

The Effect Of Tax Planning On Earnings Management Moderated By Tax Rate Reductions

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Abstract

This study aims to analyze the effect of tax planning on earnings management and examine the role of tax rate reductions as a moderating variable. Secondary data were obtained from the annual reports of manufacturing companies in the Consumer Non-Cyclical subsector listed on the Indonesia Stock Exchange (IDX) during the 2018–2023 period. Using a purposive sampling technique, 62 companies were selected out of a total of 67 that met the criteria, resulting in 372 observations. This research applies a quantitative approach using documentation methods and moderation regression analysis processed with SPSS version 27. The results show that tax planning has a significant and positive effect on earnings management, indicating that companies tend to engage in earnings management as tax efficiency increases through tax-saving strategies. However, when tax rate reduction is used as a moderating variable, the effect of tax planning on earnings management weakens. The tax rate reduction acts as a pure moderator that reduces the intensity of earnings management practices, as the incentive to manipulate earnings becomes lower. Thus, fiscal policies in the form of tax rate reductions can serve as an effective instrument to curb non-transparent financial reporting practices.

Keywords: tax planning, earnings management, tax rate reduction, moderation, manufacturing companies, IDX.



INTRODUCTION

Financial statements are a primary source of information used by organizations to make decisions. The choice of financial reporting techniques can influence how results are presented, thereby providing managers with the ability to manage earnings in various ways. The Association of Certified Fraud Examiners (ACFE) defines earnings management as deliberate or negligent actions in the preparation of financial reports that may mislead information users, especially when these reports are used as the basis for decision-making, thus potentially affecting user judgment and decisions.

According to Pramono (2020), earnings management emerges from managerial involvement in the financial reporting process. This approach includes increasing, decreasing, or smoothing profits to achieve specific organizational goals. Insyaroh and Widiatmoko (2022) emphasize that earnings management is an intentional effort by management to manipulate data in income statements, resulting in financial reports that do not accurately reflect a company's actual financial condition.

Earnings management is often driven by conflicting interests in achieving certain goals, which may harm economic, ethical, and moral standards. Kurniawansyah (2018) argues that certain earnings management practices are detrimental due to differing perspectives and understandings of these techniques. To date, earnings management remains a controversial issue among practitioners and academics, particularly in determining whether such practices constitute fraud.

Some practitioners classify earnings management as a form of fraud, while many academics tend to maintain a neutral stance. Scott (2015) provides two perspectives: the opportunistic perspective, where managers use accounting policies to achieve personal gain (e.g., through compensation schemes or debt contracts), and the efficient contracting perspective, where earnings management provides flexibility to balance the interests of parties involved in contracts.

Positive earnings management aims to present profits higher than actual, often to signal good performance to stakeholders. In contrast, negative earnings management seeks to understate profits, for example, to minimize tax burdens or manipulate performance metrics for incentives. These strategies are deployed based on management's goals (Subadriyah et al., 2020).

Numerous financial scandals have arisen from earnings management practices, including the case of PT Tiga Pilar Sejahtera Food Tbk (AISA). Allegations of earnings inflation amounting to IDR 4 trillion were revealed following a fact-based investigation by



Ernst & Young Indonesia in 2019. The manipulation included inflated accounts receivable, inventories, and fixed assets, as well as unreported fund transfers to related parties.

Similarly, Apple Korea was accused of manipulating its financial statements to reduce corporate income tax obligations by reporting low operating profits and channeling import expenditures through Apple South Asia in Singapore. These cases reflect both positive and negative earnings management and demonstrate the risks of inadequate transparency and compliance in financial reporting.

Given the growing evidence of earnings management across various organizations, this study focuses on companies in the manufacturing sector, particularly the non-cyclical consumer sub-sector, due to the sector's relevance to earnings management and tax planning practices.

Strategic motives often drive profit control practices, with tax planning being one of the main incentives. Companies typically view taxes as a cost to be minimized legally. Within this context, efficient fiscal planning is used to reduce tax burdens while remaining compliant with regulations. This has become more relevant during the COVID-19 pandemic, which severely impacted global economies and business liquidity.

Structured tax planning, often involving negative earnings management, was utilized during the pandemic to reduce tax obligations, thus helping companies maintain operations. According to Tax Justice Network (2020), Indonesia lost approximately IDR 69.1 trillion in potential tax revenue, underscoring the increase in tax avoidance and aggressive tax planning during the crisis.

