CHAPTER II
LITERATURE REVIEW

2.1. Theoretical Framework

2.1.1. Agency Theory

Agency theory is a theory that states the existence of a relationship between the authorized party (principal) and the party receiving the authority (agent) (Ardyansah & Zulaikha, 2014). According to Nugroho (2019), agency theory is a theory that describes the relationship between the principal as the owner and the agent as the company's management. The relationship between the principal and the agent is based on a contract, where the principal chooses the agent to give authority in making decisions and carrying out his duties for the principal's benefit.

Noviatna (2021) in Tavarel & Anggraeni (2021) explained that agency theory describes the conflict between the government as a tax authority (principal) and company management (agent). This is because there are differences in interests where the government as a regulator wants the company to be able to pay as much tax as possible as a source of state income, while the company's management as an agent as much as possible tries to optimize the company's profits and has a low tax burden. This difference in interests motivates agents to carry out tax management.

2.1.2. Tax

A tax is a mandatory contribution to the state-owned by a private person or entity of a coercive nature under the Act, by not getting a direct remuneration and being used for state purposes for the greatest prosperity of the people (Direktorat Jenderal Pajak, n.d.). According to Law No. 28 of 2007 concerning General Provisions and Procedures for Taxation, the tax itself is defined as a mandatory contribution to the state by a person or entity that is coercive under the law, by not getting direct rewarded and used for state purposes for the greatest prosperity of the people. According to Prof. Dr. Rochmat Soemitro, SH explaining tax is a contribution to the State treasury under the statute (which can be imposed) by not

getting lead services (counteraction) that can be directly demonstrated and which is used to pay for general expenses (Resmi, 2019, p. 1). Resmi (2019, p. 3)explained that there are two tax functions, namely:

1. The budgetary function (state financial resources) is a tax that is one of the sources of government revenue to finance both routine and development expenses.
2. The Expenditure Function is a tool to regulate to implement government policies in the social and economic fields and achieve certain goals outside the financial area.

The tax collection system in Indonesia, according to Resmi (2019, pp. 10-11), can is divided into three, which are as follows:

1. The official assessment system is a collection system that authorizes the government to determine taxpayer tax amounts.
2. Self assessment system is a collection system that fully authorizes taxpayers to calculate, calculate, pay, and self-report the amount of tax owed.
3. A withholding System is a collection system that authorizes third parties to determine the amount of tax owed by the taxpayer.

2.1.3. Effective Tax Rate

The effective tax rate (ETR) is a percentage of the effective rate used to calculate taxes borne by taxpayers. The lower the effective tax rate value, the lower the tax burden the taxpayer pays to save on corporate tax payments (Nugroho, 2019). ETR in some Countries is used as one of the indicators to compare the performance of specific industries in tax management. In addition to that, the ETR is generally used to predict what groups of companies or industry categories have the potential to pay significant amounts of taxes to the State (Azura, 2020).

ETR is often used as a reference by decision-makers and interested parties to make policies within the company and contain conclusions about the tax system in the company. This study used ETR as a dependent variable measurement of the ETR. The low effective tax rate indicates that the company is improving at controlling its tax rate level. Suggests that it has been optimal to carry out tax

management without violating applicable tax regulations in Indonesia (Wulandari & Septiari, 2015). On the other hand, if the company has a percentage of the effective tax rate higher than the set rate, the company is less than optimal in maximizing existing tax incentives because by utilizing existing tax incentives, it can reduce the percentage of tax payments from profits.

2.1.4. Tax Management

Tax management is a particular undertaking that a tax manager undertakes in an enterprise (Putra, 2021, p. 46). Wijaya & Murtianingsih (2021) defines tax management as a step or effort of a company or entity that aims to make tax savings but does not conflict with the provisions of tax laws and is legal. The purpose of tax management is that everything related to the taxation of the company can be managed appropriately, efficiently, and economically to make the maximum contribution to the company. According to Putra (2021), the objectives of tax management can be achieved through functions consisting of tax planning, tax implementation, and tax control. According to IAI, tax management is generally defined as a continuous comprehensive effort carried out by taxpayers so that all matters related to tax affairs can be managed properly, economically, effectively, and efficiently to maximize business continuity (Prawati, 2021). In general, the main objectives to be achieved from good tax management are:

1. Minimizing the burden of taxes owed;
2. Maximizing profit after tax;
3. Fulfilling tax obligations following applicable law

According to Putra (2021, p. 48), there are several benefits obtained in tax planning, such as:

1. The tax burden, an element of costs, can be reduced to save cash out.
2. Cash budget preparation can be more accurate.

