

Does Good Corporate Governance and Political Connection have an Influence a Tax Avoidance?

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ARTICLE INFO

Keywords: Institutional Ownership, Managerial Ownership, Independent Commissioners, Political Connections, Tax Avoidance

Received : 18, January

Revised : 19, February

Accepted: 17, March

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ABSTRACT

The objective of this study is to examine the impact of institutional ownership, managerial ownership, independent commissioners, and political connections on tax avoidance within manufacturing companies listed on the Indonesia Stock Exchange between 2020 and 2022. Employing a purposive sampling method, 39 eligible companies were chosen for panel data regression analysis. The findings reveal that institutional ownership has a partially positive influence on tax avoidance, managerial ownership also has a partially positive impact on tax avoidance, independent commissioners exhibit a partially negative association with tax avoidance, and political connections have a partially positive effect on tax avoidance.

INTRODUCTION

The government's goal of maximizing tax revenue is in contrast to the objectives of companies as taxpayers, where companies seek to minimize tax burdens to generate larger profits. The difference in interests between taxpayers and the government leads to taxpayer non-compliance to avoid their tax obligations. Companies, as taxpayers, make various efforts to achieve tax payment efficiency, which may reduce the government's revenue. (Amyartha, 2022)

Citing data from the Ministry of Finance, evident that a considerable number of taxpayers in Indonesia are not adhering to tax regulations.. Based on data from the Directorate General of Taxation (2022) regarding the tax compliance ratio, it is known that from the year 2018 to 2021, there has been a continuous increase from 71.10% to 84.07%. However, in the year 2022, there was a decrease with a percentage of 83.02%. The taxpayer compliance ratio has not reached 100%, even 90%. This indicates that the level of tax compliance in Indonesia is not optimal, potentially affecting the government's revenue in the taxation sector.

Tax avoidance poses a significant challenge, leading to substantial annual losses in tax revenue for the Indonesian government, ranging from tens to hundreds of billions of rupiah. The estimated annual loss is approximately 4.86 billion US dollars, equivalent to around IDR 68.7 trillion based on the current exchange rate. Out of this total, corporate tax avoidance in Indonesia accounts for approximately 4.78 billion US dollars or IDR 67.6 trillion, while the remaining 78.83 million US dollars or around IDR 1.1 trillion arises from personal taxpayers. According to data from the International Monetary Fund (IMF), Indonesia ranks 11th among 30 countries in terms of corporate tax avoidance. (Cobham et al., 2020)

The numerous cases in Indonesia related to tax avoidance indicate a lack of tax compliance, as demonstrated by a case in 2019 involving PT. Adaro Energy Tbk, which was suspected of engaging in tax avoidance practices. PT. Adaro Energy Tbk allegedly employed transfer pricing by shifting significant profits from Indonesia to a company in a tax-exempt or low-tax country. This practice reportedly occurred from 2009 to 2017, resulting in PT. Adaro Energy Tbk paying approximately IDR 1.75 trillion or over US\$125 million less in taxes than the amount owed in Indonesia. In this case, tax avoidance was carried out through transfer pricing (Source: Kompasnia.com, 2022).

In addition to tax payments, publicly listed companies in Indonesia are also required to implement corporate governance. Corporate governance is a system that regulates and controls companies to ensure good performance and create added value for stakeholders. The goal of corporate governance is to establish effective and efficient corporate governance in line with government regulations, facilitating continuous development without violating set rules . (Taufik Hidayat, 2022)

LITERATURE REVIEW

The agency theory

Management is motivated to manipulate the company's profits, ultimately leading to a reduction in the tax burden. The behavior of profit

manipulation creates information bias for shareholders. The agent may allocate current-year profits to future years to avoid high taxes. Corporate governance principles applied in the company can provide benefits in minimizing agency problems. With the appropriate implementation of Good Corporate Governance (GCG), such as transparent information disclosure, tax avoidance practices can be minimized, and tax payments can be maximized (Imanuella & Damayanti, 2022).

Good Corporate Governance (GCG)

Good Corporate Governance (GCG), or corporate governance, encompasses a set of regulations that oversee the relationships among shareholders, company executives, creditors, government entities, employees, and other internal and external stakeholders. These regulations delineate the rights and obligations of each party involved. (Imanuella & Damayanti, 2022)

Institutional Ownership

Institutional ownership refers to the ownership of shares by an institution. The entity holding these shares holds significant power in making financial decisions for the company. Additionally, high institutional ownership ensures that investors closely monitor the company to avoid mistakes that could harm both the company and investors. The proportion of shares held by institutions, measured as a percentage, is the definition of institutional ownership (Septanta, 2023)

Managerial ownership

Managerial ownership can be observed through the concentration of ownership or the percentage of shares held by the board of directors and management. One way to reduce agency conflicts is by increasing managerial ownership. Companies enhance managerial ownership to align the position of managers with shareholders, enabling them to act in harmony with shareholder interests. (Nuridah et al., 2023)

