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THE IMPACT OF FINANCIAL DISTRESS, THE COVID-19 PANDEMIC, AND CORPORATE GOVERNANCE ON TAX AVOIDANCE: EVIDENCE FROM INDONESIA

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Abstract: This study examined how corporate governance, the COVID-19 pandemic, and financial distress affected tax avoidance. The proportion of independent directors, the size of the audit committee, and the educational backgrounds of the audit committee and independent directors in accounting and finance were all considered as corporate governance criteria. The study used data from manufacturing companies listed on the Indonesia Stock Exchange (IDX) from 2017 to 2022. A total of 336 data samples were collected using the purposive sampling method. The research methodology involved multiple regression analysis using STATA. The results showed that financial distress and the number of audit committee members did not impact tax avoidance. However, the impact of the COVID-19 pandemic increased tax avoidance actions. The proportion of independent commissioners and the educational background of the audit committee related to accounting and finance were found to decrease tax avoidance efforts. In contrast, independent commissioners' educational backgrounds in accounting and finance increased tax avoidance efforts.

Keywords: *Financial Distress, Tax Avoidance, Corporate Governance*

1. INTRODUCTION

This research aims to provide empirical evidence regarding things that can encourage companies to avoid taxes, including financial distress conditions, the COVID-19 pandemic situation, and the role of corporate governance. During a company financial crisis, companies seek ways to maintain and restore company finances by organizing and determining company strategies,

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including those related to the company's tax burden. Companies that should pay taxes consider taxes to be a burden because they cause the company's profits to decrease, which will cause the company to make smaller profits (Pratomo & Rana, 2021).

Because companies and the government have distinct objectives, many Indonesian enterprises avoid fulfilling their commitments (Kurniawan et al., 2021). By reducing tax obligations, the companies usually ensure that its profits rise further (Rani, 2017). Actions to minimize tax burden payments of course involve tax management carried out by companies to maintain their tax obligations at a minimum level (Chytis et al., 2020).

The Covid-19 pandemic has significantly impacted the company's economy, and the pandemic has influenced how consumers behave. Changes in consumer behavior have caused companies to experience decreased revenues, reduced sales, and decreased company production levels (Lahmiri & Bekiros, 2020). In contrast to the COVID-19 pandemic, which is caused by external factors of the company, the financial distress situation is a financial situation of the company that is facing difficulties and cannot be detected directly by the company due to internal factors of the company itself, such as errors in company policy in making decisions by company management, and of course, this alone can have a severe impact, such as bankruptcy on the company (Annisa et al., 2022).

So that companies are not involved in tax avoidance efforts, the way that companies can do this is by implementing good corporate governance (Nugroho et al., 2020). Companies that implement good governance will have an impact on the policies taken by the company, one of which is related to tax avoidance efforts (Silvera et al., 2022). Kurniawan et al. (2021) prove that companies with good corporate governance principles will experience growth and development without deviating from government regulations.

Independent commissioners and audit committees are mandatory components that companies must have as part of good corporate governance. The existence of appropriate educational backgrounds related to accounting or finance for independent commissioners and audit committees has been proven to be able to assist independent commissioners and audit committees in determining decisions related to company financial matters (Dwiharyadi, 2017). With an educational history related to accounting and finance, independent commissioners can ensure company management complies with applicable laws and accounting standards and evaluate the company's financial performance by providing advice (Demerjian et al., 2020). Meanwhile, the audit committee, with an educational history related to accounting or finance, can critically evaluate and detect fraud related to the company's financial reporting. Therefore, the duties, roles, and educational history of independent commissioners and audit committees are very important in supervising and controlling company management to prevent companies from committing tax avoidance (Sari et al., 2018).

2. LITERATURE REVIEW

This research discusses the relationship between financial distress and corporate tax avoidance when a company is experiencing financial difficulties and the risk of bankruptcy. In that case, it will encourage company management to take aggressive tax avoidance actions to maintain the company's existence (Nugroho et al., 2020). With financial conditions currently in crisis, company management will take action that can save the company from bankruptcy by reducing the company's burden, such as reducing tax payments to survive (Ariff et al., 2023). When a company is experiencing financial difficulties, it will be difficult to fulfill its financial obligations, so the company will try to maintain its finances by reducing cash outflows, such as tax payments.

