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Does GCG moderate the financial distress on tax avoidance?

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Abstract

This study aims to determine the effect of financial distress on tax avoidance, moderated by good corporate governance. This research was conducted on transportation and logistics sector companies listed on the Indonesia Stock Exchange in 2019–2021 because the Indonesian economy began to experience a contraction as a result of the COVID-19 Pandemic in 2019 and continued until 2021, therefore it has an impact on state tax revenues. The sample was selected using a purposive sampling technique, and 14 companies were identified. The data analysis technique used is moderation regression analysis. This study also uses factor analysis techniques to find the best factors to serve as proxies for corporate governance. The results of the study show that financial distress has a positive effect on tax avoidance. This study also found that good corporate governance which is proxied by an independent board of commissioners can weaken the effect of financial distress on tax avoidance. The increasing financial distress in companies, the practice of tax avoidance is also increasing. If the company implements good governance, the management will make less effort to tax avoidance. This is because the more the number of independent commissioners, the more effective it is in supervising the performance of managers.

Keywords: Financial Distress; Tax Avoidance; Good Corporate Governance

1. Introduction

The COVID-19 pandemic that began in 2019 resulted in an economic crisis. This is as a result of the implementation of Large-Scale Social Restrictions (PSBB) which has caused a decline in economic growth. In this condition, the government is trying to reduce the adverse impact of the Covid 19 pandemic on the Indonesian economy with the National Economic Recovery (PEN) programme through the issuance of Minister of Finance Regulation Number 23/PMK.03/2020 concerning Tax Incentives for Taxpayers Affected by the Corona Virus Outbreak (Darono, 2021). The regulation contains four fiscal stimuli including Income Tax 21 incentives, Article 22 import incentives, Article 25 Income Tax incentives and VAT incentives. The government expanded the fiscal stimulus through PMK No. 44/PMK.03/2020 concerning Tax Incentives for Taxpayers Affected by the Corona Virus Disease 2019 Pandemic in connection with the spread of the Corona Virus Disease 2019 (COVID-19) pandemic as a national disaster to other sectors that affect economic stability and community productivity. The expansion of the stimulus is in the form of income tax relaxation based on Government Regulation Number 23 Year 2018 for taxpayers who have certain gross turnover in accordance with the provisions referred to in Government Regulation Number 23 Year 2018. The income tax is borne by the Government and is not calculated as income subject to tax.

According to the Ministry of Finance (MoF) report, Indonesia's tax ratio in 2021 is 9.11% of GDP. Although it has increased compared to 2020, Indonesia's tax ratio in 2021 is still below the pre-pandemic level as shown in the graph. In 2018, the tax ratio was at 10.24%, then fell to 9.77% in 2019, and fell further to 8.33% in 2020. 2020 was the year when Indonesia's tax ratio declined the most. This happened due to the Covid-19 pandemic which limited people's

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economic activities. Meanwhile, in 2021, Indonesia's tax ratio began to increase in line with the strengthening of tax performance and the recovery of the national economy from the impact of the pandemic (Dihni, 2022).

According to Segara (2019), the phenomenon of tax avoidance in Indonesia can be seen from the tax ratio of the Indonesian state. The tax ratio shows the government's ability to collect tax revenue or absorb back gross domestic product (GDP) from the community in the form of taxes. The higher the tax ratio, the higher the State Budget (APBN) so that it can be used for various State needs in terms of development or facilities.

Financial distress experienced by companies can increase the potential for companies to practice tax avoidance to remain standing. According to Alifianti H. P. & Chariri (2017), if the risk of bankruptcy is high enough, the company will inevitably aggressively practice tax avoidance and ignore the audit risk carried out by the tax authorities. According to Richardson et al. (2021), there are several implications for corporate tax regulations when the company is experiencing financial difficulties. For example, the increased cost of capital and reduced external financial resources (debt, loans) faced by companies in crisis and in general, result in increasing managers' desire to take risks that can restore corporate balance through tax avoidance.

Research conducted by Ariff et al. (2023), found that companies experiencing financial distress committed higher tax avoidance during the pandemic compared to the period before the pandemic. These results are in line with research conducted by (Dang & Tran, 2021), (Richardson et al., 2021) and (Gian et al., 2022). However, it is different from the research conducted by Kalbuana et al. (2023), Julianta & Simanjuntak (2023) and Hisa, Nadila & Haq (2022), found that financial distress has no effect on tax avoidance.

