

# Political Connections, Executive Character And Tax Avoidance: Does Audit Quality Moderate The Relationship

*by Kentris Indarti*

---

**Submission date:** 02-Sep-2023 04:17PM (UTC+0700)

**Submission ID:** 2156256856

**File name:** Kentris\_Draft\_Jurnal\_25\_Agust\_23\_Eng.docx (108.42K)

**Word count:** 6563

**Character count:** 38746

# POLITICAL CONNECTIONS, EXECUTIVE CHARACTER AND TAX AVOIDANCE: DOES AUDIT QUALITY MODERATE THE RELATIONSHIP?

Maria Goreti Kentris Indarti<sup>1\*</sup>, Jacobus Widiatmoko<sup>2</sup>  
Faculty of Economics and Business, Universitas Stikubank, Semarang, Indonesia

\*Correspondence: E-mail: [kentris@edu.unisbank.ac.id](mailto:kentris@edu.unisbank.ac.id)

## Abstract

**Main Purpose-** This study aims to investigate the effect of political connections and executive character on tax evasion, as well as examine the role of audit quality variables in this relationship.

**Method-** Manufacturing firms registered on the Indonesia Stock Exchange in 2019–2021 serve as the population for this study. Purposive sampling was employed to choose the sample, and 343 data were collected. Moderated regression analysis (MRA) was the method for data analysis.

**Main Findings-** The findings of this study suggest that political connections and executive character have a positive effect on tax avoidance. Another important finding is that audit quality, as an external governance mechanism, can reduce the impact of political connections and executive character on tax evasion. On the other hand, tax avoidance is not directly impacted by audit quality.

**Theory and Practical Implications-** The findings of this study provide implications both theoretically and practically. This study supports **agency theory which emphasizes the importance of governance mechanisms in minimizing agency conflicts**. In particular, the presence of quality auditors as an external governance mechanism is able to reduce management's tendency to commit tax evasion. For the Directorate General of Taxes, the findings of this study provide important input in determining tax policy to be more effective by conducting tighter oversight of companies that are politically connected and have executives with a risk-taking character.

**Novelty-** This research offers audit quality as an external governance mechanism as a solution to mitigate tax avoidance motivated by political connections and risk-taking executive character.

### Keywords:

audit quality, executive character, political connections, tax avoidance

## 1. INTRODUCTION

Taxes are the primary source of state income, which is then used to fund public services like those in the infrastructure, health, and education sectors (Alfiyah, Subroto, & Ghofar, 2022; Kalbuana, Taqi, Uzliawati, & Ramdhani, 2023; I. S. Prastiwi & Siregar, 2019). Although citizens generally comply with tax laws, this dependency on tax revenue has not been adequately supported. Companies often try to reduce their tax obligations because they see them as a burden (Ma & Thomas, 2020).

Tax avoidance is a widespread occurrence that is a topic of intense debate

(Badertscher, Katz, Rego, & Wilson, 2019; Oats & Tuck, 2019). Since then, scholarly research has focused on tax avoidance (Huseynov, Sardarli, & Zhang, 2017; Mahaputra, Rustiarini, Anggraini, & Sudiartana, 2018), which has gained public and mass media interest (Kanagaretnam, Lee, Lim, & Lobo, 2016). Due to tax avoidance, Indonesia's tax ratio is only 11.6%, which is significantly lower than the 21% average for other Asia Pacific nations (OECD, 2021). According to data, Indonesia's realized tax revenue fell by 19.7% in 2020 compared to 2019. Up until the end of December 2020, tax revenue from the manufacturing industrial sector likewise fell by 20.21% (CNN, 2021).

The agency theory can be used to explain the practice of tax avoidance. Information asymmetry and conflicts of interest arise from the separation of ownership and control between managers and business owners, particularly when each side desires to maintain its current level of prosperity (Ge & Zhang, 2017). The potential for management to avoid taxes rises as a result of information asymmetry (Hong, Kalcheva, & Srivastava, 2017; Rustiarini & Sudiartana, 2021).

Many academics have connected tax avoidance with the political affiliations of company CEOs since tax avoidance is a politically contentious topic (Barford & Holt, 2013). According to several studies (Rustiarini & Sudiartana, 2021; Shen, Gao, Bu, Yan, & Chen, 2019; Wang & You, 2022; Yudanto & Damayanti, 2022) political connections have a favorable impact on tax avoidance. However, some studies have found no influence of political connections on tax avoidance (Alfiyah et al., 2022; Oktavia, 2020), while others have indicated that political connections minimize tax avoidance (Ajili & Khlif, 2020; Ding, Sainani, & Zhang, 2021; Tsai, Liu, & Liu, 2021; Widarjo, Sudaryono, Sutopo, Syafiqurrahman, & Juliati, 2021).

Whether an executive chooses to avoid taxes also depends on their risk-taking or risk-averse tendencies. The level of tax avoidance is correlated with the executive's risk-taking daring (Mohammed & Sanusi, 2020). According to earlier studies, CEO risk-taking boldness reduces tax avoidance (Alfiyah et al., 2022; Baghdadi, Podolski, & Veeraraghavan, 2022; Dewi & Yasa, 2020; I. S. Prastiwi & Siregar, 2019). Novita (2016) and Fitria (2018), in contrast, did not discover a connection between the two variables.

The findings of research investigating the impact of executive character and political connections on tax avoidance behavior as indicated above show mixed results. According to Baron and Kenny's (1986) research, conflicting research findings offer a chance for researchers to include a moderating variable, namely audit quality, in the relationship between these variables. A quality audit is thought to play a significant part in lowering agency conflicts, according to agency theory. Quality auditors can act as a powerful monitoring mechanism, limiting management's opportunistic conduct, such as tax avoidance (Indarti & Widiatmoko, 2021). This is so that accurate financial reporting, which is guaranteed by a high-quality audit, would allow shareholders to efficiently monitor management operations. Additionally, the existence of a top-notch auditor will lessen the information risk that investors experience because the reliability of financial reports will be increased (Phan, Lai, Le, Tran, & Tran, 2020; Salehi, Tarighi, & Shahri, 2020).

