



Transfer Pricing Policy: The Role of Taxes, Incentive Tunneling and Bonus Mechanism

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Abstract :

This study aims to determine and examine the effect of taxes, tunneling incentive, and bonus mechanism for transfer pricing indications. The approach used in research is a quantitative approach. The population in this study uses registered manufacturing companies on the Indonesia Stock Exchange in 2016-2020. The number of samples in this research used after going through purposive sampling technique as many as 14 companies for 5 year. The data in this study are secondary data and data obtained from the site www.idx.go.id and company performance reports. The analytical method used in this study is multiple linier regression analysis with using SPSS Statistics 25 software in data processing starting from descriptive statistical tests to hypothesis testing. The results showed that the tax have an effect on indications of transfer pricing. And tunneling incentives have an effect on indications of transfer pricing. Meanwhile the variable bonus mechanism has no effect on transfer pricing indications.



Introduction

In today's era of globalization, businesses are growing, which are spread not only in one country but also in other countries, which has led to the emergence of multinational companies. With a number of companies scattered, multinational companies have a special relationship (affiliation) between companies that are in the same group. A company that does multinational business, especially in terms of exports and imports will be faced with various types of taxes. Differences in tax burdens in multinational businesses are common.

The term transfer pricing is actually a neutral term, but in practice the term transfer pricing is often interpreted as an effort to minimize the tax burden that must be paid by shifting prices or shifting profits between companies in one group.

Transfer pricing practices are usually carried out by increasing the purchase price and lowering the selling price between companies within a group and transferring the profits earned to companies located in countries that apply lower tax rates. One indicator of assessing the ability of the State to collect its tax revenues is through the tax ratio or tax ratio, namely the comparison or percentage of tax revenue to Gross Domestic Product (GDP), where the higher a country's tax revenue, the greater its tax ratio (Julaikah, 2014).). Based on the 2021 APBN data, the tax ratio is set at 8.18%. Previously, the Ministry of Finance noted that the State Revenue and Expenditure Budget (APBN) until October 2020 experienced a deficit of IDR 764.9 trillion. One of the reasons is due to tax revenues which fell by 18.8%. The deficit is equivalent to 4.67% of the Gross Domestic Product (GDP). This figure is still below the maximum limit, which is Rp 1,039.2 trillion or 6.34%. Previous research conducted by Fuest et al. (2010), one of which is the low tax ratio is caused by profit shifting, namely shifting company profits to affiliated companies with lower tax rates for the purpose of tax avoidance. According to the OECD in the BEPS (Based Erosion Profit Shifting) Action Plan (2013), transfer pricing is the most dominant scheme used in profit shifting.

One of the phenomena that has occurred is PT. Adaro Indonesia is said to have carried out transfer pricing through its subsidiary in Singapore, Coaltrade Services International. This effort is said to have been carried out from 2009 to 2017. PT. Adaro is alleged to have arranged it in such a way that they were able to pay taxes of US\$ 125 million or equivalent to Rp. 1.75 trillion (an exchange rate of Rp. 14 thousand) less than they would otherwise be paid in Indonesia. In the context of the report submitted by Global Witness, PT. Adaro is said to have carried out transfer pricing. PT. Adaro took advantage of the gap by selling its coal to Coaltrade Services International at lower prices. Then the coal is sold to other countries at a higher price. As a result, the income taxed in Indonesia is cheaper. (Julaikah, 2014). Stuart McWilliam, Climate Change Campaign Manager for Global Witness in a press release said that by moving some money through tax havens, PT. Adaro has managed to reduce its tax bill in Indonesia, which means it reduces revenue for the Indonesian government by almost US\$ 14 million annually that could otherwise be used for public purposes.