The results of previous studies state the inconsistency of research results on the effect of financial distress on tax avoidance, one of the causes is the existence of contingency factors. The contingency approach provides a view that the relationship between the independent variable and the dependent variable can be influenced by the presence of conditional variables. This study suspects the existence of corporate governance factors which are a control and direction of the company's operational activities to be able to realise the expectations of stakeholders. Good corporate governance (GCG) itself is a procedure for supervising and regulating relations between parties related to management such as shareholders and other parties to work together in providing more value to the company. Companies that implement GCG will obtain maximum value and contribute to the company through improved performance and maintain the company's going concern in the long term. Not only contributing to the company, companies with GCG are contributors to the economy and society. The implementation of corporate governance will be able to prevent tax avoidance by management in the company due to the management of the risk of directing and controlling the company.

There are 4 GCG mechanisms, namely the audit committee has duties related to tax avoidance practices. Independent commissioners as a practice of good corporate governance, can make company movements supervised. So that the role of independent commissioners will make a problem that exists can be taken with a good decision. Because the supervision of the performance of the board of directors will later be assessed whether it is appropriate. Furthermore, the GCG mechanism has managerial ownership and institutional ownership. Managerial ownership is a situation where the management of a company simultaneously holds the position of director and shareholder who actively participates in decision making (Buertey et al., 2020), while institutional ownership is ownership of company shares owned by institutions or institutions such as insurance companies, banks, investment companies and other institutional ownership.

2. Literature review and hypothesis development

Shareholders certainly want to invest in a healthy and stable company, so that with the occurrence of financial distress, the agents will certainly look for ways so that they can reduce expenses as little as possible, in order to maintain their relationship with shareholders. Based on agency theory, companies experiencing financial distress will stretch the relationship between agents and principals, differences in interests in agency theory will cause taxpayer non-compliance where companies will carry out tax planning so that tax payments are optimal (Dewi & Yasa, 2020). Managers will do their best to use existing safe methods to keep the company running, namely by practicing tax avoidance.

One possible way is to reduce its relationship with the government, such as delaying or avoiding income tax payments. Management will try to find out how to minimise tax liabilities without violating tax laws, so that the tax burden can be minimised through tax avoidance (Swandewi & Noviari, 2020).

The results of research conducted by Richardson et al. (2021), state that companies that are in financial distress will prefer to do tax avoidance rather than reduce other company costs, because companies do not have the option to take higher risks so that they become more aggressive in taxation, because it is important for companies to improve their finances. Likewise, the results of research by Ariff et al. (2023), found that companies experiencing financial distress committed higher tax avoidance during the pandemic compared to the period before the pandemic. These results are in line with research conducted by Dang & Tran (2021), and Curry & Fikri (2023), which state that there is a positive relationship between financial distress and tax avoidance, which means that companies that are experiencing financial distress tend to take tax avoidance policies. According to Gian et al. (2022), financial distress has a significant effect on tax avoidance.

From an agency theory perspective, tax avoidance is a rational strategy to reduce agency costs for companies experiencing financial distress. The management of companies experiencing financial distress can also feel that given the circumstances, the tax authorities will be less strict in enforcing tax laws, so the decision to conduct tax avoidance when the company is experiencing financial distress is the right decision so that the company continues to run well.

H_1: Financial distress has a positive effect on Tax Avoidance

In conditions of financial distress, good corporate governance is very important to help oversee decisions made by managers. Without the implementation of good corporate governance when the company is experiencing financial difficulties, managers can freely take tax avoidance actions. This is supported by compliance theory which states that taxpayer compliance is a behaviour based on the awareness of a taxpayer of his tax obligations while still based on the laws and regulations that have been determined in line with this theory, one of the objectives of implementing good corporate governance is compliance with laws and regulations which include tax obligations. Based on compliance theory, it shows that GCG can encourage companies to carry out their tax obligations properly.