In light of the context mentioned previously, the aim of this study is to obtain empirical evidence regarding the impact of political connections and executive character on tax evasion and to investigate the role of qualified auditors in preventing

and reducing the possibility of tax evasion. Numerous factors that are also this research's contribution are the motivation for it. First off, despite the fact that many prior studies have been conducted in developed nations, tax evasion is still a fascinating topic in theoretical and empirical accounting study today (Ajili & Khlif, 2020; Alkurdi & Mardini, 2020). Second, by concentrating on examining the impact of political connections and executive character on tax evasion by taking audit quality to be considered as a moderating variable, this study adds to the existing literature. To strengthen the research model, this study also adds three control variables: company size, leverage, and profitability.

### Political Connection's Impact on Tax Avoidance

<sup>6</sup> In establishing an effective tax management approach to reduce taxable income, the board of directors, act as an agent for the firm, plays a key role (Frank, Lynch, & Rego, 2009; Wahab, Ariff, Marzuki, & Sanusi, 2017). Politicians will defend businesses with political ties, lowering their danger of being found out during tax audits and shielding them from legal action (Ajili & Khlif, 2020). Because of this, businesses with political connections tend to use more aggressive taxation strategies (J.-B. Kim & Zhang, 2016; Wahab et al., 2017), as well as pay significantly less in taxes than other companies (Rustiarini & Sudiartana, 2021; Taylor & Richardson, 2014). According to several research (Ajili & Khlif, 2020; C. Kim & Zhang, 2016; Shen et al., 2019; Wahab et al., 2017), management with political connections frequently engages in tax avoidance. Numerous researchers in Indonesia (Oktavia, 2020; Rustiarini & Sudiartana, 2021; Yudanto & Damayanti, 2022) reported similar findings. The idea that follows is formulated using the above-described empirical evidence as well as thought reasoning.

H1: Political connections have a favorable impact on tax avoidance

### The Effect of Executive Character on Tax Avoidance

<sup>17</sup> Managers play an important role in generating value for the organization through their management practices and inherent skills. Company executives can be categorized as risk takers or risk averse depending on their preference for taking risks. According to agency theory, tax avoidance is one of the risky decisions made by companies and is impacted by executive corporate policies (Alfiyah et al., 2022; Mohammed & Sanusi, 2020). High-risk decisions are more likely to be made by executives who prefer them in order to increase business value, which increases the likelihood that they will promote tax evasion. Zhang et al. (2021), who assert that CEOs with risk-taking characters will focus on enhancing corporate value and embrace tax avoiding strategies, support this. Tax avoidance will reduce the tax burden that businesses must pay, resulting in greater income and, ultimately, higher firm value (Alfiyah et al., 2022). This hypothesis is consistent with study by Baghdadi (2022), which demonstrates that CEOs who are risk-takers participate in tax avoidance and dramatically lower the effective tax rate of company cash. Several studies in Indonesia that tested the effect of executive character as measured by CEO courage in taking risks also proved that CEO risk takers had a positive effect on corporate tax avoidance (Alfiyah et al., 2022; Dewi & Yasa, 2020; Noviari & Suaryana, 2019; D. Prastiwi &

Ratnasari, 2019).<sup>2</sup> Based on the logic of thought above, the following hypothesis is formulated.

H2: Executive character has a positive effect on tax avoidance

### **The Effect of Audit Quality on Tax Avoidance**

Understanding corporate tax evasion requires taking into account corporate governance, which serves as a framework for balancing the interests of shareholders and management (Bauer, Krouxous, & Krenn, 2018; Kovermann & Velte, 2019). Corporate governance can reduce the likelihood of corporate tax avoidance and reduce the impact of agency problems in tax avoidance schemes (Alfiyah et al., 2022; Armstrong, Blouin, & Larcker, 2015; Chan, Mo, & Zhou, 2013). A quality audit is viewed as an external governance instrument that plays a significant role in decreasing agency conflicts, according to agency theory. In order to mitigate management's opportunistic behavior, quality auditors can act as a powerful monitoring tool (Indarti & Widiatmoko, 2021). This is so that shareholders may effectively monitor management activities according to accurate financial reporting that is ensured by a high-quality audit. Researchers, Mira and Purnamasari (2020) and Prasetyo et al. (2021) demonstrate that audit quality has negative effects on tax avoidance. Purnomo & Eriandani (2022) reported similar findings, stating that having a good external auditor helped to reduce management tax avoidance. This description leads to the formulation of the following theory.

H3: Tax avoidance is negatively impacted by audit quality.

### **Audit Quality weakens the Positive Effect of Political Connections and Executive Character on Tax Avoidance**

Many factors, such as political connections and executive character, might have an impact on tax avoidance. Politicians on a company's board have the potential to influence CEOs' actions and frequently lead to conflicts of interest, according to agency theory (Ling, Zhou, Liang, Song, & Zeng, 2016). Kim & Zhang (2016) argue that due to government protection, businesses with political connections are able to use much more aggressive tax planning. Politically linked businesses in Malaysia pay much less in taxes than politically disconnected businesses, according to Kweh et al. (2021).

On the other hand, executives have a significant role in the level of corporate tax avoidance (Rudy, 2021). Tax avoidance is a risky action, so the more executives who are risk takers, the higher the level of tax avoidance is carried out (Mohammed & Sanusi, 2020). Agency conflict as reflected in tax avoidance behavior can be minimized by implementing good corporate governance (Armstrong et al., 2015), including by using a qualified external auditor. This external governance mechanism can mitigate the potential for companies to avoid paying taxes (Chan et al., 2013) and is expected to weaken the positive influence of political connections and executive character on tax evasion practices. The results of Ajili & Khlif's research (2020) prove that the governance mechanism as measured by joint audits causes political connections to have no effect on tax avoidance in Islamic banks in eight countries including Indonesia. Meanwhile, Alfiyah et al. (2022) proved that the implementation of good governance is able to mitigate tax avoidance behavior by executives with risk taker characteristics.

