

MODERATION OF EXECUTIVE CHARACTER IN THE EFFECT OF FOREIGN OWNERSHIP, AUDIT COMMITTEE, AND FINANCIAL DISTRESS ON TAX AVOIDANCE

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ABSTRACT

The existence of a self-assessment system implemented by Indonesia in tax collection that authorizes taxpayers to calculate, deposit, and self-report their tax obligations is actually a loophole used by taxpayers to carry out tax avoidance actions that can harm the state. Therefore, this study aims to examine the influence of foreign ownership, audit committees, and financial distress on tax avoidance with the character of executives as moderators. The population in this study is manufacturing companies in the consumer goods industry sector listed on the Indonesia Stock Exchange (IDX) with a research year period of 2021-2023. The sample in this study was selected using the purposive sampling method with certain criteria so that the sample obtained was 99 data after outlier. The analysis method used was panel data regression analysis and Moderated Regression Analysis (MRA) and then processed using the *eviews 13* program. The results of the study prove that foreign ownership and financial distress have a significant negative effect on tax avoidance, while the audit committee has no effect on tax avoidance, the executive character strengthens the negative influence of foreign ownership on tax avoidance but is unable to moderate the influence of the audit committee and financial distress on tax avoidance.

KEYWORDS: Foreign Ownership, Audit Committee, Financial Distress, Tax Avoidance, Executive Character

INTRODUCTION

Indonesia as a country has a source of income, one of which is sourced from taxes. Taxes are the largest contributor to state revenue from the total number of other sources of revenue in Indonesia, where more than 80% of state revenue comes from taxes (Wahana et al., 2023). Taxes are mandatory contributions that must be paid by taxpayers, both individuals and business entities, which are then used to finance all state expenditures, including national development, to create community welfare, so that taxes play an important role in improving community welfare (Oktaviani et al., 2023).

In Article 12 of the Law on General Provisions and Tax Procedures (KUP) No.6 of 1983, tax collection in Indonesia is carried out by a *self-assessment* system, namely by authorizing taxpayers to calculate, deposit, and report their tax obligations themselves in accordance with applicable tax laws and regulations. This tax collection mechanism is used by taxpayers to reduce the tax burden they must pay. As a taxpayer, companies consider taxes as a burden that can make the company's expenses even bigger which can then reduce the company's profits. This is the main factor that can cause tax revenues in Indonesia to be suboptimal (Ratnandari & Achyani, 2023).

One of the causes of the low tax ratio in Indonesia is due to tax avoidance. Tax *avoidance* is an action of a legally legal tax management method by taking advantage of weaknesses in tax provisions and regulations so that it can reduce the tax burden (Rizki et al., 2021). By doing *tax avoidance*, companies can reduce the amount of tax they have to pay so that not a few companies do *tax avoidance*. Tax avoidance practices in Indonesia have occurred a lot and are even carried out by multinational companies such as Google, Amazon, Starbucks, and Microsoft. The many tax avoidance practices carried out by these various companies can result in losses for the state. As stated in the *Tax Justice Network* report released on July 25, 2023, which revealed that all countries around the world experienced an increase in tax losses by 1.7%, namely US\$472 billion from the previous report to US\$480 billion. The losses were caused by losses due to corporate tax abuse of US\$311 billion and losses due to cross-border tax evasion by hiding assets or income streams abroad amounting to US\$169 billion. The report estimates that over

the next 10 years, countries will suffer losses of \$4.8 trillion which is equivalent to losing one year of public health spending worldwide over the next 10 years (State of Tax Justice 2023, n.d.).

According to Agus, Minister of Industry Gumiwang Kartasasmita, the manufacturing industry sector has always been the largest contributor to supporting national economic growth with a contribution of 16.77% in 2023 (indonesia.go.id, 2023). As part of the manufacturing sector, the consumer goods industry consists of the sub-sectors of food and beverages, cigarettes, pharmaceuticals, cosmetics and household items, household appliances, and other consumer industries with the onset of the Covid-19 pandemic where community activities have been carried out freely and without any restrictions on activities, according to Ciptadana Sekuritas Asia Analyst Putu Chantika Putri this will encourage consumption and economic resilience in Indonesia so that profits companies in the consumer goods industry sector will increase (investasi.kontan.co.id,2023). With the increase in consumer goods, it will encourage companies to avoid taxes because consumer goods are one of the manufacturing sectors that show a significant increase in profits when compared to other sectors because their products are always needed by people on a daily basis.

