

# Aggressive Tax Avoidance, Corruption, and Good Governance

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## ABSTRACT

**Purpose:** This study has two main purposes; first it is to examine the relationship between aggressive tax avoidance and corruption, second is to examine the moderating effect of good governance implementation on the relationship between aggressive tax avoidance and corruption.

**Design/methodology/approach:** A sample of 840 ASEAN companies publicly-listed from 2015-2018. This study used aggressive tax avoidance model analysis with ETR, C-ETR, and BTD measurements.

**Findings:** This study found a positive relationship between aggressive tax avoidance and the level of corruption. This study also proved the effect of good governance on the weakening of the relationship between aggressive tax avoidance and corruption empirically.

**Research limitations/implications:** These research findings are in line with the context of public-listed ASEAN countries which may have different implications on unlisted companies. Unlisted companies are beyond the scope of this study. This study has implications for the importance of more specific anti-tax avoidance policies in order to reduce state losses due to tax avoidance practices that are influenced by the effects of tax policies in ASEAN-4 countries, and also policies that can prevent corrupt practices by strengthening good government governance implementation.

**Originality/value:** This study offers a new perspective on good governance research. First, from the view of corporate governance, and second, from a view of governance. This study has important implications for developing an aggressive anti-tax avoidance policy that is more specific to reducing state losses due to tax avoidance practices and also effective corruption control mechanisms in reducing aggressive tax avoidance practices.

**Keywords:** *aggressive tax avoidance, corruption, good governance*

## 1. INTRODUCTION

Corruption and tax avoidance are not recent problems, and both are significant issues faced by the world economy today (James *et al.*, 2016), especially in developing countries. Tax avoidance is included by establishing a Special Purpose Vehicle (SPV) or 'paper company' in the country of a tax haven which is also categorized as a criminal act of corruption. Tax avoidance is a strategy model to explore differences or ambiguities in tax policy by manipulating a transaction to minimize the overall tax burden owed to the group of companies, even to the point of causing false losses (Abdallah, 2013).

Certainly not without cause, tax avoidance has become a major issue in the world of taxation by businesses, academics, and tax authorities due to the negative impact of tax avoidance irregularities that cause harm to the state (Hansen, 1992; Abdallah, 2013). There are several tax avoidance cases carried out by multinational corporations such as in the US, Europe, Asia, and ASEAN countries.

Major cases of tax manipulation that have been taken by the Directorate General of Taxes (DGT) include the Asian Agri case ([www.pajak.go.id](http://www.pajak.go.id)), Bumi Resources ([www.ikpi.or.id](http://www.ikpi.or.id)), Adaro ([www.ortax.org](http://www.ortax.org)), Indosat ([www.ortax.org](http://www.ortax.org)), Indofood (<http://pwc.blogs.com>), Kaltim Prima Coal ([bisnis.tempo.co](http://bisnis.tempo.co)), and PT. Toyota Motor Manufacturing Indonesia ([investigate.tempo.co/Toyota](http://investigate.tempo.co/Toyota)).

The severe impact of tax avoidance and massive taxpayers avoiding tax cannot be separated from the high level of corruption perception index (CPI) in ASEAN-4 countries. The low GPA achieved by ASEAN-4 countries has an impact on the increasing tendency of taxpayers to avoid tax. Research by Ronald and Ahmed (2006) and Alm J *et al.*, (2016) state that corruption is a stimulant that increases severe tax avoidance. One form of corruption is bribery. Bribery is a trend of entrepreneurs in ASEAN-4 countries in doing business. This is reflected in research conducted by Transparency International (TI) which places the ASEAN-4 countries in the lowest position (Bribe Payers Index, 2011).

Report from the 2013 Global Corruption Barometer also places ASEAN-4 countries in a high percentage of citizens

of bribery cases. David (2009) found that non-compliance of taxpayers increased through cases of bribery against officers. This condition matches the fact that the results of The Enterprise Surveys (ES) conducted by the World Bank in 2015, which found that ASEAN-4 countries had bribery cases with the largest tax official, namely, Indonesia with 31% of companies having been asked for bribes by tax officials, followed by Malaysia with 28%, the Philippines with 17%, and Thailand with 10%.

One mechanism for controlling tax avoidance behavior is through the implementation of good governance. Previous studies in 25 countries found how high public trust in the government had an impact on declining tax avoidance practices, companies trying to pay their taxes fairly to respect public trust (Kanagaretnam *et al.*, 2014). Furthermore, the component in measuring good governance also involves an assessment of control of corruption. The effectiveness of corruption control will have an impact on reducing aggressive taxation activities as a result of studies on 30 developed and developing countries found that the cost of reputation and sanctions against tax non-compliance became the trigger in increasing citizens' tax compliance when the level of control of corruption is high (Ronald and Ahmed, 2006).

This study aims to empirically examine the effect of corruption on tax avoidance and the effect of good governance on the relationship of corruption and tax avoidance in several ASEAN-4 countries. This study has specific implications for the importance of more specific anti-tax avoidance policies in order to reduce state losses due to tax avoidance practices and provide recommendations on policies that can prevent corrupt practices that are influenced by the effects of tax policies in ASEAN-4 countries.

This study is important in order to support regulators in ASEAN-4 countries in accelerating the implementation of increasingly aggressive BEPS (Base Erosion and Profit Shifting). These 15 steps have been completed on October 5, 2015, which has become an agreement with OECD countries and also ASEAN countries. One of them is in the 11<sup>th</sup> act that requires the taxation authority to update peritun. Furthermore, corruption is a serious problem in Southeast Asian countries. Based on the average ranking of Transparency International's Corruption Perception Index, ASEAN-4 are ranked as the least corrupt country among Asian countries. However, ASEAN-4 is still facing problems in its fight against corruption, in which efforts undertaken to prevent corruption has been said to be "unsatisfactory".

## 2. LITERATURE REVIEW

### 2.1 Aggressive Tax Avoidance

The view that tax is a significant burden for companies and reduces the availability of cash flow has triggered companies and shareholders to reduce the tax burden through aggressive tax activities. Aggressive tax activity leads to maximizing the company value because there are including non-taxes that arise from the manager's hidden actions.

