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THE EFFECT OF FINANCIAL PERFORMANCE, FIRM SIZE, AND ISLAMIC SOCIAL REPORTING ON TAX AVOIDANCE IN ISLAMIC COMMERCIAL BANKS IN INDONESIA

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Abstract

Introduction to The Problem: This study analyzed the effects of financial performance proxied by profitability (ROA) and leverage (DER), firm size, and Islamic Social Reporting (ISR) on tax avoidance (ETR) in Islamic Commercial Banks in Indonesia. As corporate entities, Islamic commercial banks in Indonesia are obligated to comply with taxation regulations while simultaneously adhering to the ethical principles of Islamic business conduct.

Purpose/Objective of the Study: The objective of this study is to examine Islamic Commercial Banks in Indonesia. Specifically, the research seeks to determine whether financial performance significantly affects the level of tax avoidance, whether larger Islamic banks exhibit different tax avoidance behavior compared to smaller institutions, and whether greater disclosure of Islamic Social Reporting reduces the tendency to engage in tax avoidance.

Design/Methodology/Approach: This research employs a quantitative approach using secondary data derived from the annual reports of Islamic Commercial Banks for the period 2018–2024. The sampling technique applied is purposive sampling, resulting in a sample of eight banks. The data were analyzed using panel data regression with the assistance of EViews 12.0 and Microsoft Excel.

Findings: The results of the study indicate that, simultaneously, profitability (ROA), leverage (DER), firm size, and Islamic Social Reporting (ISR) have a significant effect on tax avoidance. Partially, firm size and Islamic Social Reporting are found to influence tax avoidance, whereas profitability and solvency do not have a significant effect on tax avoidance in Islamic Commercial Banks.

Paper Type: Research Article

Keywords: Profitability; Leverage; Firm Size; Islamic Social Reporting; Tax Avoidance.

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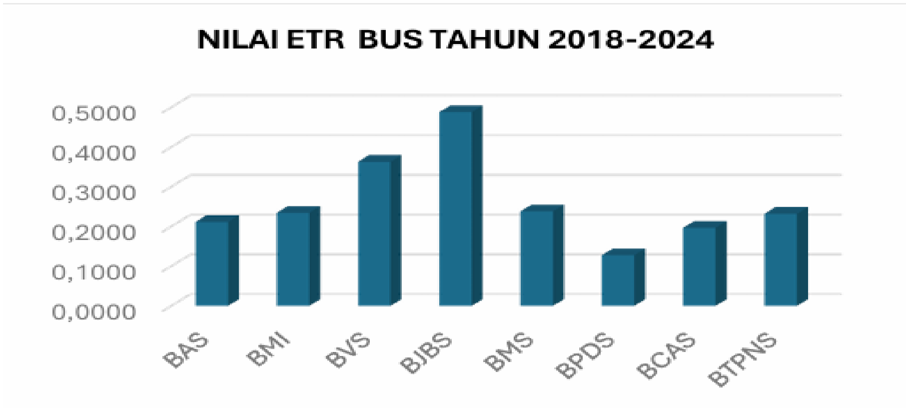
INTRODUCTION

Islamic banking plays a strategic role in supporting economic growth through its intermediation function and the provision of financial services in accordance with Sharia principles. In their operations, Islamic Commercial Banks are required not only to uphold principles of fairness and transparency but also to fulfill their tax obligations as a contribution to state revenue. Taxes constitute a primary source of government income used to finance development and enhance public welfare (DPR, 2007). However, from a corporate perspective, taxes are often viewed as a burden that reduces net income, thereby encouraging the emergence of tax avoidance practices as a legal means of minimizing tax liabilities (Firmansyah et al., 2022).

The phenomenon of tax avoidance in Islamic Commercial Banks is particularly interesting to examine because, normatively, these institutions operate on the basis of Sharia principles that emphasize fairness, transparency, and social responsibility. Nevertheless, in practice, variations in tax compliance across banks persist, as reflected in differences in the Effective Tax Rate (ETR). A lower ETR indicates a higher level of tax avoidance, whereas a higher ETR reflects better tax compliance (Novitasari & Suharni, 2019). This variation suggests a potential conflict between a firm's objective to maximize profit and its obligation to fulfill fiscal responsibilities. To further illustrate this phenomenon, this study presents data on the development of ETR values of Islamic Commercial Banks during the 2018–2024 period.

Figure 1. Effective Tax Rate (ETR) of Islamic Commercial Banks in Indonesia



Source: Author's Calculation (2026)

Several banks exhibit relatively high Effective Tax Rate (ETR) values, while others show lower ETR levels. This variation indicates differences in tax compliance and the tendency to engage in tax avoidance across

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banks. The inconsistency in ETR values suggests that tax management policies among Islamic Commercial Banks are not uniform and are still influenced by firm-specific internal characteristics.

