# Taxes and Foreign Ownership in Transfer Pricing Indications at the Covid-19 Pandemic Era

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**Abstract.** The Covid-19 pandemic has impacted economic conditions in the business sector. Several sectors' business income has decreased, impacting fiscal policy. Fiscal policies made by the government can encourage tax avoidance behavior. One of the tax avoidance that can occur is transfer pricing activity. This study investigates how transfer pricing indicators during the COVID-19 epidemic were impacted by taxes and foreign ownership. Using representative multinational corporations listed on the Indonesia Stock Exchange in 2020–2021, it examined the notion of agency and legitimacy. The results showed that taxes have a significant positive effect on transfer pricing, where the more fantastic the taxes, the higher the company to transfer pricing indications. Furthermore, this study also proves that foreign ownership has a positive effect. The study's results do not support the legitimacy theory, explaining the role of foreign ownership in gaining legitimacy from the public by not doing transfer pricing.

**Keywords**: Taxes, Foreign Ownership, Transfer Pricing Indication.

## 1 Introduction

The Covid-19 pandemic in the world in 2021 cannot be resolved until it impacts economic conditions in various countries, including Indonesia. Several business sectors experienced a declining income, so some had to stop their business. The government then responded to the impact of the Covid-19 pandemic by issuing various economic policies, including a fiscal policy related to taxes for the business sector, which was affected by the Covid-19 pandemic. Fiscal policy during the Covid-19 pandemic was focused on encouraging economic stability amidst the crisis caused by the pandemic.

The government issued fiscal incentives through tax incentives and relaxation of reporting to encourage economic stability during a crisis. This fiscal stimulus does not rule out the possibility of generating tax avoidance actions or efforts [16]. According to Dewi and Mustikasari [4], transfer pricing is one form of tax avoidance practice. Transfer pricing encompasses business transactions, taxation, and accountability for profits or expenses based on the idea of fair market prices. Transfer pricing is the cost connected with the delivery of goods or service fees [2].

From a tax standpoint, the level of state revenue can be impacted by the transfer pricing

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practices used by multinational corporations both directly and indirectly [1]. Various companies can carry out transfer pricing, often associated with high profitability and efficiency characteristics. Various interests can encourage transfer pricing activities, one of which is the controlling shareholder's interest, which has the authority to determine prices. Most companies in Indonesia have a concentrated shareholding structure so that they can be categorized into various ownerships. Foreign ownership has been extensively researched regarding its effect on tax evasion. Salihu et al. [15] and Kusbandiyah & Mat Norwani [7]when the impact of foreign share ownership on tax avoidance was evaluated, a favorable impact was discovered. Meanwhile, Rusyidi and Martani's study on how foreign ownership affects tax avoidance in Indonesia [12] needed to prove that foreign ownership affects tax evasion practices.

Various cases around the world related to tax evasion were motivated by a decrease in business income, such as the cases of Starbucks, Google, and PT. Toyota Motor. These cases illustrate that companies have reduced taxes paid through transfer pricing activities. Several researchers have examined the relationship between taxes on transfer pricing, including Hartati et al. [6] and Noviastika et al. [11], who found that taxes affect transfer pricing decisions. However, the research results from Tan (2014) and Marfuah (2014) show a different matter, namely that there is no effect between taxes on transfer pricing decisions. In other research condition, transfer pricing of multinational company after the tax amnesty program is higher than before the event (Sa'dani, 2021). In connection with the differences in the results of these studies and the events of the economic crisis due to the Covid-19 pandemic, the researcher wants to re-examine the effect of "Taxes and Foreign Ownership on Indications of Transfer Pricing in the Covid-19 Pandemic Era".

# 2 Literature Review And Hypothesis Development

## 2.1 Transfer Pricing

The price used to transfer tangible or intangible assets between companies within a group is known as transfer pricing. Many companies often use transfer pricing to avoid or evade taxes by minimizing the tax burden that companies must pay, declared Mangoting [8]. Transferring income or the basis for taxation and expenses from one company to another that has a special relationship or engages in transactions with related parties (RPT) is how the transaction is carried out, taking into account the variances in tax laws that exist between different countries. The presence of a unique connection is the key to transfer Pricing. Transactions between companies with unique relationships usually often use unfair prices, which are not the same as those in transactions between independent parties [10].

