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The Effect of Leverage and Tunneling Incentives on Transfer Pricing: A Study on Consumer Goods Industry Listed on Indonesia Stock Exchange

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Abstract: This study examines the effect of leverage and tunnelling incentive on the company's decision to transfer pricing in consumer goods industry sector companies listed on the Indonesia Stock Exchange in 2015-2020. The technique used in sampling is purposive sampling, with a sample of 15 consumer goods industry companies. The data used in this study is secondary data in companies' financial reports. The analysis model used in this study is multiple linear regression with a significant level of 5%. The analysis results showed that leverage measured by debt to equity ratio has a significant positive effect on transfer pricing, tunnelling incentive measured by ownership share above 20% has a significant positive impact on transfer pricing.

Keywords: *Leverage, Tunneling Incentive, Transfer Pricing, Consumer Goods Industry*

Introduction

The pace of globalization and increasingly rapid technology does not only have an impact on a person's personal life but also has an impact on the company's business processes. Many companies set up their subsidiaries in other countries to increase sales and economic profit. The emergence of transfer pricing practices is often caused by the sale and purchase of goods and services between taxpayers who have a special relationship (Lubis, Bukit, & Lubis, 2013). Companies use transfer pricing practices to assess performance between divisions and branches. However, in reality, Transfer pricing is often considered negative. It means "pejorative", which is usually done to reduce the total tax burden of the multinational group of companies (Sa'diah & Afriyenti, 2021). For some companies, especially multinational companies, the limitations and differences in the resources contained in each country and the opportunity to get more profits due to tax avoidance are why these companies carry out transfer pricing activities (Lingga, 2012).

In Indonesia, the practise of transfer pricing has increased by up to 20%. Almost 2000 foreign investment companies (PMA) do not pay taxes on the grounds of experiencing losses, but based on calculations made by these companies, they should pay Rp. Twenty-five billion per year, and it is known that the scheme carried out is transfer pricing (Karunia, 2020). One of the companies that practice transfer pricing is PT. Adaro Indonesia, where the company sells coal to an affiliated company in Singapore called Coltrade Service International Pte at a price below the market price, so the profit recorded in PT. Adaro is lower than it should be (Wareza, 2019). PT. Bentoel Internasional Investama made loans to related companies in the Netherlands amounting to US$ 434 million in 2013 and US$ 549 million in 2015 with a total loan interest of US$164 million, which caused PT. Bentoel Internasional Investama lost operational funds to pay the debt interest expense and admitted that it experienced an increase in net losses of 27.3% in its 2016 annual report (Kontan, 2019).

Based on this case, it can be concluded that transfer pricing is a scheme carried out by companies to maximize profits, and this makes transfer pricing a matter that needs to be studied to find out what factors affect transfer

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pricing. There are several reasons companies decide to transfer pricing, one of which is through tunnelling incentives. Tunnelling transfers company assets and profits to benefit the majority shareholder who controls the minority shareholder (Aharony, Wang, & Yuan, 2010). Transfer of resources through transactions between companies and owners at prices below market prices is one way to be done in tunnelling activities. Majority shareholders can also increase their profits without the need to transfer company assets, namely by converting securities such as notes, checks, and other securities into ordinary shares, which will reduce the value of earnings per share (F Noviastika, Mayowan, & Karjo, 2016). Based on research conducted by (Indriaswari & Aprilia, 2017), tunnelling incentives have a significant effect on transfer pricing, while Pratiwi (2018), Mulyani, Prihartini, & Sudirno (2020) state that tunnelling incentives do not have a substantial impact on transfer pricing.

In addition to tunnelling incentives, another factor that may influence companies to perform transfer pricing is leverage. Leverage (funding level) is a ratio that shows the amount of debt owed by the company to finance its operating activities (DK Wardani & Khoiriyah, 2018). The form of transfer pricing that multinational companies mainly do is through debt to equity ratio instruments. The provision that interest payments can reduce the tax burden that must be paid makes the company use more debt to fund its affiliates than by using equity participation so that the greater the composition of debt in the company. Especially, affiliates have a location in countries with high tax rates, the greater the profits earned by the company (Richardson, Taylor, & Lanis, 2013). Based on the results of research conducted by Roslita (2020), (Wijaya & Amalia, 2020) states that leverage has a negative effect on transfer pricing, while the results of research conducted by Pratiwi (2018) state that leverage has a positive impact on transfer pricing, inversely with the results of research conducted by (Azhar & Setiawan, 2021) which states that leverage does not have a positive effect on transfer pricing. Based on the background described and the differences in the results of previous studies, the researchers are interested in conducting research with the title "The Effect of Leverage and Tunneling Incentives on the Company's Decision to Transfer Pricing ".

