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The unfavorable effect of CEO narcissism: The role of the audit committee

Riesanti Edie Wijaya*, Coansheline Amathya Mansula Kweniati

Universitas Surabaya, Surabaya, East Java, Indonesia

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ABSTRACT

Narcissism is often considered a behavioral disorder that has negative impacts, especially for top management. The audit committee, as part of the governance system, plays a major role in suppressing such negative behavior. The purpose of this study is to examine the role of the audit committee in suppressing the negative impacts of CEO narcissism. This quantitative research uses secondary data obtained from the websites of manufacturing companies listed on the Indonesia Stock Exchange (IDX) for the period 2017 – 2020, consisting of 266 companies. Sampling is conducted using purpos-ive sampling method. The operational variables used in this study are CEO narcissism, audit committee, and tax avoidance. The results of this study show that CEO narcissism has a negative and significant effect on effective tax rate (ETR). In addition, the results of this study also show that the audit committee (AC) is unable to influence management decisions in car-rying out tax avoidance. The agency theory is unable to explain how the audit committee positions itself in narrowing asymmetry of information between agents and principals. On the other hand, institutional theory can explain the inability of the audit committee in carrying out its monitoring function. According to institutional theory, the existence of an audit committee in the company is merely a formality.

ABSTRAK

Narsisme sering dianggap sebagai gangguan perilaku yang berdampak negatif, terutama bagi manajemen puncak. Komite audit, sebagai bagian dari sistem tata kelola, memegang peranan besar dalam menekan perilaku negatif tersebut. Tujuan dari penelitian ini adalah untuk mengkaji peran komite audit dalam menekan dampak negatif narsisme manajemen. Penelitian kuantitatif ini menggunakan data sekunder yang diperoleh dari situs web perusahaan manufaktur yang terdaftar di Bursa Efek Indonesia (BEI) periode 2017 – 2020 yang terdiri dari 266 perusahaan. Pengambilan sampel dilakukan dengan menggunakan metode purposive sampling. Variabel operasional yang digunakan dalam penelitian ini adalah narsisme manajemen, komite audit, dan penghindaran pajak. Hasil penelitian ini menunjukkan bahwa narsisme manajemen berpengaruh negatif dan signifikan terhadap effective tax rate (ETR). Selain itu, hasil penelitian ini juga menunjukkan bahwa komite audit (KA) tidak mampu mempengaruhi keputusan manajemen dalam melakukan penghindaran pajak. Teori keagenan tidak mampu menjelaskan bagaimana komite audit memposisikan dirinya dalam mempersempit asimetri informasi antara agen dan prinsipal. Di sisi lain, teori institusional dapat menjelaskan ketidakmampuan komite audit dalam menjalankan fungsi pengawasannya. Menurut teori institusional, keberadaan komite audit di perusahaan hanya sekadar formalitas.

* *Corresponding author, email address: riesanti@staff.ubaya.ac.id*

1. INTRODUCTION

Tax revenue is the largest contributor to the Indonesian Government. Figure 1 shows that the source of central government revenue is mostly from taxes. The figure below also shows the government's efforts to increase tax revenue, as evidenced by the increasing trend in tax revenue realization from 2007-2024. As stated by the Minister of Finance in a press conference on June 26, 2023, on the official website of the Ministry of Finance, there was an increase in the contribution of Corporate Income Tax by 28.7% of total tax revenue at the end of 2023.

However, this is not in line with the wishes of the industry. For companies, taxes can reduce the company's net profit that will be distributed to shareholders. The desire to obtain high profits, by minimizing taxes, encourages company management to carry out tax evasion (TA) strategy. For the government, tax avoidance can reduce state revenues and is considered an unethical act (Goldman & Lewellen, 2020). Tax Justice Network (2020) reported an annual tax loss caused by tax avoidance of $4,785,952,836. This implies that tax avoidance practices are common in Indonesia.

