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Research Article

The Relation Between Multinationality and Tax Haven on Transfer Pricing: Moderated by Institutional Ownership

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Abstract: This study aims to analyze the influence of multinationality and tax haven utilization on transfer pricing activities, with institutional ownership as a moderating variable. The research focuses on energy sector companies in Indonesia, using 70 data samples obtained from company reports and financial statements. Regression analysis with moderation was employed to test the hypotheses. The findings reveal that both multinationality and tax haven practices significantly influence transfer pricing activities. However, institutional ownership does not moderate the relationship between multinationality and transfer pricing but does moderate the relationship between tax haven and transfer pricing. These findings indicate that multinational expansion and the use of tax havens play an essential role in determining corporate transfer pricing behavior. Furthermore, the presence of institutional ownership strengthens the influence of tax haven utilization on transfer pricing practices, showing that ownership structure affects how companies manage their tax-related strategies. This research contributes to a better understanding of the determinants of transfer pricing in multinational enterprises and offers practical implications for policymakers in designing effective tax regulations and governance standards related to corporate taxation.

Keywords: Institutional Ownership; Multinationality; Regression Analysis; Tax Haven; Transfer Pricing

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1. Introduction

Companies are expanding their business abroad because of limitations and fierce competition in the domestic market. This business expansion allows companies to gain access to new consumers and expand their market share. Some companies in Indonesia choose to open branch companies abroad to get low production costs or obtain more favorable tax rates. The mechanism commonly used by companies is to conduct transfer pricing. This transfer pricing allows companies to allocate costs and profits between connected entities within the group of companies more efficiently. That way, companies can control costs in various parts of their organization and maximize overall results, including allocating production costs.

The selection of a destination country for the company to expand is not only based on production costs, but also related to the tax rate regulations that apply to the destination country. The company's main strategy is to maximize global profits and minimize tax liabilities by placing its affiliates in countries with low tax rates (Tax Haven). These strategies often involve complex tax avoidance mechanisms, which can ultimately result in a loss of revenue for the countries of origin of the tax (Vicard, 2015).

Based on data presented by the Directorate General of Taxes (DGT) in 2022, corporate income tax revenue (Corporate Income Tax) has a contribution of 20% of total tax revenue (including Oil and Gas Income Tax), while that which comes from individual taxpayers is only 0.67%. This tax revenue structure indicates that Indonesia is highly dependent on corporate tax. This structure is the opposite of the tax revenue structure in OECD countries. In OECD countries, individual taxpayers are more prominent tax contributors than corporate taxpayers, which is 20% of total tax revenue, while corporate taxpayers only contribute 10%. Likewise, Carnahan stated that most taxpayers are aware of their obligations, but only 25% of countries are successful in collecting taxes, while Asia Pacific countries perform worse (Carnahan, 2015). In addition, de Mooij & Liu (2020) stated that transfer pricing regulations caused an 11% decrease in investment by MNC affiliates. This difference in structure ultimately resulted in a low tax ratio in Indonesia compared to OECD countries. Another problem that arises due to the state's dependence on corporate taxpayers is the behavior of companies to reduce taxes, one of which is the transfer pricing mechanism (Liu et al., 2017).

According to a CNBC Indonesia report in 2019, a case of transfer pricing practices carried out by PT Adaro Energy Tbk, a multinational company in Indonesia, was revealed. According to a report by Global Witness, the company is using a strategy involving its subsidiary in Singapore, a jurisdiction with relatively low tax rates, to reduce its tax liability in Indonesia. The case study, published in a leading scientific journal, shows the tendency of multinational companies operating in Indonesia to adopt more aggressive transfer pricing strategies when engaging in cross-border transactions with countries with low tax rates. Optimizing organizational profits through transfer pricing, impacting the competitive advantage and market share of multinational companies (Gao & Zhao, 2015).

