

Determinant of the Variability of Corporate Taxation in India: An Empirical Study

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Abstract

Purpose – The paper aims to examine determinants of variability of Indian corporate income tax rate. The role of investment and financing decision has been researched to unearth the reason for gap between statutory tax liability and effective tax liability. The objective is to highlight the economic and strategic implications of factors affecting taxation liability with regards to regulatory framework in India.

Design/methodology/approach – The present paper highlights the long-term strategic and public policy perspective for India as far as public revenue is concerned. The data set consist of NSE-500 Index, so as to capture flavor of all kind of companies for the period 2001 to 2012, from Prowess corporate data base. To proxy investment and financing decisions various company characteristics are taken. The size of company is measured by total assets, financing decision measured by financial leverage of company. The assets mix and export Intensity is examined to capture their effects. The policy variables are schedule tax rate and MAT, taken to capture time effect.

Findings – The average effective tax rate observed is 14.7 percent against GOI budget estimate of around 20-23 percent. The paper found investment and financing decisions have significant and negative association with effective tax rate of company. The paper makes recommendations for future so as to carve out a voluntary tax-paying culture on a large scale among corporate entities.

Research limitations/implications – There is lack of reliable data on various aspects of annual filling of returns and other financial information affecting tax liability. Therefore, the study focused on the availability of data and compliance to regulatory framework in India along with future implications.

Managerial and Policy implications – The gap between ETR & schedule tax rate is huge, the policy makers should reform the tax structure so that the benefits of exemptions & deduction can be minimized or are available to small or needy corporate, perhaps coming Direct Tax Code bill pave the way towards it.

Originality/value – In India, there is dearth of research in the area of corporate taxation. This paper aims at highlighting the historical relationship between statutory tax liability and effective tax liability corporate entities discharge.

Keywords

Corporate Taxation, Effective Tax Rate, Investment Decisions, Financing Decisions

Introduction

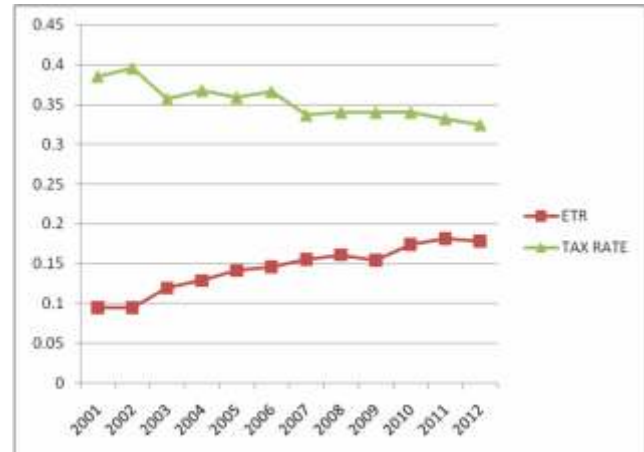
Corporate tax directly affects the expected return after tax on investments and in this way impacts the incentives available to entrepreneurs to establish and run businesses. Corporate effective tax rate (hereinafter referred to as ETR) is generally used by policy makers as a tool to make possible judgment of gap between statutory tax rate levied on corporate sector and effective tax rate that they are actually paying and implicitly forms the basis for reforming the tax system. Callihan (1994) explained two kinds of empirical ETR research, research aimed at marginal ETRs and research focusing on average ETR. Marginal ETR for a specific investment is the rate of tax paid on an additional unit of income from a specific investment project. Marginal ETRs should be used to investigate the effect of

taxation on investment decisions. Marginal ETR can also be used at the level of a company, but a company is a collection of investment projects, which makes the use of marginal ETR at that level problematic. Average ETR is better suited to express the overall tax burden on the company as these express the rate of tax paid on corporate income. Therefore, this paper looks at average ETR mainly because it is a measure to focus on differences in tax burdens across companies.

The remaining part of the paper is organized as follows. Section 2 describes the theoretical background on the role of effective and statutory tax rate in investing and financing decisions of a company within the overall business environment that exists. Section 3 describes some of the literature both nationally and internationally in this regard. Section 4 describes data and methodology employed in getting the results. Section 5 describes the analysis and findings in this paper. Section 6 enlists the managerial and policy implications of work and Section 7 concludes.

