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DOES CORPORATE SOCIAL RESPONSIBILITY EXPENDITURE INFLUENCE TAX AVOIDANCE? EVIDENCE FROM TANZANIAN LISTED FIRMS

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ABSTRACT: *This study examines the relationship between corporate social responsibility expenditure and tax avoidance in Tanzanian listed firms, utilising secondary data from 25 firms listed on the Dar es Salaam Stock Exchange over a ten-year period from 2013 to 2022. Employing a retrospective research design and purposive sampling, we applied the fixed effects model as the estimation technique. The analysis reveals a positive and significant association between corporate social responsibility expenditure and tax avoidance, indicating that firms with higher levels of corporate social responsibility expenditure are more likely to engage in tax avoidance practices. Furthermore, control variables such as firm size, profitability, and leverage also demonstrated positive and significant relationships with tax avoidance. The findings contribute to the understanding of the intricate dynamics between corporate social responsibility initiatives and tax management strategies in the Tanzanian context. The implications of this study extend to policymakers, suggesting the need for a nuanced approach to corporate tax regulation, taking into account the interplay between corporate social responsibility initiatives and tax management practices. Policymakers should recognise that firms engaging in higher corporate social responsibility activities may employ tax planning strategies that warrant attention in regulatory frameworks. This study contributes to the ongoing discourse on the complex dynamics between corporate social responsibility and financial decision-making in emerging market contexts.*

KEYWORDS: Corporate social responsibility expenditure, tax avoidance, listed firms, Tanzania.

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INTRODUCTION

Corporate Social Responsibility (CSR) has evolved into a pivotal dimension of contemporary business practices, reflecting the commitment of firms to societal and environmental concerns (Benlemlih & Bitar, 2018; Habib & Hasan, 2019). Defined as the voluntary integration of social and environmental considerations into a firm's business operations and interactions with stakeholders (Jiang, 2020), CSR goes beyond profit maximisation and underscores the broader responsibilities businesses hold in contributing to the well-being of the communities and environments in which they operate. Firms allocate resources to CSR activities, encompassing initiatives such as philanthropy, sustainability practices, and community engagement, for diverse reasons. For example, firms engage in CSR activities to gain potential financial benefits and create stakeholder value (Bo et al., 2019).

Also, studies, e.g., Adinata (2019), argue that CSR activities can enhance a firm's reputation and foster stakeholder trust, which helps mitigate risks associated with negative externalities. Moreover, CSR activities can contribute to employee satisfaction and attract socially conscious investors (Saeed & Sroufe, 2021), which ultimately influence their performance (Olusola, 2022; Oyewumi et al., 2018). Thus, the motivations for CSR expenditure by firms are diverse. However, the financial consequences of CSR, particularly in relation to tax avoidance, present a complex and underexplored terrain within the realm of corporate decision-making.

Tax avoidance, defined as the strategic and legal minimization of tax liability through financial planning (Aronmwan & Okaiwele, 2020), constitutes a critical aspect of corporate financial strategies. The link between CSR expenditure and tax avoidance has generated scholarly interest and debate. Some argue that firms engaged in CSR activities may be more adept at navigating tax regulations, utilising legal avenues to minimise tax liability (Choi et al., 2017). Conversely, ethical constraints imposed by CSR practices might deter firms from engaging in aggressive tax planning, suggesting a potential negative relationship. The interplay between CSR and tax avoidance becomes particularly intriguing in emerging markets like Tanzania, where socio-economic dynamics and regulatory frameworks add layers of complexity to these relationships.

Empirical evidence on the relationship between CSR expenditure and tax avoidance remains inconclusive, with studies presenting divergent findings. While Xu et al. (2022) find a positive association, indicating that firms with higher CSR spending are more likely to engage in tax avoidance, Du and Li (2023) and Rahman and Li (2021) argue for a negative relationship, suggesting that ethical considerations associated with CSR practices may constrain aggressive tax planning. The dynamics are further complicated by contextual factors such as firm size, profitability, and industry-specific nuances (Rahmat & Kustiawan, 2020). Understanding this relationship in the Tanzanian context is crucial as emerging markets may exhibit unique patterns due to varying institutional contexts and regulatory landscapes.