The accounting policies chosen by a company are actually a social choice (May & Sundem, 1976). Furthermore, the selection of accounting policies is closely related to top management, especially the CEO. The choice of financial accounting has the potential to avoid tax and vice versa (J. R. Graham et al., 2011; Jacob et al., 2021; Shackelford & Shevlin, 2001). Empirically, Dyreng et al. (2010a) and Payne and Raiborn (2018a) prove that management is the main determinant of tax avoidance in companies. Thus, the management determines how company's accounting reporting will be (Plöckinger et al., 2016). The selection of accounting policies is based on management's interpretation of the various strategic situations faced by the company (Conley et al., 2019). Furthermore, the selection of accounting policies is also influenced by the characteristics of a company's management (de Almeida & Lemes, 2019). One of the theories that can explain this phenomenon is the Upper Echelons Theory (UET) (Hambrick & Mason, 1984). UET also has the concept that the economic behavior of management personally reflects the experience, values, and personality of the executive (Arijit & Hambrick, 2007). Based on this theory, this study focuses on

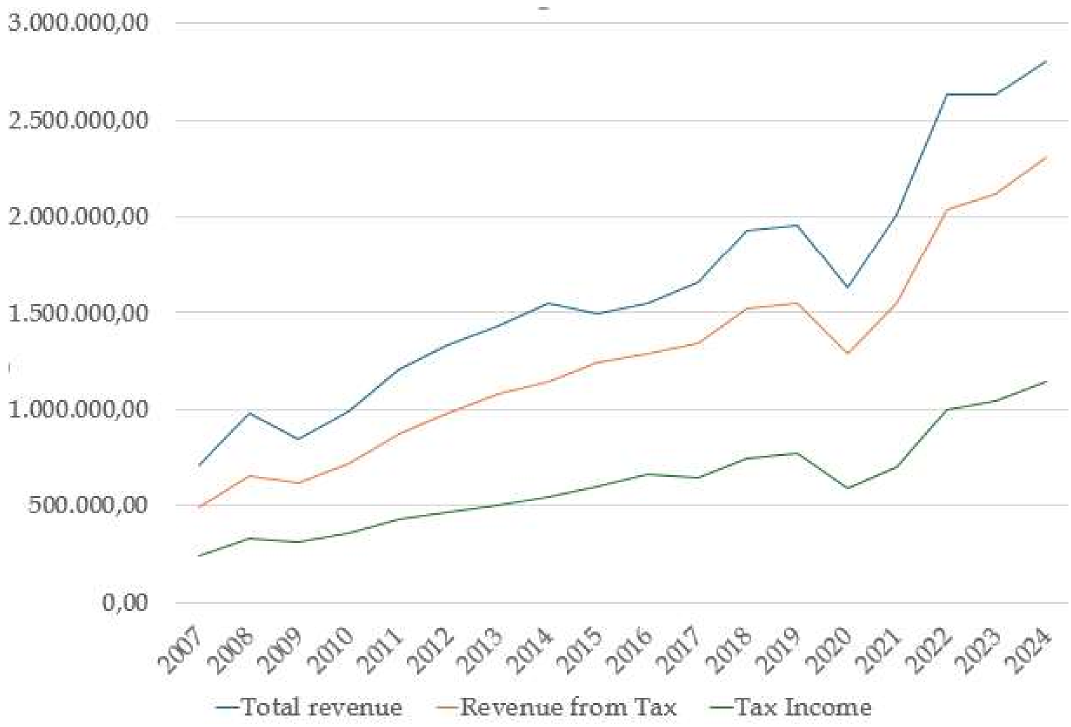

Figure 1
Revenue, Revenue from Tax, and Income Tax

Source: BPS-Statistics Indonesia

one specific characteristic of CEOs, narcissism. Narcissism is defined as a state of excessive self-admiration (Campbell et al., 2011). The presence of narcissistic management indicates alarm for the company (Ham et al., 2018). Narcissistic management tends to make high-risk decisions (corporate risk-taking) (Salehi et al., 2020). Empirically, narcissistic management has been shown to lead to unethical behavior (Blair et al., 2017; Narayan et al., 2000).

For narcissists, becoming a leader is their main goal because it is the highest position or status. Therefore, narcissism is often associated with leadership traits. According to APA (2022a), narcissistic personality is associated with arrogance, a desire for admiration, and a lack of empathy that grows from early development to adulthood. Narcissistic personality tends to lead to unethical behavior. In this study, tax avoidance is used as a proxy for unethical behavior by management. Although not against the law, tax avoidance can be considered unethical behavior. Tax avoidance often occurs in companies, even large companies such as Apple, Microsoft and Hewlett Packard (De Colle & Bennett, 2014). Tax avoidance does open the controversy between ethical and unethical.

