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The Impact of Transfer Price, Leverage, Profitability, and Firm Size on Tax Avoidance

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Abstract
Taxes have become the largest contributor to state revenue. With it, the tax government must contribute a lot of funds, so it is necessary to pay attention to tax payment compliance. As for companies that are taxpayers, they tend to want to reduce the cost of paying taxes. Conflicts of interest between the government and companies in taxation have become a frequent discussion. This study aims to continue to raise the discussion and prove the hypothesis that the variables of transfer pricing, leverage, profitability, and firm size have a significant positive effect on tax avoidance activities. The research was conducted on companies in the industrial, financial, and raw material sectors listed on the IDX during 2019-2021 using the multiple linear regression model analysis method. This research reveals that transfer price has a negative impact on tax avoidance. Leverage and profitability have a positive impact on tax avoidance. Meanwhile, firm size has no impact on tax avoidance. The lower transfer pricing tends to decrease the intensity of tax avoidance. The more leverage and profitability will drive the company to increase the intensity of tax avoidance. However, firm size is not so important in affecting the intensity of tax avoidance.

Keywords: tax avoidance, transfer price, leverage, profitability, firm size, firm value

1. Introduction

Indonesia passed the pre-pandemic period two years ago by consistently recovering the national economy. The State Economic Recovery Policy (PEN) is comprehensively carried out using fiscal and monetary policies. Based on data from the Ministry of Finance, 695.2 trillion rupiah has also been channelled from the State Revenue and Expenditure Budget (APBN) funds to restore the country's economy (Sasongko, 2020). Of the amount distributed by the State Budget, 172.1 trillion rupiah is allocated to encourage people's consumption and/or purchasing power so that it can re-energize the national economy. The government is also accelerating the realisation of the distribution of the State Budget/Regional Budget to encourage consumption by ministries/institutions/local governments (Sasongko, 2020). The State Budget is an

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extraordinarily important financial wallet for the country, from the Ministry of Finance that the State Budget has an important and decisive function for the economy and for a country to be used, relied on, and used in achieving state goals (Ministry of Finance, 2022).

The State Revenue and Expenditure Budget is sourced from at least three, namely tax revenue, Non-Tax State Revenue (PNBP), and grants, while others can also be sourced from financing. A total of 2750.0 trillion rupiah of state expenditure in the 2021 State Budget is sourced from tax revenues of IDR 1444.5 trillion, PNBP of IDR 298.2 trillion, grants of IDR 0.9 trillion, and financing of 1006.4 trillion (Ministry of Finance, 2021). Taxes are the largest contributor to the source of state budget funds. In 2022, the contribution of tax revenue to the state budget has reached 1634.36 trillion rupiah (Mutiara, 2022). Minister of Finance Sri Mulyani said that previously in October 2022 tax revenue was at 1448.2 trillion rupiah, which means that the tax revenue target in the State Budget has reached 97.5% (Novelino, 2022).

Taxes are not only an important source of revenue earned by every country, it is also a support for revenue for the country. When compared to other countries, taxes in Indonesia are a source of state revenue with a high percentage level compared to others (Mulyati et al., 2019). So it can be said that the existence of taxes is very important, compliance with taxation and tax evasion will be very *crucial* in Indonesia. In Law of the Republic of Indonesia No. 28 of 2007 Article 1 (1) states that Taxes are mandatory contributions to the state that are owed by individuals or entities that are coercive based on the Law, by not getting direct rewards and used for state purposes for the greatest possible prosperity of the people. Taxes are not only mandatory to be paid by the people of the country personally but also for entities that stand and/or take profits in the territory of the Indonesian state. In addition, the industrial sector that contributes the most taxes to the state is the processing or manufacturing sector, amounting to 29.4% (Rizaty, n.d.). With that, compliance and preventive actions from tax misappropriation in the manufacturing sector have become material for Indonesia. However, business entities in the manufacturing sector will certainly also make efforts to avoid overpaying taxes, by carrying out tax avoidance activities.

Tax avoidance is an effort made by companies to reduce the burden of taxation. Tax evasion can be carried out by companies legally or illegally. Thus, in the face of tax avoidance, the fiscal must be very careful in assessing the risk of deviations in tax regulations in the company's activities, and the company must be careful and compliant in carrying out tax avoidance. Among the instruments that companies can use for tax avoidance are transfer price, leverage, profitability, and company size.