Historical data from 2018 to 2020 further reveals consistent shortfalls in tax revenue compared to targets. However, from 2021 to 2023, revenue performance improved, supported by government policies such as the corporate income tax rate reduction under Government Regulation in Lieu of Law (Perppu) No. 1 of 2020 and the Harmonized Tax Law (UU HPP) of 2022. The tax rate dropped from 25% to 22%, aiming to ease the burden on businesses and reduce the need for manipulative financial practices.

These regulatory reforms are expected to reduce earnings management motives and improve tax compliance. With lower tax rates, businesses gain more financial freedom for productive investments, such as dividends or expansion, thereby decreasing pressure on management to manipulate earnings.

Prior studies have mostly explored positive earnings management, driven by incentives such as dividend payouts and bonus plans (e.g., He et al., 2017; Arif et al., 2011; Guidry et al., 1999; Silalahi & Warokka, 2023). Conversely, negative earnings

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management related to tax planning remains under-researched. While studies like Romantis et al. (2020) and Jeradu (2021) suggest a significant link between tax planning and earnings management, other researchers (e.g., Tartono et al., 2021; Devitasari, 2022) found no significant or even negative influence.

These inconsistent findings indicate the need for further research using a more comprehensive framework, broader sample coverage, and updated regulatory context. This study incorporates corporate tax rate reduction as a moderating variable, aligned with recent fiscal policies under Perppu No. 1/2020 and UU HPP 2022, thus offering new insight into the interaction between tax planning and earnings management.

Therefore, this research expands on the study by Romantis et al. (2020), titled “The Influence of Tax Planning on Earnings Management Moderated by Corporate Tax Rate Reduction,” and aims to contribute to accounting literature by evaluating how updated tax policies affect managerial behavior in financial reporting.

LITERATURE REVIEW

Agency Theory

Agency theory, proposed by Jensen and Meckling (1976), posits that a contractual relationship exists between principals (owners) and agents (managers), where the principal delegates decision-making authority to the agent. Ideally, this delegation should enhance firm value, as competent individuals manage the business under ownership oversight. However, agency conflicts often arise when agents pursue personal interests at the expense of the principal, exacerbated by information asymmetry (Suhartono & Hendraswari, 2020).

In the context of corporate taxation, firms (as agents) aim to maximize profits through cost minimization strategies, particularly by reducing tax burdens. Meanwhile, governments (as principals) seek to maximize tax revenue. This divergence in objectives creates a conflict of interest and may lead to opportunistic behaviors, such as aggressive tax planning or earnings management, especially under weak regulatory surveillance and high information asymmetry.

Government oversight is thus critical to mitigating moral hazard risks. While earnings management is not inherently illegal, it can exploit legal tax loopholes for corporate benefit (Astutik & Mildawati, 2016). Tax planning is considered a legitimate strategy for minimizing tax liabilities but may also act as a precursor to income manipulation. This study uses agency theory to examine the interactions between firms and tax authorities, emphasizing the role of regulatory oversight and the moderating effect

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of tax policy changes specifically the corporate tax rate reduction introduced by Government Regulation in Lieu of Law No. 1 of 2020.

Political Cost Hypothesis

Originating from Positive Accounting Theory (PAT), the Political Cost Hypothesis suggests that large firms may engage in earnings suppression to avoid political scrutiny, higher tax rates, or societal demands (Watts & Zimmerman, 1986). PAT includes three core hypotheses: the bonus plan hypothesis, debt covenant hypothesis, and political cost hypothesis. The latter is particularly relevant in the context of corporate taxation.

From this perspective, taxes represent political costs, and firms especially large or highly visible ones may strategically reduce reported earnings to mitigate such costs. Techniques include delaying revenue recognition or accelerating expense reporting. These actions not only reduce tax burdens but also deflect regulatory or public attention.

Recent Indonesian tax reforms specifically, the corporate tax cuts embedded in Perppu No. 1 of 2020 and Law No. 7 of 2021 on Tax Regulation Harmonization (UU HPP) have likely altered firms' incentives. With reduced tax rates, companies may find less reason to engage in income-reducing practices, choosing instead to report higher earnings to signal improved performance. This study investigates whether such tax cuts moderate the relationship between tax planning and earnings management, offering insights into fiscal policy effectiveness in curbing opportunistic financial behavior.

