Volume 17, Number 1, May 2025, pp 15 – 35, Jurnal Akuntansi, Program Studi Akuntansi, Fakultas Hukum dan Bisnis Digital, Universitas Kristen Maranatha. ISSN 2085-8698 | e-ISSN 2598-4977. http://journal.maranatha.edu

Audit Quality and Tax Aggressiveness: Financial Service Companies Overview

Tajudeen Adejare Adegbite[1*]
Department of Accounting,
Al-Hikmah University, Ilorin, Kwara State
adetajud@yahoo.com
*Corresponding author

Received 8 February 2025; Revised 1 March 2025; Accepted 1 March 2025

Abstrak

Tujuan – *Studi ini menyelidiki pengaruh kualitas audit terhadap agresivitas pajak di antara perusahaan jasa keuangan yang terdaftar di Nigeria dari 2014 hingga 2023.*
Desain/Metodologi/Pendekatan – *Data yang diperoleh dari laporan tahunan perusahaan jasa keuangan terpilih dianalisis dengan analisis korelasi dan uji faktor inflasi varians untuk mendeteksi multikolinearitas sementara analisis data panel digunakan untuk pemeriksaan yang signifikan.*
Temuan – *Temuan menunjukkan bahwa tenurial audit ditemukan memiliki efek positif yang signifikan terhadap CASHETR dan BTD. Biaya audit menunjukkan efek negatif yang signifikan pada CASHETR tetapi efek positif pada BTD sementara komite audit menunjukkan efek positif yang signifikan pada CASHETR tetapi negatif pada BTD. Disimpulkan bahwa ada dampak signifikan dari kualitas audit terhadap agresivitas pajak di perusahaan jasa keuangan yang terdaftar di Nigeria.*
Keterbatasan/implikasi Penelitian – *Direkomendasikan bahwa perusahaan jasa keuangan harus memprioritaskan keterlibatan perusahaan audit berkualitas tinggi, mempertahankan masa audit yang lebih lama, dan memperkuat komite audit mereka dengan keahlian yang beragam yang akan dikaitkan dengan peningkatan keselarasan antara pelaporan keuangan dan pajak serta praktik pajak yang lebih konservatif. Badan pengatur harus mengembangkan kerangka kerja komprehensif yang akan mengintegrasikan penilaian kualitas audit, perbedaan pajak-buku, dan tarif pajak yang efektif untuk mengidentifikasi area potensial yang menjadi perhatian dengan lebih baik, dan memandu perusahaan dalam menyeimbangkan efisiensi pajak dengan kepatuhan dan kualitas pelaporan.*

Keywords: ***Komite Audit, Biaya Audit, Masa Audit, Kualitas Audit, Perbedaan Pajak-Buku, Tarif Pajak Efektif Tunai, Agresivitas Pajak***

Abstract

Purpose – The study investigates the effect of audit quality on tax aggressiveness among financial service companies listed in Nigeria from 2014 to 2023.
Design/methodology/approach – Data garnered from selected financial service companies' annual reports were analyzed with correlation analysis and variance inflation factor test to detect multicollinearity while panel data analysis was employed for significant examination.
Findings – The findings indicate that audit tenure was found to have a significant positive effect on CASHETR and BTD. Audit fees showed a significant negative effect on CASHETR but positive effect on BTD while audit committee demonstrated a significant positive effect on CASHETR but negative on BTD. It is concluded that there is significant impact of audit quality on tax aggressiveness in listed financial service companies in Nigeria.
Research limitations/implications – It is recommended that financial service companies should prioritize engaging high-quality audit firms, maintaining longer audit tenures, and strengthening their audit committees with diverse expertise which will be associated with improved alignment between financial and tax reporting as well as more conservative tax practices. Regulatory bodies should develop comprehensive frameworks that will integrate assessments of audit quality, book-tax differences, and effective tax rates for better identifying potential areas of concern, and guide companies in balancing tax efficiency with compliance and reporting quality.

Keywords: Audit Committee, Audit Fees, Audit Tenure, Audit Quality, Book-Tax Differences, Cash Effective Tax Rate, Tax Aggressiveness

Introduction

Corporate tax aggressiveness has become an important global issue. Many companies have been seeking to minimize their tax liabilities by means of various tax planning strategies by ways of either avoiding or evading tax fulfilment (Adegbite & Bojuwon, 2019; Akamah *et al*., 2018; Hoopes *et al*., 2012). Although some tax avoidance practices are lawful, excessive tax aggressiveness raises ethical and economic, as it weakens a nation's tax base and undermine concerns the nation's ability to fund public services and infrastructure (Onyali & Okafor, 2018; Rego & Wilson, 2012). Tax aggressiveness through tax avoidance according to Adegbite & Bojuwon (2019) is seen as the lawful use of the tax schemes to one's advantage, reducing the value of tax payable through methods within the tax law. In contrast, tax evasion involves illegal efforts by company management to evade taxes (Ogbeide & Iyafekhe, 2018). Effective tax planning, tax avoidance, and tax shelters have similar motives which are checkmate by the external auditor quality in order to circumvent extremity level of tax aggressiveness. Potential cause of corporate tax aggressiveness has identified by Chytis *et al.* (2019) and Monika *et al*. (2016) is the quality of external audit. Audit quality measures how well the auditor performs in auditing the financial statements of a company according to the public accountant's code of ethics and Public Accountant Professional Standard (Monika & Noviari, 2021). The quality audits according to Asri & Sunandar (2018) and Elgoplu & HizliSayinglu (2019) enhances financial statements reliability, transparency and efficiency which further serves as a blockage to aggressive tax planning.
In the past decade, the rise in corporate scandals has prompted regulators to intensely scrutinize the issues of tax aggressiveness and audit quality. Some studies suggested possible adverse impact of