According to three ethical theories (utilitarianism, deontology, and virtue ethics), tax avoidance is considered unethical behavior (Preuss, 2012). All companies listed on the Indonesia Stock Exchange (IDX) are required to comply with the rules governing corporate governance. There are several elements of corporate governance, one of which is the board of commissioners (BOC). BOC has the authority to monitor the general course of business within the company (Dodd and Warner 1983). In carrying out its functions, BOC is assisted by the audit committee (AC). AC has the potential to increase the credibility of financial reports by taking part in the process of determining the company's accounting policies (Du Plessis, Hargovan, and Harris 2018). AC is one of the governance mechanisms capable of suppressing management's opportunistic behavior (Rahahleh, Hamzah, and Rashid 2021; Spira 2007; Xie, Davidson III, and DaDalt 2003).

Companies listed on the Indonesia Stock Exchange (IDX) are required to have an audit committee. The audit committee, as part of the BOC, is in charge of monitoring the operation of the company. The audit committee is a committee whose members are appointed and dismissed by BOC. Based on the Financial Services Authority (OJK) Regulation Number 55/PJOK.04/2015, companies are required to have at least three committee members. The structure of the audit committee consists of one chairman who also serves as an Independent Commissioner and two others as members of parties outside the business entity who have an understanding of financial statements and other supporting skills.

Corporate governance is closely related to agency problems that occur between principals and agencies (Shleifer and Vishny 1997). For this reason, setting up governance mechanisms is an effort to align the interests between them (Jensen and Meckling 1976; Naz et al. 2022). Governance mechanisms are designed to narrow the information asymmetry gap between principals and agents. According to Adam Smith, in The Wealth of Nations, when a company employs non-owners to manage a business, there is an expense to be paid. There is a possibility that they are not working for the benefit of the owner (Smith 1937). Conflicts of interest are actually common in an organization, because cooperative relations between individuals have the potential to trigger conflicts. The phenomenon of such conflicts in the hierarchy of commands is analogous to the principal-agent relationship (Jensen and Smith 2000).

However the theory will not apply in all circumstances. As stated by Eisenhardt (1989a), Agency theory only applies to the assumption that stakeholders have three characteristics: self-interest, bounded rationality, risk aversion. The agent's self-interest may differ from what has been agreed in the agency contract with the principal, thus giving rise to agency problems. In agency theory, agents have bounded rationality (Pepper and Gore 2015). Therefore, the agent will do something according to the limitations of his rationality which are based on the cognitive limitations of his mind, so that there is a possibility that he cannot evaluate the consequences of various potential decision alternatives thoroughly (Bahli and Rivard 2003).

This study seeks to observe how audit committees, as one of governance mechanisms) can influence the opportunistic behavior of management, because various previous studies still reveal inconsistencies in the results. Therefore, this study tries to explain how the role of the audit committee in suppressing the negative side of management. This study aims to explain how effective the audit committee's oversight function is from a power perspective (Kalbers and Fogarty 1993).

2. THEORETICAL FRAMEWORK AND HYPOTHESES

Agency Theory

Agency theory (AT) was initiated by Jensen & Meckling (1976). This theory attempts to reveal the phenomenon of information asymmetry between agents and principals. Information asymmetry arises because of the existence of a contract containing an agency relationship between the two parties and in the contract allows the agent to make various strategic decisions on behalf of the principal (Jensen & Smith, 2000). The problem is that decisions made by agents are sometimes not in line with the principal's interests (Eisenhardt, 1989b) due to the presence of self-interest and opportunistic behavior (Shapiro, 2005). In agency theory, what is meant by self-interest is limited self-interest (Bosse & Phillips, 2016). An agent tends to have bounded self-interest in conditions that deviate from common norms in a community, especially regarding just and unjust behavior (Christine et al., 1998). The behavior of agents is said to be close to the bounded self-interest when it is associated with the norms of reciprocity and equality, under the condition that all stakeholders uphold both norms (Hayibor, 2017). Agency theory assumes that all humans are rational beings who have prejudice against agents in a firm. Rationally, agents have the opportunity to maximize utility (Bjurstrøm, 2020) by making various decisions for their own interests (Thiel et al., 2020) and ignoring short-term and long-term managerial interests (Park & Lee, 2021) that may be more important for the company.

