CHAPTER I

INTRODUCTION

1.1 Background of Study

Taxes are a very large source of the nation's earnings that are used to fund state expenditures, such as providing education and health facilities, building infrastructure, and financing government administration. Since taxes are already listed in the laws and even in the existing regulations governing taxation, they are obligatory. Taxpayer participation was required for the execution and expansion of national development to proceed smoothly.

Taxes are the main source of income for a country for the development and welfare of citizens, especially in Indonesia. In accordance with Article 1 paragraph 1 of the KUP Law Number 28 of 2007, tax is defined as a payment to the state owned by entities or individuals that are forced by law to pay, without receiving direct compensation, and is used for the requirements of the country and the welfare of the people.

Different interests between companies and the government cause tax resistance. Tax resistance is an impediment that arises in tax collection which could reduce the state’s revenue. Active and passive tax resistance are the two types of resistance that exist. The two main categories of active resistance are tax avoidance and tax evasion. Tax avoidance is done by carrying out tax planning to minimize tax payments. Tax planning is a strategy used to manage company finances to minimize matters relating to tax payments and not violating tax laws.

Tax avoidance is a legal tax minimization strategy that takes advantage of loopholes in tax law. Although tax avoidance is not explicitly forbidden by law, it is often seen negatively by the government and hence receives more attention than it otherwise would. Tax avoidance can be done by using a loophole or weakness of a tax regulation (Kurnia, Suryani, & Suciarti, 2020). The effective tax rate (ETR) is used to quantify tax avoidance in this study. ETR is the ratio amount of tax expense paid by the company divided by company profits.

The tax avoiding case that PT. Coca Cola Indonesia (CCI) did in 2014 is one example of tax avoidance in Indonesia. PT CCI is thought to have tried to avoid paying taxes, which led to a tax deficit of IDR 49.24 billion. This happened during the years 2002, 2003, 2004, and 2006. The investigation results of the *Direktorat Jenderal Pajak* (DJP), the Ministry of Finance discovered that there was a huge increase in expenses in that year. Large expenses cause taxable profit to decline so that the tax deduction paid also becomes smaller. These expenses include advertisements from 2002 to 2006 with a total of IDR 566.84 billion. That was for an advertisement for Coca-Cola brand finished beverage products. Thus, there is a decrease in taxable profit. The DJP says that CCI had a total taxable profit of IDR 603.48 billion during that time. Then there is a difference of IDR 49.24 billion in the amount of CCI income tax (PPh) that was not paid. For DJP, these fees are hard to explain, so they conclude that CCI uses transfer pricing to lower their taxes. Transfer pricing is when different parts of a business group trade goods and services at prices that aren't fair. This lowers the tax expense. This practice can be seen if there are things going on that don't fit with the business. PT CCI's products are concentrates, not finished beverage products. However, they have to pay a large amount for advertising. "Advertising costs charged by PT CCI are not directly related to the products produced," said Edward Sianipar, DJP representative in court, Thursday (12/6). Naturally, advertising costs fell on the other Coca-Cola companies. Coca-Cola Indonesia is split into three companies, which is the company that focuses on concentrate, packaging, and distribution. (https://nasional.kontan.co.id).

Based on this phenomenon, the writer can analyze that PT. Coca-Cola Indonesia intends to lower the company's tax expense. Where in this case PT Coca-Cola Indonesia increases advertising costs which will ultimately lower the amount of tax expense paid by the company. Large costs or burdens on a company will cause a small amount of income to be obtained by a company so that the taxes paid to the state will be smaller.

Profitability is one thing that can lead people to avoid paying taxes. Profitability is a way to measure how well a business is doing. Yoseph et al. (2020) research shows that the ability to make money has a big effect on avoiding taxes. The power of a company to make money in a certain time frame is measured by its profitability. The return on assets (ROA) value is one measure of how profitable a business is. In this study, ROA (Return on Assets), which is a measure of how well a company can make money with all its assets, was used as the profitability indicator. Return on assets (ROA) measures how much money a company can make from all its resources or assets. (Sirait, 2017).

