ACCOUNTING CONSERVATISM, TAX AVOIDANCE, AND FIRM VALUE: IMPLICATIONS FOR FINANCIAL TRANSPARENCY AND REGULATION IN INDONESIA'S ENERGY SECTOR

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ABSTRACT

Introduction/Main Objectives: This study aims to examine the effect of accounting conservatism and tax avoidance on firm value in the energy sector of the Indonesia Stock Exchange (IDX). It evaluates whether these financial management practices contribute to or detract from firm value, using the framework of Agency Theory to explain managerial behavior and investor responses. **Background Problems:** Previous studies provide mixed evidence on how conservatism and tax avoidance affect firm value. While both are intended to improve efficiency and reduce information asymmetry, excessive conservatism can distort earnings, and aggressive tax avoidance can increase reputational and regulatory risks. These contradictions, combined with limited research in Indonesia's energy sector, create uncertainty about their true value implications. This study contributes to the literature by focusing specifically on Indonesian energy firms during the post-pandemic period (2021–2023), incorporating recent financial reforms and the use of cash effective tax rate (CETR) as a realistic measure of tax avoidance.

Novelty: This study contributes to the literature by focusing specifically on Indonesian energy firms during the post-pandemic period (2021–2023), incorporating recent financial reforms and the use of cash effective tax rate (CETR) as a realistic measure of tax avoidance.
Research Methods: A quantitative causal-explanatory approach was employed using panel data of energy firms obtained from the Bloomberg database. The data were analyzed using fixed-effects regression in STATA to control for firm-specific heterogeneity.
Findings/Results: The results indicate that both accounting conservatism and tax avoidance have negative but statistically insignificant effects on firm value. The model's explanatory power is low, suggesting that firm value is driven by other firm-specific factors.
Conclusion: These findings imply that conservatism and tax avoidance may not enhance firm value and can even reduce investor confidence when perceived as excessive or opportunistic.
Implementation Potential: The results encourage regulators (OJK and DJP) to balance transparency and flexibility in reporting standards, guide managers toward ethical accounting and tax practices, and help investors interpret conservatism and tax strategies more critically in valuation decisions.

Keywords: Accounting Conservatism; Tax Avoidance; Firm Value; Cash Effective Tax Rate; Agency Theory; Energy Sector
JEL Classification: (list the relevant JEL codes separated by commas, refer to https://www.aeaweb.org/jel/guide/jel.php)

1. INTRODUCTION

Firm value serves as a key indicator of corporate performance, encapsulating the market's comprehensive evaluation of a company's profitability, growth potential, and risk profile. In the current dynamic business landscape, particularly following the global tax and reporting reforms of 2024, investors have shifted their focus beyond short-term earnings to include the quality of financial reporting and the transparency of managerial decisions (Olubunmi et al., 2025). For companies in capital-intensive and politically sensitive sectors like energy, firm value is a crucial measure of long-term sustainability and investor confidence. On the Indonesia Stock Exchange (IDX), energy companies are significant contributors to the national economy, yet they face increased scrutiny over their accounting practices, tax strategies, and governance transparency. Thus, understanding the factors influencing firm value in this sector is vital for investors, regulators, and policymakers.

Among the various factors that influence firm value, accounting conservatism and tax avoidance hold particularly significant roles. Accounting conservatism, which prioritizes the earlier recognition of losses over gains, acts as a mechanism to alleviate agency conflicts between managers and shareholders (Xu, 2021). By curbing managerial discretion and reducing information asymmetry, conservatism bolsters the credibility of financial reports and shields investors from overly optimistic earnings forecasts. Empirical evidence supports its positive impact on firm value by enhancing investor confidence and signaling prudent financial management (Pasko et al., 2023). However, this relationship is not always consistent. Research suggests that the influence of conservatism can be undermined by managerial incentives, such as CEOs' personal tax liabilities or political connections that diminish transparency (Lonare, 2024; Mohammed et al., 2017). This raises questions about whether conservatism in Indonesian energy firms effectively functions as a value-enhancing mechanism.

