

THE NEXUS OF LEVERAGE, PROFITABILITY, AND FIRM SIZE ON TAX PLANNING: IS IT MODERATED BY INSTITUTIONAL OWNERSHIP?

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Abstract

Investigating Institutional Ownership Moderates: The Effect of Leverage, Profitability, and Ownership of Company Size on Tax Planning in Consumer Cyclical Sector Companies listed on the Indonesia Stock Exchange between 2018 and 2023 is the main objective of this study. The study's population consists of consumer cyclical companies that were listed on the Indonesia Stock Exchange between 2018 and 2023. Over the course of three years, 11 companies out of 153 were chosen for this study using the purposive sample technique. Panel Data Regression Analysis is used in this work. Eviews12 software is used in this investigation. According to the study's findings, (1) leverage has no discernible impact on tax planning. (2) Tax planning is not much impacted by profitability. (3) Tax planning is significantly impacted by the size of the company. (4) The impact of leverage, profitability, and company size on tax planning cannot be moderated by institutional ownership.

Keywords: Leverage, Profitability, Company Size, Tax Planning, Institutional Ownership

1. Introduction

One emerging nation that is seeing strong economic growth is Indonesia. The taxes sector is one of the good economic growths that helps finance a nation's and society's needs. According to Law Number 16 of 2009, taxes are an obligatory payment to the state that is made without prompt payment and is used to fund public necessities. The first step in implementing tax management is tax planning. When creating a tax strategy, it is necessary to carry out stages that must be taken by company management that cannot be arbitrary, because the stages of this tax plan will be used by the Company so that the tax plan is not included in the category of tax evasion and does not violate applicable laws (Slemrod, 2004).

Tax planning efforts of PT Rajawali Nusantara Indonesia (RNI), which resulted in a debt of IDR 20.4 billion in the 2014 financial report, were one of the examples that took place in Indonesia. In the meantime, the industry only makes 2,178 billion IDR. Additionally, the same year's report included a retained loss of IDR 26.12 billion. Government Regulation 46/2013 addressing Special Income Tax for MSMEs, with a final PPh rate of 1 percent, was another strategy that PT RNI attempted. Finally, from 2007 to 2015, two Indonesian shareholders of PT RNI failed to file accurate tax reports. Additionally, two Singaporean shareholders who own firms in Indonesia failed to pay their income taxes.

This pattern can be explained by the fact that tax preparation has gained importance and attention in recent years. In order to reduce the amount of taxes they must pay to the

state without going outside the law, businesses (taxpayers) engage in tax planning. The first step in reducing taxes for an organization is tax planning.

Research conducted by Siti Aulia Farhana et al (2022) on “The Effect of Profitability and Leverage on Tax Planning with Company Size as a Moderating Variable.” the results of the study prove that leverage has a positive relationship with tax planning. Then in the research conducted by Yesicha Windi Sari Br Haloho et al (2024) on “the effect of leverage, profitability, company size, proportion of institutional ownership and corporate social responsibility on tax planning” in the results of his research proved that the Company's leverage is detrimental to tax planning. This means that leverage has a negative impact on tax planning. In his research conducted by Evita Sysmantia et al (2023) on “Analysis of the Effect of Transfer Pricing, Leverage, Deferred Tax, and Advertising Expenses on Tax Planning in Indonesia with Company Size as a Control Variable (Empirical Study of Manufacturing Companies in the Food and Beverage Sub-Sector Listed on the Indonesia Stock Exchange for the 2016-2020 Period).” the results of his research prove that leverage does not have a significant effect on tax planning.

Research conducted by Yunita Dwi Rahmawati et al (2024) on “the impact of leverage, profitability, and company size on tax planning in manufacturing firms” the results of the study prove that profitability has a positive relationship with tax planning. Research conducted by Afni Seliana Saragih et al (2023) “on the influence of leverage, profitability, company size on tax planning in manufacturing firms.” companies and ownership institutional to tax planning “the results of the study prove that profitability has a negative impact on tax planning. Research conducted by Ika Nurjanah et al (2019) on The Influence Leverage, Profitability, Size Company and Ownership Institutional Against Tax Planning.” research results prove that profitability does not have a significant effect on tax planning.

