

The Effect of Effective Tax Rate, Moral Hazard, and Firm-Specific Determinants on Capital Structure

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ABSTRACT: This research aims to examine the effectiveness of Effective Tax Rate, Firm Size, Profitability, Non-Debt Tax Shield, and Moral Hazard toward Capital Structure in oil, gas, and coal subsector firms listed on the Indonesian Stock Exchange during the period 2016-2024. The study employs a quantitative research design using panel data regression analysis. The Fixed Effect Model is selected based on panel data model selection tests and analyzed using EViews 12. The empirical findings reveal that only Profitability has a statistically significant negative effect on Capital Structure. Meanwhile, Effective Tax Rate, Firm Size, Non-Debt Tax Shields, and Moral Hazard do not exhibit statistically significant effects. These results suggest that internal financing capacity plays a more dominant role than tax incentives, firm scale, alternative tax shields, or agency-related considerations in determining capital structure decisions within the observed subsector. These research findings suggest that the effect of internal financing capacity dominates the effect of tax and agency-related considerations in determining Capital Structure within the Indonesian energy subsector. This study is limited by its sector-specific focus and restricted observation period.

KEYWORDS: Capital Structure, Effective Tax Rate, Profitability, Firm Size, Non-Debt Tax Shield, Moral Hazard

INTRODUCTION

The determinants of capital structure remain a fundamental concern in corporate finance, giving rise to persistent theoretical debates and mixed empirical findings. These determinants are influenced by both macroeconomic dynamics and firm-specific characteristics, as extensively documented in prior literature. A comprehensive understanding of these factors is essential, as they inform financial managers in formulating optimal financing strategies and achieving long-term financial sustainability. (Ali et al. 2022)

According to Yunira (2022) dan Wijaya (2024), the primary objective of a firm is to maximize the shareholder's wealth by increasing the stock price or the firm value, these objective can be achieved by ensuring the funding efficiency through capital structure policies that can lead to an optimal capital structure. Valencia and Dermawan (2024) and Ali et al. (2022) argue that an optimal capital structure depends on the firm's ability and capacity in balancing the internal and external sources of its operational financing. These argument aligns with the pecking order theory proposed by Myers (1984), which explains the firm's hierarchy in selecting the sources of funding for operational activities

The capital structure theory created by Modigliani and Miller (1958) becomes the foundational framework for the determinants and other forms of capital structure. This theory has served as the foundation for many empirical studies, including the research of Jaworski and Czerwonka (2021) and Ali et al. (2022), that examine firm-specific factors such as Firm Size, Profitability, dan Non-Debt Tax Shield as the determinants significantly effecting the Capital Structure. Furthermore, capital structure decisions are shaped by firm's incentives to exploit the tax benefits of debt financing, especially the interest tax shield mechanism. This consideration is proposed by Kraus and Litzenberger (1973) in trade-off theory as an extend literature from capital structure theory proposed by Modigliani (1963). The empirical research by Heider and Ljungqvist (2015) is supporting this theory by incorporate effective tax rate as one of the determinants that significantly effecting capital structure formation. However, Modigliani and Miller's theory and earlier studies didn't consider external and internal factors such as asymmetric information, bankruptcy costs, and agency problems (Ali et al. 2022).

Agency theory proposed by Jensen and Meckling (1976) written in the research by Kahya et al. (2020) introduces an additional dimension, emphasizing the conflicts of interest between managers and shareholders or agency problems. Wald (1999) research extends and integrates moral hazard considerations into capital structure decisions, suggesting that managerial risk-taking



behavior can alter capital structure formation. Wald (1999) studies resulting a significant relationship between moral hazard and capital structure.

While these theoretical framework and extensive empirical investigation provide competing predictions on determinants of capital structure, findings in studies of Ali et al. (2022), Kahya et al. (2020), Jaworski and Czerwonka (2021), and Heider and Ljungqvist (2015) show that factors effecting capital structure decisions remain inconclusive and inconsistent.

The energy sector, especially the oil, gas, and coal subsector, presents unique characteristics. Firms in this sector are typically capital-intensive and require substantial long-term financing for asset investment, making them more vulnerable to leverage-related risks. Interestingly, while energy firms historically exhibit high capital structure in debt levels, recent trends show downward in long-term debt ratios compared to other sectors. Oil, gas, and coal subsector firms listed on the Indonesia Stock Exchange between 2019 and 2023. The ratio declined from 23.56% in 2019 to 13.70% in 2023, indicating potential capital structural changes in financing decision influenced by macroeconomic fluctuations and firm-level determinants.

