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Tax Avoidance in Manufacturing Firms: A Cross-Country Analysis of Financial Attributes and Law Enforcement

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ABSTRACT

This study examines the impact of firm size, leverage, and profitability on tax avoidance across six Asian jurisdictions (IDX, Bursa Malaysia, SET, PSE, SGX, HKEX) from 2020 to 2024. Analyzing 981 manufacturing companies using the Random Effect Model and Moderated Regression Analysis, the results reveal that larger firm size and higher profitability significantly reduce tax avoidance, while leverage and law enforcement enforcement as a moderator show no significant effects. These findings suggest that internal strategic factors and economic incentives supersede external legal pressures, highlighting the limitations of deterrence theory in cross-country corporate taxation.

Keywords:
Tax avoidance, cross-country analysis, firm size, law enforcement, leverage, profitability

Penghindaran Pajak pada Perusahaan Manufaktur Asia: Analisis Lintas Negara terhadap Atribut Keuangan dan Penegakan Hukum

ABSTRAK

Penelitian ini menguji pengaruh ukuran perusahaan, leverage, dan profitabilitas terhadap penghindaran pajak di enam yurisdiksi Asia (IDX, Bursa Malaysia, SET, PSE, SGX, HKEX) dari tahun 2020 hingga 2024. Melalui analisis data panel terhadap 981 perusahaan manufaktur menggunakan Random Effect Model dan Moderated Regression Analysis, hasil penelitian menunjukkan bahwa ukuran perusahaan yang lebih besar dan profitabilitas tinggi secara signifikan mengurangi penghindaran pajak, sementara leverage dan penegakan hukum sebagai moderator tidak berpengaruh signifikan. Temuan ini mengindikasikan bahwa faktor strategi internal dan insentif ekonomi lebih dominan daripada tekanan hukum eksternal, menyoroti keterbatasan deterrence theory dalam perpajakan lintas negara.

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1. Introduction

The practice of tax avoidance is a significant issue that contributes to the loss of state revenue and hampers the state's ability to finance important social and development programs (Benkraiem et al., 2022; Anggraini et al., 2025). According to the "Revenue Statistics in Asia and the Pacific 2025" report, the tax-to-GDP ratio across the Asia-Pacific region varies significantly between countries. The Philippines recorded a tax-to-GDP ratio of 17.9%, followed by Thailand at 17.1%, Singapore at 13.7%, Malaysia at 13.1%, Hong Kong at 13.1%, and Indonesia at 12% (OECD, 2025).

Countries with high tax ratios, such as the Philippines and Thailand, can raise more revenue, but high tax rates often encourage companies to avoid taxes (Beer et al., 2020; Cahyani & Faisol, 2025; Sanoran, 2025). Higher tax rates can increase companies' incentives to engage in tax avoidance because the potential economic benefits of reducing their tax burden are greater (Zeng, 2019;Bernando & Oktaviano, 2023; Cahyani & Faisol, 2025). The data in Table 1 shows the real impact of tax avoidance by large companies in developing countries.

Table 1. Annual Tax Losses

	2020	2021	2023	2024
Philippines	$1,877.6	$3,928.2	$2,996.4	$6,825.1
Malaysia	$902.6	$1,048.6	$775.0	$996.6
Indonesia	$4,785.9	$2,216.3	$2,736.5	$2,981.1
Thailand	$425.1	$1,033.4	$231.8	$1,930.0
Singapore	$2,791.0	$2,492.7	$598.6	$874.9
Hong Kong	$552.0	$207.4	$228.0	$85.3

Source: Tax Justice Network Report (2024)

Indonesia and Malaysia, with tax rates of 22% and 24% respectively, also recorded significant tax losses despite their lower rates than the Philippines' 25%. The phenomenon of tax avoidance remains rampant, mainly due to uncertainty in law enforcement and differences in regulatory frameworks across countries (Manrejo et al., 2025), which create opportunities for large companies to employ complex financial strategies Meanwhile, Thailand and Singapore, with lower tax rates of 20% and 17%, experience smaller tax losses. Hong Kong, with a tax rate of 16.5%, recorded very small tax losses, indicating that low tax rates can reduce the potential for tax avoidance (Dinata & Asqolani, 2024). The large number of annual tax losses reported in Table 1 indicates that corporate-level strategic decisions have a systemic impact on the country's fiscal stability. This suggests that tax avoidance is not simply an administrative issue, but rather the result of a complex interaction between internal corporate incentives and external environmental pressures.

