JURNAL
Riset Akuntansi dan Keuangan Indonesia
URL : http://journals.ums.ac.id/index.php/reaksi/index

Determinants of Transfer Pricing Decisions and Its Impact on Tax Avoidance

Nico Alexander*
Accounting Department, Trisakti School of Management
*nico@stietrisakti.ac.id

Keywords:
Transfer Pricing; Tax Avoidance; Bonus Mechanism; Debt Convenant; Tunneling Incentive.

ABSTRACT
The purpose of this study was to obtain empirical evidence regarding the variables that may affect a company's decision of employing transfer pricing along with how that choice may affect tax avoidance. The variables that are used consist of the bonus mechanism, debt convenant, and tunneling incentive. The study used a two-stage regression analysis to analyze its hypotheses. 12 multinational manufacturing corporations listed between 2019 and 2021 on the Indonesia Stock Exchange represent the research sample. The purposive technique was the method used for selecting the research sample. The findings proved that the tunneling incentive has a negative impact on the decision of transfer pricing. This indicates the decision to utilize transfer pricing will be fewer depending on the percentage of foreign ownership in the business. In meanwhile, transfer pricing decisions are unaffected by bonus mechanism and debt covenants. Additionally, the findings demonstrate that tax evasion is unaffected by transfer pricing. This outcome demonstrates that there are still alternative strategies for avoiding taxes; transfer pricing has not become a significant one. The results of this study cannot be applied to other sectors within the company because it solely examines multinational manufacturing companies. Future research can use different variables or different measurements to get better results because not all of the variables used have an impact on transfer pricing or tax avoidance. The study's findings may be useful as a framework for other researchers looking into related subjects, and the results can also provide parties responsible for Indonesian taxation with more information to help them develop regulations related to transfer pricing and tax avoidance.

INTRODUCTION

For a country to operate its government, it requires a source of income. The government receives money from a variety of sources, including grants, taxes, and non-tax revenues. One of the nations where taxes are the main source of income is Indonesia. The table below, which displays the Indonesian state's revenue sources.

Table. 1. Income Source of Indonesia (in Billion Rupiah)

	2021	Percentage	2022	Percentage	2023	Percentage
Taxes Revenue	1.547.841	76%	1.924.937	79%	2.016.923	82%
Non-Tax Revenue	458.493	22%	510.929	21%	426.259	17%
Grants	5.013	2%	1.010	0,04%	409	0,02%
Total	2.011.347	100%	2.436.877	100%	2443592	100%

Source: central statistics agency (2023)

The data shown above illustrates how substantially the state of Indonesia depends on tax income. The state budget will be significantly impacted if tax revenue declines. In order to raise more money through taxes, the government keeps examining regulations. The more onerous the nation's tax laws have become the more likely it is that taxpayers will find ways to minimize their tax obligations. This is due to the fact that taxpayers still view taxes as a burden. Bothcorporate andindividual taxpayers are considered taxpayers. In Indonesia, corporations are among the biggest taxpayers. Although businesses operating in Indonesia have to comply with local laws, they also have interests beyond paying taxes, such as enhancing shareholder welfare. There will undoubtedly be disagreements between the government and the company as a consequence. Companies that receive funding from investors typically act to represent the interests of investors, increasing their welfare. One way is through engaging in tax avoidance.

Tax avoidance refers to any activity that does not violate tax laws or court cases that are used to lower the proportion of taxes paid by taking advantage of legal loopholes [1]. Investors will undoubtedly receive a higher profit as a result of this tax avoidance. Tax laws still have gaps in them even though they have been correctly implemented. Companies frequently perform in taking advantage of these opportunities to boost earnings. The country will undoubtedly suffer from this since less money will come in from taxes. The process of determining prices for related party transactions is known as transfer pricing (PER-32). Multinational corporations frequently use transfer pricing, which involves transferring income to the nation with the lowest tax rate and expenses to the nation with the highest tax rate [1]. The business can avoid paying a lot of taxes in this way. Based on prior research's findings, this study attempts to investigate the impact of transfer pricing on tax evasion again.

