CHAPTER 1
INTRODUCTION

1.1 Background

In most countries, the largest state income for national development is tax. To fulfill the purposes of the Indonesian state listed in the Preamble of the Indonesian Republic Law, namely for the entire Indonesian bloodshed and to promote public welfare, describe the life of the country and contribute in carrying out world order and all Indonesian people deserve social justice based on the Pancasila and 1945 regulation. If these goals want to be achieved, huge funds are needed from natural and human resources. Along with the rapid development, natural and human resources are decreasing, hence the current tax is the main choice.

In accordance with article 1 paragraph 1 of law number 28 year 2007 concerning General Provisions And Procedures For Taxation define that tax is a compulsory impact to the country as stipulated by an entity or individual that is required under the law, through not obtaining for the determinations of the country for - the great prosperity of the people. According to (Soemitro & Soemahamidjaja, 2008), the definition of tax is obligatory contributions in the shape of cash or commodities, which are gathered by the government based on legal norms to shelter the costs of creating collective commodities and services in accomplishing public wellbeing. The tax collection system ias regulated by government in Indonesia is a self-assessment system, which is a system that provides trust and responsibility to calculate, deposit, and report on how much tax is owed by taxpayers. in this case the government has an obligation to carry out coaching, research, and supervision of the fulfillment of taxpayer obligations, one of which is income tax.

The government certainly wants revenue from the tax area to raise each year. This can be achieved by efforts to optimize the potential of taxes made by the government, such as efforts to intensify taxes and tax extensification. The ups and downs of tax revenue realization in the APBN can be seen in table 1.1.

Table 1.1 Realization of Tax Revenues (in trillion rupiahs)

Year	Tax Revenue Targets	Tax Revenue Realization	Percentage (%) Achievement
2015	Rp 1294.3	Rp 1240.4	82%
2016	Rp 1355.2	Rp 1105.8	82%
2017	Rp 1283.6	Rp 1151.1	90%
2018	Rp 1424.0	Rp 1315.5	92%
2019	Rp 1577.7	Rp 1332.1	84%

Source: LAKIN DJP 2019,2018,2017,2016

From table 1.1 shows that the figures from the realization of revenues in the tax sector indeed go up and down every year. From previous year, we can see that 2015 and 2016 only reached 82% of the set target compare to other year. This proves the ineffectiveness of government policy on the hopes of achieving tax revenue. Another reason that inhibits efforts to optimize the tax sector is the view of the taxpayer assuming that tax burden that will reduce their income, so that many of them who want the tax burden can be as minimal as possible. So, from that the practice of tax avoidance is carried out by taxpayers so that their taxes can be minimized as small as possible. Tax avoidance performed by many firms because tax avoidance is a tax reduction business, but still adheres to the provisions of tax regulations such as utilizing exceptions and allowable and postponing deductions of tax that yet to be legalized in the related tax policies and usually through policies taken by the firm leadership. The implementation of tax avoidance is not accidental, and many firms even use efforts to reduce tax burden through tax avoidance activities. Tax avoidance has a unique and complex problem because on the one hand tax avoidance is permitted, but on the other hand tax avoidance is wise and not desired (Budiman & Wijayanti, 2013).

Previous research shows that empirical findings are in line with the idea that tax avoidance has a high association with corporate risk. Example like (Rego & Wilson, 2012), who found that the CEOs of a company has a lower effective tax strategy; (Badertscher, Katz, & Rego, 2012) found that the CEO of a company with a lower effective tax strategy had a desire to carry out risky incentives, which found that managerial ownership had a positive association with ETR, which was consistent with the idea owner-managers that badly differentiated would most likely avoid the inherent risk of tax reduction strategy and (Hasan, Hoi, Wu, & Zhang, 2014), find that if firms with lower Effective Tax Rate (ETR) will create higher interest rates when loaning funds from the bank.

Tax avoidance may increase firm risk in so many factors. First, tax avoidance grow the uncertainty of firm's future tax expenses, either the persistence of the tax law that provide tax benefit or through increase of uncertainty regarding trials by tax authorities (Blouin, 2014). We can see if the tax payment is a huge factor of the firm's cash flows, the improbability of firm's tax payments may ring improbability for the firm's overall cash flows. Second, the extent of tax avoidance serves as the main sign about the risk of the firm's investments, such as volatility of the firm's cash flows. This can happen if the firm's dependent on tax-favored investments were related with the firm's entering into uncertain investments.

Company risk is the volatility of company profit, that can be calculated by the standard deviation formula. Thus, it can be interpreted that firm risk is the deviation or standard deviation of earnings whether the deviation is less than planned (downside risk) or more than planned (upset potential), the greater the standard deviation of the company's earning indicates the greater existing company risks. High and low risks of this company indicate the character of the executive whether including risk takers or risk averse (Paligorova, 2010).

According to Guenther, Matsunaga, and Williams (2016), cash ETR is the main measurement to measure the rate of tax avoidance been done by companies. Any action related to tax avoidance will have probability to cause a lower cash ETR and cause volatility in the company's shares. Low cash ETR can be determined by the capability to pay cash tax per dollar of income before tax for the long term. (Dyreng, Hanlon, & Maydew, 2008).

