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## The Effect of Multi-nationality, R&D Costs, and Institutional Ownership on Tax Avoidance

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### Abstract

This study aims to examine the effect of multi-nationality, research & development costs and institutional ownership on tax avoidance. Manufacturing companies listed on the Indonesia Stock Exchange in the period 2018 to 2023 are the unit of analysis in this study. The purposive sampling method is used to select the appropriate sample, while the multiple regression method is used to analyze the hypothesis on 100 panel data. The results of this study indicate that multi-nationality and research & development costs have no significant effect on tax avoidance, while institutional ownership has a positive effect on tax avoidance. These results contribute to government policy in analyzing taxpayers with institutional share indicators.

### Keywords

*Multinationalism, Development Costs, Institutional Ownership, Tax Avoidance*

## 1. Introduction

Taxes are the most important source of government revenue in Indonesia. In terms of expenditure, Indonesia still relies on tax revenues to finance spending needs and the implementation of development. This is in line with the main function of taxes, namely as a budget (budgetair) which serves to finance various state expenditures. In Indonesia, taxes are the largest input and contribution to the State Budget (APBN), for example in 2023, the contribution of taxes to state income and expenditure reached 80% or the equivalent of 2,118 trillion. Tax revenue in Indonesia in the last 4 years has indeed increased. However, this amount is not optimal considering that Indonesia's tax ratio is still below the average standard set by Asia-Pacific and OECD. According to the Organisation for Economic Co-Operation and Development (OECD, 2023), Indonesia's tax-to-GDP ratio increased by 0.8 per cent from 10.1% in 2020 to 10.9% in 2021. However, the ratio is still below the Asia and Pacific average (19.8%) of 8.9% and still far below the OECD average (34.1%) of 23.2%. This means that Indonesia's tax revenue is still not optimal and needs to be pushed again if it wants to seriously increase the tax ratio (OECD, 2023b). OECD (2023) revealed that the tax ratio in Indonesia is the lowest when compared to the tax ratio of neighboring countries including Papua New Guinea, Malaysia and Singapore and other Asian countries.

This shows that Indonesia still has low tax revenue performance compared to neighbouring countries as shown in the following figure. In our state budget report, there are several sectors that are the main tax contributors to the state, namely the manufacturing industry, trade, financial services and insurance, construction and real estate, mining, information and communication, transportation and warehousing, corporate services. One of the companies that contribute mainly to state revenues are companies in the manufacturing sector. In 2020, the tax contribution from the manufacturing sector was 28.9%, in 2021 it was 29.9% and in 2022 it was 29.1%, while for 2023 as of October 2023 it was 27.3%. It was mentioned that this year the percentage of national revenue experienced a positive growth of 6.7%, but the growth was still far below the growth of the manufacturing sector tax in the same period last year, which was 13.4% in October 2022, meaning that the contribution of the manufacturing sector to tax revenue weakened.

On the other hand, to optimise tax revenue in Indonesia, the Government is trying to issue policies that can increase tax revenue. However, in reality there are still many obstacles faced by the Indonesian government to collect taxes. The obstacle faced is that there are still many Corporate Taxpayers who are reluctant to pay taxes because taxes are a cost that can reduce profits for the company and there is no direct reciprocity felt by the company. The form of reluctance carried out by taxpayers is reflected in tax avoidance actions. Pohan (2019), Tax Avoidance is a tax avoidance effort that is carried out legally and safely for taxpayers because it does not conflict with tax provisions whose purpose is to reduce the amount of tax payable. Kasim & Saad (2019) reveal that tax avoidance occurs because there is an intention of the taxpayer to minimise taxes by implementing a tax planning mechanism. Tax avoidance practices can be carried out by all companies with various methods as long as they do not violate tax provisions, but tax avoidance actions have now received attention and spotlight by the government and the Directorate General of Taxes as the authority in charge of supervising tax obligations. If there is no policy firmness against tax avoidance, Indonesia will experience a loss of tax revenue that should be used for the public interest.

