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# Restatement and Tax Aggressiveness: Does Business Strategy Matter?

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ABSTRACT

*This study examines the effect of business strategy on restatement and tax aggressiveness. Prospectors' desire to generate large amount of external financing creates an incentive to hide true financial results. Defenders' propensityto focus on efficiency and having no desireto generate external financing prevent them to mislead investors through unsound accounting policies. Therefore, prospectors are likely to issue financial restatement relative to defenders. Prospectors are also predicted to be more aggressive in tax planning than defenders. A sample of Indonesian public firms were selected by applying purposive sampling method. Results show that business strategy has effect on tax aggressiveness but no effect on restatement. In addition, all corporate governance variables are not significantly associated with restatement.*

## 1. INTRODUCTION

Prior studies on determinants of restatement and tax aggressiveness have been extensively published in accounting literature using data from different capital markets (Habib, et al. 2021; Huang and Nardi, 2020; Salehi et al. 2020; Blaufus et al., 2019; Wang and Zhang (2018); Baber et.al 2012; Balakrishnan et al., 2012; Hoi et al. 2013; Chen et al. 2010). The evidences suggest that Board of Directors structure, audit firm attributes, auditor change, auditor tenure, securitization activities, and CEO characteristics are associated with restatementortax aggressiveness. Unlike foreign researchers, most researchers in Indonesia are more focused on the relation between business strategy on tax aggressiveness (Anggraini, et al. 2020; Faradiza 2019; Susanto et al. 2018; Wardani dan

Khoiriyah, 2018; Butar Butar, 2018; Wahyuni et al. 2018, Ihsan and Mustikasari, 2018; Surya, 2017; Kusumo and Meiranto, 2014) and the evidences are still inconclusive. The facts suggest that Indonesian researchers seem to have paid little or no attention on the association between business strategy and restatements. As far as the author knowledge, no studies have ever been conducted in Indonesia probing the issue. Evidence from emerging capital market may deepen our understanding on the role business strategy in shaping financial reporting practices in Indonesia. Therefore, this present study attempts to fill the gap and corroborate the findings form Indonesian capital market against other studies from different capital markets.

Specifically, the purpose of this study is to explore the association between business strategy and restatements in emerging capital market. In addition, this study also reexamines the association between business strategy and tax aggressiveness to add new evidence by using new data. Moreover, several control variables representing corporate governance attributes are also included to mitigate the effect of extraneous variables. Board of Commissioners independence, Board of Commissioners size, Audit Committee expertise, and institutional ownership are included as control variables because prior studies suggest that these variables are associated with restatementand tax aggressiveness (Baberetal., 2012; Larckeretal. 2007; Baberetal., 2010). In addition, leverage, firm size, growth, and profitability are also included to control for differences in firm characteristics.

Miles and Snow (1978, 2003) proposed four business strategies that map entire companies on a continum. The strategies are prospector, defender, analyzer and reactor. However, only three of which receive researchers' great interest. Researchers rarely focus on reactors because this kind of strategy is hardly to be found in the real world. Firms that exhibit prospector characteristics are companies that focus on rapid adaptation to market changes. These companies rely on product innovation, quick response to exploit market opportunities, and faster growth. Prospectors constantly strive to make changes and aggressively exploit all opportunities available in the market. On the other hand, firms with a defender strategy mainly focus on cost efficiency, narrow product domains and stable organizational structures as ways to compete with competitors (Higgins et al., 2015). Defenders rarely make changes to their product mix, maintain product image, and have no interest in exploiting new markets. Firms with analyzer strategy have characteristics that are a mixture of prospectors and defenders. Given the marked differences between prospector and defender strategy, their effects on the incidence of restatement and tax aggressiveness should be expected.

Chen etal. (2010) describe tax aggressiveness as an effort to reduce taxable income through tax planning resulting in less tax paid to the government. Furthermore, tax aggressiveness is anattitude of corporate aggression to pay lower taxes through tax planning and tax avoidance. Tax avoidance is an extreme form of tax aggressiveness (Boussaidi and Hamed, 2015). Desai and Dharmapala (2006) argue that tax aggressiveness is possible in situations that are complex and difficult to detect. Although tax aggressiveness is not a violation of the law, it is still considered dysfunctional behavior because it is driven by a desire to reduce the amount of tax that must be paid to the government. Since prospectors are more focused on product innovation and developing new markets, they are motivated to exploit every opportunity to engage in more aggressive tax reporting.

Restatement occurs when financial statements deviate from generally accepted accounting principles. Flanagan et al (2008) conducted anexploratory study of 919 restatements issued by the General Accounting Office (GAO) between January 1, 1997 and June 30, 2002. They discovered that restatements are not always associated with fraud. Some are triggered by unintentional mistakes in recording transactions relating to mergers, acquisitions, discontinued operations, stock splits and issues in different currencies. Additional analysis reveals that recognition of income, costs and expenses, and asset restructuring are the most dominating factor triggering the incidence of restatements. Meanwhile, Huron Consulting Group as cited in Abdullah et al (2010) reports that the main driving factors are income measurement, equity accounting, reserves, accruals, and contingencies. Furthermore, the likelihood of financial reporting irregularities is higher when incentive packages and company growth increase (Hogan et al., 2008).

