# CHAPTER I

# INTRODUCTION

## 1.1 Background of the Study

Indonesia is a legal state founded on Pancasila and the Republic of Indonesian Constitution of 1945. As there is no law without a society, the existence of a law is due to the emergence of a society. According to the fourth paragraph of the Preamble to the Republic of Indonesia's 1945 Constitution, the state has an obligation to promote public welfare. State revenue is an important component of the tax sector that can be used to fund state expenditures and achieve state goals. To keep people safe, laws must be enforced in society. The legal basis for collecting taxes is constrained in Article 23A of the Republic of Indonesia's 1945 Constitution, which clearly states that taxes and other levies are coercive in nature for the requirements of the State and are regulated by law, while the meaning of tax is regulated in Article 1 point 1 of Law No. 28 of 2007 regarding the third amendment to Law Number 6 of 1983, which explains that taxes are obligations owed by individuals or businesses to the State. Researchers discovered a gap in the tax regulations during the enactment of the Taxation Law that warrants attention since it is related to tax avoidance (Michael, 2016).

According to Moeljono (2020), tax avoidance is an attempt to avoid a tax that is carried out legally and securely for taxpayers since it does not conflict with taxation regulations, where the strategies and tactics used tend to reap the benefits of weaknesses stipulated in the law and the tax legislation itself to decrease the amount of tax payable. Tax avoidance is one of the strategies for lowering the tax burden that is frequently carried out by the company, since it remains within the framework of the applicable tax regulations. Even though tax evasion is legal, the government does not approve. The ratio Indonesia's tax ratio demonstrates the occurrence of tax avoidance in Indonesia. The tax ratio demonstrates the government's capability to collect tax revenue or absorb GDP from society through taxation. The higher a country's tax ratio, the better its tax collection results.

Tax avoidance in its broadest terms refers to any arrangement to minimize, eliminate, or postpone a tax liability. According to a report issued by the Oxford Business Tax Centre for the National Audit Office, there are three types of legal tax avoidance: ineffective avoidance means current legislation can be used to counteract; effective tax avoidance means that cannot be rectified through the courts and necessitates legislative change; and utilizing tax legislation to one's obvious benefit, such as effectively utilizing opportunities to lower tax that are offered for in tax legislation, also known as tax reliefs or tax concessions. As defined by the United Nations Committee of Experts on International Cooperation in Tax Matters, tax avoidance arises when individuals organise their affairs in such a way that they reap the benefits of legal flaws or ambiguities. Even though the methods used are legal and not fraudulent, the outcomes are deemed inappropriate or abusive (Oats & Tuck, 2019).

The Indonesian economy is presently dealing with the COVID-19 pandemic, which influences all aspects of the economy, particularly taxes that affect state revenues. Since several tax instruments are primarily used to handle COVID-19, this circumstance has an influence on the decrease in tax rate receipts so that this study finds that the goal of tax revenue has not been achieved for five years. Corporate income tax and import taxes of varying sorts involve income tax article 22 imports, income tax article 22 exports, value added tax (VAT) imports, and sales tax on luxury goods. As a result, thus according to state budget data, several of these tax instruments contracted by 24.02% compared to the corresponding time the previous year (*APBN*). According to data from the State Revenue and Expenditure Budget (*APBN*), the tax revenue objective for 2020 is IDR 1,198.82 trillion, but tax revenue accomplishment has only reached IDR 750.62 trillion, or 62.61% of the target that has been set, as of the end of September 2020. The decline in economic conditions created by the COVID-19 pandemic has impacted tax revenue effectiveness, causing the amount of economic output to fall short of its potential output (Maulani et al., n.d.). Based on data from CNBC Indonesia's R&D which shows the revenue target and realization for the last five years in Table 1.1 below:

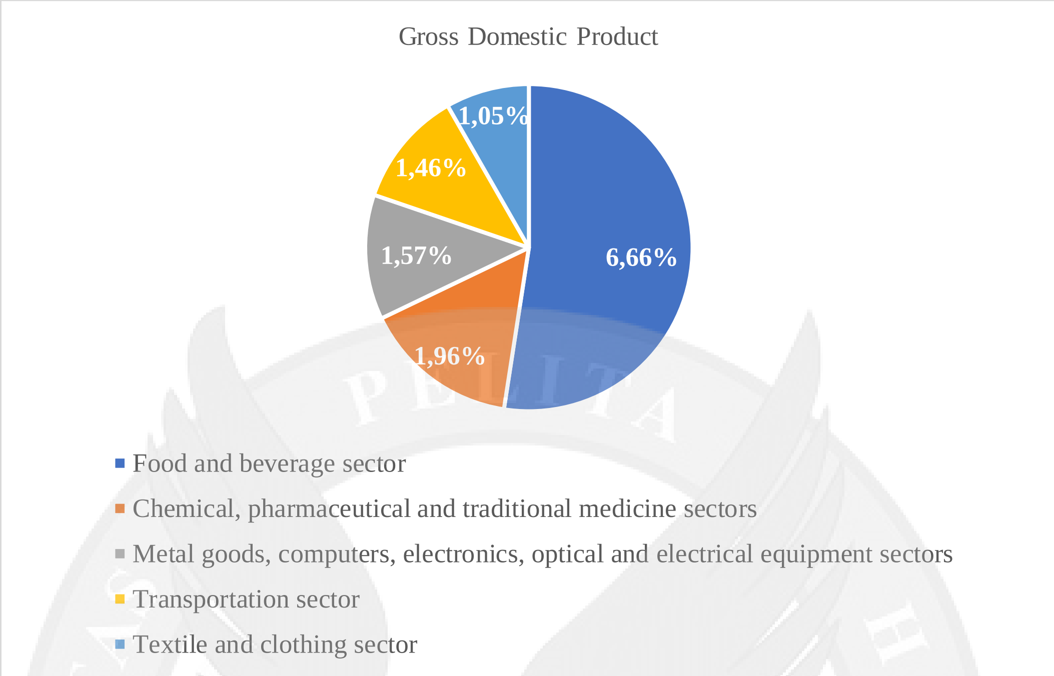
**Table 1.1 CNBC Indonesia Research and Development Data Target and Realization of Tax Revenue for the Last Five Years**

| | **2016** | **2017** | **2018** | **2019** | **2020** |
|---|---|---|---|---|---|
| **Target** | 1.539,1 | 1.283 | 1.424 | 1.577,6 | 1.198,8 |
| **Realization** | 1.283 | 1.147 | 1.315 | 1.332,1 | 1.069,5 |

Source: prepared by the writer adopted from Cnbcindonesia (2021)

Based on the Table 1.1 above indicate that the recognition of tax revenue falls short of the goal. Tax avoidance by the corporation is the factor that can contribute to the corporation failing to meet its tax revenue targets (Sembiring, 2021).

**Figure 1.1 Gross Domestic Product of Manufacturing Industry in 2021**




Source prepared by the writer adopted from Kemenperin (2022)

According to Figure 1.1 shows the food and beverage sub-sector contributes the most to GDP, accounting for 6.66%. Since the food and beverage sub-sector is classified in the consumer goods industry and the consumer goods industry is included in one of the main sectors in manufacturing companies, it is critical for the nation's economic growth, which will have a beneficial influence on increasing investment (Kemenperin, 2021).

Cash Effective Tax Rate (CETR) is the measurement chosen in order to measure tax avoidance. The purpose of the Cash Effective Tax Rate (CETR) is to accommodate the present level of cash taxation paid by the organization. The Cash Effective Tax Rate (CETR) is calculated by dividing the amount of cash tax paid by the total profit before tax. CETR stands for the cash effective tax rate calculated utilizing firm’s cash taxes paid in the recent year. The writer chose Cash Effective Tax Rate as tax avoidance measurement because customer goods industry is producing people’s primary needs, when in the operations of the company, there is cash position that becomes the important part. CETR is used because it has a function for analyzing the cash flow of tax payments and the amount of cash spent by the company (Alkausar, 2021).

The above phenomenon is referred to the corporation's capability to arrange assets that can be evaluated from leverage and capital intensity. Leverage is a funding rule that is associated to the company's decision to finance itself. Companies that use debt must pay interest and principal costs. Leverage demonstrates the company's ability to fulfil financial responsibilities both during the short and long term. Leverage will have an impact on a company’s cost due to the fact excessive leverage indicates a higher risk of investment. The use of debt in external financing carries a significant risk of non-payment of debt, the usage of debt must consider the company’s capability to raise profits (Ngadiman & Puspitasari, 2014). The research conducted by (Ulfa et al., 2017), showed that leverage has significant effect on tax avoidance. However, from the research that has been carried out by (Rifai et al., 2019), leverage has no effect on tax avoidance.

Capital Intensity refers to the amount that a company decides to invest in fixed assets and inventories. Increased fixed assets in the company will have an effect on productivity improvements, which can result in higher profits. Companies that invest in fixed assets can assist them avoid taxes since the depreciation of fixed assets diminishes taxes each year. Capital intensity is estimated by dividing fixed assets by sales. Capital Intensity has a positive effect on tax avoidance according to (Budianti & Curry, 2018a). Profitability refers to a company's capability to raise profits while also measuring operational efficiency and asset utilization (Rifai et al., 2019). Profitability can influence the relationship between leverage, and capital intensiveness and tax avoidance. Researcher of (Nguyen et al., 2019) stated that profitability does not a significant effect on financial leverage. Then, researcher that held by Nangih Efeeloo & Onuora stated that capital intensity has a significant effect on profitability (Nangih & Onuora, 2020).

