CONSEQUENCES OF TAX AVOIDANCE

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ABSTRACT

Tax avoidance is part of the tax management practices, carried out by companies in the context of tax savings. The practice of tax avoidance is not done without risk. This study aims to examine the impact of tax avoidance practices on the corporat risk, firm value, and cost of debt. The analysis use literature review method by reviewing the results of previous research in 2019-2022. The synthesis of previous research results shows that tax avoidance increases company risk. Meanwhile, tax avoidance tend to be neutral to the cost of debt.

1. Introduction

State revenues are predominantly from taxes. Taxes contribute more than 80% of state revenue. Data from the Ministry of Finance in 2021 shows that the top contributions are in income tax and value added tax. The Ministry of Finance continues to strive to achieve tax revenue targets through a series of policies. Revenue from taxes is widely used for routine expenses and the development of the state.

Various policies are made by the government to optimize state revenues from the taxation sector. Tax observers state that suboptimal tax revenues are caused by taxpayers who commit tax avoidance . Although taxes contribute to the development of the country, from the perspective of enterprises, it suggests that taxes are an organizational burden that allows for the reduction of an economic benefit. Taxes become a cost that will reduce the company's profits. (Carolina & Handayani, 2019)(Paridah & Rokhayati, 2022)

The effectiveness and efficiency of the management of the company is often associated with maximum profit . To achieve this, the company will increase revenue and reduce expenses, including tax burdens. The company will implement various strategies to reduce the tax burden. One of the mechanisms is through tax avoidance practices. (Hamidah & R, 2022)

Tax avoidance is a legally implemented yang measures to reduce the amount of tax that must be paid. Tax avoidance is part of the tax management practices carried out by companies in the context of tax savings. The emphasis on the minimum amount of tax payable is on targeted profit and

liquidity. In fact, tax avoidance is not only practiced by domestic companies but also widely practiced by multinational companies.

The practice of tax avoidance is not carried out without risks. Although it is distinguished by tax evasion and is carried out legally, it is revealed that there are costs that may arise from the implementation of tax avoidance. These costs include direct costs, reduced company reputation and potential penalties. A company's involvement in tax avoidance practices depends on obtaining benefits that outweigh the consequences of the company. (Chen dkk., 2014)

Various studies related to tax avoidance show that the practices carried out have an impact on the company. Research shows that tax avoidance has a positive influence on company risks. While finding that on the value of the company, tax avoidance actually has a positive influence. But from the creditor side, the practice of tax avoidance still has no visible effect on the cost of debt. Carolina & Handayani, (2019); Dhawan dkk. (2020); Kim from dkk. (2011) Arfiansyah (2020); Dhawan dkk. (2020); and Irawan & Turwanto (2020)(Lee dkk., 2022; Novaria & Habibah, 2022; Main dkk., 2019a)

The large variety of research results regarding the impact of tax avoidance shows that the practices carried out by these companies need to be considered from various aspects. Therefore, this research was carried out with the aim of assessing the consequences of implementing tax avoidance carried out by companies through a *literature review.* Such consequences are focused on the risks of the company, the value of the company and the cost of debt . Through this research, it can provide knowledge to company management in making policies related to taxes and provide views on further tax avoidance research. This research can provide information to managers, investors, lenders, and analysts who regularly evaluate the costs and benefits of corporate tax practices.

2. Theoretical Background

2.1. *Tax Avoidance*

Maximizing profit generation is a company mission, one of which is pursued through tax management. Tax burden is one of the business expenses that will be streamlined in order to achieve the company's mission. There are two basic strategies to minimize tax payments, namely reducing revenue or exaggerating the company's expenses. Tax avoidance is a part of tax planning aimed at regulating in such a way that the payment of taxes by companies is at a minimum. Although it does not violate the applicable tax provisions, the practice of tax avoidance has a negative connotation, especially for the tax office. Tax avoidance efforts made by companies will make state revenues from the sector not optimal.

Tax evasion is not the same as *tax evasion*. The practice of tax avoidance is carried out by taking advantage of legal loopholes due to a scheme or transaction that has not been clearly regulated so that it does not violate the law.   reveals that tax avoidance includes a wide range of tax reduction

activities ranging from tax-advantageous investments to aggressive strategies that may be undertaken if needed. Mardiasmo (2016) provides a definition of tax avoidance as an effort to minimize the tax burden by not violating applicable regulations. Thus tax avoidance is done through the utilization of opportunities in regulatory gaps and grey areas.Dyreng dkk., 2019)

Tax avoidance is carried out in several ways. As stated by Hoque et al (2011), these methods include:

1.) Generating profit from capital is actually the profit from operating activities so that net profit and tax debt are reduced.
2.) Capital expenditures are recognized in operational expenditures.
3.) Personal costs are charged in business costs so that profits look small.
4.) The depreciation and disposal burden of raw materials on the manufacturing industry is exaggerated.

