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THE ROLE OF PROFITABILITY AND THIN CAPITALIZATION IN SHAPING TAX AVOIDANCE BEHAVIOR AMONG IDX-LISTED MINING COMPANIES

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Abstract
Corporate tax avoidance is a significant issue because it has a direct impact on government revenue and reflects how companies manage their tax responsibilities. In Indonesia, this issue is especially important as tax revenue serves as a key source of funding for public spending and national development. Therefore, examining tax avoidance is important to understand the factors that encourage companies to minimize their tax burdens. This study examines whether profitability and thin capitalization affect tax avoidance in mining-sector companies listed on the Indonesia Stock Exchange during 2021–2024. The study uses secondary data from annual financial statements and applies purposive sampling. After the sample-selection process, 12 companies met the research criteria, producing 48 firm-year observations. The data are analyzed using multiple linear regression with OLS estimation and pooled firm-year observations through IBM SPSS Statistics 31. The results show that profitability has a negative and significant effect on ETR, while thin capitalization has a positive but insignificant effect on ETR. Since tax avoidance is proxied by ETR, where a lower ETR indicates a higher level of tax avoidance, the negative coefficient of profitability indicates that more profitable companies tend to have a higher tendency toward tax avoidance. Meanwhile, thin capitalization is not proven to significantly influence tax avoidance practices in the observed mining-sector companies. The results of this study are expected to provide insights for regulators in strengthening tax supervision, for investors in assessing corporate tax behavior, and for companies in formulating tax strategies that remain aligned with applicable regulations.
Keywords: Mining sector companies; Profitability; Tax avoidance; Thin capitalization

INTRODUCTION

Corporate tax avoidance remains an important issue in Indonesia because it directly affects state revenue and weakens the credibility of the tax system. Tax avoidance can be defined as the legal utilization of tax regulations and policies to reduce the amount of tax payable, either in accordance with the law or at least within the boundaries of existing tax regulation (Hossain et al., 2024). One indication of tax avoidance practices in Indonesia can be seen from the low level of tax compliance, which is reflected in the current tax ratio (Ibrahim et al., 2021). This topic is particularly relevant in sectors characterized by substantial profits, high financing requirements, and considerable opportunities for tax planning. Therefore, the mining sector is selected in this study because it has these characteristics and plays a strategic role in Indonesia's economy, while also having significant potential contribution to state tax revenue.

Tax avoidance is important as the dependent variable in this study because it represents corporate behavior in managing tax obligations and reducing tax burdens. In Indonesia, tax avoidance is not only a theoretical issue but also a real phenomenon that may reduce state revenue. For example, PT Adaro Energy Tbk., currently known as PT Alamtri Resources Indonesia Tbk., was indicated to have shifted a substantial amount of profit from coal sales in Indonesia to its overseas business network, including its subsidiary in Singapore, Coaltrade Services International. From 2009 to 2017, the company allegedly reduced its tax obligations in Indonesia by utilizing differences in tax rates between countries. Another case involved PT Antam, which was indicated to have engaged in tax avoidance related to gold imports from Hong Kong through Singapore by changing the Harmonized System Code in import documents. These cases show that tax avoidance needs to be examined because it can affect tax compliance, reduce potential state revenue, and raise concerns regarding corporate accountability.

Therefore, this study places tax avoidance as the dependent variable to analyze how firm-level factors, particularly profitability and thin capitalization, influence corporate tax behavior.

In this case, two factors at the firm level become highly relevant. The first factor is profitability. Profitability reflects a firm's ability to generate earnings from the assets it controls and remains one of the clearest indicators of financial performance. Therefore, a higher profitability value indicates greater operational success (Shubita, 2024; Titman et al., 2018). More profitable firms may have stronger incentives to manage tax burdens because higher earnings can also increase expected tax payments. However, prior research has shown varying findings. Some studies indicate that profitability has a stronger and significant relationship with tax avoidance behavior (Novianti & Masyitah, 2023; Rahmayani et al., 2023; Sinaga & Oktaviani, 2022), while others find no significant relationship (Sari et al., 2021; Worokinasih & Imamah, 2025).

The second factor is thin capitalization. Thin capitalization refers to a financing structure in which debt is prioritized over equity, allowing firms to use interest expense as a deductible item in reducing taxable income (Ravanelly & Soetardjo, 2023; Ramadhan, 2023). Theoretically, a capital structure dominated by debt provides tax shield benefits and may encourage tax minimization strategies. However, empirical findings on this relationship remain inconsistent. Some studies find a positive effect of thin capitalization on tax avoidance (Haitsamathif & Putri, 2024), whereas others report no significant effect (Pangestu et al., 2023).