Thus, based on the description and explanation above, the author is interested in making a thesis entitled **"The Impact of Leverage and Capital Intensity on Tax Avoidance through Profitability in Consumer Goods Industry Listed on Indonesia Stock Exchange". (**Empirical study of consumer goods industry in manufacturing companies listed on the Indonesia Stock Exchange in 2019-2021)

## 1.2 Problem Limitation

The author state several following of the research limitations:

1. The object of the research are companies in consumer goods industry that listed on Indonesia Stock Exchange
2. The research data is from financial statements of the company in 2019-2021
3. Leverage and capital intensity are the independent variables; profitability is the intervening variable; and tax avoidance is the dependent variable.

## 1.3 Problem Formulation

There are some formulations of the problem will be executed by researchers, as follows:

1. Does leverage have a significant impact on profitability in consumer goods industry listed on Indonesia Stock Exchange?
2. Does leverage have a significant impact on tax avoidance in consumer goods industry listed on Indonesia Stock Exchange?
3. Does capital intensity have a significant impact on profitability in consumer goods industry listed on Indonesia Stock Exchange?
4. Does capital intensity have a significant impact on tax avoidance in consumer goods industry listed on Indonesia Stock Exchange?
5. Does leverage have a significant impact on the tax avoidance through profitability in consumer goods industry listed on Indonesia Stock Exchange?
6. Does capital intensity have a significant impact on the tax avoidance through profitability in consumer goods industry listed on Indonesia Stock Exchange?
7. Does profitability have a significant impact on tax avoidance in consumer goods industry listed on Indonesia Stock Exchange?
8. Does leverage and capital intensity simultaneously have a significant impact on profitability in consumer goods industry listed on Indonesia Stock Exchange?

9. Does leverage, capital intensity, and profitability simultaneously have a significant impact on tax avoidance in consumer goods industry listed on Indonesia Stock Exchange?

## 1.4 Objective of the Research

The research objective is stipulated by organizing the studying occurring effective ways. The research objectives are as follows:

1. To find out whether leverage has a significant impact on profitability in consumer goods industry listed on Indonesia Stock Exchange.
2. To find out whether leverage has a significant impact on tax avoidance in consumer goods industry listed on Indonesia Stock Exchange.
3. To find out whether capital intensity has a significant impact on profitability in consumer goods industry listed on Indonesia Stock Exchange.
4. To find out whether capital intensity has a positive and significant impact on tax avoidance in consumer goods industry listed on Indonesia Stock Exchange.
5. To find out whether leverage has a significant impact on the tax avoidance through profitability in consumer goods industry listed on Indonesia Stock Exchange.
6. To find out whether capital intensity has a significant impact on the tax avoidance through profitability in consumer goods industry listed on Indonesia Stock Exchange.

7. To find out whether profitability has a significant impact on tax avoidance in consumer goods industry listed on Indonesia Stock Exchange.
8. To find out whether leverage and capital intensity simultaneously have a significant impact on profitability in consumer goods industry listed on Indonesia Stock Exchange.
9. To find out whether leverage, capital intensity, and profitability simultaneously have a significant impact on tax avoidance in consumer goods industry listed on Indonesia Stock Exchange.

## 1.5 Benefit of the Research

The study is expected to help research can provide theoretical and practical benefit as follows:

### 1.5.1 Theoretical Benefit

It is hoped by doing the research could make readers and author have the capability to present more information, experience, and reference regarding The Impact of Leverage and Capital Intensify, also the way Profitability moderates them on Tax Avoidance in Consumer Goods Industry listed on Indonesia Stock Exchange for future research.

### 1.5.2 Practical Benefit

The followings are the important practical that research assumed to have on the objective of the research:

1. For Researchers

   This study is aiming to obtain more knowledge regarding the impact of leverage, and capital intensify on tax avoidance through profitability in consumer goods industry listed on Indonesia Stock Exchange.

2. For Investors

   It is intended beneficial for investors in order to invest in the companies that listed on Indonesia Stock Exchange in the future.

3. For Government

   It is intended beneficial for government in Indonesia cause it help government set up the companies that take part in tax avoidance also assist to expand the regulations to minimize feral tax avoidance.

4. For companies

   It is hoped to offer more encouragement and knowing about the problems which might affect tax avoidance in a company.