Agents have complete information regarding the company (Davis et al., 2021). Meanwhile, to obtain information related to the company, the principal only relies on reports presented by the agent. The principal does not have much time and energy to monitor the agent's activities thoroughly (Spremann, 1987). The imbalance of information between the agent and the principal is called information asymmetry (Jensen & Meckling, 1976). Principals make various efforts to narrow the information asymmetry, one of which is by implementing good governance in the company. The governance structure implemented is expected to be able to act as a joint monitoring system to monitor the performance of management decisions (Fama & Jensen, 1983). Several previous research results show that good governance can narrow information asymmetry (Elbadry et al., 2015; Poursoleyman et al., 2021) due to its ability to limit the selfishness of the agent (Eisenhardt, 1989b). Therefore, agency theory is often used to explain the phenomenon of governance in companies (Clarke, 2014).

Institutional Theory

Governance structure is inseparable from institutional theory (Greenwood et al., 2002; Krenn, 2016). In addition to using agency theory, this study also uses institutional theory by Powell & DiMaggio (2012). Institutional theory is an organizational concept about how the process of forming an institution is closely related to various isomorphic pressures. As a social approach, institutional theory seeks to provide direction on how to understand the technical rationality underlying the implementation of corporate governance (Kalbers & Fogarty, 1998).

Governance practices in the world often take the form of isomorphism (Aluchna & Kuszewski, 2022; Mees & Smith, 2019; Perkins & Shortland, 2022). Isomorphism is the process of embracing various practices from routines, structures and various practices that are considered best practices (Díez-Martín et al., 2018), or in other words the process to become homogeneous (DiMaggio & Powell, 1983). According to DiMaggio & Powell (1983), there are three types of institutional isomorphism: coercive isomorphism, mimetic isomorphism, and normative isomorphism. Coercive isomorphism arises from formal and informal pressures on organizations due to political power that is closely related to legitimacy. Mimetic isomorphism occurs when there is great uncertainty (in the environment) or high ambiguity of a goal, forcing institutions to imitate other successful strategies. Normative isomorphism usually originates from professional circles who are given special privileges by the government according to their professional powers.

Institutional theory (IT) is often associated with corporate governance, because it provides a technical rationality point of view in an effort to understand the phenomenon of corporate governance (Kalbers & Fogarty, 1998). Institutional theory views the adoption of governance mechanisms as involving a prolonged process of change that takes into account various national external forces (Krenn, 2016). The governance mechanisms that must be implemented by every company listed on Indonesia Stock Exchange (IDX) are automatically manifested in the formal organizational structure. The formalization of the structure is a reflection of various rational institutional rules (Meyer & Rowan, 1977).

Governance and Audit Committee

The issue of governance was first proposed by Sir Adrian Cadbury as stated in the Cadbury Committee report (Code, 1992). The emergence of the Cadbury committee report has prompted many countries to rely on governance codification as a benchmark (Nordberg, 2020). In fact, the codification is also not free from weaknesses. (Stiles & Taylor, 1993) pointed out some weaknesses of codification. 1) There is no guarantee that imitating it will lead to good results. 2) The codification does not improve the bottom line. 3) The codification does not provide new enthusiasm for the company.

Governance is often referred to as a tool to narrow information asymmetry between management and company owners. Several studies show that strong governance will reduce information asymmetry (de Barros et al., 2021; Elbadry et al., 2015; Kanagaretnam et al., 2007). The issue of governance has actually been raised by Fama & Jensen (1983) related to infrastructure that allows for a separation between decision management and control. The manifestation of management monitoring and controlling mechanisms on behalf of the shareholders is the establishment of a board of commissioners (Healy & Palepu, 2001). In carrying out the control function, the board of commissioners is assisted by an audit committee (Nguyen, 2022). The existence of commissioners and audit committees is very strategic in the company because of their ability to exercise control over various important management actions, especially those related to opportunistic actions (Hsu et al., 2019; Klein, 2002) or aggressive actions taken by management (Nguyen, 2022).

3. RESEARCH METHOD

The population of this study is manufacturing companies listed on the Indonesia Stock Exchange (IDX). This quantitative research uses secondary data obtained from the websites of manufacturing companies listed on the Indonesia Stock Exchange (IDX) for the period 2017 - 2020. Sampling is conducted using purposive sampling method with the following criteria: 1) publishing annual reports in Rupiah currency; 2) not experiencing losses; 3) not receiving tax benefits, and 4) having a fiscal year ending on December 31 during the observation period. Table 1 shows the sample selection based on predetermined criteria.

