

CHAPTER I

INTRODUCTION

1.1 Background of the Study

In this day and age, there rarely is a country that does not implement the taxation system to run the country, as it acts as an essential key in running things smoothly, moreover, they also become a country's source of income to finance projects and developments to enhance the people's quality of life. Therefore, the implementation of collecting taxes should be systemized in a way where it has been approved by the people represented by the representative council, by establishing regulations where it will serve as the purpose of becoming the reason for implementing the taxation system. Individuals and corporates alike are obligated to pay the taxes that have been imposed on them by the government, they are also known as taxpayers. The tax collection system in Indonesia that is based on the regulations is the Self-Assessment System, where all tax obligations will be fully done by the taxpayers, whereas the tax authorities will do surveillance through the checking procedure (Gultom, 2021).

As taxpayers want to generate as much profit as they can, they would also minimize the expenditures as much as possible, one of those expenditures are tax burdens, and in order to do so, methods where the taxpayers may try in order to decrease the expected tax amount came to fruition, among those is known to be tax avoidance. Tax avoidance is defined as the interferences that occur during the process of collecting taxes which in turn result in the decrease in the country's cash

receipts, tax avoidance is also known as a legal method that taxpayers may take to avoid taxes (Mahdiana & Amin, 2020). As it can be seen as a means to decrease the amount of tax burden, tax evasion can also be seen in the same way. However, the latter is defined as the practice being done by taxpayers by using unlawful means to decrease or to eliminate tax burden (Darmayanti & Merkusyawati, 2019).

The matter of tax avoidance and the taxation system can be deemed as peculiar as taxpayers will try any means possible to decrease the amount of tax burden, hence came the fruition of the practice of tax avoidance. Whereas the government relies on the taxation system as it is their biggest source of income for the purpose of financing developments all over the country.

There are several factors that may affect firms and corporations alike in attempting their hand at the practice of tax avoidance, this research analyses the following factors, which are profitability, leverage, and firm size. The definition of profitability is a company's capability in generating profit, the calculation of profitability can be done with Return on Asset (ROA). The higher the profitability of a company, the bigger the likelihood of the company to make attempts for the purpose of generating the optimal tax by minimizing tax burden, which in turn, the bigger the possibility of the company to attempt the practice of tax avoidance (Nugrahitha & Suprasto, 2018).

Other than profitability, leverage is one of the factors being discussed in this research that might cause a corporation's decision in practicing tax avoidance. The terminology of leverage can be understood as the ratio of a company's debt that is being used for financing activities and operations (Nugrahitha & Suprasto, 2018).

The higher the amount of a corporation's debt then the lower the likelihood for a corporation to practice the methods of tax avoidance (Dewi & Noviari, 2017).

Another factor that could possibly influence a company to practice tax avoidance is firm size. Among the ways of assessing firm size is by calculating the total of the asset owned by a firm. Firms with big number of assets are likelier to generate huge amount of profit, which in turn causes the amount of tax needed to be paid to be bigger as well (Darmayanti & Merkusiwati, 2019).

Table 1.1 Table of Phenomena

Company	Year	ROA	DER	Firm Size	CETR
PT. Adaro Energy Indonesia Tbk	2017	0.078	0.665	32	0.562
	2018	0.067	0.641	32	0.505
	2019	0.062	0.811	32	0.479
	2020	0.024	0.614	32	0.846
PT. Baramulti Suksessarana Tbk	2017	0.394	0.401	29	0.221
	2018	0.281	0.639	29	0.423
	2019	0.268	0.471	28	0.605
	2020	0.256	0.383	28	0.173
PT. Indo Tambagraya Megah Tbk	2017	0.185	0.418	31	0.164
	2018	0.179	0.487	31	0.297
	2019	0.104	0.369	30	0.598
	2020	0.032	0.369	30	0.864
PT. Bukit Asam Tbk	2017	0.206	0.593	31	0.183
	2018	0.211	0.485	31	0.307
	2019	0.153	0.416	31	0.281
	2020	0.1	0.42	31	0.217

Source: Prepared by Writer (2022)

As depicted in table 1.1, the writer has taken four mining companies as representatives to be examined and discussed. As this research uses profitability, leverage, and firm size as variables to discover whether or not they have an effect on tax avoidance, their ratios are shown on the table as well. The four companies taken as representatives are PT. Adaro Energy Indonesia Tbk, PT. Baramulti Suksessarana Tbk, PT. Indo Tambagraya Megah Tbk, and PT. Bukit Asam Tbk.

As profitability might determine the probability of a company in practicing tax avoidance, this research calculates and measures the profitability ratio with

return on assets. Taking PT. Adaro Energy Indonesia Tbk as an observation, where its ratio of profitability experiences a drastic downfall from the year 2019 to 2020, this is due to the fact that there is a decline in the company's sales for the year 2020. In theory, when there's an increase in a company's profitability, the likelihood for a company to practice tax avoidance will increase as well, this is due to the fact that the more profit a company earns, the more amount of tax will be imposed on the company. Study done by Dewi and Noviari (2017) proved that profitability has a positive influence toward tax avoidance, which contradicts the study done by Fauziah and Kurnia (2021) which resulted in profitability having negative effect toward tax avoidance.

