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DETERMINANTS OF TAX AVOIDANCE IN INDONESIAN MANUFACTURING COMPANIES: EMPIRICAL EVIDENCE FROM FUNDAMENTAL FINANCIAL FACTORS

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Abstract:
Tax avoidance is a strategic issue in taxation because it can reduce government revenue even when undertaken through mechanisms that remain within legal boundaries. Prior studies of tax avoidance among Indonesian manufacturing companies have produced inconsistent results, particularly regarding the effects of sales growth, profitability, liquidity, leverage, and firm size. This study examines the influence of these five fundamental firm characteristics on tax avoidance among manufacturing companies listed on the Indonesia Stock Exchange. A quantitative approach was employed using secondary data from the companies' annual financial statements. Purposive sampling yielded 11 companies and 44 firm-year observations. The data were analyzed using multiple linear regression after all classical assumptions had been satisfied. The results show that sales growth, profitability, liquidity, leverage, and firm size jointly affect tax avoidance. Individually, liquidity has a positive effect on tax avoidance, while leverage has a significant effect in a direction indicating that greater leverage is associated with a stronger tendency toward tax avoidance, as proxied by the Cash Effective Tax Rate (CETR). Sales growth, profitability, and firm size have no significant effects. These findings reinforce the empirical evidence that tax avoidance is shaped not only by a company's capacity to generate profits but also by its financing structure and liquidity position. The results may assist corporate managers in formulating effective tax strategies and help tax authorities develop risk-based supervision of corporate taxpayers.

Keywords: Tax Avoidance, Sales Growth, Profitability, Liquidity, Leverage, Firm Size.

INTRODUCTION

Tax revenue is the primary source of government income and plays a vital role in sustaining national development, financing public services, and achieving economic development targets. In Indonesia, the contribution of taxes to the State Budget (APBN) has continued to grow alongside a series of tax reforms, including the enactment of the Tax Regulation Harmonization Law (UU HPP), the digitalization of tax administration, and the strengthening of risk-based supervision. Nevertheless, efforts to optimize tax revenue continue to face several challenges, one of which is corporate tax avoidance through the use of loopholes in prevailing tax regulations. Although such practices are legally permissible because they do not directly violate statutory provisions, they may reduce potential government revenue and raise concerns about the fairness and effectiveness of the tax system (Hanlon & Heitzman, 2010).

Tax avoidance has become an important issue in the accounting and taxation literature because it reflects how companies design strategies to minimize tax liabilities without breaching the law. From a corporate perspective, tax avoidance forms part of tax planning intended to improve cost efficiency and maximize firm value. From the government's perspective, however, these practices may weaken fiscal capacity, thereby underscoring the need for stronger regulation, improved

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compliance, and closer oversight of corporate tax activities. Research on the factors that shape tax avoidance therefore remains highly relevant, particularly in developing economies such as Indonesia, where tax revenue continues to be a major source of development financing.

Manufacturing is a strategic sector of the Indonesian economy because it contributes substantially to gross domestic product (GDP), employment, exports, and tax revenue. The sector's complex operating characteristics, high intensity of fixed-asset investment, large transaction volumes, and diverse financing sources provide manufacturing firms with greater scope for adopting tax-planning strategies than firms in many other sectors. Manufacturing companies also tend to have considerable flexibility in setting operating and financial policies that may affect their tax burden. These characteristics explain why manufacturing firms are frequently examined in studies of corporate tax avoidance.

From a theoretical perspective, tax avoidance can be explained through Agency Theory, as developed by Jensen and Meckling (1976). The theory posits a conflict of interest between shareholders as principals and managers as agents. Shareholders seek to increase firm value by optimizing after-tax earnings, whereas managers are concerned with maintaining financial performance while meeting a range of corporate targets. These competing interests may encourage managers to make various financial decisions, including the adoption of tax-avoidance strategies, provided that such actions remain within legal boundaries. Accordingly, a firm's fundamental characteristics may influence its propensity to engage in tax avoidance.

Against this background, the study analyzes the effects of sales growth, profitability, liquidity, leverage, and firm size on tax avoidance among manufacturing companies listed on the Indonesia Stock Exchange. The findings are expected not only to advance the literature on corporate tax behavior but also to offer practical implications for managers in designing efficient tax policies and for tax authorities in improving the effectiveness of corporate-taxpayer supervision.

Agency Theory. Agency Theory, developed by Jensen and Meckling (1976), explains that the relationship between shareholders (principals) and management (agents) is not always aligned because each party has different interests. Shareholders expect firm value to increase through the optimization of after-tax earnings, whereas managers may make decisions that improve corporate performance while also protecting their own interests.

