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Corporate Social Responsibility (CSR) Disclosure and Tax Planning: A Study on Malaysian Listed Companies

Mohd Waliuddin Mohd Razali[1&2], Shantny Sandimalai[1], Damien Iung Yau Lee[1] & Janifer Lunyai[1]

[1] Faculty Economics & Business, Universiti Malaysia Sarawak (UNIMAS), Malaysia

[2] Faculty of Economics & Management, Universiti Kebangsaan Malaysia (UKM), Malaysia

Correspondence: Mohd Waliuddin Mohd Razali, Faculty Economics & Business, Universiti Malaysia Sarawak (UNIMAS), Malaysia.

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Abstract

CSR Disclosure is widely practiced for effective decision making and top management of tax planning in a business. The main objective of this research is to determine the CSR disclosure influence on tax planning in Malaysia listed companies as well as examine the relationship between tax planning and other factors influencing such as profitability, company size, leverage, effective tax rate (ETR) and book tax differences (BTDs). A sample of 557 companies from Malaysia's listed companies for the period of 2014 to 2016 was collected and analysed. After controlling such as profitability, company size and leverage the regression results display tax planning has positive relationship respectively in BTDs. The first impact of polices makers is companies may use CSR activities to avoid negative impact irresponsibility engaging tax planning. Second, tax incentives given to public companies reduce Malaysia's government burden to support the public and promote companies' growth.

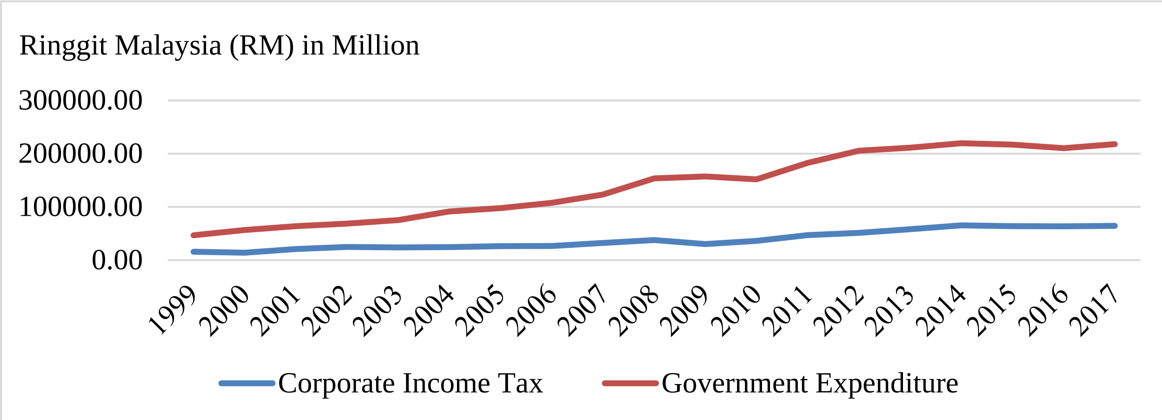
Keywords: society, tax incentive and disclosure

1. Introduction

Companies' efforts to boost societies welfare are described by Corporate Social Responsibility (CSR). CSR has become one of the focus in this economic era, which forces companies to develop and apply CSR for community duty and activities to stay in the market. This is due to CSR stress by consumers, governments, non-government organizations, and other shareholders. At the same time, it also positively improves companies' image and relationship with customers, shareholders and other stakeholders. Malaysia's government intends to encourage CSR activities by providing tax incentives not only to publicly traded companies but also to non-profit organisations that participate in CSR activities.

