CHAPTER I

INTRODUCTION

1.1. Background of the Study

Considering taxation is the primary source of income in a country's revenue, it plays a vital role in developing countries, particularly in Indonesia, and also in developed countries around the world. Taxes become the most important source of government revenue in the modern economy. Every country, through taxation, requires contributions from its population (Syahwier & Fitriani, 2018).

Taxes play a critical role in the state's life, particularly in the implementation of development, because they are the largest source of state revenue used to fund all expenditures, including development expenditures, as well as state needs, in order to achieve the prosperity and welfare of the country's citizens without receiving direct compensation.

When it comes to tax policies, the government is usually proactive. As part of the government's efforts to modernize the tax system in Indonesia, the government changed the tax system from an official assessment system to a self-assessment system. Whereas the government is solely responsible for tax collection under the official assessment system, taxpayers in Indonesia have complete independence in calculating, paying, and reporting their own tax responsibilities under the self-assessment system. It is expected that, with the replacement of the Indonesian tax system, taxpayers will be more honest and voluntarily in meeting their tax duties in compliance with current tax legislation (Arianandini & Ramantha, 2018).

In actuality, tax revenue in Indonesia is consistently lower than the *Anggaran Pendapatan dan Belanja Negara (APBN*) aim. Due to the government's high targets and the fluctuating proportion of realized tax revenue, revenue realization in the tax sector has always been lower than the target. From 2015 to 2020, the following table shows data on tax revenue target and realization in Indonesia:

Table 1.1. Target and Realization of Tax Revenue in Indonesia (in trillion rupiah)

Year	Target	Realization	Percentage of Realization
2015	1.294	1.055	81,5%
2016	1.539	1.283	83,4%
2017	1.283	1.147	89,4%
2018	1.424	1.315,9	92%
2019	1.577,6	1.332,1	84,4%
2020	1.198,8	1.069,9	89,25%

Source: Directorate General of Taxes
Prepared by: Writer (2022)

Referring to table 1.1, realized tax revenues have consistently failed to meet stated targets over the last six years, as indicated by the percentage of tax revenues still fluctuating around 81-92%. The government's inability to maximize tax revenue raises the question of whether corporate or individual taxpayers are using tax avoidance strategies to decrease their tax burden.

Many citizens still regard taxes as a financial burden. Taxes are still considered by businesses and entities as a burden that will lower their net profit.

Taxpayers will seek for ways to decrease their tax obligations, both lawfully and unlawfully, one of which is tax avoidance.

Tax avoidance is not against the law, but because it is associated with a bad stigma, it often receives less attention from the Tax Office. This is because tax avoidance lowers the state's required tax revenue. The amount of tax due is decided by the company's use of debt as a source of finances. The use of debt as a source of finances can help a firm lower the amount of tax it has to pay. By increasing interest expenses, a company's tax liability can be decreased. The more corporate debt is used as a source of funding, the more tax avoidance occurs (Fitriani, 2017).

Tax avoidance may be legal as long as the law's or government's procedures are obeyed. Several phenomenon of financial fraud in the context of tax avoidance occurred in 2019. Bank Arthagraha Indonesia Tbk was found to have failed to record operating income between 2017 and 2019, placing stakeholders in risk. From 2017 to 2018, stockholders were unable to collect dividends due to the non-reporting of profits. Aside from audit results, it was also discovered that funds were transferred to a variety of entities outside of Indonesia, with claims that the transactions were linked to undeclared profits. The alleged fraud case at Bank Atrhagraha is still pending, and Bank Atrhagraha's reputation has been tarnished on the secondary market as a result of the negative circumstances (Zeng, 2019).

In 2018, encountered another tax avoidance phenomenon by PT. Bank Permata Tbk. Pelita Cengkareng sued Molucca and PT Bank Permata Tbk in this tax avoidance scandal. This case stems from a credit given by PT Bank Permata Tbk to Pelita Cengkareng on September 19, 2016, after which the receivables were supposed to start being paid on December 31, 2017. The receivables of PT Bank Permata Tbk were transferred to Lux Mask on March 4, 2017 through a Conditional Receivables Sale and Purchase Agreement, however they have yet to be paid. Molucca and PT Bank Permata Tbk then executed a novation and amendment to the conditional receivables sale and purchase agreement on April 28, 2017. Finally, Molucca and PT Bank Permata Tbk transferred receivables via deed No. 85 about loan cessie on May 5, 2017. According to article 27 paragraph 2 of the income tax law, there are alleged benefits to be received from PT Bank Permata Tbk in terms of tax avoidance, wherein PT Bank Permata Tbk will be exempt from paying a 25% income tax. Meanwhile, PT Pelita Cengkareng has filed a complaint seeking Rp 500 billion in material compensation and Rp 1 trillion in immaterial losses. Since the lawsuit was filed, each of them have accrued a 6% annual interest rate (Kontan, 2018).

