CHAPTER I

INTRODUCTION

1.1 Background of Study

Indonesia has a wealth of different natural resources. Indonesia is blessed with a variety of potential natural resources, both renewable and non – renewable, thanks to advantageous geographic placement between two continents and two oceans. Natural variety in Indonesia has grown to be a key resource for societal wellbeing and economic development. Regarding this wealth, it needs to be balanced with per capita income that the Indonesian population receives. A country’s per capita income might increase depending on the degree of firm income in each region. Considering a company’s tax burden is exacerbated by the high amount of corporate revenue. One of the objectives of the government is to maximize state tax income (Wijayanto, 2023).

Taxes are obligatory payments that taxpayers must make to government. The state does not directly compensate taxpayers. Taxes must be employed for governmental objectives to maximize the well-being of the populace since they are coercive. Taxes are significant source for a nation's economy. The largest source of revenue for the State Budget (APBN) is taxes. Taxes accounted for an average of 80% of all state income in the years 2018, 2019, and 2020. However, throughout the past ten years, the government's tax goal has never been attained (Martinus et al., 2021).

The government sets a target for tax revenue every year.

Table 1.1 Target and Realization of tax revenue in year 2020-2022 (in Trillion Rupiah)

Year	2020	2021	2022
Target Revenue	1,404.51	1,229.59	1,485
Realization Revenue	1,285.14	1,106.63	1,716.8
Percentage of Revenue	91.50%	88.04%	115,5%

Source: pajak.com 2022

Based on table 1.1, at year 2020 and 2021, the target revenue that set by the government did not achieve. A variety of internal and external variables that have an impact on a country's economy can be blamed for the inability to generate the desired amount of tax income. One of the variables might be tax avoidance.

According to Abdul Hakim & Bujang (2012), minister of Finance for Indonesia Sri Mulyani, the increase of tax revenue has shown positive performance in line with economic growth. There are several factors that can influence tax revenue of a country such as the economic condition of that country. Economic growth or inflation can affect tax revenue. During 2020, we faced the Covid-19 pandemic cause the economic sector of country become slow for two years. But in 2022, the condition gets better and slowly our economy begins to recover. A nation with a high rate of inflation will be compelled to raise taxes on goods and services in order to stabilize consumption and aggregate spending. Other factors that can affect tax revenue are tax regulation and external factor. Changes in regulation can affect taxpayers directly. The external factor was referred to the global economic trends, international trade (Abdul Hakim & Bujang, 2012).

Tax in Indonesia is collected from various sectors such as manufacturing, agriculture, mining, construction and many more. In 2022, manufacturing sector contribute the highest contribution to Indonesia's Gross Domestic Product (GDP), which is 18,34%. There are three subsectors of the manufacturing sector, namely basic & chemical industry, miscellaneous and consumer goods. Additionally, as indicated in the below figure, can know the percentage of contribution of each sector.

