CHAPTER I

INTRODUCTION

1.1 Background of the Study

Downstream industries can significantly enhance economicgrowth and add value to Indonesia's abundant natural resources, particularly in the mining sector. By processing raw materials locally rather than exporting them in their raw form, Indonesia can capture more value, create jobs, and foster technological development.

Down-streaming in the mining sector involves activities such as refining minerals, manufacturing finished goods, and developing related infrastructure. This strategy not only boosts revenue but also reduces dependency on raw material exports and enhances the resilience of the economy against commodity price fluctuations.

Moreover, by focusing on sustainable practices in down-streaming, Indonesia can mitigate environmental risks associated with mining and promote responsible resource management. This approach aligns with global trends towards sustainable development and can attract investment from environmentally conscious industries.

Overall, prioritizing down-streaming in the mining sector can contribute to Indonesia's long-term economic growth and competitiveness while ensuring the responsible utilization of its natural resources. Down-streaming in the mineral and coal sector plays a crucial role in maximizing the value of mineral and coal mining products. In the future, downstream activities are expected to become a significant contributor to state revenues, in addition to taxes.

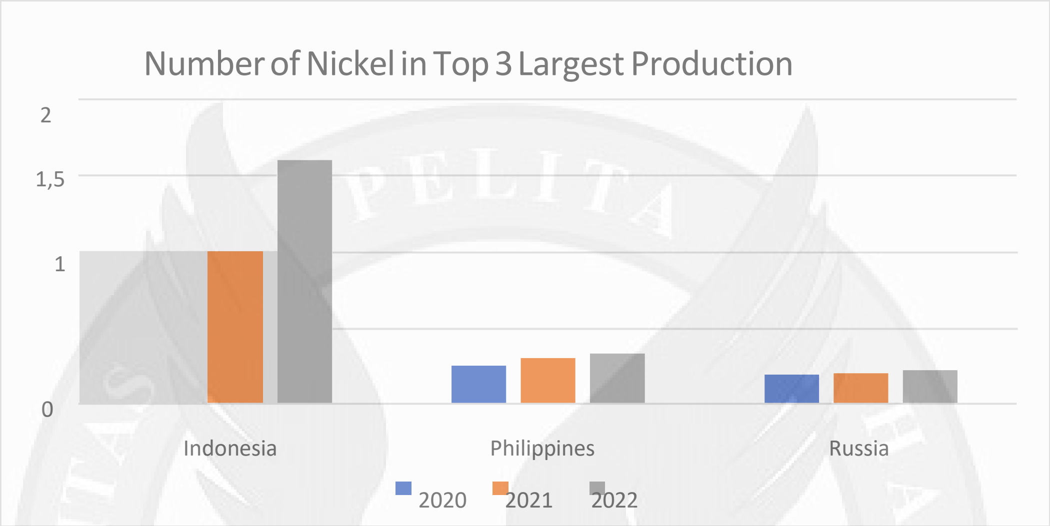

Figure 1.1 Top 3 of Largest Nickel Production
Source: Prepared by Writer (2024)

Nickel is a versatile metal with many important uses, particularly in the production of stainless steel. Its shiny appearance and corrosion-resistant properties make it a valuable material for various industries. In addition to its use in stainless steel, nickel is also used in the production of other alloys, such as nickel-copper and nickel-molybdenum, which have applications in electronics, aerospace, and chemical industries.

Indonesia is the leading global producer of nickel ore, with substantial reserves primarily found in Sulawesi, Maluku, and Papua. The country's nickel ore production plays a crucial role in global supply chains, especially for stainless steel and electric vehicle battery manufacturers.

Capital intensity can indeed influence tax avoidance strategies for companies. This is because higher capital intensity often implies higher depreciation expenses, which can be used to offset taxable income. Companies with high capital intensity may strategically allocate their assets to maximize depreciation deductions, thereby reducing their tax liability.

Capital intensity is a crucial metric that reflects how effectively a company utilizes its assets to generate revenue. It measures the amount of capital, represented by assets, required to produce a given level of revenue. A high capital intensity ratio signifies that a corporation necessitates a substantial amount of capital investment to create income. This is particularly true in industries with high infrastructure or equipment expenses, such as manufacturing or mining. Conversely, a low capital intensity ratio indicates that a corporation may create revenue using fewer assets, which is commonly observed in service-oriented industries such as consulting or software development.

Comprehending capital intensity enables firms to make well-informed decisions regarding the allocation of resources, investment strategies, and operational effectiveness. The level of capital investment has a substantial impact on the practice of minimizing tax payments. This finding supports the political cost theory, which suggests that large firms frequently use accounting strategies to reduce reported profits and thereby lower their tax liabilities. They accomplish this by channeling profits into fixed assets, which can be depreciated over time, leading to depreciation expenses that further decrease their reported profits (Yusuf et al., 2020). In contrast to the results reported by Safitri & Wahyudi (2022), the level of capital intensity does not have a significant impact on tax avoidance.