The findings of the research [1]–[3] demonstrate that transfer pricing affects tax avoidance. The impact on corporate tax payments increases with the magnitude of the transfer pricing action. In addition to examining how transfer pricing affects tax evasion. This study additionally examines at variables that may affect a company's choice of employing transfer pricing. This study analyzes the use of three variables—incentive tunneling, bonus mechanisms, and debt covenant—that have the empirical potential to affect transfer pricing decisions. Controlling shareholders can participate in tunneling incentives, which involve using company assets or profits for personal gain. Companies that set outrageous amounts and have special ties to majority shareholders are the ones who carry out this tunneling incentive [4]. According to [5]–[7]pricing transfer, tunneling incentive, intangible assets and profitability The purpose of this study is to analyze the effect of good corporate governance (GCG, tunneling incentives can help companies generate greater transfer pricing decisions.

Transfer pricing decisions may be influenced by bonus mechanisms. Management receives bonuses in the situation that company profits rise significantly [8]. The bonus obtained increases with the amount of profit made. Transfer pricing is one strategy for boosting profits. [8]–[10] indicates that the company's transfer pricing activities may increase as a result of the bonus mechanism. Another factor that may have an impact on the choice for utilizing transfer pricing is debt convenant. A debt covenant is a type of agreement that prevents creditors from managerial decisions that might risk the condition of the deal [11]. Transfer pricing is used by companies that frequently violate debt agreements to improve profits and avoid violating creditor agreements [12]. The findings of [11], [12] demonstrate that debt convenant can enhance transfer pricing activities.

Due to the background above, researchers are eager to reexamine transfer pricing decisions are impacted by tunneling incentives, bonus mechanisms, and debt covenants, as well as how these factors relate to tax avoidance. By using variables that have been used in the past research, the 2-stage regression method as the novelty to this research. The question being examined in this study is to determine if debt covenants, bonus mechanism, and tunneling incentives affect the decision to use transfer pricing, as well as how transfer pricing affects tax avoidance. Tax regulators can use the information from this study to inform the creation of tax policies.

Agency Theory

A particular theory developed by [13] is agency theory. According to this theory, the management of the company (agents) and stakeholders (principals) have conflicting goals. The management has the power to run the company as a result to this principle. However, management occasionally abuses their power for their own gain. There are two different kinds of conflicts that can arise: a conflict of interest between management and stakeholders, and a conflict between minority and majority shareholders. There are two forms of conflicts of interest in this research: one is tax avoidance, which involves a conflict between the government and the company, and the other is transfer pricing, which may involve a conflict between the majority and minority parties.

Tunneling Incentive and Transfer Pricing

Controlling shareholders may engage in tunneling incentives, which involve transferring profits and assets for the controller's personal benefit while minority shareholders bear the cost [8], [14]. The related party of the company's controlling party allows for the transfer of profits or assets. Tunneling incentives are closely associated with multinational corporations [9]. The ease with which corporations can implement tunneling incentives has led to a greater frequency of transfer pricing actions by these multinational corporations. They transfer profits to low-tax nations from nations with high tax rates. Transfer pricing may be influenced by tunneling incentives. Multinational corporations can use related parties that operate across multiple nations to gain an advantage by implementing transfer pricing through tunneling incentives. The transfer pricing action will rise in proportion to the current tunneling incentive [10], [14], [15]. There is a conflict of interest between controllers and minority shareholders in regards to agency theory. Minority shareholders are going to lose out when the controlling party utilizes its influence to impose transfer pricing through incentive tunneling. Based on explanation above, the hypothesis was:

H1: Tunneling Incentive has positive effect on Transfer Pricing

Bonus Mechanism and Transfer Pricing

Management that meets stakeholder expectations and company targets is rewarded with bonuses [8]. The company's management is engaging in transfer pricing in an attempt to increase profits, which will be converted into larger bonuses for them when their performance improves [9], [10], [16]. A conflict arises between stakeholders and management as a consequence of this bonus. Any management that is motivated to increase their bonuses will make every effort to raise the company's performance. Based on explanation above, the hypothesis was:

H2: Bonus Mechanism has positive effect on Transfer Pricing

Debt Convenant and Transfer Pricing

A debt covenant is an agreement between a creditor and a debtor that prohibits the debtor from taking any actions that might lead to the debtor's payment failure [4]. Debt covenants protects creditors from acts that would prevent them from getting their interests met [17]. Transfer pricing will be used by the business to boost earnings and support the interests of its creditors, namely the ability to make debt payments [11], [12], [16]. In line with agency theory, management of the company will act in a way that favors creditors over the interests of minority shareholders. Based on

p-ISSN:1411-6510
e-ISSN :2541-6111

explanation above, the hypothesis was:
H3: Debt Convenant has positive effect on Transfer Pricing

Transfer Pricing and Tax Avoidance

Transfer pricing is the price for transactions with parties to which a special relationship exists, as defined by the Director General of Taxes Regulation PER-32/PJ/2011. Multinational corporations frequently use transfer pricing by shifting earnings to countries with low tax rates. and transferring expenses to countries with high tax rates [1]. This happens in international tax transfer pricing because different countries have different tax rates. By using transfer pricing, the business directly saves money on taxes. The company should turn a profit in the nation in which it conducts business, but these profits are moved to another nation in order to avoid paying taxes in the nation in which the company conducts business. The results of [1], [18]–[20] show that a company's tax avoidance increases with the amount of transfer pricing activity. It is evident in relation to agency theory that corporate management disadvantages the government, which serves as the principal. Based on explanation above, the hypothesis was:
H4: Transfer Pricing increase corporate Tax Avoidance

In accordance with the previously hypotheses and explanations the conceptual framework of this research is:

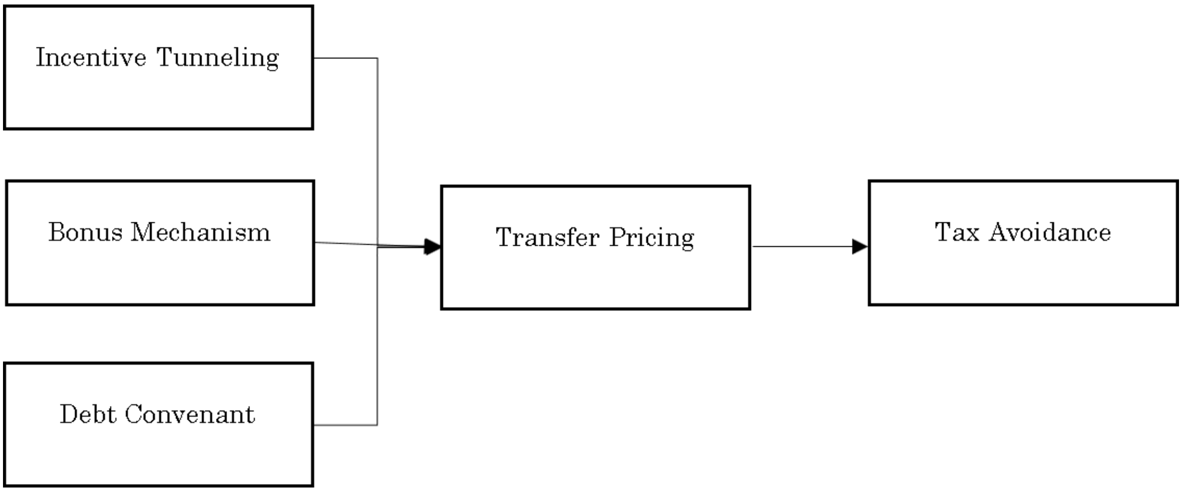

Figure 1. Research Framework

RESEARCH METHOD

Multinational manufacturing companies listed on the Indonesia Stock Exchange within 2019 to 2021 included the research sample used in this study. Purposive sampling was used to choose the sample based on a number of considerations, such as foreign ownership of at least 20%, financial reports ending on December 31, ETR between 0-1 and multinational manufacturing companies listed on the Indonesian stock exchange during the research period. A total of 12 companies fit the requirements to serve as research samples. 2-Stage regression is used to test the hypothesis. The research model can be described as follows:

TP = b0 + b1 TI + b2 BM + b3 Debt + e
TA = b0 + b1 TP
TP = Transfer Pricing
TI = Tunneling Incentive
BM = Bonus Mechanism
Debt = Debt Convenant
TA = Tax Avoidance

Table below show definition operation of each variable

Table 2. Definition Variable

No	Variable	Measurement
1	Transfer Pricing	$TP = \frac{Related\ Party\ Receivable}{Total\ Receivable}$
2	Tax Avoidance	$ETR = \frac{Tax\ Expense}{Income\ Before\ Tax}$
3	Tunneling Incentive	$TI = \frac{Foreign\ Ownership}{Total\ Share\ Outstanding}$
4	Bonus Mechanism	$BM = \frac{Net\ Income\ t}{Net\ Income\ t-1}$
5	Debt Convenant	$Debt = \frac{Total\ Liabilities}{Total\ Equity}$

RESULTS AND DISCUSSION

The following are descriptive statistical results and hypothesis testing results

Table 3. descriptive statistic

Variable	Minimum	Maximum	Mean	Standard Deviation
TP	0.002191	0.981999	0.171636	0.276818
TA	0.046195	0.814617	0.248869	0.122988
TI	0.207870	0.921300	0.510343	0.204346
BM	0.105407	10.87860	1.711080	2.397864
Debt	1.658416	0.200495	0.822935	0.367885

The descriptive table above shows that the average foreign ownership of multinational companies in Indonesia is 51%, which shows that the controllers of multinational companies in Indonesia are foreign companies. and the average tax rate imposed on companies in Indonesia is 24%.

Table 4. Hypothesis Result

	Coefficient	Sig
TI → TP	0.459125	0.0421*
BM → TP	0.175225	0.1563
Debt→ TP	0.028451	0.1293
TP → TA	-0.037221	0.6323

Tunneling incentives have an effect on transfer pricing decisions, according to hypothesis testing results, with a significance value of 0.0421 and a coefficient value of 0.4592. This demonstrates how transfer pricing activities can rise when tunneling incentives are measured based on foreign ownership. This is because corporate controllers want to shift profits to countries with lower tax rates in order to increase profits. Naturally, this will have a negative impact on the nation in which the business is located. These findings are according to [10], [14], [15]. It argues that transfer pricing decisions will increase as a result of tunneling incentives. Transfer pricing decisions are not influenced by the bonus mechanism as well as debt covenant variables.

Transfer pricing has no effect on tax avoidance, according to the results of the second test. This demonstrates that transfer pricing is not yet a popular strategy for tax evasion in Indonesia. In Indonesia, very strict tax laws prevent this transfer pricing from leading to a large amount of tax avoidance. In addition, the volume of transactions with related parties is still small when compared to transactions with third parties, which account for 17% of the total. These findings have been proven by [2], [3], [21]

CONCLUSION

The objective of this research is to obtain evidence of how debt covenants, bonus mechanism, and tunneling incentives affect transfer pricing decisions and how it affect tax avoidance. Tunneling incentives are found to have an impact on transfer pricing actions, according to research conducted with a sample of 12 multinational companies that are listed on the Indonesian stock exchange. This is because the transfer pricing can be done because the controlling company is a foreign entity that owns businesses in multiple nations. Meanwhile, transfer pricing decisions are unaffected by debt covenants and bonus systems. Furthermore highlighting that transfer pricing has no impact on tax avoidance. This study only considers a few variables that may affect transfer pricing, and it only looks at transfer pricing as a potential source of tax avoidance. Since only multinational corporations were included in the sample, it cannot be applied to all businesses. For further research, we can add other factors that can influence transfer pricing and can use other schemes in determining factors that cause tax avoidance. The research sample can be supplemented with other sectors so that it can be generalized to all company sectors

