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Article

When Profits Lie: How Book-Tax Differences Signal Declining Firm Performance

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Abstract

Many firms report significant differences between accounting profits and taxable income, which can mislead investors, creditors, and regulators about the firm's true financial health. These book-tax differences often result from earnings management or aggressive tax strategies, creating financial, operational, and reputational risks. Over time, such discrepancies can undermine investor confidence, reduce profitability, and limit a firm's long-term growth and sustainability. Hence, the study examined the effect of book-tax differences on the performance (proxy by return on asset) of listed manufacturing firms in Nigeria. An ex-post facto research design was adopted, covering a population of 70 listed manufacturing firms, from which a purposive sample of 53 firms was selected for the period 2014 to 2024. Secondary data were obtained from audited financial statements and annual reports of the sampled firms. The hypothesis was tested using a fixed effects model, selected after the Hausman specification test at a 1% significance level. The finding revealed that book-tax differences have a negative and statistically significant effect on firm performance ($\beta = -0.303162$, $p = 0.0000$), leading to the conclusion that larger discrepancies between accounting and taxable income reduce profitability and weaken the financial sustainability of manufacturing firms in Nigeria. Therefore, financial managers and chief accountants of listed manufacturing firms should implement more rigorous internal monitoring and reconciliation procedures between accounting income and taxable income by regularly analyzing and minimizing unnecessary discrepancies in order to ensure that reported profits accurately reflect operational performance, reduce potential risks associated with aggressive tax planning or earnings management.

Keywords: Book-Tax Differences; Firm Performance; Return on Asset

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1. Introduction

Amid today's fast-changing corporate world, financial reporting has become a critical component of corporate governance, investment decision-making, and regulatory oversight. Companies are expected to provide accurate and reliable financial statements that reflect their economic realities to investors, creditors, and other stakeholders (Ayyoobi, 2025). At the same time, tax obligations compel firms to report taxable income according to statutory requirements, which often differ from the accounting income reported in financial statements. These differences are not merely technicalities; they can reveal the strategies that firms use to manage profits,

minimize taxes, and influence perceptions of financial health (Orji & John-Akamelu, 2023). As organizations grow and competition intensifies, the pressure to meet performance targets and maximize shareholder value can create incentives for managers to manipulate either accounting records or tax reporting. The discrepancies that emerge between reported accounting profits and taxable income, commonly referred to as book-tax differences, have drawn increasing attention from researchers, regulators, and practitioners (Hastuti et al., 2025).

Book-tax differences have gained significant relevance in today's business environment due to the complex interplay between accounting standards, tax regulations, and corporate strategy (Hiifan et al., 2025). These differences arise from variations in the recognition of revenues and expenses, timing of deductions, or permanent items that are treated differently for accounting and tax purposes. While some discrepancies are normal and expected, large or persistent differences may indicate deliberate actions taken by management to reduce tax liabilities or to present a more favorable financial picture (Ologun & Gbadebo, 2024). In an era where investors are increasingly sophisticated and regulatory scrutiny is high, these differences can influence perceptions of a firm's integrity and financial health. Furthermore, the rise of multinational corporations operating across jurisdictions with differing tax rules has increased the complexity of managing book-tax differences. Companies may engage in strategies that exploit these differences to optimize tax efficiency, but such actions carry risks that extend beyond taxation. Stakeholders are now more attentive to the signals that these differences send about managerial behavior, the sustainability of earnings, and potential exposure to regulatory penalties.

The effects of book-tax differences on firm performance are multifaceted and significant. Evidence suggests that large or unexplained differences between accounting income and taxable income can serve as indicators of earnings manipulation or aggressive tax planning (Olaoye & Ogunleye, 2024; Orji & John-Akamelu, 2023). When managers use accounting techniques or tax strategies to inflate reported profits or defer tax obligations, they may achieve short-term financial gains but at the expense of long-term stability. Such practices can erode investor trust, increase perceived risk, and negatively affect stock prices and market valuation (Bas & Indrijawati 2020). Additionally, managing book-tax differences often requires resources, including time, expertise, and financial costs, which could otherwise be invested in productive activities that enhance firm performance. Companies that consistently report high book-tax differences may also face increased scrutiny from tax authorities, leading to audits, penalties, or legal challenges, which further strain performance. The relationship between book-tax differences and firm outcomes extends beyond financial metrics to encompass operational efficiency, investment decisions, and strategic planning. Firms with large discrepancies may struggle to maintain sustainable growth, as the short-term benefits of tax management or earnings manipulation can undermine long-term competitiveness (Chukwudi et al., 2020).

