

THE ANALYSIS OF THE CHARACTERISTICS OF EXTERNAL AUDITOR AND AUDIT COMMITTEES: TAX AVOIDANCE

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Abstract

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Companies have an obligation to pay taxes to the state. Tax revenues require supervision to prevent tax avoidance activities. Regulatory gaps governing the tax system and aggressive tax strategies are used by the company to minimize payment of tax costs. The monitoring mechanism to minimize tax avoidance is carried out by auditors. The research objective is to test and provide empirical evidence regarding the characteristic factors of external auditors and the existence of an audit committee that influences tax avoidance. This study uses a quantitative approach. Research data was taken using a purposive sampling technique. The research object is an energy company listed on the Indonesia Stock Exchange, IDX (*Bursa Efek Indonesia*, BEI) with the observation year 2012–2021. The analysis technique uses classical assumption tests, multiple linear regression, and hypotheses testing. The research results show that the length of the audit engagement has a negative influence on tax avoidance. Audit opinions, audit fees, and audit committees have no effect on tax avoidance. The conclusion of this research emphasizes the importance of supervision to control and minimize the negative impact of tax avoidance practices.

Keywords: Characteristics of External Auditors, Audit Opinion, Audit Committee, Tax Avoidance, Corporation

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1. INTRODUCTION

Taxes are an important instrument for state revenue. The tax payment system in Indonesia uses a self-assessment system, that is, taxpayers, both individuals and companies, can fulfill their tax obligations starting from calculating, and paying, to reporting their taxes independently. Indonesia has a State Revenue and Expenditure Budget (*Anggaran Pendapatan dan Belanja Negara*, APBN) for 2021,

with details of state income of IDR 2,011.3 trillion, 76.96% of which comes from taxes with actual tax revenues reaching IDR 1,547.8 trillion (Ministry of Finance, 2022). Indonesia is also estimated to experience losses of US\$4.864 billion, with details of losses of US\$4.785 billion originating from tax avoidance by corporate taxpayers, and the remaining US\$78.831 million originating from tax avoidance by individual taxpayers each year due to tax avoidance practices (Tax Justice Network, 2020). Indonesia had

a tax ratio in 2018 of 10.24%, then it decreased in 2019 to 9.76%, then in 2020 it became 8.33%, and in 2021 it increased to 9.11% (Ministry of Finance, 2023). This ratio shows that Indonesia's state income from taxes is not yet optimal.

The case of tax avoidance that occurred in energy sector companies was the case of PT Adaro Energy Indonesia Tbk reduced the amount of tax by 125 million US dollars from 2009 to 2017 (Global Witness, 2019). In 2019, PT Adaro Energy Indonesia Tbk avoided tax by paying a tax burden of Rp.1.75 trillion less than the tax owed (Kompasiana, 2022). The impact is that state revenues originating from taxation are not optimal. In general, tax avoidance activities do not conflict with tax regulations, but if carried out on a large scale it will have a significant impact on state tax revenues. Tax avoidance practices usually use loopholes that are not regulated by tax regulations.

Tax avoidance activities do not violate tax provisions but are detrimental to the state (Fauzan et al., 2019; Lee & Kao, 2018). Tax avoidance practices can be influenced by internal factors such as company characteristics and corporate governance and external factors such as institutional factors and macroeconomic conditions (Wang et al., 2020). Tax avoidance is a problem related to inadequate transparency and accountability for the imposition of corporate tax costs. The large tax costs can reduce the profits earned by the company. The company has the main goal of maximizing profits, especially for shareholders, and improving the welfare of company management, so the company tries to minimize tax costs through tax avoidance mechanisms.

Tax avoidance also creates legal risks for the company from interested parties because they feel disadvantaged (Donohoe & Knechel, 2014). Efforts to minimize the impact of tax avoidance are by monitoring tax payment activities from the company to the state. Supervision of tax payments can be carried out by internal auditors, audit committees, and external auditors who provide audit services on the company's financial reports. Internal auditors have the duty and authority to carry out evaluations, provide recommendations, monitor follow-up, and provide information on the results of audits carried out within the company (Rodakos et al., 2021; Shahini-Golopeni et al., 2022; Hayek et al., 2022). The audit committee has the task of supervising the company's operational activities. The existence of an audit committee helps companies ensure the quality of financial reports, accountability, and prevention management fraud, thus reducing the emergence of tax avoidance practices.