Based on the phenomenon that occurs, there are several factors that can affect the occurrence of *tax avoidance*. In this study, foreign ownership, audit committees, and *financial distress* are suspected to cause *tax avoidance practices*.

According to Suryati et al. (2022:46), foreign ownership is a person, legal entity, or foreign government that owns shares in a company and is considered concerned about improving *good corporate governance*. The higher the proportion of shares by foreign ownership in the company, the better the supervision of the company's performance, including in monitoring fraud. In line with the results of research (Hasan et al., 2022) and (Ikraam & Ariyanto, 2020) which state that foreign ownership has a negative effect on *tax avoidance*, meaning that the higher the foreign ownership in the company, the less *tax avoidance practices* will be. However, it is not in line with the results of research (Susilawati & Tarmidi, 2024) and (Alianda et al., 2021), which state that foreign ownership has a positive effect on *tax avoidance*. And the results of the study (Apriyani, 2021) stated that foreign ownership had no effect on *tax avoidance*.

According to (Arens et al., 2015:104) the audit committee is a number of members of the board of directors who are tasked with helping auditors maintain management independence. The more audit committees that have expertise in accounting and finance, the more effective the audit committee's performance will be. In line with the results of research (Prihatono et al., 2019), and (Liani & Karlina, 2023) which states that audit committees have a negative effect on *tax avoidance*, meaning that the more audit committees have expertise in accounting and finance, the less *tax avoidance practices* will be. However, it is not in line with the results of research (Wahana et al., 2023), and (Fitrianiingsih & Wulandari, 2024) which states that the audit committee has a positive effect on *tax avoidance*. As well as the results of the study (Pratomo & Rana, 2021) stated that the audit committee had no effect on *tax avoidance*.

According to Septiawan et al. (2021:57), *financial distress* is a condition in which a company is unable to fulfill its obligations due to a shortage or insufficient funds. The financial difficulties faced by companies can reduce the tax burden that must be paid so that companies no longer need to do *tax avoidance*. In line with the results of research (Aldaniar & Sapari, 2023), (Ramadani, 2023), and (Ferawati & Bimantoro, 2022) which state that *financial distress* has a negative effect on *tax avoidance*, meaning that the more companies experience *financial distress*, the more *tax avoidance practices* will be reduced. However, it is not in line with (Ananda & Wahyuni, 2024) and (Angela & Frederica, 2023) who state that *financial distress* has a positive effect on *tax avoidance*.

In this study, executive character is used as a moderation variable. Executive character is a trait possessed by company leaders in decision-making and policy (Anjilni & Fahrezi, 2024). Company executives can have a *risk taker* or *risk averse* character so that the higher the company's risk, the more executives tend to have a *risk taker* character, and vice versa, the lower the company's risk, the more executives tend to have a *risk averse* character (Septiawan et al., 2021:61).

Research conducted by (Sawitri et al., 2022) shows that the character of executives is not able to moderate foreign ownership against tax aggressiveness, meaning that the lower the risk of the company showing risk-absorbing executives, the company will not practice *tax avoidance* when there is foreign ownership in the company. Research conducted by (Sahara, 2022) shows that the character of executives weakens the influence of the audit committee on *tax avoidance*, meaning that the lower the risk of the company showing risk-averse executives, the company will not carry out *tax avoidance* with the existence of an audit committee. Research conducted by

(Pratiwi & Djajanti, 2022) shows that the character of executives moderates the influence of *financial distress* on *tax avoidance*, meaning that with *risk-averse* executives, they will make policies with less risk when the company experiences *financial distress*. Meanwhile, research conducted (Rohmah & Romadhon, 2023) states that executive character is not able to moderate the influence of the audit committee on *tax avoidance*

LITERATURE REVIEW

Tax avoidance is an effort to avoid the tax burden legally and safely for taxpayers without contradicting tax provisions and usually takes advantage of weaknesses or *gray areas* in tax laws and regulations to reduce the amount of tax that must be paid (Pohan, 2011:11). Tax avoidance is carried out by companies with the aim of streamlining the tax burden by taking advantage of loopholes in the provisions of tax laws and regulations. Although tax evasion can be done legally, the government does not want it because it does not support the state's goals and can reduce state tax revenue (Aji & Kartikaningrum, 2024). Where if it does not support the state's goals, the welfare of the community will not be achieved.

