CHAPTER I

INTRODUCTION

1.1 Background of Study

The purpose of a nation to tax its people is to ensure the development of the country for the greater good of its people. The administration and development of a nation depend heavily on tax income. This function is called the *budgetair* function. With this function, the tax officer will try to increase state revenues as much as possible (Faradiza, 2018). With the depletion of Indonesia's natural resources, the government will rely more on the tax sector for revenue in the APBN. The large role of taxes in contributing to state revenues requires efforts so that these revenues can be realized. Efforts to increase tax revenue do not only rely on the role of the Directorate General of Taxes, but also the participation and enthusiasm of the taxpayers themselves (Rizki, 2020).

As the largest source of income for a country, it is no wonder that taxes are extremely crucial for the growth of a nation. Taxes are being used as one of the ways to finance and developing a country. To increase tax revenues, it is very important to gather as many taxpayers as possible. Paying taxes become the responsibility for each of the people in the nation with the taxes officials as the supervising agents. (Tiraada, 2013).

Table 1.1 State Revenue (APBN) Data

Source of Income	Realization of State Revenue (Billion Rupiah)				
	2016	**2017**	**2018**	**2019**	**2020**
Tax Income	1.284.970,10	1.343.529,80	1.518.789,80	1.546.141,90	1.404.507,50
Non-taxable Income	261.976,30	311.216,30	409.320,20	408.994,30	294.141,00
Grant	8.987,70	11.629,80	15.564,90	5.497,30	1.300,00
Total	1.555.934,20	1.666.375,90	1.943.674,90	1.960.633,60	1.699.948,50

Source: *Badan Pusat Statistik* (2021)

In Table 1.1, data from *Badan Pusat Statistik* shows that the highest contributor from 2016 to 2020 comes from income tax. This proves that Indonesia's largest income is from taxes, and it can be said that taxes play an important role as a support for Indonesia's growth (Kemenkeu, 2020).

Tax collection is a form of obligation of citizens as taxpayers as well as an active role to finance various state needs, namely in the form of national development whose implementation is regulated in laws and regulations for the purpose of the welfare of the nation and state. Tax determination in Indonesia is always based on the law, in accordance with the mandate of the 1945 amendment, in the provisions of article 23 paragraph (2) which states that all taxes for the use of the state treasury are based on the law (Warmandan Riewanto, 2018).

However, optimization of tax revenue still has obstacles, one of which is the high tax arrears. There are several reasons for the high tax arrears, one of them is ranging from tax avoidance to the inability of taxpayers to pay their tax debts (Nalle, 2017).

