

The Effect of Book Tax Difference, Foreign Ownership and Transfer Pricing on Tax Avoidance with Profit Management as Moderating Variables

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ABSTRACT

Purpose — The main objective of this research is to test which is to find out the effect of the book-tax difference, on the other hand, foreign ownership and transfer pricing that is adjusted for tax avoidance, which focuses on the level of profit management which is positioned as an aspect of the moderating variable.

Design/methodology/approach — This study focuses on secondary data in the form of samples from several companies engaged in manufacturing where these companies have been listed on the Indonesia Stock Exchange in the period from 2016 to 2019. The companies sampled in this study amounted to 31 companies for four years, used as a purposive sampling method. The form of data analysis used leads to the Partial Least Square (PLS) method, where it is necessary to use SmartPLS version 3. software.

Findings — The study found that book-tax difference and transfer pricing are essential in avoiding a tax. However, the level of foreign ownership does not affect the level of tax avoidance. The research results regarding profit management variables could be moderated regarding the relationship between book-tax difference and transfer pricing on tax avoidance. However, they cannot relate to the relationship between foreign ownership and tax avoidance practices.

Keywords — book-tax difference, foreign ownership, transfer pricing, tax avoidance, earnings management.

Paper type — Quantitative

INTRODUCTION

Tax revenue must experience a significant increase both nominally and proportionally to the total state revenue. On the other hand, the proportion of taxpayers is still very low compared to the total population of Indonesia. That shows that public awareness of paying taxes is still deficient. As a great power, Indonesia has not been able to raise taxes fairly compared to other developing countries. Indonesia's tax rates have fallen sharply since 2015, according to data from the Ministry of Finance of the Republic of Indonesia. The tax rate hit 13.7% in 2014 but fell further over the next three years. In 2015, Indonesia's tax rate fell to 11.6%, falling again to 10.8% in 2016 and 10.7% in 2017. In 2018, it increased to 11.5%.

However, in 2019, a further decline of 9.76% was seen due to weakening international trade and some central world commodity prices. According to the government of DDTC News, the existence of tax avoidance and the tendency of high levels of informal activities that are not recorded in the tax system are the causes of the suboptimal achievement of Indonesia's tax rates. It cannot be denied that there are differences in interests between the company as a taxpayer and the state as a tax authority in its implementation.

For a company, tax is a burden or expense that reduces the company's net profit. If a company generates high profits, then the income tax that must be paid to the state is also high. As a result, companies may try to keep taxes as low as possible. However, on the other hand, the government needs to increase resources yearly to fund development and governance.

Tax avoidance is an effort to minimize the impact on tax obligations. The technique used is to take advantage of the weakness of tax laws and regulations to reduce the amount of tax paid so that transactions are not taxed. While tax evasion is not unlawful, tax evasion is a complex issue, as many companies can cause government losses if they practice this practice.

One of the tax avoidance methods commonly used in the application of tax laws is the book-tax difference. That is the difference between taxable income under tax laws and pre-taxable income according to accounting standards. Since tax laws and accounting regulations serve different purposes, these differences create opportunities for revenue management and earnings quality for companies. Lestari (2011) states that one way to identify earnings management is to use the book-



tax difference. The underlying logic is that because of the limited freedom of accounting in assessing taxable income, differences in the amount of tax on the books can provide information about management's discretion in accrual accounting.

A study (Hanlon, 2005; Blaylock et al., 2010; Tang and Firth, 2012) found that BTD affects investors' perceptions of income stability. Hanlon (2005) states that investors' expectations for earnings stability and provisions for high BTD firms are reduced because these are investors' "dangerous signs" of earnings and tax management actions. Logically, the ultimate goal of income management and tax management firms is to change or influence tax revenues and expenditures. Since BTD is the difference between book profit and tax profit, this action increases the value of BTD.

According to Rego (2003), the larger the company, the more complex the transactions. That allows businesses to use existing loopholes to evade taxes on any transaction. Multinational companies have more opportunities to avoid taxes than local companies because they benefit from geographic flexibility, allowing them to take advantage of differences in tax rates across countries through revenue and cost bias (Ragayu, 2009). One way to avoid taxes is to shift profits to countries with lower tax rates to reduce tax arrears.