According to Suryati et al. (2022:46), foreign ownership is the ownership of shares owned by multinational companies that are considered concerned about improving *good corporate governance*. Law Number 25 of 2007 article 1 paragraph 8 concerning investment states that foreign capital is capital owned by foreign countries, individual foreign citizens, and foreign business entities, foreign legal entities, and Indonesian legal entities whose capital is partly or wholly owned by foreign parties. Foreign investors in companies that have a proportion of shares of 20% or more will have a significant influence on the company so that the more foreign ownership in the company, the greater the foreign investor has great control in determining the company's policies (Hidayat & Mulda, 2019).

According to Arens et al. (2015:104), the audit committee is a number of members of the board of directors who help the auditor maintain management independence. The audit committee was formed with the aim of ensuring the implementation of good corporate governance (Rusdiyanto & Elan, 2019:114). Based on OJK Regulation Number 55/POJK.04/2015, the audit committee in a company consists of at least three members who come from independent commissioners and external parties of issuers or public companies. Members of the mandatory audit committee must have at least one member with an educational background and expertise in the field of accounting and finance. An audit committee consisting of members who have an accounting and finance education background will be more effective in supervising the internal control of an entity (Rusdiyanto & Elan, 2019:114).

According to Septiawan et al. (2021:57), *financial distress* is a condition in which a company is unable to fulfill its obligations at maturity due to a shortage or insufficient funds. Hery (2023:35) revealed that *financial distress* can occur because it is caused by internal and external factors. Internal factors such as credit for customers that are too large, weak qualifications of human resources, bankruptcy of working capital, and abuse of authority and fraud. Meanwhile, external factors such as fierce business competition, reduced demand for products or services, selling prices have decreased continuously, and accidents or natural disasters. Companies that are facing *financial distress* will try to escape bankruptcy by not doing *tax avoidance* because it will reduce investment by investors (Ari & Sudjawoto, 2021).

According to Setyawan et al. (2022:89), executive character is the nature of the company's leadership in helping to direct the management to carry out the company's activities in accordance with the goals that have been made. In carrying out their leadership duties in the company, executives have two characters, namely *risk takers* and *risk averse*, which can be seen from their courage in taking risks. Executives who are *risk takers* are executives who are more daring to take high-risk policies. Meanwhile, executives who are *risk averse* do not dare to take policies that can pose a number of risks so that they will make decisions with the lowest risk (Low, 2009). Thus, the greater the company's risk, the executive has a *risk-taker* character, and vice versa, the lower the company's risk, the executive has a *risk averse character*.

METHOD

Tax avoidance is an effort to avoid the tax burden legally and safely for taxpayers without contradicting tax provisions to reduce the amount of tax that must be paid (Pohan, 2011:11). The amount of *tax avoidance* in this study is calculated by looking at the difference between *the Statutory Tax Rate* (STR), which is the applicable tax rate and set by the tax authority, and the *Effective Tax Rate* (ETR). Based on Law No. 2 of 2020 and Law No. 7 of 2021 concerning the Harmonization of Tax Regulations (HPP Law), the corporate income tax rate is 22% so that if the ETR value produced is lower than the STR value, the greater the company will take *tax avoidance* actions, and vice versa, if the ETR value is greater than the STR, it will describe the lower the *tax avoidance* actions taken by the company (Jamei, 2017)

Foreign ownership is the ownership of shares owned by multinational companies that are considered *concerned* about improving *good corporate governance*. Foreign ownership can consist of individuals, companies, legal entities, governments, and their parts with foreign status (Putra, 2022:59). Foreign ownership is measured by looking at the proportion of company shares owned by individuals, legal entities, the government and their parts with foreign status in % (Salihu et al., 2015)

The audit committee is a number of members of the board of directors who are tasked with assisting the auditor in maintaining the independence of management (Arens et al., 2015:104). In a company, there must be at least one member of the audit committee who has an educational background and expertise in the field of accounting and finance. In this study, the audit committee is measured by dividing the number of audit committees that have expertise in the field of accounting and finance with audit committee members (Dwiharyadi, 2017)

Financial distress is a condition in which a company is unable to fulfill its obligations at maturity due to a shortage or insufficient funds (Septiawan et al., 2021:57). In this study, *financial distress* is measured using the Z-Score formula, which is to predict the bankruptcy of a company (Altman, 1968). *Financial distress* is proxied by the following formula:

$$Z = 1.2A + 1.4B + 3.3C + 0.6D + 1E$$

Where:

A = (Current assets – current liabilities) / total assets

B = Retained earnings / total assets

C = Profit before tax / Total assets

D = (Number of shares x price per share) / total debt

E = Sales / total assets

In this case, Altman Z-Score explained that if the Z value ≥ 2.99 then the company is in the safe zone. If the value of $1.81 \leq Z < 2.99$ then the company is in the gray zone, and if the Z value < 1.81 then the company is in the distress zone.