REFERENCE

[1] C. F. Syawalina, Irmawati, dan R. Julia, "Pengaruh Transfer Pricing Terhadap Penghindaran Pajak Pada Perusahaan Manufaktur Sub Sektor Farmasi yang Terdaftar di Bursa Efel Indonesia Periode (2018-2020)," *J. Akunt. Muhammadiyah*, vol. 12, no. 1, pp. 67–78, 2022.

[2] H. Hartono, Sabaruddin, and A. Priharta, "Pengaruh Profitabilitas, Kepemilikan Keluarga dan Transfer Pricing Terhadap Penghindaran Pajak Dimediasi Oleh Good Corporate Governance," *JRB-Jurnal Ris. Bisnis*, vol. 6, no. 1, pp. 18–40, 2022, doi: 10.35814/jrb.v6i1.3994.

[3] P. A. Panjalusman, E. Nugraha, and A. Setiawan, "Pengaruh Transfer Pricing Terhadap Penghindaran Pajak," *J. Pendidik. Akunt. Keuang.*, vol. 6, no. 2, p. 105, 2018, doi: 10.17509/jpak.v6i2.15916.

[4] S. P. L. . Sintia, "Determinan Perusahaan Melakukan Transfer Pricing dengan di Moderasi Ukuran Perusahaan (Perusahaan Energy 2017-2021)," *J. Ekon. Akuntansi, Manaj.*, vol. 2, no. 2, pp. 91–107, 2023.

[5] M. Komarudin and G. C. Dewi, "Empirical Study of Tranfer Pricing on Consumption Companies on the Indonesia Stock Exchange," *J. Ekon.*, vol. 11, no. 01, pp. 359–365, 2022, [Online]. Available: http://ejournal.seaninstitute.or.id/index.php/Ekonomi

[6] C. S. Azzura and A. Pratama, "Influence of Taxes, Exchange Rate, Profitability, and Tunneling Incentive on Company Decisions of Transferring Pricing," *J. Akunt. Berkelanjutan Indones.*, vol. 2, no. 1, p. 123, 2019, doi: 10.32493/jabi.v2i1.y2019.p123-133.

[7] I. K. Sujana, I. M. S. Suardikha, and G. A. R. S. Saraswati, "Tax, Bonus Mechanism, Tunneling Incentive, Debt Covenant and Transfer Pricing in Multinational Companies," *Matrik J. Manajemen, Strateg. Bisnis dan Kewirausahaan*, p. 63, 2022, doi: 10.24843/matrik:jmbk.2022.v16.i01.p05.

[8] N. Rahmawati dan S. D. Mulyani, "Pengaruh Mekanisme Bonus Dan Tunneling Incentive terhadap Praktik transfer Pricing, Dimoderasi Tax Avoidance," *Pros. Semin. Nas. Pakar*, pp. 1–7, 2020, doi: 10.25105/pakar.v0i0.6824.

[9] I. Cristina and T. Murtiningtyas, "ANALISIS PAJAK, TUNNELING INCENTIVE, DAN MEKANISME BONUS TERHADAP KEPUTUSAN TRANSFER PRICING," *J. Adm. dan Bisnis*, vol. 15, no. 1, pp. 16–21, 2021.

[10] A. Syuheri, J. Syahputra, M. Harahap, and P. Herman, "Penerapan Mekanisme Bonus dan Tunneling Incentive Terhadap Transfer Pricing Perusahaan," *BULLET J. Multidisiplin Ilmu*, vol. 2, no. 2, pp. 403–408, 2023.