In taxation, agency conflict arises when management attempts to reduce the company's tax burden through various tax-planning strategies. As long as these strategies remain within the boundaries of tax law, they are categorized as tax avoidance. The decision to engage in tax avoidance is therefore a managerial policy shaped by fundamental firm characteristics, including profitability, liquidity, leverage, sales growth, and firm size. Agency Theory provides the main foundation for explaining how a company's financial condition affects managerial decisions regarding the degree of tax aggressiveness.

Tax Avoidance. Tax avoidance refers to corporate efforts to minimize tax liabilities by making use of legally permissible provisions in tax regulations. Unlike tax evasion, which violates the law, tax avoidance exploits loopholes without directly contravening applicable rules. Although legal, the practice frequently attracts regulatory concern because it may reduce government revenue and create inequity within the tax system.

Hanlon and Heitzman (2010) describe tax avoidance as a strategic corporate decision influenced by firm characteristics, governance, ownership structure, and financing policy. In this study, tax avoidance is proxied by the Cash Effective Tax Rate (CETR), which compares the cash

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taxes actually paid by a company with its pre-tax income. A lower CETR indicates a stronger tendency to engage in tax avoidance.

The Effect of Sales Growth on Tax Avoidance. Sales growth reflects a company's ability to expand its operating activities over time. Higher sales are generally followed by higher profits, potentially increasing the company's tax burden. This condition may encourage management to adopt tax-planning strategies to preserve optimal after-tax earnings. However, growth in sales does not necessarily lead to greater tax avoidance because it may also be accompanied by higher operating costs, investment expenditure, and other tax obligations. The relationship between sales growth and tax avoidance therefore remains debated in the empirical literature: some studies report a positive association, while others find no significant effect.

H1: Sales growth has a positive effect on tax avoidance.

The Effect of Profitability on Tax Avoidance. Profitability reflects a company's ability to generate earnings from the resources under its control. Higher profitability produces greater income and, consequently, a larger tax obligation. This creates an incentive for management to use tax planning to reduce the tax burden. From an Agency Theory perspective, management seeks to preserve after-tax earnings through efficient policies, including tax avoidance. Highly profitable firms may therefore have stronger incentives to avoid taxes than firms with lower earnings. Recent evidence likewise suggests that profitability remains an important determinant of tax avoidance among manufacturing companies.

H2: Profitability has a positive effect on tax avoidance.

The Effect of Liquidity on Tax Avoidance. Liquidity indicates a company's ability to meet its short-term obligations. Firms with high liquidity generally have a stronger cash position and greater flexibility in financial management. High liquidity may also enable a company to undertake more effective tax planning because it has sufficient resources to develop and implement tax strategies. Conversely, firms with weak liquidity are more likely to prioritize operational continuity rather than tax-avoidance strategies. Liquidity is therefore expected to have a positive relationship with tax avoidance.

H3: Liquidity has a positive effect on tax avoidance.

The Effect of Leverage on Tax Avoidance. Leverage represents the proportion of debt used in a company's financing structure. Debt generates interest expenses that may be deducted from taxable income, thereby creating a tax shield. Under Agency Theory, management may use financing structure as a strategy for reducing the tax burden. The greater the leverage, the larger the potential tax benefit derived from interest expense, and the stronger the firm's tendency to engage in tax avoidance. Recent studies also identify leverage as a factor that consistently influences tax avoidance among manufacturing companies.

H4: Leverage has a positive effect on tax avoidance.

The Effect of Firm Size on Tax Avoidance. Firm size reflects the scale of economic resources controlled by a company. Large firms typically have more complex transactions, greater access to professional tax advisers, and a stronger capacity to design effective tax-planning strategies than smaller firms. Large companies also face higher tax liabilities and thus have incentives to improve tax efficiency through tax avoidance. At the same time, however, they are subject to closer scrutiny from regulators and the public. This tension helps explain why empirical findings on the relationship between firm size and tax avoidance remain mixed.

H5: Firm size has a positive effect on tax avoidance.

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Previous studies have identified several factors that may influence tax avoidance, including sales growth, profitability, liquidity, leverage, and firm size. Their findings, however, remain inconsistent. Devi et al. (2023) found that profitability, liquidity, firm size, and sales growth affected tax avoidance. In contrast, Manurung et al. (2024) reported that only profitability and sales growth had significant effects, while liquidity did not. Febrilyantri (2022) found that liquidity and firm size influenced tax avoidance, whereas leverage had no effect. Aritonang et al. (2024), meanwhile, found no significant effects of profitability or leverage. These differences indicate that the relationship between firms' fundamental characteristics and tax avoidance has yet to yield a consistent conclusion.