Meanwhile, explaining that tax avoidance has three characteristics stated by the (Finnerty dkk., 2007)*Organization for Economic Cooperation and Development* (OECD), namely (1) the existence of artificial elements carried out due to the absence of tax factors so that there seem to be various arrangements in it when they are not, (2) Utilization of *loopholes* although the intent of the provision maker is not actually as interpreted by the taxpayer, and (3) The secretive nature of the tool or means in the practice of tax avoidance carried out by consultants and taxpayers.

Tax avoidance is seen as an effort made by companies to save taxes. Nevertheless, tax avoidance is not only a financial problem for tax authorities, but also erodes the important common space necessary for the smooth functioning of compliance with regulations, the integrity of the organization and society . Defining tax avoidance as a sustainability issue offers a broader and more holistic understanding of the organizational and societal consequences of tax avoidance behavior.(Bird & Davis-Nozemack, 2018)

2.2. *Company Risk*

Risk is the possibility of adverse conditions occurring. Risk can be interpreted more broadly as an opportunity for an outcome that is not or even the opposite of what is expected. This means risks are related to uncertainty that could have beneficial or detrimental repercussions. All activities carried out by the company contain risks. (Budhijana & Nelmida, 2018)(Siswanti dkk., 2020)

In business activities, risks become natural and unavoidable. For this reason, knowledge about the risks and their types is important to know. Quoted from, there are 7 types of risks according to experts, namely:(Siswanti dkk., 2020)

1.) Strategy risk, which is the risk of uncertainty caused by the lack or immaturity of the strategy carried out by the company.

2.) Legal and compliance risks, namely the risk of financial or reputational losses that arise due to lack of awareness, misunderstanding or confusion and unawareness of applicable laws and regulations.
3.) Operational risk, namely the potential for not achieving the desired results due to systems, resources and technology that are not functioning properly.
4.) Financial risk, which is the risk related to losses due to movements in the financial market.
5.) Reputational risk, which is the risk of achieving company goals caused by positive or negative effects of the company's reputation.
6.) Credit risk, which is the opportunity for failure in the transfer of obligations at maturity.
7.) Market risk, namely the opportunity for changes in financial market sentiment in the form of stocks and applications that result in a fluctuating Net Asset Value (NAV).

Corporate risk is a condition where the company's performance opportunities become less than expected. According to it, the company's risks reflect future uncertainties that must be addressed. This uncertainty relates to any aspect that may cause losses or put the company in an unfavorable state. Tax avoidance can be stated to be one of the factors affecting the risk of the company. But according to tax avoidance shows the risk to the company is not related to the company. Tax avoidance will add to the risks that the company must bear. Guenther dkk. (2017)(Susilawati dkk., 2022) Firmansyah and Febriyanto (2018)

2.3. *Company Values*

Increasing value is one of the missions that the company wants to achieve. The value of the company provides a description of the company's performance so that investors and potential investors can make investment decisions more precisely. The perception of the success of the company is demonstrated through the value of the company. The value of the company is high, so the prosperity received by the owners and shareholders is also high. (Paridah & Rokhayati, 2022)

The stock price is often associated with the value of the company. Through the high value of the company, investors are also willing to pay high to buy shares of the company. That way, the value of the company reflects the transfer price if the company is sold . The indigo of the company is associated also with the image of the company. The value of the company is good, then the image owned is also good.(Arfiansyah, 2020)(Farah Dinah & Darsono, 2017)

The process of maximizing the value of a company can give rise to conflicts of interest between management and shareholders. The difference in interests according to *agency theory* allows for additional costs that can reduce the company's profit and have an impact on the company's stock price so that there is a change in the value of the company. The practice of tax avoidance is carried

out to maximize the company's profits by saving taxes. But on the other hand, tax avoidance carried out by the company can be viewed as an interest by the management which is not necessarily justified by the owners and shareholders as well as potential investors. (Jensen & Meckling, 1976)