Transfer Pricing can also be interpreted as a transaction activity between the head office and branches or between branch offices and others. The parties will agree on the price or value of the object to be transferred to the other party, thus giving rise to obligations to the party receiving the object of goods or services and giving rise to receivables or income to the party transferring the object of goods or services. Transfer pricing activities can generate maximum profits; for example, when transfer pricing activities occur between separate divisions in a company that set prices equal to market prices, they can also set maximum prices with pricing that is too large

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(Lascar & Guglielmi, 2010). For those who receive greater profits, their taxable income can increase so as to increase the amount of tax burden. As for transfer pricing transactions that are carried out for tax aggressiveness, such as by shifting profits, these activities can be used to avoid paying taxes. For example, profits are transferred to areas that are subject to lower taxes or are not taxable. The transfer of profits can be done through transfer pricing activities.

There is a study conducted by Wijaya & Hidayat (2022) regarding the influence of transfer pricing activities on tax avoidance in agricultural sector companies. Tax avoidance activities were measured by *GAAP ETR proxies* and it was proven by the results of the t-test that transfer pricing activities had a significant positive influence on tax avoidance. The results of this study are not in line with the research conducted by Falbo & Firmansyah (2019) which proves that the aggressiveness of transfer pricing has no effect on tax avoidance. The difference may be due to differences in the use of proxies, if the research conducted by Hanafi and Wijaya uses the GAAP ETR proxy which is measured as the ratio of income tax expense to profit before tax, Teza and Amrie's research uses *the Abrnormal Book Tax Differences* (ABTD) proxy, where BTD is the difference between the value of accounting profit and the company's tax profit in a given year.

Leverage can also be used for tax avoidance activities because it incurs interest costs from debts, which will reduce the company's pre-tax income, thereby reducing the amount that the company will pay. Leverage can be said to be the activity of using the company's source of funds that incurs interest costs. This is because the funds are sourced from the company's debt, where the debt is used for funds or company assets that are used to increase the company's profits. After that, the company will be burdened by interest costs. In Article 6 (1) letter a of Law Number 36 of 2008, it is explained that interest arising from part of business expenses is allowed to be a *deductible expense* in the process of calculating corporate income tax. It is this interest that can be a risk or return of profit for the company. The income generated by the company, where there is a leveraged contribution in its capital structure, can lead to an increase in tax payments, which is due to an increase in taxable income. However, the interest cost from leverage also causes a decrease in income that becomes taxable income so that it can reduce tax costs.

Research was conducted by Sulaeman (2021) with the population of *property* and *real estate* companies. The measurement of tax avoidance activities is measured by the *cash effective tax rate (CETR) proxy*, where the leverage variable positively affects CETR, it means that leverage has a negative effect on tax avoidance. In the study, it was proven that leverage has a positive effect on CETR, which means that the higher the company's leverage, the lower the tax avoidance activities carried out by the company. Other research also supports these results which prove that the level of debt or leverage reduces tax avoidance activities (Yulianty et al., 2021).

Still related to revenue, there are profits or profitability that the company has. Getting profits or profits in addition to having become a neo-classical theory that companies run naturally is also a must for companies. In order to be stable and run its business activities continuously, companies need profits. With that, the company implements the principle of business continuity. With profits, the company can also continue to develop its business, increase growth, avoid liquidation

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and dissolution. From the company's profits, you can compare business performance, get financial input so that you can generate maximum profits again. Maximum income is indeed the most important goal for business activities. In addition to being the company's goal, from this value, the government, especially the fiscal department, also determines the amount of corporate tax paid. The income earned by the company before it becomes a net profit will be charged by tax on the amount of income or taxable income. The high and low income affects the efficiency of corporate tax avoidance. This is because companies tend to avoid taxes to get more net profits, they will do various ways and even aggressiveness to avoid taxes.

The study was conducted by Sulaeman (2021) with the population of *property* and *real estate* companies, where the measurement of tax avoidance activities is proxied with *the cash effective tax rate (CETR)*. The results of the study show that profitability has a regression coefficient of -1,787, which means that it is significantly negative for *CETR* and significantly positive for corporate tax avoidance activities. These results are also supported by other studies that use mining company objects and *Effective Tax Rates (ETR)* proxies to measure tax avoidance activities (Yulianty et al., 2021).