Transfer pricing can also be used for dishonest and unlawful purposes, such as tax avoidance through deliberate manipulation of transfer prices, including overcharging and undercharging in transfer pricing transactions. To ensure that the transfer fees paid by companies are equivalent to the transfer fees between unrelated businesses, the government relies primarily on arm's length pricing (Kumar et al., 2021). Multinational corporations often use their size and complexity to manipulate internal transfer prices and shift profits from high-tax jurisdictions to low-tax jurisdictions, thereby lowering their overall tax liabilities; transfer pricing choices can have a significant impact on developing countries' tax revenues (Choi et al., 2020). Thus transfer pricing by multinational corporations shifts income to low-tax countries, leading to tax base problems and international imbalances (Vicard, 2015). Meanwhile Muhammadi et al. (2016) stated that the transfer pricing audit of intangible assets presents various problems for Indonesian tax auditors. The findings of the case related to transfer pricing indicate the need for serious government efforts, such as tightening supervision and conducting more law enforcement, to anticipate the negative impact of transfer pricing. This activity's negative impact can reduce state tax revenue, resources available for state development, and social programs and services to the community.

Previous research has looked at various aspects of transfer pricing. The sensitivity of income tax rate differences decreases with tighter transfer pricing (Marques & Pinho, 2016). Several related studies have identified factors that influence transfer pricing behavior, such as corporate multinationalism and the use of tax havens. Research has also explored the role of institutional ownership moderation variables in the Relationship. Previous research (Janský & Prats, 2015) multinational companies with ties to tax havens report lower profits and lower asset taxes, thereby eroding the tax base. Transfer pricing aggressiveness is still limited. However, the capacity of the tax authorities is likely to influence transfer pricing (Nguyen et al., 2019). While Richardson & Taylor (2015) states that there is a positive correlation between multinationalism, thin capitalization, aggressive transfer pricing, intangible assets, and the use of tax havens with listed US multinationals, indicating a profit shifting strategy. Therefore, this study will complement the existing literature by analyzing these factors and their Relationship with transfer pricing behavior in the.

This study aims to investigate the impact of multinationalism and the use of tax havens on transfer pricing practices by considering the role of institutional Ownership in multinational companies operating in the energy sector in Indonesia. The focus is to identify and understand how multinationals affect transfer pricing practices by tracing the tendency of multinational companies to implement transfer pricing strategies based on geographic scope and the type of business they have. In addition, this study also analyzed the influence of the use of tax havens in transfer pricing practices to determine whether companies tend to take advantage of jurisdictions with low tax rates in their business transactions. By examining the role of institutional Ownership, it can be seen whether institutional investors play a significant role in strengthening corporate decisions and practices related to transfer pricing in multinational companies operating in tax haven countries. This analysis can provide insight into how institutional Ownership can influence transfer pricing strategies and provide an understanding of the broader dynamics of corporate governance, regulatory compliance, and shareholder influence in multinational contexts.

2. Literature Review

Positive Accounting Theory

Positive accounting theory is an accounting theory introduced by Watts and Zimmerman (1978). According to Watts & Zimmerman (1990), positive accounting theory is a theory that explains a process by using understanding, ability, and knowledge of accounting in accordance with accounting policies to deal with certain conditions in the future. Positive accounting theory is characterized by problem solving that is adjusted to the reality of accounting practices. Positive accounting theory in principle assumes that the purpose of accounting theory is to explain and predict accounting practices.

The approaches used in positive accounting theory are economic and behavioral approaches. The economic approach relates to the costs and benefits of using accounting methods in terms of submitting financial statements, as well as the impact of financial reporting results on the internal and external of the company in terms of economics. The behavioral approach relates to management who have the freedom to choose various alternatives from existing accounting policies in terms of submitting financial statements (Godfrey & Parker, 2010).

Financial reporting depends on management decisions. Management decisions are influenced by management's understanding of the applicable accounting policies. Therefore, the selection of accounting policies used for financial reporting is influenced by management decisions. With positive accounting theory, management as policy makers can predict the economic consequences of various accounting practice policies that they implement.

