

THE EFFECT OF EARNINGS MANAGEMENT, LEVERAGE, AND CAPITAL INTENSITY ON TAX AVOIDANCE

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ABSTRACT

The study analyzed companies listed in the LQ45 index (IDX) in the 2021-2023 period, and met the research criteria. A total of 84 samples with three periods of financial statements from 28 companies have been received. Using quantitative methods in research, and multiple regression analysis as an analysis tool. The conclusion of this study is that profit management does not affect tax avoidance. Leverage and Capital Intensity affect tax avoidance.

Keywords: *Manajemen Laba, Leverage, Capital intensity, Tax Avoidance*

INTRODUCTION

The revenue of a country is crucial for financing its needs, which are commonly referred to as state expenditures. These expenditures include infrastructure development, public facilities, employee salaries, subsidies, social assistance, debt payments, and others. Such spending is balanced with state income or revenue derived from various sources, namely tax and non-tax revenues. To date, the tax sector remains the largest contributor to national income. Taxes are essential for the government as they represent funds collected through a systematic process. Taxpayers, both individuals and entities from domestic and international sources, play a critical role in this system. They fulfill their obligations through a self-assessment system, independently calculating, paying, and reporting their tax liabilities, in alignment with the taxation system implemented in Indonesia.

From the government's perspective, the target for revenue growth through the tax sector continues to rise, driving maximum efforts to increase income. However, this perspective contrasts sharply with that of taxpayers, who see no direct benefit from paying taxes. For them, taxes represent mandatory expenditures that reduce profits. Consequently, taxpayers often seek to minimize their tax liabilities. Lawful efforts to reduce taxes are known as tax avoidance, where taxpayers manage taxes within the boundaries of legal regulations. Putra and Merkusivati (2016) argue that tax avoidance can reduce government revenue and national income. To address this, Harnanto (2015), in his book **Tax Planning**, emphasizes the importance of managerial knowledge in tax planning for reducing, saving, and avoiding taxes, achieved legally and without violating regulations.

Earnings management and tax avoidance are two interrelated concepts in accounting and finance. Earnings management involves adjusting a company's financial reports to increase profitability or stabilize income in line with specific objectives, such as attracting investors, boosting share value, or meeting performance targets. On the other hand, tax avoidance refers to minimizing tax liabilities through strategic tax planning within the confines of tax rules. Earnings management is a key tax avoidance strategy, where management may reduce income through accounting mechanisms, resulting in reduced profits and, consequently, lower tax liabilities. Suyanto and Supramono (2012) state that reduced profits lead to reduced tax obligations. However, the practice of earnings management is influenced by government policies on corporate income tax (Badertscher et al., 2009).

Agency theory highlights a conflict of interest between management and shareholders regarding tax avoidance. Management aims to minimize taxes, while shareholders may perceive tax avoidance as potentially altering financial statements, thereby failing to reflect the company's true financial condition (Hariseno & Pujiono, 2021). Furthermore, a company's tax avoidance practices are influenced by its characteristics, such as leverage, size, and capital intensity (Dharma & Ardiana, 2016). Leverage refers to the use of debt in a company's capital structure to enhance shareholder returns. Companies with high leverage often use debt as a primary financing source and may utilize the tax-deductible nature of interest expenses to reduce taxable income. This strategy not only minimizes tax burdens but also ensures liquidity to meet debt obligations.

Capital intensity, or the proportion of fixed assets in a company's total assets, is another characteristic influencing tax strategies.

Companies with high capital intensity often have significant depreciation on fixed assets, which can reduce taxable income. In this context, depreciation serves as a legal strategy to lower tax burdens, demonstrating a potential link between capital intensity and tax avoidance.

Research on the influence of earnings management on tax avoidance is important for understanding how these practices shape a company's financial and tax objectives. Furthermore, studying the impact of capital intensity on tax avoidance behavior clarifies how asset structures influence financial tax strategies. This insight is crucial for financial managers, auditors, and policymakers in formulating effective tax management strategies while ensuring compliance with applicable tax regulations. Previous studies present mixed findings on these

relationships. For instance, Henny (2019) found that leverage positively influences tax avoidance, whereas size, capital intensity, and earnings management do not. Conversely, Ivan Vandi et al. (2000) demonstrated that leverage and profitability influence tax avoidance, while earnings management does not. Other studies, such as those by Abdul Rahman (2001), David Emanuel et al. (2022), and Thalia Renata et al. (2022), suggest that earnings management and leverage have no effect on tax avoidance.

The objectives of this study are to analyze the effects of earnings management, leverage, and capital intensity on tax avoidance. By addressing these objectives, the study seeks to provide valuable insights into corporate tax strategies and their implications for financial and tax management.