Transfer Pricing In commercial accounting, there are no specific provisions governing transfer pricing, but in the commercial accounting standards issued by IAI (Indonesian Institute of Accountants), statements relating to unique relationships can be found. PSAK No.7 is a statement of financial accounting standards that regulates the disclosure of related parties and transactions between reporting companies and related parties. Meanwhile, tax accounting focuses more on preparing tax returns and considering the consequences of taxation on transactions or company activities. Article 1 paragraph (8) Regulation of the Director General of Taxes Number PER-43/PJ./2010, which was last amended by PER-32/PJ./2011, defines transfer pricing as "pricing in transactions between parties who have a special relationship," according to Desriana [5].

According to UU No. 36 Tahun 2008, a special relationship is deemed to exist if any of the following conditions are met: (1) The taxpayer has direct or indirect capital participation of at least 25% in other taxpayers; (2) Taxpayers who control other taxpayers or two or more taxpayers are under the same control either directly or indirectly; and (3) There is a financial relationship between the taxpayer and the other taxpayers.

### 2.2 Taxes

According to the Law on Taxation UU No. 36 Tahun 2008, what is meant by the tax is: "Compulsory contributions to the State owed by individual taxpayers or corporate taxpayers that are coercive by law, and do not receive compensation directly and are used for the needs of the State with the largest possible amount for the welfare of the people." These contributions become a burden for taxpayers who must be paid.

The relationship between parent entities overseas and subsidiaries in Indonesia is separate from a tax perspective. Thus, the two companies, the subsidiary companies, and the parent company, carry out transactions arranged so that companies located in Indonesia suffer losses, but their businesses outside Indonesia experience profits (Rahayu, 2010). They were transferring their income from a subsidiary in Indonesia to a holding company in another country so that the total tax paid by the company to the state would be reduced. Kusnadi (2009) argued that minimize the total tax burden, the practice of pricing is chosen by multinational companies. Yuniasih et al. (2012) found that taxes positively relate to transfer pricing indications. To reduce corporate taxes, it is logical if managers choose to transfer Pricing, the first hypothesis that can be formulated right.

H1: Taxes have a positive effect on transfer pricing indications

### 2.3 Foreign Ownership

The ownership structure in the company arises from the comparison of individual shareholders, the wider community, the government, foreign parties, and six people in the company (Tiwa et al., 2017). Undang-Undang Nomor 25 Tahun 2007, shows that foreign investment is an investment activity carried out by foreign parties to conduct business on Indonesian soil. This covers both joint ventures with domestic and entirely foreign investors.

Multinational companies operate in more than one country and are possible if foreign parties own ownership. Significant foreign majority ownership will motivate decision-making to make various decisions because majority shareholders have control rights, including transfer pricing policies. The controlling shareholder can obtain personal benefits, which can harm non-controlling shareholders indirectly because the transfer pricing decision is made for personal gain (Refgia et al., 2017).

Other research also proves that the intensity of foreign ownership can influence the decision of multinational companies to exercise transfer prices. Multinational companies with foreign ownership with a history of carrying out transfer pricing will tend to carry out transfer prices continuously (Cristea & Nguyen, 2013). The hypothesis for foreign ownership's impact on transfer pricing is formulated as follows:

H2: Foreign ownership affects negatively related to the transfer pricing indications.

## 3 Research Methods

### 3.1 Population, Sample, Sampling Technique

International businesses with presence in Indonesia and listed on the Indonesia Stock Exchange make up the study's population and sample. The MUC Consulting Group research states that several multinational corporations used transfer pricing to lower their tax obligations, which is why those companies were chosen. Purposive sampling was the method of selection that was employed in this study. Using the following standards: companies continuously listed on IDX from 2020 to 2021; Companies must have full knowledge of the measurement indicators utilized as variables in this study and must give comprehensive annual reports during the observation period.

### 3.2 Method of Collecting Data

The data collection method was carried out using a literature study, namely collecting secondary data by studying the literature relevant to this research to obtain a theoretical description of the research topic and documentation, namely collecting, recording, and reviewing documents on financial data. Figure 2 describes the design of this study, which illustrates tax implications and foreign ownership's impact on transfer pricing.

