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RESEARCH ARTICLE

Taxation and Financial Performance of an Insurance Company in Nigeria: A Study of Consolidated Hallmark Insurance Plc

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ABSTRACT

This study was on the effect of taxation on the financial performance of insurance companies in Nigeria. The specific objectives were to examine the effect of income tax on the Gross premium income of Consolidated Hallmark Insurance Plc; to assess the effect of income tax on the investment income of Consolidated Hallmark Insurance Plc, and to evaluate the effect of income tax on Total comprehensive income of Consolidated Hallmark Insurance Plc. The study used Ex-post facto research design. Three hypotheses were formulated and tested using Ordinary least square regression as an analytical technique. It was found that income tax has no significant effect on the gross premium income of Consolidated Hallmark Insurance Plc, the p-value at 0.2796 being higher than the level of significance of 0.05. Next was that income tax has no significant effect on the investment income of Consolidated Hallmark Insurance Plc, the p-value at 0.0730 being higher than the level of significance of 0.05. Lastly, that income tax has no significant effect on the total comprehensive income of Consolidated Hallmark Insurance Plc, the p-value at 0.8621 being higher than the level of significance of 0.05. Based on the findings of the study it was concluded that taxation has no significant effect on the financial performance of an insurance company. In line with the findings of the study, it was recommended that insurance operators should expand their customer base in order to generate more premiums. When they do so they will feel less effect of tax on their operations. Also, investments in the insurance industry should be directed to financial instruments with proven high yields. This will allow the industry to earn more and at the same time feel less effect of taxation.

Keywords: Financial Performance; Taxation; Insurance Company; Nigeria

Introduction

The performance of the Nigerian insurance industry has not been admirable. When examined on an industry-wide scale it is seen as poor. For example, insurance penetration, at 0.31%, is extremely low, even when compared with countries with similar GDP per capita, for example, India with insurance penetration at 3.69% (Coronation Merchant Bank, 2019). Nigeria's insurance industry has not shared in the growth experienced by other Nigerian financial services, notably banks, pension funds and mutual funds. In fact, it has hardly grown in real terms over 10 years. Without scale, the industry suffers from poor returns on equity (Coronation Merchant Bank, 2019). Insurance density (another industry wide performance indicator of the industry) is at 8US Dollars (which is equivalent to N3044 as at April 15, 2021) (Atlas Magazine, 2021). However, on a firm specific level the performance of lots of insurance companies are different. A lot through their respective annual reports are declaring profits. For example, Consolidated Hallmark Insurance Plc in 2020 financial year had a Gross premium income of ₦7,202,245,287 as against ₦6,323,411,221 in 2019. Investment income was at ₦424,974,702 in 2020 and ₦576,670,465. Total comprehensive income was ₦404,031,900 in 2020 and ₦470,193,391. A unique rider in the report is the declaration of profit before and after tax. In 2020 it was ₦587,177,871 and ₦404,031,900 respectively. Previously in 2019 it was ₦586,295,784 and ₦470,193,391 respectively.
A key differentiator in the both categories of profits is income tax. This is the type of tax that governments impose on income generated by businesses and individuals within their jurisdiction (Berry-Johnson, 2020). Personal income tax is a type of income tax that is levied on an individual's wages, salaries, and other types of income while Business income taxes apply to corporations, partnerships, small businesses, and people who are self-employed. Income is the most widely used tax base internationally (Skipper, 2001). Many policy makers consider net income to be the best measure of ability to pay and so the most equitable means of taxing both individuals and businesses. Significant deductions and other

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tax concessions are typically provided to derive net taxable income. For the year 2020 and 2019 the income tax paid by Consolidated Hallmark Insurance Plc was ₦174,145,971 and ₦116,102,392 respectively. This represents 43.1 percent and 24.69 percent of the profits after tax for the years 2020 and 2019. Being a regular and compulsory requirement, income tax is always attended to by insurance companies. It is an obligation that cannot be neglected. In this position it exerts some measure of influence on the financial performance of insurance companies as it is derived from profits made. Corporate income tax reduces the amount of income individuals have available to spend, save, or invest. Of course, any tax has this result. The question is whether the taxes achieve the same end more efficiently or with fewer undesirable side effects. In line with this background this study seeks to determine the effect of taxation on financial performance of insurance companies in Nigeria.

