CHAPTER I

INTRODUCTION

1.1. Background of The Study

Indonesia is a developing country with a large population, making potential to meet its country growth targets. Efforts to meet these targets will require substantial funds, so taxes are a source of state funds. In a country, taxes have an essential role in improving the country's economy and also contribute to the state budget. Tax is obliged both upon individuals and companies. The taxes paid by the public will become state income. The proceeds from tax collection can build infrastructure and pay off the state's debt. For the community, this tax is a burden that reduces the amount of income or profits they receive, and there is evidence that taxpayers evade it in order to reduce their tax bills.

Most taxpayers, either individuals or entities, believe that tax is a burden that adds to the costs of doing business. In Indonesia, the current tax system is a self-assessment system that triggers a company to do tax avoidance to minimize costs and attract investors. Companies will try to figure out how to make tax savings legal and reasonable. Usually, this is done by the company to cut the burden. Based on this, it is often the case that companies engage in tax avoidance.

Collecting taxes is not an easy task to do. Taxation must be considered by companies because taxes are seen as a burden that can threaten the sustainability of the company. According to Rahmawati et al. (2018), tax avoidance is an action to maximize after-tax income. Tax avoidance is a legal way to reduce taxes because they do not violate existing regulations, only to take advantage of existing tax law loopholes. According to Income Tax Law Number 36 Year 2008, Article 6 stated that interest expense is categorized as deductible expense. Most companies use debt for tax avoidance to decrease tax payment. Tax avoidance is the deliberate behavior of a company to minimize the amount of tax payments required while simultaneously increasing the cash flow of the business.

In Indonesia, one of the tax avoidance cases involves PT Adaro Energy Tbk (ADRO). Sugianto (2019) reported that Indonesia's largest mining company committed tax avoidance by conducting transfer pricing, which was distributed to its Singapore subsidiary, Coaltrade Services International. This action was carried out between 2009 and 2017. As a result of this action, it avoided paying 1.75 trillion rupiahs based on tax regulation in Indonesia. By exploiting the loophole, the company sells its coal products to Coaltrade Services International at lower price, and then resells them to other countries at inflated prices. ADRO benefits from the taxation of excess profits being shifted from one country to another that has a lower tax rate (tax haven). ADRO takes advantage from the fact that tax in Singapore is lower than Indonesia's. Indonesia levies a 25% tax, while Singapore levies only a 17%. Expenses are transferred by manipulating prices in an unreasonable manner. Thus, this taxable income in Indonesia is significantly lower, and this action is considered tax avoidance by exploiting existing loopholes, but it is unethical.

Many factors can influence tax avoidance, especially internal factors, because basically, tax avoidance occurs based on the company's desire, which expects the maximum profit. Tax avoidance can be achieved by reducing the tax burden as much as possible. The first factor that can influence tax avoidance activity is profitability. Profitability represents the company's capacity to generate revenue. The calculation of the profitability ratio measurement uses the Return on Assets (ROA) indicator. ROA interprets the ratio to determine how much net income earned from its assets. When ROA is high, the tax burden is likely high. This can encourage a company to conduct tax avoidance to reduce its tax burden.

Besides profitability, the writer also uses sales growth and leverage as the second and third factors affecting tax avoidance activities. Sales growth has a significant influence that can impact sales made by the company. Normally, if sales increase, assets will also increase (Dewinta & Setiawan, 2016). So the writer uses the measurement of sales growth in this study because it can determine whether the company's sales growth rate is good or bad. Therefore, company profits can be predicted from the size of sales growth. Increased sales growth tends to make companies want to practice tax avoidance. Sales growth can be determined by subtracting the current year's sales from those of the previous year and dividing the result by the prior year's sales.

According to Sonia and Suparmun (2019), when a company has a high degree of debt concerning its financing policies, this is referred to as leverage. The Debt to Assets Ratio (DAR) is a debt ratio that determines the ratio of total debt to total assets. In other words, the debt is used to acquire company's assets (Andhani, 2019). By dividing the total debt owed by a company by its total assets, leverage can be determined. A high level of leverage indicates that a company is heavily dependent on debt. The existence of debt will result in a fixed cost, known as interest. The greater a company's relying on debt, the greater their debt burden. The greater the company's debt, the lower its tax burden.

