

The Composition of Top Management with General Counsel and Tax Avoidance*

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10 January 2014

JEL classification: G34; G38; M41

Keywords: General counsel, tax avoidance, equity incentives.

* We thank Brown Bag participants at Singapore Management University for helpful comments. Goh, Lee, and Ng thank the School of Accountancy Research Center (SOAR) at Singapore Management University for financial support.

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Abstract

We examine whether the composition of top management with general counsel is associated with a firm's tax avoidance because it is essential to better understand the role of the general counsel in firms' tax decisions (Hanlon and Heitzman, 2010). We find that firms with a general counsel as part of top management are more aggressive in their tax planning, as evidenced by a larger discretionary permanent book-tax difference, a higher likelihood of engaging in tax shelter activities, and more uncertain tax positions. This result is consistent with the general counsel among top management using her legal expertise to help the firm minimize explicit taxes. In addition, we find that the positive association between general counsel in top management and tax avoidance is attenuated in the post-FIN 48 periods, consistent with FIN 48 constraining the general counsel from facilitating tax avoidance. Finally, we document some evidence that the positive association between general counsel in top management and tax avoidance is stronger when the CEO has a higher degree of influence, and is weaker when the general counsel also sits on the board of directors or has more equity incentives.

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“Positioned as an officer within a corporation, a general counsel who is an influential member of its senior management cohort may help shape the corporation’s activities and policies in directions that are highly desirable, exercising influence that may extend beyond the bare bones of ensuring legal compliance. A general counsel also may be uniquely well positioned to champion a transformation of the organizational culture that shapes how the corporation addresses its relationship with law and regulation” (DeMott, 2005, p. 955-956).

1. Introduction

We examine whether the composition of top management with general counsel is related to corporate tax avoidance. The general counsel, who is the chief attorney for a corporation, has the important role of overseeing and advising on the legal issues within the firm, including tax compliance. According to Hanlon and Heitzman (2010), the theory on corporate tax avoidance indicates that tax compliance is determined by many factors such as tax rates, the probability of detection and punishment, penalties, risk-aversion, and civic duty. To maximize profits for shareholders, the firm is expected to go after opportunities to reduce tax liabilities as long as the expected incremental benefits exceed the incremental cost (Slemrod, 2004).¹ Given her legal expertise and the potential legal complexities surrounding tax decisions, the chief counsel is likely to be instrumental in assessing important aspects of the decisions such as legality and probability of detection and punishment, and penalties, especially for tax decisions that are considered to be tax aggressive.² Bagley (2008) argue

¹ From a tax compliance perspective, this profit-maximization goal suggests that shareholders might prefer managers to be non-tax-compliant as long as the tax savings of non-compliance is expected to be greater than the costs of being investigated and/or penalized for non-compliance.

² Hanlon and Heitzman (2010) define tax avoidance broadly as the reduction of explicit taxes. A tax planning activity or a tax strategy could be anywhere along the continuum of tax avoidance depending on how aggressive the activity is in reducing taxes. Not surprisingly, the aggressive end of the continuum (e.g., evasion) is likely to involve more legal considerations. It is important to note, however, that aggressive tax avoidance is not necessarily illegal; it could just reflect extremely good tax planning within the confines of existing tax laws.

that top management teams that “include the general counsel have a higher degree of legal astuteness than those that do not” (p. 383). The heightened legal astuteness is not surprising because when the general counsel is part of top management, she is more likely to be more involved in business strategies and be in a better position to identify legal opportunities and threats. To date, there is little research on how the composition of top management relates to important firm decisions with legal implications (e.g., Kwak et al. 2012; Hopkins et al. 2012) or in particular, the role of the general counsel in tax decisions (e.g., Hanlon and Heitzman 2010, p.146).

It is important to clarify at the outset what we mean by the term “tax avoidance.” Hanlon and Heitzman (2010) state that “if tax avoidance represents a continuum of tax planning strategies where something like municipal bond investments are at one end (lower explicit tax, perfectly legal), then terms such as “noncompliance,” “evasion,” “aggressiveness,” and “sheltering” would be closer to the other end of the continuum. In other words, tax avoidance does not necessarily imply that firms are engaging in anything improper. There are numerous provisions in the tax code that allow and/or encourage firms to reduce their taxes. In addition, in practice there are many areas in which the law is unclear, particularly for complex transactions, and firms may take positions on their returns in which the ultimate tax outcome is uncertain (Dyreng et al. 2008). Hence, we define tax avoidance broadly to encompass anything that reduces the firm’s taxes relative to its pretax accounting income. Our measures of tax avoidance will reflect both tax reductions that are squarely in compliance with the law as well as those that result from gray-area interpretations, and our measures are unable to distinguish between the two.

While it seems obvious that the general counsel has an important legal role in tax strategies and that her inclusion within top management increases legal astuteness, it is unclear how the heightened astuteness translates into tax avoidance. On one hand, the

presence of a general counsel in top management can provide a more conducive environment for top management to pursue more aggressive tax strategies. Corporate tax avoidance is generally considered as exploiting the complexities, technicalities and loopholes in the tax laws (Dowling 2013) and maximizing tax savings might involve risky and uncertain tax strategies (e.g., transfer pricing, offshore intellectual property havens) that sometimes stretch the limits of legal interpretation of tax laws. The general counsel's involvement in high-level strategic decisions gives her intimate knowledge of the corporation and its business, and this business insight in addition to legal skill gives her greater ability to justify the business purpose or economic substance of the risky tax strategies. Top management is likely to be more confident and comfortable proceeding with a risky tax strategy when there is a general counsel among the team who can defend the controversial tax strategy and provide the legal assurance that the strategy would subsequently be considered sustainable. Under this view, we expect a positive association between the presence of general counsel in top management and tax avoidance.

On the other hand, the general counsel can set a conservative tone at the top and promote among the top management team a more cautious approach to the firm's business strategies, including those of tax decisions. Because the general counsel is expected to practice preventive law (Demott 2005) and help to "intervene early and prevent the company from being involved in litigation" (Brown 2003), it seems conceivable that a general counsel who is part of top management would influence top management not to proceed with risky tax strategies, especially those that push the envelope of tax laws. Consistent with corporate tax avoidance being risky is the evidence in Kim et al. (2010) that more aggressive corporate tax avoidance is associated with a higher likelihood of stock price crash risk. Aggressive tax strategies have a greater likelihood of being challenged by IRS and can subject the firm to significant legal and reputational costs. The general counsel could be blamed for her failure

to mitigate the firm's legal and compliance risks. Under this alternative view, we expect a negative association between the presence of general counsel in top management and tax avoidance.

How the composition of top management with general counsel is associated with the extent of a firm's tax avoidance is ultimately an empirical question. To test this link, we identify firms with general counsel in top management using data from Compustat ExecuComp, which covers the S&P1500 firms. To increase the robustness of our results, we rely on three measures of tax avoidance used in prior literature - discretionary permanent book-tax difference (Frank et al. 2009), likelihood of engaging in tax shelter activities (Wilson 2009), and predicted unrecognized tax benefits (Rego and Wilson 2012). Based on all three measures and controlling for other documented factors that affect tax avoidance, we find that firms with a general counsel in top management are more aggressive in their tax planning. These results are consistent with the general counsel in top management using her legal expertise to facilitate top management in avoiding taxes, rather than acting as a gatekeeper who exerts a conservative influence on the firm's tax policies.

There can be a potential endogeneity in our tests because firms that decide to be more tax aggressive may choose to elevate a general counsel to their top management team. Although this concern does not take away the key insight that a general counsel among top management can help to facilitate aggressive tax planning, we nevertheless mitigate this concern by utilizing an instrumental variable approach using three instruments. Our inferences are unchanged.³

Next, we examine the effect of FIN 48 on the relation between general counsel in top management and tax avoidance because FIN 48 increases the likelihood that IRS will be able

³ Our two-stage least square results should however be interpreted with caution. For instance, Larcker and Rusticus (2010) show that many instrumental variables applications in accounting are likely to produce highly misleading parameter estimates and inferential tests. We detail how we address these issues related to the use of the instrumental variables approach in section 4.3.

to act against the firm for potentially illegal tax-aggressive behavior (Lisowsky et al. 2013; Kennedy 2011). To the extent that general counsels in top management were more actively pursuing and facilitating tax avoidance prior to FIN 48, we expect FIN 48 to have a larger impact in constraining their behavior. We find that after in the post-FIN 48 periods, the likelihood of engaging in tax shelter activities and uncertain tax positions are less positively associated with general counsel in top management.

In our final set of analyses, we examine some cross-sectional variations in the relation between general counsel in top management and tax aggressiveness. First, we find that when the CEO has relatively more influence, having a general counsel in top management is even more positively associated with the likelihood of engaging in tax shelter activities and more uncertain tax positions. Second, when the general counsel in top management also sits on the board of directors, the firm is less likely to have uncertain tax positions. This result is consistent with board membership increasing the fiduciary duties and legal responsibilities of the general counsel such that the general counsel might feel less inclined to facilitate aggressive tax policies, especially those that test or go beyond the boundaries of tax law. Finally and interestingly, we find that when the general counsel in top management has more equity incentives, the firm is less likely to engage in tax shelter activities and has less uncertain tax positions.⁴ One explanation for this result is that when the general counsel in top management has substantial current and future wealth tied to the firm, she becomes more conservative and is less inclined to facilitate the firm in engaging in potentially legally risky tax-aggressive decisions.

Our paper contributes to the literature in several ways. First, it answers the call for more research on the role of the general counsel in tax decisions (Hanlon and Heitzman,

⁴ There is mixed evidence in the literature on the relation between compensation incentives of different executives and the corporate avoidance of the firm. For example, in a comprehensive analyses of incentives and corporate avoidance using proprietary data, Armstrong et al. (2012) find that tax director incentives are associated with GAPP effective tax rate but not with cash effective tax rate. Interestingly, CEO, CFO, and general counsel incentives are not associated with either rate.