Tax avoidance is another critical factor influencing firm value, as it directly affects profitability and perceptions of corporate integrity. Moderate tax avoidance may be viewed positively by investors, as it increases after-tax income and signals efficient financial management (Elamer et al., 2024). However, aggressive tax avoidance can harm firm value by inviting regulatory scrutiny, damaging reputation, and increasing perceived risk particularly in emerging economies with limited tax enforcement (Hossain et al., 2024; Mazurenko et al., 2023). In Indonesia, where energy companies account for a major portion of government revenue, tax strategies are particularly sensitive, as the government and public expect fair tax contributions while firms seek to maintain competitiveness in a highly regulated industry.

Despite the significance of these two financial behaviors, previous studies have largely examined accounting conservatism and tax avoidance independently, leading to fragmented conclusions about their individual and combined effects on firm value. Theoretically, conservative accounting could act as a monitoring tool that constrains aggressive tax behavior, but empirical evidence supporting this interaction remains limited. Furthermore, most prior research is based on data before 2022 and does not capture recent global and domestic developments, such as the implementation of the OECD's Pillar Two global minimum tax rules in 2024 and Indonesia's efforts to enhance tax compliance and financial transparency. These regulatory changes are expected to alter corporate behavior, making it essential to reassess how conservatism and tax avoidance influence firm value under the current economic environment.

Previous empirical studies have produced inconsistent results on how accounting conservatism and tax avoidance affect firm value. Several studies support the notion that accounting conservatism enhances firm value by improving the credibility of financial reports and protecting investors from managerial opportunism. For example, Pasko et al. (2023) found that conservatism increases stakeholders' trust by ensuring timely loss recognition, which aligns with agency theory's prediction that conservative reporting mitigates agency conflicts. Similarly, Hu & Jiang (2019) reported that conservatism helps reduce firm risk arising from excessive managerial incentives. However, contrasting evidence suggests that conservatism does not always enhance firm value. Lonare (2024) found that CEOs' personal tax burdens reduce their preference for conservative reporting, implying that managerial incentives can weaken its effectiveness. Likewise, Mohammed et al. (2017) observed that in politically connected firms, board independence has a weaker effect on enforcing conservatism, suggesting that political influence can diminish its positive impact on firm performance. These findings indicate that the effect of accounting conservatism on firm value may depend on contextual factors such as managerial incentives, ownership structure, and political environment.

Similar contradictions are found in studies on tax avoidance and firm value. Several research have shown that tax avoidance can increase firm value by improving cash flows and after-tax profits. For instance, Elamer et al. (2024) found a positive association between moderate tax avoidance and firm value among French-listed companies, suggesting that investors reward efficient tax planning. Hossain et al. (2024) found that excessive tax avoidance in Bangladesh undermines firm performance due to weak enforcement and public distrust. Mazurenko et al. (2023) similarly demonstrated that shadow tax evasion decreases the competitiveness of national tax systems, indirectly harming firm value. In the Indonesian context, where the tax authority has intensified audits on large energy companies, aggressive tax avoidance could signal higher risk, potentially reducing investor confidence and firm valuation.

2. LITERATURE REVIEW

The relationship between accounting conservatism, tax avoidance, and firm value can be best understood through the lens of Agency Theory, which serves as the grand theory underpinning this research. Proposed by Jensen & Meckling (1976), Agency Theory explains the conflict of interest between principals (shareholders) and agents (managers), where managers may act to maximize their own benefits rather than shareholder wealth. This misalignment gives rise to agency costs, prompting firms to adopt mechanisms that reduce managerial opportunism and enhance transparency. Accounting conservatism is one such mechanism. By requiring losses to be recognized more quickly than gains, conservative accounting practices limit earnings manipulation, improve the credibility of financial information, and strengthen investor confidence. Empirical evidence supports this argument, showing that conservatism can increase firm value by mitigating information asymmetry and protecting stakeholder interests (Pasko et al., 2023). However, Agency Theory also suggests that the effectiveness of conservatism is conditional on managerial incentives and external pressures. For instance, CEOs facing high personal tax burdens may prefer less conservative reporting to inflate short-term earnings, while political connections can weaken governance structures that enforce conservatism (Lonare, 2024; Mohammed et al., 2017).