The inconsistency of the empirical evidence points to a research gap that warrants further investigation. Earlier studies have employed different observation periods, examined firms with varying characteristics, and operated within a tax regulatory environment that has continued to evolve. In addition, recent policies, including the Tax Regulation Harmonization Law and the accelerating digitalization of tax administration, may have altered corporate tax-planning behavior. Re-examining the determinants of tax avoidance among manufacturing firms is therefore necessary to provide more current evidence that reflects today's regulatory and business environment.

This study offers several contributions that distinguish it from earlier research. First, it examines five fundamental firm characteristics—sales growth, profitability, liquidity, leverage, and firm size—within a single model, providing a more comprehensive account of the determinants of tax avoidance. Second, it focuses on manufacturing companies, whose operations are relatively complex and which remain among Indonesia's major contributors to tax revenue. Third, it provides updated empirical evidence on the influence of fundamental financial factors in the period following major tax reforms in Indonesia. Unlike Devi et al. (2023) and Manurung et al. (2024), whose data largely predated the full implementation of the Tax Regulation Harmonization Law and did not fully capture changes in tax behavior associated with administrative digitalization, this study specifically draws its sample from the period after those reforms had taken effect. Its findings are therefore expected to be more relevant to the current regulatory and business setting. In this way, the study seeks both to enrich the tax-accounting literature and to inform regulators in designing more effective tax-supervision policies.

METHODS

This study employed a quantitative, causal-associative design to examine relationships among variables. The research objects were the annual financial statements of manufacturing companies listed on the Indonesia Stock Exchange, obtained through www.idx.co.id. The population comprised all manufacturing companies listed on the exchange. The sample was selected using non-probability purposive sampling based on the following criteria: (1) the company was consistently listed on the Indonesia Stock Exchange throughout the observation period; (2) it consistently published audited financial statements as of December 31 and was not delisted; (3) it used the Indonesian rupiah as its reporting currency; and (4) it did not report a loss during the observation period. These criteria yielded 11 sample companies observed over four years, producing 44 firm-year observations, as presented in Table 1.

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Table 1. Sample Selection Process

Criteria	Number of Companies
Manufacturing companies consistently listed on the IDX	136
Companies that did not consistently publish audited financial statements or were delisted	(72)
Manufacturing companies that did not use the Indonesian rupiah as their reporting currency	(46)
Manufacturing companies that reported losses during the observation period	(7)
Number of sample companies	11
Number of observation years	4
Number of observations (companies × years)	44

Source: Processed data, 2025

Operational Definitions of Variables. Tax avoidance, the dependent variable, was measured using the Cash Effective Tax Rate (CETR), calculated as cash taxes paid divided by pre-tax income. Sales growth was measured as the difference between current-year and prior-year sales divided by prior-year sales. Profitability was measured using Return on Assets (ROA), calculated as net income after tax divided by total assets. Liquidity was measured using the Current Ratio (CR), calculated as current assets divided by current liabilities. Leverage was measured using the Debt-to-Asset Ratio (DAR), calculated as total liabilities divided by total assets. Firm size was measured as the natural logarithm of total assets.

Data Analysis. The data were analyzed using multiple linear regression in SPSS, based on the following equation: $TA = \alpha + \beta 1PP + \beta 2PB + \beta 3LD + \beta 4LR + \beta 5UP + e$, where TA denotes tax avoidance; PP, sales growth; PB, profitability; LD, liquidity; LR, leverage; UP, firm size; and e, the residual error. Before estimating the regression model, the data were subjected to classical-assumption tests comprising the Kolmogorov-Smirnov normality test, multicollinearity tests based on tolerance and variance inflation factor (VIF), the Glejser heteroscedasticity test, and the Durbin-Watson autocorrelation test. Model-feasibility testing subsequently included the simultaneous significance test (F-test), the coefficient of determination (R^2), and the partial significance test (t-test), all evaluated at a 5% significance level (0.05).

RESULT AND DISCUSSION

Descriptive Statistics. The descriptive statistics for research variables are presented in Table 2.