2010). Dyreng et al. (2010) examine whether individual executives such as the CEO and CFO have an effect on their firms' tax avoidance by tracking the movement of these executives across firms during the period 1992 to 2006. Their results indicate that individual executives play a significant role in determining the level of tax avoidance that firms undertake, incremental to firm characteristics. Dyreng et al. (2010) also find that executives' backgrounds do not explain much of the variation in tax avoidance across executives. Our paper extends their study and focuses on how the composition of top management with a general counsel is associated with the firm's tax avoidance, and we find that the general counsel in top management can influence tax decisions.

Second, our paper adds to the literature on the economic consequences of management composition with general counsel. Kwak et al. (2012) find that firms with a general counsel in top management are more likely to issue forecasts, particularly bad news forecasts, than other firms. Further, their forecasts are less optimistic and more accurate than those issued by others. Hopkins et al. (2013) find that firms with general counsel in top management have lower accounting quality and engage in more earnings management than do firms with less powerful general counsel. Given the importance of the general counsel in ensuring tax compliance, a natural extension of this literature is to investigate how such a management composition relates to tax avoidance, especially since there is significant tension in the hypothesis about this relation.

The rest of this paper is organized as follows. We discuss related research and develop the hypotheses in the next section. We present the sample selection, measures of tax aggressiveness and the empirical models used in the study in section three and report the main empirical analyses in section four. We discuss further analyses in section five and six, and provide our conclusions in the final section.

2. Hypotheses Development

2.1. Top management composition with general counsel and roles of general counsel

The role of the general counsel in U.S. corporations has been evolving over time (Demott 2005; Lipson 2012). As the top legal officer of the firm, the general counsel is responsible for advising the board of directors and senior management on regulatory compliances, legal matters, and litigation risk facing the firm. They also help to facilitate transactions such as mergers, acquisitions, and patenting of intellectual property. As the business environment gets more complex and litigious, members of senior management have come to expect general counsel's involvement in high-level strategic decisions as an adviser with intimate knowledge of the corporation and its business and who is able to bring to bear business insight in addition to legal skill (DeMott 2005). Consistent with the general counsel being an important member of the top management team, many general counsels hold the title of vice president and has a close relationship with the CEO and other members of top management (Duggin 2006). In addition, the general counsel is often among the top-paying executives of the company. As reported by Equilar's 2013 Executive Compensation Survey, the median total compensation for general counsels at Fortune 1000 companies was \$1,613,654, and in our sample, 38.1 percent of firms have the general counsel among its top paying executives and their average compensation is \$1,293,731, which is approximately 25.4 percent of the CEO's remuneration. Positioned as an important member of top management team, the general counsel now wields considerable influence and power within the organizational structure (Duggin 2006).

Recent studies begin to explore how the presence of general counsels in the top echelons of management influences the firm's disclosure and financial reporting policies. For instance, Bamber et al. (2010) test the influence of individual executives on a firm's voluntary disclosure policy and find that top managers, including the general counsel, exert

economically significant individual-specific influence over five attributes of management earnings forecasts: the frequency of forecasts, forecast precision, news conveyed by the forecast, and the bias in and accuracy of the forecasts. Kwak et al. (2012) find that firms with general counsel in the top management issue more management earnings forecasts that are more accurate and less optimistic. Their results are consistent with the general counsel being an important internal advisory and governing mechanism in improving voluntary disclosure. Hopkins et al. (2013) find that firms with general counsel in top management have lower accounting quality and engage in more earnings management, suggesting that general counsel in top management team facilitate aggressive financial reporting behavior by the firm. Hence, there appears to be mixed evidence as to how having general counsel in top management influences the aggressiveness and/or quality of firms' disclosures.

2.2. Composition of top management with general counsel and tax avoidance

In this paper, we examine how the composition of top management with a general counsel is related to the firm's tax avoidance. Firms have incentives to reduce their tax burden through tax planning because the incurrence of income taxes is a substantial expense for firms and the payment of income taxes can reduce the cash available for shareholders.⁵ Prior research has documented that firms engage in different forms of tax avoidance strategies to reduce taxes, and some firms are more aggressive than others in avoiding taxes (Dyreng et al. 2008). As firms get progressively more aggressive in reducing their tax liabilities, they are more likely to stretch the limits of legal interpretation of tax laws or even push the envelope of tax laws (Hanlon and Heitzman 2010).

For instance, a form of aggressive and controversial tax avoidance activity that firms engage in is that of tax shelter, such as lease-in, lease out, transfer pricing, corporate-owned

⁵ Under the traditional view of tax avoidance, tax planning represents a value maximizing activity for a firm because it entails a transfer of wealth from the government to a firm's shareholders (Swenson 1999; Graham and Tucker 2006).

life insurance, etc.⁶ A problem with tax shelters is that it is almost always ambiguous whether the transaction is permissible or not (Hanlon and Heitzman 2010) and determining whether a tax shelter will be prohibited by the IRS can be challenging due to the complexities of tax laws (Soled 2008; McCormack 2009). Bankman (2003) argues that tax shelters are tax-motivated vehicles that use a literal interpretation of government statute or regulation to misstate economic income in a manner that is inconsistent with the spirit or intent of the statute or regulation. Generally, tax shelters are considered to be abusive by the IRS when they do not exhibit “economic substance” or a “business purpose”—that is, when they are created for the sole aim of evading tax rather than filling a non- (or pre-) tax economic need (Lisowsky 2010). In the event that the tax strategies of the firm are subsequently challenged by the IRS, the firm can either concede the invalidity of the tax transactions—and pay taxes owed, interests, and penalties—or dispute the IRS challenge, which would involve protracted litigation with an uncertain outcome.⁷ Court cases involving tax shelters are legally complex, which explains why the U.S. government has developed and invoked several non-mutually exclusive judicial doctrines to prosecute illegal tax shelter firms—sham transaction doctrine, economic substance doctrine, business purpose doctrine, substance over form doctrines, and step transaction doctrine (Graham and Tucker 2006).⁸

Given her legal expertise and the potential legal complexities surrounding tax decisions, the general counsel is likely to be instrumental in assessing important aspects of

⁶ Tax shelter activities can result in substantial tax savings for the firm. For example, Graham and Tucker (2006) find that, for 24 of the sample tax sheltering firms in their study, the median tax deduction associated with tax shelter use is more than \$1 billion per firm per year, or about 9 percent of total assets.

⁷ Costs can increase significantly if tax authorities are successful in challenging an aggressive tax position. For example, in 14 cases of tax sheltering, Wilson (2009) finds the interest charges paid by firms to tax authorities amounted to 40% of the tax savings originally generated by the tax shelter transactions. Firms can also suffer reputational penalties, not only in the increased scrutiny in future audits with tax authorities, but also if aggressive tax avoidance becomes public knowledge and negatively affects investors’ assessments of firm value (e.g., Hanlon and Slemrod 2009).

⁸ For instance, the business purpose doctrine speaks to the motivation of the taxpayer when entering the transaction. The doctrine tests whether, when entering the transaction, the taxpayer was motivated by a business purpose other than obtaining tax benefits. The economic substance doctrine tests whether transactions have economic substance (a profit motive) separate and distinct from any economic benefit achieved solely from tax reduction..

the decisions such as legality and probability of detection and punishment, and penalties, especially for tax decisions that are considered to be aggressive and risky. On one hand, the presence of a general counsel in top management can provide a more conducive environment for top management to pursue more aggressive tax strategies. Corporate tax avoidance is generally considered as exploiting the complexities, technicalities and loopholes in the tax laws (Dowling 2013) and maximizing tax savings might involve risky and uncertain tax strategies (e.g., transfer pricing, offshore intellectual property havens) that sometimes stretch the limits of legal interpretation of tax laws. The general counsel's involvement in top management strategy meetings and discussions gives her greater insights into the firm's business transactions. This intimate knowledge of the corporation and its business, coupled with her legal skills, enables the general counsel to better justify the "economic substance" and/or "business purpose" of an aggressive and risky tax strategy. Top management is likely to be more confident and comfortable proceeding with a risky tax strategy when there is a general counsel among the team who can defend the controversial tax strategy and provide the assurance that the strategy would subsequently be considered sustainable by the tax authorities.⁹ The general counsel is also able to use this business knowledge to imbue a tax transaction with an alleged business purpose, hence facilitating the implementation of risky tax strategies that have better chances of being legitimate in the eyes of the tax authorities. Under this view, we expect a positive association between the presence of general counsel in top management and tax avoidance.

On the other hand, the general counsel can set a conservative tone at the top and promote among the top management team a more cautious approach to the firm's business

⁹ The representation of the general counsel in the tax courts may increase the likelihood of the firm successfully defending the aggressive tax strategies. Consistent with the line of reasoning, Lederman and Hrungr (2006) find that parties represented by experienced attorneys who are legal experts and seasoned negotiators obtain more favorable case outcomes than unrepresented parties. Specifically, they employ a unique data set consisting of a random sample of Tax Court cases and find that taxpayer representation has a significant effect on financial outcome in cases that go to trial, and the magnitude of the effect increases with the experience of the attorney.

strategies, including those of tax decisions. According to Coffee (2003), the general counsel acts as the “gatekeeper” of the firm to monitor the accuracy of corporate disclosures and represent the shareholder and public. The general counsel is expected to practice preventive law by proactively assisting management with the assessment of legal risks and in making decisions on how to handle legal risks (Demott 2005). By doing so, the general counsel helps to “intervene early and prevent the company from being involved in litigation” (Brown 2003). Following the series of corporate failures and the enactment of the Sarbanes-Oxley Act in 2002, the general counsel is expected to assume greater legal and professional responsibilities to ensure that financial goals of the firm are attained lawfully. For instance, the Sarbanes-Oxley Act obligates the general counsel to take certain mandatory measures to prevent corporate malfeasance and to report allegations of corporate misconduct “up the ladder”.¹⁰ It is conceivable that a “conservative” general counsel who is part of the top management team would influence top management not to proceed with aggressive tax strategies, especially those that push the envelope of tax laws. This is because in the event that the tax strategies are being challenged by IRS or are considered to be non-tax-compliant, the firm can suffer significant legal and reputational costs and the general counsel could be blamed for her failure to mitigate the firm’s legal and compliance risks.¹¹ Presumably, the blame will be greater if the general counsel is part of top management. Under this view, we expect a negative association between the presence of general counsel in top management and tax avoidance.