The phenomenon of transfer pricing that occurred at PT Toyofuji Manufaktur Indonesia. In 2015 the gross margin of PT Toyofuji Manufacturing increased 11% to 14% per year. However, after restructuring, PT Toyofuji Manufacturing Indonesia's gross margin is only

around 1.8% to 3% per year. Meanwhile, at PT Toyota Astra Motor (a sole agent company holding the brand that was established after the restructuring), the gross margin reached 3.8% to 5%. If the gross margin of PT Toyofuji Manufaktur is combined with PT Toyota Manufacturing Indonesia, the percentage is still 7%. This means that the profit margin before tax after restructuring is 7% lower than the gross profit margin in 2014 of 14%. Based on that, the tax inspector then corrected the price on the Toyofuji Manufacturing transaction to Toyota Motor Asia Pacific in Singapore. The export mode with an unnatural value also repeated that year. The results were fantastic: Toyofuji Manufacturing's 2015 sales turnover jumped from half a trillion as seen from the company's initial report. Its value is now Rp 1.7 trillion. Monday (28/8/2015) (Source: <https://investigasi.tempo.co>)

Seeing this, the government made a new policy on transfer pricing, namely that every company with a certain turnover was asked to make a transfer pricing document. Where the document must include the value of transactions made with affiliated companies. This is regulated in the Minister of Finance Regulation (PMK) Number 213/PMK.03/2015 (Aurinda, 2018).

Furthermore, the company's decision to transfer pricing is also influenced by the tunneling incentive (share ownership). According to Hartati (2015) tunneling incentive is a behavior of the majority shareholder who temporarily transfers their assets to members or subsidiaries with transfer pricing in order to reduce expenses which can later reduce company profits for their own benefit, but minority shareholders also bear the costs. which is charged.

Then, another factor that can also affect transfer pricing is the bonus mechanism. The bonus mechanism is a component of calculating the amount of bonuses given by company owners or shareholders through the GMS to members of the board of directors every year if they get a profit (Suryatiningsih, 2009).

This research is the development of research conducted by Hidayat et al. (2019) entitled The Effect of Taxes and Tunneling Incentives on Transfer Pricing Decisions. The author adds another independent variable, namely the bonus mechanism referred to in Rachmat's (2019) research entitled Taxes, Bonus Mechanisms, and Transfer Pricing.

The reason the author adds the bonus mechanism variable is because of differences in research conducted by Prayudiawan and Pamungkas (2020) which examines that the bonus mechanism has no effect on transfer pricing. Meanwhile, in Rachmat's research (2019), the bonus mechanism can influence companies in implementing transfer pricing policies. In addition, there are differences in the research period Hidayat et al. (2019) which was conducted in the 2013-2017 period, while this study used the 2016-2020 period, so that it could affect the results of the study.

This study uses manufacturing companies as research objects because manufacturing companies are the sector companies that are the most listed and most actively trade their shares on the Indonesia Stock Exchange than other sector companies. In addition, when compared to other sector companies, manufacturing companies have the highest average share price growth. Manufacturing companies have sustainable production so that they require good management of capital and company assets so as to generate large profits to

provide large returns on investment, so that this is something that can attract investors to invest their capital.

Referring to the phenomena and previous studies, the authors indicate that transfer pricing is a practice that is prone to be used as a shortcut through existing regulatory loopholes in the framework of a profit-making strategy. This makes transfer pricing an important thing to research and it is necessary to know what variables can influence it.

Hypothesis testing are:

H1 : Tax has an effect on transfer pricing policies.

H2 : Incentive tunneling has an effect on transfer pricing policies.

H3 : Bonus mechanism has no effect on transfer pricing policies.

Research Method

Dependent variable

According to Lanis (2012), Effective Tax Rate (ETR) can be calculated using the formula :

$$\text{ETR} = \frac{\text{Income tax expense}}{\text{Profit before tax}}$$

According to Ratna (2018), Incentive Tunneling can be calculated using the formula :

$$\text{TNC} = \frac{\text{The largest number of shareholdings owned by foreign companies}}{\text{Number of share outstanding}}$$

According to Saraswati (2017), Bonus Mecanism can be calculated using the formula :

$$\text{ITRENLB} = \frac{\text{Net profit for the year t}}{\text{Net profit for the year t-1}} \times 100\%$$

Independent variable

Transfer Pricing

Transfer pricing is the value of Related Party Transactions (RPT) or related party transactions (Refgia, 2017).

$$\text{RPT} = \frac{\text{Receivable from related party transactions}}{\text{Company's total receivable}}$$