Based on the above thoughts, the following two hypotheses are formulated.

H4: The positive effect of political connections on tax avoidance is weakened by audit quality

H5: The positive impact of executive character on tax avoidance is weakened by audit quality.

## 2. METODE

Manufacturing firms registered on the Indonesia Stock Exchange in 2019–2021 are used as the population for this study. The reason for this is that the manufacturing industry in Indonesia is the one that pays the highest rates of income taxes (Kemenperin, 2018), however empirical data still indicates that public firms engage in tax avoidance (Rustiarini & Sudiartana, 2021). Purposive sampling was employed to choose the sample, and the following criteria were used: 1) The company released audited financial reports; 2) It suffered no losses; and 3) It possessed all the information required for this investigation. The 343 data were collected using these criteria and 246 final data were generated after the residual normality test, which were subsequently processed in this study.

Table 1. Operational Definition and Measurement of Variables

No.	Variables	Operational Definition	Measurement	Reference
1	Tax avoidance	Measures taken by a company to reduce its tax liability	ETR = Income Tax expense/ Income before tax	(Ajili & Khlif, 2020; Ding et al., 2021)
2	Political connection	Conditions that indicate a political relationship between directors or commissioners and external parties within the company, where both parties benefit from political relations.	The measurement uses a dummy variable, namely the board of directors with a political connection, code 1, and code 0 if otherwise.	(Rustiarini & Sudiartana, 2021)
3	Executive character	An action taken by the executive when faced with a risk	Standard deviation of (EBITDA/Total Assets). EBITDA = earnings before income tax, depreciation, and amortization.	(Alabede, 2018; Alfiyah et al., 2022)
4	Audit quality	Auditors who have high values of independence, objectivity and honesty.	The dummy variable is a value of 1 for companies audited by KAPs affiliated with the Big Four Public Accounting Firms (KAP) and 0 otherwise.	(Indarti & Widiatmoko, 2021)
5	Firm size	The size of the company is classified based on total assets	Total Assets	(Widiatmoko & Indarti, 2018)
6	Profitability	The company's ability to earn profits	Return on Assets (ROA) = (Net Income/Total Assets)	(Widiatmoko & Indarti, 2019)
7	Leverage	The company's ability to meet long-term obligations	Leverage = (Total debt/Total assets)	(Widiatmoko & Indarti, 2019)

This study uses four variables, namely tax avoidance, political connections, executive character, and audit quality, as well as three control variables, namely firm size, profitability and leverage. In Table 1, operational definitions and variable metrics are shown. Modified regression analysis (MRA) was used in this study to examine the hypotheses. The use of the MRA regression, which comprises the multicollinearity, autocorrelation, and heteroscedasticity tests, is a criterion that must be met before testing the hypothesis. The following equation provides a mathematical description of the research model.

$$ETR = \alpha + \beta_1PC + \beta_2RISK + \beta_3AQ + \beta_4PC* AQ + \beta_5RISK* AQ + \beta_6SIZE + \beta_7ROA + \beta_8LEV + e$$

**Keterangan**

- ETR : Tax avoidance
- $\alpha$  : Constant
- $\beta_1 - \beta_7$  : Regression coefficient
- PC : Political connections
- RISK : Executive character
- AQ : Audit Quality
- PC\* AQ : The interaction of political connections and audit quality
- EC\* AQ : Interaction of executive character and audit quality
- SIZE : Company size
- ROA : Profitability
- LEV : Leverage
- e : Error term

**3. RESULTS AND DISCUSSION**

**Descriptive statistics**

Table 2 provides descriptive statistics for each variable employed in this study. The average value of the effective tax rate is 0.239, which indicates that companies pay 23.90% of their net income in taxes on average. The sample companies' level of tax avoidance is rather high because this average value is low. The average value of the executive character shows a fairly low number, which is 0.030. This figure indicates that the executives in the sample companies have a risk averse character. The sample companies that have political connections are 36.20%, while the remaining 63.80% have no political connections. Meanwhile, 37.40% of the sample companies were audited by Big Four KAPs and the remaining 62.60% were audited by Non Big Four KAPs.

Table 2. Descriptive Statistics

Variables	N	Minimum	Maximum	Average	Standard Deviation
ETR	246	0.056	0.412	0.239	0.061
RISK	246	0.002	0.079	0.030	0.017
SIZE	246	0.043	367.311	16.982	46.564

ROA	246	0.002	0.189	0.063	0.043
LEV	246	0.067	2.248	0.772	0.496
PC	246	PC	89 (36.20%)	Non PC	157 (63.80%)
AQ	246	Big Four	92 (37.40%)	Non Big Four	154 (62.60%)

Note: ETR = effective tax rate; RISK = executive character; SIZE = company size; ROA = return on assets; LEV = leverage; PC = political connection; AQ = audit quality

The average sample company size as a proxy for total assets is 16,982 trillion with a maximum value of 367,311 trillion and a minimum value of 0.043 trillion. The return on assets of the sample companies shows an average figure of 0.063. This means that in general the sample companies generate a profit of 6.3% of the total assets owned. The average leverage of the sample companies shows the number 0.772, meaning that 77.20% of the asset structure in the sample companies is funded by debt.

### Matriks Korelasi Pearson

Table 3 Pearson Correlation Matrix

	ETR	PC	RISK	AQ	SIZE	ROA	LEV
ETR	1						
PC	-.196***	1					
RISK	-.218***	-.018	1				
AQ	.091	.327***	.090	1			
SIZE	.016	.293***	-.102	.257***	1		
ROA	-.176***	.125*	.317***	.247***	-.002	1	
LEV	.062	.142**	-.062	-.064	.089	-.444***	1

Note: ETR = effective tax rate; RISK = executive character; SIZE = company size; ROA = profitability; DER = leverage; PC = political connection; AQ = audit quality  
 \*\*\*, \*\* and \*, mengindikasikan bahwa estimasi signifikan pada level 1%, 5%, and 10% secara berturut-turut.

