# Paper P2

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# How does organisational capital influence firm value? Moderating effect of tax haven utilisation

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**Abstract:** This study investigates whether organisational capital and tax haven utilisation through subsidiaries are associated with firm value. We use 705 observations of Indonesia-listed firms from the agriculture and manufacturing sectors as the main contributors to the gross domestic product (GDP). The sample has been analysed using the weighted least square panel regression technique over the period 2015 – 2019. The findings suggest that the positive association between organisational capital and firm value is stronger when tax haven subsidiaries are utilised. High organisational capital (OC) firms are often linked to limited access to financing since intangible assets are difficult to use as collateral. Tax haven subsidiaries can serve as a risk trade-off for OC firms. Our study provides novel empirical evidence supporting social tax justice and stakeholder theory and encourages the cooperation of all stakeholders to resolve the recognition and assessment of intangible capital in financial reports.

**Keywords:** Organisational capital, intangible capital, tax haven utilisation, firm value, tax audit, sustainable tax behaviour.

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## 1. Introduction

Organisational capital (OC) plays a crucial role in improving enterprise value. Several studies have investigated the OC (Rahko, 2014; Piekkola. 2016; Amathachaya and Saengchote, 2018; Boguth et al., 2021; Boubaker et al., 2021; Chiu et al., 2021; Hasan et al., 2021; Li and Wu, 2021) found that OC associates with firm value. OC is characterised by knowledge, capabilities, culture, systems, and business processes that match human skills with physical capital to improve efficiency (Hasan et al., 2021). It is a key element of the IT-driven growth productivity of the firm (Hasan and Cheung, 2018; Li et al., 2018; Li and Wu, 2021), as a continuous competitive advantage, increasing profitability, cash flow stability and reducing business risks (Chiu et al., 2021). Organisational capital positively contributes to a firm's valuation because the market value increases substantially more than the book value of digital-based companies (Piekkola, 2016).

However, OC firms have several challenges. OC is mobile and has the ability to shift to competitor businesses (Amathacaya and Saengchote, 2018). In addition, OC's most significant challenges lie in its unresolved global recognition and measurement. Popescu (2020) questions whether the BEPS (Base Erosion and Profit Shifting) action five projects on harmful tax regimes can end the debate over recognising and measuring intangible capital. Global competition between countries creates new tax haven jurisdictions that create opportunities for tax rate arbitration, financial secrecy and intellectual property protection arbitration between countries. Organisational capital that is mobile has the potential to easily move to tax haven countries to take advantage of the arbitration and ultimately increase the firm's competitiveness. Popescu and Banța (2019) and Popescu (2020) highlight the need for balancing sustainability, competitiveness, productivity, and financial and non-financial performance, including considering the tangible and intangible benefits of business values such as brand, human capital, corporate culture, and reputation. Corporations need to maintain all stakeholder values, such as paying taxes and creditors, remuneration to employees, and dividends (Serrano-Cinca et al., 2021a). Mella and Gazzola (2018) state that firms integrate ethical values and stakeholder engagement in corporate strategy. The challenge of recognising and measuring intangible capital has a more significant impact on OC firms connected to tax havens, specifically in countries with low intellectual property rights.

Prior studies have not investigated the connection between OC, tax haven utilisation, and corporate valuation. Previous research on OC and taxation has addressed tax avoidance (Hasan et al., 2021), tax aggressiveness, and tax havens (Borkowski and Gaffney, 2021). Hasan et al. (2021) showed a positive relationship between organisational capital and firm value when the firm has a higher level of tax avoidance than other companies. This result is supported by evidence that tax avoidance generates more cash flow and after-tax earnings, which shareholders and managers claim on these cash flows. Borkowski and Gaffney (2021) showed that the pattern of tax avoidance behaviours during the FIN 48 decade showed a high level of aggressiveness when intangible

intensity and the use of tax havens were high. Our study differs from the two studies in that it interacts between OC and tax haven utilisation and analyses their impact on firm value. This is consistent with Dyreng et al. (2019) that enterprises with high intangible intensity and tax-haven subsidiaries can take advantage of avoiding taxes by transferring ownership of these assets to tax-haven countries and, with these assets, shifting income from the base country to tax-haven countries.

The stakeholder theory is related to a firm's social contribution to the community, specifically to the base country. Managing stakeholders means simultaneously creating value for multiple parties and society (Serrano-Cinca et al., 2021b). The risks faced by high OC firms associated with recognising and measuring intangible capital cause limited access to capital due to minimal tangible assets as collateral and relatively higher financial expenses compared to other companies. High-OC businesses are often linked to limited access to financing. Since intangible assets are difficult to use as security, Marwick et al. (2020) found that high-OC businesses have a harder trouble securing funding. Stakeholders of OC firms also demand greater expected returns, which may influence stakeholders' evaluation of the tax haven utilisation used by the firms. On the other hand, tax haven subsidiaries are typical "shell firms" that lack economic substance or serve only financial and accounting roles. Therefore, the problem creates tax injustice for the host country since the cost of establishing tax haven subsidiaries is insignificant. Hoh and Tang (2021) indicated that enterprises were shifting accounting and finance operations to acquire talent and technological advancement that could be trained with firm-specific information. Indeed, tax haven subsidiaries owned by high-OC enterprises can serve as both a good indication and risk trade-off for OC firms. In some countries, enterprises have the potential to experience higher audit probabilities, interest or penalties, and higher tax court litigation rates (Borkowski and Gaffney, 2021). However, in certain countries, the focus of tax enforcement is on firms that use the net operating loss carryforward, which has great potential to minimise their taxes. Consistent with Christensen et al. (2021), most low effective tax rate (ETR) firms use a large net operating loss carryforward.