The size of the company also affects tax avoidance activities. Watts & Zimmerman (1978) said that the influence of accounting standards on operating income may vary depending on the size of the company. Accounting standards include regulations, compensation, and tax policies. The larger the size of the company is expected to reflect the higher the change in the amount of revenue that the company will report (Watts & Zimmerman, 1978). Besides that, the larger the size of the company, the greater the costs that the company will incur, the greater the revenue, the greater the costs. One of them is the tax burden imposed on the company's taxable income. Companies that are classified as large usually want their profitability to be recognized as greater so that they reduce costs, one of which is the tax burden through tax avoidance activities.

Research conducted by Sulaeman (2021) the used the population of *property* and *real estate* companies also proves that the larger or higher the size of the company, the higher the level of corporate tax avoidance activities. These findings are in line with research conducted by Wulandari & Purnomo (2021) on *non-service* companies with *ETR* proxies, which proves such results.

Based on those arguments, this research proposed the following hypothesis:
H1: Transfer pricing has a positive effect on tax avoidance.
H2: Leverage has a positive effect on tax avoidance.
H3: Profitability has a positive effect on tax avoidance.
H4: Firm Size has a positive effect on tax avoidance.

2. Method

Population and Sample
The researcher used *time series* data from sample companies obtained using *a purposive sampling approach*. The data was taken from the trusted website of the Indonesia Stock

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Exchange (IDX) and processed using IBM SPSS version 22. In addition, the collected company data must meet the following requirements:

1. Companies in *the industry, finance, & basic materials* sector listed on the Indonesia Stock Exchange during the period 2019-2021.
2. The company did not suffer any losses during the 2019-2021 period.
3. The company paid taxes during the period of 2019-2021.
4. The company has receivables in other companies that have a special relationship during the period 2019-2021.
5. The company presents complete financial information and in accordance with the research variables.

Variables

Dependent variables or also known as bound variables are defined as variables that are influenced or that result from the existence of independent variables. In this study, there is one dependent variable, namely corporate tax avoidance. Tax avoidance in this study is measured using a cash *effective tax rate* proxy formulated by:

$$CETR = \frac{\text{Cash paid for taxes}}{\text{Earnings before taxes}} \qquad (1)$$

When the value of CETR is higher or closer to the tax rate, it shows that tax avoidance will be lower (Dyreng et al., 2008). With that, corporate tax avoidance activities can be formulated as follows:

$$\text{Tax Avoidance} = -CETR \qquad (2)$$

Thus become:

$$Tax\ Avoidance = -1x\frac{\text{Cash paid for taxes}}{\text{Earnings before taxes}} \qquad (3)$$

Independent variables or also known as independent variables are defined as variables that affect or are the cause of changes in the occurrence of bound variables. In this study, there are four independent variables that will be tested for their effect on dependent variables. The four dependent variables used are *transfer pricing, leverage, profitability*, and *firm size*.

In transfer pricing activities, both parties will agree on a transfer price for the product, the price will very likely decrease or increase. This can create an opportunity to avoid corporate taxes. That way, price transfer activities will only occur if there is a transaction of goods or services between related parties or has a special relationship, the price can be recorded on the company as a receivable. Thus, the high price transfer transactions that occur intra-company can be represented by the high intra-company receivables (Rathke et al., 2021). With that, the transfer price can be measured by the formula:

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$$Transfer\ Pricing = \frac{\text{Receivables to Companies with Special Relationships.}}{\text{Total receivables}} \quad (4)$$

Leverage is a ratio used to measure the extent to which a company's asset limits are financed by long-term debt. Leverage can be measured using *Debt-to-Asset Ratio* (DAR) and *Debt-to-Equity Ratio* (DER). Research conducted by Zhang et al. (2022) and Pangathousands et al. (2021) regarding the effect of leverage on tax avoidance. Leverage is proxied using a DER that can be measured as long-term debt, which is also scaled using total assets (Zhang et al., 2022). Therefore, in this study, the size of leverage is determined using the *Debt to Equity Ratio proxy*, which is formulated by:

$$Debt\ to\ Equity\ Ratio\ (DER) = \frac{\text{Total Liabilities}}{\text{Total Equity}} \quad (5)$$