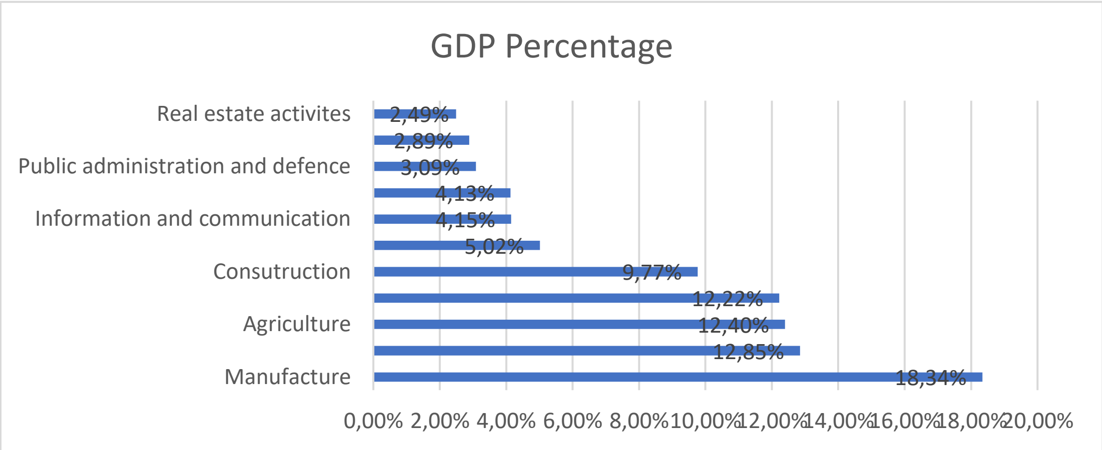

Figure 1.1 Contribution of Indonesia GDP in year 2022

Source: Badan Pusat Statistik (2023)

The figure show that manufacturing contributes the largest to the GDP which also means contribute the largest to the Indonesia tax revenue. This study only focuses on the manufacturing subsector which is consumer goods company that listed on Indonesia Stock Exchange.

The largest portion of GDP that produced by the manufacturing sector as a whole. Mostly made up for the consumer goods sector. Consumer Goods sector, usually referred to as the consumer discretionary sector, is a large economic sector that include business that create and offer customers non-essential item or services. As contrast to necessities like food, house, healthcare, these are goods and services that people can choose to purchase when they have the extra cash on hand. The spending power of customers brought on by their income and changes in people's lives is the key to this industry's success. One of the things that boosting Indonesia's economy is this industry.

Despite the efforts, Indonesian government continues to face difficulties in improving its tax colleting system such as tax avoidance. Tax avoidance refers to a taxpayer's attempt to lawfully, securely, and without violating any tax law rules, minimize or even eliminate tax bills that must be paid. This is done by exploiting loopholes (grey areas) in a country's tax code. In Indonesia, tax avoidance is frequently the result of a number of circumstances, from ambiguous tax regulations to company incentives aimed to maximizing profits. (Dwiyanti & Jati, 2019) Companies have chances to lawfully minimize their tax payments due to the complex tax system and frequent changes in tax legislation. However, tax avoidance is not only carried out by corporate taxpayers but also by individual taxpayers (Rahmawati & Nani, 2021).

In Indonesia, tax avoidance can be done in several ways such as take advantages of the reasonableness of tax law interpretation to pay less tax than would otherwise be owed, shifting profit to countries with lower tax rate, take advantages of tax incentives provided by the government, using a complex corporate structure to reduce taxes be paid, transfer pricing, thin capitalization, treaty shopping and Controlled Foreign Corporations (CFC).

One of the examples of tax avoidance carried out by corporate taxpayer is utilizing PP Number 23 of 2018, which provides 0.5% tax rates for MSMEs with gross revenue under Rp 4.8 billion. This is frequently used by companies looking to reduce the amount of income tax owed. For instance, business may postpone recording its sales toward the end of the year to use PP 23. Although the invoice will be issued in the next period, the product is still being delivered to the customer. At the end, the companies can keep its gross turnover below Rp 4.8 billion thanks to this. Meanwhile, a common example of tax avoidance carried by individuals is not reporting their assets and not fully report their income.

The economic consequences of tax avoidance are complex, with serious implication for Indonesia's growth and fiscal sustainability. The government's ability to support important public services, infrastructure projects, and social welfare programmed is hampered by the fall in tax income. As a result, socioeconomic progress has become difficult, and the government's attempts to eliminate inequality and encourage economic growth are undermined. Furthermore, tax avoidance might create an unequal playing field for enterprises. Companies that engage in active tax avoidance obtain a competitive advantage by lowering their operational expenses, allowing them to provide lower – priced products and services than conforming enterprises. This arrangement has the potential to inhibit fair competition, impede market expansion, and limit the growth of local enterprises (Handayani, 2021).