Theoretical Framework

In India, the Income Tax Act, 1961, provides for various exemptions and deductions for investing in capital assets like deduction under various subsections of section 10 and deductions listed under various subsections of section 80. Similarly deductions are available if a company relies on debt financing. These are the direct factors which are exploited by companies while minimizing their tax liability. Taxation of foreign investment is an important deciding factor in operations of multinational corporations (MNCs). On micro level, taxation affects all aspects of MNC's financial and investment activities by influencing, among others, the investment location, the timing of intra firm transfers and remittances and the ratio of debt to equity. In recent years, tax policy towards foreign investment income has become even more important as world economic integration continues to scale unprecedented levels. Foreign direct investment (FDI) now accounts for a substantial portion of global economic interaction, a phenomenon that carries significant implications for economic development and world economic growth. The transfer of capital from one country to another affect efficiency, wealth, income distribution and employment levels, all with important consequences for world economy.



Source: While ETR is as per Author Estimates, Tax rate is statutory tax rate

Figure 1 : Comparative Chart Showcasing Statutory Tax Rates vs. Effective Tax Rates During 2001-2012

Figure 1 shows financial data of NSE-500 Index companies. ETR is the mean yearly average of final tax liability that companies are paying. Tax rate is the statutory tax rate on companies as levied by the Government. The figure shows the gap between effective tax rate and statutory tax rate that companies are facing. For instance in 2001, the statutory tax rate was 38.5 percent whereas the average ETR was just 9.4 percent. In 2012, the tax rate was 32.4 percent whereas ETR increased to 17.8 percent. Overall, the ETR ranged from 9.4 percent to 18.1 percent whereas statutory tax rate ranged from 32.4 percent to 39.5 percent over the time period of 2001 to 2012. In this backdrop, the aim is to shed light on effective tax rate that the companies actually pay and its relationship with investment and financing decisions of the company.

Literature Review

Zimmerman (1983) suggests that large companies would because of their larger political visibility, have less tax incentives available to them than small companies. A counter argument to this is that large companies have more tax expertise or political clout to obtain advantageous tax incentives supported by later studies taking multivariate dimension. Shevlin and Porter (1992) report the finding of corporate tax to increase with corporate size within a univariate framework. Stickney and McGee (1982) using US data, have studied both leverage and capital intensity in a multivariate framework and found negative effects for these factors and found no effect for company size. Gupta

and Newberry (1997) used several asset mix variables and leverage within the multiple regression model with ETR as dependent variable and found no company size effect. Almas and Bjuggren (2010) argued effective corporate tax rates to affect the size distribution of firms as well as the composition of industries. They suggested effective corporate tax rates to differ by firm size, industry and over time, as far as Swedish economy is concerned. The t-tests demonstrated inequality in mean and variance of effective corporate tax rates between industrial sectors and service sector reports a higher effective corporate tax rate than production sector. The regressions showed effective corporate tax rates to have: a negative effect on size distribution of large firms, negative effect on transportation, financing and service sector and a positive effect on manufacturing, electricity and on production sector. Another study by Molloy (1998) showed that a comparison of statutory rates between countries is misleading. Determination of effective tax rate is important for understanding the impact of a particular country's tax policy on actual cost of operating in that country. Japan's substantially higher statutory rate resulted in a lower effective income tax rate for a firm in electronics industry when compared to similar U.S. firms. The paper concluded that even though Japan appears to impose a heavy income tax, the combination of overall lower compliance costs and effective tax rates provides a comparative cost advantage to a Japanese electronics firm relative to U.S. firms operating in the electronics industry. Further Richardson and Lanis (2007) examined the determinants of variability in corporate effective tax rates in Australia. The results indicated corporate effective tax rates to be associated with several major firm-specific characteristics including firm size, capital structure (leverage) and asset mix (capital intensity, inventory intensity and; research and development intensity).