The Pearson correlation matrix between variables is presented in Table 3. Based on the information in Table 3, it can be seen that the correlation between the independent variables is less than 50%, so there is no collinearity problem in this study. A significant negative relationship is shown in the political connection (PC) and effective tax rate (ETR) variables, which are proxies for tax avoidance. When the directors and commissioners of the sample companies have political relations with external parties, management will tend to take tax evasion actions as indicated by the lower ETR value. Executive character (RISK) has a significant negative relationship with



ETR. This condition indicates that the more courageous executives take risks, the higher their tendency to take tax avoidance. The relationship between audit quality (AQ) and ETR shows a positive direction but is not significant. The presence of quality auditors does not encourage management to reduce tax avoidance. Firm size (SIZE) has a positive but not significant relationship with ETR. The larger the size of the company, does not encourage management to take tax avoidance. Profitability and ETR show a significant negative relationship. Companies with higher levels of profitability will encourage management to take tax avoidance measures, which is indicated by the lower the ETR value. The level of corporate leverage (DER) has a positive but not significant relationship with ETR. This condition can be interpreted that the higher the level of corporate debt does not encourage management to take tax avoidance.

### Test Results of Moderated Regression Analysis

Before testing the classical assumptions and panel data regression, a model selection is first carried out to determine the best model as presented in Table 4. Based on the information in Table 4 it can be seen that the best model is the REM model.

Table 4. Model Selection of Panel Data

Test	Explanation	Prob.	Selected Models
Chow Test	CEM VS FEM	0.000	FEM
Hausman Test	FEM VS REM	0.076	REM

The residual errors are regularly distributed, as seen by the normality test with Jarque-Bera findings, which reveal a probability value of 0.116, greater than 0.05. Durbin Watson autocorrelation analysis yields a value of 2.05. This indicates that there is no autocorrelation issue with the regression model since the value is in the range of the du value of 1.852 and the 4-du of 2.148.

Table 5 displays the results of data analysis using moderated regression analysis. According to information in Table 5, the adjusted R2 value is 0.1182. The power of political connection variables, executive character, audit quality, company size, profitability, and leverage to explain variances in tax avoidance as measured by an effective tax rate of 11.8% may be predicted from this number. While additional factors not included in this research model account for the remaining 88.2%. The political connection, executive character, audit quality, leverage, and profitability variables all simultaneously effect tax avoidance, according to the F-statistic value of 5.105 with a significance value of 0.000, indicating that the model is considered feasible.

Table 5. Moderated Regression Analysis Test Results

Variables	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.225	0.044	-5.066	0.000
PC	0.058	0.013	4.512	0.000
RISK	1.034	0.294	3.520	0.001

AQ	0.019	0.020	0.961	0.337
PC*AQ	-0.040	0.018	-2.198	0.029
RISK*AQ	-0.894	0.467	-1.916	0.057
SIZE	-0.004	0.003	-1.161	0.247
ROA	0.178	0.104	1.704	0.090
LEV	-0.008	0.010	-0.814	0.417

Weighted Statistics			
R-squared	0.147	Mean dependent var	-0.155
Adjusted R-squared	0.118	S.D. dependent var	0.051
S.E. of regression	0.046	Sum squared resid	0.499
F-statistic	5.105	Durbin-Watson stat	2.105
Prob(F-statistic)	0.000		

Note: ETR = effective tax rate; RISK = executive character; SIZE = company size; ROA = return on assets; LEV = leverage; PC = political connection; AQ = audit quality

The first and second hypotheses are supported by the information provided in Table 5 since it is clear that political connections and executive character have a favorable impact on tax evasion. This is evident from the beta coefficient values for the two variables, which each show figures that are statistically significant at the 1% level of 0.058 and 1.034. The beta value of 0.019 with the probability value of 0.337 suggests that audit quality has no direct impact on tax avoidance. The fourth hypothesis is accepted since it shows that audit quality mitigates the positive influence of political relationships on tax avoidance. The beta coefficient value of -0.894, which is significant at the 5% level, indicates this. The fifth hypothesis also shows that audit quality has a power to reduce the impact of executive character on tax avoidance, even at the 10% level. Profitability promotes tax avoidance, according to the test results on the control variable, while company size and leverage have no impact.

## Discussion

The findings of verifying the first hypothesis demonstrate that political connections have a positive effect on tax avoidance. These results are consistent with agency theory, which contends that management might engage in tax avoidance due to information asymmetry and conflicts of interest between principals and agents. By taking riskier activities brought on by a lack of control and supervision from the principal, management, the party with more knowledge about the company, seeks to maximize its interests while ignoring the interests of shareholders (Alfiyah et al., 2022). Management's political relationships with the government and policy makers are what motivate management's bravery in taking risks. Companies with political connections will receive guarantees or preferential treatment from the government (Faccio, 2016), are able to access tax regulations and law enforcement efforts (Ajili & Khelif, 2020), are protected from litigation risks in the future (Rustiarini & Sudiartana, 2021), and has a low tax detection risk (C. Kim & Zhang, 2016). The findings of this study are consistent with the results of previous research (Ajili & Khelif, 2020; Shen et al., 2019; Wahab et al., 2017), which proves that companies with political connections will tend to do tax evasion, which causes a low tax burden paid. Several studies conducted in Indonesia

(Oktavia, 2020; Rustiarini & Sudiartana, 2021; Yudanto & Damayanti, 2022) also prove that companies with political connections have a lower effective tax rate, which means tax avoidance. Management has an incentive to get into politics in order to be less burdened by tax regulations and less exposed to monitoring and supervision.