Earnings Management

Earnings management refers to the manipulation of financial reporting to achieve specific objectives, often by exploiting the flexibility of accounting standards (Scott, 2015). While sometimes used as a communication tool to convey private information (Arya et al., 2003; Ronen & Yaari, 2015), it is frequently employed opportunistically to deceive stakeholders, particularly in the context of tax avoidance or incentive compensation (Jamadar et al., 2022). High-profile accounting scandals such as Enron, WorldCom, and Parmalat have revealed how earnings management can severely distort financial transparency. In response, stricter regulations like the Sarbanes-Oxley Act (SARBOX) and listing requirements by NASDAQ have sought to improve audit oversight and governance structures (Jiraporn et al., 2008). Not all earnings management is illegal or detrimental. However, it becomes problematic when it undermines stakeholder trust. Scholars have developed various models to detect such behavior, including the Jones (1991) model and its modified version by Dechow et al. (1995), which more accurately

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distinguishes between discretionary and non-discretionary accruals. This research focuses on income-minimizing earnings management—a tactic firms employ to reduce taxable income. It is highly relevant to tax planning activities and can be effectively detected using accrual-based models like the modified Jones model.

Tax Planning

Tax planning involves legally minimizing tax liabilities through strategic business decisions. According to Suandy (2017), the goal is to achieve tax efficiency without violating prevailing tax laws. It encompasses compliance with tax policies, administration, and statutory regulations, all of which create the framework within which tax strategies are executed. Common tax planning approaches include:

1. Tax avoidance: exploiting legal loopholes;
2. Tax saving: selecting the most tax-efficient treatments;
3. Tax shifting: transferring tax burdens to affiliates or consumers;
4. Tax deferment: postponing tax liabilities;
5. Capitalizing vs. expensing: choosing cost recognition methods (Suandy, 2017).

In this study, tax saving is the focal strategy due to its legality and measurability using public financial data. The Tax Retention Rate (TRR) is employed as a proxy. Other strategies, like tax shifting or deferment, are less observable given data limitations. This focus ensures analytical clarity and robustness.

Corporate Tax Rate Reduction

In response to the economic downturn caused by COVID-19, Indonesia enacted a reduction in corporate income tax rates from 25% to 22% for 2020–2021 via Perppu No. 1 of 2020. This was followed by the Tax Regulation Harmonization Law (UU HPP) in 2021, which refined several aspects of tax legislation, including:

1. Exemptions for small enterprises (up to IDR 500 million turnover);
2. Adjusted tax rates for individuals and corporations;
3. Reforms in treatment of non-cash benefits and deductible expenses.

These reforms aim to align Indonesia's tax system with ASEAN and global best practices while stimulating economic recovery. This study uses the corporate tax rate reduction as a moderating variable, assessing whether lower tax rates reduce the incentive for earnings manipulation. By doing so, it evaluates the efficacy of fiscal policy in promoting financial transparency and discouraging aggressive tax strategies.



RESEARCH METHODOLOGY

This study focuses on manufacturing companies in the Consumer Non-Cyclical sector listed on the Indonesia Stock Exchange (IDX) during the 2018–2023 period, including both profitable and loss-making firms. This sector was selected due to the essential nature of its products, which generally maintain stable demand, requiring firms to sustain consistent financial performance. According to Alfabana and Dewayanto (2023), this sector was significantly affected by the COVID-19 pandemic, prompting the use of earnings management practices to preserve corporate reputation. Transparent and structured financial reporting in this sector presents both opportunities and challenges in managing earnings and tax planning.

Out of 67 companies within this sector, the sample was selected using a non-probability sampling method, specifically purposive sampling (Sugiyono, 2019). The criteria for sample selection were as follows: (1) the company must be categorized under the Consumer Non-Cyclical sector and listed on the IDX continuously from 2018 to 2023, (2) the company must have published audited annual financial reports during the observation period, and (3) the reports must be presented in Indonesian Rupiah (IDR). Based on these criteria, 62 companies met the requirements, resulting in a total of 310 firm-year observations over five years.