The market potential of the Nigerian insurance industry is quite huge yet the volume of patronage reflects poor followership. This is a market that has a large population of which a significant part of it is within the working-class category and in need of insurance cover. The market has large financial inclusion which platform can be taken advantage of by the insurance industry. Also, economic activities in the country is high being an import dependent country with high consumption rate. Despite these market potentials the poor performance of the industry has persisted for a long number of years. The industry has failed repeatedly to contribute up to one percent of gross domestic product of Nigeria's economy. As at 2019 its penetration was 0.31 percent. It is seen that on an industry wide scale the performance of the Nigerian insurance industry has been poor.

Quite a number of factors have been empirically determined as affecting the performance of the insurance industry. Some of these include employee skill, macroeconomic variables – inflation, poverty rate, per capita income, exchange rate, interest rate, etc., location of the branch in the country – Northern Nigeria hardly practice contemporary insurance, and many more. These factors were linked in various empirical studies to the insurance business while examining the industry as a whole. However, on a firm specific level the performance of lots of insurance companies are different. The respective income categories on their annual reports have been mostly higher than that of the previous year. These include gross premium income, investment income and total comprehensive income.

A company like Consolidated Hallmark Insurance Plc's 2020 financial year declared a profit before and after tax of ₦587,177,871 and ₦404,031,900 respectively. The key difference between both profits is the income tax. In other words, income tax is an important variable in the measurement of the performance of the insurance industry. Empirical evaluation of the financial performance of the insurance industry on a firm-specific level has failed to use tax as an independent variable. It is this gap in empirical considerations that necessitated this study. Therefore, this study seeks to determine the extent to which tax affects the respective incomes that an insurance company declares.

Objectives of the Study

The main objective of the study is to investigate the effect of taxation on the financial performance of insurance companies in Nigeria. The specific objectives of the study are:

I. To examine the effect of income tax on the Gross premium income of Consolidated Hallmark Insurance Plc
II. To assess the effect of income tax on the investment income of Consolidated Hallmark Insurance Plc

Statement of Hypotheses

The following null hypotheses were formulated for the study:

I. Income tax has no significant effect on the gross premium income of Consolidated Hallmark Insurance Plc
II. Income tax has no significant effect on the investment income of Consolidated Hallmark Insurance Plc

Time Scope of the Study

The study is time series based as already existing data was used. The period of the study is from 2007 to 2020, a period of thirteen years. The base year of 2007 was chosen given that it marked the end of the most recent recapitalization exercise in the Nigerian insurance industry. The specific firm focused on is Consolidated Hallmark Insurance Plc. The choice of Consolidated Hallmark Insurance Plc was given following a merger in 2007

recapitalization exercise, Consolidated Hallmark Insurance Plc emerged as one of the top ten General Business and Special Risk Insurance underwriters in Nigeria. In the last twelve years, the company has played a leadership role in the underwriting of key transactions in Aviation, Oil & Gas, Marine Cargo and Hull Business as well as in Motor insurance business. Presently it is the second insurance company in Nigeria to obtain the prestigious ISO 9001:2015 (Quality Management Systems Certification). The end year of 2020 was selected given it was the year the latest report available from the selected company ended.

Theoretical Review

This study was based on Resource-Based View Theory. This theory was propounded by Wernerfelt in 1984. Pearce and Robinson (2011) define the resource-based view as a method of analyzing and identifying a firm's strategic advantages based on examining its distinct combination of assets, skills, capabilities and intangibles as an organization. This theory views the firm-specific factors and their effect on performance. Grant (1991) views the firm as a bundle of resources which are combined to create organizational capabilities which it can use to earn above average profitability and in turn settle its tax obligations. Firms develop competencies from these resources and when they are well developed, these become the source of the firm's sustainable financial performance. Simply put, resource-based theory focuses on the internal factors that affect the performance of a firm.

