

# TAX AVOIDANCE OF COAL MINING COMPANIES IN INDONESIA

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**Abstract:** The objective of this research was to determine the impact of transfer pricing, yield management, thin capitalization, and hedging on tax avoidance. Tax avoidance refers to the legal framework for transactions that obtain tax benefits or relief by exploiting existing tax loopholes to minimize or avoid paying taxes owed. This research applied descriptive and quantitative methods. The population of this research consisted of coal mining companies listed on the Indonesian Stock Exchange between 2015 and 2019. Using targeted sampling techniques, the sample was drawn from 16 companies that met the research criteria. The statistical program Eviews12 was used to process the data. Transfer pricing, earning management, or hedging had no significant effect on tax avoidance. Simultaneously, thin capitalization had a significant effect on tax avoidance.

**Keywords:** Transfer Pricing, Earning Management, Thin Capitalization, Hedging, and Tax Avoidance.

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## INTRODUCTION

Tax avoidance is a business practiced to keep taxpayers free of taxation while posing no risk to the taxpayers themselves because it follows tax regulations (Pohan, 2014). Furthermore, (Sari, 2013) states that tax avoidance is used before the issuance of a tax assessment letter (SKP), and taxpayers do not openly violate the law, even though they sometimes explicitly assess the law as being contrary to what the lawmaker intended. 2016 (Mardiasmo) Tax avoidance is a method of lowering one's tax burden without breaking the law.

Google is an example of a high-profile case of tax avoidance in Indonesia. According to tax observer Danny Darussalam, as quoted by detik.com, Google purposefully did not establish a Permanent Business Entity (BUT) because it did not want to be subject to income tax in Indonesia. According to the media Tirto, Adaro diverted income and profits overseas to reduce the amount of taxes owed in Indonesia. According to Global Witness, Adaro used this method by selling new coal bricks at a low price to Coaltrade Services International in Singapore, where they were resold at a high price. Furthermore, Global Witness discovered Adaro evading US\$125 million in taxes owed to the Indonesian government.

Furthermore, in 2010, Indonesia Corruption Watch reported fraudulent sales by three Bakrie Group coal companies. (Olivia & Dwimulyani, 2019) discovered that coal companies used thin capitalization to minimize capital. Even in various conditions, some companies have negative equity due to the erosion of

company losses over time. PT Bumi Resources Tbk is aware of this (BUMI). According to (Zherniansyah, 2013), companies that use coal in their business processes understandably want to manage the risk of fluctuating coal prices.

Previous research on the variables mentioned above, such as (Amidu et al., 2019), indicates that transfer pricing and earnings management have an impact on tax avoidance in Ghana. Wang Chen (2012) demonstrates that tax avoidance activities motivate earnings management. (Panjalusman Paskalis et al., 2018) discovered that transfer pricing did not affect tax avoidance. According to (Putri, 2014), earnings management has no significant impact on corporate tax aggressiveness. Furthermore, (Nadhifah & Arif, 2020) claims that thin capitalization affects tax aggressiveness, whereas (Olivia & Dwimulyani, 2019) claims that thin capitalization does not affect tax avoidance. Finally, (Lee, 2017) discovers that hedging affects tax avoidance, whereas (Novianti & Firmansyah, 2020) discovers that hedging does not affect tax avoidance. This means that the findings of the research on the variables listed above still have many inconsistencies.

## Literature Review

### Theory of Agency

Theory of Agency A contract between the manager and the owner in which the owner wishes to delegate authority to the manager is put forward in this theory.

### Tax Avoidance

Tax avoidance is a valid tax avoidance technique that does not harm taxpayers

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because it does not violate tax regulations (Pohan, 2014). Meanwhile, (Mardiasmo, 2016) mentions it as an attempt to reduce the tax burden while remaining within the law.

### Transfer Pricing

(Feinschreiber, 2001) defines transfer pricing for tax purposes as the price of inter-company transactions made between affiliated companies in his book *Transfer Pricing Methods*. According to (Horngren, 2008), transfer pricing is the amount charged by one organizational segment for products supplied to other organizational segments in multinational corporations.

### Earning Management

(Fischer & Rosenzweig, 1995), also known as earnings management, is the behavior of managers in increasing (decreasing) profits from units under their authority, regardless of whether long-term profitability is increasing or decreasing.

### Thin Capitalization

Thin capitalization occurs when a company's debt exceeds its capital (OECD, 2013). The emergence of capitalization is inextricably linked to the distinction between debt and capital financing.

### Hedging

(Hardjito, 2002) Hedging is a strategy used to limit potential losses caused by fluctuations in currency exchange rates (exposure). Furthermore, (Hull, 2008) defines positive hedging as one that eliminates all risks.

## MATERIALS AND METHODS

The quantitative research method with a descriptive approach was chosen by the researcher (Sugiyono, 2015). The population chosen was the coal mining companies listed on the IDX from 2015 to 2019. Purposive sampling yielded a sample of 16 companies. Multiple linear regression analysis with descriptive analysis, regression analysis mode, classical assumption testing, and hypotheses was used.

## RESULTS AND DISCUSSION

For the research, 80 samples were obtained from 16 companies. The EViews program version 12 for Windows was used to process written data in this thesis.