Audit characteristics describe the characteristics of an auditor seen from the assignment of an independent auditor who has experience in accepting the task of conducting an audit at a company (Cahyadi et al., 2020). Audit characteristics include the audit engagement period, audit opinion, audit fee, and size of the public accounting firm. An auditor who has an audit engagement period of more than one year at a client company will be able to provide better advice to the client company regarding tax issues (Salehi et al., 2020). The audit engagement period is the length of the audit engagement between the independent auditor and the client company (Lestari & Nedy, 2019).

An auditor's engagement period over a certain period will create closeness and a better understanding of the client company's business. On the other hand, this will disrupt the auditor's independence (Lestari & Nedy, 2019). Auditors with inadequate independence will be able to reduce audit quality which is reflected in the audit opinion. Stakeholders consider the audit opinion as a basis for assessing the company's performance. If a company practices tax avoidance, it will reduce the transparency of financial reporting which will lead to the giving of opinions by auditors (Salehi et al., 2020; Riguen et al., 2021). The opinion of Salehi et al. (2020) regarding the length of engagement is the professional attitude of the auditor in carrying out the assignment and completing the audit as stated in the independent auditor's report by providing an audit opinion according to the findings and evidence.

Tax imposition is generally based on profits earned by the company. The company's ability to generate profits is a reflection of the company's financial performance. In general, companies with high-profit levels are owned by large-scale companies. Company size and ability to generate profits (profitability) will influence tax avoidance (Lestari & Solikhah, 2019) because companies prioritize the welfare of shareholders and management. Research conducted by (Fauzan et al., 2019) found empirical evidence of factors that have an influence on tax avoidance, namely audit committee, leverage, return on assets, company size, and sales growth.

It cannot be denied that there is a tax gap that influences tax avoidance and has an impact on audit fees (Kraft & Lapotta, 2016). The company will provide audit service fees in accordance with the assurance services provided by independent auditors (Hu, 2018). Research by (Martinez & Lessa, 2014; Hu, 2018) found that there is a positive relationship between tax avoidance and audit fees. Other research conducted by (Riguen et al., 2021) shows that audit fees have a negative effect on tax avoidance. The amount of the audit fee can vary depending on the assignment, the complexity of the services provided, the level of expertise required to carry out the audit services, and other professional considerations. Determination of the audit fee amount refers to the Decree of the General Chair of the Indonesian Institute of Public Accountants (*Institut Akuntan Publik Indonesia*, IAPI) Number 2 of 2016.

Tax avoidance is part of tax planning by reducing the tax costs paid by the company without violating statutory provisions (Hanlon & Heitzman, 2010). Auditors have an important role in ensuring the quality of financial reports so that companies can carry out their tax obligations without reducing tax costs (Hanlon et al., 2012). In this case, both internal and external auditors play a role in supervising the company's operational activities. This research was conducted to examine in more depth the characteristics of external auditors and audit committees as monitoring mechanisms, and whether they can minimize tax avoidance efforts by the company. This research also uses profitability and company size as control variables for the relationship between the characteristics of external auditors and audit committees on tax avoidance. This research contributes to improving the monitoring system carried out by auditors in reducing tax avoidance practices.

The rest of this paper is structured as follows. Section 2 reviews the relevant literature. Section 3 analyses the methodology that has been used to conduct empirical research on tax avoidance. Sections 4 and 5 provide findings and conclusions subsequently.

2. LITERATURE REVIEW

2.1. Agency theory

In the field of taxation, two parties have very rational interests, namely the company (agent) and the government (principal). Both parties have an interest in gaining profits, namely management tries to eliminate taxes and the government maximizes tax revenues as regulated in the tax law (Ghozali, 2014). To increase state revenues originating from taxation, regulations are established in the context of supervision by optimizing the audit function carried out by external auditors and audit committees within the company.

Tax avoidance is often carried out by management based on personal interests. Tax avoidance will reduce the tax costs paid by the company (Ariff & Hashim, 2014; Annuar et al., 2014). The problem of tax avoidance shows that there are deficiencies in management, related to the lack of transparency in financing the tax burden. Agency theory has helped explain that managers as agents tend to avoid taxes to increase company value and tend not to be transparent in carrying out company operations (Utama et al., 2019).