Profitability reflects the financial performance of a company in generating *returns* on the management of the company's assets, so the lower the return on assets will show the lower the profit generated from the use of assets in the company's operations (Pangathousands et al., 2021). Profitability can thus be formulated by:

$$Return\ On\ Asset\ (ROA) = \frac{\text{Net income}}{\text{Total assets}} \quad (6)$$

The size of the company can be used to determine the size of the business through its total quality, total sales, total employees, total assets, etc. (Prakosa & Hudiwinarsih, 2018). The study was conducted by Zhang et al. (2022) who looked for the effect of company size on tax avoidance with gender diversification as a moderation variable, the size of the company was proxied by the researcher with total assets by believing that the total number of assets owned by a corporation could be used to determine the size of a company. With that, in this study, the size of the company will be formulated by:

$$Firm\ Size\ = ln\ \text{Total Assets} \quad (7)$$

Analysis Methods

The analysis method used in this study is multiple linear analysis. The data will be processed using the help of IBM SPSS version 22 and presented with three analysis methods, namely descriptive statistics, data quality tests and hypothesis tests.

Descriptive statistics will be used to describe the main financial variables disclosed by the sample companies in the financial statements in the period 2019-2021. The analysis tools used are mean, median, mode, sum, percentage, minimum, maximum, quartile, percentile, range, distribution, variance, standard deviation, standard error, slope value, and others (Soecahyadi, 2019).

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The second analysis that will be carried out after the descriptive statistical test is the classical assumption that will test the feasibility of the data used for the study. Among the analysis tools are the normality test, multicollinearity test, heterokedasticity test, and autocorrelation test The normality test is said to be normally distributed if the significance value is higher than 0.05 ($\alpha > 0.05$). The study is said to pass the multicollinearity test when the variance inflation factor (VIF) value is less than 10 and when the tolerance value is more than 0.10. The heterokedasticity test was carried out by *the glacier method* and was said to pass the heterokedasticity symptoms if the significance value of the independent variable showed more than 0.05. Furthermore, the autocorrelation test is carried out using *the Watson Durbin* method.

The test model carried out is multiple linear regression. With several tests, namely the determination coefficient, the T significance test, and the F significance test. If the value produced is close to 1, it means that the independent variable is better at explaining the independent variable and vice versa. Furthermore, the T significance test was carried out with the aim of measuring the significance of the influence of an independent variable on the dependent variable partially. If the significance value is less than 5% ($\alpha < 0.05$) and the number is positive, the relationship is said to be significantly positive. Furthermore, the F significance test was carried out with the aim of measuring the significance of the influence of independent variables simultaneously or as a whole on the dependent variables. The influence is measured by the significance value or probability of the f test resulting from the test is less than 5% ($\alpha < 5\%$), then the independent variable is said to have a simultaneous influence on the dependent variable.

3. Results

Descriptive Statistic

Based on the purposive sampling method, this research collected 68 observed data. The descriptive statistics is presented in table 1.

Table 1. Descriptive Statistics

	N	Range	Min.	Max.	Mean	Std. Dev.
Transfer Pricing	68	.99	.00	.99	.1221	.20114
Leverage	68	5.88	.09	5.97	1.3150	1.31989
Profitability	68	.32	.00	.32	.0531	.04567
Firm Size	68	9.57	25.52	35.08	29.9586	2.21960
Tax Avoidance	68	.88	-.89	-.02	-.2652	.17741
Valid N (listwise)	68					

Source: SPSS 22 data processing results

Classic Assumption Test

The results of the classic assumption test are presented in the following table 2:

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Table 2. Classic Assumption

Test Type	Test Criteria	Test Results	
Normality	Kolmogorov-Smirnov	Asymp. Sig. (2-tailed)	0.200
Multicollinearity	VIF	Transfer Pricing (TP)	1.123
		Leverage (DER)	1.577
		Profitability (RoA)	1.251
		Firm Size (ln Assets)	1.506
Heteroskedasticity	Significance	Transfer Pricing (TP)	0.078
		Leverage (DER)	0.413
		Profitability (RoA)	0.366
		Firm Size (ln Assets)	0.361
Autocorrelation	Durbin Watson		2.039*
Coefficient of Determination		Adjusted R Squared	0.035

The result of the normality test as can be seen from table 2 of the normality test is that the data has been distributed normally. This is evidenced by the *Asymp. Sig. (2-tailed)* value of 0.200, which means more than 0.05 (0.200>0.05). With that, it can be said that research with data samples can be carried out.

