CHAPTER I

INTRODUCTION

1.1 Background of the Study

Taxes are the main source of income for the state that aims to improve the welfare of the people by improving public services, which include health services, education services, judicial services, marine navigation services, security services, traffic services, and market services. The government always strives to optimize tax revenue, but there are always obstacles. Tax collection implemented by the government is not always well received by the taxpayer. Taxes may be the state’s main income, but from the taxpayer’s viewpoint, it is an expense that reduces their income.

Source: ekonomikita.id (2021)

Figure 1.1 shows how important tax revenue is for the country. It can be seen from the figure that the state's tax revenue amounts to 1.444,5 trillion rupiahs out of the total state's revenue of 1.743.6 trillion rupiahs. Tax contributes more than 82.8% of the state's income.

Although tax is the state's primary source of income, companies recognize tax as an expense. The amount of taxes that must be paid increases in direct proportion to the company's profit. The higher the company's profit, the higher the tax that must be paid. This is the reason that triggers companies to carry out tax avoidance. Tax avoidance is a legal strategy that companies can utilize to avoid paying taxes or at the very least reduce their tax burden.

According to Saprudin et al. (2022), tax avoidance refers to a strategy used by taxpayers to minimize the tax burden that is enforced on them by taking advantage of legal loopholes or other flaws in the tax regulations. Even though this practice may harm the state, it is legal because it complies with all applicable laws. A company is more likely to engage in tax avoidance activity if its ETR value is lower, whereas a higher ETR value indicates a lower probability of tax avoidance.

The Tax Justice Network reports that as a result of tax avoidance, Indonesia is estimated to lose up to 4.86 billion USD annually. This number is equal to Rp. 68.7 trillion when it is converted to Indonesia's currency. A total of 4.78 billion USD was lost, which is equal to Rp. 67.6 trillion, as a result of corporate tax avoidance in Indonesia. The remaining 78.83 million USD were lost, which is around Rp. 1.1 trillion, as a result of tax avoidance by individual taxpayers in Indonesia.

The agricultural sector in Indonesia, particularly in the palm oil industry, is often considered to be tax avoidance. The Corruption Eradication Commission (*KPK*) identified approximately 63,000 taxpayers as problematic due to claims of tax payment fraud and insufficient tax collection from the Directorate General of Taxes in the palm oil industry. The *KPK*, citing data from the Directorate General of Taxes, stated that there were around 70,000 taxpayers, both entities and individuals, who were registered in the tax administration system. However, only about 9.6 percent reported tax notification letters. It means that there are around 63 thousand taxpayers in the palm oil industry that does not report tax notification letter.

Transparency International Indonesia (TII) stated that the potential loss of state revenue is an average of IDR 22.83 trillion per year due to alleged tax avoidance by palm oil companies. In fact, the palm oil sector is one of the country's mainstay export commodities. According to Kacaribu (2020), the agricultural sector has the lowest contribution to tax revenue compared to other sectors, although the contribution of the agricultural sector is very large for Indonesia's Gross Domestic Product (GDP), an average of 13%.

Profitability is one of the factors that affect tax avoidance. Profitability can be used to assess whether management is successfully managing the company. The term "profit" refers to the financial benefit achieved when the income from a commercial activity is greater than the costs, expenses, and taxes incurred to maintain that activity (Kenton, 2022). The profitability ratio has a close relationship to corporate income tax. A higher profitability ratio shows how efficiently the company gains profit so that the corporate income tax that must be paid will also be higher. Hypothetically, the profitability ratio affects corporate income tax.

The return on asset ratio can be used to calculate the profitability ratio. The ROA, or return on assets, is a profitability ratio that displays the company's net profit margin as a percentage of total resources or the average number of assets. Generating income for the company is one of the goals of corporate assets. For this reason, ROA can show management how effectively a company can turn its asset investment into profit.

Besides profitability, leverage also affects tax avoidance. The leverage ratio is a ratio that assesses the amount of debt the company has. Companies should have to balance how much debt is worth taking and what sources can be used to pay off this debt (Anggraini & Kusufiyah, 2020). The amount of tax that the company must pay can be affected by the size of the leverage. This is because interest costs from debt are a deductible expense in calculating the tax burden (Barli, 2018).

Leverage can be measured using Debt to Equity Ratio (DER). DER shows the company's capability to fulfill all of its debt, which is measured by the amount of its capital used to pay debts.