H_1: Financial distress has a positive effect on tax avoidance

The impact of the COVID-19 pandemic has encouraged companies to determine alternatives by trying to carry out tax planning by minimizing tax payments to maximize profits by paying lower taxes (Tasios et al., 2022). Managers manage their income during this period to reduce losses and defend the company's finances from financial pressure (Efendi, 2021; Septiawan et al., 2021). By minimizing tax payments, companies can continue to increase revenue and improve their business performance.

H_2: The COVID-19 pandemic had a positive influence on tax avoidance efforts

Under Indonesia Financial Services Authority (OJK) regulations, it is stated that the percentage of independent commissioners on the board of commissioners is at least 30% (Pandapotan & Nurlis, 2023). The proportion of independent commissioners increasing indicates that the supervisory function of independent commissioners is getting better, so company management can act more carefully in making decisions and take reasonable consideration to minimize company management's actions to commit irregularities such as tax avoidance practices (Pratomo & Rana, 2021). Apart from minimizing tax avoidance practices, by increasing the proportion of independent commissioners, company management performance can be improved optimally and effectively, as well as increase the company's finances (Rani, 2017). Previous research from

Rahma and Firmansyah (2022) found that the influence of the proportion of independent commissioners in a company can weaken tax avoidance efforts.

H_3: The proportion of independent commissioners has a negative influence on tax avoidance

The presence of an audit committee can minimize tax avoidance efforts, and it has a role as a corporate governance supervisor who assists the board of commissioners (Pandapotan & Nurlis, 2023). Apart from ensuring financial reports, the audit committee can review mistakes made by management if management has the intention of carrying out tax avoidance efforts (Pratomo & Rana, 2021). The responsibility and authority of the audit committee in the corporate governance system is to ensure that the company's operational activities are carried out ethically and morally by tax regulations (Palupi et al., 2021). This result is in line with Yuliani et al. (2021), who explain that with an audit committee, the company can review its operational and internal activities to inform and provide input to its management. To carry out its functions and roles, the audit committee requires many members because the larger the number of audit committee members, the tighter and more effective the control and supervision function will be on company management, especially on tax avoidance practices (Palupi et al., 2021).

H_4: The number of audit committee members negatively influences tax avoidance.

To carry out his role and duties as an independent commissioner, an educational history related to accounting and finance is required to be able to carry out his duties in supervising company management processes and activities effectively, productively, and professionally (Mardjono & Chen, 2020). With an educational history related to accounting and finance, independent commissioners can be wiser in making and determining appropriate and effective decisions to help company management deal with serious problems (Sumartini, 2020). Independent commissioners with an educational history in accounting or finance can impact management strategies in managing the company so that it complies with established provisions (Rahma & Firmansyah, 2022). This indicates that independent commissioners with an educational background in accounting and finance can have better knowledge of managing company tax risks and limit potential acts of accounting manipulation related to tax avoidance efforts implemented by company management (Astutik & Venusita, 2020).

H_5: The educational background of independent commissioners related to accounting or finance negatively influences tax avoidance.

The audit committee's educational background is essential in supervising company management because, with its educational history related to accounting and finance, it can control company management decisions and strategies (Abdeljawad et al., 2023). Audit committees with an educational history in accounting and finance tend to be more thorough in investigating aggressive accounting decisions, so their educational history can help improve the monitoring of financial information and control the company's tax risk management (Deslandes et al., 2020). The responsibility of the audit committee in carrying out corporate governance is to verify that the company has implemented policies with the relevant provisions and regulations in the field of accounting and finance; therefore, it is necessary to select an audit committee that has education in the field of accounting and finance to be able to monitor the actions of the company's management. To prevent tax evasion (Dang & Nguyen, 2022). This condition indicates that an audit committee's educational history related to accounting or finance can prevent company management from committing tax avoidance (Lim-U-Sanno et al., 2023).

