EFFECTIVENESS OF THE SUPERVISION OF COMMISSIONERS AND AGRESSIVE TAX ON FINANCIAL REPORTING FRAUD

[a]Wiralestari
[b]Riski Hernando

Abstract

This study aims to test the effectiveness of commissioner supervision and aggressive tax on financial reporting fraud. This research was conducted at manufacturing companies listed on the Indonesian stock exchange. The research sample was conducted using a random sample and obtained as many as 61 samples of manufacturing companies from 155 total manufacturing companies listed on the Indonesia stock exchange. The results of the study showed that the effectiveness of commissioner supervision and aggressive tax had an effect on financial reporting fraud.

Keywords: Commissioners, Agresive Tax, Financial Reporting Fraud

INTRODUCTION

Tax is a compulsory contribution to the state that is owed by an individual or entity as a taxpayer by not receiving direct, compelling, and reciprocal reciprocity based on the law. The government uses taxes to carry out national development in order to achieve general welfare in various sectors of life (Rochmat Soemitro, 2011).

Taxpayers in Indonesia can be divided into two, namely individual taxpayers and corporate taxpayers. For taxpayers, tax is a manifestation of service and a role to contribute to increasing national development (Rochmat Soemitro, 2014). Based on data from the Ministry of Finance of the Republic of Indonesia (2018), the manufacturing industry is an industry that contributes the largest tax revenue (30.03%). The manufacturing industry experienced the largest growth in industrial sectors, namely 17.1% in 2017 (Airlangga Hartaro, 2018). According to the law, the government uses taxes to carry out national development in order to achieve general welfare in various sectors of life (Rochmat Soemitro, 2011).

Indonesia adheres to a self-assessment system where this system provides convenience to taxpayers, but this convenience is used by taxpayers to carry out tax avoidance according to or contrary to applicable tax regulations called aggressiveness tax or aggressive tax (Frank et al. 2009). Furthermore Frank et al. (2009) said that aggressive tax actions can be carried out by manipulating corporate taxable income through tax planning, both using legal (tax avoidance) or illegal (tax evasion) methods.

The Association of Certified Fraud Examiners (ACFE) (2018) places the manufacturing industry in the first position of the industry that was disadvantaged caused by the fraud in Asia Pacific financial reporting with a percentage of 17% with a total of 33 cases of fraudulent financial reporting. The impact caused by the fraud, the manufacturing industry suffered an average loss of US $ 500,000 (US $ 500,000).

Financial reporting fraud occurs because the company minimizes the amount of tax paid, namely minimizing the value of taxes while adhering to the applicable tax regulations (tax avoidance) or minimizing the value of taxes by taking actions that are not in accordance

[a]Universitas Jambi, Indonesia, e-mail: wiralestari11@unja.ac.id
[b]Universitas Jambi, Indonesia, e-mail: riskihernando@unja.ac.id

with tax laws (tax evasion) (Brian and Martani, 2014). Chen et al. (2010) say that company owners tend to prefer company management to take aggressive tax actions. Aggressive tax action is an action aimed at reducing taxable income through tax planning using either classified or not tax evasion methods (Frank et al. 2009). Although not all actions taken violate the rules, but the more loopholes used by the company, the company is considered to be more aggressive (Dewi Kartika Sari and Dwi Martani, 2010).

Richard Susilo (2017) stated that based on a survey conducted by Ernesto Crivelly, companies in Indonesia were ranked 11th out of 30 countries that carried out aggressive taxation by not paying taxes to the Indonesian Tax Service at 6.48 billion US dollars. According to Imanul Hakim (2018) revealed that there are four industrial sectors in Indonesia that are prone to tax evasion through transfer pricing. The four sectors are mining, plantations, electronics and automotive. One of them is, the case of transfer pricing as an act of conducting aggressive taxation occurs at PT. Toyota Manufacturing Indonesia, resulting in a state loss of IDR 1.2 trillion.

Dhaliwal et al. (2004) argue that company managers see the tax department as a profit center that is responsible for increasing the company's cash flow through aggressive tax reporting and managing income through estimated tax costs. Therefore, consistent with this view, it can be expected that companies can be aggressive both in their financial and tax reporting (Frank et al. 2009). This causes managers to exploit complex tax avoidance strategies, to reduce taxes to divert company resources, which they then hide by distorting the company's financial statements (Desai and Dharmapala, 2006). Frank et al. (2009) prove that there is an influence of aggressive tax on financial reporting, where aggressive tax implies the existence of hidden information so that it has the effect of fraud

In running the company, a supervisory function is needed where the supervisory function is carried out by the board of commissioners. The public oversight board (1995) in America stated that the board of commissioners played an important role in the financial reporting process. The board of commissioners has the duty to oversee the financial reporting process so that it can produce financial reporting with good quality. Corporate governance describes the procedures for improving the quality of financial statements, has an emphasis on the role of the board of commissioners in suppressing earnings manipulation and in convincing that providing appropriate information about the company's operations.