Research conducted by Afni Seliana Saragih et al (2023) on “the influence of leverage, profitability, size companies and ownership institutional to tax planning.” the results of the study prove that Company Size has a positive effect on tax planning. In his research conducted by Yesicha Windi Sari Br Haloho et al (2024) on “the effect of leverage, profitability, company size, proportion of institutional ownership and corporate social responsibility on tax planning.” the results of his research prove that Company Size has no effect on tax planning. In his research conducted by Ika Nurjanah et al (2019) on “The Effect of Leverage, Profitability, Size Company and Ownership Institutional Against Tax Planning.” the results of his research prove that company size does not have a significant effect on tax planning.

2. Theoretical Background

2.1 Agency Theory

Agency theory, as pioneered by Jensen & Meckling (1976), explains the contractual relationship between principals (owners/shareholders) and agents (managers) who are delegated authority to manage the firm. This relationship inherently contains potential conflicts of interest due to the separation between ownership and control.

Jensen and Meckling identified two primary problems in agency relationships:

- 1) Moral Hazard: Occurs when agents take actions that are not aligned with the pre-agreed contract after the agreement is in place, often because their actions are not fully observable.
- 2) Adverse Selection: Arises when the principal cannot verify whether the agent's decisions are based on reliable information or are influenced by self-interest.

In the context of taxation, agency problems manifest in the relationship between corporate management (agent) and tax authorities (principal). Tax authorities seek to maximize tax revenue collection, while management has incentives to minimize tax payments to increase reported profits, even as profitability grows (Kasmir, 2014). This conflict creates the foundation for corporate tax planning activities.

2.2 Compliance Theory

Compliance theory provides insights into why entities adhere to regulations. Tyler (1990), as cited in Zubaedah and Setyawan (2017), identified two fundamental perspectives on legal compliance:

- 1) Instrumental Approach: Individuals are motivated by self-interest, responding to tangible incentives and disincentives. Compliance is calculated based on potential rewards and punishments.
- 2) Normative Approach: Compliance stems from internalized values, legitimacy of authorities, and moral obligations rather than mere calculation of costs and benefits.

Both perspectives are relevant in understanding corporate tax compliance behavior, where companies balance between minimizing tax burdens (instrumental) and maintaining legal and social legitimacy (normative).

2.3 Literature Review and Hypothesis Development

2.3.1 Tax Planning

Tax planning represents the initial stage of tax management, involving the strategic organization of business affairs by individual taxpayers or corporate entities to minimize tax liabilities through legal means (Pohan, 2013). In this study, tax planning is measured using the Effective Tax Rate (ETR), which represents the percentage of tax burden borne by the company relative to its accounting profit (Hery, 2013). The ETR formula is calculated as follows:

$$\text{Effective Tax Rate} = \text{Income Tax Expense} / \text{Profit Before Tax}$$

2.3.2 Leverage and Tax Planning

Leverage reflects the extent to which a company relies on debt financing relative to equity (Fahmi, 2010). The debt-to-equity ratio serves as a key leverage indicator, measuring the proportion of debt used to finance assets relative to shareholders' equity. Higher leverage indicates greater dependence on debt financing.

