CHAPTER I

INTRODUCTION

1.1 Background of the Study

Tax is the source of national development funds as well as society's contribution to the state. Tax itself is an important tool for the government in achieving economic, political and social objectives. As a developing country, Indonesia is constantly striving to improve national development for the benefit of society. In order to carry out and improve national development, the state requires a large amount of funds to provide better education, health care, infrastructure and other public services, which are typically funded through the allocation of the State Budget (*Anggaran Pendapatan dan Belanja Negara*).

According to Article 1 paragraph (2) of the Law of the Republic of Indonesia Number 12 Year 2014 regarding the State Budget, “State Income is the Central Government’s right, which is acknowledged as an addition to net assets, including Tax Revenue, Non-Tax Revenue and Grant Revenue.” Specifically, the biggest source of state income is derived from tax revenue. This is proven by the state budget posture, which indicates that the tax revenue generated in 2020 was IDR 1,285.14 trillion from the total state income of IDR 1,647.78 trillion. In other words, approximately 78.02% of the state’s income is derived from tax revenue. As a result, the government is very concerned about tax revenue because the amount of tax revenue has a significant impact on the state budget.

Table 1.1 Tax Revenue Target and Realization in 2018-2020

Year	2018	2019	2020
Tax Revenue Target	1,618.09 T	1,786.38 T	1,404.51 T
Tax Revenue Realization	1,518.79 T	1,546.14 T	1,285.14 T
Percentage of Realization	93.86%	86.55%	91.50%

Source: Ministry of Finance of the Republic of Indonesia

However, from Table 1.1, it can be seen that from 2018 to 2020, tax revenue has never met the government's target. This might indicate there are issues holding back the government's effort to maximize tax revenue. One of the issues faced by the government in optimizing tax revenue is the practice of tax avoidance by companies. Even though tax is a major source of revenue for the state, it is considered a burden for company, because it is against its goal to earn profit as much as possible. This eventually leads to a conflict of interest between the government as the tax authority, who seeks to maximize tax revenue and companies as taxpayers, who seek to pay the least amount of taxes possible (Budi, 2016).

According to the Tax Justice Network's report, due to tax avoidance activity, Indonesia is estimated to lose up to IDR 68.7 trillion, of which 98.4% or equivalent to IDR 67.6 trillion is the result of corporate tax avoidance (Sukmana, 2020). Furthermore, the Minister of Finance of the Republic of Indonesia, Sri Mulyani Indrawati, also revealed that many companies have avoided paying taxes by continuously reporting losses. This is reflected in the increase in corporate taxpayers' loss reports from 8% in 2018 to 11% in 2019 (Pratiwi, 2021). This action is supported due to the Indonesian tax calculation system that applies the self-assessment system, which requires taxpayers to calculate, report and pay the amount of tax payable on their own. In this case, taxpayers will always try to pay the least amount of taxes, which is conducted through the practice of tax avoidance (Zain, 2008).

According to Brown (2012), tax avoidance is defined as the lawful attempt to minimize tax payment which is carried out by taking advantage of the loophole in the taxation laws. It is considered lawful because the taxpayer can obtain the tax benefit without violating any tax regulations. The existence of loopholes in tax regulations tends to encourage taxpayers to engage in tax avoidance activities (Manurung, 2020).

One example of a tax regulation loophole that companies may exploit in order to avoid paying taxes is regarding the benefit-in-kind provision. A benefit-in-kind is a reward that is received as additional financial capability and obtained not in the form money but in the form of goods. As mentioned in the PMK No. 167/PMK.03/2018 Article 3, food and beverages provided for employees in the workplace are categorized as deductible expenses. The food and beverages coupons that are provided for employees, in this case the employees from the marketing department, transportation department, or other external services who are unable to take advantage of the food and beverages at the workplace due to the nature of their work, are also categorized as deductible expenses. It is also mentioned in PMK No. 167/PMK.03/2018 Article 4 regarding the benefit-in-kind that is related to the work implementation in certain areas to support the government's development policy is categorized as deductible expenses as long as the required facilities are not available, so the employer must provide them to the employees. Furthermore, according to PMK No. 167/PMK.03/2018 Article 5 regarding the benefit-in-kind related to work implementation as necessary of work safety or due to the nature of the work that must require it, such benefit-in-kind can also be categorized as deductible expenses. As an additional, it is also advantageous for the company to replace the benefit-in-kind with an allowance that is given in the form of money since an allowance in the form of money can be charged as deductible expenses according to Income Tax Law Article 6 paragraph (1a).

Several factors have been discovered that affect companies when they engage in tax avoidance activities. However, the author will only focus on sales growth, leverage and profitability as factors in this research. The first factor is sales growth, which indicates the growth of sales from year to year. According to Subramanyam (2014), analyzing sales growth is used to assess a company's profit levels. Increase in sales growth will enable the company to achieve higher profit, which will eventually result in higher tax payable borne by the company. Therefore, the company engages in tax avoidance to reduce the tax payable (Mariani, 2020).