Therefore, this study aims to contribute to the empirical literature by providing comprehensive insights into how CSR spending influences tax avoidance in the Tanzanian business environment. Departing from existing studies, our research incorporates control variables such as firm size, profitability, and leverage, offering a more nuanced understanding of the interplay between CSR expenditure and tax avoidance. By employing a fixed effects model and focusing on a specific geographical context, we aim to contribute empirical evidence that enriches the

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global understanding of this intricate relationship and provides actionable insights for policymakers, practitioners, and academics.

LITERATURE REVIEW

This section provides a comprehensive review of both theoretical and empirical literature investigating the nexus between corporate social responsibility (CSR) expenditure and tax avoidance. The study is anchored in the theoretical frameworks of agency and stakeholder theories, offering a solid foundation for understanding the complex interplay between CSR and tax-related behaviour.

Agency theory, rooted in the principal-agent relationship, illuminates potential conflicts of interest between managers and shareholders, shaping managerial decisions and their impact on tax practices (Zogning, 2017). On one hand, it suggests that managers may exercise discretion in CSR spending, potentially diverting resources from tax obligations for personal gain. Conversely, Cherian et al. (2020) argue that CSR can function as a governance mechanism, aligning managerial and shareholder interests and mitigating agency conflicts.

Turning to stakeholder theory, which posits that firms' success hinges on balancing the interests of various stakeholders (Freeman et al., 2018), the study seeks to explore how this perspective influences the relationship between CSR expenditure and tax avoidance. Stakeholder theory suggests that firms actively involved in CSR are likely to recognize and address a broader set of stakeholder interests, potentially extending to ethical tax practices (Mahmud et al., 2021). The literature within this framework (e.g., Brown & Forster, 2013; Freeman et al., 2018; Friedman & Miles, 2001) emphasizes the contextual nuances, highlighting that the relationship between CSR and tax avoidance is contingent on factors such as stakeholder pressures, industry characteristics, and the regulatory environment.

Furthermore, the relationship between CSR and tax avoidance is not a one-size-fits-all proposition. The intersection of CSR and tax avoidance has become a focal point for both business practitioners and scholars, as indicated by considerable scholarly focus (Nurhaliza & Widarjo, 2023). CSR encompasses a wide range of activities through which firms aim to positively impact the environment and society. These practices also address governance issues, including integrity, ethics, and transparency (Xu et al., 2022). Additionally, the principles for responsible investment underscore the significance of paying a fair share of taxes as one of the key firm responsibilities (Benlemlih et al., 2023).

It is crucial to recognize that taxation plays a vital role in shaping the character and functionality of the state, economy, and society, with tax revenues serving as a primary means for governments to provide public goods and services (Janský, 2023). In Tanzania, for instance, tax revenues contribute substantially to government finances, constituting 68% in 2021 and 72% in 2022 of total revenues and around 12% of the GDP in the financial year 2022 (NBS, 2022). However, businesses may perceive tax avoidance as a value-maximizing strategy (López-González et al., 2019). Tax avoidance, as described by scholars like Nurhaliza and Widarjo (2023) and Zeng (2019), involves the reduction of explicit taxes paid by firms. This strategic approach allows firms to decrease their tax rates while adopting positions that are less likely to be challenged by tax authorities, such as establishing subsidiaries in low-tax jurisdictions or leveraging accelerated depreciation deductions.

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The existing literature presents inconclusive findings regarding the association between CSR and tax avoidance. Studies, such as those conducted by Gulzar et al. (2018), López-González et al. (2019), Nurhaliza and Widarjo (2023), and Winarno et al. (2021), have found a negative relationship between CSR and tax avoidance. This perspective is grounded in stakeholder theory, emphasizing the need for firms to strike a balance between their economic interests and ethical responsibilities to society. Firms committed to CSR, according to this view, are more likely to adopt transparent and ethical tax practices, aligning with societal expectations and fostering long-term stakeholder relationships.