Data were collected through documentation techniques, which involved retrieving and recording information from annual reports available on the official IDX website (www.idx.co.id) and the respective companies' official websites (Kusuma & Priantinah, 2018). The data include accounting and fiscal variables such as net income, operating cash flows, assets, revenues, trade receivables, and tax expenses.

This research adopts a quantitative approach. Data analysis was performed using SPSS version 27. The analysis began with descriptive statistics to provide an overview of the data characteristics. Subsequently, classical assumption tests were conducted to ensure the validity of the Ordinary Least Squares (OLS) regression model, including the normality test (Kolmogorov–Smirnov), multicollinearity test (Variance Inflation Factor and Tolerance), and heteroscedasticity test (Glejser test). Hypothesis testing was then carried out using simple linear regression for the first model and Moderated Regression Analysis (MRA) for the second model. The coefficient of determination (R^2), F-test, and t-test were employed to evaluate the significance and explanatory power of the models.



Research Results and Discussion**Descriptive Statistics****Table 1. Descriptive Statistics**

Variable	N	Minimum	Maximum	Mean	Std. Deviation
Earnings Management	337	-0.5387	58.2743	1.787641	4.6019791
Tax Planning	337	-3.3210	15.0191	0.964566	1.7353298
Tax Rate Reduction	337	0	1	0.67	0.471
Valid N (listwise)					

Source: Processed using SPSS 27, 2024.

Based on the results above, the dependent variable (Y), earnings management, has a maximum value of 58.2743, which belongs to Leyand International Tbk (LAPD) in 2021. This indicates highly aggressive earnings management practices by the company during that year. Such behavior may reflect the company's attempts to adjust or manage financial statements for specific purposes, such as improving investor perception, meeting market expectations, or optimizing tax burdens. In some cases, companies may use earnings management techniques to create a more stable or favorable profit image than the actual performance.

The minimum value of -0.5387 also comes from Leyand International Tbk (LAPD), in 2018. This suggests the company experienced a significant decline in earnings or possibly a loss that year. The negative figure indicates that the firm may not have engaged in aggressive earnings management, and the financial statements reflected actual conditions. Such outcomes could result from factors like operational underperformance, unexpected cost increases, or external factors affecting the industry. Although the company reported lower earnings or losses, this may demonstrate transparency in financial reporting to stakeholders such as investors and regulators by avoiding earnings manipulation.

The mean of earnings management is 1.787641 per year, suggesting that on average, companies tend to manage earnings to reach certain targets annually. This indicates the extent to which earnings management practices influence corporate financial statements, typically to reduce tax liabilities or meet financial goals.



The standard deviation of 4.6019791 shows the data is widely dispersed. The mean being lower than the standard deviation suggests the presence of many extreme values or outliers, which could indicate data instability or inconsistency, potentially affecting interpretation and decision-making.

The independent variable (X), tax planning, has a maximum value of 15.0191, recorded by Mustika Ratu Tbk in 2023. This indicates that the company engaged in highly aggressive or structured tax planning, potentially maximizing benefits from tax incentives or favorable regulations.

The minimum tax planning value of -3.3210 belongs to Prasadha Aneka Niaga Tbk (PSDN) in 2023, implying that the company experienced inefficiencies in its tax planning strategy. A negative value could indicate suboptimal use of tax incentives or higher-than-expected tax liabilities. Companies with such outcomes should reassess their tax strategies, as this might signal inefficiencies or misalignment with current tax regulations.

The mean value of tax planning is 0.964566 per year, indicating that most companies in the sample tend to optimize their tax strategies while remaining compliant with regulations. A mean close to 1 suggests these firms make effective use of tax policies legally and ethically, aiming to reduce tax burdens without breaching legal boundaries. Nonetheless, optimal tax planning should also consider ethical responsibilities and contributions to the national economy.

The standard deviation of 1.7353298 shows that tax planning data vary considerably across firms. As with earnings management, the mean being lower than the standard deviation indicates the presence of outliers, which may affect the data distribution and complicate interpretations.

Meanwhile, the moderating variable (Z), tax rate reduction, has a maximum value of 1 and a minimum of 0, with a mean of 0.67 and a standard deviation of 0.471. This indicates that the values are relatively concentrated around the mean, with limited deviation. In other words, the data is relatively homogeneous, and most observations do not stray far from the average.