Positive accounting theory has a concept known as the political cost hypothesis. According to Watts & Zimmerman (1990), this political cost hypothesis indicates that large companies often choose accounting methods that reduce their earnings reports compared to smaller companies. In addition, Godfrey & Parker (2010) added that the main goal of positive accounting theory is to explain the opportunistic behaviors that companies may engage in when they choose a particular accounting policy. In this context, the political cost hypothesis implies that the higher the political costs that a company has to bear, the more likely it is that the company's managers will choose accounting policies that may affect the recognition of their income or expenses, especially in order to optimize tax withholding or delay the recognition of income

Transfer Pricing

Transfer pricing is a policy made by the company to determine transfer prices for goods, services, intangible assets, and financial transactions. Transfer pricing can be done intra-company (within a company in the same country) and inter-company (the same company in a different country). Transfer pricing is initially an activity in management accounting, which is the delivery of goods or services between departments in a company to measure the performance of each department. Along with the development of the times, transfer pricing is also used by multinational companies that previously implemented decentralization of operations, as a tool to minimize operating costs and to minimize the tax burden borne by the company (Kalra & Afzal, 2023). Transfer pricing is a practice carried out by companies by shifting their income from countries with high tax rates to countries with lower tax rates, thereby reducing the company's tax bill. Companies can also increase operational costs to reduce the taxes owed. This is also called transfer pricing manipulation. Companies can manipulate the selling price, purchase price, allocation of administrative costs, interest charges on loans given by shareholders, commission payments, licenses, franchises, rent, royalties, compensation for management services, compensation for technical services, and compensation for other services, etc. Transfer pricing is a complex concept that determines the price of goods and services exchanged between related entities, particularly subsidiaries of multinational corporations (MNCs). Transfer pricing involves setting prices for these transactions, which can affect profit allocation and tax liabilities across jurisdictions (Kalra & Afzal, 2023). In various countries, transfer pricing is indeed legal for companies to do. However, this technique is often used by rogue companies to avoid tax bills that must be paid by the company.

The Relationship Between Multinational and Transfer Pricing

Corporate multinationalism is a strategy for companies to expand their market share and obtain resources at a lower cost. By setting up subsidiaries in different countries, companies can look for opportunities to enter international markets that have high demand for the company's products and services. Setting company subsidiaries in different countries allows the company to grow faster and increase revenue from a broader market. Multinational corporations often face challenges related to tax compliance in different countries, and transfer pricing practices are often used by multinational corporations to allocate profits between corporate entities located in different countries.

Corporate multinationalism can give rise to transfer pricing because of transactions between internationally connected companies and corporate entities in different countries. A company's multinationalism allows companies to take advantage of differences in tax policies between countries and flexibility in regulating transaction prices between subsidiaries to minimize their tax liabilities. According to positive accounting theory, corporate multinationalism creates opportunities for companies to reduce tax burdens and maximize global profits. The decision to carry out transfer pricing is based on rational decision-making, where companies use the transfer pricing mechanism to move profits from countries with high tax rates to countries with low tax rates. Thus, companies can make greater profits in countries with lower tax rates. This problem causes multinational companies to carry out aggressive transfer pricing actions (Richardson et al. (2013), Huu Anh et al.(2018), Dinca & Fitriana (2019)). Therefore, we propose a positive relationship between the characteristics of the multinational and the level of aggressiveness of the company's transfer pricing.

H1 : Multinational has a positive influence on company transfer pricing

The Relationship Between Tax Haven and Transfer Pricing

As a rational entity, the company has the desire to increase the profits it earns. One of the legal ways that companies can use it is to set transfer prices between company entities that are located in areas with low tax rates. Companies will tend to place their company in a tax haven country, especially if the company's home country has a high tax rate. Thus, the company will transfer its profits to corporate entities in tax haven countries, which often have low or even zero tax rates. Thus, the company will be able to reduce its overall tax burden.

In the political cost hypothesis, high tax rates also lead to high political costs. The company has to pay a large amount of taxes, which causes the company's profits to be smaller. The higher amount of taxes the company should pay gives rise to an incentive for companies to allocate their profits to tax haven countries as their tax hideouts Atwood & Lewellen (2019) and Lewellen et al. (2021).