Literature Review and Hypothesis Development

Agency Theory

Agency theory was first introduced by Jensen & Meckling. Agency theory arises because a party (principal) assigns a task to another party (agent) to perform a service activity that requires the principal to delegate authority in making decisions (Jensen & Meckling, 1976). The separation of ownership and management functions by management results in an agency conflict in which the agent and principal maximize their function in giving rise to indications that what the agent does is not always in accordance with what is desired, where the manager tries to maximize profits for his interests and makes all means including the transfer pricing policy.

Transfer Pricing

Transfer pricing is a transaction between countries created because of a special relationship between related parties (such as the relationship between a parent company and a subsidiary). It appears for three different purposes from various sides, namely the legal side of the company to strengthen the relationship between the company and its shareholders, managerial accounting to maximize corporate profits and taxation purposes to reduce the tax burden (Sa'diah & Afriyenti, 2021). Based on Article 1 paragraph (8) of the Director-General of Taxes Regulation Number PER-32/PJ./2011, it defines transfer pricing, namely "Pricing in transactions between parties that have a special relationship". Transfer pricing is usually set for intermediate products, goods and services supplied by the selling division to the buying division.

Effect of leverage on transfer pricing decisions

Leverage is a ratio used to measure how much of the assets owned by the company come from debt or capital. It is known as the company's position and obligations fixed to other parties

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and the balance of the value of fixed assets with existing capital (Rahayu, Masitoh, & Wijayanti, 2020). One way for companies to obtain capital that will generate interest expense to reduce the company's tax burden is through leverage. The higher the use of leverage in the company, the greater the tax burden that is avoided (PK Wardani & Kurnia, 2018). Bernard, Jensen, & Schott (2006) argue that companies with high debt-to-equity ratios tend to be tax aggressive than companies with low debt-to-equity ratios. Companies with high debt ratios will try to reduce the tax burden that must be paid so that the higher the level of leverage will make the company's potential for transfer pricing more taken into account (Richardson et al., 2013).

H1: Leverage has a significant positive effect on the company's decision to transfer pricing.

Effect of Tunneling Incentive on Transfer Pricing Decisions

According to Brundy & Siswantaya (2014), the Tunnelling incentive transfers resources in assets and profits by the majority shareholder outside the company. Hartati, Desmiyawati, & Julita (2015) say that tunnelling incentive is a behaviour of majority shareholders who transfer company assets and profits for their benefit but make minority shareholders share the costs they incur. Controlling shareholders tend to explore the benefits of company resources more than pursuing profits from investments without noticing minority parties through tunnelling activities (Rahmawati, 2016). F Noviastika et al. (2016) said that the greater the share ownership by a party, the more likely it is to carry out transfer pricing.

Wafiroh & Hapsari (2016) argue that based on agency theory, the largest shareholders usually have significant participation rights in decision making and can act opportunistically, which causes the emergence of information asymmetry between agents and principals . So it can be concluded that tunnelling incentives are carried out because agency problems are driven by the majority shareholders' desire to receive significant dividends considering that they have included large capital in the company (Pratiwi, 2018).

H2: Tunneling incentive has a significant positive effect on the company's decision to transfer pricing

Methods

In this study, the type of research used is quantitative research. The population used in this study are all consumer goods industrial sector companies listed on the Indonesia Stock Exchange in 2015-2020, with a total population of 41 companies. There is also the determination of the sample in this study is through purposive sampling method using specific criteria, namely:

Table 1. Sample Selection Criteria

No.	Criteria	Sample
1	Companies in the consumer goods industry sector listed on the Indonesia Stock Exchange during the 2015-2020 period	41
2	Companies that do not publish financial statements as of December 31 during the 2015-2020 period in a row	(5)
3	Companies that do not have a share ownership percentage of 20% or more	(6)
4	Availability of data needed in research is not complete	(12)
Total Sample		18

Based on the criteria in the table above, the sample used in this study amounted to 18 companies, then multiplied by six years of observation. The method of collecting data is through the documentation method, which is a method that collects and examines data obtained through the company's financial statements presented on the Indonesia Stock Exchange. The data analysis method used is by using a multiple linear regression test. The data analysis technique used descriptive statistical tests, classical assumption tests, hypothesis testing, and the coefficient of determination test.