Liquidity is also a factor that can influence tax avoidance. Companies with more liquidity show that they have enough cash flow to meet all their responsibilities, like paying taxes in accordance with the law. On the other hand, companies that don't have enough cash on hand won't be able to pay their taxes or follow tax law. Due to a lack of cash, the company will keep the cash flow going rather than pay taxes. The more debt a company has, the more likely it is to avoid paying taxes.

Another factor that influences tax avoidance is company size. Company size shows the company's capability to execute its economic activities. Large company size means that the transactions will be more complex, thus enabling the company to exploit the loopholes in the laws to carry out tax avoidance for each transaction. Company size in this research will be measured by the total assets of the company.

Table 1.1 Table of Phenomena

Companies	Year	Profitability (ROA)	Liquidity (CR)	Company Size	Tax Avoidance (ETR)
PT. Akasha Wira International Tbk (ADES)	2019	0.102	2.004	27.435	0.239
	2020	0.142	2.970	27.589	0.191
	2021	0.204	2.509	27.897	0.213
PT Industri Jamu Dan Farmasi Sido Muncul Tbk (SIDO)	2019	0.229	4.198	28.892	0.248
	2020	0.243	3.664	28.979	0.221
	2021	0.310	4.131	29.034	0.218
PT. Kalbe Farma Tbk (KLBF)	2019	0.125	4.355	30.640	0.254
	2020	0.124	4.117	30.747	0.228
	2021	0.126	4.445	30.876	0.220

Source: Prepared by writer (2023)

Based on the information in Table 1.1, there is some inconsistency between profitability (ROA), liquidity (CR), company size (measured by total assets), and tax avoidance (ETR) for consumer goods sector listed on the Indonesian Stock Exchange from 2019 to 2021.

From 2019 to 2020, the return on asset (ROA) for ADES has been increasing from 0,102 to 0,142. This is due to the increase in net income from 83,885 million Rupiah in 2019 to 135.789 million Rupiah in 2020. The increase in ROA is mainly due to the increase in net income which is influenced by the company's success in minimizing the COGS from 417.281 million Rupiah to 330.799 million Rupiah and the total expense from 226.204 million Rupiah to 180.603 million Rupiah although the net sales decrease from 764.703 million Rupiah to 673.364 million Rupiah. However, the ETR value continues to decrease from 0,239 to 0,191. This is due to the increase of profit before income tax by 52,41% but not along with the growth of tax expense which only increase by 22,20%. The difference in growth is related to fiscal asset depreciation which caused lower tax expenses.

The outcomes of previous research stated that the return on assets (ROA) affects tax avoidance (Darsani & Sukartha, 2021). This is because a higher ROA leads to a bigger net income for the company. High-profitability companies tend to position themselves in tax planning to lower tax expenses since a high profit will incur a high tax expense. However, according to Artinasari & Mildawati (2018), profitability represented by ROA does not influence tax avoidance represented by ETR. Companies with high profitability will choose to pay tax expenses instead of doing tax avoidance.

From 2020 to 2021, the current ratio for SIDO increases from 3,664 to 4,131. This is due to the increase in the current asset from 2.052.081 million Rupiah in 2020 to 2.244.707 million Rupiah in 2021 and the decrease in current liabilities from 560.043 million Rupiah to 543.370 million Rupiah. The increase in the current asset is affected by the increase in cash and cash equivalents, trade receivables, and inventories. Current liabilities decreased due to decreases in accrued expenses, trade payables, and other current liabilities. Other current liabilities for SIDO represent preparation for possible tax penalties arising from tax assessments. Meanwhile, the effective tax rate (ETR) of SIDO decreased from 0,221 to 0,218. This is mainly due to the increase of profit before income tax by 34,49% but not along with the growth of tax expense which only increase by 32,69%.

According to the findings of other studies, liquidity has a favorable and considerable impact on tax evasion (Urrahmah and Mukti, 2021). A measure of the company's capacity to meet its immediate obligations is its liquidity. Febrilyantri (2022) states that liquidity has no effect on tax avoidance. This occurs because it's crucial to keep a company's liquidity high. The corporation can easily meet its short-term obligations, such as tax payment demands, because it has a healthy level of liquidity.

