

CHAPTER I

INTRODUCTION

1.1 Background of the Study

Indonesia, also known as the developing country, has the potential of becoming a better country. And one of the major contributions to a country is tax. According to Prof Dr. Rochmat Soemitro, S.H. in Siti Resmi (2017), tax is citizens' contributions to the state (which can be enforced) according to the regulations, with no return of achievement (contra-accomplishments) that are visible and used to pay general costs.

As a source of funds and as a regulator for a country, tax is collected from the public and store in the state treasury. It is used in finance government expenditures, such as construction, infrastructure, spending for employees working related to government, buying goods and others. In order to increase a country's economy, taxpayers (individuals or corporate) need to contribute by fulfilling their duty to pay tax voluntarily or compulsively to the state.

However, companies often treat tax as a burden since it reduces company's net profit. This results in many taxpayers pay less amount of tax, which makes the tax target and realization have a different amount. Thus, the tax government releases a regulation related to the decrease of entity tax incentives as regulated in Law Number 36 the Year 2008 Article 17 Paragraph 2a. The article

stated that the lowest tax rate for entity taxpayers and the permanent establishment is 25% which applies to start from the tax year of 2010.

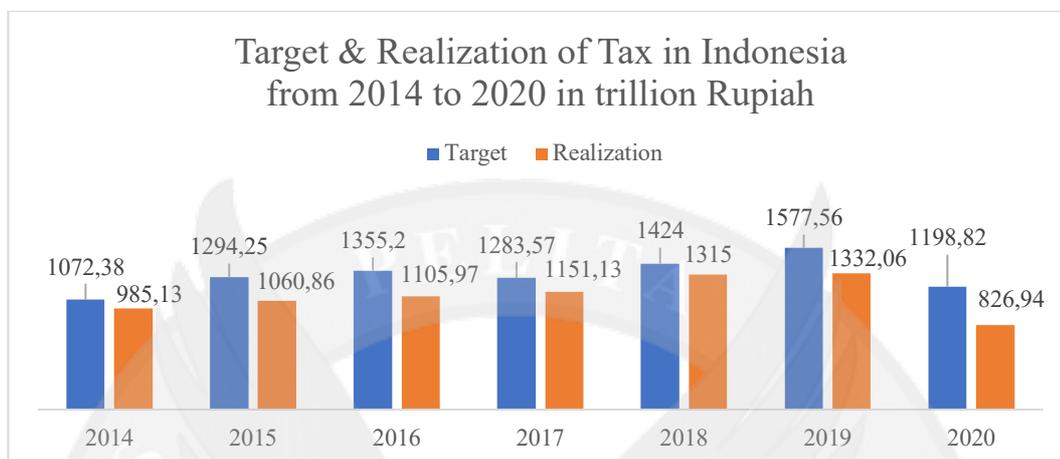


Figure 1.1: Tax Target and Realization in Indonesia from 2014 to 2020 in trillion Rupiah
Source: *Lokadata (2020)*

There are ways to minimize the amount of tax paid legally and illegally, such as tax planning, tax avoidance and tax evasion (Pohan, 2017). Practically, tax planning often being used too aggressively, which later leads to tax avoidance and also tax evasion. One example of tax planning is using the proper accounting method to decrease the effective tax rate. The effective tax rate is intended to measure tax compliance compared to economic revenue. The lack of tax management effectiveness results in massive tax avoidance practices. Thus, an effective tax rate is needed to maximize tax management within an entity and achieve the predetermined government revenue target.

Some companies practice aggressive tax avoidance and have been noted down by the Directorate General of Taxes, for example, PT Adaro Energy Tbk. PT Adaro Energy Tbk manipulated by using transfer pricing along with a company in Singapore, Coaltrade International Pte Ltd. From the report, PT

Adaro Energy Tbk is suspected of selling coal below international standard prices with an average of US \$26.3 per tonne during 2005-2006. The coal trade sold the coal at market price and tended to avoid royalties and taxes paid to the national treasury. Coaltrade International Pte Ltd's financial report document shows that Coaltrade International Pte Ltd 's profit was higher than PT Adaro Energy Tbk's. It raises suspicions of PT Adaro Energy Tbk, who owns the mine but has a small profit. It is thought to be the existence of transfer pricing at PT Adaro Energy Tbk by using the resale method. It is estimated that the transfer pricing activity done by PT Adaro Energy Tbk causes Indonesia to lose at least 10 trillion Rupiah (Oktavia et al., 2012).

The measurement of aggressive tax planning can also be measure using an effective tax rate (ETR). Several factors such as profitability, leverage and company size affect a company to do tax avoidance. A profitability ratio is a measurement that shows a company's ability to make a profit from its operational activities. Research is done by Noor et al. (2010), Waluyo et al. (2015), Handayani (2018), Salaudeen and Eze (2018) and Kasim and Saad (2019) stated that profitability has a significant positive effect on tax avoidance. However, Irianto et al. (2017) and Yahaya and Yusuf (2020) stated that profitability negatively influences aggressive tax avoidance.

