

# CHAPTER I

## INTRODUCTION

### 1.1. Background of Study

Taxes play an important role in national life, especially in the implementation of development, as they constitute the largest source of government revenue that finances all types of expenditures, including development expenditures. According to *Undang-Undang Republik Indonesia Nomor 28 Tahun 2007*, taxes are paid by the taxpayer to the State by natural or legal persons by the provisions of the law. Taxes are compulsory, contain no direct rewards, and serve the state's interest in improving the welfare of its people. From a development spending perspective, taxes are an important source of funding for states to develop infrastructure, education, health care, and public facilities. The more tax revenue we raise, the more public facilities and infrastructure we can build, and the better the quality of services our state can provide to our communities. Therefore, society needs to understand the importance of tax for the development of a country and consciously fulfill its tax obligations.

According to Pohan (2013), Tax avoidance is a practice that is done by companies to reduce the amount of the tax expenses in legal way without violating the existing law. The company recognized tax as burden that reduce and detain the net income of the companies. Therefore, the companies will try to avoid paying tax by observing and utilizing the flaws in the tax regulations. Tax avoidance that occurs is triggered by various things such as transfer pricing,

leverage, and company size. Transfer pricing is a policy regulated by a company to determine the transfer price for a transaction, whether the price of goods, services, intangible assets, or financial transactions carried out by the company. Transfer pricing can also be interpreted as the price charged by individual business units to multi-unit companies for transactions between them. Leverage is the use of capital and funding sources by a company that has fixed expenses. The source of these funds comes from debt where the debt has interest, which is included in fixed costs, so that potential profits from investors can be developed. Leverage is included in a regulation that is carried out by a business company when investing funds or obtaining sources of funds where there are fixed expenses that must be borne by the company.

According to Sonya et al. (2022), stated that Companies use transfer pricing as a tactic to intentionally move revenue from high-tax countries to low-tax countries, so lowering the total tax burden. To minimize and avoid taxes, this entails adjusting prices between various divisions within a business group. By modifying sales and purchase prices, assigning administrative expenses, controlling interest rates on shareholder loans, and figuring out commissions, licenses, franchises, rentals, royalties, and pay for different services, businesses can manipulate transfer pricing. Companies may also raise their operating expenses to reduce their taxable income. All things considered, transfer pricing is a tax optimization tactic that helps businesses minimize their tax obligations and manage global tax laws.

According to Ridho et al. (2023), stated that Leverage can be strategically employed by businesses by using debt to meet their investment and operational

needs. But there's a fixed expense associated with this: interest. Because debt interest offers larger tax benefits, a company's taxable profit falls as its debt levels rise. This incentivizes businesses to use more debt to fund their ongoing operations, which raises the interest load on them. Company management often uses debt as a means of lowering the company's tax responsibilities, as interest expenses are deducted from taxable income. This is an example of tax avoidance.

A significant measure of a company's size, depending on variables like total assets and income, is its size. According to Ulhaq & Effendi (2021), Due to their significant resources, larger businesses frequently have an advantage in operational activities and profit production. A company's size often reflects its financial health; large, stable businesses have more flexibility since it's easier for them to get funding from the market. A company's potential for substantial profits and tax obligations is influenced by its size, especially as indicated by its total assets.

According to Saragih & Ali (2023), around 55.4% of tax violations committed by global companies are driven by tax avoidance. One of the companies that carries out tax avoidance actions is agricultural sector companies, where many palm oil companies carry out tax avoidance actions. This can be seen from the increasing amount of land used for the palm oil industry, but the resulting tax revenue is decreasing. Viola and Baihaqi (2023), stated that the agricultural sector in Indonesia plays a role in increasing Indonesia's economic growth in the era of globalization. The agricultural sector supports the economic activities of society in general. Not only as a source of food for the community every day, but as a source of foreign exchange for the country as well. Until now, the agricultural sector is still

the mainstay of labor absorption from time to time. This is based on the conventional nature of the activities and agricultural products are always needed. This means that working in the agricultural sector does not require high skills. So that employment opportunities in this sector are flexible in accommodating workers who are less able to compete in other sectors Kusumaningrum (2019).

**Table 1.1 table of phenomenon**

Company	Year	ETR	RPT	DAR	CS
PT. ASTRA AGRO LESTARI	2020	0.389	0.272	0.307	17.140
	2021	0.290	0.382	0.304	17.230
	2022	0.262	0.413	0.240	17.191
PT. BISI INTERNATIONAL	2020	0.245	0.016	0.157	14.885
	2021	0.202	0.006	0.129	14.957
	2022	1.232	0.006	0.134	15.042
PT. LONDON SUMATERA INDONESIA	2020	0.192	0.795	0.150	16.206
	2021	0.206	0.863	0.142	16.288
	2022	0.193	0.828	0.119	16.335

Source: Prepared by writer. (2023)

The researchers would be able to determine the operating measurement ratio utilized in the study from this phenomena table. They employ (RPT) Related parties' receivables to measure transfer pricing, Debt to Assets Ratio (DAR) to measure leverage, and Effective Tax Rate (ETR) to monitor income tax payments and identify instances of tax avoidance. We can infer from the lower ETR that the business will probably use tax avoidance strategies common to their sector to maximize profits by identifying legal loopholes in tax regulations without breaching the law.

