

# DOES MANAGERIAL OWNERSHIP AND ISLAMIC CORPORATE SOCIAL RESPONSIBILITY REDUCE TAX AGGRESSIVENESS?

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**Abstract:** This study aims to test empirically the effect of managerial ownership on tax aggressiveness with Islamic corporate social responsibility as the intervening variable. The populations of this study were all entities listed in Jakarta Islamic Index from 2015-2019. 40 entities were obtained by using purposive sampling technique. All data were analyzed by using multiple linear regression analysis and sobel test. The results showed that managerial ownership has a significant positive effect on Islamic corporate social responsibility. In contrast, managerial ownership has a negative and insignificant effect on tax aggressiveness. Furthermore, Islamic corporate social responsibility has a significant negative effect on tax aggressiveness and Islamic Corporate Social Responsibility is able to moderate the effect of managerial ownership on tax aggressiveness.

**Keywords:** Managerial ownership, Islamic corporate social responsibility, tax aggressiveness, Jakarta Islamic Index

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## INTRODUCTION

Tax aggressiveness is the actions taken by companies to reduce their tax obligations (Dyreg, et al., 2008, 2010; Hanlon and Heitzman, 2010). Usually, companies as corporate taxpayers take advantage of weaknesses contained in tax laws and other regulations. This grey area is used as a gap or regulatory looseness that lies between the practice of planning or calculating permissible and prohibited taxes (Hardeck and Hertl, 2014). The more gaps a company uses to avoid taxes, the company will be more aggressive.

Companies with tax aggressive actions have a higher risk than companies that do not engage in tax aggressive practices (Frank, et al., 2009). This risk is in form of the threat of sanctions or fines. The sanction has an impact on the decline in share prices and the company's reputation. As the result, the company's reputation is not good enough in the eyes of investors (Akhtar, et al., 2019; Tanimura and Okamoto, 2013). On the other hand, company management needs to make company profits small so that the taxes that must be paid are also small. Not only potentially to result losses, the practice of tax aggressiveness also aims to earn profits, such as saving on tax expenditures so that the profits of entrepreneurs are greater. Subsequently, the profit can be used to fund investments which can increase company profits in the future. Meanwhile, for management, tax aggressiveness can increase the compensation received from the owners or shareholders of the company. In fact, there are several factors that can reduce tax aggressiveness, including through managerial ownership and Islamic corporate social responsibility.

Managerial ownership is the shareholder who also acts as the company's owner. The shareholder comes from the management, so that he actively participates in decision making

(Bebczuk, 2005). Share ownership can motivate managers to improve their performance and prosper shareholders so that they can increase company value while maintaining the company's survival. (Hardinata & Tjaraka, 2013) added that it can be realized by disclosing social activities and minimizing tax aggressiveness (Dyrenge, et al., 2010; Rego & Wilson, 2012). Chyz and White (2014) believed that the relation between tax avoidance and the existence of agency conflicts is strongest for firms with low levels of CEO monitoring. On the contrary, Hadi & Mangouting (2014); Jamei (2017); Khan, et al., (2013); Razak & Mustapha, (2013) showed no relationship between managerial ownership and CSR.

Islamic Corporate Social Responsibility (ICSR) is believed to be an appropriate benchmark for CSR disclosure. According to Arshad, et al., (2012) a body that applies sharia-based business is essentially rooted in the philosophy of the Qur'an and Sunnah, so that it becomes the basis for executors when dealing with the environment and society. Al-Qur'an Surat Al-Qashash ayat 77:

“And look for what Allah has bestowed upon you (happiness) of the afterlife, and do not forget your happiness from worldly (enjoyment), and do good (to others) as Allah has done good to you, and do not do anything damage on earth. Surely Allah does not like those who do mischief”.

Islam holds accountability which is comparable in all arrangements and fields, between soul and body, between individual and family, between individuals and social, and between a community with another society (Darmawati, 2014). Social responsibility states about obligations industry in order to protect and convey participation to society where the industry is located.

