



## **EARNINGS MANAGEMENT AND DIVIDEND PAYOUT OF NIGERIAN LISTED MONEY DEPOSIT BANKS**

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### **Abstract**

*Banks in Nigeria are exposed to liquidity and solvency problems due to huge non-performing loans yet they can manage to pay dividend. This study examines whether dividend payout, profitability, tax rate and size influences earnings management of Nigerian listed deposit money banks. The research is a post-positivism paradigm that relied on secondary sources of data extracted from the financial statements of the banks that made the sample of the study. The population of the study is the 14 listed money deposit banks in Nigeria for period ranging from 2010 to 2019. Regression techniques aided the analysis of data. Findings revealed that Dividend payout, profitability, size and tax rate influences earnings management of deposit banks at less than 1% level of significance. Based on the finding, the study concludes that banks manipulate profit in order to pay less tax and more dividend despite its liquidity problems and the existence of huge nonperforming loans. The study recommends the sustainability of CBN policy on liquidity position and thresholds regarding payment of dividend. Secondly the study recommends that banks pursue a conservative working capital management policy that will secure their future liquidity position.*

**Keywords:** *Earnings Management, Dividend Payout, Profitability, Tax Rate*

### **1. Introduction**

Paying tax and dividends as at when due by banks is an indication that they are profitable, and this attracts potential investors and sustains existing shareholders. This has been seen to be true with companies that pay regular dividends (Colombo, 2021; Mamaro & Tjano, 2019). However, over the years without necessarily retaining earnings to increase investment or capital against operational risk most banks in Nigeria preferably and regularly paid dividends to their shareholders. Alhadab and Al-own (2017) state that banks manipulate their loan loss provision to report inflated earnings, and this negatively affects banks' current and future performance. In 2019 the CBN restricted the payment of dividends subject to certain threshold, thus some banks could not pay dividend for 2018 financial year. As mentioned earlier, in order to sustain steady dividend payment, banks have to maintain their profit. Jahanzaib, Ali and Sadiq (2012) establish that in condition of inconsistent earnings such as losses or much bigger profits, the management tends to smooth their earnings to report profit to pay dividend.



Ahmed, Mohammed and Adisa (2014); Ali (2015) establish that banks in Nigeria actually use loan loss provisions to manage earnings. This is why Akenbor & Ibanichukwu (2012) empirically conclude that Nigerian banks practice earnings management to boost the market value of their shares.

Additionally, literature has evidenced that earnings management is a function of size (Kothari, Leon & Wasley, 2005). More so, Aini, Takiah, Pourjalali and Teruya, (2006), Watts and Zimmerman (1990) observed that size of a firm determines earnings management; larger firms might have more reasons to manage earnings than smaller firms. Furthermore, profitability is a determinant to paying company income tax and Hepworth (1953) showed that tax is one of the several reasons that make management to smooth earnings. Lin, Thaker and Khaliq (2018), Pandey and Mansuri (2017), Arif and Akbar (2013) indicated that tax rate influences dividend payout of firms. Thus, the current study is different from the reviewed previous studies and it tries to examine dividend payout and earnings of money deposit banks in Nigeria for the period 2010 -2019. Management of banks will benefit from the findings of this study on the policy to adopt and strategy to employ on efficiency and liquidity management. Also, regulators like the CBN and SEC will find the findings of this study as empirical evidence that supports their policy efforts on quality earnings in the banking sector.

The objective of this study to find out whether dividend payout, profitability, tax rate and size of banks influence earnings management. The following hypotheses were formulated and tested based on the objective:

- H<sub>1</sub>:** Dividend Payout (**DP**) is not significantly related to earnings management of listed deposit money banks in Nigeria.
- H<sub>2</sub>:** Profitability (**PR**) is not significantly related to earnings management of listed deposit money banks in Nigeria.
- H<sub>3</sub>:** Size (**SZ**) is not significantly related to earnings management of listed deposit money banks in Nigeria.
- H<sub>4</sub>:** Tax rate (**TR**) is not significantly related to earnings management of listed deposit money banks in Nigeria.