From a tax perspective, interest expenses on debt are tax-deductible, creating a tax shield that reduces taxable income. Research by Siti Aulia Farhana et al. (2022) demonstrated that leverage positively influences tax planning, as companies with higher debt levels have stronger incentives to utilize interest tax shields. Therefore, we hypothesize:

H1: Leverage has a positive effect on Tax Planning

2.3.3 Profitability and Tax Planning

Profitability ratios measure a company's efficiency in generating profits from its assets. Return on Assets (ROA) specifically indicates how effectively a company utilizes its total assets to generate net income (Kasmir, 2014). The ROA formula is:

$$\text{Return on Assets} = \text{Net Profit} / \text{Total Assets}$$

Higher profitability creates greater tax liabilities, providing stronger incentives for tax planning activities. Research by Yulia & Aprijuriati (2023) found a significant positive

relationship between profitability and tax planning, as management seeks to preserve profits through strategic tax management. Thus, we propose:

H2: Profitability has a positive effect on Tax Planning

2.3.4 Company Size and Tax Planning

Company size, typically measured as the natural logarithm of total assets (Klapper & Love, 2002), reflects the scale of operations and resource availability. Larger companies typically have more complex transactions and greater resources to engage in sophisticated tax planning strategies. Research by Afni Seliana Saragih et al. (2023) indicated that company size positively influences tax planning, as larger firms face higher absolute tax burdens and have better access to tax expertise. Therefore, we hypothesize:

H3: Company Size has a positive effect on Tax Planning

2.3.5 The Moderating Role of Institutional Ownership

Institutional ownership refers to shareholding by financial institutions such as investment banks, insurance companies, and pension funds (Veronica and Urama, 2005). Institutional investors typically possess greater monitoring capacity and expertise compared to individual shareholders, enabling more effective oversight of management decisions (Kartikawati, 2009). Institutional ownership is measured as:

$$\text{Institutional Ownership} = \text{Number of Shares Owned by Institutions} / \text{Total Outstanding Shares}$$

The moderating effect of institutional ownership on the relationship between corporate characteristics and tax planning is theoretically ambiguous. On one hand, institutional investors may constrain aggressive tax planning to protect corporate reputation and avoid regulatory scrutiny. On the other hand, they may encourage tax efficiency to enhance shareholder returns.

Research by Siti Aulia Farhana et al. (2022) found that company size could not moderate the leverage-tax planning relationship, while Desai & Dharmapala (2006) provided evidence that company characteristics can influence how institutional ownership affects tax planning. Based on these conflicting findings, we propose the following moderation hypotheses:

H4: Institutional ownership moderates the effect of leverage on tax planning

H5: Institutional ownership moderates the effect of profitability on tax planning

H6: Institutional ownership moderates the effect of company size on tax planning

3. Methods

3.1 Research Design

This study employs a quantitative research approach using panel data regression analysis to examine the effect of leverage, profitability, and company size on tax planning, with institutional ownership serving as a moderating variable. The research adopts an explanatory design to test the formulated hypotheses through empirical data from financial reports of companies listed on the Indonesia Stock Exchange (IDX).

3.2 Definition and Measurement of Variables

Table 1. Operational Definitions of Variables

No	Variables	Indicator / Formula	Reference	Scale
1	Leverage (X_1)	$DER = (\text{Total Debt}) / (\text{Total Equity})$	Munawir (2010)	Ratio

No	Variables	Indicator / Formula	Reference	Scale
2	Profitability (X ₂)	ROA = (Net Income) / (Total Assets)	Kasmir (2014)	Ratio
3	Company Size (X ₃)	Company Size = Ln (Total Assets)	Klapper & Love (2002)	Ratio
4	Tax Planning (Y)	ETR = (Income Tax Expense) / (Profit Before Tax)	Hery (2013)	Ratio
5	Institutional Ownership (Z)	Institutional Ownership = (Number of Institutional Shares) / (Total Outstanding Shares)	Kartikawati (2009)	Ratio

Source: Self-processed (2025)

3.3 Population and Research Sample

The population of this research consists of consumer cyclicals sector companies listed on the Indonesia Stock Exchange (IDX) during the period 2018–2023. The sample was determined using purposive sampling, with 11 companies selected from a total of 153 firms that met the following criteria:

- 1) Companies belong to the consumer cyclicals sector listed on the IDX in 2018–2023.
- 2) Companies publish complete annual financial statements for the period 2018–2023.
- 3) Companies that recorded profits during the 2018–2023 period.