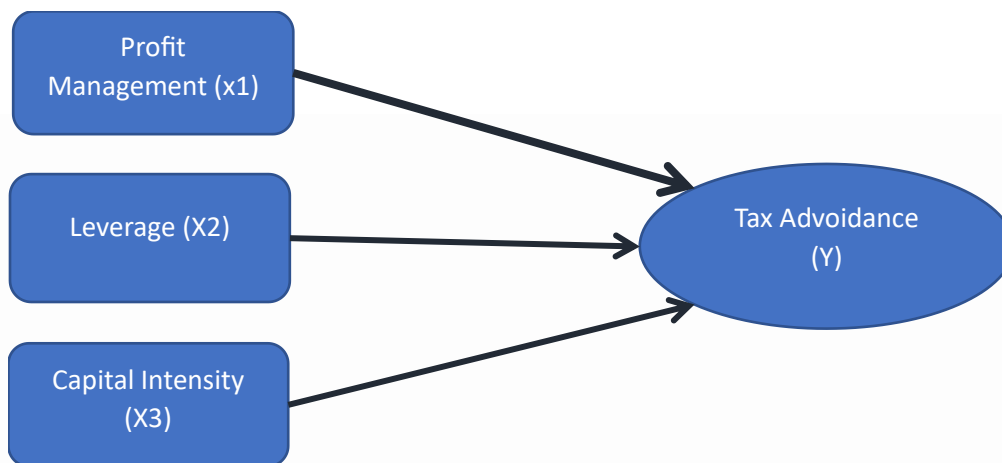


Figure 1. Research Concept Framework

Based on the background, problem formulation, research objectives, theoretical review, and previous studies, the conceptual framework and hypotheses of this study are formulated as follows:

H1: Earnings management has a negative effect on tax avoidance

Previous studies, such as those by Wardani et al. (2019), indicate that earnings management practices influence tax avoidance. Companies engaging in income-decreasing activities for tax aggressiveness, as measured by the effective tax rate, demonstrate that earnings serve as a basis for calculating corporate tax liabilities. As a result, companies may adjust their financial statements to align with their objectives, utilizing accounting choices that reduce earnings as a form of tax avoidance (Suryanto & Supramono, 2012). It can be concluded that the greater the income-decreasing actions undertaken by a company, the higher the indication of tax avoidance.

H2: Leverage has a negative effect on tax avoidance

Previous research by Febrianti and Faisal (2023), as well as Henny (2019) and Hutape et al. (2020), explains that companies with debt can utilize interest expenses on loans as a tax-deductible expense. Therefore, companies with high tax burdens may reduce their tax payments by increasing corporate debt. The higher the leverage, the greater the tax avoidance practices.

H3: Capital intensity has a negative effect on tax avoidance

Corporate fixed assets can be leveraged for tax avoidance through depreciation expenses calculated based on their economic lifespan. Research by Dharma and Ardiana (2016) highlights that capital intensity impacts tax avoidance. The higher the capital intensity, the greater the company's effective tax rate influence on tax avoidance practices.

RESEARCH METHODS

This research is quantitative in nature, as it emphasizes the analysis of numerical data processed using statistical methods. Specifically, it employs multiple regression analysis to determine the extent to which independent variables influence the dependent variable (Ghozali, 2018). The research utilizes secondary data, which consists of time-series information obtained from external sources. This data includes documents and financial reports relevant to the study's subject, focusing on the impact of earnings management, leverage, and capital intensity on tax avoidance.

The population of this study includes companies listed on the Indonesia Stock Exchange (IDX) as part of the LQ45 index. A purposive sampling technique was employed, selecting samples based on predefined criteria. Companies included in the sample were actively trading during the study period, remained in the LQ45 index, did not incur losses over the three-year period (2021–2023), and had complete and audited financial reports. This ensures the sample represents a reliable dataset for analysis.

The study defines its variables through operational definitions to ensure precise measurement. The independent variables (X1, X2, X3) include earnings management (measured using discretionary accruals via the Modified Jones Model), leverage (the ratio of total debt to total assets), and capital intensity (the ratio of fixed assets to total assets). The dependent variable (Y), tax avoidance, is measured using the Effective Tax Rate (ETR), calculated as tax expenses divided by pre-tax income. Data analysis is conducted with SPSS, involving descriptive statistics, classical assumption tests (normality, multicollinearity, heteroscedasticity), and hypothesis testing through multiple linear regression, coefficient of determination (R^2), and F and T tests.

RESULTS AND DISCUSSION

The research population examining the impact of earnings management, leverage, and capital intensity on tax avoidance consists of companies listed in the LQ45 index from 2021 to 2023. The research data were sourced from the Indonesia Stock Exchange (IDX) website (www.idx.co.id) and the official websites of the respective companies. Samples were selected using purposive sampling, based on criteria that included being listed as an active LQ45 member, having no recorded losses during the three-year study period, and possessing complete and audited financial statements for 2021–2023. Following these criteria, 28 companies were selected, resulting in a total of 84 financial reports across three years.

The descriptive statistical analysis aimed to summarize and describe the data collected by examining variables through their mean, minimum, maximum, and standard deviation values (Ghozali, 2009). The analysis confirmed that the dataset comprised 84 valid samples for each variable. This provides an initial overview of the dataset and ensures its adequacy for further statistical tests.