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Table 2. Variable Operational Definitions

No	Variable	Indicator	Scale
1.	Leverage (X1)	$\text{DER} = \frac{\text{Total Liability}}{\text{Total Equity}}$	Ratio
2.	Tunnelling Incentive (X2)	$\text{TUN} = \frac{\text{a Total most considerable amount of shareholding}}{\text{Total outstanding shares}} \times 100\%$	Ratio
3.	Good Corporate Governance (X3)	$\text{GCG} = \frac{\text{Total institutional shareholding}}{\text{Total outstanding shares}} \times 100\%$	Ratio
4.	Transfer Pricing (Y)	$\text{TP} = \frac{\text{Related party debt}}{\text{Total Asset}}$	Ratio

Result

Descriptive Statistics

Based on the statistical results in descriptive table 3, it can be seen that leverage occupies the lowest value of 0.188, which is owned by PT. HM Sampoerna Tbk. in 2015. The highest value for the leverage variable is 2,995, which is owned by PT. Unilever Indonesia Tbk. in 2020. Meanwhile, the average value of the leverage variable is 0.99376. The lowest value of the tunnelling incentive variable is 0.258, which is owned by PT. Nippon Indosari Corpindo Tbk. in 2017 to 2020. The highest value of the tunnelling incentive variable is 0.935, which is owned by PT. HM Sampoerna Tbk. in 2015 to 2020. Meanwhile, the average value of the tunnelling incentive variable is 0.66087. The lowest value of the transfer pricing variable is 0.001, which is owned by PT. Mandom Indonesia Tbk. in 2015 and 2020. The highest value of the transfer pricing variable is 0.181, which is owned by PT. Multi Bintang Indonesia Tbk. in 2016. Meanwhile, the average value of the transfer pricing variable is 0.04795.

Table 3. Descriptive Statistic

	N	Minimum	Maximum	Mean	Standard Deviation
Leverage	108	0.188	2,995	0.99376	0.725814
Tunnelling Incentive	108	0.258	0.935	0.66087	0.212162
Transfer pricing	108	0.001	0.181	0.04795	0.052074
Valid N (listwise)	108				

Classical Assumption Test

A normality test was conducted to test whether the regression model of the dependent variable and the independent variable was normally distributed or not through the Kolmogorov-Smirnov Normality Test. Based on the results of the normality test in this study, it can be seen that the regression model is normally distributed because the Asymp value is 0.235.

Multicollinearity Test, This test is run to know whether there is a correlation between the independent variables that can be seen through the value of Tolerance or Variance Inflation Factor. Based on the results of the multicollinearity test, the regression model is free from multicollinearity because all variables have a Tolerance value above 0.10 and a Variance Inflation Factor value below 10.

Heteroscedasticity Test, the purpose of the heteroscedasticity test is to test the

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similarity of the variance of the residuals of observation with other observations through the Spearman's rho correlation test. Test results indicate that the regression model is free from heteroscedasticity. All variables have an unstandardized residual significance value greater than 0.05.

