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The Effect of Thin Capitalization, Capital Intensity, Financial Distress and Independent Commissioners on Tax Avoidance

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ABSTRACT : This research aims to analyze whether thin capitalization, capital intensity, financial distress and independent commissioners have an effect on tax avoidance. This research uses a sample of Consumer Goods manufacturing companies listed on the Indonesia Stock Exchange for the 2020-2022 period. The sample selection procedure used purposive sampling. The research used multiple linear regression with SPSS software. Results of research on capital intensity which influences tax avoidance.

KEYWORDS: *thin capitalization*; *capital intensity*; *financial distress*; *independent commissioners*, *tax avoidance*

I. INTRODUCTION

Business has the goal of getting maximum profits. To achieve this goal, companies must pay attention to tax aspects. Tax is an additional burden for companies so that companies can carry out tax saving strategies without violating applicable tax regulations (tax avoidance). Companies try to maximize income after tax (after tax return), because tax is an element of reducing profits that are available to be distributed to shareholders or reinvested(Ilyas, Wirawan B, 2016)

In recent years, the practice of tax avoidance has become a serious problem that threatens tax revenues in many countries. All countries struggle to prevent the erosion of the tax base due to avoidance practices. Tax avoidance is a challenge for every country that is always discussed at meetings of the G-20 Finance Ministers. The realization of state revenue targets from taxes is always not met, as in the picture below:

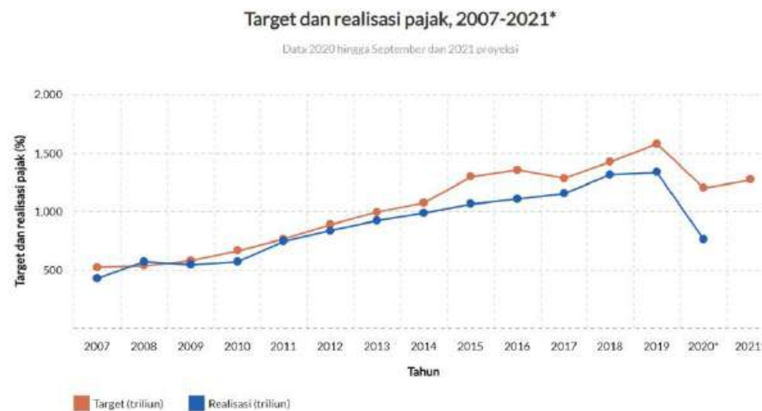

Figure 1. Tax targets and realization

After tax reform in 1983, Indonesia used a self-assessment tax collection system, namely a tax collection system that gives taxpayers the authority to calculate, deposit and report themselves. Indirectly, the self-assessment system is a tax system that is very vulnerable to causing fraud and violations. The Directorate General of Taxes (DJP) carries out priority audits of taxpayers with relatively large tax potential (tax gap) by conducting analysis of financial reports using financial ratios. The impact of the level of tax avoidance carried out by taxpayers is directly proportional to the tax gap that can be secured by the DJP (Rahmana, 2022).

A company's decision to avoid taxes is influenced by many factors, including thin capitalization, capital intensity, financial distress and the role of independent commissioners. Tax avoidance strategies carried out through the feasibility of company financing can be carried out either through debt instruments (debt financing) or through equity (equity financing). Generally, financing for multinational companies comes from

groups of companies (intercompany financing). The development of financing through debt instruments is relatively rapid, which has also encouraged companies to increase the portion of debt in financing which nominally can result in cheaper interest charges. With many affiliates and subsidiaries spread across various countries, there is an opportunity for tax evasion(Waluyo & Doktoralina, 2018).

Tax avoidance is carried out through thin capitalization by using debt instruments for company financing, so that debt is relatively large compared to equity which has an impact on the cost of capital or in a narrow sense the interest burden on loans increases so that profits become small, company taxes become lower. The practice of thin capitalization is able to provide tax incentives for companies through loan interest charges to reduce taxable income(Falbo & Firmansyah, 2019). Research resultsYoshida, (2023),Ravanelly & Soetardjo (2023), Turwanto (2022), thin capitalization has an effect on tax avoidance. In contrast to the results of research Simamora & Sari (2021), thin capitalization has no effect on tax avoidance.