Chatterjee & Hambrick (2011) develop four proxies to measure CEO narcissism. CEO narcissism is measured by (1) the CEO's photo in the annual report; (2) how often the CEO's name is mentioned divided by the frequency of other top executives' names being mentioned; (3) the CEO's cash compensation divided by the compensation of the second-highest executive in a company; (4) the CEO's non-cash compensation divided by the compensation of the second-highest executive in a company. These indicators have been validated and used in various research literature related to CEO narcissism, so this measurement is certainly appropriate to use (Al-Shammari et al., 2019; Buyl et al., 2019; She et al., 2020).

The independent variable used in this study is CEO narcissism (CEO_NARC). CEO narcissism is measured through the size of the CEO's photo in the annual report released. This measurement refers to research conducted by Arijit & Hambrick (2007), where a score of 1 is when there is no photo of the CEO; a score of 2 is when the CEO is photographed with other executives; a score of 3 is when the CEO's photo alone is less than half a page; a score of 4 is when the CEO's photo is more than half a full page. The higher the score, the higher the level of narcissism of a CEO is. This is based on the personality of a CEO who wants to stand out and is hungry for public recognition and attention, considering that the annual report is information that can be accessed publicly through the company's website and the IDX. This study uses the effective tax rate (ETR) as a proxy for negative behavior carried out by management. ETR is obtained from the tax burden divided by profit before tax (Dyreng et al., 2017). ETR reflects how much tax is paid by a business entity. Therefore, ETR has the opposite relationship with tax avoidance. This study uses the number of audit committees as a measure of the effectiveness of their roles (Ragab & Saleh, 2021). Based on the perspective of the agency theory, the effectiveness of the monitoring role is obtained when the audit committee is small in size (Xie et al., 2003).

Table 1
Samples Selected

Notes	Totals
Business entities listed on the IDX during the period 2017-2020	701
Business entities that do not issue annual reports or delist or are suspended during 2017-2020	-36
Business entities that use currencies other than Rupiah in their reporting	-127
Business entities that suffer losses and/or receive tax benefits in the 2017-2020 period	-141
Outlier	-131
Total	266

Source: IDX

Some other variables used in this study are leverage (LEV), return on assets (ROA), firm size (FSIZE), and auditor size (AUD). ROA measures a company's ability to generate profits. Profit is a strong indicator that shows a company's ability to pay taxes (Basu, 2016; Saka et al., 2019; Smith, 1937). Leverage is used as a control variable. Leverage has the potential to reduce the effective tax rate (ETR), because the interest on the loan is tax deductible (García-Meca et al., 2021). Firm size (the logarithm of firm's total assets) also has the potential to affect ETR. Several studies show inconsistent results. Alkurdi & Mardini (2020) find that large companies tend to be inactive in tax avoidance due to fears of losing their reputation which can potentially reduce their market value. Meanwhile, Brown et al. (2016) and Deslandes et al. (2020) prove that large companies have greater resources for tax planning which have the potential to reduce tax payments. Auditor size is a proxy for audit quality. A quality audit lowers the likelihood of tax evasion (Riguen et al., 2020). In this study, the size of the public accounting firm is used as a reference for measuring audit quality (Kristabel & Wijaya, 2021). The size of the public accounting firm is determined based on the following scores: a score of 0 is for a local public accounting firm with no foreign affiliation; a score of 1 is for a local public accounting firm affiliated with a non-Big 4; and a score of 2 is for a local public accounting firm affiliated with a Big 4.

The first equation is used to test whether CEO narcissism has a negative side. The second equation shows how strongly the audit committee suppresses the negative impact of CEO narcissism.

$$ETR = \alpha + \beta 1CEO\_NARC + \beta 2ROA + \beta 3LEV + \beta 4\,FSIZE + \beta 7\,AUD + \varepsilon$$

$$ETR = \alpha + \beta 1CEO\_NARC + \beta 2AC + \beta 3CEO\_NARC{*}\,AC + \beta 4ROA + \beta 5LEV + \beta 6FSIZE + \beta 7AUD + \varepsilon$$

4. DATA ANALYSIS AND DISCUSSION

Table 2 shows the results of descriptive statistics after the removal of the outlier. The mean value of CEO_NARC is 3.07, indicating that the average CEO working in manufacturing companies is narcissistic. The mean value of audit committee (AC) is 3, indicating that the average number of audit committee members in manufacturing companies is 3 people. The mean value of effective tax rate (ETR) is 0.2494 or 24.94%, indicating that the average manufacturing company listed on the IDX for the period 2017-2020 has a tax rate of 24.94% of the profits earned. Judging from the standard deviation, ETR has the smallest value, indicating that the ETR data is the least diverse compared to other variables.