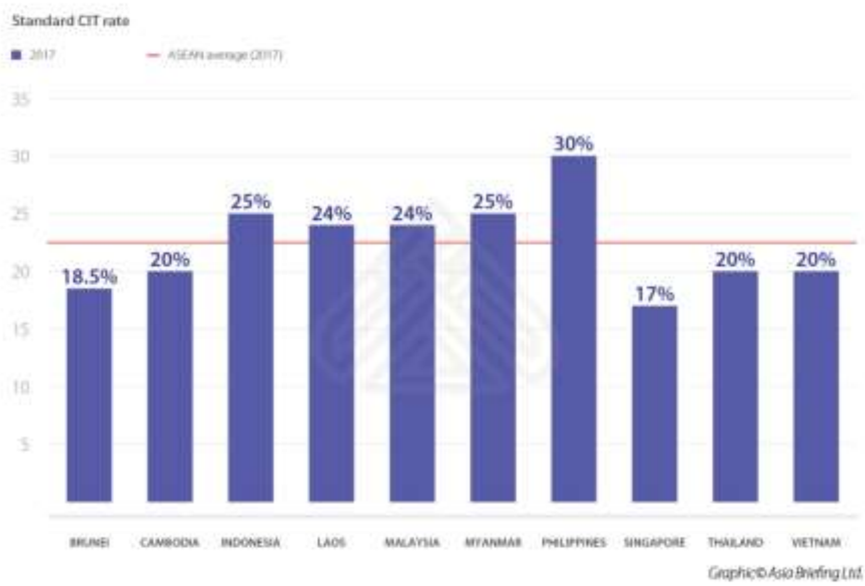
If a company does not incorporate CSR into its business, it will be rejected in this society. In addition, tax planning has become necessary for companies and their stakeholders, government and customers. Reductions in tax are favourable to shareholders because they will increase their wealth in companies. However, government are worried that tax planning by companies will reduce government's earnings are needed for other social reasons like training programmes for workers, programmes for the disabled and social assistance, and so on. Moreover, the customers stress the tax payments to know whether the company is responsible and pays its fair shares to society. Therefore, CSR and tax planning should have a significant impact on society's wellbeing and economic growth.

Graph 1 shows the government expenditures and direct corporate taxes in Malaysia from 1999 to 2017. This graph shows that the government is less dependent on the corporate income tax (CIT) starting in 2014 and it gradually decreases until 2017. This is due to the fall in income tax collected while government expenditures rose by years. The introduction of goods and services (GST) could be one of the reasons why the government is less reliant on corporate income tax. Graph 2 shows Malaysia among countries that levy a high CIT above the average across ASEAN countries in 2017. This led to tax competition among the regions, which made the government under pressure to reduce CIT by non-government organizations (NGOs)~~,~~ to encourage more outside investors to invest in Malaysia.



Graph 1. Malaysia's Corporate Income Tax (CIT) and Government Expenditure

(Source retrieved from CEIC database)



Graph 2. CIT across ASEAN Countries

(Source: https://www.aseanbriefing.com/news/2018/07/26/comparing-tax-rates-across-asean.html)

The self-assessment tax system is one of the instruments within tax law implemented by the government of Malaysia which requires any company to file a tax computation to the Inland Revenue Board Malaysia (IRBM), which enables Malaysian companies to perform tax planning within tax law (Dave, 2013).

The income tax law 1967 within Malaysia does not penalise companies for doing tax planning in the eyes of CSR. Social donation made by companies will be given a deduction subject to 10% of aggregate income in term of cash to approve organisation (under Section 44(6)), and cash or in kind for project of national interest approve by minister (under Section 44(11C)). For religious contribution in terms of "*zakat perniagaan*" (business zakat) is restricted to 2.5%. Other than that, cash donations to public, school libraries~~,~~ and higher education institutions are restricted to RM20,000 (under Section 44(8)). There are no deduction restrictions for social donations to the government of artefacts, manuscripts or paintings (under section 44(6A).

The tax payer (company) will receive a full revenue deduction for social responsibility payments if they incurred expenditure on the provision of services, public amenities, or contributed to a charity or community project pertaining to education, health, housing, conservation or preservation of the environment, enhancement of poor infrastructure's income and communication technology's income (under Section 34(6)(h) (ha)). Further deduction, another term is referred to as "double deduction", will be given to companies on salaries paid to disabled employees (under Income Tax Act 1982).