The abuse of tax haverins is supported by the absence of the need to have substantial activities in the country when setting up a company, the lack of transparency of information, and difficulties in exchanging information with other tax authorities. The lack of tax regulation makes multinational companies conducting transactions with tax haven countries carry out aggressive transfer pricing. Therefore, we propose a positive relationship between companies that establish branch companies in tax haven countries and corporate transfer pricing (Huu Anh et al., 2018).

H2 : The existence of companies in tax haven countries has a positive effect on transfer pricing

The Relationship of Institutional Ownership Moderation on Mutitnationality to Transfer Pricing

Institutional Ownership refers to the Ownership of shares by large entities such as investment companies, insurance companies, and other institutions. Institutional Ownership in a company can affect the company's behavior in relation to transfer pricing. Institutional Ownership within a company has a greater capacity to exercise supervision and control over the company's decisions, including the placement of subsidiaries abroad. In companies with more extensive institutional Ownership, the influence of multinationals tends to be limited to transfer pricing. Institutional Ownership will put more emphasis on companies to comply with regulations and reduce companies from aggressive transfer pricing—studies show that institutional Ownership significantly impacts corporate tax policies. The study concluded that institutional Ownership tends to reduce aggressive taxation practices (Hanlon & Heitzman, 2010).

H3 : Institutional Ownership Weakens the Relationship Between Multinationals and Transfer Pricing

The Relationship of Institutional Ownership Moderation in Tax Havens to Transfer Pricing

The existence of institutional investors in the company pays more attention to regulatory compliance and the long-term sustainability of the company. Institutional Ownership is a limitation on the use of tax havens in the transfer pricing strategy of multinational companies. Companies with institutional investors tend to use more conservative transfer pricing and be cautious in shifting profits to companies in tax haven countries. Therefore, companies with high institutional Ownership will adopt tax policies that are more legitimate and transparent and avoid actions that risk the sustainability of the company's business.

H4 : Institutional Ownership weakens the relationship between tax haven and transfer pricing

3. Research Method

This quantitative research focuses on analyzing data in numbers to produce conclusions. The data source used in this study is secondary data obtained through the annual reports of energy companies listed on the IDX for the period 2019 to 2023. Samples were obtained using the purposive sampling method with the following criteria: 1. Energy companies listed on the IDX in the period 2019 to 2023, 2. Companies have branches abroad during the observation period, 3. Companies have transaction data with parties who have special relationships. The analytical tool used to answer the hypothesis formed is regression analysis with moderation.

The variables used in this study consisted of Transfer pricing as a dependent variable, multinationality and tax heaven as independent variables, and institutional Ownership as a moderation variable. Explanations related to variables are explained in the following table:

Table 1. Variable Operational Definition

Variable Type	Variable Name	Formula
Dependent.	Transfer pricing aggressiveness	$= \left(\frac{Total\ receivables\ from\ related\ parties}{Total\ receivables}\right)$
Independent	Multi Nationality	$= \frac{Total\ number\ of\ foreign\ subsidiaries}{Total\ subsidiaries}$
Independent	Tax Haven	Dummy variable 1 if the company has at least one related party in a tax haven country transacting with the company. If not, then it is declared 0.
Moderation	Institutional Ownership	$Z = \left(\frac{Total\ institutional\ shares}{Total\ outstanding\ shares}\right) X\ 100\%$

4. Results and Discussion

This research was conducted with an object on energy sector companies on the Indonesian stock exchange in the period 2019 – 2023. Based on the criteria determined, as many as 70 data were obtained used in the observation. The data obtained has a description of the data as shown in the following table:

Table 2. Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
Transfer_Pricing	70	.000001156344141	1.000000000000000	.176108173358349	.242506471744003
Multinationalitas	70	.035714285714286	1.000000000000000	.308178514788682	.285538941415712
taxHaven	70	0	1	.87	.337
KepInstitusional	70	.100000000000000	.898000000000000	.542331428571428	.234249414051427
Valid N (listwise)	70				

Based on the table above, it is known that all data have a low data variance which can be seen from the standard deviation value that is lower than the average value. The data obtained has been confirmed to have met classical assumptions, so the test results do not show bias. The results of the model test showed a significant value in the F test of 0.00 with an adjusted r square value of 0.361. Based on these values, it can be said that the model that is formed is fit to be used to prove the hypothesis.