## 2. Literature Review and Theory

### Conceptualization of the Study Variables

**Earnings Management-EM:** This study explains EM as controlling of stated earnings by using specific accounting methods to attain stable and predictable business results. It is a deliberate measure used by management to report that the business is doing well. In order to avoid undesirable net income, banks seek income smoothing (Bornemann, Kick, Memmel, & Pfungsten 2012; Bortoluzzo Sheng & Gome, 2015). They pursue to spend more to draw better outcome (Ahmed, Takeda, Thomas 1999; Kanagaretnam, Lobo & Yang 2005). Anandarajan, Hassan and Vivas (2003); El Sood (2012); Ali, (2015); Farouk and Isa (2018) prove that banks use loan loss provisions to indulge in earnings management practices.

**Dividend Payout-DP:** This study defines DP as the unearned income paid to an investor after deducting tax from net income. The following study evidenced dividend payout influences earnings management (Edelstein, Liu & Tsang, 2009; Shah, Yuan & Zafar, 2010; Jahanzaib *et al.*, 2012; Moghri & Galogah, 2013; Aladwan, 2019). Particularly with lower information asymmetry



dividend policy determines earnings management (Nguyen & Bui, 2019; He, Lilian, Zaiat & Zang, 2012). However, the studies of Ajide and Aderemi 2014; Aurangzeb and Dilawer, 2012 and Savov (2006) evidence that dividend payout has no influence on earning management.

**Profitability-PR:** This study defines PR as when expenses and entitlements are absorbed by a company's income. Some studies evidenced that low profit influences earnings management Alhadab and Al-own, (2017); Kothari, Mizik & Roychowdhury, 2016; Cohen & Zarowin, 2010; Doyle, Ge and McVay, (2007) Lee, Li and Yue (2006); Kim, Liu and Rhee (2003). While other studies proved it is not (Ardekani, Nejat & Hashemijo, 2012; De Angelo, De Angelo & Skinner, 1994).

**Size-SZ:** This study defines as the total existing amount of assets owned by a company. Findings of Jahmani and Niranjani (2015) revealed that the size of a firm relates significantly to earnings management. More so, studies of Aini, Takiah, Pourjalali and Teruya (2006) establish that larger firms have more interest in managing earnings. Kim, Liu and Rhee (2003) show that larger firm considers the implication of earnings management on their reputation while smaller firms manage earnings to avoid reporting loses. However, Gu, Lee and Rosett (2005) observe that size of a firm does not attract earnings management.

**Tax Rate TR:** This study defines TR as the amount of money charged on net income and remitted to the federal Inland Revenue services FIRS on a preceding Year basis. Edelstein *et al.* (2009) and Aini, Takiah, Pourjalali and Teruya (2006) prove that tax rate influences earnings management by companies manipulating profit to pay less tax.

### **Related Empirical Studies**

All the related studies reviewed in this section are of the post positivism paradigm that relied on quantitative data as evidence to establish their findings. This implies that these studies data source is strictly secondary and the literature has shown that regression technique is the most appropriate for analyzing secondary data which these studies used. Also studies on earnings management and dividend payout, profitability, size and tax rate in money deposit banks are scanty.

### **Earnings Management and Dividend Payout**

Aladwan (2019) investigated whether dividend payout influences earnings management, the study examined 15 listed Jordan companies for the period 2008-2015. Nguyen and Bui (2019) assessed also whether dividend payout influences earnings management and the study examined 390 listed Vietnam companies for the period 2010-2016. Srikanth and Prasas (2015) investigated whether dividend payout influences earnings management, the study examines 142 nonfinancial companies on Karachi stock exchange for the period 2009-2014. Akenbor and Ibanichukwu (2014) used responses from questionnaire survey of 42 bank managers in Lagos to establish that loan loss provision are influences dividend payout determines earnings management of banks. Moghri and Galogah (2013) assessed whether dividend payout influences earnings management, and the study examined 140 companies on Tehran stock exchange for the period of 2006-2011. Similarly, Jahanzaib *et al.* (2012) assessed whether dividend payout influences earnings management in Pakistan by examining 100 indexes on the Karachi stock exchange for the period 2005-2009. He, Lilian, Zaiat and Zang (2012) investigated whether dividend payout influences earnings management, the study examined listed companies on the Indonesian stock exchange for the period