¹⁰ Following the Sarbanes Oxley Act, the fiduciary and professional responsibilities of general counsel are increasingly codified and explicit. For example, section 307 of the SOX Act requires “an attorney to report evidence of a material violation of law or breach of fiduciary duty or similar violation by the company or any agent thereof...”

¹¹ For example, in a FBI Press Release on October 22, 2009 titled “General Counsel of Auburn Hills Employment Firm Sentenced to Prison in \$50 Million Tax Fraud”, the FBI stated the following “Today’s sentence demonstrates the serious consequences that come from committing tax fraud. In this case, the crime was committed by an attorney who should have helped his client steer clear of criminal activity, not commit fraud more effectively.” (source: <http://www.fbi.gov/detroit/press-releases/2009/de102209.htm>)

Given the opposing views on having a general counsel in top management affects a firm's tax policies, we formulate our first hypothesis in the null form as follows:¹²

Hypothesis 1: Firms with a general counsel among top management exhibit no different tax avoidance compared to firms without a general counsel among top management.

3. Sample and research design

3.1 Sample of firms with a general counsel in top management

We construct our initial sample to identify firms with a general counsel in top management from CompuStat ExecuComp for the sample period 1995-2012. ExecuComp collects the annual compensation data of the five highest-paid executives from the proxy statements reported by the S&P1500 firms. In our sample, 93.5% (97.6%) of the firms report the compensation details of at least five (four) executives. Following Kwak et al. (2012) and Hopkins et al. (2012), we examine the annual title (“titleann”) of every executive reported by ExecuComp for the presence of general counsel in top management. We consider the following titles on ExecuComp to be a general counsel in our study: “general counsel,” “chief counsel,” “corporate counsel,” “senior counsel,” “chief legal counsel,” “chief legal officer,” “chief legal executive,” “chief counsel,” “vice president of law,” “vice president of legal affairs,” etc. In our sample, 38.1% of firm-year observations report the presence of general counsel in top management ($GC = 1$). This reported incidence of general counsel in top management is lower than that reported in Kwak et al.'s (2012) reported incidence of 43.0%. The difference is likely due to missing annual titles in the earlier years of the sample, which

¹² Our paper does not take a position as to whether having a general counsel who is a “facilitator” or “gatekeeper” in tax avoidance increases firm value because the firm value outcome hinges on how tax avoidance is associated with firm value. For example, if tax avoidance increases firm value and having a general counsel in top management is associated with greater tax avoidance, then one might expect having such top management composition to increase firm value. The focus of our paper is to establish the link between general counsel in top management and tax avoidance.

Kwak et al. (2012) supplement with hand-collecting annual titles from 10-Ks and other sources. When we examine the incidence of general counsel in top management in the later years of the sample after fiscal year 2000, the incidence is 41.1%, which is very similar to that reported in Kwak et al. (2012). We then merge this sample with CompuStat and CRSP to obtain variables necessary to compute the various measures of tax aggressiveness and control variables. We also winsorize each continuous variable at the 1% and 99% level to mitigate the effect of outliers. Our final sample for our main analyses yields 21,036 firm-year observations.

3.2 *Measures of tax aggressiveness*

Hanlon and Heitzman (2010) recommend that researchers carefully consider the appropriateness of tax avoidance measures for the research question at hand. As explained in our hypothesis development, we want to examine how general counsel in top management influences tax planning activities that may be considered aggressive and test the boundaries of legality. Therefore, we focus on three measures of tax avoidance used in prior literature that more suitably and more effectively capture tax aggressiveness.

The first measure we use in this paper is discretionary book-tax difference (*DTAX*) based on Frank et al. (2009), which is defined as the residuals from the regression of permanent differences on several determinants of nondiscretionary permanent differences unrelated to tax planning (estimated by year and two-digit Standard Industrial Classification (SIC) code, firm and time subscripts omitted):

$$\begin{aligned} \text{PERMDIFF} &= \alpha_0 + \alpha_1(1/\text{ATLAG}) + \alpha_2\text{INTANG} + \alpha_3\text{UNCON} + \alpha_4\text{MI} + \alpha_5\text{CSTE} \\ &+ \alpha_6\Delta\text{NOL} + \alpha_7\text{LAGPERM} + \varepsilon \end{aligned}$$

where PERMDIFF refers to permanent book-tax differences, ATLAG refers to lagged total assets (AT), INTANG refers to goodwill and other intangibles (INTAN), UNCON refers to

income/loss reported under the equity method (ESUB), MI refers to income/loss attributable to minority interest (MII), CSTE refers to current state tax expense (TXS), Δ NOL refers to the change in net operating loss carry forwards (TLCF) and LAGPERM is the lagged PERMDIFF. PERMDIFF, INTANG, UNCON, MI, CSTE and Δ NOL are all scaled by lagged total assets.

The advantage of using *DTAX* as a measure of tax aggressiveness is that it is designed to capture permanent differences that are unrelated to items that are not considered aggressive tax reporting such as state income taxes and tax credits. Also, this measure is consistent with the claim that permanent differences reflect the more aggressive type of tax avoidance because a tax strategy that generates a permanent book-tax difference reduces a firm's effective tax rate and also increases accounting earnings and hence believed to be an "ideal" tax sheltering strategy (e.g., Shevlin 2002).

The second measure we utilize is based on the tax shelter prediction score (*SHELTER*) developed by Wilson (2009), computed as follows:

$$\begin{aligned} SHELTER = & -4.86 + 5.20 \times BTD + 4.08 \times DAC - 1.41 \times LEV + 0.76 \times Size \\ & + 3.51 \times ROA + 1.72 \times Foreign_Income + 2.43 \times R\&D \end{aligned}$$

where BTD refers to book income less taxable income scaled by lagged total assets, DAC refers to the discretionary accruals from the performance-adjusted modified cross-sectional Jones Model, LEV refers to long-term debt divided by total assets, Size refers to the log of total assets, ROA refers to pre-tax earnings divided by total assets, Foreign_Income refers to foreign pre-tax earnings divided by lagged total assets, and R&D refers to research and development expenditure divided by lagged total assets.

Based on a sample of identified tax shelter participants, Wilson (2009) develops a model to detect potential tax sheltering participants based on several observable firm

characteristics. We use the estimated coefficients from his regression model to measure the likelihood of a firm's involvement in tax sheltering activities.

The third measure we utilize is the predicted unrecognized tax benefits (*PRED_UTB*) based on Rego and Wilson (2012), computed as follows:

$$\begin{aligned} PRED_UTB = & -0.004 + 0.011 \times PT_ROA + 0.001 \times SIZE + 0.010 \times FOR_SALE \\ & + 0.092 \times R\&D - 0.002 \times DISC_ACCR + 0.003 \times LEV + 0.000 \times MTB \\ & + 0.014 \times SG\&A - 0.018 \times SALES_GR \end{aligned}$$

where *PT_ROA* refers to pre-tax income scaled by lagged total assets, *SIZE* refers to the log of total assets, *FOR_SALE* refers to the percentage of foreign sales, *R&D* refers to research and development expenditure divided by lagged total assets, *DISC_ACCR* refers to discretionary accruals calculated using performance-adjusted modified Jones model, *LEV* refers to long-term debt divided by lagged total assets, *MTB* refers to the market to book ratio, *SG&A* refers to selling, general and administrative expenses divided by lagged total assets, and *SALES_GR* refers to the average of the past three years' sales growth.

Based on a proprietary sample of firms with reportable transactions to the IRS¹³, Lisowsky et al. (2013) find that reported unrecognized tax benefits (or tax reserves) have the greatest ability to predict tax sheltering activities among various measures of tax avoidance. Because the actual reported tax reserves is only available after the implementation of FIN 48 which only becomes effective for public corporations for fiscal years beginning after December 15, 2006, we use the predicted unrecognized tax benefits based on Rego and Wilson (2012) to increase our sample size and enhance the generalizability of our results. Nonetheless, our main inferences are unchanged when we use the actual reported tax reserves

¹³ Regulations under Internal Revenue Code require a firm to attach a Form 8886 to its tax return for each "reportable transaction" in which it is involved and for each year that the transaction affects taxable income. This regulation is enacted to help the IRS combat tax sheltering by requiring firms to disclose information about transactions that potentially involve tax sheltering.

as an alternative measure for tax aggressiveness. All measures of tax avoidance are increasing in aggressiveness, and the detailed explanation of each measure is described in Appendix A.

3.3 Research design for the test of H1

To test H1, we estimate the following pooled cross-sectional regression:

$$TAX_{it} = \alpha + \beta GC_{it} + \psi FIRM_CONTROLS_{it} + YEAR_FE + IND_FE + \varepsilon_{it} \quad (1)$$

where *TAX* refers to the measure of tax aggressiveness (*DTAX*, *SHELTER* and *PRED_UTB*), *GC* is an indicator equals one if the general counsel is in top management for a particular firm-year, *FIRM_CONTROLS* refers to a vector of firm-level controls and *YEAR_FE* and *IND_FE* refer to time and industry fixed-effects respectively. The Appendix includes the detailed definition of all variables.

We select *FIRM_CONTROLS* that are documented in prior literature to be associated with tax aggressiveness (e.g., Chen et al. 2010). The first set of control variables (*ROA*, *LEV*, *NOL*, *NOLCHG* and *FI*) captures firms' profitability, leverage and foreign operations. For example, profitable firms have greater incentives to engage in tax planning activities. The second set of control variables (*PPE*, *RD*, *INTANG* and *EI*) captures differences in book and tax reporting that can affect our measures of tax aggressiveness. For example, capital intensive firms are affected by different treatment of depreciation expense for financial and tax reporting purposes. Finally, we control for *SIZE* and *MB* to control for other firm characteristics that likely affect firms' inclination to be tax aggressive.

