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The Effect of Profitability, Company Size, and Tunneling Incentive on Tax Avoidance with Transfer Pricing as a Moderating Variable

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ABSTRACT

Tax avoidance is one of the ways carried out by taxpayers as an effort to reduce the burden of taxes paid legally by utilizing *the gray area of* taxes. However, in 2020 state losses reached Rp. 68.7 trillion due to tax avoidance. This study aims to examine the effect of profitability, company size, and tunneling incentives on tax avoidance with *transfer pricing* as a moderation. The research population is manufacturing companies listed on the IDX in 2019-2021. The research sample was 29 companies, selected using the purposive sampling method. This research is a quantitative study using Moderated Regression Analysis (MRA). The results of this study show that profitability, *tunneling incentives* and *transfer pricing* have a positive effect on tax avoidance. The size of the company has no effect on tax avoidance. *Transfer pricing* has been shown to moderate the effect of profitability and company size on tax avoidance, while in the *tunneling incentive* variable, *transfer pricing* has not been shown to moderate the effect of the tunnelling incentive variable on tax avoidance.

Keywords: Company Size, Profitability, Tunneling Incentives, Transfer Pricing, Tax Avoidance

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INTRODUCTION

Tax avoidance is an effort made by companies to avoid the nominal tax paid by utilizing the weaknesses of tax regulations or gray areas in the provisions of tax laws so as to reduce the tax burden owed (Wardana & Asalam, 2022). Although tax avoidance is an act that is considered legal and only by taking advantage of loopholes from the weaknesses of legislation, however, tax avoidance can result in reduced state revenues, especially in the tax sector, resulting in losses for the countrya (Gunawan & Surjandari, 2022). Based on the theory of stakeholders, where the government in this case the Directorate General of Taxes (DGT) is one of the company's stakeholders. Therefore, companies must also pay attention to the interests of the government, one of which is by following all regulations made by the government such as compliance with paying taxes and not doing tax avoidance that can harm the state (Fitri & Pratiwi, 2021).

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According to the Tax Justice Network report, Indonesia is estimated to face a loss of US$ 4.86 billion per year or equivalent to Rp 68.7 trillion due to tax avoidance. This is done in order not to report the actual amount of profit from the country in which the company is located. Therefore, businesses engaged in this practice end up paying less tax than they should (Fatimmah, 2020). A case of tax evasion was once carried out by PT. Adaro Energy Tbk, in 2019 conducted tax avoidance with a transfer pricing scheme through its Singapore subsidiary Coaltrade services international Pte Ltd. PT Adaro energy tbk allegedly carry out transfer pricing practices to avoid domestic tax obligations so as to provide higher income for company shareholders. Indications of misuse of *transfer pricing* carried out by the company are identified in the financial statements containing transactions that are considered unreasonable, which shows an inequality in transfer prices when compared to the global coal market price in at that time (Narsa, 2022).

Based on the results of literature observations, profitability is one of the factors causing tax avoidance. Profitability is one way to measure a company's ability to make a profit during a certain period which is proxied by Return on Asset or ROA (Sanjaya & Rizky, 2016). Agency theory encourages agents to increase company profits. When the profit generated by the company increases, then the amount of tax will increase in line with the increase in profit (Felix & Jamaludin, 2020). Research conducted by Anggraeni and Oktaviani (2021) states that profitability has a positive effect on tax avoidance. The more efficient a company is, the less tax paid will be so that the company's effective tax rate becomes lower. However, this research contradicts the research conducted by Robin et al. (2021) in their research shows that profitability has a negative effect on tax avoidance.

