Eduvest – Journal of Universal Studies
Volume 4 Number 10, October, 2024
p- ISSN 2775-3735- e-ISSN 2775-3727

THE ROLE OF CORPORATE GOVERNANCE IN MODERATING THE RELATIONSHIP BETWEEN TAX RISK AND LEVERAGE TO FIRM VALUE

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ABSTRACT

This study aims to examine the effect of tax risk and leverage on firm value, with corporate governance acting as a moderating variable. The research focuses on manufacturing companies listed on the Indonesia Stock Exchange (IDX) during the period of 2017 to 2021. By using a purposive sampling method, the study selects companies based on specific criteria, including those that have consistently published audited financial statements in Rupiah. The independent variables in this study are tax risk and leverage, while corporate governance serves as the moderating variable. The dependent variable, firm value, is measured using Tobin's Q, a widely accepted indicator. The analysis is conducted through panel data regression, with the Fixed Effect Model used to estimate the relationships among the variables. The results reveal that tax risk positively affects firm value, suggesting that effective tax management can enhance firm value by stabilizing cash flow and reducing tax penalties. However, leverage has a negative effect on firm value, as high debt levels increase financial risk, which may deter investors. Corporate governance significantly moderates the relationships, enhancing the positive effect of tax risk and reducing the negative impact of leverage on firm value. These findings underscore the importance of sound corporate governance practices in maintaining firm value by managing financial and tax-related risks. The study provides valuable insights for policymakers and corporate management on improving governance structures to optimize firm value.

KEYWORDS *Tax Risk, Leverage, Corporate Governance, Firm Value, Indonesia Stock Exchange.*

How to cite: Nur Rohmah Zainul Fitri, Hexana Sri Lastanti. (2024). The Role Of Corporate Governance In Moderating The Relationship Between Tax Risk And Leverage To Firm Value. Journal Eduvest. *4*(9): 9434-9441
E-ISSN: 2775-3727
Published by: https://greenpublisher.id/

INTRODUCTION

Initially, the company was built with the intention of optimizing shareholder wealth. Firm value is crucial because it reflects the condition of the company which can affect investors' perception of it. Therefore, every company owner strives to show superior performance to attract potential investors to invest (Ningrum, 2022). Investors respond to fundamental data presented by the company in its financial statements, such as profit and revenue growth. They also take into account tax policies and corporate tax activities, and react to tax policies set by the government with various sentiments, both positive and negative (Arora & Gill, 2022) (Irawan & Turwanto, 2020).

Currently, the government is considering the implementation of a progressive export tax on nickel commodities. According to Bernadus Irmanto, Chief Financial Officer of PT Vale Indonesia Tbk (INCO), this policy has the potential to pressure the domestic nickel industry. Ryan Santoso, an analyst from RHB Sekuritas Indonesia, stated in his research that if a 2% export tax on nickel is imposed, Antam's net profit is expected to decline by 4.3%. However, this only applies to the sales of Antam's FeNi products and assumes that other factors remain constant (www.cnbcindonesia.com). The tax amnesty program was a key factor that provided positive sentiment towards the movement of the composite stock price index at the beginning of 2017 (www.tempo.com). Companies participating in this program do not need to pay tax penalties and will not be audited by the Directorate General of Taxes for the fiscal year prior to the implementation of the tax amnesty. As a result, corporate tax risk becomes lower. Thus, investors view the reduction in tax risk as a positive aspect that can enhance firm value (Akbari et al., 2019).

According to Linawaty & Ekadjaja (2017), the Demand Hypothesis Theory explains that companies with high insider ownership tend to use more debt to finance their operations. This is done to maintain control over the company. On the other hand, the Supply Hypothesis states that companies with high insider ownership have lower debt agency costs, allowing them to use more debt. Both theories indicate that managerial ownership can drive corporate debt policy, which indirectly positively impacts the firm's value (Nesbitt et al., 2017). In other words, managerial ownership is believed to encourage the use of leverage, which ultimately affects the firm's value. One external mechanism believed to be able to suppress agency costs is the use of leverage. Lenders, such as financial institutions and banks, monitor the performance of managers in optimizing the firm's value. This monitoring allows creditors to assess the creditworthiness of the company and ensure compliance with loan agreements. The application of leverage creates incentives for managers to increase the firm’s value (Jensen & Meckling, 2019).

Related to Leverage, recently it was revealed that there was a case of SOEs entangled in online loans (pinjol). State-owned enterprise observer Toto Pranoto assessed the state-owned company that was involved in loans as a tragic phenomenon (Nebie & Cheng, 2023). In the financial aspect, Toto explained that SOEs have generally implemented Standard Operating Procedures (SOPs) that regulate financial management mechanisms. This SOP covers a wide range of funding instruments, including working capital loans for short-term liquidity needs,

long-term loans for investments, and the issuance of financial instruments such as bonds to finance long-term investments (Supatmi et al., 2021).