H_6: The audit committee's educational background related to accounting or finance has a negative influence on tax avoidance

3. METHODOLOGY

The empirical model applied is using multiple linear regression and is based on the following mathematical model equation:

ETRi,t = α_0+ β_1Zi,t + β_2COVID19i,t+ β_3KOMINDi,t + β_4KAUDi,t + β_5KIDUi,t + β_6KAUDi,t + β_7LVRGi,t+ β_8FSi,t + β_9ROAi,t +β_{10}CIi,t + ε

Z	:	Financial Distress using Altman Z Score 1968 (***Z = 1.2X1 + 1.4X2 + 3.3X3 + 0.6X4 + 1X5)***
COVID19	:	Dummy Pandemic (1 if year 2020, 2021, 2022; 0 if others)
KOMIND	:	The proportion of independent commissioners is measured by comparing the number of independent commissioners with the number of commissioners in the company)
KAUD	:	number of audit committee members in a company's annual reports
KIDU	:	Dummy (1 if the independent commissioner has an educational background in accounting or finance; 0 if others)
KADU	:	Dummy (1 if the audit committee has an educational background in accounting or finance; 0 if others)

LVRG : Ratio of total debt to total equity

FS : Natural logarithm of Total assets

ROA : Ratio of net income to total assets

CI : Ratio of Total fixed assets to total assets.

The research samples were obtained from manufacturing companies listed on the Indonesian Stock Exchange. Initially, 165 companies were included in the study. However, 72 of these companies incurred losses between 2017 and 2022, 31 did not publish complete financial reports during the same period, and 6 did not make tax payments. This left 56 companies suitable for the research sample. Financial data spanning 6 years (2017-2022) was collected from these 56 companies for analysis. The table 1 below outlines the sample selection method:

Table 1: Purposive Sampling

Detail	*Total*
Observations of Manufacturing Companies Listed on the Indonesia Stock Exchange (IDX)	165
Less:	
Companies that experienced losses during the period 2017-2022	(72)
Companies that did not publish complete financial reports during the period 2017-2022	(31)
Companies that did not make tax payments during the period 2017-2022	(6)
Total companies available for sampling	56
Number of samples used (period 2017-2022)	336

4. STUDY FINDINGS

4.1. Descriptive statistics

Based on the descriptive statistics results as presented in table 2 for the independent variable financial distress, the sample of manufacturing companies in this study is safe from bankruptcy and in good financial condition. The average value of variable Z is 8.7938, which is entirely above the 2.99 limit in the Altman Score to determine a healthy company.

The second independent variable used in this research is the COVID-19 pandemic. For the COVID-19 variable, a dummy variable indicator is used, where a value of 0 indicates that it is not included in the year of the COVID-19 pandemic, and a value of 1 indicates that it is in the year of the COVID-19 pandemic. The average value of COVID-19 is 0.3333, which means that most of the samples used in this study were from the year before the COVID-19 pandemic.

The other independent variable is corporate governance with a proxy for the proportion of independent commissioners (KOMIND), with the lowest value based on the descriptive statistics results table being 0.125 for three consecutive years, namely 2020, 2021, and 2022, where the proportion is below 30% of the specified criteria—determined by OJK. Meanwhile, the maximum KOMIND value is 1, meaning that a company has independent commissioners and a board of 3. It has met the criteria for the proportion of independent commissioners set by the OJK.

The KIDU variable, which measures the educational history of independent commissioners in accounting and finance, shows that, on average, companies have one independent commissioner with an educational background in accounting and finance. However, some companies still need independent commissioners with this background.

In the KAUD variable (number of audit committees), companies have three audit committees following OJK regulations on average. Although there are still companies with only one audit committee person, there are also companies with five audit committee members. Some companies have audit committees that are also independent commissioners. On the other hand, the KADU variable (audit committee educational history in accounting or finance) shows that, on average, companies have two audit committee members with an educational background in accounting or finance. At least in every company, there is one audit committee with an educational background appropriate to their profession.

Table 2: Descriptive statistics

Variable	*Obs*	*Mean*	*Std. Dev.*	*Min*	*Max*
ETR	318	0.2700174	0.1265518	0.0147	0.9712
Z	318	8.793823	2.151832	6.0523	23.234
COVID19	318	0.3333333	0.4721076	0	1
KOMIND	318	0.4314945	0.128576	0.125	1
KAUD	318	3.0208333	0.2831284	2	5
KIDU	318	1.217262	0.9193442	0	4
KADU	318	2.511905	0.6779081	1	4
LVRG	318	0.7331199	0.6738476	0.0025	6.0745
FS	318	15.27604	1.782834	11.5109	19.8937
ROA	318	0.0884829	0.0816825	0.0001	0.5267
CI	318	0.3793568	0.1853659	0.001	0.7812

4.2. Analysis

4.2.1. Pearson correlation

The Pearson correlation values for the variables in this study are shown in table 3 below, and the regression results are shown in table 4.