The development of tax avoidance taxation is quite monumental. In the past, many parties equated tax avoidance as legal action, but now in tax avoidance itself is branched out. Some consider that there is acceptable tax avoidance and unacceptable tax avoidance. The differences are as revealed by Slamet (2007); acceptable tax avoidance/tax planning, namely: (1) have good business goals, (2) not merely to avoid taxes, (3) in accordance with the spirit and intention of parliament, and (4) do not make transactions that are engineered. Aggressive tax avoidance includes: (1) do not have good business goals, (2) solely to avoid taxes, (3) not in accordance with the spirit and intention of parliament, and (4) the existence of transactions that are engineered to incur costs or losses.

However, of the two differences above are very feeble to distinguish which are acceptable and which are unacceptable. While Brian and Michael (2002) distinguish tax planning into defensive tax plannings which are tax planning that is done by not placing taxation experts or advisors and is based only on domestic law and offensive tax planning which places experts as tax advisors and performed by utilizing countries that fall into the category of tax haven countries.

The development of research in tax avoidance is quite monumental. A large number of studies in measuring tax avoidance used ETR, as well as previous studies conducted by Richardson and Lanis (2007; 2012; 2013), Chen *et.al.* (2010), Minnick and Noga (2012).

$$ETR = \frac{\text{Tax Expense } i, t}{\text{Pretax Income } i, t}$$

Where:

- ETR is the effective tax rate based on applicable financial accounting reporting
- Tax expense is the corporate income tax expense for the company *i* in year *t* based on the company's financial statements
- Pretax Income is the income before tax for company *i* in year *t* based on the company's financial statements.

This study also uses another measurement, namely Cash ETR that is used to strengthen the model in predicting research findings. The use of this model is also carried out by several studies such as Zimmerman (1983), Chen et.al. (2010), and Minnick and Noga (2012). The purpose of using this model is also different if the ETR aims to see the tax burden paid in the current year while the Cash ETR is to accommodate the amount of tax cash that is currently paid by the company. In this study, Cash ETR will be calculated by the formula demonstrated by Hanlon (2010);

$$\text{Cash ETR} = \frac{\text{Cash Tax Paid } i, t}{\text{Pretax Income } i, t}$$

Table 1. Tax Avoidance Measurement Models

Measure	Computation	Description
GAAP ETR	$\frac{\text{Worldwide total income tax expense}}{\text{Worldwide total pre-tax accounting income}}$	Total tax expense per dollar of pre-tax book income
Current ETR <sup>a</sup>	$\frac{\text{Worldwide current income tax expense}}{\text{Worldwide total pre-tax accounting income}}$	Current tax expense per dollar of pre-tax book income
Cash ETR <sup>b</sup>	$\frac{\text{Worldwide cash taxes paid}}{\text{Worldwide total pre-tax accounting income}}$	Cash taxes paid per dollar of pre-tax book income
Long-run cash ETR <sup>c</sup>	$\frac{\sum (\text{Worldwide cash taxes paid})}{\sum (\text{Worldwide total pre-tax accounting income})}$	Sum of cash taxes paid over n years divided by the sum of pre-tax earnings over n years
ETR Differential <sup>d</sup>	Statutory ETR—GAAP ETR	The difference of between the statutory ETR and the firm's GAAP ETR
DTAX <sup>e</sup>	Error term from the following regression: ETR differential × Pre-tax book income = a + b × Controls + e	The unexplained portion of the ETR differential
Total BTDF	Pre-tax book income - ((U.S. CTE + Fgn CTE) / U.S. STR) - (NOL <sub>t</sub> - NOL <sub>t-1</sub> )	The total differences between book and taxable incomes
Temporary BTDF	Deferred tax expense / U.S. STR	
Abnormal total BTDF <sup>g</sup>	Residual from BTDF/TA <sub>it</sub> = βTA <sub>it</sub> + βm <sub>it</sub> + e <sub>it</sub>	A measure of unexplained total book-tax differences
Unrecognized tax benefits <sup>h</sup>	Disclosed amount post-FIN48	Tax liability accrued for taxes not yet paid on uncertain positions
Tax shelter activity <sup>i</sup>	Indicator variable for firms accused of engaging in a tax shelter	Firms identified via firm disclosures, the press, or IRS confidential data
Marginal tax rate <sup>j</sup>	Simulated marginal tax rate	Present value of taxes on an additional dollar of income

Another method of measuring tax avoidance is accounting differences and book-tax differences (BTD). These differences are distinguished by 2 (two), namely permanent and temporary differences. Permanent differences occur when income or expenses recognized in an account, but not allowed to be recognized as taxable income or expense, while temporary differences occur when the tax and accounting system recognize the amount of income or expense but differ regarding the time of recognition. Temporary differences can be positive or negative. Positive temporary differences arise when accounting income is higher than taxable income, while negative temporary differences occur when accounting income is lower than taxable income (Hanlon, 2005).

Some tax aggressiveness calculation methods listed in Table 1 used by researchers are ETR, Cash ETR, and BTDF. These three methods are deep in reflecting the impact

Where :

- Cash ETR is the effective tax rate based on the amount of tax cash paid by the company in the current year
- Cash tax paid is the amount of tax cash paid by company i in year t based on the company's financial statements
- Pretax income is the income before tax for the company i in year t based on the company's financial statements

on accounting earnings, the impact on tax avoidance, and also in accordance with the method of calculating earnings based on rules or regulations taxation.

## 2.2 Corruption

The literature on corruption primarily focuses on bribes to public officials made by employers to avoid taxation and regulation and win public contracts (Shleifer and Visny, 1993). The literature has also been limited to a detailed microeconomic analysis of corruption. Kaufman (2010) found that there was a direct relationship between corruption activities by the government and various aspects of their fiscal policy that are not working through bribery and "small" corruption from bureaucrats, but through forming their policies or "big" corruption.

Corruption is generally defined as a behavior that deviates from the formal duties of the public role because private money is related to the person (close family, personal clicks); or breaking the rules against the use of certain types of personal influence (Nye, 1967). Gupta et al. (2002) found that the corruption contributed to income inequality and poverty. In particular, corruption understanding according to ordinary people is an act of taking state money in order to obtain personal benefits.