Several previous studies have examined the determinants of tax avoidance, including profitability, leverage, firm size, and social responsibility. Higher profitability tends to increase a firm's incentive to engage in tax avoidance due to higher taxable income (Devi & Arinta, 2021). Leverage may also influence tax avoidance, as interest expenses from debt can reduce pre-tax income (Permata et al., 2021). In addition, larger firms are considered to have greater opportunities to exploit tax loopholes (Puspitasari & Wulandari, 2022). Meanwhile, the disclosure of Sharia-based social responsibility through Islamic Social Reporting (ISR) is expected to reduce tax avoidance by reflecting a firm's ethical commitment and adherence to social values (Indarningsih et al., 2023).

However, prior research findings remain inconsistent. Some studies report that profitability has a significant effect on tax avoidance, while others find that profitability actually reduces the tendency for tax avoidance (Naufal et al., 2024; Sulastri et al., 2022). Similar inconsistencies are observed for leverage and firm size, which do not always show significant effects (Fitriya & Bawono, 2023; Rustiani et al., 2024). Furthermore, studies on ISR remain relatively limited and have not widely integrated Sharia-based variables with financial variables into a comprehensive research model.

Previous studies exhibit inconsistent findings and a lack of integration between financial variables and Sharia-based variables in explaining tax avoidance practices. Therefore, this study aims to examine the effects of financial performance (proxied by profitability and solvency), firm size, and Islamic Social Reporting on tax avoidance in Islamic Commercial Banks in Indonesia. This research seeks to address the existing gap by integrating financial and non-financial Sharia-based variables into a single analytical framework.

The novelty of this study lies in examining the role of Islamic Social Reporting as a representation of Sharia-based social responsibility in influencing tax avoidance, and in utilizing the most recent panel data covering the period 2018–2024 for Islamic Commercial Banks in Indonesia. Accordingly, this study is expected to contribute to the academic literature by enriching discussions on taxation practices within Islamic financial institutions.

Based on the above considerations, this research is important for understanding the determinants of tax avoidance in Islamic Commercial Banks and for providing implications for both management and regulators in maintaining a balance between financial performance, tax compliance, and adherence to Sharia principles. Thus, identifying research issues and objectives is crucial in strengthening the role of Islamic banking institutions as entities that not only pursue profitability but also uphold ethical values and compliance within the Islamic financial system.

METHODOLOGY

This study employs a quantitative research design with an explanatory approach to analyze the effects of financial performance, firm size, and Islamic Social Reporting on tax avoidance in Islamic Commercial Banks in Indonesia. The data used in this study are secondary in the form of annual reports of Islamic Commercial Banks for the period 2018–2024, obtained from each bank's official publications and relevant authorities.

The population of this study consists of all Islamic Commercial Banks operating in Indonesia. The sampling technique used is purposive sampling based on specific criteria, resulting in a final sample of eight Islamic Commercial Banks that meet the research requirements.

The dependent variable in this study is tax avoidance, measured using the Effective Tax Rate (ETR). The independent variables include profitability, proxied by Return on Assets (ROA); solvency, proxied by Debt-to-Equity Ratio (DER); firm size, measured by the natural logarithm of total assets; and Islamic Social Reporting (ISR), measured using the ISR disclosure index.

The data analysis method employed is a panel data regression using EViews 12.0. Prior to hypothesis testing, model selection tests were conducted using the Chow Test and Hausman Test to determine the most appropriate regression model. In addition, classical assumption tests, including normality, multicollinearity, heteroskedasticity, and autocorrelation tests, were performed to ensure the validity of the model. Hypothesis testing was carried out using partial tests (t-tests), simultaneous tests (F-tests), and the coefficient of determination (R^2) to assess the explanatory power of the independent variables for the dependent variable.

RESULTS AND DISCUSSION

The following are the results of the t-test (partial test) between variables X and Y in this study. This can be seen in the following Table 1:

Table 1. Partial Test Results (t-test)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	140433.0	48271.24	2.909247	0.0057
X1	1.907950	1.379330	1.383244	0.1736
X2	-2.690609	5.103992	-0.527158	0.6007
X3	-12.67475	4.348524	-2.914723	0.0056
X4	1.728018	0.663334	2.605049	0.0125

Source: EViews data is processed by researchers (2026)

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The Effect of Profitability (Return on Assets/ROA) on Tax Avoidance in Islamic Commercial Banks

The statistical test results indicate that the Return on Assets (ROA) variable has a probability value of 0.1736 (> 0.05) and a t-statistic of 1.383244 (< 1.6730). Therefore, the hypothesis is rejected, indicating that profitability does not significantly affect tax avoidance. These findings imply that the level of profitability in Islamic Commercial Banks does not directly influence corporate decisions to engage in tax avoidance practices. This result is consistent with studies by (2020) and Naufal et al., which suggest that firms with higher profitability tend to fulfill their tax obligations and maintain their reputation among stakeholders, as explained by stakeholder theory. However, this finding contradicts the results of Andalenta & Ismawati (2022) and Fatmasari et al. (2025), which report that profitability has a significant effect on tax avoidance. Therefore, it can be concluded that profitability is not a primary determinant of tax avoidance. Instead, firms with higher profits tend to demonstrate greater compliance with tax regulations and prioritize maintaining their reputation.