The Tax Justice Network Report in The State of Tax Justice 2020: Tax Justice in the time of Covid 19, Indonesia experiences a loss of 4.78 billion US Dollars or the equivalent of Rp. 67.6 trillion each year due to tax avoidance practices carried

out by corporations in Indonesia (O'Hare, 2020). Furthermore, in 2019, there was a case of tax evasion committed by PT Bentoel Internasional Investama. In the Tax Justice Network report (2019), it was stated that the Indonesian cigarette production and distribution company, PT Bentoel Internasional Investama, which is a subsidiary of British American Tobacco (BAT), had committed tax evasion in Indonesia. as a result, Indonesia lost \$14 million in revenue. Another tax evasion case was conducted by Google Asia Pacific Pte Ltd. Google conducted a tax avoidance strategy by utilising the physical presence requirement. The practice of tax avoidance carried out by Google is not an open secret anymore, some countries such as the United States and the United Kingdom have provided policies where Google will pay taxes even though its income is transferred to tax haven countries. The form of tax problems on Google is that they do not build a Permanent Establishment (PE), where PE is a requirement for countries to be able to tax. Although in Indonesia it does not establish a PE, Google has a branch in Singapore to manage its business around Asia. In Indonesia itself, Google only established a marketing representative office where the establishment is not included in the BUT category, for this reason it is difficult for the state to pursue taxes and Google feels that it is not physically present besides that contract transactions by consumers are also online. From the above cases, it is said that tax avoidance arises one of them because of the multi-nationality factor.

Multinational companies are companies whose private, public ownership is built in various countries and each other exert influence on the activities of other individuals including resources and other knowledge. Multinational companies are seen as having greater opportunities to avoid taxes by applying aggressive tax planning techniques such as exploiting any loopholes in tax laws to gain tax advantages from mismatches between a country's tax regulations to minimise their tax burden (Kasim & Saad, 2019). Multinational companies conduct tax avoidance by lowering the tax burden through lower effective tax rates and profit shifting methods (Koivisto et al., 2021). Another potential tax avoidance is through research and development (R&D) costs. These costs are incurred in order to acquire intangible assets. According to PSAK 19 Revised (2015) Paragraph 51, states that sometimes it is difficult to determine whether an internally generated intangible asset meets the criteria for recognition. The difficulty arises because it must determine whether an identifiable asset has arisen, and when it arises, that will generate future economic benefits and determine the cost of the asset reliably.

Therefore, paragraph 52 states that in determining whether internally generated intangible assets meet the requirements for recognition, an entity classifies the process of generating assets into two stages, namely the research stage or research stage and the development stage. Furthermore, the company must be able to distinguish between the research and development stages. If the company cannot distinguish between the research stage and internal development to produce an intangible asset, then the company treats the expenditure for the project as if it were an expenditure incurred only at the research stage. Expenditure incurred during the research stage without any development should not be recognised as an intangible asset. Research expenditure is recognised as an expense when incurred and can be expensed to calculate taxable income. The transaction allows the company to take tax avoidance measures. Lee (2019) states that companies tend to take advantage of research and development costs to reduce taxes and perform tax avoidance by utilising research and development (R&D) accounting policies. Components in research and development are costs, so companies may fully finance research and development costs in their gross income in the year the costs are incurred to minimise the tax burden. According to Laplante et al. (2019) shows that research and development costs have an influence on tax savings and can be used as a tax avoidance strategy.

Another factor that can affect tax avoidance is Institutional Ownership. Handayani & Ibrani (2019), said that the presentation of share ownership shows strong ownership and influence on the company. One form of share ownership is institutional ownership. According to Eskandar & Ebrahimi (2020), Institutional Ownership is the proportion of shareholders owned by institutional owners such as insurance, banks, investment companies, and other institutional ownership. Khan et al. (2017), state that Institutional Ownership has a big role in influencing tax avoidance. The proportion of institutional share ownership affects the level of corporate tax avoidance, high institutional share ownership, the more share ownership owned by institutions, the higher the supervision of tax avoidance (Jiang et al., 2021). So, institutional ownership in the company will encourage and increase more optimal supervision of management performance. The greater the share ownership by the institutional, the greater the supervision of management policies so that the company tries to avoid behaviour that can harm shareholders. According to Tarmidi et al. (2022) that the role of institutional ownership has a strong influence on tax avoidance practices. However, according to research (Hassan et al., 2022; Jamei, 2017) that institutional ownership has no significant effect on tax avoidance. This study was conducted to empirically test the factors that influence tax avoidance. The factors used are multi-nationality, Research and Development costs and institutional Ownership with the object of research on multinational companies because they are considered to have great potential for tax avoidance.