This phenomenon illustrates the major challenges developing countries face in overcoming tax avoidance, which is influenced by company characteristics such as size, leverage, and profitability, which significantly determine a company's tendency to engage in tax avoidance

(Kurniawati & Prasetyo, 2023; Negkakis et al., 2025). Companies with larger size, higher leverage, and high profitability tend to carry out tax earnings management that provides a positive signal regarding the company's prospects (Hendayana et al., 2024; Hossain et al., 2025; Jesika, 2022), but also increases cash flow to support investment, thus making tax avoidance a strategy to increase firm value (Khuong et al., 2020).

Weak supervision and law enforcement can be one of the factors associated with high levels of tax avoidance (Gavious et al., 2022; Cahyani & Faisol, 2025). Weak law enforcement can encourage corporate tax avoidance by providing additional incentives for companies to reduce their tax liabilities (Chu et al., 2025). These conditions indicate that effective tax law enforcement is essential to combat tax avoidance (Pan & Wu, 2026; Sumantri et al., 2024).

Previous studies yield mixed findings on the effect of company characteristics on tax avoidance. Some studies, such as Hossain et al. (2024); Ernawati et al. (2021); Hapsoro et al. (2024), report that company size, leverage, and profitability increase the tendency of tax avoidance, while Mustika et al. (2022) show that leverage has no effect and profitability has a significant effect in increasing tax avoidance. Research by Darmansyah et al. (2022) shows that company size and profitability increase the likelihood of tax avoidance, but leverage can actually reduce it. Several other studies, such as Apriatna & Oktris (2022); Bernando & Oktaviano (2023); Dewi & Oktaviani (2021), found no significant effect. This difference in findings indicates inconsistencies in the research, which opens the door to further research on the influence of financial attributes on tax avoidance.

Previous studies focused on a single country (Harymawan et al., 2023; Hendayana et al., 2024; Hossain et al., 2025; Sanoran, 2025). This study offers novelty by integrating law enforcement variables as external factors that may mitigate tax avoidance across multiple countries. This integration is important to fill a literature gap on how law enforcement strength in a country can influence companies' financial attributes related to tax avoidance practices.

While the empirical literature on corporate tax avoidance is extensive, existing cross-country investigations have predominantly focused on the direct macroeconomic or institutional determinants of tax avoidance (e.g., Atwood et al., 2012a; Rachmawati et al., 2020). These pioneering studies frequently treat institutional factors as uniform direct predictors, thereby overlooking how macro-level legal environments interact dynamically with micro-level corporate financial characteristics. This study addresses this critical literature gap by shifting the role of law enforcement from a traditional direct explanatory factor into a conditional, moderating framework. Specifically, we investigate its boundary role in strengthening or weakening the influence of firm-specific attributes, namely firm size, leverage, and profitability on tax avoidance behavior.

The selection of six distinct Asian jurisdictions (Indonesia, Malaysia, Thailand, the Philippines, Singapore, and Hong Kong) provides a unique and compelling institutional matrix for this moderation analysis. These jurisdictions represent highly polarized environments; for instance, Singapore and Hong Kong pair low corporate tax rates with exceptionally strong institutional governance, whereas developing economies like Indonesia and the Philippines operate with higher statutory tax rates alongside emerging legal frameworks. To measure this institutional environment accurately, this study utilizes the World Justice Project Rule of Law Index as a proxy for law enforcement. This index provides a comprehensive and internationally comparable measure of legal institutions encompassing dimensions such as regulatory

enforcement, absence of corruption, and the effectiveness of civil and criminal justice systems making it highly suitable for cross-country studies examining the relationship between firm characteristics and tax avoidance.

Consequently, this study contributes to the literature in three distinct ways. First, it extends the application of Stakeholder and Public Interest theories by demonstrating the conditional mechanics of macro-micro institutional interactions in Asia. Second, methodologically, by utilizing the comprehensive Rule of Law Index rather than narrow tax-specific metrics, this study captures the broader regulatory environment that shapes corporate compliance. Finally, by examining the contemporary post-pandemic period of 2020–2024, this research delivers timely empirical evidence during an era characterized by accelerated global tax transparency initiatives. Furthermore, manufacturing companies were specifically chosen for this analysis because they engage in highly complex activities, from purchasing raw materials to producing finished goods ready for market (Ratnasari & Nuswantara, 2020), which involve intricate taxation aspects and play a strategic role in the global economy (UNIDO, 2025).

2. Theoretical framework and hypotheses development

This study integrates three main theoretical perspectives to explain tax avoidance: Agency Theory as an internal determinant, and Deterrence Theory and Compliance Theory as external determinants.

Theoretical framework

Agency theory

Agency theory, proposed by Jensen & Meckling (1976) provides the main foundation for understanding the conflict of interest between shareholders (principals) and managers (agents). In business operations, principals delegate authority to managers to manage the company for profit optimization (Safitra & Totanan, 2025). However, information asymmetry creates opportunities for managers to engage in opportunistic behavior, including aggressive tax avoidance. From this perspective, tax avoidance is a strategy to increase free cash flow, which can be used to advance managerial interests or strengthen the company's value in shareholders' eyes (Wenwu et al., 2023). Therefore, firm characteristics such as size, debt, and earnings are often manipulated to achieve such tax efficiency.

