

APPRAISAL OF TAX INCENTIVE ON CORPORATE PERFORMANCE IN CALABAR FREE TRADE ZONE

BY

EMENYI, EMMANUEL OKON

BEREDUGO, SUNNY BIOBELE

PATRICK AKININNYI

Abstract

The study was on the appraisal of tax incentive on corporate performance in the Calabar free trade zone. This was due to the fact that in spite of the tax incentives put in place, companies are not investing in Calabar Free Trade Zone. The study therefore evaluate if there is any significant difference between the effect of profit with exempt profit taxes and profit without exempt profit taxes on the profitability of companies in the Calabar Free Trade Zone. Ex-post facto design was used for the study. The hypothesis was tested using, the independent sampled t-test. It was discovered that there is a significant difference between the effect of profit with exempt profit taxes ($M=253.0708$, $SD=350.07458$), and profit without exempt profit taxes on companies in the Free Trade Zone ($M=172.1630$, $SD=237.87061$); $t(94) = 1.324$, $p=.016$. The magnitude of the differences in the means is very high ($\eta^2 = 0.18$). The government should sustain the tax incentives in order to maintain industrial and economic development growth potentials of the Zone and that of the nation as a whole. If these incentives are sustained, the government on the other hand, tends to recover revenue lost to tax incentives from personal income tax of employees and sales taxes of products generated by the industrial growth of the Zone.

Keywords; Tax incentive, corporate performance, Exempt profit taxes, Calabar free trade zone

1.1 Introduction

Income tax forms one of the major sources of revenue for all levels of government in Nigeria. It therefore requires careful planning to evolve tax policies that will enhance the general economic growth of the nation. While there are tax incentives in areas where the government has special interest, there is disincentive where the government seems to pay less attention.

Tax reduces net return on investment and also decreases the balance available for private savings. Though Taxpayers view tax as a burden being imposed on them by the government, they on the other hand, benefit from it through the provision of social amenities such as water, electricity, good roads and other infrastructure supplied by the government and finance by tax money.

In Nigeria, as a developing country, there is need to encourage investors whether foreign or domestic so as to encourage growth and development. One way, among several others, of achieving this goal is by giving tax incentives. According to Ayua (1996) as far back as 1950, tax incentives had been part of industrial policy directed at private firms. It is however to be noted that incentives in form of tax credits may not be the sole determinants of investment in Nigeria. Other factors like market size, expansion of sales into markets, forestallment of major competitors, a conducive business environment, good political climate, etc. should be taken into consideration in choosing a place of investment. The question here is whether the objective of encouraging investment through tax incentives has been achieved, if not, what better ways could this be achieved?

According to Obioma (2003), the use of tax incentives as instruments of enhancing corporate performance is yet to gain prominence in Nigeria generally and Cross River State in particular, where the Export Processing Zone (EPZ), Free Trade Zone (FTZ) and TINAPA are still lying fallow. It is an opening for companies/investors to exploit the opportunities given them through tax incentives in Cross River State. It is observed by Bergsman (1999) that most tax incentive schemes that are available in most countries are simply not effective. They attract very little additional investment.

Upon the fact that these incentives are not effective, they constitute a drain on the government treasury. Furthermore, Bergsman (1999) discovered that these tax incentives are sometimes counterproductive because they make investment procedures too complex, and sometimes lead to significantly greater corruption. Therefore, the government needs to adopt better policy recommendations to tax incentives that will attract investment, ease the cumbersome tax planning processes devoid of corrupt practices. Bergsman (1999) further pointed out that tax incentives in less developed regions are often limited to certain sectors and/or regions, or if not strictly limited, they are liberal in certain sectors and regions. The record of both of these is that they are not very effective, but they are very popular around the world.