For companies in the manufacturing sector, the role of fixed assets is very important in company operations to produce quality products. Investments in the form of fixed assets (capital intensity) incur depreciation costs. Ownership of fixed assets can reduce the taxes paid by the company due to depreciation costs. In accordance with Article 6 paragraph 1 letter b of Law Number 36 of 2008, depreciation costs are a fiscal cost (deductible expense). The company will increase its investment in the form of fixed assets which will incur large depreciation costs so that the company has to pay less tax. Ownership of fixed assets by a company can incur depreciation costs every year so that companies will try to avoid taxes to reduce the tax rate they have to pay (Anasta & Putranto, 2022). Research results Nadhifah, Mauliddini,Arif (2020), Monika & Noviari (2021) show that capital intensity influences tax avoidance. Meanwhile, researchFaradisty et al.,(2019) found different results.

The economic conditions that occur cause companies to experience financial difficulties which can result in bankruptcy. One way to do this is by implementing cost efficiency, including tax costs. Companies experiencing financial difficulties will be more aggressive in making tax savings by looking for loopholes to minimize the tax burden (Nadhifah, Mauliddini,Arif, 2020). The risk will be greater if corporate taxes become the main burden in cash outflows (Taylor & Richardson, 2013). Research Fadhila & Andayani (2022), Siburian & Siagian (2021), Dhian Mahardhika & Surjandari (2022)shows that financial distress influences tax avoidance. In contrast to the results of research Dhamara & Violita (2018), financial distress has no effect on tax avoidance.

To implement the principles of good corporate governance, Independent Commissioners as members of the Board of Commissioners who come from outside the Issuer or Public Company have the function and responsibility of ensuring that the company complies with the internal control system and applicable laws and values implemented by the company. in carrying out its operations.
Independent Commissioners in companies can provide direction to the company's Directors to manage the company and formulate strategies that the company can implement to make it better, including determining policies regarding tax payments that will be made by the company(Sinurat & Jasman, 2021). Research resultsTaylor & Richardson (2013),Alifianti H. P. & Chariri (2017) show that independent commissioners have an influence on tax avoidance. Meanwhile, the results of research Yulianty et al., (2021) show different results.

The lack of consistency in research results prompted researchers to carry out research again with the title "The Influence of Thin Capitalization, Capital Intensity, Financial Distress and Independent Commissioners on Tax Avoidance" (Empirical Study of Manufacturing Companies listed on the BEI for the 2020-2022 Period). The research objective is to analyze the influence of Thin Capitalization, Capital Intensity, Financial Distress and Independent Commissioners on Tax Avoidance.

II. LITERATURE REVIEW AND HYPOTHESIS

Agency Theory

Agency theory according to Jensen & Meckling (1976)is a contract where one or more people (principals) involve one person (agent) to perform services that are in the interests of the principal in terms of separation of ownership and control of the company. In general, it describes two forms of agency relationships, namely between managers and shareholders (shareholders) and between managers and lenders (bondholders). In this agency theory, it is explained that the relationship between management as agent and the company owner as principal. The principal is the party who gives a mandate to another party, in this case the agent, to carry out all activities on behalf of the principal in his capacity as a decision maker. The company's performance has been achieved by management and has been informed to the owner (principal) in the form of a financial report. Shareholders want management to produce financial reports that benefit shareholders, and management achieves this by managing large revenues while paying the least taxes. In this case, management took various steps to reduce the company's tax burden.

Cost and Benefit Theory

The cost and benefit theory proposed by Dreze & Stern (1987) states about comparing the costs and benefits obtained. Policies will be taken by considering the benefits and costs arising from an action taken. Thus, if tax avoidance provides greater benefits than the costs incurred, the company will tend to avoid taxes.

Tax Avoidance

According to Suandy (2017) tax avoidance is a transaction carried out by minimizing the tax burden by exploiting weaknesses in a country's tax provisions. Meanwhile, according to Pohan (2016), tax avoidance is an effort to avoid taxes that is carried out legally and safely for taxpayers because it does not conflict with tax regulations, because the methods and techniques used tend to take advantage of the weaknesses (gray areas) contained in the tax regulations themselves. to reduce the amount of tax paid.

Based on several definitions of tax avoidance, it is a legal action to reduce the tax burden in accordance with applicable tax provisions by exploiting loopholes that are not regulated in tax laws and regulations. The tax avoidance carried out does not conflict with tax laws and regulations because it takes advantage of loopholes in tax laws which will affect state revenues from the tax sector (Yenni Mangoting, 2000).