Hermawan & Aryati (2022), it states that the independent board of commissioners is alleged to have a positive impact on monitoring and controlling business management and reducing agency costs so that tax avoidance can be suppressed. In line with the results of research conducted by Gian et al. (2022), that good corporate governance proxied by institutional ownership and managerial ownership managed to have a significant influence on the relationship between financial distress and tax avoidance. According to Alkurdi & Mardini (2020), in their research stated the results of the more shares owned by managers in the company, managers tend to minimise tax avoidance practices. The same results are stated in research conducted by Pricilia, Refila & Nugrahanti (2020), stating that the greater the proportion of managerial ownership, the less the efforts made by management to carry out tax avoidance. From the perspective of compliance theory, good corporate governance can moderate the negative effect of financial distress on tax avoidance, which means that the better the implementation of good corporate governance, the more effective it is in supervising the performance of company managers so that it can prevent companies from experiencing financial distress so that it will reduce managers' opportunities for tax avoidance.

H_2: Good corporate governance weakens the effect of financial distress on tax avoidance.

3. Material and methods

This research was conducted at transportation and logistics sector companies listed on the Indonesia Stock Exchange in 2019-2021. The population for this study were all transportation and logistics sector companies listed on the Indonesia Stock Exchange (IDX) for the period 2019 - 2021. The sampling method used is purposive sampling method, which is a sampling technique based on certain criteria with consideration. The criteria that are taken into consideration in sampling this study can be seen in table 4.1 below.

- Transport and logistics sector companies listed on the Indonesia Stock Exchange
- Companies that IPO (Initial Public Overing) before 2019
- Companies that have published annual reports for the period 2019 - 2021
- Companies that experience financial distress

The reason for selecting the population using transportation and logistics companies is because it is the sector of companies most affected by the Covid 19 Pandemic which shows dynamic profit movements. Based on these criteria, 14 company samples were obtained that met the sample selection criteria. The observation year was 3 years, namely in 2019, 2020 and 2021 and the total number of observation period samples was 48 samples. The hypothesis in this study was tested using MRA (Moderated Regression Analysis).

4. Results and discussion

4.1. Descriptive Statistic

Table 1 Descriptive Statistic

	N	Min	Max	Mean	Std. Deviation
TA	42	-154.613	781.343	23.468	126.296
FD	42	-60.631	3.651	-7.462	15.946
KM	42	0.000	65.531	4.829	15.850
KI	42	0.645	98.961	67.361	30.301
DKI	42	33.000	66.000	44.000	10.181
KA	42	2.000	7.000	3.000	0.954

Secondary Data. 2023

Based on table 1. it shows that the total number of observations used is 42. The tax avoidance (TA) variable is measured using the effective tax rate (ETR). the minimum value is -154.613 which indicates a large tax avoidance act in the AirAsia Indonesia Tbk company. in 2019 observations. The maximum value is 781.343 which indicates a low level of tax evasion at the Samudera Indonesia Tbk company. in 2020 observations. The average value is 23.468 <25% which indicates an act of tax evasion in the sample companies. because the ETR percentage is less than 25% and the lower the company's ETR percentage. the higher the company's tax avoidance level. The standard deviation value or standard deviation is 126.296. which means that the tax avoidance variable has a large data distribution because the standard deviation value is greater than the average value. So that it can be concluded that the TA variable data is not well distributed or the data is heterogeneous which indicates that research observations have TA values that are not balanced between one another.

The financial distress (FD) variable is measured using the z-score. the minimum value of -60.631 <1.22 which is owned by the Berlian Laju Tanker Tbk company. on observations in 2020 which indicates the company is in the unhealthy category. The maximum value is 3.651 > 2.9 which is owned by Jaya Trishindo Tbk. in 2019 observations which show the company is in the healthy category. The average value is -7.462 <1.22 which indicates that the sample companies in the study period are in the category of unhealthy and experiencing financial distress. The standard deviation value or standard deviation is 15.946. which means that the financial distress variable has a large data distribution because the standard deviation value is greater than the average value. So that it can be concluded that the FD variable data is not well distributed or the data is heterogeneous which indicates that research observations have FD values that are not balanced between one another.