Empirical studies on the effect of foreign ownership structure on tax avoidance have been conducted in several countries, including Grubert and Mutti (1991), Hines Jr. and Rice (1994), and Kinney and Lawrence (2000). They show that US multinationals are more profitable but pay lower taxes in developing countries. Huizinga and Nicodem (2006) found that firms with high levels of foreign ownership also have higher tax rates. Egger, Eggert and Winner (2010) and Demirguch Kunt and Heizinga (2001) find that tax avoidance rates are higher in most foreign-owned firms. Foreign investors want to invest in foreign countries that offer tax incentives. For example, European countries have high tax rates (Huizinga & Nicodème, 2006).

According to estimates, the Finance Ministry's Tax Directorate (DGT) Suryo Utomo disclosed tax evasion that cost the country 68.7 trillion rupees of loss. The Tax Justice Network published results published in November 2020 based on Indonesia's total corporate tax evasion losses of 68.7 trillion rupees (67.6 trillion rupees) based on this figure. While the remaining Rp 1.1 trillion comes from individual taxpayers. According to the fix, the tax authorities should take steps to minimize tax evasion by tracking transactions related to specific transactions. This tax avoidance is mainly caused by transactions between domestic and foreign related parties, or transactions commonly referred to as transfer pricing practices. Pre-pricing practices take into account value opportunities that can increase personal income and encourage tax avoidance. The company's transfer pricing mechanism is to minimize taxes by distributing profits to countries with lower tax jurisdictions or risk levels. A former senior fellow at the Brookings Institution argues that almost all multinational companies use transfer pricing to move their profits worldwide at will (Baker, 2005).

Of course, from the government's point of view, this transfer pricing practice can potentially reduce the government's tax revenues as multinational corporations shift their tax obligations, lower selling prices between entities in the same group, and transfer profits to businesses. They live in a country with customs—much lower taxes. The public rarely sees Transfer pricing mobilization for tax avoidance, and it is challenging to detect regulators. It is a very complex game that can be played by various parties, including the businesses themselves, accountants, lawyers, consultants, governments, and tax authorities, who are involved in setting and modifying the game's rules. Development of ways to make prices acceptable and manipulate existing rules. Ernst and Young (2006) argue that transfer pricing continues to be one of the most important international tax issues facing MNCs. Measuring tax avoidance is very difficult because data on tax payments can be found in

Notification Letters (SPTPPH) are confidential and complex to obtain directly from the field. Therefore, we use an indirect approach to measure tax avoidance. There are several ways to measure tax avoidance, and one of them is to calculate the difference between pretax profit and taxable income. However, in previous studies, the existence of an earnings management system was only examined using the difference. An earlier study by Sundvik (2017) et al., published in

Nordic Tax Journal states that companies manage their profits to change the tax rate applied. In addition, Tang (2015) found that a high level of consistency in accounting and tax and financial reporting is closely related to a lack of earnings management efforts and tax avoidance. Therefore, it can be concluded that earnings management is applied as part of the company's efforts to avoid proper tax payments and minimize tax obligations (Sommerman and Goncharov, 2004).

This study has several objectives, which include examining the effect of book-tax differences on tax avoidance, examining the effect of foreign ownership on tax avoidance, examining the effect of transfer pricing on tax avoidance, examining the effect of earnings management in moderating the relationship between book-tax differences and tax avoidance, to examine the effect of earnings

management in moderating the relationship between foreign ownership and tax avoidance, to examine the effect of earnings management in moderating the relationship between transfer pricing and avoidance. Tax (tax avoidance).

METHOD

The method used in this research leads to qualitative research, where a hypothesis is tested. The type of method used is the method that leads to the explanatory survey method. The explanatory survey is a method that is carried out by exploring problem situations that focus on finding ideas or insights into the problems that must be solved that are faced by the management or researchers (Maholtra, 2010). This method was chosen due to the existence of a hypothesis that needs to be tested for truth. This study has three kinds of variables: the dependent, independent and moderating variables. The technique used in collecting data in this study was documentation steps based on information from annual reports on a company that the IDX has published through the Indonesia Capital Market Directory (ICMD). On the other hand,

FINDINGS AND DISCUSSION

FINDINGS

Variable Descriptive Analysis

The hypothesis of this study was tested using multiple regression models, to obtain a comprehensive picture of the effect of the explanatory variables, namely accounting taxes, foreign ownership, and transfer prices, on the dependent variable. That is tax evasion. There are other goals, too. That is, to get a picture of the effect of the explanatory variable on the dependent variable, which is adjusted to earnings management.