Therefore, the problem identified is that, in spite of the tax incentives put in place, why are companies not investing in Calabar Free Trade Zone? Does it mean that doing business in the Zone is not profitable? We may deduce from this problem that such incentives do not adequately influence profitability which is a function of the investment decisions of prospective investors. This is because the benefits are not passed onto the public by way of low prices to encourage consumption, sales and profit.

This seminar attempts to critically appraise the significance of tax incentive on corporate performance of companies in the Calabar Free Trade Zone. Obviously, corporate management takes advantage of tax incentives as provided by the available tax laws to make investment decisions to enhance profitability of the enterprise. In the view of Osuegbu (2007), it is thus in the interest of the Taxpayer to exploit the tax laws through good tax planning to reap from tax avoidance. The Taxpayer in order to secure his net earnings, devices means of minimizing tax liabilities by exploiting the tax incentives as provided by the tax laws.

As part of the efforts to provide an enabling environment for growth and development of industries, the Federal Government of Nigeria (FGN) has developed a package of tax incentives for various sectors of the economy to stimulate the expansion of domestic production capacity. These incentives, it is believed will help strengthen the economy, accelerate growth and development and reduce poverty. All these depend on the response of corporate organizations to government's benevolence by adopting strategies to utilize these incentive opportunities in making investment decisions aimed at enhancing corporate profitability.

The Calabar Free Trade Zone is earmarked for some special tax incentives such as exempt company income tax, exempt customs duties, exempt Cross River State urban development tax etc. The thrust of this work was to find out the extent to which these tax incentives have influenced profitability and thus promote investment in the Zone. It is also worthy of note that profitability is a function of investment decision. On the part of the government, there is need to know if the tax incentives have yielded result by attracting investors for industrial growth.

1.2 Objective of the study

- To determine if there is any significant difference between the effect of profit with exempt profit taxes and profit without exempt profit taxes on the profitability of companies in the Calabar Free Trade Zone.

2.1 Theoretical framework

Tax incentives can be granted in a variety of ways with differing implications for the burden on the domestic treasury (Zee, Stotsky & Ley, 2002). This is backed up by the following theories.

2.1.1 Tax incentives in a capital theory context

According to Harberger (1980), Economists often develop the "wrong" instincts by concentrating on a particular "wrong" subset of models. He said, the "wrong" subset is either

- One with an infinitely lived capital stock or
- One with a capital stock which all assets are depreciated at the same rate.

Under (a), there simply is no depreciation of the capital stock so the user cost of an asset = $(P+D)\ell_{t-1}$ is equal to its net return, $(P)\ell_{t-1}$.

Under (b), there is depreciation but it is at a given rate equivalent to an incentive or (tax) that strikes “net return” only, but at a higher rate.

Under (a) or (b), then, one does not fall into error but talking about incentives to user cost when we really mean incentives to net return.

Tax incentives which strike at an equal rate the net depreciation income from all investments in a given class have the property of giving a stimulus to all such investments. Harberger (1980) further alluded that the nature of the stimulus is as follows:

- i. For non-covered investments, an expected marginal productivity of ℓ_t marks the dividing line between projects which are not.
- ii. The characteristic of what he called well-calibrated incentives is that they modify the critical level of expected marginal utility in a very orderly way, reducing it by a constant amount for all activities subject to the same incentive scheme.

Thus, it would be possible for a government to have a normal tax regime in which the cutoff gross-of-tax rate of return was 20% per annum plus a ‘super-preferred’ category in which this rate was 11% per year, plus a ‘super-preferred’ category in which this cut off rate was 10% per annum. Samuelson (1964) showed that a proportional income tax based on the economic depreciation reduces that rate of return to all assets in the same proportion, not discriminating among them according to length of life, shape of benefit profile, etc.

Different propositions about taxes, tax incentives and other fiscal policies can be demonstrated easily within the framework developed here. Musgrave neutrality. Musgrave (1959), showed that to allow full expensing of investment outlays is equivalent to abolishing the corporation income tax. We have $PVY + PVD - PV(Y+D)$. Expensing allows instantaneous depreciation of assets at the amount of purchase, the investing entity gains. Now however, it has nothing to depreciate in the future. Hence it pays tax on the income plus depreciation. The investing entity thus loses on this account. Overall, in present value terms, the first account cancels the second.