audit quality on tax aggressiveness while some extant researchers advocated positive impact of audit quality on tax aggressiveness. There is a need to understand the factors that influence tax aggressiveness and identify measures to curb excessive tax avoidance practices. The quality of its external audit is a contributing factor that impacts a company's propensity towards tax aggressiveness. High-quality audits performed by reputable and independent auditors are expected to increase the reliability and transparency of financial statements, thereby reducing opportunities for aggressive tax planning (Chytis *et al*., 2019; Kanagaretnam *et al*., 2016). However, the effectiveness of audit quality in mitigating tax aggressiveness among listed financial service companies in Nigeria remains unclear. Meanwhile, prior research has demonstrated mixed and inconclusive results on the association between audit quality and tax aggressiveness. Some studies have found a negative association, suggesting that higher audit quality mitigates tax aggressiveness (Asri & Sunandar, 2018; Chytis *et al*., 2019), while others reported no significant relationship among tax aggressiveness and audit quality (Elgoplu & HizliSayinglu, 2019; De Simone *et al*., 2015).

Recent research investigating the correlation connecting audit quality and tax aggressiveness has produced varying and inconclusive findings. Furthermore, most of the research have been carried out in developed economies and their findings might not be directly relevant to the Nigerian context due to differences in institutional, regulatory, and economic environments (Appah & Ogbonna, 2014; Ezeoha & Ogbonna, 2010). Given the relance of tax revenue for economic development and the potential impact of tax aggressiveness on Nigeria's fiscal sustainability, there is a pressing need to examine the effect of audit quality on tax aggressiveness specifically among listed financial service companies in Nigeria (Adegbite & Nakajima, 2011; Edori & Ogbonna, 2017). Thus, this study, therefore, analyze the effect of audit quality on tax aggressiveness with involvement of both the cash effective tax rate; and book-tax difference in listed financial service companies in Nigeria. By addressing this knowledgeable gap, this study can produce valuable insights to policymakers, regulatory authorities, and stakeholders in the financial service sector, enabling them to develop strategies and policies to promote tax compliance and responsible corporate tax practices.

Literature Review & Hypothesis

Tax Aggressiveness

Tax aggressiveness is a legal concept created to explicit the two types of tax circumvention. The first type, tax evasion, is deemed completely illegal which is punishable by law, while tax avoidance which is the second type is considered legal but is unnecessarily desirable and typically unpunishable by law. The primary tax law focuses how to determine whether any act of tax aggressiveness violates legal standards (Adegbite, & Bojuwon, 2019). Despite this legal differentiation, many organization still deliberately avoid tax payment illegally because of their aggressiveness to downplay tax liability. Tax aggressiveness encompasses more than just distinguishing it from tax evasion and remains a somewhat ambiguous concept (Adegbite, 2020). The word tax aggressiveness is frequently used interchangeably with similar terms such as tax avoidance, tax planning, and tax shelter. However, from a precise perspective, each of these terms is used as synonyms for tax avoidance which highlights a distinct aspect of behavior. Arguably, terms like tax mitigation, tax minimization, and tax planning are the instruments of tax avoidance. According to Adegbite & Bojuwon (2019), one of the strategies adopted by the organization to aggregate profits and enhance corporate value is tax planning. Tax planning is employed by organization to minimize tax liability and maximize profit.

Effective tax planning referred as a strategy that involves recognizing all parties to a transaction and considerate all associated non-tax and tax benefits and costs. With this, tax planner (organization) avoids any actions that raise tax or non-tax costs, while leveraging legal allowances and reliefs to their full extent (Adegbite & Azeez, 2022). Tax avoidance is an intentional act of the taxpayer to pay less than it meant to pay legally. It is the legal application of tax laws' loopholes to organization's advantage, the taxpayer leverages on tax law loopholes and arranges tax liabilities in a manner that takes advantage of circumstances that were not properly defined or that bear different meaning in the tax law (Adegbite & Bojuwon, 2019).

Cash Effective Tax Rate (CASHETR)

CASHETR is tax aggressiveness measure of that focuses on actual taxes paid but not total tax expense. According to Dyreng *et al.*, (2008), it provides insights into a company's ability to reduce cash tax payments in relation to its pre-tax income. It is realized by dividing cash taxes paid with Pre-tax Income (Adegbite, 2019). Cash taxes paid is typically obtained from cash flows statement, while pre-tax income is from the income statement. A lower Cash ETR in comparison to the statutory tax rate indicate higher tax aggressiveness, but otherwise indicate lower tax aggressiveness (Adegbite, *et al.*, 2020). Cash effective tax rate remains unaffected by alterations in tax accounting accruals and but reflects a firm's actual tax payments. It also shows the impact of temporary and permanent tax avoidance approaches (Hanlon & Heitzman, 2010). Some extant researchers employed CASHETR to provide a more robust assessment of tax aggressiveness. Khurana *et al.* (2018) employed CASHETR to examine the relationship that exists between tax aggressiveness and corporate transparency which invariably discovered inverse relationship with each other. Badertscher *et al.* (2019) utilized CASHETR to investigate how tax aggressiveness affects firm value during the financial crisis. Their outcome divulged positive significant relationship between tax aggressiveness and corporate transparency.

Book-Tax Differences (BTD)

BTD refers to the discrepancies between income reported for financial accounting purposes (book income) and income reported for tax purposes (taxable income). Large BTDs are often considered an indicator of tax aggressiveness, which is the strategy using by the company to reduce its taxable income relative to its reported financial income (Hanlon & Heitzman, 2010; Adegbite & Bojuwon 2019). It is calculated by deducting taxable profit from accounting profit and divided by total Assets Larger positive BTDs generally indicate more aggressive tax planning. However, it is vital to consider both the magnitude and persistence of BTDs when assessing tax aggressiveness (Guenther *et al.*, 2021). Hasan *et al.* (2021) and Guenther *et al.*, (2021) employed BTD to study the effect of tax aggressiveness on stock price crash risk which invariably realized positive significant relationship between tax aggressiveness and corporate transparency.