Two justifications are provided for why this study empirically examines this premise using data from the Indonesian market. First, mandatory disclosure for subsidiaries in financial statements, which has been enforced since 2015 based on IFRS 12, adopted PSAK 67, followed by the transformation of domestic tax regulations, mainly related to international profit-shifting activities, to exert external pressure on enterprises. The BEPS consensus has influenced changes in Indonesia's domestic policies. For example, BEPS number 4 regards restrictions on financial expenses on debt that have been in effect since 2015, BEPS number 6 regarding the obligation to disclose beneficial ownership, bilateral/multilateral tax information exchange implemented since 2018, and the obligation to report affiliate transactions to certain amounts since 2016. In addition, strict tax enforcement during the period of policy change also had an impact on firm behaviour. This study explores how stakeholders assess the utilisation of tax havens as measured by the disclosure of tax haven subsidiaries in audited financial reports, specifically in OC firms. Second, as a developing country, Indonesia has set Sustainable Development Goals (SDGs) since 2017, where point 17 discusses increasing transparency in the taxation sector to achieve the long-term goal of a sustainable tax. Therefore, the Indonesian market provides a unique setting for researchers to examine the effect of tax haven utilisation on the relationship between OC and firm value.

The findings provide novelty supporting stakeholder theory by emphasising the importance of consensus regarding recognising and measuring intangible capital to minimise the potential risks inherent in OC firms that can affect corporate valuation and encourage an increase in sustainable tax behaviour in OC firms. Recent important studies on the relationship between OC, taxation, and firm value include Hasan et al. (2021) and Borkowski and Gaffney (2021). Our study differs from these studies in several ways. First, Hasan et al. (2021) study discusses tax avoidance rather than tax havens utilisation, which is associated with OC and firm value. Indeed, tax haven utilisation has a broader motivation than tax avoidance, specifically tax minimisation, financial secrecy (Aziani et al., 2020), intellectual property protection (Karhunen et al., 2021), and global networking (Mukundhan et al., 2019). Thus, it can potentially affect the competitiveness and value of OC firms. Second, although Borkowski and Gaffney (2021) show that there is a significant difference in the mean between high and low-intangible intensity firms in tax haven utilisation, they do not address how the intensity of tax haven utilisation can affect the relationship between the level of OC stock and corporate valuation. Thus, the originality of our findings is that the use of tax havens can influence the relationship between the level of OC stock and the firm value of OC enterprises.

The remainder of the paper is structured as follows. Section 2 examines the relevant literature and formulates a hypothesis. The third section describes the sample selection and research methodology. The fourth section presents empirical results and robustness tests. The final component of the paper is section 5.

## 2. Literature review and hypothesis development

### 2.1 Tax Justice, Competitiveness, and Stakeholders Theory

Tax justice is a fair share of tax burdens between individuals assessed on the baseline. Murphy and Nagel (2002) express the principle that tax justice must be part of all social justice theory and is the goal of legitimate government. Several previous studies have explained that extensive internationalisation related to the economy, especially financial transactions, has made countries vulnerable to tax competition between countries, which in turn has prompted multinational firms to relocate their operations (Leaman & Waris, 2013). The tax arrangements between countries and multinational firms have made states less powerful in developing countries such as Africa, Asia, and Latin America (Otusanya et al., 2023). Tax justice must consider the fundamental interdependence of the global economy and the particular disadvantages faced by poor countries with weak tax governance due to the sophisticated tax and regulatory arbitrage strategy of highly mobile multinational firms (Leaman & Waris, 2013; Murphy & Nagel, 2002).

Intangibles omitted from investment measurement affect capital growth causing a downward bias in the measurement of total factor productivity (Crouzet & Eberly, 2021). Byrne et al. (2016) identified that mismeasurement of IT capital has an effect on measurable productivity but cannot explain slowing productivity growth over time. Crouzet and Eberly (2019) show that intangible capital can explain 30 to 60 per cent of productivity declines based on firm-level and industry-level data. The failure of high-OC companies to measure and recognise their intangible capital as part of their financial reporting has an effect on enhancing the value of firms' utilisation of tax havens and has an influence on the sustainable tax behaviour of companies. Tax haven utilisation is identical to free markets, free trade, and reduced state intervention (Otusanya et al., 2023). Further, tax haven utilisation enables companies to cross international borders in order to seek low tax regimes to maximise profits and capital returns. All stakeholders must collaborate to find solutions to overcome problems faced by high OC firms related to recognising and measuring organisational capital and minimising long-term anti-social tax practices.

### 2.2 Indonesia's Regulatory Reform and Sustainable Tax Behaviour

Tax transparency is one of the points in the National Medium-Term Development Plan Indonesia Sustainable Development Goals (SDGs) (Bappenas, 2020). Indonesia has participated in the international tax cooperation initiated by the IMF, the World Bank and OECD. The Indonesian government also promotes domestic resource mobilisation and international tax cooperation through collaboration between finance and tax authorities in developing countries, such as the IMF, the World Bank, the OECD, and regional tax associations.

Indonesia's regulatory reform related to tax haven utilisation and transfer pricing began in early 2015. The obligation of Indonesian multinational firms to disclose subsidiary information in audited reports has been effective since early 2015. IFRS12, adopted by PSAK 67, requires entities to disclose each subsidiary in audited financial statements, including the name of subsidiaries, the main location of business activity and country of establishment of a subsidiary, and the proportion of ownership owned by MNEs (IAI, 2014). Practically, several companies optionally disclose the type of business and status of subsidiaries, whether they are active or inactive or direct or indirect ownership. In addition, regulation No. 169 was also issued in 2015, which is the implementation of BEPS number 4 to limit interest deductions related to cross-border financing (Republic of Indonesia, 2015). Cross-border financing is an incentive to finance affiliates located in other jurisdictions through internal loans as the variation in tax rates between jurisdictions increases.