2000-2011. Moradzadehfard and Babaie (2012) studied whether dividend payout influences earnings management, the study examined 135 companies for the period 2004-2011. Edelstein, Liu and Tsang (2009) assessed whether dividend payout influences earnings management, the study examined 55 listed US companies for the period 2000-2005. These studies used secondary data and regression technique to establish that dividend payout influences earnings management. However, Arif *et al.* (2011) examined 86 companies listed on Karachi stock exchange for the period 2004-2009 the following studies did not state the number of companies they sampled but they also relied on secondary data and regression technique to evidence that dividend payout does not influence earnings management. Ajide and Aderemi (2014) examined selected listed Nigerian companies for one year period of 2012. Aurangzeb and Dilawer (2012) examined listed Pakistan companies for the period 1966-2008. Also, Shah, Yuan and Zafar, (2010) examined listed companies in Pakistan and China for the period 2001-2007. Again, Savov (2006) examined listed German companies for the period 1982-2003. Despite having different findings, these studies recommend implementing robust policies that decrease expenses and increase more liquidity to companies. The current study is different because it examines money deposit banks in Nigeria for the period 2010 -2019.

### **Earnings Management and Profitability**

Using secondary data, regression as the technique of data analysis and with the objective of determining whether profit influences earnings management. Lin, Thaker and Khaliq (2018) sampled 30 listed property companies in Malaysia for the period of 2010-2016. Pandey and Mansuri (2017) sampled 12 companies listed on Indian stock exchange for the period 2003-2012. Arif and Akbar (2013) sampled 174 nonfinancial companies on Karachi stock exchange for the period 2005-2010 establish that profitability influences dividend payout. More so, Lee, Li and Yue (2006) sampled 1,013 companies for the period 1988-2001 to evidence that high profit significantly relates to earnings management. But the following studies proved that low profit companies manage earnings too. Kothari, Mizik and Roychowdhury (2016); Cohen and Zarowin (2010); Doyle, Ge and McVay (2007) sampled 779 companies for the period 2002-2005. Also, Kim, Liu and Rhee (2003) sampled companies for the period 1983-2000. Contrarily, Alhadab and Al-own (2017) sampled 55 listed European banks for the period 2001-2015. Ardekani, Nejat and Hashemijo (2012) sampled companies in Malaysia for the period 2004-2010. De Angelo and Skinner (1994) sampled 76 companies on the New York stock exchange proved that low profit is not significantly related to earnings management. The recommendations from these studies summed up to advising companies to put in place very strong oversight scrutiny and solvency policies that can attract consistent profits. This study differs from reviewed studied because it is a Nigeria data base that focused on deposit money banks.

### **Earnings Management, Size and Tax rate**

The size of a company and the rate of tax have been established to influence earnings management. Using secondary data and regression as a technique Mohammad, Wasiuzzaman, Morsali, & Mzaini (2018) studied 350 firms in Malaysia for a period of 2008-2009, Jahmani and Niranjani (2015) examined 180 listed US firms for the period 2012-2014. Aini, Takiah, Pourjalali and Teruya (2006) studied companies on Kuala Lumpur stock exchange for the period 1995-1999 and Kothari *et al.* (2005) used a 552, 521 firm year observation from financial reports of companies for the period 1959-1998 to establish that firm size influence earnings management. Also, Kim, Liu and Rhee (2003) studied listed companies for the period 1983-2000 reported a positive relationship. Watts