Thin Capitalization

Thin capitalization is the formation of a company's capital structure with as much debt contribution and as little capital as possible. Taxes that should belong to one country can be transferred to another country. In financing its subsidiary, a holding company will make a contribution in the form of debt (not capital)(Taylor & Richardson, 2012), stated that the rules regarding thin capitalization differ in each country depending on the needs and policies of that country. Through thin capitalization rules, companies can calculate the maximum amount of interest-bearing debt that is allowed as a deduction from income, which is called "maximum allowable debt"(Falbo & Firmansyah, 2019).The Income Tax Law in Indonesia already regulates thin capitalization, namely in article 18 paragraph (1). This article stipulates that the Minister of Finance has the authority to issue a decision regarding the ratio between a company's debt and capital for the purposes of calculating taxes based on the Income Tax Law.

Capital Intensity

Capital intensity is a form of financial decision. A company's capital intensity measures the amount of capital required to generate revenue. A decrease in fixed assets (sold) or an increase in fixed assets (purchased) can be a source of funding or capital growth. Depreciation occurs on almost all fixed assets, and depreciation expense can lower corporate taxes. The ratio of fixed assets, such as machinery, equipment, and other buildings, to total assets is known as capital intensity. How much of a company's assets are invested in fixed assets is shown by this ratio.

Financial Distress

Financial distress is the stage of decline in financial condition that occurs in a company before bankruptcy or liquidation occurs. A company can be categorized as experiencing financial distress or financial difficulties if the company shows negative numbers in operating profit, net profit and book value of equity and the company carries out a merger. Companies that are in financial distress encourage managers to implement tax avoidance practices (Siburian & Siagian, 2021).

Independent Commissioner

Independent Commissioners are members of the Board of Commissioners who do not own shares, either directly or indirectly, have no affiliated relationships with Securities Companies, with the Board of Directors, other members of the Board of Commissioners and controlling shareholders, and are free from business relationships or other relationships that could affect their ability to act independently.

Independent Commissioners according to the Explanation of Article 120 paragraph (2) of Law Number 40 of 2007 concerning Limited Liability Companies (UUPT) are commissioners from outside parties: Independent Commissioners who are in the good corporate governance guidelines (code of good corporate governance) are " Commissioners from outside parties.” The Company's articles of association may regulate the existence of 1 (one) or more independent commissioners and 1 (one) delegate commissioner. Independent commissioners are appointed based on the decision of the General Meeting of Shareholders ("GMS") from parties who are not affiliated with the main shareholders, members of the Board of Directors and/or other members of the Board of Commissioners.

Hypothesis

1.The Effect of Thin Capitalization on Tax Avoidance

Company financing can be done either with debt (debt financing) or through equity (equity financing). Generally, financing for multinational companies comes from groups of companies (intercompany financing). Thin capitalization uses debt instruments to finance the company, so that debt is relatively large compared to equity which has an impact on the cost of capital or in a narrow sense the interest burden on loans increases so that profits become small, so that company taxes are lower.

Multinational companies tend to provide loans to their subsidiaries or branches, due to the lower tax burden. Apart from that, it is easier to make loans with subsidiaries or company branches. Due to this convenience, multinational companies use debt more often than equity. Companies that avoid tax in the long term have a high level of leverage (Dyreng et al., 2008).

Research results Khomsatun & Martani (2015), Prastiwi & Ratnasari (2019) state that thin capitalization has an effect on tax avoidance.

H1: Thin Capitalization has an effect on Tax Avoidance

2. The Effect of Capital Intensity on Tax Avoidance

Investments in the form of fixed assets (capital intensity) incur depreciation costs. Ownership of fixed assets can reduce the taxes paid by the company due to depreciation costs. In accordance with Article 6 paragraph 1 letter b of Law Number 36 of 2008, depreciation costs are a fiscal cost (deductible expense). The company will increase its investment in the form of fixed assets which will incur large depreciation costs so that the company has to pay less tax. Ownership of fixed assets by a company can incur depreciation costs every year so that companies will try to avoid taxes to reduce the tax rate they have to pay (Anasta & Putranto, 2022). Research results Nadhifah, Mauliddini,Arif (2020), Monika & Noviari (2021)state that capital intensityinfluences tax avoidance.

H2: Capital Intensity influences Tax Avoidance

3. The Effect of Financial Distress on Tax Avoidance

The economic conditions that occur cause companies to experience financial difficulties which can result in bankruptcy. One way to do this is by implementing cost efficiency, including tax costs. Companies experiencing financial difficulties will be more aggressive in making tax savings by looking for loopholes to minimize the tax burden(Nadhifah, Mauliddini,Arif, 2020). The risk will be greater if corporate taxes become the main burden in cash outflows(Taylor & Richardson, 2013). Research Fadhila & Andayani (2022), Siburian & Siagian (2021), Dhian Mahardhika & Surjandari (2022) shows that financial distress influences tax avoidance.