Further, from 2016 to 2018, there were several further reforms related to transparency and transfer pricing regulations in Indonesia. In 2016, Indonesia introduced a transfer pricing regulation that requires firms to monitor documents related to related-party transactions. Indonesia's domestic regulations have implemented several BEPS action plans, including Country-by-Country (CbC) reporting. CbC reporting is applied to multinational firms with consolidated revenue of more than 11 trillion rupiahs. MNEs are required to report the global allocation of income,

tax paid, and other economic indicators. In 2018, Indonesia implemented the first exchange of global information (AEOI) together with the implementation of AEOI in tax haven countries which Indonesia's multinational firms widely use as subsidiaries, such as the British Virgin Islands, Cayman Islands, the Bahamas, Bermuda, Singapore, Hong Kong, and Mauritius (AEOI commitment, 2021; Tjondro & Tjaraka, 2023). Significant tax haven utilisation and transfer pricing regulatory reforms between 2015 and 2018 can influence the management's tax strategy decisions and the firm's sustainable tax behaviour. In terms of effectiveness, the previous study discovered that fiscal policy is a superior tool for economic stability in the short run, but it may impair growth in the long and medium ranges (Ahmad & Iqbal, 2023), specifically for high-OC firms.

2.3 Hypotheses development

Organisational capital is related to efficiency, productivity, future profits, and high stock return. Organisational capital represents a stock of knowledge, capabilities, culture, business processes, and systems that integrate human skills with physical capital to enhance organisational efficiency (Eisfeldt and Papanilau, 2013; Hasan and Uddin, 2022). Thus, according to Belo et al. (2021), labour, knowledge capital, and brand capital are the most critical inputs for explaining business value. Therefore, companies with high OC levels guarantee large future stock returns (Amatachaya and Saengchote, 2018; Boguth et al., 2021; Eisfeldt and Papanikolaou, 2013).

However, organisations with a high OC face more significant business risks than other firms. Boguth et al. (2021) found that organisational capital, specifically human capital, is associated with systematic risk. The risk of shifting key talents and invaluable information to competitors (Boguth et al., 2021; Habib et al., 2021), cash flow risk where stockholders and key talents have claims on cash flows originating from OCs, thereby increasing overall cash flow risk (Eisfeldt and Papanikolaou, 2013; Habib et al., 2021), and agency risk management can overinvest in OC, which impacts greater employment opportunities (Eisfeldt and Papanikolaou, 2013; Marwick et al., 2020). High-OC enterprises are frequently connected to restricted capital access. Marwick et al. (2020) discovered that high-OC enterprises have a more challenging time obtaining financing since intangible assets are difficult to utilise as security. Consequently, investing in OC firms has the potential to lower debt capacity and incur higher financial expenses than non-OC firms.

Although there are two perspectives on OC companies, the increase in the value of intangible capital exceeds that in tangible capital. During the 25-year study period, Juneja and Amar (2018) discovered that corporations that emphasised the OC budget as policy firms had tremendous financial success. Following Piekkola (2016), who undertook a 15-year study, OC investment enhanced the market value above what could be explained by economic analysis. Efficiency, productivity, future profitability, and a high stock return are all dependent on organisational capital, which is one of the most crucial elements in determining the value of a business. In addition, firms with a high OC guarantee considerable future stock returns and an increase in asset value relative to firms with tangible assets, which has the potential to increase firm value. Our first hypothesis is

H1: Organisational capital is positively associated with an increase in firm value.

Managing stakeholders means simultaneously creating value for multiple parties, such as customers, employees, investors, creditors, regulators, suppliers, and the environment, including society (Serrano-Cinca et al., 2021). This study focuses on employees, investors, creditors, and regulators, such as the OECD and state tax authorities, as well as investors and creditors. Investors' investment value buildup, loans obtained from creditors, and government subsidies are inputs for enterprises that are paid as dividends, taxes, personnel compensation, and interest payments (Serrano-Cinca et al., 2021a; 2021b). On the other hand, global competition is becoming more intense at both corporate and country levels. As a result, stakeholders have high expectations, specifically for OC firms, higher stock returns, higher earnings expectations, higher employee costs, and higher efficiency.

Previous studies have discussed the drivers of enterprises' connection with tax havens, including tax minimisation (Klassen et al., 2017), financial secrecy of beneficial ownership (Aziani et al., 2020), intangible intensity, intellectual property rights (Jones and Temouri, 2016 ; Karhunen et al., 2021), global networking and greater capacity to raise capital and debt (Jones and Temouri, 2016; Mukundhan et al., 2019; Sigler et al., 2020). The utilisation of tax havens is identical to outsourcing of finance and accounting activities (Eulaiwi et al., 2021; OECD, 2009; Sigler et al., 2020). Consistent with the characteristics of high-OC firms, they tend to seek the availability of resources related to technological advancement and talent in digital finance and accounting. Hoh and Tang (2021) show that financial technology and talent are drivers of enterprises to relocate finance and accounting activities. Subsidiaries in tax haven jurisdictions are responsible for the group's treasury as a whole

(Eulaiwi et al., 2021). Delatte et al. (2022) discovered that 40 per cent of global assets, including foreign direct investments (FDI), debt, and stock in tax haven countries, are aberrant, and the movement of funds cannot be tracked. Banks in tax haven countries provide significant stability and substantial regulation (Sigler et al., 2020) despite low financial rules (Hampton & Christensen, 2002). Profit-shifting activities have been shown to ma[18] multinational enterprises more lucrative and competitive than domestic enterprises (Tørsløv et al., 2018; Sigler et al., 2020).

On the other hand, several studies have found the risks inherent in enterprises with tax haven utilisation, including tax haven subsidiaries related to tax uncertainty (D[29]ng et al., 2019), financial reporting and complian[43] risk (Eulaiwi et al., 2021), transparency risk related to the nature[31]d the origin of the funds (De Simone, 2019). Eulaiwi et al. (2021) discovered that the use of tax havens had significant effects on the pricing of audit and non-audit services; therefore, companies with tax haven connections were being charged higher costs than those wi[5]ut tax haven ties. According to De Simone (2019), enterprises that exploit tax havens are typically involved in concealing the nature and origin of funds, making it difficult for tax authorities to ascertain the sources and appropriate tax liabilities associated with these funds. Tax haven utilisation may also lead to rent extraction (e.g., misuse of firm funds for personal gain, misuse of loans, and unlawful remuneration) and resource diversion (Atwood and Lewellen, 2019). Further, significant [51] haven utilisation and transfer pricing regulatory adjustments implemented between 2015 and 2018 may have an impact on the firm's sustainable tax behaviour. The earlier study found that fiscal policy may have negative effects on growth in the long and medium term (Ahmad and Iqbal, 2023), particularly for enterprises with high OC. The presence of inherent risks has the potential to undermine the link between organisational capital and firm value.