Studies have shown that firms engaging in moderate, well-managed tax avoidance tend to achieve higher valuations due to improved cash flows and efficient resource utilization (Elamer et al., 2024). On the other hand, aggressive tax avoidance may reflect opportunistic managerial behavior aimed at concealing rent extraction or manipulating performance indicators, which increases agency costs and can damage the firm’s reputation (Hossain et al., 2024; Mazurenko et al., 2023).

Accounting conservatism requires firms to recognize losses earlier than gains, which traditionally serves to protect investors by providing timely and cautious financial information. However, several studies have argued that excessive conservatism can reduce firm value, particularly when it limits the usefulness of financial statements for investors and distorts earnings information. Overly conservative reporting can understate assets and profits, leading to a perception of weaker performance and lower firm valuation in the capital market (Zhong & Li, 2017).

From an Agency Theory perspective, conservatism may create information asymmetry if managers use it opportunistically to smooth income or conceal poor performance. Pasko et al. (2023) found that while some degree of conservatism improves disclosure credibility, excessive conservatism can hinder stakeholders' ability to assess the firm's true financial health.

In the Indonesian energy sector, where firms are capital intensive and rely on external financing, conservative accounting may be perceived as a signal of weak profitability and limited growth prospects. This perception can discourage investment and depress market valuation, especially when investors prefer transparent and forward-looking financial reporting. Therefore, based on prior evidence and theoretical reasoning, the following hypothesis is proposed:

H1: Accounting conservatism has a negative effect on firm value.

Tax avoidance is another managerial strategy that can influence firm value, but its impact is also context-dependent. While moderate tax avoidance can reduce tax burdens and improve cash flow, aggressive or opaque tax practices often lead to reputational risk, increased regulatory scrutiny, and long-term financial uncertainty all of which can harm firm value. Studies have shown that markets tend to penalize firms perceived as engaging in excessive tax avoidance due to the potential for future penalties and ethical concerns (Hossain et al., 2024).

Durtschi & Easton (2009) found that public announcements of corporate tax avoidance are often associated with negative abnormal stock returns, suggesting that investors view such behavior unfavorably. Likewise, Desai & Dharmapala (2009) documented that tax avoidance does not necessarily increase firm value and can even decrease it when accompanied by weak corporate governance, as managers may exploit tax shelters for private benefits rather than shareholder interests. In the Indonesian context, where tax compliance is a significant aspect of corporate social responsibility and government scrutiny of large taxpayers (including energy firms) has intensified since 2021, aggressive tax avoidance may trigger negative perceptions and erode firm reputation.

From the Agency Theory standpoint, aggressive tax avoidance increases agency costs by creating opacity in financial reporting and allowing managers to obscure rent-seeking behavior.

Investors, recognizing these risks, may discount the firm's value to reflect the potential for tax penalties, loss of reputation, and reduced transparency. Therefore, consistent with this reasoning and empirical findings, the following hypothesis is proposed:
H2: Tax avoidance has a negative effect on firm value.

3. METHOD

This study adopts a quantitative research design with a causal–explanatory approach to examine the effect of accounting conservatism and tax avoidance on firm value in the energy sector of the Indonesia Stock Exchange (IDX). The causal approach is appropriate because the study aims to determine the extent to which variations in accounting conservatism and tax avoidance explain changes in firm value. This design also allows for hypothesis testing to provide empirical evidence of the relationships between the variables grounded in Agency Theory.