Prior literature shows mixed results in terms of the association between CSR and tax avoidance. For instance, Col and Patel (2016); Lanis and Richardson (2012a); Lin, et al., (2017) find that firms disclose CSR activities to hedge against the reputational risks of tax-avoidance practices. In contrast, Hoi, et al., (2013); Huseynov and Klamm, (2012); Lanis and Richardson (2012, 2015) showed that company with high CSR disclosure engage in lower level of tax avoidance. Rudyanto & Pirzada (2020) argued that CSR can moderate between tax avoidance and firm value. Based on the variation of prior studies' findings regard the link between ownership structure, CSR and tax avoidance, this study investigates whether the ICSR disclosure can moderate the association between managerial ownership and tax aggressiveness.

## LITERATURE REVIEW

### Agency Theory

Agency theory describes the relationship between the principal (company owner) and the agent (company management) (Jensen & Meckling, 1976) which can trigger agency conflicts. The behavior of managers / agents acts only to benefit them by violating the interests of other parties / owners. This happens because the manager has complete information about the company, while the information is not owned by the owner of the company (in this case asymmetric information arises). Asymmetric information and self-serving behavior to managers / agents enable them to make decisions and policies that are less beneficial to the company. It results unhealthy corporate governance because there is no openness from management to disclose the results of their performance to the principal as the owner of the

company. Agency theory analyzes and seeks solutions to two problems that arise in the relationship between principals and agents.

### **Sharia Enterprise Theory**

Triyuwono (2015) stated that sharia enterprise theory is a theoretical concept that recognizes accountability not only to the owner of the company but to a wider stakeholder group. Shari'ah enterprise theory states that corporate stakeholders are not only humans and nature around them, but also Allah SWT. God is the last center of responsibility for all activities in the world (Triyuwono, 2015). The link between this concept and Islamic Corporate Social Responsibility is the perspective of resources by the company, as a mandate from God that is inherent in a responsibility. Indriastuti & Najihah, (2020) argued that corporate social activity is a form of compliance and responsibility of the company owner for his beliefs, in order to maintain and share with the surrounding. It is a way to contribute to the good of all those who need it.

### **Tax Aggressiveness**

Hoffman (1961) defined tax aggressiveness as “the taxpayer's ability to organize his financial businesses in such a way as to suffer a minimum tax liability. Frank, et al., (2009) claimed that tax aggressiveness is an act of reducing payable tax through a tax planning, whether permitted by the tax regulations or not. Taxes paid by the entity represent transfers of the entity's assets to the government which are deemed as burdensome to the entity. Therefore, the entity has a tendency to avoid / save taxes as efficiently as possible (Dyrenge, et al., 2018).

### **Managerial Ownership**

Managerial ownership is the shareholder who also acts as the owner of the company from the management, so that they actively participate in decision making (Khan, et al., 2013). Share ownership can motivate managers to improve their performance and prosper the shareholders, so that they can increase company value while maintaining the company's survival. Furthermore, (Hardinata & Tjaraka, 2013) stated that it able to minimize the occurrence of tax aggressiveness.

### **Islamic Corporate Social Responsibility (ICSR)**

Arshad, et al., (2012) explained that Islamic Corporate Social Responsibility (ICSR) concepts consist of the concept of zakat, justice, benefit, responsibility, and falah (success). The disclosure index used in this study was Islamic Social Reporting (ISR) disclosure index compiled by Othman, et al., (2009). It covers six disclosure themes including; finance and investment, products and services, employees, society, environment, and corporate governance.

