www.birci-journal.com/index.php/birci
Budapest International Research and Critics Institute-Journal (BIRCI-Journal)
Humanities and Social Sciences
ISSN 2615-3076 Online)
ISSN 2615-1715 (Print)
Budapest Institute

# The Influence of Capital Intensity, Political Cost, and Financial Distress on Tax Avoidance in Coal Mining Companies in Indonesia 2014-2020

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**Abstract**

*This study aims to determine the effect of capital intensity, political cost, and financial distress on tax avoidance in companies listed on the Indonesia Stock Exchange. This study uses a samples of mining companies in the mining coal sector who listed on the IDX during the 2014-2020 period. The data in this research are secondary data obtained fromwww.idx.co.id, datacollection techniques using purposive sampling method, then processed in Eviews 10. In analyzing the data, the researcher conducts descriptive statistics techniques, classical assumption tests, multiple linear regression, and hypothesis testing. Based on the results of hypothesis testing, it was found that capital intensity has negative influence on tax avoidance, political cost has no influence on tax avoidance, and financial distress has positive influence on tax avoidance.*

Keywords
capital intensity; political costs; financial distress; tax avoidance

## I. Introduction

Tax is a mandatory contribution to the state that is owed by an individual or entity that is coercive under the law, without receiving direct compensation and is used for the needs of the state for the greatest prosperity of the people as stipulated in Law Number 28 of 2007 Article 1 paragraph (1) (Law, 2007). Because of the nature of the tax, the government regulates tax collection through law in order to have legal certainty.

Taxes for Indonesia are the main source of state revenue. Taxes are often interpreted as a good and reliable source of state financing for uses from routine state expenditures to state development (Indopajak.id, 2021). So the proportion of state tax revenue is the majority.

**Table 1.** Percentage of Total Domestic Tax on State Expenditure 2013-2019

| | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|---|---|---|---|---|---|---|---|
| Percentage | 62.39% | 62.08% | 66.73% | 67.02% | 64.98% | 66.55% | 70.82% |

*Source: Data processed from the Central Statistics Agency (2021)*

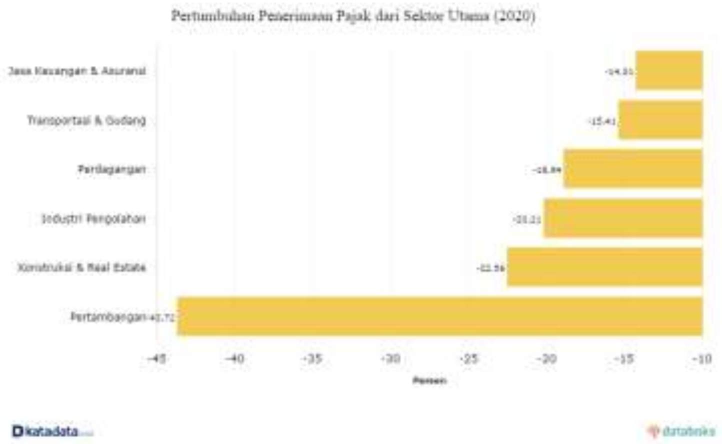
In the table above, it can be seen that the data published by the Central Statistics Agency (2022) to date has a very high percentage of total domestic taxes on state spending. In fact, in 2019 it became the highest percentage gain of 70.82%. While the lowest was 62.08% in 2014 due to economic contraction. So that the average tax contribution to the State Budget (APBN) is 65.80% annually.

Minister of Finance Sri Mulyani said that in 2020 tax growth declined. As reflected in the graph below:



**DOI:** https://doi.org/10.33258/birci.v5i3.6478

*Budapest International Research and Critics Institute-Journal (BIRCI-Journal)*
*Volume 5, No 3, August 2022, Page: 24547-24558*
*e-ISSN: 2615-3076 (Online), p-ISSN: 2615-1715 (Print)*
*www.bircu-journal.com/index.php/birci*
*email: birci.journal@gmail.com*




*Source: Data Word (2022)*
***Figure 1.*** *Tax Revenue Growth from Key Sectors (2020)*

Based on the graph above, tax revenues in 2020 from the 5 main sectors all experienced a fairly deep correction. The highest correction was in the mining sector by -42.7%. Meanwhile, the lowest correction was -14.31% in the financial services and insurance sectors. This is due to the Corona Virus Disease (COVID-19) pandemic throughout the world which has made the economy, including Indonesia, experience contraction and the disbursement of various tax incentives (Republika, 2022).