The population of this study comprises all energy companies listed on the Indonesia Stock Exchange (IDX). The energy sector was chosen due to its strategic role in Indonesia's economy, its large contribution to national tax revenues, and its frequent involvement in financial transparency and tax management discussions. The sample was selected using purposive sampling, with the following criteria:

a. Companies classified under the energy sector based on IDX's industry classification.
b. Companies that published complete and audited annual financial statements for the period 2021 - 2023.
c. Companies with complete financial and tax data available through the Bloomberg database.
d. Companies that were not delisted or suspended during the observation period.

This study uses secondary data obtained from the Bloomberg Terminal. Data collected include annual financial statement information such as total assets, total liabilities, market capitalization, operating cash flow, tax expenses, pre-tax income, and stock price data for each firm from 2021 to 2023. Bloomberg is used because it provides consistent, audited, and standardized financial information suitable for cross-company and time-series analysis.

The study employs three key variables: firm value as the dependent variable and accounting conservatism and tax avoidance as the independent variables. Control variables are also included to reduce estimation bias.

The relationship between accounting conservatism, tax avoidance, and firm value is tested using a multiple linear regression model, expressed as follows:

$FVi=\beta 0-\beta 1CONi-\beta 2CETRi+\epsilon$

Where:

FV = Firm value

CON = Accounting conservatism

CETR = Cash effective tax rate

ϵ = Error term

4. RESULTS AND DISCUSSION

Table 1. Regression Results

	Coef	t	p
Cons	2,531707	14,00	0,000
CON	-2,469494	-1,08	0,285
CETR	0,0037678	0,01	0.991
F Score			0,5584
Adj R-squared			0.021

The fixed-effects regression results show that both accounting conservatism and tax avoidance have negative but statistically insignificant effects on firm value among energy companies listed on the Indonesia Stock Exchange (IDX) during the period 2021–2023. The coefficient of accounting conservatism (β_1 = –2.469, p = 0.285) indicates an inverse relationship between conservatism and firm value; however, this relationship is not statistically significant at the 5% level. Likewise, the coefficient of tax avoidance (β_2 = 0.0038, p = 0.991) is close to zero and statistically insignificant, suggesting that variations in firms' cash effective tax rates do not materially influence market valuation. The overall model fit is weak, with a within R^2 of 0.021, meaning that the independent variables explain only 2.1% of the changes in firm value across time. Nonetheless, the fixed-effects test (Prob > F = 0.0000) confirms significant firm-specific heterogeneity, justifying the use of the fixed-effects estimator.

The negative coefficient of accounting conservatism is consistent with studies that suggest excessive conservatism may distort earnings and reduce the informational value of financial statements. Overly conservative accounting can lead to persistent understatement of assets and income, which may cause investors to undervalue the firm. Beaver & Ryan (2005) argue that high levels of conservatism can bias book values downward, lowering firms' market valuations. Similarly, Givoly & Hayn (2000) found that persistent conservatism leads to reduced earnings persistence and lower market responses to accounting numbers. In the Indonesian energy sector, this effect may be amplified because investors often rely on earnings performance as a key valuation metric. When reported profits appear suppressed due to conservative recognition of income and accelerated loss recognition, market participants may interpret this as a signal of weaker financial performance, thereby lowering firm value.

Regarding tax avoidance, the insignificant and slightly negative relationship aligns with previous research indicating that aggressive or opaque tax strategies often fail to enhance firm value and can even harm it. Hanlon & Slemrod (2009) found that announcements of corporate tax shelter activities are associated with negative abnormal stock returns, implying that investors perceive aggressive tax planning as risky or unethical. Similarly, Desai & Dharmapala (2009) reported that tax avoidance does not increase firm value when governance quality is weak, as managers may exploit tax savings for personal benefits rather than shareholder gain. Hossain et al. (2024) further noted that in emerging economies, aggressive tax avoidance tends to reduce investor trust and increase reputational risks. This finding is particularly relevant for Indonesia's energy sector, where government scrutiny over large taxpayers has intensified since 2021, and reputational concerns surrounding tax compliance have become increasingly significant.