Table 1. Descriptive Test Results

	mean	Min	Max	Standard Deviation
FOR	0.659	0.294	0.998	0.178
BTD	0.024	-0.066	0.274	0.054
TP	0.190	0.000	0.963	0.273
ETR	0.285	0.092	0.839	0.099
DAC	-6.882	-15,461	6.606	3.043

Source: must be written.

As a result of the analysis of the difference between the balance sheet variables, which is measured by dividing the amount of accounting profit minus corporate tax income by total assets for the year, the average value of the balance sheet difference between the 128 data that can be processed is 0.024. smallest value (Minimum) Has 0.066 PT. 2017 Charoen Pokfand Indonesia Tbk and PT. 2018 Merck Tbk.

PT. 2017 Mark Dynamics Indonesia Tbk owns the most significant (maximum) balance tax difference of 0.274. Transfer prices are measured using a formula that divides trade receivables for certain parties by total trade receivables. The previous pricing results have a mean of 0.190 and a standard deviation 0.273. The smallest (minimum) value produced is 0.000, belonging to PT. Wire and Cable KMI 2016 Tbk. While PT. 2019 Surya Toto Indonesia Tbk owns the largest (maximum) value of 0.963.

The control variable, the earnings management variable, is calculated with discretionary accruals based on the modified Jones model. The results of the calculation of earnings management provide a standard deviation of 3,043 and an average value of 6,882. The smallest value (minimum) is 15,461 PC results. Nippon Indosari Corpindo Tbk has a maximum of \$6,606 owned by PT in 2016. 2017 Nusantara Inti Corpora Tbk.

Partial Least Square (PLS) Analysis

The software uses software developed at the University of Hamburg named SmartPLS version 3.3.3. There are two stages of data processing in this software. The first step is to evaluate the external model or measurement model. The second step is to evaluate the internal model or structural model. The measurement model consists of observable indicators.

Evaluation of the Measurement Model (Outer Model)

The measurement, or external model, shows how each indicator block relates to the hidden variable. Evaluation of the measurement model using confirmatory factor analysis using the MTMM (MultiTraitMultiMethod) approach by testing convergent and discriminant validity. The reliability test was carried out in two ways, namely using Cronbach's Alpha and Composite Reliability (Ghozali & Latan, 2015).

Convergent Validity (Convergent Validity)

Convergent Confidence aims to determine the reliability of each relationship between indicators and hidden variables. The validity of the convergence of the measurement model with reflective indicators is evaluated based on the correlation between factor or component scores and hidden variable scores or construct scores calculated using PLS.

Table 2. Outer Loading Results

	BTD	DA*BT	DA	ETR	KA	DA*KA	TP	DA*TP
BT	1,000							
BT *		1.071						
DA			1,000					
DA				1,000				
ET					1,000			
ET						1,249		
KA *							1,000	
KA								1.309
TP								
TP *								
DA								

The table above describes each indicator's factor loadings (convergence confidence). It can be said that the factorial load value > 0.7 is considered valid, but the rules for interpreting the factorial load value > 0.5 are valid. From this table, it can be seen that the factor loading values for the metrics of Tax Difference (X1), Foreign Owned (X2), Transfer Prices (X3), Tax Avoidance (Y), and Earnings Management (Z). all equal to greater than 0.7. That indicates that the metric is considered valid. The next convergent validity test looks at Cronbach's alpha and synthetic reliability. The results can be seen in the following table.

Table 3. Cross Loading Results

	Cronbach's Alpha	rho_A	Composite Reliability	Average Variance Extracted (AVE)	R Square	R Square Adjusted
BT	1,000	1,000	1,000	1,000		
DA	1,000	1,000	1,000	1,000		
DA*BT	1,000	1,000	1,000	1,000		
DA*KA	1,000	1,000	1,000	1,000		
DA*TP	1,000	1,000	1,000	1,000		
KA	1,000	1,000	1,000	1,000		
TP	1,000	1,000	1,000	1,000		
ET	1,000	1,000	1,000	1,000	0.418	0.383

Cronbunch alpha and composite confidence values greater than 0.7 indicate high reliability of the measurement tool, which means that the performance of each design is highly correlated. The third check for convergent validity is checking the AVE value. Values greater than 0.5 are considered to have reached the AVE. The table above shows that all designs have an AVE value greater than 1.00 or 0.5.