Our study indicates that the pros and cons of multinational corporations' tax havens remain a matter of contention among relevant parties. Several stakeholders believe that the tax haven utilisation can contribute to social value in the form of paying taxes for the base country, firm efficiency, meeting profit and dividend expectations, rewards for boards and employees, and financial expenses for creditors. Thus, there is a trade-off for OC firms' inherent risk. By contrast, another stakeholder group, the tax authority in the base country, controls that all revenues associated with the firm's operations in the base country are returned to that country. The disputes between these parties pave the way for the future existence of tax havens, particularly in nations that prioritise tax enforcement on enterprises. Our second hypothesis is

[22]

H2: Organisational capital has a stronger (weaker) positive association with firm value when a tax haven is utilised.

[18]

## 3. Research design

### 3.1 Data and sample

[3]

The research sample consists of 705 observations from 141 enterprises listed on the Indonesia Stock Exchange in the agriculture and manufacturing sectors as the primary sector generating the gross domestic product (GDP) from 2015 to 2019. The 2015 observation period was chosen due to the adoption of IFRS 12 in PSAK 67, which requires listed corporations to declare their st[66]s in other entities, such as local and overseas subsidiaries and their locations. Prior to 2020, the corporate tax rate in Indonesia was still 25 per cent, which is among the highest in the ASEAN area (OECD, 2020). However, the firm tax rate was reduced gradually starting in 2020. In addition, changes in domestic regulations and transparency related to multilateral information exchange that is in line with the BEPS project have led to changes in management behaviour related to tax decision-making. Variable data is obtained from the Bloomberg database, excluding tax haven subsidiaries and tax audits hand-collected from the audited financial report. The sampling technique begins with 725 observations from 145 firms with five years of complete data. Twenty observations were excluded due to the lack of data on organisational capital in 2014. The final sample is 705 firm-year observations.

### 3.2 Measurement of Organisational Capital

Based on prior research, Hasan et al. (2021) organisational capital proxy assess the accumulated inventory of human capital, brand capital, systems, and business processes recorded as selling, general, and administrative expense (SG&A) after deducting the preceding period's amortisation. SG&A components include employee training charges, system and strategic consultant payments, brand promotion activities, information technology

expenditures, and internet supply and distribution maintenance costs (Lev and Radhakrishnan, 2005). Our research has assumed an SG&A amortisation rate of 20 per cent, which is consistent with the prevailing rate in Indonesia, following Amatachaya and Saengchote (2018), who conducted an OC research in Thailand utilising a 20% amortisation rate under domestic regulation.

### 3.3 Mesurement of tax haven utilisation

Data on tax haven subsidiaries is obtained manually from audited financial reports in two stages. Initially, we locate foreign subsidiaries with direct ownership having reported by the firms. We select subsidiaries with direct ownership since the establishment of these subsidiaries is a decision made by the management of the Enterprise. Second, from the list of foreign subsidiaries per year, the jurisdictions included in the tax haven are determined based on the list of tax havens Dyreng and Lindsey (2009), Dyreng et al. (2015, 2020), Tax Justice Network (2019) top ten list, Chang et al. (2013), Dyreng et al. (2013), Palan et al. (2013), Gravelle (2015). Determination of tax haven jurisdiction is included in the tax haven list of at least two references. The list of the jurisdictions are

"Andorra, Anguilla, Antigua and Barbuda, Aruba, Bahamas, Bahrain, Barbados, Belize, Bermuda, Botswana, British Virgin Islands, Brunei Darussalam, Cape Verde, Cayman Islands, Cook Islands, Costa Rica, Cyprus, Dominica, Gibraltar, Grenada, Guernsey and Alderney, Ireland, Isle of Man, Jersey, Kitts and Nevis, Latvia, Lebanon, Liberia, Liechtenstein, Luxembourg, Macao/Macau, Maldives, Malta, Marshall Islands, Mauritius, Monaco, Montserrat, Nauru, Netherlands Antilles, Niue, Palau, Panama, Samoa, San Marino, Seychelles, Singapore, St. Lucia, St. Vincent and the Grenadines, Switzerland, U.S. Virgin Islands, Uruguay, Vanuatu, Hong Kong, Netherlands, Turks and Caicos Islands, Delaware-USA)"

The measurement scale of tax haven subsidiaries uses two proxies, specifically the number of tax haven subsidiaries per year and a dummy variable to show the existence of tax haven subsidiaries.

### 3.4 Empirical model

Model 1 tests hypothesis 1, which is indicated by β1. Table 1 presents the variable's comprehensive operational definition.

$$\text{Tobin's } Q_{it} = \alpha 0_{it} + \beta 1 OC_{it} + \beta 2 SIZE_{it} + \beta 3 ROA_{it} + \beta 4 GWTH_{it} + \beta 5 LQ_{it} + \beta 6 LEV_{it} + \beta 7 OCF_{it} + \beta 8 CAPINT_{it} + \beta 9 AUDIT_{it} + IndustryDummy_{it} + YearDummy_{it} + \varepsilon_{it} \quad (1)$$

Model 2 tests hypothesis 2, which is indicated by the β2.

$$\text{Tobin's } Q_{it} = \alpha 0_{it} + \beta 1 OC_{it} + \beta 2 OC_{it} * TH_{it} + \beta 3 SIZE_{it} + \beta 4 ROA_{it} + \beta 5 GWTH_{it} + \beta 6 LQ_{it} + \beta 7 LEV_{it} + \beta 8 OCF_{it} + \beta 9 CAPINT_{it} + \beta 10 AUDIT_{it} + IndustryDummy_{it} + YearDummy_{it} + \varepsilon_{it} \quad (2)$$

Several approaches have been adopted to overcome the potential endogeneity problem, specifically the measurement bias on the tax haven utilisation variable. The empirical test results demonstrate robust and consistent outcomes using two metrics of tax haven utilisation, indicating that tax haven utilisation acts as a stimulant that enhances the stronger positive correlation between OC and business value. Moreover, an additional test demonstrates that the use of tax havens does not increase the likelihood of tax audits for enterprises in Indonesia during the observation period. Our research indicates that a higher intensity of tax haven utilisation does not result in higher tax audit potential than firms with lower intensity. From the tax audit disclosure data, the focus of tax audits in Indonesia is on firms with lower firm value, OC and profitability, which commonly use the net operating loss carryforward to minimise taxes.