In 2021, after the company is able to adapt in the midst of the existing conditions, the growth of tax revenue will increase again. Although the mining sector experienced the deepest contraction in the previous year, in 2021 it grew by 38.4% (Data said, 2022).

The growth of state revenue is highly reliable in the post-pandemic National Economic Recovery (PEN). However, tax collection is not easy in the implementation process, especially in the limited conditions after COVID-19. Although taxes are the main source of income for the state, this is in contrast to companies that recognize taxes as a burden (Suheri, Fitriyani, & Setiawan, 2020). Because many taxpayers assume that the obligation to pay taxes is a burden, so they are reluctant to pay taxes which ultimately tends to do tax avoidance (Leung, Leung, Richardson, & Taylor, 2018). In the end, many companies as taxpayers make strategies to keep complying with their tax obligations but can minimize the tax burden they owe. The economic condition of the population is a condition that describes human life that has economic score (Shah et al, 2020). Economic growth is still an important goal in a country's economy, especially for developing countries like Indonesia (Magdalena and Suhatman, 2020).

One of the phenomena of tax avoidance by one of the largest coal mining companies in Indonesia is PT Adaro Energy Tbk. Global Witness (2019) released its report entitled "Adaro Energy, one of Indonesia's largest coal companies, has been moving vast amounts of profit from coal mined in Indonesia to its growing offshore network, raising the question of whether the network helps Adaro avoid or minimize tax in Indonesia.".

The report revealed that from 2009 to 2017 the arrangement of PT Adaro Energy Tbk with its subsidiary in Singapore, Coaltrade Services International, could allow for the potential to pay taxes of US$ 125 million. The report also shows that the role of the tax heaven country in tax avoidance by PT Adaro Energy Tbk can reduce its tax bill of US$ 14 million annually. Various kinds of tax avoidance schemes may be carried out by the company.

Companies are looking for ways to minimize their tax burden, one of which is accounting and investment policies. This is related to capital intensity. Where the company invests more of its capital in the form of assets. This resulted in a high depreciation expense on large asset holdings. Moreover, mining companies need a lot of infrastructure to increase their productivity. So that the company can determine its accounting policy to take advantage of the depreciation expense attached to the asset to minimize its tax burden. Supported by research results (Saputra, Suwandi, & Suhartono, 2020) capital intensity has a negative effect on tax avoidance.

However, this is not in line with several studies including Noor, Fadzillah, & Mastuki (2010), Maulana, Marwa, & Wahdyudi (2018), Nadhifah & Arif (2020), showing the results that capital intensity is a scheme that companies can use to reduce their income tax. Furthermore, political costs can also be used by companies in the context of tax avoidance. According to Watts & Zimmerman (1990) that the burden of antitrust, regulations, government subsidies, taxes, labor demands and so on is a political cost that must be borne by the company. The wealth transfer process is based on the company's profits disclosed in the company's financial statements. So that the political cost paid by the company is related to the size of the company (Novita, 2016).

In line with research conducted by Richardson, Taylor, & Lanis (2013), Swingly & I MS (2015), Widiasmara, Novitasari, & Hasanah (2018), Mailia & Apollo (2020) that the larger the size of the company will provide motivation to do business. more policies that can lead to lower profits in order to reduce political costs. This is due to the opinion that the size of the company is a benchmark for its ability to fulfill its obligations, including transferring wealth (Permatasari, Aziz, & Siswantini, 2021).

Several previous studies have also linked the financial condition of companies with tax avoidance (Puspita & Ismail, 2017). The company's financial ability also provides motivation to do tax avoidance. Like when the company is in financial distress. Therefore, companies must have the ability to analyze financial statements. So that companies can avoid losses and bankruptcy, as well as assess the company's policies and directions to support sustainable business processes (Muttaqin & Husen, 2020). For example, research conducted by Mailia & Apollo (2020) shows that financial distress has an effect on tax avoidance. However, different results are shown in the results of research conducted by Christin & Triyani (2019) and Valensia &

Based on the background described above, the formulation of the problem in this research is whether capital intensity, political cost, and financial distress affect tax avoidance?