Discriminant Validity

Discriminant validity proves that the latent construct predicts block size better than other blocks. The discriminant validity of the measurement model with reflex measurement was evaluated based on the cross load of the construct and measurement.

Table 4. Cross Loading Value

	BTD	DA	DA*BTD	DA*KA	DA*TP	ETR	KA	TP
BTD	1,000	-0.181	0.180	0.150	-0.104	-0.239	0.034	-0.265
DAC	-0.181	1,000	-0.362	-0.220	0.115	0.329	-0.278	0.206
BTD * DA	0.180	-0.362	1,000	0.332	-0.525	-0.208	0.175	-0.127
KA * DA	0.150	-0.220	0.332	1,000	-0.571	-0.357	0.054	-0.156
TP * DA	-0.104	0.115	-0.525	-0.571	1,000	0.498	-0.149	0.308
ETR	-0.239	0.329	-0.208	-0.357	0.498	1,000	-0.168	0.427
FOR	0.034	-0.278	0.175	0.054	-0.149	-0.168	1,000	-0.067
TP	-0.265	0.206	-0.127	-0.156	0.308	0.427	-0.067	1,000

Based on the cross-load results, all indicators correlate with each contract. Cross-loading describes how strongly the indicator affects each hidden variable (configuration). For example, for the BTD indicator, the most significant correlation value is in the hidden variable BTD. Similarly, the FOR indicator shows that the externally held variable (KA. Thus, the latent construct predicts its indicator better than other hidden indicators.

Evaluation of the Structural Model (Inner Model)

After verifying the measurement model, the next step is to validate the structural model. This study includes the significance of the path ratio and R-squared (R2) to see the results of evaluating the significance of the structural model, especially the control variables. The structural model was evaluated using the significance of the structural path parameter coefficients and R-square for the dependent t-test construction.

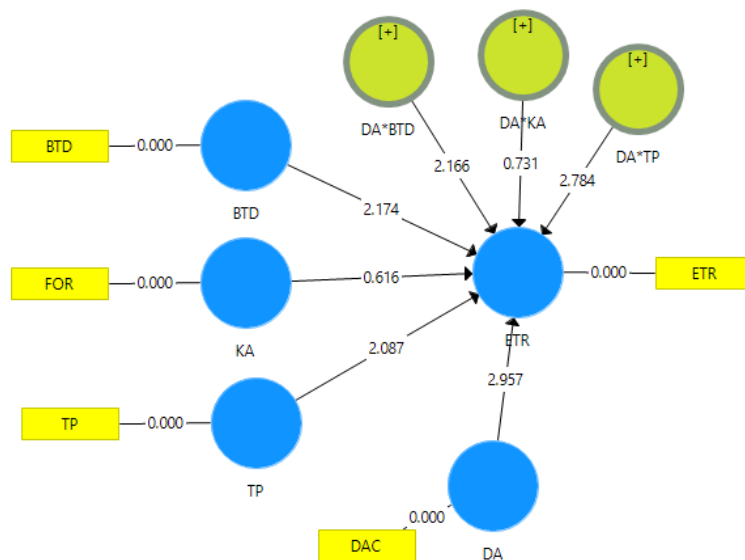


Figure 1. Structural Model (Inner Model)

R-Square

Table 5. R-Square. Value

Variable	R2
ETR	0.418

Source: Data processing with PLS, 2021

Table 5 shows that the Rsquare value for the tax avoidance variable is 0.418. The R-square value shows that 41.8% of the tax avoidance variable can be influenced by foreign ownership, differences in tax accounting, transfer pricing and earnings management as mediators. Other variables outside the study influence the remaining 58.2%.

Predictive Relevance (Q)

According to Jaya and Sumertajaya (2008), the fit quality model is measured as a quadratic latent variable with the same interpretation as regression. It measures and estimates the predictive relevance of QSquare to the structural model and how well the model generates conservation value. The value of Q2 is 0 & lt; <i>Q2</i> 1, where the closer to 1, the better the model. The magnitude of Q2 is equal to the total coefficient of determination from path analysis.

Based on 7, the calculation of predictive relevance is as follows.

$$Q2 \text{ value} = 1 - (1 - R2)$$

$$Q2 \text{ value} = 1 - (1 - 0.418)$$

$$= 0.418$$

Information :

Q²: score *Predictive Relevance*

R₁₂: Score *R-Square Tax Avoidance variable*

From the results of these calculations, it can be seen that the Q2 value is 0.418, and the value of the diversity of research data that can be explained using the structural model developed is 41.8% and the remaining 58.2%. —other factors outside the model.