This study is anchored on resource-based theory. Income or Corporate tax is a statutory levy that must be paid by a business firm. It is an internal factor in the books of a company. Given its financial nature it affects the financial output of a company. For instance, when tax is deducted from Profit-before-tax it gives the final profit of the firm. In this example the size of the tax can affect the volume of profit that will be shared to stakeholders. The resource-based theory helps to see tax as a critical resource that should be managed in a manner that allows the obtaining of new resources.

Empirical Review

Albertazzi and Gambacorta (2006) investigated how bank profitability is affected by corporate income tax (CIT). Content analysis was applied. The study finds the extent to which a bank is able to shift its tax-burden forward to its lenders, depositors, and purchasers of fee-generating services. Jens and Schwellnus (2008) assessed the effect of corporate income taxes on two of the main drivers of growth, profitability and investment of over the time period of 1996-2004. The results suggest that corporate income taxes reduce investment through an increase in the user cost of capital.

Desai and Dharmapala (2009) examined whether corporate tax avoidance activities advance shareholders' interests. The ordinary least squares (OLS) estimates indicated that the average effect of tax avoidance on firm value is not significantly different from zero, but is positive for well governed firms, as predicted by an agency perspective on corporate tax avoidance. Rohaya, Nor'Azem and Bardai (2010) examined the association between income tax and profitability of corporate institutions in Malaysia. The conclusion is that corporate income tax adversely affects the profitability of corporate institutions but has a positive relationship with the firm size and age of companies.

Adegbie and Fakile (2011) studied the relationship between Company Income Tax and Nigeria Economic Development relationship. It was concluded that there is a significant relationship between company income tax and Nigerian economic development. And that tax avoidance and evasion are major hindrances to revenue generation. Raza, Ali and Abassi (2011) examined the effect of corporate income tax and firm size on investment in Pakistan. The result concluded that there is a negative relationship between Corporate Income Tax and Investment, while firm size and investment reveal a positive relationship with each other.

Lucaman (2012) sought the connections between revenue smoothing and the tax ratio on revenue and profitability. The findings of the study show that there is significant relationship among smooth revenue, tax on revenue and the profitability ratio of the enterprise. Kipngetich (2012) did a study on the relationship between tax paid and level of investment for the quoted companies in Kenya. It was concluded that there is a relatively strong relationship between tax paid and investment made especially pronounced in the financial sector and agricultural sector. Taufik and Barne (2012) used square root transformation of ordinary least square to investigate whether tax generate more on economic development. The study revealed that tax revenue helps to accelerate economic development in an environment that is open trade without unnecessary policies that hinders business transactions.

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Margereta and Asa (2012) used fixed effect regression on a panel data of OECD countries of about 25 between the period 1970 – 2010, and found that the taxation of corporate entities and that of personnel income does not have any significant impact on economic growth. Gatsi, Gadzo and Kportorgbi (2013) determined the effect of corporate income tax on financial performance. The study reveals that there is a significant negative relation between corporate income tax and financial performance. On the other hand, firms' size, age of the firm and growth of the firm show a significant positive relationship with financial performance.

Beigi, Rafat and Panah (2013) investigated tax effects over the profitability indices. Results of the regression indicate that the debts ratio to asset and the type of the industry shows a negative effect on profitability and capital ratio to asset and the size of the company indicated positive significant effects on profitability index. Njuru, Ombuku, Wawire and Okeri (2013) investigated the impact of taxation on private investment in Kenya. The study found that VAT, income tax and establishment of Kenya Revenue Autonomy (K.R.A) had negative impact on private investment, while excise tax, import tax amnesty impact positively on private investment.