Table 3: Pearson correlation result

Variables		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
(1)	ETR	1.0000									
		336									
(2)	Z	-0.1910 *	1.0000								
		0.0004 ***									
		336	336								
(3)	COVID 19	-0.0993 *	-0.0682	1.0000							
		0.0689 *	0.2126								
		336	336	336							
(4)	KOMIND	-0.0176	0.2935 *	0.0113	1.0000						
		0.7481	0.0000 ***	0.8365							
		336	336	336	336						
(5)	KAUD	-0.0606	0.0309	-0.0298	-0.0023	1.0000					
		0.2679	0.5723	0.5865	0.9670						
		336	336	336	336	336					
(6)	KIDU	-0.0301	-0.0383	0.0390	0.4018 *	0.1316 *	1.0000				
		0.2679	0.5723	0.4765	0.0000***	0.0158 **					
		336	336	336	336	336	336				
(7)	KADU	0.1179 *	-0.0801	0.0062	0.0295	0.2242 *	0.4293 *	1.0000			
		0.0308 **	0.1426	0.9096	0.5904	0.0000 ***	0.0000 ***				
		336	336	336	336	336	336	336			
(8)	LVRG	0.0216	0.2014 *	-0.0372	0.2178 *	0.1253 *	0.3337 *	0.1550 *	1.0000		
		0.6930	0.0002 ***	0.4967	0.0001 ***	0.0216 **	0.0000 ***	0.0044 ***			
		336	336	336	336	336	336	336	336		
(9)	FS	-0.1167 *	0.0460	0.0340	0.1791 *	0.3068 *	0.2121 *	-0.0307	-0.0772	1.0000	
		0.0325 **	0.4008	0.5348	0.0010 ***	0.0000 ***	0.0001 ***	0.5851	0.1581		
		336	336	336	336	336	336	318	336	336	
(10)	ROA	-0.2730 *	0.8470 *	-0.0370	0.2442 *	0.0529	-0.0505	-0.0931 *	0.0383	0.0863	1.0000
		0.0000 ***	0.0000 ***	0.4988	0.0000 ***	0.3335	0.3557	0.0883 *	0.4841	0.1143	

4.2.2. Regression analysis of financial distress on tax avoidance

Based on the results of the hypothesis test on H1 regarding the correlation between financial distress and tax avoidance efforts, it states that financial distress has no impact on tax avoidance efforts. This is in line with Pandapotan and Nurlis (2023), who said that if a company experiences financial distress, it is not sure that it will take tax avoidance efforts because tax avoidance actions are not the right solution, so the company's finances can recover still if the company takes tax avoidance actions. In that case, this can cause other problems for the company, such as damage to the company's reputation, which can have more fatal consequences for the company's finances. Based on the explanation above, when a company is faced with a financial crisis such as financial distress, it will look for a more ethical and safe solution for the company in recovering the company's finances rather than carrying out actions that deviate from and violate ethical principles, such as tax avoidance efforts. Suppose a company carries out deviant actions, such as attempting to avoid taxes. In that case, it can damage the company's reputation and reduce the trust of stakeholders in the company, which can worsen the company's condition and make the company's finances increasingly difficult. The company will use wiser steps to align with corporate values and social responsibility.

4.2.3. Regression analysis of the effect of the Covid-19 pandemic on tax avoidance

Based on the hypothesis test results on H2 regarding the relationship between the COVID-19 pandemic and tax avoidance efforts, it is stated that the COVID-19 pandemic supports tax avoidance efforts. This is in agreement with Tasios et al. (2022), Wicaksono and Adi (2023), and Supriyati and Hapsari (2021), who state that if a company is in a COVID-19 pandemic situation, it will experience a decline in income, resulting in a decline in their finances, causing Companies are looking for solutions in trying to maximize their revenue by minimizing tax payments, and to reduce company tax payments, companies are taking advantage of the tax incentives provided by the government during the COVID-19 pandemic so that this means company profits do not decrease. Based on the explanation above, if a company is facing the COVID-19 pandemic situation, it will experience a decline in revenue and sales. This will impact the company's finances, which will decline. This will be burdensome for the company in terms of operational costs, so the company will look for solutions to minimize operational costs by reducing the tax burden.