Deterrence theory

Deterrence theory is rooted in the economic assumption that individual behavior is influenced by profit-loss calculations (Matsueda et al., 2006). In relation to taxation, companies will comply if the cost of non-compliance (sanctions and audit risk) exceeds the tax savings. Vincent (2021) emphasizes that audit intensity and the severity of sanctions are the main determinants of non-compliance suppression. Effective law enforcement serves as an external monitoring mechanism, increasing the likelihood of detecting improper tax avoidance practices (Cahyani & Faisol, 2025). The strength of law enforcement depends on many factors (Bird & Davis-Nozemack, 2018). In the Asian region, with diverse legal systems, the effectiveness of law enforcement is a key variable that determines whether companies will be bold in exploiting regulatory loopholes or choose to comply.

Compliance theory

In contrast to Deterrence Theory, which focuses on punishment, Compliance Theory emphasizes legitimacy and social reputation (Chen et al., 2026). Pratama & Muhammad (2025) state that tax compliance is a form of corporate commitment to the social contract, aimed at maintaining operational stability and good relations with all stakeholders. Companies that comply with regulations tend to gain more trust from the capital market and access more favorable financing (Tanjung, 2023; Vemberain & Triyani, 2021). This theory explains why large companies with massive resources often choose to comply; they have high public exposure, so reputational risk is much more expensive than short-term tax savings (Vemberain & Triyani, 2021).

Hypotheses development

Financial attributes and tax avoidance

Firm size is an indicator of operational complexity. There are two views regarding the effect of company size: a political power perspective, which argues that large companies can lobby the authorities for tax relief (Hossain et al., 2024), and a political cost perspective, which argues that large companies are more compliant due to strict public scrutiny (Ernawati et al., 2021). In addition, large companies may have a greater ability to engage in tax planning through access to consultants, complex financial structures, and the use of tax provisions, potentially increasing tax avoidance (Hossain et al., 2024). However, other studies have found the opposite: larger companies tend to reduce tax avoidance due to higher public scrutiny and reputational risk (Ernawati et al., 2021).

Meanwhile, leverage reflects the company's funding strategy. Debt interest expense is a deduction from taxable income (a tax shield), so, in theory, companies with high debt have a greater incentive to minimize their tax burden. However, close supervision from creditors often limits managers' room for maneuver in risky tax avoidance. Empirical research on the effect of leverage on tax avoidance is evident in studies by Darmansyah et al. (2022), Hapsoro et al. (2024), Hossain et al. (2024), and Ernawati et al. (2021) which found that leverage is associated with tax avoidance. However, the research Dewi & Oktaviani (2021), Apriatna & Oktris (2022) and Bernando & Oktaviano (2023) found that leverage does not affect tax avoidance. This shows that certain conditions restrain managers from using debt to avoid taxes.

In terms of profitability, companies with superior financial performance tend to have higher tax liabilities. This condition encourages managers to exploit regulatory loopholes to pursue more aggressive tax planning, ensuring that after-tax profits remain high. Research findings Alkurdi et al. (2024); Ernawati et al. (2021); Darmansyah et al. (2022); Mustika et al. (2022); Hapsoro et al. (2024), and Hossain et al. (2024) show that profitability affects tax avoidance. However, high profitability also provides cash flow flexibility, so companies do not need to engage in legally risky tax avoidance (Apriatna & Oktris, 2022). In contrast to the research of Apriatna & Oktris (2022); Bernando & Oktaviano (2023) and Shubita (2024), which show that profitability does not affect tax avoidance.

The influence of company size, leverage, and profitability on tax avoidance can be explained through Agency Theory, supported by Compliance Theory. Based on Agency Theory, these three characteristics reflect a company's financial condition, where management has incentives to optimize resources and exploit regulatory loopholes to minimize tax burdens and increase

shareholder value (Wenwu et al., 2023). However, management's ability to utilize these three financial aspects is limited by the principles of Compliance Theory. According to this theory, companies, especially large-scale and highly profitable ones, will always face stricter scrutiny from tax authorities and the public (Vemberain & Triyani, 2021). Consequently, management is required to remain compliant with regulations to avoid legal sanctions and maintain business reputation. This trade-off between internal financial incentives and external regulatory constraints underlies the importance of further testing. Based on this framework, the research hypothesis is formulated as follows:

H_{1a} : Company size has a significant effect on tax avoidance.
H_{1b} : Leverage has a significant effect on tax avoidance.
H_{1c} : Profitability has a significant effect on tax avoidance.