## 2. Literature Review

Collaboration is a term commonly used to describe a pattern of cooperative relationships carried out by more than one party. Collaboration is a form of cooperation, with the underlying values of common goals, common perceptions, mutual benefits, willingness to process and honesty. Many definitions of collaboration have been put forward by various experts with diverse perspectives. This diversity is based on the same principles of togetherness, cooperation, sharing tasks, equality, responsibility and accountability. Collaboration theory according to Chaffee (2019), explains that a corporation is a collaboration between the Government and individuals who govern, run, and own the corporation. This theory explains how and why corporations exist, namely as a collaboration in an effort to complete a task for economic development and economic benefits. Collaboration theory also explains why the government has a greater ability to regulate the rights of corporations. Because the government is a collaborator in the entity, the government has the ability to direct its existence through laws and regulations. Thus, the company cannot prevent the government from collecting tax revenue that is expected to result in corporate creation. When the company performs tax avoidance actions, the company hinders the government's goal of obtaining funds through tax revenues used for state development.

Compliance theory is part of the theory of behavioural accounting research. Compliance theory was coined by Milgram (1963). In this theory, it is explained about a condition where a person obeys the orders or rules that have been set. According to the Big Indonesian Dictionary Compliance comes from the word "obey" which means like to obey orders, obey orders or rules and be disciplined. Compliance means being obedient, obedience to teachings and rules. In compliance, what is assessed is whether the activities or actions carried out are in accordance with applicable policies, regulations, provisions and laws. In addition, compliance can determine whether the party concerned has followed the procedures, standards and rules set by the authorities. Compliance theory, a theory that places more emphasis on the importance of socialisation in influencing an individual's compliance behaviour. State that taxpayer compliance concerns the extent to which

taxpayers fulfil their tax obligations in accordance with applicable tax regulations. The relationship between compliance theory and tax avoidance is the difference in interests between the tax authorities and the company which will lead to non-compliance by taxpayers or company management to carry out various tax avoidance strategies whose aim is to minimise the tax burden and maximise company profits. Thus, this allows taxpayers to take tax avoidance.

Tax avoidance according to Dyreng & Hanlon (2019), tax avoidance is an effort made by taxpayers to reduce the tax burden by not violating the law. Tax avoidance does not directly violate tax provisions, but utilises the loopholes that exist in tax provisions. Tax avoidance is an effort made by companies to deliberately reduce their tax obligations through legal means or strategies including location migration, profit shifting, transfer pricing, and others (Tang, 2020). Because the boundaries between legal and illegal are not clear, the legality of a company's tax position is determined by the authorised body. Helgadóttir (2023), explains that tax avoidance is an opportunity to reduce the value of taxes, as managers do to achieve personal benefits or for the benefit of shareholders, and it is often done with the approval of major shareholders in terms of ownership concentration. Pohan (2019), defines tax avoidance as an effort made by taxpayers to minimise their tax payments legally and safely without contradicting the applicable tax provisions. The methods and techniques used are by exploiting the loopholes and weaknesses (grey areas) contained in tax laws and regulations, so that there is no violation of the constitution or applicable tax laws.

Multi-nationality in this case is a multinational company. Multi-nationality is a company whose private, public ownership is built in various countries and each other exerts influence over the activities of other individuals including other resources and knowledge (OECD, 2023). Foley et al. (2021), in *Global Goliaths*, suggests multi-nationality as a business entity with one or more foreign affiliates in which the parent company holds at least a 10 percent ownership stake. Because most foreign affiliates are 100 percent owned by their parents, and because more data are available for majority-owned foreign affiliates, most of our calculations focus on majority-owned affiliates. That a multinational company is a business entity that has one or more foreign affiliates in which the parent company has a share ownership of at least 10%. Define a multinational company as a company that has subsidiaries in different countries from its home country or its operations cover a number of countries and has production and service facilities outside its own country. Multinational companies have several strategies in developing their business. There are several strategies commonly used by multinational companies, including; Wholly Owned Subsidiary, Joint Venture, Licence agreement, subcontracting, and Outsourcing. Multinational companies carry out operations spread across various countries by expanding into other countries which hope to improve performance through scale economies, access to technology and differences in operating costs (Porter, 1986).