Apart from that, companies also take advantage of tax incentives provided by the government to carry out tax avoidance actions.

4.2.4. Regression analysis of the effect of the proportion of independent commissioners on tax avoidance

Based on the hypothesis test results on H3 regarding the correlation between the proportion of independent commissioners and tax avoidance efforts, it states that the proportion of independent commissioners in a company can reduce the company's efforts to avoid tax. This is following research by Egbunike et al. (2021), Pandapotan and Nurlis (2023), Pratomo and Rana (2021), and Rani (2017), which states that the role and mechanism of independent commissioners is significant in controlling and supervising company management so that they do not do anything—deviant ones such as tax avoidance efforts. To carry out their duties effectively, of course, a large proportion of independent commissioners can help tighten supervision of company management, which has an impact on company performance becoming more transparent. Based on the explanation, independent commissioners need many members to carry out their supervisory and control roles over company management. This is so that independent commissioners can handle problems and provide solutions with different perspectives and expertise in handling and evaluating wiser and ethical tax strategies following applicable tax regulations. In addition, a large proportion of independent commissioners can ensure and monitor company management policies in making decisions so that company management does not take deviant actions and cause internal conflict within the company.

4.2.5. Regression analysis of the effect of the number of audit committees on tax avoidance

Based on the hypothesis test results on H4 regarding the correlation between the number of audit committee members and tax avoidance efforts, it states that the number of audit committee members has no impact on tax avoidance efforts. This agrees with (Yuliani et al., 2021), which states that the number of audit committee members does not affect tax avoidance efforts because it is not sure that the more the number of audit committee members, the more influential the audit committee's supervisory role will be on company management in minimizing tax actions. Avoidance. This is also following Dang and Nguyen (2022), who state that if the number of audit committee members is too large, it can reduce the effectiveness of the audit committee because it becomes difficult for each member of the audit committee to express their respective opinions in the limited time during board meetings so that the impact could hamper the audit committee's ability to respond quickly to immediately required actions such as in dealing with corporate tax avoidance efforts. Based on the explanation above, carrying out the role of the audit committee effectively is not based on many members, and this, of course, could be less effective in the audit committee's function in reviewing errors and monitoring the transparency of company management in carrying out company financial reporting. So, with less effective roles and functions, company management can take advantage of the opportunity to perform deviant actions.

4.2.6. Regression analysis of the effect of educational background of independent commissioners in accounting and finance on tax avoidance

The results of the hypothesis test on H5 regarding the correlation between the educational background of the independent commissioner concerned and the field of accounting and finance support the occurrence of tax avoidance actions. This is in line with Hsu et al. (2018) and Oktaviani et al. (2022), who states that the educational history of independent commissioners related to the accounting and finance sector has a positive impact on tax avoidance efforts because, with a history of accounting and finance education, independent commissioners can tend to see tax efficiency as an essential element in managing company finances so that they are more proactive and encouraged to look for more aggressive tax strategies to benefit the company. Based on the explanation above, with his educational history related to accounting and finance, independent commissioners will tend to take tax avoidance actions to minimize company tax payments and maximize company profits by using opportunities so that company finances can continue to run smoothly in the long term.

4.2.7. Regression analysis of the effect of audit committee educational background in accounting and finance on tax avoidance

Based on the results of the hypothesis test on H6 regarding the correlation between the educational background of the audit committee concerned and the field of accounting and finance, it weakens the company's efforts to avoid tax. This is in line with the research of Abdeljawad et al. (2023), Deslandes et al. (2020), Dang and Nguyen (2022), and Lim-U-Sanno et al. (2023), which states that audit committees can use their knowledge from a history of accounting or financial education to controlling decisions from company management in the financial reporting process so that company management takes action following policies and regulations. In addition, with a history of education in the field of accounting or finance, the audit committee can understand the principles of ethical taxation critically so that it can supervise and limit company management who are encouraged to carry out unethical actions such as carrying out tax avoidance efforts. Based on the explanation above, it can be concluded that the audit committee, with its educational history in accounting and finance, can understand and identify deviant actions carried out by company management in carrying out financial reporting, such as carrying out tax avoidance actions that are not following ethical principles so that the audit committee can prevent and direct company management to carry out tax strategies that comply with ethics.