### **Managerial Ownership and Islamic Corporate Social Responsibility**

Managerial ownership can align differences in interests between principals and agents in order to minimize the opportunistic behavior (Jensen & Mecking, 1976). Managers will strive to improve their performance and prosper the shareholders so that they can create a good image. This has an impact on company value while maintaining the survival of the company (Hardinata & Tjaraka, 2013). The Islamic corporate social responsibility disclosure is one of the efforts of a manager. Managers do not only care about themselves but also care about the

social and surrounding environment, which is ultimately a form of responsibility to Allah SWT. The higher the managerial ownership, the higher the level of corporate social responsibility disclosure (Jo & Harjoto, 2011). First hypothesis:

H<sub>1</sub>: Managerial ownership has a positive effect on Islamic corporate social responsibility

### Managerial Ownership and Tax Aggressiveness

Managerial ownership of shares makes management more careful in making decisions (Jensen & Mecking, 1976), because whatever decisions are made by management, the management will also feel the impact of the decisions. In addition, the management will also bear losses for decisions made if the decisions are not correct. Apart from being careful in making decisions, management will also be more active in fulfilling shareholders' interests and eliminating agency problems. The high level of managerial ownership makes the company more compliant with the applicable tax laws and practices a bit tax. Thus it can balance the interests of both parties when making decisions to set taxes (Chyz and White, 2014). Consistent with (Dyrenge, et al., 2010; Rego & Wilson, 2012). Chyz and White (2014) that managerial ownership can reduce tax aggressiveness. Second hypothesis:

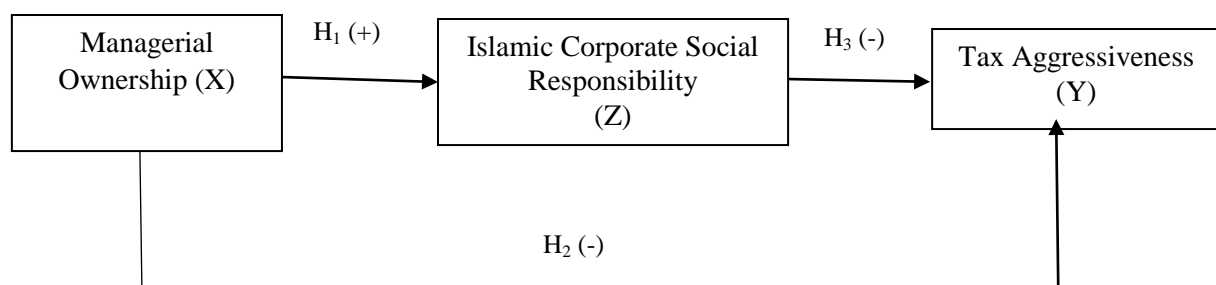
H<sub>2</sub>: Managerial ownership has negative effect on tax aggressiveness.

### Islamic Corporate Social Responsibility and Tax Aggressiveness

Islamic corporate social responsibility (ICSR) is a disclosure of social responsibility carried out by companies. It is also a form of responsibility to Allah SWT and stakeholders (Hadi, 2016). The ICSR disclosure is a form of communication between the company, the community and the surrounding environment. It aims to attract public and investor trust that the company does not act a tax aggression. The more disclose ICSR activities of a company, the less tax aggressiveness they take (Alsaadi, 2020). This is in accordance with the sharia enterprise theory. It states that the practice of ICSR disclosure is not only done to create a good response from the community but also as a form of responsibility to Allah SWT. In other words, everything that is done will be accounted for at the end of the day. By this belief, the entity will not carry out tax aggression intentionally or unintentionally, because they know that they are being watched by Allah SWT. Moreover, a positive response from the public can foster good value for entities in the public which not only has an impact on the profit that continues to increase. (Lanis and Richardson, 2012) argued that it also adds blessings to the entity itself. (Hoi, et al., 2013; Huseynov and Klamm, 2012; Lanis and Richardson, 2012b, 2015) showed that companies with high CSR disclosure engage in lower level of tax avoidance. Third hypothesis:

H<sub>3</sub>: ICSR has negative effect on tax aggressiveness

Figure 1: Research Model



## METHOD

The populations in this research were all entities listed in Jakarta Islamic Index from 2015-2019. The sampling used purposive sampling method with criteria: (1) entities registered in Jakarta Islamic Index during the observation period; and (2) entities that have a complete annual report related to research variables. Based on the criteria, the number of samples during the observation period was 40 entities (8 entities x 5 years). The independent variable of this study is managerial ownership, whereas the dependent variables are tax aggressiveness and Islamic corporate social responsibility as an intervening variable. Managerial ownership is the amount of share ownership by the company's managerial compared to the total outstanding shares (Jensen & Mecking, 1976). Islamic Corporate Social Responsibility (ICSR) is the responsibility of organizations that run their businesses based on sharia on the Qur'an and Sunnah (Arshad, et al., 2012). ICSR measurement used a ratio between the number of ICSR disclosed items and the total number of ICSR items (Arifin dan Wardani, 2016). The ICSR measurement scale used a ratio scale that has an absolute zero and has the same distance. Tax aggressiveness is an entity's move to reduce the payable tax either legally or illegally (Frank, et al., 2009). ETR is used to measure a company's ability in reducing its relative tax payments to profit before tax (Lanis and Richardson, 2012b; Ying, 2011).

The data analysis technique in this research used multiple linear regression analysis and sobel test (Ghozali, 2016). The regression equation is as follows:

$$\begin{array}{lll} \text{ICSR} & : \alpha + b_1\text{MO} + e & \text{Model .....(1)} \\ \text{TA} & : \alpha + b_1\text{MO} + b_2\text{ICSR} + e & \text{Model .....(2)} \end{array}$$

Information :

ICSR : Islamic Corporate Social Responsibility

TA : Tax Aggressiveness

MO : Managerial Ownership

b1, b2 : Coefficient

e1, e2 : Error of term

## RESULT

### Descriptive Statistic

The results of descriptive statistical calculations in managerial ownership, Islamic corporate social responsibility, and tax aggressiveness are shown in table 1.

Table 1: Descriptive Statistic

	N	Minimal	Maximal	Mean	Deviation Std.
Managerial Ownership	40	,00001	,90530	,10122	,37647
ICSR	40	,26435	,56138	,32375	,17424
Tax Aggressiveness	40	-,49526	,72821	,11895	,37363

Source: SPSS Output (2020)

Managerial ownership variable has the lowest value = 0.00001; highest value = 0.90530; mean = 0.10122 with a standard deviation of 0.37647. The mean below the standard deviation indicates that the managerial ownership data is unstable (a deviation occurs). ICSR with ICSR DI proxy has the lowest value = 0.26435; highest value = 0.56138; mean = 0.32375 with a standard deviation of 0.17424. The mean above the standard deviation indicates that the ICSR data is stable (no deviation occurs). Tax aggressiveness with ETR

proxy has the lowest value = -0.49526; highest value = 0.72821; mean = 0.11895 with standard deviation = 0.37363. The mean below the standard deviation indicates that the ETR data is unstable (a deviation occurs).

### Classic Assumption Test

A good regression model must fulfil the absence of classic assumption problem. The results of classic assumption test are presented in table 2.

Table 2: The Results of Classic Assumption Test

Model	Dependent Variable	Independent Variable	Normality Test		Multicollinearity Test		Heteroscedasticity Test (Glejzer Test)		Auto Correlation Test (Run Test)
			K-S	Sig	Tolerance	VIF	t	Sig	Sig
Model 1	ICSR	Managerial Ownership	0.202	0.771	1,455	4.339	.466	0.322	.146
Model 2	Tax Aggressiveness	Managerial Ownership	0.177	0.642	1,662	5.911	.661		.255
		ICSR			1,883	3.445			

Source: SPSS Output (2020)

Table 2 shows the results of classic assumptions test for each variable. Kolmogorov Smirnov value shows a significance value of 0.202 and 0.177. It means that the data is normally distributed. Muticollinearity test results show that all variables have met the multicollinearity criteria with a tolerance value higher than the default standard value for 0.10 and the VIF value showed lower than 10. Heteroscedasticity test results show a significance value above 5%. It can be interpreted that there is no heteroscedasticity problems in the effect of managerial ownership and ICSR variables on tax aggressiveness. The autocorrelation test results of model 1 and 2 show that run test sig values are .146 and .255. This means that regression models 1 and 2 have no autocorrelation problem because the asym sig value is more than 5%.