This study also ensures whether the processed data can use ordinary least squares. There are four tests conducted in this study, including the data normality test. The data normality test is conducted using the Kolmogorov-Smirnov test as shown in Table 3. After removing outlier data, the significance value increases to 0.073. A significance value above 0.05 indicates that the data has been normally distributed.

Basically, moderated regression analysis is the application of multiple linear regression. From the processed data, the value of adjusted R2 is 0.104, indicating that the research model is only able to explain 10.4%, while the rest is explained by other variables. The F test shows a significance value of 0.000 (< 0.05), indicating that all operational variables are simultaneously able to affect ETR (dependent variable).

Table 2
Descriptive Statistics

Construct	N	Min.	Max.	M	SD
CEO_NARC	266	1	4	3,07	0,67
AC	266	3	5	3,03	0,22
CEO_NARC*AC	266	3	16	9,21	2,17
ETR	266	0,15	0,39	0,25	0,04
ROA	266	0	0,23	0,07	0,04
LEV	266	0,07	0,95	0,38	0,18
FSIZE	266	25,08	32,2	28,37	1,4
AUD	266	0	2	1,25	0,58
Valid N (listwise)	266				

Note. M = Mean, *SD* = Standard Deviation
Source: Data Processed

Table 3
Kolmogorov-Smirnov Test

	Unstandardized Residual
N	266
Test Statistic	.052
Asymp. Sig. (2-tailed)	.073

Source: Data Processed

Table 4 shows the t-test values and the decision to accept or reject the research hypothesis. CEO_NARC has a significance value of 0.013 (<0.05), with a negative direction, indicating that CEO_NARC variable tends to have a negative effect on ETR. ETR and tax avoidance have an inverse relationship. Thus, it can be said that CEO_NARC increases the tendency to tax avoidance, so the first hypothesis is accepted. Model 2 illustrates how effective AC is on management leadership. The significance value of CEO_NARC*AC is 0.193 (>0.05), indicating that the audit committee failed in carrying out its role as an element of monitoring system of management behavior [measured by ETR].

Does CEO Narcissism Create a Negative Side?
According to Campbell et al. (2011), narcissism is a personality trait in which a person views himself as a person of high value. Narcissistic people tend to be exploitative, lack empathy, like to seek recognition and praise, and feel superior (Wallace & Baumeister, 2002). Based on the psychological literature, people with narcissistic personality tend to have a strong motivation to pursue a desired outcome while having a weak motivation to escape from negative outcomes (Campbell et al., 2011; Foster & Trimm IV, 2008; Kontesa et al., 2021). Even in times of failure, they remain optimistic and hopeful that they will succeed in the future. A typical tendency of narcissism is the courage to take higher risks than others (Chatterjee & Hambrick, 2011). They show little fear of failure but also hope of continuing to excel in order to get the recognition and praise they seek (Arijit & Hambrick, 2007). A narcissistic CEO will be more courageous to take risky long-term opportunities, such as the acquisition of several companies of varying sizes, because this will be the attention-grabbing action that the narcissistic CEO wants (Lyle et al., 2013).

The term narcissism is associated with a negative impression, because it creates an arrogant character, unwilling to listen to criticism, and tends to violate integrity standards (O'Reilly III et al., 2021; Resick et al., 2009). However, narcissism also has a positive side. Narcissism creates a strong commitment to bringing business entities to achieve more success (Galvin et al., 2015). Several studies have shown that narcissistic CEOs have a strong desire to achieve success. They are charismatic and enthusiastic leaders. They are always optimistic that the company they lead will be successful (Brown, 2016; Wales et al., 2013). A narcissistic CEO loves to see himself as the center of attention. Therefore, he tends to be bold in taking risks because the higher the risk faced, the more attention will be drawn to him (Braun, 2017; Ham et al., 2017).

CEO narcissism has a significant negative effect on ETR. ETR and tax avoidance have an inverse relationship. Low ETR tends to be considered as tax avoidance behavior. Therefore, this study proves that CEO narcissism has a negative effect and is detrimental to the country as a recipient of corporate taxes. In this context, this study tries to observe whether narcissism is related to ethical decision making. Most decisions made by humans contain bias (Cabitza, 2019; Featherston et al., 2020), including ethical decision-making (Jones, 1991). Humans are free to choose. Actually, human decisions are in the range between the limited cognitive rationality and the limits of morality (Hindman et al., 2021). These two conditions will determine which decision will be taken by the human being.