Based on the description above, the researcher is interested in conducting research on "The Effectiveness of Commissioner Supervision and Aggressive Tax on Financial Reporting Fraud".

LITERATURE REVIEW

Financial Reporting Fraud

AICPA (2002) defines financial reporting fraud as an intentional misstatement or negligence in the amount or disclosure in financial statements designed to harm the users of financial statements. ACFE (2010) defines financial reporting fraud as an action taken by officials intentionally on material information with the aim of covering up the actual financial condition of the company and will provide an advantage for those who commit fraud, where this fraud can be financial and non-financial.

Board of directors is the basic mechanism of effective corporate governance, both for public companies and ordinary companies that function to control management actions and prioritize the interests of shareholders (Fama and Jensen, 1983). The board of commissioners can be effective in conducting supervision if they have competence, where important competencies are knowledge of company affair and knowledge of the company's management process, adequate boarding education background will greatly determine the quality and expertise, knowledge and processing of company information, number of members in board of commissioners (number or number of members) in the company as well as the activeness of board members in conducting activities and frequency of meetings (Cadbury, 1992 and Beasley, 1996). Carcello et al. (2002) suggest that board members who have more experience make it possible to demand high-quality audit work. In addition, commissioners who have financial / accounting expertise, they can understand and resolve financial statement problems.

In addition, Carpenter and Feroz (2001) argue that board members with international experience are individuals who have more value. International experience of board members can be obtained through international assignments / experience working in foreign companies. The habit of working in a foreign company that is likely to be influenced by culture, rules, laws / regulations and regulations in the country where this company operates has an impact on them to conduct supervision effectively so as to reduce the level of fraud in financial reporting.

In this study the effectiveness of the board of commissioners can be seen from four dimensions, namely: 1) competence, in competence seen from two indicators namely expertise in the field of accounting / finance / auditing and international experience. 2) the interaction of commissioners and directors and committees viewed from the frequency of meetings / meetings conducted in a year, and 3) human resources seen from the number of independent commissioners owned.

H1: The effectiveness of commissioner supervision affects the financial reporting fraud

Aggressive tax is an action that aims to reduce taxable income through tax planning using either methods classified or not classified as tax evasion (Frank et al. 2009). In this case, the company considers the tax as a cost so that efforts or strategies are needed to mitigate taxes (Mangoting, 1999 in Ida Farida et al. 2018). Dyreng (2009 in Ida Farida et al. 2018) revealed that companies make higher financial reporting choices when they face violations of debt agreements. They pay taxes on these profits to avoid costs associated with violating the debt agreement. Frank et al. (2009) argue that companies that commit financial reporting fraud are involved in tax aggressiveness, they find that there is a significant and positive relationship between accounting fraud and tax aggressiveness. On the other hand, Lennox et al. (2013) provide evidenced that companies that are aggressively taxing tend to commit fraudulent reporting.

In this study aggressive tax is seen from Effective Tax Rates (ETR), which is calculated by dividing the income tax expense with pre-tax profit. The use of ETR is expected to be able to provide a comprehensive picture of the tax burden that will have an impact on accounting profits that can be seen in the notes to the company's financial statements

H2: Aggressive tax has an effect on financial reporting fraud

RESEARCH METHODS

Research method is a method used by researchers during an investigation to solve problems (Kothari, 2004: 08). While Jujun Suriasumantri (2010: 328) states the research method is the methods used in research. The research methods used in this study will be explained as follows:

a. Judging from the purpose of the study, this research is descriptive, namely a study that aims to explain the characteristics of research variables (Sekaran and Bogie, 2010: 105).
b. Viewed from the type of study, this type of research is verificative and explanatory or causal, because this study wants to find the cause or causal relationship of one or more problems as stated in the formulation of the problem (Sekaran and Bougie, 2010: 165).
c. In terms of time horizons, this study belongs to a cross-sectional study group. Because in a cross-sectional studies study / research conducted by collecting data only once, it is possible to be daily, weekly, or monthly, in order to answer research questions (Sekaran and Bogie, 2010: 119).

Population and Sampling

The population in this study is a manufacturing company listed on the Indonesia Stock Exchange, with the target population in this study being manufacturing companies listed on the Indonesia Stock Exchange in 2017, where the target population according to Sekaran and Bougie (2013: 245) is defined as part of the element, geographic circle, and time. The number of manufacturing companies listed on the Indonesia Stock Exchange is 155 manufacturing companies listed on the Indonesia Stock Exchange.