Conceptual framework

Figure 1 presents the research model examined in this study.

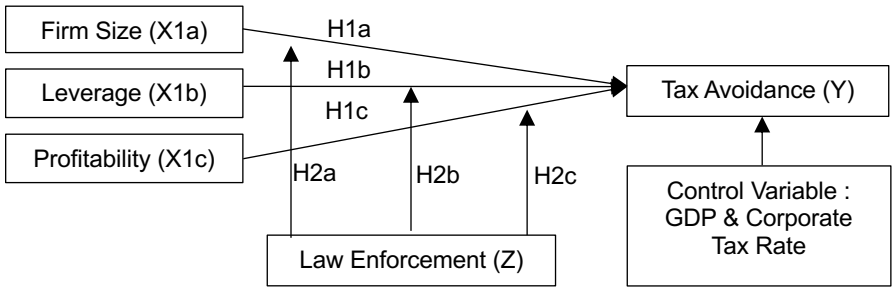

Figure 1. Conceptual framework

3. Research method

Research sample and data

This study uses a quantitative approach and secondary data from the OSIRIS database. The study population includes all manufacturing companies listed on six major stock exchanges in Asia, namely: Indonesia Stock Exchange (IDX), Bursa Malaysia, The Stock Exchange of Thailand (SET), The Philippine Stock Exchange (PSE), Singapore Exchange (SGX), and The Stock Exchange of Hongkong Limited (HKEX) for the observation period 2020-2024.

The selection of these six jurisdictions is based on three strategic considerations: (1) They are the major economic powers in Southeast Asia (ASEAN-5) plus Hongkong as a global financial center that represents the characteristics of both emerging and developed markets; (2) There are contrasting variations in corporate tax rates, ranging from low rates in Hongkong (16.5%) and Singapore (17%) to higher rates in the Philippines (25%) and Malaysia (24%). This difference is crucial to examine the effectiveness of enforcement in different fiscal environments; (3) These six jurisdictions have varying Enforcement Index scores, allowing this study to conduct a cross-country analysis of how institutional power affects corporate tax compliance behavior.

The sampling technique used a purposive sampling approach based on the criteria presented in Table 2. Based on the data screening results, 991 manufacturing companies were initially identified. After an elimination process for companies that did not present complete

financial reports during the 2020-2024 period, 10 companies were dropped, leaving 981 that met the criteria. Furthermore, the panel data are unbalanced, as 105 firm-year observations were excluded due to missing or incomplete data in certain years. At the same time, the respective companies remained in the sample for the duration of their availability. Consequently, this process yields a total of 4,800 observations (unbalanced).

Table 2. Research Sample

Criteria	Country						Total
	Indonesia	Malaysia	Thailand	Philippines	Singapura	Hong Kong	
Manufacturing companies listed on IDX, Bursa Malaysia, SET, PSE, SGX, HKEX during the observation period 2020-2024	166	400	206	38	132	49	991
Manufacturing companies that do not present complete financial reports from 2020 to 2024	6	0	0	2	2	0	10
Total number of companies	**160**	**400**	**206**	**36**	**130**	**49**	**981**

Source(s): Processed Data (2026)

Operational definition and measurement of variables

The measurement of all variables in this study uses measures adopted from several previous studies presented in Table 3.

Table 3. Operational definition and measurement of variables

Variable	Definition	Measurement	Reference
Dependent Variable			
Tax Avoidance	The company's efforts to reduce the tax obligations it pays by using existing legal loopholes.	ETR = $\frac{Income\ Tax\ Expense}{Income\ Before\ Tax}$	(Amin et al., 2023); (Du & Li, 2022); (Huseynov & Klamm, 2012); (Jarboui et al., 2020); (Syahputri, 2025)
Independent Variable			
Firm Size	The capacity and scale of the company's operations as measured by total assets	Firm Size = Ln(Total Assets)	(Amidu et al., 2016); (Eddy et al., 2020); (Jarboui et al., 2020); (Apriatna & Oktris, 2022)
Leverage	Describes the company's ability to finance its operations with debt rather than with its own capital resources.	DER = $\frac{Total\ Liability}{Total\ Equity}$	(Lanis & Grant, 2012); (Saputra et al., 2015); (Jarboui et al., 2020);