Non neutrality of standard Investment Tax Credit (ITC). ITC involves a credit at the rate, r to the amount invested, y . The investing entity gains in this case also. $r(PVY+PVD)$. This is non-neutrality as long as the ratio PVD/PVY differs among investments (Harberger, 1980).

Neutrality of credit to net investment. Cary brown in Bradford (1980) suggested many years ago that the ITC be granted on net gross investment. Each year, the credit would be given on gross investment for the year, minus the true economic depreciation of the existing capital stock (generated by part investments). If we follow a single project, there arises a tax credit of $r(PVD+PVY)$ at the time of the investment followed by later “anti-credit” equal to $-rD$. Taking present value, the net outcome is a credit of $r(PVD+PVY)+PV(-rD)-r(PVY)$. This meets the condition of striking Y at the same rate across all covered investments.

The Jorgenson – Auerbach scheme: This scheme was proposed by Auerbach and Jorgensen (1980) as a way of insulating the tax treatment of investments from the effects of inflation. It entailed estimating the fraction that PVD bore to the purchase price of an asset ($-PVY+PVD$), and allowing this fraction to be expensed immediately, at the time the asset was purchased. Under this scheme, the investor receives a tax offset of $-tPVD$ at the time of investments, then pays tax on the full flow of $Y+D$. in present value terms, the result is $-tPVD+PV(ty+tD)-tPvy$. This is equivalent to Samuelson neutrality of an income tax.

2.2 The nature of tax incentives and profitability in the private sector

Tax incentives is seen as the fiscal measures among others to promote innovation and that it has assumed much importance in current discussions on public organization for economic co-operation and development, innovation policies by OECD (1996a and 1996b), this means to say that the essence of tax incentives is to encourage investment. And by implication, such investments are essentially profitable in order to achieve this goal. This is because increasingly, developing countries such as India are showing signs of replacing direct support to R & D with that of indirect subsidies like tax concessions (Mani, 1999).

Mani (1999) in survey of tax treatment of R & D expenditure across twenty developed and developing countries came up with the following findings.

- i. Majority of the countries allow almost the entire revenue and capital expenditure on R & D to be deducted from the taxable income during a year.
- ii. In some 10% of the countries, an amount even greater than what is spent is allowed to be deducted and
- iii. Much of the revenue expenditure deductions are admissible in the first year itself while much of the capital expenditure deductions are admissible in the first five years.

Mani (1999) further made findings that among 100 countries studied about 10 only have production enterprises which invest in industrial R & D, while others are encouraged by some form of tax credits for investment in some specific industries.

As explained by ICAN (2009), tax planning involves taking conscious efforts to consider the tax that will be payable by a Taxpayer at a future date and how such tax can be minimized. In relationship with profit or income, the tax to be paid can be minimized by reducing the assessable profit of the taxpayer. The available laws regulating tax administration, assessment and collection give the Taxpayer grounds to manipulate his income within the limits of the tax laws to pay less tax.

If the Taxpayer pays less tax, it means, he will be reporting higher profit after tax (PAT), as a basis of calculating profitability growth ratios. The higher the profit, the higher the profitability ratios and vice versa. It then means that as far as the law provides, a Taxpayer can plan his tax in such a way as to report good profitability ratios. The various methods of achieving this tax planning are through tax incentives.

Tax incentives are the provisions of the tax that enable the Taxpayer to minimize his tax liabilities as far as possible. Therefore, tax planning is based on tax incentives and knowledge of the tax laws by the taxpayer. The available tax incentives are as follows according to ICAN (2009).