This sampling design ensures that all selected firms provide sufficient data for consistent panel regression analysis.

3.4 Data Analysis Methods

This study employed a quantitative approach using panel data regression analysis to examine the relationships among variables. The analytical process included descriptive statistics, model estimation, model selection, classical assumption testing, and hypothesis testing.

Descriptive statistics were used to summarize the data characteristics, including mean, minimum, maximum, and standard deviation values of each variable. Panel data regression was estimated using three approaches Common Effect Model (CEM), Fixed Effect Model (FEM), and Random Effect Model (REM) as suggested by Ghozali (2016). Model selection was determined sequentially using the Chow, Hausman, and Lagrange Multiplier (LM) tests to identify the most appropriate estimation model.

To ensure model validity, classical assumption tests were performed, including the multicollinearity test and heteroscedasticity test, following Ghozali (2018). Finally, hypothesis testing was conducted using the F-test and t-test to assess the simultaneous and partial effects of independent variables on the dependent variable. The coefficient of determination (R²) was also used to measure the explanatory power of the model.

3.5 Panel Data Regression Analysis

Panel data linear regression is used to test the research hypotheses and assess the effect of leverage, profitability, and company size on tax planning, moderated by institutional ownership. The regression model is expressed as follows:

$$Y_{it} = \alpha + b_1 DER_{it} + b_2 ROA_{it} + b_3 SIZE_{it} + b_4 INST_{it} + b_5 (LEV \times INST)_{it} + b_6 (PROF \times INST)_{it} + b_7 (SIZE \times INST)_{it} + e_{it}$$

Where:

Y_{it} = Tax Planning for company i in year t
α = Constant

$\beta_1 \text{DER}_{it}$	= Leverage for company i in year t
$\beta_2 \text{ROA}_{it}$	= Profitability for company i in year t
$\beta_3 \text{SIZE}_{it}$	= Company Size for company i in year t
$\beta_4 \text{INST}_{it}$	= Institutional Ownership for company i in year t
$\beta_5 (\text{LEV} \times \text{INST})_{it}$	= Interaction between Leverage and Institutional Ownership
$\beta_6 (\text{PROF} \times \text{INST})_{it}$	= Interaction between Profitability and Institutional Ownership
$\beta_7 (\text{SIZE} \times \text{INST})_{it}$	= Interaction between Company Size and Institutional Ownership
ε_{it}	= Error term

4. Results and Discussion

4.1 Descriptive Statistics

Table 2 presents the descriptive statistics for all variables used in the study. The data reveals considerable variation across the sampled companies, providing a robust foundation for subsequent analysis.

Table 2. Descriptive Statistics

Variable	Mean	Minimum	Maximum	Std. Deviation
Tax Planning	0.278182	0.000000	0.940000	0.240785
Leverage	0.908182	0.200000	2.860000	0.687651
Profitability	0.058333	0.000000	0.240000	0.062279
Company Size	29.01197	26.250000	31.210000	1.384377

Source: Processed data from Eviews12, 2024

The descriptive analysis shows that Tax Planning, measured by Effective Tax Rate (ETR), averages 27.82%, with values ranging from 0% to 94%. Leverage demonstrates substantial variability with a mean Debt-to-Equity Ratio of 0.91, indicating that sampled firms maintain relatively conservative financing structures. Profitability remains modest across the sector, averaging 5.83% Return on Assets. Company Size exhibits the least relative variation among the variables studied.

4.2 Panel Data Regression Model Selection

The model selection process involved three sequential tests to determine the most appropriate estimation technique for the panel data.

Table 3. Model Selection Test Results

Test	Comparison	Result	Selected Model
Chow Test	CEM vs FEM	Prob. = 0.0000	FEM
Hausman Test	FEM vs REM	Prob. = 0.1043	REM
Lagrange Multiplier	CEM vs REM	Prob. = 0.0000	REM

Source: Processed data from Eviews12, 2024

Based on the testing hierarchy, the Random Effects Model (REM) was selected as the most appropriate estimator for this study. The Hausman test result (p-value = 0.1043 > 0.05) indicates that the REM specification is consistent and efficient for the data.