2.2. Audit tenure and tax avoidance

Audit tenure allows the external auditor to have adequate knowledge of the company's business and industry, including the potential for anything within the company that can be done to avoid taxes (Serafat & Barzegar, 2015). Research by Bae (2017), Lee and Kao (2018), Frey (2018), and Lestari and Nedya (2019) state that the longer the audit engagement period, the higher the level of tax avoidance carried out by a company. Because the longer the engagement period between the auditor and the client company, the independence, integrity, and objectivity will decrease and the quality of the audit will become doubtful, thus providing opportunities for management to take tax avoidance actions (Rizqia & Lastiati, 2021).

H1: There is a positive relationship between auditor tenure and tax avoidance.

2.3. Audit opinion and tax avoidance

In the context of agency theory, agency problems between agents and principals can be minimized by monitoring mechanisms carried out by auditors. The audit process carried out by the independent auditor will produce an opinion and be stated in the independent auditor's report. An audit opinion will add credibility to the company's financial reports because it reflects the auditor's independent attitude toward the company's financial reports (Salehi et al., 2020). Audit opinion is the result of the quality of the auditor's work, one of which is identifying whether tax avoidance has occurred or whether there has been no tax avoidance. Research results from McGuire et al. (2012) and Mehrabanpour

et al. (2017) provide empirical evidence that audit opinions will influence tax avoidance practices. Audit opinions reflect the quality of financial reports and suppress tax avoidance.

H2: There is a positive relationship between audit opinion and tax avoidance.

2.4. Audit fees and tax avoidance

Auditors often use additional audit procedures to minimize the impact of tax avoidance risks. Auditors need more resources and time to carry out the audit process and ensure that the financial reports do not identify tax evasion which will affect the payment of audit fees. Comprehensive examinations carried out by auditors will minimize tax avoidance (Kovermann & Velte, 2019). The results of research by Martinez and Lessa (2014) are that when companies avoid taxes, the company will tend to pay more auditor fees.

H3: There is a positive relationship between audit opinion and tax avoidance.

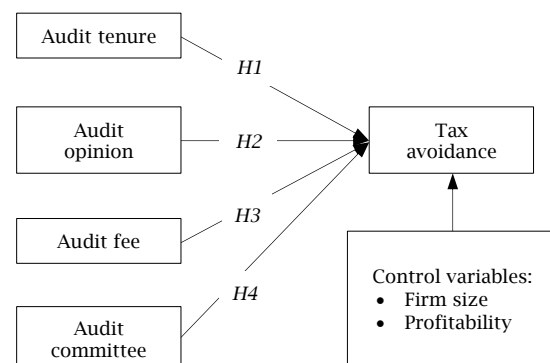
2.5. Audit committee and tax avoidance

Agency theory states that the existence of an audit committee in a company will have an impact on better supervision of company activities and agency conflicts that occur due to management's desire to avoid taxes can be minimized. Companies that have audit committees will be more responsible and open in presenting financial reports. An audit committee that monitors and evaluates company performance effectively will also reduce tax avoidance practices (Richardson et al., 2013; Fauzan et al., 2019; Hsu et al., 2018).

H4: There is a positive relationship between the audit committee and tax avoidance.

Research was conducted to examine the factors that determine tax avoidance practices from the aspects of the characteristics of external auditors and the existence of an audit committee. As part of the implementation of good corporate governance, external auditors and audit committees carry out evaluation, control, and supervision functions over the risk of tax avoidance practices. Company size and profitability were added as control variables in this research. Companies with large sizes tend to have large assets to manage in an effort to generate high levels of profit and have the opportunity to make tax payment obligations efficient through tax avoidance. The research model can be illustrated in Figure 1.