- i. Capital allowance – timing of assets

Particularly initial allowance and investment allowance are allowed once in the first year in full regardless of the time in the accounting basis period that the asset is put to use. Example, a company that purchases an asset in December will claim the same amount of initial and investment allowance as the one in January under the same circumstances. In this case, the company that purchased in December will claim more allowance proportionately as compared application to the one acquired on a later date than on an earlier date.

- ii. Where to invest

According to the tax laws, companies in the agricultural, agro-allied and manufacturing industries are given no restrictions to the percentage of assessable profit that capital allowance must not exceed. But for others, it is limited to 66 2/3%. In tax planning, a company can decide to invest in these industries in order to enjoy the benefit. Also, there are rural allowances, industry allowances, etc the knowledge of which can inform a Taxpayer to lessen his tax burden by investing in these industries rather than in others.

- iii. Avoidance of penalty

Knowledge of due date for tax payment and prompt payment helps the Taxpayer to avoid the penalty of late payment. Such penalties are avoidable expenses that infringe on the profit and hence profitability index.

- iv. Exemption from capital tax (CGT)

Stocks and shares investment are exempted from capital gain tax (CGT). A Taxpayer's knowledge of this will inform his decision to invest in stocks and shares rather than buildings that attract CGT. This exemption will boost the profit and profitability growth ratios.

- i. Pioneer companies and rural investment allowances

Pioneer companies are granted qualifying capital expenditure on application by issuing them the pioneer company certificate. This benefit may elude any such company that lacks the knowledge. Tax planning by consulting with professional accountants will earn the Taxpayer such benefits. A tax holiday of say three years is usually stated on the pioneer certificate granted and thereafter can be extended on application of the Taxpayer, to five years.

Rural allowances are as well granted companies who qualify and have applied on bases of lack of electricity, bad roads, no water supply etc. Other forms of tax incentives are export processing zone allowance, export free zone allowance, exemption profit of solid minerals, mining etc. This is to encourage investment in these areas. Companies in these industries can take advantage of the provisions of the tax laws.

The various tax incentives provide bases in the tax laws for corporations to plan for taxes in a manner that ensures the amount of tax due is minimized and maximized profitability of the firm. The importance of tax planning is reveal by Kumarasingam (2010) as:

- i. Tax work accounts for almost 40% of revenue of CPA firms in the USA, rank of the revenue is as follows-tax compliance form of consulting and tax planning, and representing clients before government.
- ii. Large firms generally generate more revenue from planning as clients place more reliance on them.

In the light of this, firms derive growth in profitability and therefore engage professional tax consultants to maximize tax advantages of the various tax incentives available to them.

2.3 Advantages and disadvantages of tax incentives

Flatters (2005) identified that the advantages and disadvantages of the various incentives can be analyzed in terms of four criteria:

- i. Effectiveness in stimulating investment;
- ii. Impact on revenue;
- iii. Economic efficiency; and
- iv. Impact on tax administration.

Arguments in favour of investment tax incentives are widely known (Nathan – MSI Group, 2004). According to the Group, the merits of tax incentives include that: Tax incentives clearly enhance returns on investment; they may be justified by positive externalities stemming from investments, they are relatively easy to target and fine tune; they signal openness to private investment; they are useful in a world of capital mobility; they are necessary for responding to tax competition from other jurisdictions; and they compensate for other deficiencies in the investment climate. The group further identified another strong argument in favour of tax incentive to be that, it can enhance revenue by stimulating investments that generate other taxable income via employment and linkage effects.