2.4. Debt Cost

Debt is one of the main sources of funds obtained from external parties, namely creditors. Companies with one of the sources of funds are from debt, they will be willing to pay interest as a *cost of debt*. Any bank debt or corporate bond will give rise to obligations that must be paid by the company which are referred to as debt costs. External funding from loans will incur debt costs in the form of interest while external funding through bond issuance makes the rate of return expected by bond buyers a debt cost.(P, 2021)

The characteristics and management of the company will have an impact on the cost of debt. The creditor will consider it as a risk and will be charged to the company through interest so that the amount of debt costs also follows . Thus, creditors consider the risks of the company in determining the expected rate of return. The greater the risk of the company, the greater the cost of debt.(Wardani & Rumahorbo, 2018)

The cost of debt is the cost of the company as a tax deduction. In line with the external funding structure and (Princess Setya Goddess & Educate Ardiyanto, 2020)*trade off theory*, companies will be able to lower their taxes through the use of debt. However, the use of high debt can eliminate the benefits of debt as corporate *tax shields*. This is because the cost of debt that arises will also be high when the company uses debt that is too high so that the cost of debt will also increase. In addition, tax avoidance carried out by the company is seen as containing risks by creditors.

3. Methodological Research

This research was conducted through a qualitative approach with *the literature review* method. The method is carried out through the study and synthesis of previous research with the selection of relevant literature, analysis, mapping and interpretation of previous literature. The stages in the *literature review* method are to determine the literature to be reviewed for later analysis and finally map the results of the study.(Sekaran & Bougie, 2016)

The selection of literature is carried out through various sources using *google scholar* to get articles directly or connected to the journal *website* that publishes the article. The search was conducted using the keywords "Tax Avoidance, Corporate Value, Risk, External Funding and Debt Costs" published within the last 4 years. Taking on this time span is carried out so that the latest information can be guaranteed and relevant to current conditions. From the articles generated

through the search, *data screening* is carried out by filtering out irrelevant titles, abstracts and *full text* so that articles that do not match the criteria of the research topic are eliminated. Furthermore, extraction is carried out in the form of a table that presents information on the year of publication, the name of the author, journal publication, article title, variables, objectives, methods, results and conclusions for the implementation of the content analysis of the article.

4. Results and Discussion

4.1. Impact of Tax Avoidance on Corporate Risk

The synthesis of research on the impact of tax avoidance associated with corporate risk resulted in two groups. The first group is the one that concludes that tax avoidance has a positive effect on the company's risk. Meanwhile, the second group, which concluded that it was not clear to what extent tax avoidance increases corporate risk.(Carolina & Handayani, 2019; Dhawan dkk., 2020; Mahdi dkk., 2019)(Hutchens dkk., 2020)

Research conducted by and showing results that the greater the tax avoidance, the company's risk related to stock price volatility will increase. While in research, tax avoidance will increase the risk of bankruptcy of the company. It is good to suggest that there are several reasons tax avoidance can exacerbate risks to companies, namely: (1) tax avoidance practices will make tax authorities distrustful of future corporate tax payments, (2) the magnitude of tax avoidance is often considered a key indicator of corporate investment risk, lastly (3) The use of complex and ambiguous reporting systems on tax avoidance practices will increase the uncertainty of future cash flows companies and reduce information transparency.Carolina dan Handayani (2019)Mahdi dkk. (2019)(Dhawan dkk. (2020)Carolina & Handayani (2019), Dhawan dkk. (2020) And Mahdi dkk. (2019)

Different results regarding the impact of internal control on company risks are shown by research . The results of his research concluded that the extent to which tax avoidance increases corporate risk is unclear, but 19% of his research results show that there is a positive influence of tax avoidance on company risk. Predicted companies showed a positive relationship between tax avoidance and corporate risk experiencing negative tax outcomes over the next three years, including larger payments to tax authorities and more negative tax news coverage.Hutchens dkk. (2020)

Tracing the location, research conducted by carilina and Salehi was carried out in developing countries. Meanwhile, the research conducted by Dhawan used a company registered with Australia Stock Exchage as a sample. Results showing the vagueness of the effect of tax avoidance on company risk were obtained in a sample of companies listed on the America Stcok Exchange. Although it is possible that the application of tax avoidance has no effect on the risks of the company, when a tax inspection occurs, all tax avoidance practices carried out will usually result in a greater tax liability

because the tax inspector corrects the taxpayer's fiscal financial statements. In other words, more and more tax avoidance practices are carried out by companies, increasing the likelihood of re-correction by tax inspectors and resulting in greater tax liability than before. As a result, according to the results of the flow research, the company's cash will also experience some uncertainties related to tax payment obligations.(Guenther dkk., 2017)

4.2. Impact of Tax Avoidance on Corporate Value

The synthesis of research on the effect of tax avoidance on the value of enterprises produced two main groups. The first group is the one that concludes that tax avoidance has a positive effect on the value of the company . Meanwhile, the second group concluded that tax avoidance has noArfiansyah, 2020; Irawan & Turwanto, 2020; Puguh Wibowo dkk., 2022; Warno & Fahmi, 2020) impact on the value of the company by Kalbuana et al 2020; Violeta and Serly 2020; Pertiwi and Prihandiai 2021.