The notion of corruption develops with so many definitions. This is because the definition of corruption can be found in various perspectives, both through the literal meaning of words, opinions of various experts, and based on the legislation that governs. Internationally, there is no single definition established throughout the world about what is meant by corruption. Corruption is the act of someone who misuses trust in a problem or organization to get profit.

### **2.3 Good Governance**

Good governance is a way of power used in managing various resources and economies for community development and also the practice of applying authority to manage various affairs in the administration of the country politically, economically, and administratively at all levels (web.worldbank.org). Good governance can be applied in several contexts; corporate governance, international governance, national governance, and local governance (UN, 2009). While in the context of research, there are two views, namely the corporate level (corporate governance) and the second level of the state (government governance) (Judge et al., 2010; Christopher, 2013).

Government governance is defined as securing a reciprocal relationship between management, control, and supervision by the government and by organizations formed by government authorities, which aim to carry out policies efficiently and effectively, as well as disclosure of information and provide accountability for the welfare of all stakeholders (The Netherlands Ministry of Finance Government Audit Policy Directorate, 2000).

This different definition is a consequence of differences between the business sector and the government sector. The business sector is more oriented to profit objectives as reflected in the financial statements, while the government sector is oriented to the creation of a safeguard and welfare framework for all stakeholders to achieve the goals of establishing a government or country that is reflected in the state budget. The form of government sector organization is usually more complex and also has various levels from central government to those in local government as basic service providers to the community or stakeholders.

Furthermore, good governance research on government ownership shows that countries that adopt a civil law legal system tend to have low-quality governance (Ginka et al.,

2012). Government ownership in a business entity is not solely to increase the value of the company, and government ownership also tends to reduce the number of board committees, especially in countries that use civil law in their legal system. The low quality of governance is also related to the low internal supervision by the government. Chan et al. (2013) added the impact of good governance on Chinese government ownership, in which corporate governance on government ownership plays a role in tax management in China. The results of the study showed that managers of companies controlled by the government were more likely to achieve political goals to protect government revenue in their tax strategies.

The existence of better government governance in a country also has an impact on increasing foreign investment. This is due to better protection of investment from investors, even the World Bank recommends the application of good governance because it has a positive effect on investor protection (Byung and Robert, 2015). Implementation of good governance in several studies is also considered capable of reducing the opportunistic behavior of companies, both owners and directors. Moataz (2014) found that good governance is able to reduce management behavior towards earnings management and also abuse of related party transactions. Some institutions also publish government governance measurement mechanisms, such as world banks that use the Worldwide Governance Indicators (WGI) for the country level which consists of 6 (six) dimensions namely; Voice and Accountability, Political Stability and Absence of Violence, Government Effectiveness, Regulatory Quality, Rule of Law, and Control of Corruption. Some use country-level analysis by measuring the use of the legal system in force in the country (Jensen, 1993; La Porta et al., 1998), anti-takeover policies (Christopher et al., 2013), control mechanisms, supervision, accountability (The Netherlands Ministry of Finance Government Audit Policy Directorate, 2000).

### **2.3 Hypothesis**

#### **1) Effect of Corruption on Aggressive Tax Avoidance**

Aggressive tax avoidance behavior is a part of aggressive tax actions. The perception of corruption is one of the triggers for tax avoidance. The reciprocity between corruption and aggressive tax avoidance is inseparable from corruption which is an important factor that negatively affects the decision of companies or individuals to pay taxes (Uslaner, 2010). Alm et al. (2016) found that corruption is a factor driving higher tax avoidance practices. Thus, it is expected that the results of this study indicate that the application of good governance at the state level will be able to reduce the level of corruption which has an impact on decreasing aggressive tax avoidance practices. Therefore, the researcher has an initial conclusion that corruption has

a positive relationship with aggressive tax avoidance that is a part of aggressive tax practices;

H1: Corruption has a positive effect on aggressive tax avoidance.

## **2) The Effect of Good Governance (Firm Analysis & Country Analysis) on Corruption Relations to Aggressive Tax Avoidance**

Good governance as one of the monitoring mechanisms is expected to be able to have a positive effect on opportunistic behavior. Good governance can be seen from corporate governance and government governance (Judge et al., 2010). Several studies found that good corporate governance has a positive influence on the level of tax compliance companies, so as to minimize tax aggressiveness and increase state tax revenue (Sartori, 2009; Minnick and Noga, 2010). Richardson and Lanis (2011) found a negative relationship between good corporate governance and aggressive tax behavior on companies in Australia. Vafeas (2010) found a negative relationship between the compositions of the board of commissioners (an element of good corporate governance) with tax aggressiveness in companies listed on Fortune 500. Mahenthiran and Kasipilai (2012) found a negative relationship between good corporate governance and tax behavior aggressive on companies listed on the Malaysian stock exchange.

The economic crisis in ASEAN-4 of 1997 also had an impact on improving the quality of good government governance within the government bureaucracy. The establishment of anti-corruption institutions is a form of monitoring corruption, control of corruption is an element of good government governance. The results of Ronald and Ahmed's research (2006) proved the effectiveness of corruption control on the level of tax compliance of its citizens. The results of the study strengthen the argument for the importance of good government governance in reducing the practices of aggressiveness of transfer pricing in the structure of family ownership.

The results of the research by Kanagaretnam et al. (2014) also showed the importance of good government governance in increasing public trust in the government which has an impact on decreasing tax avoidance practices, companies trying to fulfill their tax obligations fairly as a form of appreciation for public trust. Based on the research literature above and also the phenomenon of cases that exist in ASEAN-4, there is a common thread that concludes the relationship between owners, management, and employees within the scope of agency theory making good governance a monitoring and internal control mechanism that is expected to reduce aggressive tax avoidance actions, both good corporate governance and good government governance, so the authors arrange the following hypothesis.

H2a: Good Corporate Governance weakens the positive relationship between corruption and aggressive tax avoidance practices.

H2b: Good Government Governance weakens the positive relationship between corruption and the practice of aggressive tax avoidance

## **3. METHODOLOGY**

The population in this study is manufacturing companies registered in ASEAN countries that have capital markets. The manufacturing industry is transforming through one or more processing materials into products that will be exported across national borders and become the main investment destination of multinational companies (bkpm.go.id). ASEAN countries are also some of the developing countries that have a significant impact due to the practice of aggressiveness tax avoidance, so this research is important to be carried out in ASEAN countries in order to help evaluate its anti-aggressiveness tax avoidance policies.