A company with high profitability does not always free from the risk of debt. Therefore, it is essential to know the company leverage ratio, as it implies whether the company is using debt to finance it. According to Waluyo et al. (2015), Delgado et al. (2018), Kasim and Saad (2019) and Yahaya and Yusuf

(2020), stated that leverage positively influences tax avoidance. On the contrary, research done by Salaudeen and Eze (2018) stated that leverage have negative influence tax avoidance. While Sulistyowati and Hendrawati (2018) and Handayani (2018) stated that leverage does not influence on tax avoidance.

Besides, tax avoidance practice is also affected by company size. A company's size can affect revenue since profit is generated, affecting company assets, corporate debt and tax payment. Research is done by Noor et al. (2010), Waluyo et al. (2015), Irianto et al. (2017) and Handayani (2018), Kasim and Saad (2019) and Yahaya and Yusuf (2020) proves that company size significantly affects the tax avoidance. However, research is done by Sulistyowati and Hendrawati (2018), Delgado et al. (2018) and Fitria and Handayani (2019) stated that company size does not have any significant effect on the tax avoidance.

Ministry of Industry Airlangga Hartarto said that manufacturing industry is the backbone of the national economy. The consumer goods industry is a part of the manufacturing industry. The sub-sector under consumer goods are food & beverage, cigarette, pharmaceuticals, cosmetics & household goods, and household appliances. Mr. Hartarto stated that Indonesia's food and beverage industry is potential and could become a champion, mainly because there are many suppliers and users. Besides, Indonesia has a high population and an outstanding market share, which bring helps to the development of consumer goods industry. Figure 1.2 shows food and beverage industry development to Indonesia economic growth (GDP) from year 2014 to 2020.

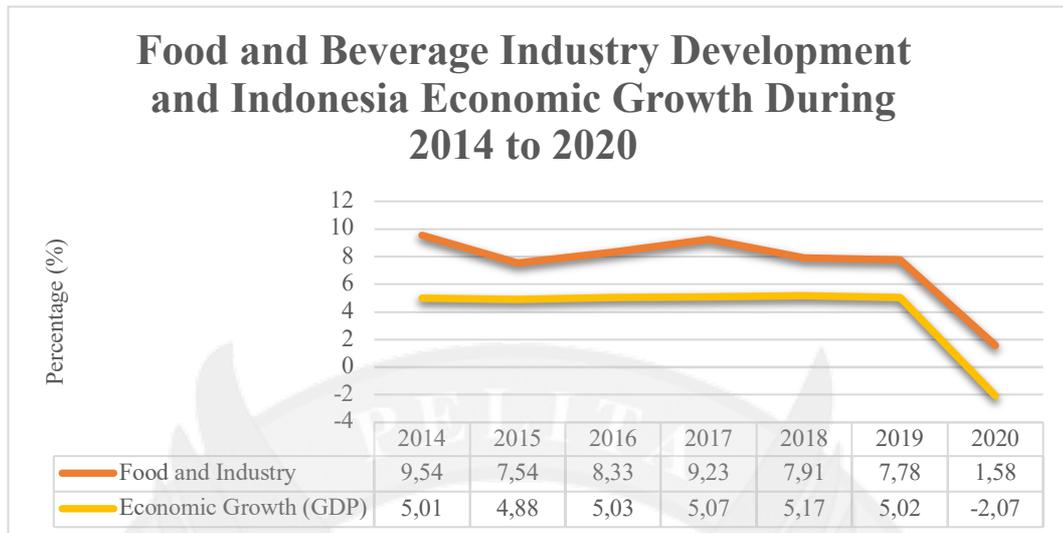


Figure 1.2: Food and Beverage Industry Development and Economic Growth During 2014 to 2020

Source: Prepared by researcher (2021)

Figure 1.2 shows food and beverage industry development and Indonesia Economic Growth during 2014 to 2020. During 2015 to 2017 the development of food and industry have the average of 8.16. As for the economic growth shows a stable result. The sudden drop of both food and beverage industry development and economic growth on 2020 is caused by the coronavirus-19 (COVID-19) pandemic. The pandemic causes not only the decreasing in Indonesia economic growth but also impacts to other country's economic growth as well. Below are some data of consumer goods companies listed as LQ-45 Index for year 2014 to 2020.

Table 1.1 The Phenomena of Profitability, Leverage, Company Size and Tax Avoidance at Consumer Goods Companies Listed as LQ-45 Index in Indonesia Stock Exchange from 2014 to 2020