4. Main results

4.1 Descriptive statistics

Table 1 reports the descriptive statistics on the regression variables. As reported earlier, 38.1% of our sample firm-year observations have a general counsel in top

management. For our various measures of tax aggressiveness, the mean (median) discretionary permanent book-tax difference (*DTAX*) is 0.003 (0.003), which is comparable to that reported in Frank et al. (2009). The mean (median) *SHELTER* is 1.128 (1.174) and the mean (median) *PRED_UTB* is 0.012 (0.011), which are comparable to that reported in another large sample study by Goh et al. (2013).

Table 2 reports the Pearson correlation table of the variables in our paper. The Pearson correlations between the three measures of tax aggressiveness (*DTAX*, *SHELTER* and *PRED_UTB*) are positively correlated with one another, which suggest that all three measures capture tax planning activities in general. However, the correlations among the three measures, between 0.03 to 0.25, suggest that each measure likely captures different dimensions of tax aggressiveness and hence supports our choice of using all three measures in our analyses to triangulate our results and increase the robustness of our findings. Turning to our variable of interest, we find that the presence of general counsel in top management (*GC*) is positive and significantly correlated with two measures of tax aggressiveness (*DTAX* and *SHELTER*), while it is negative and significantly correlated with *PRED_UTB*. Because these are pairwise univariate correlations, we defer the main analyses to multivariate tests in section 4.2. None of the correlations between control variables are high enough to impose a multicollinearity problem.

4.2 Main empirical analyses – Test of H1

In this section, we report our results for the test of H1 which examines the association between the presence of general counsel in top management and corporate tax aggressiveness. As shown in Table 3 Panel A, the presence of general counsel in top management is positive and significantly associated with all three measures of tax aggressiveness (t -statistic = 3.49, 7.61 and 4.22 for *DTAX*, *SHELTER* and *PRED_UTB*,

respectively). This result is more supportive of the view that the general counsel in top management uses her legal expertise to facilitate corporate tax avoidance. The effect of having a general counsel in top management on tax aggressiveness is also economically significant. Specifically, firms with general counsel in top management are associated with a 43.3%, 15.7%, and 5.0% increase in *DTAX*, *SHELTER* and *PRED_UTB*, respectively.¹⁴

To mitigate the concern that an omitted correlated variable may be driving our results, we include firm fixed-effects to control for time-invariant firm characteristics and assume that the potential endogeneity is constant over time. As reported in Table 3 Panel B, the presence of general counsel in top management continues to be positive and significantly associated with two measures of tax aggressiveness, even after controlling for firm fixed-effects (*t*-statistic = 2.66 and 2.17 for *SHELTER* and *PRED_UTB*, respectively), though the effect is positive but insignificant for *DTAX* (*t*-statistic = 1.64). Overall, the above analyses indicates that general counsel in top management likely play an important facilitating role in advising firms in their strategic tax planning activities.

4.3 *Instrumental variables approach*

We recognize that our earlier analyses might be subject to endogeneity concerns because firm's decision to place a general counsel in top management is arguably endogenously determined. That is, firm characteristics that affect the decision to place a general counsel in top management could also possibly be related to the decision to avoid tax aggressively. As highlighted in the earlier section, we mitigate this concern by including firm fixed-effects and assume that the potential omitted variable is constant over time. In this section, we utilize an instrumental variable approach to further address endogeneity concerns.

¹⁴ The impact of having a general counsel in top management (*GC*) on discretionary permanent book-tax difference (*DTAX*) is computed as 0.0013 (coefficient on *GC*) \div 0.003 (the absolute value of the sample mean of *DTAX*) = 43.3%. The other comparative statics are computed analogously.

We select three instruments which we argue to be related to the decision to place a general counsel in top management but unrelated to the decision to avoid tax aggressively. The first instrument that we use is the *ex-ante* probability of security class action lawsuit that allege a violation of SEC Rule 10b-5 (*10b5_LAWSUIT*). SEC Rule 10b-5 is specifically targeted at the intentional misstatement or omission of material information in connection with the purchase or sale of securities and hence specifically applies to corporate disclosure issues. We argue that a firm is more likely to elevate the general counsel's in-house status to the top management when it is subjected to a higher likelihood of future security class action lawsuit because of the importance of her role in handling potential lawsuits and mitigating the risk of such future lawsuits. However as highlighted earlier, because these lawsuits are specifically related to disclosure issues, we do not think that the *ex-ante* probability of security class action lawsuit relating to the violation of SEC Rule 10b-5 will directly affect firm's inclination to avoid tax. We measure *10b5_LAWSUIT* based on the estimated coefficients from Kim and Skinner (2012) who develop a model to predict the *ex-ante* risk of lawsuits pertaining to the violation of SEC Rule 10b-5. The detail of this estimation is described in the Appendix.

The second instrument that we use is the concentration of resident and active lawyers in the state where the firm's headquarters are located (*STATE_LWYR_CON*), which is computed as the number of resident and active lawyers in each state scaled by the total number of resident and active lawyers in the US. We hand-collect the data from annual statistics collated by the American Bar Association. We argue that the higher the concentration of lawyers in the state, the greater the availability of law firms that can provide outside legal expertise and advice to the firm. Therefore, there is a lower need for the firm to maintain a large in-house legal department and hence less necessity to appoint a highly-

ranked general counsel to supervise this department. However, we do not think that the availability of outside counsel expertise directly affects firm's inclination to avoid tax.

The third instrument that we use is firm age (*FIRMAGE*). Chayes and Chayes (1985) argue that more established corporations have more opportunities for legal participation in corporations' on-going planning and decision-making processes. Further, such corporations are likely to have attained the size and scope of operations that justify substantial internal legal departments. Hence, the general counsels of more established corporations are likely to have higher status. Likewise, we do not think that the degree of establishment directly affects firm's inclination to avoid tax.¹⁵ We capture the degree of establishment using firm age. As discussed below, we conduct the tests suggested by Larcker and Rusticus (2010) and find the three instruments are relevant and valid.

We report the first stage regression results in Column (1) of Table 4, where we regress *GC* on the three instruments as well as the controls used in the second stage regression.¹⁶ As predicted, we find that firms that are subjected to a higher *ex-ante* probability of lawsuits relating to SEC Rule 10b-5 (*10b5_LAWSUIT*) and more established firms (*FIRMAGE*) are more likely to appoint a general counsel in top management (*t*-statistic = 2.01 and 6.66, respectively), while firms residing in states with higher concentration of practicing lawyers (*STATE_LWYR_CON*) are less likely to appoint a general counsel in top management (*t*-statistic = -1.85). The weak identification test suggests that these three instruments are

¹⁵ Of course, it can be argued that established firms are also more profitable and hence have greater incentives to avoid tax. Because we also explicitly control for various measures of performance such as return on assets and net operating losses carry forward, we do not think that our measure of the degree of establishment is capturing firm performance.

¹⁶ We use the *ivreg2* module in Stata 12 written by Baum et al. (2010) to conduct our instrumental variables analyses. Note that for *ivreg2*, the first stage regression is based on a linear model regression despite *GC* being a binary variable. Cameron and Trivedi (2010) highlight that this treatment is reasonable because the underlying assumption of the instrumental variable (IV) estimator does not change when the endogenous regressor is binary as in our case. We opt to use an IV regression instead of a more structured treatment-effects model because as highlighted by Cameron and Trivedi (2010), if the errors are heteroskedastic (which is likely), the IV estimator remains consistent but the treatment-effects estimator becomes inconsistent. Nonetheless, we check the robustness of our results by using a probit model in the first stage and use the predicted values in the second stage regression. The results are similar to that reported here.

powerful: the F statistic for the joint explanatory power of the instrument variables is 16.82, significantly higher than the critical value suggested in Stock et al. (2002). This diagnostic test provides some assurance that our three instruments are jointly relevant.

We report the second stage regression results in Columns (2) to (4) of Table 4, and we find that the predicted incidence of having a general counsel in top management (*PREDICTED_GC*) estimated from the first-stage regression is still positive and significantly associated with all three measures of tax aggressiveness (*t*-statistic = 3.33, 7.05 and 6.91 for *DTAX*, *SHELTER* and *PRED_UTB*, respectively). The result from the over-identification test of all instruments is insignificant for two out of three measures of tax aggressiveness (*J*-statistic = 2.00 and 2.95 for *DTAX* and *SHELTER*, respectively), suggesting that two of the instruments are valid (i.e. uncorrelated with the error term in the second stage). Overall, the results from the instrumental variable approach indicate that our results still hold after controlling for potential endogeneity concern.

5. Further analyses of the positive association between general counsel in top management and tax aggressiveness

In this section, we provide additional analyses to corroborate our earlier findings and provide additional insights. In section 5.1, we examine the impact of the implementation of Financial Interpretation No. 48 (FIN 48) on the relation between the presence of general counsel in top management and tax aggressiveness. In section 5.2 to 5.4, we explore cross-sectional variation in general counsel's characteristics to see how it her ability to influence tax aggressiveness.

5.1 Pre- and post-FIN 48 analysis

FIN 48 requires firms to report their assessment of tax reserves in the financial statements, which potentially increases political scrutiny by tax authorities and others. FIN 48

also makes it easier for the IRS to detect attempts to mitigate or avoid taxes. First, Lisowsky et al. (2013) find that public disclosures of tax reserves made available through FIN 48 reflect corporate tax shelter activities. Specifically, based on a proprietary sample of reportable transactions to the IRS, the authors find that tax reserves is a good predictor of the likelihood of a firm disclosing reportable transactions and hence indicative of potential tax sheltering activities. Second, under FIN 48, in determining contingent tax liabilities, taxpayers, their accountants, and their attorneys have to produce supporting work papers to substantiate their estimation of uncertain tax positions; these work papers are known as tax accrual work papers (Kennedy, 2011). Kennedy (2011) highlight that such work papers, if provided to IRS, could allow a roadmap for the IRS to question the tax positions taken by the taxpayer. In fact, she noted that after the IRS received a favourable 2009 court decision when summoning taxpayer accrual work papers, the IRS become more aggressive in requiring the disclosure and analyses of uncertain tax positions. To the extent that the general counsel in top management is expected to be more participative in the tax strategies adopted by the firm, she is more likely to be concerned about the increased likelihood of being implicated in tax enforcement actions after FIN 48. Hence, our hypothesis is:

Hypothesis 2a: The positive association between the presence of general counsel in top management and tax aggressiveness reduces after the introduction of FIN 48.