Tax management is a legal thing to do by the company because this activity follows applicable regulations in Indonesia. A company carries out tax management to minimize its tax burden so that the company is not mistaken in paying taxes. Tax Management is often interpreted as tax avoidance, but tax management is not tax

avoidance because tax management is legal to do so, and there is a governing Law. Tax management is often considered as such because of how taxpayers minimize the tax burden they have to bear, so many people misinterpret tax management.

2.1.5. Company Size

Company size is a measure, scale, or variable that describes the size of a company based on several provisions, such as total assets, market value, shares, total sales, and others. According to Machfoedz (1994), company size is a scale where a large and small company can be classified in various ways (total assets, log size, stock market value, etc.). The size of the company is only divided into three categories, namely large companies (large firms), medium companies (medium-size), and small companies (small firms). The determination of the size of the company is based on total assets. The size of the company can also be used to obtain tax incentives.

2.1.6. Leverage

Leverage is the amount of debt used by a firm to finance its assets. The leverage ratio can describe an ability to meet its long-term obligations. Leverage is often interpreted as the amount of debt used to finance or buy company assets, and the goal is, of course, to maximize business profits, aka return on investment. Funds from debt are used to enlarge the business, such as purchasing tools to increase production, increase the number of workers, or expand the business. That way, the results obtained can be more significant. But the use of leverage also requires some consideration. Leverage is not always profitable. Because the more influential the company uses funds from debt, the greater the risk because the higher the interest that must be paid. Companies with a high Leverage ratio (having large debts) can impact the onset of significant financial risks but also have an excellent opportunity to make high profits. This substantial financial risk arises because the company has to bear or be burdened with hefty interest payments. Conversely, companies with low Leverage ratios have little financial risk but may also have a slight chance of making a significant profit (Azura, 2020).

2.1.7. Profitability

Profitability is the ability of a company to make a profit over a certain period at a certain level of sales, assets and share capital. Companies that can profit must prepare a tax that will be paid on the income earned. Agency theory will spur managers to increase company profits so that the compensation obtained is even greater. Increased profits will lead to an increase in taxes owed. At that time, the owner of the capital who earns a small profit due to the tax paid will pressure the manager to reduce the amount of tax owed (Wijaya & Febrianti, 2017).

2.1.8. Audit Committee

According to the OJK, the Audit Committee is a committee established and responsible to the Board of Commissioners to assist the Board of Commissioners in monitoring and ensuring the effectiveness of the internal control system and the implementation of the duties of internal and independent/external auditors. According to Mayangsari (2004) in Guna & Herawaty (2010), the existence of an Audit Committee in a company serves to assist the Board of Commissioners in supervising the management in the preparation of the company's financial statements. The existence of the Audit Committee is expected to ensure that the transparency of the company's financial statements has met the standards, the application of various principles of internal control, and maintains relationships through effective communication with external auditors.

2.2. Empirical Studies

The previous research used as the basis for this research is shown in the following table.

Table 2. 1

Empirical Studies

No	Author	Research Problem	Research Variable	Research Method	Results
1	Azura (2020)	1. Can the high or low size / total assets owned by the company affect the company in carrying out Tax Management? 2. Can the high or low leverage of the company affect the company in conducting Tax Management? 3. Can the high or low profitability of the company	**Dependent Variable**: Tax Management (ETR) **Independent Variable**: Size, Leverage, Profitability, Inventory Intensity, Fixed	Using the purpose sampling method. This study used Descriptive Statistics, Panel Data Model Selection and Hypothesis Testing.	1. Size has no effect on Tax Management 2. Leverage has no effect on Tax Management 3. Profitability negatively affects Tax Management 4. Inventory intensity has no effect on Tax Management

		affect the company in conducting Tax Management? 4. Can the high or low inventory intensity owned by the company affect the company in conducting Tax Management? 5. Can the high or low of fixed assets owned by the company affect the company in carrying out Tax Management? 6. Can the high or low of the audit committee owned by the company affect the company in conducting Tax Management? 7. Can the high or low ratio of Size, Leverage, Profitability, Inventory Intensity, Fixed Assets and Audit Committee affect Tax Management?	Assets, and Audit Committee		5.Fixed assets have no effect on Tax Management 6.The audit committee has a positive effect on Tax Management. 7.Size, leverage, profitability, inventory intensity, fixed assets, and audit committees have a significant effect simultaneously on Tax Management.