Furthermore, companies that engage in conserving the natural environment for the benefit of society such as utilisation of biomass to produce value-added products and generation of renewable energy, can apply for pioneer status or an investment tax allowance (under Promotional of Investment (Amendment) Act 2007). This will make the company eligible to get up to a 100% exemption of statutory income. In response to the alarming effect of global warming, the Malaysian government will give an industrial building allowance to any company that obtains a green building certificate (under Income Tax Act 1967, Section 3). The allowance will be set off against the company’s adjusted income.

Companies that are ethically and socially responsible will pay more taxes or engage in less tax planning, allowing the government to increase expenditure in support of public activities for society's benefit. This will help their business sustain in the market by getting support from various stakeholders such as (non-governmental organizations) NGOs, societies, customers, etc. Most prior studies use the effective tax rate (ETR) to measure tax planning. Studies suggest book tax differences (BTDs) is a suitable proxy for tax planning (e.g., Hoi, Qiang & Chun, 2013; and Razali et al., 2018a). Therefore, our main objective is to examine the relationship between CSR disclosure and tax planning of Malaysian listed companies.

2. Literature Review

2.1 CSR Disclosure and Tax Planning

According to stakeholder theory, CSR is an important element~~,~~ where the concept acknowledges the responsibilities of companies in the world today, even if the company is economic, legal, ethical, or liberal (Freeman, 2010). The future of a company is secured by good public relations, which is the main reason larger companies focus on CSR in their management. Tax affairs arguments are mainly highlighted in stakeholder theory by recently recognised companies such as Google and Starbucks in the United Kingdom. Companies consider it unethical to use the weakness of the British tax system by reducing their company tax payments even though the CSR system that companies follow is legal. According to Hawkins (2006), the external values of the company have been boosted and maximised the shareholders’ value by practising this approach. The aim of this theory is to help the company integrate community contracting with the internal workings and external activities. Even though, the company is involved in tax planning, the company still pays tax charges on their operational income without excluding their responsibility towards society. Therefore, a company which is involved under this theory is not seen as harmful to society, even if they are also involved in tax planning.

According to the legitimacy theory, researchers say company CSR information can be used as a part of communicating with the community. CSR disclosure will be legitimised in some companies by managing their shareholders' perception. However, the companies that give focus on tax planning would not consider the legitimacy theory that gives focus on community responsibilities. This highlights the concept of community relations between the company and the community. Therefore, the CSR method exercised in a company will motivate a corporation with analysis through the stakeholder theory to offer greater reputation or legitimacy (Lanis & Richardson, 2012). The development in prestige of a company will support the long existence of a company and lower the risk if the company is operated by a person whom society trusts. This will increase the company’s costs and, at the same time, increase the reputation of the company, which may help the company’s growth.

Corporate tax payments play a main role in the economic income of a country, which develops the living standards of the people of that country. These taxes are recognised as a company’s expenses, and therefore, the company’s managers try to reduce this expense by practising several strategies that help them improve the image of the company while at the same time helping the community of a country. The main strategy that is used by the managers is CSR, which can be defined as additional commitments that apply to external social welfare in the concern of the company where it is compulsory according to law (Lanis & Richardson, 2013). Even though there are companies that do not focus on tax planning and CSR disclosure. The higher tax planning, in the long term, will have a negative effect on the communities as it will critically influence the capacity of the government to support the development of the country. It can also cause a company’s market value to drop due to a loss of reputation in public perception.

In Australia, plans or arrangements made by companies mainly for the purpose of tax planning are not treated with the spirit of the law. Thus, under Australian tax legislation, the Australian Taxation Office (ATO) has the right to remove any tax advantages received from such plans and arrangements, to charge further tax and to levy significant tax penalties on the corporation (Gilders et al., 2004). However, companies that engage in CSR for the purpose of tax planning are not illegal in developing countries and reduce the burden on the government to support the public. For example, in China, tax environmental planning does not just promote more inflow of foreign direct investment (FDI) and companies' growth but also benefits society in the reduction of pollution in the country (Tung and Cho, 2001).