The size of the company is also a factor that affects tax avoidance activities. This is illustrated by the larger the company, the greater the resources owned by the company, in the hope of managing taxes well. According to Munandar et al. (2016) large or small companies can be classified according to various ways, including: total assets, log size, sales and market capitalization and others. Tax avoidance practices in Indonesia involve many relatively large multinational companies. Several major cases of tax evasion have been carried out by the Directorate General of Taxes (DGT), including the case of agricultural and mining companies. This fact indicates an aggressive relationship between tax avoidance and multinational corporations, most of which have great corporate value (Rusydi, 2013). Research conducted by Fauzan et al. (2019), Suripto and Novitaria (2021) said that the size of the company has a positive effect on tax avoidance The larger the size of the company, the more complex the transaction. Thus allowing companies to take advantage of existing gaps to take higher tax avoidance measures, whereas according to Wulandari and Maqsudi (2019) the size of the company has no effect on tax avoidance this means that the company is unable to utilize all assets owned for the company's operational activities.

Tunneling incentives are also a factor in a company doing tax avoidance. Tunneling incentive is a behavior of majority shareholders who transfer company assets and profits for their own benefit, but minority shareholders also bear the costs they incur (Rahmawati & Mulyani, 2020). Therefore, if tunneling activities are increasingly carried out, tax avoidance activities will also increase. This opinion is supported by research from Lestari and Solikhah (2019) which states that tunneling incentives have an effect on tax avoidance, but the opposite is conveyed by Sari and Hermawan, (2021) where in their research it is stated that tunneling incentives have no effect on tax avoidance. Transfer pricing is a company policy in determining the price of a transaction between parties who have a special relationship (Melmusi, 2018). Transfer pricing is an interesting issue and has received attention from tax authorities in various countries due to the shift in profits from the tax sector (Rusydi, 2013). Many companies use transfer pricing as a strategy to reduce their taxes. In addition, making sales at a price below the market price will make the company appear to lose by maximizing expenses and ultimately resulting in reduced revenue. This can ultimately reduce the tax allowance that should be imposed (Lestari & Solikhah, 2019). This is in line with research conducted by Fitri and Pratiwi, 2021) which states that transfer pricing has a positive effect on tax avoidance. Transfer pricing is one of the most important issues in international taxation (Rejeki et al., 2019), the transfer

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pricing variable is suspected to be able to strengthen the reasons for a company in avoiding taxes. Profitability, company size and Tunneling incentives affect transfer pricing (Marfuah & Azizah, 2014; Sari, 2021; Sari et al., 2021), because the higher the company's profit or the larger the size of the company, the more likely the company will be to carry out transfer pricing transactions to reduce the high tax burden. Likewise with tunneling incentives, companies that have relationships with related parties will have the convenience of tunneling incentives. The practice of transferring assets or profits carried out by the manager of a company due to encouragement from the majority shareholder is a major trigger for transfer pricing. This condition is an effort to avoid taxes, namely through manipulation of the tax burden paid by the company.

Based on the description above, there are many factors that affect a company in carrying out tax avoidance, but based on the results of previous research there is a research gap where the influence of profitability variables, firm size and tunneling incentives on tax avoidance still shows different results and tends to be inconsistent. The research conducted earlier by Rejeki et al. (2019) which examined the influence of institutional ownership, managerial ownership and the proportion of the board of commissioners on tax avoidance and transfers pricing as a moderation variable. Based on the research carried out only variables proportion board of commissioners which have a positive effect on tax avoidance, while institutional ownership and managerial ownership have no effect positive to tax avoidance, in addition, transfer pricing has not been shown to moderate the institutional ownership of managerial and proposed by the board of commissioners on tax avoidance. Therefore, researchers want to re-examine the moderation variables, namely transfer pricing in relation to the influence of profitability, company size and tunneling incentives on tax avoidance.

METHODS

This research uses a quantitative approach with a type of causality research, where this type of research aims to test the influence of independent variables on dependent variables. The population in this study is a manufacturing company listed on the IDX in 2009-2021. The data collection method used is purposive sampling. The sample used must meet the predefined criteria, as shown in Table 1. The number of samples in this study was 29 companies during the 3 research periods. The type of data used in this study is secondary data in the form of financial statements and annual reports obtained from the www.idx.co.id page.