Jha and Wadhwa (1990) claimed that Feldstein (1983) equation is more suited to Indian data than later study by Chirinko (1987) and established clear and direct relationship between business investment and taxes that is an increase in taxes on earnings tends to discourage investment. Sharma (1987) argued that tax incentives lower the cost of capital and this provides an incentive to entrepreneurs to step up the rate of investment. Xiaohong and Guisinger (1993) tests whether tax policy is effective in attracting foreign direct investment and examines differences in tax policies between developed and developing countries. Seventeen developed countries on an average, having high effective tax rates (compared to developing countries) appeared to

compete vigorously through tax policies and had tax rates that tended to converge over time. Forty Eight developing countries exhibited divergent tax behavior within the group, suggesting less competition. The study also found tax sensitivity of foreign direct investment to be significantly greater within the developed country group than within the developing country group. Datar (2000) argued that it is not necessary to sacrifice equity in taxation for capital market development. Nor is it necessary to prop up mutual funds by providing disincentives for direct investment in shares, debentures and securities. Janssen (2005) found Dutch effective tax rates to not differ significantly from statutory tax rates. Although capital intensity is negatively associated with effective tax rates, only a small portion of variance in effective tax rates could be explained.

The Indian corporate sector study by Guha (2007) examined the relationship between company size and effective corporate tax rate in multivariate framework. He argued larger companies to enjoy greater tax benefits like developing plant in special economic zone (SEZ) area and paying no taxes for so many years. The findings include a negative association between average effective tax rate and company size.

Research Design

Development of Hypotheses

Empirical studies in the past have found various relationships between company characteristics and ETR. The discussion in the previous section motivates the study of ETR especially in the context of Indian companies where the structure and complexity is enormous. Secondly this kind of study has not been undertaken in India on a regular basis. There are two competing view about relationship between ETR and firm size : first is political cost theory and second is political power theory. Zimmerman and Watt (1986) emphasized political cost theory and advocate that higher visibility of larger and more prosperous firms cause them to become victims of greater regulatory policy by government and wealth transfers. The alternative political power theory is that larger firms have lower ETR as they have substantial resources to influence the political process in their favor and exploiting best tax-planning through organizing their activities to minimize tax liability (Siegfried).

In India, corporate tax liability is based on Income Tax Act 1961 which distinguishes between book profit as per Companies Act 1956 and the taxable profits. It allows for deductions from book profit which is attributable for firms financing and investment activities.

The higher the investment in size of firm, higher the depreciation claim would be and lower would be taxable profits. The firms that are more capital intensive expected to have lower ETR's (Stickney and McGee). Fixed Assets (for instance patents and goodwill) on which depreciation claim is not allowed are subject to other forms of deduction like write-offs from taxable profits. So it is rational to expect a negative relation between size and firm's effective tax rate. The plan is to account for investment decision of companies in the form of both total assets and fixed assets to examine the relationship in Indian context. Financing cost in the form of payment of heavy interest to lenders is deductible under Income Tax Act, 1961 from book profit which further reduces tax liability. Given that interest expenditure is tax deductible while dividends are not, firms with higher leverage are expected to have lower ETR's. Gupta and Newberry (1997) find a negative relation between ETRs and leverage. Financial Leverage will examine how capital structure decision relates to tax liability. Similarly other exemption for export sales lowers the taxable profits. There is special exemption for export oriented units under Income Tax Act, 1961. Therefore export intensity is expected to find a negative association with ETR's. To account for policy changes, the attempt is to examine the relation between the schedule tax rate and ETR. The schedule tax rate is the statutory income tax rate for domestic companies on taxable profits. It was 38.5 percent for the year 2000-2001 and has been declining gradually since then. The schedule corporate tax rate is same for all companies but it can be used in the model as proxy for time specific effects as used by earlier studies too like Harris and Fenny (1999). Through various exemptions and deductions available under the Income Tax Act, companies dilute this statutory tax rates, therefore a negative relation between schedule tax rate and effective tax rate could be expected. The second statutory tax which domestic companies have to comply in India is Minimum Alternate Tax (MAT). This is the minimum taxation liability which company has to pay even if schedule tax liability is nil for the respective year. MAT provision was especially targeted to zero tax companies which otherwise through innovative reorganizing of activities do not pay any tax. This is the minimum tax which company cannot ignore. Therefore we may expect some kind of positive relation with ETR's. From the above discussion, the hypothesis can be listed as under:

- H1: ETRs are negatively associated with firm size.
H2: ETR's are negatively associated with firm financial leverage.