The second factor is leverage, which is used to determine how much debt a company relies on (Ross et al., 2014). The Debt to Assets Ratio (DAR) can be used to measure leverage. A higher DAR indicates the company is using more debt to finance its assets. As the company's debt level increases, the amount of interest expense will be increasing as well. Eventually, this will reduce the taxable income and result in a lower amount of tax payment. Therefore, leverage can affect the tax avoidance activity performed by the company (Antari & Merkusiwati, 2022).

The last factor is profitability, which is the primary goal for ensuring the survival of a company. According to Melicher & Norton (2017), the profitability ratio is used to measure a company's ability in generating profit over its sales, assets and equity. Return on Assets (ROA) can be used to measure profitability. A higher ROA indicates the company is more efficient and productive at managing its assets to generate more profit. High profits will lead to a higher tax burden that must be paid by the company to the government. This will increase the company's effort to minimize tax burden by practicing tax avoidance. Therefore, profitability can affect the tax avoidance activity performed by the company (Rahmawati et al., 2021).

According to Kemenperin.go.id (2022), the manufacturing industry contributes the most to the national Gross Domestic Product (GDP). One of the manufacturing industries is the consumer goods companies, which has several sub-sectors, which are food and beverages, cosmetics and household, pharmaceuticals, tobacco manufacturers, housewares and others. Moreover, consumer goods companies provide the state with the highest tax revenue contribution.

According to the data from the Ministry of Finance, the industry contributed 30% of the total tax revenue in 2018. However, the growth of tax revenue realization generated from the industry kept on decreasing each year during the period from 2018 to 2020. In 2018, the tax revenue realization from the industry amounted to IDR 363.60 trillion, which grew by 11.12%, but this figure was still slowing down compared to the growth in 2017 which was 18.28%. In 2019, tax revenue realization from the industry decreased by 1.8% and continued to decrease by 20.21% in 2020. This might indicate the practice of tax avoidance.

Since the discovery of COVID-19 at the end of 2019, the outbreak has spread to a number of countries. In Indonesia, the first case of COVID-19 was discovered on March 2, 2020 (Basri, 2020). One of the government's policies to prevent the spread of the COVID-19 is to restrict people's mobility through the implementation of Large Scale Social Restriction (Gitiyarko, 2021). This policy certainly has a negative impact on the country’s economic growth, especially in the domestic sector, which has a major impact on declining household consumption.

According to the data from the Ministry of Industry, Indonesia's economic growth decreased to -5.32% in the second quarter of 2020. The component of household consumption experienced the most severe contraction. Low household spending and declining public purchasing power will have an impact on the economy as a whole (Indahsari & Fitriandi, 2021). This indicates consumer goods companies have significant role in the country's economic growth. Thus, the author will use consumer goods companies as the object to be observed in this research.

Furthermore, the author is motivated to conduct this observation because of the phenomena in consumer goods companies listed in the table below:

Table 1.2 The Phenomena of Sales Growth, Leverage, Profitability and Tax Avoidance in Consumer Goods Companies Listed on the Indonesia Stock Exchange from 2018 to 2020

Company	Year	Sales Growth	Leverage (DAR)	Profitability (ROA)	Tax Avoidance (ETR)
PT Gudang Garam Tbk (GGRM)	2018	14.89%	34.68%	11.28%	25.63%
	2019	15.48%	35.24%	13.83%	24.90%
	2020	3.58%	25.15%	9.78%	20.86%
PT Kino Indonesia Tbk (KINO)	2018	14.27%	39.12%	4.18%	25.09%
	2019	29.55%	42.44%	10.98%	18.94%
	2020	-13.98%	50.96%	2.16%	15.90%
PT Akasha Wira International Tbk (ADES)	2018	-1.25%	45.32%	6.01%	24.41%
	2019	3.73%	30.94%	10.20%	23.86%
	2020	-19.29%	26.94%	14.16%	19.13%

Source: Prepared by Author (2022)

The Effective Tax Rate (ETR) can be used to measure tax avoidance by dividing the total income tax expense with the pretax income (Hanlon & Heitzman, 2010). A lower ETR value indicates that a company is more likely to engage in tax avoidance activity, while a higher ETR value indicates less involvement in tax avoidance activity (Palupi et al., 2021).

As shown in Table 1.2, from 2018 to 2019, PT Gudang Garam Tbk's (GGRM) sales growth increased from 14.89% in 2018 to 15.48% in 2019. This is due to the significant increase in sales of machine-made clove cigarettes. The company's strong sales performance and efficiency in maintaining the cost of sales have caused the profit to increase as well. However, the ETR value shows a decrease from 25.63% in 2018 to 24.90% in 2019. This is because of the fiscal reconciliation regarding fixed asset depreciation, which results in a lower taxable income and eventually has an impact on a lower tax payment. Based on the result, it might suggest that the fluctuation in sales growth has an effect on tax avoidance. According to the research conducted by Wulandari & Purnomo (2021), sales growth has significant effect on tax avoidance. Meanwhile, based on the research conducted by Mahdiana & Amin (2020), sales growth has no significant effect on tax avoidance. This demonstrates inconsistencies in previous research results.