This study proves that executive character as measured by risk takers has a positive impact on tax avoidance. The findings of this study support the agency theory which states that the separation of ownership and control between managers and company owners causes information asymmetry and conflict of interest (Bauer et al., 2018; Widiatmoko, Indarti, & Pamungkas, 2020), especially when each party tries to maintain its level of prosperity (Ge & Zhang, 2017). This situation causes company executives to be more opportunistic and make risky decisions due to the lack of control from the principals. Tax evasion is a risky action taken by company management, which is influenced by the character of company executives (Alfiyah et al., 2022; Mohammed & Sanusi, 2020). CEOs who are risk takers tend to be a significant factor affecting corporate tax planning activities, considering that tax planning strategies require creativity, a willingness to pursue new and complex strategies, and risk acceptance (Chen, Tang, Wu, & Yang, 2021). The findings of this study support the results of the study of Baghdadi et al. (2022) which reported that companies with a risk-taking CEO character tend to have a low effective tax rate.

Unlike the first and second hypotheses, the third hypothesis in this study is not supported by empirical facts. Audit quality is not able to reduce management's motivation to take tax avoidance actions. The results of this study contradict agency theory which states that conflicts of interest between management and principals can be minimized by good governance practices (Alfiyah et al., 2022; Armstrong et al., 2015; Chan et al., 2013). The existence of a quality audit is seen as an external governance mechanism that has an important role in reducing agency conflicts. Quality auditors are a strong monitoring mechanism, thereby reducing management's opportunistic behavior (Indarti & Widiatmoko, 2021) in the form of tax evasion. However, the results of this study show the opposite, audit quality is not able to prevent tax evasion by management. The explanation that can be given is that the big four KAPs as a proxy for audit quality, not only provide services as independent auditors, but they also provide tax consulting services. As tax advisors, they may facilitate corporate tax minimization strategies by legally exploiting loopholes in the tax system in the form of tax evasion (Elbra, Mikler, & Murphy-Gregory, 2023).

The results of testing the fourth hypothesis indicate that audit quality weakens the positive influence of political connections on tax avoidance practices. The findings of this study support the agency theory which states that quality auditors can function as an external mechanism capable of mitigating the opportunistic behavior of management who is subject to scrutiny due to political connections (Chan et al., 2013). The results of this study are in line with the findings of Ajili & Kliff (2020), which proves that an effective external governance mechanism will cause political connections to have no effect on management's tax avoidance actions.

In accordance with the hypothesis, the findings of this study prove that a quality audit is able to weaken the positive influence of executive character on tax evasion. The findings of this study are in accordance with agency theory which states that

agency conflict will encourage management's opportunistic behavior which is manifested in the form of tax avoidance practices. This tax avoidance action will tend to occur in companies with executives who have the character of risk takers because tax avoidance is a risky action (Mohammed & Sanusi, 2020). However, the implementation of an effective external governance mechanism through a qualified independent auditor will reduce management's motivation to take tax avoidance actions. This finding is in line with the results of research reported by Alfiah et al. (2022) that the implementation of good governance is able to mitigate tax avoidance behavior by management. Good corporate governance minimizes the possibility of corporate executives being involved in dangerous acts such as accounting fraud which leads to aggressive tax enforcement. The presence of qualified external auditors will increase transparency and accountability resulting in best practices that ensure the quality of financial reports and disclosures (Zhang et al., 2021).

10

## CONCLUSION

Tax avoidance and its relation to political connections is an important research topic, which still requires exploration especially in a developing country like Indonesia. The practice of tax avoidance is also a complex phenomenon and involves the character of company managers because tax avoidance is a risky act. This study aims to examine the effect of political connections and executive character on tax avoidance practices. This study also examines the role of quality auditors in mitigating the influence of political connections and executive character on tax avoidance practices. The results of the study show that political connections and executive character can trigger tax avoidance. However, the presence of a quality auditor is able to mitigate the positive influence of these two variables.

The findings of this study are consistent with agency theory, which highlights the value of governance measures in reducing agency conflicts. In particular, the presence of competent auditors can lessen management's propensity for tax evasion. The findings of this study add to the accounting literature showing executives with risk-taking personalities, in particular, have a propensity to engage in risky behavior like tax evasion. The results of this study are crucial for the Directorate General of Taxes in identifying how to better oversee businesses with risk-taking leaders and political connections in order to make tax policy more effective. This study has several limitations, including this study only uses one proxy for tax avoidance, namely ETR. Future researchers need to use cash effective tax rate (CETR), discretionary measure of tax avoidance (DTAX) or abnormal book tax differences (BTD) as proxies for tax avoidance. This research is limited to manufacturing companies as the largest taxpayers in Indonesia, but exploration of the banking industry needs to be done as a comparison.

## References

Ajili, H., & Khlif, H. (2020). Political connections, joint audit and tax avoidance: evidence from Islamic banking industry. *Journal of Financial Crime*, 27(1), 155–171. <https://doi.org/10.1108/JFC-01-2019-0015>