The results of the multicollinearity test which can be seen in table 2 of the multicollinearity test show that the research data has passed the classic multicollinearity assumption test, with evidence that it does not have symptoms of multicollinearity. The *coeeficient* table shows that the *tolerance* value of all research variables has exceeded 0.01, which indicates that it has passed the multicollinearity test. Likewise, *the variance inflation factor* (VIF) value of all research variables has been less than 10.00, which indicates that it has passed the multicollinearity test. According to Ghozali (2013), if there are no independent variables that have a tolerance value of less than 0.10 and a VIF value of not more than 10.00, then there is no correlation between the independent variables.

The results of the heterokedasticity test presented in table 2 of the heterokedasticity test, *coefficient* above show that the research data has passed the classical heterokedasticity assumption test with the glacier method. In the table, *the coefficient* shows that the *sig value (significance)* of all research variables has been more than 0.05, which indicates that it does not have symptoms of heterokedasticity. According to Ghozali (2013), if the *probability of the sig* is above the confidence level of 5%, then it is stated that there is no heterokedasticity between the independent variable and the dependent variable.

To find out whether or not the research variable from the test passes or not, the DW value must be between -2 to +2 (du < db < 4-du or du < db > 4-du or du < db > 4-du). In addition, the DB value must also be between the DL and DU values. DU is generated from = K(4) : N(68). From the results of table 4.7 of the Durbin-Watson test, the *summary model* table shows that the DB value (Durbin-Watson) of the research variable is 2.039. The DU value was 1.7335, and the DL

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value was 1.4853, obtained from K(4) and N(68) with a significance level of 5% (Junaidi, n.d.). The results show that the DB value is between DU and 4-DU, the result shows 1.7335 <2.039<2.2665. DESPITE ≤ DW ≤ 4-DU indicates that there are no autocorrelation symptoms, either positive or negative, so the regression model is not rejected (Ghozali, 2013).

From table 2 of the determination coefficiency test, it can be seen that the *adjusted r square* value is 0.035 or 3.5%. This shows that the Tax Avoidance represented through *CETR* has explained the independent variables (*TP, DER, ROA, Ln (Total Asset))* from this study by 3.3%. It also shows that the remaining 3.5%% is 96.5% influenced by other variables that are not used in this study. Because the value is close to 0 (0<0.035<1), the independent variable used in the study is said to be weak in explaining the dependent variable of the study.

Regression Analysis

The regression analysis test results are presented in Table 3.

Table 3. Regression Analysis Test

Model		Unstandardized Coefficients		Std. Coef.		
		B	Std. Error	Beta	T	Sig.
1	(Constant)	-.330	.351		-.940	.351
	Transfer Pricing (TP)	-.182	.112	-.206	-1.621	.018
	Leverage (DER)	.007	.020	.055	.366	.044
	Profitability (RoA)	.776	.521	.200	1.487	.023
	Firm Size (ln Assets)	.001	.012	.015	.102	.153
F Test						.022

a. Dependent Variable: Tax Avoidance

Based on data presented in Table 3, this research reveals that transfer price has a negative impact on tax avoidance. Leverage and profitability have a positive impact on tax avoidance. Meanwhile, firm size has no impact on tax avoidance. The lower transfer pricing tends to decrease the intensity of tax avoidance. The more leverage and profitability will drive the company to increase the intensity of tax avoidance. However, firm size is not so important in affecting the intensity of tax avoidance.

4. Discussion

After analyzing the influence of transfer pricing, leverage, profitability, and company size on tax avoidance in industrial, finance, and basic materials companies on the Indonesia Stock Exchange (IDX) in 2019-2021, all results prove:

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The results of the study prove that transfer pricing has a significant negative influence on tax avoidance. This means that when the transfer pricing value increases, it reduces the likelihood of the company carrying out tax avoidance activities. Likewise, if the transfer pricing value decreases, it increases the likelihood of sample company tax avoidance activities increasing. The results of this research test are in line with research conducted by Irawan et al., (2020).