Table 1. Sample Selection

Criterion	Sum
Manufacturing Sector Companies listed on the Indonesia Stock Exchange in 2019-2021	193
Sample companies whose data is not available are complete according to the required information	(13)
Number of manufacturing sector companies that suffered losses during the research period	(69)
The number of manufacturing sector companies that do not have a percentage of foreign ownership is at least 25%	(82)
Number of companies sampled for research	(29)
Research Period (years)	X3
Total Research Sample	87

Source: Data processed (2022)

The dependent variables in this study are tax avoidance, while the independent variables in this study are profitability, company size, and tunneling incentives, in addition to that in the study it also uses a moderation variable transfer pricing. The tax avoidance variable in this study was measured using the Cash Effective Tax Rate (CETR) ratio, namely the tax burden divided by profit before tax, this

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is due to the CETR ratio is considered to be able to know or identify whether a company is minimizing taxes through cash issued to pay the tax burden owed (Sujannah, 2021).

Profitability is a financial ratio used to measure the effectiveness or ability of a company to obtain a profit on the assets it owns (Cahyadi & Suganda, 2021). Profitability in this study is measured by the Return On Assets (ROA) ratio, namely by comparing net profit with total assets owned by the company (Anggraeni & Oktaviani, 2021). Company size is a scale of company classification that is grouped in categories, namely large, medium and large scales (Wulandari & Maqsudi, 2019). In this study, the size of the company was proxied by natural logs multiplied by the company's total assets. Tunneling incentive is the behavior of the majority shareholder who moves assets or profits out of the company for the benefit of the majority shareholder (Suripto & Novitaria, 2021), in this study tunneling incentive is proxied by share ownership by foreign companies above 25% as a controlling company divided by the total shares outstanding (Marfuah & Azizah, 2014; Rahayu et al., 2020). Transfer pricing is a policy of pricing transfers for transactions with parties who have a special relationship in the form of goods, services, or intangible assets. Transfer pricing is measured using the Related party transaction formula, which compares the amount of receivables of related parties with total receivables (Refgia, 2017).

RESULTS AND DISCUSSION

Descriptive statistical tests showed a general understanding of the samples used in the study. This study uses five variables, namely profitability, company size, tunneling incentives, transfer pricing, and tax avoidance. Data were obtained from 29 companies observed during the years 2019 to 2021. The description of the research variables is presented based on the average value, standard deviation, lowest value, and highest value with the following results:

Table 2. Descriptive Satistic Test

No.	Variable	N	Minimum	Maximum	Mean	Std Deviation
1	Profitability	87	0.003	0.158	0.08299	0.037711
2	Firm Size	87	26,002	31,869	28.85109	1.635724
3	Tunneling incentives	87	0.052	0.895	0.38534	0.181690
4	Transfer pricing	87	0.001	1,040	0.39918	0.389665
5	Tax Avoidance	87	0.106	0.371	0.23666	0.061657

Source: Data processed (2022)

Table 2 shows the results of descriptive statistical calculations of variable N as many as 87 in the period 3 years 2019-2021, it can be explained as follows: (1) mean in the profitability variable which is 0.8299, while the standard deviation value is 0.37711, it can be said that the average ROA value is 8.3%, which means that the sample company has made good use of its assets; (2) mean in variable firm size which is 28.85109, while the standard deviation value is 1.635724, it can be said that the average sample company is a company with a large scale or with an average total assets of Rp.1 trillion; (3) mean in the variable tunneling incentive is 0.38534, while the standard deviation value is 0.181690, it can be said that the average sample company has a foreign shareholding of 38%; (4) mean value in variable transfer pricing is 0.39918, while the standard deviation value is 0.389665, it can be said that the average sample company makes transactions with related parties by 39%. (5) mean value in the variable tax avoidance is 0.23666, while the standard deviation value is 0.061657, it can be said that the average sample company, pays a tax burden of 23% of the total profit earned.

Before testing linear regression analysis of research hypotheses, it is necessary to first test the classical assumptions of the data to be processed. The purpose of fulfilling this classical assumption is intended so that the free variable as an estimator over the bound variable becomes unbiased. The

classical assumption tests used include normality tests, heteroskedasticity tests, multicollinearity tests, and autocorrelation tests.