and Zimmerman (1990) used quantitative data to evidence that size of a company explains its earnings management. While, the study of Gu, Lee and Rosett (2005) examined 4,401 listed US companies for the period 1974-2003 proved that size does not relate to earnings management. Additionally, Arif and Akbar (2013) examined 174 nonfinancial firms in Pakistan for the period of 2005-2010 to evidence that tax rate is used to influence dividend payout to explain earnings management also, Edelstein *et al.* (2009) and Aini *et al.* (2006) reported that tax rate positively influences earnings management. The current study is also a quantitative study that is different in examining deposit money banks for the period 2010-2019.

## 2.2 Theoretical Framework

The underpinning theory of this study is the signaling theory, the theory is very important in portraying the financial capability of a firm in paying dividend. Though the theory was established by Micheal spencer in 1973 to show that signaling educational qualification can influence job application success. This theory has been revalidated since then by several studies *like* (Colombo, 2021; Baier, Göttsche, Hellmann & Schiemann, 2020; Gao, Darroch, Mather & MacGregor, 2008; Zhang & Wiersema, 2009; Bhattacharya, 1979; Ross, 1977) over and over again. The aim of the theory is to basically reduce information asymmetry. This reduction is always to the advantage of the existing or prospective party in the business relationship.

The undue advantage has been argued to be a flaw of the theory (Arthurs, Busenitz, Hoskisson & Johnson, (2008). Spencer (1973) shows that signaling education as a function in the labor market makes the behavior of a job applicant reduce the information asymmetry of the selection process of employers of labor, because the job applicant alone knows his acquired skills or educational qualification not the potential employer. The theory assumes that individuals are defined by different innate level of productivity and such productivity is characterized by information asymmetry.

From the perspective of finance, Bernheim and Wantz (1995) shows that increase in dividend payout signals financial prospects of a company's increase in its stock price. In that regard dividend signaling theory shows that increase in dividend payment increases stock prices and investors seeking ever increasing dividend will be attracted to companies like that. Hence, despite the liquidity problems of banks in Nigeria they still paid dividend which sent signal of good prospects to existing and prospective investors.

## 3. Methodology

This study extracts data from all the 14 listed deposit money banks on the Nigerian stock exchange as at December, 2018 making it a census sampling. The secondary nature of the data for this study makes the design an ex-post facto research that is based on post positivism approach and covers the period 2010 to 2019. The choice of this period is greatly influenced by the intervention of CBN in the banking sector regarding dividend payout and capital adequacy.

### 3.1 Variable Measurement and Model Specification

This study has earnings management **EM** as it dependent variable and it is measured using loan loss provision of banks by adopting Ben Othman and Mersni (2014) Model. The choice of this model is influenced by the fact the model recognizes the different category of banks in Nigeria; interest; noninterest and interest based with non interest window.



$$LLP_{it} = \beta_0 + \beta_1NPL_{it-1} + \beta_2\Delta NPL_{it} + \beta_3\Delta TL + \varepsilon_{it}$$

Where:  $LLP_{it}$  = Total loan loss provision LLP for bank i at the year t, deflated by beginning loans.

$NPL_{it-1}$  = The beginning balance of non-performing loan for bank i at the year t deflated beginning loans.

$\Delta NPL_{it}$  = Change in the value of non-performing loan for bank i at the year t, deflated by beginning loans.

$\Delta TL$  = Change in the value of total loan, for bank i at the year t, deflated by beginning loans.

$\varepsilon_{it}$  = The absolute residual of the model is considered the Discretionary loan loss provision

DLLP = It is used to measure EM. Table 3.1 is a presentation of variable measurement.