Audit Quality

Audit quality can be defined as the degree of assurance and dependability offered by an audit engagement. It evaluates the effectiveness of an audit in ensuring that financial statement is accurate and comprehensive. This notion encompasses various elements, including the auditor's proficiency, impartiality, objectivity, and ethical conduct, alongside the excellence of the audit procedures and the articulation of audit results. According to Knechel and Vanstraelen (2020), the two components of audit quality are audit competence and auditor independence. For short-term audits, a reduction in quality might stem from a lack of competence or a loss of independence, whereas for long-term audits, a drop in quality is primarily associated with a loss of independence.

Watkins *et al.* (2021) delineated audit quality with auditor reputation as well as auditor monitoring competence regarding financial statements. Auditor reputation involves others' assessments, especially by financial statement users, based on the view of auditor independence and competence. Auditors perceived as highly competent and independent are deemed to produce reliable financial statements. The latter aspect of audit quality pertains to auditor monitoring competence over financial statements, where independence and competence are gauged by the quality of audited financial information. This quality is evidenced by information accuracy and the ability to mitigate biases in provided information (Watkins *et al.*, 2021; Wallace, 2018).

Hope and Langli (2018) conceptualize audit quality as auditor's execution of work with heightened objectivity and independence which defines auditor independence as the ability to maintain objectivity and resist pressures from clients, which could include both financial and non-financial influences. They emphasize that audit quality involves both the auditor's competence in detecting breaches and their willingness to report such breaches independently.

Lowe *et al.* (2018) states that a lack of independence in audit engagements diminishes objectivity and reduces the likelihood of reporting identified misstatements. ICAN divides auditor independence into independence of mind and independence in appearance, crucial for maintaining professional judgment and integrity in issuing opinions.

Audit quality, according to this study, signifies the independence of auditors from entity management control, enabling the objective identification and reporting of financial statements misstatements and errors, including instances of earnings management.

One of the primary aims of external financial reporting is to mitigate agency conflicts between firms and their stakeholders (Healy & Palepu, 2021; Hope *et al.*, 2018). The effectiveness of financial reports in reducing information asymmetries hinges significantly on their quality, with auditing intended to enhance this quality (Boone, 2020).

H0$_1$: Audit Quality Is Significantly Connected With Tax Aggressiveness In Nigeria Financial Service Companies

Audit Fees

Audit fees are often considered a representation of audit quality, based on the premise that higher fees indicate more audit effort, resources, and expertise devoted to the engagement. The relationship that exists between audit quality and audit fees is rooted in the idea that higher fees allow for more thorough and comprehensive audits. Mao et al. (2020) opined that higher audit fees significantly associated with greater audit effort, which in turn is anticipated to dispense higher audit quality. This increased effort may manifest in various ways, such as more extensive testing, the use of specialized experts, or more senior auditor involvement. Many studies support a positive connection between audit quality and audit fees. Alzoubi (2018) found that higher audit fees were absolutely connected with earnings management lower levels, suggesting improved audit quality. The author argues that increased audit fees are a sign of better audit effort and enhanced audit quality. Some researchers have proposed a non-linear relationship between audit fees and quality. Karim *et al.* (2022) found an inverted U-shaped relationship, where audit quality rises with audit fees up to a certain point, after which it begins to decline. They realized that audit fees moderate levels are connected with the highest audit quality. Kuo and Lee (2022) opined that higher audit fees might be related to more complex tax planning activities in Taiwanese firms. Halioui *et al.* (2022) discovered a positive association between audit fees and tax aggressiveness in French companies. Therefore, it is postulated that:

H0$_2$: Audit Fees Is Significantly Connected With Tax Aggressiveness In Nigeria Financial Service Companies

Audit Tenure

Audit tenure is the duration for which an auditor or audit firm has been engaged with a client. It is widely used in accounting and auditing research as a measure that can potentially influence audit quality. Connection that exists between audit quality and audit tenure has been a subject of ongoing debate and research in recent years. Audit tenure is based on two main theoretical perspectives which underpin the relationship with audit quality. Expertise hypothesis which is the first perspective suggests according to Elshawarby (2022) that longer tenure results in higher audit quality as auditors develop client-specific knowledge over time, enhancing their ability to detect misstatements while familiarity threat hypothesis posits that longer tenure may compromise auditor independence and professional skepticism, potentially reducing audit quality (Widodo *et al*., 2022). Some studies have found a positive linear connection between audit tenure and audit quality. For instance, Yustina and Gondomono (2019) examined Indonesian financial institutions and found that longer audit tenure positively affected audit quality. They argued that as auditors become more familiar with the client's business and internal control systems, they can perform more effective audits. Widodo *et al.* (2022) found that positive impact of audit tenure on audit quality was moderated by audit partner rotation. This suggests that periodic rotation of audit partners might help maintain the benefits of longer firm tenure while mitigating potential familiarity threats. Elshawarby (2022) examined Egyptian firms and found that the positive relationship between audit tenure and audit quality was stronger for industry specialist auditors. This indicates that the benefits of longer tenure might be enhanced when combined with industry expertise. Widyati *et al.* (2023) found that longer audit tenure is linked with higher audit quality and more conservative financial reporting in Indonesian companies. Asiriuwa *et al.* (2019) established that longer auditor tenure is associated with higher earnings quality and smaller book-tax differences in Nigerian firms,

H0$_3$: Audit Tenure Is Significantly Connected With Tax Aggressiveness In Nigeria Financial Service Companies

Audit Committee (AUDITCOM)

AUDITCOM plays a dynamic role in guaranteeing audit quality within an organization. As a subcommittee of the board of directors, it is saddled with responsibility of oversight of financial reporting process, external audit function and internal controls (Ghafran & Yasmin, 2018). The effectiveness and usefulness of the audit committee is frequently regarded as a critical determinant of audit quality, as it directly impacts the trustworthiness and dependability of financial reporting. Pertinent way in which an audit committee contributes to audit quality is through its independence and expertise. A well-structured audit committee will usually consists of independent directors with relevant financial and industry knowledge. This independence helps ensure objective oversight of the audit process and reduces the risk of management influence (Sultana *et al.*, 2019). Research has shown that audit committees which embedded with financial professionals are more likely to detect and prevent financial reporting irregularities, thereby enhancing audit quality (Bilal *et al*., 2018; Adegbite, 2019).