Narcissism is closely related to self-interest. Narcissists tend to have feelings of superiority and are exploitative. A narcissist is motivated by rewards and praise and shows no fear of failure. He is very aggressive in pursuing what he believes in and feels that the law is under his control. Furthermore, these narcissists tend to be more daring in taking risky actions than others, such as those related to tax evasion practices (Araújo et al., 2020). This empirical research is supported by Brown et al. (2016) who consider narcissism as one of the CEO personality traits that influences tax avoidance activities. Compared to other CEOs, narcissistic CEOs tend to pursue lower tax payments through aggressive tax avoidance, even though it has the potential to give a negative value to the company because it violates government regulations. Narcissistic CEOs tend to have higher courage in taking risks. They feel superior and have short-term desires in the form of recognition for what they have achieved without considering the consequences that will be faced.

Table 4
Regression Results CEO_NARC, CEO_NARC*AC and ETR

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	0,331	0,053		6,221	0,000
	CEO_NARC	-0,007	0,003	-0,149	-2,51	0,013
	LEV	0,029	0,015	0,129	1,964	0,051
	FSIZE	-0,003	0,002	-0,102	-1,458	0,146
	AUD	0,019	0,005	0,27	3,716	0,000
	ROA	-0,170	0,061	-0,191	-2,773	0,006
2	(Constant)	0,313	0,072		4,318	0,000
	CEO_NARC	-0,024	0,013	-0,515	-1,805	0,072
	LEV	0,026	0,015	0,118	1,799	0,073
	FSIZE	-0,003	0,002	-0,112	-1,620	0,107
	AUD	0,018	0,005	0,253	3,494	0,001
	ROA	-0,159	0,061	-0,178	-2,600	0,010
	CEO_NARC*AC	0,007	0,006	0,394	1,306	0,193
	AC	0,005	0,020	0,026	0,238	0,812

Note:
a. Dependent Variable: ETR
b. Adjusted R2 (model 1) = 0.085;
Adjusted R2 (model 2) = 0.104
Source: Data Processed

According to Araújo et al. (2020), narcissistic CEOs are more likely to adopt tax avoidance strategies by reducing or delaying tax payments and making financial results look more attractive for their prestige. Brown (2016) argues that narcissistic CEOs have less empathy and moral sensitivity, so they are more likely to reduce costs by engaging in aggressive tax avoidance. Narcissistic CEOs tend to show off and be ambitious (Arijit & Hambrick, (2007). Thus it can be said that narcissistic CEOs tend to choose to avoid taxes to lower their expenses. Previous research conducted by Chatterjee & Hambrick (2011) and Bachrach et al. (2022) show that narcissistic CEOs prefer to show off and choose aggressive strategic actions rather than pursuing gradual improvements.

This empirical research strengthens two assumptions in agency theory: self-interest and bounded rationality. Economically, humans will always use rationality in their decision making. However, have we ever thought about the negative side of humans who always prioritize rationality? Humans who uphold rationality in every decision they make will tend to ignore the existence of emotions, feelings, ethics, and so on (Zhong, 2007). If a decision is taken without considering feelings, morality and ethics, it can turn into an inhumane decision.

How Strong is the Audit Committee in Reducing the Negative Impact of CEO Narcissism??

The term governance is different from government. Governance talks about how the agent's performance can meet the expectations of the principal (Fukuyama, 2013). According to Graham et al. (2003), governance is a continuous process in which an organization is obliged to determine various decisions that are considered important, determine the parties involved, and determine how the parties involved are accountable for their performance. So it can be said that governance is related to how stakeholders in the company are accountable for their performance. Empirical studies in Indonesia show that several components of governance attract potential stakeholders by increasing the value of the company (Nugroho & Budiman, 2022).

World donor agencies also pay great attention to governance issues. In fact, the UN also encourages companies to comply with global governance standards that are more inclined to the Anglo-Saxon concept than the continental (G. H. Roberts, 2004). How about Indonesia? According to Tariq et al. (2022), companies in Indonesia, India, China and Malaysia are more compliant with UN governance code than their own countries' governance code. Regardless of the involvement of Anglo-Saxons or Continental, all public companies in Indonesia are required to comply with the national governance code.