This article therefore tests whether profitability and thin capitalization affect tax avoidance in mining-sector companies listed on the Indonesia Stock Exchange during 2021–2024.

LITERATURE REVIEW

Agency theory

Agency theory explains the relationship between principals and agents, in which owners delegate decision-making authority to managers to operate the company on their behalf (Sutisna et al., 2024). In this relationship, both parties are assumed to pursue their own interests. Shareholders as principals generally focus on increasing firm value and investment returns, while managers as agents may be driven by compensation, incentives, and short-term performance targets. This difference in interests may lead to agency conflicts and agency costs, especially when managers have more information about the company than shareholders or external parties (Setyawan et al., 2023). In the taxation context, agency theory helps explain why managers may engage in tax avoidance, as they may use tax strategies to reduce tax burdens and increase after-tax earnings, making the company's financial performance appear better (Alkausar et al., 2023). However, aggressive tax avoidance may also create risks, such as tax sanctions, higher monitoring costs, reputational damage, and declining investor trust. Therefore, agency theory is relevant in this study because it explains how managerial decisions related to profitability and thin capitalization may influence corporate tax avoidance practices.

Stakeholder Theory

Stakeholder theory explains that firms must consider the interests and expectations of various parties who can affect or be affected by corporate activities, including shareholders, managers, employees, creditors, the government, and society (Awa et al., 2024; Salah, 2024). In the taxation context, this theory helps explain that tax avoidance decisions may create conflicting interests, as shareholders may prefer tax efficiency, while the government and society expect firms to fulfill their tax obligations. Therefore, although legal tax avoidance may improve after-tax cash flows, aggressive tax avoidance can harm corporate legitimacy, reputation, and stakeholder trust.

Tax Avoidance

Tax avoidance refers to a legal activity in which firms deliberately seek to reduce or defer their income tax obligations (Francis et al., 2025). It involves the use of tax regulations and policies to minimize the amount of tax payable while remaining within the boundaries of the law (Hossain et al., 2024). In general, tax avoidance can be understood as a legal effort to reduce tax liabilities through various strategies that may create value for shareholders, although it is strongly influenced by corporate governance mechanisms (Pratama & Muhammad, 2025). Corporate tax avoidance remains a key concern in Indonesia because it can limit government revenue and weaken the credibility of the tax system. One indication of tax avoidance practices in Indonesia is reflected in the low level of tax compliance, as shown by the current tax ratio (Ibrahim et al., 2021). Therefore, tax avoidance in this study refers to a company's legal effort to reduce the amount of tax paid without violating applicable tax regulations.

Profitability

Profitability is one of the key financial indicators of firm performance and is used to evaluate a company's ability to generate sustainable earnings (Worokinasih & Imamah, 2025). Profitability ratios assess whether a firm's investments provide adequate returns by considering profit margins, which reflect cost efficiency, and return on investment achieved by the firm (Titman et al., 2018). Business entities generally focus on maximizing profitability through operational activities that require commitment from both owners and management (Rodriguez et al., 2024). A higher level of profitability indicates a greater ability to generate profits and reflects stronger financial performance (Anggreini & Kusuma, 2024; Hendayana et al., 2024). Therefore, profitability in this study refers to a key performance indicator that reflects a firm's ability to generate sustainable earnings and maintain financial health.

Thin Capitalization

Thin capitalization refers to a firm's financing decision to prioritize debt over equity in funding its operations (Mahmudi & Lasulita, 2025). It is commonly understood as a capital structure condition in which a company relies more heavily on debt than equity (Ravanelly & Soetardjo, 2023). Similarly, Rini et al. (2022) define thin capitalization as a strategy in which firms finance business activities primarily through debt rather than their own capital. In taxation, thin capitalization is often associated with tax avoidance because interest expenses from debt can be deducted from taxable income, thereby reducing the firm's tax burden (Nurdiansyah & Masripah, 2023). Thin capitalization rules are designed to limit a company's ability to deduct excessive interest expenses from taxable income (Goerdt & Eggert, 2022). Therefore, thin capitalization in this study refers to a financing practice in which firms rely more on debt than equity, allowing deductible interest expenses to reduce fiscal income.

