

Business groups, taxes and accruals management

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Abstract:

This paper provides evidence that Belgian business group member firms are subject to lower effective tax rates (ETRs) and face a less positive association between pre-tax income and ETRs, compared to independent firms. These findings suggest that firms belonging to a business group apply efficient tax planning across group entities. As a rationalization for this, we hypothesize that group firms strategically adjust firm-level reported earnings levels in response to tax incentives. We find evidence consistent with this hypothesis, in that the intrinsic negative association between total accruals and operating cash flows is more (less) pronounced for group firms facing a positive (zero) marginal tax rate status compared to independent firms. In addition, we find that a group firm's net tax-paying situation is an important determinant of its discretionary accruals management level. Finally, we identify intra-group receivables as important tax-reducing accruals components. Results are robust to alternative model specifications, variable definitions and measures.