## II. Review of Literature

### 2.1 Agency Theory

*Agency theory*focuses on two parties, namely the principal and the agent. Jensen & Meckling (1976) in their research, states that the agency theory describes each party wanting the maximum interest for both of them. Because of this, a conflict arises between the agent and the principal which is called the agency problem (Panda & Leepsa, 2017). Agency problems are universal. In this study a form of fraud committed by the agent (company), where there is a discrepancy between the agreement or contract agreed upon with the principle (government). Because the tax system used in Indonesia is a self-assessment system, which gives companies the authority to calculate, pay and report their own taxes (Directorate General of Taxes, 2022). So that the agent has the opportunity to do tax avoidance, that way, the company hopes that the tax burden paid is lower than it should be. The scheme used by agents to practice tax avoidance in this study is capital intensity and political cost.

### 2.2 Positive Accounting Theory

*Positive accounting theory*explains that companies can choose to use accounting policies that benefit the company under certain conditions (Trisnawati, Wiyadi, & Sasongko, 2012). At least, the profit the company means is to minimize the tax burden that must be incurred, so that the company can optimally record its net profit (Chaezahranni, 2016). As a result, companies tend to do tax avoidance by using accounting policies to minimize their tax burden. In this study, tax avoidance is carried out through a capital intensity, political cost scheme, and data on financial distress occurs while taking into account generally accepted accounting policies.

### 2.3 Signal Theory

*Signaling theory*provide an explanation of how the company acts in conveying its information. The message conveyed by the company is in the form of information about how the company's prospects will be in the future (Brigham & Houaton, 2001). The signals conveyed by the company will affect customers, and in turn will provide feedback through their perceptions and the resulting behavior (Kharouf, Lund, Krallman, & Pulling, 2019). In this study, the company's financial distress can be reflected in the financial statements which will be a signal for users. In addition, tax avoidance measures are also expected to increase the company's ability to withstand bad news.

### 2.4 Tax Avoidance

*Tax avoidance*or tax avoidance according to the Organization for Economic Cooperation and Development (OECD) (1987) is a form of taxpayer effort to reduce the tax payable. Tax avoidance is considered a legal tax planning effort because it utilizes "loopholes" that exist in applicable tax regulations (lafwull) (Santoso & Rahayu, 2019). Companies that are able to minimize their tax payments, the more the burden incurred by the company. Because the tax burden is calculated from net income earned in the current year. So that by minimizing the tax burden, the company can book its net profit optimally and inform good financial performance.

### 2.5 Capital Intensity

*Capital intensity*or capital intensity is a fixed asset that comes from the company itself as a form of investment (Widagdo, Kalbuana, & Yanti, 2020). This shows that capital intensity can be defined as how much the company invests its capital in the form of assets. Capital intensity is often seen from the ratio of total assets or fixed assets to sales or labor input (Lee & Xiao, 2011). When comparing the investment in a company's physical assets to its sales, the resulting ratio reflects the efficiency of the company in utilizing physical assets to generate sales.

### 2.6 Political Cost

*Political cost*or political costsaccording to Watts & Zimmerman (1990) is closely related to the size and transfer of wealth. The value transferred for political costs is usually determined by the size of the company. So that large companies will incur greater political costs than small companies. Companies incur political costs to maintain good relations with the government and politicians (Wang, Wilson, Zhang, & Zou, 2021). This tends to be used by companies to carry out tax avoidance. The goal is for companies to minimize the tax burden incurred without being subject to additional political costs.

### 2.7 Financial Distress

*Financial distress*or financial difficulties is a company condition that is not only limited to when it is declared bankrupt, but also when it is unable to fulfill its obligations (Permatasari, Aziz, & Siswantini, 2021). When a company experiences financial distress, the priority is to relieve financial pressure and shareholder interests (Wu, Shao, Yang, Ding, & Zhang, 2020). So, the company tends to do tax avoidance in order to achieve these interests. The company will try to minimize the tax burden it owes in order to maintain cash flow. Then the company also maintains its financial performance for the benefit of shareholders.