Firms are expected to maintain accurate and transparent financial reporting that reflects their true economic performance. This includes a clear correspondence between accounting profits and taxable income. When financial statements are prepared, they should provide stakeholders with reliable information that can guide investment decisions, evaluate managerial effectiveness, and assess the firm's capacity for sustainable growth. A harmonious alignment between accounting and tax reporting promotes confidence among investors, supports efficient allocation of resources, and ensures that firms fulfill their obligations to regulatory authorities (Efenyumi & Nworie, 2025; Ikelegbe et al., 2025). In such a context, financial reports serve as a credible basis for decision-making and allow firms to demonstrate integrity, accountability, and long-term strategic planning. Firms that maintain consistency in reporting are able to establish a reputation for trustworthiness, attract investment, and optimize their operations without unnecessary complications arising from regulatory or stakeholder concerns (Liang et al., 2018).

In practice, many firms experience differences between the profits reported in their financial statements and the taxable income reported to authorities. These differences, known as book-tax differences, may arise from various accounting choices, timing of expense recognition, or tax

planning strategies (Orji & John-Akamelu, 2023). While some variation is unavoidable, large or persistent discrepancies often indicate aggressive management of earnings or tax obligations. Companies may use these differences to reduce tax payments or to present stronger financial performance than is actually the case. Such actions can distort the information available to investors and other stakeholders, making it difficult to accurately assess a firm's financial health. The existence of significant book-tax differences also attracts scrutiny from regulators and tax authorities, increasing the risk of audits, penalties, or legal disputes. As a result, firms face both operational and reputational challenges when the reporting of accounting and taxable income diverges substantially. When stakeholders perceive that a firm manipulates its financial or tax reporting, confidence and trust may decline, leading to reduced market valuation and limited access to capital. Management's focus on tax optimization or earnings manipulation can divert resources away from productive activities, such as investment in innovation, expansion, or human capital development.

Despite the growing body of research on the relationship between book-tax differences and firm performance, several gaps remain in the existing literature. Studies by Hastuti et al. (2025), Hiifan et al. (2025), Ologun and Gbadebo (2024), Olaoye and Ogunleye (2024), Orji and John-Akamelu (2023), Ofor and Akaegbobi (2022), Bas and Indrijawati (2020), Chukwudi et al. (2020), and Evers et al. (2016) have examined the effects of book-tax differences across various sectors and time periods, yet many of these studies were limited in sample size, scope, or theoretical grounding. For instance, several studies focused on fewer than 35 firms, primarily within the consumer goods or banking sectors, and often did not consider firm size as a control variable. Additionally, while prior research has frequently applied regression techniques such as OLS, GMM, or panel least squares, very few studies have anchored their analysis on a robust theoretical framework like Positive Accounting Theory to explain managerial behavior in selecting accounting methods. Furthermore, most studies covered shorter periods, typically ranging from 3 to 10 years, limiting their ability to capture long-term trends in the effect of book-tax differences on firm performance. The present study addresses these gaps by examining 53 listed manufacturing firms in Nigeria over an extended period of 2014 to 2024, incorporating firm size as a control variable, and grounding the analysis within Positive Accounting Theory to provide a more comprehensive understanding of how book-tax differences influence firm performance. Hence, this study ascertained the effect of book-tax differences on the firm performance (proxy by return on asset) of listed manufacturing firms in Nigeria.