H3: Financial Distress influences Tax Avoidance

4. The influence of independent commissioners on tax avoidance.

As one of the important organs in a Limited Liability Company, the existence of an Independent Commissioner is very important and strategic, because their role as a supervisor is relatively independent compared to other commissioners. An independent position means objectivity in carrying out the supervisory function of policies and operations carried out by the company's Board of Directors. So it is hoped that the company's operations will be in accordance with the directions of the General Meeting of Shareholders (GMS).

Thus, the more effective the function of the Independent Commissioner, the higher the quality of the company's profits due to increased efficiency, including efficiency in taxation. So that the remaining retained earnings (Retained Earnings) or dividends for the benefit of shareholders also increase. Even though tax avoidance does not violate tax regulations. The Independent Commissioner continues to supervise the company in minimizing the tax burden. The greater the number of independent commissioners, the greater the number of people who supervise the company's internal activities. Research Alifianti H. P. & Chariri (2017), Faradisty et al., (2019), independent commissioners influence tax avoidance.

H4: Independent Commissioners influence Tax Avoidance.

III. METHODOLOGY

Population and Sample

Population is a generalized area consisting of objects/subjects that have certain qualities and characteristics determined by the researcher to be studied and then drawn conclusions (Sugiyono, 2013). In this study, the research population is all consumer goods manufacturing companies listed on the Indonesia Stock Exchange (BEI) during the period 2020 to 2022.The sample selection process in this research uses a purposive sampling method. The sample criteria are: manufacturing companies in the consumer goods industry sub-sector that are listed on the Stock Exchange and/or experience delisting and companies that do not experience losses during the 2020-2022 period. And a sample of 72 was obtained. Data processing uses SPSS 25(Ghozali, 2018).

Variable Operations

The independent variables are Thin Capitalization, Capital Intensity, Financial Distress and Independent Commissioner with the dependent variable Tax Avoidance. Tax Avoidance is proxied by CETR, Thin Capitalization usesdebt to equityratio, Capital Intensity is a comparison of fixed assets with total assets, financial distress uses the Z Score and independent commissioners have a large number of independent commissioners divided by the board of commissioners.

IV. RESULT AND DISCUSSION

Classical Assumption Test

By using SPSS software, the classic assumption test is summarized in the table below:

Table 1. Classical Assumption Test

Variable	Normality Test	Multicollinearity Test		Autocorrelation Test	Heterocedasticity Test
		Tolerance	VIF	Durbin Watson	
TC		0.340	2.940		0.095
CI	0.200	0.745	1.342	2.240	0.095
FD		0.342	2.922		0.184
KI		0.965	1.036		0.552

From the results of normality test, it indicates that the significant value of 0.200 is greater than 0.05 so it can be said that the residual data is normally distributed. The VIF value is less than 10 and the tolerance value is greater than 0.1 so there is no multicolonierity between the independent variables in regression model. A sig value greater than 0.05 for all independent variables indicates no heteroscedasticity. While the durbin Watson value of 2.240 does not result in autocorrelation.

Hypotheses Test

The results of hypotheses testing are summarized in table 2

Table 2. Hypotheses Test

Variable	R-Square	F Test	T Test
TC			0.331
CI	0.121	0.014^{b}	0.024
FD			0.492
KI			0.410

Based on the table above, it is known that the coefficient of determination (R-Square) is 0.121 or 12.1%, which means that 12.1% of tax avoidance is explained by the variables such as Thin Capitalization, Capital Intensity, Financial Distress and Independent Commissioners, while the remaining 87.9 % is explained by other factors not contained in the model. The research model with sig. 0.014 below 0.05 means that the model in this study is fit (appropriate) and can be used to predict tax avoidance variables. The results of test indicate that Thin Capitalization (TC) variable have a sig. value of 0.331 greater than 0.05, so hypothesis 1 is rejected, Capital Intensity (CI) variable has a sig. value of 0.024 lower than 0.05, so hypothesis 2 is accepted, Financial Distress (FD) variable has a sig. value of 0.492 higher than 0.05, so hypothesis 3 is rejected, and Independent Commissioners (KI)variable has a sig. value of 0.410 higher than 0.05, so hypothesis 4 is rejected.