Research and development costs can be abbreviated as R&D, related to research and development of company goods or services. In creating a product or service, companies generally incur research and development costs. Frankenfield (2022), explains that research and development costs are directly attributed to the research and development of a company's goods or services and any intellectual property generated in the process. Research and development are a systematic activity that combines basic and applied research to find solutions to new or existing problems or to create or update goods and services. Institutional ownership is the proportion of shareholders owned by institutional owners such as insurance, banks, investment companies and other institutional ownership. According to Moradi et al. (2022), institutional ownership refers to share ownership in a company owned by large financial institutions, pension funds, or endowments. Khan et al. (2017),

state that institutional ownership comes from banks, insurance and other capital institutions and has the authority to monitor the company's management capabilities. Institutional Ownership is the number of company shares owned by mutual or pension funds, insurance companies, investment companies, private foundations or other large entities that manage funds on behalf of other parties.

A multinational company is a company that has one or more subsidiaries in different countries from its home country. Multinational companies tend to be successful in carrying out tax avoidance practices because of greater opportunities than domestic companies. There are many ways that can be used to avoid taxes including transfer pricing, profit shifting, tax heaven, tax effective rate, thin capitalisation and so on. Thus, the more subsidiaries abroad, the higher the opportunity for tax avoidance (Kasim & Saad, 2019; Koivisto et al., 2021; Zia et al., 2018).

*H1: Multi-nationality has a positive effect on tax avoidance*

Research and development costs used to find new technologies or systems for company development can be charged as company costs so that they will reduce the tax burden payable. The inability of a research and development expenditure to be identified as an intangible asset is possible for companies to carry out tax avoidance. Research by Laplante et al. (2019), shows that practices that use the ambiguity inherent in tax reporting to classify indirect costs such as research and development costs, have a significant tax saving effect. Thus, internal research & development costs affect tax avoidance practices.

*H2: Research & development costs has a positive effect on tax avoidance.*

Theoretically, institutional ownership produces two impacts on tax avoidance, namely encouraging or suppressing tax avoidance behaviour. On the one hand, institutional ownership with a high percentage of share ownership is able to intervene in corporate tax avoidance behaviour and obtain greater benefits than minority shareholders (Dakhli, 2022). The above theoretical assumptions are proven through empirical studies regarding the effect of Institutional ownership on tax avoidance behaviour in companies. The study found that a higher percentage of Institutional Ownership affects a higher level of tax avoidance (Jiang et al., 2021; Khan et al., 2017; Tarmidi et al., 2022).

*H3: Institutional ownership has a positive effect on tax avoidance.*

### **3. Methods**

The population of this study is Manufacture companies listed on the Indonesia Stock Exchange for the period 2018-2023. With purposive sampling method, 20 manufacturing companies were selected for 6 years of research and after eliminating incomplete data, there were 100 panel data analysed using STATA software. In this study, the Tax Avoidance variable is measured using the proxy statutory tax rate (STR) minus the effective tax rate (ETR). ETR is used to reflect tax avoidance and is the ratio of tax expense to profit before income tax. The assumption is that if the company does tax avoidance, it is indicated by tax payments that are not less than the statutory tax rate and vice versa the company is classified as non-compliant and tax avoidance if the tax payment is less than the statutory tax rate in Indonesia (Jamei, 2017; Tarmidi et al., 2024). Multi-nationality is a company that has subsidiaries in different countries from its home country. Kasim & Saad (2019), define multinational companies as companies with significant operations and marketing activities outside their country. In this study, the multi-nationality variable is measured by calculating the number of foreign subsidiaries owned by a company divided by the total subsidiaries owned by a company (Anh et al., 2018). Research by Laplante et al. (2019), shows that tax

avoidance practices that use the ambiguity inherent in tax reporting to classify research and development costs, have a significant tax saving effect. In this study, researchers used the natural logarithm proxy for the disclosure of Intangible Assets in the research year. Khan et al (2017) state that institutional ownership comes from bank ownership, insurance, institutions and other capital industries, and has a very useful effect on monitoring the company's management capabilities. In this study, the Institutional Ownership variable is measured by comparing the number of shares owned by the institution with the company's total shares outstanding (Jiang et al., 2021).