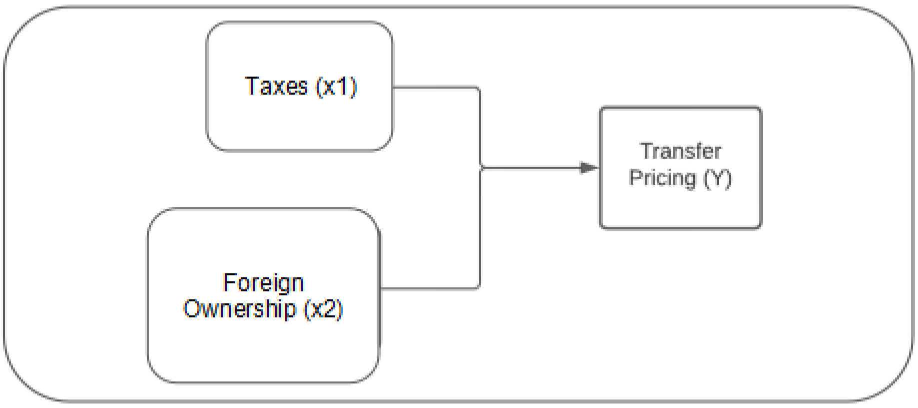


**Fig.. 2.** Research Design

### 3.3 Research procedure

*Transfer Pricing*

The Transfer Pricing Decision is the dependent variable utilized in this study (TP). Transfer Pricing (TP) explains the possibility of a company transferring profits through a transfer pricing mechanism. Transfer pricing in this study is measured through a dummy variable. The specified category, Companies that engage in sales transactions with related parties are assigned a value of 1 (one), while those that do not engage in such transactions are assigned a value of  0 (zero).

*Foreign Ownership*

Foreign ownership, namely a dummy variable with a value of "1" for Indonesian companies that have significant foreign ownership, or more than equal to 25%, and "0" for Indonesian companies that do not have significant foreign ownership.

*Tax*

Tax by comparing the amount of tax expense payable with taxable profit.

$$\text{ETR} = \frac{tax\ expense}{income\ before\ tax} \quad (1)$$

*Data analysis*

Descriptive statistics in Ghozali [26] are intended to provide an overview of the distribution and behavior of the sample data. The logistic regression analysis approach was employed in this study to analyze the data. The Hosmer and Lemeshow Goodness of Fit Test was used to evaluate the regression model's viability. The Nagelkerke R Square value is used to express the logistic regression coefficient of determination. Square Nagelkerke R. The logistic regression equation can be stated as equation (1).

$$Y = \alpha + \beta 1\ X1 + \beta 2\ X2 + e \quad (2)$$

Information:

Y: Transfer Pricing

α: Constant

β1- β2 : Regression Coefficient

X1 : Tax

X2: Foreign Ownership

e: Error Term, namely the error level in the estimator research.

*Hypothesis test*

*Individual Parameter Significance Test (Statistical Test t)*

Individual parametric tests are designed to demonstrateHow well the dependent variable's variance can be described by the influence of a single explanatory or independent variable. the significance threshold was used to conduct the test of 0.05 (α=5%) with the following criteria:

If the p-value <0.05, then the research hypothesis is supported, meaning there is a significant influence between one independent and dependent variable.

If the p-value> 0.05, the research hypothesis is not supported, meaning no significant effect exists between one independent variable and the dependent variable.

*R2 Test or Coefficient of Determination*

The amount of variance in the dependent variable that is explained by all of the independent variables is measured by their coefficient of determination. Between 0 and 1, the coefficient of determination (0 R2 1). The better the regression results, which are determined by the R2 value or how near it is to 1, the more information the independent variables may predict about the variation in the dependent variable.

## 4 Results And Discussion

## 4.1 Population and Research Sample

In 204 observations, criteria were developed utilizing a total of 102 sample companies. Table 1 shows the number of samples used in the observations.

**Table 1.** Research Samples

| Samples of Company Research | Total Sample | Total observation, two years |
|---|---|---|
| Multinational companies listed on the Indonesia Stock Ex-change in 2020-2021 | 114 | 228 |
| Financial statements of businesses with incomplete data | 10 | (20) |
| Companies that do not complete information on measurement indicators | 2 | (4) |
| The number of businesses that comply with the study's requirements and the research sample | 102 | 204 |

## 4.2 Regression Logistic Analysis

The regression model's viability must first be evaluated. Based on the Hosmer and Lemeshow test results, the Chi-square value was 5.494 with a sig. of 0.704. The result shows that the model can predict the observed value because it matches the observed data. The second step assesses the regression model by comparing the values of -2 Log Likelihood Block Number = Step 0 and -2 Log Likelihood Block Number = Step 1. There is a significant decrease in the value of -2 Log Likelihood Block Number = Step 0 of 264.893 to 256.195 in the -2 Log Likelihood Block Number = Step 1, indicating that the regression model by including all independent variables is better or, in other words, the hypothesized model fits the data. Examining each independent variable's impact on the dependent variable comes next. Examining each independent variable's impact on the dependent variable comes next.

