

The Effect of Tax Differences Book on Income Growth

(Empirical Study of Manufacturing Companies Listed on the Indonesia Stock Exchange in 2014-2018)

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Abstract—This study aims to find empirical evidence of the effect of book-tax differences on earnings growth. Earnings growth is measured using changes in net profit after tax. The independent variables used in this study are temporary differences and permanent differences, while the dependent variable is earnings growth for the next period. The sample is determined based on the purpose sampling method of manufacturing companies listing on the Indonesia Stock Exchange in the 2014-2018 period with a total of 150 companies. The sample was determined based on the purposive sampling method, then the number of samples obtained in this study amounted to 39 companies, so that the total observation in this study was 195 observations. The data used in this study were secondary data, in the form of financial reports and annual reports downloaded via the official IDX website: www.idx.co.id. Data were analyzed using panel data regression analysis which was processed using Eviews software version 10.0. Hypothesis testing using statistical tests *t*. The results obtained are permanent variable differences from book-tax differences and temporary differences from book-tax differences do not affect earnings growth.

Keywords: *book tax differences, permanent differences, temporary differences, profit growth*

I. INTRODUCTION

For the government, in this case government agencies related to taxation include the Directorate General of Tax (DGT). In a policy or regulation that has been regulated in the Taxation Law that profits earned by taxpayers both individuals and entities are obliged to report the profits obtained. The reported profits of the company become the basis in determining the tax payable that must be paid by a company.

Law General Provisions and Tax Procedures (KUP) No. 28 of 2007 Article 1 Paragraph 1, tax is a mandatory contribution to the state owed by individuals or entities that are coercive based on the law, with no direct compensation and used for the country's needs for the greatest prosperity of the people. For the state, tax is one source of income [1].

The difference in interests from the government is to expect large and continually increasing tax revenues each year, and of course contrary to the interests of companies that want to pay as little or as little tax as possible. On the other hand, for tax

companies is the cost that must be spent so as to reduce net income. This can lead to efforts to fight or avoid tax both in the form of tax avoidance and tax evasion.

There is a difference of interest in the financial statements that the company calculates based on financial accounting standards and financial statements that are calculated based on applicable taxation provisions. From the two versions of the financial statements there are differences in the amount of profit. This is due to the difference in the treatment of recognition in the calculation of earnings according to accounting (book income) with earnings / income according to tax (taxable income) or often referred to as the book-tax difference.

Book tax differences are differences in the amount of accounting profit or commercial profit with fiscal profit or taxable income. Book-tax differences arise from differences that are temporary (temporary differences) and are permanent (permanent differences).

Temporary differences are due to differences in accounting methods and when revenue and costs are recognized. Temporary differences are projected to affect earnings in the future because this temporary difference will result in deferred tax assets and deferred tax liabilities.

There is a difference in purpose and a loss in the previous year that can be compensated for profit in the current year and this is a permanent difference. So companies have to make adjustments due to a difference in interests, namely accounting interests and tax interests. Therefore it is necessary to calculate profit according to fiscal or referred to as fiscal reconciliation.

Permanent differences arise due to differences in recognition of transactions between accounting rules and tax regulations. Permanent differences are items included in one profit measure, but not included in another profit size. For example deposit interest is recognized as income in accounting profit, but in taxes it is not recognized as income and income is final. So that it can affect the amount of profit the company earns.

Because some of the income recognized in the accounting rules can add to the company's profit, but in the tax regulation the income is not recognized and must be excluded from the

calculation of fiscal profit (taxable income). This causes the profit according to fiscal (taxable income) to be low so that it will affect the payment of taxes or taxes owed that must be paid by companies getting smaller and vice versa. If the net profit generated by the company increases, it can affect the company's profit growth.

In commercial financial statements that are used as a basis in fiscal reconciliation for the calculation of taxable income or taxable income (PKP) often do not represent the actual state of the company's economy. This is due to the company's management trying to display good financial performance through accounting policies, so that it will affect the amount of profit growth that will come.

Previous research conducted that book tax differences can provide information about company profits and future company performance. The information was obtained not only due to earnings management practices conducted by companies, but because of differences in applications between accounting provisions based on Financial Accounting Standards with fiscal provisions based on Taxation. This is proven by research that the relationship between book tax differences and earnings growth is not always caused by earnings management, but also due to the treatment of different economic transactions and fluctuating effective tax rates [2].

In Nia's research, permanent and temporary differences affect earnings growth [3]. And there was no influence between permanent and temporary differences with earnings growth [4].