Table 2. Descriptive Statistics

Variable	Minimum	Maximum	Mean	Std. Deviation
Sales Growth (%)	-14.00	123.00	10.4091	18.89668
Profitability/ROA (%)	0.09	46.30	13.7702	11.33342
Liquidity/CR (×)	0.61	5.27	2.7727	1.33883
Leverage/DAR (%)	0.13	74.40	11.6084	21.76133
Firm Size (Ln Assets)	28.70	32.20	30.7830	0.92358
Tax Avoidance/CETR	0.07	0.44	0.2623	0.05689

Source: Processed data, 2025

The number of observations for all variables was 44. The mean CETR of 0.2623 indicates that, on average, the sampled companies paid cash taxes at a rate close to the statutory corporate income

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tax rate, while variations across firms suggest the presence of tax-avoidance behavior among part of the sample.

Classical Assumption Tests. The Kolmogorov-Smirnov normality test produced an Asymp. Sig. (2-tailed) value of 0.899, which exceeded 0.05, indicating that the model residuals were normally distributed. The multicollinearity test showed that all independent variables had tolerance values above 0.10 and VIF values below 10, confirming the absence of multicollinearity. The Glejser test produced significance values above 0.05 for all independent variables, indicating that the regression model was free from heteroscedasticity. The Durbin-Watson statistic was 1.803, falling between du (1.7777) and 4-du (2.2223), which confirmed the absence of autocorrelation. All tests followed the criteria proposed by Ghozali (2018). Overall, the regression model met the Best Linear Unbiased Estimator (BLUE) requirements and was suitable for hypothesis testing.

Multiple Linear Regression and Model Feasibility. The multiple regression results are presented in Table 3.

Table 3. Multiple Linear Regression and Hypothesis Testing Results (t-test)

Variable	Coefficient (B)	t-statistic	Sig.	Result
Constant	0.492	-	-	-
Sales Growth (PP)	0.001	1.393	0.172	Not Significant
Profitability (PB)	0.001	0.781	0.439	Not Significant
Liquidity (LD)	0.028	3.531	0.001	Significant
Leverage (LR)	-0.001	-2.240	0.031	Significant
Firm Size (UP)	-0.005	-0.535	0.596	Not Significant

Source: Processed data, 2025. Significance level: 0.05.

Based on Table 3, the estimated regression equation is $TA = 0.492 + 0.001PP + 0.001PB + 0.028LD - 0.001LR - 0.005UP + e$. The constant of 0.492 indicates that when all independent variables are held at zero, the predicted value of the tax-avoidance proxy (CETR) is 0.492. The F-test yielded a significance value of 0.018, below 0.05, indicating that sales growth, profitability, liquidity, leverage, and firm size jointly affect tax avoidance. The adjusted R^2 of 0.199 shows that the five independent variables explain 19.9% of the variation in tax avoidance, while the remaining 80.1% is attributable to factors outside the model.

The Effect of Sales Growth on Tax Avoidance. Sales growth had no significant effect on tax avoidance. This finding indicates that an increase in corporate sales does not automatically lead to greater tax avoidance. Although higher sales may increase earnings, they are generally accompanied by higher operating and production costs, asset investment, and other tax obligations. Changes in sales therefore do not necessarily translate into changes in taxable income, which forms the basis for corporate income tax calculations.

From an Agency Theory perspective, management's decision to engage in tax avoidance is shaped not simply by the level of revenue but by the broader strategy used to manage earnings and tax expense. Sales growth is therefore not necessarily a primary indicator that encourages more aggressive tax planning.

This finding is consistent with Faradilla and Bhilawa (2022), who reported that sales growth had no significant effect on tax avoidance. It differs, however, from Devi et al. (2023) and Manurung et al. (2024), who found a positive effect. These differences suggest that the relationship is context-dependent and may vary according to industry characteristics, operational efficiency, and economic conditions during the observation period.

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In practical terms, tax authorities should not rely on sales growth as the sole indicator when identifying companies that may engage in tax avoidance. Risk assessment should also consider financial characteristics that more directly reflect a company's capacity to undertake tax planning.

The Effect of Profitability on Tax Avoidance. Profitability had no significant effect on tax avoidance. This result suggests that companies with high profitability do not necessarily have a stronger propensity to avoid taxes.

In theory, highly profitable companies face larger tax liabilities and therefore have an incentive to engage in tax planning. Nevertheless, such companies also tend to have stronger governance systems, more robust internal controls, and reputations that must be protected before investors and regulators. These considerations may make them more cautious about tax policies that could increase audit risk.

Under Agency Theory, management considers not only tax efficiency but also political costs and reputational risk. Higher profitability therefore does not automatically result in greater tax avoidance.

This result is consistent with Aritonang et al. (2024), but differs from Gultom (2021), Manurung et al. (2024), and Rasyid and Muid (2024). The inconsistency confirms that profitability is not the sole determinant of tax-avoidance behavior; governance, ownership structure, and corporate tax policy may also play important roles.