Companies grow because they have vision and mission to achieve a better future, to obtain best value. Firm's value can be appraised by the company's stock price. Stock price is the main factor company's value, if a firm's have a small value that's mean the companies have small chance or yet successful. Because of that, investor and managers of companies have a symbiosis relationship. Both have same goals that is gaining a big profit from the companies. But both have a different way to achieve their goals. Managers or any other upper positions can do a tax non-compliance actions that will lead into unwanted news that can increase of stock price volatility such as doing tax avoidance. According to Guenther, Matsunaga, and Williams (2013), they find that the level of Cash ETR doesn't necessarily effect the firm risk because the activities assumed as not risky activities. But this statement is contrary from (Rego & Wilson, 2012) findings, aggressive tax strategy assumed as risky activities and affect stock volatility. Tax strategies that are aggressive can be used as motivation for managers to do risky activities that caused uncertainty on greater stock volatility.

The reason why this research use manufacturing companies that are listed in Indonesian Stock Exchange 2015-2019 because manufacturing companies are the highest number of companies that have high number of investor affect the stock price volatility in Indonesia Stock Exchange (Prameswari, 2017) manufacturing companies is not final. Also, in this period of sample there is a major event called Tax Amnesty that may be a big effect to this research which according to (Permata, Nurlaela, & Masitoh, 2018) Tax Amnesty do affect companies in making decision on doing tax avoidance. According to Budiman and Wijayanti (2013) in (Susilatri, Zulbahridar, & Sartika, 2015) company that are subjected to final income tax on income is deemed completed when the deduction, collection or payment is made. So, this final income tax cannot be used as a tax credit for annual tax returns. And manufacturing companies in Indonesia doesn't use final tax to compute net income. Effective Tax Rate (ETR) is used in this research rather that Cash ETR because in Indonesia which is the sample location for this research as the taxation that stated in financial statements of firms mostly are combined which means it is hard and unreliable to measure using Cash ETR because Indonesian tax regulation recognize tax burden and from the statement above, there are final deductible tax and nonfinal deductible tax.

1.2 Research Gap

Studies that occurred by (Guenther et al., 2016) fail to get evidence whether the degree of tax avoidance have an association with higher future tax rate stock return volatility but find a positive relation between future tax rate volatility and tax rate. Studies occurred by (Hutchens, Rego, & Williams, 2019) that examine the relation between firm risk and tax avoidance by dividing companies into different classes find that where tax avoidance do affect firm risk but the result is in low significant level. Studies occurred by (Kim, Li, & Zhang, 2011) also get evidence where tax avoidance do affect companies to cover up unpleasant information for long periods can lead to stock price crashes where huge stock price volatility in this research we assume are associated with firm risk. This research hope to get different results because this research uses Effective Tax Rate (ETR) as measurement for tax avoidance rather than use Cash ETR like previous studies as well Cash ETR has been limitation because.

1.3 Research Purposes

To analyze and get empirical evidence whether tax avoidance have impact on firm risk on manufacturing company that are listed on Indonesia Stock Exchange on 2015-2019 also to proof whether there are any different between the results of this research with previous research because there is a a phenomenon called tax amnesty.

1.4 Summary of Research Methods

Data analysis method conducted in this research are descriptive analysis and multiple linear regression. Descriptive analysis is used to assess the data characteristic while multiple linear regression used to help this research to get whether tax avoidance affect firm risk in anyway.

1.5 Summary of Research Results

From this research that has been conducted, tax avoidance doesn’t affect firm risk in anyways that means the one and only hypothesis is rejected.

1.6 Benefits of Research

The benefits that can be obtained from this research are:

Theoretical Benefits

a. For Government

This thesis can be a material evaluation of the tax policy which is related to Company that listed in IDX.

b. For Company

As a company to evaluate and anticipate any probability of stock volatility because of tax non-compliance behaviour by companies.

c. For Investor

As a good investor, investor must examine the tax that are paid in financial statement of a certain period also the movement of stock prices.

Academic Benefits

This thesis can used to be empirical evidence, which is able to support previous research regarding the effect of tax avoidance on firm risk.

1.7 Systematics

CHAPTER 1 Introduction

This chapter explains the age picture of firm's risk against tax avoidance, research gap, the purpose of research, the benefits of research for related parties, and finally systematics research.

CHAPTER 2 Literature Review

This chapter explains theoretical basis related to this research, namely firm risk which are elaborated with tax avoidance and supported with stock return, institutional ownership, company's size, pre-tax book income, outstanding shares and book value of equity. This chapter also discusses previous research related to this research, explanations using hypotheses.

CHAPTER 3 Research Methodology

This chapter explains that the approach used by this research uses a quantitative approach with multiple linear regression analysis methods, identification and explanation of the dependent variable which is firm risk, and independent variables, which is tax avoidance. This research uses 1 dependent variable, 1 independent variable and 6 control variables.

CHAPTER 4 Findings and Discussion

This chapter explains the outcomes of the research which is does tax avoidance affect firm risk in any way? The explanation of the research from the measurement of statistical methods such as descriptive analysis that gave the descriptions of mean, minimum, maximum, and standard deviation value of each variable with total of 58 manufacturing companies that are listed on Indonesia Stock Exchange of total amounted of 280 observations and hypothesis testing using multiple linear regression implemented by using IBM SPSS Statistic 25.

CHAPTER 5 Conclusions and Recommendations

This chapter proposes the conclusions based of the results of this research model analysis, as well there are some recommendations for limitations and completion of shortcomings in this research. Recommendations also stated for future research to use different proxies and for the wellbeing of the investors or shareholders to carefully analysis the annual reports of companies concerning activities that affect the consideration of investor on investing in companies.