Audit committee (AC) has the potential to improve governance within the company. Strong governance will reduce corporate financial misconduct (Velte, 2021), because the role of the audit committee includes supporting the whistleblowing mechanism in the company (Lee & Fargher, 2018). Basically, the audit committee's main task is to monitor financial reporting (Khoo et al., 2020). They should also ensure that management has selected appropriate accounting policies for the company according to generally accepted accounting standards (Hancock et al., 2020). In relation to improving the quality of financial reporting, an audit committee with an accounting background can reduce the possibility of misstatements in financial reports (Das et al., 2022). An effective audit committee is also able to reduce opportunistic management behavior (Kirchler, 2019). In addition, audit committee also has a great opportunity to improve audit quality (Sailendra et al., 2020). However, strong governance would never be achieved without the key role of top management. A leadership style that is in line with the elements of governance will create a strong corporate governance synergy (Yuliastuti & Tandio, 2020).

The existence of an audit committee (AC) plays an important role in a company to ensure that good governance has been implemented effectively, which will ultimately drive better company performance (Chaudhry et al., 2020; Kallamu & Saat, 2015). Unfortunately, empirical data reveal that the audit committee (AC) has no effect on the relationship between CEO narcissism and tax avoidance. The AC cannot directly influence important management decisions. In this case, the audit committee is apparently unable to ensure that the company has adopted morally appropriate accounting policies. Based on these findings, the AC is not an effective monitoring system, especially for financial reporting.

Empirical experience in Korea also shows that AC fails to improve the quality of financial statements (Doo & Yoon, 2020). If the audit committee (AC) is unable to carry out its supervisory role, how can it provide useful information to the Board of Commissioners? Other research results also show that the AC fails to carry out its main function as an external monitor (Sumajow et al., 2022). It turns out that governance mechanisms are also unable to increase the value of companies that implement them (Fitriyah et al., 2020). The results of this study also show that agency theory fails to explain the role of the audit committee as part of the monitoring system in an institution. This finding tends to support institutional theory to explain this phenomenon. According to institutional theory, companies that adopt an audit committee (AC) structure are only symbolic in order to obtain recognition of compliance with rules or regulations, so as not to arouse suspicion from outside parties regarding the company's operational activities (Kalbers & Fogarty, 1998).

This study uses the size of the audit committee (AC) as a measure of its work effectiveness. Supported by greater human resources and diverse capabilities, the audit committee is expected to be able to intervene in the important management decision-making process (García-Meca et al., 2021). It turns out that a large audit committee size is not always able to influence management decisions. Chatterjee & Hambrick (2011) argue that even though executives operate under considerable external and internal supervision (such as the audit committee), they still have the freedom to act and make their own choices. This is based on the personality of CEOs who always feel that they are great (above average effect) so that they tend to glorify their ability to make certain decisions, which are actually beyond their capabilities. The results of research conducted by Zengin-Karaibrahimoglu et al. (2021) show that CEO narcissism can undermine the effectiveness of a strong audit committee.

Why are governance models unable to influence agent behavior? What is wrong with governance stereotypes? Are we too insistent on following Western governance codes? According to Western agency theory, the audit committee (AC) is designed as a monitor of management activities. In agency theory, there is a sense of distrust in the relationship between the principal and the agent in an organization. (Besar, 2019; J. Roberts, 2001). These norms or rules are part of Western culture that may not be in accordance with Eastern culture, such as Indonesia. Therefore, not all best practices in a region can be suitable for everyone. Agency theory may be suitable for Western countries, but not for Eastern countries. Further research on the effectiveness of Western governance in Eastern countries is very useful to fill the research gap.

5. CONCLUSION, IMPLICATION, SUGGESTION, AND LIMITATIONS

Most people consider CEO narcissism as a negative thing. This study proves that CEO narcissism has the potential to increase tax avoidance. Although tax avoidance is not always illegal, it is an unethical decision. The concept of ethics views tax avoidance as immoral behavior. This behavior has the potential to reduce the state's ability to provide services to poor people who need help. To prevent this unethical management behavior, the government has encouraged companies to comply with the national governance code. The government has issued regulations regarding the obligation to establish an audit committee (AC) for public companies. AC, as a sub-BOC, is in charge of monitoring the business within the company, especially related to financial reporting. Unfortunately, the audit committee (AC) has failed to carry out its obligations as part of the monitoring system. There are several possibilities that make this governance element ineffective. Therefore, further research is suggested to add several variables related to the audit committee, such as accounting and financial expertise, meeting frequency, and experience.

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