Below is the table of profitability, leverage, and tax avoidance on several agriculture companies listed on the Indonesia Stock Exchange from 2017 to 2021:

Table 1.1 Table of Phenomena

Companies	Year	Profitability (ROA)	Leverage (DER)	Tax Avoidance (ETR)
PT. Astra Agro Lestari Tbk (AALI)	2017	0,082	0,345	0,281
	2018	0,057	0,379	0,311
	2019	0,009	0,421	0,631
	2020	0,032	0,443	0,389
	2021	0,068	0,436	0,290
PT. Dharma Satya Nusantara Tbk (DSNG)	2017	0,068	1,565	0,291
	2018	0,036	2,208	0,293
	2019	0,015	2,114	0,364
	2020	0,034	1,271	0,312
	2021	0,054	0,952	0,234
PT. Sinar Mas Agro Resources and Tech Tbk (SMAR)	2017	0,043	1,372	0,019
	2018	0,020	1,393	0,148
	2019	0,032	1,542	0,229
	2020	0,044	1,797	0,262
	2021	0,070	1,798	0,213

Source: Prepared by Writer (2023)

Table 1.1 above shows the value of return on assets, debt to equity ratio, and effective tax rate found in agriculture companies listed on the Indonesia Stock Exchange for the 2017-2021 period. Based on the table above, there are differences between profitability and leverage concerning the effective tax rate in the view of applied theory and the phenomena in the industry.

From 2019 to 2021, the ROA of AALI and DSNG increase every year while the ETR continued to fall from 2019 to 2021. This supports previous research by Darsani & Sukartha (2021) that states profit that can be generated by a company increases with its level of profitability, so the tax imposed on that profit will increase as well. Companies typically engage in tax avoidance because they do not want to pay high taxes due to their substantial earnings. The higher tax avoidance action is indicated by the declining ETR from 2019 to 2021.

The first phenomenon shows an inconsistent relationship between profitability and tax avoidance. Different from AALI and DSNG, the ROA of SMAR increased every year as well as the ETR from 2018 to 2020. It means that the company did not engage in tax avoidance activity although they have an increased profit every year. This was supported by the research from Artinasari & Mildawati (2018) that state profitability proxied by ROA does not affect tax avoidance proxied by ETR.

Another phenomenon is reflected by the inconsistent relationship between leverage and tax avoidance. The Debt to Equity Ratio of AALI increased consecutively from 2019 to 2021 while the ETR kept dropping in the same year. But for SMAR, the DER increase consecutively from 2018 to 2020 as well as the ETR. Sasiska et. al (2018) stated that leverage affects tax avoidance. Higher leverage ratios indicate that a company will use more debt to finance its business activities and pay higher interest rates on that debt. As a result, business management usually attempts to use debt as effectively as possible to reduce the amount of taxes that must be paid. However, Putri & Suryarini (2017) stated that leverage does not affect tax avoidance.

Based on the background above, similar research did not produce the very same result as the researchers had anticipated, the researcher felt it is needed to carry out another research in other types of industry. The title of the research is “The Effect of Profitability and Leverage Toward Tax Avoidance in Agriculture Sector Listed on the Indonesia Stock Exchange."

1.2 Problem Limitation

There is a limitation of variable that attempt to concentrate on the main problem and does not point in the opposite direction other than the topic being discussed to produce a consistent result. The following are the problem limits of this research:

1. The object of this research is limited to agriculture companies listed on the Indonesia Stock Exchange.
2. The period of the data used in this research is from the year of 2017-2021.
3. The independent variables in this research are profitability and leverage.
4. The dependent variable in this research is tax avoidance.

1.3 Problem Formulation

Based on the background above, there are several main problems in this research:

1. Does profitability partially have a significant impact on tax avoidance in agriculture companies listed on the Indonesia Stock Exchange?
2. Does leverage partially have a significant impact on tax avoidance in agriculture companies listed on the Indonesia Stock Exchange?
3. Do profitability and leverage simultaneously have a significant impact on tax avoidance in agriculture companies listed on the Indonesia Stock Exchange?

1.4 Objective of Research

Based on the problem formulation, the researcher formulated research objectives as follows:

1. To determine whether profitability partially has a significant impact on tax avoidance in agriculture companies listed on the Indonesia Stock Exchange.
2. To determine whether leverage partially has a significant impact on tax avoidance in agriculture companies listed on the Indonesia Stock Exchange.
3. To determine whether profitability and leverage simultaneously have a significant impact on tax avoidance in agriculture companies listed on the Indonesia Stock Exchange.

1.5 Benefit of Research

This research is expected to benefit various parties related to the research topic, including:

1.5.1 Theoretical Benefit

The outcomes of this research should deepen our understanding of how profitability and leverage affect tax avoidance. It can also be used as a resource for further research or information for future development.

1.5.2 Practical Benefit

To give an overview in gathering information and data about "The Effect of Profitability and Leverage Toward Tax Avoidance in Agriculture Sector Listed on the Indonesia Stock Exchange." It can also be used as literature material or reference for another researcher in conducting future research related to tax avoidance with profitability and leverage as the variable.