The Effect of Liquidity on Tax Avoidance. Liquidity had a positive effect on tax avoidance. Companies with a stronger ability to meet short-term obligations appear to have greater scope for implementing tax-planning strategies.

Highly liquid firms have greater financial flexibility and can allocate resources more readily to effective tax management, including the use of tax advisers, the design of tax-planning arrangements, and the utilization of available tax incentives. A healthy liquidity position may therefore provide firms with additional room to optimize tax efficiency.

This finding supports Agency Theory, which suggests that managers use the resources available to them to enhance firm value, including through more efficient tax payments. The greater the firm's financial capacity, the greater the opportunity for management to adopt strategies that improve after-tax earnings.

The result is consistent with Febrilyantri (2022), Devi et al. (2023), and Aritonang et al. (2024), all of whom identified liquidity as an important determinant of tax avoidance.

A practical implication is that highly liquid companies warrant attention within compliance risk management systems because their financial capacity may enable more sophisticated tax planning.

The Effect of Leverage on Tax Avoidance. Leverage had a significant effect on tax avoidance. Its negative regression coefficient with respect to CETR means that higher leverage is associated with a lower CETR and, consequently, a higher level of tax avoidance.

This relationship can be explained by the tax-shield benefit generated by interest expense on debt. Because interest is deductible from taxable income, companies with a higher proportion of debt tend to pay less tax than firms that rely more heavily on equity financing.

From an Agency Theory perspective, debt use is also a strategic managerial decision for optimizing capital structure. In addition to improving financing flexibility, debt offers tax savings through the tax-shield mechanism. Highly leveraged companies therefore tend to exhibit higher levels of tax avoidance.

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This finding is consistent with Syahputra (2023) and Rasyid and Muid (2024). It differs, however, from Febrilyantri (2022) and Aritonang et al. (2024), who found no significant effect. These differences indicate that leverage's effectiveness in reducing the tax burden depends on the company's financing structure, industry characteristics, and applicable limitations on the deductibility of interest expense.

The implication is that capital structure should be an important consideration for tax authorities when identifying potential corporate tax avoidance.

The Effect of Firm Size on Tax Avoidance. Firm size had no significant effect on tax avoidance, indicating that corporate scale is not a primary factor determining whether a company adopts tax-avoidance strategies.

Large firms possess greater resources, better access to tax advisers, and more sophisticated management systems. At the same time, they are subject to closer scrutiny by regulators, auditors, investors, and the public. This heightened scrutiny may encourage large firms to exercise greater caution when adopting tax policies that could increase the risk of tax disputes or damage their reputation. Smaller companies may likewise engage in tax avoidance when sufficient economic incentives are present. Firm size is therefore not a decisive determinant of tax avoidance among manufacturing companies.

This finding is consistent with Manurung et al. (2024), but differs from Febrilyantri (2022), Devi et al. (2023), Aritonang et al. (2024), and Syahputra (2023). These divergent results suggest that the effect of firm size depends strongly on sample characteristics, the observation period, and the monitoring mechanisms applied to individual firms.

CONCLUSION

Conclusion. This study analyzed the effects of sales growth, profitability, liquidity, leverage, and firm size on tax avoidance among manufacturing companies listed on the Indonesia Stock Exchange. The results show that the five variables jointly affect tax avoidance. At the individual level, only liquidity and leverage have significant effects, while sales growth, profitability, and firm size do not. These findings indicate that a firm's financial condition—particularly its liquidity and financing structure—plays a more decisive role in tax avoidance than its operating characteristics.

This study has several limitations that should be considered when interpreting the findings. First, the sample was relatively limited, comprising 11 companies and 44 firm-year observations; the findings should therefore be generalized to all manufacturing companies listed on the Indonesia Stock Exchange with caution. Second, the adjusted R^2 of 0.199 indicates that the five independent variables explain only 19.9% of the variation in tax avoidance, while the remaining 80.1% is attributable to factors outside the model, such as corporate governance, ownership structure, capital intensity, and audit quality. These limitations suggest that the determinants of tax avoidance among manufacturing companies are multidimensional and cannot be explained solely by fundamental financial characteristics.

Companies should formulate tax-planning strategies that continue to observe the principles of compliance with tax regulations. For tax authorities, the findings may inform the design of risk-based supervision, particularly for firms with certain liquidity and leverage profiles. Future research should extend the observation period, increase the sample size, and incorporate additional variables such as corporate governance, institutional ownership, capital intensity, audit quality, and environmental, social, and governance (ESG) factors to provide a more comprehensive understanding of the determinants of tax avoidance.

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