### Multiple Linear Regression Analysis

The results of multiple linear regression analysis tests that include the coefficient of determination test results and t test results can be seen in table 3.

Table 3: The Results of Multiple Linier Regression

Model	Unstandardized Coefficients	t	sig	Decision
1. Managerial Ownership	0,275	3.866	0.000	H1 Accepted
Dependent Variable: ICSR F count = 5.844; sig 0.004 Adjusted R square = 0.211				
2. Managerial Ownership	-0,122	-0.269	0.072	H2 Rejected
ICSR	-1,693	-2.991	0.001	H3 Accepted
Dependent Variable: Tax Aggressiveness F count = 6.551; sig 0.002 Adjusted R square = 0.343				

Source: Regression estimation output (2020)

**Model 1**, managerial ownership variable has t count = 3.866 and sig t = 0.000 < 0.05, which means that managerial ownership has a significant positive effect on ICSR or **H1 is accepted**. **Model 2**, the managerial ownership variable has t count = - 0.122 and sig t = 0.072 > 0.05, it

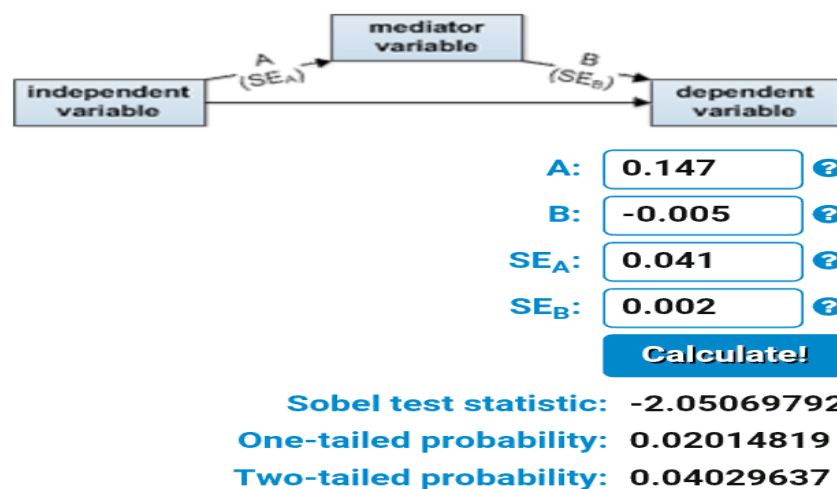


means that managerial ownership has a negative and insignificant effect on tax aggressiveness or **H2 is rejected**. The ICSR variable has t count = -2.991 and sig t = 0.001 < 0.05, which means that ICSR has a significant negative effect on tax aggressiveness or **H3 is accepted**.

### Sobel Test

The sobel test is used to analyze the mediation between exogenous and endogenous variables (Ghozali, 2016). Mediation calculations used a calculation for the sobel test. The test criteria; if the statistical value > 1.96 and the significance value < 0.05, it can be an intervening variable. The following is the sobel test result for the ICSR variable which moderates the effect of managerial ownership and tax aggressiveness.

Figure 2: Sobel Test – Managerial Ownership and Tax Aggressiveness through ICSR



The Sobel test statistic is -2.050 and the two-tailed probability is 0.040 < 0.05. It means, ICSR can be an intervening variable between managerial ownership and tax aggressiveness.