Table 1. Definition of variables

| Variable | Abbreviation | Description |
|---|---|---|
| Firm value | Tobin's Q | year-end market value plus book value of debt divided by total assets in year t. |
| Organisational capital | OC | The measurement of OC used is Hasan et al. (2021), which divides OC by total assets, instead of Peter and Taylor (2017), who use PPE as the divisor. $$OC_{i,t} = (1 - \delta oc) OC_{i,t-1} + (SG\&A_{i,t}\ x\ \lambda OC)$$ $$OC_{i.0} = \frac{(SG\&A_{i,t}\ x\ \lambda_{OC})}{g + \lambda_{OC}}$$ |

| | | |
|---|---|---|
| Tax haven subsidiaries | TH (THS) | THS is the intensity of tax haven utilisation measured by the number of subsidiaries in tax haven jurisdictions in year t. |
| Tax haven subsidiaries | TH (THdummy) | THdummy is a dummy variable to measure the existence of tax haven subsidiaries, given one if there is a subsidiary in a tax haven and 0 otherwise. |
| Firm size | SIZE | Firm size uses a natural logarithm of total assets in year t. |
| Profitability | ROA | Net income after tax divided by total assets in year t. |
| Sales growth | GWTH | The ratio of sales growth in year t compared to year t-1. |
| Liquidity | LQ | Current assets divided by current liabilities in year t. |
| Leverage | LEV | The ratio of total liabilities divided by the total assets in year t. |
| Cash flow | OCF | Cash inflow (outflow) from operating activities divided by total assets in year t. |
| Capital intensity | CAPINT | Gross property plant equipment divided by total assets. |
| Tax audit | AUDIT | Tax audit experienced by the firm, as measured by a tax assessment letter disclosed in the financial report in year t. |

**Notes:** $OC_{it}$ is OC of firm i at time t, δOC represents the depreciation rate of 20% of OC, $SG\&A_{it}$ is the firm i's SG&A expenses in year t, λOC represents the percentage growth in SG&A expenses capitalised 30% in OC inventory, $g$ represents the firm-level average SG&A expense growth rate, the previous year's accumulated organisational capital ($OC_{t-1}$) in the $OC_{i,t}$ calculation uses the perpetual inventory method to capitalise SG&A.

## 4. Empirical findings

### 4.1 Descriptive statistics

Table 2 shows the descriptive statistics of the model variables. The mean (median) OC per year is 0.1792 (0.1112) with a standard deviation of 0.2336. The number of tax haven subsidiaries owned by Enterprise is between zero to six subsidiaries per year. The average SIZE and ROA are 26.83 and 0.04881, respectively. The average sales growth per year is 0.0861. The average liquidity (LQ) and leverage (LEV) are 0.02105 and 0.3324, while the average operating cash flow (OCF) and capital intensity (CAPINT) are 0.049 and 0.439.

Table 2 Descriptive Statistics

| | Mean | Median | S.D. | Min | Max |
|---|---|---|---|---|---|
| Tobin's $Q_{it}$ | 1.778 | 1.135 | 3.064 | 0.023 | 35.33 |
| $OC_{it}$ | 0.1792 | 0.1112 | 0.2336 | 0.0065 | 3.11 |
| $THS_{it}$ | 0.4411 | 0 | 1.008 | 0 | 6 |
| $SIZE_{it}$ | 26.83 | 27.96 | 3.866 | 17.72 | 33.49 |
| $ROA_{it}$ | 0.0488 | 0.0385 | 0.1216 | -0.6057 | 0.7301 |
| $GWTH_{it}$ | 0.0861 | 0.039 | 0.9793 | -0.984 | 24.18 |
| $LQ_{it}$ | 0.0210 | 0.0147 | 0.0189 | 0.0003 | 0.217 |
| $LEV_{it}$ | 0.3324 | 0.309 | 0.2257 | 0.006 | 1.648 |
| OCF | 0.0607 | 0.049 | 0.0984 | -0.427 | 0.813 |
| $CAPINT_{it}$ | 0.4404 | 0.439 | 0.1982 | 0.001 | 0.959 |
| $AUDIT_{it}$ | 0.4511 | 0 | 0.498 | 0 | 1 |

**Note(s):** Tobin's Q represents year-end firm value, OC shows the stock of organisational capital, THS indicates the intensity of tax haven utilisation, SIZE is natural log of total assets, ROA is Return on assets ratio, GWTH is ratio of growth of sales annually, LQ represents liquidity ratio, OCF is ratio of net operating cash flow divided by total assets, CAPINT is ratio of gross property plant equipment divided by total assets, AUDIT is dummy variable of tax audit experienced by the firm.

## 4.2 Pearson correlation

Table 3 shows the Pearson correlation matrix. The results show that organisational capital positively correlates with firm value, with a significance level of less than 1%. Based on the coefficient between variables, the value is less than 0.08, meaning there is no multicollinearity between independent and control variables.