There are a variety of elements that may impact tax avoidances in business. In this research, tax avoidance becomes the dependent variable along with three independent variables such as leverage, capital intensity, and inventory intensity that affect the dependent variable. Tax avoidance in this research is measured by Effective Tax Rate (ETR). ETR is the proportion of actual tax paid by a person or company based on their income after taking into account all variable tax credit and deduction, which is more accurate indicator compared to the tax rate (Gloria & Apriwenni, 2020). ETR is determined by dividing the company's tax expense to pre – tax income. An elevated risk of task avoidance is indicated by a low ETR. There are many other variables that can affect tax avoidance that have been studied. In this paper, it will focus on leverage, capital intensity and inventory intensity as the variables that affect tax avoidance.

The factor in tax avoidance that is discussed in this research is leverage. Leverage is a ratio that displays the percentage of debt utilized to fund investment. The leverage ratio is used to assess a firm's capacity to fulfil both long – term and short – term commitments in order to finance corporate assets (Maulana et al., 2023). Leverage is measured by using Debt to Equity Ratio (DER). DER is a financial metric that indicates how much debt and equity were used to fund a company's assets. DER can be calculated by dividing total liabilities into total equity. Investors tend to find companies with smaller DER more appealing since they have fewer financial obligations. A bigger DER, on the other hand, denotes a bigger debt obligation, demonstrating that the firm is funded by a creditor rather than its own revenue. This ratio is essential for determining the financial health of a corporation (Suciarti et al., 2020).

The second factor that is discussed in this research is capital intensity. Capital intensity is company's investment activity in the form of fixed asset. The amount of capital invested by the business in the form of fixed assets is referred to as capital intensity. Due to the depreciation expenses associated with owning fixed asset, the company's tax expenses may be reduced (Kalbuana et al., 2020). Capital intensity can be calculated by dividing total fixed asset to total asset, a high CIR suggest that the company must spend too much on its asset to create revenue (MasterClass, 2022).

The third factor in this research is inventory intensity. Inventory intensity is the amount of inventory the firm has. The company may incur maintenance costs and storage cost because of its inventory. As a result of this load, company profit will decline, resulting in a drop in the amount of taxes that must be paid. Inventory intensity can be calculated by dividing total inventory into total asset. When a firm has high inventory intensity and its profit declines, the company will become more aggressive with regard to the size of its tax burden (Efrinal & Afia Hilda Chandra, 2020).

Table 1.2 ETR, Leverage, Capital Intensity, and Inventory Intensity 2020-2022

Company	Year	Leverage (DER)	Capital Intensity	Inventory Intensity	Tax Avoidance (ETR)
PT. Indonesian Tobacco Tbk (ITIC)	2020	0.804	0.282	0.263	0.559
	2021	0.622	0.262	0.229	0.263
	2022	0.518	0.276	0.261	0.257
PT. Soho Global Health Tbk (SOHO)	2020	0.335	0.814	0.251	0.310
	2021	0.319	0.830	0.278	0.202
	2022	0.194	0.865	0.256	0.216
PT. Merck Tbk (MERK)	2020	0.764	0.758	0.304	0.131
	2021	0.532	0.707	0.309	0.228
	2022	0.332	0.764	0.310	0.227

Source: Data Prepared by Writer (2023)

From Table 1.2 above, it can be seen that there are several very significant changes in leverage, capital intensity, inventory intensity with tax avoidance in consumer goods sector that listed on the Indonesia Stock Exchange from year 2020 to 2022. Table 1.2 shows that leverage which is calculated by Debt-to-Equity Ratio (DER) for PT. Indonesian Tobacco Tbk (ITIC) is decrease from 0.804 in 2020 to 0.622 in 2021, meanwhile the ETR also decrease from 0.559 in 2020 to 0.263 in

2021. ETR and DER in this is directly proportional, which should be inversely proportional because higher DER indicates that the company is funded by its creditor rather than the revenue means there are more liabilities that lead to higher interest expense and will cause the profit lower which means lower tax will be paid. Previous study that done by Suciarti et al. (2020) concluded that that leverage and deferred tax expense do not affect tax avoidance. But based on other study that done by (Maulana et al. (2023) concluded that that leverage affect tax avoidance. And from the study done by Rahmawati & Wahyudi (2021) concluded that leverage has no significant on tax avoidance.

