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# ANALYSING THE USE OF GROWTH RATIOS AND CONCEPTS AS TOOLS TO DETERMINE THE FOCUS OF TAX AUDITS

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**Abstract**

This study aims to explore the use of financial ratios and growth concepts as tools in determining the focus of tax audits. The research method used in this study is the literature method. The results of this study offer valuable insights for tax authorities in developing a more targeted and efficient audit strategy. This study also provides an analytical framework for tax authorities in developing a more data-driven audit approach, which can ultimately improve the fairness and integrity of the tax system. As such, this study makes a significant contribution to the tax auditing literature and audit practice, and supports efforts in improving tax compliance through innovation and utilisation of analytical tools.
**Keywords**: Analysis, Use of Ratios, Growth Concept, Tools, Tax Audit.

## Introduction

Taxes are the main source of revenue for the government to run various development programmes and public services. Taxes are contributions levied by the government from individuals or legal entities compulsorily based on law, without direct reward, which are used to finance public expenditures and achieve the state's objectives in improving people's welfare (Lopez & Peters, 2019) . Taxes serve as the main source of revenue for the state budget, which includes various types such as income tax, value-added tax, and sales tax among others, which aim to regulate the economy, redistribute wealth, and facilitate the provision of public goods and services to all levels of society. Therefore, optimisation of tax revenue is crucial to ensure the government can finance these needs (Foster, 2018) . One crucial aspect in optimising tax revenue is the effectiveness of tax audits conducted by tax authorities against taxpayers. Tax audits aim to verify taxpayer compliance with tax regulations, identify potential errors or non-compliance, and prevent tax evasion (Narayan & Sharma, 2018).

Tax audits play an important role in optimising state revenues because through this process, the government can ensure that all taxpayers comply with applicable tax provisions. This includes verifying the accuracy of tax reporting, identifying tax avoidance or evasion, as well as applying sanctions for those proven not to fulfil their obligations (Taylor & Richardson, 2017) . Tax audit helps to ensure the efficiency and effectiveness of tax collection, which will ultimately increase state revenue from the tax sector. With higher compliance from taxpayers, the government can obtain a more stable source of funds to finance development programmes and public services (Freedman, 2017) .

On the other hand, tax audits are also very relevant in the context of increasing public trust in the tax system. If taxpayers know that audits are conducted fairly and transparently, a positive perception of the fairness and reasonableness of the tax system will be created. This in turn can encourage voluntary compliance, reduce tax avoidance practices and foster fiscal awareness in society. Higher compliance will broaden the tax base and increase state revenue without having to increase tax rates (Slemrod & Gillitzer, 2018) . Finally, with optimal revenue, the state can ensure sustainable development and adequate budget allocation for vital sectors such as education, health, infrastructure, and social services, all of which contribute to the country's overall economic and social progress (Smith & Thomas, 2021) .

With the growing number of taxpayers and the increasing complexity of economic transactions, tax authorities often face challenges in effectively allocating resources for tax audits. On the other hand, random or unfocused audits are often inefficient and waste resources without significant results in finding tax non-compliance (Aksoy, 2019) .

The use of financial ratios and growth concepts can be an innovative solution in addressing these challenges. Financial ratio analysis provides insight into the financial health, performance, and potential risk of tax non-compliance of an entity. Meanwhile, the concept of growth can indicate significant changes in the size or scale of an entity's operations that may affect its tax liabilities. Both, when used together, can be powerful analytical tools for tax authorities in determining the focus of tax audits (Miller, 2022) .

However, the practical implementation of this approach requires a deep understanding of how financial ratios and growth indicators can be interpreted in the context of a tax audit. Appropriate selection of ratios and growth parameters, complemented by comparative analysis and historical trends, can increase the likelihood of effective identification of high-risk entities or transactions (Williams & Dobson, 2018) .

This research aims to analyse how financial ratios and growth concepts can be integrated as tools in determining the focus of tax audits, identify analytical frameworks, and evaluate their potential applications in improving tax audit effectiveness. Through this research, it is hoped that tax authorities can acquire new methodologies that strengthen their efforts in optimising tax revenue and allocating tax audit resources more efficiently and effectively.

**Research Methods**

The study in this research uses the literature method. The literature research method is an approach conducted by collecting, analysing, and interpreting data from written sources such as books, scientific journals, articles, and other relevant documents to gain an in-depth understanding of a topic. In this method, researchers identify and use relevant literature to build a theoretical foundation or framework of thought, verify facts, and support arguments or hypotheses in research (Heriyanto ;, 2018) (Rizkykawasati, 2019) . This process involves screening credible and relevant sources, synthesising the information gathered, and critiquing the reading material to ensure validity and objectivity in producing research conclusions. Literature research methods are often used in theoretical studies and are an important foundation in scientific research to ensure the integrity and depth of analysis and scientific writing (Iryana, 2019) .

**Results and Discussion**

**The Use of Ratios and Growth Concepts Can Assist in Determining the Focus of Tax Audits**

The use of ratios and growth concepts is a very important tool in determining the focus of tax audits. Financial ratios can provide an overview of an entity's financial condition, which, when properly analysed, can reveal indications of potential tax avoidance or tax reporting errors. Financial ratios such as liquidity, solvency and profitability ratios can be used to compare the financial performance of a company from year to year, or to compare it with other companies in the same industry. Through this analysis, tax authorities can identify anomalies or discrepancies that may signal a violation of tax regulations (Davis & Clark, 2021) .