Research Hypothesis Testing

Table 6. Path Coefficient (Mean, STDEV, T-Values)

	Original Sample (O)	T Statistics (O/STDEV)	P Values	Information
BTD -> ETR	-0.113	2.174	0.030	Significant
KA -> ETR	-0.041	0.616	0.538	Not significant
TP -> ETR	0.217	2,087	0.037	Significant
DA -> ETR	0.261	2,957	0.003	Significant
DA*BTD -> ETR	0.186	2.166	0.031	Significant
DA*KA -> ETR	-0.040	0.731	0.465	Not significant

Source: Data Processing With PLS, 2021

The structural equations obtained are:

$$Y = -0.113X1 - 0.041 X2 + 0.217 X3 + 0.186 M1 - 0.040 M2 + 0.351 M3$$

Based on the table above, it can be seen that the balance tax difference and transfer price have statistical significance of 2.174 and > 1.960 for the transfer price, respectively. The significance shown by the statistical value of foreign ownership is only 0.616, indicating that the statistical value of " When foreign ownership does not affect tax avoidance 1960 Also, in this study, earnings management does not reduce the relationship between foreign ownership and tax avoidance, but can lighten the relationship between balance sheet tax differences and transfer prices in tax avoidance. Therefore, it can be said that if a company manages earnings, it does not affect foreign ownership regarding tax avoidance.

DISCUSSION

First Hypothesis: Book-Tax Difference Has Positive Effect on Tax Avoidance

SmartPLS analysis shows that BTD positively and significantly affects tax avoidance practices through statistics $t > t$ table 1.96 (2.174 > 1.96). That can be seen in the t-statistic of 2.174, which means that the composition of BTD affects the composition of tax avoidance. In other words, companies that maintain tax and commercial financial statements can demonstrate tax avoidance practices. However, the results of the original sample indicate that the direction of the relationship between tax accounting and tax avoidance is negative. Therefore, the results of this study reject the first hypothesis that tax accounting differences have a positive (+) effect on tax avoidance behaviour.

Second Hypothesis: Foreign Ownership Positively Affects Tax Avoidance

According to research by Anthony and Govindarajan (2009), an agency relationship occurs when the owner hires an agent to empower the agent to make decisions. The existence of a difference in desire between the master and the agent is the cause of the agent's problems. The more shares owned by foreigners in a company, the greater the voting rights of investors in determining company policies. Investors invest in companies that they believe can provide returns that meet expectations.

Therefore, in the case of companies with high foreign ownership ratios, it is also possible to minimize the tax burden caused by the policy decisions of foreign companies. However, from processing the data, it is seen that foreign ownership does not affect tax avoidance practices. The t-test value was obtained at 0.538, resulting in a statistic of "Value to ensure that foreign ownership designs do not affect tax avoidance practices. We can say that the second hypothesis is rejected. That means that companies with more foreign ownership have no effect in minimizing the company's tax burden. Tax evasion. Tax.

Third Hypothesis: Transfer Pricing Has a Positive Effect on Tax Avoidance

The analysis results using SmartPLS show that transfer prices have a positive and significant effect on tax avoidance behaviour with a statistical value of $t > t$ in Table 1.96 ($2.087 > 1.96$). That can be seen from the t-statistic 2.087, which means that the transfer pricing design affects the tax avoidance design. This analysis indicates that companies that use transfer pricing increasingly encourage tax avoidance. It can be said that the third hypothesis is accepted.

Hypothesis testing shows that transfer pricing affects tax avoidance, so the relationship between companies and the state creates different interests in paying corporate taxes. The emergence of transfer pricing policies when determining transfer prices for third-party transactions is often used by multinational companies to seek profits to avoid large amounts of taxes from the country. Transfer pricing practices are usually carried out between companies in a relationship and are often used by multinational companies. Several reasons underlie what companies do when doing transfer pricing.

In political cost theory, tax is a coercive property that forces the government to pay taxes to multinational companies, which forces companies to pay taxes according to the taxes imposed by the government. Transfer pricing is one way that companies often use tax payments to pay minimum taxes (Indriaswari, 2017).