The independent board of commissioners

The independent board of commissioners assumes a pivotal role in corporate management. Serving as a corporate body, it is entrusted with general and/or specific oversight duties as outlined in the articles of association. Additionally, the board of commissioners offers guidance and advice to the board of directors. Consequently, the board of commissioners plays a substantial role in influencing tax management decisions within the organization. (Hasanah & Wardatul Afiqoh, 2023)

Political Connections

A company is considered to have political connections if one of its shareholders is a member of parliament, a minister, or closely associated with politicians or political parties. Therefore, political connections can be a cause of tax avoidance. The measurement used to determine political connections in a company is by assigning a value of 1 if the company includes members of

parliament, ministers, or individuals closely associated with politics in its hierarchy, and 0 if there are no members of parliament, ministers, or individuals associated with politics in the company's hierarchy. (Komite et al., 2022)

Tax Avoidance

Tax avoidance is an action that does not violate regulations, meaning no tax laws are breached. The tax avoidance scheme utilized by certain individuals involves identifying weaknesses in tax regulations to reduce the amount of tax owed. Tax avoidance often occurs due to differences in interests between the government and companies (Ishak & Asalam, 2023)

Hypothesis

(H1): Institutional ownership has a positive effect on tax avoidance.

(H2): Managerial ownership has a positive effect on tax avoidance.

(H3): Independent Board of Commissioners has a negative effect on tax avoidance.

(H4): Political connections have a positive effect on tax avoidance.

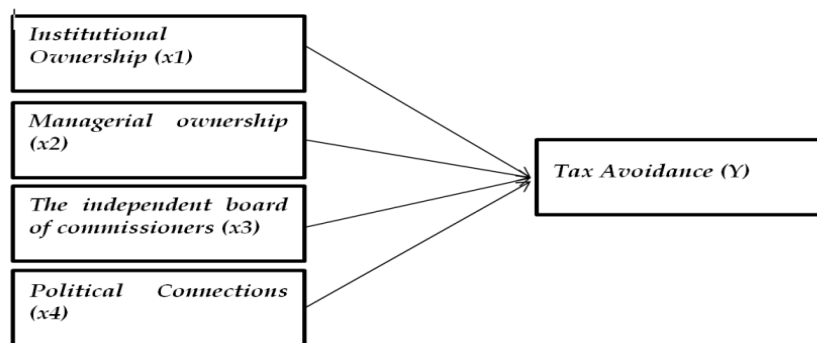


Figure 1. Conceptual Framework

METHODOLOGY

This study adopts a quantitative approach, with institutional ownership, managerial ownership, independent commissioners, and political connections as independent variables. The dependent variable under examination is tax avoidance. The study's population comprises manufacturing companies listed on the Indonesia Stock Exchange from 2020 to 2022. Sample selection was conducted using the purposive sampling method, leading to the inclusion of 39 companies that satisfied the specified criteria. The analytical techniques employed in this research include descriptive statistics, classic assumption tests, selection of panel data regression models, panel data regression analysis, t-test, and determination coefficient test using the EViews 9 program.

RESEARCH RESULT

Classical Assumption Tests

1. Multicollinearity Test

	X1	X2	X3	X4
X1	1.000	0,819	-0,643	0,667
X2	0,819	1.000	-0,741	0,736
X3	-0,643	-0,741	1.000	-0,515
X4	0,667	0,736	-0,515	1.000

Table 1. Results of Multicollinearity Tes

Based on the table, all values for X1, X2, X3, and X4 are less than 0.85, indicating that there is no multicollinearity issue.

2. Heteroskedasticity Test

Table 2. Result of Heteroskedasticity Test

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.001303	0.008626	-0.151078	0.8803
X1	-0.003851	0.011758	-0.327527	0.7442
X2	0.051243	0.019579	2.617252	0.0707
X3	0.016170	0.018126	0.892109	0.3752
X4	-0.000856	0.003211	-0.266428	0.7907

The variable of Institutional Ownership (X1) has a value of 0.7442, and the variable of Managerial Ownership (X2) has a value of 0.0707. The variable of Independent Commissioners (X3) has a value of 0.3752, while the variable of Political Connections (X4) has a value of 0.7907. Thus, all independent variables have values > 0.05 . This indicates that the regression model is homoskedastic, and there is no heteroskedasticity problem.

Panel Data Regression Model Selection

a. Chow Tes

Table 3. Result of Chow test

Test cross-section fixed effects			
Effects Test	Statistic	d.f.	Prob.
Cross-section F	2.105431	(38,74)	0.0031
Cross-section Chi-square	85.752687	38	0.0000

The Chi-Square probability is found to be 0.0000, leading to the rejection of H_0 . This implies that the most appropriate model to use is the fixed effect model

b. Hausman Test

Table 4. Hausman Test

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	67.581273	4	0.0000

The probability of cross-section random is 0.0000 or less than 5%. Thus, it can be concluded that H_0 is rejected, indicating that the most suitable model for this analysis is the **fixed effect model**.