The audit committee's responsibility is to appoint, oversee and compensate external auditors work. This oversight function involves carrying out an evaluation of the auditor's independence, discussing the audit scope and approach, and reviewing the results of the audit (Lisic *et al.*, 2019). By maintaining a direct line of communication with external auditors, the audit committee can tackle potential issues promptly and ensure a thorough and high-quality audit process. Effective internal controls are critical for reliable financial reporting. The audit committee displays a key responsibility in monitoring and evaluating the effectiveness of internal control systems. By regularly reviewing internal control processes and addressing any weaknesses, the audit committee contributes to improved audit quality and reduced risk of material misstatements (Alzeban & Sawan, 2020). Zandi *et al.* (2020) advocated that audit committee characteristics are linked with less tax avoidance in Malaysian companies. Pratama (2022) also found that stronger corporate governance, including audit committee effectiveness, is associated with less tax avoidance in Indonesian firms.

$H0_4$: Audit Committee Is Significantly Connected With Tax Aggressiveness In Nigeria Financial Service Companies

Theoretical Review

Agency Theory

Jensen and Meckling introduced this theory in 1976, and since then, it has become widely utilized in management and social sciences (Ezelibe *et al*., 2018). The theory examines the dynamic between investors which is either owners or shareholders, and managers. It posits that the agency connection functions as an agreement where one individual or more (principal(s)) enlist another person (agent) to accomplish services on principal behalf, thereby granting decision-making right to the employed agent. This delegation of authority results in the principal acquiring certain costs, known as agency costs. According to Jensen and Meckling (1976), these costs arise from the differing interests of agents and principals in the principal-agent relationship. The agency relationship exacerbates the issue of information asymmetry because managers typically have greater access to information compared to shareholders. To alleviate this, Jensen and Meckling (1976) advocated that owners launch monitoring devices in order to execute oversight functions. Higher audit quality and high transparency to the investors is therefore a sufficient method of alleviating agency problem. To sustain a high audit quality, auditor is employed based on the interests of shareholders, third parties and managers. According to the theory, auditor is appointed to administer the connection that exists amid them. The auditor is irresponsibility for the process of accounting, but responsible credible financial statements presented to the stakeholders by the manager for effective decisions making.

To maximize their personal interests, such as receiving higher bonuses or stock options, managers may engage in tax aggressiveness at the expense of shareholders' interests. High-quality audits can mitigate this agency problem by providing an independent assessment of the establishment's tax positions and financial statements, thereby reducing the likelihood of opportunistic behavior by managers (El-Mahdy & Beecher, 2019). Agency theory has been widely adopted in numerous studies, indicating its broad acceptance and applicability. However, its scope is limited to the agent-principal relationship and does not encompass other stakeholders within an organization, such as suppliers, creditors, and the broader environmental context in which the organization operates.

Empirical Review

This section reviews empirical studies examining the correlation between audit quality and tax aggressiveness across developed countries, developing countries, and specifically within Nigeria.

Chyz *et al.* (2021) investigated the moderating role of industry concentration on the link between audit quality and tax aggressiveness. They found that companies with higher-quality audits are less tax aggressive, and this effect is more notable in concentrated industries where tax aggressiveness is more likely to be detected and scrutinized. This study highlights the relevance of considering industry dynamics when examining audit quality effect on tax aggressiveness. Furthermore, Lim (2022) carried out a meta-analysis of studies from the United States and reported a significant negative association amid tax aggressiveness and audit quality, supporting the notion that high-quality audits can mitigate aggressive tax planning practices in American firms.

In Australia, Kanagaretnam *et al.* (2020) examined auditor industry specialization effect on tax aggressiveness and found that companies that were audited by industry specialist auditors are less tax aggressive when compared with those that are audited by non-specialist auditors. This finding reinforces the idea that auditor industry expertise can enhance audit quality and, consequently, mitigate tax aggressiveness.

Bauer (2020) reported a negative association amid tax aggressiveness and audit quality indicating that higher-quality audits can effectively constrain aggressive tax planning practices in Canadian firms. Similarly, Xu *et al.* (2020) established that audit quality, represented by industry specialization and audit firm size was negatively connected with Canadian tax aggressiveness. Luo and Zhou (2022) examined the link among tax aggressiveness and audit quality in firms from various European countries. They established a negative connection between tax aggressiveness and audit quality, signifying that high audit quality ignited a crucial efforts in tumbling tax aggressiveness across European nations.

Adegbite and Bojuwon (2019) investigated tax avoidance effect in Nigeria listed firms in Nigeria. The study advocated that corporate tax avoidance strategies engaged by Nigerian firms aggressively reduced Nigeria firms' tax liabilities. In the same vein, Adediran *et al.* (2018) examined the link amongst tax aggressiveness and corporate governance in listed Nigerian firms. While their study did not find a significant association between tax aggressiveness and audit quality, they highlighted the need for further research to understand the specific dynamics of this relationship in the Nigerian context. Akinyomi *et al.* (2022) focused on listed manufacturing firms in Nigeria and found a negative connection amid tax aggressiveness and audit quality. Their study suggests that higher-quality audits can mitigate aggressive tax planning practices in Nigerian manufacturing sector. The authors attribute this finding to the role of auditors in ensuring compliance with tax regulations and enhancing transparency in financial reporting.