Since prospectors pursue high growth through product innovation and developing markets in new regions, the availability of massive financing for R&D activities is urgently required. Accordingly, prospectors are motivated to prepare attractive financial statements through erroneous accounting policies. In this sense, the possibility of prospectors to restate their financial statements is expectedly high. On the other hand, defenders are primarily focused on cost leadership and thus have less incentive to manipulate accounting policies to boost earnings. In a such situation, the likelihood of restatement is expected to decrease.

Zhizhong et al (2011) collected a sample of restatements from Chinese public companies and show that effective corporate governance prevents financial restatement occurrences. More specifically, they found that the proportion of independent Commissioners and the existence of the Audit Committee are negatively related to restatement. Abdullah et al (2010) examine restatement data from Malaysian stock market and find that the number of blockholders is associated with lowerre statements. However, Board of Commissioners independence and auditor quality are not significantly associated with restatements. In addition, Audit Committeeis inversely related to restatement but the directionis not consistent with the hypothesis. Nasri and Mohammadi (2015) collected a sample fromTehran Stock Exchange and provide evidence of negative association between Board of Commissioners independence and restatement. They also find that Audit Committeeis inversely related to restatements.

## 2. LITERATURE REVIEW AND HYPOTHESIS

### Business Strategy Typology

Increased business environment uncertainties have forced firms to develop the most suited strategy to survive and prosper in fierce market competition. A well-fitted business strategy will ultimately determine future success through improving firm’s competitive advantage (Dvorský et al.,2020). Various types of business strategies along with rational behind them have been widely discussed and empirically examined in strategic management literature (Fuertes et al., 2020). The findings suggest that companies follow certain patterns to anticipate changes in surrounding business environments The most widely recognized typology is the one that was proposed by Miles and Snow (1978, 2003). They develop a business strategy typology based on the speed at which companies adjust their product mix to the changing market environment. By observing patterns that firms follow in anticipating business changes, Miles and Snow (1978, 2003) propose four business strategies: prospector, defender, analyzer, and reactor. However, previous studies in the field of management and accounting mostly compare between prospector and defender strategies due to marked differences between the two strategies (Bently et al., 2013).

Prospectors possess certain characteristics that heavily focus on product innovation, expanding market share, fast growth, and constant changes to achieve competitive advantage through offering best price and service (Wang et al., 2021). These firms require large financing in support of marketing and R&D activities which are directed to develop product mix and to react quickly to the changing business environment. On the other hand, defenders intensely direct firm resources to maintain stability, avoiding risk, and protecting the existing market through continuous improvement of their technology use (Navissi et al., 2017). They are not interested in expanding market share through product innovation but only concentrated on a narrow market.  In other word, defenders tend to develop similar products rather than developing new products. In addition, theyare continuously striving for efficiency in financing and production activities. With these characteristics, defenders pursue constant growth through market penetration. As for Analyzer, they possess characteristics that are a combination of prospectors and defenders and constantly adapt to technology, management and marketing capabilities (Bently et al., 2013). Finally, companies with reactor strategies tend to be slow in adapting environmental changes and also have less business integration( Bently et al., 2013).

Following prior studies (Wang et al., 2021; Hassan, 2021; Navissi et al., 2017, Houge et al. 2017; Bently et al., 2013), this study focuses on prospector and defender due to marked characteristics differences. Specifically, this study examines the association between the two strategies with restatement and tax aggressiveness.

**Financial Restatement**

Financial restatement, or widely stated as restatement in empirical research, occurs when financial statementsare not prepared in accordance with generally accepted accounting principles. According to Abbot etal (2004), three factors might be attributed to the incidence of restatements.First, inherent factors such as aggressive accounting practices, incorrect application of GAAP, and staffing problems. Second, inadequate internal control to prevent or detect material misstatements. Third, the failure of external auditors to detect material misstatements. Recommendation of financial restatement might be initiated by firms, auditors, or driven by regulations.

Flanagan et al (2008) conducted an exploratory study of 919 restatements issued byGeneral Accounting Office (GAO) between January 1, 1997, and June 30, 2002.They suggest that restatements must not necessarily associate with fraud but may be triggered by accounting errors resulting from mergers, acquisitions, discontinued operations, stock splits and currency issues. Furthermore, three most dominant factors driving restatement were errors in revenue, cost and expense recognitionand asset restructuring. Meanwhile, Huron Consulting Group (2003) as cited in Abdullah etal (2010) reported that the main factors driving the restatement are revenue recognition, equity accounting, reserves, accruals, and contingencies.

Previous studies consistently found that restatements were associated with declining firm values. Richardson et.al (2002) report that the stock values decline following the announcement of restatements. Hribar and Jenkins (2004) show that the cost of capital for restating firmsis higher than for non-restating firms. Palmrose et al. (2004) found that restating firms experience a negative two-day abnormal return around the restatement announcement. In addition, restatements are positively associated with bankruptcy or law suits. Restatements drive investors to have a negative view of corporate auditors. Palmrose and Sholz (2004) show that restatements trigger negative reaction from investors. Restatement also affects manager's reputation. Desai etal (2006) provide evidence that the restating firm's manager is most likely to lose his job.

The role of corporate governance mitigating financial restatements has become an interesting research topic that attracting researchers from developed and developing countries. Baber etal. (2012), Larcker etal. (2007), Abbott etal. (2004), and Agrawal and Chadha (2005) collected samples of American firms. Meanwhile, Butar Butar (2018), Zhizhong et al (2011), and La Porta et al (1999) gathered samples from developing capital markets.