**Table 2.** Regression Logistic and Hypothesis Testing Results

| Variabel | B | Sig |
|---|---|---|
| Taxes (X1) | 0.916 | 0.005 |
| Foreign Ownership (X2) | 0.175 | 0 .683 |
| Constant | 0.250 | 0.214 |
| Hosmer and Lemeshow Test: | Chi-Square<br>5.494 | Sig<br>0.704 |
| Overall Model Fit Test : | -2 Log Likehood Block Number = Step 0<br>264.893 | -2 Log Likehood Block Number = Step 1<br>256.195 |
| Nagel Karke R Square : | 0.057 | |
| Cox & Snell R Square : | 0.042 | |

The results of the research hypothesis test with the logistic regression model are presented in Table 2. Regression Equation:

$$Y = 0.250 + 0.916\ X1 + 0.175\ X2 + e \tag{2}$$

### 4.3 Hypothesis Testing

**Taxes and Transfer Pricing Indication**

According to Table 2, the tax variable's regression coefficient is 0.916 with a sig-Wald value of 0.005, which is a significant value. Because taxes have a considerable negative impact on transfer pricing decisions, the first hypothesis—which claims that taxes have a good impact on business transfer pricing decisions—is supported. These findings are in line with study by Yuniasih, Rasmini, and Wirakusuma (2012), which discovered that taxes have a favorable impact on company transfer pricing decisions. Therefore, corporations engage in transfer pricing to lessen the impact of the higher tax burden.

The findings of this study are at odds with research by Marfuah (2014), which claims that fiscal authorities (tax officers) erroneously believe that transfer pricing is used to dodge taxes. In general, the fiscal authorities must pay close attention to two key factors in the transfer pricing matter so that businesses can limit transfer pricing practices and tax remedies to transfer pricing allegations obtain sufficient reason. The two key factors are (2) fairness or the arm's-length principle and (1) affiliation or special relationship.

**Foreign Ownership and Transfer Pricing Indication**

Table 2 is known that the magnitude of the regression coefficient of the foreign ownership variable 0.175 with a sig-Wald value of 0.683. The second hypothesis, which states that foreign ownership have a negative effect on company transfer pricing decisions, is not supported, based on testing this hypothesis, foreign ownership have not a significant adverse effect on transfer pricing decisions. This study is in line with Refgia et al. (2017), which explains that if a company has a high percentage of foreign ownership, the greater the influence of foreign shareholders to determine decisions within a company, including the policy of determining transfer prices.

The preceding result lends weight to the legitimacy theory. According to this concept, enterprises continue to seek to ensure that they operate inside the framework and norms of a society where companies endeavor to ensure that outsiders acknowledge their actions as legitimate. Companies with foreign ownership structures must benefit society by applying transfer pricing to existing laws and regulations.

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## 5 Conclusion

Based on the research problem at the Covid-19 Pandemic Era, the following conclusions may be drawn. Taxes and Foreign ownership have a positive effect on transfer pricing indication. It indicates that the higher the effective tax rate and foreign ownership structure of the company, the higher the transfer pricing indications taken by the company. Consistent with agency theory, Egger et al. (2010) further emphasized that foreign-owned companies, especially multinational companies, have more opportunities to carry out transfer pricing indications (sales) by taking advantage of revenues transferred elsewhere, as well as utilizing accounting standards and tax treatment in foreign countries that make profit and debt shifting.

This study has some implications. Differences in regulations experienced by foreign companies and the amount of tax burden borne by companies can be used as a reason for companies to carry out transfer pricing to minimize the amount of the tax burden and maximize company profits. The regulations governing the presence of a foreign board of commissioners in a corporation, particularly those pertaining to the obligations, responsibilities, and makeup of foreign commissioners for businesses with a foreign ownership structure, need to be clarified by regulators, particularly tax authorities.

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