### 2.8 Hypothesis Formulation

#### a. Effect of Capital Intensity on Tax Avoidance

*Capital intensity*proxied in a ratio that reflects the company invests more of its capital in assets. Judging from the ratio of total assets to total sales. Companies with a high proportion of investment in assets tend not to need to do tax avoidance because high asset ownership can result in a decrease in tax burden and optimize bookable net income. The research of Saputra, Suwandi, & Suhartono (2020) supports the results that capital intensity has a negative effect on tax avoidance.

H1: Capital Intensity has a negative effect on Tax Avoidance

#### b. The Effect of Political Cost on Tax Avoidance

*Political cost*proxied by firm size. Permatasari, Aziz, & Siswantini (2021) state that wealth transfer is measured based on the ability to fulfill its obligations. The larger the size of the company will provide motivation to carry out more policies that can lead to decreased profits in order to reduce political costs. This is in line with research conducted by Richardson, Taylor, & Lanis (2013), Swingly & I MS (2015), Widiasmara, Novitasari, & Hasanah (2018), and Mailia & Apollo (2020) that political cost affects tax avoidance.

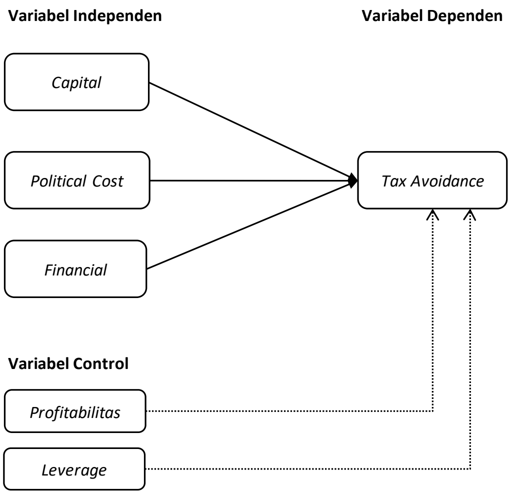
H2: Political Cost has a positive effect on Tax Avoidance

#### c. Effect of Financial Distress on Tax Avoidance

*Financial distress*is a condition of a company experiencing a decline in economic capacity. The company will take various ways in order to improve and polish the company's capabilities so that it continues to give a good signal to creditors or investors. In order to reduce costs that are deemed unimportant, such as the income tax burden, the greater the possibility of the company doing tax avoidance. This is supported by research by Valensia & Khairani (2019) and Muttaqin & Husen (2020) which show that financial distress has an effect on tax avoidance.

H3: Financial Distress has a negative effect on Tax Avoidance

### 2.9 Framework




## III. Research Method

This research uses descriptive quantitative method. The variables studied consisted of independent variables, namely capital intensity, political cost, and financial distress and the dependent variable was tax avoidance. The object of research is a coal sub-sector mining company listed on the Indonesia Stock Exchange (IDX) in the period 2014 to 2020 which is determined by the purposive sampling method, namely sampling based on certain criteria.

The data used are secondary data sourced from financial reports obtained from the company's official website and the Indonesia Stock Exchange. The analytical technique used to examine the variables above is with multiple regression analysis of balance panel data through the help of the Eviews 10 application. The analysis stages consist of model estimation which is carried out by the Chow Test, Hausman Test and Langrangge Multiplier Test which is interpreted through hypothesis testing (Hypothesis Testing) in the form of Coefficient of Determination Test (r2), Simultaneous Test (F Statistics Test) and Individual Parameter Significant Test (t Statistical Test). Then to determine the decisions taken, namely with a tolerance level of 5%.