Company Name	Year	Profitability (ROE)	Leverage (DER)	Company Size (Ln Asset)	Tax Avoidance (ETR)
PT Gudang Garam Tbk (GGRM)	2014	16.24%	0.75	31.70%	25.13%
	2015	16.98%	0.67	31.78%	25.27%
	2016	16.87%	0.59	31.77%	25.29%
	2017	18.38%	0.58	31.83%	25.69%
	2018	17.27%	0.53	31.87%	25.63%
	2019	21.36%	0.54	32.00%	24.90%
	2020	13.07%	0.34	31.99%	20.86%
PT Indofood CBP Sukses Makmur Tbk (ICBP)	2014	16.83%	0.66	30.85%	25.29%
	2015	17.84%	0.62	30.91%	27.10%
	2016	19.63%	0.56	30.99%	27.22%
	2017	17.43%	0.56	31.08%	31.95%
	2018	20.52%	0.51	31.17%	27.74%
	2019	20.10%	0.45	31.29%	27.93%
	2020	14.74%	1.06	32.27%	25.51%
PT Unilever Indonesia Tbk (UNVR)	2014	124.78%	2.11	30.29%	25.25%
	2015	121.22%	2.26	30.39%	25.26%
	2016	135.85%	2.56	30.45%	25.45%
	2017	135.40%	2.65	39.57%	25.26%
	2018	120.21%	1.58	30.60%	25.25%
	2019	139.97%	2.91	30.66%	25.34%
	2020	145.09%	3.16	30.65%	22.19%

Source: Prepared by researcher (2021)

The table above indicates the inconsistency between profitability and effective tax rate. For example, the profitability in PT Indofood CBP Sukses Makmur Tbk (ICBP) increase in 2016 compared to 2015, and the effective tax rate in 2016 also increases. However, the reversed condition happens on PT Gudang Garam Tbk (GGRM), where the profitability in 2019 is higher than in 2018, but the effective tax rate in 2018 is higher than in 2019.

PT Unilever Indonesia Tbk (UNVR) shows that leverage in 2017 is higher than in 2018, the effective tax rate of UNVR shows that 2018 is lower than 2017. Reversely, PT Indofood CBP Sukses Makmur Tbk (ICBP) leverage in 2018 is the same with 2017. Still, the effective tax rate in 2017 is higher than in 2018, which shows the inconsistency between leverage and effective tax rate.

The inconsistency between company size and effective tax rate also happens at PT Unilever Indonesia Tbk (UNVR). The company size in 2019 is more extensive than in 2018, shows the increase of effective tax rate in 2019 compares to 2018. Meanwhile, the company size at PT Gudang Garam Tbk (GGRM) in 2015 is more prominent than in 2016. However, the effective tax rate in 2015 is lower than in 2016.

By seeing the factors that may affect the income tax, resulting from previous research and table phenomena above, the researcher decided to analyze how profitability, leverage and company size will affect the company's effective tax rate. The researcher chooses to use the consumer goods sector companies listed as LQ-45 Index, with the limitation of the period from 2014 to 2020 market as the research object. Through the background of the research that is explained above, this research title will be **"The Influence of Profitability, Leverage and Company Size toward Tax Avoidance at Consumer Goods Companies Listed as LQ45 Index in Indonesia Stock Exchange."**

1.2 Problem Limitation

The object of this research is limited to consumer goods companies that is listed as LQ-45 Index in Indonesia Stock Exchange (IDX). This research uses documentation of financial reports of the selected companies from 2014 to 2020. The independent variables in this research are profitability measures by return on equity (X_1), leverage measures by debt to equity ratio (X_2), and company size measure by natural logarithm of total asset (X_3). While the dependent variable in this research is tax avoidance which is measures by effective tax rate (Y)

1.3 Problem Formulation

According to the background of the study, the researcher decided to choose and identify some problems, such as:

1. Does profitability influence tax avoidance at consumer goods companies listed as LQ-45 Index in Indonesia Stock Exchange?
2. Does leverage influence tax avoidance at consumer goods companies listed as LQ-45 Index in Indonesia Stock Exchange?
3. Does company size influence tax avoidance at consumer goods companies listed as LQ-45 Index in Indonesia Stock Exchange?
4. Do profitability, leverage, and company size influence tax avoidance at consumer goods companies listed as LQ-45 Index in Indonesia Stock Exchange?

1.4 Objective of the Research

Here are some objective of the research that you can make to solve the problem that've been found, which are:

1. To know the influence of profitability toward tax avoidance at consumer goods companies listed as LQ-45 Index in Indonesia Stock Exchange.
2. To know the influence of leverage toward tax avoidance at consumer goods companies listed as LQ-45 Index in Indonesia Stock Exchange.
3. To know the influence of company size toward tax avoidance at consumer goods companies listed as LQ-45 Index in Indonesia Stock Exchange.
4. To know the influence of profitability, leverage and company size toward tax avoidance at consumer goods companies listed as LQ-45 Index in Indonesia Stock Exchange.

1.5 Benefit of the Research

Through the research purpose stated above, researcher hopes that this research will give some impacts and benefits to:

1.5.1 Theoretical Benefit

- a. This research can add more knowledge regarding the factors that can affect tax avoidance to the company listed as LQ-45 Index in Indonesia Stock Exchange.
- b. The result of this research can be a guide for further researchers who have the same research object.

1.5.2 Practical Benefit

- a. For investors, it can be used as a material and knowledge for deep consideration investment decision-making.
- b. For the company, it can be used as a consideration of to pay more attention on the company's condition for the amount of profitability, leverage and company size of each annually when creating an effective tax planning.
- c. For academics and researcher, it can be used as empirical evidence, insight and reference to further research.