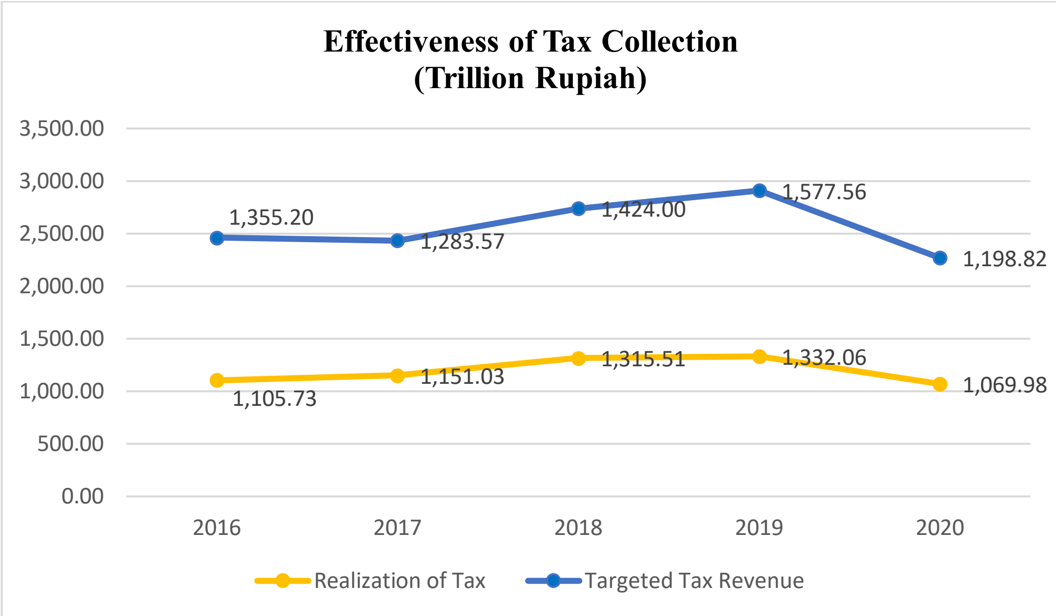

Figure 1.1 Effectiveness of Tax Collection

Source: Data compiled by the writer (2021)

Based on figure 1.1 above which data is derived from Directorate General of Tax, shows that tax revenue realization is fluctuating and decreasing recently. In 2019 the realization of tax revenue was Rp. 1.332,06 trillion from the target of Rp. 1.577,56 trillion, so that there was still a shortfall of Rp. 245 trillion from the 2019 State Revenue (APBN) target. Furthermore, since 2009, the government has not been able to meet its revenue targets (Sembiring, 2020).

The government and companies have different perspectives regarding tax payments. The government wants large tax revenues from companies to finance development, on the other hand companies try to reduce tax payments to the government so that the profits obtained are even greater (Manurung, 2020).

The object of this research is mining sector companies listed on the Indonesia Stock Exchange. The mining sector in Indonesia has long been a major driving force in the country's economic development, contributing significantly to GDP through profitable exports. The development has resulted in a diverse range of job opportunities. Indonesia is a resource-rich country, and it leads the world in coal mining production (Cekindo, 2021).

Moreover, mining companies are one of the biggest tax contributors in Indonesia, which is quite problematic. This is evidenced by the Ministry of Finance noting that more taxpayers holding mineral and coal mining business permits do not report their annual tax returns than do those who do. In 2015 out of 8,000 taxpayers in the coal industry there were 4,532 taxpayers who did not report their tax returns. This figure certainly does not include small-scale coal players who are not registered as taxpayers. It should also be noted that among taxpayers who report their tax returns, there is the potential for not reporting according to the facts on the ground. Not a few also report their SPT correctly but are the result of tax avoidance and tax savings such as aggressive tax planning, corporate inversion, profit shifting and transfer mispricing. As a result, tax revenues from the mineral and coal sector, especially coal, are still far from their true potential (Katadata, 2019).

Table 1.2 The Largest Tax Contributor Sector in Indonesia

Sector	Amount of tax collected in trillion rupiah				
	2016	2017	2018	2019	2020
Manufacturing industry	57.079,11	60.831,95	372.821,91	371.713,77	60.854,67
Trade	163.089,73	200.276,25	241.860,55	245.835,29	162.235,75
Transportation and warehousing	33.792,42	47.169,85	42.644,56	50.774,77	50.786,73
Mining	74.111,01	103.927,45	155.318,34	123.308,12	123.316,1
Construction	57.079,11	60.831,95	64.495,98	66.631,70	66.647,72

Source: Data compiled by the writer (2021)

Based on table 1.2, which data is derived from *Data Statistik*, shows that from many business sectors listed in BEI, the mining sector is one of the sectors categorized as the top five tax contributors in Indonesia for the year 2016 until 2020.

Tax avoidance is manipulating income to minimize taxes paid through loopholes in the legislation. Basically, tax avoidance is seen as a common practice, which is usually done by companies/entrepreneurs to reduce their tax burden (Masri, 2019). In addition, according to Ichsani and Susanti (2019) also stated that tax avoidance is an effort made to reduce and minimize taxes to be obtained whose actions are legal which can be done through tax management. The case of PT. Adaro Energy is an example of a phenomenon that occurred in the mining industry. From 2009 to 2017, Adaro performed transfer pricing through their Singapore branch company, Coal-Trade Services International. The sales and profit reported to the government are significantly lower than the actual figures. As a result of this action, Adaro was able to reduce their estimated tax liability by 125 million dollars, or 1.75 trillion rupiah (Sugianto, 2019).