The sample according to Sekaran and Bougie (2010: 263) is explained as part of the population. The sampling method used is Propability sampling. The technique used is Random Sampling, so that 61 manufacturing companies are listed on the Indonesia Stock Exchange.

Operational Variable

Table 1: Operational Variable

Variable	Dimension	Indicator	Scale
Effectiveness of Commissioner Supervision (X1)	Competence	1. Accounting / Financial / Auditing Expertise 2. International Experience	Ordinal
	Interaction with Directors and Committees	Frequency of meetings held during the year	Ordinal
	Human Resources	Independent Commissioners Owned	Ordinal
Aggressive Tax (X2)	*Effective Tax rates* (ETR)	$\frac{\text{Income Tax Expanse}}{\text{Pre-Tax Income}}$	Ratio
Financial Reporting Fraud (Y)	Disclosure of Financial Reporting Fraud	The amount of Financial Reporting Fraud Reported for a year	Nominal

FINDINGS

This study has a profile of respondents which can be seen from the table below:

Table 2: Respondent Profile

Gender	Man	30%

	Woman	70%
Age	< 35 Years Old	11%
	35 – 45 Years Old	80%
	>45 Years Old	9%

The Effectiveness of Commissioner Supervision affects the Financial Reporting Fraud

From the results of data processing using hierarchy regression modeling, the results obtained from the effectiveness of supervisory supervision of financial reporting fraud. This means that the effective supervision of the commissioners owned will reduce the level of financial reporting fraud.

This shows that the knowledge and experience of commissioners is an important element in ensuring the effectiveness of the board's oversight function. Carcello et al. (2002) suggest that board members who have more experience make it possible to demand high-quality audit work. In addition, commissioners who have financial / accounting expertise, they can understand and resolve financial statement problems.

Carpenter and Feroz (2001) argue that board members with international experience are individuals who have more value, are rare, and have unmatched characteristics that can contribute to the competitive advantage of companies that use their experience. International experience of board members can be obtained through international assignments / experience working in foreign companies. These people are shown / shown to the organization's management in financial information and also in the preparation of financial statements and also shown in monitoring activities in an organization by foreign companies.

The habits of the company may be influenced by culture, rules, laws / regulations in the country where the company operates. This exposure and experience can help board members manage the complexity associated with earnings management practices. Simultaneously, with international experience that is different from local experience, it is also believed that board members like this will assist in promoting and implementing preventive actions and mechanisms for earnings management more proactively in the organization. Furthermore, with frequent meetings between commissioners and directors and committees, it can also reduce the occurrence of financial reporting fraud, this is because the commissioners pay more attention and provide advice on the solutions that occur (Cadbury, 1992).

Aggressive Tax has an effect on Financial Reporting Fraud

Processing data using hierarchy regression modeling, the results of aggressive tax regression obtained on financial reporting fraud are positive. This means that doing aggressive tax indicates financial reporting fraud.

This is in accordance with the results of the research conducted by Dyreng (2009 in Ida Farida et al., 2018) that companies make higher financial reporting choices when they face violations of debt agreements. They pay taxes on these profits to avoid costs with violating the debt agreement. Frank et al. (2009) argue that companies that commit financial reporting fraud are involved in tax aggressiveness, they find that there is a significant and positive relationship between accounting fraud and tax aggressiveness. On the other hand, Lennox et al. (2013) provide evidence that companies that are aggressively taxing tend to commit fraudulent reporting.

Companies that have low ETR (effective tax rate) will try to increase ETR by reducing profits because companies tend to want small accounting profits to avoid the possibility of high tax payments in the future so that the company can carry out policies on accruals contained in the deferred tax expense is to make the deferred tax expense smaller. Deferred tax expense is a multiplication of temporary differences with the applicable tax rate (Harnanto, 2003).

DISCUSSIONS

The results of this study result that:

a. The effectiveness of commissioner supervision has a significant effect on financial reporting fraud. This shows that commissioners who have expertise in accounting, auditing, finance and international experience can reduce financial reporting fraud actions and the more frequently held meetings make the commissioners better understand the problems that occur within the company and can provide appropriate solutions.
b. Aggressive taxes have a significant effect on financial reporting fraud. This shows that companies make higher financial reporting choices when they face violations of debt agreements. They pay taxes on these profits to avoid costs associated with violating the debt agreement

RECOMMENDATIONS

a. To fulfill the characteristics of scientific research, namely replicability and generalizability, it is recommended for other researchers to conduct research again by adding other variables that are thought to have an effect on financial reporting fraud such as the board of directors, audit committee, internal audit objectivity, red flag.
b. The next researcher can conduct research with different populations and samples and using a qualitative approach.

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