2	Mahdiah, Darmawati, & Kurbani (2021)	Is there any influence of company size, profitability and intensity of fixed assets on tax management with effective tax rate indicators on manufacturing companies listed on the Indonesia Stock Exchange for the period 2016-2018?	**<u>Dependent Variable</u>**: Effective Tax Rate (ETR) **<u>Independent Variable</u>**: Company Size, Profitability (ROA), and Intensity of Fixed Assets.	Sampling in this study using purposive sampling. Data analysis was carried out by classical assumption test, simple linear regression, multiple linear regression analysis test, Correlation Coefficient, Hypothesis Test and Coefficient of Determination.	1. Company size has a significant effect on ETR 2. ROA has no significant effect on ETR 3. Fixed asset intensity significantly affects ETR 4. The size of the company, ROA, and the intensity of fixed assets simultaneously affect the ETR.
3	Ambarukmi & Diana (2017)	1. Does size, leverage, profitability, capital intensity ratio and activity ratio affect the effective tax rate?	**<u>Dependent Variable</u>**: Effective Tax Rate (ETR)	Sample selection using purposive sampling.	1. Size has an insignificant positive effect on the Effective Tax Rate.

		2. Does size affect the effective tax rate? 3. Does leverage affect the effective tax rate? 4. Does profitability affect the effective tax rate? 5. Does the capital intensity ratio affect the effective tax rate? 6. Whether the activity ratio affects the effective tax rate?	**Independent Variable**: Size, Leverage, Profitability, Capital Intensity Ratio, Activity Ratio	Using data analysis methods, namely descriptive statistical analysis, normality test and classical assumptions, regression analysis, hypothesis test.	2. Leverage has an insignificant positive effect on the Effective Tax Rate. 3. Profitability has an insignificant positive effect on the Effective Tax Rate. 4. Capital intensity ratio has an insignificant negative effect on the Effective Tax Rate. 5. The activity ratio has an insignificant negative effect on the Effective Tax Rate.
4	Susilo & Sari (2022)	1. Does leverage, profitability, capital intensity ratio affects the effective tax rate?	**Dependent Variable**:	Using purposive sampling.	1. Leverage affects the effective tax rate.

		2. Is there a simultaneous effect of Leverage, Profitability, Capital Intensity Ratio on the Effective Tax Rate?	Effective Tax Rate (ETR) **Independent Variable**: Leverage, Profitability, Capital Intensity Ratio	This study uses descriptive statistical analysis, classical assumption test, hypothesis test and linear regression analysis	2. Profitability does not affect the effective tax rate. 3. The capital intensity ratio has no effect on the effective tax rate. 4. Leverage, Profitability, and Capital Intensity Ratio can simultaneously affect the effective tax rate.
5	Saragih & Halawa (2022)	1. Does the debt to equity ratio affect the effective tax rate? 2. Does the intensity of fixed assets affect the effective tax rate? 3. Does profitability (ROA) affect the effective tax rate?	**Dependent Variable**: Effective Tax Rate (ETR) **Independent Variable**: Debt to Equity Ratio,	The analysis method of this study uses descriptive statistics, determinant coefficient test, multiple linear	1. The debt to equity ratio has no effect on the effective tax rate. 2. The intensity of fixed assets has a significant negative effect on the effective tax rate.

			Intensity of Fixed Assets, and Profitability.	regression, hypothesis test.	3. Profitability (ROA) has a significant positive effect on effective tax rates.
6	Panda & Nanda (2020)	Do company size, profitability, growth rates and non-debt tax shields in most sectors, and debt ratios, asset tangibility, and corporate age impact ETR differently across sectors?	**<u>Dependent Variable</u>**: Effective Tax Rate (ETR) **<u>Independent Variable</u>**: Firm Size, Profitability, Growth Rate, Financial Leverage, Asset Tangibility, Non-Debt Tax Shields, Interest Coverage Ratio, and Age of The Firms	The study is using Arellano–Bond dynamic panel regression model to identify the key drivers of ETR,	The study concludes that ETRs are significantly explained by company size, profitability, growth rates and non-debt tax shields across most sectors, and debt ratios, asset tangibility, and company age impact differently across sectors. ETR is positively related to the size of the company. Similarly, ETR is negatively related to the

					tangibility of the asset, but responds positively after an immediate shock to it. The determining factor of tax management is profitability, while the level of corporate debt and the intensity of fixed assets have no effect on tax management variables.
7	Wijaya & Murtianingsih (2021)	Is there a determinant of tax management with variables of profitability, debt level and asset intensity in manufacturing companies listed on the Indonesia Stock Exchange for the 2018-2019 period?	**Dependent Variable**: Tax Management **Independent Variable**: Profitability, Corporate Debt,	The sampling technique used is purposive sampling. The research approach uses a quantitative approach.	The factor that is a determinant of tax management is profitability, while the level of the company's debt and the intensity of