Tax incentives also offer political advantages over direct expenditure programs to stimulate investment (Wells and Allen, 2001). Finally, tax incentives have been successfully used in well known cases, such as Malaysia, Ireland and Mauritius (Nathan-MSI Group, 2004). The case against tax incentives is less widely understood, but essential to any careful policy analysis. Those who advised against tax incentives argue that:

- i. The actual revenue cost can be high if the investments would have been viable anyway; the incentives are offset by source country tax laws, or tax-favoured investors take business away from taxable producers.
- ii. Tax incentives also direct administrative resources from revenue collection.
- iii. such revenue losses require painful fiscal adjustments in the form of higher taxes on other entities, cuts in expenditure or greater dependence on other costly forms of financing.
- iv. Tax differentials can introduce services economic distortions that reduce efficiency and productivity.
- v. Tax preferences create inequities by favouring some taxpayers over others. This can undermine general compliance

- vi. The cash value of tax incentives stimulates political manipulation and corrupt practices.
- vii. Alternative instruments for promoting investment can have more favourable and lasting effects on productivity, growth and development.
- viii. International experience shows that tax incentives most often do not deliver favourable result (Nathan-MSI Group, 2004).

In summary, there are arguments both for and against the use of investment tax incentives, which must be taken seriously. The application balance will vary according to circumstance. The danger is that in the political discourse, the benefits are usually exaggerated, while the costs are downplayed or ignored. This creates a strong bias towards the implementation of poor tax incentive policies (Nathan – MSI Group, 2004).

2.4 Design of tax incentives

2.4.1 Tax holidays

Tax holidays are the most popular tax incentive among developing countries, but interestingly these are rare, and becoming more so, among developed countries (Zee, Stotsky & Ley, 2002). Blomstrom and Kokko (2003) pointed to the fact these incentives do not require any outlay from public funds as an explanation for their wide spread popularity within developing countries, where public funds are particularly scarce. There is a further advantage since by excluding these firms from the tax base, monitoring and administration costs are avoided by the host country treasury (UNCTAD, 2000). Investing firms are also relieved of the burden of tax administration costs.

However, the advantages of tax holidays are substantial. Besides the difficulty of determining which investments are incrementally generated by the incentive, with the firm removed from the tax base, there is no record of how much tax revenue is foregone (Zee, Stotsky & Ley, 2002). Furthermore, the existence of tax neutral entities increases the opportunities for tax avoidance through transfer pricing and restructuring (McLure, 1999). There also exists a significant danger of another type of rent seeking behaviour through restructuring projects or lobbying for policy extensions to increase the duration of incentive benefits (Wells and Allen, 2001). Even where none of these adverse outcomes emerges, this type of incentive is extremely costly, in terms of taxes foregone.

As for those investors that are attracted by this type of incentive, since they only provide benefits for projects that turn positive projects, those projects that will be most benefited by this incentive are those that are the most likely to have invested regardless (Zee, Stotsky & Ley, 2002). They further posited that there is also a significant bias towards smaller projects with payback periods that will be able to make more substantial use of incentives, but will provide the least of spillover benefit, these types of investments are often quick to move on once the incentive expire, further reducing their value (Wells & Allen, 2001).

2.4.2 Preferential tax rates

This is an effectively a weakened form of tax holidays. To a large extent they maintain the same advantages and disadvantages, but the differences on aggregate appear to be more position (Zee, Stotsky & Ley, 2002). Integrating firms into the tax base from the beginning ensures that at least some tax revenue will be received from any profit made. The disadvantage is that the treasury and the firm must go through the usual process compliance monitoring and tax returns respectively. However, since these firms are part of the tax base, foregone tax revenues can be explicitly calculated, improving the transparency of the policy (Zee, Stotsky & Ley, 2002).

Policies based on preferential tax rates reduce the problems associated with tax holidays. Nevertheless, these incentives still maintain, at least in part, most of the same problems as the tax

holidays and as such, despite exceeding the usefulness of tax holidays, remain problematic policy instruments (Farrell, Remes & Schulz, 2004).

2.4.3 Tariff and duty incentives

Exemption from import and/or export tariffs are common worldwide (Zee, Stotsky & Ley, 2002). UNCTAD (2000) observed that there are several ways in which these can be used to insensitive investment. Governments can grant protective import tariffs on final goods that protects an investor's local markets. Another option is give exemptions to import tariff on capital goods, reducing the cost of investment to firms. The third option is to grant firms exemptions from taxes for their inputs and/or exemptions from export taxes for their output product. Export processing zones are a popular means of applying these types of trade based tax incentives (Zee, Stotsky & Ley, 2000).