Managerial ownership has a minimum value of 0.000 which indicates that there are managers who do not own shares in the companies Mineral Sumberdaya Mandiri Tbk.. Berlian Laju Tanker Tbk.. AirAsia Indonesia Tbk.. Garuda Indonesia Tbk.. Steady Safe Tbk.. and Express Transindo Utama Tbk. .. The maximum value is 65.531. which means that there are companies whose majority shares are held by managers. namely Sidomulyo Selaras Tbk. The average value of 4.829 indicates that the percentage of share ownership by managers in the sample companies during the study period is still small. The standard deviation value is 15.850. which means that the managerial ownership variable has a large data distribution because the standard deviation value is greater than the average value. So that it can be concluded that the KM variable data is not well distributed or the data is heterogeneous which indicates that research observations have KM values that are not balanced between one another.

The institutional ownership variable has a minimum value of 0.645 which is owned by the company Adi Sarana Armada Tbk. in 2020. The maximum value is 98.961 which is owned by the company AirAsia Indonesia Tbk. in 2020. The average value is 67.361. which means that there are companies whose majority shareholders are institutional parties and the standard deviation value is 30.301 which indicates that there is no data deviation in the institutional ownership variable because the standard deviation value is smaller than the average value. So that it can be concluded that the KI variable data has been well distributed or the data is homogeneous which indicates that the sample companies during the study period have institutional shares that are balanced between each other.

The independent board of commissioners variable has a minimum value of 33.000 in the company Mitra International Resources Tbk. and Sidomulyo Selaras Tbk. The maximum value of 66.000 is found in the company Temas Tbk. The average value is 44.000 > 30%. which means that there are sample companies during the observation period that have met the minimum percentage of independent commissioners from the total number of members of the board of commissioners (Santoso. 2017). The standard deviation value is 10.181 which indicates that there is no data deviation in the independent board of commissioners variable because the standard deviation value is smaller than the average value. So that it can be concluded that the DKI variable data has been well distributed or the data is homogeneous which indicates that the sample companies during the study period had a percentage of independent commissioners that was balanced between one another.

The audit committee variable has a minimum value of 2.000 in Berlian Laju Tanker Tbk. in 2020 and AirAsia Indonesia Tbk. in 2019. The maximum value of 7.000 is in the company Garuda Indonesia Tbk. in 2020. The average value is 3.000. which means that the sample companies. seen from the average. have fulfilled the minimum number of audit committees. namely 3 people from independent commissioners and outsiders from issuers or public companies (Financial Services Authority. 2015). The standard deviation value is 0.954 which indicates that there is no data deviation in the audit committee variable because the standard deviation value is smaller than the average value. So it can be concluded that the KA variable data has been well distributed or the data is homogeneous which indicates that the sample companies during the study period had an equal percentage of audit committees.

After conducting descriptive analysis. the researcher conducted a factor analysis on good corporate governance (GCG) variable proxies. This factor analysis was carried out with the aim of filtering out which proxies are the most superior or most dominant of several proxies for GCG variables. The assumptions based on whether or not factor analysis can be used are that the matrix data must have sufficient correlation and the desired KMO (Kaiser-Meyer-Olkin) value must be > 0.5. The results of the KMO and Bartlett's Test in this study are presented in Tables 2 and Table 3.

Table 2 KMO Value and *Bartlett's Test*

Kaiser-Meyer-Olkin Measure of Sampling Adequacy.	0.639
Bartlett's Test of Sphericity Approx. Chi-Square	13.595
Df	3
Sig.	0.004

Secondary Data. 2023

Based on table 2. the KMO value is 0.639 > 0.50 and a significance level of 0.004 <0.05 indicates that the data adequacy requirements are met.

As for the results of the Anti-Image Matrices test as presented in table 3 below.

Table 3 Anti-Image Matrices Test Results

		KM	**KI**	**DKI**	**KA**
Anti-image Covariance	KM	0.746	0.275	0.133	0.222
	KI	0.275	0.623	-0.191	0.312
	DKI	0.133	-0.191	0.836	-0.028
	KA	0.222	0.312	-0.028	0.783
Anti-image Correlation	KM	0.485[a]	0.404	0.169	0.290
	KI	0.404	0.496[a]	-0.265	0.447
	DKI	0.169	-0.265	0.696[a]	-0.035
	KA	0.290	0.447	-0.035	0.350[a]

Secondary Data. 2023

Based on table 3 that there are three variables that have a Measure of Sampling Adequacy (MSA) value of <0.5. namely the variables KM. KI. and KA. Whereas the DKI variable has an MSA value of > 0.5. Therefore. it is necessary to re-factor analysis on the 3 variables that have the highest MSA values. namely the KM. KI and DKI variables to find 1 factor that can be used as a proxy for Good Corporate Governance.