The character of executives is seen from the level of risk faced by the company, where if the company's risk value is high, the executive is a *risk taker*, i.e. more daring to take risks, and vice versa, if the company's risk value is low, the executive is *risk averse*, i.e. does not like risk (Rizki et al., 2021). Executive character is measured by dividing the standard deviation of EBITDA (*Earning Before Income Tax, Depreciation, and Amortization*) by the company's total assets (Paligorova, 2010).

In this study, the population used is 90 manufacturing companies in the consumer goods industry sector listed on the Indonesia Stock Exchange (IDX) in 2024. As for the sampling in this study, it was carried out by a *non-probability sampling technique*, namely *purposive sampling*, where the determination of the sample was carried out with certain considerations according to the specified criteria so that the research results were in accordance with the research objectives. The criteria for selecting samples in this study are:

- Manufacturing companies in the consumer goods industry sector that have accessible financial statements for the year 2021-2023.
- Companies that have foreign shareholders during 2021-2023.

DISCUSSION

Based on the results of the tests that have been carried out in this study, a discussion of the results of the research will be described to prove the hypothesis in accordance with the theory used and previous research.

The Effect of Foreign Ownership on Tax Avoidance

Foreign ownership has a negative effect on *tax avoidance*. This means that during the year under observation, companies with higher foreign ownership showed lower *tax avoidance* practices. This is due to foreign shareholders who bring in the practice of

Good corporate governance, transparent, and in accordance with international standards. Foreign shareholders will implement strict supervision and encourage companies to comply with tax regulations in order to maintain integrity and legal compliance.

This is in line with the agency theory where foreign shareholders as principals want the company as an agent to be able to maximize the company's profits in a legal and rule-based way. Foreign shareholders will strive to ensure that the company in which they invest always complies with existing regulations because *tax avoidance* practices can have a bad impact on the company's reputation. Therefore, foreign shareholders will encourage companies to implement ethical business strategies and comply with regulations.

The results of this study are in line with the results of previous research conducted by (Hasan et al., 2022) and (Ikraam & Ariyanto, 2020) which stated that foreign ownership has a negative effect on tax avoidance. However, the results of this study are not in accordance with research conducted by (Susilawati & Tarmidi, 2024) and (Alianda et al., 2021) which state that foreign ownership has a positive effect on *tax avoidance*.

The Influence of the Audit Committee on Tax Avoidance

The audit committee has no effect on *tax avoidance*. This means that during the year of observation, the expertise in accounting and finance possessed by the audit committee does not directly affect the level of *tax avoidance* carried out by the company. This is due to the role of the audit committee which focuses on overseeing financial statements, internal controls, and compliance with accounting standards so that attention to the tax aspect is not their top priority.

This is in line with the agency's theory that the audit committee which is part of corporate *governance* has a role to supervise the process of preparing financial statements and monitor the company's financial problems, where efforts to prevent *tax avoidance* practices require special attention to tax aspects that may be outside the main duties of the audit committee.

The results of this study are in line with the results of previous research conducted by (Pratomo & Rana, 2021) which stated that the audit committee has no effect on *tax avoidance*. However, the results of this study are not in accordance with the research conducted by (Prihatono et al., 2019) and (Liani & Karlina, 2023) which states that the audit committee has a negative effect on *tax avoidance*.

The Effect of Financial Distress on Tax Avoidance

Financial distress has a negative effect on *tax avoidance*. This means that during the observation year, companies that are in *financial distress*, especially when losses occur, tend to practice lower *tax avoidance*. This is because the tax that must be paid by the company has been adjusted to the profits obtained, meaning that when the company experiences *financial distress*, the tax that must be paid will be lower and when the company suffers a loss, the company will obtain facilities in the form of compensation for fiscal losses so that the tax that must be paid will also be lower.

This is in line with the agency theory, where companies that experience *financial distress* tend to be pressured by stakeholders so that the company will focus on maintaining the company's operations by prioritizing the recovery of financial performance and complying with tax regulations to maintain the trust of stakeholders, as well as to avoid new risks that can worsen the company's financial condition if *tax avoidance*.

The results of this study are in line with the results of previous research conducted by (Aldaniar & Sapari, 2023), (Ramadani, 2023), and (Ferawati & Bimantoro, 2022) which stated that *financial distress* has a negative effect on *tax avoidance*. However, the results of this study are not in accordance with research conducted by (Ananda & Wahyuni, 2024) and (Angela & Frederica, 2023) which states that *financial distress* has a positive effect on *tax avoidance*.