On the contrary, a number of studies propose a positive relationship between CSR and tax avoidance. Pratiwi and Siregar (2019) and Zeng (2019) argue that a corporation operates as a contractual agreement between shareholders and managers, guided by a singular objective to maximize shareholder wealth. In this scenario, CSR is considered a constraint, prompting managers to navigate a trade-off between societal concerns and the pursuit of shareholder wealth maximization. Managers perceive the reduction of taxes or the adoption of tax avoidance strategies as advantageous for shareholders (Liu & Lee, 2019). Simultaneously, managers express apprehension about potential adverse impacts associated with engaging in aggressive tax planning activities, such as facing sanctions, harming the firm's reputation, eliciting public concerns, and attracting media pressure (Rahmat & Kustiawan, 2020). Consequently, managers tend to augment their CSR activities either to mask the adoption of tax avoidance strategies or to reap the anticipated benefits associated with CSR activities.

Furthermore, Duhoon and Singh (2023) considered that specific firm characteristics play crucial roles in shaping the empirical landscape of the relationship between CSR expenditure and tax avoidance. For example, firm size, often associated with greater financial resources, introduces a potential dichotomy wherein larger firms may engage in more sophisticated tax planning but also face heightened scrutiny (Pranata et al., 2021). Additionally, Yevilia and Mukhlasin (2020) suggest that firm age plays a pivotal role in shaping tax behaviour; younger firms might prioritize short-term financial goals, potentially leading to a higher likelihood of engaging in tax avoidance practices. On the other hand, older firms, with established reputations and longer-term perspectives, may adopt more conservative and ethical tax practices.

Moreover, Safiinatunnajah and Setiyawati (2022) argue that highly profitable firms may have both the incentive and the resources to engage in aggressive tax planning. However, profitability may interact with CSR expenditure, influencing the ethical considerations of tax practices. For instance, firms with high profitability and a commitment to CSR may find a balance between financial success and ethical tax behaviour. Leverage, as another control variable, introduces a layer of complexity. Highly leveraged firms may have financial incentives for tax planning, but the risk of financial distress and debt covenants may counteract aggressive tax strategies (Pranata et al., 2021).

Generally, the literature review reveals inconclusive results regarding the influence of CSR expenditure on tax avoidance. This ambiguity prompts the central question: Does corporate social responsibility expenditure influence tax avoidance? This study aims to explore this question within the context of Tanzanian listed firms, seeking to contribute empirical evidence to the existing body of knowledge.

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METHODOLOGY

Research Design and Data

This study employs a retrospective research design, gathering quantitative data from 25 firms listed on the Dar es Salaam Stock Exchange (DSE), spanning the period from 2013 to 2022. Initially, our plan was to collect data from all 28 listed firms, but three firms were excluded due to incomplete disclosure of required information in their annual reports, particularly regarding the amount spent on CSR activities. As a result, we based our analysis on 250 observations. Our data was sourced from the firms' annual reports, chosen for their adherence to auditing standards and accounting rules. Additionally, these reports offer comprehensive information on the social and environmental performance of the firms (Wang, 2021).

Measures of Variables

Tax avoidance denoted by TAV is a dependent variable and was measured by the current Effective Tax Rate (*ETR*). The ETR was calculated by dividing the total taxes paid by the firms' taxable income (Benlemlih et al., 2023). The selection of ETR as the measure of TAV is grounded in the recognition that ETR is widely acknowledged as a robust indicator of TAV (Benlemlih et al., 2023) and applicable across diverse industries (Janský, 2023). Given the diverse nature of our study, encompassing firms from various sectors such as telecommunications, manufacturing, banking, energy and petroleum, the use of ETR emerges as a fitting measure. Its adaptability makes it particularly well-suited for use in this study. Therefore, the ETR is expressed as follows:

$$CETR = \frac{\text{Tax Expense - Deferred tax expense}}{\text{Pre-Tax Income}}$$

The independent variable was the total amount spent on CSR activities by a firm in a given financial year. It is denoted by CSRE and was measured by the natural log of the actual total amount spent on CSR activities in a given financial year. The measure has also been applied to various related studies, e.g., Mokuolu and Oladele (2018), Musa et al. (2019), and Oware and Mallikarjunappa (2020).