5.2 *General counsel's relative power in top management*

Among the top executives of the firm, the CEO is likely to be the one under the greatest pressure to maximize firm value (Rego and Wilson 2012). As discussed earlier, a common way to maximize firm value is to adopt aggressive tax policies that maximize after-tax income. Prior studies have investigated the relative power/status of the different constituents within an organization, with the underlying assumption that if one constituent

has relatively more power than another constituent, the former is able to exert a greater influence on certain outcomes (e.g., Kwak et al., 2012; Badolato et al., 2013). In the context of tax aggressiveness, it is plausible that the more power that CEO has within the top management team, the more likely she is able to exert her influence on the general counsel to facilitate aggressive tax policies. Hence, our prediction is:

Hypothesis 2b: When the CEO has relatively more power than the general counsel in the top management team, there is a stronger positive association between the presence of general counsel in top management and tax aggressiveness

5.3 *General counsel in top management and board of directors*

Being on the board of directors increases the fiduciary duties and legal responsibilities of the general counsel. By acting in multiple capacities, the general counsel can compound potential personal liability. In lawsuits alleging that director violated his duty of care to the firm, the business judgment rule normally insulates directors from personal liability for corporate financial losses when the directors make decisions in good faith, loyalty and due care (Bainbridge, 2004). However, given his presumed legal expertise and knowledge of the firm's tax policies, it is likely to be difficult for the general counsel in top management and board of directors to argue that he had performed his oversight duties in good faith and due care if the firm is later found to be non-tax compliant and penalized by the tax authorities. For example, the court has held that directors who knowingly approved of illegal conduct or who knowingly or deliberately withheld material information from the board would not be protected by the business judgment rule (Branson 2002). Hence, the general counsel might feel less inclined to facilitate aggressive tax policies, especially those that test or go beyond the boundaries of tax law. Our next prediction is as follows:

Hypothesis 2c: When the general counsel in the top management team is also in the board of directors, there is a weaker positive association between tax aggressiveness of the firm and the general counsel.

5.4 Equity incentives of general counsel in top management

There is a recent literature that examines how equity incentives for executives are associated with tax avoidance. Rego and Wilson (2012) find a positive association between option vega and corporate tax aggressiveness, consistent with equity risk incentives motivating managers to undertake more aggressive tax planning.¹⁷ Robinson et al. (2010) find that tax manager incentives, measured by whether the tax department is viewed as a profit center (i.e., a “contributor to the bottom line”), are associated with lower GAAP ETRs. Using a proprietary data set with detailed executive compensation information, Armstrong et al. (2012) find that the incentive compensation of the tax director exhibits a strong negative relationship with GAAP ETR and conclude that tax directors are provided with incentives to reduce the level of tax expense reported in the financial statements. In their analyses, they also include general counsel, CEO, and CFO incentives as control variables and find that these incentives are not significantly associated with tax aggressiveness.

It is important to recognize that the link between equity incentives and risk taking, be it in the form of tax aggressiveness, financial misreporting, or other transactions, is not clear-cut. Armstrong et al. (2013) highlight the importance of considering two economic consequences of offering additional equity incentives to executives. On one hand, the executives might benefit from an increase in stock price (e.g., Cheng and Warfield 2005; Bergstresser and Philippon 2006), just like the investors in the firm. However, it is important to recognize that executives are not exactly like the typical investors. They might also have

¹⁷ Option vega measures the change in value of a manager’s equity portfolio in response to a given change in stock return volatility and hence this measure provides an estimate of the payoff to managers for increasing firm risk.

substantial negative monetary and nonmonetary consequences of risk-taking (e.g., loss of employment, loss of reputation and social status, and criminal penalties like fines and jail terms), and such considerations are likely to be exacerbated if the executive is risk averse and has substantial current and future wealth tied to the firm (e.g., Lambert et al. 1991; Carpenter 2000; Ross 2004; Lewellen 2006; Armstrong and Vashishtha 2012). In cases of non-tax compliance, for the general counsel, the presumption of guilt (or at least failure to exercise care to avoid the problems) is likely to be even greater if they are part of top management and have more equity incentives.

Given the tension in the link between tax incentives of general counsel and firms' tax aggressiveness, and prior preliminary evidence on an insignificant association in Armstrong et al. (2012), we state our hypotheses in the null form as follows:¹⁸

Hypothesis 2d: There is no association between tax aggressiveness of the firm and equity incentives given to general counsel who is part of the top management team.

6. Results of cross-sectional hypotheses

6.1 Empirical analyses of H2a

To test H2a, we estimate the following pooled cross-sectional regression:

$$TAX_{it} = \alpha + \beta GC_{it} + \psi FIRM_CONTROLS_{it} + \gamma POSTFIN48_{it} + \eta GC_{it} \times POSTFIN48_{it} + TIMETREND + IND_FE + \varepsilon_{it} \quad (2)$$

where *POSTFIN48* is an indicator variable equals one if the firm-year observation is on or after fiscal year 2007, and zero otherwise, and the other variables are previously defined.

Because of the inclusion of *POSTFIN48*, we include a time trend (*TIMETREND*) variable instead of time fixed-effects. We expect η to be negative in equation (2).

¹⁸ Armstrong et al. (2012) use a proprietary data set that has compensation data for all executives. Our analyses rely on publicly available data and hence, we only have compensation data for general counsels who are part of top management. Hence, our analyses of the link between tax aggressiveness and equity incentives are restricted to the sample of general counsels who are part of the top management team.

The result of the above estimation is presented in Table 5. Consistent with our prediction in H2a, we find that the positive association between the presence of general counsel in top management and tax aggressiveness is weaker in the post-FIN48 regime (t -statistic = -2.51 and -1.67 for $SHELTER \times POSTFIN48$ and $PRED_UTB \times POSTFIN48$, respectively), though the effect is negative but insignificant for $DTAX$ (t -statistic = -0.73 for $DTAX \times POSTFIN48$). The results suggest that the general counsel who is also part of top management is more concerned about being implicated in tax enforcement actions and hence more reluctant to facilitate aggressive tax planning in the post-FIN 48 regime.

6.2 Empirical analyses of H2b-d

To test H2b-d, we estimate the following pooled cross-sectional regression:

$$TAX_{it} = \alpha + \beta GC_{it} + \varphi GC_VAR_{it} + \psi FIRM_CONTROLS_{it} + YEAR_FE + IND_FE + \varepsilon_{it} \quad (3)$$

where GC_VAR is either: 1) CEO's total compensation divided by the general counsel's total compensation for the test of H2b ($CEO_RELPOWER$); 2) An indicator that equals one if the general counsel also sits on the board of directors, and zero otherwise for the test of H2c ($GC_INSIDEDIR$); 3) The natural logarithm of the sensitivity of the change in the general counsel's equity portfolio value to a 1% change in stock price (Core and Guay 1999) for the test of H2d ($GC_LNDELTA$).¹⁹ For the test of H2d, we additionally control for equity risk incentives (GC_LNVEGA). Because we only observe the above variables for firms with general counsel in the top management ($GC=1$), we replace the above variables with zero for firms without general counsel in the top management ($GC=0$).²⁰

¹⁹ Our results are similar when we use stock-based compensation divided by total compensation as an alternative proxy for equity incentives.

²⁰ This is similar to a modified zero-order regression (Greene 2003) where we replace the variable with zeros for missing observations and create an indicator variable that equals one for missing observations and zero for complete observations. Note that we do not need to create this additional indicator variable as the variable GC is essentially such a variable.

Table 6 reports the result of the test of H2b. When we examine *SHELTER* and *PRED_UTB* as proxies for tax aggressiveness, we find evidence consistent with our prediction that when the CEO is relatively more powerful than the general counsel in the top management team, she is better able to exert more influence on the general counsel to facilitate aggressive tax policies (t -statistic = 3.11 and 1.94 for *CEO_RELPOWER*, using *SHELTER* and *PRED_UTB* as a proxy for tax aggressiveness, respectively). However, we do not find significant results when we examine *DTAX* as a measure of tax aggressiveness.

Next, when we examine the effect of general counsel who also sits on the board of directors (Table 7), we also find some evidence consistent with our prediction in H2c. In particular, when we examine *PRED_UTB* as a proxy for tax aggressiveness, we find that when the general counsel is also a board member, she becomes more concerned about her fiduciary duties as a monitor on the board of directors and hence less inclined to facilitate aggressive tax policies (t -statistic = -3.02 for *GC_INSIDEDIR*). We do not find significant results for the other measures of tax aggressiveness.

Finally, we report the results of the test of H2d where we examine the whether the general counsel's equity incentives affects her inclination to facilitate aggressive tax policies. As shown in Table 8, we find that as the general counsel's equity portfolio value becomes more sensitive to changes in firm value, she becomes more conservative and less inclined to facilitate aggressive tax policies (t -statistic = -1.78 and -2.34 for *GC_LNDELTA*, using *SHELTER* and *PRED_UTB* as a proxy for tax aggressiveness, respectively). However, we do not find significant results when we examine *DTAX* as a measure of tax aggressiveness. In addition, we do not find that the general counsel's equity risk incentives (*GC_LNVEGA*) are significantly associated with tax aggressiveness. In untabulated analyses, we use an alternative measure of the general counsel's equity incentives based on the annual proportion

of stock-based compensation and our results are stronger and consistent with those reported above.