The sampling technique used in this study is purposive sampling with the following criteria: (1) is a company that is consistently listed on the Exchange in ASEAN countries from 2015-2018, this is intended to maintain consistency of comparability data in formulating the variable aggressiveness tax avoidance (2) companies that successively publish annual reports in English, so that it can make it easier to calculate and compare the good governance variables of companies that successively publish annual reports, (3) companies that have not experienced losses in a row from 2015-2018, and (4) companies that have positive ETR, BTD, and C-ETR values, this is associated with an aggressive tax avoidance measurement model.

The dependent variable is Aggressive Tax Avoidance (ATA) that is measured based on Effective Tax Rate (ETR), Cash-Effective Tax Rate (C-ETR), and Book-Tax Difference (BTD). ETR is the most used tool to measure how much a company can do tax avoidance which is a part of tax management. ETR was calculated by the formula used by Dyreng et al. (2008). This model uses a one-year tax burden as a numerator and one-year pre-tax income as a denominator to estimate the value of ETR.

$$ETR = \frac{\text{Tax Expense } i, t}{\text{Pretax Income } i, t}$$

$$\text{Cash ETR} = \frac{\text{Cash Tax Paid } i, t}{\text{Pretax Income } i, t}$$

$$BTD = \frac{\text{Total Dif Book - Tax } i, t}{\text{Total Aset } i, t}$$

The independent variable is corruption which is measured by the Corruption Perception Index (CPI). CPI score has the opposite meaning with the number of corruption events. A high CPI score in a country shows that the country is perceived as a country that is free of corruption. Conversely,

a low CPI score in a country shows that the country is perceived as a country that has a lot of corrupt practices. The moderating variable is the good governance which is measured by corporate governance and government governance. Corporate governance measurement was operationalized using the ASEAN CG Scorecard. The construct for the calculation of the ASEAN CG Scorecard value was referred to the components in the Annual Report and information from the firms' websites. This study also uses dummy variables. If the statement contained in ASEAN CG Scorecard is listed in the Annual Report or company website, a score of 1 is given. If the statement contained in ASEAN CG Scorecard is not in the Annual Report or the company website the score is 0. Afterwards, each part is summed and multiplied with the weightage assigned for each part; Part B: Equitable treatment of shareholders is given a weightage of 15%; then Part D: Disclosure and transparency are given a weightage of 25%; and Part E: Responsibilities of the board are given a weightage of 40%. The measurement for government governance uses the worldwide governance indicators from the World Bank (2014). The estimated value for the strength of governance is if it is the range of -2.5, then it is considered weak and if 2.5 is declared as strong, therefore, the model in this study is:

$$ATA_{i,t} = \alpha_0 + \beta_1 Corp_{i,t} + \beta_2 GG-GL_{i,t} + \beta_3 GG-FL_{i,t} + \beta_4 SCorp * GG-FL_{i,t} + \beta_5 SIZE_{i,t} + \beta_6 ROA_{i,t} + \beta_7 LEV_{i,t} + \epsilon_{i,t}$$

- ATA: Aggressive Tax Avoidance calculated using Effective Tax Rate (ETR), Cash Effective Tax Rate (CETR), Books Tax Different (BTD)
- Corp: Corruption is a variable level of corruption that is calculated by the CPI score.
- GG\_FL: Good corporate Governance (Firm-Level) is ASEAN Corporate Governance Scorecard Firms n period t
- GG\_CL: Good Government Governance (Country Level) is Worldwide Governance Indicators (WGI) country n period t
- SIZE: The size of the company calculated by total assets
- ROA: Return on Assets is profitability measured by net income compared to total assets
- LEV: The company's leverage ratio is calculated by comparing the long-term debt to total equity.
- $\alpha, \beta, \gamma$  : The estimated coefficients
- $\epsilon_{it}$ : error term
- $i$  : 1, 2,, N
- $t$  : 1, 2,, T

## 4. RESEARCH FINDINGS

### 4.1 Descriptive Analysis

This study uses secondary financial data obtained from data stream databases and annual reports obtained from the Stock Exchange in ASEAN. The population of this study uses manufacturing companies listed on the Stock Exchange of ASEAN countries, namely Singapore, Indonesia, Malaysia, Thailand, Vietnam, and the Philippines. However, since Singapore is categorized as an advanced/developed economy (www.worldbank.org), but, the annual report published by the stock exchange in Vietnam does not use much English, so this study only took a sample of four (4) ASEAN countries or ASEAN-4, namely: Indonesia, Malaysia, Thailand, and the Philippines.

This study used 289 companies from 4 ASEAN countries or 1,156 sample companies, namely Indonesia, Malaysia, Thailand, and the Philippines. Table 2 shows descriptive statistics for the dependent variable namely ATA consisting of ETR, C-ETR, and BTD, for the independent variables consisting of company, and the moderating variables are GGFL and GGCL, and for the control variables consisting of SIZE, ROA, LEV. The dependent variables namely ETR, C-ETR, and BTD have an average value of 0.247, 0.310, and 0.101 consecutively, which means that the average sample in this study falls within the range of tax rates that exist in ASEAN-4 countries, while the standard deviation values of ETR, C-ETR, and BTD are 0.148, 0.188 and 0.214, respectively.

Based on the standard deviation, it shows that the distribution for ETR, C-ETR, and BTD has a small sample distribution because of the small standard deviations. The independent variable has a moderate sample distribution. This is according to the standard deviation in Table 2, which shows the number of company independent variables is 5,830. Likewise, the GGFL moderation variable has a standard deviation of 4016, and for the moderating variable GGCL has a standard deviation that is smaller than the GGFL of 0.332. The standard deviation control variable also vary, the smallest is the LEV of 0.440 and the largest is the SIZE of 3,788.

The results of the regression analysis from model 1 are used to provide evidence of the effect of corrupt practices on aggressive tax avoidance. The hypothesis of this study was first tested with the OLS (Ordinary Least Square) regression model which is a simple linear regression to determine the relationship between two variables, one of which becomes the dependent variable and the other variable becomes the independent variable. In this OLS test, the researchers used the BLUE estimator specifically related to multicollinearity and heteroscedasticity because it used panel data.