- H3: ETR's are negatively associated with capital intensity.
H4: ETR's are negatively associated with export intensity.
H5: ETR's are negatively associated with schedule tax rates.
H6: ETR's are positively associated with MAT.

Sample and Data

The sample consists of panel data of NSE-500 Index as on March 31, 2013 from Prowess Corporate Data base as provided by centre for monitoring Indian economy. NSE-500 Index companies have been selected to ensure balanced selection from all the industry groups.

Industry Group	No. of Companies
Manufacturing	107
Construction	17
Trading	9
Diversified	10
Automobile & Transportation	27
Real Estate	7
Service	20
Pharmaceutical	25
Consumer Goods	43
Petroleum	9
Software	16
Media	7

Table 1 : Industry Wise Breakup of Sample Companies

In order to capture higher accuracy in the model and results, those companies for which financial variables are not available for most of the years have been eliminated. This resulted in selection of 297 companies. Among these too, very few entries were still missing for some of variables. So the panel data is an unbalanced one.

Time period

A study has been undertaken by Guha (2007) to study effective tax rate in India for the period 1992-2001. The panel data for the period 2001 to 2012 has been taken to study any difference in results vis-a-vis Guha.

Regression Model

The empirical analysis involves estimating the following regression model.

$$ETR_{it} = a + b_1 Size_{it} + b_2 FL_{it} + b_3 Capinv_{it} + b_4 Expint_{it} + b_5 Trate_{it} + b_6 MAT_t$$

Where the dependent variable, ETR_{it}, is the corporate effective tax rate proxy for firm *i* in the year *t*. ETR has been taken as corporate income tax expense as ratio of profit before depreciation, interest and taxes for company *i* in year *t*. The profit before deductions and exemptions which relate to independent variable has been taken so as to capture the effect of these tax exemptions and deductions. Where negative ETR is found, it is replaced by zero and where it is greater than one, it is replaced by one so as to minimize the effect of extreme values. The independent variables include proxies for firm size (*size*) which is measured as natural logarithm of real total assets as small variance is required for correct and consistent results of the regression modeling. The size represents firm investment decision. So here it would be interesting to know how firm investment decision relates to taxation liability. Financial leverage (*FL*) which is proxy for capital structure is taken as ratio of long term debt to total assets. The proxy for assets mix is taken as ratio of net fixed asset to total assets (*capinv*). Export intensity (*Expint*) is measured as ratio between export sales to total sales. Corporate schedule tax rate (*Trate*) is calculated as corporate tax rate + surcharge + education cess if applicable for the respective year. Minimum alternative tax rate (*MAT*) is taken to study its effect on effective tax rate. Moreover schedule tax rate and *MAT* are used as proxy for time effect. These two tax rates are same across all companies but vary over time.

Analysis and Findings

Descriptive statistics

Table 2 reports descriptive statistics for dependent and independent variables over period 2001-2012.

Descriptive Statistics over Period 2001-2012					
Statistics	Mean	Median	Maximum	Minimum	Std. Devi.
ETR	0.147033	0.135620	0.913838	0.000103	0.096323
Size	9.509843	9.437500	14.89808	-1.203973	1.679863
FL	0.177798	0.141088	8.875000	0.000000	0.242321
CAPINV	0.299723	0.285463	0.911615	0.000000	0.179465
EXPINT	0.221389	0.087839	18.75908	0.000000	0.430368
TAX RATE	0.353550	0.348450	0.395500	0.324400	0.020994
MAT	0.106667	0.087500	0.190000	0.075000	0.042742