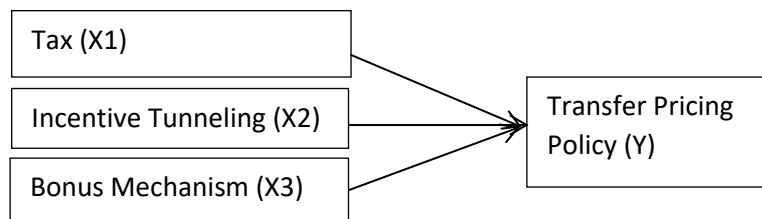


Figure 1. Conceptual Framework

This study uses a quantitative approach with an associative type, which is a research formulation that is asking the relationship between two or more variables.

The type of data in this study is secondary data. The secondary data used is data on the annual financial statements of each manufacturing company listed on the Indonesia Stock Exchange for 2016-2020 which was obtained from www.idx.co.id. In addition, other data or information is obtained from previous research, journals, and websites.

The data collection method used in this research is library research. The data collection technique used is the documentation technique. The data of this research was obtained through searching internet media information with the website address www.idx.co.id, to obtain secondary data, namely the annual financial report (annual reports).

The sample selection was carried out using the purposive sampling method, namely the sampling method based on the criteria and characteristics of the population that had been previously carried out to produce representative data. The sample criteria are:

1. Manufacturing companies listed on the Indonesia Stock Exchange for the 2016-2020 period.
2. The company publishes financial statements successively during the period 2016-2020.
3. The company is controlled by a foreign company (transfer pricing policy is mostly carried out by foreign companies) with an ownership percentage of 25% or more. Because based on Article 18 paragraph (3) of Law Number 36 of 2008 concerning Income Tax, a special relationship is considered to exist if there is an ownership relationship in the form of equity participation of 25% (twenty five percent) or more directly or indirectly.
4. The company did not experience a loss during the study period, because the transfer pricing policy can only be carried out by companies that are profitable.
5. The company has receivables from related parties in the study period.

Result and Discussion

The following are the results of descriptive statistical tests for the variables of transfer pricing, taxes, tunneling incentives, and bonus mechanisms for the years 2016-2020.

Table 1. Descriptive Statistics Test Results

	N	Minimum	Maximum	mean	Std. Deviation
Tax	70	,066	,839	,277	,105
Tunneling Incentive	70	,268	,931	,589	,231
Bonus Mechanism	70	,034	2,290	1.013	,458
Transfer Pricing	70	,001	,413	,134	,103
Valid N (listwise)	70				

Source: SPSS 25, 2022. Data processing results

Based on table 1 above, it shows the measurement of the variable from N as many as 70 in the 2016-2020 period regarding descriptive statistics using SPSS 25, it can be explained as follows:

1. Tax variable (X1) which is measured by the value of the tax ratio or ETR, has a minimum value of 0.06641 contained in PT. Indocement Tunggal Prakarsa Tbk (INTP) in 2016 and the maximum value of 0.83925 is at PT. Lion Metal Works Tbk (LION) in 2019. The mean tax value is 0.2772889 or 27.72% which indicates that the average amount of taxes borne by the companies in this sample is quite low. The standard deviation of 0.10463811 which means that the size of the data spread of the tax variable is 0.10463811 from 70 data.
2. The tunneling incentive variable (X2) which is measured by the ratio of the number of share ownership to the number of outstanding shares, has a minimum value of 0.26780 which is found in PT. Sekar Laut Tbk (SKLT) and the maximum value of 0.93058 is at PT. Sumi Indo Kabel Tbk (IKBI). The mean value of tunneling incentive is 0.5885602 or 58.85% which indicates that the average share ownership in the sample companies tends to be concentrated in a small number of parties. The standard deviation of 0.23115722 which illustrates that the spread of data from the tunneling incentive variable is 0.23115722 from 70 data.
3. The bonus mechanism variable (X3) seen from the net profit trend, has a minimum value of 0,03392 contained in PT. Japfa Comfeed Indonesia Tbk (JPFA) in 2018 and the maximum value of 2.29000 is at PT. Sumi Indo Kabel Tbk (IKBI) in 2017. The mean value of the bonus mechanism is 1.0132921 which shows that the trend of net income in the sample companies on average has increased by 1.01% during the study period. Standard deviation of 0,45783766 which means that the size of the data spread of the bonus mechanism variable is 0,45783766 of 70 data.