Table 4 Anti-Image Matrices Test Results

		KM	KI	DKI
Anti-image Covariance	KM	0.814	0.255	0.154
	KI	0.255	0.778	-0.225
	DKI	0.154	-0.225	0.837
Anti-image Correlation	KM	0.643[a]	0.321	0.187
	KI	0.321	0.615[a]	-0.279
	DKI	0.187	-0.279	0.666[a]

Secondary Data. 2023

Based on table 4 the DKI variable consistently has the highest MSA value and is more than 0.5. it can be concluded that the proxy that can represent the Good Corporate Governance variable is DKI (Independent Board of Commissioners).

4.2. Moderating Regression Analysis (MRA)

Table 5 Moderation Regression Test Results

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(constant)	1.941	0.492		3.946	0.000
	Financial Distress	0.045	0.009	0.598	5.259	0.000
	Good Corporate Governance	0.011	0.011	0.090	0.932	0.357
	Financial Distress* Good Corporate Governance	-0.173	0.019	-1.100	-8.996	0.000

Secondary Data. 2023

The resulting moderation regression equation is as follows.

$$Y = \alpha + \beta 1X + \beta 2Z + \beta 3X*Z + e$$

$$Y = 1.941 + 0.045X + 0.011Z - 0.173X*Z + e$$

$$ETR = 1.941 + 0.045(z\text{-score}) + 0.011(DKI) - 0.173(z\text{-score}*DKI + e$$

Tax Avoidance = 1.941 + 0.045 (Financial Distress) + 0.011 (Good Corporate Governance) - 0.173 (interaction of Financial Distress with Good Corporate Governance)

Based on table 1 if the independent variable of financial distress (X) has no contribution (constant) to the dependent variable. namely tax avoidance. then tax avoidance will increase by 1.941%. The regression transformation coefficient of the financial distress variable (X) is 0.045. which means that if financial distress (X) increases by one point. tax avoidance (Y) will increase by 0.045%.

The regression transformation coefficient of the good corporate governance variable (Z) is 0.011. which means that if good corporate governance (Z) increases by one point while the financial distress variable (X) remains. then tax avoidance decreases by 0.173%.

The regression transformation coefficient of the financial distress and good corporate governance variables (X*Z) is the interaction between financial distress and good corporate governance resulting in a regression value of -0.173.

4.3. Coefficient of Determination (R^2)

Table 6 T Coefficient of Determination (R^2)

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.838[a]	0.703	0.679	0.678

Secondary Data. 2023

The acquisition of the R Square value is known to be 0.703. this explains that the determination of all variables. namely financial distress. and the moderating variable good corporate governance. can explain or describe tax avoidance of 0.703 or 70.3% and the remaining 29.7% is explained by other variables not examined in this study.

4.4. Hypothesis

4.4.1. Financial Distress on Tax Avoidance

The regression coefficient of the financial distress variable is positive. and the t test results show a value of 5.259 with a significance of 0.000. The significance value is less than 0.05. it can be stated that financial distress has a positive and significant effect on tax avoidance. This result is in accordance with the proposed hypothesis.

The first hypothesis states that Financial Distress has a positive effect on Tax Avoidance. This study shows that financial distress has a positive effect on tax avoidance or in other words H1 is accepted. This means that the increasing financial distress in the company. the tax avoidance will also increase. It also applies vice versa. decreasing financial distress. tax avoidance decreases as well. The significant effect indicates that financial distress has an important role in tax avoidance. These results are in line with research conducted by Dang & Tran (2021). which found a positive relationship between financial distress and tax avoidance. which means that companies that are experiencing financial distress tend to take tax avoidance policies. Likewise. research conducted by Richardson et al. (2021). which states that financial distress has a positive and significant effect on tax avoidance. The results of Curry & Fikri's research (2023) state that financial distress has a positive effect on tax avoidance practices. the greater the financial difficulties faced by the company. the greater the company's desire to practice tax avoidance. When the company experiences high financial distress. the desire to practice tax avoidance will be higher. When the company experiences financial distress. at the same time the company's income or revenue begins to decline so that the company will be more aggressive towards its tax obligations.