Table 3 Pearson correlation

| | Tobin's $Q_{it}$ | $OC_{it}$ | $THS_{it}$ | $SIZE_{it}$ | $ROA_{it}$ | $GWTH_{it}$ | $LQ_{it}$ | $LEV_{it}$ | $OCF_{it}$ | $CAPINT_{it}$ | $AUDIT_{it}$ |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Tobin's $Q_{it}$ | 1 | | | | | | | | | | |
| $OC_{it}$ | 0.110*** | 1 | | | | | | | | | |
| | 0.003 | | | | | | | | | | |
| $THS_{it}$ | -0.024 | -0.082** | 1 | | | | | | | | |
| | 0.531 | 0.029 | | | | | | | | | |
| $SIZE_{it}$ | 0.137*** | 0.083** | -0.133*** | 1 | | | | | | | |
| | 0.000 | 0.027 | 0.000 | | | | | | | | |
| $ROA_{it}$ | 0.302*** | 0.208*** | -0.007 | 0.191*** | 1 | | | | | | |
| | 0.000 | 0.000 | 0.851 | 0.000 | | | | | | | |
| $GWTH_{it}$ | 0.018 | -0.051 | -0.021 | 0.032 | 0.017 | 1 | | | | | |
| | 0.628 | 0.177 | 0.573 | 0.402 | 0.657 | | | | | | |
| $LQ_{it}$ | -0.073* | 0.080** | -0.043 | 0.019 | 0.278*** | -0.035 | 1 | | | | |
| | 0.054 | 0.035 | 0.252 | 0.607 | 0.000 | 0.358 | | | | | |
| $LEV_{it}$ | -0.068* | -0.115*** | 0.106*** | 0.017 | -0.423*** | 0.050 | -0.422*** | 1 | | | |
| | 0.073 | 0.002 | 0.005 | 0.652 | 0.000 | 0.182 | 0.000 | | | | |
| $OCF_{it}$ | 0.276*** | 0.155*** | -0.008 | 0.147*** | 0.513*** | -0.036 | 0.100*** | -0.217*** | 1 | | |
| | 0.000 | 0.000 | 0.833 | 0.000 | 0.000 | 0.339 | 0.008 | 0.000 | | | |
| $CAPINT_{it}$ | -0.025 | -0.193*** | 0.053 | 0.016 | -0.294*** | 0.046 | -0.404*** | 0.388*** | 0.105*** | 1 | |
| | 0.499 | 0.000 | 0.161 | 0.671 | 0.000 | 0.218 | 0.000 | 0.000 | 0.005 | | |
| $AUDIT_{it}$ | -0.087** | -0.104*** | 0.033 | 0.005 | -0.126*** | -0.047 | -0.142*** | 0.102*** | -0.028 | 0.017 | 1 |
| | 0.020 | 0.006 | 0.379 | 0.894 | 0.001 | 0.210 | 0.000 | 0.007 | 0.458 | 0.652 | |

### 4.3 Hypotheses testing

Before testing the hypothesis, multicollinearity and heteroscedasticity tests were carried out to avoid biased results. The results of the multicollinearity test in table 4 show that the Variance Inflation Factor (VIF) value is less than 10, which means that there is no multicollinearity problem in the model. Since the data is panel data, determining the estimation method to assess the data is very important. The best estimation model is determined through three stages of testing. First, the Chow test of F-test determines the proper model between Pooled OLS and Fixed Effect (FE). Secondly, the Breusch-Pagan Test determines the best panel model between Pooled OLS and Random Effect. Lastly, the Hausman Test determines the best model between Random Effect and Fixed Effect to estimate the data. The test to determine the panel data estimation method in table 4 shows a more precise estimation model using the FE model. The heteroscedasticity test of the FE model using the Groupwise test shows a heteroscedasticity problem. This study used a weighted least square (WLS) panel to overcome the problem of heteroscedasticity.

Table 4 Multicollinierity analysis and result of panel test

| | (1) Controls only | (2) Tax haven analysis No | (3) Tax haven analysis Yes | (4) Tax haven analysis Yes |
|---|---|---|---|---|
| Multicollinierity test | | | | |
| $OC_{it}$ | | 1.091 | 1.107 | 1.128 |
| $OC_{it}$*$THS_{it}$ | | | 1.017 | |
| $OC_{it}$*$THdummy_{it}$ | | | | 1.048 |
| $SIZE_{it}$ | 1.109 | 1.114 | 1.114 | 1.118 |
| $ROA_{it}$ | 1.708 | 1.723 | 1.724 | 1.726 |
| $GWTH_{it}$ | 1.019 | 1.022 | 1.022 | 1.022 |
| $LQ_{it}$ | 1.378 | 1.380 | 1.381 | 1.380 |
| $LEV_{it}$ | 1.542 | 1.543 | 1.543 | 1.551 |
| $OCF_{it}$ | 1.392 | 1.397 | 1.397 | 1.397 |
| $CAPINT_{it}$ | 1.453 | 1.479 | 1.479 | 1.480 |
| $AUDIT_{it}$ | 1.045 | 1.055 | 1.055 | 1.055 |
| Heteroskedasticity | 0.00012 | 0.00001 | 0.00014 | 0.0001 |
| Panel data estimation | | | | |
| Fixed effects estimator | 2.7935e-145 | 3.33501e-146 | 7.89971e-146 | 9.22043e-146 |
| Result | Fixed | Fixed | Fixed | Fixed |
| Random effects estimator | | | | |
| Breusch-Pagan test | 1.18964e-162 | 1.21425e-163 | 1.79937e-163 | 4.32169e-163 |
| Result | Random | Random | Random | Random |
| Hausman test | 0.000000847192 | 0.0000040585 | 0.00000837608 | 0.00000796357 |
| Result | Fixed | Fixed | Fixed | Fixed |
| Summary | Weighted Least Square | Weighted Least Square | Weighted Least Square | Weighted Least Square |

**Note(s):** Tobin's Q represents year-end firm value, OC shows the stock of organisational capital, OC*THS indicates the intensity of tax haven utilisation in OC firms, OC*THdummy is the existence of tax haven subsidiaries in OC firms, SIZE is natural log of total assets, ROA is Return on assets ratio, GWTH is ratio of growth of sales annually, LQ represents liquidity ratio, OCF is ratio of net operating cash flow divided by total assets, CAPINT is ratio of gross property plant equipment divided by total assets, AUDIT is dummy variable of tax audit experienced by the firm.