**Business Strategy and Restatement**

Prospectors pursue competitive advantage through product innovations and market expansion. Accordingly, a huge external financing is required to support Research and Development (R&D) activities, especially from the capital market. Intense focuses on product innovation and product differentiation to boost sales growth requires aggressive business conducts and demand highly skillful risk-taker workers. Those involved in risky projects are expected to demand a proper compensation package in order to be willing to work in a situation where success in creating and selling new productsis highly unpredictable (Rajagopalan, 1997; Sing and Agrawal, 2002). A study conducted by Simon (1987) supports argument that prospectors exhibit aggressive behavior in spurring growth.

Prior studies documented bulk of evidence that business strategy is associated with financial reporting integrity (Hassan, 2021; Pourali, et al. 2019; Xiangfeng and Xine, 2018; Hogan et al. 2008; Bently, et al. 2013). Hogan et al. (2008) suggested that Prospectors' emphasis in rapid growth increases the likelihood of financial reporting irregularities. Rapid growth through product innovation requires large investments and massive external source of capital, mainly from equity investors. A desire to generate large amount of external fund creates an incentive to hide true financial results. Prospectors are motivated to manage investor belief in order to look good in the eyes of investors. However, such dishonest conducts may not go undetected and thus increase the likelihood of financial restatements. On the other hand, defenders that largely focuses on efficiency have no such urgency to generate external funds. No reasonable motivation to mislead investors through unsound accounting policies making incidence of restatement decreases.

Another reason that may compel prospectors to intervene financial reporting is related to compensation packages. Aggressive business conducts demand risk-taker workers. Prospectors have to offer interesting incentive to attracts skillful workers to participate in risky projects. Bentley et al. (2013) argue that compensation packages induce irregularities in financial statements. An aggressive performance-based compensation requires massive resources that is primarily generated from equity investors. In order to accomplish the necessary funds, firms should have impressive financial results to attracts investors. They are most likely to engage in accounting manipulation achieve expected targets and thus increases the likelihood of restatement. Hassan (2021) suggest that business strategy is associated with financial reporting process. Xiangfeng and Xine (2018) find that radical strategy is associated with higher earnings management.

On the other hand, defendersare less compelled to provide aggressive performance-based compensation because they are mainly concerned on finding ways to maintain product market share and less involved in high risky projects. Therefore, compensation packagesoffered by these companies do not encourage aggressive behavior (Rajagopalan, 1997; Sing and Agrawal, 2002) and it can be expected that firms with such characteristics are less likely to select inapropriate accounting policies that might lead to restatements.

Based on the preceeding discussion, relationship between business strategy and restatement is formulated in the following hypothesis:

**H1: Prospectors are more likely to restate their financial statements relative to the defenders.**

**Business Strategy and Tax Aggressiveness**

Defenders are very concerned about customer satisfaction and make every effort to protect the existing market through continuous improvement (Navissi et al., 2017). They spend much of their time and effort to find new ways to improve product qualities and lower production costs. Apart from reducing selling prices and improving product qualities, defendersare also concerned about their reputation and image. Since maintaining good image and reputation have been primarily focused by defenders, they tend to refrain from unethical conduct and deviant business practices. Pursuing competitive advantage through cost leadership and maintaining company image suppresses aggressive tax reporting behavior. Therefore, it is expected that defenders are less likely to engage in tax aggressiveness.

On the other side, characteristics of prospectors provide wider opportunities to engage in tax aggressiveness because massive capital is required to exploit new markets and create new products. Accordingly, prospectors aggressively seek opportunities to report lower income taxes in order to secure sufficient funds for intended risky projects and more likely to engage in tax aggressiveness. Prior studies examining the relationship between company characteristics and tax avoidance have reported that companies with prospector characteristics tend to engage in tax avoidance (Mills et al., 1998; Phillips, 2003). Similarly, recent studies also reported that business strategy is associated with tax aggressiveness. Wang (2017) shows that prospectors are more likely involved in tax avoidance. Higgins et al. (2015) reported that prospectors have higher propensity to engage in tax aggressive behavior. Sadjiarto et al. (2020) reported that prospectors are associated with higher tax avoidance. Based on the preceding discussion, the relationship between business strategy and restatement can be formulated in the following hypothesis:

**H2: Prospectors engaged in greater tax aggressiveness than defenders**

## 3. RESEACH METHOD

### Sample

The sample is firms listed on Indonesia Stock Exchange for the period of 2014-2018. The necessary data were collected from annual reports and had been downloaded from www.idx.co.id. As much as 1630 firm-year observations were available after applying a purposive sampling method. Table 1 presents sample selection procedure in detail.

**Table 1. Sample Selection Procedure.**

| Descriptions | Company-years |
|---|---|
| Firm-year observations in the period of 2014-2018. | 2664 |
| Delisted firms during sample period. | (49) |
| Firms belong to the insurance, securities and banking industry. | (550) |
| Annual reports are stated in US Dollars as a denominator. | (247) |
| Annual reports are unavailable from the data source. | (188) |
| Total Observations | 1630 |

### Model Specification

As described earlier, the purpose of this study is to test the effect of business strategy on restatements and tax aggressiveness. Two separate regression models are employed to test hypotheses. Model 1 is estimated with logistic regression to test the effect of business strategy on restatement. Model 2 is estimated with multiple regressions to assess the role of business strategy on tax aggressiveness. Note that eight control variables are included in the model to control for differences in corporate governance practices and firm characteristics.