Based on the literature review above, this study proposes the following hypotheses:
H1: Profitability has a positive and significant effect on tax avoidance
H2: Thin capitalization has a positive and significant effect on tax avoidance

METHODS

This study uses quantitative and associative design. The data used in this study are secondary data obtained from the annual financial reports of mining sector companies listed on the Indonesia Stock Exchange (IDX) during the 2021–2024 period. The statistical analysis was conducted using IBM SPSS Statistics 31.

This study applies multiple linear regression using the ordinary least squares (OLS) estimation method. Since the data consist of cross-sectional and time-series observations, all firm-year observations are pooled into one regression model without estimating firm-specific or time-specific effects. This method is used because the main objective of this study is to examine the general effect of profitability and thin capitalization on tax avoidance across the observed mining-sector companies.

The use of multiple linear regression with OLS estimation is supported by the characteristics of the research data. Since the data consist of cross-sectional observations from several companies and time-series observations from 2021 to 2024, all firm-year observations are pooled into one regression model. The sample consists of companies from the same broad industry group, namely mining-related companies classified under the energy and basic materials sectors. These companies operate under the same national tax regulations and are observed over a relatively short period of four years. In addition, the variables are measured using financial ratios, which help reduce scale differences across firms. Therefore, this pooled estimation approach is considered appropriate to examine the overall relationship among the variables in this study.

The population of this study consists of 204 mining-sector firms listed on the Indonesia Stock Exchange. Following the implementation of the IDX Industrial Classification (IDX-IC), mining-related companies are classified into two sectors: the energy sector and the basic materials sector. Additional criteria required firms to report profits throughout the observation period, remain unsuspended, report in rupiah, publish complete financial statements, avoid tax-overpayment status, and avoid final-income-tax treatment. After those filters, the final sample consisted of 12 firms, or 48 firm-year observations.

The study uses one dependent variable and two independent variables. Profitability is proxied by Return on Assets (ROA), thin capitalization by the Debt to Equity Ratio (DER), and tax avoidance by the Effective Tax Rate (ETR).

Table 1. Research Variable

No	Variable	Proxy	Formula
1	Profitability	Return on Asset (ROA)	$\frac{\text{Net Income}}{\text{Total Assets}}$
2	Thin Capitalization	Debt to Equity Ratio (DER)	$\frac{\text{Total Debt}}{\text{Total Equity}}$
3	Tax Avoidance	Effective Tax Rate (ETR)	$\frac{\text{Tax Expense}}{\text{Income Before Tax}}$

Source: Compiled by author

Tax avoidance in this study is proxied by the Effective Tax Rate (ETR). It should be emphasized that ETR is interpreted inversely in relation to tax avoidance. A lower ETR indicates a higher level of tax avoidance because the company pays a lower effective tax burden relative to its income before tax. Conversely, a higher ETR indicates a lower level of tax avoidance. Therefore, the interpretation of the regression coefficients is based on this inverse relationship.

RESULTS AND DISCUSSION

Descriptive Statistics

Table 2. Descriptive Statistics

Variable	N	Minimum	Maximum	Mean	Standard Deviation
Profitability	48	0,008859	0,340600	0,111764	0,0888127
Thin Capitalization	48	0,042329	1,491440	0,517338	0,3068284
Tax Avoidance	48	0,019502	0,418502	0,210178	0,0931396

Source: Data processed by author using IBM SPSS Statistics 31

Based on Table 2 of the descriptive statistics, it is evident that the profitability variable has an average value of 0.111764, with a range between 0.008859 and 0.340600. Meanwhile, the thin capitalization variable shows an average value of 0.517338, ranging from 0.042329 to 1.491440. In terms of tax avoidance, which is proxied by ETR, the variable records an average value of 0.210178, with a range between 0.0195023 and 0.418502. Since ETR is inversely related to tax avoidance, lower ETR values reflect higher indications of tax avoidance. Furthermore, the standard deviation values are 0.0888127 for profitability, 0.306828 for thin capitalization, and 0.093139 for tax avoidance proxied by ETR, indicating variation in each variable across the observed companies.

Classic Assumption Tests

Table 3. Result of Classic Assumption Tests

Classic Assumption Tests	Test Result	Conclusion
Normality Test	Sig. 0,2	Normal
Multicollinearity Test	TOL 0,869; VIF 1,151	No multicollinearity
Heteroscedasticity Test	X1 0,686; X2 0,908	No heteroscedasticity
Autocorrelation Test	DW 0,889	No autocorrelation

Source: Compiled by author using IBM SPSS Statistics 31

Based on the results of the classical assumption tests presented in Table 3, the regression model in this study has met the required assumptions. Therefore, the multiple linear regression model using OLS estimation with pooled firm-year observations is considered statistically appropriate for further analysis.