4. Transfer pricing variables(Y) as measured by the ratio of the company's related party transaction receivables, has a minimum value of 0.00112 which is found at PT. Multi Bintang Indonesia Tbk (MLBI) in 2018 and the maximum value of 0.41286 is at PT. Sumi Indo Kabel Tbk (IKBI) in 2019. The mean value of transfer pricing is 0,1341348 which shows that related transactions or transfer pricing are carried out by 13.41% of the sample companies, this means that there is an indication of transfer pricing in a small number of sample companies. Standard deviation of 0,10272722 which illustrates that the spread of data from the transfer pricing variable is 0,10272722 of 70 data.

Table 2. Multiple Linear Regression Test Results

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
	B	Std. Error	Beta		
(Constant)	-.106	.057		-1,880	.065
Tax (X1)	.299	.116	.304	2,576	.012
¹ Tunneling Incentive (X2)	.184	.049	.414	3,756	.000
Bonus Mechanism (X3)	.049	.027	.217	1,786	.079

Source: SPSS 25, 2022. Data processing results

Based on table 2 multiple linear regression calculation, the following results are obtained:

$$Y = \alpha + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \varepsilon$$

$$Y = -0,106 + 0,299X_1 + 0,184X_2 + 0,049X_3 + \varepsilon$$

From the multiple linear regression equation above, it can be interpreted that:

1. The constant value is 0.106 with a negative sign, this indicates that if the variables of tax, tunneling incentive, and bonus mechanism are 0 or constant, the transfer pricing value will decrease by 0.106.
2. The coefficient of the tax variable is 0.299. This shows that if there is an increase in tax of 1% or 1 unit, transfer pricing will increase by 0.299 assuming other variables are constant.
3. The tunneling incentive variable coefficient is 0.184. This shows that if there is an increase in the tunneling incentive of 1% or 1 unit, the transfer pricing will increase by 0.184 assuming other variables are constant.
4. The coefficient of the bonus mechanism variable is 0.049. This shows that if there is an increase in bonus of 1% or 1 unit, transfer pricing will increase by 0.049 with the assumption that other variables are constant.

Table 3. Hypothesis Test Results (t Test)

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	-.106	.057		-1,880	.065
Tax (X1)	.299	.116	.304	2,576	.012
¹ Tunneling Incentive (X2)	.184	.049	.414	3,756	.000
Bonus Mechanism (X3)	.049	.027	.217	1,786	.079

Source : SPSS 25, 2022. Data processing results

From table 3 it can be explained that:

1. Tax Variable (X1)

In the tax variable with a value of = 2.5% (0.025), $df = n - k$ (70 – 4) obtained t table of 1.997, then the value of t count 2.576 > t table 1.997 with a significant value (Sig.) 0.012 < 0,05. So it can be concluded that the tax variable has a significant effect on transfer pricing indications. So that H1 is accepted and there are similarities with the previous hypothesis, namely that taxes have an effect on transfer pricing indications.

2. Tunneling Incentive Variable (X2)

In the tunneling incentive variable with a value of = 2.5% (0.025), $df = n - k$ (70 – 4), the t table is 1.997, then the t count is 3.756 > t table is 1.997 with a significant value (Sig.) 0.000 < 0.05. So it can be concluded that the tunneling incentive variable has a significant effect on transfer pricing indications. So that H2 is accepted and there are similarities with the previous hypothesis, namely that tunneling incentives have an effect on transfer pricing indications.

3. Bonus Mechanism Variable (X3)

In the bonus mechanism variable with a value of = 2.5% (0.025), $df = n - k$ (70 – 4) obtained t table of 1.997, then the value of t count 1.786 < t table 1.997 with a significant value (Sig.) 0.079 > 0.05. So it can be concluded that the bonus mechanism variable has no significant effect on the indication of transfer pricing. So that H3 is rejected and there is a difference with the previous hypothesis, namely the bonus mechanism affects the indication of transfer pricing.