The above phenomenon is related to the company's ability to manage assets which can be assessed from the measurement Return on Asset, Leverage, Company Size, Institutional Ownership and Political Connections.

Return on Assets is a profitability ratio that shows the percentage of profit (net income) obtained by the company in relation to overall resources or the average number of assets, the higher the Return on Assets owned by the company, the higher the tax burden paid by the company. Therefore, companies tend to take tax avoidance actions in order to reduce the tax burden that should be paid by the company (Rusmanto et al., 2020). According to the previous research, conducted by Febrianti & Puspita (2017), Ningrum (2017), Fadila (2017), Sanjaya et al (2020), return on asset has significant impact towards tax avoidance.

Leverage is the level of debt used by the company in financing. Leverage describes the level of risk of the company which is measured by comparing the total liabilities of the company with the total assets of the company. Therefore, the greater the level of debt owned by the company, the greater the risk that will be borne. Companies with high leverage risk result in high supervision carried out by debt holders on company activities. Companies that have a high level of leverage have a dependence on external loans to finance their assets. Meanwhile, companies that have a low level of leverage are more likely to finance their assets with their own capital. (Rizki, 2020). According to the previous research, conducted by Krisyandi & Mulfandi (2021), Fadillah (2017), Damayanti & Wulandari (2021), Sanjaya et al (2020), leverage has significant impact towards tax avoidance.

Company size is being calculated based on several factors which are the number of the total assets, the market valuation, and many more. The size of the company also indicated how well it might perform when being faced with problems arise. According to Hery (2017), the larger the company, the more likely it is to increase the value of the company with the assumption that the company is understood by the wider community. According to Putri et al (2019) company size has a meaning, namely a scale that can classify companies in terms of total assets, total sales, number of workers, and others. Investors tend to pay special attention to large companies because they are considered to have more stable conditions and it is easier to obtain internal and external funding sources. Large companies have more resources to increase firm value because they have easier access to external funding sources than small companies. Investors will respond positively to large companies, thereby adding value to large companies. According to the previous research, conducted by Oktamawati (2017), Handayani (2018), Febrianti & Puspita (2017), Fadillah (2017), Sanjaya et al (2020), Priccila & Sinabutar (2020), and Prasetyo et al (2018), company size has significant impact towards tax avoidance.

When it comes to ownership of a company, it can actually be divided into two which are individual ownership and institutional ownership. Arianto (2019) stated that when majority of the company shares is owned by insurance companies, banks, and other institution is called the institutional ownership. In fact, institutional ownership has a lot of effect on one company due to their ability in monitoring corporate management action. Based on the data of Indonesia stock exchange, institutional ownership proportion in Indonesia stock exchange is 73.14%. According to Lusi et al (2019) study, it is shown that there is a relationship between institutional ownership have positive impact towards the earning management of the company. Under the agency theory, institutional company might perform under their own interest to improve the company value which is one of the ways is to lower the tax burden. By maximizing profit and minimize the expenses, shareholders expectation will be achieved. According to Jiang and Zheng (2021), the higher the number of institutional investors, the higher the possibility of company to conduct tax avoidance. According to the previous research, conducted by Damayanti & Wulandari (2021), Fadila (2017), Dewi (2019), Lawita & Putri (2019), institutional ownership has significant impact towards tax avoidance.