Researchers are more interested in researching on manufacturing companies because of changes in product prices that are fast enough, visible and tight competition, unstable conditions with global conditions and manufacturing companies can generalize the characteristics of companies listed on the Indonesian stock exchange.

The sample used in this study is manufacturing companies listed on the Indonesia Stock Exchange, and the period of this research is 2014 to 2018. Based on the above background, the researchers are interested in conducting research with the title: "The Effect of Book Tax Differences on Profit Growth" "Empirical Study of Manufacturing Companies Listed on the Indonesia Stock Exchange in 2014-2018".

II. METHODS

The type of data used in this study is secondary data in the form of financial statements of manufacturing companies that have been published during the period of 2014 to 2018, taken through the site www.idx.co.id.

The population used in this study are all manufacturing companies listed on the Indonesia Stock Exchange in 2014, 2015, 2016, 2017 and 2018. Sampling in this study by using purposive sampling method. The purposive sampling method is the technique of determining the sample with certain consideration [1]. The selected sample is based on the suitability of the characteristics with the sample criteria specified in order to obtain a representative sample.

- Manufacturing companies listed on the Indonesia Stock Exchange (IDX) period 2014-2018. Amount 150.

- Manufacturing companies that do not publish complete and consecutive annual reports in 2014-2018 (51).
- Manufacturing companies that present annual reports in foreign currencies (27).
- Companies that suffered losses in the 2014-2018 period (30).
- Companies that do not have the variable components needed in the study (3).

The number of research samples (39 x 5 years = 195).

A. Definition and Operational Variables

The definition of operational variables is an explanation of the theoretical meaning of variables that can be observed and measured, and the parameters used in this study are:

1) Variable depend (Y)

a) *Profit growth*: Earnings growth is the change in profits generated by the company from period to period. This profit growth can be used as a basis by stakeholders for decision making. Earnings growth is calculated by subtracting current period earnings by prior period earnings then divided by previous period earnings [5], and formulated as follows:

$$\Delta NI = \frac{NI_{it} - NI_{i(t-1)}}{NI_{i(t-1)}} \quad (1)$$

2) Independent variable (X)

a) *Permanent differences or permanent differences (X₁)*: Permanent differences or permanent differences occur because income and expense transactions are recognized according to commercial accounting and not recognized according to fiscal terms. Permanent differences are obtained from the number of differences presented in the notes to the financial statements divided by total assets [6].

$$\text{Permanent Difference} = \frac{\text{Total Permanent Differences in fiscal reconciliation}}{\text{Total Asset}} \quad (2)$$

b) *Temporary differences or time differences (X₂)*: Time or temporary differences are temporary differences due to the unequal time of recognition of income and burdens between tax regulations and financial accounting standards. Temporary differences occur because of the time of recognition of income and expenses between taxes and accounting [7]. Temporary differences in this study were obtained from the amount of temporary differences contained in the notes to the financial statements divided by total assets [6].

$$\text{Temporary Difference} = \frac{\text{Total Temporary Difference in fiscal reconciliation}}{\text{Total Asset}} \quad (3)$$

B. Research Strategy

Analyser used in this research is by multiple linear regression analysis by using panel data. This study uses quantitative data obtained from annual reports and financial statements of the company in 2014, 2015, 2016, 2017 and 2018. The data obtained from the official website of Indonesia

Stock Exchange is <http://www.idx.co.id>. Data obtained from annual reports and financial statements of the company will be researchers though using software Eviews Version 10.0.

C. Research Panel Data Regression Model

The data used in this study is the annual time series data (annual) for 5 years, 2014 - 2018 and cross section data as many as 39 manufacturing companies that have been selected based on predetermined criteria.

III. RESULTS AND DISCUSSION

A. Profit Growth

Operating profit is the difference between realized revenue arising from transactions during one period and the costs associated with that income. Profit is an increase in economic benefits during an accounting period (for example, an increase in assets or a decrease in liabilities) which results in an increase in equity, other than those involving transactions with shareholders [8]. The size of the profit as a measure of increase depends on the accuracy of the measurement of income and costs. So in this case profit is only an articulation number and is not defined separately economically like assets and debt [9]. Earnings have several characteristics including the following [10]:

- Profit is based on transactions that actually took place.
- Profit is based on periodic postulates, meaning that it is the company's achievements in a certain period.
- Profit is based on the principle of income which requires a special understanding of the definition, measurement and recognition of income.
- Profit requires measurement of costs in the form of historical costs incurred by the company to get certain income.
- Profit is based on the principle of matching (matching) revenue and costs that are relevant and related to income.