The size of a firm can affect its tax avoidance strategies. Bigger firms frequently have more assets, counting budgetary and human capital, to lock in in complex charge arranging techniques pointed at minimizing their charge liabilities. These methodologies may include transfer pricing, tax havens, and other methods to reduce taxable income.

There has to be a comprehensive investigation of the complex link between the size of a corporation and its tendency to dodge taxes. Tax planning and the promotion of advantageous tax legislation are often the purview of bigger organizations, but smaller businesses may still make good use of tax methods to reduce their tax payments. Industry, regulatory climate, and individual company circumstances all have a role in determining the relative importance of business size in explaining tax evasion practices.

Nyman et al. (2022) suggest that a company's size positively influences tax avoidance, which contrasts with Yantri (2022), who argues that companies with substantial total assets are generally more stable and capable of generating profits and fulfilling their obligations compared to those with smaller assets. Larger assets imply better long-term prospects, reducing the incentive to avoid taxes. This study, however, finds that firm size has a minimal impact on tax avoidance.

Manufacturing companies, which fall under the category of asset-intensive businesses, possess substantial assets like materials, equipment, and factories. In light of this, Return on Assets (ROA) serves as an appropriate metric for assessing the profitability of miscellaneous industry companies, given that these firms derive their income from the utilization of their assets.

Profitability and tax avoidance did not correlate significantly, according to the study. Interest expenditures do not significantly reduce tax obligations for the firms investigated, especially those with a larger reliance on loan funding from connected corporations. On the other hand, tax evasion is positively correlated with increased leverage. A study conducted by Apriliyani and Kartika (2021) found that enterprises with greater levels of debt tend to disclose their taxes more accurately than those with lower levels. Yohanes and Sherly (2022) found the opposite to be true; they showed that tax evasion is affected by profitability.

Based on the background study mentioned, the writer is interested in researching Mining Sector Companies listed on the Indonesia Stock Exchange (IDX) and is focusing on this topic which entitled **"The Influence of Capital Intensity, Firm Size, and Return on Assets on Tax Avoidance in Mining SectorCompanieslisted on Indonesia Stock Exchange."**

1.2 Problem Limitation

Based on the study's background, the research faces the following limitations, namely:

1. The variables that used by the writer in this study are tax avoidance, capital intensity, firm size, and return on assets.
2. In this research, the writer will use return on assets (ROA) to measure profitability.
3. The object of research in this study focused on mining sector companies listed on the Indonesia Stock Exchange.

4. The period of research are 2020-2022.

1.3 Problem Formulation

Based on the context that was previously provided, the research problems may be formulated as follows:

1. Does Capital Intensity have significant influence toward Tax Avoidance in Mining Sector Companies listed on the Indonesia Stock Exchange?
2. Does Firm Size have significant influence toward Tax Avoidance in Mining Sector Companies listed on the Indonesia Stock Exchange?
3. Does Return On Assets have significant influence toward Tax Avoidance in Mining Sector Companies listed on the Indonesia Stock Exchange?

1.4 Objective of the Research

The research's objectives are as follows:

1. To find out whether Capital Intensity has significant influence toward Tax Avoidance in Mining Sector Companies listed on the Indonesia Stock Exchange.
2. To find out whether Firm Size has significant influence toward Tax Avoidance in Mining Sector Companies listed on the Indonesia Stock Exchange.
3. To find out whether Return on Asset has significant influence toward Tax Avoidance in Mining Sector Companies listed on the Indonesia Stock Exchange.

1.5 Benefit of the Research

This research is likely to offer benefits to various parties interested in the topic. These benefits can be categorized into two types, which are:

1.5.1 Theoretical Benefit

This research is anticipated to benefit education both directly and indirectly, aligning with the research objectives. The expected theoretical outcomes are valuable as they aim to provide deeper insights into the effects of Capital Intensity, Firm Size, and Return on Assets (ROA) on tax avoidance in Mining Sector Companies listed on the IDX. Additionally, the study is intended to serve as a reference for future research on tax avoidance, contributing to the academic understanding of the topic.

1.5.2 Practical Benefit

Practically, the writer expects that this research can be used as follows:

1. For inventors

   The study's results are anticipated to offer insights and examples regarding the status of the companies, particularly those examined in this research. Furthermore, the findings can serve as valuable inputs for decision-making in the context of investments.

2. For company

   By doing this research, the result of this research is expected to be used by the companies as a consideration of factors that effect to tax avoidance. So, the company must perform a strategy to decrease tax avoidance by control return on assets.

3. For scholars

This research is anticipated to provide data, references, and empirical evidence for researchers interested in exploring the same field of study.

4. For creditors

This research can be taken to decide whether to grant or extend loans to a company it can be considered to prevent potential loan repayment issues due to debtor inability.