of tax planning on firm value. This chapter tested a hypothesis, which predicted a positive and significant relationship between tax planning and firm value. The GMM technique used in the data analysis suggested that tax planning was negatively and significantly associated with firm value. This result implied that the hypothesis was rejected, which is consistent with the results found in Slemrod (2005), Desai and Dharmapala (2009) and Chen et al. (2010). Generally, the result was consistent with the agency theory of tax avoidance, which perceives the intricacies of tax planning as providing a shield for self-serving managers to mask their actions and exploit wealth from tax-saving activities. As a result, tax avoidance does not enhance firm value. In other words, the likelihood of tax avoidance increasing firm value is potentially offset by the increased possibilities of rent diversion in the agency framework.

This result was consistent with the results of prior studies. The study conducted by Wang (2011) found that tax avoidance benefits are outweighed by agency costs, which reduces firm value. Moreover, the result validated the finding of Desai and Dharmapala (2009) that tax avoidance is not a transfer of wealth from the government to the shareholders of a company because it increases the possibility of managerial opportunism and allows tax savings to be channelled towards opportunistic managers.

9.3.4 Tax Planning, Corporate Governance and Firm Value

Chapter Eight explained how the study investigated whether corporate governance plays a role in mitigating the overall negative effect of tax planning on firm value in the agency framework. The study predicted that the agency problem would be lessened with governance control in place, and tax avoidance activities would represent a transfer of value from the government to shareholders, which would essentially increase firm value. The GMM results showed that corporate governance was a significant moderating factor in the relationship between tax planning and firm value. This result supported the view that the strength of corporate governance can influence the relationship between tax planning and firm value (Desai & Dharmapala, 2009; Wang, 2011; Wilson, 2009).

9.4 Contributions of the Study

This section discusses the contributions of the study to research methodology, to academic literature, to theories, and to practice and policy. The methodological contributions are related to the sample selection and the estimation techniques used in the study. The contribution to the academic literature is related to the country-specific nature of findings. The theoretical contribution is based on how the study expanded the understanding and implication of the various theories related to tax planning in an emerging economies context.

9.4.1 Methodological Contributions

The first contribution of the study to research methodology is related to sample selection. The study used a sample comprising listed firms in EACs. The literature shows a general dearth of studies exploring the impact of tax planning in developing countries by using a sample of listed firms in EACs (Wahab & Holland, 2012). Therefore, the study contributes to methodology by using an East African dataset to provide empirical evidence of the effect of tax planning on firm value in developing nations. In fact, to the researcher's best knowledge, this is the first research work of its kind that uses such a sample to explore the impact of tax planning on firm value. Similarly, as most studies use single country samples, their results cannot be generalised to other countries. However, as the current study used data from three countries, its results may be relevant to countries with similar environments.

Because of the sample selection, the empirical evidence of the study provides a significant contribution to the body of knowledge about tax planning in developing nations, in particular, as the tax regulations and enforcement policies in these countries differ from those of developed nations, where there are plenty of studies on tax planning. Developing nations appear to be characterised by revenue authorities that are less aggressive when curbing tax avoidance. In addition, weak enforcement laws and poor compliance with corporate governance principles characterise these countries.

The second methodological contribution of the study is its selection of the estimation technique. Previous tax planning studies used traditional methods in data estimations, such as the ordinary least squares. The current study used a unique estimation technique, which strengthened its findings. Wintoki, Linck and Netter (2012) contend that the lack of consensus among the results of previous studies was due to weak estimation methods. The current study used the GMM, which is a more advanced and sophisticated data estimation technique, which is superior to the majority of estimation techniques used in previous studies.

9.4.2 Contribution to the academic literature

The study's findings contribute to the academic literature by providing evidence to clarify the ambiguous and contradicting evidence of previous studies on the relationship between tax planning, firm value and corporate governance. However, the researcher suggests that the results of tax research depend on the tax laws, enforcement measures and government regulations of particular counties or economies. This implies that tax planning researchers and academics, particularly those in developing nations, should consider practical and policy differences when generalising the finding of studies in other counties' settings.

9.4.3 Theoretical Contribution

This study used mainly the agency theory; however, the stakeholder theory, the legitimacy theory, the political power theory, the political cost theory, the resource dependence theory and stewardship theory were also mentioned. The empirical evidence of this study contributes to the application of these theories in explaining the relationship between tax planning, firm value and corporate governance. Although previous studies apply these theories (Masnawaty, 2019;

Steinmüller et al., 2019; Taylor et al., 2018), they focus on developed nations. As previously highlighted, the tax regulations and enforcement measures of developed countries differ from those of developed countries, whereas the current study expanded the understanding of these theories in the context of developing countries.

9.5. Recommendations for Practice and Policy

Based on the findings of the current study, practical and policy recommendations can be made to regulatory authorities (government agencies responsible for taxation, financial reporting and corporate governance) and company managers.