Other phenomenon of PT Bank Century Tbk, which subsequently became PT Bank Mutiara Tbk and was managed by the Japanese J Trust corporation, went through a similar situation. The Deposit Insurance Corporation (DIC) took over Century Bank in November 2008, while it was experiencing a liquidity issue. The authorities identified Century Bank President Commissioner Robert Tantular as the prime suspect after it was determined that Rp 1.45 trillion in client cash had been stolen. The method involves offering customers phony mutual funds. Since 2002, PT Bank Century Tbk have been selling phony mutual funds. However, *BI* and *Bapepam-LK* discovered it in 2005. *BI* and *Bapepam-LK* did not promptly stop the fraudulent conduct in the financial business although knowing about it since 2005. Then, in 2018, the same Century Bank case resurfaced, claiming that the bank had led the government to lose up to Rp. 6.7 trillion (Ramelan, 2018).

Based to the findings of the phenomenon occurrences, many Indonesian banking companies continue to engage in tax avoidance. According to Kontan, (2018) the banking sector is one of the most essential sectors for Indonesia's economic growth because, after manufacturing and trade, banking sector is one of the largest tax contributors. In terms of net profit, the banking sector took the first place in 2017. This sector made a net profit of Rp 115.98 trillion, with 5.42% average net profit growth. The realization of financial industry tax revenues increased 7.7% yoy in August 2019 compared to the same period in 2018, which increased 5.7% on an annual basis.

The Ministry of Finance stated in the 2019 *Laporan Keuangan Pemerintah Pusat (LKPP)* that the income from the profit share of Banking SOCs amounted to Rp. 185.95trillion, but revenues from the financial services and insurance sectors experienced a minus 5.5% growth in 2020, due to credit slowdown and lower interest rates. Furthermore, the Covid-19 fiscal incentive, which went into effect in April, has increased revenue pressure (Kemenkeu, 2020).

Four main issuers, namely BBRI, BBCA, BMRI, and BBNI, have reported the highest net profit in the banking sector during the last five years. Hence, the focus of this research will be on banking companies listed on the Indonesia Stock Exchange. As a result, the purpose of this research is to investigate the object to discover if any tax avoidance is taking place. Profitability, independent commissioner and leverage are all factors that can effect tax avoidance. The following are data from several banking companies for each indicator, as shown below:

Table 1.2. ROA, IC, DER and ETR in Banking Companies Listed on the Indonesia Stock Exchange

Company Name	Year	Return on Assets (ROA)	Independent Commissioner (IC)	Debt to Equity Ratio (DER)	Effective Tax Rate (ETR)
PT. Bank Central Asia Tbk	2016	3,05%	60%	497%	20,15%
	2017	3,11%	60%	468%	20,02%
	2018	3,13%	60%	440%	20,96%
	2019	3,11%	60%	425%	21,27%
PT Bank Rakyat Indonesia Tbk	2016	2,61%	55,6%	584%	22,80%
	2017	2,58%	55,6%	571%	21,55%
	2018	2,50%	55,6%	600%	22,36%
	2019	2,43%	55,6%	567%	20,64%
PT Bank Mandiri (Persero) Tbk	2016	1,41%	50%	538%	21,12%
	2017	1,91%	50%	522%	21,04%
	2018	2,15%	50%	509%	23,84%
	2019	2,16%	50%	491%	21,91%
PT. Bank Negara Indonesia (Persero) Tbk	2016	1,89%	62,5%	552%	20,22%
	2017	1,94%	50%	579%	19,78%
	2018	1,87%	55,6%	608%	23,86%
	2019	1,83%	62,5%	551%	19,93%

Sources: Prepared by Writer (2022)

PT. Bank Central Asia Tbk, PT. Bank Rakyat Indonesia Tbk, PT. Bank Mandiri (Persero) Tbk, and PT. Bank Negara Indonesia (Persero) Tbk are some of the companies included in the table above. These companies were chosen because they are the four largest capitalization banks in their sector, with complete financial reports.

The tax avoidance indicator, which is the Effective Tax Rate (ETR), shows that the four companies suffered fluctuations throughout 2016-2019. While on Return on Assets (ROA), an indicator of profitability, shows that PT. Bank Central Asia Tbk and PT. Bank Negara Indonesia (Persero) Tbk experienced fluctuations, while PT Bank Rakyat Indonesia Tbk experienced decline and PT Bank Mandiri (Persero) Tbk experienced growth.

The return on assets (ROA) can be used to assess how well bank management utilizes the bank's real investment sources to create profits. Despite the fact that previous experts established the effect of profitability on tax avoidance in many research, there are still variances in research results. Profitability has no significant effect towards tax avoidance, according to Marpaung & Eduard (2020), whereas profitability has a significant effect towards tax avoidance, according to (Kimsen et al., 2019).

