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Does Index Addition Affect Corporate Tax Avoidance?

Fariz Huseynov^{*}, Sabuhi Sardarli[†], and Wei Zhang[‡]

Abstract

We examine corporate tax avoidance of firms around addition to the S&P 500 index. We find that corporate tax avoidance for firms at high levels of tax avoidance decreases after index addition, whereas tax avoidance for firms at low levels of tax avoidance increases after index addition. We disentangle the impact of changing governance practices from that of declining investment opportunities. Our findings indicate that the changes in tax avoidance can be attributed to improving governance practices, specifically higher institutional ownership and executive compensations, and this impact is above and beyond the changes in growth opportunities of index firms.

Keywords: Tax avoidance; Effective tax rate; Corporate governance; Index addition.

JEL classifications: G14; G3; H26

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