Leverage serves as an indicator of a company's usage in liabilities as funds to finance its operations and activities. As observed from the table shown above, the leverage ratio of the company PT. Baramulti Suksessarana Tbk experiences a spike from the year 2017 to 2018, this is due to the fact that there's an increase in the short-term and long-term debt of the company gained from PT. Bank CIMB Niaga Tbk and ICICI Bank Limited. When a company loans from a bank, there is bound to be an interest expense from the said bank loans. Hence, with the appearance of the interest expense account, it will also deduct the profit earned by the company and as a result will decrease the amount of tax imposed on the company. Research carried out by Nugrahitha and Suprasto (2018) showed results where leverage has a positive effect toward tax avoidance, contradicting the results of a research done by Robin et al., (2021) that showed leverage having a negative effect toward tax avoidance.

The last independent variable as shown on the table is firm size, as observed from the table, the firm size of PT. Indo Tambangraya Megah Tbk from the period 2018 to 2019 has declined, as the current assets as well as the non-current assets have decreased in the following year. When there's an increase or decrease in the assets, the amount of depreciation will be affected as well. Which in turn will result in the fluctuation in the amount of expenses that the company has to bear, this also means that the amount of taxes being imposed on the companies will be affected as well. Study done by Fauziah and Kurnia (2021) indicated that firm size has a positive effect toward tax avoidance. On the other hand, study done by Dewi and Noviani (2021) indicated that firm size has a negative effect toward tax avoidance.

In a case dating back to 2019, PT. Adaro Energy Indonesia Tbk which is also known to be is suspected to be practicing tax avoidance, the practice also known as transfer pricing through its subsidiary in Singapore, called the Coaltrade Services International. Where the company allegedly to have done in such a way so that they were able to pay taxes of Rp 1,75 trillion less than they should have paid in Indonesia. Supposedly, the company took advantage of the loophole by selling coal to Coaltrade Services International at a cheaper price, where the coal is then sold to other countries with prices that were higher than it was sold. Therefore, the tax income that has been imposed on the company in Indonesia would be cheaper as well. Although this method, also known as transfer pricing does not violate the laws, it is still considered to be unethical. As it is using the resources in Indonesia, however the amount of tax receipts received by Indonesia itself is not maximal, rather that profit is earned by other country with a lower tax rate (Sugianto, 2019).

As Indonesia is known to have resourceful lands, where it is known to be beneficial to the mining industry and it is no secret that the mining industry serves as one of Indonesia's significant income contributors, hence it is imperative that the mining companies should pay the appropriate amount of taxes to ensure that the economy in a country is running well. Based on the information shown on the table of phenomena and theories found above, the writer wishes to find out more whether or not the variables of this research have an impact toward tax avoidance on the mining companies listed on the Indonesia Stock Exchange, where the title of this paper would be **“The Effect of Profitability, Leverage and Firm Size Toward Tax Avoidance on Mining Companies Listed on the Indonesia Stock Exchange”**.

1.2 Problem Limitation

In consideration of the fact that time and resources are limited, the scope of this research will be limited to the variables of profitability, leverage, and firm size. Focusing on its effects toward tax avoidance on the mining companies as listed on the Indonesia Stock Exchange. The data being used for this research has been limited to the financial statements of the mining companies listed on the Indonesia Stock Exchange with the time period ranging from 2017 to 2020. The reason being that with a clear view of the variables and a specific time period, the writer and the reader will have a clear understanding of this research, Hence, the determinants that have been decided by the writer are limited to profitability, leverage, and firm size

of which serve as the independent variables and tax avoidance will be serving as a dependent variable.

1.3 Problem Formulation

As per mentioned in the background of the study being discussed beforehand as its basis, the problem formulations that the writer has chosen are as follows:

1. Could profitability have a significant effect toward tax avoidance on the mining sector listed on the Indonesia Stock Exchange?
2. Could leverage have a significant effect toward tax avoidance on the mining sector listed on the Indonesia Stock Exchange?
3. Could firm size have a significant effect toward tax avoidance on the mining sector listed on the Indonesia Stock Exchange?
4. Is there a simultaneous effect that profitability, leverage, and firm size have toward tax avoidance on the mining sector listed on the Indonesia Stock Exchange?

1.4 Objectives of the Research

After preparing the problem formulations as listed above, the objectives that are surmised to be met by conducting this research are as follows:

1. To find out and analyse whether there is a significant effect that profitability has toward tax avoidance on the mining companies listed on the Indonesia Stock Exchange.

2. To find out and analyse whether there is a significant effect that leverage has toward tax avoidance on the mining companies listed on the Indonesia Stock Exchange.
3. To find out and analyse whether there is a significant effect that firm size has toward tax avoidance on the mining companies listed on the Indonesia Stock Exchange.
4. To find out and analyse whether there is a simultaneous effect that profitability, leverage, and firm size simultaneously have toward tax avoidance on the mining companies listed on the Indonesia Stock Exchange.

1.5 Benefit of the Research

The benefits of this research are classified into two, which are as follows:

1.5.1 Theoretical Benefit

1. This research is expected to be utilized as a source of information for the future research being conducted on similar topics.
2. This research is expected to give an in-depth knowledge on the topics being discussed in the paper.

1.5.2 Practical Benefit

1. Mining companies can use this research as a guidance to help them make decisions relating to the topics that are being discussed and analysed in this research.

2. With this research, the writer hopes to give the readers a means to pay taxes with less than the amount that they could have with tax avoidance, and to avoid illegal methods such as tax evasion.