From a theoretical standpoint, the insignificant and negative effects of both accounting conservatism and tax avoidance on firm value support a refinement of Agency Theory in the context of emerging markets. Traditional Agency Theory posits that conservative accounting can mitigate agency problems by restricting managerial discretion and reducing information asymmetry (Jensen & Meckling, 1976). However, the findings of this study suggest that when conservatism is applied excessively or strategically by managers, it may instead obscure firm performance and reduce investors' ability to accurately assess firm value. This aligns with Beaver & Ryan (2005), who noted that conditional conservatism can distort book values and earnings persistence, thus lowering valuation relevance. Consequently, the results highlight the dual role of conservatism depending on managerial intent and reporting incentives.

Similarly, the negative but insignificant relationship between tax avoidance and firm value contributes to the agency-based understanding of corporate tax behavior. According to Desai & Dharmapala (2009), the value implications of tax avoidance depend heavily on governance quality. When monitoring mechanisms are weak, managers may use tax avoidance to hide opportunistic actions rather than enhance firm efficiency. The results of this study are consistent with this argument, suggesting that in the Indonesian energy sector, tax avoidance may not be perceived as a value-creating strategy. Instead, it may raise concerns about managerial transparency, regulatory risk, and ethical conduct factors that investors often penalize. Thus, these findings extend Agency Theory by showing that in emerging economies with strong political influence and growing regulatory oversight, the agency costs of opacity may outweigh the financial benefits of tax savings.

5. CONCLUSION

This study aimed to examine the effect of accounting conservatism and tax avoidance on firm value in the energy sector of the Indonesia Stock Exchange (IDX) during the period 2021–2023, using secondary data from the Bloomberg database and analyzed with a fixed-effects regression model in STATA. Grounded in Agency Theory, the research sought to understand whether conservative financial reporting and tax avoidance practices function as mechanisms that enhance or diminish firm value.

Finally, this study acknowledges several limitations that open avenues for future research. First, the sample is limited to energy sector firms and a three-year observation period (2021–2023), which may constrain the generalizability of the findings. Future studies could extend the sample to other sectors or employ longer time horizons to capture post-2024 regulatory impacts. Second, the study focuses solely on accounting conservatism and tax avoidance; incorporating governance quality, ESG performance, or political connections as moderating factors could provide deeper insights into firm valuation mechanisms. Third, qualitative approaches such as management interviews or case studies could complement quantitative results and explore the strategic motives behind conservatism and tax behavior.

In summary, this research concludes that neither accounting conservatism nor tax avoidance significantly enhances firm value in Indonesia's energy sector. Instead, their negative and insignificant effects suggest that market participants may perceive these practices as indicators of risk or information opacity rather than value creation. The findings reaffirm that, consistent with Agency Theory, transparency, accountability, and effective governance remain the primary drivers of firm value, especially in capital-intensive and government-influenced industries such as energy.

6. IMPLICATIONS, LIMITATIONS, AND FUTURE RESEARCH

The findings of this study carry several theoretical, practical, and methodological implications. Theoretically, the negative and insignificant effects of accounting conservatism and tax avoidance on firm value refine the assumptions of Agency Theory by showing that mechanisms traditionally intended to mitigate agency problems may instead generate new agency costs when applied excessively or opportunistically. This suggests that both practices, rather than enhancing transparency, can obscure performance and increase information asymmetry, consistent with the arguments of Beaver and Ryan (2005) and Desai and Dharmapala (2009). Practically, the results provide insights for regulators, investors, and managers in Indonesia's energy sector. This study, however, is limited by its focus on energy companies listed on the Indonesia Stock Exchange (IDX) over a relatively short observation period (2021–2023) and by its reliance on quantitative secondary data from the Bloomberg database, which may not fully capture managerial or institutional dynamics. Future research could extend the study period to include post-2024 data, compare across sectors, or incorporate moderating factors such as corporate governance quality, political connections, and ESG performance to provide a deeper understanding of how accounting and tax practices affect firm value in emerging markets.

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