Table 3. Normality Test Results & Autocorrelation Test

No.	Equation	Residual Standards		Durbin-Watson
		Kolmogorov-Smirnov Z	Asymp. Sig. (2-tailed)	
1	CETR = α + β1ROA + β2Size + β3TI + ε	0,075	0,200	1,948
2	CETR = α + β1ROA + β2Size + β3TI + β4TP + ε	0,86	0,161	1,908
3	CETR = α + β1ROA + β2Size + β3TI + β4TP + β1ROA*TP + β2Size *TP+ β3TI *TP + ε	0,055	0,200	2,177

Source: Data processed (2022)

Table 3 shows the results of normality tests with a one-sample of Kolmogorov-smirnov, obtained the significance value of Kolmogorov Smirnov Z (2-tailed) on all equations which is greater than 0.05 (p > 0.05) or by 0.200, 0.161 and 0.200, which means that the data have been distributed normally. The results of the autocorrelation assumption test with the Durbin-Watson test from 3 equations obtained DW values of 1.948, 1.908, 2.177. For comparison, a dU value of 1.749 and a 4-dU value of 2.251 were obtained. The results show that the DW value is within the range of dU values and the value of 4-dU (dU < DW < 4-dU) means that no autocorrelation problems were found so that the autocorrelation assumption was met.

Table 4. Multicollinearity Test Results & Heteroscedasticity Test

No.	Equation	Variable	Tolerance	VIF	Sig.
1.	CETR = α + β1ROA + β2Size + β3TI + ε	Profitability	0.865	1,156	0.717
		Firm Size	0.918	1,090	0.507
		Tunneling incentives	0.920	1,087	0.548
2.	CETR = α + β1ROA + β2Size + β3TI + β4TP + ε	Profitability	0.859	1,164	0.565
		Firm Size	0.810	1,235	0.723
		Tunneling incentives	0.875	1,143	0.630
		transfer pricing	0.850	1,177	0.997
3.	CETR = α + β1ROA + β2Size + β3TI + β4TP + β1ROA*TP + β2Size *TP+ β3TI *TP + ε	Profitability	0.842	1,188	0.608
		Firm Size	0.698	1,432	0.324
		Tunneling incentives	0.775	1,290	0.968
		transfer pricing	0.710	1,409	0.103
		Profitability*Transfer pricing	0.866	1,155	0.298
		Firm Size*Transfer pricing	0.763	1,310	0.927
		Tunneling incentive*Transfer pricing	0.839	1,192	0.080

Source: Data processed (2022)

Table 4 is the results of the multicollinearity test and the heteroskedasticity test. The results of the multicollinearity test using the VIF test obtained the VIF value of each free variable on the three equations less than 10 (VIF < 10) meaning that no multicollinearity problem was found in the model so that the assumption of multicollinearity was met. Based on the glejser test in Table 4, it can also be seen that the significant value in the independent variable in each equation has a sig. value of > 0.05, it can be said that in this study there was no heteroskedasticity.

Moderation regression analysis aims to obtain an idea of the influence between free variables on bound variables in the presence of moderation variables both as a whole (simultaneously) and individually (partially). The following are presented the results of the regression of moderation

between profitability, company size, and tunneling incentives towards tax avoidance and transfer pricing moderation.

Table 5. MRA Test Results, Coefficient of Determination and Hypothesis of Sig the Simultan

No.	Type	R Square	Adjusted R Square	F	Sig.
1	CETR = α + β1ROA + β2Size + β3TI + ε	0,252	0,225	9,302	0,000
2	CETR = α + β1ROA + β2Size + β3TI + β4TP + ε	0,256	0,219	7,039	0,000
3	CETR = α + β1ROA + β2Size + β3TI + β4TP + β1ROA*TP + β2Size *TP+ β3TI *TP + ε	0,438	0,388	8,779	0,000

Source: Data processed (2022)

Based on the data shown in table 5, it can be seen that the value of R square after the existence of variable moderation (transfer pricing) in the second and third equations, the value of R square increases from 25.2% to 25.6% in equations 1 and 2. Then from 25.2% to 43.8% in equations 1 and 3. Thus, it can be concluded that the existence of transfer pricing as a moderation variable strengthens the influence of profitability, firm size, and tunneling incentives on tax avoidance variables.

