Executive Character and Tax Avoidance Decisions: The Intervening Effect of CEO Overconfidence

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***Abstract*— This research aims to analyze the indirect relationship between executive character and tax avoidance decisions through CEO's Overconfidence. Executives with a risk-taker character are considered to tend to be bolder in making decisions regarding tax avoidance to maximize company profits. This research tries to test this by using a population of state-owned companies listed on the Indonesia Stock Exchange for the 2017-2021 period, totaling 38 companies with 10 companies used as research samples using a purposive sampling method. The collected data was processed using path analysis with the e-views 9 statistical tools and a Sobel calculator to carry out a Sobel test. The research results show that executive character influences tax avoidance decisions, CEO's overconfidence has no influence on tax avoidance decisions and is unable to mediate the direct relationship between executive character and tax avoidance decisions.**

***Keywords*— CEO's Overconfidence; Executive Character; Tax Avoidance**

I. INTRODUCTION

Problems in the field of taxation continue to arise in the government's efforts to fund state expenditures with funds originating from taxes. This is strongly suspected to be due to differences in interests between the tax authorities and taxpayers who must pay taxes. The Indonesian government will always make efforts to maximize revenue in the taxation sector, which is one of the largest revenues in the APBN. Based on data released by the Ministry of Finance in 2022, the total revenue in the 2021 APBN was IDR 1,743.6 trillion, of which IDR 1,229.6 trillion came from the taxation sector. So, it can be concluded that state expenditures relies heavily on the taxation sector. However, taxpayers always consider that paying taxes is a burden for companies, so companies tend to minimize their tax payments to maximize profits. Efforts to streamline the tax burden are what cause state revenues from the tax sector to be maximized again. These efficiency measures are carried out through tax avoidance mechanisms. Generally, tax avoidance is carried out by exploiting loopholes contained in tax laws and regulations [1]. According to (Bivianti, 2022) tax avoidance is one of the strategies carried out by companies in their tax policy to legally reduce tax payments based on applicable tax regulations..

Tax avoidance practices are often related to efforts to maximize profits carried out by top management or CEOs. According to [3] upper echelon theory states that top-level managers (CEOs) can directly influence company choices and performance. The decisions taken by top management will influence the characteristics of each management, where there are risk-taker management types and there are also risk avoiders. CEOs who have the characteristics of being risk-takers have the potential to be more active and brave in making tax avoidance decisions [4]. Apart from that, a CEO with a risk-taker character will have high self-confidence in making management decisions. Top management who have a risk-taking character will immediately have the courage to make decisions, especially regarding tax avoidance decisions. Decisions taken in the hope of maximizing company profits will increase management's overconfidence. This research is a development of previous research regarding Tax Avoidance, namely research conducted by [2] with the title The Effect Of Executive Characteristics, CEO Overconfidence, Capital Intensity On Tax Avoidance with results showing that executive characteristics have a positive effect on tax avoidance, while CEO overconfidence has a negative effect on tax avoidance. Researchers try to use CEO's Overconfidence as an intervening variable to determine the indirect influence of executive characteristics on tax avoidance. This research aims to provide input to policy makers regarding maximizing state revenue from the tax sector which is influenced by internal company factors, especially those originating from individual management factors.

The theory used as the basis for this research is Agency Theory which is considered relevant to Tax Avoidance Decisions, where agency theory is a theory which states that there is a relationship between the party giving authority and the party receiving authority which causes agency conflict [5]. As is known, taxpayers are given the authority to calculate, calculate and report their own taxes owed, but this authority is often misused to maximize profit value and this is detrimental to the state as a tax collector because it reduces state income from the tax sector.

II. METHODS

This research is a type of quantitative research that uses secondary data, where data is obtained from the annual reports of State-Owned Enterprises (BUMN) listed on the Indonesia Stock Exchange in the 2017-2021 period, totaling 38 companies with 10 companies as research samples selected using the purposive method. sampling. The research period was 5 years, bringing the number of observations in this study to 50 companies. The data collected was analyzed using a statistical data processing tool, namely e-views 9, using path analysis, where path analysis is an extension of multiple linear regression analysis which is used to test indirect effects between variables. In path analysis, there is

I. Abrori et al. (eds.), *Proceedings of the Conference on SDGs Transformation through the Creative Economy: Encouraging Innovation and Sustainability (TCEEIS 2023)*, Advances in Economics, Business and Management Research 271,
https://doi.org/10.2991/978-94-6463-346-7_42

one variable that plays a dual role, namely as an independent variable in one relationship, but becomes a dependent variable in another relationship considering the existence of a multi-level causal relationship. This is illustrated in the following section:

Sub Structural I

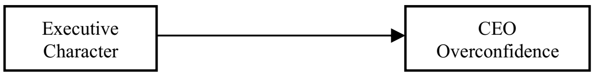

Fig 1. Sub-Structural Research Model I

Sub Structural II

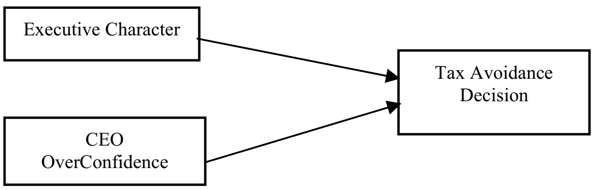

Fig 2. Sub-Structural Research Model II

Below are presented the measurements of the variables used in this research:

A. Dependent Variable

Tax Avoidance Decision (Y)