			and The Intensity of Fixed Assets	The analysis method in this study aims to test hypotheses with a multiple regression method with a significance level of 5% (0.05).	fixed assets have no influence on variables tax management.
8	Ardyansah & Zulaikha (2014)	Is there an effect of size, leverage, profitability, capital intensity ratio and independent commissioners on the effective tax rate (ETR)?	**<u>Dependent Variable</u>**: Effective Tax Rate (ETR) **<u>Independent Variable</u>**: Size, Leverage, Profitability, Capital Intensity Ratio, and Independent Commissioners	The sampling technique used is purposive sampling. This study used multivariate analysis using multiple regression for hypothesis testing.	1. size has a significant influence on the effective tax rate (ETR) in a negative direction. 2. Leverage does not have a significant effect on the effective tax rate (ETR). 3. Profitability does not have a significant

					effect on the effective tax rate (ETR). 4. The capital intensity ratio does not have a significant effect on the effective tax rate (ETR). 5. Independent commissioners have a significant influence on the effective tax rate (ETR) in a positive direction.
9	Rahmawati, Sumiati, & Zulaihati (2020)	Is there any effect of profitability, capital intensity, company size and leverage on tax management?	**Dependent Variable**: Tax Management **Independent Variable**: Profitability,	Using quantitative methods. This type of research data is secondary data obtained using documentation	1. Profitability no significant effect on tax management 2. Capital intensity has a positive effect on tax management

			Capital Intensity, Firm Size, Leverage	techniques through the company's financial statements with 87 samples. Data analysis techniques use requirement analysis tests, classical assumption tests, multiple regression tests, and hypothesis tests.	3. Firm size no significant effect on tax management 4. Leverage no significant effect on tax management
10	Wijaya & Febrianti (2017)	Is there an effect of size, leverage, profitability, inventory intensity and corporate governance on tax management?	**Dependent Variable**: Tax Management **Independent Variable**: Size, Leverage, Profitability,	The selected population is all companies registered in the period from 2013 to 2015.	1. Size has no effect on tax management. 2. Leverage has no effect on tax management. 3. Profitability has an effect in a negative

			Inventory Intensity, Independent Commissioner	The statistical method used is multiple regression analysis	direction on tax management. 4. Inventory intensity has no effect on tax management. 5. The percentage of independent commissioners has a positive effect on tax management.

2.3. Conceptual Framework and Hypothesis

2.3.1. Conceptual Framework

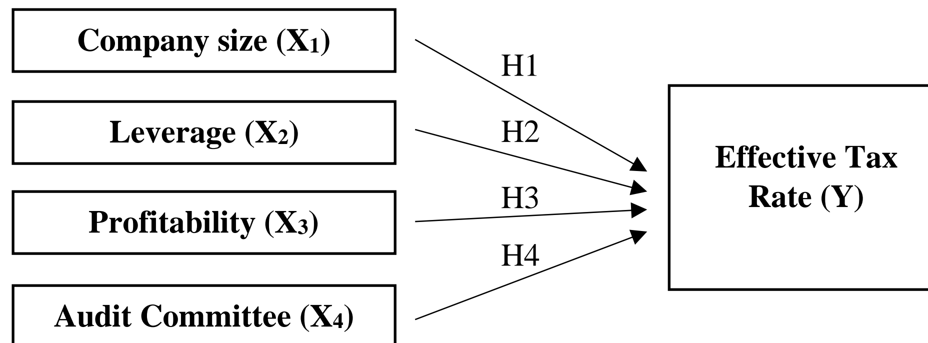

Figure 2. 1

Conceptual Framework

2.3.2. Hypothesis

2.3.2.1. The Effect of Size on Effective Tax Rate

Company size is large-scale small enterprises that can be classified according to various ways. The larger the company, the greater the resources it has to plan its taxes because large companies will receive considerable attention from the government regarding the profits obtained. Hence, they often attract the government's attention to be taxed following the applicable rules (Azura, 2020). Based on agency theory, the resources owned by the company can be used by managers to maximize manager performance compensation, namely by reducing company tax costs to maximize company performance (Imelia, 2015). The greater the assets owned by the company, the more the amount of productivity increases. That will result in an increasing profit and affect the level of tax payments. The larger the size of a company, the tendency of companies to require funds will also be greater than smaller companies, this makes large companies tend to want large incomes.