The normality test shows a significance value of 0.200, which is greater than 0.05. This indicates that the data are normally distributed. Furthermore, the multicollinearity test shows a tolerance value of 0.869 and a VIF value of 1.151. Since the tolerance value is greater than 0.10 and the VIF value is less than 10, it can be concluded that there is no multicollinearity among the independent variables.

The heteroscedasticity test also shows that the significance values of both independent variables are greater than 0.05, with X1 having a significance value of 0.686 and X2 having a significance value of 0.908. These results indicate that the regression model is free from heteroscedasticity. In addition, the autocorrelation test using the Durbin-Watson statistic shows a value of 0.889. Based on (Santoso, 2019), a Durbin-Watson value between -2 and +2 indicates that there is no autocorrelation. Therefore, the regression model used in this study is free from autocorrelation and is considered appropriate for further regression analysis.

Table 4. Coefficient of Determination Test

Model	**R**	**R Square**	**Adjusted R Square**	**Std. Error of the Estimate**
1	0,420	0,177	0,140	0.08637851

Source: Data processed by author using IBM SPSS Statistics 31

Based on Table 4, the R value of 0.420 indicates a moderate relationship between the independent variables, profitability and thin capitalization, and the dependent variable, tax avoidance. The R Square value of 0.177 shows that the regression model is able to explain 17.7% of the variation in tax avoidance. However, because this study uses more than one independent variable, the Adjusted R Square value is more appropriate to interpret. The Adjusted R Square value of 0.140 indicates that profitability and thin capitalization explain 14% of the variation in tax avoidance, while the remaining 86% is influenced by other factors outside the model. These factors may include corporate governance, firm size, leverage, corporate social responsibility, capital intensity, institutional ownership, audit quality, managerial factors, tax regulations, and tax supervision.

F Tests (Simultaneous)

Table 5. F Tests Results

Model	Sum of Squares	Df	Mean Square	F	Sig.
Regression	0,72	2	0,36	4,823	0,013[b]
Residual	0,336	45	0,007		
Total	0,408	47			

Source: Data processed by author using IBM SPSS Statistics 31

The F-test was used to assess the simultaneous effect of profitability and thin capitalization on ETR as a proxy for tax avoidance. The ANOVA results show a significance value of 0.013, which is below the 0.05 threshold. This indicates that the regression model is statistically feasible and that profitability and thin capitalization jointly have a significant effect on ETR as a proxy for tax avoidance.

Hypothesis Testing (t-test)

Table 6. t-tests Results

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig
	B	Std. error	Beta		
(Constant)	0,212	0,035		5,997	<0,001
Profitability	-0,309	0,152	-0,295	-2,032	0,048
Thin Capitalization	0,064	0,044	0,211	1,454	0,153

Source: Data processed by author using IBM SPSS Statistics 31

The regression equation is:

Tax Avoidance (ETR) = 0.212 – 0.309 Profitability + 0.064 Thin Capitalization + e

The t-test results indicate that profitability partially has a negative and significant effect on ETR. This is shown by a regression coefficient of -0.309 and a significance value of 0.048, which is lower than 0.05. Since ETR is inversely related to tax avoidance, a decrease in ETR indicates an increase in tax avoidance. Therefore, the negative coefficient of profitability on ETR implies that higher profitability is associated with higher tax avoidance. Thus, the first hypothesis is accepted. In contrast, thin capitalization shows a positive but insignificant effect on ETR, with a regression coefficient of 0.064 and a significance value of 0.153, which exceeds 0.05. The positive coefficient suggests that higher thin capitalization tends to increase ETR, which reflects a lower tendency toward tax avoidance. However, because the effect is not statistically significant, thin capitalization is not proven to significantly influence tax avoidance. Therefore, the second hypothesis is rejected.

The Effect of Profitability on Tax Avoidance

Based on the partial statistical test using the t-test, hypothesis H1, which states that profitability has a positive and significant effect on tax avoidance, is accepted. The regression result shows that profitability has a negative and significant effect on ETR, with a coefficient of -0.309 and a significance value of 0.048. Since tax avoidance in this study is proxied by ETR, the interpretation must consider the inverse relationship between ETR and tax avoidance. A lower ETR indicates a higher level of tax avoidance. Therefore, the negative coefficient of profitability on ETR indicates that higher profitability is associated with lower ETR, which reflects a higher tendency toward tax avoidance. The effect is statistically significant, as the significance value of 0.048 is below the 0.05 threshold.