Furthermore, the results of hypothesis testing with WLS in table 5 column (2) show an OCit coefficient of 0.48320 at a significant level of 0.01, which means that OC is positively associated with firm value (H1 accepted). These findings explain that high OC firms are positively associated with higher firm value since OC firms are believed to be more efficient and productive in the long run, with more future profit and stock return potential than other companies. Therefore, consistent with Belo et al. (2021) and Piekkola (2016), OC is the main factor in explaining

the increase in firm value, and the increase in market value due to OC is very significant and cannot be explained economically.

The test results of model 2 in columns (3) and (4) show consistent results using the two proxies of tax haven utilisation, specifically THS and THdummy, that OC has a stronger positive association with firm value when tax haven is utilised. The OCit*THSit coefficient of 0.55813 at a significant level of 0.01 is greater than the OCit coefficient (0.48320), indicating that stakeholders positively value the intensity of tax haven utilisation in high OC firms. The same conclusion is also obtained regarding the existence of tax haven subsidiaries in high OC firms, which are also associated with higher firm value than companies that are not connected to tax haven jurisdictions. The coefficient value of OCit*THdummyit is 0.75025 at a significant level of 0.05, which is greater than the OCit coefficient (0.48320), or H2 is accepted. This finding corroborates the study of Tørsløv et al. (2018) and Sigler et al. (2020) that enterprises are considered more profitable than domestic firms, specifically those connected to tax havens since they are more efficient. Moreover, our study finds that tax audit disclosure in financial statements impacts the decline in firm value, which means that stakeholders consider tax audits in Indonesia a negative reputation.

Table 5 Hypotheses results

| | (1) Controls only | (2) Tax haven analysis No | (3) Tax haven analysis Yes | (4) Tax haven analysis Yes |
|---|---|---|---|---|
| Const | −0.98557*** | −1.03591*** | −1.15040*** | −1.12287*** |
| $OC_{it}$ | | 0.48320*** | 0.38278** | 0.38007** |
| $OC_{it}$ *$THS_{it}$ | | | 0.55813*** | |
| $OC_{it}$ *$THdummy_{it}$ | | | | 0.75025** |
| $SIZE_{it}$ | 0.06711*** | 0.06492*** | 0.06915*** | 0.06776*** |
| $ROA_{it}$ | 0.05777*** | 0.05787*** | 0.05849*** | 0.05969*** |
| $GWTH_{it}$ | −0.00752 | −0.00547 | −0.00370 | −0.00507 |
| $LQ_{it}$ | −0.13724*** | −0.13878*** | −0.13698*** | −0.13807*** |
| $LEV_{it}$ | 0.52886*** | 0.52265*** | 0.45293*** | 0.48795*** |
| $OCF_{it}$ | 3.54115*** | 3.52970*** | 3.48437*** | 3.50387*** |
| $CAPINT_{it}$ | 0.28161* | 0.37352** | 0.42258*** | 0.417237*** |
| $AUDIT_{it}$ | −0.40908*** | −0.41910*** | −0.43405*** | −0.421300*** |
| $Industry_{it}$ | Yes | Yes | Yes | Yes |
| $Year_{it}$ | Yes | Yes | Yes | Yes |
| Adj R-Squared | 0.69656 | 0.71342 | 0.71682 | 0.71570 |
| Prob (F-statistics) | 0.00000 | 0.00000 | 0.00000 | 0.00000 |

*** ** significant at level 0.01, 0.05

**Note(s):** Tobin's Q represents year-end firm value, OC shows the stock of organisational capital, OC*THS indicates the intensity of tax haven utilisation in OC firms, OC*THdummy is the existence of tax haven subsidiaries in OC firms, SIZE is natural log of total assets, ROA is Return on assets ratio, GWTH is ratio of growth of sales annually, LQ represents liquidity ratio, OCF is ratio of net operating cash flow divided by total assets, CAPINT is ratio of gross property plant equipment divided by total assets, AUDIT is dummy variable of tax audit experienced by the firm.

### 4.4 Robustness test

This investigation employs two distinct robustness testing methods. First, alternative tax haven utilisation measurements (THS and THdummy), where each employs a ratio scale and a dummy. Table 5 models (3) and (4) demonstrate robust results and a consistent relationship for both tax haven utilisation proxies. This demonstrates that tax haven utilisation strengthens the association between organisational capital and firm value. Second, quantile regression for testing robustness permits the examination of correlations between variables other than the mean of the data. Quantile regression appears to be effective at providing an all-encompassing perspective (Moreno-Ureba et al., 2022; Jiang et al., 2021). Using quantile regression as a robustness test allows the study to

estimate various distribution functions where each quantile indicates a different distribution function. In addition, quantile regression is also robust to outliers. Table 6 shows the three quantiles of firm value on independent and interaction variables. The test results show the measurement of organisational capital is robust at the highest quantile (0.75). This finding indicates that stakeholders value the stock of OC more in companies with high firm value, companies with large market capitalisation and book value of debt. The results of interaction testing of organisational capital and tax haven subsidiaries are robust at the lowest (0.25) and the highest quantile (0.75). These results explain that stakeholders positively value the intensity of tax havens in OC firms with extremely high or extremely low firm values since the firm outperforms other companies in terms of competitiveness and efficiency.

Table 6 Robustness test with quantile regression

| Variables | 0.25 | | 0.50 | | 0.75 | |
|---|---|---|---|---|---|---|
| | Coef | T-ratio | Coef | T-ratio | Coef | T-ratio |
| $OC_{it}$ | 0.14226 | 0.83941 | 0.50866 | 1.92196 | 0.998091 | 2.21179 |
| $OC_{it}$ *$THS_{it}$ | 0.36554 | 3.18856 | 0.39882 | 0.89479 | 0.935297 | 3.61055 |

**Note(s):** t-ratio >±1.96. OC shows the stock of organisational capital, and OC *THS indicates the intensity of tax haven utilisation in OC firms.

### 4.5 Endogeneity test

Omitted variable bias is associated with the potential for omitting control variables, which may result in outcome bias. Table 5 demonstrates that seven of the ten control variables in the research model were found to significantly influence firm value in models (1) through (4). The consistency of the test results for the control variable across all four models indicates that the problem of omitted variable bias has been minimised in this study.