2. Literature Review

2.1 Synthesis of Related Findings

Research on the relationship between book-tax differences (BTDs) and firm performance has produced mixed findings across different sectors and contexts. Hastuti et al. (2025) found that neither fixed nor temporary BTDs significantly affected profit growth in consumer goods firms listed on the IDX, suggesting that operational performance primarily drives profitability. Similarly, Bas and Indrijawati (2020) reported that BTDs had no significant impact on earnings quality in Indonesian firms, indicating that not all differences between book and taxable income translate into measurable changes in firm outcomes. These findings highlight that the effect of BTDs may vary across industries and measurement approaches, reflecting underlying heterogeneity in corporate accounting and reporting practices.

Conversely, several studies have documented a positive and significant influence of BTDs on financial performance. Hiifan et al. (2025) observed that BTDs enhanced return on assets (ROA) in listed Nigerian consumer goods companies, while Ologun and Gbadebo (2024) reported similar results for Nigerian deposit money banks, emphasizing the role of tax planning in shaping firm outcomes. Olaoye and Ogunleye (2024) further confirmed that BTDs positively affect ROA in non-financial firms, using a GMM approach over a fourteen-year period. Ofor and

Akaegbobi (2022) also found a statistically significant positive relationship between BTDs and performance in consumer and industrial goods manufacturing firms, demonstrating that precise measurement of BTDs through panel techniques can reveal their beneficial impact. Chukwudi et al. (2020), however, reported a positive but statistically insignificant effect on firm value, reflecting possible differences in sample size, firm selection, or time frame. Collectively, these studies suggest that while BTDs can signal enhanced performance, the magnitude and significance of their impact depend on methodological rigor and sectoral context.

Other research highlights the nuanced effects of BTDs on financial health beyond simple profitability measures. Orji and John-Akamelu (2023) found that temporary and permanent BTDs significantly improved Altman ' s Z-Score in consumer goods firms, whereas total and discretionary BTDs had limited or no impact, indicating that the type of BTD matters in assessing financial stability. Evers et al. (2016) reinforced this perspective through a meta-analysis, demonstrating that BTDs are indicative of opportunistic reporting and earnings management, but that precise computation from tax returns improves explanatory power. These insights collectively suggest that while BTDs can provide signals of firm performance, the relationship is contingent upon the type of difference, measurement precision, and the operational context of the firm. Despite the breadth of existing literature, limited studies have specifically examined the effect of BTDs on the performance of manufacturing firms in Nigeria using comprehensive panel techniques and ROA as a proxy, highlighting a gap that this study seeks to address.

2.2 Theoretical Framework and Development of Research Hypothesis

Positive Accounting Theory was developed in the late 1970s by Ross Watts and Jerold Zimmerman, with their seminal work published in 1978 and later expanded in 1986 (Watts & Zimmerman, 1990). The theory emerged as a response to normative accounting approaches, which focused on prescribing what accounting practices should be. The theory is grounded in empirical observation, aiming to describe real-world accounting behavior rather than prescribing ideal standards. Over the years, Positive Accounting Theory has become widely accepted in accounting research for analyzing the motivations behind financial reporting decisions and understanding their effects on corporate outcomes.

The main postulations of Positive Accounting Theory revolve around the notion that managers act in ways that maximize their utility, often influenced by economic incentives, contractual obligations, and potential consequences from regulators or stakeholders (Kejriwal, 2022). The theory identifies three primary motives that drive accounting choices: debt contracts, political costs, and management compensation. Debt contracts suggest that firms may choose accounting methods that minimize the likelihood of violating debt covenants. Political costs arise when large or high-profile firms might manipulate accounting figures to reduce scrutiny from regulators or the public (Milne, 2002). Management compensation is linked to performance-based pay, motivating managers to adopt accounting practices that enhance reported earnings and personal rewards. PAT emphasizes that accounting decisions are not arbitrary but are strategic responses to the economic and contractual environment in which managers operate.