Nnadi and Akpomi (2021) investigated corporate governance mechanisms effect on tax aggressiveness in listed Nigerian firms. While their study did not specifically investigate audit quality, they realized a positive connection amid tax aggressiveness and managerial ownership, supporting the agency theory prediction that managers should adopt tax aggressiveness to maximize their personal interests. Okougbo (2020) examined corporate social responsibility (CSR) effect on Nigerian firms' tax aggressiveness. The study found that firms with higher CSR engagement tend to be less tax aggressive, suggesting that stakeholder considerations influence tax decisions. However, the study did not specifically examine audit quality role in this relationship. Oladipupo and Obazee (2021) examined audit quality impact on tax avoidance in Nigerian deposit money banks. They found a negative relationship amid tax avoidance and audit quality indicating that higher-quality audits can effectively constrain aggressive tax planning practices in Nigerian banking sector.

Gaps in Literatures

Conceptually, few studies in Nigeria examined the relationship between audit quality and tax aggressiveness in Nigeria with mixed outcomes which indicating the need for further research to understand the specific dynamics in the Nigerian context, particularly in the financial service sector. The literatures examined acknowledge that certain factors unique to Nigeria, such as limited availability of skilled auditors, corruption, weak regulatory environment, complex tax laws, political interference, and limited access to information, may impact the relationship between audit quality and tax aggressiveness. However, most of the reviewed studies do not explicitly consider or examine the influence of these factors. While the review mentions that various factors, such as regulatory environment, corporate governance, auditor independence, firm culture, and industry factors, may affect the relationship between audit quality and tax aggressiveness, few studies have explicitly investigated the moderating or mediating effects of these factors in the Nigerian context.

Methodologically, most of the extant studies relied on regression analysis to examine the relationship between audit quality and tax aggressiveness which ignited an opportunity to explore alternative methodologies, such as experimental research analysis like panel data analysis through random and fixed effect models as well as Hausman test with other post estimation test in this regard to provide additional insights into this relationship. Lastly, the extant studies that combined both BTD and CASHETR to gauge tax aggressiveness are scarce among the literatures. Most of the existing researchers employed only one out of BTD and CASHETR as a proxy of tax aggressiveness.

Research Method

The study utilized secondary sources for data collection. Specifically, data were gathered from annual reports and financial accounts of listed financial services companies from 2014 to 2023. Nigeria stock exchange (NSE) Fact Book was used to extract the listed financial services companies for the selected periods. The decision to use secondary data in this study is driven by the quantitative research methodology, which necessitates quantitative data to test research hypotheses. Data relevant to the variables of the study were extracted from the financial statements of individual companies and NSE Fact Book. Regarding data analysis, the panel data models were employed which split into fixed effects and random effects where Hausman gauges appropriate model (Adegbite, 2024). This choice is motivated by the dataset consisting of a cross-section of 10 companies over a time series spanning 10 years approximately.

Model Specification

To analyse the effect of audit quality on tax aggressiveness on Nigeria financial services companies, audit quality was tagged as an independent variable, which is the quality of audits measured using auditor type, audit committee and audit fee as proxies while tax aggressiveness is represented by two variables which are CASHETR and BTD.

Model I

This model examines the effect of audit quality on Cash Effective Tax rate (CASHETR)

CASHETR = f(Audit Quality) 1

CASHETR = β_0 + β_1AUDITTR + β_2AUDITFEE + β_3 AUDITCOM + β_4FIRMSZ + β_5LEVERAGE + ε **2**

Fixed Effect Model

Yit = βXit + αi + $u$it **3**

CASHETR it = β_0 + β_1AUDITTR $_{it}$ + β_2AUDITFEE $_{it}$ + β_3 AUDITCOM$_{it}$ + β_4FIRMSZ$_{it}$ + β_5LEVERAGE$_{it}$ + y_2E2 +…+ ynEn + $u$it **4**

CASHETR it = β_0 + β_1AUDITTR$_{it}$ + β_2AUDITFEE$_{it}$ + β_3 AUDITCOM$_{it}$ + β_4FIRMSZ$_{it}$ + β_5LEVERAGE$_{it}$ + y_2E2 +…+ ynEn + δ2T2 +…+ δtTt + $u$it **5**

Random Effect Model

CASHETR it = β_0 + β_1AUDITTR$_{it}$ + β_2AUDITFEE$_{it}$ + β_3 AUDITCOM$_{it}$ + β_4FIRMSZ$_{it}$ + β_5LEVERAGE$_{it}$ + y_2E2 +…+ ynEn + $u$it + εit **6**

Model 2

This model examines the effect of udit quality on Book-Tax Differences (BTD)

BTD = f(Audit Quality) **7**

BTD = f(AUDITTYPE, AUDITTENURE, AUDITFEE, AUDITCOMMITTE, FIRMSIZE, LEVERAGE) **8**

BTD = β_0 + β_1AUDITTR + β_2AUDITFEE + β_3 AUDITCOM + β_4FIRMSZ + β_5LEVERAGE + ε **9**

Fixed Effect Model

BTDit = β_0 + β_1AUDITTR $_{it}$ + β_2AUDITFEE $_{it}$ + β_3 AUDITCOM$_{it}$ + β_4FIRMSZ$_{it}$ + β_5LEVERAGE$_{it}$ + y_2E2 +…+ ynEn + $u$it **10**

BTDit = β_0 + β_1AUDITTR$_{it}$ + β_2AUDITFEE$_{it}$ + β_3 AUDITCOM$_{it}$ + β_4FIRMSZ$_{it}$ + β_5LEVERAGE$_{it}$ + y_2E2 +…+ ynEn + δ2T2 +…+ δtTt + $u$it **11**

Random Effect Model

BTDit = β_0 + β_1AUDITTR$_{it}$ + β_2AUDITFEE$_{it}$ + β_3 AUDITCOM$_{it}$ + β_4FIRMSZ$_{it}$ + β_5LEVERAGE$_{it}$ + y_2E2 +…+ ynEn + $u$it + εit **12**

Results and Discussion

1. Effect Of Audit Quality On Effective Tax Rate In Nigeria Listed Financial Service Companies

This section examines the impact of audit quality on tax aggressiveness using CASHETR as proxy. Various statistical models were used to analyze the relationship, including correlation analysis, pooled regression, fixed effects regression, and random effects Generalized Least Squares (GLS) regression.