Also, we introduced firm size, firm age, leverage, and profitability as the control variables in the study, in order to reduce bias and increase the causal inference of the analysis (Baltagi, 2021). The firms' size donated by FSIZE was measured by the natural log of firms' total assets in a given financial year. The firm's age (FAGE) was measured by the natural log of the number of years since the firm was established until the time this research was conducted. The measure was also applied by similar studies, e.g., Fuadah and Kalsum (2021). The profitability was measured by Return on Assets (ROA). Lastly, the firms' leverage, denoted by (LEV) was measured by the firms' total debts divided by their total assets.

Empirical Model

In order to examine the influence of CSR expenditure on tax avoidance, we state the empirical model in general terms as follows:

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$$TAV = \beta_0 + \beta_i \chi_i + cntV + \varepsilon_i TAV = \beta_0 + \beta_i \chi_i + cntV + \varepsilon_i \quad (1)$$

where: β_i represents coefficients for the independent variables; χ_i represents independent variables; *cntV* means control variables and ε_1 is the error term, β_0 β_0 represent the intercept. By using the variables described in Section 3.2, the full empirical model is specified as follows:

$$TAV = \beta_0 + \beta_1 LnCSRE + \beta_2 LnFSIZE + \beta_3 LnFAGE + \beta_4 Profitability + \beta_5 LEV + \varepsilon_i$$
$$TAV = \beta_0 + \beta_1 LnCSRE + \beta_2 LnFSIZE + \beta_3 LnFAGE + \beta_4 Profitability + \beta_5 LEV + \varepsilon_i \quad (2)$$

FINDINGS AND DISCUSSIONS

This section encompasses both descriptive and empirical analyses. Before delving into the empirical analysis, diagnostic tests were conducted to ensure that the selected model assumptions in this study were not violated.

Descriptive Analysis

From Table 1, the mean tax avoidance (TAV) value of 0.38 indicates a moderate level of tax avoidance among Tanzanian listed firms, with a standard deviation of 0.65. This suggests a considerable degree of variability in tax avoidance practices. The minimum and maximum values of 0.30 and 0.73, respectively, indicate a variation in tax avoidance behaviour within listed firms. Additionally, the corporate social responsibility expenditure (CSRE) variable, measured in millions of Tanzanian shillings, shows a mean expenditure of 313 million with a substantial standard deviation of 526 million. The wide range, from 7.6 million to 2,900 million, suggests significant diversity in CSR expenditure among listed firms. This variation might be attributed to different organisational priorities, industry norms, or the extent to which firms perceive the importance of CSR in their operations.

Furthermore, firm size (FSIZE), measured in millions of Tanzanian shillings, has a mean value of 1,700,000 with a standard deviation of 2,990,000. The minimum and maximum values of 1,460 and 11,600,000, respectively, indicate a broad spectrum of firm sizes within the sample. The dispersion in firm size might have implications for the study as larger firms may have different dynamics in terms of CSR practices and tax avoidance compared to their smaller counterparts. The firm age (FAGE) variable, with a mean age of 38 years and a standard deviation of 27, shows a diverse range of firm ages, varying from 14 to 89 years. This diversity in the age of firms can influence their corporate culture, historical practices, and possibly their approach to CSR and tax strategies.

Furthermore, the profitability variable, with a mean of 3.54 and a standard deviation of 2.980, indicates the variability in the profitability levels of Tanzanian listed firms. The range from 1 to 16 suggests that firms in the sample exhibit different levels of financial performance, which may be a crucial factor influencing both CSR expenditure and tax avoidance. The leverage (LEV) variable, with a mean value of 0.70 and a standard deviation of 0.83, indicates a moderate level of leverage among the sampled firms. The narrow range from 0.01 to 0.78 suggests that the firms have relatively similar leverage levels. Therefore, this descriptive analysis provides a comprehensive overview of all variables in this study.