Model 1: $Restate_{it} = \beta_0 + \beta_1 Strategy_{it} + \beta_2 BdIndp_{it} + \beta_3 BdSize_{it} + \beta_4 AudCom_{it-} + \beta_5 Inst_{it} + \beta_6 Lev_{it} + \beta_7 Size_{it} + \beta_8 Growth_{it} + \beta_9 ROA_{it} + \varepsilon_{it}$

Model 2: $CETR_{it} = \beta_0 + \beta_1 Strategy_{it} + \beta_2 Bd\_Indp_{it} + \beta_3 Bd\_Size_{it} + \beta_4 AudCom_{it-} + \beta_5 Inst_{it} + \beta_6 Lev_{it} + \beta_7 Size_{it} + \beta_8 Growth_{it} + \beta_9 ROA_{it} + \varepsilon_{it}$

Where,

Restate = *Restatment*
Strategy = Business strategy
CETR = Tax Aggressiveness

| | |
|---|---|
| BdIndp | = Board of CommissionersIndependence |
| BdSize | = Board Size |
| AudCom | = Audit Committee Expertise |
| Inst | = Institutional Ownership |
| Lev | = Leverage |
| Size | = Company size |
| Growth | = Company Growth |
| ROA | = Profitabilitas |

## Variable Measurements

### Business strategy

Following Navissi et al. (2017), four ratios were used to capture dimensions of business strategy: (1) ratio of general and administrative expenses to total sales (to capture marketing efforts); (2) percentage change in annual sales (to capture growth patterns); (3) employee to sales ratio (to capture production efficiency); (4) standard deviation of the number of company employees (to capture organizational stability). For each year, the four variables are sorted from lowest to highest and grouped into five quintiles. Each group is given a score of 1 to 5. Thus, a company that scores 1 will have a total score of 4, which is the lowest score. A company that scores 5 for the four variables will have a score of 20, which is the highest score. The final scores will be in the range of 4-20. The next step is to calculate the median score. The total score for each company is then compared to the median value. Business strategy is a dummy variable that takes 1 if the score is above median and classified as prospectors. Likewise, a firm is classified as defenders if its score is below median.

### Restatement

Restatement is a dummy variable that takes 1 if a company restated its financial statement and 0 otherwise. Information on restatements is observed manually from financial statements. Note that restatement might be triggered by the application of new standards, earnings management, mergers and acquisitions, and mathematical errors. This study does not take into account the causes of restatements from merger and acquisition, stock split, and mandatory changes in accounting standards. These factors are part of regular events that may cause restatements but they should not be regarded as intention restatements (Plumlee and Yohn, 2010; Hennes et al. 2012; Lobo and Zhao, 2013).

**Tax Aggressiveness**

Following Desai and Dharmapala (2006), tax aggressivenessis measured as a ratio of tax paid in cash to income before tax (CETR = tax paid / income before tax). For ease of interpretation, CETR is multiplied with -1 so that the higher CETR ratio suggests higher tax aggressiveness.

**Control Variables**

**Board of CommissionersIndependence**

Aggressive behavior that triggers restatement and tax aggressiveness is an example of dysfunctional behavior. Prior studies have reported that Board of Commissioners independence is negatively associated with manager dysfunctional behavior (Beasely, 1996; Klein, 2002, Xie et al., 2003). Thus, it is expected that Board independence is negatively associated with restatement and tax aggressiveness. The Board of Commissioners independence is measured as a proportion of independent Commissioners to the total of the Board of Commissioners.

**Audit Committee Expertise**

Previous studies have shown that the Audit Committee expertise is negatively associated with lower abnormal accruals, restatements, and cases of lawsuits (Abbot et al, 2004; Bedard et al., 2004; Agrawal and Chadha 2005). Thus, it is reasonable to control this variable. Audit Committee expertise is measured as the proportion of Audit Committee members who have backgrounds in accounting or finance. It is expected that Audit Committee expertise is negatively associated with restatement and tax aggressiveness.

**Institutional Ownership**

Previous studies found that ownership concentration reduces agency problems (Shleifer and Vishny, 1986; La Porta et al., 1999). Effective monitoring by institutional investors may prevent managers from manipulating financial reporting for private gain (Hartzell et al., 2014). Institutional ownership is measured as a percentage of shares owned by institutional investors. It is expected that institutional ownership is negatively associated with restatement and tax aggressiveness.

**Firm Characteristics**

Firm size, leverage, sales growth, and profitability were previously reported to have an effect on restatement and tax aggressiveness (Chen et al., 2010; Bentley et al., 2013). For this reason, these variables are included in the model to control for the differences in firm characteristics. The control variables are measured as follows: 1) firm size is Ln total. 2) leverage is the ratio of total debt to total assets. 3) Sales growth is current sales minus last year sales divided by current sales. 4) Profitability is the ratio of net income to total asset. These variables, except leverage, are expected to be negatively associated with restatement and tax aggressiveness