The next phenomenon is displayed through the leverage of PT Kino Indonesia Tbk (KINO), which continues to rise from 42.44% in 2019 to 50.96% in 2020. However, the ETR value of PT Kino Indonesia Tbk (KINO) decreased from 18.94% in 2019 to 15.90% in 2020. The increase in leverage is primarily due to the increase in short-term and long-term bank loans, which were mostly used by the company for operational purposes. As debt increases, there will be higher interest expenses. This is reflected in the company’s financial statements, where the interest expenses continue to rise from IDR 83.25 million in 2019 to IDR 137.91 million in 2020. The interest expense is a deductible expense that reduces the company's taxable income, resulting in a lower amount of taxes that the company must pay. Leverage is associated with tax avoidance activity since a company gains tax benefit from the interest payment as a result of debt financing (Kasim & Saad, 2019). According to the research conducted by Putra et al. (2020) and Sormin (2020), leverage has a significant effect on tax avoidance. Meanwhile, according to the research conducted by Putri & Suryarini (2017), leverage has no significant effect on tax avoidance. This demonstrates inconsistencies in previous research results.

Another phenomenon is reflected in the profitability of PT Akasha Wira International Tbk (ADES) from 2018 to 2019, which has been increasing from 6.01% to 10.20%. This is due to the increase in net income from IDR 52.95 million in 2018 to IDR 83.88 million in 2019. The increase is mainly due to the increase in sales and the company’s success in managing the cost of goods sold. However, the ETR value continues to fall from 24.41% to 23.86%. This is due to the fiscal reconciliation of finance income, which is subjected to final income tax and fixed asset depreciation that decreases the taxable income and eventually has an impact to lower tax expense. Based on the result, fluctuation in profitability has effect on tax avoidance since companies tend to retain profit as much as possible from the tax payment. According to the research conducted by Waruwu & Kartikaningdyah (2019), profitability has a significant effect on tax avoidance. Meanwhile, according to the research conducted by Januari & Suardikha (2019), Salaudeen & Akano (2018) and Okerekeoti (2022), profitability has no significant effect on tax avoidance. This demonstrates inconsistencies in previous research results.

From the explanation above, there are still a variety of results regarding the factors that give effect to the tax avoidance in consumer goods companies listed on the Indonesia Stock Exchange from 2018 to 2020. Therefore, the author is interested in conducting the research entitled, **"The Effect of Sales Growth, Leverage and Profitability on Tax Avoidance in Consumer Goods Companies Listed on the Indonesia Stock Exchange."**

1.2 Problem Limitation

Based on the background of the study, the problem limitations of this research are as follows:

1. The object of this research is limited to consumer goods companies listed on the Indonesia Stock Exchange.
2. The periods observed in this research are limited to 2018 until 2020.
3. The independent variables in this research are limited to sales growth, leverage and profitability.
4. The dependent variable in this research is limited to tax avoidance.

1.3 Problem Formulation

Based on the previous description, the problem formulations in this research are as follows:

1. Does sales growth partially have a significant effect on tax avoidance in consumer goods companies listed on the Indonesia Stock Exchange?
2. Does leverage partially have a significant effect on tax avoidance in consumer goods companies listed on the Indonesia Stock Exchange?
3. Does profitability partially have a significant effect on tax avoidance in consumer goods companies listed on the Indonesia Stock Exchange?
4. Do sales growth, leverage and profitability simultaneously have a significant effect on tax avoidance in consumer goods companies listed on the Indonesia Stock Exchange?

1.4 Objective of the Research

Based on the previously described problem limitations, the objectives of this research are as follows:

1. To determine the partial significant effect of sales growth on tax avoidance in the consumer goods companies listed on the Indonesia Stock Exchange.
2. To determine the partial significant effect of leverage on tax avoidance in the consumer goods companies listed on the Indonesia Stock Exchange.
3. To determine the partial significant effect of profitability on tax avoidance in the consumer goods companies listed on the Indonesia Stock Exchange.

4. To determine the simultaneous significant effect of sales growth, leverage and profitability on tax avoidance in the consumer goods companies listed on the Indonesia Stock Exchange.

1.5 Benefit of the Research

There are several benefits provided by the research as follows:

1.5.1 Theoretical Benefit

The author expects that the findings of this study will enhance knowledge regarding the impact of sales growth, leverage and profitability on tax avoidance in consumer goods companies listed on the Indonesia Stock Exchange. The author also expects that this study might be useful as a reference and source of literature for future researchers who are going to conduct a study on a similar topic regarding the factors that have an effect on tax avoidance.

1.5.2 Practical Benefit

The following are some of the practical benefits of conducting this research:

1. For companies, it is expected that this research can be used to raise awareness not to avoid paying taxes, which might reduce state revenue and to make decisions that do not violate tax regulations.
2. For the government, it is expected that this research can be used as an evaluation tool to develop new tax policies in order to reduce the practice of tax avoidance by companies.