This particular version of incentives strays into the region of trade reform. This is essentially a protectionist policy since it gives advantages to domestic firms. The evidence on these policies is that they promote efficiency and market distortions are to be avoided (UNCTAD, 2000). General reforms to trade policy avoid the distortions caused by protectionism. Also, where incentives are offered for, "export only" producers, there are often problems with corruption and/or lack of enforcements, resulting on leakages into the domestic market (Zee, Stotsky & Ley, 2002). These types of policies also risk violating World Trade Organization (WTO) rules (Blomstrom & Kokko, 2003).

2.5 Reasons for government offering tax incentives

While the existence of signally effects supports the decisions of governments to provide incentives, this can easily lead to "keeping up with the neighbours" situation (Oman, 2000). Indeed, when Rematex announced its decision to invest over R1bn in Namibia over South Africa, the South Africa Government took criticism, for not offering better incentives. The government defended its stance by saying that South Africa did not want to involve its self in such a "race to the bottom", meaning that they would not compete on incentives (Leuvenink, 2001).

Ireland's success in attracting FDI is attributed to strong fundamentals including low corporate taxes, access to skilled labour, first class infrastructure and access to the EU market (Blomstrom & Kokko, 2003). Intel, in deciding to invest in Costa Rica, claimed that the most important reason for the decision rested on a good match of the fundamental factors that they required (Spar, 1998). These examples lend support to the hypothesis that the popularity of investment incentives was partially caused by a misunderstanding of what really drove all these success stories.

2.6 Tax incentives in Nigeria

The Nigerian Government has put in place a number of investment incentives for the stimulation of private sector investment from within and outside the country. While some of these incentives cover all the sectors, others are limited to some specific sectors. The nature and application of these incentives have been considerably simplified. The incentives include:

2.6.1 Companies income tax

The Companies Income Tax Act has been amended in order to encourage potential and existing investors and entrepreneurs. The current rate in all sectors, except for petroleum, is 30 per cent.

2.6.2 Pioneer status

The grant of pioneer status to an industry is aimed at enabling the industry concerned to make a reasonable level of profit within its formative years. The profit so made is expected to be ploughed

back into the business (Carmichael, 2006). According to Ola (2000), pioneer status is a tax holiday granted to qualified or (eligible) industries anywhere in the Federation and seven year tax holiday in respect of industries located in economically disadvantaged local government area of the Federation. At the moment, there is a list of 69 approved industries declared pioneer industries, which can benefit from tax holiday.

The Industrial Development Income Tax Act (IDITA), (1971), as amended identified that to qualify, a joint venture company or a wholly foreign-owned company must have incurred a capital expenditure of not less than five million naira whilst that of qualified indigenous company should not be less than N150,000. In addition, an application in respect of pioneer status must be submitted within one year the applicant company starts commercial production otherwise the application will be time-barred.

2.6.3 Tax incentives in the Nigerian Free Trade Zones

According to NEPZA (2004) under section 8 of the Act, Nigeria Export Processing Zones Act No 63 of 1992, approved enterprises operating within Free Zones shall be exempted from all Federal, State and Local Government taxes, levies and rate. Section 18 (1) further provides that all legislative provisions pertaining to taxes shall not apply within the Free Zones.

Also Zee, Stotsky and Ley (2002), investigated the cost effectiveness and the comparative merits of alternative forms of such incentives. Their finding was that the tax incentives are useful for the rectification of market features and that the incentives that provide faster recovery of investment cost are preferred. A survey of 600 executives of large multinational firms from 7 countries; Honkong, Singapore, Australia, Canada, PR China, US and UK, carried out by Simmons (2003), showed that there is significant positive correlation between indices of the attractiveness of the tax system of the selected countries and the size entries of FDI.