## 4. RESULT AND DISCUSSION

**Descriptive Statistics**

**Table 2. Descriptive Statistics**

| Variabel | N | Minimum | Maximum | Mean | Stand. Dev |
|---|---|---|---|---|---|
| Restate | 1420 | 0 | 0.039 | 0.036 | 0.188 |
| CETR | 1420 | -2.633 | 2.246 | 0.234 | 0.422 |
| Strategy | 1420 | 0 | 1 | 0.641 | 0.479 |
| Bd_Indp | 1420 | 0.167 | 0.833 | 0.406 | 0.101 |
| Bd_Size | 1420 | 2 | 10 | 4,170 | 1,702 |
| AudCom | 1420 | 0,250 | 1 | 0,730 | 0.245 |
| Inst | 1420 | 1.950 | 100 | 0.657 | 0.210 |
| Size | 1420 | 21.361 | 33.474 | 28.575 | 1.601 |
| Lev | 1420 | 0.002 | 2.617 | 0.467 | 0.253 |
| Growth | 1420 | -1. 000 | 2.152 | 0.079 | 0.296 |
| ROA | 1420 | -1.465 | 0.920 | 0.038 | 0.199 |

As much as 1630 firm-years observations were available for further analysis. However, 210 observations were eliminated to minimize the effect of extreme values on the results. After going through the process of elimination, the remaining observations for the test of hypothesis are 1420. Table 2 displays descriptive statistics of variables in the study.

Note that Restate is a dummy variable that has a mean of 0.036. It suggests that 3.6% of observations or about 51 are restating firms. Meanwhile, the mean for tax aggressiveness

(CETR) is 0.234, suggesting that the tax rate imposed on sample firms is 23.4%. Corporate strategy (Strategy), which is a dummy variable, has a mean of 0.641, suggesting that 64.1% of observations adopted the defender strategy. While the remaining 35.9% employs a prospector strategy. Mean for Board of Commissioners independence (Bd_Indp) of 0.406 indicates that 40.6% of Board of Commissioner members are from outside the company. The mean of 4,170 for Board size (Bd_Size) suggests that on average the Board of Commissioners consists of four or five people. Meanwhile, the mean for background of the Audit Committee (AudCom) and institutional ownership are 0.730 and 0.657, respectively. These numbers suggest that 73% of firms' Audit Committee have an accounting or financial background and 65.7% of the shares are owned by institutional investors. As for control variables, the statistics suggest that sample firms are medium-sized firms with a growth rate of 7.9%, moderate leverage level with the mean for debt to total asset ratio of 43.7% and low profitability with net income to asset ratio of 3.8%.

**Correlation Coefficients**

**Table 3. Correlation Coefficient**

| | Restate | CETR | Strategy | Bd_Indp | Bd_Size | AudCom | Inst | Size | ROA | Lev | Growth |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Restate | 1 | 0.011 | -0,018 | -0.021 | 0.005 | -0.033 | -0,041 | 0,030 | 0.009 | -0,013 | -0,034 |
| CETR | 0.011 | 1 | -0.062* | -0.053* | -0.030 | 0.051 | -0,033 | -0,005 | 0.147** | -0,016 | 0,064* |
| Strategy | -0.018 | -0.062* | 1 | 0.024 | -0.001 | -0.056* | 0,044 | -0,020 | -0.008 | -0,026 | 0,047 |
| Bd_Indp | -0.021 | -0.053* | 0.024 | 1 | -0.061* | 0,011 | 0,056* | 0,066* | 0.013 | 0,120** | 0,008 |
| Bd_Size | 0.005 | 0.030 | -0.001 | -0.061* | 1 | -0.023 | -0.070** | 0.560** | 0.157** | 0.037 | 0.014 |
| AudCom | -0.033 | 0.051 | -0.056* | 0.011 | -0.023 | 1 | 0,118** | -0,023 | 0.006 | 0,008 | -0,018 |
| Inst | -0.041 | -0.033 | 0.044 | 0.056* | -0.070** | 0.118** | 1 | -0,168** | 0.028 | -0,041 | 0,017 |
| Size | 0.030 | -0.005 | -0.020 | 0.066** | 0.560** | -0.023 | -0,168** | 1 | 0.156** | 0,106** | 0,085** |
| ROA | 0.009 | 0.147** | -0.008 | 0.013 | 0.157** | 0.006 | 0.028 | 0.156** | 1 | -0.270 | 0.178** |
| Lev | -0.013 | -0.016 | -0,026 | 0.120** | 0.037 | 0,008 | -0,041 | 0,106** | -0.270** | 1 | -0,026 |
| Growth | -0.034 | 0.064* | 0,047 | 0.008 | 0.014 | -0,018 | 0,017 | 0,085** | 0.178** | -0,026 | 1 |

*Signifikan pada tingkat 5%, **Signifikan pada tingkat 1%

Table 3 shows that restatement (Restate) and strategy are not statistically correlated (two tails). Similarly, none of the control variables is correlated with strategy. Correlation between dependent variables and independent variables is presented first to see the pattern of the relationship between these variables. Table 3 presents the correlation coefficients for all variables. However, discussion is focused on the correlation between strategy and restatement and on the correlation between strategy and ax aggressiveness. These are preliminary evidences to reject H1. On the other hand, tax aggressiveness (CETR) and strategy are negatively correlated at 10% level of significance. Three control variables are statistically correlated with CETR at 1% and 5%. More specifically, CETR is negatively correlated with Bd_Indp at 5%. CETR and ROA are positively correlated at 1%. Significant correlation is also found for CETR and Growth at 5%. The correlation results provide preliminary evidence to accept H2.

**Results**

Hypothesis one (H1) posits that the prospectors are more likely to issue financial restatements relative to the defenders. Hypothesis two (H2) posits that the prospectors are engaged in greater tax aggressiveness than defenders. The two hypotheses are tested by estimating two separate regression models as described earlier. Logistic regression is used to estimate Model 1 and multiple regressions analysis is used to estimate Model 2. Table 4 presents the estimation results for the two models.