The Effect of Taxes on Transfer Pricing Indications

Based on the results of the hypothesis testing that has been done, the tax variable obtained a t-count value of 2.576 > t-table 1.997 with a positive direction, and a significant value of 0.012 < 0.05. So that H1 is accepted, which means that the tax has a significant effect on the indication of transfer pricing.

The results of this study are in line with research conducted by Rachmat (2019) which shows that taxes have an effect on transfer pricing. In the sample company PT. Indo Kordsa

Tbk (BRAM) which has an ETR (Effective Tax Rate) value of 28.15%, there is an indication of transfer pricing as measured by the RPT (Related Party Transaction) value of 28.14% and PT. Unilever Indonesia Tbk (UNVR) which has an ETR (Effective Tax Rate) value of 25.24%, there is an indication of transfer pricing as measured by the RPT (Related Party Transaction) value of 29.99%. By using the ETR proxy to calculate the percentage of the tax rate borne by the company,

As the theory put forward by Suryana (2012) that the purposes of doing transfer pricing include: to outsmart the amount of profit so that tax payments and dividend distributions are low, as well as to inflate profits for window-dressing of financial statements. Transfer pricing is usually done by increasing the purchase price and reducing the selling price between companies within a group and transferring the profits earned to a group of companies domiciled in countries that apply low tax rates.

The practice of transfer pricing is believed to be able to reduce the potential tax revenue of a country because multinational companies tend to shift their tax obligations from countries with high tax rates (high tax countries) to countries that apply low tax rates (low tax countries). Therefore, many multinational companies practice transfer pricing as a tool to minimize the amount of tax that must be paid. Meanwhile, for companies by practicing transfer pricing, it is believed that they can increase company profits because they can minimize the tax burden to be lower (Rachmat, 2019). The results of this study are not in line with the research conducted by Novira, Suzan, and Assalam (2020)

Effect of Tunneling Incentive on Transfer Pricing Indications

Based on the results of the hypothesis testing that has been done, the tunneling incentive variable obtained a t-count value of $3.756 > t\text{-table } 1.997$ with a positive direction, and a significant value of $0.000 < 0.05$. So H2 is accepted, which means that tunneling incentive has a significant effect on transfer pricing indications.

The results of this study are in line with research conducted by Hidayat, Winarso, and Hendrawan (2019) which shows that tunneling incentives have an effect on transfer pricing. In the sample company PT. Sumi Indo Kabel Tbk (IKBI) which has a share ownership proportion of 92.19%, there are indications of transfer pricing as measured by the RPT (Related Party Transaction) value of 41.28% and PT. Shoes Bata Tbk (BATA) which has a share ownership proportion of 82.01%, there is an indication of transfer pricing as measured by the RPT (Related Party Transaction) value of 40.25%. This explains that the tunneling incentive, which is proxied by the largest share ownership, indicates that there is a controlling shareholder that influences management in making transfer pricing decisions. Related party transactions can be used as an opportunistic goal by the controlling shareholder to conduct tunneling. The related party transactions can be in the form of sales or purchases used to transfer cash or other current assets out of the company through the determination of unreasonable prices for the benefit of the controlling shareholder.

Based on agency theory, it explains that agency problems arise due to conflicts between majority shareholders and minority shareholders. In multinational companies the majority

shareholder and company management can take actions that can be detrimental to the government and minority shareholders. Companies with ownership that are concentrated in one party or one interest tend to have tunneling in them (Hidayat, Winarso, and Hendrawan, 2019). If shareholders have large ownership in a company, then automatically they also want large returns or dividends. For this reason, when the dividends distributed by the company must be shared with minority shareholders, the majority shareholder prefers to carry out transfer pricing by transferring the company's wealth for their own interests rather than distributing dividends to minority shareholders. Therefore, the greater shareholder ownership, the more it will trigger the practice of transfer pricing (Saraswati and Sujana, 2017).

Tunneling incentive carried out by the controlling shareholder to obtain private benefits, namely the transfer of resources out of the company. The company does this tunneling with the aim of minimizing transaction costs. By tunneling to parties who have a special relationship, costs can be reduced so that it is more economical compared to parties who do not have a special relationship (Sarifah, Probowulan, and Maharani, 2020). The results of this study are not in line with the research conducted by Ayshintia, Agustin, and Afriyenti (2019) which showed that tunneling incentives had no significant effect on the company's decision to transfer pricing.