Lanis and Richardson (2012) studied the relationship between CSR and tax planning using a sample of 408 publicly listed Australian corporations for the periods of 2008 and 2009. The empirical result showed that socially responsible companies have a higher level of CSR disclosure and lower tax planning. They concluded that social investment commitment and corporate and CSR strategy (including the ethics and business conduct) of a corporation are essential aspects of CSR activities that have a negative impact on tax planning. Their study is consistent with other researchers (e.g. Laudry et al., 2013, Garcia et al., 2014, and Reselaar, 2016, Inger & Vansant, 2019, Aronmwan, & Igbinoba, 2021,).

Family companies have different long-term objectives than non-family companies. It being argued that family companies may not always follow an economic rationale, and they may act in another way toward risk if needed to secure the family benefits (eg Zellweger, Kellermanns, Chrisman, and Chua, 2012). The owners of the family companies have enough incentive and power to monitor management, which can mitigate the agency problem. Laudry et al. (2013) found that family firms are less tax planning than non-family firms. For family companies, the financial incentives for tax planning are much lower in the face of risky tax positions, which may yield negative outcomes that can significantly impact socio-emotional wealth (SEW), especially the family's name and reputation, which have been continued for a few generations, even though there are few family companies that focus on reducing costs and maximising profit. This leads to the family companies paying low tax payments where their CSR commitments are higher.

Lanis and Richardson (2013) studied a relationship between CSR and tax planning to test for legitimate purposes. They compared 20 Australian corporations accused by the ATO of engaging in tax-aggressive activities with 20 non-tax aggressive corporations during the 2001–2006 period. Their empirical results showed a positive and significant relationship between tax planning and CSR disclosure, which confirmed the legitimacy theory in the context of tax planning. CSR disclosure in the annual report is being used to mitigate public awareness of the negative community impact tax planning and to indicate they are meeting community expectations. Similarly, Hoi, Qiang and Chun (2013) also found a positive relationship between CSR and tax planning. They point out that companies may use CSR activities as a risk management strategy to mitigate the risk associated with negative corporate events. The higher CSR reputation will reduce the severity of potential negative sanctions consequences from performing tax planning activities. CSR reputation provides some degree of insurance protection against the risk of market, political, regulatory, and social sanctions when negative events occur. Even though it helps the company to reduce tax, the company will still pay tax according to the revenue percentage. The empirical evidence of this study suggests that high-CSR companies tend to disclose more information in order to reduce tax while projecting a positive image towards investors and stakeholders. The results are consistent with Gulzar, Cherian, Sial, Badulescu, Thu, Badulescu and Khuong (2018) and Sari and Prihandini (2019).

2.2 Tax Planning

According to Dias and Reis (2018), tax planning is the result of a number of activities and legal procedures which aim to minimise expenses with taxes, such as investments in tax free assets or maximising tax benefits. Purpose of tax planning is to induce or facilitate certain activities or business behaviour deemed desirable for the society and economy. Tax planning also purposely to increased employment, higher number of capital transfers, research and technology development, and also improvement to less developed areas in a country.

Two proxies use by past researchers to measure tax planning are book tax differences (BTDs) and effective tax rate (ETR). BTDs can be measure the differences pre-tax or accounting book income minus the taxable income divided by total assets (Koubaa & Anis 2015). The higher BTDs indicate higher tax planning. This is because company is charged tax expenditure lower when the taxable income is lower than accounting book income. ETR can be measure by dividing tax expenses to taxable income (Dias & Reis, 2018). The higher of the ETR will indicate the lower is tax planning. This is because high tax expenditure burden charge to company.