Estimation of Model 1 shows the likelihood of issuing financial restatements is no different between prospectors and defenders as indicated from p-value of 0.573. The result suggests that business strategy is not associated with restatement. Similarly, all control variables are statistically insignificant at the traditional level of significance, suggesting that corporate governance and firm's characteristics differences have no effect on the incidence of restatements. Thus, H1 is not supported statistically.

On the other hand, estimation of Model 2 shows that business strategy is positively associated with tax aggressiveness. Note again that strategy is a dummy variable that takes 1 for prospectors and 0 for defenders. The positive coefficient suggests that CETR of prospectors is greater than of defenders with p-value of 0.029. In other word, firms with prospector strategy are engaged in tax aggressiveness more than defenders. Thus, H2 is statistically supported.

As for corporate governance variables, the results show that Board independence (BdIndp), Audit Committees expertise (Aud_Com) and institutional ownership (Inst) are negatively associated with tax aggressiveness (CETR). Specifically, the correlation between CETR and BdIndp is significant at the 10% level. The correlation between CETR and institutional ownership is significant at the 10% level as well. However, the correlation between CETR and Aud_Com is significant at 5% level. Similar results are also found for firms' characteristics variables. Specifically, the correlation between CETR and ROA is significant at 1%. The correlation between CETR and size is significant at 10%. Lastly, the correlation between CETR and growth is significant at 10%

**Table 4. Regression Results**

| | *Expected Sign* | Model 1 | | Model 2 | |
|---|---|---|---|---|---|
| | | Wald-Stat | *P-value* | T-Stat | *P-value* |
| Strategy | + | 0.317 | 0.573 | 2.188 | 0.029 |
| BdIndp | - | 0.638 | 0.424 | 1.875 | 0.061 |
| BdSize | - | 0.557 | 0.455 | -1.007 | 0.314 |
| Aud_Com | - | 1.321 | 0.250 | -2.011 | 0,044 |
| Inst | - | 1.235 | 0.266 | 1.704 | 0,089 |
| Size | - | 1.704 | 0.192 | 1.815 | 0,070 |
| Lev | + | 0.205 | 0.650 | -1.229 | 0,219 |
| Growth | - | 2.206 | 0.137 | -1.775 | 0.076 |
| ROA | - | 0.167 | 0.683 | -5,441 | 0.000 |

## Discussions

### Association Between Business Strategy and Restatement

As previously discussed, firms tend to choose a business strategy that best fits their surrounding business environment. In order to anticipate rapid and unexpected changes in the business environment, prospectors are more likely to focus on introducing new products and actively exploiting opportunities to create new markets in areas that have never been entered. Such an aggressive strategy requires large external financing to support research and product development activities. As a consequence, prospectors must find ways to attract investors, and one of them is through manipulating accounting policies to present impressive financial performance. But note that overly emphasis on innovation creates greater uncertainty of the outcome. Risky projects require risk-taking managers. The compensation package must be designed in certain ways to encourage managers to take risks. The compensation package associated with aggressive behavior increases the likelihood of financial misreporting (Burns and Kedia, 2006; Efendi et al., 2007) and in turn triggers restatement.

On the other hand, defenders are more focused on cost leadership and confined to less risky products. Intense focus on efficiency lowers the risks associated with market demand of their products. In addition, defenders are more inclined to choose product efficiency for they possess sufficient knowledge of the competitiveness landscape. They concentrate on maintaining existing product market share. Since the strategy does not require aggressive behaviors, the compensation packages offered by defenders do not encourage aggressive behaviors (Rajagopalan, 1997; Sing and Agrawal, 2002). Therefore, motivations for seeking massive external financing and the urge to window dress financial reports is expectedly lower. As a result, the likelihood of financial restatement remains low. Bentley et al. (2013) examine the effect of business strategy on financial reporting irregularities and find that prospectors are more likely to experience financial irregularities.

Contrary to the prediction, the evidence shows that business strategy is not significantly associated with restatements. Moreover, it is not consistent with prior studies documented in Hassan (2021), Pourali, et al. (2019), Xiangfeng and Xine. (2018), Hogan et al. (2008). These studies showed that business strategy has significant effect on financial reporting policies. The insignificant result is probably related to the sample characteristics. Descriptive statistics show that on average the sample is taken from medium-sized companies with moderate growth rates and low debt levels. The fact that firm samples have a relatively low level of debt suggests that these firms require no large external financing to support profit creation activities. In this stable condition, firms are not inherently compelled to manipulate financial statements which might trigger restatements. Future research should address the problem and gather sample with more heterogeneous characteristics. Another possible explanation is the procedure used in this study to distinguish restating and non-restating firms might be inaccurate. As described before, firm samples were divided into restating and non-restating firms based on observation in annual reports without giving consideration to the reasons underlying restatements. It is possible that a firm restated its financial statement due to reasons other than accounting error. Incorrect inclusion of firms as restating firms may lessen the effect of business strategy on restatements. Therefore, future research should consider reasons for restatements when dividing firm samples into restating and non-restating firms.