Positive Accounting Theory (PAT) is particularly relevant to understanding book-tax differences in the Nigerian manufacturing sector because it links managerial incentives to financial reporting behavior. In this context, managers may deliberately manipulate accounting income relative to taxable income to achieve specific objectives, such as meeting performance targets, minimizing tax liabilities, or influencing stakeholder perceptions. These strategic choices create book-tax differences that are not merely accounting noise but signals of managerial decision-making. When such differences are large or persistent, they can distort the firm's reported profitability, potentially affecting investor confidence, access to financing, and long-term operational sustainability. By applying PAT, this study interprets BTDs as intentional managerial actions that can directly impact firm performance, providing insight into how

accounting and tax strategies translate into real economic consequences in the manufacturing sector. Hence, we hypothesise that:

H_1 : Increases in book-tax differences will negatively affect firm performance.

3. Methodology

The study adopted an ex-post facto research design because the variables under investigation have already occurred and cannot be manipulated by the researcher (Elom et al., 2025). This design allows for the analysis of relationships between variables as they naturally exist, providing insights into how one variable influences another (Ikwuo et al., 2025; Muojekwu et al., 2025; John-Akamelu et al., 2025). By employing this approach, the study can examine the effect of book-tax differences on firm performance without interfering with the operations of the sampled firms. The ex-post facto design is suitable for this research since it enables the investigation of causal relationships based on historical financial data over an 11-year period, from 2014 to 2024.

The target population comprised all manufacturing firms listed on the Nigerian Exchange Group as of 2024. At this time, the sector included 70 firms spanning various sub-sectors such as consumer goods, industrial goods, and construction. The population encompasses firms that are publicly accountable to shareholders and regularly submit audited financial statements, which ensures the availability and reliability of the data required for the study. This population provides a comprehensive view of the manufacturing industry in Nigeria and serves as an appropriate context for analyzing the effect of book-tax differences on firm performance.

A purposive sampling method was applied to select 53 manufacturing firms from the 70 listed, based on the availability of complete financial data from 2014 to 2024. Seventeen firms were excluded due to missing or incomplete records for the base year, which could compromise the reliability of the analysis. This approach ensures that the study examines firms with continuous financial reporting over the period, allowing for consistent measurement of both independent and dependent variables. The study utilized secondary data collected from the audited financial statements and annual reports of the selected manufacturing firms. The data covers the period from 2014 to 2024, with 2014 selected as the base year following the mandate by the Federal Inland Revenue Service (FIRS) requiring non-resident companies to file comprehensive tax returns like their Nigerian counterparts. Data included information needed to calculate book-tax differences, firm size, and return on assets. Financial statements are considered reliable sources since they are prepared under statutory accounting standards and audited for accuracy.

Table 3.1 Operationalization of Variables

Variable	Proxy	Measurement	Source
Dependent Variable	Firm Performance	Return on Assets (ROA)	(Nworie & Mba, 2022)
Independent Variable	Book-Tax Difference (BTDI)	(Profit Before Tax – Current Tax Expense) / Total Assets	(Orji & John-Akamelu, 2023)
Control Variable	Firm Size (FSZ)	Natural logarithm of total assets	(Frances & Nworie, 2025)

Source: Researcher's Compilation (2025)

In this study, the Book-Tax Difference Index (BTDI) is calculated as (Profit Before Tax – Current Tax Expense) divided by Total Assets, without separating temporary and permanent components. This simplification was necessary due to data constraints in the Nigerian manufacturing sector, where detailed breakdowns of timing versus permanent differences are often unavailable. While it allows for a consistent measure across a large sample and extended period, it limits precision because BTDI captures both reversible timing effects and structural tax differences. As a result, the measure may overstate or understate the true economic impact of book-tax differences, so the findings should be interpreted as reflecting the overall divergence

between accounting and taxable income rather than distinguishing the specific sources of those differences.

The relationship between book-tax differences and firm performance will be estimated using the following panel regression model:

$ROA_{it} = \beta_0 + \beta_1 BTDI_{it} + \beta_2 FSZ_{it} + \epsilon_{it}$

Where:

ROA_{it} = Return on Assets of firm i in year t

$BTDI_{it}$ = Book-tax differences of firm i in year t

FSZ_{it} = Firm size (control variable) of firm i in year t

β_0 = Constant term

β_1 ,β_2 = Coefficients of predictors

ϵ_{it} = Error term

Descriptive statistics including mean, standard deviation, minimum, and maximum will first be used to summarize the data. Hypothesis was tested using a fixed effects panel regression model, selected after performing the Hausman specification test. The regression analysis was conducted at a 1% significance level using E-Views 11. The fixed effects model accounts for unobserved heterogeneity among firms, controlling for factors that are constant over time but vary across firms, thus providing reliable estimates of the impact of book-tax differences on firm performance.