Company characteristics influence tax planning activities. First, larger companies have higher income and greater government control compared to the smaller companies. They have greater possibility of carrying out of policies of fiscal planning and/or engaging accounting policies to reduce tax expenditure (Delgado, Fernandez-Rodriguez, & Martinez-Arias, 2014). Second, the profitability of company tends to have positive relation with tax planning because of the higher the revenue the company earned the higher the tax rate will be charge to company (Garcia & Cloyd, 2014). Third, company that has higher debt financing may apply tax deduction of interest payments to help company in tax planning (Lanis and Richardson, 2014)

3. Methodology

3.1 Sample Data

The sample collection in this study is based on the secondary data that was collected from DataStream and the annual report. The data of this research consists of 557 companies from listed companies on Bursa Malaysia under various industrial products over a 3-year time period from 2014 until 2016. The sample is considered to be representing the population if it contains observations of at least 30 companies from the population (Keller and Warrack, 2005). Although the GST implementation on April 2015 in Malaysia, there is no much impact of the GST on the corporate income tax. The data on CSR was gathered manually from companies' annual reports, whereas the financial data to calculate effective tax rate (ETR), book tax differences (BTDs), return on assets (ROA), company size, and leverage were collected from DataStream.

3.1 Regression Model

Multiple regression analysis was used to analyse the relationship between CSR disclosure and tax planning in Malaysia. The estimation model used in this research is as follows:

$$TAX\_PLANNING_{it} = \alpha + \beta_1 CSR_{it} + \beta_2 CSIZE_{it} + \beta_3 LEV_{it} + \beta_4 ROA_{it} + \epsilon_{it} \text{ (equation 1)}$$

Where:

Dependent Variable

TAX_PLANNING = (i) book tax differences (BTDs); (ii) effective tax rate (ETR)

Independent Variable

CSR = corporate social responsibility (CSR) activities disclosure

Control Variable

CSIZE = company size

LEV = leverage

ROA = return on assets

Others

α = constant

ϵ = standard normal, randomly assigned error term

i = companies

t = Time

4. Results and Discussion

4.1 Descriptive Statistics of Variables.

Table 1. Summary of Descriptive Statistics

Variable	N	Minimum	Maximum	Mean	Std. Deviation
BTDs	1671	-0.63	0.88	0.0055	0.0968
ETR	1671	-0.0735	0.0788	0.0020	0.6502
CSR	1671	0.00	300.00	26.1676	27.8759
FV	1671	6.21	11.12	8.6757	0.6689
ROA	1671	-.82	0.98	0.0544	0.1140
LEV	1671	-.01	0.75	0.1242	0.1310

Table 1 provides the descriptive statistics of tax planning, CSR disclosure, and company characteristics of public listed companies in Malaysia. This table covers minimum and maximum values, means, and standard deviation for the variables. In this study, two proxies are used to interpret tax planning: book tax differences (BTDs) and effective tax rate (ETR). BTDs have an average of 0.0055 with a range from a minimum of -0.63 to a maximum of 0.88, which has a standard deviation of 0.0968. The ETR has an average of 0.20% (range from -7.35% to 7.88%). The standard deviation lies at 0.6502. Following Razali et al., (2018), they used the word count method to measure CSR disclosure. Usage of word counts method helped in shielding against irregularities in calculating the quantity of disclosure (Zeghal and Ahmed, 1990). The CSR for this study has an average of 26.1676 words (ranging from 0.00 to 300.00 words). The standard deviation lies at 27.8759. Company size (CSIZE) is a control variable that was used in this study. CSIZE is measured by the natural log of the total assets of the companies. The company size had an average of 8.6757, with the range of the lowest number of 6.21 and the highest number of 11.12. It had a standard deviation of 0.6689. Leverage (LEV) has a mean of 12.42% and is determined by total debt to total assets of the companies. The range of LEV is the minimum percentage of -1% and the maximum number of 75%. Its standard deviation is 13.10%. Lastly, the return on assets (ROA) has an average of 5.44%. The range of ROA lies between minimum percentages with a value of -82% and a maximum percentage of 98%. The standard deviation of ROA is 11.40%.