Therefore, this research aims to provide updated empirical evidence on the impact of Effective Tax Rate, Firm Size, Profitability, Non-Debt Tax Shield, and Moral Hazard on Capital Structure within Indonesia's energy subsector.

LITERATURE REVIEW AND HYPOTHESIS

Trade Off Theory

Trade off theory proposed by Kraus and Litzenberger (1973) in Ali et al. (2022) research is an extension from capital structure theory by Modigliani (1963) that consider the exchange of tax benefit and bankruptcy cost to create an optimal debt ratio for the firm through identification of cost and benefit from debt financing.

Pecking Order Theory

Pecking order theory proposed by Myers (1984) creates a hierarchy for firm financing system by stating that firms prefer internal financing over external financing such as debt and equity. According to Kahya et al. (2020) research pecking order theory posits that firms follow a financing hierarchy in which internally generated funds are preferred, and external financing is undertaken only when internal resources are inadequate, typically starting with lower-risk debt instruments before issuing equity.

Agency Theory

Agency theory proposed by Jensen and Meckling (1976) postulate the cost created from conflicts of interest between manager and shareholders. Alabdulkarim (2023) states that agency problems arise from the separation of control and ownership by delegation from shareholders to managers. This delegation creates information asymmetry and divergent incentives, potentially leading managers to engage in self-interested behavior that deviates from firm's overall objective to maximize shareholders wealth.

Effective Tax Rate and Capital Structure

The relation between debt financial decision and the tax benefit associated with interest deductibility play a crucial role in shaping an optimal capital structure from adjustments in debt ratio (Ali et al. 2022). According to Yunira (2022) research and under trade-off theory corporate taxation increases the marginal of debt financing through interest tax deductibility. Firms with higher tax rates are expected to employ greater debt in their capital structure to reduce taxable income, creating in a positive relationship between effective tax rate and capital structure.

However according to Heider and Ljungqvist (2015) research effective tax rate may exhibit an inverse effect towards capital structure. Their findings suggest that firms choose equity over debt because the tax burden increase and outweighs the tax benefit derived from interest deductibility

H₁: There is a significant relationship between effective tax rate and capital structure in oil, gas, and coal subsector firms

Firm Size and Capital Structure

Based on the findings of Ali et al. (2022) research firm size as an essential factor in shaping the firm's capital structure through debt financing. Suharsono and Setiadi (2020) contend that firms possessing a larger asset base will be perceived more creditworthy by the creditor, as stronger liquidity ratio enhance the firm's capacity to repay outstanding loans.

Alabdulkarim (2023) reports a positive significant relationship between firm size and capital structure, suggesting that larger firms benefit from reduced agency and monitoring costs and possess greater access to financial markets, which enhances their capacity to utilize debt financing. In contrast, Ariani and Wiagustini (2017) document an inverse relationship, indicating that larger firms are inclined toward equity financing as their substantial asset capacity and financial strength reduce dependence on debt financing.

H₂: There is a significant relationship between firm size and capital structure in oil, gas, and coal subsector firms

Profitability and Capital Structure

According to pecking order theory, Ali et al. (2022) and Kahya et al. (2020) argue that firms prefer to use retained earnings derived from operating profit as their source of funding for operational activities before resorting to external sources such as debt. This hierarchy arises from information asymmetry between managers and shareholders, which makes the cost of external financing to increase rather than the cost of internally generated funds.

However, trade-off theory and Alabdulkarim (2023) provide contradictory evidence, indicating a positive relationship between profitability and capital structure. Firms with higher profitability tend to adopt higher debt financing to maximize after-tax returns.

H₃: There is a significant relationship between profitability and capital structure in oil, gas, and coal subsector firms

Non-Debt Tax Shield and Capital Structure

Non-debt tax shields are expected to exert negative and significant relationship influence on capital structure, as they serve as substitutes from the tax benefit of debt financing. According to Ali et al. (2022), firms with substantial fixed assets generate higher depreciation and amortization expenses, which provide tax deductions independent of interest payments.

