CHAPTER I
INTRODUCTION

1.1 Background of the Study

Taxes are the largest source of funding for the Indonesian state. Taxes have become the largest source of funding accounting for around 70% of total government revenue (Savitri, 2017). Individual and business taxpayers are the primary sources of taxation in Indonesia.

According to Law No. 28 of 2007 on Taxation, an individual or corporation owes an obligatory payment to the state that is coercive under the law, without receiving a direct return, and is utilized for the state's goals for the greatest prosperity of the people. Paying taxes, according to the idea behind tax law, is not only a responsibility, but also a right of every person to participate in governmental finance and national development. (Susilowati, 2020).

The government seeks to optimize tax revenue, which is inextricably linked to a number of challenges; additionally, the tax system in Indonesia is based on a self-assessment system, which means that taxpayers are responsible for calculating, paying, and reporting the amount of tax in accordance with tax laws and regulations. (Susilowati, 2020).

Taxes are the state's primary source of revenue, yet they are a hardship for firms, lowering their net profits. As a result, costs that lower net revenue drive firms to work as hard as they can to pay as little tax as possible and minimize their tax responsibilities. As a result of the disparity in interests, taxpayers can lower their tax payments. Because it is considered that the government's purpose of maximizing tax collection conflicts with the goals of firms seeking big profits. (Susilowati et al., 2020).

Tax avoidance is a strategy for lowering the amount of lawful tax owed. Tax avoidance is a legitimate approach for a corporation to decrease its tax burden that does not breach tax laws because tax avoidance is permitted by law. Many take use of this loophole to decrease the delayed burden on individual or business taxpayers by permitting tax avoidance (Susilowati et al., 2020).

Avoiding taxes is a complex and unusual challenge. On one side, tax avoidance is allowed, but on the other hand, this is not desired by the government. This tax avoidance is thought to be legal since it is believed that tax avoidance methods take advantage of gaps in the tax code, which will have an impact on state income from the tax sector (Mahdiana & Amin, 2020).

Only 30% of the 40 largest mining firms in Indonesia have embraced tax transparency reporting by 2020, according to PricewaterhouseCoopers (PwC) Indonesia (PricewaterhouseCoopers, 2021).

On the other hand, their tax returns were not yet transparent. This was found in PwC's most recent report, Mine 2021. The findings of the investigation reveal that a number of significant mining corporations are not completely complying with the government's tax and other levies. For example, the AO firm has been in the news because of its tax avoidance activities. The corporation aims to move income to Singapore, a tax haven nation, through its Singapore subsidiary. Consequently, the tax paid in Indonesia is less than the requirement that the corporation should be responsible for. (ekonomi.bisnis.com,2021).

The news website www.ddtc.co.id describes a similar situation, stating that mining corporations are prone to tax avoidance through transfer pricing strategies. The Corruption Eradication Commission (*KPK*) considers the mining industry to be prone to corruption, including tax fraud. The Corruption Eradication Commission (*KPK*) has reported a Rp. 15.9 trillion annual shortfalls in mining tax payments in forest regions. Even as of 2017, the mining and coal sector's non-tax state revenues (*PNBP*) arrears were IDR 25.5 trillion. This graph depicts the amount of potential state income that is wasted year after year. These bad difficulties have morphed into their own set of financial problems, one of which is linked to transfer pricing activities. (news.ddtc.co.id, 2019).

In this situation, multinational corporations are said to always try to reduce the amount of tax they pay by manipulating prices and passing the savings on to related organizations in other countries. The determination of the selling price and efforts to reduce taxes in the source country through modifications in the whole supply chain scheme are two important difficulties in the mining sector connected to transfer pricing by multinational firms. (news.ddtc.co.id, 2019).

This is attributable to the product's qualities, namely the standards for the product's quality and substance. Each of these parameters has a direct impact on the selling price due to its impact on processing and delivery. (news.ddtc.co.id, 2019)

Continue with mining firms. The Directorate General of Taxes (DGT) is currently investigating tax avoidance by PT Adaro Energy using a transfer pricing technique by its subsidiary in Singapore, according to the news website tirto.id. In a multinational corporation, transfer pricing refers to the price set in transactions between division members, which may differ from the market price and be consistent across divisions. Global Witness alleged that PT Adaro Energy Tbk diverts income in order to avoid paying higher taxes, according to the news website merdeka.com.(tirto.id, 2019).

According to Global Witness' financial report, the entire sales commission value received by Singapore's low-tax coal trade climbed on average yearly from USD 4 million before 2009 to USD 55 million from 2009 to 2017. More than 70% of the coal it sells is sourced from an Indonesian affiliate of Adaro Energy. To avoid paying taxes in Indonesia. Adaro might have decreased Indonesia's tax burden and the amount of money the government had available to fund crucial public services by close to USD 14 million annually (tirto.id, 2019).