According to Government Regulation in Lieu of Law (Perppu) No. 1 of 2020, the corporate income tax rate was reduced from 25% to 22% for the 2020 and 2021 fiscal years. As a result, the calculation of Article 25 income tax installments in 2020 could use the new 22% rate, applying to both the 2019 fiscal year and subsequent periods. In this study, the tax rate change is operationalized as a dummy variable to distinguish between periods before and after the policy. Manufacturing firms in 2018 and 2019 were coded as 0, while those in 2020, 2021, and 2022 were coded as 1.

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The implementation of Perppu No. 1 of 2020, later ratified as Law No. 2 of 2020, had a significant impact on companies, including those in the consumer non-cyclical sector. Issued to address the economic impact of the COVID-19 pandemic, this regulation aimed to maintain national economic stability by lowering the income tax rate for affected businesses and simplifying tax compliance. Companies listed on the Indonesia Stock Exchange (IDX) could benefit from these incentives, such as the reduced 22% corporate tax rate or even lower for qualifying firms.

Classical Assumption Tests

This study conducted normality, multicollinearity, and heteroscedasticity tests, with the following results:

1. Normality Test

The Kolmogorov-Smirnov test produced an Asymp. Sig. value of 0.006 (< 0.05), suggesting non-normal distribution. However, the Monte Carlo Sig. value was 0.178 (> 0.05), indicating that the residuals are normally distributed.

2. Multicollinearity Test

Tolerance and VIF values were used to detect multicollinearity. The results showed a Tolerance of 1.000 and VIF of 1.000 for the tax planning variable, indicating no multicollinearity.

3. Heteroscedasticity Test

Using the Glejser test, the significance value for the tax planning variable was 0.842 (> 0.05), indicating no heteroscedasticity. Thus, the homoscedasticity assumption is fulfilled.

Regression Analysis

This study applies multiple regression analysis using two models to test the hypotheses. Model I, which excludes a moderating variable, assesses the direct effect of the independent variable (tax planning, X_1) on the dependent variable (earnings management, Y). This model employs simple linear regression to examine the extent to which one independent variable affects the dependent variable, identifying the direct relationship between tax planning and earnings management.

Model II incorporates a moderating variable to evaluate whether the tax rate reduction moderates the effect of tax planning on earnings management. An interaction test is applied to determine whether the tax rate reduction strengthens or weakens the influence



of tax planning. Table 2. presents the results of both the simple and moderated regression analyses.

Table 2. Regression Analysis Results

Model	Unstandardized Coefficients	B	Std. Error
I	(Constant)	1.785	0.093
	Tax Planning	0.129	0.047
II	(Constant)	1.518	0.158
	Tax Planning	0.278	0.065
	Tax Rate Reduction	0.441	0.194
	Interaction (Tax Planning × Tax Rate Reduction)	-0.292	0.092

Source: Processed using SPSS 27, 2024.

Model I – Simple Linear Regression Equation:

$$Y = \alpha + \beta X + e$$

$$Y = 1.785 + 0.129X + e$$

The constant (α) of 1.785 indicates the initial value of earnings management when the independent variable is zero. The coefficient for tax planning is 0.129, suggesting that a one-unit increase in tax planning leads to a 0.129 increase in earnings management. The positive coefficient indicates a positive relationship.

Model II – Moderated Regression Analysis (MRA) Equation:

$$Y = \alpha + \beta X + \beta M + \beta XM + e$$

$$Y = 1.518 + 0.278X + 0.441M - 0.292XM + e$$

The coefficient for tax planning (0.278) indicates a positive influence on earnings management. Similarly, tax rate reduction (0.441) also has a positive effect. However, the interaction term has a coefficient of -0.292 , indicating that an increase in the interaction variable decreases earnings management, meaning the moderating effect is negative.

Coefficient of Determination Test

The adjusted R^2 value reflects the extent to which the regression model explains variations in the dependent variable. Values closer to 1 indicate a stronger explanatory power, while lower values suggest limited predictive capability. Table 3. presents the results.



Table 3 Coefficient of Determination Results

Model	R	R Square	Adjusted R Square
I	0.149	0.022	0.019
II	0.230	0.053	0.044

Source: Processed using SPSS 27, 2024.