Similarly, Wijaya (2024) argues that because non debt tax shield derive from depreciation-based tax deductions, firms have reduced incentives to employ debt financing when depreciation-generated tax savings are already substantial or sufficiently large. In contrast, Saif-Alyousfi et al.(2020) document a significant and positive relationship between non debt tax shield and capital structure proposing that depreciation-induced tax savings strengthen firm's financial positions and incentivize greater use of long-term debt, particularly to support fixed assets investments.

H₄: There is a significant relationship between non-debt tax Shield and capital structure in oil, gas, and coal subsector firms

Moral Hazard and Capital Structure

From an agency perspective, Moral Hazard may effect capital structure through its impact on asset structure and risk perception. Kahya et al. (2020) suggest that higher Moral Hazard ratio proxied by the proportion of inventory to total assets may lead to an increase in capital structure. They argue that greater inventory holdings can reduce perceived bankruptcy risk, particularly when such assets are financed through structured capital arrangements, thereby encouraging higher debt utilization. Similarly Saleh and Nuzleha (2024) argues argue that a lower proportion of inventory relative to total assets reflects more efficient asset management and stronger capital discipline. Under this perspective, improved operational efficiency is associated with a reduced debt ratio, leading to a decline in capital structure with debt financing.

H₅: There is a significant relationship between moral hazard and capital structure in oil, gas, and coal subsector firms

METHODOLOGY

This research employs a quantitative research design using a causal inference approach to examine the relationships between the proposed variables. The research object consists of oil, gas, and coal subsector firms listed on the Indonesian Stock Exchange from 2016-2024 period. The sampling technique applied in this study is non-probability sampling, whereby elements within the population do not have an equal probability of being selected as research samples. Specifically, purposive sampling is employed, requiring the selection of firms that meet predetermined criteria. The sample is therefore restricted to companies that satisfy the following selection criteria Table 1.



TABLE 1. SAMPLE SELECTION CRITERIA

No	Sample Criteria	Total Sample
1.	Oil, gas, and coal subsector companies that were consistently listed on the Indonesia Stock Exchange during the period 2016–2024.	51
2.	Energy sector companies within the oil, gas, and coal subsector that consistently published annual financial statements for the fiscal years 2016–2024, covering a full twelve-month reporting period (fourth-quarter financial reports).	45
	Outlier	(38)
	Total sample use for research	7
	Total research period	9
	Total Sample	63

Capital Structure

Capital Structure represents the proportion to which a firm finances its assets through long-term debt, consistent with Ali et al. (2022) and Shkrekova and Naumoski (2024). The focus on long-term debt is based on the premise that short-term debt primarily supports working capital needs and routine operational expenditures, whereas long-term debt reflects strategic financing decisions that shape the firm's capital structure over time.

Effective Tax Rate

Effective Tax Rate reflects the proportion of pre-tax earnings paid as corporate tax and is calculated as total tax expense divided by Earnings Before Tax (EBT). Noted by Ali et al. (2022), this ratio captures the firm's effective tax burden and provides insight into how taxation may affect financing decisions.

Firm Size

Firm Size reflects the scale of a firm's operations and is commonly used as a proxy for firm stability, resource availability, and access to external financing. Larger firms typically possess greater asset bases, which enhance their capacity to secure external funding for expansion activities. Consistent with Ali et al. (2022), Firm Size is measured as the natural logarithm of total assets.

Profitability

Profitability represents a firm's ability to generate earnings from its assets and serves as a primary source of internal financing. Higher profitability strengthens internal funding capacity and reduces reliance on external debt, consistent with pecking order theory. Following Ali et al. (2022) research, Profitability is measured using Earnings Before Interest and Taxes (EBIT) divided by Total Assets.

Non-Debt Tax Shield

Non-Debt Tax Shields represent tax deductions derived from depreciation and amortization expenses. These deductions provide tax benefits independent of debt financing and may substitute for the interest tax shield associated with capital structure consist of debt. Non-Debt Tax Shield is measured as depreciation and amortization expenses divided by total assets (Ali et al. 2022).

Moral Hazard

Moral Hazard captures agency-related risk behavior and managerial incentives that may influence capital structure decisions. In this study, Moral Hazard is proxied by the ratio of inventory to total assets, which reflects asset structure characteristics and potential bankruptcy risk exposure.

This study employs panel data regression analysis with a fixed effects model is utilized to estimate the equation., which combines both time-series and cross-sectional observations. The use of panel data is particularly appropriate as it allows for the



examination of individual heterogeneity across firms while capturing dynamic changes over time (Ali et al. 2022). Compared to purely cross-sectional or time-series analyses, panel data provide greater variability, reduce potential multicollinearity among explanatory variables, and enhance the efficiency and robustness of parameter estimates.