Autocorrelation test, the purpose of the autocorrelation test is to test the correlation between a certain period and the previous period through the Durbin-Watson test . The results of the autocorrelation test indicate that the Durbin-Watson value is 0.656. The value is smaller than the Lower Bound value of 1.5892 and the Upper Bound value of 1.7273. These results suggest that there is a positive autocorrelation in the regression model. Therefore, it is necessary to re-test using the Cochrane Orcutt method by transforming the independent and dependent variables. The results are 1.890, while the Upper Bound value is 1.7273 and the 4- Upper Bound value is 2.2739. The results obtained are 1.7273 < 1.890 < 2.2739, which means no longer autocorrelation in the regression model

Hypothesis Testing

Based on the results of the multiple linear regression analysis in table 4, it is known that the regression equation formed is as follows: TP = -0.157 + 0.049LEV + 0.108TUN +

The coefficient of the multiple linear regression equation can be interpreted as follows:

1. The constant value is -0.157, which indicates that if the value of the independent variable is considered constant, transfer pricing will decrease by 0.157.
2. The leverage variable has a positive regression coefficient of 0.049, which indicates that every 1% increase in debt to capital in the leveraged variable will increase the probability of the company's decision to transfer pricing by 0.049.
3. The tunnelling incentive variable has a positive regression coefficient of 0.108, indicating that every 1% increase in the percentage of share ownership in the tunnelling incentive variable will increase the probability of the company's decision to transfer pricing 0.108.

Table 4. Multiple Linear Regression Analysis Test

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	-157	0.022		-6.752	.000
Leverage	0.049	0.005	0.652	9.982	.000
Tunnelling Incentive	0.108	0.020	0.432	5.375	.000

Partial Test (T-test), The t-value of the leverage variable is 9.982, which is greater than the t-table value of 1.98761. The significance value of this variable is 0.000, which is smaller than 0.05. Thus, the first hypothesis (H1), which states that the leverage variable has a positive and significant effect on the company's decision to transfer pricing, can be accepted.

The t-count value of the tunnelling incentive variable is 5.375, more significant than the t-table value of 1.98761. The significance value of this variable is 0.000, which is smaller than 0.05. Thus the second hypothesis (H2), which states that the variable tunnelling incentive has a positive and significant effect on the company's decision to transfer pricing, can be accepted.

Table 5. Coefficient of Determination Test (R^2)

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.807	0.660	0.645	0.031454

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Based on the table above, it can be seen that the value of R Square is 0.660, so it can be said that transfer pricing as the dependent variable can be explained by the leverage and tunnelling incentive variables of 67% and the remaining 33% are defined by other variables.

Discussion

The effect of leverage on the company's decision to transfer pricing

The results of the multiple linear regression coefficient tests show that the beta value of the leverage variable is 0.049, and the t-value of the leverage variable is 9.982, which is greater than the t-table value of 1.98761, with a significance value of 0.000, which is smaller than 0.05. So it can be concluded that partially the leverage variable has a positive and significant effect on the company's decision to transfer pricing. From the economic aspect, the debt-to-equity ratio shows the ability of the company's capital to fulfil all its obligations to measure the level of the company's financial health. However, this ratio manipulates transfer pricing to avoid tax from the taxation aspect.

The effect of tunnelling incentive on the company's decision to transfer pricing

The results of the multiple linear regression coefficient tests show that the beta value of the tunnelling incentive variable is 0.108, and the t-count value of the tunnelling incentive variable is 5.375, which is greater than the t-table value of 1.98761 with a significance value of 0.000, which is smaller than 0.05. So it can be concluded that partially the tunnelling incentive variable has a positive and significant effect on the company's decision to transfer pricing. The greater the number of shareholdings, the greater the shareholder's control to make various decisions, including transferring pricing through multiple means. One of which is by performing transactions with related parties at unreasonable prices, whether prices are too high or too low.

Conclusion

Based on the results of tests that have been carried out on all research variables in consumer goods industrial sector companies for the 2015-2020 period, the following conclusions can be drawn (1) Leverage (DER) has a significant positive effect on the company's decision to transfer pricing (2) Tunneling Incentive has a significant positive effect on the company's decision to transfer pricing.

There are several limitations to this research. First, the object of this research is Industrial Sector Companies Consumer Goods Registered in IDX 2015-2020. Second, factors are expected to affect transfer pricing, namely Leverage and Tunneling Incentives.

Based on the conclusions above, the researchers put forward several suggestions, including (1)It is recommended to use more samples and extend the observation period to provide more valid results, (2) For users of financial statements, creditors, or potential investors should consider the number of company audit committees that they will aim to reduce the possibility of investing to companies that have the potential to practice transfer pricing, (3) For companies, it is recommended to conduct transactions with third parties special in accordance with the provisions that have been set so as not to harm the other party.

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