Research conducted by shows that the higher the tax avoidance applied, the higher the value of the company. The emergence of positive influences is supported by the condition of the company with good governance. Tax avoidance by investors is seen as an activity of saving the amount of tax effectively and efficiently thus providing better cash flow that increases the value of the company. Arfiansyah (2020), Irawan & Turwanto (2020), Puguh Wibowo dkk. (2022) and Warno & Fahmi (2020)

Research conducted byKalbuana dkk. (2020), Earth & Prihandini (2021) and Violet & Serly (2020)providing tax avoidance results does not contribute to the value of the company. The rise and fall of the company's value is not influenced by the tax avoidance practices carried out. This condition is based on the argument that the value of the company is not seen from the application of tax avoidance so that it does not change the company's image in the view of investors and stakeholders. In addition, this finding is also supported by research in which issues related to tax avoidance carried out by companies do not have an influence on the company's stock price. This would be different if what emerged was the issue of tax evasion.Blaufus dkk. (2019)

The dominance of the two previous groups of results does not mean that tax avoidance cannot have a negative influence on the value of the company. Research showing that tax avoidance will reduce the value of the company is carried out by . This means that the greater the application of tax avoidance carried out by the company, the value of the company will fall. This condition was discovered through companies with large government ownership on research. Rezki dkk. (2020)Rezki dkk. (2020)

4.3. *Impact of Tax Avoidance on Debt Costs*

An analysis of research into the impact of tax avoidance on corporate debt costs resulted in a predominance of findings of no influence between the two. The research conducted by Novaria & Habibah (2022), Main dkk., (2019), and Zamifa dkk. (2022) gives the result that tax avoidance has no effect on the cost of debt. Meanwhile, although research shows a positive relationship of tax avoidance to the cost of debt, this relationship is not significant. That is, tax avoidance does not contribute to the cost of debt. Musaddad dkk. (2022), Princess Setya Goddess & Educate Ardiyanto, (2020), and Sherly & Fitria (2019)

The absence of the effect of tax avoidance on the cost of debt is reinforced by research showing the result that tax avoidance is positively related to the possible cost of equity rather than the cost of debt. In fact, in line with the external funding structure and Lee dkk. (2022)*trade off theory*, companies will be able to lower their taxes through the use of debt. The cost of debt that arises will also be high when the company uses debt that is too high so that the cost of debt will also increase. Looking at the dominance of research findings, companies that implement tax avoidance mean that they do not have to have a lot of debt. also revealed that there is a possibility that with the tax reforms that began to be launched in 2015, companies are cautious in debt management and use other methods such as Musaddad dkk. (2022), Princess Setya Goddess & Educate Ardiyanto, (2020), and Sherly & Fitria (2019) *transfer pricing* and the use of *tax heaven* as a tax avoidance mechanism.

5. Conclusion

Tax avoidance is one of the mechanisms carried out by companies toreduce taxes but still have a greater profit. Although it does not violate the provisions, the application of tax avoidance to the company has consequences that must be faced. Through this research, it can be concluded that tax avoidance has a tendency to positively affect company risk. Tax avoidance practices will magnify the company's risks related to stock prices and also bankruptcy. It is possible that the implementation of tax avoidance does not have an impact on the risks of the company. However, the occurrence of tax checks may result in greater tax liabilities as a result of fiscal corrections that arise.

From the investor side, through research, it is concluded that tax avoidance can have a positive impact on the value of the company. This is because investors view tax avoidance as part of tax planning to maximize company profits. Other results suggest that no impact will be had by tax avoidance practices on corporate value and debt costs. Although companies can lower taxes through the use of debt, high debt costs will also increase the cost of bankruptcy. Ultimately, companies should pay attention to the acquisition of benefits that outweigh the consequences of implementing tax avoidance. Taxavoidance is indeed a sustainability issue that requires a broader and more holistic understanding of the organizational and societal consequences of the practice.

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