

EXECUTIVE SUMMARY

Research question

The research on the effects of taxes on capital structure has its origins in the paper of Miller and Modigliani (1958) and has been an important field of research until now. Despite a huge body of research on whether an increased tax rate leads to increased levels of financial leverage in the firms, the evidence is not yet conclusive. This thesis pursues the goal to review the most important capital structure theories and examine whether financial leverage positively correlates with the tax rate. The gathered data also allow to analyze if the effective tax rate differs from the statutory tax rate and to quantify this gap for the examined countries.

Procedure

The data set includes companies from the S&P 500, the SMI, the DAX and the FTSE 100 and therefore covers companies from the United States, Switzerland, Germany and the UK. The regression analysis examines whether the hypothesis that firms which face a higher tax rate employ higher degrees of financial leverage holds true. The design of the regression analysis is inspired by Graham (1996) and used the inputs of other researchers (e.g. Long and Malitz (1985), Rajan and Zingales (1995), Thomas (1988), Scholes, Wilson, and Wolfson (1990)). A second regression analysis on two data subsets is conducted to examine whether the economic crisis which erupted in 2007 (Phillips and Yu (2011)) affected the financing behavior of the firms. The examination of the difference between what firms effectively pay and what they should pay is measured as the absolute value of the difference between the effective tax rate and the statutory tax rate.

Results

Despite including many factors which are regarded to be crucial in capital structure decisions, the regression model is only able to explain around 8.1% of the incremental financing decisions. This low figure of R^2 illustrates that the model is not able to explain the largest part of the variation in incremental financing decisions. It is furthermore interesting that the coefficient of the tax variable is slightly negative. Recent evidence which suggests a positive relation between the tax rate and financial leverage could therefore not be reproduced with the data set. The analysis of the two data subsets did not indicate that firms altered their financing behavior in the post-crisis period

in comparison to the pre-crisis data. The tax gap has a mean of 9.137 % for the KPMG tax data respectively 8.9960 % for the OECD tax data. This implies that there is a considerable difference in what firms effectively pay and what they should pay according to the statutory tax rate.

References

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