

## The Profitability, Leverage, and Company Size of the IDX80 Index on Tax Avoidance in Indonesia Stock Exchange

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### ABSTRACT

In this study, the influence of profitability, leverage, and company size on tax avoidance for several companies listed in the IDX80 Index of the Indonesia Stock Exchange was investigated. The index consisted of 80 companies, but only 69 companies were chosen as a sample. The samples were determined by applying the purposive sampling method. The analysis of profitability, leverage, and company size on tax avoidance was shown by multiple linear regression. The results showed that profitability yielded a positive influence on tax avoidance, while, leverage and company size did not influence tax avoidance.

Keywords: IDX80, profitability, leverage, company size, tax avoidance

### 1. INTRODUCTION

Tax is one of the most significant contributions to a country paid by citizens as individuals or companies. All citizens as the taxpayer must obey to pay tax since it is mandatory and regulated by the law. For a company, the tax can give a significant impact to the profit due to its characteristics as the profit deduction factors. The companies usually expect to pay the tax minimally. It has been reported that several efforts had been conducted by companies to reduce tax payment without violating the regulation (Pohan, 2016). These can be done by exploiting limitations/ loopholes in taxation regulations (Pratiwi, 2017). The term of tax deduction that is conducted by taxpayers without violating the regulation is known as tax avoidance (Suandy, 2011). Practically, tax avoidance may cause different perceptions (a grey area) between the taxpayer and tax officer in defining the limits of taxation regulations. In the Indonesia constitution income tax regulation no. 36 years of 2008 states that the income tax consists of deductible and non-deductible tax. The deductible tax is expense taxed that can be deducted, such as allowance, salary, etc. The non-deductible tax is the expense taxed that can not be deducted, such as a voucher for vacation, lunch, etc.

There are several financial ratios such as profitability and leverage that may have a relationship to the tax avoidance. Profitability is used to see the efficiency carried out by the company, and it is measured using Return On Assets (ROA). ROA is known as a ratio that shows the return on the total assets used in the company (Kasmir, 2010). The greater the profit, the higher the level of profitability. The high profitability will result in high taxes that must be paid by the companies. Leverage is debt funding. According to Jaya (2016), the company will increase the debt to reduce the tax payment. Leverage is measured using the Debt to Asset Ratio (DAR). Companies with high leverage levels usually have low tax avoidance since the interest of debt can reduce the tax payment (Brigham and Houston, 2010).

Besides using financial ratios indicators, the company size has also been reported used to indicate tax avoidance (Hartono, 2007). Company size is measured using ln total assets. The bigger the company, the more complex the transaction will be. In the part of transactions such as accounts receivable, fixed asset, etc. allows companies to do tax avoidance.

It has been reported that tax avoidance is measured using the cash effective tax rate (CETR) (Hanlon and Heitzman, 2010). CETR is calculated by dividing cash disbursed for tax expenses by earnings before interest and tax. According to Dyreng et al. (2008), the CETR is proper to describe the existence of tax avoidance activities since CETR does not affect the change of tax protection. The higher the CETR percentage level, the lower the level of company tax avoidance, and vice versa. The higher the CETR percentage level, which is higher than the company income tax rate of 25%, indicating that the company does not do tax avoidance.

In this study, the investigation of tax avoidance is conducted to the companies listed on IDX80 Indonesia stock index. This index consists of 80 issuers that have high liquidity and large market capitalization and are supported by good stock fundamentals. The IDX80 index has just launched in 2019. The influence of profitability, leverage, and company size in IDX80 index are analysed to the tax avoidance.

## 2. HYPOTHESIS DEVELOPMENT

### 2.1. Profitability on Tax Avoidance

Companies with high profitability have a higher tendency to do tax avoidance than companies with small profitability. The higher the profitability, the higher the tax expense to be paid. The companies with high profitability are more likely to apply tax avoidance than companies with low profitability. The companies with high profitability will result in more significant tax savings than companies with low profitability. Based on this concept, the following hypothesis is formulated:

**H1** = Profitability yields a positive influence on tax avoidance.

#### 2.2.1. Leverage on Tax Avoidance

Leverage can also be defined as the ability of the company to pay off long-term debt. Practically, the higher value of leverage, the smaller the tax expense. Companies with greater leverage have reasonable, effective tax rates. The company, with a large amount of leverage, will have low tax avoidance. Based on this concept, the following hypothesis is formulated:

**H2** = Leverage yields a negative influence on tax avoidance.

#### 2.2.2. Company size on Tax Avoidance

The company size is determined based on the total assets, resources, and average total net sales of the company. Companies with large sizes usually have more advantages when compared to small size companies. Large companies have resources with the superior quality to apply tax avoidance compared to small companies. The larger the company, the more complex the transaction will be. This allows companies to find loopholes for each transaction as tax avoidance. Based on this concept, the following hypothesis is formulated:

**H3** = Company size yields a positive influence on tax avoidance.

### 3. RESEARCH METHOD

#### 3.1. The Reserach Data

The data used in this research is the IDX80 index listed in Indonesia Stock Exchange in 2019. The total population of companies in the IDX80 index is 80. The sampling is determined by purposive sampling method based on specific criteria (Hartono, 2013). Based on predetermined criteria, only 69 companies can be used. According to the hypotheses development, the research model can be described as shown in figure 3.1. The relationship between profitability, leverage, and company size with tax avoidance is analysed by multiple regression method.

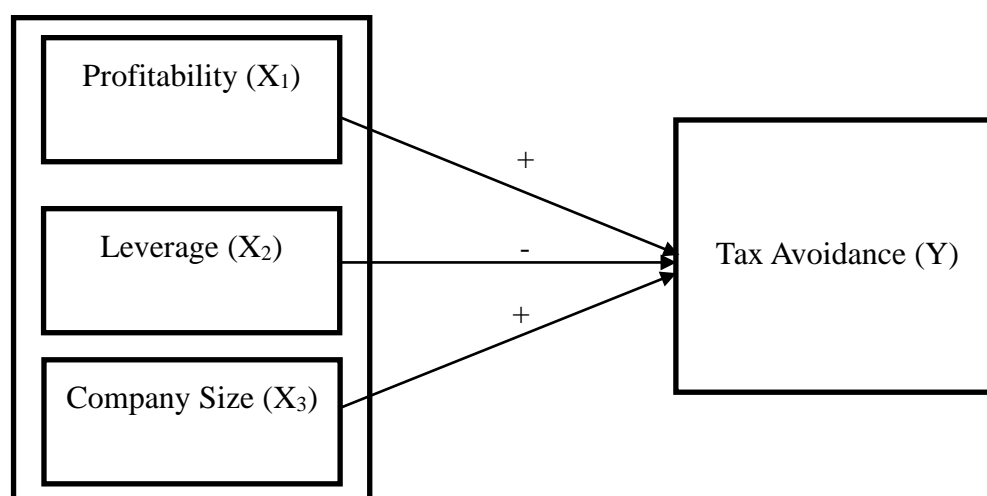


Figure 3.1 Research model

### 4. DATA ANALYSIS

#### 4.1. Statistic Description

Statistic values of mean, standard deviation, maximum, and minimum for profitability, leverage, company size, and tax avoidance are listed in table 1. The results show that the profitability variable (ROA) has the lowest value of 0.01 and the highest value of 0.68. This variable shows an average value of 0.1371, with a standard deviation of 0.11861. The leverage variable (DAR) has the lowest value of 0.15 and the highest value of 0.93. This variable shows an average value of 0.4565, with a standard deviation of 0.18182. The company size variable (SIZE) has the lowest value of 30.63 and 35.32 and shows an average value of 32.6374, with a standard deviation of 1.02712. The tax avoidance variable (CETR) has the lowest value of 0.00 and the highest value of 0.99. This variable shows an average value of 0.3011, with a standard deviation value of 0.19688.

Table 4.1 Statistical table description of research variables

	N	Minimum	Maximum	Mean	Std. Deviation	N
ROA	69	.01	.68	.1371	.1186	69
DAR	69	.15	.93	.4565	.1818	69
SIZE	69	30.63	36.32	32.6374	1.0271	69
CETR	69	.00	.99	.3011	.1968	69
Valid N (listwise)	69					

4.2. Hypothesis Testing

4.2.1. Hypothesis result

The Hypothesis testing result listed in table 4.2 is obtained by applying the multiple regression method. The following equation can express the relationship of profitability, leverage, company size, and tax avoidance

$$= -0.288 - 0.075X_1 - 0.135X_2 + 0.025X_3 + e$$

Where:

X<sub>1</sub> : Profitability

X<sub>2</sub> : Leverage

X<sub>3</sub> : Company Size

E : Error

Table 4.2 Hypothesis testing results

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	-.288	.525		-.570	.570
ROA	-.075	.024	-.340	-3.524	.000
DAR	-.135	.101	-.116	-1.342	.210
SIZE	.025	.017	.077	.856	.392

a. Dependent Variable: Tax Avoidance

4.2.2. T-Testing Value

The effect of ROA on CETR has a negative regression coefficient of 0.075 with a significance level of 0.000. This significant level can be accepted since the error value smaller than the 0.05. The tax avoidance variable proxied by CETR has an inversely proportional effect. The lower the CETR percentage level, the higher the level of

corporate tax avoidance (Dyreng et al., 2010). Based on this statement, it can be concluded that profitability has a positive effect on tax avoidance. This means that **Ha1** is accepted. Thus, **H1**, which states that profitability has a positive effect on tax avoidance, is supported statistically by empirical research.