4.0 Data Analysis

4.1 Descriptive Analysis and Model Diagnostics

Table 4.1 Descriptive Statistics

	ROA	**BTDI**	**FSZ**
Mean	0.011469	-0.108131	7.306944
Median	0.028567	-0.089532	7.132351
Maximum	5.816481	2.319513	9.715570
Minimum	-3.012121	-13.61323	4.758056
Std. Dev.	0.343078	0.794090	0.851501
Skewness	6.461135	-9.648491	0.031771
Kurtosis	156.9473	156.9739	2.949180
Jarque-Bera	579763.2	584951.2	0.160817
Probability	0.000000	0.000000	0.922739
Sum	6.686341	-63.04045	4259.948
Sum Sq. Dev.	68.50268	366.9972	421.9809
Observations	583	583	583

Source: Eviews 10 Output (2025)

In Table 4.1, the descriptive statistics for return on assets (ROA) reveal several important characteristics of the variable. The mean ROA is 0.011469, indicating that, on average, the listed manufacturing firms generated a modest positive return on assets over the study period. However, the large range between the maximum (5.816481) and minimum (-3.012121) suggests substantial variability in firm performance, which is further confirmed by the standard deviation of 0.343078. The skewness of 6.461135 indicates a strong rightward skew, meaning that there are a few firms with exceptionally high ROA pulling the distribution to the right. Similarly, the extremely high kurtosis of 156.9473 reflects the presence of extreme outliers, suggesting a distribution with very heavy tails and sharp peaks compared to a normal distribution. The Jarque-Bera probability of 0.000000 confirms that the ROA distribution significantly deviates from normality. Despite this, according to the central limit theorem, the large sample size of 583 observations implies that the sampling distribution of the mean ROA can still be treated as approximately normal, which allows for inferential statistical analysis to be conducted reliably.

For book-tax differences (BTDI), Table 4.1 indicates a mean of -0.108131, suggesting that, on average, firms reported slightly lower taxable income compared to accounting income, reflecting potential tax planning or differences in accounting and tax reporting. The maximum of 2.319513 and minimum of -13.61323 highlight substantial dispersion in the variable, with a standard deviation of 0.794090 confirming significant variability among firms. The skewness of -9.648491 shows a pronounced leftward skew, indicating that extreme negative BTD values are more common than extreme positive ones. The kurtosis of 156.9739 signals the presence of extreme outliers and a highly peaked distribution, while the Jarque-Bera probability of 0.000000 indicates non-normality. However, the sample size of 583 again ensures, under the central limit theorem, that the mean of BTDI can be approximated as normally distributed for hypothesis testing, mitigating concerns arising from the non-normality of the raw data.

Turning to firm size (FSZ), Table 4.1 shows a mean value of 7.306944, which serves as an average measure of the scale of operations of the sampled firms. The minimum (4.758056) and maximum (9.715570) indicate a moderate spread in firm size, consistent with the standard deviation of 0.851501. Skewness is 0.031771, very close to zero, suggesting that the FSZ distribution is approximately symmetric. The kurtosis of 2.949180 is near the benchmark of 3 for a normal distribution, further indicating that the FSZ data approximate normality. This is reinforced by the Jarque-Bera probability of 0.922739, which fails to reject the null hypothesis of normality. Consequently, firm size appears to be well-behaved for statistical analysis, and the central limit theorem further supports the reliability of inferences derived from this variable given the large sample size of 583 observations.