The Influence of Foreign Ownership on Tax Avoidance with Executive Character as a Moderator

The character of the executive reinforces the negative influence of foreign ownership on *tax avoidance*. This means that during the observation period, companies with high foreign ownership and supported by executives who have a *risk-averse* character tend to show lower *tax avoidance* practices. Foreign ownership, which often brings stricter corporate governance standards, becomes more effective in reducing tax avoidance practices when followed by careful executive leadership.

Executives with a *risk-averse* character tend to avoid actions that can pose a major risk to the company, including legal risks and reputational losses due to *tax avoidance* practices. This character encourages policy-making that supports transparency, accountability, and compliance with tax regulations. *Risk-averse* executives will support foreign ownership in creating business practices that comply with tax rules through policies that comply with regulations, thereby strengthening good corporate governance and reducing potential adverse risks. The results of this study are not in accordance with previous research conducted (Sawitri et al., 2022) stating that the character of executives is not able to moderate foreign ownership against tax aggressiveness.

The Influence of the Audit Committee on Tax Avoidance with Executive Character as a Moderator

The character of the executive is not able to moderate the influence of the audit committee on *tax avoidance*. The existence of executives in the company is not able to affect the relationship between the audit committee and *tax*

avoidance because the effectiveness of the audit committee measured based on expertise in the field of accounting and finance is more influenced by the internal factors of the committee itself than the characteristics of individual executives. A competent and independent audit committee is able to carry out its supervisory duties well without being affected by the leadership style, risks, or personal character of the company's executives.

With its accounting and finance expertise, the audit committee with its authority and independence will operate based on the principles of good governance, which prioritizes objectivity in supervising the company's financial practices without being influenced by the character of executives who are *risk averse* or *risk takers*. The results of this study are not in accordance with previous research conducted by (Sahara, 2022) which stated that the character of the executive weakens the influence of the audit committee on *tax avoidance*.

The Effect of Financial Distress on Tax Avoidance with Executive Character as a Moderation

The character of the executive is not able to moderate the influence of *financial distress* on *tax avoidance*. This is because when a company is in a state of *financial distress*, both executives who tend to avoid risks (*risk averse*) and those who dare to take risks (*risk takers*), will not focus on the risks associated with tax avoidance practices. However, executives will focus on how to maintain the company's viability so that the company's operations can continue and ensure that the company can survive in the long term.

The results of this study are in line with the results of previous research conducted by (Rohmah & Romadhon, 2023) which stated that character is not able to moderate the influence of *financial distress* on *tax avoidance*. However, the results of this study are not in accordance with research conducted by (Pratiwi & Djajanti, 2022) which states that executive character moderates the influence of *financial distress* on *tax avoidance*.

CONCLUSION

Based on the results of data testing and discussion on the influence of foreign ownership, audit committee, and *financial distress* on *tax avoidance* with executive character as a moderation variable, the conclusions of this study are as follows:

1. Foreign ownership has a significant negative effect on *tax avoidance*.
2. The audit committee has no effect on *tax avoidance*.
3. *Financial distress* has a significant negative effect on *tax avoidance*.
4. The character of the executive reinforces the negative influence of foreign ownership on *tax avoidance*.
5. The character of the executive is not able to moderate the influence of the audit committee on *tax avoidance*.
6. The character of the executive is not able to moderate the influence of *financial distress* on *tax avoidance*.

SUGGESTION

For Theory Development

In this study, the researcher did not find any influence of the audit committee on *tax avoidance* so that the researcher could then add or use other independent variables that were not used in this study and could use different proxies to be used as a basis in future research to reflect the results of different studies. In addition, the researcher is also recommended to use moderation variables that are different from the research conducted in order to find a stronger influence in moderating the influence of foreign ownership, audit committees, and *financial distress* on *tax avoidance*.

For Companies

The researcher suggests that companies can be more careful in making decisions related to *tax avoidance* practices so that companies can avoid sanctions and losses that can have a long-term impact on *tax avoidance*. Considering the ever-evolving tax policy and tax avoidance that is often carried out in any situation can have a bad impact on the company.

Government and Regulators

The researcher suggests that the government can strengthen regulations and supervision related to taxation to reduce *tax avoidance* practices and strengthen law enforcement against *tax avoidance* practices. Considering how the practice of *tax avoidance* that is legalized is used as a loophole by taxpayers in order to reduce their obligations but can harm the government which can then affect state tax revenue.

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