The results of the Uji hypothesis simultaneously (Test F) which can be seen in table 5, show the results in the first equation which are 0.00 < 0.05 and F count 9.302 > 2.479 F table. In the second safe it yields a significant value of 0.00 < 0.05 and F counts 7,039 > 2,479 F of the table. And in the third equation it produces a significant value of 0.00 < 0.05 and F counts 8,779 > 2,479 F of the table. If a significant value < 0.05 and the value of F counts > in the F table then H1 is accepted and H0 is rejected as well as possible. So from the test results above, it can be concluded that the three regression equations have a simultaneous effect on the tax avoidance variable (Y) so that H1 is received.

The adjusted value of R square in the first regression equation is 0.225 so it can be said that the variable profitability, firm size and tunneling incentive affects the variable tax avoidance by 22.5%, and the remaining 77.5% is influenced by other variables that were not tested in this study. Firm size, tunneling incentives and transfer pricing affected the variable tax avoidance by 21.9%, and the remaining 78.1% was influenced by other variables that were not tested in this study. The value of R square in the third regression equation is 0.388 so it can be said that the variables of profitability, firm size, tunneling incentive, transfer pricing, as well as profitability, firm size, and tunneling incentives against tax avoidance with transfer pricing moderation have an effect of 38.8%, and the remaining 61.2% is influenced by other variables that were not tested in this study.

The t-test (hypothesis test) basically shows how far the influence of one independent variable individually (partially) in explaining the variation of the dependent variable. The step used as the basis for decision making, the first by looking at the signification value (sig.) and the second comparing between the calculated t value with the t table. The level of significance used is 5% or (α) = 0.05

Table 6 Hypothesis Test Results (t Test)

Type	Hypothesis	Independent Variables	Sign expansion	B	Beta	T	Sig.	Decision against Ho
CETR = α + β1ROA + β2Size + β3TI + ε	1	Profitability	+	0.461	0.282	2.762	0.007**	Rejected
	2	Firm Size	+	0.007	0.194	1.959	0.053**	Accepted
	3	Tunneling incentives	+	0.079	0.234	2.365	0.020**	Rejected
		Profitability	+	0.452	0.276	2.688	0.009**	Rejected

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CETR = α + β1ROA + β2Size + β3TI + β4TP + ε	4	Firm Size	+	0.008	0.218	2.061	0.042**	Rejected
		Tunneling incentives	+	0.074	0.219	2.151	0.034**	Rejected
		Transfer pricing	+	0.011	0.069	2.663	0.409**	Rejected
CETR = α + β1ROA + β2Size + β3TI + β4TP + β1ROA*TP + β2Size *TP+ β3TI *TP + ε		Profitability	+	0.399	0.244	2.656	0.010**	Rejected
		Firm Size	+	0.011	0.287	2.843	0.006**	Rejected
		Tunneling incentives	+	0.033	0.098	1.026	0.308**	Accepted
		Transfer pricing	+	0.026	0.162	1.617	0.110**	Accepted
	5	ROA*TP	+	0.931	0.192	2112	0.038**	Rejected
	6	Size*TP	+	0.039	0.379	3.927	0.000**	Rejected
	7	TI*TP	+	-0.16	-0.153	-1.663	0.100**	Accepted

Dependent variable: Tax Avoidance
Source: Data processed (2022)