**Association Between Business Strategy and Tax Aggressiveness**

The test of hypothesis suggests that prospectors are more aggressive in managing tax planning relative to defenders. Prospectors intensely pursue product innovation and seek new business opportunities. They are willing to take risks to attain high growth. Consequently, prospectors tend to take aggressive actions to exploit any opportunities available to reduce tax spending and save sufficient cash to finance new investment projects. On the other hand, defenders are mainly focused on maintaining reputation, image and cost leadership. Maintaining stability through narrow and stable product and avoiding financial reporting risks are the goals (Bently et al., 2013). Such different focuses have implications for corporate tax management. Martinez and Ferreira (2019) suggest that effective tax planning provides an opportunity to reduce tax burden.

The evidence found in this study is consistent with Phillips (2003), Higgins et al. (2015), and Sadjiarto et al. (2020). Phillips (2003) found that firms with prospector characteristics are more likely to engage in tax avoidance suggesting more aggressive behavior toward tax planning. Higgins et al. (2015) state that different focus of the two strategies are reflected in the organizational structure, risk tolerance, and strategic focus of the company. Defenders tend to avoid risks and have centralized organizational structures. Prospectors, on the other hand, are more willing to take risks and tend to have a decentralized organizational structure. They examine the effect of business strategy on tax aggressiveness by employing three measures; book effective tax rate, cash effective tax rate, and permanent book-tax differences. The test results show that prospectors have lower book and cash effective tax rates and higher permanent book-tax differences suggesting that prospectors are more aggressive in their tax policies relative to defenders. Additional test reveals that prospectors are more likely to operate in tax haven countries. Sadjiarto et al. (2020) found that prospectors exhibit more aggressive behavior on tax reporting practices.

Martinez and Ferreira (2019) analyze the typology of business strategies in Brazil. The analysis shows that most Brazilian companies have the characteristics of an analyzer which is a mixture of prospectors and defenders. Furthermore, companies that adopt the defender and prospector strategy are 21% and 1.76% respectively. They also tested whether prospector firms are more inclined to tax aggressiveness than defenders. Surprisingly, they found that defenders engaged in more aggressive tax planning than prospectors.

**Corporate governance and the firm's characteristics**

The presence of independent commissioners is expected to improve monitoring function of the Board of Commissioners. Unique expertise and experience an independent commissioner bring into the company enhance the ability of the Board of Commissioners to detect financial reporting manipulation. In addition, independent commissioners are expected to have higher motivation in supervising managers for the need to show impressive performance which increases their reputation in the labor market. They also have a stronger incentive to maintain shareholders' belief in their capabilities for the sake of future career. Related to monitoring functions, independent Commissioners are expected to be able to escape pressure from managers when voicing criticism and providing suggestions to uphold good corporate governance. They can act impartially when discussing supervisory issues, including financial reporting process. Consequently, effective monitoring toward financial reports mitigates the opportunities for managers to exploit company resources for personal gain. It also prevents managers from hiding the dysfunctional behavior through certain accounting policies. Tendency for managers to use accounting policies that do not reflect economic reality can be suppressed or even eliminated and in turn reduces the incidence of restatements. The logic for including an independent commissioner to enhance the Board's monitoring function is also applied to the size of the Board of Commissioners. The larger Board of Commissioners is expected to increase monitoring function.

However, the test results only find a weak relationship between Board of Commissioners size and restatement with p-value of 0.061 and no significant effect of Board independence on restatement. The evidence suggests that the Board of Commissioners was not able to perform effective monitoring function. In particular, independent commissioners seem to fail to contribute to effective monitoring. The insignificant effect may be partially explained by the process of hiring independent commissioners. It should be noted that the firm's directors may have contributed to the process of appointing independent commissioners. The situation can create a conflict of interest which may harm the loyalty of the independent commissioner to stockholders

(Pass, 2004). As a consequence, an independent commissioner may not perform well in carrying out his monitoring function.

Similar result is also found for tax-aggressiveness. The existence of independent commissioners has no effect on corporate tax management policy. The result may be explained by using the argument of tax avoidance benefit for shareholders. As a shareholder's representative, the Board of Commissioners must put shareholders' interests before other things in companies. From this perspective, aggressive behavior toward tax policies might bring positive consequences on shareholders. Conceptually, tax avoiding activities would generate cash flow to the companies enabling them to invest in many projects. These projects generate more profit that attracts more investors to buy more stocks. In turn, high demand for the company's stock drives stock prices up. On the other hand, tax avoidance may be deemed unethical by some investors and independent commissioners are expected to prevent the unethical business practices.

Audit Committees with accounting or financial backgrounds are expected to have necessary skills to prevent financial reporting irregularities. A number of studies show that the Audit Committee with a financial or accounting background is better able to prevent unhealthy accounting practices and thus reducing the occurrence of restatements. But this study finds no evidence of such convictions suggesting that restatement can occur in any companies regardless of Audit Committee background. The result is rather confusing. It is difficult to explain why Audit Committee with financial or accounting background are not associated with the incidence of restatements. One possibility is that the measure of restatements in this study is unreliable to distinguish between restatement triggered by mistakes in selecting accounting policies and restatement caused by other reasons such as mergers or new standards imposed by accounting authorities. As stated before, this study does not take into account the reasons for restatements. It could be triggered by unintentional errors in applying sound accounting policies or other reasons irrelevant of accounting such as mathematical errors or mergers. In addition, there is a possibility that a company issues financial restatement due to errors in interpreting a particular accounting standard.