PT. Kalbe Farma Tbk (KLBF) shows that the total asset from 2020 to 2021 increased from 22.564 billion Rupiah to 25.666 billion Rupiah due to the increase of cash and cash equivalents which caused by increasing net sales of the company. It can be seen from Table 1.1 that although the company size for KLBF increased, the ETR for KLBF decreased from 0,228 to 0,220. The decrease of ETR was led by the growth of 10,05% for tax expense in 2021 but was not along with the growth of earnings before tax which only increase by 14,21% in 2021. As the company size increases, the transaction will become more complex which might cause the company to exploit the loophole to conduct tax avoidance.

According to the results of previous research, the size of the company has a positive and significant impact on tax avoidance (Irianto, Sudibyo, & Wafirli, 2017). It implies that a larger company size will have a lower effective tax rate, and a lower effective tax rate will lead to more tax avoidance. However, according to Faizah & Adhivinna (2017), company size has no influence on tax avoidance. Companies with more assets typically have a better chance of producing consistent earnings than those with fewer assets, so companies with high assets are able to manage and pay their tax expense.

From the explanation above, there are still a variety of results regarding the factors that give effect to the tax avoidance in consumer goods sector listed on the Indonesia Stock Exchange from 2019 to 2021. The author will carry out the research with the title **“The Impact of Profitability, Liquidity and Company Size Toward Tax Avoidance in Consumer Goods Sector Listed on The Indonesia Stock Exchange”.**

1.2 Problem Limitation

The problem limitation of this research are as follows, based on the study's background:

1. The periods observed in this research are limited to 2019 until 2021.
2. The object of this research is limited to consumer goods sector listed on the Indonesia Stock Exchange.
3. The independent variables in this research are limited to profitability, liquidity, and company size.
4. The dependent variable in this research is limited to tax avoidance.

1.3 Problem Formulation

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

1. Does profitability have a significant impact towards tax avoidance of consumer goods sector listed on the Indonesia Stock Exchange?
2. Does liquidity have a significant impact towards tax avoidance of consumer goods sector listed on the Indonesia Stock Exchange?
3. Does company size have a significant impact towards tax avoidance of consumer goods sector listed on the Indonesia Stock Exchange?
4. Do profitability, liquidity, and company size simultaneously have a significant impact toward tax avoidance of consumer goods sector listed on the Indonesia Stock Exchange?

1.4 Objectives of the Research

Based on the above background, the objectives of this study are as follows:

1. To analyse the effect of profitability on tax avoidance of consumer goods sector listed on the Indonesia Stock Exchange partially.
2. To analyse the effect of liquidity on tax avoidance of consumer goods sector listed on the Indonesia Stock Exchange partially.
3. To analyse the effect of company size on tax avoidance of consumer goods sector listed on the Indonesia Stock Exchange partially.
4. To analyse the effect of profitability, liquidity, and company size on tax avoidance of consumer goods sector listed on the Indonesia Stock Exchange simultaneously.

1.5 Benefit of the Research

There are several benefits provided by the research as follows:

1.5.1 Theoretical Benefit

The author hopes that this study can be used as a basis for theory and as a point of reference for other academics who want to do more research on tax avoidance. The writer also thinks that the results of this study will help us learn more about how profitability, liquidity, and company size affect tax avoidance.

1.5.2 Practical Benefit

The writer thinks that this study can be used in the following ways:

1. For Scholar

   It is hoped that this study can help other students do research on tax avoidance by giving them information and a place to start.

2. For Investor

The results of this study are supposed to give information and examples about how the companies are doing, and they can also be used to help make decisions about investments.

3. For the Government

This study is meant to help the directorate general of taxes figure out what makes a company do things to avoid paying taxes.

4. For the Author

The goal of this study is to add new ideas, information, and tips for how to build on and use what has been learned in class.

5. For Further Research

The results of this study should be used as a starting point for more research into how company size, profit, and liquidity affect tax avoidance.