The Fixed Effects Model assumes that differences across entities are reflected in variations in the intercept term. This approach controls for unobserved, time-invariant heterogeneity that may be correlated with the independent variables. By accounting for firm-specific characteristics that remain constant over time, the FEM produces more consistent and unbiased estimates when such unobserved effects are present. As a result, the estimate panel data regression for this research:

$$CS_{t,i} = CS_{t-1,i} - ETR_{t,i} - FZ_{t,i} - PROF_{t,i} - NDTSt,i + MH_{t,i} + e_{t,i}$$

Where

- $CS_{t,i}$ = Capital Structure at time t for firm i
- $CS_{t-1,i}$ = Capital Structure at time $t-1$ for firm i
- $ETR_{t,i}$ = Effective tax rate at time t for firm i
- $FZ_{t,i}$ = Firm size t for firm i
- $PROF_{t,i}$ = Profitability at time t for firm i
- $NDTSt,i$ = Non debt tax shield at time t for firm i
- $MH_{t,i}$ = Moral hazard at time t for firm i
- $e_{t,i}$ = Error term

TABLE 2. VARIABLES

Variable	Definition	Abbreviation
Capital Structure (Y)	$\frac{\text{Long Term Debt}}{\text{Total Assets}}$	CS
Effective Tax Rate (X1)	$\frac{\text{Corporate Tax Paid}}{\text{Taxable Income}}$	ETR
Firm Size (X2)	Total Assets Natural Logarithm	FZ
Profitability (X3)	$\frac{\text{Earnings before Interest and Taxes}}{\text{Total Assets}}$	PROF
Non-Debt Tax Shields (X4)	$\frac{\text{Depreciation and Amortization Expenses}}{\text{Total Assets}}$	NDTS
Moral Hazard (X5)	$\frac{\text{Inventory}}{\text{Total Assets}}$	MH

RESULTS

TABLE 3. DESCRIPTIVE STATISTICS

Sample: 2016-2024

	CS	ETR	FZ	PROF	NDTS	MH
Mean	0.055030	0.299040	33.52795	55.76556	1.008661	1.335626
Standard Deviation	0.051296	0.180689	0.991211	0.246531	0.030407	0.034357
Maximum	0.181158	0.886499	21.44040	1.144430	0.115832	0.131598
Minimum	0.000000	0.000000	18.04000	-0.043913	0.009811	0.001250
Observation	63	63	63	63	63	63

Source: Eviews 12

TABLE 4. REGRESSION RESULTS

Variable	Coefficient	Std. Error	t-Statistic	Prob.
ETR	-0.003441	0.028700	-0.119887	0.9050
FZ	-0.007699	0.020092	-0.383201	0.7032
PROF	-0.058478	0.028877	-2.025086	0.0481
NDTS	-0.337732	0.294916	-1.145183	0.2575
MH	0.074521	0.236615	0.314946	0.7541
C	0.232175	0.389029	0.596806	0.5533

Source: Eviews 12

Effective Tax Rate exhibits a probability value of 0.9050 and a t-statistic of -0.119887 . Since the probability value exceeds the significance level of 0.05 ($0.9050 > 0.05$) and the absolute value of the t-statistic is lower than the critical t-value of 2.00247 ($|-0.119887| < 2.00247$), it can be concluded that **Effective Tax Rate** does not have a statistically significant effect on **Capital Structure** in oil, gas, and coal subsector firms during the 2016–2024 period. It is consistent with Yunira (2022) research, who reports that firms tend to abandon long-term debt due to high bankruptcy costs and declining in liquidity capacity, thereby weakening the influence of tax considerations on capital structure decisions.

Firm Size, the probability value is 0.7032 with a t-statistic of -0.383201 . Given that the probability value is greater than 0.05 ($0.7032 > 0.05$) and the absolute t-statistic is smaller than the critical value ($|-0.383201| < 2.00247$), **Firm Size** is not found to have a significant effect on **Capital Structure** in oil, gas, and coal subsector firms during the 2016–2024 period. This results aligns with Ali et al. (2022) research, who suggest that firms in oil, gas and coal subsector may prefer equity financing over debt despite possessing substantial reputational strength and access to money market. This indicates that firm scale alone does not necessarily determine capital structure decisions.