The Effect of Leverage (Debt to Equity Ratio/DER) on Tax Avoidance in Islamic Commercial Banks

The statistical test results indicate that the Debt to Equity Ratio (DER) variable has a probability value of 0.6007 (> 0.05) and a t-statistic of -0.527158 (< 1.6730). Thus, the hypothesis is rejected, suggesting that leverage does not have a significant effect on tax avoidance. These findings imply that the use of debt in Islamic Commercial Banks is primarily intended to support operational financing and business expansion rather than to reduce tax burdens. This result is consistent with agency and stakeholder theories, which suggest that debt decisions are driven not solely by tax-avoidance motives but also by financial risks and stakeholder pressures, such as from regulators and the Sharia Supervisory Board. This study is supported by Rustiani et al., (2024) and Handoyo et al., (2022), who also found that leverage does not significantly influence tax avoidance. However, this finding contrasts with Mastura et al., (2023), who reported a positive effect of DER on tax avoidance. Therefore, it can be concluded that solvability (leverage) is not a primary determinant of tax avoidance practices, as the high risks associated with debt reduce its effectiveness as a tax minimization strategy.

The Effect of Firm Size (SIZE) on Tax Avoidance in Islamic Commercial Banks

The statistical test results show that the Firm Size (SIZE) variable has a probability value of 0.0056 (< 0.05) and a t-statistic of -2.914723. Thus, the hypothesis is accepted, indicating that firm size has a significant effect on tax avoidance. The negative regression coefficient suggests that larger firms tend to exhibit lower levels of tax avoidance. These findings imply that large-scale firms are more likely to maintain tax compliance, in line with agency theory and stakeholder theory. Larger firms are subject to greater scrutiny from regulators and the public, leading them to be more cautious in making tax-related decisions. This result is consistent with the study by Puspitasari & Wulandari (2022), which found that firm size influences tax avoidance practices. Therefore, it can be concluded that firm size is an important determinant of tax avoidance, with larger firms tending to be more transparent and to prioritize maintaining their reputation by complying with applicable tax regulations.

The Effect of Islamic Social Reporting (ISR) on Tax Avoidance in Islamic Commercial Banks

The statistical test results indicate that the Islamic Social Reporting (ISR) variable has a probability value of 0.0125 (< 0.05) and a t-statistic of 2.605049 (> 1.6730). Thus, the hypothesis is accepted, suggesting that ISR has a significant effect on tax avoidance. The positive regression coefficient implies that higher levels of ISR disclosure are associated with an greater tendency for firms to engage in tax avoidance through legal strategies. This finding is consistent with Sharia Enterprise Theory, which emphasizes that companies are accountable not only to stakeholders but also to Allah SWT, thereby encouraging transparency and accountability in corporate management, including taxation practices. This study is supported by prior research conducted by Fatmasari et al. (2025) and Amri & Sovita (2024), which also found that ISR has a significant influence on tax avoidance. Therefore, it can be concluded that ISR is an important factor affecting tax avoidance practices. Firms with higher levels of ISR disclosure tend to have more structured governance systems, enabling them to manage tax obligations through tax planning strategies that comply with applicable regulations.

CONCLUSION

Based on the analysis, it can be concluded that tax avoidance practices in Islamic Commercial Banks are influenced not only by financial performance factors but also by firm characteristics and aspects of Sharia-based governance. Firm size and Islamic Social Reporting have been shown to significantly explain variation in tax avoidance, whereas profitability and solvency do not appear to be primary determinants of such practices.

These findings indicate that larger firms tend to place greater emphasis on compliance and reputational considerations in managing their tax obligations. Meanwhile, the disclosure of Islamic Social Reporting reflects

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the presence of a more structured governance system in implementing tax strategies within legal boundaries. Therefore, tax avoidance practices in Islamic banking are influenced not only by economic motivations but also by stakeholder pressure and adherence to Sharia values that underpin operational activities.

The implications of this study highlight the importance of Islamic Commercial Banks managing a balance between tax efficiency and compliance with regulatory requirements and Sharia principles. For regulators, these findings may serve as a basis for strengthening supervision and tax policies in the Islamic banking sector, particularly in relation to transparency and social reporting.

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