#### 4. Results and Discussion

The tax avoidance variable has a mean value of minus -0.05967, which means that on average the analysis unit books tax costs in excess of the applicable income tax rate, this is thought to be due to a positive correction in fiscal profit compared to commercial profit. With a standard deviation value exceeding the mean value, it means that the distribution of data is uneven, the data is heterogeneous due to the distribution of data varies. The multi-nationality variable has a mean value of 0.45974, this means that on average the analysis unit has an overseas subsidiary as much as 45% of the number of subsidiaries owned. With a standard deviation value smaller than the mean, it explains that the average number of overseas subsidiary presentations in the analysis unit does not vary. The research & development cost variable has a mean value of 24.19560. With a standard deviation value smaller than the mean, it explains that R&D costs in the analysis unit do not vary. The institutional ownership variable has a mean value of 0.82138, meaning that on average the analysis unit is owned by an institution of 82%. With a standard deviation value greater than the mean, it means that the institutional shares of the analysis unit do not vary.

**Table 1.** Statistic Descriptive

Variable	TAV	MNAT	RND	INST
Min	0.89894	0.07143	17.82937	0.01545
Max	0.22000	1.00000	29.08030	0.99998
Mean	0.05967	0.45974	24.19560	0.82138
Stdev	0.14469	0.33218	2.86083	0.24052

Panel model selection is carried out to find out the best panel regression model, there are three tests carried out, namely the Chow test with the results finding the best Common effect model (CEM), the Hausman test with the results finding the Random Effect Model (REM), the last is the LM test with the results finding the Common effect model (CEM). From these three tests, it is concluded that the model to be used in this study is the Common Effect Model (CEM). Based on the model fit test on the research data, it is known that the best model is the Common Effect Model (CEM), so Ordinary Least Square (OLS) is used in estimating the effect of independent variables on the dependent variable. Furthermore, the classical assumption test is carried out to test the panel data using STATA. The classic assumption tests carried out for the Common Effect Model through the Ordinary Least Square (OLS) approach are heteroscedasticity test and multicollinearity test. Based on the multicollinearity test results, it is found that the VIF value is in the range of 1.16 - 1.65, all of which are smaller than the value of 10, so the research data passes the multicollinearity test. From the results of the heteroscedasticity test, the Prob>chi2 value is greater than the significance level of 0.05 so it is said that there is no heteroscedasticity.

Based on table 2, it is found that the R-Square value is 0.1340, which means that the multi-nationality, research & development cost and institutional ownership variables explain the tax avoidance variable by 13.40%, while the remaining 86.60% of tax avoidance is explained by other variables outside this study. With a Prob>F value of 0.0031 smaller than 0.05, it explains that this research model is Fit or Good. so it can be continued to the t-test. Based on table 2, it is known that multi-nationality has a probability value of 0.330 which exceeds 0.05 so it is concluded that multi-nationality has no significant effect on the tax avoidance variable and hypothesis 1 is rejected. Research & development cost has a probability value of 0.606 which exceeds 0.05 so it is concluded that research & development cost has no significant effect on the tax avoidance variable and hypothesis 2 is rejected. Institutional ownership has a probability value of 0.002 which is smaller than 0.05 so it is concluded that institutional ownership has a significant effect on the tax avoidance variable and hypothesis 3 is rejected. With a coefficient value of 0.19833, it explains that institutional ownership has a positive effect on tax avoidance.

Table 2. Main Hypotheses

Tax Avoidance (Y)	Coef.	Prob.
Multi-nationality (X1)	0.05103	0.330
RnD Cost (X2)	-0.00319	0.606
Institutional Ownership (X3)	0.19833	0.002***
N	100	
R-Square	0,1340	
Prob F	0,0031***	

\* Significant 90%, \*\* Significant 95%, \*\*\* Significant 99%

The test of hypothesis 1, it is known that multi-nationality does not have a significant effect on tax avoidance, this is thought to be because the majority of analysis units (87%) have subsidiaries in countries that are not tax haven countries as presented in Figure 1. Tax avoidance in multinational companies tends to be done through subsidiaries located in tax haven countries so that consolidated tax costs can be shifted to countries with lower tax rates (tax haven countries). This is in line with the results of research by Anh (2018), which analyses tax avoidance in multinational companies with indicators of subsidiaries located in tax haven countries, the results show that the more subsidiaries in tax haven countries, the higher the tax avoidance practices.