Variable	Definition	Measurement	Reference
			(Ernawati et al., 2021)
Profitability	Measured using Return on Assets (ROA), namely by dividing net profit after tax by total assets	ROA = $\frac{Net\ Profit}{Total\ Asset}$	(Hossain et al., 2024); (Jarboui et al., 2020); (Isin, 2018); (Mafrolla & D'Amico, 2016)
Moderating Variable			
Law Enforcement	The ability and effectiveness of the legal system in ensuring compliance with regulations. While the World Justice Project (WJP) Rule of Law Index is a broad macroeconomic metric, its application as a proxy is justified because corporate tax behavior is fundamentally shaped by the overall institutional environment, not solely by tax-specific audits. Dimensions such as the absence of corruption, strict regulatory enforcement, and the effectiveness of civil and criminal justice directly dictate the legal certainty, the cost of non-compliance, and the probability of escaping penalties. Consequently, a strong overall legal infrastructure prevents firms from exploiting regulatory loopholes, making it a robust proxy for deterrence against aggressive tax avoidance.	*Overall Rule of Law Score* : 1. *Constraints on Govern-ment Powers* 2. *Absense of Corruption* 3. *Open Govern-ment* 4. *Fundamental Rights* 5. *Order and Security* 6. *Regulatory Enforce-ment* 7. *Civil Justice* 8. *Criminal Justice*	(World Justice Project, 2025)
Control Variable			
***Gross Domestic Product* (GDP)**	GDP is used to control for a country's economic conditions when assessing tax avoidance	GDP = Ln(GDP)	(Zeng, 2019) & (Eichfelder et al., 2023)
Statutory Tax Rate	Is the corporate tax rate applicable in the country where the company operates, including state corporate income tax as well as other local and additional taxes applicable in the country.	Statutory corporate income tax rate	

Source(s): Processed Data (2026)

Data analysis technique

This study uses panel data regression and moderated regression analysis. Panel data combines time-series and cross-sectional data and is analyzed in three stages: determining the

estimation model, testing classical assumptions, and interpreting regression results. The Hausman test is conducted to determine the right model in hypothesis testing. The Hausman test results show a p-value of 0.2125, which is greater than the 5% significance level, indicating that the random-effect model is better suited for analyzing the research data (Ghozali, 2018). The regression equation model applied in this study is organized as follows:

$$TA_{i,t} = \beta_0 + \beta_1 FS_{i,t} + \beta_2 LEV_{i,t} + \beta_3 ROA_{i,t} + \beta_4 GDP_{i,t} + \beta_5 CTR_{i,t} + \gamma_t + \epsilon_{i,t} \quad (1)$$

$$TA_{i,t} = \beta_0 + \beta_1 FS_{i,t} + \beta_2 LEV_{i,t} + \beta_3 ROA_{i,t} + \beta_4 LE_{i,t} + \beta_5 GDP_{i,t} + \beta_6 CTR_{i,t} + \gamma_t + \epsilon_{i,t} \quad (2)$$

$$TA_{i,t} = \beta_0 + \beta_1 FS_{i,t} + \beta_2 LEV_{i,t} + \beta_3 ROA_{i,t} + \beta_4 LE_{i,t} + \beta_5 (FS_{i,t} \times LE_{i,t}) + \beta_6 (LEV_{i,t} \times LE_{i,t}) + \beta_7 (ROA_{i,t} \times LE_{i,t}) + \beta_8 GDP_{i,t} + \beta_9 CTR_{i,t} + \gamma_t + \epsilon_{i,t} \quad (3)$$

Notes:

TA	= Tax Avoidance
FS	= Company Size
LEV	= Leverage
ROA	= Return on Assets
LE	= Law Enforcement
GDP	= Gross Domestic Product
CTR	= Corporate Tax Rate
β0	= Constant
β1, β2, ..., β7	= Regression Coefficient
γt	= Year Fixed Effects (time-fixed effects)
i	= Entity Unit
t	= Observation Period

4. Results and Discussion

Descriptive statistics

At the data processing stage, a winsorizing technique is applied to the tax avoidance, leverage, and profitability variables to reduce the influence of extreme values (outliers) that could distort regression estimates. In cross-country research, differences in economic structures, fiscal policies, and firm characteristics often yield very high or very low values, which can bias the measurement of means and variances. Winsorizing is done by limiting extreme values to the 1st and 99th percentiles, so that values outside these limits are adjusted to a specified threshold value without removing observations from the sample. This process aims to increase the validity of the panel regression model used in the study. The descriptive statistics in Table 4 show a more controllable distribution of data after winsorizing.