The results of this study do not prove the hypothesis that transfer pricing has a significant positive relationship with tax avoidance. Multiple linear regression analysis shows that transfer pricing is negatively correlated with tax avoidance. Research conducted by Irawan et al., (2020) proves that transfer pricing has a significant negative effect by using ETR proxies on research samples of manufacturing companies for the period 2014-2017, Irawan et al., (2020) stated that transfer pricing has a significant negative effect on tax avoidance. On the other hand, there is a study conducted by Putri & Mulyani (2020) proving that transfer pricing has a significant positive effect, with ETR proxies on research samples of multinational construction companies for the period 2014-2018, Putri & Mulyani (2020) stated that transfer pricing has a significant positive effect on tax avoidance. Differences in results and the non-acceptance of research hypotheses stating that transfer pricing has a positive effect may occur due to differences in research population data. Differences in population data selection can provide differences in company conditions and tax regulations.

The results of the study prove that leverage has an influence or has a significant positive influence on tax avoidance. Which means that when the value of leverage increases, the likelihood of the company carrying out tax avoidance activities also increases. Likewise, if the transfer pricing value decreases, the possibility of corporate tax avoidance activities also decreases. The results of this research test are in line with research conducted by Anggriantari & Purwantini (2020) on manufacturing companies listed on IDX for the 2015-2019 period.

The results of this study prove the hypothesis that leverage has a significant positive relationship with tax avoidance. Leverage sourced from company funds obtained from debt has been proven to have a positive influence on corporate tax avoidance. The company is run to get revenue, where the income will later be reduced by cash expenditure from costs. Costs are not only from operating activities but also from the company's funding activities, for example, the interest that must be paid from leverage. Companies certainly want to reduce costs, but they also need incoming funds. Due to the tendency of companies to maximize profits, one of the efforts that companies can make to reduce the costs that will come out (one of which is from leverage activities) is to carry out tax avoidance activities.

The results of the study prove that profitability has a significant positive influence on tax avoidance. Which means that when the transfer pricing value increases, it also increases the likelihood of the company carrying out tax evasion activities. Likewise, if the profitability value decreases, the possibility of tax avoidance activities of the sample company also decreases. The results of this research test are in line with research conducted by Mahdiana & Amin (2022) on manufacturing companies listed on the IDX for the 2015-2018 period.

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Profitability is the goal of business activities. Not only the company's internal management, but also external parties of the company, such as investors, creditors, and consumers also assess the image and performance of a company, one of which is from profitability. With that, the company's internal parties are indeed encouraged to always maximize profitability. The tendency of companies that want to maximize high profitability is to keep costs as low as possible. One of the costs is the tax burden, so tax avoidance activities occur.

The results of the study prove that firm size has no effect or has a positive *but* insignificant effect on tax avoidance. This means that when the size of the company is large, it increases the possibility of the company carrying out tax avoidance activities insignificantly. Likewise, if the size of the company is small, it will reduce the possibility of corporate tax avoidance activities insignificantly. The results of this research test are in line with research conducted by Rahmawati & Nani (2021) on mining companies listed on IDX for the 2016-2019 period.

The results of this study do not prove the hypothesis that firm size has a significant positive relationship with tax avoidance. This is possible because the size of the total assets owned by the company does not affect the company's decision to avoid taxation.

5. Conclusion

This study was conducted to prove empirically the influence of independent variables, namely transfer pricing, leverage, profitability, and firm size on dependent variables, namely, tax avoidance. From the results of the analysis carried out during the study, the researcher concluded that there is a negative influence between transfer pricing on tax avoidance, which means that the higher the transfer pricing, the lower the likelihood of corporate tax avoidance activities. Additionally, there is a positive influence between *the debt-to-equity ratio* on tax avoidance, which means that the higher the leverage, the more likely it is that corporate tax avoidance activities occur. Furthermore, there is a positive effect between *return on assets* on tax avoidance, which means that the higher the profitability, the more likely it is that corporate tax avoidance activities occur. However, there is no significant influence between *Ln (total assets)* on tax avoidance, which means that firm size does not have a direct relationship with the rise and fall of corporate tax avoidance activities.

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