Table 1
Correlation Matrix

	CASHETR	AUDITTR	AUDITFEE	AUDITCOM	FIRMSZ	LEVERAGE
CASHETR	1.0000					
AUDITTR	-0.1005	1.0000				
AUDITFEE	-0.6564*	0.1952	1.0000			
AUDITCOM	-0.1193	0.3046*	0.1411	1.0000		
FIRMSZ	-0.2961*	-0.0501	-0.5961*	-0.1448	1.0000	
LEVERAGE	0.2428*	0.0500	0.5697*	0.1665	-0.9247*	1.0000

Source: Authors' Compilation (2024)

A correlation matrix was examined to explore the relationships among the variables. It was observed that FIRMSZ has a moderate negative correlation with

CASHETR, with a coefficient of -0.2961, suggesting no significant collinearity between CASHETR and FIRMSZ. Additionally, AUDITTR shows a weak negative association with CASHETR (-0.1005), while AUDITFEE has a strong negative association with CASHETR (-0.6564), indicating it is indispensable expenses which reduces CASHETR. AUDITCOM presents a weak negative correlation with CASHETR (-0.1193), and LEVERAGE displays a weak positive correlation with CASHETR (0.2428). Since most correlations are below 0.7, there is generally no strong collinearity between CASHETR and the other variables, except for AUDITFEE. The strong correlation between AUDITFEE and CASHETR, as well as the very strong negative correlation between FIRMSZ and LEVERAGE (-0.9247), may require further examination. Thus, based on the correlation matrix results, performing a VIF (Variance Inflation Factor) test would be advisable to evaluate collinearity among the variables.

Table 2
Variance Inflation Factor (VIF)

Variable	VIF	1/ VIF
FIRMSZ	7.28	0.137451
LEVERAGE	6.98	0.143225
AUDITFEE	1.63	0.615077
AUDITTR	1.15	0.872021
AUDITCOM	1.13	0.883547
Mean VIF	3.63	

Source: Authors' Compilation (2024)

VIF test was conducted to assess the presence of high correlation among predictors. The results indicate that multicollinearity is not a significant concern for the variables used in this study, as all VIF values in Table 2 are below the critical threshold of 10. FIRMSZ exhibits the highest VIF at 7.28, closely followed by LEVERAGE at 6.98. AUDITFEE shows a moderate VIF of 1.63, while AUDITTR and AUDITCOM demonstrate low VIFs of 1.15 and 1.13 respectively. The mean VIF across all variables is 3.63, which is considerably below the level of concern. These findings suggest that the variables in the model do not suffer from problematic levels of multicollinearity.

Table 3
Effects of Audit Quality on Effective Tax Rate (Using Different Models)

	(1)	(2)	(3)	(4)
CASHETR	Regression	Linear Regression	Fixed-Effects (Within) Regression	Random-Effects GLS Regression
AUDITTR	0.00256	0.00256	0.00494***	0.00316*
	(0.162)	(0.135)	(0.008)	(0.068)
AUDITFEE	5.25e-08	5.25e-08	-0.0153**	-9.09e-09
	(0.133)	(0.154)	(0.028)	(0.848)
AUDITCOM	0.0285***	0.0285***	0.0201**	0.0280***
	(0.001)	(0.001)	(0.017)	(0.000)

FIRMSZ	4.8258	4.8258	1.3918***	6.4543
	(0.202)	(0.302)	(0.007)	(0.126)
LEVERAGE	0.0825**	0.0825**	0.289***	0.129***
	(0.029)	(0.027)	(0.000)	(0.010)
_cons	-0.200***	-0.200***	-0.278***	-0.221***
	(0.000)	(0.000)	(0.000)	(0.000)
N	100	100	100	100
R^2	0.322	0.322	0.357	
adj. R^2	0.286	0.286	0.251	

Source Authors' Compilation (2024)

In Table 3, various analytical methods were employed to assess the impact of audit quality on the effective tax rate (CASHETR). The first column presents the pooled regression outcomes of the analytical model. However, to address potential issues like heteroskedasticity, Linear Regression (Robust) was employed, as shown in column According to the Robust Regression results, audit tenure (AUDITTR) and audit fees (AUDITFEE) do not have significant effects on ETR. The audit committee (AUDITCOM) has a significant positive effect on CASHETR. Firm size (FIRMSZ) does not show a significant effect, while LEVERAGE has a significant positive effect on CASHETR at the 0.05 level. The fixed effect regression model and the random effect model were also tested, as shown in columns 3 and 4 respectively. A Hausman test was conducted to determine the suitable model between fixed and random effect model. According to the Hausman test in Table 6, the fixed effect was deemed suitable because Prob>chi2 = 0.0078, which is less than the 0.05 significance level. This result rejects the null hypothesis that the random effects model is appropriate. Based on the Fixed Effects model audit tenure (AUDITTR) has a significant positive effect on CASHETR a percentage increase in audit tenure increases CASHETR by approximately 0.00494%. Audit fees (AUDITFEE) have a significant negative effect on CASHETR at the 0.05 level the audit committee (AUDITCOM) has a positive effect on CASHETR, significant at the 0.05 level a percentage increase in the audit committee measure increases CASHETR by approximately 0.0201%. Firm size (FIRMSZ) has a significant positive effect on CASHETR at the 0.01 level. LEVERAGE has a significant positive effect on CASHETR a percentage increase in LEVERAGE increases CASHETR by approximately 0.289%.