Table 2 : Descriptive Statistics

For dependent variable, effective tax rate has a mean of 0.147 and median 0.135. Although the schedule tax rate is 35 percent, companies are paying 14.7 percent as effective tax rate over the sample period. The maximum ETR is 91 percent and the minimum ETR is 0.01 percent showing huge disparity in liability owing to respective management of affairs. For independent variable size, we have taken log of absolute value. The mean value is 9.50 and median 9.43. Financial leverage observed mean value is 17.77 percent among companies that is companies on average rely on debt financing. There are instances where companies are heavily burdened with debt financing. The maximum value of financial leverage is as high as 887 percent of total assets employed by the company. The variable CAPINV finds mean value of 29.97 percent indicating thereby that on an average net fixed assets are to the tune of 30 percent of total assets of company. The export intensity has mean value 22.13 percent and median value 8.78 percent. The schedule tax rate has mean value 35.35 percent and median value 34.84 percent. MAT found a mean value 10.67 percent and median value of 8.75 percent. A reasonable level of consistency is observed between the mean and median for all variables except export intensity, which is as per expectation.

Panel Unit Root Test

The null hypothesis (H_0) is that the variable has unit root. Using Levin, Lin and Chu (t^*), Im, Pesaran and Shin (W-Stat), ADF - Fisher (Chi-square) and PP-Fisher (Chi-square), all panel data series are found to be stationary after first difference and consequently any further testing is undertaken with first difference of respective variable. The panel unit root test results are shown in Table 3. In such backdrop, ETR is now Δ ETR and similarly other variables.

Stationarity test for panel data over the period 2001-2012								
Variable	Levin, Lin and Chu t*		Im, Pesaran and Shin W-stat		ADF - Fisher Chi-square		PP - Fisher Chi-square	
	t-stat	Prob.	t-stat	Prob.	t-stat	Prob.	t-stat	Prob.
ETR	-21.1873	0.0000	-13.5297	0.0000	1154.45	0.0000	2270.14	0.0000
SIZE	22.7864	1.0000	-7.96207	0.0000	886.203	0.0000	1691.88	0.0000
FL	-4030.72	0.0000	-218.813	0.0000	1330.72	0.0000	2462.07	0.0000
CAPINV	-43.9348	0.0000	-17.2645	0.0000	1310.30	0.0000	2449.39	0.0000
EXPINT	-24.7596	0.0000	-16.3364	0.0000	1326.12	0.0000	2541.30	0.0000
TAX RATE	4.16167	1.0000	-21.7795	0.0000	1616.71	0.0000	6355.66	0.0000
MAT	-34.6122	0.0000	-14.1192	0.0000	1157.60	0.0000	895.954	0.0000

Table 3 : Stationarity Test for Panel Data

Auto Correlation test

Serial correlation (LM test) applies to macro panels with long time series (over 20-30 years). Serial correlation causes the standard errors of coefficients to be smaller than they actually are and higher R-squared as per Baltagi. We have relied on Durbin Watson test to check for auto correlation.

Multi-collinearity

Correlation test result is shown in Table 4. As shown in table, low correlation among independent variables is found and in this way all of them can be used for modeling.

Correlation Matrix							
Variable	ETR	Size	Capinv	Expint	FL	MAT	Tax Rate
ETR	1.000000	0.145951	-0.23207	-0.02186	-0.13022	0.277258	-0.24571
SIZE	0.145951	1.000000	-0.22422	0.015719	-0.07996	0.609887	-0.53354
CAPINV	-0.23207	-0.22422	1.000000	-0.09847	0.079805	-0.25676	0.231436
EXPINV	-0.02186	0.015719	-0.09847	1.000000	-0.00779	0.019973	-0.02464
FL	-0.13022	-0.07996	0.079805	-0.00779	1.000000	-0.07804	0.049376
MAT	0.277258	0.609887	-0.25676	0.019973	-0.07804	1.000000	-0.73398
TAX RATE	-0.24571	-0.53354	0.231436	-0.02464	0.049376	-0.73398	1.000000

Table 4 : Correlation Matrix

Fixed Effects vs. Random Effects Model

The rationale behind random effect model is that, the variation across entities is assumed to be random and uncorrelated with predictor/independent variable. Fixed effect models are designed to study the causes of changes within a person (entity). If we have reasons to believe that differences across entities have some influence on our dependent variable then we should use random effects. Random effects models can

include time-invariant variable like gender whereas in fixed effects model these variables are absorbed by the intercept. Random effects assume that the entity's error term is not correlated with the predictor which allows for time-invariant variables to play a role as explanatory variables. The limitation of a fixed effect model is that it parameter estimates which are conditional or sample specific, so inferences cannot be generalized. Random effect model overcomes this.