The results of testing model 1 shows no multicollinearity as indicated by a VIF (Variance Inflation Factor) value smaller than 5 and a tolerance value (1/ VIF) greater than 0.1. Whereas for heteroscedasticity test aims to test whether there was an inequality of residual variance from one observation to another in the regression model in this study. If the variance of the residual value changes from one observation to the next, it is called heteroscedasticity. Heteroscedasticity can cause OLS estimators to be inefficient because the resulting variants are not minimum. This condition causes the drawing conclusions on the t-test and F test can be misleading, which makes the conclusions drawn are wrong. This study uses the Breuch-Pagan Test method in detecting. Testing of all hypotheses was carried out using three (3) aggressive tax avoidance measurement models, namely Effective Tax Rate (ETR), Cash-Effective Tax Rate (C-ETR), and Book-Tax Difference (BTD). Meanwhile, for testing hypotheses using moderating variables, good governance used two (2) measurement models of good governance at the company level and good governance at the country level.

**Table 2.** Descriptive Statistics

	Obs	Mean	Std.Dev	Min	Max
<b>ATA;</b>					
<b>ETR</b>	1156	0.247	0.148	0.001	0.953
<b>C-ETR</b>	1156	0.310	0.188	0.010	0.957
<b>BTD</b>	1156	0.101	0.214	0	0.547
<b>Corp</b>	1156	40.359	5.830	34	50
<b>GG-FL</b>	1156	0.236	4.984	2.5	37.4
<b>GG-CL</b>	1156	-0.048	0.332	-0.38	0.5
<b>SIZE</b>	1156	1.585	3.788	5.46	30.005
<b>ROA</b>	1156	0.441	0.472	-	1.963
<b>LEV</b>	1156	0.923	0.440	0	0.981

ATA: Aggressiveness Tax Avoidance calculated as ETR (Effective Tax Rate): is an ATA that is calculated by the total tax burden divided by profit before tax, C-ETR (Cash-Effective Tax Rate) is an ATA that is calculated based on the amount cash tax paid is divided by total profit before tax. BTD (Books Tax Different) is an ATA which is calculated based on the amount of difference based on the book minus the profit based on the tax divided by the total assets. GG\_FL: Good Governance (Firm-Level), calculated using the ASEAN CG Scorecard. GG\_CL: Good Governance (Country Level), calculated by the Worldwide Governance Indicators (WGI) index, which has been published on the website of the world bank. SIZE: The size of the company calculated by total assets. ROA: Return on Assets is profitability measured by net income compared to total assets. LEV: The company's leverage ratio is calculated by comparing the long-term debt to total equity

Hypothesis testing is done with three (3) testing models and three (3) dependent variable measurement models, the results of testing model 1 of the study shows that the highest r square (R2) value is 24.0% for using the ATA variable measurement model with C-ETR and the lowest is 23.2% by measurement of ATA variability with ETR. This illustrates that the independent variables in Model 1 were able to explain the C-ETR variable by 24.0% and only 23.2% were able to explain the ETR variable.

The first hypothesis statement (H1) in this study is that there is a positive influence of corrupt practices on aggressive tax avoidance. There are three (3) measurements of aggressive tax avoidance in this study, namely Effective Tax Rate (ETR), Cash-Effective Tax Rate (C-ETR), and Book-Tax Difference (BTD). Regression test results listed in Table 4 show that aggressive tax avoidance using ETR and BTD measurements has a significant positive effect (10%) on aggressive tax avoidance (ATA) practices, which means that the higher the practice of corruption in a country, the greater a company that is in a country to conduct aggressive practices tax avoidance.

Likewise, company has a significant positive effect on (1%) ATA by using C-ETR measurement, which means that the higher the practice of corruption in a country, the greater a company that is in a country to practice aggressive tax avoidance. This is consistent with the H1 hypothesis. Thus, overall, it can be concluded that there is a positive influence on the level of corrupt practices on aggressive tax avoidance practices. The results of this study are consistent with the results of the study by Ronald and Ahmed (2006) and Alm J, *et al.* (2016) who

stated that corruption is a stimulant for increasing high tax avoidance.

This study also supports the results of David (2009) who found that non-compliance of taxpayers increased with increasing cases of bribery against officers. This condition is in accordance with the fact that the results of the Enterprise Surveys (ES) conducted by the World Bank in 2015 found that Indonesia with bribery cases with the largest tax officer, 31% of the company, has

been asked to pay a bribe by the tax official, followed by Malaysia by 28%, the Philippines by 17% and Thailand by 10%. Bribery is a form of corruption; bribery is a trend of entrepreneurs in Indonesia in conducting their business. This is reflected in research conducted by Transparency International (TI) which places Indonesia in 25<sup>th</sup> position out of 28 countries (Bribe Payers Index 2011). The 2013 Global Corruption Barometer report also placed Indonesia in the highest position for ASEAN-4 countries with the percentage of 36% of citizens who committed bribery in the country, then

Malaysia at 3%, Thailand 18% and the Philippines at 12%.

Sacit (2006) also found that the amount of bribes is negatively related to tax avoidance. This shows that when bribes are large enough, taxpayers prefer to pay their taxes voluntarily. Likewise, the results of the research of Alm *et al.* (2016) who found that corruption was a factor driving higher tax avoidance practices. In addition, greater bribery resulted in higher tax avoidance rates.