4.2 Pearson's Correlation Coefficient Test

Table 2. Pearson's correlation

	BTDs	ETR	CSR	CSIZE	LEV	ROA
BTDs	1					
ETR	-0.015 0.533	1				
CSR	-0.057** 0.020	-0.018 0.455	1			
CSIZE	-0.128*** 0.000	0.015 0.538	0.449*** 0.000	1		
LEV	0.020 0.416	0.069*** 0.005	0.196*** 0.000	0.387*** 0.000	1	
ROA	-0.728*** 0.000	0.014 0.563	0.088*** 0.000	0.105*** 0.000	-0.097*** 0.000	1

***. Correlation is significant at the 0.01 level (1-tailed), and **. Correlation is significant at the 0.05 level (1-tailed)

According to Berg (n.d.), the pearson correlation coefficient is a test that estimates the statistical relationship or association between two variables to improve the reliability of the study. The information provided by the test will be the magnitude of the association or correlation and the direction of the relationship. The perfect correlation between two variables will be indicated in a range from -1 to +1, where the negative 1 shows the perfect negative relationship and the positive 1 shows a perfect positive relationship between two variables. The variables' outcomes will differ due to the different data that was used. The strongest relationship between variables will be explained by the higher the correlation figure. Table 2 shows the correlation between the dependent variables, independent variables, and control variables which display CSR disclosure, company size, leverage, and profitability are related to tax planning for the 557 companies in Bursa Malaysia.

As shown in Table 2, BTDs is negatively correlated with CSR disclosure at a 5% level of significance and negatively correlated with CSIZE disclosure at a 1% level of significance. ROA is also negatively correlated with BTDs at a 1% significant level. ETR positively correlated with LEV at a 1% level of significance. Besides that, CSR shows a significant positive relationship with LEV, ROA, and CSIZE at a 1% level. Next, CSIZE shows a positive and significant relationship with LEV and ROA at 1% level of significance. Furthermore, LEV also shows a negative relationship with a 1% level of significance with ROA.

4.3 Multiple Regression Analysis

Table 3. Results of Multiple Regression

	BTDs model	ETR model
Constant	-0.622***	0.185
	-3.257	0.308
CSR	0.001*	-0.048
	1.863	-0.328
CSIZE	0.103***	0.004
	4.494	0.056
LEV	-1.863***	0.571**
	-23.156	2.112
ROA	-0.914***	0.090*
	-65.428	1.920
R2	0.874	0.003
Adjusted R2	0.874	0.001
Anova Statistic p-value	0.000***	0.000***

***. Correlation is significant at the 0.01 level (1-tailed), **. Correlation is significant at the 0.05 level (1-tailed), and *. Correlation is significant at the 0.10 level (1-tailed).

In above table, both models are significant at 1%. However, the adjusted r-square of BTDs model is 87.4 % which higher compares ETR model is 0.1%. The results of independent variable and control variable are discussing in the following sections.

4.3.1 Relationship Between Tax Planning and CSR Disclosure

Table 3 presents panel data results by using two different dependent variables: BTDs (model 1) and ETR (model 2) in estimating equation 1. The results of the study show that BTDs is positively related to CSR at 10% significant level which indicate Malaysian's companies do tax planning related to CSR.

CSR was expected there is negative relationship with effective tax rate (ETR) which has reverse relationship between tax planning. The coefficient for CSR disclosure is -0.048. From table, the CSR disclosure and tax planning is positive relationship but the result not significant. The CSR is expected to has positive relationship with book tax differences (BTDs) which has direct relationship between tax planning. The coefficient for CSR disclosure is 0.001. From table 3, the CSR disclosure and tax planning is positive relationship and significant at 10% level. The result consistent with Lanis and Richardson (2013) and Hoi, Qiang and Chun (2013), Gulzar, Cherian, Sial, Badulescu, Thu, Badulescu and Khuong (2018) and Sari and Prihandini (2019). Companies tend to disclose more information in order to reduce negative sanctions consequences performing tax planning activities while projecting a positive image towards investors and stakeholders. Furthermore, companies will have a lot of CSR disclosure compared to non-tax planning companies which in long term will bring negative effect on the community as it will critically influence the capacity of the government in supporting the development of country however these CSR activities disclose by companies helps the society improvements and the country.