Hausman test

To decide between fixed effect or random effect model, Hausman test is performed, where null hypothesis is preferred model is random vs. the alternate the fixed effect model. It tests whether the unique errors (μ_i) are correlated with regressor. The null hypothesis is based on a central assumption of random effects estimation that the random effects are uncorrelated with explanatory variables.

The result suggest random effects model is most appropriate model among the fixed effect, random effect and simple pooled cross section time series model. There are no

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	7.299662	6	0.2940

Table 5 : Specification Test for Appropriate Panel Data Model

sufficient reasons to reject null hypothesis, so proceed to conclude that random effect model is most suitable to the selected panel data.

Regression Results

The three possible models for panel data are run, panel least square, fixed effect model and random effect model. The results are shown in Table 6, Table 7 and Table 8 respectively.

Variable	Coefficient	Std. Error	t-Statistics	Prob.
C	9.06E-05	0.001275	0.071029	0.9434
SIZE	-0.00659	0.001848	-3.565852	0.0004
CAPINV	-0.137588	0.013397	-10.26988	0
EXPINT	-0.008306	0.002975	-2.792343	0.0053
FL	-0.036899	0.005775	-6.388943	0
MAT	0.428663	0.05373	7.978135	0
TAX RATE	-0.321862	0.083378	-3.860295	0.0001
F-Statistics				0
Durbin-watson stat			2.18	

Table 6 : Panel Least Square Results

Variable	Coefficient	Std. Error	t-Statistics	Prob.
C	9.19E-05	0.001318	0.069696	0.9444
SIZE	-0.00652	0.001963	-3.32192	0.0009
CAPINV	-0.13902	0.014146	-9.82759	0
EXPINT	-0.00804	0.003087	-2.60364	0.0093
FL	-0.03592	0.005991	-5.99623	0
MAT	0.425829	0.055784	7.633535	0
TAX RATE	-0.31748	0.08626	-3.68049	0.0002
F-Statistics				0
Durbin-watson stat			2.23	

Table 7 : Fixed Assets Model Results

Variable	Coefficient	Std. Error	t-Statistics	Prob.
C	9.06E-05	0.001318	0.068736	0.9452
SIZE	-0.00659	0.00191	-3.45074	0.0006
CAPINV	-0.13759	0.013844	-9.93834	0
EXPINT	-0.00831	0.003074	-2.7022	0.0069
FL	-0.0369	0.005968	-6.18269	0
MAT	0.428663	0.055522	7.720578	0
TAX RATE	-0.32186	0.086159	-3.73567	0.0002
F-Statistics				0
Durbin-watson stat			2.18	

Table 8 : Random Effects Model Results

All three model giving significance of company characteristics with ETR. The company size which measured as natural log of real total assets is found to be negatively associated with ETR as expected in all the three models. So the result are consistent with H1 and it appears that large firms do possess superior economic and political power relative to small firms and are able to reduce their tax burdens. In addition, financial leverage is there in the model as a proxy for firm capital structure decision. The results indicate that it has a significant negative association with ETR in all three models and consistent with H2. Because companies paying financing cost in the form of interest which is tax deductible, firms with higher leverage have lower ETR. The CAPINV which is asset-mix variable has negative association with ETR, consistent with H3 and supporting the argument that investment in capital assets give huge tax exemptions to firms. These exemptions lower the effective tax liability of firms. The fourth hypothesis was exports are negatively associated with effective tax liability. In India, to boost exports, GOI apart from other assistances in the form of subsidies, provide tax exemption on income derived from exports of goods and services. In fact, tax holiday has been provided for long to export oriented units (EOU). The results under three models are consistent with hypothesis and negatively associated with ETR. The policy variables taken were schedule tax rate and MAT rate which don't vary across companies but vary over time. First discussing schedule tax rate. The hypothesis was that it is negatively associated with ETR, owing to dilution of schedule tax rate. We got consistent result. The second result on MAT liability is significant and positively associated in all three models.