There is also a tendency among older firms to avoid paying taxes. firm age has an impact on tax avoidance because the longer a firm has been in existence, the more experience it has and the more human resources it has, the better it is at managing the tax burden, and the more likely it is to uncover loopholes in tax avoidance This is because, once a firm is listed on the IDX and is public, it is required to make its financial reports available to the public and financial report users so that the information included in them may be used promptly by those who want it. Firms will become inefficient over time, due to the firm's experience and learning, as well as external forces in the same and different sectors, aging enterprises must cut expenditures, particularly tax costs. The longer a firm has been in existence, the more experience it has and the more likely it is to engage in tax avoidance. (Sari et al. , 2021).

Based on the descriptions of the phenomena above, several variables that could affect tax avoidance were obtained, namely profitability, leverage, and also Firm Age. This research will certainly focus on researching mining Firms in the coal sub-sector because it is based on the phenomena described above.

Profitability is a metric that assesses the efficiency of an organization's overall management, as measured by the magnitude of profit generated in relation to sales and investment. (Ariska et al. 2020) Profitability is also believed to be the ultimate outcome of a variety of firm policies and initiatives. As a consequence, profitability may be defined as a firm's capacity to generate profits or earnings that can be used to assess the efficiency of asset utilization, as well as the end result of policies and decisions made by the organization. (Artinasari & Mildawati, 2016).

If a firm's ability to make profits improves, the firm's operational profit rises, and the tax value rises as well, since profitability influences tax avoidance, but as profits rise, tax avoidance lowers. This is due to the fact that the corporation does not pay taxes efficiently. (Pratiwi et al. , 2020)

Research with the same results was obtained by (Sholeha, 2018) and (Anasta, 2021)that profitability has a big impact on tax avoidance or, to put it another way, there is a significant link between firm profitability and tax avoidance. (Rozak et al. , 2018)

Next is leverage, which refers to a firm's capacity to meet all of its short- and long-term obligations. The link between total assets and ordinary share capital is depicted by leverage, which demonstrates the utilization of debt to boost firm earnings.

The greater the debt, the smaller the taxable profit because the greater the tax incentive on debt interest is expressed by (Mahdiana & Amin, 2020) that leverage has a positive effect on tax avoidance.

The impact of a firm's longevity on performance is evaluated using the firm's age. A company will be more competent the more experience it has. Additionally, the longer a firm is in business and thrives, the more the public will recognize its success. Customers will trust the company if it is a good company and promises positive outcomes. Aging due to their experience and other factors in the same industry as well as other industries, firms must lower costs, including tax costs. In earlier studies undertaken by (Dewinta, 2016), The firm's age was calculated starting from the year of its founding, which was noted on the official organization record.

Based on the descriptions above, this research will be carried out with the title "**The Effect of Profitability, Leverage and Firm Age toward Tax Avoidance on Mining Sector Companies listed on the Indonesia Stock Exchange**)".

1.2 Problem Limitations

The following phenomena are used to define the problem boundaries:

1. The object of this research is Mining companies included into the coal mining subsectors listed at Indonesia Stock Exchange from 2018 to 2020.
2. In this research, the independent variables are Profitability (Return on Assets), Leverage (Debt Ratio or Debt-to-Assets Ratio), and Firm age., while the dependent variable is Tax Avoidance

1.3 Problem Formulation

Based on the background and limitations of the problem above, the formulation of this research is:

1. Does profitability significantly affect tax avoidance in mining firms listed on the Indonesian Stock Exchange partially?
2. Does leverage significantly affect tax avoidance in mining firms listed on the Indonesian Stock Exchange partially?
3. Does firm age significantly affect tax avoidance in mining firms listed on the Indonesian Stock Exchange partially?
4. Do Profitability, Leverage, and Firm Age significantly affect tax avoidance in mining companies listed at Indonesia Stock Exchange simultaneously?

1.4 Objective of the Research

The formulation of the problem above leads researchers to the following goals:

1. To determine whether Profitability has significant impact toward Tax Avoidance in Mining Companies listed at Indonesia Stock Exchange partially.
2. To determine whether leverage has significant impact toward Tax Avoidance in Mining Companies listed at Indonesia Stock Exchange partially.
3. To determine whether firm age has significant impact toward Tax Avoidance in Mining Companies listed at Indonesia Stock Exchange partially.
4. To find out whether Profitability, Leverage, and Firm Age have significant impact toward Tax Avoidance in Mining Companies listed at Indonesia Stock Exchange simultaneously

1.5 Benefit of the Research

1.5.1 Theoretical Benefit

1. As a discourse in economics, as well as enriching theories related to Tax Avoidance.
2. Can add scientific information that is used as a reference in the next research study with the same topic

1.5.2 Practical benefit

This research is expected to provide useful information and understanding to help mining companies avoid tax avoidance that is detrimental to the state and to enrich the results of research related to Tax Avoidance