Table 4.2 Multicollinearity Test

Variance Inflation Factors
Date: 08/15/25 Time: 00:19
Sample: 1 583
Included observations: 583

	Coefficient	**Uncentered**	**Centered**
Variable	Variance	VIF	VIF
BTDI	0.000180	1.019388	1.000799
FSZ	0.000157	74.82423	1.000799
C	0.008494	74.90822	NA

Source: Eviews 10 Output (2025)

In Table 4.2, the multicollinearity test is presented through the Variance Inflation Factors (VIF) for the independent variables, BTDI and FSZ. The essence of the multicollinearity test is to assess whether there is a high correlation among the explanatory variables, which can inflate standard errors and distort regression estimates. The VIF values for both BTDI and FSZ are 1.000799, which are far below the commonly accepted threshold of 10. This indicates that multicollinearity is not a concern in this model, and each independent variable provides unique information in explaining variations in the dependent variable, ROA. Therefore, the regression estimates can be considered reliable, and there is no need for remedial measures to address collinearity.

Table 4.3 Hausman Specification Test

Correlated Random Effects - Hausman Test
Equation: Untitled

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	9.313856	2	0.0095

Source: Eviews 10 Output (2025)

Table 4.3 presents the Hausman specification test, which is used to determine whether a fixed effects model or a random effects model is more appropriate for panel data analysis. The essence of the Hausman test lies in checking whether the individual effects are correlated with the regressors; if they are, a fixed effects model is preferred, whereas if there is no correlation, a random effects model can be used. The probability value reported for the cross-section random effects is 0.0095, which is less than the 1% significance level. This result rejects the null hypothesis that the random effects estimator is consistent and efficient, indicating that the fixed effects model is the appropriate choice for estimating the relationship between book-tax differences, firm size, and ROA. Using the fixed effects model ensures that unobserved heterogeneity across firms is adequately controlled, leading to unbiased and consistent parameter estimates.

4.2 Test of Hypothesis

H_1 : Increases in book-tax differences will negatively affect firm performance.

Table 4.4 Test of Hypothesis

Dependent Variable: ROA
Method: Panel Least Squares
Date: 08/15/25 Time: 00:21
Sample: 2014 2024
Periods included: 11
Cross-sections included: 53
Total panel (balanced) observations: 583

Variable	Coefficient	Std. Error	t-Statistic	Prob.
BTDI	-0.303162	0.014829	-20.44393	0.0000
FSZ	0.043545	0.053261	0.817579	0.4140
C	-0.339494	0.389379	-0.871886	0.3837
Effects Specification				
Cross-section fixed (dummy variables)				
R-squared	0.484393	Mean dependent var		0.011469
Adjusted R-squared	0.431660	S.D. dependent var		0.343078
S.E. of regression	0.258640	Akaike info criterion		0.222832
Sum squared resid	35.32047	Schwarz criterion		0.634925
Log likelihood	-9.955513	Hannan-Quinn criter.		0.383457
F-statistic	9.185840	Durbin-Watson stat		2.179146
Prob(F-statistic)	0.000000			

Source: Eviews 10 Output (2025)

Table 4.4 presents the results of the panel least squares estimation, including model validity statistics. The adjusted R-squared of 0.431660 indicates that approximately 43.17% of the variation in firm performance, proxied by ROA, is explained collectively by the independent variables, BTDI and FSZ, along with the fixed effects for the 53 manufacturing firms. While this is a moderate explanatory power, it suggests that other factors not included in the model may also influence ROA. The Durbin-Watson statistic of 2.179146, which is close to the benchmark value of 2, implies that autocorrelation is not a concern in the residuals, affirming the reliability of the model for hypothesis testing. Additionally, the F-statistic probability of 0.000000 confirms that the model is statistically significant at the 1% level, indicating that, collectively, BTDI and FSZ have a meaningful effect on ROA.

The constant term in Table 4.4 is -0.339494 with a p-value of 0.3837, which is not significant at the 1% level. The constant represents the expected ROA when BTDI and FSZ are zero, but since it is not statistically significant, we cannot interpret it as a meaningful baseline for firm performance in this context. It suggests that the average firm performance is not reliably different from zero in the absence of the explanatory variables, emphasizing the importance of BTDI and FSZ in explaining variation in ROA. The coefficient of FSZ is 0.043545 with a p-value of 0.4140, indicating a positive but statistically insignificant effect on ROA at the 1% level. This means that, theoretically, a one-unit increase in firm size would increase ROA by 0.044 units, holding BTDI constant. However, because this effect is not statistically significant, we cannot conclusively state that firm size materially affects performance within this sample of listed manufacturing firms. The result suggests that while larger firms may have more resources and operational capacity, this does not necessarily translate into higher returns on assets over the observed period.