Contradictory results are found for tax-aggressiveness. The results suggest that Audit Committee with accounting or finance background have the capability to mitigate managers' aggressive behavior toward tax planning. Effort to opportunistically reduce tax spending can be considered dysfunctional behavior because it causes negative effects on government which has responsibility to provide infrastructures needed for businesses to grow and thrive in the profit-making process. Effective Audit Committee functions can only be achieved through adequate understanding of accounting and financial issues encountered by in daily activities.

Firms with high institutional ownership are expected to reduce the incidence of restatements. Institutional investors arguably have sufficient capacity and resources to monitor companies. The capacity to close scrutiny over strategic and financial issues mitigate the opportunities for managers to influence financial reporting. Accordingly, errors in the presentation of financial statements can be prevented and the possibility of restatement is decreased. However, the evidence found in this study is not consistent with the predictions. It seems that institutional investors fail to exercise its monitoring function effectively. One possible explanation is due to the small number of shares that institutional investors have that causes them to be reluctant to monitor managers. This possibility can be rejected because the descriptive statistics show that on average institutional investors own 63.5% of firm samples' stocks. The percentage is quite large to be able to perform close monitoring on companies. Another possibility is that the procedure to determine restatement in this study does not distinguish the causes of restatement as previously stated.

Firms with higher institutional ownership are predicted to be less aggressive in their tax policies. But the results are not consistent with the prediction. It is probably due to the benefit of tax avoidance for institutional investors. Institutional investors are primarily concerned with managerial opportunistic behavior that is inconsistent with their interests. From the standpoint of institutional investors, tax aggressiveness does not have a negative effect on their stock investments. On the contrary, tax aggressiveness might enhance firm value because the amount of cash that is supposed to be paid to the government can be diverted to finance profitable projects which have a positive effect on the firm's stock price. Thus, the aggressive tax policies are not associated with the number of shares owned by institutional investors.

As for the firm's characteristics, the results show that firm size, growth, and profitability are associated with tax aggressiveness. The evidence is consistent with Zheng et al. (2019). In addition, firm size, leverage, growth and profitability have no effect on the restatement. The insignificant results are consistent with Bentley et al. (2013). Taken together, the evidence suggests that the firm's characteristics matter only in tax planning.

## 5. CONCLUSION

In increasingly fierce competition, companies must adopt strategies that help improve their firm's competitiveness. Two business strategies have received wide attention of academics and researchers. Prospectors emphasize product innovation and rapid market response to achieve intended growth rates. They are striving to make changes and very aggressive to exploit any opportunities in the market. On the other hand, defenders are intensely focused on efficiency and stability and not interested in product innovations.

Since prospectors are actively engaged in product innovation and developing new markets, large cash flow is needed to support those activities. The need for large funds encourages companies to engage in more aggressive tax reporting than defenders. On the other hand, defenders are not relatively aggressive in managing taxes because they do not want to create a negative impression that can damage the company's image and reputation. In addition, defenders do not have many opportunities to engage in tax aggressiveness because they are rarely involved in risky projects and have no desire to rapid growth providing fewer opportunities to aggressive behavior.

A part from tax aggressiveness, prospectors and defenders also differ in the likelihood of restatements. Prospectors' focus on rapid growth through product innovation and market expansion require large external financing for R&D activities. They must attract investors to invest in the company. One way is to constantly display impressive financial performance. Prospectors are compelled to window dress financial statements through inappropriate accounting policies. Mistakes in choosing sound accounting policies increase the likelihood of restatements. On the other hand, defenders that prioritize efficiency and cost leadership do not have an urgent need to obtain large numbers of funds. Thus, the motivation to choose inappropriate accounting policies to make a better financial report is diminished, and the incidence of financial restatement can be avoided.

This study examines the effect of corporate strategy on tax aggressiveness and restatement. To increase the validity of the research results, eight control variables related to company characteristics and corporate governance are included in the regression model.

The control variables are firm size, leverage, growth rate, profitability, board of commissioners independence, board of commissioners size, audit committee expertise, and institutional ownership.

The regression results show that while business strategy has a significant effect on tax aggressiveness, no significant effect found for restatements. As for control variables, board of commissioners independence, board of commissioners size, audit committee expertise, and institutional ownership are not associated with restatement. Conversely, board of commissioners independence, audit committee expertise, and institutional ownership are significantly associated with tax aggressiveness. Taken together, the results suggest that business strategy and corporate governance play a significant role in managers' aggressive behavior toward tax planning but not for the incidence of financial restatements. As for the firm's characteristics, results show that firm size, leverage, growth and profitability are not significantly associated with restatement. The insignificant results are consistent with Bentley et al. (2013). On the contrary, firm size, growth, and profitability are significantly associated with tax aggressiveness. The findings are consistent with Zheng et al. (2019). Taken together, the evidence suggests that the firm's characteristics matter only in tax planning.

## 6. LIMITATIONS AND SUGGESTIONS

None of the independent variables have significant effects on restatement, which raises the issue of measurement. As described before, it is possible that a firm restated its financial statement due to reasons other than accounting error. Incorrect inclusion of firms as restating firms may result in no association between all independent variables, including business strategy, with restatements. In addition, the number of companies classified as restated firms is only 3,6%, making the conclusion need to be made carefully. Therefore, subsequent research needs to consider restatement measurements which are limited only to the application of inappropriate accounting policies. Companies that perform restatements due to mergers and changes in accounting standards should be excluded from the sample. For tax aggressiveness, future studies need to consider real tax cases to enhance the validity of results.

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