Figure 1. Research model



3. RESEARCH METHODOLOGY

The research is quantitative research that uses company financial data in the company's annual report. The research has a dependent variable, namely *tax avoidance*. The independent variables in

this research are *audit tenure*, *audit opinion*, *audit fee*, and *audit committee*. This research also has two control variables, namely *firm size* and *profitability*. Operational measurement of each variable is provided in Table 1:

Table 1. Operational measurement of the variables

Variable	Definition
<i>Tax avoidance</i>	The ratio of effective tax rate, ETR (Dyreng et al., 2010)
<i>Audit tenure</i>	The number of consecutive years that an audit firm undertakes the responsibility of a company's auditing (Myers et al., 2003)
<i>Audit opinion</i>	It equals one if the auditor issues an unqualified opinion without any additional language and zero otherwise (Jha & Chen, 2014)
<i>Audit fee</i>	The natural logarithm of the total audit fee of the external auditor (Jha & Chen, 2014)
<i>Audit committees</i>	The number of audit committees (Fauzan et al., 2019)
<i>Firm size</i>	The natural logarithm of the total assets of a company (Salehi, Tarighi, et al., 2018)
<i>ROA</i>	Return on assets is calculated by dividing a company's annual earnings by its total assets (Salehi, Tahervafaei, et al., 2018)

The research data is secondary data from annual reports of energy sector companies. The research used a purposive sampling technique. The sampling criteria are 1) energy companies listed on the Indonesia Stock Exchange, IDX (*Bursa Efek Indonesia*, BEI) in 2012–2021; 2) energy companies that publish and publish annual reports during 2012–2021; 3) energy companies did not experience delisting during 2012–2021; 4) energy companies did not experience loss during 2012–2021. Statistical tests include classical assumption tests, multiple linear regression, and hypotheses testing. The research equation is:

$$TAV = \alpha + \beta 1AT + \beta 2AO + \beta 3FS + \beta 4AC + \beta 5FS + \beta 6ROA + \epsilon \quad (1)$$

where, *TAV* = tax avoidance; *AT* = audit tenure; *AO* = audit opinion; *AF* = audit fee; *AC* = audit committee; *FS* = firm size; *ROA* = Return on asset.

4. RESULTS AND DISCUSSION

This research uses annual report data from energy sector companies listed on the IDX for 2012–2021. There were 80 energy sector companies registered during 2012–2021. Fifteen companies in the energy sector experienced delisting and/or suspension on

the IDX, 25 companies experienced losses, eight companies could not access their annual reports and 20 companies had outlier data. The research data uses 12 energy sector companies and the total research data for 2012–2021 is 120.

The normality of the research data was tested using the Kolmogorov-Smirnov test with a significance value of 0.200, which means the data is normally distributed (Table 2). Autocorrelation test using the Durbin Watson statistic with a value of 1.820. The multicollinearity test uses tolerance and VIF values (Table 3). The heteroscedasticity test uses the Glejser test by looking at the significance value of each variable, namely *audit tenure* of 0.815, *audit opinion* with a significance value of 0.489, *audit fee* with a significance value of 0.396, *audit committee* with a significance value of 0.125, *firm size* with a significance value of 0.230 and *profitability* with a significant value of 0.060. It can be concluded that there are no symptoms of heteroskedasticity. Considering the significance value (Table 4), the obtained test significance of 0.000 is smaller than the error rate of 5% ($\alpha = 0.05$). The results of hypotheses testing to see the influence of the characteristics of external auditors and audit committees on tax avoidance are presented in Table 5.

Table 2. Normality analysis using one-sample Kolmogorov-Smirnov test

		Unstandardized residual
N		120
Normal parameters ^{a,b}	Mean	0.0000000
	Std. Deviation	4.82544135
Most extreme differences	Absolute	0.071
	Positive	0.071
	Negative	-0.055
Test statistic		0.071
Asymp. Sig. (2-tailed)		0.200 ^{c,d}

Note: a. Test distribution is normal; b. Calculated from data; c. Lilliefors significance correction; d. This is a lower bound of the true significance.

Table 3. Multicollinearity test

Variable	Tolerance	VIF	Provision
<i>Audit tenure (AT)</i>	0.902	1.108	No symptoms of multicollinearity occurred
<i>Audit opinion (AO)</i>	0.978	1.022	No symptoms of multicollinearity occurred
<i>Audit fee (AF)</i>	0.750	1.334	No symptoms of multicollinearity occurred
<i>Audit committee (AC)</i>	0.876	1.142	No symptoms of multicollinearity occurred
<i>Firm size (FS)</i>	0.804	1.244	No symptoms of multicollinearity occurred
<i>ROA</i>	0.934	1.071	No symptoms of multicollinearity occurred

Note: Data processed in 2024.