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Table 1: Descriptive Analysis

Variable	Obs.	Mean	Std.Dev.	Min.	Max.
TAV	250	0.38	0.65	0.30	0.73
CSRE	250	313	526	7.6	2,900
FSIZE	250	1,700,000	2,990,000	1,460	11,600,000
FAGE	250	38	27	14	89
Profitability	250	3.54	2.980	1	16
LEV	250	0.70	0.83	0.01	0.78

Authors (2023); CSRE and FSIZE are in millions Tanzania Shilling

Diagnostic Tests

Before the empirical analysis, we conducted diagnostic tests to ensure that the model assumptions were met. The dataset was examined for outliers using a box plot, revealing outliers in the FSIZE, CSRE, and Profitability variables. To address this, winsorization of 5% from the top and bottom of variables with outliers was applied, mitigating the impact of extreme values and facilitating a more normalized dataset for analysis. The normality assumption was verified through skewness and kurtosis tests; Table 2 confirms the normal distribution of the data, where skewness was less than +/-2, and kurtosis was less than +/-3 (Hair et al., 2015). The pairwise correlation matrix was employed to assess multicollinearity, with results indicating no significant issues, as coefficient values ranged from 0.044 to 0.537, all below the acceptable cut-off point of 0.7 (Creswell, 2012). Serial correlation was tested using the Pesaran test, revealing its absence (p-value = 0.275). Heteroscedasticity was examined through the Breusch-Pagan/Cook-Weisberg test (p-value=0.730), demonstrating its absence. Lastly, the Breusch and Pagan Lagrangian multiplier test (LM) wit p-value=0.000 identified the presence of panel effects, prompting the application of the Hausman test. The significant result of the Hausman test affirmed the appropriateness of the Fixed Effects (FE) estimation technique over Pooled Ordinary Least Squares in this study.

Table 2: Multicollinearity and Normality Tests

Variable	TAV	CSRE	FSIZE	FAGE	Profitability	Leverage	Kurtosis	Skewness
TAV	1.0000						2.58	0.45
CSRE	0.2429	1.0000					0.02	0.13
FSIZE	0.2363	0.5373	1.0000				2.33	1.00
FAGE	0.0833	0.3164	0.1177	1.0000			2.64	-0.36
Profitability	0.2522	0.1569	0.0443	0.1848	1.0000		2.96	0.43
Leverage	0.1103	-0.1392	-0.2501	-0.3902	0.1078	1.0000	1.87	0.40

Authors (2023)

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Empirical Analysis

The results from the fixed effect estimation technique, as presented in Table 3, provide valuable understandings into the influence of corporate social responsibility expenditure on tax avoidance, while controlling for firm size, firm age, profitability, and leverage.

From Table 3, the values of corporate social responsibility expenditure indicate that CSRE positively and significantly influences tax avoidance of firms listed in Dar Es Salaam Stock Exchange. This means that, as the amount spent on CSR activities by firms increases, the tax avoidance by firms also increases. Further, the finding suggests that firms that spend on CSR activities are more likely to engage in legal tax planning strategies, e.g., claiming deductions and credits or structuring transactions in a tax-efficient manner to reduce their tax burden. Our finding is also supported by the agency theory which suggests that managers make decisions based on their own self-interest and might choose to spend in CSR activities in order to reduce their tax obligations. However, managers may engage in tax planning to create the funds required to spend in CSR activities. In this case, CSR expenditure may be viewed as a way for management to show their commitment to stakeholders, whereas tax avoidance could be considered as a strategy to guarantee that there are resources available to fulfil these CSR obligations. Similar results have been reported by Abdelfattah and Ahmed (2020) and Pandapotan (2023) but contrary to Gulzar et al. (2018) and Winarno et al. (2021) who found a negative relationship between CSR expenditure and tax avoidance. The difference in the findings could be influenced by different measures of tax avoidance as well as estimation techniques.