Asogwa and Okeke (2013) examined the impact of Value added tax on Investment. The result show that value added tax has significant effect on investment growth in Nigeria. The sign of VAT does not conform to prior expectation of the model. Yan and Lu (2013) examined the effect of Value added tax transformation on non-current assets investment based on the data of Jiang Su listed companies. Overall, the transformation of Value added tax has a positive effect on management and development of Jiangs listed companies. Mucai, Kinya, Noor and James (2014) studied tax planning and financial performance of small-scale enterprises in Kenya. It was found that the legal forms of small enterprises have no significant relationship. The study established that small scale enterprises should be ready to seek advice on tax planning. It was further established that there is a need to have NGOs to sensitize the tax payers on how to do formal tax planning and, as such, increase their business profitability.

Oloichi (2014) examined the effect of Company Income Tax (CIT) on investment decision of companies liable under the company income tax act in Nigeria. Findings revealed that company income tax has influence on the rate of return on investment and investment evaluation criteria. Edame and Okoi (2014) examined the impact of Taxation on investment and economic growth in Nigeria from 1980-2010. The result of the analysis showed that the taxation is negatively related to the level of investment and the output of goods and services (GDP) and is positively related to Government Expenditure in Nigeria. Adegbite (2015) assessed the effect of corporate tax on revenue profile in Nigeria and also examined the impact of corporate tax revenue on economic growth in Nigeria. It was concluded that corporate income tax has positive significant impact on revenue profile in Nigeria which directly enhanced growth in Nigeria.

Madugba, Ekwe and Kalu (2015) worked on corporate tax and revenue generation. The result of the correlation showed a positive significant relationship between Petroleum Tax Income and TCR. Also, it showed a positive significant relationship between Companies' Income Tax (CIT) and Total Consolidated Revenue (TCR). The regression result revealed a negative significant relationship between Petroleum Tax Income and Total Consolidated Revenue and Companies Income Tax and TCR. Chude and Chude (2015) ascertained the impact of taxation on the profitability of companies in Nigeria. The study revealed that the level of company tax has significant effect on the profitability, that company income tax (CIT) has significant effect on profitability.

Ezejiofor, Adigwe and Echekoba (2015) assessed whether tax as a fiscal tool affect the performance of the selected manufacturing companies in Nigeria. It was found that Taxation as a fiscal policy instrument has a significant effect on the performance of Nigeria manufacturing companies. Goh (2016) investigated the relationship between firm cost of equity and corporate tax avoidance. The result further revealed that this effect was stronger for firms with better outside monitoring. This was evident from firms with better information quality and likely to realize higher marginal benefits from tax savings. Heitzman and Ogneva (2016) examined the relationship between corporate tax planning and stock returns of all US firms traded on NYSE, AMEX or NASDAQ from 1988 to 2013, using panel regression analysis. The study established that high tax planning firms indeed earn higher returns, but only when tax enforcement is low. The study also discovered that small firms have less diversified tax strategies, as compared to large and complex firms, as a result of lack of scale and complexity, high exposure to adverse consequences of government actions and inability to finance the high fixed costs of tax planning strategies.

Ilaboya, Izevbekhai and Ohiokha (2016) assessed the impact of tax planning on firm value. Content analysis was used. The review revealed a general absence of theory in explaining the issue of tax planning. Also, the bulk of empirical studies existing on the dynamics of tax planning and firm value are from developed economies leaving out

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developing countries. Ofoegbu, Akwu and Oliver (2016) examined the effect of tax revenue on the economic development of Nigeria. Findings show a positive and significant relationship between tax revenue and economic development. Bauer, Kourouxous and Krenn (2018) undertook a review of the influence of taxation on agency conflicts between firm owners and managers. The review indicates that there are many cases in which taxes influence the behavior of all contracting parties as corporate taxes do not only reduce a firm's profit but can also alter the manager's optimal compensation contract.