In table 1.2, capital intensity for PT. Soho Global Health Tbk (SOHO) increases from 0.830 in 2021 become 0.865 in 2022, while the ETR is also increase from 0.202 in 2021 to 0.216 in 2022. There is a direct proportional between ETR and capital intensity although it should be inversely proportional because higher capital intensity ratio suggests that more assets, particularly fixed asset, are required to crease sales. Since depreciation expenditures are deducted from taxable income, depreciation expenses from fixed assets enable business to reduce their tax burden. Previous research that done by Suciarti et al. (2020) stated that capital intensity partially has a positive effect on effective tax rate or has a negative effect on tax avoidance. Other research that done by Urrahmah & Mukti (2021) stated that capital intensity has a positive effect on tax avoidance. Research done by Kalbuana et al. (2020) also stated the same as other research and agree that capital intensity has a positive effect on tax avoidance.

From the table shown above, inventory intensity for PT Merck Tbk (MERK) increases from 0.304 in 2020 to 0.309 in 2021 and the ETR increase from 0.131 in 2020 to 0.228 in 2021. There is a direct proportional between inventory intensity and ETR although it should be inverse proportional because higher inventory means that higher Cost of Goods Sold (COGS) that leads to lower profit and lower tax burden. Based on previous research done by Efrinal & Afia Hilda Chandra (2020) conclude that inventory intensity did not significantly affect tax avoidance, while other research that done by Dwisyanti & Jati (2019) concluded that inventory intensity positively affects to tax avoidance, and other researcher Urrahmah & Mukti (2021) stated that inventory intensity has no effect on tax avoidance.

Based on the problem and various results from previous studies that was mentioned above, the topic tax avoidance is addressed in this research, with factors like as leverage, capital intensity and inventory intensity having an impact on it. Therefore, the title is **"The Impact of Leverage, Capital Intensity and Inventory Intensity toward Tax Avoidance in Consumer Goods Companies Listed on the Indonesia Stock Exchange".**

1.2 Problem Limitation

There are several restrictions in this research to avoid extensive from the research subject:

1. The object that used in this research is consumer goods companies that listed on Indonesia Stock Exchange.

2. The variables are limited to leverage, capital intensity, inventory intensity and tax avoidance.
3. The period of the research is 2020 to 2022.

1.3 Problem Formulation

The formulation of this research's problems:

1. Does leverage have an impact on tax avoidance in the consumer goods companies listed on the Indonesia Stock Exchange?
2. Does capital intensity have an impact on tax avoidance in the consumer goods companies listed on the Indonesia Stock Exchange?
3. Does inventory intensity have an impact on tax avoidance in the consumer goods companies listed on the Indonesia Stock Exchange?
4. Do leverage, capital intensity and inventory intensity have an impact on tax avoidance in the consumer goods companies listed on the Indonesia Stock Exchange?

1.4 Objective of the Research

Based on the formulation above, the objective of this research is:

1. To analyze if tax avoidance in the consumer goods companies that listed on the Indonesia Stock Exchange is significantly impacted by leverage.
2. To analyze if tax avoidance in the consumer goods companies that listed on the Indonesia Stock Exchange is significantly impacted by capital intensity.

3. To analyze if tax avoidance in the consumer goods companies that listed on the Indonesia Stock Exchange is significantly impacted by inventory intensity.
4. To analyze if tax avoidance in the consumer goods companies that listed on the Indonesia Stock Exchange is significantly impacted by leverage, capital intensity and inventory intensity.

1.5 Benefit of the Research

The expected benefit from this research is as follows:

1.5.1 Theoretical Benefit

By conducting this research, it was anticipated that this study can provide further information and may be utilized as literature and a source of reference for further research on tax avoidance.

1.5.2 Practical Benefit

This research aims to provide insight into factors influencing tax avoidance, enable companies to concentrate on tax management, execute plan appropriately, and lower the chances of facing tax penalties. Additionally, it provides useful information for researchers and helps people in comprehend according to their interests.