This finding suggests that more profitable companies may have stronger incentives to manage their tax burden because higher earnings can increase the amount of tax payable. This result is consistent with agency theory, which explains that managers may use tax planning strategies to reduce tax expenses and increase after-tax earnings. In this context, higher profitability provides greater room and incentive for companies to engage in tax planning.

However, from the stakeholder theory perspective, this condition may create a conflict between shareholders' interest in tax efficiency and the government's expectation that companies fulfill their tax obligations fairly.

This study is consistent with Novianti & Masyitah (2023), who found that profitability has a positive and significant effect on tax avoidance. However, this finding contradicts Sari et al. (2021), who reported that profitability has no significant effect on tax avoidance.

The Effect of Thin Capitalization on Tax Avoidance

The results of the t-test indicate that thin capitalization has a positive but insignificant effect on ETR, leading to the rejection of H2. The regression coefficient of 0.064 suggests that an increase in thin capitalization tends to increase ETR. Since tax avoidance is proxied by ETR, where a higher ETR indicates a lower level of tax avoidance, this result implies that thin capitalization tends to reduce tax avoidance. However, the effect is not statistically significant, as the significance value of 0.153 exceeds the 0.05 threshold.

Thin capitalization reflects a firm's reliance on debt over equity, where interest expenses can reduce taxable income and potentially lower the effective tax burden. Nevertheless, this study finds that thin capitalization does not significantly affect ETR or tax avoidance. This may be explained by the relatively low Debt-to-Equity Ratio (DER) observed in the sample, ranging from 0.042 to 1.491, which remains well below the 4:1 limit set by Regulation of the Minister of Finance of the Republic of Indonesia Number 169/PMK.010/2015. This indicates that firms' capital structures are still within reasonable limits and do not reflect excessive debt usage, thereby limiting the tax benefits derived from interest expenses.

Additionally, the sample consists of energy and basic materials companies with diverse operational characteristics, leading to varying financing needs and capital structure policies. In the mining sector, debt is primarily used for long-term investments such as heavy equipment, infrastructure, and exploration activities, rather than as a tax minimization strategy.

The insignificant result may also be attributed to the use of alternative, more compliant tax planning strategies, such as tax incentives, fiscal depreciation, loss compensation, and arm's length transfer pricing. Moreover, tax avoidance may be influenced by other factors not included in this study, such as firm size, leverage, CSR, corporate governance, capital intensity, and audit quality.

These findings are consistent with Pangestu et al. (2023), who reported no significant effect of thin capitalization on tax avoidance, but contradict Haitsamathif & Putri (2024), who found a positive and significant relationship.

CONCLUSION

This study examines the effect of profitability and thin capitalization on tax avoidance in mining sector companies listed on the Indonesia Stock Exchange during the 2021–2024 period. Based on purposive sampling, 12 companies with 48 observations were selected and analyzed using IBM SPSS Statistics 31.

The results show that profitability has a negative and significant effect on ETR. Since tax avoidance is proxied by ETR, where a lower ETR indicates a higher level of tax avoidance, this finding indicates that more profitable companies tend to have lower ETR, reflecting a higher tendency toward tax avoidance. This result suggests that companies with higher profitability may have stronger incentives to manage their tax burden because higher earnings can increase the amount of tax payable. Therefore, H1 is accepted. This finding is consistent with Novianti & Masyitah (2023).

Meanwhile, thin capitalization has a positive but insignificant effect on ETR. A positive coefficient on ETR indicates that higher thin capitalization tends to be associated with a lower tendency toward tax avoidance. However, because the effect is not statistically significant, thin capitalization is not proven to significantly influence tax avoidance practices. Therefore, H2 is rejected. This result is consistent with Pangestu et al. (2023).

Although this study uses panel data, multiple linear regression using OLS estimation with pooled firm-year observations is applied because the analysis focuses on estimating the general relationship between profitability, thin capitalization, and ETR as a proxy for tax avoidance across the observed sample, rather than examining firm-specific or time-specific effects.

This study provides practical implications for regulators, investors, and companies in understanding factors that influence tax avoidance in the mining sector. Theoretically, this study contributes empirical evidence that profitability is significantly associated with tax avoidance when measured through ETR, while thin capitalization does not significantly affect tax avoidance.

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