Gap in Empirical Studies

Variables: Empirical evaluation of financial performance of the insurance industry on firm specific level failed to use tax as an independent variable.
Time Scope: The end year of this study was 2020 which is an improvement on the time previous empirical studies were conducted.
Industry: Empirical studies reviewed did not cover the insurance industry.
It is these gaps in empirical considerations that were addressed by this study.

Methodology

The study was based on *Ex-post facto* research design. This design became necessary considering that the study was time-series base. Data used was sourced from the annual reports of Consolidated Hallmark Insurance Plc.

Model Specification

In line with each objective of the study the following models were designed:
Model for hypothesis one:
$GPI = \beta_0 + \beta_1 IT + \mu_t$ (i)
Where: GPI = Gross Premium Income, IT = Income Tax
Model for hypothesis two:
$INVI = \beta_0 + \beta_1 IT + \mu_t$ (ii)
Where: INVT = Investment Income, IT = Income Tax

Description of Model Variables
Dependent Variable

Gross Premium Income: This is money that an insurer has earned from premiums and eliminates any money that is or will be paid out elsewhere from those premiums.

Investment income: This is money that is received in interest payments, dividends, capital gains realized with the sale of stock or other assets, and any other profit made through an investment vehicle.

Independent Variable
Income tax: This is a levy placed on the profit of a firm.

Data Analysis Technique

Stationarity test was carried out to determine appropriateness of data for the study. This involved the use of Phillips Perron method of unit root test. The goodness of fit of each model was assessed using the Co-efficient of Determination. Thereafter, Ordinary Least Squares technique was applied to test the formulated hypotheses.

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Data Analysis
Stationarity Test

A stationarity test was carried out to guard against spurious regression result. This was done using the Phillips Perron unit root test method.

Table 1: Result of Stationarity Test at Level

Variable	*Phillips-Perron test statistic*	*Critical value @ 5%*	*Order of Integration*	*P-value*
COM	-12.99159	-1.958088	1(1)	0.0000
INV	-3.597350	-1.958088	1(1)	0.0010
PRE	-8.925868	-3.658446	1(1)	0.0000
TAX	-3.529028	-1.958088	1(1)	0.0012

Source: Author's E views 10 output, 2022

Where:
COM = Comprehensive income
INV = Investment income
PRE = Premium income
TAX = Income tax

Table 1 reveals that the time series that were stationary at first difference were COM, INV, PRE and TAX. This is evidenced by each Phillips-Perron test statistic at first difference being less than their respective Critical value @ 5%. This is corroborated by their respective p-values being lower than 0.05 (the level of significance) which shows statistical significance.

Table 2: Test of Hypothesis One
Dependent Variable: DPRE
Method: Least Squares
Date: 10/16/22 Time: 03:32
Sample (adjusted): 1 14
Included observations: 13 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	5.68E-05	7.60E-05	0.747693	0.4638
DTAX	-0.421638	0.378826	-1.113014	0.2796

R-squared	0.061209	Mean dependent var	2.52E-05
Adjusted R-squared	0.011799	S.D. dependent var	0.000325
S.E. of regression	0.000323	Akaike info criterion	-13.14715
Sum squared resid	1.98E-06	Schwarz criterion	-13.04767
Log likelihood	140.0451	Hannan-Quinn criter.	-13.12556
F-statistic	1.238801	Durbin-Watson stat	2.184148
Prob(F-statistic)	0.279586		

Source: Author's EViews 10 Output, 2022

Decision: Table 2 shows that p-value at 0.2796 is higher than the level of significance of 0.05. Thus, we accept the null hypothesis and conclude that Income tax has no significant effect on gross premium income of Consolidated Hallmark Insurance Plc

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Table 3: Regression Result for Test of Hypothesis Two

Dependent Variable: DINV
Method: Least Squares
Date: 10/16/22 Time: 03:35
Sample (adjusted): 1 14
Included observations: 13 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-5.69E-06	6.87E-05	-0.082915	0.9348
DTAX	0.107839	0.056829	1.897619	0.0730