Table 4. ANOVA^a

	Model	Sum of squares	Df	Mean square	F	Sig.
1	Regression	459.992	6	76.665	3.169	0.007 ^b
	Residual	2733.308	113	24.189		
	Total	3193.300	119			

Note: a. Dependent variable: ETR; b. Predictors: (Constant), ROA, AO, FS, AC, AF, AT. Data processed in 2024.

Table 5. Hypotheses testing

Variable	Significance	Provision
Audit tenure	0.043	Accepted
Audit opinion	0.887	Rejected
Audit fee	0.606	Rejected
Audit committee	0.239	Rejected
Firm size	0.169	Rejected
ROA	0.001	Rejected

Note: Data processed in 2024.

4.1. Effect of tenure audit on tax avoidance

Audit tenure has a coefficient value of 0.914 with a significance value of 0.043. The first hypothesis is accepted. A long audit engagement relationship between the external auditor and the company will provide a better understanding of the company's industry and business. On the other hand, long audit engagements also threaten the auditor's integrity and objectivity in assessing and monitoring company performance. External auditors will have a close relationship with the client company, thereby providing opportunities for tax avoidance practices. The research supports previous research conducted by Bae (2017), Lee and Kao (2018), Frey (2018), and Lestari and Nedya (2019).

4.2. Effect of audit opinion on tax avoidance

An audit opinion is an assessment of the audit results carried out by the auditor and stated in the independent auditor's report. The test results obtained a significance value of $0.887 > 0.05$. This means that the second hypothesis is rejected, namely, audit opinion has no significant positive effect on tax avoidance. The audit opinion given by the auditor provides information to stakeholders regarding the condition and performance of the company. The implementation of supervision carried out by external auditors is sometimes limited by time so they may not be able to detect tax avoidance activities.

4.3. Effect of audit fee on tax avoidance

Audit fees are the amount of fees received by external auditors for providing audit services to the company. The statistical test obtained a significance value of 0.606 and a coefficient value of 0.330. This means that audit fees do not have a significant positive influence on tax avoidance. The audit process is carried out using audit procedures and requires adequate resource allocation to identify possible irregularities such as tax avoidance. Payment of large audit fees without adequate audit implementation will not be able to detect tax avoidance.

4.4. Effect of the audit committee on tax avoidance

The audit committee is part of the company's governance structure in evaluating and monitoring the company's operational activities. The test results

obtained a significance value of 0.239 and a coefficient value of -1.504. This means that the audit committee does not have a significant influence on tax avoidance. The existence of internal supervision carried out by the audit committee will be able to minimize the negative impact of tax avoidance practices. However, audit committees in companies function more to supervise the company's operations, so they are sometimes unable to control tax avoidance practices.

Large companies will have a lot of encouragement to pay taxes in accordance with statutory regulations. The ability to generate good profits from large-scale companies for management will be used more to improve shareholder welfare and management welfare. As a result, this will make management take steps to avoid tax.

5. CONCLUSION

Taxes are mandatory and compelling contributions for citizens, both individuals and companies, to the state. Tax avoidance by companies will have an impact on reducing state revenues and in the long term will disrupt the state's financial stability. Energy companies are large-scale companies that are capital-intensive and therefore require strict supervision regarding the fulfillment of their tax obligations. Control and supervision mechanisms are needed so that tax avoidance practices do not occur on a massive scale. Optimizing supervision over tax avoidance practices is carried out by external auditors and the audit committee.

Mapping the characteristics of external auditors helps identify dominant factors that can influence tax avoidance practices. The characteristics of external auditors are seen from the length of the audit engagement, audit opinion, and audit fees. The audit committee as one part of the company's governance structure is tasked with evaluating, controlling, and supervising the company's operational and financial activities effectively, thereby minimizing the occurrence of tax avoidance. This research provides empirical evidence in the form of first, audit tenure has a significant positive influence on tax avoidance. Second, audit opinions, audit fees, and audit committees have no effect on tax avoidance. Third, company size in this study does not have a significant influence on tax avoidance. Finally, profitability as a control variable with a proxy for ROA has a significant negative effect on tax avoidance. The limitation of this research is that it only examines the dimensions of tax avoidance supervision carried out by external auditors and audit committees. Research has not looked at the legal risk aspect of tax avoidance by companies. Therefore, it provides future research opportunities to examine aspects of legal risk and supervision of internal auditors to prevent tax avoidance.

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