Seeing these phenomena, Corporate Governance (CG) plays an important role in determining the company's policies and strategic decisions (Fooladi & Farhadi, 2017). The application of good CG will have a positive impact on the company's performance, which ultimately increases the company's value. This is reflected in the increase in the company's share price, which is one of the indicators of the company's value. Thus, the effective implementation of CG can maximize the company's value for stakeholders. This study aims to examine the influence of tax risk and leverage on firm value, as well as the role of governance as a moderating variable (Drake et al., 2019).

RESEARCH METHOD

Types and Data of Research

This study uses secondary data, namely data obtained from other sources that have been published in the form of annual reports of manufacturing companies listed on the Indonesia Stock Exchange (IDX) in 2017 - 2021.

Population and Sample

This research focuses on manufacturing companies listed on the Indonesia Stock Exchange (IDX) in the period 2019 to 2021. With the technique, Purposive Sampling is used in this study to select a representative sample. This technique allows researchers to select companies based on certain criteria that have been set. And the sample criteria in this study are manufacturing companies that are listed on the IDX and consistently publish audited financial statements published during the period 2017 to 2021. Companies included in the IDX main board. The audited financial statements were presented in Rupiah for the period from December 31, 2017 to December 31, 2021. And there is an exception to the sample, namely companies that suffered losses during the period 2017 to 2021.

Variable Definitions and Measurements

Dependent Variable

According to Turwanto & Irawan (2020), Firm Value is the value formed on the company's share price, which reflects the value of shareholders measured by the proxy value of the company used is Tobins Q. The formula of Tobins Q according to Chung and Pruitt (1994) in Sari, et al. (2012) is as follows:

$$\text{Tobin's Q} = (\text{MVE} + \text{Debt}) / \text{Total Asset}$$

Independent Variable

The independent variables in this study include:

Tax Risk

According to Turwanto & Irawan (2020), tax risk encompasses all uncertainties related to taxes that surround transactions, operations, financial reporting decisions, and the company's reputation, measured by:

$$\text{TAXRISK} = \sqrt{\ } {}^{1}/_{N-1} \sum^{t}_{i=t-4} (\text{Cash ETR}_i - \text{Cash ETR})$$

Where:

N is the number of years (in this case, 5 years).
Cash ETRi is the cash ETR for year i.
Cash ETR is the average cash ETR over five years.

Leverage

The leverage ratio, also known as the solvency ratio, is an important financial metric for assessing a company's ability to meet its long-term obligations. This ratio measures the proportion of a company's assets that are financed by debt. In other words, the leverage ratio indicates how much debt burden a company carries compared to its total assets (Kasmir, 2016). In this study, leverage is proxied using the Debt to Asset Ratio (DAR). According to Kasmir (2010), DAR is calculated as:

DAR = Total Debt / Total Assets

Moderating Variable

The moderating variable in this study is corporate governance, measured using an index developed by Wulandari & Wahidahwati (2022) based on the research of Klapper & Love (2003) as follows:

TKP = f (DK, M, KA, I).

Where:

DK = Board of Commissioners
M = Management
KA = Audit Committee
I = Investors

Table 1 Corporate Governance Measurement Indicators\

Indicator	Assessment Criteria	Weight
Board of Commissioners	- Size of the Board of Commissioners - Independent Commissioners - Percentage of Ownership - Public Accounting Office	45%
Management	- Size of the Board of Directors - Percentage of Ownership - Affiliation Relationships	20%
Audit Committee	- Size of the Audit Committee - Independent Audit Committee - Area of Expertise	20%
Investors	- Institutional Ownership	15%

Source : Wulandari & Wahidahwati (2022)

Control Variables

This study includes control variables in the analysis to account for other factors that are suspected to influence the dependent variable, namely:

a. Company Size (SIZE) = Ln (Total Assets)
b. ROA = Net Income / Total Assets

Data Analysis Methods

Descriptive Analysis

Descriptive statistics can be defined as a form of data analysis technique used to describe the condition of variables.

Selection of Panel Data Regression Estimation Model

In panel data analysis, there are three main methods used to estimate the regression model: Pooled Least Squares (Common Effect), Fixed Effect, and Random Effect. The selection of the best method for estimating the panel data regression model depends on the characteristics of the data and the research objectives. To determine the appropriate method, model specification tests are necessary, which include the Chow test, Hausman test, and Lagrange Multiplier test.

Chow Test

The Chow test is used to determine the appropriate panel data analysis model. This test helps in choosing between the fixed effect model and the common effect model. If the specification results show a chi-squared probability greater than 0.05, the common effect model is preferred. Conversely, if the chi-squared probability is less than 0.05, the fixed effect model will be selected.