- Alabede, J. O. (2018). Economic freedom and tax revenue performance in sub-Saharan Africa. *Journal of Financial Reporting and Accounting*, 16(4), 610–638. <https://doi.org/10.1108/JFRA-04-2017-0024>
- Alfiyah, N., Subroto, B., & Ghofar, A. (2022). IS TAX AVOIDANCE CAUSED BY POLITICAL CONNECTIONS AND EXECUTIVE CHARACTERISTICS? *Jurnal Akuntansi Multiparadigma*, 13(1), 32–41. <https://doi.org/10.21776/ub.jamal.2021.13.1.03>
- Alkurdi, A., & Mardini, G. H. (2020). The impact of ownership structure and the board of directors' composition on tax avoidance strategies: empirical evidence from Jordan. *Journal of Financial Reporting and Accounting*, 18(4), 795–812. <https://doi.org/10.1108/JFRA-01-2020-0001>
- Armstrong, C. S., Blouin, J. L., & Larcker, D. F. (2015). Corporate Governance, Incentives, and Tax Avoidance. *Accounting Paper*, 60, 1–17.
- Badertscher, B. A., Katz, S. P., Rego, S. O., & Wilson, R. J. (2019). Conforming Tax Avoidance and Capital Market Pressure. *The Accounting Review*, 94(6), 1–30. <https://doi.org/10.2308/accr-52359>
- Baghdadi, G., Podolski, E. J., & Veeraraghavan, M. (2022). CEO risk-seeking and corporate tax avoidance: Evidence from pilot CEOs. *Journal of Corporate Finance*, 76. <https://doi.org/10.1016/j.jcorpfin.2022.102282>
- Barford, V., & Holt, G. (2013). Google, Amazon, Starbucks: The rise of “tax shaming.” *BBC News*, (May). Retrieved from <https://www.bbc.co.uk/news/magazine-20560359>
- Baron, R. M., & Kenny, D. A. (1986). The Moderator-Mediator Variable Distinction in Social Psychological Research: Conceptual, Strategic, and Statistical Considerations. *Journal of Personality and Social Psychology*, 51(6), 1173–1182. <https://doi.org/10.1037/0022-3514.51.6.1173>
- Bauer, T., Kouroukous, T., & Krenn, P. (2018). Taxation and agency conflicts between firm owners and managers: a review. *Business Research*, 11(1), 33–76. <https://doi.org/10.1007/s40685-017-0054-y>
- Chan, K. H., Mo, P. L. L., & Zhou, A. Y. (2013). Government ownership, corporate governance and tax aggressiveness: evidence from China. *Accounting & Finance*, 53(4), 1029–1051. <https://doi.org/10.1111/acfi.12043>
- Chen, H., Tang, S., Wu, D., & Yang, D. (2021). The political dynamics of corporate tax avoidance: The Chinese experience. *Accounting Review*, 96(5), 157–180. <https://doi.org/10.2308/TAR-2017-0601>
- CNN, I. (2021). Penerimaan Pajak Anjlok 19,7 Persen. *Pajakonline.Com*, pp. 197–199. Retrieved from [https://www.cnnindonesia.com/ekonomi/20210106180340-532-590340/penerimaan-pajak-anjlok-197-persen-jadi-rp1070-triliun#:~:text=Pada 2020%2C pajak yang dihimpun,FOTO%2Fakbar Nugroho Gumay\).&text=Menteri](https://www.cnnindonesia.com/ekonomi/20210106180340-532-590340/penerimaan-pajak-anjlok-197-persen-jadi-rp1070-triliun#:~:text=Pada 2020%2C pajak yang dihimpun,FOTO%2Fakbar Nugroho Gumay).&text=Menteri)

Keuangan Sri Mulyani menyatakan,Rp1.332%2C7 triliun.

- Dewi, K. S., & Yasa, G. W. (2020). The Effects of Executive and Company Characteristics on Tax Aggressiveness. *Jurnal Ilmiah Akuntansi Dan Bisnis*, 15(2), 280. <https://doi.org/10.24843/JIAB.2020.v15.i02.p10>
- Ding, R., Sainani, S., & Zhang, Z. (John). (2021). Protection of trade secrets and corporate tax avoidance: Evidence from the inevitable disclosure doctrine. *Journal of Business Research*, 132(April), 221–232. <https://doi.org/10.1016/j.jbusres.2021.03.042>
- Elbra, A., Mikler, J., & Murphy-Gregory, H. (2023). The Big Four and corporate tax governance : From global harmony to national regulatory incrementalism, 14(1), 72–83. <https://doi.org/10.1111/1758-5899.13150>
- Fitriaa, G. N. (2018). Pengaruh Kepemilikan Institusional, Komisaris Independen, Karakter Eksekutif Dan Size Terhadap Tax Avoidance. *Profita: Komunikasi Ilmiah Akuntansi Dan Perpajakan*, 11(3), 438–451.
- Frank, M. margaret, Lynch, L. J., & Rego, S. O. (2009). Tax Reporting Aggressiveness and Its Relation to Aggressive Financial Reporting. *The Accounting Review*, 84(2), 467–496. <https://doi.org/10.2308/accr.2009.84.2.467>
- Ge, R., & Zhang, J. J. (2017). Regulatory investigations of audit partners and audit quality improvement. *China Journal of Accounting Studies*, 5(3), 275–293. <https://doi.org/10.1080/21697213.2017.1375647>
- Hong, H. A., Kalcheva, I., & Srivastava, A. (2017). A reexamination of the theory of agency costs of tax avoidance Hyun A. Hong, Ivalina Kalcheva, Anup Srivastava \* January 15, 2017. *Emma*, 1–43.
- Huseynov, F., Sardarli, S., & Zhang, W. (2017). Does index addition affect corporate tax avoidance? *Journal of Corporate Finance*, 43, 241–259. <https://doi.org/10.1016/j.jcorpfin.2017.01.008>
- Indarti, M. G. K., & Widiatmoko, J. (2021). The Effects of Earnings Management and Audit Quality on Cost of Equity Capital: Empirical Evidence from Indonesia. *Journal of Asian Finance, Economics and Business*, 8(4), 769–776. <https://doi.org/10.13106/jafeb.2021.vol8.no4.0769>
- Kalbuana, N., Taqi, M., Uzliawati, L., & Ramdhani, D. (2023). CEO narcissism, corporate governance, financial distress, and company size on corporate tax avoidance. *Cogent Business and Management*, 10(1). <https://doi.org/10.1080/23311975.2023.2167550>
- Kanagaretnam, K., Lee, J., Lim, C. Y., & Lobo, G. J. (2016). Relation between auditor quality and tax aggressiveness: Implications of cross-country institutional differences. *Auditing*, 35(4), 105–135. <https://doi.org/10.2308/ajpt-51417>