Overall, we find that the effect of having a general counsel in top management on tax aggressive (*GC*) remains relatively unchanged in statistical significance after considering these additional dimensions of the general counsel's relative influence and equity incentives. These results suggest that having a general counsel as part of the top management team in itself is likely the key influence behind firm's tax aggressiveness.

7. Conclusion

Motivated by calls for more research on the role of the general counsel in corporate tax avoidance and the recent literature studying the economic consequences with general counsel in top management, we document that the presence of general counsel in top management is associated with greater tax aggressiveness. This evidence is consistent with general counsel in top management using her legal expertise to implement tax policies to more aggressively reduce explicit taxes. This inference is supported by further evidence that after the implementation of FIN 48 (which constrained aggressive tax strategies), the positive association between general counsel in top management and tax aggressiveness weakened. We also examine how the positive association varies cross-sectionally with relative power of the CEO and general counsel, having a general counsel who is also on the board of directors, and sensitivity of the general counsel's wealth to the stock performance. While the results are generally not consistent across all measures of tax aggressiveness, the statistically significant results suggest that the positive association is stronger when the CEO has a relatively higher degree of influence but weaker when the general counsel is on the board of directors. An interesting finding is that when the general counsel has more wealth that is sensitive to the stock performance, she is less likely to facilitate tax aggressiveness. One interpretation of this

result is that as her equity incentives increases, the general counsel becomes more risk averse and/or more concerned about the presumption of guilt in the event of IRS enforcement.

We emphasize that our results should not be taken to mean that firms with general counsels in top management are more likely to engage in tax evasion or fraud. Greater tax aggressiveness simply means the adoption of tax strategies that reduce more explicit taxes. While the literature generally assumes that more aggressive tax strategies are more likely to test or go beyond the boundaries of tax laws, our measures are not able to distinguish between legal and illegal tax strategies. Hence, for many firms with general counsels in top management, the reason that they pay less explicit taxes could simply be a reflection of more effective tax planning.

While the objective of the paper is to address some gaps in the existing literature on corporate tax avoidance and top management composition with general counsel, one might want to consider practical implications of our findings. One implication might be that to the extent that the tax regulators are not already doing so, they might want to scrutinize the tax reports of firms with general counsels in top management more carefully. Successfully identifying tax aggressiveness represents an important potential source of revenue for tax regulators, especially with declining corporate tax revenues and the increasing gap between reported earnings and taxable income in recent years (Friedman 2003). Another implication might be that one avenue for firms to increase after-tax income through effective tax planning is to enhance the legal astuteness of top management by elevating the status of the general counsel.

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APPENDIX
Variables Definition

<i>DTAX</i>	=	<p>Discretionary component of the permanent book-to-tax differences, as in Frank et al. (2009). This variable is the residuals from the following regression (estimated by year and two-digit Standard Industrial Classification (SIC) code):</p> $\text{PERMDIFF} = \alpha_0 + \alpha_1(1/\text{ATLAG}) + \alpha_2\text{INTANG} + \alpha_3\text{UNCON} + \alpha_4\text{MI} + \alpha_5\text{CSTE} + \alpha_6\Delta\text{NOL} + \alpha_7\text{LAGPERM} + \varepsilon$ <p>where PERMDIFF is permanent book-tax difference, ATLAG refers to lagged total assets (AT), INTANG refers to goodwill and other intangibles (INTAN), UNCON refers to income/loss reported under the equity method (ESUB), MI refers to income/loss attributable to minority interest (MII), CSTE refers to current state tax expense (TXS), ΔNOL refers to the change in net operating loss carry forwards (TLCF) and LAGPERM is the lagged PERMDIFF. PERMDIFF, INTANG, UNCON, MI, CSTE and ΔNOL are all scaled by lagged total assets.</p>
<i>SHELTER</i>	=	<p>The tax shelter prediction score developed by Wilson (2009), computed as:</p> $\text{SHELTER} = -4.86 + 5.20 * \text{BTD} + 4.08 * \text{DAC} - 1.41 * \text{LEV} + 0.76 * \text{Size} + 3.51 * \text{ROA} + 1.72 * \text{Foreign_Income} + 2.43 * \text{R\&D},$ <p>where <i>BTD</i> is book income less taxable income scaled by lagged total assets, <i>DAC</i> is the discretionary accruals from the performance-adjusted modified cross-sectional Jones Model, <i>LEV</i> is long-term debt divided by total assets; <i>Size</i> is the log of total assets, <i>ROA</i> is pre-tax earnings divided by total assets, <i>Foreign_Income</i> is foreign pre-tax earnings divided by lagged total assets, <i>R&D</i> is research and development expenditure divided by lagged total assets.</p>
<i>PRED_UTB</i>	=	<p>The predicted unrecognized tax benefits based on Rego and Wilson (2012), computed as:</p> $\text{PRED_UTB} = -0.004 + 0.011 * \text{PT_ROA} + 0.001 * \text{SIZE} + 0.010 * \text{FOR_SALE} + 0.092 * \text{R\&D} - 0.002 * \text{DISC_ACCR} + 0.003 * \text{LEV} + 0.000 * \text{MTB} + 0.014 * \text{SG\&A} - 0.018 * \text{SALES_GR},$ <p>where <i>PT_ROA</i> is pre-tax income scaled by lagged total assets, <i>SIZE</i> is the log of total assets, <i>FOR_SALE</i> is the percentage of foreign sales, <i>R&D</i> is research and development expenditure divided by lagged total assets, <i>DISC_ACCR</i> is discretionary accruals calculated using performance-adjusted modified Jones model, <i>LEV</i> is long-term debt divided by lagged total assets, <i>MTB</i> is the market to book ratio, <i>SG&A</i> is selling, general and administrative expenses divided by lagged total assets, <i>SALES_GR</i> is the average of the past three years' sales growth.</p>
<i>GC</i>	=	<p>An indicator variable that equals one if the general counsel is in the top management and zero otherwise.</p>

<i>ROA</i>	=	Pre-tax income scaled by total assets at the beginning of the fiscal year.
<i>LEV</i>	=	Long-term debt scaled by total assets at the beginning of the fiscal year.
<i>NOL</i>	=	An indicator variable that equals one if loss carry forward is positive at the beginning of the fiscal year and zero otherwise.
<i>NOLCHG</i>	=	Change in loss carry forward scaled by total assets at the beginning of the fiscal year.
<i>FI</i>	=	Foreign income scaled by total assets at the beginning of the fiscal year.
<i>PPE</i>	=	Net property, plant and equipment scaled by total assets at the beginning of the fiscal year.
<i>RD</i>	=	Research and development expenses scaled by total assets at the beginning of the fiscal year.
<i>INTANG</i>	=	Intangible assets scaled by total assets at the beginning of the fiscal year.
<i>EI</i>	=	Equity income in earnings scaled by total assets at the beginning of the fiscal year.
<i>SIZE</i>	=	Natural logarithm of the market value of equity at the end of the fiscal year.
<i>MB</i>	=	Market value of equity scaled by book value of equity, measured at the end of the fiscal year.
<i>10b5_LAWSUIT</i>	=	<p><i>Ex-ante</i> probability of security class action lawsuit that allege a violation of SEC Rule 10b-5 (a misstatement or omission of material information) measured at the beginning of the fiscal year. The probability is measured based on Kim and Skinner (2012) Table 7 Model 3 estimated coefficients:</p> $10b5_LAWSUIT = -7.883 + 0.566 * FPS + 0.518 * LNASSETS + 0.982 * SALES_GROWTH + 0.379 * RETURN - 0.108 * RETSKEW + 25.635 * RETVOL + 0.00007 * TURNOVER$ <p>where <i>FPS</i> equals one if the firm is in the biotech (SIC codes 2833-2836 and 8731-8734), computer (3570-3577 and 7370-7374), electronics (3600-3674), or retail (5200-5961) industry, and zero otherwise, <i>LNASSETS</i> is the natural logarithm of total assets, <i>SALES_GROWTH</i> is the change in sales scaled by total assets at the beginning of the year, <i>RETURN</i> is the market-adjusted 12-month stock returns, <i>RETSKEW</i> is the skewness of the firm's 12-month stock returns, <i>RETVOL</i> is the standard deviation of the firm's 12-month stock returns, <i>TURNOVER</i> is the trading volume accumulated over the fiscal year, scaled by shares outstanding at the beginning of the fiscal year.</p>
<i>STATE_LWYR_CON</i>	=	The concentration of resident and active lawyers in the state where the firm's headquarters are located, computed as the number of resident and active lawyers in each state scaled by the total number of resident and active lawyers in the US. Data is collected from the American Bar Association.
<i>FIRMAGE</i>	=	Firm age measured by the number of years the company has

		data on Compustat.
<i>POSTFIN48</i>	=	An indicator variable equals one if the firm-year observation is on or after fiscal year 2007, and zero otherwise.
<i>CEO_RELPOWER</i>	=	CEO's total compensation divided by the general counsel's total compensation.
<i>GC_INSIDEDIR</i>	=	An indicator that equals one if the general counsel also sits on the board of directors, and zero otherwise.
<i>GC_LNDELTA</i>	=	The natural logarithm of the sensitivity of the change in the general counsel's equity portfolio value to a 1% change in stock price, computed similarly to Core and Guay (1999)
<i>GC_LNVEGA</i>	=	The natural logarithm of the sensitivity of the change in the general counsel's option portfolio value to a 1% change in stock price, computed similarly to Guay (1999)

TABLE 1
Descriptive Statistics

Variables	Mean	Median	Std. Dev.	Q1	Q3
<i>DTAX</i>	0.003	0.003	0.029	-0.006	0.014
<i>SHELTER</i>	1.157	1.219	1.679	-0.066	2.353
<i>PRED_UTB</i>	0.012	0.011	0.009	0.007	0.017
<i>GC</i>	0.388	0.000	0.487	0.000	1.000
<i>ROA</i>	0.088	0.090	0.138	0.029	0.157
<i>LEV</i>	0.197	0.163	0.196	0.012	0.302
<i>NOL</i>	0.069	0.000	0.226	0.000	0.026
<i>NOLCHG</i>	0.010	0.000	0.069	0.000	0.000
<i>FI</i>	0.021	0.001	0.040	0.000	0.031
<i>PPE</i>	0.302	0.231	0.248	0.117	0.414
<i>RD</i>	0.040	0.006	0.066	0.000	0.055
<i>INTANG</i>	0.193	0.113	0.227	0.011	0.296
<i>EI</i>	0.001	0.000	0.004	0.000	0.000
<i>SIZE</i>	7.272	7.124	1.627	6.180	8.268
<i>MB</i>	3.350	2.352	3.360	1.533	3.790

This table presents descriptive statistics for the sample of 21,036 firm-year observations from 1995-2012 for which we have all the variables in the table. The detailed definitions of the variables are provided in the Appendix. All continuous variables trimmed at the 1 and 99 percentiles.