**Table 3.** Regression results for the three aggressiveness tax avoidance measures (Model 1)

**Model 1:**

$ATA_{i,t}$		$\alpha_0 + \beta_1 Corp_{i,t} + \beta_2 GG-FL_{i,t} + \beta_3 GG-CL_{i,t} + \beta_4 SIZE_{i,t} + \beta_5 ROA_{i,t} + \beta_6 LEV_{i,t} + \epsilon_{i,t}$		
	<b>ATA</b>			
<b>Dep-Var</b>	<b>Ekspektasi Tanda</b>	<b>ETR</b>	<b>C-ETR</b>	<b>BTD</b>
<b>Corp</b>	+	0.003* (0.057)	0.000*** (0.000)	0.002* (0.000)
<b>GG-FL</b>	-	-0.002** (0.051)	-0.002*** (0.000)	-0.005*** (0.003)
<b>GG-CL</b>	-	-0.032** (0.000)	-0.022*** (0.001)	-0.077*** (0.000)
<b>SIZE</b>	+	0.008** (0.019)	0.002*** (0.000)	0.001 (0.546)
<b>ROA</b>	+	0.004*** (0.000)	0.001*** (0.000)	0.002*** (0.000)
<b>LEV</b>	+	0.001 (0.663)	0.001** (0.034)	0.002** (0.014)
<b>N</b>		1156	1156	1156
<b>R<sup>2</sup></b>		0.232	0.240	0.237
<b>Adj-R<sup>2</sup></b>		0.221	0.233	0.230

\*, \*\*, \*\*\* = significant at the 10%, 5%, 1% levels; ATA: Aggressiveness Tax Avoidance calculated as ETR (effective tax rate): is an ATA that is calculated by the total tax burden divided by profit before tax, C-ETR (cash effective tax rate) is an ATA that is calculated based on the amount cash tax paid is divided by total profit before tax. BTD (Books Tax Different) is an ATA which is calculated based on the amount of difference based on the book minus the profit based on the tax divided by the total assets. GG\_FL: Good Governance (Firm-Level), calculated using the ASEAN CG Scorecard. GG\_CL: Good Governance (Country Level), calculated by the Worldwide Governance Indicators (WGI) index, which has been published on the website of the world bank. SIZE: The size of the company calculated by total assets. ROA: Return on Assets is profitability measured by net income compared to total assets. LEV: The company's leverage ratio is calculated by comparing the long-term debt to total equity

The first moderation effect test uses good governance at the company level (GGFL) as listed in Table. 3, good governance at the company level (GGFL) adopts the ASEAN CG Scorecard. The results of the moderation variable testing as presented in Table 5 shows that with the ETR, C-ETR, and BTD variables as ATA measurements and the GGFL moderation variable indicate the value of R square (R2) regression before using the moderating variable shows an increase in the value of R square (R2). This section is an indicator to report the goodness of fit of the model, i.e. what "percent" variation in the dependent variable can be explained by the model, i.e. R2 and adjusted

r square (R2). This adjusted r square (R2) corrects the positive bias in R2 due to the addition of the independent variable.

In the second group in this study examines the effect of moderating variables in the form of good corporate governance (GGFL) on the relationship between corruption and tax avoidance. Good corporate governance is one of the mechanisms for controlling corruption and tax avoidance, and good corporate governance practices are expected to weaken the positive relationship between corruption and tax avoidance as stated in hypothesis H (2a) of this study. The results of this study, as contained in Table 5, shows the



alignments of good corporate governance in the company's analysis unit in weakening the positive relationship between corruption and tax avoidance practices.

R square value (R<sup>2</sup>) in model 2 which is the result of regression using moderation variables results in a higher value than the regression results before using moderation variables. Then, these results can be concluded that good governance at the company level (GGFL) weakens the relationship between corruption and ATA. Based on Table 3, it can be concluded that the H2a hypothesis can be accepted by measuring the ATA variable using ETR, C-ETR, and BTD, so that good governance at the company level weakens the positive relationship of corruption and aggressive tax avoidance practices. This shows the important role of good governance as one of the control mechanisms for aggressive tax avoidance practices in manufacturing companies in ASEAN-4.

The hypothesis research findings (H2a) are in line with the role of good corporate governance to minimize conflicts of interest and asymmetry information, both opportunistic behavior, moral hazard and adverse selection between principals and principal-agents (Marie et al., 2010). The role of good corporate governance threats to the practice of tax avoidance can be minimized as a result of this study. The results of this study support the research (Burkart et al., 2003; Steijvers and Niskanen, 2014; Raoul et al., 2015) which states that good corporate governance as a protective mechanism for all stakeholders' interests from opportunistic attitudes.

Implementation of good corporate governance provides a more effective monitoring effect on each tax policy that will be carried out by management. This monitoring effectiveness is carried out by independent commissioners and professional management from outside who are able to bridge the interests of minority stakeholders. So that tax avoidance policies that will negatively impact the loss of the company or stakeholders can be minimized by implementing good corporate governance (Steijvers and Niskanen, 2014; Raoul et al., 2015).

The implementation of good corporate governance in ASEAN countries in a study conducted by ADB in 2015 found that companies in ASEAN experienced many changes in the implementation of good corporate governance including; (1) increasing the level of transparency, especially disclosure of non-financial and price information-sensitive or insider information, which is often not disclosed, (2) improve the function of the board of commissioners, such as increasing the level of independence, (3) strengthening risk management, internal control, and audit functions, (4) better management of conflicts of interest and related-party transactions through a fair and transparent process, (5) enhancing shareholder rights and practices, including more formal shareholder meeting arrangements and stronger protection for minority shareholders ([www.ifc.org](http://www.ifc.org)).

Therefore, the weakening of the positive relationship between corruption and tax avoidance is the impact of the implementation of good corporate governance that is increasingly transparent, and the company has submitted

financial reports accompanied by reports on related-party transactions and other transactions.

The results of previous studies showed how good corporate governance is able to reduce asymmetry information (Marie et al., 2010). This has an impact on monitoring mechanisms or contracts between the principal agents, and principals can be controlled in accordance with the existing rules of good corporate governance, as the results of research from Forte and Antonio (2007) and Byung and Robert (2015). Good governance as a bulwark in reducing the practice of aggressive tax avoidance is proven in this study, this proves the benefits of implementing good corporate governance at the company level capable of being a media of protection from opportunistic attitudes both by principals and agents seeking benefits for themselves and their groups. The existence of good corporate governance in a company has an impact on increasing foreign investment, this is more the protection of investor protection (Byung and Robert, 2015).

In the third model (3), this study examines the effect of moderating variables in the form of good government governance (GGCL) on the relationship between corruption and tax avoidance (H2b). Government governance is defined as securing a reciprocal relationship between management, control, and supervision by the government and by organizations formed by government authorities, which aim to carry out policies efficiently and effectively, as well as disclosure of information and provide accountability for the welfare of all stakeholders (The Netherlands Ministry of Finance Government Audit Policy Directorate, 2000). This study uses six (6) indicators in measuring the governance of a country.