Profit shows the company's performance as a result of its operational activities. The exact comparison of revenues and costs is reflected in the income statement. Presentation of earnings through financial statements reports aims to provide useful information for interested parties. According information about company profits can be used:

- As an indicator of the efficiency of the use of funds embedded in the company which is realized in the rate of return.
- As a measure of management achievement.
- As a basis for determining the amount of tax.
- As a means of controlling the allocation of a country's economic resources.
- As a basis for compensation and bonus distribution.

- As a motivational tool for management in corporate control.
- As a basis for increasing prosperity.
- As a basis for dividend distribution [9].

B. Book Tax Differences

According to PSAK no. 1 paragraph 9 (Revised 2015), Financial statements are a structured presentation of the financial statements and financial performance of an entity [11]. The purpose of financial statements is to provide information about the financial position, financial performance and cash flow of the entity to users such as investors. Book tax differences are differences in the amount of accounting profit or commercial profit with fiscal profit or taxable income.

The cause of differences in commercial financial statements and fiscal financial statements is because there are differences in accounting principles, differences in accounting methods and procedures, differences in recognition of income and costs, as well as differences in treatment of income and costs [12]. According to Financial Accounting Standards, the purpose of financial statements is to provide information regarding the financial position, as well as changes in the financial position of a company that is useful for a large number of users in the context of decision making. Some generally accepted principles (Financial Accounting Standards abbreviated as SAK) that have been generally recognized in the business and professional world but are not recognized in the fiscal, namely the principle of conservatism, the principle of cost acquisition, the principle of cost-benefit matching [12].

Costs recognized as a deduction from accounting profit, but not recognized as a deduction from profits according to tax stated in Article 9 (1) of Tax Regulations These costs include costs that may not be deducted from gross income, such as giving benefits to employees in the form of benefits or benefits, etc. In the context of tax accounting, these differences lead to two types of differences, namely permanent differences and time differences [1].

C. Temporary Difference

Temporary difference is the difference between accounting profit and taxable profit or Fiscal profit which is caused by taxation provisions and gives future influence in a certain period so that the effect on accounting profit and Fiscal profit finally becomes the same. The time difference occurs because of the time difference between the recognition of revenues and costs in calculating profits [12]. A cost or income that has been recognized according to commercial accounting and has not been recognized according to Fiscal, or vice versa.

In the case of acknowledgment of correction income due to time difference occurs due to receipt of cash basis income for more than one year. In commercial accounting the income must be allocated according to the acquisition period in accordance with the principle of matching cost with revenue. Whereas according to the Income Tax Law, such income must be recognized at the same time upon receipt [1].

Temporary differences will cause a shift in the recognition of income or costs to the following year or to another year. Four transactions that can cause time / temporary differences include [13]:

- Income that is included in the tax calculation after accounting profit: gross profit on instalment sales, gross profit on long-term contracts, income from investment in shares.
- Tax calculation cost or loss after accounting profit: estimated cost of guarantee / product guarantee, estimated loss of purchase contract, inventory, losses on receivables and short-term investment.
- Tax income before accounting profit: rent, interest and slush.
- Tax costs or losses before accounting profit: depreciation and costs during the construction of fixed assets (such as taxes and interest).

Temporary differences are a reflection of certain discretionary accruals implemented by companies. This accrual policy results in a time difference between the recognition of income or costs between accounting and tax. Given that the accrual policy allows managers to manage earnings, the temporary differences that contain the accrual policy are relevant in predicting the company's future performance. Temporary differences used as variables in this study were obtained from the amount of temporary differences contained in the financial statement notes divided by total assets.

D. Permanent Difference

The permanent difference is the difference between accounting profit and fiscal profit caused by taxation provisions and will not cause fibre accounting problems to have no effect on tax obligations in the future. Permanent differences occur because income and expense transactions are recognized according to accounting and not recognized according to Fiscal and vice versa. Permanent differences result in net income (loss) according to accounting (permanently) with taxable income (profit) according to Fiscal [12]. Permanent differences are caused by different arrangements related to the recognition of income and costs between Financial Accounting Standards and Provisions in Tax Regulations. So it can be said that based on the provisions of the taxation legislation there are some income which is not a tax object, but commercially the income is recognized as income. Vice versa, there are several costs according to the provisions of tax legislation, including fiscal costs that should not be deducted, whereas according to the commercial, these costs are calculated as costs. In general, permanent differences that occur due to differences in recognition of income and costs, for example:

- Aid, donations, including zakat received by amil zakat bodies that are formally established.
- Inheritance.