4.3 Classical Assumption Tests

4.3.1 Multicollinearity Test

Table 4 presents the correlation matrix for the independent variables. All correlation coefficients remain below the 0.80 threshold, with the exception of the interaction terms which are intentionally correlated with their component variables. This confirms the absence of severe multicollinearity in the model.

Table 4. Multicollinearity Test Results

Variable	DER	ROA	SIZE	DER_INST	ROA_INST	SIZE_INST
DER	1.0000					
ROA	-0.4049	1.0000				
SIZE	0.1644	-0.1094	1.0000			
DER_INST	0.8640	-0.3648	0.2197	1.0000		
ROA_INST	-0.3684	0.9779	-0.0904	0.2800	1.0000	
SIZE_INST	0.2336	0.0654	0.1518	0.6116	0.2240	1.0000

Source: Processed data from Eviews12, 2024

4.3.2 Heteroscedasticity Test

The heteroscedasticity test results in table 5 show that all probability values exceed the 0.05 significance level, confirming that the model is free from heteroscedasticity issues.

Table 5. Heteroscedasticity Test Results

Variable	Prob. Value	Conclusion
DER	0.2154	No heteroscedasticity
ROA	0.8932	No heteroscedasticity
SIZE	0.3781	No heteroscedasticity
DER_INST	0.1057	No heteroscedasticity
ROA_INST	0.7643	No heteroscedasticity
SIZE_INST	0.4921	No heteroscedasticity

Source: Processed data from Eviews12, 2024

4.4 Hypothesis Testing Results

4.4.1 Regression Results and Hypothesis Testing

Table 6 presents the complete results of the Random Effects Model estimation, including coefficient estimates and hypothesis test outcomes.

Table 6. Random Effects Model Estimation Results

Variable	Coefficient	Std. Error	t-Statistic	Prob.	Hypothesis
C	0.589013	0.170467	3.455297	0.0012	
DER	0.013850	0.048256	0.286993	0.7757	H1: Rejected
ROA	-0.058206	0.525663	-0.110729	0.9129	H2: Rejected
SIZE	-0.011378	0.002831	-4.019287	0.0002	H3: Accepted
DER_INST	-0.027590	0.039552	-0.697546	0.4895	H4: Rejected
ROA_INST	0.179947	0.430519	0.417978	0.6788	H5: Rejected
SIZE_INST	0.000209	0.001985	0.105362	0.9166	H6: Rejected

Source: Processed data from Eviews12, 2024

4.4.2 Model Goodness-of-Fit

The overall model fitness tests in table 6 indicate that the regression model is statistically significant and provides meaningful explanatory power.

Table 7. Model Goodness-of-Fit Tests

Test	Value	Conclusion
F-statistic	4.541035	Significant (p = 0.000443)
Adjusted R ²	0.261818	26.18% variance explained

Source: Processed data from Eviews12, 2024

The F-test result ($p = 0.000443 < 0.05$) confirms that the model is statistically significant overall. The Adjusted R^2 value of 0.261818 indicates that 26.18% of the variation in tax planning is explained by the independent variables, while the remaining 73.82% is attributable to other factors not included in the model.

4.5 Discussion of Findings

4.5.1 Direct Effects on Tax Planning

The analysis reveals that leverage (H1) does not significantly affect tax planning ($\beta = 0.013850$, $p = 0.7757 > 0.05$). This finding contradicts agency theory expectations and suggests that Indonesian Consumer Cyclical companies may not utilize debt strategically for tax shield benefits, possibly due to conservative financial policies or limited access to debt financing.

Similarly, profitability (H2) shows no significant relationship with tax planning ($\beta = -0.058206$, $p = 0.9129 > 0.05$). This challenges conventional wisdom that more profitable firms engage in greater tax planning. The result aligns with compliance theory, indicating that firms may prioritize regulatory compliance over aggressive tax minimization strategies.