Table 3. Hypothesis testing

Multi →TP	B = 0.333	sig = 0.000	Influential +
TH → TP	B = -0.256	sig = 0.001	Influential-
Multi_KepIn → TP	B = -0.865	sig = 0.09	Not Moderation
TH_KepIn → TP	B = -0.992	sig = 0.002	Moderate (weaken)

In Table 3 above, it is known that multinationalism has a positive effect on transfer pricing. So, hypothesis 1 is accepted. The result can be interpreted as multinational companies being more likely to set transfer prices. By operating in different countries, multinational corporations have more flexibility in moving profits between subsidiaries. The more subsidiaries owned by companies in various countries, the more likely the company will be to aggressive transfer pricing. By having multiple subsidiaries operating overseas, the company can manipulate the allocation of risk and profit between different entities using favorable transfer pricing. In addition, companies can also take advantage of tax regulatory gaps between countries to be able to minimize tax burdens through transfer pricing.

The test results on the second hypothesis show a negative influence between Tax Haven and Transfer Pricing, so hypothesis 2, which states that tax haven has a positive effect on transfer pricing, is rejected. This negative result shows that there is an opportunity for companies to transfer profits in an untransparent manner by using transfer prices that are not in accordance with the principle of arm's length, which ultimately causes losses in the countries where the company operates. There will be a risk of fines or legal action for companies that are too aggressive in transfer pricing by moving profits to tax-haven countries. For this reason, companies become more cautious when their subsidiary companies are in tax-haven countries.

The results of the test related to the Relationship between institutional ownership moderation in multinationals and transfer pricing showed that institutional Ownership was not a moderator, so H3 was rejected. Institutional Ownership in the energy sector company was initially thought to influence the company's behavior in relation to transfer pricing. In this study, institutional Ownership within the company was unable to show evidence that strengthened the company's decision to locate its subsidiary overseas. Although institutional Ownership in companies is large, transfer pricing is further strengthened by other factors in multinational companies, such as global tax strategies and complex international tax regulations.

Testing the moderation relationship of institutional Ownership of tax havens to transfer pricing showed that institutional Ownership weakened the Relationship between tax havens and transfer pricing, so H4 was accepted. Institutional Ownership can act as a moderator that can reduce the negative influence of tax havens on transfer pricing, by encouraging companies to always comply with international tax regulations, maintain transparency, and avoid aggressive tax behavior. Institutional Ownership tends to introduce stricter oversight, which can help companies avoid the overuse of tax havens and encourage more ethical and transparent tax policies.

5. Conclusions

The test results showed that multinationalism had a positive effect on transfer pricing. The positive effect of multinationalism in transfer pricing means that companies with operations in different countries tend to set transfer prices more often. The more subsidiaries a company has abroad, the greater the tendency of companies to carry out aggressive transfer pricing in order to minimize the tax burden by taking advantage of regulatory gaps between countries. The negative influence between tax havens and transfer pricing means that while tax havens provide opportunities to move profits in a non-transparent manner, companies that are too aggressive can face legal risks and fines. Therefore, companies are more careful in transferring pricing by moving profits to tax-haven countries. Institutional Ownership does not moderate the Relationship between multinationals and transfer pricing, which means that even though companies have large institutional holdings, other factors, such as global tax strategies and international tax regulations, are more influential in transfer pricing decision-making. Institutional Ownership acts as a moderator that weakens the Relationship between tax haven and transfer pricing, by encouraging companies to comply with international tax regulations, maintain transparency, and avoid aggressive tax behavior. Institutional Ownership introduces stricter oversight, which helps companies avoid overusing tax havens and encourages more ethical tax policies.

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