Table 4. Descriptive Statistics

Variable	Obs.	Mean	Std. Dev.	Min	Max
ETR	4,800	.1420156	.3319404	-1.464278	1.587211
Firm Size	4,800	21.22986	1.763511	11.0749	27.62303
Leverage	4,800	.8858976	1.356935	-3.857961	8.255798
Profitability	4,800	3.354377	11.54178	-43.425	36.365
Law Enforcement	4,800	.0058183	.0009501	.0046	.0079
GDP	4,800	26.95523	.4227416	26.5447	27.96485
Corporate Tax Rate	4,800	.2154969	.0272815	.165	.25

Source(s): Processed Data (2026)

The statistical results show an average Effective Tax Rate (ETR) of 0.142 (14.2%). Given that the average statutory tax rate in the sample is 0.215 (21.5%), there is a 7.3% gap, suggesting a general tax-planning practice among manufacturing companies in the region. Profitability (ROA), expressed as a percentage (%), and leverage variables exhibit high volatility, as reflected in the standard deviation exceeding the mean. This reflects the contrasting variation in financial performance and capital structure across companies, ranging from entities with fiscal losses to those with a return on assets of 36.3%. In contrast, the firm size and enforcement variables have a more stable distribution, providing a consistent basis for panel regression analysis.

To minimize extreme outliers, the Debt to Equity Ratio (DER) variable has been winsorized at the 1% and 99% levels. Prior to winsorization, the minimum DER value was -235.216, which was reduced to -3.857 after adjustment at the 1st percentile. This remaining negative value reflects several companies in the sample that experienced negative equity due to the accumulation of large losses (financial distress). This observation was maintained to maintain the authenticity of the panel data and capture the phenomenon of tax behavior in companies with critical capital structures.

Before hypothesis testing, a classical assumption test is conducted to ensure that the regression model meets the basic assumptions. A multicollinearity test is conducted to ensure the stability of the model. Based on Table 5, all variables have a Variance Inflation Factor (VIF) value below 10, with a mean VIF value of 1.38. This finding confirms that there is no correlation among the independent variables that would compromise the reliability of the regression coefficients, so the model is suitable for the next stage of testing.

To address potential heteroskedasticity and autocorrelation issues in panel data, the study employs heteroskedasticity- and autocorrelation-robust standard errors clustered at the firm level (vce(cluster id)). This approach ensures that statistical inference remains valid even in the presence of non-constant error variance and within-firm serial correlation.

Table 5. Multicollinearity Test Results

Variable	VIF	1/VIF
Tax Avoidance	1.06	0.943082
Firm Size	1.03	0.968420
Leverage	1.06	0.944916
Profitability	2.02	0.495449
Law Enforcement	1.23	0.816217
GDP	1.87	0.533780
Mean VIF	**1.38**	

Source(s): Processed Data (2026)

Hypothesis testing results

Hypothesis testing is carried out using the Random Effect Model (REM), which is divided into three estimation models to provide a comprehensive picture of the dynamics of the relationship between variables. The REM model was confirmed by the Hausman test, as shown in Table 6. Hausman Test Results, which yielded a probability value of 0.2125. This value exceeds the 5% significance level, so the null hypothesis is not rejected.

Table 6. Hausman Test Results

	Nilai
Chi2(4)	5.83
Prob>Chi2	0,2125

Source(s): Processed Data (2026)

The results of hypothesis testing are shown in Table 7.

Table 7. Hypothesis Test Results

	Model 1	**Model 2**	**Model 3**
Firm Size	0.008***	0.008***	-0.009
	(3.27)	(3.27)	(-0.57)
Leverage	0.001	0.002	-0.015
	(0.27)	(0.35)	(-0.57)
Profitability	0.005***	0.005***	0.007***
	(19.59)	(19.89)	(4.61)
GDP	0.038***	0.048***	0.048***
	(3.33)	(3.99)	(4.05)
Corporate Tax Rate	0.824***	1.125***	1.169***
	(4.33)	(4.82)	(4.96)
Law Enforcement		13.437**	-50.930
		(2.16)	(-0.90)
Mod_Firm Size			2.935
			(1.12)
Mod_*Leverage*			2.740
			(0.60)
Mod_Profitability			-0.385
			(-1.47)
_cons	-1.248***	-1.654***	-1.312***
	(-3.95)	(-4.67)	(-2.84)
R-squared (overall)	0.041	0.042	0.043
Observations	4800	4800	4800

t statistics in parentheses
* $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$
Source: Researcher Data, 2026

Model 1 shows that firm characteristics simultaneously affect tax avoidance. Partially, firm size (β=0.008; p<0.01) and profitability (β=0.005; p<0.01) are significantly positively related to ETR. This indicates that larger, more profitable companies tend to have higher levels of compliance (lower tax avoidance). Meanwhile, leverage shows no significant effect (p>0.05), which suggests that debt interest expense is not a major instrument in tax avoidance strategies in the manufacturing sector in Asia.