[6] states that Tax Avoidance is a taxpayer's efforts to avoid tax burdens legally and safely without violating tax laws. Tax avoidance is proxied using the Effective Tax Rate (ETR) which can provide an overview of tax aggressiveness in a company:

$$\mathrm{ETR} = \frac{\text{Total Tax Expense}}{\text{Pre Tax Income}}$$

B. Independent Variable

Executive Character (X_1)

According To [7], Executives are company leaders who have the most influence in decision-making in a company. In carrying out their duties, executives have the character of a risk-taker or risk averse. [8] measuring executive character using corporate risk as follows :

$$\mathrm{Risk} = \frac{\text{EBIT}}{\text{Total Aset}}$$

C. Intervening Variables

CEO's OverConfidence (Z)

A CEO's self-confidence determines policy and strategic decision-making in a company. The measurement of CEO's Overconfidence in this study uses a sales growth model which has a role in measuring the CEO's level of success in increasing company profits. [9].

$$\mathrm{OVMA} = \frac{\text{Total Current Sales} - \text{Total Sales Last Period}}{\text{Total Sales Last Period}}$$

III. RESULT AND DISCUSSION

This research data was processed using panel data regression analysis and a Sobel test which was used to determine the indirect influence of executive character on tax avoidance through CEO's Overconfidence. The following are presented the results of the data processing using e-views Version 9:

Table 1. t-statistic numbers sub-structural I

Variable	Coeff.	Std.Error	t-Statistic	Prob.
C	0.0797	0.0405	1.9639	0.0567
X_1 (Character Executive)	3.7896	0.3849	9.8445	0.0000

Table 2. t-statistic numbers sub-structural II

Variable	Coeff.	Std.Error	t-Statistic	Prob.
C	0.3663	0.0412	8.8723	0.0000
X_1 (Character Executive)	1.0146	0.4744	-2.1387	0.0389
Z (CEO Overconfidence)	0.0172	0.0146	-1.1730	0.2481

Table 3. Sobel Test

Sobel Test Statistic	**1.1654**
One-Tailed Probability	0.1219
Two-Tailed Probability	0.2438

The regression analysis result show that probability value for Character Executive is 0.0000 < 0.05. This means that the character executive has a positive impact to CEO Overconfidence. This shows that executives who have a risk taker character will have higher self-confidence compared to CEOs who have a risk averse character. This influences the decisions that will be taken by the executive (Table 1).

The regression analysis for sub structural II show that probability value for Character Executive is 0.0389 < 0.05. This probability value indicated that character executive has a positive impact to tax avoidance decisions. Executives are company leaders who have important and influential positions in the decision-making process in a company [7]. When carrying out their functions in a company, the CEO has at least two characteristic, namely risk-taker or risk averse. Executives with a risk-averse character tend not to have the courage to make decisions so they will choose the lowest risk when faced with a choice. Meanwhile, executives who are risk-takers are braver in making decisions even though the decisions to be taken have quite high risks. This is also related to the decision to avoid taxes that will be made by executives to maximize profits. Companies that have many executives with risk-taker characteristics will be bolder in making decisions related to efforts to maximize profits through tax avoidance practices. This is in line with the Upper Echelon Theory put forward by [3] which states that top level managers can directly influence choices on company performance. The results of this research are in line with research conducted by [2], [10] and [11] which states that executives who have a risk-taker character will have the courage to commit tax avoidance. However, this is contrary to research conducted by [12] dan [13] which states that the executive's character does not influence on tax planning decisions, where tax planning decisions are sometimes directly related to threats of punishment and sanctions so executives do not have enough courage to commit tax avoidance (Table 2).

CEO Overconfidence show that probability value is 0.2481 > 0.05. This probability value indicated that CEO Overconfidence has no impact on tax avoidance. This shows that confidence in the CEO within a company tends to be in a positive direction, such as increasing profits in a way that does not violate the rules to increasing the number of sales by maximizing promotions. This is in contrast to agency theory which states that there are differences in interests between the CEO or company owner and the tax authorities as tax collectors, where the company owner and his staff will make every effort to avoid tax. A CEO with a high level of self-confidence will tend to make choices that will benefit him and not damage his credibility. The results of this study are in contrast to research conducted by [2], [14], dan [15] which states that a CEO who is too self-confident will make every effort to lighten the company's tax burden so that there will be a lot of operational funds available that can be used by the company to finance the company's operational activities (Table 2).

This research uses the Sobel test to test the strength of the indirect influence of the independent variable on the dependent variable through intervening variables. The Sobel test in this study was carried out using a Sobel calculator via the Sobel Test Calculation for Significance of Mediation application with the following results that the one-tailed probability value shows several of 0.1219 or greater than the significance level of 0.05, this shows that CEO's overconfidence is unable to mediate the influence of executive characteristics on tax avoidance or in other words it can be said that executive character has a significant influence on tax avoidance. directly to tax avoidance. CEO's Overconfidence in this study is measured by looking at the level of sales generated by management levels and above. Sales levels that tend to be stable or increasing will make management's self-confidence increase, but this self-confidence is supported by sufficient resources to make tax payments so that management's self-confidence it used to find ways to increase sales in each period. So it can be concluded that the higher the level of sales achieved by managers will make the company complete its tax payments, so that executives will not avoid taxes with high levels of sales and choose to allocate company resources to investments and expansion that are more profitable than tax avoidance risky. This is in contrast to research conducted by [16] which states that CEO's Confidance can moderate the influence of corporate governance on tax avoidance.

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