Hausman Test

The Hausman test is used to choose between the fixed effect model and the random effect model. If the chi-squared probability is less than 0.05, the fixed effect model will be chosen.

Lagrange Multiplier Test

The Lagrange Multiplier (LM) test is used to determine whether the random effect model or the common effect model (OLS) is more appropriate. If the test results show a chi-squared probability value greater than 0.05, then H0 is accepted and Ha is rejected, indicating that the common effect model is used. Conversely, if the chi-squared probability value is less than 0.05, then H0 is rejected and Ha is accepted, indicating that the random effect model is chosen.

Panel Data Regression Analysis

The multiple regression model in this study is analyzed using Eviews 9 software. This study utilizes panel data, which is a combination of cross-section data and time-series data. Regression analysis with panel data is necessary to determine the most suitable model for estimating the data, namely: common effect approach, fixed effect approach, and random effect approach. The panel data regression equation in this study is formulated as follows:

$$FV = \alpha + \beta 1RP + \beta 2LEV + \beta 3RP*TKP + \beta 4LEV * TKP + \beta 5UP + \beta 6ROA + \varepsilon$$

Description:

FV = Firm Value
RP = Tax Risk
LEV = Leverage Crime
Scene = Corporate Governance
UP = Company Size
ROA = Return On Asset

Hypothesis Testing

Partial Significance Test (t-Test)

The t-statistic test essentially measures the extent to which explanatory or independent variables affect variation in the dependent variable. One way to conduct a t-test is by comparing the t-statistic values accurately and critically based on the t-distribution table. This test is conducted on both sides with a significance level of 5%. The decision rules for the t-test are as follows:

a. If the significance probability value > 0.05, then H0 is accepted.
b. If the significance probability value < 0.05, then Ha is accepted.

Simultaneous Significance Test (F-Test)

The F-statistic significance test is used to determine whether all independent variables in the model together influence the dependent variable.

a. If the significance value > 0.05, then the conclusion is that H0 is accepted, meaning the independent variables do not simultaneously affect the dependent variable.
b. If the significance value < 0.05, then the conclusion is that Ha is accepted, meaning the independent variables do simultaneously affect the dependent variable.

Coefficient of Determination (R^2) Test

The coefficient of determination (R^2) is used to assess how well the model explains variation in the dependent variable. When additional independent variables are included, R^2 will increase, although this does not always mean that those variables have a significant impact on the dependent variable.

RESULT AND DISCUSSION

Results of Fixed Effect Panel Data Regression Estimation

From the statistical data processing below, the following results of the panel data regression are obtained:

Table 2. Results of Fixed Effect Panel Data Regression Estimation
Dependent Variable: FV
Method: Panel Least Squares
Date: 06/26/24 Time: 16:12
Sample: 2019 - 2021
Periods included: 3
Cross-sections included: 37
Total panel (unbalanced) observations: 99

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	11.92748	4.751094	2.510471	0.0150
RP	5.666414	3.198014	1.771854	0.0819
LEV	-0.446511	1.661927	-0.268671	0.7892
LEV_TKP	2.643253	3.236896	0.816601	0.4176
RP_TKP	-11.86209	6.577071	-1.803552	0.0767
UP	-1.585546	0.688089	-2.304275	0.0249
ROA	2.050564	0.934891	2.193372	0.0324
Effects Specification				
Cross-section fixed (dummy variables)				
Summary Statistics				
R-squared: 0.950694				
Mean dependent var: 1.357244				
Adjusted R-squared: 0.913714				
S.D. dependent var: 0.723306				
S.E. of regression: 0.212467				
Akaike info criterion: 0.038857				
Sum squared resid: 2.527959				
Schwarz criterion: 1.166030				
Log likelihood: 41.07660				
Hannan-Quinn criterion: 0.494913				
F-statistic: 25.70864				
Durbin-Watson stat: 3.220825				
Prob(F-statistic): 0.000000				

Source: Data Regression Data Processing Panel Eviews 9

So the regression equation of panel data is:

$$Y = 11{,}92748 + 5.666414RP - 0.446511LEV + 2.643253TKP*LEV - 11.86209TKP*RP + -1.585546UP + 2.050564ROA + E$$

CONCLUSION

The study examines the impact of tax risk and leverage on firm value, with corporate governance serving as a moderating variable. The findings indicate that tax risk has a positive relationship with firm value, while leverage has a negative relationship with firm value. Corporate governance plays a crucial role in moderating the relationship between these variables, strengthening the positive impact of tax risk on firm value and mitigating the negative effect of leverage. This study highlights the importance of effective corporate governance in enhancing firm value by managing tax risks and controlling the negative aspects of leverage. The results provide insights for companies to focus on improving their governance practices to optimize their value in the eyes of investors. Future research could further explore other moderating factors that may influence the relationship between tax risk, leverage, and firm value.

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