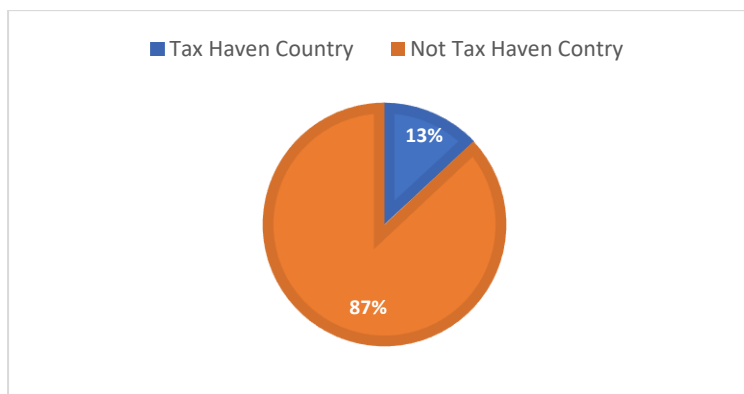
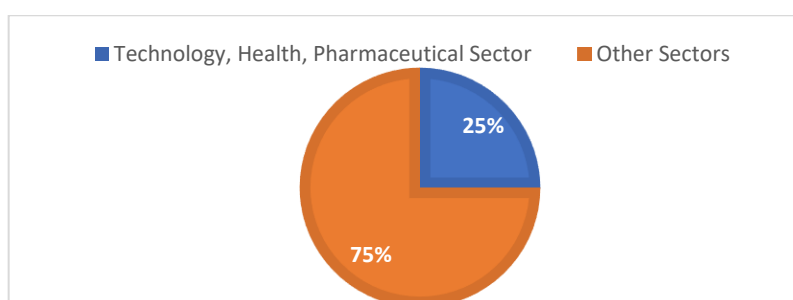


Figure 1. Location of subsidiaries

The results of this study are not in line with research conducted by Koivisto et al. (2021); O'Hare et al. (2020), which state that multinational companies have an

effect on tax avoidance. The tendency of multinational companies will take advantage of the opportunities of parent and subsidiary relationships to reduce the cost of taxes paid by taking advantage of existing tax regulation loopholes.

Hypothesis 2 test, it is known that Research & Development Costs have no significant effect on tax avoidance, this explains that the unit of analysis in this study does not use Research & Development Costs in tax avoidance. Based on the decision of the minister of finance 769 / KMK.04 / 1990 and Circular Letter of the Director General of Taxes Number SE-22 / PJ.31 / 1990 which explains that Research & Development costs used for activities to obtain, collect and maintain income (3M) can be deducted from gross income to calculate taxable income. However, the type of industry in the analysis unit is suspected of not actively conducting Research & Development activities in the observation year as explained in the diagram below.



**Figure 2.** Industry Type of Analysed Unit

The results of this study are not in line with research conducted by Laplante et al, (2019) and Pfeiffer & Spengel (2017), which state that the practice of utilising research and development costs has a significant tax saving effect and can be used as a tax avoidance strategy. The company will have a lower tax burden due to higher tax benefits related to the expenditure on research & development costs.

Based on hypothesis 3 test, it is known that Institutional Ownership has a significant effect on tax avoidance. This explains that the proportion of institutional ownership is an indicator that the company is doing tax avoidance. The higher the share ownership owned by the institution, the higher the level of tax avoidance. The proportion of institutional ownership is share ownership by other institutions, namely ownership by other companies or institutions. The large proportion of institutional shares invested in the company puts pressure on company management to adopt proactive fiscal policies aimed at maximising profitability. In addition, the high proportion of share ownership owned by institutions compared to other shareholders will require management to manage the company for its own interests, especially those related to profit optimisation, so that with that, the tendency to make tax avoidance efforts will increase which aims to reduce the weight of taxes payable. The results of this study are in line with research conducted by Tarmidi et al. (2022) and Jiang et al. (2021), which say that Institutional Ownership has a positive effect on tax avoidance. Shareholders with a high percentage of institutional ownership are more motivated and able to intervene in tax avoidance behaviour in the company. Institutional shareholders use knowledge about tax avoidance, tax havens and communication with management to help improve corporate governance, the purpose of which is to encourage more profit.

## 5. Conclusion

The results of this study found the multi-nationality has no significant effect on tax avoidance. This is suspected because there are several units of analysis whose subsidiaries are in countries that are not tax haven countries. Research & Development costs have no significant effect on tax avoidance. This explains that the unit of analysis in this study does not use Research & Development Costs in tax avoidance. Institutional Ownership has a positive effect on tax avoidance. This shows that the higher the proportion of institutional ownership of a company, the higher the tendency of management to take tax avoidance actions. These results can be used as a reference by the tax authorities in the taxpayer supervision process.

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