Based on agency theory. companies experiencing financial distress will stretch the relationship between agents and shareholders. Shareholders certainly want to invest in a healthy and stable company. so that with the occurrence of financial distress. the agents will certainly look for ways so that they can reduce expenses as small as possible. in order to maintain their relationship with shareholders. One way that might be done is to reduce its relationship with the government. such as delaying or avoiding income tax payments. Swandewi & Noviari (2020). also support the effect of financial distress on tax avoidance in the perspective of agency theory that the agent tries to maintain the quality of its performance so that it still looks good in front of shareholders even though the company is experiencing financial distress. Thus. they will be triggered to do tax avoidance to improve the condition of the financial statements which will certainly be presented to shareholders and the public. Managers will do their best to use the safe methods available to keep the company running. namely with tax avoidance practices. Manajamen will try to find out how to minimise tax liabilities without violating tax laws. so that the tax burden can be minimised through tax avoidance.

4.4.2. Good Corporate Governance Moderate the Effect of Financial Distress on Tax Avoidance

The regression coefficient of the interaction variable financial distress * good corporate governance is negative. and the t test results show a value of -8.996 with a significance of 0.000. The significance value is less than 0.05. it can be stated that good corporate governance can moderate the effect of financial distress on tax avoidance. The negative regression coefficient indicates that good corporate governance weakens the effect of financial distress on tax avoidance. This result is in accordance with the hypothesis proposed.

The second hypothesis in this study states that Good Corporate Governance is able to moderate and weaken the effect of financial distress on tax avoidance. This study shows that Good Corporate Governance. proxied by the independent board of commissioners. has a negative and significant effect in moderating the effect of financial distress on tax avoidance so that the second hypothesis is accepted. The results of this study indicate that the greater the number of independent commissioners. the supervision of company management will be tighter and more effective so that the strict supervision carried out by independent commissioners will reduce managers' opportunities for tax avoidance and will encourage management to be careful in making decisions for the sake of the company's economic activities.

The results of this study were able to confirm the research conducted by Lauren et al. (2022). in their research stated that the independent board of commissioners can moderate the relationship between financial distress and tax avoidance. The same results were stated in research conducted by Gian et al. (2022). which states the results of Good Corporate Governance can have a significant effect on the relationship between financial distress and tax avoidance. Hermawan & Aryati's research (2022) states that the independent board of commissioners is alleged to have a positive impact on monitoring and controlling business management and reducing agency costs so that tax avoidance can be suppressed. This is because based on POJK Number 57 / POJK.04 / 2017 article 1 the independent board of commissioners is tasked with carrying out a form of activity that is able to oversee various aspects and indicators of management based on the provisions and provide direct advice or input to the board of directors.

In accordance with compliance theory. to manage company activities carried out by agents must be supervised to ensure that management has been carried out in full compliance with applicable rules and regulations. The greater the proportion of independent commissioners. the tighter the supervision. so it will be more difficult for management to take tax avoidance actions. So that even though the company is experiencing financial distress. management still complies with tax regulations. so that later it will not be subject to administrative sanctions or criminal sanctions.

5. Conclusion

Financial distress has a positive effect on tax avoidance. This means that financial distress or financial difficulties experienced by the company due to the decline in the company's economic and financial conditions which results in an increased risk of bankruptcy. can increase the potential for companies to practice tax avoidance so that the company can remain standing. Good corporate governance proxied by the independent board of commissioners weakens the effect of financial distress on tax avoidance. This means that the greater the number of independent commissioners in a company. the more effective and tighter the supervision of the independent board of commissioners on manager performance so as to reduce the possibility of managers doing tax avoidance as an effort to reduce the tax burden triggered by financial distress.

Managerial Implication

In making a policy for the company. management must have sensitivity to environmental developments that can affect the company's business. have broad insight and strategic thinking skills and comply with all applicable regulations. in this case complying with tax regulations in order to avoid sanctions and the company can grow sustainably. For other parties. this research is expected to be a consideration and reference for future research interested in examining the same studies regarding tax avoidance. good corporate governance and financial distress in the future.

Compliance with ethical standards

Disclosure of conflict of interest

No conflict of interest to be disclosed.

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