Rochananonda (2006) applied the effective tax rate as the indicator of FDI policy to trace the direction of economic development and analyzed the impact of tax incentives of FDI in 14 productive sectors. The sectors were grouped into three thus; export-oriented sector, cross-border sector and domestic-specific sector. The study revealed that the overall tax rate was 17% while the statutory tax rate was 30% of net profit indicating that many tax incentives have been introduced. Secondly, the tax incentives were not evenly distributed but concentrated more on export-oriented sector.

Klemm and VanParys (2012) used a panel of African Caribbean and Latin American countries to test for tax competition in tax incentives on FDI and total investment. They found out that countries react to other counties' tax incentives, just as they do to their tax rates. They also found out that FDI increases if tax incentives, particularly, tax holidays, are offered. Morisset and Pirnia (2001) however differed in their literature review of tax policy and foreign direct investment. They observed that tax incentives neither makeup for serious deficiencies in a country' investment environment nor generate the desired externalities. They concluded that long-term strategies to improve human and physical infrastructure and where necessary, to streamline government policies and procedures, are more likely than incentives to attract genuine long-term investment.

3.1 Research methodology

Ex-post facto design was used for the study. This is because; exempt excise duties of companies in the Calabar Free Trade Zone already exist. The 48 companies operating in the Calabar Free Trade Zone were adequately used. The hypothesis was tested using, the independent sampled t-test.

Table 1
Independent t-test

Classification			Number of	Mean	Std. Deviation	t-value	Eta Squared	Sig
Profit With Taxes	Exempt		48	253.0708	350.07458	1.324	.018	0.16
Profit Without taxes	Except		48	172.1630	237.87061			

Source: Fieldwork, 2017

Descriptive statistics and independent t-test for hypothesis one: Table 4.3 shows the result of the independent samples t-test conducted to determine if there is a significant difference between the effect of profit with exempt profit taxes and profit without exempt profit taxes on the profitability of companies in the Calabar Free Trade Zone. The Levene's test for equality of variances gives a significant value of .110. This means that the data does not violate the assumption of equal variance since it is larger than .05. There is a significant difference between the effect of profit with exempt profit taxes (M=253.0708, SD=350.07458), and profit without exempt profit taxes on companies in the Free Trade Zone (M= 172.1630, SD= 237.87061); $t(94) = 1.324, p=.016$. The magnitude of the differences in the means is of high effect (eta squared = 0.18). Thus, H_0 is rejected and H_1 is retained. This indicates that there is any significant difference between the effect of profit with exempt profit taxes and profit without exempt profit taxes on the profitability of companies in the Calabar Free Trade Zone.

This finding was not in consonant with Morisset and Pirnia (2001) who found out that tax incentives neither makeup for serious differences in a country's investment environment nor generate the desired externalities and therefore have negative influence on profitability. The findings of this study also revealed that tax incentives are important determinants of firm performance. This result is in line with findings arrived at by Zee, Stotsky and Ley (2002) who in their study classified tax incentives to be related to firm performance (profitability).

5. Conclusion and recommendations

This study has established that the various tax incentives granted to companies operating in the Free Trade Zones in Nigeria have propelled growth in corporate earnings. This was substantiated by the fact that the exempt profit taxes and *exempt* customs duties have positively influenced corporate profitability of companies in Calabar Free Trade Zone (CFTZ). Therefore, tax incentive policies for companies operating in the Free Trade Zones have achieved the expected objectives by government which included aggressive drive of growth and earnings of companies and hence, increased investments in the Zones.

It is also recommended that the government should sustain the tax incentives in order to maintain industrial and economic development growth potentials of the Zone and that of the nation as a whole. If these incentives are sustained, the government on the other hand, tends to recover revenue lost to tax incentives from personal income tax of employees and sales taxes of products generated by the industrial growth of the Zone.

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