Model I explains only 1.9% of the variance in earnings management, while Model II explains 4.4%. The low adjusted R^2 values indicate that the models have limited explanatory power, implying that other factors not included in the model may influence earnings management.

Previous studies have identified several such factors, including corporate governance (Insyarah & Widiatmoko, 2022), managerial ownership and IFRS adoption (Ayem & Ongirwalu, 2020), firm characteristics (Giovani, 2017), firm size (Gayatri & Wirasedana, 2021), and free cash flow (Abubakar et al., 2021).

Model Feasibility Test (F-Test)

According to Sugiyono (2017), the F-test evaluates the joint influence of independent variables on the dependent variable. A model is considered feasible if the significance value (Sig. F) is ≤ 0.05 . The results are presented in Table 4.

Table 4. Model Feasibility Test Results

Model	Sum of Squares	df	Mean Square	F	Sig.
1	Regression	16.857	1	16.857	7.654
	Residual	737.782	335	2.202	
2	Regression	39.886	3	13.295	6.194
	Residual	714.753	333	2.146	

Source: Processed using SPSS 27, 2024.

As shown, Model 1 yields a Sig. F of 0.006, indicating that tax planning significantly affects earnings management. Model 2, with a Sig. F of 0.000, also confirms statistical significance, showing that the addition of the moderating variable does not compromise model validity.



Hypothesis Testing**Table 5. Hypothesis Testing Results**

Model	Variable	Coefficient (B)	Sig.	Conclusion
I (RS)	(Constant)	—	0.000	H1 supported
	Tax Planning	0.129	0.006	
II (RM)	(Constant)	—	0.000	H2 supported
	Tax Planning × Tax Rate Reduction	-0.292	0.002	

Source: Processed using SPSS 27, 2024.

For Model I, the tax planning variable has a significance value of 0.006 (< 0.05), indicating a significant positive effect on earnings management. This supports Hypothesis 1. In Model II, the interaction between tax planning and tax rate reduction has a significance value of 0.002 (< 0.05) and a negative coefficient (-0.292), suggesting that the tax rate reduction weakens the influence of tax planning on earnings management. Thus, Hypothesis 2 is also supported.

CONCLUSION

The following are several limitations of the study that may be identified based on previous findings and discussions regarding the Impact of Tax Planning on Earnings Management Moderated by Tax Rate Reduction:

1. The results of the first hypothesis test indicate that tax planning has a significant and positive effect on earnings management. This shows that the tendency of companies to engage in earnings management—particularly through strategies that minimize reported income—increases in line with the level of tax efficiency achieved through tax-saving strategies. This finding aligns with agency theory and the political cost hypothesis, which suggest incentives for adjusting financial statements to reduce tax burdens.
2. The effect of tax planning on earnings management diminishes when tax rates are reduced, which serves as a significant moderating variable. This implies that while businesses may still engage in tax planning, their incentive to manipulate accounting results decreases when tax rates are lowered, thereby reducing the intensity of income-reducing actions.



3. The results of the moderation interaction test indicate that the reduction in tax rates acts as a pure moderator, directly altering the strength of the relationship between tax planning and earnings management. Companies engaged in tax-saving strategies, yet facing lower tax rates, tend to be less inclined to conduct aggressive earnings management. This suggests that fiscal policies in the form of tax rate reductions can serve as control tools against non-transparent financial reporting practices..

Suggestion

Several parties can benefit from the following recommendations, which are based on the findings and previous presentations regarding the influence of tax planning on earnings management moderated by tax rate reduction:

1. Future research can examine tax planning in the form of more complex or aggressive strategies, such as tax avoidance or tax shifting, which may require more in-depth methodological approaches and data access—e.g., through internal company data or interviews with management. This is important for understanding how gray-area tax strategies interact with earnings management practices.
2. Further exploration is needed on various forms of earnings management—not limited to income minimizing—but also real earnings management and income smoothing. For this, the use of alternative measurement models such as real activity manipulation (RAM) or accrual-quality measures can contribute methodologically to expanding the understanding of managerial strategies in the taxation context.
3. Future studies may consider contextual or institutional variables as additional moderators, such as the influence of corporate governance quality (GCG), institutional ownership, capital market pressure, or litigation risk. These factors are believed to affect the strength of the relationship between tax planning and earnings management across different sectors and economic conditions.

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