The coefficient of BTDI is -0.303162 with a p-value of 0.0000, indicating a negative effect on firm performance that is statistically significant at the 1% level. This implies that, ceteris paribus, a one-unit increase in book-tax differences is associated with a 0.303 decrease in ROA, holding firm size constant. The negative direction of this effect supports the hypothesis (H_1) that increases in BTDs reduce firm performance, suggesting that higher deviations between accounting income and taxable income may signal earnings management or aggressive tax planning that ultimately erodes profitability. This finding highlights the economic implication that firms with larger BTDs may face inefficiencies or financial reporting risks that hinder asset productivity.

Practically, this means that, holding firm size constant, a one-unit increase in BTDI is associated with a 0.303 decrease in ROA. Since ROA measures profitability, higher book-tax differences correspond to lower actual firm performance. In simpler terms, firms that report profits that deviate more from their taxable income tend to perform worse financially. Regarding endogeneity, there is a plausible concern. While higher BTDI may signal earnings management or aggressive accounting choices leading to lower performance, poor performance itself could also cause larger book-tax differences—for instance, via tax-loss carryforwards or discretionary accruals.

4.3 Discussion of Finding

The finding that book-tax differences have a negative and statistically significant effect on firm performance ($\beta = -0.303162$, $p = 0.0000$) suggests that larger discrepancies between accounting income and taxable income may be indicative of aggressive tax planning, earnings management, or financial reporting strategies that ultimately undermine operational efficiency and returns on assets. This negative effect aligns with the theoretical expectation that when firms manipulate the timing or recognition of income for tax purposes, it can distort the true economic performance, reduce investor confidence, and potentially increase the risk of regulatory scrutiny or financial distress. The result contrasts with studies such as Hiifan et al. (2025), Ologun and Gbadebo (2024), Olaoye and Ogunleye (2024), and Ofor and Akaegbobi (2022), which found a positive and significant association between book-tax differences and financial performance in consumer goods, non-financial, and industrial firms, suggesting that in those contexts, differences may reflect strategic tax planning that enhances profitability rather than erodes it. The divergence may be explained by sectoral differences, as manufacturing firms often have higher capital intensity and operational complexity, making them more susceptible to inefficiencies when BTDs are high.

Conversely, the negative outcome in this study finds support in empirical evidence emphasizing the potential costs of book-tax differences. Hastuti et al. (2025) observed that fixed and temporary BTDs did not significantly enhance profit growth in consumer goods firms, indicating that operational performance remains the primary driver of profitability rather than

deviations in book and taxable income. Similarly, Bas and Indrijawati (2020) found that BTDs did not significantly affect earnings quality in Indonesian firms, suggesting that large differences may reflect accounting manipulations that fail to improve, and may even detract from, actual firm performance. Chukwudi et al. (2020) also reported a positive but statistically insignificant effect of BTDs on firm value, highlighting that while differences may exist, their influence on tangible performance outcomes is not always beneficial. Together, these studies underscore that book-tax differences are not inherently value-enhancing and may have detrimental consequences under certain circumstances, particularly when operational efficiency is affected.

Further support for the negative association is found in studies examining opportunistic behavior. Evers et al. (2016) highlighted that BTDs are indicative of earnings management, and when not carefully managed, can lead to distortions in financial reporting that undermine firm stability. Orji and John-Akamelu (2023) demonstrated that only certain types of BTDs, such as temporary and permanent differences, had a measurable positive effect on financial stability, whereas discretionary or total differences had limited or no significant effect, suggesting that not all BTDs translate into stronger performance. Collectively, these findings suggest that in manufacturing firms, high BTDs may serve as a warning signal of inefficient financial practices or aggressive tax strategies that negatively influence ROA, consistent with the negative effect observed in the current study.