Regression equation $TA = 0{,}312 - 0{,}050\ TC - 0{,}166\ CI - 0{,}008\ FD + 0{,}093\ KI + e$

The regression equation explains the constant value of 0.312, it means that if thin capitalization, capital intensity, financial distress and independent commisioners are equal to zero, tax avoidance is 31.2%. Thin capitalization is worth -0.050 which means that every increase in the thin capitalization variable by one unit, tax avoidance will decrease by 0.050 or 5%. Capital intensity is worth -0.166, it means that every increase in the capital intensity variable by one unit, tax avoidance will decrease by 0.165 or 16.5%. Financial Distress is worth -0.008 which means that every increase in the financial distress variable by one unit, tax avoidance will decrease by 0.008 or 0.8%. Independent commisioners is worth 0.093 which means that each increase in the independent commisioners variable by one unit, tax avoidance will increase by 0.093 or 9.3%.

Discussion

1. The Effect of Thin Capitalization on Tax Avoidance

The research results show that Thin Capitalization has no effect on tax avoidance. Thin Capitalization in this research has an effect. The company's financing pattern can be through debt instruments (Debt Financing) or through equity instruments (Equity Financing). The size of the portion of debt or equity instruments really depends on the composition of the company's assets and the return to be obtained. If it is used for long-term investments or those with relatively high risk, the equity portion tends to be larger, but from a tax perspective there are restrictions as regulated in the Regulation of the Minister of Finance of the Republic of Indonesia No. 169/PMK.010/2015 concerning Determining the Amount of Comparison between debt and capital which is also indirectly related to assets. If the average company has a debt portion that exceeds the ratio as regulated by PMK 169, then thin capitalization has no effect on tax avoidance and conversely, if the debt portion or debt instruments are still below the ratio regulated by PMK, then thin capitalization has an effect on tax avoidance. This research is in line with research with research results Simamora & Sari (2021), and is not in line with research results Yoshida (2023), Ravanelly & Soetardjo (2023), Turwanto (2022).

2. The effect of capital intensity on tax avoidance.

Capital Intensity in this research influences tax avoidance. Manufacturing companies generally have a relatively large portion of fixed assets that can be depreciated (Depreciable Assets), such as machines, factory buildings, so that depreciation expenses are also relatively large in the Company's operational expense structure, which has an impact on taxable income and ultimately corporate income tax. relatively small outstanding due to the effect of depreciation charges. Thus, tax avoidance is not a company goal, on the contrary.The results of this study are in line with the results of researchNadhifah, Mauliddini,Arif (2020), Monika & Noviari (2021) show that capital intensity influences tax avoidance. Meanwhile, researchFaradisty et al., (2019)capital intensity has no effect on tax avoidance.

3. The Effect of Financial Distress on Tax Avoidance.

The results of the Financial Distress research have no effect on tax avoidance. The average Z score describes a good position. This means that the company is in a healthy position, especially the EBIT (earnings before interest tax) component. With a relatively large EBIT, the impact on taxable income is large, so the corporate income tax payable is also large, thus providing empirical evidence that financial distress does not have a tax deduction impact.The results of this research are in line with the results of research Dhamara & Violita (2018), not in line with the results of research Fadhila & Andayani (2022), Siburian & Siagian (2021), Dhian Mahardhika & Surjandari (2022)because financial distress has an effect on tax avoidance.

4. Influence of Independent Commissioners on Tax Avoidance

Independent Commissioners in this research have no effect on tax avoidance. An independent commissioner whose main function is to act objectively in carrying out the company's supervisory function. As a public company, issuers strive to increase profits in a sustainable manner, because with increasing profits, share prices will also increase. With increasing profits, taxable income also increases and corporate income tax payable also increases. Independent commissioners cannot influence company policy because they lack competence in their field. The research results are in line with Yulianty et al., (2021), while the results of research Taylor & Richardson (2013),Alifianti H. P. & Chariri (2017)show that independent commissioners have an influence on tax avoidance.

V. CONCLUSION AND SUGGESTION

Conclusion

1. Thin Capitalization has no effect on tax avoidance, because financial expenses can be recognized fiscally (Deductible Expense), so that fiscal profit decreases. In this way, corporate income tax becomes smaller.
2. Capital Intensity influences tax avoidance. The number of fixed assets in the company has an impact on the depreciation expense. Depreciation expense is an expense that can be borne by the company so that the corporate income tax payable is relatively small.
3. Financial Distress has no effect on tax avoidance. A fairly high average z score results in identifying a healthy company so that the company does not have difficulty paying taxes.
4. Independent Commissioners have no effect on tax avoidance. Independent commissioners cannot influence company policy because they only fulfill regulatory demands such as the Limited Liability Company Law.

Suggestions

1. Companies can use a larger portion of fixed assets because the depreciation expense can be financed fiscally.
2. Future researchers are advised to add other variables besides earnings management, institutional ownership and use other proxies for measuring tax avoidance such as Effective Tax Rate, Book Tax Different.

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