Thus, the model of this study is as follow:

$$EM = \beta_0 + \beta_1DPL + \beta_2PR + \beta_3SZ + \beta_4TR + \varepsilon_{it}$$

**Table 3.1**

Variables	Measurement
Earnings Management-EM	Absolute value of Residuals (Ben Othman & Mersni, 2014).
Dividend Payout-DP	the ratio of total dividend payment to total profit after tax (Kuzucu, 2015).
Profitability-PR	the ratio of profit before tax & interest to total asset (Sheikh, Rafique & Abbas, 2016).
Size-SZ	the natural logarithms of total asset value in the statement of assets and liabilities (Gusni, 2016).
Tax Rate TR	the ratio of current year tax to profit before tax (Arif & Akbar, 2013, Lin <i>et al.</i> , 2018).

Source: Authors measures, 2020

#### 4. Results and Discussions

**Table 4.1: Descriptive Statistics**

Variables	Mean	Std. Dev	Min	Max
EM	0.5049	0.5295	-0.4746	5.0400
DP	0.3581	0.7920	0.7209	6.0729
PR	0.0136	0.2677	-0.1068	0.0656
SZ	20.9354	0.9105	18.8300	22.8300
TR	0.1512	0.2151	-1.0016	0.8142

Source: Authors' Computation, 2020 using STATA

Table 4.1 is the summary statistics of the explanatory variables. The average of Earnings Management (EM) is 0.5049 with the minimum of -0.4746 and a maximum of 5.0400. The result indicated that average Earnings Management (EM) of these banks is 5%. Dividend Payout (DP) has an average of 0.3581 and ranging from the extreme values of 0.7209 to 6.729 as the maximum. This implies that while some Banks pay dividend of less than ₦1 to their shareholders at a particular year others were able to pay ₦6 at a particular year. The standard deviation of profitability of the sample banks stand as 0.2677 followed by a minimum and maximum values of -0.1068 and 0.0656 respectively. Similarly, Size (SZ) has an average value of 20.9354 with a standard deviation of 0.9105 and minimum and maximum values of 18.8300 and 22.8300. Tax rate (TR) recorded an average value of 0.1512, a standard deviation of 0.2151 and minimum and



maximum values of 1.0016 and 0.8142 respectively. This result indicated that on average the total value of tax rate (TR) paid by the sample firms is 15%.

**Table 4.2: Summary of Regression Result**

<b>Variables</b>	<b>Coefficient</b>	<b>T-Values</b>	<b>P-Values</b>
<b>DP</b>	-0.1425	-2.1800	0.0310
<b>PR</b>	-1.1340	-6.9500	0.0000
<b>SZ</b>	0.1428	7.8800	0.0000
<b>TR</b>	-0.5092	-3.0500	0.0030
<b>Constant</b>	-1.9052	-5.9000	0.0000
<b>R2</b>			<b>0.4853</b>
<b>F-Sta</b>			<b>131.8900</b>
<b>F-Sig</b>			<b>0.0000</b>
<b>Mean VIF</b>			<b>3.5700</b>
<b>Heteest</b>			<b>0.1500</b>
<b>Het-Sig</b>			<b>0.7027</b>
<b>Hausman</b>			<b>33.4800</b>
<b>Hausman-Sig</b>			<b>0.0000</b>

**Source: Authors' Computation, 2020 using STATA**

The result showing the extent of the association between the independent variables and the dependent variable is presented and discuss in Table 3. The result of the Multicollinearity shows the mean VIF of 3.5700 and VIF's are consistently less than 10 and tolerance value less 1, implies that multicollinearity is not a problem (Cassey & Anderson, 1999). However, the result obtained from the heteroscedasticity test is not significant from the probability value of 0.7027 indicates that the panel elements were homoscedestic for the fact that it is a panel data the test for fixed and random effect were conducted. In addition, the result obtained from the Hausman specification test conducted indicates, that the probability value < 0.05 which suggested the use and subsequent interpretation of fixed effect model in favor of the random effect. The cumulative R<sup>2</sup> (0.4853) which is the multiple coefficient of determination gives the proportion or percentage of the total variation in the dependent variable as explained by the independent variables jointly. Hence, it signifies 49% of total variation in Earnings Management (EM) of listed Deposit Money Banks (DMBs) in Nigerian is caused by the collective efforts of dividend payout, profitability, size, and tax rate. This result further indicates that the model is fit.