The Effect of the Bonus Mechanism on Transfer Pricing Indications

Based on the results of hypothesis testing that has been carried out, the bonus mechanism variable obtained a t-count value of $1.786 > t\text{-table } 1.997$ with a significant value of $0.079 > 0.05$. So H3 is rejected, which means that the bonus mechanism has no significant effect on the indication of transfer pricing.

The results of this study are not in line with the research conducted by Istiqomah and Fanani (2020) which showed that the bonus mechanism had an effect on transfer pricing. Management performs transfer pricing in order to maximize company profits, the large profits generated will make management appear to have good performance. With good performance, management has the opportunity to get a large bonus compensation from the board of directors. However, the results of this study are in line with research conducted by Prayudiawan and Pamungkas (2020) which shows that the bonus mechanism has no effect on transfer pricing decisions. This indicates that the provision of bonus compensation does not affect the company in conducting transfer pricing. The bonus mechanism is not a strong reason that can be used by management in considering transfer pricing. Because in giving bonuses to directors, company owners will certainly see the performance of the directors in managing their company. In this case, the owner of the company will see the company's profit as a whole as an assessment of the performance of its directors.

In the sample company PT. Darya Varia Laboratoria Tbk (DVLA) although there are indications of transfer pricing as measured by the value of RPT (Related Party Transaction) where in 2016 it was 24.62% and in 2017 it was 26.45%, the company's profit tends to decrease with the ITRENDLB value (Trend Index). Net Profit) in 2016 was 1.40% and in 2017 it

decreased to 1.06% and at PT. Lion Metal Works Tbk (LION) which has indications of transfer pricing with an RPT (Related Party Transaction) value in 2018 of 16.78% and in 2019 of 19.91%, the company's profit tends to decrease with the value of ITRENDLB (Net Profit Trend Index) in 2018 by 1.58% and in 2019 it decreased to 0.06%. This shows that the bonus mechanism has no effect on indications of transfer pricing. This happens because the bonus compensation given is not based on the company's profit so that a large profit does not necessarily provide a large bonus for management. In addition, if transfer pricing is done only to get a bonus, then it is not profitable from the company's side but only benefits the directors as bonus recipients (Ayshinta, Agustin, and Afriyenti, 2019).

Giving bonuses is not always used as a motivation for the board of directors or company management to obtain maximum overall profit by implementing transfer pricing. This can happen because the company's management previously analyzed the risks that would be faced when conducting transfer pricing (Novira, Suzan, and Assalam, 2020). Because if only because of the motive of wanting to get a bonus, the directors dare to carry out transfer pricing transactions to provide a temporary increase in profits for the company, then this is very unethical considering that there is a much bigger interest, namely maintaining the value of the company in the eyes of the public and the government by presenting financial statements that are more comprehensive, close to reality and can be used for decision-making purposes that are more important for the company going forward.

According to Sarifah, Probowulan, and Maharani (2020) companies that still carry out earnings management in it are generally carried out by small companies, because larger companies have less incentive to do earnings management than small companies. This is because large companies are companies that are noticed by the wider community, so that they will produce financial reports that can provide more accurate information about the company to its users.

Conclusion

Based on the results of research and discussion, the conclusion of the study is that the tax variable has a significant effect on the indication of transfer pricing (H1) is accepted. The tunneling incentive variable has a significant effect on the indication of transfer pricing (H2) is accepted. The bonus mechanism variable has no significant effect on transfer pricing indications (H3) is rejected.

This research has limitations. First this study has a weakness because the transfer pricing proxy in this study is not the actual measure used to measure transfer pricing. Second, there is still a lack of theory and sources related to transfer pricing and bonus mechanisms. Third, the value of Adjusted R Square in this study is still relatively small, namely 0.228 which indicates that the variables of tax, tunneling incentive, and bonus mechanism are only able to influence the company's decision to transfer pricing by 22.8%, meaning that there are other variables outside the study of 77.2% which can affect the variables studied.

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