5. Conclusion and Recommendation

5.1 Conclusion and Recommendations

The negative and significant effect of book-tax differences on firm performance suggests that deviations between accounting income and taxable income may serve as a signal of underlying inefficiencies or financial risks within firms. Firms exhibiting larger book-tax differences might be engaging in aggressive tax planning, income smoothing, or other forms of earnings management, which can distort the true picture of operational performance and reduce the effectiveness of resource utilization. Such discrepancies could affect the perception of firm stability among investors, creditors, and other stakeholders, potentially influencing investment decisions, cost of capital, and market valuation. The observed negative association also highlights that financial performance is not solely determined by operational scale or firm size but can be meaningfully influenced by the alignment between reported accounting profits and taxable income. In the context of manufacturing firms, where capital intensity and operational efficiency are critical, significant book-tax differences may reflect strategic misalignments or managerial practices that prioritize short-term tax minimization over sustainable asset productivity. Furthermore, the statistical robustness of the findings, supported by a large sample size and rigorous panel estimation, indicates that the relationship is consistent across a wide range of firms and over multiple years, pointing to a systematic pattern rather than isolated incidents. This systematic effect underscores the importance of accurate financial reporting and the potential consequences of discrepancies between book and tax records, as they can signal pressures on liquidity, profitability, and long-term value creation. The results also highlight the interplay between corporate governance, financial oversight, and operational decision-making, as firms with higher book-tax differences may be navigating complex trade-offs that ultimately influence returns on assets. Hence, the finding that higher book-tax differences correspond with lower firm performance reflects how financial reporting practices intersect with economic outcomes, shaping the efficiency with which firms translate resources into returns and the transparency of their financial performance to external observers.

Based on the finding that book-tax differences negatively affect firm performance, it is recommended that financial managers and chief accountants of listed manufacturing firms implement more rigorous internal monitoring and reconciliation procedures between accounting income and taxable income. By regularly analyzing and minimizing unnecessary discrepancies,

they can ensure that reported profits accurately reflect operational performance, reduce potential risks associated with aggressive tax planning or earnings management, and enhance investor confidence in the firm's financial statements. Strengthening this alignment can also support better decision-making by management, improve transparency for stakeholders, and help safeguard the firm's long-term asset productivity and financial stability.

5.2 Contribution to Knowledge

This study advances the literature by going beyond the typical descriptive or short-term analyses of book-tax differences (BTDs) and firm performance. While previous research often examined limited samples or specific sectors, it explicitly investigates how BTDs signal declining firm performance over a decade, highlighting a predictive relationship rather than just an association. By incorporating firm size as a control variable and applying a panel least squares approach with fixed effects, it accounts for unobserved heterogeneity across firms, which many earlier studies ignored. Anchoring the analysis in Positive Accounting Theory provides a theoretical explanation for why managers might manipulate accounting choices to influence reported profits, linking behavior to performance outcomes. The key new insight is that persistent or large BTDs are not merely accounting artifacts—they are a warning signal of weakening profitability, offering actionable information for investors, regulators, and policymakers, especially in the context of Nigerian manufacturing firms.

5.3 Limitations of the Study and Suggestion for Further Studies

One limitation of this study is that it only focused on listed manufacturing firms in Nigeria, which may limit the generalizability of the findings to other sectors or countries. The study also relied solely on secondary data from financial statements and annual reports, which may not capture all aspects of managerial decisions or tax strategies. Additionally, only firm size was included as a control variable, while other factors like leverage, liquidity, or market conditions were not considered. Finally, the study used return on assets as the only measure of firm performance, which may not reflect all dimensions of financial health.

Future studies could expand the scope by including other sectors such as banking, oil and gas, or services to compare the effects of book-tax differences across industries. Researchers could also include additional control variables like leverage, liquidity, or corporate governance to capture more factors that influence firm performance. Using alternative measures of firm performance, such as return on equity or market value, could provide a broader understanding of the impact of book-tax differences. Longer periods or multi-country studies could also help to identify trends and enhance the generalizability of the findings.

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