The Fisher's statistics (F-statistics) of 131.8900 which is significant at 1% indicates that the firm specific characteristics model is fit. In addition, it also implies that for any change in firm specific characteristics variables used in this study, the earnings management of these DMBs will be directly affected. The probability value of (0.000) of the F-statistics which is significant at 1% implies that there is 99.9 percent likelihood that the association among variables is not due to mere chance. The regression result reveals that dividend payout has a t-value of -2.1800 with regression coefficient of -0.1425 which is statistically significant at 5% level. This implies that dividend payout has significant effect on the Earnings Management (EM) of listed Deposit Money Banks (DMBs) in Nigeria. This finding gives evidence of rejecting the first null hypothesis of the study which says dividend payout is not significantly related to earnings management of listed Deposit



Money Banks (DMBs) in Nigeria. This is not consistent with Ajide and Aderemi (2014); Aurangzeb and Dilawer (2012); and Savov (2006) showed that dividend payout has no influence on earning management.

The regression result reveals that profitability has a t-value of -6.9500 and a coefficient beta value of -1.1340 with a significant p-value of 0.000. This indicates that for every 1% increase in the proportion of profitability of listed deposit money banks (DMBs), the earnings management will reduce by 1kobo which is negligible. The findings from this result serve as a sufficient evidence of rejecting hypothesis two of this study which states that profitability is not significantly related to earnings management. This finding does not support the studies of Ardekani, Nejat and Hashemijo (2012); and De Angelo and Skinner (1994). The result also revealed that size has a t-value of 7.8800, coefficient value of 0.1428 which is statistically significant at 1% level as proven by the probability value of 0.000.

This signifies that size is positively, strongly and statistically influencing Earnings Management (EM) of listed deposit money banks. This implies that for every 1% increase in the size as represented by the natural log of total asset of DMBs listed in Nigeria, the earnings management (EM) will also increase significantly by 14k. This is not surprising considering the fact that a significant proportion of bank's asset is represented by loans (facility) which is a major avenue of earnings management by banks. However, this finding serves as an evidence of rejecting hypothesis three (3) of the study which states that size is not significantly related to earnings management. This finding is different from Gu, Lee, Rosett (2005) evidenced that size of a firm does not attract earnings management.

In addition, the result of tax rate reveals a t-value of -3.0500 and a beta value of -0.5092 with a p-value of 0.0030. This signifies that tax rate is another factor that influences Earnings Management (EM) in deposit money banks listed in Nigeria. This result is consistent with the study priority expectations that tax rate influences manager's opportunistic tendencies. This result confirms the earlier result presented for profitability. Hence, this finding provides sufficient reasons of rejecting the fourth null hypothesis of the study which states that tax rate is not significantly related on Earnings Management (EM) of Deposit Money Banks (DMBs) in Nigeria. This supports the finding of Edelstein *et al.* (2009) proved that tax rate influences earnings management by companies manipulating profit to pay less tax.

## 5. Conclusion

This study has proved that profitability can be manipulated so that it reduces the amount banks will pay as tax and then pay dividend. This study concludes profit, dividend paid, size and tax rate influences earnings manipulation. Theoretically this study evidenced that bank directors can signal shareholders and potential investors by reporting managed earnings used to sustain dividend payout. This study recommends the sustainability of the CBN directives on the payment of dividend based on thresholds. Secondly, the study recommends that banks pursue a conservative working capital management policy that will secure their future liquidity position. Thirdly, banks should introduce more attractive products that will increase their turn over and surpass their expenses so that when they actually pay tax, available amount for dividends and other charges will be adequate to remain robust. lastly, efficiency should be adopted in managing the entire assets of the banks so that profitability position can greatly increase.





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