## DISCUSSION

### Managerial Ownership and Islamic Corporate Social Responsibility

Managerial ownership has a significant positive effect on ICSR. It means, the more managerial ownership that the manager has, the more ICSR activities will be disclosed. This is because the ICSR disclosure is not only a form of concern for the environment and society but also as a form of responsibility to Allah SWT as a faithful and pious servant of Allah who is able to invite goodness and stay away from His prohibitions (amar ma'ruf nahi mungkar). The principles of sharia in running a business related to CSR are protecting and preserving the environment, trying to alleviate poverty, clean up from something dirty, bring greater benefits, honesty and trust. In the context of sharia enterprise theory, ICSR activities are a need that is not only oriented for the short term, but also for the long term to achieve the pleasure of Allah SWT. Moreover, economic activities are not only related to material aspects, but also the quality of faith in Allah SWT.

The research results are in line with Agustia, et al., 2018; Jo & Harjoto, 2011) that managerial ownership can increase the number of CSR disclosures. Otherwise, (Khan, et al., 2013; Razak & Mustapha, 2013) showed no relationship between managerial ownership and CSR.

## **Managerial Ownership and Tax Aggressiveness**

Managerial ownership has a negative and insignificant effect on tax aggressiveness. These results indicate that the size of the share ownership owned by the manager has no effect on tax aggressiveness. This is due to the dual role of the managers so that there are two interests that must be fulfilled. In addition to increase bonuses, managers who act as shareholders also want high dividends. Thus, managers will be more careful in making decisions, because whatever decisions are made by management, management will also get the impact of these decisions. In addition, the management will also bear losses if the decisions are not correct. (Jensen & Mecking, 1976).

Managerial ownership does not significantly affect tax aggressiveness, because share ownership by managers is too small as indicated by a percentage of less than 1% (Timothy, 2010). Uniamikogbo, et al., (2019) reinforced the findings that ownership structure has a negative and insignificant effect on tax aggressiveness. On the contrary, Chyz and White, (2014); Dyreng, et al., (2010); Halioui, et al., (2016); Rego & Wilson, (2012) found that corporate governance structure has a significant negative effect on tax aggressiveness.

## **Islamic Corporate Social Responsibility and Tax Aggressiveness**

Islamic Corporate Social Responsibility has a significant negative effect on tax aggressiveness. The increase of ICSR disclosure can reduce tax aggressiveness. This is because the ICSR obligations carried out by entities registered in Jakarta Islamic Index are in accordance with the sharia enterprise theory. In this theory, the practice of ICSR disclosure is not only conducted to create a good response from the community but also as a form of responsibility to Allah SWT. In other words, everything that is done will be accounted for at the end. With this belief, the entity will not carry out tax aggression intentionally or unintentionally.

The ICSR disclosure is a form of communication between the company, the community, and the surrounding environment in order to attract public and investor trust. It is a proof that the company does not act tax aggression, so that it does not only affect profit but also creates a good reputation in the eyes of the public. Indeed (Lanis and Richardson, 2012) explained that it adds blessings for the entities. This research results are inconsistent with Madarina & Ardiyanto (2019) who concluded that CSR has positive and significant effect on tax aggressiveness. In contrast, Alsaadi (2020); Luke & Zulaikah (2016); Huseynov and Klamm (2012); Lanis and Richardson (2012b); Hoi et al. (2013); Lanis and Richardson (2015) found that companies with high CSR disclosure engage in lower level of tax avoidance.

## **CONCLUSION**

Managerial ownership has a significant positive effect on ICSR, but has a negative and insignificant effect on tax aggressiveness. Islamic corporate social responsibility has a significant negative effect on tax aggressiveness and ICSR is able to moderate the effect of managerial ownership with tax aggressiveness. The limitation of this study is that the ability of the independent variable to explain the dependent variable is still below 50%, namely 21.1% and 34.3%. Therefore, the further research can add other variables which can reduce tax aggressiveness (such as: company size, leverage, and others) as well as expanding other research objects. This research contributes to the importance of adopting managerial ownership and ICSR as a company strategy in reducing acts of tax aggression without violating tax laws. Second, the findings of this study can be used by the government as a



reference for formulating regulations related to tax aggressiveness. Third, for investors it can be used as a guide for making investment-related decisions.

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