[11] D. A. M. Sari dan C. Djohar, "Pengaruh Profitabilitas, Debt Covenant Dan Mekanisme Bonus Terhadap Transfer Pricing," *Yudishtira J. Indones. J. Financ. Strateg. Insid.*, vol. 2, no. 2, pp. 227–243, 2022, doi: 10.53363/yud.v2i2.38.

[12] M. Pondrinal, Y. P. Sari, and D. A. Putri, "Company Size, Leverage, Bonus Mechanism and Tax Planning On Transfer Pricing With Profitabilias As Moderating Variables," *J. Pajak dan Bisnis*, vol. 4, no. 1, pp. 160–170, 2023.

[13] Jensen;Meckling, "Racial diversity and its asymmetry within and across hierarchical levels: The effects on financial performance," *Hum. Relations*, vol. 72, no. 10, pp. 1671–1696, 1976, doi: 10.1177/0018726718812602.

[14] F. Setyorini dan I. Nurhayati, "Pengaruh Pajak (Etr), Tunneling Incentive (Tnc), Mekanisme Bonus (Itrendlb) Dan Firm Size (Size) Terhadap Keputusan Transfer Pricing," *JIMAT (Jurnal Ilm. Mhs. Akuntansi)*, vol. 13, pp. 233–242, 2022.

[15] H. E. Jafri dan E. Mustikasari, "Pengaruh Perencaan Pajak, Tunnneling Incentive dan Aset Tidak Berwujud Terhadap Perilaku Transfer Pricing pada Perusahaan Manufaktur yang Memiliki Hubungan Istimewa yang Terdaftar di Bursa Efek Indonesia Periode 2014-2016," *Berk. Akunt. dan Keuang.*

Indones., vol. 3, no. 2, p. 63, 2018, doi: 10.20473/baki.v3i2.9969.

[16] D. Rosmawati and W. Ginting, "Pengaruh Effective Tax Rate, Bonus Mechanism, Debt To Equity Ratio, Dan Exchange Rate Terhadap Keputusan Transfer Pricing," *Acman Account. Manag. J.*, vol. 2, no. 1, pp. 51–65, 2022, doi: 10.55208/aj.v2i1.32.

[17] G. Arfananda, A. Marundha, dan U. Khasanah, "Mekanisme Bonus, Ukuran Perusahaan, Debt Covenant Dan Transfer Pricing Pada Perusahaan Manufaktur Yang Terdaftar Di Bursa Efek Indonesia Pada Tahun 2018-2022," *J. Ekon. Manajemen, dan Akunt.*, vol. 2, no. 3, 2023, [Online]. Available: http://jurnal.anfa.co.id/index.php/mufakat

[18] A. A. Al Hasyim, N. I. Inayati, A. Kusbandiyah, dan T. Pandansari, "Pengaruh Transfer Pricing, Kepemilikan Asing, Dan Intensitas Modal Terhadap Penghindaran Pajak," *J. Akunt. dan Pajak*, vol. 23, no. 02, pp. 1–12, 2022.

[19] J. Jarkoni dan J. Juniyati, "Pengaruh Transfer Pricing dan Debt Convenant Terhadap Keputusan Penghindaran Pajak Penghasilan Badan pada Perusahaan Manufaktur yang Terdaftar di BEI (2015-2020)," *J. Ekon. dan Bisnis*, vol. 3, no. 1, pp. 30–38, 2023, doi: 10.56145/ekonomibisnis.v3i1.52.

[20] M. Komarudin, H. Gursida, and Y. Indrayono, "The Effect of Transfer Pricing On Taxes Is Reviewed From Its Relationship With Tunneling Incentives, Intangible Assets, Leverage, And Profitability," *Asian J. Manag. Entrep. Soc. Sci.*, vol. 02, no. 04, pp. 305–322, 2022, [Online]. Available: https://ajmesc.com/index.php/ajmesc

[21] J. Sutanto dan H. F. A. T. Lasar, "Pengaruh Transfer Pricing dan Karakteristik Perusahaan terhadap Penghindaran Pajak," *Media Bisnis*, vol. 15, no. 2, pp. 169–180, 2023.