According to Gomez & Jomo (2009) in Pranoto & Widagdo (2015), companies that have political connections are companies or conglomerates that have close relations with the government. Companies that have close relations with the government can be interpreted as government-owned companies, namely companies in the form of BUMN or BUMD. Conglomerates (owners) who have close ties to the government are conglomerates or company owners who are prominent political figures. The political figure is a member or former member of the council in the central government or the military. According to the previous research, conducted by Fajri (2020), Maidina & Wati (2020), Lestari & Putri (2017), political connections has significant impact towards tax avoidance

With the above-mentioned phenomenon of tax avoidance in the mining sector, it can be concluded that tax avoidance is still frequently done by companies for their own benefit. Return on asset, leverage, company size, institutional ownership and political connections have all been found to have a significant impact on tax avoidance in previous research. However, the subject is focused on either manufacturing, consumer products, real estate, or the chemical industry. Because of these factors, the writer is motivated to establish if return on asset, leverage, company size, institutional and political connections all play a role in tax avoidance in mining sector. As a result, the writer is encouraged to perform own research under the title of "**The Impact of Return on Asset, Leverage, Company Size, Institutional Ownership, and Political Connections Towards Tax Avoidance in Mining Sector Companies Listed in Indonesia Stock Exchange.**"

1.2 Problem Limitation

The study is limited to:

1. The object of the research is the companies of mining sectors registered in Indonesia Stock Exchange within the time period of 2016-2020.
2. The studies have 5 independent variables and 1 dependent variables. The independent variables are return on asset, leverage, company size, institutional ownership and political connections and the dependent variable is tax avoidance.

1.3 Problem Formulation

The problem being analyzed in this study are:

1. Does return on asset at mining sector companies listed in Indonesia Stock Exchange have significant impact on tax avoidance?
2. Does leverage at mining sector companies listed in Indonesia Stock Exchange have significant impact on tax avoidance?
3. Does company size at mining sector companies listed in Indonesia Stock Exchange have significant impact on tax avoidance?
4. Does institutional ownership at mining sector companies listed in Indonesia Stock Exchange have significant impact on tax avoidance?
5. Do political connections at mining sector companies listed in Indonesia Stock Exchange have significant impact on tax avoidance?

6. Do return on asset, leverage, company size, institutional ownership and political connections simultaneously at mining sector companies listed in Indonesia Stock Exchange have significant impact on tax avoidance?

1.4 Objective of The Research

The objective of the research is to have greater understanding on the propose problem formulation. The objectives are:

1. To examine whether return on asset has significant impact on tax avoidance at mining companies listed in Indonesia Stock Exchange.
2. To examine whether leverage has significant impact on tax avoidance at mining companies listed in Indonesia Stock Exchange.
3. To examine whether company size has significant impact on tax avoidance at mining companies listed in Indonesia Stock Exchange.
4. To examine whether institutional ownership has significant impact on tax avoidance at mining companies listed in Indonesia Stock Exchange.
5. To examine whether political connections has significant impact on tax avoidance at mining companies listed in Indonesia Stock Exchange.
6. To examine whether return on asset, leverage, company size, institutional ownership and political connections simultaneously have significant impact on tax avoidance at mining sector companies listed in Indonesia Stock Exchange.

1.5 Benefits of The Research

This research is expected to bring benefits in term of theoretical and also practical benefits.

1.5.1 Theoretical Benefit

In terms of theoretical, the benefits are:

1. From the writer perspective, this research is done to improve the understanding of how significant the impact of return on asset, leverage, company size, institutional ownership and political connections toward tax avoidance.
2. For the company, this research will provide reference and knowledge about the significance of return on asset, leverage, company size, institutional ownership and political connections toward tax avoidance.
3. For the investors, this research is expected to be use as consideration material before investing into a company in order to avoid investors being aggrieved by company management.
4. For the government, this research is expected to give insights to the regulators in making tax and hence, the potential of tax revenue can be maximized.

1.5.2 Practical Benefit

As from the practical perspectives, the benefits are:

1. Providing an overview about the implementation of return on asset, leverage, company size, institutional ownership and political connections and the impact of tax avoidance in mining companies listed in Indonesia Stock Exchange.
2. Providing insights to all mining companies listed in Indonesia Stock Exchange about the importance of fulfilling their tax obligations and the benefits it will bring to the government.
3. Used as future research reference material and hopefully the result of this research may serve as guidance and additional information related to the subject and variables used.