### 4.6 Additional analysis

Additional analysis in table 7 shows the comparison of the average variables between companies audited and not audited by the tax authorities in year t. The comparison results show no difference in potential tax audits based on the intensity of tax haven utilisation. This finding indicates that the higher intensity of tax haven utilisation has not resulted in higher tax audit potential than companies with lower intensity. A higher potential for tax audits is found in the sample of companies that have lower firm value (Tobin's Q) and organisational capital (OC), lower profitability (ROA) and liquidity (LQ), and higher debt ratio (LEV) than other companies. Companies with lower financial performance, significant financial expenses, and incurring losses are often indicated by using net operating loss carryforward to avoid taxes (Christensen et al., 2021). As additional information, disclosure of tax audits in financial reports for corporations in Indonesia is still voluntary. There is no mandatory tax disclosure for listed companies in Indonesia. Karpoff (2021) stated that third-party laws and regulations have an essential role in deterring unethical behaviour by managers. Voluntary tax disclosure is substantive variations between companies, especially in completeness (Wang et al., 2019), since firms can selectively only disclose certain tax-related information. Chow et al. (2019) showed that the mandatory disclosure of penalties and adjustments for underpayment tax could provide evidence of management's efforts to minimize taxes. Companies are required to disclose the financial restatement after they receive the verdict (Chow et al., 2019).

The multilateral and bilateral exchange of information that began to be implemented in September 2018 has not been proven to provide future risk for enterprises through tax audits. This finding is contradicted by Borkowski and Gaffney (2021), who indicate that enterprises are identical with higher audit probabilities, interest or penalties, and tax court litigation.

Table 7 Comparing means different tests of variables between tax-audited and non-audited

| Variables | Mean different test | | | |
|---|---|---|---|---|
| | Audited by the tax authority | | Diff. | t-value |
| | Yes | No | | |
| Tobin's Q | 1.48342 | 2.02083 | -0.53741 | -2.32456 |
| $OC_{it}$ | 0.15249 | 0.20116 | -0.04867 | -2.76643 |
| $THS_{it}$ | 0.47799 | 0.41085 | 0.06713 | 0.87951 |

| | | | | |
|---|---|---|---|---|
| $SIZE_{it}$ | 2.68531 | 2.6814 | 0.03910 | 0.13359 |
| $ROA_{it}$ | 3.19365 | 6.26762 | -3.07397 | -3.36427 |
| $GWTH_{it}$ | 0.03505 | 0.12804 | -0.09299 | -1.25511 |
| $LQ_{it}$ | 1.80942 | 2.34817 | -0.53875 | -3.79377 |
| $LEV_{it}$ | 0.35778 | 0.31150 | 0.04627 | 2.72123 |
| $OCF_{it}$ | 0.05766 | 0.06319 | -0.00553 | -0.74209 |
| $CAPINT_{it}$ | 0.44409 | 0.43732 | 0.00678 | 0.45155 |
| N | 318 | 387 | | |

**Note(s):** t-ratio >±1.96. Tobin's Q represents year-end firm value, OC shows the stock of organisational capital, OC*THS indicates the intensity of tax haven utilisation in OC firms, SIZE is the natural log of total assets, ROA is Return on assets ratio, GWTH is ratio of growth of sales annually, LQ represents liquidity ratio, OCF is ratio of net operating cash flow divided by total assets, CAPINT is ratio of gross property plant equipment divided by total assets.

## 5. Conclusion and Implications

This study investigates the positive association of the level of OC with firm value. The study also shows that stakeholders, which are shareholders and creditors, positively value tax haven subsidiaries of OC firms. This result is robust using two proxies for measuring tax haven utilisation. In addition, this study supports evidence that tax haven utilisation through subsidiaries does not have the potential to increase the probability of a tax audit by the tax authorities in Indonesia. Tax enforcement through tax audits in Indonesia still emphasises companies with a low stock of OC and profitability or experiencing losses, identical to tangible-intensive firms that take advantage of net operating losses carry forward to minimise profits. A country's tax enforcement policy contributes to the competitiveness of enterprises that can manage the risks inherent in tax decision-making.

This study contributes to the international business and accounting literature in the following ways. First, this study enriches the strategic accounting literature in developing countries in the ASEAN region (Amatachaya and Saengchote, 2018) on the relationship between organisational capital and firm value, which the study is still limited. Second, this study provides new empirical evidence supporting stakeholder theory and social tax justice in the literature of international business (Serrano-Cinca et al., 2021a; Serrano-Cinca et al., 2021b; Otusanya et al., 2023) by identifying the value of tax haven utilisation as a risk trade-off in OC firms.

The results of this study need to be interpreted with caution when generalising to other sectors or countries. The results can only be generalised to the agriculture and manufacturing sectors in other developing Asian countries where these two sectors are the main contributors to the country's gross domestic product (GDP); otherwise, the corporate tax behaviour has the potential to be different. In addition, the results can be generalised to countries with strict tax audit policies so that, in general, tax audits lead to negative firm value assessments for firms in that country. This study only employs a single proxy measurement of organisational capital, which could yield different results if other measurement alternatives were utilised.

The results of this study have several important practical and policy implications. First, this study emphasises the need for consensus to address global issues related to the recognition and measurement of organisational capital to increase the competitiveness of OC firms and long-term sustainable tax behaviour. This needs to be a concern for the governments of nontax haven countries since, ultimately, it will affect the income of the base country. Second, tax authorities in nontax haven countries need to intensively utilise the exchange of tax information between countries and the disclosure of tax haven subsidiaries in financial reports as the basis for conducting tax audits for enterprises, Thereby creating a negative reputation for corporate valuation. Third, increasing transparency through mandatory tax disclosure needs to be implemented immediately. Finally, our study believes that cooperation between corporations and all stakeholders, in this case, is shareholders, creditors, government, and standard-setting bodies of accounting to overcome the ethical problems of tax haven utilisation.

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