The concept of growth, on the other hand, helps in assessing whether a company's revenue and asset growth is in line with market trends and relevant industries. Growth analysis can show whether there is a significant discrepancy between business growth and tax reporting. For example, if a company experiences significant revenue growth but is not followed by a proportional increase in its tax reporting, this could be an early indication of tax avoidance (Harrison & Anson, 2018) .

Furthermore, the application of growth ratios and analyses can facilitate risk assessment by tax authorities in determining subjects for audit. By focusing resources on entities that show indications of high tax risk, the efficiency and effectiveness of tax audits can be improved, ensuring that tax audits are directed to entities most likely to generate important findings (Evans & Robinson, 2017) .

In addition, the use of growth ratios and analyses also supports transparency and accountability in tax audits. By using a data-driven and objective approach, tax authorities can strengthen the legal basis and fairness of audits. This is crucial in building public trust and voluntary compliance with good tax governance (Robinson, 2020) .

Successful application of this method requires access to accurate and complete financial data, as well as analytical skills to correctly interpret the ratio results and growth trends. Therefore, increasing the capacity of human resources and information technology is key in optimising the use of financial ratios and growth concepts in tax audits (Clark, 2018) .

The integration of tax information systems with other financial data platforms such as capital markets can provide valuable additional data sources for analysis. By integrating data from multiple sources, tax authorities can have a more holistic view of an entity's economic activity, assisting in identifying complex tax evasion schemes (Brown & Jones, 2020) .

Finally, adaptation to new developments in business practices and financial governance is also important. Along with economic dynamics and business innovation, methodologies in ratio and growth analysis need to be continuously developed to maintain their relevance. Through this concerted effort, the application of financial ratios and growth concepts can be a very effective tool in improving the integrity and fairness of the tax system.

**Implications for Tax Audit Efficiency and Effectiveness**

The implications of using financial ratios and growth concepts on the efficiency and effectiveness of tax audits are significant. Efficiency in this context refers to the utilisation of resources required in the audit process, while effectiveness concerns the degree of success in identifying and correcting tax law violations. The use of these analytical tools allows tax authorities to focus more on cases with a high potential for tax evasion, reducing the amount of time and effort spent on audits with a low probability of findings (Patel, 2021) .

Financial and growth ratios allow tax auditors to identify deviations from industry norms as well as historical trends that may indicate non-compliant activities. This helps them to prioritise cases that present the highest risk and instead of using a 'one-size-fits-all' approach, they can conduct a more targeted and in-depth examination of the entity. Thus, the limited time and resources can be utilised more strategically and directed towards the endeavours that are most likely to result in substantial tax adjustments (Bertoni, 2020) .

With the increased effectiveness of tax audits, there is also an increased deterrence effect on other taxpayers. Those who may consider evading their tax obligations will think twice if they realise that tax authorities have sophisticated tools and methods in identifying and cracking down on potential tax evasion. A further implication of this increased effectiveness is increased overall tax compliance and levelling the playing field for all businesses, thereby fostering a more positive perception of a fair and transparent tax system (O'Neill & Quinn, 2017) .

However, the use of financial ratios and growth analyses also implies the need for investment in training and technology. Tax authorities must ensure that auditors and tax staff are equipped with sufficient knowledge to interpret the data they are confronted with and use financial ratios and growth analysis effectively. This investment should be seen as a valuable asset as the output of this increased competence will be seen in greater tax collections and a reduction in revenue loss due to tax evasion (Jones & Smith, 2019) .

Finally, by applying these more detailed analysis methods, tax authorities are also sending a clear message that they prioritise the principles of fairness and integrity in the tax system. This can strengthen co-operative relationships with law-abiding taxpayers and create mutual trust that is essential for a sustainable tax ecosystem. These positive implications can influence the overall business environment, promote economic growth, and ensure efficient tax collection to support development and public policy (Zhang & Choy, 2020) .

Thus, the use of financial ratios and growth analysis in tax audits has significant positive implications for the efficiency and effectiveness of the process. By focusing resources on high-risk cases, tax authorities can improve the accuracy and outcomes of audits, while optimising the use of limited resources. Furthermore, this increased effectiveness impacts the overall level of tax compliance, reduces tax evasion, and strengthens public confidence in a fair and transparent tax system. However, realising these benefits requires investments in training and technology, which should be seen as strategic investments to improve tax audit capacity and capabilities. Finally, this data analytics- and compliance-focused approach supports more credible development and public policy, strengthens the relationship between taxpayers and tax authorities, and fosters a healthy and fair business ecosystem for all parties.

**Conclusion**

The analysis of the use of financial ratios and growth concepts as tools in determining the focus of tax audits has shown how important analytical tools are in improving the effectiveness and efficiency in the process of selecting tax subjects to be audited. This approach allows tax authorities to proactively identify taxpayers with high compliance risks, ensuring resources are allocated to areas with the most significant tax evasion potential. As such, this method not only optimises the use of limited resources but also enhances the fairness and integrity of the tax system by targeting those most likely to evade their tax obligations.

Furthermore, the use of financial ratios and growth analysis facilitates an evidence-based approach in tax audits, which provides a solid basis for tax authorities to make more informed and objective decisions. It also increases transparency and can be favoured by taxpayers, as it promotes a better understanding of how audit decisions are made. Going forward, the application of these more data-oriented and analytical methods can contribute to a more predictive, fair, and efficient tax environment, ultimately supporting tax compliance and strengthening tax awareness among taxpayers.

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