Conversely, company size (H3) demonstrates a significant negative effect on tax planning ($\beta = -0.011378$, $p = 0.0002 < 0.05$). Larger companies exhibit lower effective tax rates, supporting agency theory predictions that larger firms possess greater resources and sophistication for tax planning activities while maintaining compliance.

4.5.2 Moderating Effects of Institutional Ownership

The moderating role of institutional ownership was not supported for any of the hypothesized relationships. The interaction terms for leverage (H4: $p = 0.4895$), profitability (H5: $p = 0.6788$), and company size (H6: $p = 0.9166$) with institutional ownership were all statistically insignificant.

This suggests that institutional investors in Indonesian Consumer Cyclical companies may not actively influence corporate tax strategies. Several explanations are plausible: institutional investors may prioritize other governance aspects over tax planning, lack specialized tax expertise, or face regulatory constraints that limit their influence on tax-related decisions.

4.5.3 Theoretical and Practical Implications

The findings present a nuanced perspective on tax planning behavior in emerging markets. While agency theory provides some explanatory power for the size effect, the non-significant results for leverage and profitability, coupled with the ineffective moderating role of institutional ownership, suggest that compliance considerations and institutional factors may outweigh purely economic motivations in tax strategy formulation.

From a practical standpoint, these results indicate that tax authorities should focus monitoring efforts on larger corporations while recognizing that conventional indicators like leverage and profitability may not reliably predict tax planning behavior in the Consumer Cyclical sector.

5. Conclusion

Based on the comprehensive data analysis and hypothesis testing conducted in this study, the following conclusions can be drawn regarding tax planning determinants in

Consumer Cyclical companies listed on the Indonesia Stock Exchange during the 2021-2023 period:

- 1) Leverage does not exhibit a statistically significant effect on Tax Planning. This suggests that debt financing decisions, as measured by the Debt-to-Equity Ratio, do not substantially influence corporate tax planning strategies in the sampled companies.
- 2) Profitability similarly demonstrates no significant impact on Tax Planning. The findings indicate that the level of corporate profitability, measured by Return on Assets, does not serve as a determining factor for tax planning activities within the Consumer Cyclical sector.
- 3) Contrary to theoretical expectations, Company Size does not significantly affect Tax Planning. The results reveal that larger company scale, measured by the natural logarithm of total assets, does not necessarily correlate with more aggressive or sophisticated tax planning practices.
- 4) Institutional Ownership fails to moderate the relationships between leverage, profitability, company size, and tax planning. This indicates that institutional shareholders' monitoring role does not significantly influence how these corporate characteristics affect tax planning decisions.

This study acknowledges several limitations that should be considered when interpreting the findings:

- 1) The coefficient of determination test reveals that only approximately 9% of the variance in tax planning is explained by the independent variables included in the model. The remaining 91% is influenced by other factors not captured in this research framework.
- 2) The exclusive focus on Consumer Cyclical sector companies limits the generalizability of the findings to other industrial sectors or geographical contexts beyond the Indonesian market.
- 3) The three-year research period (2021-2023) may be insufficient to capture long-term relationships and trends in tax planning behavior, particularly given the unusual economic conditions during the post-pandemic recovery period.

Based on the findings and limitations of this study, the following recommendations are proposed for future research:

- 1) Future studies should incorporate additional explanatory variables that may influence tax planning, such as corporate governance mechanisms, audit quality, managerial ownership, or specific industry regulations, to enhance the explanatory power of the research model.
- 2) Extending the research timeframe would allow for the examination of long-term patterns and provide more robust insights into the evolution of tax planning strategies over different economic cycles.
- 3) Subsequent research could employ alternative methodologies, such as qualitative approaches or case studies, to gain deeper insights into the contextual factors and decision-making processes underlying corporate tax planning strategies in emerging markets.

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