Government governance is one of the mechanisms of control and monitoring of behavior that can harm stakeholders, the practice of good governance in a country is expected to weaken the positive relationship between corruption and aggressive tax avoidance as stated in hypothesis H (2b). The results of this study, as displayed in Table 5 shows the alignment of good government governance in the state analysis unit (government governance) able to weaken the positive relationship between corruption with aggressive tax avoidance.

The findings of this hypothesis (H2b) are in line with the role of good governance in governments which have the tasks of; (1) securing and defending the integrity of the country, (2) providing public order and domestic security, (3) promoting political, social, and policy economics for the benefit of public goods, (4) applying those policies fairly and uniformly to national borders and including all elements of the population, and (5) mobilizing and mobilizing the resources needed to carry out governmental tasks (Jamil et al., 2015). The role of good governance at the country level threat to the

practice of aggressive tax avoidance can be minimized as stated in the results of this study.

**Table 4.** Regression result with moderation of Good Corporate Governance (GG-FL)

**Model 2: Good Corporate Governance as Moderating**

$$ATA_{i,t} = \beta_0 + \beta_1 Corp_{i,t} + \beta_2 GG-FL_{i,t} + \beta_3 GG-CL_{i,t} + \beta_4 Corp_{i,t} * GG-FL_{i,t} + \beta_5 SIZE_{i,t} + \beta_6 ROA_{i,t} + \beta_7 LEV_{i,t} + \varepsilon_{i,t}$$

Dep-Var	ATA			
	Ekspektasi Tanda	ETR	C-ETR	BTD
Corp	+	-0.000* (0.033)	-0.001** (0.008)	-0.010* (0.060)
GG-FL	-	-0.004*** (0.001)	-0.002** (0.003)	-0.007** (0.051)
GG-CL	-	-0.037 (0.404)	-0.025** (0.007)	-0.060*** (0.000)
Corp*GGFL	-	-0.000** (0.006)	-0.000* (0.060)	-0.000** (0.051)
SIZE	+	0.008** (0.002)	0.002*** (0.000)	0.001 (0.573)
ROA	+	0.004*** (0.001)	0.001*** (0.000)	0.002*** (0.000)
LEV	+	0.408 (0.514)	0.000** (0.004)	0.002** (0.033)
N		1156	1156	1156
R <sup>2</sup>		0.261	0.249	0.241
Adj-R <sup>2</sup>		0.256	0.233	0.232

\*, \*\*, \*\*\* = significant at the 10%, 5%, 1% levels; ATA: Aggressiveness Tax Avoidance calculated as: ETR (Effective Tax Rate): is an ATA that is calculated by the total tax burden divided by profit before tax, C-ETR (cash-Effective Tax Rate) is an ATA that is calculated based on the amount cash tax paid is divided by total profit before tax. BTD (Books Tax Different) is an ATA which is calculated based on the amount of difference based on the book minus the profit based on the tax divided by the total assets. GG\_FL: Good Governance (Firm-Level), calculated using the ASEAN CG Scorecard. GG\_CL: Good Governance (Country Level), calculated by the Worldwide Governance Indicators (WGI) index, which has been published on the website of the world bank. SIZE: The size of the company calculated by total assets. ROA: Return on Assets is profitability measured by net income compared to total assets. LEV: The company's leverage ratio is calculated by comparing the long-term debt to total equity.

Good governance in the government will be able to reduce opportunistic behavior both by government officials and from the private sector, such as bribery that is a part of the measurement of good governance indicators, namely Control of Corruption (Kaufmann *et al.* 1999). The results of this study are in line with the results of research conducted by Sacit (2006) who also found that the amount of bribery is negatively related to tax avoidance. It means that when a country has a low bribe level, then the tendency of a company will avoid the practice of aggressive tax avoidance. Likewise, the results of the research of Alm *et al.* (2016) who found that corruption is a factor driving higher tax avoidance practices, so, it is expected that the results of this study indicate that the application of good governance at the state level will be able to reduce the level of corruption

which has an impact on decreasing aggressive tax avoidance practices.

The impact of the implementation of good governance at the country level will also make the company owners

tend to avoid damaging the reputation and also the additional costs of the tax auditor's examination results in countries that have effective control of corruption as stated by Ronald and Ahmed (2006) and Kanagaretnam *et al.* (2014). The results of this study indicate that increasing the tax compliance of its citizens when the level of control of corruption is high will have an impact on the decline in the practice of aggressiveness of transfer pricing, so that the weakening of the positive relationship between corruption and aggressive tax avoidance is the impact of the implementation of good governance at the country level which is getting better,

either on the effectiveness of policies, quality of regulations, legislation, and corruption control.

The existence of better government governance in a country also has an impact on increasing better protection of investment from investors. Even the World Bank recommends the application of good governance because it has a positive effect on investor protection (Byung and Robert, 2015). This study is in line with the results of the research by Marie *et al.* (2010) and Byung and Robert (2015) that if a country is strong in its good governance (effective laws and

regulations), it will be able to protect the interests of investors, especially minority shareholders. The role of good governance at the country level threatens the existence of practices of aggressiveness of transfer pricing that can harm the interests of minority shareholders both because fines and damage to reputation can be minimized as the results of this study.

Based on agency theory, as in the hypothesis (H2b), it is found that the weakening of the positive relationship between corruption and aggressive tax avoidance is the impact of implementing effective good governance implemented by the state. The existence of good regulatory quality and the rule of law will be able to support the transparency of its taxation practices. The results of previous studies that showed how good governance is able to reduce asymmetry information (Marie *et al.*, 2010). This has an impact on monitoring mechanisms or contracts between the principal and the principals can be controlled in accordance with the rules that exist in good governance according to the research results from Forte and Antonio (2007) and Byung and Robert (2015). Good governance will strengthen a more effective monitoring model in ensuring the investment and interests of minority stakeholders from taxation practices that can harm stakeholders' minority, such as the practice of aggressiveness of transfer pricing.