### 3.1 Independent Variable

The independent variables used in this study are:

### a. Capital Intensity

*Capital intensity*In this study, it will be proxied using the fixed asset intensity ratio in the form of a comparison of fixed assets to the total assets of a company. This ratio can describe the ratio or proportion of the company's fixed assets from the total assets owned by a company. The fixed asset intensity ratio according to Lee & Xiao (2011) is measured using the following formula:

$$Capital\ Intensity = \frac{Total\ Assets}{Total\ Sales}$$

### b. Political Cost

*Political cost*In this study, it is proxied using the natural logarithm of company size, namely total assets. Because the amount of wealth transferred for political costs usually reflects the size of the company. This proxy refers to the research of Widiasmara, Novitasari, & Hasanah (2018) with the following formula:

$$Political\ Cost = Ln(Total\ Assets)$$

### c. Financial Distress

*Financial distress*measured using the springate method which refers to researchChristin & Triyani (2019). Where the value of financial distress is obtained from the following formula:

$$Financial\ Distress = X1 + X2 + X3 + X4$$

Note:
- X1 = Working capital divided by Total Assets
- X2 = Earning Before Interest and Taxes divided by Total Assets
- X3 = Earning Before Taxes divided by Current Liabilities
- X4 = Sales divided by Total Assets

### 3.2 Dependent Variable

The dependent variable in this study is tax avoidance which is measured using the Effective Tax Rate proxy which refers to the research of Widiasmara, Novitasari, & Hasanah (2018) with the following formula:

$$Effective\ Tax\ Rate = \frac{Tax\ Expense}{Earning\ Before\ Tax}$$

## IV. Result and Discussion

### 4.1 Data Description

This study uses 17 companies that have met the sample criteria with a total of 119 financial statements as shown in the following table:

**Table 2.** Sample Observation Results

| No | Information | Amount |
|---|---|---|
| 1. | Number of coal mining companies listed on the Indonesia Stock Exchange during 2014-2020 | 28 |
| 2. | Newly listed companies in 2014-2020 | 6 |
| 3. | Companies that were delisted between 2014-2020 | 5 |
| | Number of companies that meet the criteria | 17 |
| | Year of Observation | 7 |
| | Number of companies studied in 2014-2020 | 119 |

*Source: Processed data (2022)*

### 4.2 Descriptive Statistical Analysis

The table below describes the descriptive statistics in this study:

**Table 3.** Descriptive statistics

| | TA | CI | PC | FD |
|---|---|---|---|---|
| mean | 0.263600 | 1999506 | 2,636,590 | 1217749 |
| Maximum | 0.952841 | 9173371 | 3,215,626 | 7420856 |
| Minimum | -0.502829 | 0.498203 | 1,279,608 | -4099458 |
| Std. Dev. | 0.239024 | 1833675 | 5,252,903 | 7741364 |

*Source: Data Processed Eviews 10 (2022)*

Based on the table above, the results of descriptive statistical tests with observations of 119 data, the tax avoidance variable has a minimum value of -0.502829 at PT Bumi Resources Tbk. While the maximum value at PT Darma Henwa Tbk is 0.952841. The mean of the research data is 0.263600. While for the capital intensity variable, the mean value is 1999506. So, it can be concluded that most companies are indicated to practice capital intensity, with a maximum value of 9173371 at PT Atlas Resources Tbk and a minimum value of 0.498203 at PT Mitrabara Adiperdana Tbk.

The political cost mean variable is 2,636,590. This defines most companies have large asset values. Then the maximum value obtained is 3,215,626 at PT Adaro Energy Tbk with a minimum at PT Atlas Resources Tbk worth 1,279,608. Financial distress has a mean value of 1217749 with a maximum value obtained by PT Darma Henwa Tbk of 7420856, and a minimum value of -4,099,458 at PT Borneo Olah Sarana Sukses.

**Table 4.** Frequency

| Description | Frequency | Percent |
|---|---|---|
| Maximum | 3,215,626 | 7,420.856 |
| Minimum | 1,279,608 | -4,099,458 |
| Total | 5,252,903 | 7.740.149 |

*Source: Data Processed Eviews 10 (2022)*

## 4.3 Panel Effect Test

**Table 5.** Chow test

| ***Effects Test*** | **Prob.** | ***Conclusion*** |
|---|---|---|
| Cross-section F | 0.2752 | H0 Accepted |

*Source: Data Processed Eviews 10 (2022)*

Based on the results of the Chow test in table 4 shows that the probability value of the cross-section F is 0.2752 > 0.1 (alpha 10%) thenH0 is accepted or selected Common Effect Model. So that the test is continued with the Langrangge Multiplier test.