- Kemenperin. (2018). *Analisis Kerja Industri 2018*. *Kemenperin.go.id*. Retrieved from <https://kemenperin.go.id>
- Kim, C., & Zhang, L. (2016). Corporate Political Connections and Tax Aggressiveness. *Contemporary Accounting Research*, 33(1), 78–114. <https://doi.org/10.1111/1911-3846.12150>
- Kim, J.-B., & Zhang, L. (2016). Accounting Conservatism and Stock Price Crash Risk: Firm-level Evidence. *Contemporary Accounting Research*, 33(1), 412–441. <https://doi.org/10.1111/1911-3846.12112>
- Kovermann, J., & Velte, P. (2019). The impact of corporate governance on corporate tax avoidance—A literature review. *Journal of International Accounting, Auditing and Taxation*, 36. <https://doi.org/10.1016/j.intaccaudtax.2019.100270>
- Kweh, Q. L., Ting, I. W. K., Azizan, N. A., & Ahmad, N. (2021). Political connections and cash holdings in financially constrained firms: evidence from top 500 firms in Malaysia. *International Journal of Business Excellence*, 24(1), 125. <https://doi.org/10.1504/IJBEX.2021.115372>
- Ling, L., Zhou, X., Liang, Q., Song, P., & Zeng, H. (2016). Political connections, overinvestments and firm performance: Evidence from Chinese listed real estate firms. *Finance Research Letters*, 18, 328–333. <https://doi.org/10.1016/j.frl.2016.05.009>
- Ma, M. (Shuai), & Thomas, W. B. (2020). Legal Environment and Corporate Tax Avoidance: Evidence from State Tax Codes. *Journal of the American Taxation Association*, 42(2), 57–83. <https://doi.org/10.2308/atax-52510>
- Mahaputra, I. N. K. A., Rustiarini, N. W., Anggraini, N. P. N., & Sudiartana, I. M. (2018). National Culture and Perceived Ethics of Tax Evasion: Case of Bali Province. *Journal of Economics, Business & Accountancy Ventura*, 21(1), 89–104. <https://doi.org/10.14414/jebav.v21i1.1118>
- Mira, M., & Purnamasari, A. W. (2020). PENGARUH KUALITAS AUDIT TERHADAP TAX AVOIDANCE PADA PERUSAHAAN SEKTOR PERBANKAN YANG TERDAFTAR DI BEI PERIODE 2016-2018. *Amnesty: Jurnal Riset Perpajakan*, 3(2), 211–226. <https://doi.org/10.26618/jrp.v3i2.4415>
- Mohammed, F., & Sanusi, S. (2020). Quality of Governance and Tax Revenue Generation in West Africa: A Political Process Theory Perspective. *Management and Accounting Review*, 19(1). <https://doi.org/10.24191/mar.v19i01-08>
- Noviari, N., & Suaryana, I. G. N. A. (2019). Mampukah Corporate Governance Mengurangi Eksekutif Risk Taker Melakukan Penghindaran Pajak? *Jurnal Ilmiah Akuntansi Dan Bisnis*, 14(2), 265. <https://doi.org/10.24843/JIAB.2019.v14.i02.p11>
- Novita, N. (2016). Executives Characters, Gender and Tax Avoidance: A Study on Manufacturing Companies in Indonesia. In *Proceedings of the 2016 Global*

- Conference on Business, Management and Entrepreneurship* (Vol. 15, pp. 1–35). Paris, France: Atlantis Press. <https://doi.org/10.2991/gcbme-16.2016.15>
- Oats, L., & Tuck, P. (2019). Corporate tax avoidance: is tax transparency the solution? *Accounting and Business Research*, 49(5), 565–583. <https://doi.org/10.1080/00014788.2019.1611726>
- OECD. (2021). Revenue Statistics in Asia and the Pacific 2022 - Indonesia. *OECD Tax Statistics (Database)*. Retrieved from <http://www.oecd.org/tax/tax-policy/oecd-classification-taxes-interpretative-guide.pdf>
- Oktavia, O. (2020). Independent Corporate Governance Organs' Activities, Tax Avoidance, and Country Tax Environment: Evidence from ASEAN Countries. *Pertanika Journal of Social Sciences and Humanities*, 28(2), 1485–1505.
- Phan, T. T. H., Lai, L. A., Le, T. T., Tran, D. M., & Tran, D. T. (2020). The impact of audit quality on performance of enterprises listed on Hanoi Stock Exchange. *Management Science Letters*, 10(1), 217–224. <https://doi.org/10.5267/j.msl.2019.8.001>
- Prasetyo, T., Djaddang, S., & Ahmar, N. (2021). Rata-rata CETR Perusahaan Pertambangan Periode 2015-2019. *Jurnal Riset Akuntansi Dan Keuangan*, 9(2), 267–280. <https://doi.org/10.17509/jrak.v9i2.31919>
- Prastiwi, D., & Ratnasari, R. (2019). The Influence of Thin Capitalization and The Executives' Characteristics Toward Tax Avoidance by Manufacturers Registered on ISE in 2011-2015. *AKRUAL: Jurnal Akuntansi*, 10(2), 119. <https://doi.org/10.26740/jaj.v10n2.p119-134>
- Prastiwi, I. S., & Siregar, S. V. (2019). The Effect of Corporate Social Responsibility on Tax Avoidance and Earnings Management: The Moderating Role of Political Connections. *International Journal of Business*, 24(3), 229–248. Retrieved from <https://scholar.ui.ac.id/en/publications/the-effect-of-corporate-social-responsibility-on-tax-avoidance-an>
- Purnomo, H., & Eriandani, R. (2022). Pengaruh Efektivitas Komite Audit dan Penghindaran Pajak: Peran Moderasi Kualitas Audit. *E-Jurnal Akuntansi*, 32(7), 1743. <https://doi.org/10.24843/EJA.2022.v32.i07.p06>
- Rudy, K. V. (2021). Political tax cycles: Cyclicity of the tax burden in election periods. *Journal of Tax Reform*, 7(2), 193–205. <https://doi.org/10.15826/jtr.2021.7.2.098>
- Rustiarini, N. W., & Sudiartana, I. M. (2021). Board Political Connection and Tax Avoidance: Ownership Structure as A Moderating Variable. *Jurnal Dinamika Akuntansi Dan Bisnis*, 8(2), 128–144. <https://doi.org/10.24815/jdab.v8i2.20760>
- Salehi, M., Tarighi, H., & Shahri, T. A. (2020). The effect of auditor characteristics on tax avoidance of Iranian companies. *Journal of Asian Business and Economic Studies*, 27(2), 119–134. <https://doi.org/10.1108/JABES-11-2018-0100>