Based on the model estimation, the reported R^2 is 0.041. This indicates that the variation in firm size, leverage, profitability, and the moderating effect of law enforcement collectively accounts for 4.1% of the variance in ETR. While statistically low, a minor R^2 is remarkably common and widely acceptable in empirical accounting and corporate finance research. Corporate decisions regarding tax strategies represent highly complex behavioral phenomena that are heavily driven by various unobserved institutional, internal governance, and macroeconomic factors omitted from the financial model. Because the primary objective of this study is hypothesis testing (i.e., examining the statistical significance and directional effects via p-values) rather than economic forecasting, a low R^2 does not diminish the statistical validity or the inferential power of the significant coefficients

In Model 2, including the law enforcement variable as a direct predictor yields a significant positive effect (β = 13.437; p < 0.05). While the coefficient magnitude appears unusually large compared to other variables, this is a mathematical artifact of the variable's scale. The World Justice Project Rule of Law Index is measured on a narrow scale from 0 to 1. Therefore, the coefficient of 13.437 represents the hypothetical impact of a full 1-unit increase (i.e., moving from an absolute absence of law to a perfect legal system), which is empirically impossible. To assess the economic significance, a more realistic incremental change must be considered. For instance, a 0.1-point improvement in a country's law enforcement index reflecting a realistic policy reform would translate to an increase in the Effective Tax Rate (ETR) of approximately 1.34 units (or 1.34 percentage points). This economically significant finding demonstrates that even moderate improvements in a country's institutional and regulatory quality can substantially suppress tax avoidance practices and increase corporate tax compliance. Control variables, such as GDP and the Corporate Tax Rate, consistently show significant effects, consistent with Zeng (2019).

Finally, Model 3 tests the moderating effect of law enforcement on the interaction between law enforcement and firm characteristics. The results show that the R^2 value increases to 4.3%, but none of the moderating interactions reach statistical significance (p>0.05). This confirms that enforcement in Asia acts as a predictor variable (a direct independent variable) rather than a moderator variable (Sharma et al., 1981). Thus, hypotheses H1a and H1c are accepted, while H1b and all moderation hypotheses (H2a, H2b, H2c) are rejected.

Discussion

Determinants of Financial Attributes on Tax Avoidance

Hypothesis testing results show that company size has a significant positive effect on Effective Tax Rate (ETR). This finding indicates that the larger the scale of manufacturing companies in Asia, the lower their tendency to engage in aggressive tax avoidance. This phenomenon is consistent with the tenets of Agency Theory (Jensen & Meckling, 1976), in which large companies seek to minimize agency costs by increasing transparency in response to stricter

external scrutiny from governments and regulators (Apriatna & Oktris, 2022; Ma & Thomas, 2020). Specifically, large companies on Asian stock exchanges such as SGX, HKEX, and IDX are theoretically characterized by higher public visibility. Based on Compliance Theory, this institutional position implies that larger firms face greater pressure to comply to avoid audit risks and sanctions that can damage the corporation's image in the eyes of international investors (Vanstraelen & Zou, 2022). In this context, tax compliance is seen as an instrument to maintain business reputation and legitimacy in the global market.

Regarding leverage, the results found no significant effect on ETR, which supports the findings of Dewi & Oktaviani (2021) and Nguyen (2021). This suggests that debt structure is not a major determinant of tax avoidance for manufacturing companies in Asia. The non-use of tax incentives on interest expense is likely due to strict regulations on interest expense limits (Thin Capitalization Rules) that apply in several Asian countries, such as Indonesia and Malaysia (Dianawati & Agustina, 2020). This restriction causes only debt from certain third parties to be deductible from taxable income (Prasetyo & Primasari, 2021). Instead of tax avoidance through debt, companies tend to maintain financial stability to avoid the risk of bankruptcy and creditor pressure, in line with the Agency Theory (Jensen & Meckling, 1976). Highly leveraged companies are more cautious in tax reporting to avoid legal sanctions that could worsen their liquidity position (Dewi & Oktaviani, 2021; Nguyen, 2021).

Meanwhile, profitability is shown to have a significant positive effect on ETR, suggesting that higher profits are associated with greater tax compliance. Profitable companies have sufficient cash flow to meet tax obligations without disrupting net income stability (Mocanu et al., 2021). This finding aligns with Agency Theory (Jensen & Meckling, 1976), which posits that managers in profitable companies in Asia tend to choose legal tax planning to maintain harmonious relationships with principals and regulators and to avoid litigation risks (Apriatna & Oktris, 2022). Furthermore, this result supports Compliance Theory, which emphasizes the importance of legitimacy; financially successful firms tend to be more compliant with regulations as a form of corporate social responsibility to maintain a positive reputation in the eyes of stakeholders (Pratama & Muhammad, 2025; Vemberain & Triyani, 2021).

The Role of Law Enforcement as a Moderating Variable

The findings of this study provide empirical evidence that law enforcement is ineffective in moderating the effects of company size, leverage, or profitability on tax avoidance. Based on Model 3 testing, the interaction between law enforcement variables and company characteristics is not significant.