In addition to avoiding tax by using loopholes in the law, companies can take advantage of providing allowance as the replacement of benefits-in-kind to reduce taxes. Benefits-in-kind is a form of reward or other facilities usually given by the company to employees. Benefits-in-kind is not in the form of money, but in goods, based on the Circular Letter of the Director General of Taxes No SE-03/PJ.23/1984 (Cristin, 2021). For example, with incentives in the form of giving in kind and enjoyment to employees who are diligent and work hard. However, since natura is not a tax object for employees and then for a natura company, it is not a deductible expense to reduce gross income. The company replaces it by providing allowances, so that it is deductible. In addition, through providing employees with shuttle transportation facilities, company can have deductible expenses from the depreciation of company bus, its maintenance costs, routine repairs, fuel, and insurance (Gresia, 2021). Even though it is legal for the company to do, its income tax is lower than it should be owed.

This research uses the basic industry and chemical companies as objects. Based on tax revenue data published by Hartarto (2018) in Kemenperin website, the industrial sector contributed the largest portion to total tax revenue of 30% in 2018. Basic industry and chemical include changes in raw organic and non-organic materials with chemical processes and product formation. The final product is intended to increase the growth of domestic and international trade in supporting development in manufacturing, agriculture, infrastructure, and real estate. The basic industry and chemical sectors have a role in the country's economic growth.

According to DDTC News (2019), the government has failed to achieve the tax revenue target from 2017 to 2019. In 2017, tax revenues could only collect IDR 1.283,57 trillion or 89.67% of the target set at IDR 1.151,03 trillion. Meanwhile, in 2018 and 2019, the government managed to collect 92.23% and 84.44% of the set targets.

Table 1.1 Profitability (ROA), Sales Growth, Leverage (DAR) and Tax Avoidance (ETR) of PT Semen Indonesia Tbk., PT Wijaya Karya Beton Tbk., PT Indocement Tunggal Prakarsa Tbk. for Year 2017-2019

Company Name	Year	Profitability (ROA)	Sales Growth	Leverage (DAR)	Tax Avoidance (ETR)
PT Semen Indonesia Tbk. (SMGR)	2017	3.36%	6.43%	38.77%	26.79%
	2018	6.03%	10.33%	36.01%	24.83%
	2019	2.97%	31.55%	55.03%	25.80%
PT Wijaya Karya Beton Tbk. (WTON)	2017	4.82%	54.01%	61.12%	18.84%
	2018	5.48%	29.25%	64.68%	21.41%
	2019	4.94%	2.20%	66.06%	18.45%
PT Indocement Tunggal Prakarsa Tbk. (INTP)	2017	6.44%	-6.06%	14.92%	18.69%
	2018	4.12%	5.26%	16.43%	18.16%
	2019	6.62%	4.93%	16.70%	19.31%

Source: Prepared by the writer (2022)

Based on Table 1.1, the profitability ratio of PT Semen Indonesia Tbk (SMGR) from 2017 to 2019 showed inconsistent movements. The profitability ratio increased from 2017 to 2018 due to an increase in net income by 87% as the impact of decrease in depreciation expenses. This increase was mainly due to the increase in the company's operational activities, namely the increase in revenue from the sale of cement in order to meet customer demand. The increase in profits encourages companies to avoid taxes because they are trying to get maximum profit. Table 1.1 shows that the profitability factor has a positive influence on tax avoidance. In other words, the higher the company's profitability, the lower tax payment by the company it shows from the decreasing percentage of ETR. Research conducted by Sonia and Suparmun (2019) explained that Profitability (ROA) has a significant negative influence on tax avoidance. According to Irianto et al. (2017), the result of the research showed the same result as Sonia and Suparmun (2018) that ROA has a negative influence on tax avoidance. Meanwhile, Kim (2017) stated that ROA has a positive effect on tax avoidance. This result shows that every researcher has different results.

Sonia and Suparmun (2019) research stated that sales growth does not affect tax avoidance. Meanwhile, according to Kim (2017), sales growth positively affects tax avoidance, because when a company’s sales increase, it will become more active in tax avoidance to reduce cash outflow from the growing sales. However, based on Table 1.1, PT Wijaya Karya Beton Tbk (WTON), sales growth from 2017 to 2018 decreased due to lower infrastructure projects obtained and an increasing percentage of ETR. From the results of these phenomena, the lower the sales growth, the lower the tax avoidance implemented. If sales growth is higher, the company will be able to generate more profits along with increased sales. High profits result in high tax rates that the government must collect. As a result, sales growth will indicate that the company is trying to avoid paying taxes. This shows a positive influence on tax avoidance. According to previous researchers on sales growth toward tax avoidance, the relationship between sales growth and tax avoidance does not have a solid outcome because each source presents different results.