- Reimbursement or compensation in connection with work or services received or obtained in kind and / or enjoyment from taxpayers or the government;
- Payments from insurance companies to private persons in connection with health insurance, accident insurance, life insurance, dual purpose insurance and scholarship insurance;
- Dues received or obtained by pension funds, the establishment of which has been approved by the Minister of Finance.
- Share of profits received or obtained by members of limited partnership companies whose capital is not divided into shares, partnerships, firms and partnerships.
- Distribution of profits by name and in any form such as dividends, including dividends paid by insurance companies to policyholders, and the distribution of the remainder of the cooperative's business results.
- Costs charged or incurred for the personal benefit of shareholders, allies, or members.
- Establishment or fertilization of reserve funds, except for reserves of uncollectible accounts for the business of banks and other business entities that distribute credit, leases with option rights, consumer finance companies, and factoring companies.
- Reimbursement or compensation in connection with work or services provided in kind and enjoyment.
- Amount that exceeds the fairness paid to shareholders or to parties who have a special relationship.
- Income tax.
- Expenditures for obtaining, collecting, and maintaining income that has a useful life of more than 1 (one) year are not allowed to be charged at once, but are charged through depreciation or amortization.

Permanent differences occur if the difference in fiscal earnings and annual commercial profits will not be recovered in the future so that there are also differences in fiscal and commercial profits. Permanent differences can be positive if the commercial profit is greater than the fiscal profit) or negative if the commercial profit is smaller than the fiscal profit. Because viewed from the accounting side, the positive or negative terminology is the opposite of the term positive / negative correction for taxation purposes. For the calculation of taxable income, different arrangements that cause fiscal profits to be greater than commercial profits in tax administration are called positive corrections, whereas differences in regulations that cause smaller fiscal profits than commercial profits are called negative corrections. Because book tax differences and their components have a value that is relevant to earnings in the current year and can be used to evaluate future performance and explain company equity, permanent differences are used as independent variables that will complement the temporary differences in predicting earnings growth. Permanent differences referred to in this study were obtained from the

amount of permanent differences presented in the financial statement notes divided by total assets.

The following will be described test results on hypothesis regression statistical test results t:

1) *Hypothesis test results 1: Permanent differences from book tax:* The first hypothesis in this study is that permanent differences from book tax differences do not affect earnings growth. The results of the regression test, show the value of t is smaller than t table (-1.794248 < 1.972396). While the probability results are greater than the significance level (0.0810 > 0.05). Based on the test results above, it can be concluded that H1 which states that permanent differences from book tax differences affect earnings growth, is rejected differences on earnings growth.

2) *Hypothesis test results 2: Temporary differences from book tax differences on earnings growth:* The second hypothesis in this study is the temporary differences from book tax differences do not affect earnings growth. The results of the regression test, show the value of t is greater than t table (1.719212 < 1.972396). While the probability results are greater than the significance level (0.3457 > 0.05). Based on the test results above, it can be concluded that H2, which states that the temporary differences from book tax differences, affect earnings growth is rejected. This can be interpreted that there is no significant effect between the temporary differences of the book tax differences on profit growth which is proxied by the amount of profit for the period with the previous period profit then divided by the previous period profit.

IV. CONCLUSION

Based on the results of research on the factors that affect tax avoidance. Empirical study of manufacturing companies listed in Indonesia Stock Exchange (IDX) period 2014-2018, it can be concluded as follows:

- The first variable shows that the first hypothesis in this study is the permanent difference from the book tax differences does not affect earnings growth. In this study permanent differences that do not affect earnings growth are the effects of the amount of permanent differences from the book tax differences that are not too significant to the amount of taxable income or taxable income. Tax is a component of forming corporate income tax burden in addition to deferred tax. The amount of tax has a large influence on the amount of income tax expense paid by the company. Income tax expense is a deduction from profit before tax to net income. This is that the high or low value of a permanent difference will not guarantee a growth in operating profit in the future or future periods. In addition, permanent differences from book tax differences have a negative impact on business profit growth. The results of this study are in line with the results of research conducted by Amos which states that

permanent differences do not have a significant positive effect on earnings growth [14].

- The second variable in this study is the temporary differences from book tax differences do not affect earnings growth. In this study shows the temporary differences from book tax differences have a positive regression coefficient which means the higher the temporary difference from book tax differences, it will have an impact on increasing earnings growth with a significant effect. This is due to a temporary difference from the book tax differences with a positive fiscal correction and the net increase in deferred tax assets and deferred tax liabilities that are not too significant to the income tax burden. So that the tax burden or tax owed to be paid by the company is getting higher or increasing which results in a smaller amount of profit after tax paid. The results of this study are in line with the results of Purnama et al. which states that temporary differences do not have a significant positive effect on earnings growth [15].

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