On the first table of phenomenon show that PT Astra Agro Lestari ratio. The first ratio of transfer pricing indicates that increase for 2020 to 2022, this could

represent the transaction of the good, services transferred between related entities within the same company, and the second ratio about the Debt to Asset Ratio (DAR) shows that the proportion of the assets that is used by fund/debt was decreased in 2020 to 2022 it is indicating that the improving the management of the used debt, and for the third ratio the company size shows that the ratio from 2020 to 2022 relatively stable.

On the second table of phenomenon show that PT Bisi International the first ratio. The first ratio of transfer pricing indicates that the value from 2020 to 2022 is decreased, this value if compared to PT Agro Lestari were relatively low. The second ratio about the Debt to Asset Ratio (DAR) shows same with the company before because it was decreasing. And the third ratio of company size value was increasing in 2022 to 2022.

And the third table of phenomenon show that PT London Sumatera Indonesia ratio. The first ratio of transfer pricing indicates that the value from 2020 to 2022 is increased to 2021 but slightly decreased in 2022 and the second ratio about the Debt to Asset Ratio (DAR) Shows that decreased from 2020 to 2022 and the third ratio of company size show that in 2020 to 2022 was relative stable.

In this research, the researcher uses research references from Sadeva, et al. (2020) entitled *Pengaruh Kepemilikan Institusional, Ukuran Perusahaan, Leverage Dan Transfer Pricing Terhadap Tax Avoidance (Studi Pada Perusahaan Pertambangan Yang Terdaftar Dalam Bursa Efek Indonesia Tahun 2014-2018)*. The difference between this research is that in previous research there was an

independent variable in the form of institutional ownership, whereas in this research it was only limited to independent variables in the form of transfer pricing, leverage and company size. Regarding the differences in research objects, previous research used mining companies listed on the Indonesia Stock Exchange, while this research used agricultural companies listed on the Indonesia Stock Exchange. The previous research period was 2014-2018, while in this research it was 2020-2022.

Based on the explanation of the background that has been described accompanied by a study of previous research which can be a reference for this research, it shows that tax avoidance practices are still often carried out by agricultural companies in Indonesia. This avoidance practice is carried out by companies by exploiting various existing loopholes such as transfer pricing along with other things that can influence it such as leverage and company size. Thus, the phenomenon that occurred made the writer interested in conducting research with the title: **“The Effect of Transfer Pricing, Leverage, and Company Size on Tax Avoidance in Agriculture Sector Companies Listed on the Indonesia Stock Exchange.”**

## **1.2. Problem Limitation**

To generate a consistent outcome, there is a limitation on the variables that try to focus on the main issue and do not point in the opposite direction from the topic being addressed. The research's problem limits are as follows:

1. The focus of this research is agricultural companies listed in Indonesia Stock Exchange.
2. The period of this research is from 2020-2022.

3. The independent variables are transfer pricing, leverage, and company size.
4. The operating measurements on the variables are RPT (Related Party Transaction), DAR (Debt to Asset Ratio), CS (Company Size).
5. The dependent variable is tax avoidance and measured with ETR (Effective Tax Rate).

### **1.3. Problem Formulation**

Based on the description of the background of the problem above, there are identification problem in this study can be identified:

1. Does transfer pricing significantly have a partial effect towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector?
2. Does leverage significantly have a partial effect towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector?
3. Does company size significantly have a partial effect towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector?
4. Do transfer pricing, leverage and company size significantly have a simultaneous effect towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector?

#### **1.4. Objective of the Research**

The objective of the research as follow:

1. To analyze whether transfer pricing has a significant effect towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector.
2. To analyze whether leverage has a significant effect towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector.
3. To analyze whether company size has a significant effect towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector.
4. To analyze whether transfer pricing, leverage and company size have a significant effect towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector.

#### **1.5. Benefit of Research**

##### **1.5.1. Theoretical Benefit**

- a. For Readers

The result from this study can be proof for readers to know that transfer pricing, leverage and company size have a significant effect towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector.



b. For Writer

The result from this study were to provide insight and experience as well as observations in a real-life situation which is very useful for the writer about the effect of transfer pricing, leverage, and company size towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector.

c. For Other Researchers

The result from this study can be used for reference for those who are interested in studying the same problem in the future about the effect of transfer pricing, leverage, and company size towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector.

### **1.5.2. Practical Benefit**

a. For Agricultural Company Listed in Indonesia Stock Exchange

The researcher expects the result from this study could benefit the business to evaluate and take the result as suggestion to know the effect of transfer pricing, leverage, and company size towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector.

b. For Writer

The result from this study is to make the writer gain new experience and more knowledge about the importance of transfer pricing, leverage, and company size towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector.

c. For Future Research

The researcher expects the result from this study could become a comparison for the future researchers who are interested of studying the same topic which is the effect of transfer pricing, leverage, and company size towards tax avoidance of companies listed on the Indonesia stock exchange in the agricultural sector.