On the other hand, PT. Bank Central Asia Tbk, PT Bank Rakyat Indonesia Tbk and PT Bank Mandiri (Persero) Tbk have a consistent number of Independent Commissioners, while PT. Bank Negara Indonesia (Persero) Tbk had fluctuation. Because of the problem of tax avoidance, one approach for preventing or reducing tax avoidance is to have good corporate governance in a company. As it is the obligation of good corporate governance to evaluate management performance, it plays a key function in a company because it pushes management to be more compliant with tax payments. This research used independent commissioner as the variable. Independent commissioners have been found to have an effect on numerous researches by previous researchers, yet there are still variances in research outcomes. Handayani (2017) concluded that the independent commissioner has no significant effect towards tax avoidance, however Masrurroch et al. (2021) found the opposite, concluding that the independent commissioner has a significant positive effect towards tax avoidance.

However, leverage using the Debt to Equity Ratio (DER) as an indicator, PT. Bank Central Asia Tbk and PT Bank Mandiri (Persero) Tbk showed declines, while the others showed fluctuation. According to Widodo & Wulandari (2021) on earlier research concluded that leverage has a significant positive effect towards tax avoidance, with the supporting argument that debt that results in interest expense can be deducted from taxable profit. Interest expense that emerges as a result of loans to third parties or creditors who have no contact with the company is interest expense that can be deducted from taxable profit.

The lower income tax burden will be offset by the higher interest payments. Because interest expenses incurred as a result of debt can be deducted from taxable profit, it can be claimed that the higher the leverage value, the more likely the corporation is to engage in tax avoidance actions. According to Masrurroch et al., (2021) however, leverage has no significant effect towards tax avoidance.

Based on the previous research, the results are still inconsistent. Hence, based on background of the study, the writer wants to conduct further research regarding the effect of tax avoidance on profitability, independent commissioner, and leverage. As a result, this research entitled with **"The Effect of Profitability, Independent Commissioner and Leverage toward Tax Avoidance in Banking Companies listed on the Indonesia Stock Exchange".**

1.2. Problem Limitation

There are limitations in this problem research, which based on what was submitted in the background of study section:

1. Profitability using Return on Assets (ROA), Independent Commissioner and Leverage using Debt to Equity Ratio (DER) are the independent variables of the research, while Tax Avoidance using Effective Tax Rate (ETR) is the dependent variable of the research.
2. The banking companies listed on the Indonesia Stock Exchange will be the only focus of the object research.
3. The Research period is from 2017-2020.

1.3. Problem Formulation

Based on the background of study, the writer formed the problems formulation to be examined in this research, which are as follows:

1. Does Profitability have significant effect towards Tax Avoidance in Banking Companies Listed on the Indonesia Stock Exchange?

2. Does Independent Commissioner have significant effect towards Tax Avoidance in Banking Companies Listed on the Indonesia Stock Exchange?
3. Does Leverage has significant effect towards Tax Avoidance in Banking Companies Listed on the Indonesia Stock Exchange?
4. Do Profitability, Independent Commissioner and Leverage simultaneously have significant effect toward Tax Avoidance in Banking Companies Listed on the Indonesia Stock Exchange?

1.4. Objective of the Research

The objectives of this research are as follows, based on the background of the study above:

1. To analyse and determine whether Profitability has effect towards Tax Avoidance in Banking Companies listed on the Indonesia Stock Exchange.
2. To analyse and determine whether Independent Commissioner has effect towards Tax Avoidance in Banking Companies listed on the Indonesia Stock Exchange.
3. To analyse and determine whether Leverage has effect towards Tax Avoidance in Banking Companies listed on the Indonesia Stock Exchange.
4. To analyse and determine whether Profitability, Independent Commissioner and Leverage have simultaneous effect toward Tax

Avoidance in Banking Companies listed on the Indonesia Stock Exchange.

1.5. Benefit of Research

This research is expected to be valuable both theoretically and practically, as mentioned below:

1.5.1. Theoretical Benefit

This research is expected to improve taxation knowledge and understanding of the effects of Profitability, Independent Commissioner, and Leverage toward tax avoidance. It can also be used as a reference and a guideline in future researches.

1.5.2. Practical Benefit

The expecting Practical Benefit on this research, as follow:

1. For writer, this research is expected to provide information and understanding towards the effect of Profitability, Independent Commissioner and Leverage toward Tax Avoidance in Banking Companies listed on the Indonesia Stock Exchange.
2. For investors, this research is expected to provide information to future investors, who are interested on investing in the banking companies listed on the Indonesia Stock Exchange.
3. For companies, which expected to provide a better understanding of the factors that might give effect towards tax avoidance.