Table 4
Hausman Test For CASHETR

	(b) Fixed Effect	(B) Random Effect	(b-B) Difference	sqrt(diag(V_b-V_B))S.E.
AUDITTR	.0049433	.003164	.0017793	.0005637
AUDITFEE	-1.53e-07	-9.09e-09	-1.44e-07	4.94e-08
AUDITCOM	.0200845	.0279815	-.007897	.0025799
FIRMSZ	1.39e+07	6454381	7464015	2805174

LEVERAGE	.2891196	.1286751	.1604445	.0568109

chi2(1) = (b-B)'[(V_b-V_B)^(-1)](b-B)
= 7.08
Prob>chi2 = 0.0078
(V_b-V_B is not positive definite)

Source: Authors Compilation (2024)

2. The Effect of Audit Quality on Book Tax Difference in Nigeria listed financial service companies

This section examines the impact of audit quality on tax aggressiveness using BTD as proxy. Various statistical models were used to analyze the relationship, including correlation analysis, pooled regression, fixed effects regression, and random effects Generalized Least Squares (GLS) regression.

Table 5
Correlation Matrix

	BTD	AUDITTR	AUDITFEE	AUDITCOM	FIRMSZ	LEVERAGE
BTD	1.0000					
AUDITTR	-0.1354	1.0000				
AUDITFEE	-0.5462*	0.1952	1.0000			
AUDITCOM	-0.3321	0.3046*	0.1411	1.0000		
FIRMSZ	-0.4256*	-0.0501	-0.5961*	-0.1448	1.0000	
LEVERAGE	0.2876*	0.0500	0.5697*	0.1665	-0.9247*	1.0000

Source Authors' Compilation (2024)

A correlation matrix was analyzed to investigate the interrelationships among the variables. It was found that AUDITTR shows a weak negative correlation with BTD (-0.1354), while AUDITFEE exhibits a strong negative correlation (-0.5462*) with BTD, suggesting potential collinearity. AUDITCOM shows a weak negative correlation with BTD (-0.3321), and LEVERAGE has a weak positive correlation (0.2876*) with BTD. Since most correlations are below 0.7, there is generally no strong collinearity among BTD and the other variables, except for AUDITFEE. The strong correlation between AUDITFEE and BTD, as well as the very strong negative correlation between FIRMSZ and LEVERAGE (-0.9247), may warrant further investigation. BTD has a moderate negative association with FIRMSZ, with a coefficient of -0.4256. This indicates that there is no significant collinearity between BTD and FIRMSZ. Therefore, based on the results of this correlation matrix, conducting a VIF (Variance Inflation Factor) test would be appropriate to assess collinearity among the variables.

Table 6
Variance Inflation Factor (VIF)

Variable	VIF	1/ VIF
FIRMSZ	7.28	0.137451
LEVERAGE	6.98	0.143225
AUDITFEE	1.63	0.615077
AUDITTR	1.15	0.872021
AUDITCOM	1.13	0.883547
Mean VIF	3.63	

Source: Authors' Compilation (2024)

VIF was tested to examine the presence of multicollinearity. All variables used in this study exhibit no significant multicollinearity because the values in Table 2 are less than 10. The highest VIF value is for FIRMSZ at 7.28, followed closely by LEVERAGE at 6.98. AUDITFEE has a moderate VIF of 1.63, while AUDITTR and AUDITCOM have low VIFs of 1.15 and 1.13 respectively. The mean VIF for all variables is 3.63, which is well below the threshold of concern. This shows that multicollinearity is not a major issue in this set of variables.

Table 7
Effects Of Audit Quality On Book Tax Difference Using Different Models

BTD	(1) Regression	(2) Linear Regression	(3) Fixed-effects (within) Regression	(4) Random-effects GLS Regression
AUDITTR	-2.5610***	-2.5610***	-2.4766**	-2.5582***
	(0.007)	(0.004)	(0.021)	(0.006)
AUDITFEE	1607.0***	1607.0***	1625.4***	1607.3***
	(0.000)	(0.000)	(0.000)	(0.000)
AUDITCOM	-7.5588*	-7.5588*	-9.8081**	-7.6098*
	(0.067)	(0.094)	(0.042)	(0.062)
FIRMSZ	-1.00844e+16	-1.00844e+16	-9.65449e+15	-1.0132
	(0.599)	(0.516)	(0.742)	(0.597)
LEVERAGE	-2.8670	-2.8671**	-2.0417	-2.86807379.3
	(0.132)	(0.019)	(0.641)	(0.131)
_cons	6.3222**	63222*	6.9547	6.3516**
	(0.024)	(0.015)	(0.053)	(0.022)
N	100	100	100	100
R^2	0.535	0.535	0.306	
adj. R^2	0.511	0.511	0.192	

Source: Authors' Compilation (2024)

In Table 7, various analytical tools were adopted to examine the effect of audit quality on book tax difference (BTD). The first column presents the pooled regression outcomes of the analytical model. However, to address potential issues like heteroscedasticity, Linear Regression (Robust) was employed. According to the Robust Regression results, audit tenure (AUDITTR) has a significant negative effect on BTD. Audit fees (AUDITFEE) show a significant positive effect on BTD. The audit committee (AUDITCOM) has a negative effect on BTD, firm size (FIRMSZ) does not show a significant effect, while LEVERAGE is significant and negative in the robust model. The fixed effect regression model and the random effect model were also tested, as shown in columns 3 and 4 respectively. A Hausman test was conducted to determine the suitable model between fixed and random effect models. The result from the Hausman test in Table 7 indicates that the random effect model was considered appropriate because Prob>chi^2 = 0.9827, which is much higher than the conventional 0.05 significance level. This result fails to reject the null hypothesis that the random effects model is appropriate. According to the Random Effects model Audit tenure (AUDITTR) has a significant negative effect on BTD, a percentage increase in audit tenure decreases BTD by approximately 2.56%. Audit fees (AUDITFEE) have a significant positive effect on BTD at the 0.01 level a percentage increase in audit fees increases BTD by about 1.607%. The audit committee (AUDITCOM) has a negative effect on BTD, significant at the 10% level; a percentage increase in the audit committee measure decreases BTD by approximately 7.61%. Firm size (FIRMSZ) and LEVERAGE do not show significant effects on BTD in the random effects model.