The study results showed that there was a negative relationship between corporate tax planning and firm value in EACs firms, which indicated that the minimisation of the tax burden had a negative and significant impact on firm value in those countries. These results suggested that a firm's investments in tax planning activities do not create firm and shareholder value, which could be due to the risks and costs associated with tax planning (Chen et al., 2010; Slemrod, 2004; Wahab & Shaipah, 2010; Wahab & Holland, 2012).

Thus, it is recommended that regulatory authorities use the findings for regulation and enforcement purposes. The study's results provided evidence of the existence of tax planning activities amongst the firms in EACs. However, as most EACs plan to become middle-income countries by 2025, or 2030 at the latest, they need to collect domestic revenue for this goal, which is impeded by tax. Therefore, it is recommended that East African governments, through their tax revenue authorities, implement additional tax enforcement mechanisms to reduce identified tax avoidance and evasion schemes, which may increase tax revenue collection.

The negative relationship between tax planning and firm value found in this study suggests that associated tax and non-tax costs serve as a deterrent to tax avoidance without legislative action. However, due to information asymmetry between shareholders and managers, the latter may continue implementing tax planning without the knowledge of the former to serve their own self-interests regardless of the adverse effects on their firms. Therefore, it is recommended that the capital market and financial reporting authorities enforce transparency and disclosure in all firms engaged in tax management.

Furthermore, the study results found that corporate governance has a significant moderating effect on the association between tax planning and firm value. This result implied that the situation in EACs at the time of the study, which was related to corporate governance compliance to disclosures requirements, was adequate in preventing moral hazards in tax planning. However, it is recommended that capital markets and financial reporting authorities in EAC implement more rules and regulations that will require the management of firms to be more transparent to its shareholders.

Similarly, it is recommended that shareholders use corporate governance regulations, which are already in place in EACs, to access information related to tax planning activities and become more active in controlling harmful tax planning activities. Shareholders may use various methods, such as representatives on the board of directors, to be informed about decisions related to tax planning and thus limit opportunistic managers.

It is recommended that firms institute tax-planning practices that are more robust to reduce their tax liabilities, and therefore improve their overall value. In general, it is recommended that firms engage in effective and efficient tax planning practices for higher firm value. Tax management activities can increase firm value; however, shareholders may perceive it negatively because of information asymmetry. Consequently, it is recommended that the management of the firms be more transparent to shareholders when informing them about its tax-planning decisions, strategies and initiatives.

9.6 Limitations

Despite the novel contributions of the study, there were limitations. However, appropriate research procedures were taken to limit their effect on the attainment of the study objectives. The main limitations of this research were the sample framework and data collection. Thus, users of the research findings should consider the limitations of the research when interpreting its findings

Firstly, like much of the research conducted in emerging economies, the study faced the challenge of inadequacy of data. The study obtained data that covered a period of 11 years (2008–2018). However, some of the firms had missing data, which made the study use unbalanced panel data. Another potential limitation was the number of firms included in the sample, which consisted of only 99 firms. However, this sample size was large, compared to other cross-country studies, for

instance, that of Kyereboah-Coleman (2008), which included 16 firms in South Africa, and Mangena and Chamisa (2008)'s study that used 81 firms. Time limitations, cost and practical circumstances meant that the sample was chosen to ensure that it was large enough for statistical significance and significant contribution while ensuring that the PhD was completed within the planned period. However, this limitation challenges future research to conduct a similar study with larger sample size or a sample including other countries.

Secondly, the sample used by the study was limited to listed firms. The companies that were not listed on the stock market did not form part of the sample. Two reasons for not including these were (i) the annual reports of these firms were difficult to collect, and (ii) the study used Tobin's Q to measure firm value. The Tobin's Q can be established only on listed firms, the market values of which are known. As the results of the current research cannot be generalised to firms that are not listed in EACs, future studies could consider the inclusion of non-listed firms, although this would only be possible with the use of alternative measures of firm value.

Thirdly, the study used financial, corporate governance and taxation data collected from secondary sources, which may give rise to data validity issues. Even though financial statements, without doubt, are globally recognised sources of research data, they are limited by different sets of assumptions about the impact of their preparation and their context on some of the variables employed. More so, as the enforcement of good practices and accounting standards in emerging economies is notably weak, the information in annual reports may not have reflected the actual state of affairs.

In addition, some concerns may arise on annual reports disclosures. Some companies provide very detailed information relating to corporate governance in annual reports, while others may provide a simple description. This is the limitation of gathering information only from the annual reports. However, the use of annual reports in the study was consistent with previous studies conducted in Africa that principally used annual reports (Assidi, Aliani, & Omri, 2016; Sani & Madaki, 2016; Zhang, 2016; Maama, 2020). Therefore, it is recommended that future studies consider collecting data from sources other than the published annual reports of companies, such as the annual reports of regulatory agencies (revenue authorities, capital market authorities and national boards of accountants) that are required to file their annual reports.