**Table 6.** Langrangge Multiplier Test

| ***Effects Test*** | **Prob.** | ***Conclusion*** |
|---|---|---|
| Breusch-Pagan | 0.9101 | H0 Accepted |

*Source: Data Processed Eviews 10 (2022)*

Test results*Langrangge Multiplier*which is shown in table 4 that the Breusch-Pagan value is 0.9101 > 0.1 (alpha 10%) thenH0 is accepted, so it can be concluded that the best model in this study is the comment effect model.

### 4.4 Hypothesis test

**Table 7.** Hypothesis testing

| *Variable* | *Direction* | *Coefficient* | *Prob.* | *Conclusion* |
|---|---|---|---|---|
| **C** | Positive | 0.224530 | 0.0166 | |
| **CI** | Negative | -0.022317 | 0.0227 | H1 accepted |
| **PC** | Positive | 0.004209 | 0.2141 | H2 rejected |
| **FD** | Positive | 0.000382 | 0.0980 | H3 accepted |
| **Adj R2** | | 0.055648 | | |
| **Prob F-statistics** | | 0.022423 | | |

*Source: Data Processed Eviews 10 (2022)*
*Description: Significance Level 10%*

Based on the table above, the regression model in this study is:

**CTAit =0.0166 - 0.022317CIit +0.004209 PCit + 0.000382 FDit**

The regression coefficient in Table 7 shows the Adjusted R-Square (R2) value of 0.055648, meaning that the variables of capital intensity, political cost, and financial distress are only able to explain tax avoidance of 5.6%. While the remaining 94.4% explained other independent variables that were not used in this study. Then, the F-statistic probability value of 0.022423 < 0.1 (alpha 10%) explains that the independent variables used simultaneously or jointly affect tax avoidance.

### 4.5 Discussion of Research Results

#### a. Capital IntensityNegative Effect on Tax Avoidance

Based on the test results, the coefficient is -0.022317 with a significance of 0.0227 <0.1 (alpha 10%). That is, statistically it can be concluded that at the 90% confidence level, there is a negative effect of capital intensity on tax avoidance so that H1 is accepted. So it shows that companies that have implemented accounting and investment policies with a larger proportion of assets tend not to do tax avoidance. This is because the greater the company's assets, the higher the depreciation expense which results in lower income taxes payable. The results of this study are supported bySaputra, Kelvin, & Suhartono (2020). However, this is not in line with previous research conducted byNoor, Fadzillah, & Mastuki (2010), Maulana, Marwa, & Wahdyudi (2018), and Nadhifah & Arif (2020).

#### b. Political CostPositive Effect on Tax Avoidance

Based on the test results, the coefficient value is 0.004209 with a significance of 0.2141 > 0.1 (alpha 10%) so that H2 is rejected. The results of this study are not in line withRichardson, Taylor, & Lanis (2013), Swingly & I MS (2015), Widiasmara, Novitasari, & Hasanah (2018), and Mailia & Apollo (2020).

#### c. Financial DistressPositive Effect on Tax Avoidance

Based on the test results, the coefficient is 0.000382 with a significance of 0.0980 <0.1 (alpha 10%). That is, statistically it can be concluded that at the 90% confidence level, there is a positive effect of financial distress on tax avoidance so that H3 is accepted. In line with research resultsValensia & Khairani (2019) and Muttaqin & Husen (2020), but different from Christin & Triyani (2019). In conditions of difficult financial capacity, companies need to maintain cash flow for the sustainability of their business and the interests of shareholders. This is important for the company to maintain its financial performance. So the company does tax avoidance in order to minimize its tax burden.

## V. Conclusion

Based on the results of the analysis and discussion, it can be concluded that capital intensity, political cost, and financial distress simultaneously affect tax avoidance. Capital intensity has a negative effect on tax avoidance. Meanwhile, political cost has no effect on tax avoidance. Then financial distress has a positive effect on tax avoidance.

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