**Table 5.** Regression Result with Moderation of Good Government Governance (GG-CL)

**Model 3: Good Government Governance as Moderating**

$$ATA_{i,t} = \gamma_0 + \gamma_1 Corp_{i,t} + \gamma_2 GG\_FL_{i,t} + \gamma_3 GG\_CL_{i,t} + \gamma_4 Corp_{i,t} * GG\_CL_{i,t} + \gamma_5 SIZE_{i,t} + \gamma_6 ROA_{i,t} + \gamma_7 LEV_{i,t} + \epsilon_{i,t}$$

Dep-Var	ATA			
	Ekspektasi Tanda	ETR	C-ETR	BTD
Corp	—+	-0.003** (0.016)	-0.001** (0.021)	-0.003*** (0.001)
GG-FL	—	-0.002*** (0.008)	-0.008*** (0.000)	-0.000*** (0.000)
GG-CL	—	-0.396 (0.593)	0.651 (0.245)	-0.053** (0.022)
Corp*GGCL	—	-0.008** (0.006)	-0.011*** (0.002)	-0.002** (0.016)
SIZE	—+	-0.008*** (0.000)	-0.002*** (0.000)	0.001 (0.476)
ROA	+	-0.001*** (0.004)	-0.001*** (0.000)	-0.002*** (0.000)
LEV	+	0.008 (0.531)	0.000* (0.074)	-0.002*** (0.001)
N		1156	1156	1156
R <sup>2</sup>		0.261	0.210	0.245
Adj-R <sup>2</sup>		0.256	0.241	0.216

\*, \*\*, \*\*\* = significant at the 10%, 5%, 1% levels; ATA: Aggressiveness Tax Avoidance calculated as ETR (effective tax rate): is an ATA that is calculated by the total tax burden divided by profit before tax, C-ETR (cash effective tax rate) is an ATA that is calculated based on the amount cash tax paid is divided by total profit before tax. BTD (Books Tax Different) is an ATA which is calculated based on the amount of difference based on the book minus the profit based on the tax divided by the total assets. GG\_FL: Good Governance (Firm Level), calculated using the ASEAN CG Scorecard. GG\_CL: Good Governance (Country Level), calculated by the Worldwide Governance Indicators (WGI) index, which has been published on the website of the world bank. SIZE: The size of the company calculated by total assets. ROA: Return on Assets is profitability measured by net income compared to total assets. LEV: The company's leverage ratio is calculated by comparing the long-term debt to total equity

## 5. CONCLUSION

This study aims to examine the effect of corruption with aggressive tax avoidance. This study also provides empirical evidence of the effect of good governance both at the corporate level and government (government governance) on the relationship of corruption with aggressive tax avoidance in ASEAN-4 countries, which are Indonesia, Malaysia, Thailand, and the Philippines. The test results show that corruption is positively related to aggressive tax avoidance in ASEAN-4 countries. The results of this study are consistent with the results of the study (Ronald and Ahmed, 2006; Alm J. *et al.*, 2016) which stated that corruption is a stimulant for increasing high tax avoidance. This study also supports the results of David (2009), who found that non-compliance of taxpayers increased with increasing cases of bribery against officers. In testing good corporate governance, this study provided evidence that good corporate governance is able to weaken the positive relationship between corruption and aggressive tax avoidance in ASEAN-4 countries. Furthermore, good corporate governance is also able to reduce the practice of aggressive tax avoidance. This research shows that good governance provides a more effective monitoring effect, and makes the media a stimulant for transparency and accountability in the selection of aggressive taxation strategies. This study supports the results of previous studies (Forte and Antonio, 2007; Han, 2008; Mark *et al.*, 2010; Agnes and Wong, 2011; Zhang, 2012; Robinson *et al.*, 2012; Steijvers and Niskanen, 2014; Moataz, 2014 ; Raoul *et al.*, 2015; Byung and Robert, 2015).

The testing of good government governance has proven to be able to weaken the positive relationship between corruption and aggressive tax avoidance in ASEAN-4 countries. The results of this study indicate that effective monitoring is carried out by the state and all components in protecting the interests of minorities (Burkart *et al.*, 2003; Raoul *et al.*, 2015). Effective control of corruption is one of the measures in good government governance has an impact on aggressive taxation activity reduction as a result of research (Ronald and Ahmed, 2006; Alm J. *et al.*, 2015).

The study provides comprehensive empirical evidence about aggressive tax avoidance with 3 (three) measurements, namely ETR, C-ETR, and BTD. The majority of previous studies conducted aggressive tax avoidance testing with just one or two measurements. This research provides evidence that the impact of good governance at both the company and country-level in reducing the behavior of aggressive tax avoidance practices committed by corporations in ASEAN-4 countries. Many previous studies have done it partially and some are only focused on corporate governance (Moataz, 2014; Klassen *et al.*, 2016), those that only

focus on government governance (Bonu, 2011). The moderation test with two (2) levels of good governance shows that there are differences in the reduction in weakening the relationship of corruption with aggressive tax avoidance. In corporate governance, all ATA measurements are proven to be able to reduce the practice of aggressive tax avoidance, while government governance.

In Indonesia and in most ASEAN-4 countries, based on the results of Irish research (1986) stated that transfer pricing transactions in developing countries dominate more than 60% of their trade balance and developing countries only receive tax revenue less than 5% of these transfer pricing transactions. Therefore, the results of this study are expected to be a reference for regulators in increasing their role in several respects. First, encouraging the issuance of policies on anti-abuse of aggressive tax avoidance. This is done in order to strengthen policies that can reduce acts of abuse of aggressive tax avoidance practices. The second is to encourage regulators to strengthen the implementation of good governance in various sectors for companies, especially for law enforcement. The results of this study reinforce previous research (Burkart *et al.*, 2003; Raoul *et al.*, 2015) which stated that good governance as a medium in reducing aggressive tax behavior. The results of this study indicate that corruption affects aggressive tax avoidance, so that regulators need to be more intensive in examining companies that have a lot to do with the government or BUMN. The BEPS action plan has prepared effective regulations in capturing aggressive tax avoidance transactions, for this reason, there needs to be cooperation between ASEAN-4 countries in implementing the BEPS action plan. The existence of CbCR is an entry point for tax authorities in ASEAN-4 countries in monitoring the existence of aggressive tax avoidance behavior. Besides the exchange of information between tax authorities, it needs to be increased to tighten aggressive tax avoidance practices by companies in ASEAN-4 countries.

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