TABLE 2
Pearson Correlation Table

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1 <i>DTAX</i>	1.00														
2 <i>SHELTER</i>	0.10	1.00													
3 <i>PRED_UTB</i>	0.03	0.25	1.00												
4 <i>GC</i>	0.02	0.08	-0.03	1.00											
5 <i>ROA</i>	0.21	0.40	0.09	-0.07	1.00										
6 <i>LEV</i>	0.02	-0.02	-0.21	0.10	-0.12	1.00									
7 <i>NOL</i>	0.06	-0.15	0.14	0.02	-0.19	-0.05	1.00								
8 <i>NOLCHG</i>	0.03	-0.14	0.05	0.00	-0.24	0.04	0.13	1.00							
9 <i>FI</i>	0.13	0.55	0.33	-0.01	0.32	-0.07	-0.03	-0.05	1.00						
10 <i>PPE</i>	0.01	0.00	-0.31	0.04	0.08	0.34	-0.10	-0.01	-0.05	1.00					
11 <i>RD</i>	-0.01	-0.08	0.68	-0.07	-0.12	-0.20	0.26	0.14	0.10	-0.28	1.00				
12 <i>INTANG</i>	0.04	0.12	-0.05	0.06	-0.01	0.31	-0.01	0.04	0.02	-0.27	-0.06	1.00			
13 <i>EI</i>	-0.07	0.15	-0.01	0.02	0.08	0.03	-0.03	-0.03	0.09	0.07	-0.07	-0.02	1.00		
14 <i>SIZE</i>	0.05	0.75	0.18	0.05	0.31	0.07	-0.15	-0.07	0.34	0.08	-0.02	0.15	0.14	1.00	
15 <i>MB</i>	0.02	0.06	0.19	-0.01	0.25	0.04	0.04	0.03	0.15	-0.05	0.22	-0.04	0.00	0.31	1.00

This table reports the Pearson correlation between the variables used in the regression analysis. The detailed definitions of the variables are provided in the Appendix. All correlations (with the exception of those shaded) are statistically significant at the 0.05 level or better (two-tailed).

TABLE 3
General Counsel in Top Management and Tax Avoidance

Panel A: Main regression analyses

	(1)		(2)		(3)	
	<i>DTAX</i>		<i>SHELTER</i>		<i>PRED_UTB</i>	
	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>
<i>GC</i>	0.0013	3.49 ***	0.1770	7.61 ***	0.0006	4.22 ***
<i>ROA</i>	0.0598	9.19 ***	1.9200	9.61 ***	0.0058	4.26 ***
<i>LEV</i>	0.0092	4.67 ***	-0.0460	-0.66	0.0020	3.41 ***
<i>NOL</i>	0.0132	8.32 ***	-0.0056	-0.09	-0.0003	-0.60
<i>NOLCHG</i>	0.0328	5.76 ***	-0.6940	-4.92 ***	0.0008	0.72
<i>FI</i>	0.0511	6.27 ***	11.3000	17.18 ***	0.0376	12.93 ***
<i>PPE</i>	-0.0027	-1.51	-0.3500	-3.96 ***	-0.0039	-6.76 ***
<i>RD</i>	-0.0177	-1.67 *	-1.6750	-6.45 ***	0.0850	28.28 ***
<i>INTANG</i>	0.0019	0.67	-0.0386	-0.46	-0.0040	-6.71 ***
<i>EI</i>	-0.6500	-8.83 ***	6.5720	2.41 **	0.0288	2.00 **
<i>SIZE</i>	-0.0004	-1.85 *	0.6890	57.40 ***	0.0007	8.06 ***
<i>MB</i>	-0.0006	-3.62 ***	-0.1040	-17.73 ***	-0.0001	-2.09 **
<i>CONSTANT</i>	0.0050	0.85	-4.2420	-31.15 ***	0.0021	1.62
Industry and Year FE	YES		YES		YES	
Adjusted R ²	0.098		0.747		0.614	
Observations	21,036		21,036		21,036	

TABLE 3 (Con't)

Panel B: Including firm fixed effects

	(1)		(2)		(3)	
	<i>DTAX</i>		<i>SHELTER</i>		<i>PRED_UTB</i>	
	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>
<i>GC</i>	0.0010	1.64	0.0454	2.66 ***	0.0002	2.17 **
<i>ROA</i>	0.0884	9.67 ***	3.3260	14.60 ***	0.0071	5.21 ***
<i>LEV</i>	0.0063	2.36 **	-0.6120	-11.72 ***	0.0018	3.32 ***
<i>NOL</i>	0.0165	7.52 ***	-0.1180	-1.69 *	0.0017	3.77 ***
<i>NOLCHG</i>	0.0404	6.35 ***	-0.4000	-3.19 ***	0.0031	3.63 ***
<i>FI</i>	0.0474	3.90 ***	10.0100	19.16 ***	0.0109	4.32 ***
<i>PPE</i>	-0.0120	-3.82 ***	-0.0664	-0.74	-0.0002	-0.34
<i>RD</i>	-0.0597	-3.20 ***	-1.4750	-3.36 ***	0.0924	23.30 ***
<i>INTANG</i>	0.0067	1.81 *	0.5290	6.20 ***	-0.0011	-2.55 **
<i>EI</i>	-0.6730	-6.57 ***	-2.5690	-1.10	0.0129	0.97
<i>SIZE</i>	-0.0022	-3.24 ***	0.3230	11.46 ***	-0.0006	-3.13 ***
<i>MB</i>	-0.0004	-2.14 **	-0.0658	-17.13 ***	-0.0001	-1.73 *
Firm and Year FE	YES		YES		YES	
Adjusted R ²	0.143		0.856		0.825	
Observations	20,888		20,888		20,888	

This table reports the regression results of the relation between general counsel in top management and tax avoidance. The detailed definitions of the variables are provided in the Appendix. *t*-statistics are calculated using robust standard errors based on two-way clustering by firm and year. ***, **, and * indicate statistical significance at the 0.01, 0.05 and 0.10 level or better, respectively (two-tailed test).

TABLE 4
General Counsel in Top Management and Tax Avoidance – Instrumental Variables (2SLS) Approach

	(1)		(2)		(3)		(4)	
	<i>GC</i>		<i>DTAX</i>		<i>SHELTER</i>		<i>PRED_UTB</i>	
	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>
<i>PREDICTED_GC</i>			0.0284	3.33 ***	6.1700	7.05 ***	0.0358	6.91 ***
<i>ROA</i>	-0.2490	-7.93 ***	0.0654	15.49 ***	3.4710	10.90 ***	0.0144	7.62 ***
<i>LEV</i>	0.1420	6.16 ***	0.0060	2.78 ***	-0.9840	-5.07 ***	-0.0034	-2.96 ***
<i>NOL</i>	0.0517	2.91 ***	0.0113	6.12 ***	-0.3170	-2.58 ***	-0.0026	-3.43 ***
<i>NOLCHG</i>	-0.0403	-0.73	0.0351	5.81 ***	-0.3430	-0.97	0.0028	1.29
<i>FI</i>	-0.0929	-0.94	0.0543	7.58 ***	11.7400	18.70 ***	0.0400	10.73 ***
<i>PPE</i>	-0.1130	-4.98 ***	0.0004	0.19	0.4370	2.46 **	0.0015	1.43
<i>RD</i>	-0.4630	-6.64 ***	-0.0031	-0.36	1.7560	2.73 ***	0.1090	28.22 ***
<i>INTANG</i>	0.0225	1.10	0.0006	0.41	-0.0179	-0.14	-0.0036	-4.69 ***
<i>EI</i>	-1.6620	-2.01 **	-0.6330	-10.27 ***	15.4500	2.93 ***	0.0804	2.59 ***
<i>SIZE</i>	0.0090	3.18 ***	-0.0007	-3.09 ***	0.5960	27.82 ***	0.0001	0.78
<i>MB</i>	0.0021	1.63	-0.0008	-7.11 ***	-0.1090	-13.57 ***	-0.0001	-1.48
<i>10b5_LAWSUIT</i>	0.0048	2.01 **						
<i>STATE_LWYR_CON</i>	-0.1590	-1.85 *						
<i>FIRM_AGE</i>	0.0021	6.66 ***						
<i>CONSTANT</i>	0.3160	5.71 ***	-0.0053	-1.12	-6.1960	-50.95 ***	-0.0111	-16.86 ***
Industry and Year FE	YES		YES		YES		YES	
Adjusted R ²	0.060		0.095		0.756		0.669	
Observations	19,491		19,491		19,491		19,491	
Kleibergen-Paap rk Wald F statistic (Weak identification test)				16.82 ***		16.82 ***		16.82 ***
Hansen J-statistic (Over-identification test of all instr.)				2.00		2.95		43.15 ***

This table reports the regression results of the relation between general counsel in top management and tax avoidance using an instrumental variables (2SLS) approach where Column 1 reports the results of the first-stage regression. The detailed definitions of the variables are provided in the Appendix. *t*-statistics are calculated using robust standard errors. ***, **, and * indicate statistical significance at the 0.01, 0.05 and 0.10 level or better, respectively (two-tailed test).