**Table 1.** Data Analysis

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.335923	0.162572	2.066307	0.0423
TRANSFER_PRICING	-0.070554	0.151472	-0.465788	0.6427
MANAJEMEN_LABA	0.060482	0.045043	1.342749	0.1834
THIN_CAPITALIZATION	-0.034236	0.012969	-2.639892	0.0101
HEDGING	0.004676	0.016985	0.275332	0.7838
Weighted Statistics				
R-squared	0.129898	Mean dependent var	0.974387	
Adjusted R-squared	0.083492	S.D. dependent var	1.213583	
S.E. of regression	0.827930	Sum squared resid	51.41006	
F-statistic	2.799195	Durbin-Watson stat	1.988948	
Prob(F-statistic)	0.031813			
Unweighted Statistics				
R-squared	-0.008841	Mean dependent var	0.014355	
Sum squared resid	206.2189	Durbin-Watson stat	2.509188	

### F Test (Simultaneous Effect)

Table 1 shows that the prob value (F-statistics) was 0.0318 less than 0.05, indicating that transfer pricing, earnings management, thin capitalization, and hedging all have an impact on tax

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avoidance at the same time.

### **Determination Coefficient**

The Adjusted R-Square value was 0.083, as could be seen. This demonstrated that transfer pricing, earnings management, thin capitalization, and hedging could have an 8.3% impact on tax avoidance. This figure depicts the less powerful influence of the four independent variables, and there was another effect of 91.7% that might have an impact on tax avoidance but was not investigated in this research.

### **The Influence of Transfer Pricing on Tax Avoidance**

The transfer pricing variable had a significant value of 0.6427 which was greater than 0.05. That was, transfer pricing did not affect the tax avoidance variable. Variable transfer pricing did not affect tax avoidance; this could be due to the proxy's dissimilarity to previous studies, in which many studies only measured sales transactions as an indicator of transfer pricing, whereas this research used sales to affiliates as well as other transactions carried out by the research sample to affiliates making use of dummy variables (Yuniasih et al., 2012). According to (Astuti & Aryani, 2017), transfer pricing involved business groups because it happened between affiliates; this was related to agency theory. Principals who had an interest in the company's long-term viability and agents who carry out those interests frequently had opposing viewpoints. Because transfer pricing involved multiple agents and companies, there were various taxation interests at

stake. This finding was consistent with studies that found transfer pricing did not affect tax avoidance (Panjalusman Paskalis et al., 2018), (Napitu & Kurniawan, 2016), (Mukhtar, 2021); (Vicard, 2015), and (Hasibuan & Gultom, 2021). Meanwhile, this finding differed from those of (Amidu et al., 2019) and (Eriotis et al., 2021), who discovered that transfer pricing affects tax avoidance. Transfer pricing has also been found to have an impact on tax avoidance in studies (Nadhifah & Arif, 2020); (Wijaya & Rahayu, 2021).

### **The Influence of Earning Management on Tax Avoidance**

The earnings management variable had a significant value of 0.1834 which was greater than 0.05. As a result, earnings management did not affect tax avoidance. Companies use earnings management to minimize tax obligations in the context of taxation. Law of the Republic of Indonesia Number 36 of 2008 concerning the Fourth Amendment to Law Number 7 of 1983 concerning Income Tax, 2008 confirms that costs can be deducted from company profits. This is what the company will use to manage its taxes so that they are not excessive. However, according to this research, coal mining companies did not use earning management to reduce their taxes. Earning management did not affect tax avoidance, according to (Putri, 2014), (Nadhifah & Arif, 2020), (Githaiga et al., 2022), and (Wijayanti et al., 2016). Meanwhile, these findings contradict each other (Amidu et al., 2019). Additionally, (Nurhandono & Firmansyah, 2017) and (Pratama, 2020) discovered that earnings management affects tax avoidance.

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### **The Influence of Thin Capitalization on Tax Avoidance**

The variable thin capitalization had a significant value of 0.0101, which was less than 0.05. That was, thin capitalization affected the tax avoidance variable. (Minister of Finance Regulation 169/PMK.010/2015 concerning determining the ratio between debt and company capital to calculate income tax, 2015) governs the composition limit of debt and capital, stating that mining companies are exempt from the regulation's scope. This was what coal mining companies could do to increase their debt and thus their interest expense. As a result, coal companies used thin capitalization schemes to reduce their taxes. Thin capitalization had a significant impact on the level of tax avoidance (Lanis & Richardson, 2012), (Winarto & Daito, 2021), and (Waluyo & Daktoralina, 2018). Thin capitalization affected tax avoidance (Andawiyah et al., 2019) and (Nadhifah & Arif, 2020).

### **The Influence of Hedging on Tax Avoidance**

The hedging variable had a significant value of 0.7838 which was greater than 0.05. As a result, hedging did not affect the variable of tax avoidance. This finding was consistent with that of (Lianty et al., 2017), who found that hedging does not affect tax aggressiveness. Furthermore, (Nurhandono & Firmansyah, 2017) claimed that hedging did not affect tax aggressiveness. In terms of tax avoidance, it has been discovered that the aggressiveness of tax reporting encourages the use of derivatives

(Donohoe, 2015). Derivatives used in this research were those that were not used for speculating or trading, such as those used for hedging. In Indonesia, (Brian & Martani, 2017) shows that derivative users are more aggressive than non-derivative users (without comparing their goals). (Lee, 2017) investigated tax aggressiveness through hedging and discovered a significant positive relationship between hedging and tax avoidance.

### **CONCLUSIONS**

Transfer pricing, earnings management, or hedging do not affect tax avoidance. For the 2015-2019 period, coal companies listed on the IDX used transfer pricing not to avoid taxes, but for other reasons that necessitated additional investigation. Although profit is used to determine how much tax a company should pay, it is not used by coal companies to avoid paying taxes. Hedging is used to protect a company from opportunities that may arise as a result of changes in interest rates, currency exchange rates, and major commodity prices. Thin capitalization, on the other hand, has a significant impact on tax avoidance. Miller's theory that debt with interest charges can be used by companies to increase spending and affect the amount of corporate taxes can explain this effect.

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