The research conducted by Nugroho (2019) stated that the size of the company has a significant on the effective tax rate. The size of the enterprise has a negative direction on the regression coefficient. Based on the explanations and

theories from previous studies, the following hypotheses in this study were proposed:

H_1: There is significant effect of company size on ETR

2.3.2.2. The Effect of Leverage on Effective Tax Rate

According to Putri (2016), leverage is the use of assets and sources of funds by companies with fixed costs (expenses) to increase company profits. More debt has lower ETR since interest payments might cut their pre-tax profits by Liu and Cao (2007) in Ardyansah & Zulaikha (2014). Proportion of long-term debt and capital, companies that have a larger proportion of long-term debt and capital, will have a smaller ETR. This is due to the effect of the cost of paying interest on loans that can be used as a deduction fee in determining the company's taxable income.

According research by Ardyansah & Zulaikha (2014) that leverage does not significantly influence the ETR. Meanwhile, this is not in line with the research conducted by Susilo & Sari (2022) that leverage significant effect on ETR. From the statement above, the second hypothesis is:

H_2: There is significant effect of leverage on ETR

2.3.2.3. The Effect of Profitability on Effective Tax Rate

Profitability is the ability of a company to make a profit over a certain period at a certain level of sales, assets and share capital. Profitability measured using Return on Assets (ROA) is an indicator that reflects the company's financial performance, the higher the ROA value, the better the performance of a company (Susilowati, Widyawati, & Nuraini, 2018). The existence of agency theory will spur managers to increase company profits. When the profit earned is enlarged, the amount of income tax will automatically increase following the increase in the company's profit. Profitability is one of the determining factors of the tax burden, because companies that have a large profit will pay taxes every year. Meanwhile, companies that have a low level of profit or even suffer losses will pay less or no taxes. In addition, by using loss compensation, the company can reduce the obligation to pay taxes for the previous or subsequent financial year. Profitability

is the ability of an enterprise to obtain or make a profit from the activities of an enterprise. Profitability is not only used to measure the company's ability to make a profit, but also to find out how far the effectiveness of the company's management is in managing the assets owned by the company. According to Sjahril, Yasa, & Dewi (2020) that profitability has significant effect on ETR. The third hypothesis derived from the statement is:

H_3: There is significant effect of profitability on ETR

2.3.2.4. The Effect of Audit Committee on Effective Tax Rate

The Board of Commissioners established the Audit Committee to help carry out its duties and functions, such as assisting the Board of Commissioners in providing professional opinions to improve the company's good performance. Of course, the company is also expected to carry out effective tax management (Azura, 2020). Investors consider that the existence of an audit committee is an added value for a company that has implemented GCG Refassy (2017). The existence of an audit committee will provide supervision carried out on a company's management so that it can produce quality information and effective performance. With the increasing number of audit committee members, it is expected that can carry out supervision that makes management in a company more careful to make decisions, including in terms of tax evasion. According to Yensi & Sandra (2019) research, the audit committee has significant impact on ETR. States that with the increasing number of audit committees, it is hoped that the audit committee can play an effective role as a supervisor in a company to be careful in making company decisions and policies, including tax evasion. From the statement above, the fourth hypothesis is:

H_4: There is significant effect of audit committee on ETR

CHAPTER III
RESEARCH METHODS

3.1. Research Type

This research will use quantitative research. This strategy focuses on analyzing and quantifying the variable to produce outcomes. Variables are processed using numbers, then analyzed and implemented with statistical procedures. This research also emphasizes testing theories with variables as gauges in the study.

3.2. Data

3.2.1. Data Type

The data sources in this study used secondary data. Secondary data is previously available data collected from indirect or second-hand sources e.g. from written sources belonging to the government or libraries. (Hardani, et al., 2020). This study also used quantitative data. Quantitative data is research data in the form of numbers, statistical data and data can be analysed. In this study, the data collected was taken from the official website of the IDX and from the company's website.

3.2.2. Data Sources

The data source used in this study is the annual financial report data of Manufacturing Companies listed on the Indonesia Stock Exchange (IDX) or from 2017-2021 or www.idx.co.id; other websites researchers use www.sahamok.net and www.eddyelly.com.

3.2.3. Data Collection

Data Collection techniques used in this research use documentation studies by collecting and studying the necessary documents and data. The data in question is the data on the annual financial statements of manufacturing companies listed on the Indonesia Stock Exchange that have been selected following specified criteria.