TABLE 5
General Counsel in Top Management and Tax Avoidance conditioning on the Passage of FIN48

	(1)		(2)		(3)	
	<i>DTAX</i>		<i>SHELTER</i>		<i>PRED_UTB</i>	
	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>
<i>GC</i>	0.0016	2.58 ***	0.2080	7.41 ***	0.0008	4.73 ***
<i>POSTFIN48</i>	0.0000	0.02	0.0690	1.64	0.0003	0.58
<i>GC</i> × <i>POSTFIN48</i>	-0.0005	-0.73	-0.0846	-2.51 **	-0.0003	-1.67 *
<i>ROA</i>	0.0588	9.64 ***	1.9390	9.31 ***	0.0054	4.17 ***
<i>LEV</i>	0.0095	5.02 ***	-0.0468	-0.67	0.0018	3.02 ***
<i>NOL</i>	0.0127	7.75 ***	-0.0051	-0.08	-0.0002	-0.44
<i>NOLCHG</i>	0.0324	5.68 ***	-0.6850	-4.83 ***	0.0005	0.43
<i>FI</i>	0.0495	6.09 ***	11.3100	17.26 ***	0.0383	12.81 ***
<i>PPE</i>	-0.0027	-1.58	-0.3490	-3.98 ***	-0.0038	-6.91 ***
<i>RD</i>	-0.0168	-1.60	-1.6680	-6.39 ***	0.0833	27.76 ***
<i>INTANG</i>	0.0018	0.65	-0.0380	-0.46	-0.0041	-7.25 ***
<i>EI</i>	-0.6620	-8.85 ***	6.6220	2.42 **	0.0266	1.83 *
<i>SIZE</i>	-0.0004	-2.08 **	0.6870	56.31 ***	0.0008	8.03 ***
<i>MB</i>	-0.0006	-3.38 ***	-0.1050	-18.19 ***	-0.0001	-2.32 **
<i>TIMETREND</i>	-0.0002	-0.77	0.0130	3.42 ***	0.0001	2.68 ***
<i>CONSTANT</i>	0.0090	1.60	-4.2830	-30.34 ***	0.0011	0.91
Industry FE	YES		YES		YES	
Adjusted R ²	0.090		0.746		0.610	
Observations	21,036		21,036		21,036	

This table reports the regression results of the relation between general counsel in top management and tax avoidance, conditioning on the passage of FIN48. The detailed definitions of the variables are provided in the Appendix. *t*-statistics are calculated using robust standard errors based on two-way clustering by firm and year. ***, **, and * indicate statistical significance at the 0.01, 0.05 and 0.10 level or better, respectively (two-tailed test)

TABLE 6
General Counsel in Top Management and Tax Avoidance – CEO’s Relative Power

	(1)		(2)		(3)	
	<i>DTAX</i>		<i>SHELTER</i>		<i>PRED_UTB</i>	
	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>
<i>GC</i>	0.0021	2.48 **	0.1130	3.66 ***	0.0003	2.08 **
<i>CEO_RELPOWER</i>	-0.0002	-1.31	0.0157	3.11 ***	0.0001	1.94 *
<i>ROA</i>	0.0589	8.60 ***	1.9060	9.94 ***	0.0057	4.11 ***
<i>LEV</i>	0.0091	4.72 ***	-0.0421	-0.62	0.0022	3.55 ***
<i>NOL</i>	0.0126	7.71 ***	-0.0095	-0.16	-0.0003	-0.62
<i>NOLCHG</i>	0.0328	5.93 ***	-0.6930	-4.51 ***	0.0009	0.76
<i>FI</i>	0.0518	6.21 ***	11.1500	17.46 ***	0.0369	12.92 ***
<i>PPE</i>	-0.0022	-1.15	-0.3480	-3.85 ***	-0.0040	-6.65 ***
<i>RD</i>	-0.0150	-1.36	-1.6980	-6.39 ***	0.0844	27.32 ***
<i>INTANG</i>	0.0016	0.59	-0.0369	-0.44	-0.0040	-6.38 ***
<i>EI</i>	-0.6610	-8.82 ***	6.3740	2.37 **	0.0270	1.85 *
<i>SIZE</i>	-0.0003	-1.45	0.6900	59.21 ***	0.0007	7.96 ***
<i>MB</i>	-0.0006	-3.50 ***	-0.1040	-17.98 ***	-0.0001	-2.01 **
<i>CONSTANT</i>	0.0036	0.58	-4.2490	-30.94 ***	0.0023	1.67 *
Industry and Year FE	YES		YES		YES	
Adjusted R ²	0.096		0.750		0.612	
Observations	20,128		20,128		20,128	

This table reports the regression results of the relation between general counsel in top management and tax avoidance, conditioning on the relative compensation of the general counsel. The detailed definitions of the variables are provided in the Appendix. *t*-statistics are calculated using robust standard errors based on two-way clustering by firm and year. ***, **, and * indicate statistical significance at the 0.01, 0.05 and 0.10 level or better, respectively (two-tailed test).

TABLE 7
General Counsel in Top Management and Tax Avoidance – General Counsel sitting on the Board of Directors

	(1)		(2)		(3)	
	<i>DTAX</i>		<i>SHELTER</i>		<i>PRED_UTB</i>	
	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>
<i>GC</i>	0.0013	3.33 ***	0.1760	7.37 ***	0.0007	4.42 ***
<i>GC_INSIDEDIR</i>	0.0003	0.17	0.0223	0.30	-0.0013	-3.02 ***
<i>ROA</i>	0.0598	9.18 ***	1.9200	9.59 ***	0.0058	4.27 ***
<i>LEV</i>	0.0092	4.67 ***	-0.0460	-0.66	0.0020	3.40 ***
<i>NOL</i>	0.0132	8.32 ***	-0.0056	-0.09	-0.0003	-0.60
<i>NOLCHG</i>	0.0328	5.76 ***	-0.6950	-4.93 ***	0.0008	0.73
<i>FI</i>	0.0511	6.27 ***	11.3000	17.16 ***	0.0376	12.98 ***
<i>PPE</i>	-0.0027	-1.51	-0.3500	-3.96 ***	-0.0039	-6.77 ***
<i>RD</i>	-0.0177	-1.67 *	-1.6750	-6.45 ***	0.0849	28.25 ***
<i>INTANG</i>	0.0019	0.67	-0.0387	-0.46	-0.0040	-6.70 ***
<i>EI</i>	-0.6500	-8.83 ***	6.5690	2.41 **	0.0290	2.02 **
<i>SIZE</i>	-0.0004	-1.84 *	0.6890	57.30 ***	0.0007	8.02 ***
<i>MB</i>	-0.0006	-3.61 ***	-0.1040	-17.72 ***	-0.0001	-2.10 **
<i>CONSTANT</i>	0.0050	0.85	-4.2420	-31.15 ***	0.0022	1.63
Industry and Year FE	YES		YES		YES	
Adjusted R ²	0.098		0.747		0.614	
Observations	21,036		21,036		21,036	

This table reports the regression results of the relation between general counsel in top management and tax avoidance, conditioning on the general counsel sitting on the board of directors. The detailed definitions of the variables are provided in the Appendix. *t*-statistics are calculated using robust standard errors based on two-way clustering by firm and year. ***, **, and * indicate statistical significance at the 0.01, 0.05 and 0.10 level or better, respectively (two-tailed test).

TABLE 8
General Counsel in Top Management and Tax Avoidance – General Counsel’s Equity Incentives

	(1)		(2)		(3)	
	<i>DTAX</i>		<i>SHELTER</i>		<i>PRED_UTB</i>	
	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>	<i>Coef.</i>	<i>t-stats</i>
<i>GC</i>	0.0004	0.41	0.2070	7.32 ***	0.0009	5.18 ***
<i>GC_LNDELTA</i>	0.0000	0.28	-0.0051	-1.78 *	0.0000	-2.34 **
<i>GC_LNVEGA</i>	0.0002	1.31	0.0031	0.77	0.0000	0.44
<i>ROA</i>	0.0589	9.11 ***	1.8910	9.44 ***	0.0059	4.35 ***
<i>LEV</i>	0.0092	4.66 ***	-0.0659	-0.95	0.0021	3.48 ***
<i>NOL</i>	0.0128	8.35 ***	-0.0091	-0.16	-0.0003	-0.50
<i>NOLCHG</i>	0.0323	5.47 ***	-0.7110	-4.98 ***	0.0006	0.58
<i>FI</i>	0.0525	6.45 ***	11.3000	17.08 ***	0.0375	12.93 ***
<i>PPE</i>	-0.0023	-1.30	-0.3300	-3.69 ***	-0.0039	-6.77 ***
<i>RD</i>	-0.0179	-1.69 *	-1.6910	-6.53 ***	0.0849	28.23 ***
<i>INTANG</i>	0.0020	0.69	-0.0393	-0.46	-0.0041	-6.81 ***
<i>EI</i>	-0.6510	-8.95 ***	6.4790	2.35 **	0.0296	2.04 **
<i>SIZE</i>	-0.0004	-1.74 *	0.6930	57.42 ***	0.0007	8.19 ***
<i>MB</i>	-0.0006	-3.57 ***	-0.1040	-17.40 ***	-0.0001	-2.09 **
<i>CONSTANT</i>	0.0050	0.84	-4.2760	-31.01 ***	0.0020	1.54
Industry and Year FE	YES		YES		YES	
Adjusted R ²	0.097		0.748		0.616	
Observations	20,967		20,967		20,967	

This table reports the regression results of the relation between general counsel in top management and tax avoidance, conditioning on the general counsel’s equity incentives. The detailed definitions of the variables are provided in the Appendix. *t*-statistics are calculated using robust standard errors based on two-way clustering by firm and year. ***, **, and * indicate statistical significance at the 0.01, 0.05 and 0.10 level or better, respectively (two-tailed test).