The classical assumption tests included normality, multicollinearity, and heteroscedasticity tests. The Kolmogorov-Smirnov normality test yielded a significance value greater than 0.05, indicating that the data were normally distributed. Multicollinearity tests revealed tolerance values above 0.10 and VIF values below 10, showing no multicollinearity among the independent variables. Finally, the heteroscedasticity test using the Glejser method indicated significance values greater than 0.05 for all independent variables, confirming the absence of heteroscedasticity in the regression model.

Multiple Linear Regression Analysis

The results of multiple linear regression analysis can be seen in the following table

| Coefficients ^a | | | | |
|--------------------------------------|-----------------------------|------------|---------------------------|------|
| Model | Unstandardized Coefficients | | Standardized Coefficients | t |
| | B | Std. Error | Beta | Sig. |
| 1 (Constant) | | | | |
| Profit Management | | | | |
| Leverage | | | | |
| Capital Intensity | | | | |
| a. Dependent Variable: Tax Avoidance | | | | |

From the table above, the form of regression equation in this study is as follows:

$$\text{ETR} = a + \beta_1 \text{EM} + \beta_2 \text{LEV} + \beta_3 \text{CAP} + e$$

$$= 0,32 - 0,235 X_1 - 0,078 X_2 - 0,088 X_3 + e$$

Information :

ETR = *Effective Tax Rate* untuk variabel *Tax Avoidance*

EM = *Earnings Management*

LEV = *Leverage*

CAP = *Capital Intensity*

α = Constant;

$\beta_1, \beta_2, \beta_3$ = Regression coefficients of each independent variable

e = *Error*

From the results of this equation, it can be concluded that the relationship between *tax*

avoidance and all x variables, namely profit management, *leverage* and *capital intensity*, is negative. The higher the value of the variable x, the lower the probability of LQ45 companies committing tax avoidance.

Analysis of the Determination Coefficient Test (R²)

This analysis measures the model's ability to explain the variation of the dependent variable of the determination coefficient (R²) value ranges from 0-1.

| Model Summary | | | | |
|---------------|-------------------|----------|-------------------|----------------------------|
| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
| | .194 ^a | .038 | .002 | .123078 |

a. Predictors: (Constant), Capital Intensity, Manajemen Laba, Leverage

Based on the output table, the summary model shows that the value of the determination coefficient or R square (R²) is 0.038. This value shows that profit management, *leverage* and *capital intensity* have an effect on *tax avoidance* by 3.8%. While the remaining 96.2% is influenced by other variables.

Test Analysis F

The statistical F test aims to show whether all independent variables in the model have a simultaneous influence on the dependent variables. This test is to test the feasibility of the regression model. The basis for decision-making for this test is to use a level of confidence. McSgahane et al. in the journal *Abandon Statistical Significance* (2019) proposed to lower the p value of its role as a threshold filtering tool and use confidence intervals and subordinate factors in the context of their research. Based on this, profit management, *leverage* and *capital intensity* simultaneously have a significant effect on *Tax Avoidance*.

Partial Test Analysis (T-Test)

This test is also known as the partial test, this test aims to find out whether or not the independent variable is significant to the dependent

variable. The decision to reject and accept a hypothesis is a value of level of confidence. The use of the level of confidence level is based on the journal *Abandon Statistical Significance* (2019) by MsSgahane et al. and statisticians such as Harold Hotelling and Ronald Fisher. In the book "Quantitative Methods for Business Research" by Arisyahidin (2023) explains that the level of confidence is the opposite of sig or p value in statistical analysis tools. If the sig is obtained at 0.05, it can be interpreted that the results of the analysis prediction have a probability of error of 5%. Or conversely, have a level of confidence in the prediction results of 95%. If the analysis data is based on secondary data, especially financial data, the potential for a sig below 0.05 is small. The potential of the sig is above 0.05. So that tolerance is accepted or rejected by the hypothesis in magnification, as long as the level of confidence is still above 60%.

Table 2. T Test Results

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| Model | Variable | Coefficient B | Sig | Level Of Confidence | Results |
|-------|-------------------|---------------|------|---------------------|----------|
| | Constant | .322 | .000 | 100% | - |
| | Manajemen Laba | -.235 | .408 | 59.2% | Rejected |
| | Leverage | -.078 | .264 | 73.6% | Accepted |
| | Capital Intensity | -.088 | .130 | 87% | Accepted |

Source : Data Processing Results

CONCLUSION

Based on the research conducted, several conclusions can be drawn. Among the three independent variables studied—earnings management, leverage, and capital intensity—only earnings management was found to have no effect on tax avoidance in LQ45 companies during the 2021–2023 period. The other variables, leverage and capital intensity, have a negative effect, meaning that as leverage and capital intensity increase, tax avoidance decreases.

This study has several limitations. First, the researcher did not include all companies listed on the Indonesia Stock Exchange (IDX). Second, the study only utilized three variables: earnings management, leverage, and capital intensity. These limitations suggest opportunities for future research to explore additional variables and expand the sample scope to provide a more comprehensive understanding of tax avoidance practices.

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