Based on the results of the hypothesis test in table 6, it can be seen that the calculated t value in the profitability variable is 2.762 and a significant value of 0.007. Value t calculate > t Table which is 2.762 > 1.989, and a significant value of 0.007 < 0.05, then it can be said that Ha is accepted and Ho is rejected. This means that the first hypothesis is accepted, then there is a significant positive influence between profitability and tax avoidance. The calculated value of t in the variable size of the company is 1.959 and the significant value is 0.053. The value of t calculate < t table which is 1.959 < 1.989, and the significant value is 0.053 > 0.05, then it can be said that Ha is rejected and Ha is accepted. Therefore, the second hypothesis that states that the size of the company has a positive effect on tax avoidance is not proven or rejected. The calculated t value on the tunneling incentive variable is 2.365 and the significant value is 0.020, t calculate > t table which is 2.365 > 1.989, and the significant value is 0.020 < 0.05, then it can be said that Ha is accepted and Ho is rejected. Which means the third hypothesis is accepted, then there is a significant positive influence between tunneling incentives on tax avoidance. The calculated value of t in the transfer pricing variable is 2.663 and the significant value is 0.0409, t calculate > t table which is 2.663 > 1.989, and a significant value of 0.0409 < 0.05, then it can be said that Ha is accepted and Ho is rejected. Which means that the fourth hypothesis is accepted, then there is a significant positive influence between transfer pricing and tax avoidance. The value of t counts on the profitability variable with the interaction of transfer pricing is 2.112 and a significant value of 0.038. t calculate > t table which is 2.762 > 1.989, and a significant value of 0.038 < 0.05, then it can be said that Ha is accepted and Ho is rejected. Which means that the fifth hypothesis is accepted, then there is a significant positive influence between profitability on tax avoidance of 0.000. t count > tTable which is 3.927 > 1.989, and a significant value of 0.000 < 0.05, then it can be said that Ha is accepted and Ho is rejected. Which means the sixth hypothesis is accepted, then there is a significant positive influence between the size of the company on tax avoidance. The calculated value on the tunneling incentive variable with the interaction of transfer pricing is -1663 and a significant value of 0.100. t Calculate < t Table which is -1.663 < 1.989, and a significant value of 0.100 > 0.05, then it can be said that Ho is accepted and Ha is rejected, yang means that the results of hypothesis testing in this study state that transfer pricing does not moderate the influence of the influence of Tunneling incentives against tax avoidance.

CONCLUSION

This study aims to determine the relationship between profitability, company size, tunneling incentives to tax avoidance and transfer pricing as a moderation variable. The research sample is a number of manufacture companies listed on the Indonesia Stock Exchange in 2019-2022. These findings prove that profitability affects tax evasion, agency theory spur agents to increase company

profits. When the profit obtained by the company is enlarged, the amount of income tax will increase according to the increase in the company's profit, the higher the probability of the company to carry out tax avoidance. The size of the company does not affect tax avoidance, based on these results it can be interpreted that companies that have a large size do not necessarily take tax avoidance actions. Likewise, companies that are small in size do not necessarily take tax avoidance actions. The size of the company is not an indicator in carrying out tax avoidance actions, so by looking at the assets owned by the company, it has not been able to encourage the company to take tax avoidance actions. Tunneling incentives affect tax avoidance, the conflict between the majority shareholder and the minority shareholder causes the company to easily carry out actions that tend to be negative such as doing tax avoidance. This effort is carried out by moving the assets or profits owned by the company so that the resulting profit becomes lower. Transfer pricing has a positive effect on tax avoidance, the transfer pricing action is one of the ways for companies to save their tax expenses. However, this transfer pricing is often also misused by companies to be used as a tax avoidance tool. transfer pricing moderates the effect of profitability on tax avoidance, companies with high profitability in multinational companies will have a higher tendency to shift profits to countries that have lower tax rates or different jurisdictions, thus the higher the profitability, the more aggressive a company will be in transferring pricing, where it will cause the taxes borne by the company to be low, the low tax value is an indication that the company is doing tax avoidance. Transfer pricing has proven to moderate the influence of firm size on tax avoidance. Large companies that have great advantages also tend to be involved with transactions to avoid taxes due to high tax payments. The way that companies use to make payments low is to make transfer pricing. Transfer pricing has not been shown to moderate the effect of tunneling incentives on tax avoidance. The results of the tunneling incentive regression test identified that foreign shareholders did not exercise their right of control to order management to determine unreasonable prices on transactions such as purchasing raw materials, obtaining rental income, renting office space and vehicles, royalties and engineering services, management services, and foreign labor costs, for the benefit of controlling shares located in countries whose tax rates were lower than Indonesian.

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