Hypothesis Testing

Panel Data Regression Analysis

Table 5. Panel Data Regression Analysis

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.103407	0.022106	4.677845	0.0000
X1	0.136328	0.030130	4.524648	0.0000
X2	0.316102	0.050172	6.300411	0.0000
X3	-0.174407	0.046448	-3.754897	0.0003
X4	0.024024	0.008229	2.919630	0.0046

- X1 has a value of 0.0000 below < 0.05 , and a coefficient of 0.1363, which means that institutional ownership, partially, has a positive effect on tax avoidance. Thus, an increase in institutional ownership (X1) will lead to an increase in tax avoidance (Y).
- X2 has a value of 0.0000 below < 0.05 , and a coefficient of 0.3161, indicating that managerial ownership, partially, has a positive effect on tax avoidance. Thus, an increase in managerial ownership (X2) will lead to an increase in tax avoidance (Y).
- X3 has a value of 0.0003 below < 0.05 , and a coefficient of -0.1744, indicating that independent commissioners, partially, have a negative effect on tax avoidance. Thus, an increase in independent commissioners (X3) will lead to a decrease in tax avoidance (Y).
- X4 has a value of 0.0000 below < 0.05 , and a coefficient of 0.0240, indicating that political connections, partially, have a positive effect on tax avoidance. Thus, an increase in political connections (X4) will lead to an increase in tax avoidance (Y).

Coefficient of Determination Test

Table 6. Coefficient of Determination Test

R-Squared	Adjusted R-Squared
0,9733	0,9582

The adjusted R-squared value is 0.9582, rounded to 0.96. This means that institutional ownership (X1), managerial ownership (X2), independent commissioners (X3), and political connections (X4) Together, the independent variables in this study can account for 96% of the variation observed in tax avoidance (Y). The residual 4% signifies the portion of the variation that is attributed to other variables not explicitly considered in this research.

DISCUSSION

The Influence of Institutional Ownership on Tax Avoidance

X1 has a value of 0.0000 below < 0.05 , indicating that institutional ownership, partially, has a positive effect on tax avoidance. Thus, an increase in institutional ownership (X1) will result in an escalation of tax avoidance (Y). According to the research by (Putri & Titik Aryati, 2023), institutional ownership has a positive influence on tax avoidance, suggesting that institutional ownership plays a crucial role in disciplining managers. Hence, managers are less likely to act in their own interest, and decisions made tend to benefit shareholders, Facilitating the occurrence of practices related to tax avoidance.

The Influence of Managerial Ownership on Tax Avoidance

X2 has a value of 0.0000 below < 0.05 , indicating that managerial ownership, partially, has a positive effect on tax avoidance. Thus, an increase in managerial ownership (X2) will result in an escalation of tax avoidance. (Y). Income tax payments are based on the company's profit. Companies aim to achieve high profits, but high profits also mean higher tax expenses. Significant tax expenses prompt companies to engage in tax avoidance with minimal risks. Managers must optimize the company's profit, which will be reported to the company's owners. Managerial ownership enables decision-making that benefits shareholders, allowing the occurrence of tax avoidance practices (Prastiyanti & Mahardhika, 2022)

The Influence of Independent Commissioners on Tax Avoidance

X3 has a value of 0.0003 below < 0.05 , indicating that independent commissioners, partially, have a negative effect on tax avoidance. Thus, an increase in independent commissioners (X3) will result in an escalation of tax avoidance (Y). Independent commissioners can oversee the company's management in formulating strategies, including tax-related strategies. This oversight makes management more cautious in making decisions, minimizing activities related to tax reduction through tax avoidance.

The Influence of Political Connections on Tax Avoidance

X4 has a value of 0.0000 below < 0.05 , indicating that political connections, partially, have a positive effect on tax avoidance. Thus, an increase in political connections (X4) will result in an escalation of tax avoidance (Y). Political connections enable companies to receive special treatment, such as ease in obtaining capital loans and low tax examination risks, making companies more aggressive in implementing tax planning, resulting in decreased financial statement transparency. The loss of investors due to reduced financial statement transparency can be compensated by the government's role as the main source of funds. Moreover, companies with political connections to the ruling government tend to exhibit significantly higher levels of tax avoidance compared to similar companies without political connections (Hapsari Ardianti, 2019).

CONCLUSIONS AND RECOMMENDATIONS

- 1) The research results indicate that X1 has a probability value of 0.0000 below < 0.05 , meaning that institutional ownership, partially, has a positive effect on tax avoidance. Therefore, an increase in institutional ownership (X1) will result in an escalation of tax avoidance (Y).
- 2) X2 has a value of 0.0000 below < 0.05 , indicating that managerial ownership, partially, has a positive effect on tax avoidance. Thus, an increase in managerial ownership (X2) will result in an escalation of tax avoidance (Y).
- 3) X3 has a value of 0.0003 below < 0.05 , meaning that independent commissioners, partially, have a negative effect on tax avoidance.

Therefore, an increase in independent commissioners (X3) will result in an escalation of tax avoidance (Y).

- 4) X4 has a value of 0.0000 below < 0.05 , indicating that political connections, partially, have a positive effect on tax avoidance. Therefore, an increase in political connections (X4) will result in an escalation of tax avoidance (Y).

ADVANCED RESEARCH

Future researchers are encouraged to utilize or add other variables besides those in this study, such as audit committees, company size, and others.

This study only used manufacturing companies as the research population, so it is recommended for future researchers to expand the research population.

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