Table 8
Hausman Test For BTD

	(b) Fixed-effect	(B) Random-effect	(b-B) Difference	sqrt(diag(V_b-V_B)) S.E.
AUDITTR	-2.48e+07	-2.56e+07	816565.1	5074016
AUDITFEE	1625.356	1607.337	18.01892	352.7924
AUDITCOM	-9.81e+07	-7.61e+07	-2.20e+07	2.43e+07
FIRMSZ	-9.65e+15	-1.01e+16	4.78e+14	2.21e+16
LEVERAGE	-2.04e+08	-2.87e+08	8.26e+07	3.93e+08

chi2(1) = (b-B)'[(V_b-V_B)^(-1)](b-B)
= 0.00
Prob>chi2 = 0.9827

Source: Authors' Compilation (2024)

Discussion of Findings

This study examines the effect of audit quality on tax aggressiveness in listed financial service companies in Nigeria. The data collected from annual published reports were analyzed using multiple regression models, with the fixed effects model confirmed as appropriate by the Hausman test for the analysis of cash effective tax rate (CASHETR), while the random effects model was deemed suitable for book-tax difference (BTD) analysis.

Audit tenure (AUDITTR) was found to have a significant positive effect on CASHETR. The Policy implementation is that longer audit engagements may lead to higher effective tax rates, possibly due to improved audit quality and more conservative tax positions. This finding aligns with the results of Asiriuwa *et al.* (2019); Elshawarby (2022); Yustina & Gondomono (2019); and Widyati *et al.* (2023) but against the views of Halioui *et al.* (2022), Adegbite & Shittu (2018); Adegbite & Araoye (2018) and Pratama (2022). Audit fees (AUDITFEE) showed a significant negative effect on CASHETR. This suggests that higher audit fees may be linked with more aggressive tax planning strategies, resulting in lower effective tax rates. This outcome is consistent with the findings of Hendi & Sherly (2024); Kuo & Lee (2022); Yustina & Gondomono (2019); & Idyati *et al.* (2023) but rejected the submission of

Asiriuwa *et al.* (2019); Adegbite & Bojuwon (2019) and Elshawarby (2022). The audit committee (AUDITCOM) demonstrated a significant positive effect on CASHETR. This indicates that a more effective audit committee may lead to more conservative tax practices and higher effective tax rates. This result supports the findings of Zandi *et al.* (2020); Halioui *et al.* (2022); Pratama (2022); and Yustina & Gondomono (2019).

Audit tenure (AUDITTR) showed a significant negative effect on BTD. The policy implementation is that longer audit engagements may lead to smaller BTDs, possibly as a result of improved alignment between financial and tax reporting. This finding is in line with the research of Hendi & Sherly (2024); Asiriuwa *et al.* (2019); Elshawarby (2022); Yustina & Gondomono (2019); and Widyati *et al.* (2023) but against the views of Halioui *et al.* (2022) and Pratama (2022). Audit fees (AUDITFEE) demonstrated a significant positive effect on BTD. This suggests that higher audit fees may be associated with larger book-tax differences, possibly due to more complex financial and tax reporting structures. This result is consistent with the findings of Halioui *et al.* (2022); Hendi & Sherly (2024); Kuo & Lee (2022); Yustina & Gondomono (2019); and Widyati *et al.* (2023) but rejected the submission of Asiriuwa *et al.* (2019) and Elshawarby (2022). The audit committee (AUDITCOM) showed a negative effect on BTD. This suggests that more effective audit committee may result to smaller book-tax differences, possibly through improved oversight of financial and tax reporting. This outcome supports the research of Zandi *et al.* (2020); Halioui *et al.* (2022); Pratama (2022); and Yustina & Gondomono (2019).

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Conclusion and Recommendation

This study was conducted to examine the effect of audit quality on tax aggressiveness of listed financial service companies in Nigeria. It shows that panel data regression model was used and the data were collected from ten financial service companies over ten years where hundred (100) observation were obtained. The data were gathered from annual financial reports of ten financial service companies in Nigeria from 2014 to 2023. A panel data was adopted to analyze the data and to examine the effect of audit quality on tax aggressiveness in financial service companies in Nigeria. A panel data analysis included pooled regression fixed effect regression, random effects GLS regression, Robust and Linear regression as well as Hausman test.

Following the outcome of the study, after the thorough scrutinizing of the data with panel data analysis models such as Random effect model and fixed effects model, it was concluded that audit quality has significant impact on tax aggressiveness in listed financial service companies in Nigeria. Effective Tax Rate (ETR) has a positive correlation with audit tenure and audit committee, while it has a negative correlation with audit fees. It was also discovered that Book-Tax Difference (BTD) possessed a negative relationship with audit tenure and audit committee. More so, audit fees demonstrated a positive relationship with BTD. Therefore, it is concluded that there is significant impact of audit quality on tax aggressiveness in listed financial service companies in Nigeria. It is recommended based on the study's findings that financial service companies should prioritize engaging high-quality audit firms, maintaining longer audit tenures, and strengthening their audit committees with diverse expertise which will be associated with improved alignment between financial and tax reporting as well as more conservative tax practices. Regulatory bodies should develop comprehensive frameworks that will integrate assessments of audit quality, book-tax differences, and effective tax rates for better identifying potential areas of concern, and guide companies in balancing tax efficiency with compliance and reporting quality.

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