Leverage is the amount of debt a company uses to finance its operations. Leverage benefits the company that use liabilities as a central focus, as it results in the emergence of interest debt, which can helps the company reduce its tax liability. According to the results of the table above, PT Indocement Tunggal Prakarsa Tbk, the DAR ratio increased from 2017 to 2018, while the ETR ratio decreased. In 2018, DAR increased due to an increase in liabilities. Debt is used by companies to fund operations and capital expenditures. Debt involves a fixed expense known as interest. The interest expense incurred by the company can be deducted from its taxable income, by reducing the company's tax liability. Thus, the higher the leverage ratio reflects greater reliance on debt financing from third parties and the greater interest expenses associated with that debt. The increase in interest expenses will reduce the corporation's tax liability. This demonstrates that leverage has a substantial positive effect on tax avoidance, as high levels of debt increase interest expenses, allowing businesses to avoid taxes. Based on the previous research, the results of leverage toward tax avoidance are various. Kim (2017) stated that leverage has a significant positive effect on tax avoidance, whereas Sonia and Suparmun (2019) showed no effect on tax avoidance. On the other hand, Irianto et al. (2017) mentioned that leverage has negative and no significant influence on tax avoidance. Even though a company has debts, they are obliged to pay taxes because taxes are an obligation. Therefore, from the problem above, there is a question about the impact of leverage on tax avoidance.

There are various results in previous research that encourage the writer interested in researching further. Therefore, the writer conducted a research on the basic industry and chemicals companies listed on the Indonesia Stock Exchange and chose **"The Influence of Profitability, Sales Growth and Leverage Toward Tax Avoidance In Basic Industry and Chemicals Companies Listed On The Indonesia Stock Exchange"** as the research title for the final paper.

1.2. Problem Limitation

There is a limitation for the writer to research due to the limitation of time and capability of the writer. The research focuses on basic industry and chemicals companies for the year 2017 – 2019. The main objective of this research is to analyze the influence of profitability, sales growth, and leverage that affect tax avoidance. The writer uses the company annual report year 2017 to 2019 for the research.

In Basic Industry and Chemicals Sector have 83 companies that are listed on the Indonesia Stock Exchange. The independent variables in this research are profitability, sales growth, and leverage. The indicator used by the writer for the independent variable is the financial ratio. The independent variable is Profitability (ROA), Sales Growth, and Leverage (DAR), while the dependent variable is Tax Avoidance (ETR).

1.3. Problem Formulation

Background of the problem that is used on this research as the problem formulations is:

1. Does profitability have an impact towards tax avoidance in basic industry and chemicals companies listed at Indonesia Stock Exchange partially?
2. Does sales growth have an impact on towards tax avoidance in basic industry and chemicals companies listed at Indonesia Stock Exchange partially?
3. Does leverage has an impact towards tax avoidance in basic industry and chemicals companies listed at Indonesia Stock Exchange partially?
4. Do profitability, sales growth and leverage have a impact towards tax avoidance in basic industry and chemicals companies listed at Indonesia Stock Exchange simultaneously?

1.4. Research Object

Purpose of this study is to determine the influence of basic industry and chemicals companies' profitability, sales growth, and leverage on tax avoidance. The following are the specific research objectives:

1. To analyze whether there is a positive or negative effect of profitability toward tax avoidance in Basic Industry and Chemicals company that are listed on The Indonesia Stock Exchange.

2. To analyze wheter there is a positive or negative effect of sales growth toward tax avoidance in Basic Industry and Chemicals company that are listed on The Indonesia Stock Exchange.
3. To analyze wheter there is a positive or negative effect of leverage toward tax avoidance in Basic Industry and Chemicals company that are listed on The Indonesia Stock Exchange.
4. To analyze wheter there is simultaneously effect of profitability, sales growth and leverage toward tax avoidance in Basic Industry and Chemicals company that are listed on The Indonesia Stock Exchange.

1.5. Benefit of The Research

The writer expects the result can give benefits. The benefits of doing this research are as follows:

1.5.1 Theoretical Benefits

The results of this research, the writer hope, can provide insight and knowledge about profitability, sales growth, and leverage on tax avoidance in basic industry and chemicals companies listed on the Indonesia Stock Exchange. This research is expected to be a reference for future researchers, especially in accounting related to the title.

1.5.2 Practical Benefits

1. For Academics

   This research can give knowledge and information as a literature study material and increase research at Pelita Harapan University, especially the accounting study program

2. For Future Researchers

   This research result will give information about the factors that effect on tax avoidance. From this research, it can be a references for future researchers.

3. For Company

   The research result can give information to the company about tax avoidance and can be a a benchmark for companies to make wise decisions in avoiding tax without harming their country.