The significance of the leverage effect on tax avoidance is 0.210, which is higher than the significance level of 0.05. Based on this level of significance, it can be concluded that the leverage variable does not affect tax avoidance. This means that **Ha2** cannot be accepted (rejected). Thus, **H2**, which states that leverage has a negative effect on tax avoidance, is not supported statistically by the results of empirical research.

The level of significance of the company size effect on tax avoidance is 0.392, which is higher than the significance level of 0.05. Based on this level of significance, it can be concluded that the company size variable does not affect tax avoidance. This means that **H3** cannot be accepted (rejected). Thus, **H3**, which states that company size has a positive effect on tax avoidance, is not supported statistically by the results of empirical research.

#### 4.2.3. Determination Coefficient Test Results

Table 4.3 shows the magnitude of the determination coefficient, *adj. R<sup>2</sup>* is 0.093. This *adj. R<sup>2</sup>* value indicates that the independent variables of profitability, leverage, and company size can explain the variance of changes in the tax avoidance variable by 9,3%. In comparison, the remaining 90,7% is influenced by other variables.

Table 4.3 Coefficient test results

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.326 <sup>a</sup>	.2117	.093	.18917

a. Predictors: (Constant), profitability, leverage, company size

### 4.3. Discussion

#### 4.3.1. The Effect of Profitability to the Tax Avoidance

Based on the hypotheses testing results, it is shown that profitability measured by ROA has a positive effect on tax avoidance. These results are following the investigation result conducted by Dewinta et al. (2016). The regression coefficient value of -0.075 and a significance value of 0.000 indicates that ROA has a negative effect on the CETR value. The tax avoidance variable proxied by CETR has an inversely proportional effect. The lower the CETR percentage level indicates the higher the level of corporate tax avoidance (Dyreng et al., 2008).

The company with high profitability will carry out tax planning carefully to estimate an optimal tax expense. Kurniasih et al (2013) state that companies can manage their assets well by finding tax incentives and other tax concessions to optimize tax avoidance. By optimizing the tax avoidance, CETR value will reduce, and the regression test results will have a negative direction. The CETR value is inversely proportional to tax avoidance. The higher the percentage level of CETR, the lower the level of company tax avoidance (Dyreng et al., 2008).

#### 4.3.2. The Effect of Leverage to the Tax Avoidance

It has resulted that the leverage measured by the DAR does not affect tax avoidance. The results of this study are in line with research by Dewinta et al. (2016) and Kurniasih et al. (2013). The various leverage values will not affect and do not have any relationship with the tax avoidance conducted by the company. This is because of the higher debt of the company, and the more conservative the management will be in conducting financial reporting on company operations (Dewinta et al, 2016). The funding with debt describes the tax avoidance activities in a company related to effective tax rates.

In contrast, the tax regulations govern the structure policy in company funding (Gupta and Newberry, 1997). Leverage is a source of external funding. Logically, the higher the value of leverage, the higher the amount of funding from third party debt used by the company, and the higher the interest costs arising from the debt. The higher interest costs will have the effect of reducing the tax expense in a company. The higher the leverage value in a company, the lower its CETR value will be (Lanis and Richardson, 2012).

#### 4.3.3. The Effect of Company Size to the Tax Avoidance

It has resulted that company size does not affect tax avoidance. The size of the company, large or small, does not affect the possibility of the company taking tax action avoidance. The company size does not affect the company in taking tax avoidance since it is related to reputation. In general, a company will always maintain the right name and reputation. The company will not take any action that will cause their reputation to become bad.

According to Badriyah (2017), big companies will be more comfortable to conduct tax avoidance since they have many resources with superior quality compared to small companies. The bigger the company, the more complex the transaction will be. However, in reality, companies cannot always do tax avoidance because it is related to reputation. Watts and Zimmerman (1978) stated that companies cannot always use their power to carry out tax planning because there are limitations in the form of the possibility of being the spotlight and the target of the decision of regulators.

## 5. CONCLUSION

In this study, the relationship between profitability, leverage, company size, and tax avoidance was analysed and formulated by a multiple regression method. From the regression line, it can be concluded that profitability yielded a positive influence on tax avoidance, while leverage and company size did not influence tax avoidance.

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