Fourthly, to investigate tax avoidance, the study used financial statement data, as tax return data of firms were not in the public domain and thus unavailable. As tax information is confidential, the study used only publicly available information when investigating tax planning. The extant literature questions the accuracy and reliability of financial statement-based tax avoidance data (Hanlon & Heitzman, 2010; Plesko, 2004). Therefore, this study results should be interpreted with some caution. Thus, it is recommended that future research conduct a similar study using administrative data from revenue authorities. This is possible for those who have access to the data of revenue authorities, particularly staff of research departments of revenue authorities.

The fifth limitation of this study was its measurement methods. There is no universal agreement on using certain proxies, as different measures may produce inconsistent results. The study was limited to two measures of firm value (Tobin's and ROA). Previous studies have used several corporate governance measures; however, the current study was limited to six proxies: board size, board independence, gender diversity, managerial incentives, ownership concentration and institutional investors.

Another measurement issue was related to proxies for tax planning. In line with previous studies, the study measured tax planning using the ETR, which is regarded as the most appropriate measure of tax planning. However, the literature argues that all tax-planning measures suffer various limitations and thus cannot cover all the ranges of tax planning activities. Therefore, it is suggested that studies use more than one measure, as was done in this study, where two tax planning measurements were used (cash effective tax rate and accounting effective tax rate). However, the study challenges future researchers to conduct a similar study with different tax planning measures, firm value and corporate governance.

Therefore, the above-highlighted limitations must be considered in the interpretation of the findings of the study. However, as indicated already in this section, the limitations of this study provide potential avenues for future research. In the following paragraph, this study highlights more areas for future research.

9.7 Recommendations for Future Research

Firstly, the study was based on EACs, and thus its findings may not be generalised to other economies. This provides an avenue for future research to consider other emerging economies,

particularly other African countries, which would be useful for comparative analysis purposes. Moreover, the findings of the current study that contradicted those of studies conducted in developed nations might be due to weak rules and regulations in emerging economies, particularly those related to taxation and governance. Therefore, to confirm this argument, a future study should investigate the impact of tax planning on firm value in another emerging economy, with a different set of rules and regulations, and compare its findings with those of the current study.

Secondly, the quality of the disclosure of tax information in the annual reports is said to influence tax planning (Ozman, 2014). Therefore, future studies should consider disclosure requirements and the quality of tax information disclosure in annual reports.

Thirdly, this research was conducted using data from three countries, which may have precluded a detailed investigation of each country. Additionally, because of limited data on individual countries, the study did not do a country analysis. Therefore, future research should consider conducting similar studies on each individual country.

Fourthly, the media has played a significant role in identifying and fighting against the corporate tax planning practices of multinational companies (Kanagaretnam, Lee, Lim, & Lobo, 2018; Sikka, 2018). Future studies could consider conducting a study that investigates the role of the media in curbing tax avoidance.

Fifthly, studies such as the current one, which followed a quantitative research design when investigating corporate governance, tax planning and firm value, produced conflicting results. To obviate this, future research could employ other methodologies involving qualitative or mixed methods research designs. This could provide a more detailed understanding of the reason behind tax planning practices by researching the opinions of executives, for example.

Finally, a small but notable body of literature maintains that the relationship between tax planning and firm value is not linear but rather U shape (Delgado, Fernandez-Rodriguez & Martinez-Arias, 2014). To this end, future studies are encouraged to reinvestigate this relationship using quantile regression analysis, which will establish the impact of tax planning on firm value at different distribution levels.

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APPENDICES

APPENDIX A: ETHICAL CLEARANCE LETTER



25 June 2018

Mr Alfred James Kimea (217080982)
School of Accounting, Economics & Finance
Westville Campus

Dear Mr Ngcobo,

Protocol reference number: HSS/0698/018D

Project Title: The impact of Tax Planning and Corporate Governance on firms' value in East Africa

Approval Notification – No Risk / Exempt Application

In response to your application received 19 June 2017, the Humanities & Social Sciences Research Ethics Committee has considered the abovementioned application and the protocol has been granted **FULL APPROVAL**.

Any alteration/s to the approved research protocol i.e. Questionnaire/Interview Schedule, Informed Consent Form, Title of the Project, Location of the Study, Research Approach and Methods must be reviewed and approved through the amendment /modification prior to its implementation. In case you have further queries, please quote the above reference number.

PLEASE NOTE: Research data should be securely stored in the discipline/department for a period of 5 years.

The ethical clearance certificate is only valid for a period of 3 years from the date of issue. Thereafter Recertification must be applied for on an annual basis.

I take this opportunity of wishing you everything of the best with your study.

Yours faithfully



Professor Shenuka Singh (Chair)

/ms

Cc Supervisor: Dr Msizi Mkhize
Cc Academic Leader Research: Professor Josue Mbonigaba
Cc School Administrator: Ms Nondumiso Mfungeni

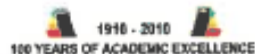
Humanities & Social Sciences Research Ethics Committee
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Founding Campuses: Edgewood Howard College Medical School Pietermaritzburg Westville

APPENDIX B: TURNITIN SIMILARITY REPORT

The impact of Tax Planning and Corporate Governance on Firms' Value in East Africa

ORIGINALITY REPORT

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