Profitability shows a probability value of 0.0481 and a t-statistic of -2.025086 . Since the probability value is below the 0.05 significance level ($0.0481 < 0.05$) and the absolute t-statistic exceeds the critical value ($|-2.025086| > 2.00247$), **Profitability** has a statistically significant effect on **Capital Structure** in oil, gas, and coal subsector firms during the 2016–2024 period. This findings supports the pecking order theory and is consistent with Kahya et al. (2020), who argue that firms with higher profitability prioritize internal financing over external long-term debt.

Non-Debt Tax Shields (NDTS), the probability value is 0.2575 with a t-statistic of -1.145183 . As the probability exceeds 0.05 ($0.2575 > 0.05$) and the absolute t-statistic is below the critical value ($|-1.145183| < 2.00247$), **Non-Debt Tax Shields (NDTS)** does not significantly affect **Capital Structure** in oil, gas, and coal subsector firms during the 2016–2024 period. This result is consistent with Benyamin and Soekarno (2023), who argue that firms may seek alternative mechanisms to obtain the tax benefit such as equity financing or other non-debt-related tax strategies, thereby reducing the substitutive role of depreciation-based tax incentives.

Moral Hazard records a probability value of 0.5533 and a t-statistic of 0.596806. Since the probability value is greater than 0.05 ($0.5533 > 0.05$) and the absolute t-statistic is lower than 2.00247 ($|0.596806| < 2.00247$), **Moral Hazard** does not have a statistically significant effect on **Capital Structure** in oil, gas, and coal subsector firms during the 2016–2024 period. This result is align with Saleh and Nuzleha (2024), suggesting that firms in oil, gas and coal subsector may rely on alternative financing sources to manage their working capital needs and high-risk long-term projects, rather than adjusting long-term debt ratio in response to agency related consideration.

CONCLUSION

Based on the empirical analysis conducted, this study provides evidence regarding the influence of Effective Tax Rate, Firm Size, Profitability, Non-Debt Tax Shields, and Moral Hazard on Capital Structure in energy sector firms within the oil, gas, and



coal subsector listed on the Indonesia Stock Exchange during the 2016–2024 period. The findings indicate that among the examined independent variables, only **Profitability** has a statistically significant effect on **Capital Structure**. Specifically, profitability demonstrates a negative relationship with leverage, suggesting that more profitable firms rely less on debt financing. This result supports the pecking order theory and is consistent with prior studies by Valencia and Dermawan (2024), Mardani et al. (2023), Jaworski and Czerwonka (2021), Kahya et al. (2020), Suharsono and Setiadi (2020), Saif-Alyousfi et al. (2020), dan Moradi and Paulet (2019). In contrast, **Effective Tax Rate**, **Firm Size**, **Non-Debt Tax Shields**, and **Moral Hazard** are found to have no statistically significant effect on Capital Structure. These findings align with previous research conducted by Ali et al. (2022), Yunira (2022), Benyamin and Soekarno (2023), Erwan and Dewi Kartika (2022), dan Saleh and Nuzleha (2024). This evidence suggests that tax-related incentives, firm scale, alternative tax shields, and agency-related considerations may not serve as the primary determinants of capital structure decisions in the oil, gas, and coal subsector during the observed period.

Despite its contributions, this study has several limitations. First, the research sample is restricted to firms operating in the energy sector, specifically the oil, gas, and coal subsector listed on the Indonesia Stock Exchange from 2016 to 2024. Therefore, the findings may not fully represent all publicly listed companies in Indonesia. Second, the study incorporates only five independent variables Effective Tax Rate, Firm Size, Profitability, Non-Debt Tax Shields, and Moral Hazard leaving open the possibility that other determinants may also influence Capital Structure decisions. Future research is encouraged to expand the scope of analysis by including firms from different sectors to enhance generalizability. Additionally, subsequent studies may incorporate other explanatory variables, such as Growth Investment opportunities, Board Independence, and macroeconomic factors including Inflation, in order to provide a more comprehensive understanding of both firm-specific and macroeconomic determinants of Capital Structure.

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Cite this Article: Sutantio, D., Stella (2026). *The Effect of Effective Tax Rate, Moral Hazard, and Firm-Specific Determinants on Capital Structure*. *International Journal of Current Science Research and Review*, 9(5), pp. 2780-2787. DOI: <https://doi.org/10.47191/ijcsrr/V9-i5-52>