R-squared	0.159328	Mean dependent var	2.52E-05
Adjusted R-squared	0.115082	S.D. dependent var	0.000325
S.E. of regression	0.000306	Akaike info criterion	-13.25754
Sum squared resid	1.78E-06	Schwarz criterion	-13.15806
Log likelihood	141.2042	Hannan-Quinn criter.	-13.23595
F-statistic	3.600956	Durbin-Watson stat	2.221061
Prob(F-statistic)	0.073048		

Source: Author's E views 10 Output, 2022

Table 3 shows that p-value at 0.0730 is higher than the level of significance of 0.05. Thus, we accept the null hypothesis and conclude that income tax has no significant effect on investment income of Consolidated Hallmark Insurance Plc.

Discussion of Findings

Hypothesis One

The result of hypothesis one test shows that if each index for income tax is held constant, gross premium income in Nigeria will increase by an intercept value of 0.0000568 basis points. Also, it is seen that income tax has a regression coefficient of -0.421638. This is a negative coefficient. It shows that there is a decreasing interaction between premium income and income tax in Nigeria. That is to say for any unit increase in income tax, gross premium income will decrease by 0.421638 basis points. The Adjusted Co-efficient of Determination which was 0.011799 shows that in the model used, the independent variable (income tax) can only explain 1.1799 percent of any variation seen in gross premium income. The remaining 98.8201 percent can be attributed to other variables not used in the model. The p-value of life income tax at 0.2796 is higher than the level of significance of 0.05. It shows there was statistical insignificance. In other words, there was not enough evidence against the null hypothesis. The finding of hypothesis one test agreed with Rohaya, Nor'Azem and Bardai (2010) who fund that corporate income tax adversely affects the profitability of corporate institutions but has a positive relationship with the firm size and age of companies.

Hypothesis Two

The result of hypothesis two test shows that if each index for income tax is held constant, investment income will decrease by an intercept value of -0.00000569 basis points. Also, it is seen that income tax has a regression coefficient of 0.107839. This is a positive coefficient. It shows that there is an increasing interaction between income tax and investment income. That is to say for any unit increase in income tax, investment income will increase by 0.107839 basis points. The Adjusted Co-efficient of Determination which was 0.115082 shows that in the model used, the independent variable (income tax) can only explain 11.5082 percent of any variation seen in investment income. The remaining 88.4918 percent can be attributed to other variables not used in the model. The p-value of

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income tax at 0.0730 is higher than the level of significance of 0.05. It shows there was statistical insignificance. In other words, there was not enough evidence against the null hypothesis. The finding of hypothesis two test disagreed with Lucaman (2012) who found that there is significant relationship among smooth revenue, tax on revenue and the profitability ratio of the enterprise.

Summary of Findings

The following are the findings of the study:

I. Income tax has no significant effect on gross premium income of Consolidated Hallmark Insurance Plc. The p-value at 0.2796 is higher than the level of significance of 0.05.
II. Income tax has no significant effect on investment income of Consolidated Hallmark Insurance Plc. The p-value at 0.0730 is higher than the level of significance of 0.05.

Conclusion

Being a regular and compulsory requirement, income tax is always attended to by insurance companies. It is an obligation that cannot be neglected. In this position it exerts some measure of influence on the financial performance of insurance companies as it is derived from profits made. Corporate income tax reduces the amount of income individuals have available to spend, save, or invest. Of course, any tax has this result. The question is whether the taxes achieve the same end more efficiently or with fewer undesirable side effects. In line with this background this study examined the effect of taxation on financial performance of insurance companies in Nigeria. Based on the findings of the study it was concluded that taxation has no significant effect on financial performance of an insurance company.

Recommendations

Based on the findings of the study the following recommendations were made:

I. Insurance operators should expand their customer base in order to generate more premium. When they do so they will feel less effect of tax on their operations
II. Investment of the insurance industry should be directed to financial instruments with proven high yield. This will allow the industry to earn more and at the same time feel less effect of taxation.

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