Fourth Hypothesis: Earnings Management Moderates The Relationship Between Book Tax Difference and Tax Avoidance

SmartPLS analysis shows that earnings management can bridge the relationship between the balance sheet tax gap and tax avoidance practices. The t statistic is 2.166, greater than the t table (1.960). The results of this analysis indicate that H4 has been adopted, which indicates that earnings management has a significant effect on the relationship between the tax balance gap and tax avoidance practices.

Earnings management can be defined as intentionally interfering with the intent or purpose of the financial reporting process for personal gain. Scott (2006) states that earnings are managed for several reasons, such as target bonuses, contract incentives, political incentives, tax incentives, CEO replacement, IPOs and investor communication. Earnings management with a tax motive uses the difference between accounting rules and tax rules (tax accounting differences) so that the company can pay the minimum amount of tax.

Fifth Hypothesis: Earnings Management Moderates The Relationship Between Foreign Ownership and Tax Avoidance

The analysis results using SmartPLS show that revenue management is a t-statistic & lt; Table 1.96 ($0.731 & lt; 1.96$). That can be seen from the t-statistic of 0.731, which means that the earnings management design cannot mitigate the relationship between the concept of foreign ownership and the concept of tax avoidance. The results of this analysis found that in the case of companies that have equity, it is difficult for companies to avoid taxes even though there is intervention from management. It can be said that the fifth hypothesis is rejected.

Sixth Hypothesis: Earnings Management Moderates The Relationship Between Transfer Pricing and Tax Avoidance

The analysis results using SmartPLS, the statistical value of $t > t$ in Table 1.96 ($2.748 > 1.96$), show that earnings management can control the relationship between transfer pricing and tax avoidance. That can be seen from the t-statistic of 2.748, which means that the composition of earnings management loosens the relationship between the composition of transfer pricing and tax avoidance. This analysis indicates that companies that use transfer pricing increasingly encourage tax avoidance. We can say that the hypothesis has been accepted.

CONCLUSION

Conclusion

The difference in Booktax is measured by using the difference between accounting profit and tax profit divided by total assets; the results of this variable have a significant effect on tax avoidance practices, and the results of this study are in line with the results of research from Jackson (2015).

Foreign share ownership is symbolized by FROWN by using the division between the number of shares owned by foreign parties and outstanding shares. This analysis shows that foreign ownership has no significant effect on tax avoidance practices. The results of this study are not in line with research from Shackelford and Shevlin (2001) and research from Rusyidi and Martani (2014). However, this study's results align with Hadi and Mangothing (2014) and Sissandhi (2014).

The transfer price is calculated using trade receivables divided by the total trade receivables for certain parties. The results of statistical analysis have a significant effect on tax avoidance. This research is in line with the research of Maulana (2018) and Herianti & Chairina (2019) that the existence of transfer pricing affects tax avoidance.

The effect of earnings management on the relationship between tax avoidance and balance sheet differences, measured as discretionary accruals obtained by dividing total accruals by total sales, has a statistically significant effect. The results of this study support the results of Desai (2006) and Kristanto (2015).

The effect of foreign-owned earnings management on tax avoidance practices as measured by discretionary accruals obtained by dividing gross accruals by gross sales. The results show that there is no statistically significant effect. This research is not in line with the research of Idzni and Purwanto (2017). However, this study is consistent with the research of Chung et al. (2004) and Alzoubi (2016), which state that increased knowledge of accounting and corporate governance, reinforced by all foreign investors, allows firms to control their financial reporting and operating activities. Suitable. More effective. Effective.

The effect of earnings management on the relationship between transfer pricing and tax avoidance, measured as discretionary accruals obtained by dividing total accruals by total sales, has a statistically significant effect. This study's results align with the research of Masna (2018) and Gusnardi (2019).

Suggestion

By using earnings management as a control variable, research to extend or extend the research period is needed to provide conclusions that can more accurately describe the effect of differences in tax balances, foreign ownership, and transfer prices on tax avoidance. To get more accurate findings, we recommend further research by comparing the types or sectors of all companies listed on the Indonesia Stock Exchange. Because the significance of the balance sheet tax difference is vast and the scope of using a proxy for the balance sheet tax difference is also vast, further research is encouraged to add controlled variables. Further research is suggested to add other variables of share ownership, such as institutional ownership or managerial ownership, because these ownerships are very important in the company's management, and the results may differ from the effect of foreign ownership.

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