Table 4: Regression result

$$\mathbf{ETR}i,t = \alpha_0 + \beta_1 Zi,t + \beta_2 COVID19i,t + \beta_3 KOMINDi,t + \beta_4 KAUDi,t + \beta_5 KIDUi,t + \beta_6 KAUDi,t + \beta_7 LVRGi,t + \beta_8 FSi,t + \beta_9 ROAi,t + \beta_{10} CIi,t + \varepsilon$$

	Expected Hypothesis s	*Coefficient*	*Std. error*	*t-value*	*p-value*	*Sig (One-Tailed)*
Z	(+)	0.0047777	0.0062455	0.77	0.2225	
COVID19	(+)	-0.0270565	0.013988	-1.93	0.027	**
KOMIND	(-)	0.1100773	0.060947	1.81	0.036	**
KAUD	(-)	-0.0181563	0.0256977	-0.71	0.240	
KIDU	(-)	-0.019524	0.0093663	-2,08	0.019	**
KADU	(-)	0.0261397	0.0115545	2.26	0.012	**
LVRG		0.0052263	0.011218	0.47	0.321	
FS		-0.0038777	0.0041458	-0.94	0.175	
ROA		-0.5516619	0.1585379	-3.48	0.0005	***
CI		0.0418053	0.0369819	1.13	0.1295	
CONS		0.2908397	0.100964	2.88	0.002	
Observations		336				
Number of Firms		56				
Fixed Effects?		Firm, Year				
Clustered Standard Error		Firm				
***p<0.01, **p<0.05, *p<0.1						

Sources: Data is processed using STATA version 17

5. CONCLUSIONS AND RECOMMENDATIONS

5.1. Conclusions

This study aims to understand how two different factors, internal financial distress and the external impact of the COVID-19 pandemic, affect a company's tax avoidance strategies. Data from the company's annual reports and the S&P

Capital IQ database will be analyzed to explore the effects of these conditions over various periods. The study also looks at the influence of key elements of corporate governance, such as the proportion of independent commissioners, the number of audit committee members, and the educational background of these individuals in accounting and finance, on the company's tax avoidance practices. Although this research shows that financial distress conditions do not impact tax avoidance efforts, the difficult conditions presented by the COVID-19 pandemic have been proven to increase tax avoidance efforts by companies. The results also show that corporate governance components, such as the proportion of independent commissioners, can reduce companies' efforts to avoid tax. However, the number of audit committees does not show a similar impact. Educational history also influences the company's efforts to avoid taxes, whereas the academic history of independent commissioners in accounting and finance can increase the company's tax avoidance efforts. On the other hand, the audit committee's educational history related to accounting and finance can reduce the company's efforts to do so—tax avoidance.

5.2. Practical implications

For regulatory agencies, this research practically emphasizes the relevance of corporate governance through the presence of parties capable of independently monitoring the policies adopted by the corporation. Nonetheless, it is imperative to take into account the educational background that can function as a primary criterion for the audit committee and independent commissioners. This is to ensure that the company strikes a balance between its responsibilities to stakeholders, specifically the government, and its comprehension of its adopted policies.

5.3. Limitations

Because this research focuses on manufacturing companies, it is not possible to extend the findings to other industries. The COVID-19 pandemic is included in the study's coverage period of 2017 to 2022; therefore, the effects of each variable may change over time. The information is derived from publicly validated annual reports of businesses that are listed on the Standard & Poor's Capital IQ (S&P Capital IQ) database and the Indonesia Stock Exchange (IDX). Multiple linear regression was employed by the researcher to examine the relationship between independent and dependent variables. In addition, financial distress was measured and calculated using the 1968 Altman Z-Score approach.

5.4. Recommendations

To observe corporate governance's indirect impact, it is recommended that the sample size be expanded, the research period extended, and moderating variables from the corporate governance component be incorporated.

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Conflict of Interest

There is no conflict of interest involved in the publication of this paper

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