In terms of company size, strong law enforcement does not automatically suppress tax behavior among large companies. According to Deterrence Theory, compliance should increase as the risk of detection rises (Becker, 1974). However, in the Asian region, large companies have the resources and support of professional tax consultants who can perform economic analyses to navigate complex legal structures (Oktrivina, 2022). The "profit vs. penalty cost calculation" effect (Allingham & Sandmo, 1972) makes general enforcement policies less effective in changing the tax behavior of companies with massive organizational structures.

Similarly, with respect to the leverage and profitability variables, strengthening law enforcement does not result in significant changes in behavior. Despite the increased sanction

risk, firms with certain capital structures continue to focus on their own internal risk management. Companies with high profitability, for example, have the financial resilience to bear both compliance costs and legal risks (Hossain et al., 2024; Alkurdi et al., 2024; Allingham & Sandmo, 1972). The insignificance of this moderation indicates that, in Asia, law enforcement acts more as a predictor variable (direct effect) than as a moderator (Sharma et al., 1981).

This is supported by the statistical results on the control variables, where the Corporate Tax Rate shows much stronger significance than law enforcement. This provides a strong signal that manufacturing firms in Asia are more responsive to direct economic incentives (tariff rate) than external legal pressure (detection risk). The non-moderating law enforcement reflects the divergence of institutional quality among the six countries studied, where countries with high rule of law, such as Singapore, already have stable compliance levels, so legal interactions no longer impose drastic behavioral changes on firms' internal characteristics.

5. Conclusion

This study evaluates the internal and external determinants of tax avoidance practices of manufacturing firms in six Asian jurisdictions (Indonesia, Malaysia, Thailand, the Philippines, Singapore, and Hong Kong). Based on panel data regression analysis and Moderated Regression Analysis (MRA), this study concludes that firm size and profitability are significant internal determinants of tax avoidance. Large-scale manufacturing companies with superior financial performance tend to exhibit higher tax compliance. This confirms that firms with strong public visibility and profitability prioritize preserving reputation and social legitimacy over aggressive tax planning. Second, leverage is not proven to affect tax avoidance behavior. This finding indicates that the use of debt in the Asian manufacturing sector is primarily for capital structure and operational stability rather than as a tax shield, which may be due to thin capitalization regulations in many of the sample countries. Third, law enforcement in the Asian region acts as a direct predictor variable, increasing tax compliance but not moderating the effect of firm characteristics on tax avoidance. The quality of legal institutions does not automatically change the way firms respond to their internal structure (size, debt, profit) in tax decisions. This confirms that tax avoidance decisions are predominantly influenced by internal corporate economic considerations rather than external legal pressures.

Theoretically, this study contextualizes the literature on Deterrence Theory and Compliance Theory within a cross-country framework. The empirical findings reveal insignificant moderation effects, indicating that while cross-country law enforcement serves as a vital institutional foundation, it does not act as an active interaction mechanism that alters the relationship between internal financial drivers and corporate tax strategies. This lack of statistical interaction highlights specific empirical boundaries of the moderation model, without necessarily discounting the broader, direct influence that law enforcement may exert on corporate compliance overall. In practice, these results provide input for tax authorities in Asia that policies to suppress tax evasion are not enough to strengthen legal sanctions; they also need to pay attention to economic incentives, such as adjusting competitive corporate tax rates, given that the tax rate variable proved to have a significant effect in this study.

This study acknowledges several limitations. First, the use of tax avoidance proxies relies solely on the Effective Tax Rate (ETR), which may not capture non-routine tax avoidance practices. Second, the research scope is limited to the manufacturing sector. Third, methodologically, the reliance on the Random Effect Model (REM) as dictated by the Hausman test assumes that unobserved country-specific effects are uncorrelated with the independent variables. Although this study attempted to control for cross-country heterogeneity by including GDP and statutory tax rates, it is possible that other unobserved institutional or cultural heterogeneities across the six Asian jurisdictions are not fully captured. Future researchers are advised to use alternative proxies, such as the Book-Tax Difference (BTD) or Cash ETR, and to expand coverage to more industries or compare industry sectors to determine whether the quality of law enforcement has different impacts across sectors with different asset characteristics. Furthermore, future studies could address the methodological limitation by employing alternative estimation strategies, such as incorporating country-fixed effects or clustering standard errors at the country level, to provide stricter controls for unobserved macroeconomic heterogeneity.

Disclosure of AI Use

The authors utilized ChatGPT (OpenAI) and Gemini (by Google) during the drafting phase to polish the manuscript's readability and grammatical structure. Following the use of this tool, the authors carefully reviewed and revised the content as necessary, assuming full responsibility for the final content of the publication.

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