From Table 3, we also find that the firms' size positively and significantly influences tax avoidance. This means that as the size of the firm increases, tax avoidance also increases. This finding suggests that larger firms may have greater resources and be able to afford the costs associated with tax planning. Additionally, larger firms could have organisational structures that are more complicated, opening up more potential chances for tax planning. Further, the stakeholder theory suggests that larger firms have more stakeholders to consider and are under greater pressure to engage in CSR initiatives. This may result in a higher demand for resources, which could drive larger firms to engage in tax planning activities in order to finance these initiatives. Similar results were reported by Christopher et al. (2017).

Furthermore, the positive and statistically significant coefficient for profitability suggests that more profitable firms tend to engage in higher levels of tax avoidance. This finding aligns with the predictions of agency theory, which posits that managers, acting in their own self-interest, may strive to maximise firm profits through strategic tax planning. Profitable firms may have the financial resources and flexibility to implement tax avoidance strategies effectively, contributing to enhanced financial performance. This result implies that stakeholders, including investors and shareholders, may need to consider the impact of profitability on tax avoidance when evaluating a firm's financial health and ethical practices.

Lastly, the positive and significant relationship between leverage and tax avoidance supports the view that firms with higher leverage ratios are more likely to engage in tax planning activities. According to agency theory, the interests of shareholders and debt holders may diverge, leading managers to pursue strategies that maximise shareholder wealth, such as tax avoidance, potentially at the expense of debt holders. This finding underscores the importance of considering the capital structure of firms when assessing their tax avoidance practices. It

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also highlights the potential agency conflicts that can arise between different stakeholders with varying interests.

Table 3: Fixed Effects Estimation Technique: Taxa Avoidance Dependent Variable

Variable	[1]	[2]
CSRE	0.027	0.027
	(0.021)**	(0.020)**
FSIZE	0.124	0.122
	(0.000)***	(0.000)***
FAGE	0.086	
	(0.245)	
Profitability	0.611	0.441
	(0.034)**	(0.042)**
LEV	0.201	0.200
	(0.045)**	(0.041)**
Constant	-0.458	-0.470
	(0.475)	(0.458)
Observation	250	250
Adj. R-Squire	0.58	0.66
Breusch-Pagan LM-test	365.70***	365.70***
Pesaran's CD test (prob.)	0.275	0.272
Hausman test	160.86***	160.86***
Breusch-Pagan / Cook-Weisberg test	0.730	0.730

Source: *Authors' survey data (2021).* Robust standard errors are reported in parentheses. *p<0.10, **p<0.05 and ***p<0.01.

CONCLUSIONS

The aim of this study was to examine the influence of CSR expenditure on tax avoidance by firms listed on the Dar es Salaam Stock Exchange. In conclusion, the findings suggest a positive relationship between corporate social responsibility expenditure and tax avoidance, suggesting that firms strategically manage their tax liabilities in conjunction with CSR activities. The results are generally in line with stakeholder theory and agency theory, and highlight the importance of considering firm size, profitability, and leverage when examining the relationship between CSR expenditure and tax avoidance.

Additionally, the findings have relevant implications for tax authorities, firms, and policymakers, as follows: Firstly, tax authority firms that spend on CSR activities could be engaging in tax planning to reduce their tax liabilities. This could be an area of focus for tax authorities when conducting tax audits and investigations, as they may need to pay closer attention to companies that engage in both CSR activities and tax planning. Moreover, tax authorities may consider implementing tax policies that encourage companies to engage in CSR activities while discouraging aggressive tax planning practices. Secondly, firms should be mindful of the potential trade-off between spending on CSR and reducing their tax liability through tax planning. Firms that invest in CSR may need to make sure that their tax planning

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strategies align with the organisation's objectives to avoid aggressive tax planning strategies. Lastly, policymakers should take into account the potential relationship between CSR expenditure and tax planning when formulating tax policies that will encourage firms to invest in socially responsible activities while discouraging aggressive tax planning practices.

Like many other studies, the current study also has limitations. Therefore, we suggest future studies consider a cross-sectional research design with a focus on one industry. The aim is to obtain a holistic understanding of the influence of CSR expenditure on a specific industry. Also, future studies could consider other measures of tax avoidance and firms' size.

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