- Shen, Y., Gao, D., Bu, D., Yan, L., & Chen, P. (2019). CEO hometown ties and tax avoidance-evidence from China's listed firms. *Accounting and Finance*, 58(5), 1549–1580. <https://doi.org/10.1111/acfi.12442>
- Taylor, G., & Richardson, G. (2014). Incentives for corporate tax planning and reporting: Empirical evidence from Australia. *Journal of Contemporary Accounting and Economics*, 10(1), 1–15. <https://doi.org/10.1016/j.jcae.2013.11.003>
- Tsai, P. H., Liu, Y., & Liu, X. (2021). Collusion, political connection, and tax avoidance in China. *Kyklos*, 1–25. <https://doi.org/10.1111/kykl.12265>
- Wahab, E. A. A., Ariff, A. M., Marzuki, M. M., & Sanusi, Z. M. (2017). Political connections, corporate governance, and tax aggressiveness in Malaysia. *Asian Review of Accounting*, 25(3), 424–451. <https://doi.org/10.1108/ARA-05-2016-0053>
- Wang, L., & You, K. (2022). The impact of political connections on corporate tax burden: Evidence from the Chinese market. *Finance Research Letters*, 47(1), 102944. <https://doi.org/10.1016/j.frl.2022.102944>
- Widarjo, W., Sudaryono, E. A., Sutopo, B., Syafiqurrahman, M., & Juliati, J. (2021). The Moderating Role of Corporate Governance on the Relationship between Political Connections and Tax Avoidance. *Jurnal Dinamika Akuntansi*, 13(1), 62–71. <https://doi.org/10.15294/jda.v13i1.26359>
- Widiatmoko, J., & Indarti, M. G. K. (2019). Book Tax Differences, Operating Cash Flow, Leverage and Earning Persistence in Indonesia Manufacturing Companies. *Jurnal Dinamika Akuntansi*, 11(2), 151–159. <https://doi.org/10.15294/jda.v11i2.20481>
- Widiatmoko, J., Indarti, M. G. K., & Pamungkas, I. D. (2020). Corporate governance on intellectual capital disclosure and market capitalization. *Cogent Business and Management*, 7(1), 1–14. <https://doi.org/10.1080/23311975.2020.1750332>
- Widiatmoko, J., & Indarti, M. K. (2018). The Determinans Of Earnings Response Coefficient: An Empirical Study For The Real Estate And Property Companies Listed On The Indonesia Stock Exchange. *Accounting Analysis Journal*, 7(2), 135–143. <https://doi.org/10.15294/aaj.v7i2.27321>
- Yudanto, L. A., & Damayanti, T. W. (2022). Political Connection, Foreign Ownership, and Tax Avoidance: Does Executive Gender Moderate the Relationship? *Journal of Economics, Business, & Accountancy Ventura*, 24(3), 408–419. <https://doi.org/10.14414/jebav.v24i3.2899>
- Zhang, T., Zhang, X., & Yang, D. (2021). Does industrial policy suppress corporate tax avoidance ? — a study on the perspective of provincial industrial policy. *China Journal of Accounting Studies*, 9(2), 143–167. <https://doi.org/10.1080/21697213.2021.1980954>

# Political Connections, Executive Character And Tax Avoidance: Does Audit Quality Moderate The Relationship

## ORIGINALITY REPORT

14%

SIMILARITY INDEX

14%

INTERNET SOURCES

8%

PUBLICATIONS

1%

STUDENT PAPERS

## PRIMARY SOURCES

1	<a href="http://jurnal.unsyiah.ac.id">jurnal.unsyiah.ac.id</a> Internet Source	2%
2	<a href="http://koreascience.or.kr">koreascience.or.kr</a> Internet Source	2%
3	<a href="http://www.ssbfn.net">www.ssbfn.net</a> Internet Source	1%
4	<a href="http://www.atlantis-press.com">www.atlantis-press.com</a> Internet Source	1%
5	<a href="http://www.cell.com">www.cell.com</a> Internet Source	1%
6	<a href="http://www.researchgate.net">www.researchgate.net</a> Internet Source	1%
7	<a href="http://iaeme.com">iaeme.com</a> Internet Source	1%
8	<a href="http://repository.paramadina.ac.id">repository.paramadina.ac.id</a> Internet Source	1%
9	<a href="http://repository.ibs.ac.id">repository.ibs.ac.id</a> Internet Source	1%

10	Hana Ajili, Hichem Khelif. "Political connections, joint audit and tax avoidance: evidence from Islamic banking industry", Journal of Financial Crime, 2020 Publication	1 %
11	www.aessweb.com Internet Source	1 %
12	conference.upnvj.ac.id Internet Source	1 %
13	www.ijbel.com Internet Source	1 %
14	"Artificial Intelligence (AI) and Finance", Springer Science and Business Media LLC, 2023 Publication	1 %
15	gatreenterprise.com Internet Source	1 %
16	journal.unnes.ac.id Internet Source	1 %
17	psasir.upm.edu.my Internet Source	1 %

Exclude quotes  On

Exclude matches  < 1%

Exclude bibliography  On