4.3.2 Relationship Between Tax Planning and Company Size

There is negative relationship between company size (CSIZE) and ETR which shows positive relationship between tax planning. The coefficient of company size is 0.004. The result not significant. At the same time BTDs shows positive relationship with company size which positively related with tax planning. The coefficient of company size is 0.103 at 1% significant level. Big companies enjoy greater economic and political power compared with smaller companies. They tend to reduce can reduce their tax burdens (Gracia, 2016; Lanis & Richardson, 2015; Agundu & Siyanbola, 2017).

4.3.3 Relationship Between Tax Planning and Leverage

There is positive relationship between leverage (LEV) and ETR which shows negative relationship between tax planning. The coefficient of leverage is 0.571 at 5% significant level. The result concludes in ETR model similar to BTDs model which is leverage negatively related to tax planning. The coefficient of leverage is -1.863 at 1% significant level. The result is consistent with Hasan et al. (2014). It proves that creditors impose more stringent and costly credit terms on companies engaging in greater tax planning, indicating that creditors favour less aggressive tax planning strategies. However, this is not consistent with many prior studies such as Hoi, Wu & Zhang, 2013; Laudry, Deslandes & Fortin, 2013; Renselaar & Dam, 2016; Agundu & Siyanbola, 2017).

4.3.4 Relationship between Tax Planning and Profitability

There is positive relationship between profitability in term of return on assets (ROA) and ETR which shows negative relationship between tax planning. The coefficient of profitability is 0.090 at 10% significant level. The result concludes in ETR model similar to BTDs model which is ROA negatively related to tax planning. The coefficient of ROA is -0.914 at 1% significant level. The result negative consistent with prior studies found by Huseynov and Klamm (2012), Lanis & Richardson (2012), Renselaar (2016) and Agundu and Siyanbola (2017). Higher the profitability of the company earns will result the higher the tax rate will be charge to company.

5. Conclusion and Implication of the Study

Based on this study, CSR has a significant positive relationship with tax planning, measured by BTDs. The result suggests that one of the motivations companies to implement CSR is to reduce the amount of taxes paid and negative sanctions consequences from performing tax planning activities while projecting a positive image towards investors and stakeholders. Increase tax planning activities (social cost) may give more benefit to societies in term of company organising variety social activities. Social cost in this study refer to the reduction of the government income receives from corporate income tax to support societies. Most of the literature views corporate tax planning as socially irresponsible as it will reduce government income to support the delivery of public goods and services. Nevertheless, the tax planning incentive is very important to developing countries such as Malaysia to attract more foreign direct investment (FDI) and promote economic growth. It also reduces the burden on the government to support public goods and services. For example, in Malaysia, the government needs to spend around RM600 to train an unemployed graduate. If a company trains unemployed graduates, it will get a tax incentive of RM150 for each graduate (assume Malaysia's tax rate is 25%, so corporate tax will be reduced by RM150 = RM600*25%). From another point of view, it may reduce government expenditure on training unemployed graduates by RM450 (75%).

All control variables have a significant relationship when tax planning is measured by BTDs. However, there are two control variables, which are leverage and profitability, which have a significant relationship with tax planning when measured by ETR. Under model 1, company size has a positive relationship with tax planning. Large companies enjoy greater economic and political power compared with smaller companies which motivates them to get involved in tax planning more. Leverage has a negative relationship with tax planning, which indicate creditors impose more stringent and costly credit terms on companies engaging in greater tax planning. Finally, profitability has a positive relationship with tax planning. The higher the profitability of the company earns, the higher the tax rate will be charged to the company.

For future studies, this study suggests that exploring the relationship between CSR and tax planning in developing or underdeveloped countries could yield new findings. Most empirical studies focus on developed countries (e.g., the US, Australia). Developing or underdeveloped countries may have different tax structures and cultures. The tax incentives are very important to attracting more FDI and promoting economic growth. It can also be used as a government strategy to delegate burden support to companies by offering CSR tax incentives. Lower GDP is one of the reasons that the government is not able to support high public expenditure.

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