Managerial and Policy Implications

The empirical work clearly points out that company's characteristics are associated with ETR and exhibits negative relation. The gap between ETR and schedule tax rate has not been reduced significantly as shown in Table 9. The average ETR is observed at 14.7 percent for NSE listed company is far below corporate face across globe. The gap between ETR and statutory tax rate is huge, nullifying the efforts to mobilize resource from corporate sector for government exchequer. If this is the results for NSE-500 Index companies then one can inference for unlisted companies. The companies publish very rosy picture of the financial affairs of the company but when it comes to contribution to exchequer, it is very meager. The reason behind is a long list of exemption and deductions available to reduce tax liability. There has been sincere attempt on reducing schedule tax rate from

more than 50 percent in 1970s to 30 percent in the last decade to encourage voluntary compliance and increase tax revenue but exemption and deduction dilute these efforts. One major policy implication follows that along with reducing tax rates, these exemptions and deduction should be abolished altogether. The MAT introduction has helped to mobilize the revenue as a mandatory policy regulation. The empirical results also showed that ETR and MAT are positively associated. Therefore MAT has helped to increase ETR over the study period. The policy suggestion is that MAT should continue to be levied. However the MAT rate can be debated under the context of economic conditions for the relevant financial year.

The corporate is a social entity and when it exploits resources of society; it should give equal in exchange. The new Companies Act 2013 makes mandatory for companies to contribute for social responsibility. There should be similar reform desired in the Income Tax Act, the policy makers should reform the tax structure so that loss of revenue through exemptions and deductions can be minimized.

Effective Tax Rates vs Schedule Tax Rate for NSE-500 Co's			
Year	ETR (%)	Schedule Tax Rate (%)	MAT (%)
2001	9.47	38.5	7.5
2002	9.50	39.55	7.5
2003	11.96	35.7	7.5
2004	12.91	36.75	7.5
2005	14.16	35.88	7.5
2006	14.65	36.59	7.5
2007	15.57	33.66	10
2008	16.12	33.99	10
2009	15.45	33.99	10
2010	17.45	33.99	15
2011	18.20	33.22	19
2012	17.86	32.44	19

Table 9 : Gap between ETR and Schedule Tax Rate over the years

Conclusion

This paper examines the determinants of the variability in corporate ETRs in India. The findings are consistent with the historical background as presented in the earlier section of the present paper except MAT which exhibits positive relation to ETR. All the three models conclude in the same manner. The empirical results found both investment and capital structure decisions

affect tax liability. We can say that companies give enough thought to future tax liability before they finalize their investment and financing decisions. The various exemption and deduction schemes available under the Income Tax Act are exploited to the extent that location of factory is decided with tax exemption schemes like SEZ, FTZ and similar other schemes. ETR is found to be associated with firm characteristics under study. We found a significant negative association between ETRs and Firm Size. We found that ETRs have a significant negative association with capital structure for leverage. A significant negative association is found between ETRs and asset mix. Export sales were also found to be negatively associated with ETRs. It may appear that political power theory is more dominant in Indian context. The companies presents financial statement as per Companies Act 1956 and report income but never publish the income reported to tax departments nor the departments comes out with such details. These tax income are not accessible. The big companies manage to have greater lobby for favorable tax exemptions. They have brains to convert the affairs of companies into tax neutral. At present, the Income Tax Act is riddled with tax concessions, which take the form of full or partial exemptions, deductions, and tax holidays. These concessions may have been justified in the era when the marginal tax rates were exorbitantly high. However, over the years the marginal tax rates have been steadily reduced substantially and corporate sector demands further reduction in tax rates. It is therefore, important to review the large number of these exemptions, deductions and tax holidays so as to expand the tax base and also increase the average tax liability. The gap between ETR and statutory tax rate is still huge, the policy makers should reform the tax structure so that the benefits of exemptions and deduction can be minimized or are available to small or needy corporate, perhaps coming Direct Tax Code bill pay the way towards it.

The study also suffers from limitations. First ETR has been taken as ratio of income tax expense and book income, the other variation that could be studied is income tax expense as ratio of operating cash flows. Second, the tax expense has been taken as tax provision shown by different companies in the annual reports. The annual reports does not provide details of corporate tax paid and various tax exemption availed by companies.

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