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Literature Review Tax Minization, Tunneling Incentive, Debt Covenant, Bonus Mechanisms and Good Corporate Governance on Transfer Pricing

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Abstract

This research provides criticism of literature that examines and analyzes how Tax Minization, Tunneling Incentive, Deb Covenant, Bonus Mechanisms and Good Corporate Governance affect Transfer Pricing. The problem discussed in this research is to see the extent of the influence of Tax Minization, Tunneling Incentive, Deb Covenant, Bonus Mechanisms and Good Corporate Governance on Transfer Pricing. Based on the literature studied, there is an influence between Tax Minization, Tunneling Incentive, Deb Covenant, Bonus Mechanisms and Good Corporate Governance on Transfer Pricing.

Key words: transfer pricing, tax minization, tunneling incentive, deb covenant, bonus mechanisms, and good corporate governance

INTRODUCTION

Transfer pricingremains an important and dynamic issue in the world of international taxation, with many countries working to ensure that this practice is used fairly and in accordance with fair market principles. There has been a significant increase in regulations and compliance requirements in many countries regarding transfer pricing. The Organization for Economic Co-operation and Development (OECD) and the G20 have developed comprehensive Transfer Pricing Guidelines, known as the Base Erosion and Profit Shifting (BEPS) Action Plan. This guideline aims to reduce tax avoidance practices which often use unfair transfer pricing. Countries around the world are increasingly demanding that multinational companies provide more detailed and transparent transfer pricing documentation. This includes Master File, Local File, and Country-by-Country Reporting (CbCR) reports.(Khoirunisa & Wahyudin, 2022) (Quoc Thinh & Thi Hai An, 2023)

Transfer pricingis important for companies for various strategic, operational and regulatory reasons. According to Charles T. Horngren, he emphasized that transfer

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pricing is an important tool in internal performance management. It helps in evaluating the profitability of different business units in a company. By setting appropriate transfer prices, companies can ensure that each business unit is evaluated fairly based on their contribution to the company's overall performance. It helps in performance management, tax burden optimization, regulatory compliance, business strategy, fair profit allocation, and increased transparency and corporate governance. Experts agree that appropriate transfer pricing is the key to the success and sustainability of multinational companies' operations in a complex and changing global business environment.

LITERATURE REVIEW

Transfer Pricing

Transfer pricingis an important tool that covers various strategic and operational aspects within the company. It helps in performance management, tax burden optimization, regulatory compliance, business strategy, fair profit allocation, and increased transparency and corporate governance. Experts agree that appropriate transfer pricing is the key to the success and sustainability of multinational companies' operations in a complex and changing global business environment. Transfer pricing is the price set for goods, services or intangible assets transferred between entities within a multinational company group. The goal is the allocation of income and expenses among different parts of a company, often with the aim of minimizing global taxes.(Handayani, 2021)

Ptransfer pricing practices when viewed from the government side as stated in the Director General of Taxes Regulation Number 43 of 2010 as amended by the Director General of Taxes Regulation Number 32 of 2011 concerning the Application of the Principles of Fairness and Business Customs in Transactions Between Taxpayers and Parties Who Have Special Relationships are believed to be able to result in legal losses. - loss or loss of a country's potential tax revenue because multinational companies tend to shift their tax obligations from countries that have high tax rates (high tax countries) to countries that apply low tax rates (low tax countries) shift in income from other countries. countries that have high tax rates to countries that have low tax rates. Transfer pricing is regulated in Article 18 of Law Number 36 of 2008 concerning income tax. The transfer pricing regulations cover several things, namely the definition of a special relationship, the authority to determine the ratio of debt and capital, and the authority to make corrections in the event of a transaction that is not at arm's length. Based on Law Number 36 of 2008 Article 18 paragraph (4), a special relationship between corporate taxpayers can occur because of ownership or control of the share capital of an entity by another entity of 25% (twenty five percent) or more, or between several entities. where

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25% (twenty five percent) or more of the shares are owned by an entity. Special relationships can result in unfair prices, costs or other benefits realized in a business transaction.(Lo et al., 2010)

Tax Minization

Tax minimizationis a legal and strategic practice used by companies to reduce their tax burden through various means, such as efficient corporate structures, the use of transfer pricing, and the utilization of tax incentives. Experts emphasize that while this practice can improve a company's efficiency and profitability, it is important to maintain transparency, comply with regulations, and consider ethical aspects. A good tax minimization strategy must be a balance between optimizing financial profits and maintaining good relationships with tax authorities and other stakeholders.(Handayani, 2021)

(Handayani, 2021)James R. Hines Jr stated that tax minimization is part of a company's strategy to allocate resources efficiently. By reducing the tax burden, companies can allocate more funds for investment, research and development, and business expansion, which in turn can increase competitiveness and economic growth.

Tunneling Incentives

In the business world, tunneling often occurs but is difficult to detect. The share ownership structure in Indonesia is concentrated in a few owners, resulting in agency conflicts between majority shareholders and minority shareholders. This concentrated ownership structure allows controlling shareholders to monitor and have better access to information than non-controlling shareholders. Based on law number 36 of 2008, a controlling shareholder is an entity that owns shares of 20% or more, either directly or indirectly. Controlling shareholders can be owned by individuals, the government, or foreign parties (Husna, 2017). Apart from taxes, the company's decision to carry out transfer pricing is Tunneling incentive is a behavior that can be said to benefit the majority shareholder because they transfer assets and profits for their benefit. Alone. Meanwhile, if there are costs that arise, minority shareholders will also bear these costs(Quoc Thinh & Thi Hai An, 2023)

Transfer pricing decisions are also influenced by tunneling.(Handayani, 2021)stated that there are several steps that majority shareholders can take to obtain personal benefits through controlling company operating policies such as dividends, bonuses, salaries and allowances and steps to obtain personal benefits through contractual policies, including tunneling. It could be said that the company will do things that make the tax costs small. Tunneling is the action of majority shareholders who divert

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company assets and profits to obtain private benefits, but the burden is also borne by minority shareholders. Tunneling activities are closely related to share ownership in the company (Mutami-mah, 2009).

Debt Covenant

Debt covenantis an important instrument in a debt agreement that is used to protect creditors and ensure the borrower manages his business wisely. By setting financial and operational boundaries, covenants help reduce the risk of default, overcome agency problems, increase transparency and trust, and reduce the risk of moral hazard.(Khalil & Simon, 2014)And(Chao & Horng, 2020)

According to Stephen A. Ross(Kinney & Wempe, 2004)Debt covenants are a risk control tool used by creditors to reduce the risk of default. By setting certain limits, creditors can monitor the borrower's financial performance and take preventive action if the borrower's financial condition begins to worsen. These include limitations on leverage ratios, liquidity ratios, and restrictions on dividend payments.

E. Bonus Mechanism

Bonus mechanismis a system designed to provide incentives to employees or management in the form of bonuses based on individual, team or company performance. The main purpose of the bonus mechanism is to motivate employees to achieve or exceed predetermined targets, which will ultimately increase company productivity and performance. Jensen and Meckling argue that the bonus mechanism is an effective tool to overcome agency problems between management and shareholders. By linking bonuses to company performance, the bonus mechanism aligns management interests with the interests of shareholders, so that management is motivated to increase company value.(Mamay Komarudin, Naufal Affandi, Ende, Nugrahini Kusumawati, Siti Fatonah, 2023)And(Marfuah et al., 2021)And(Aryati & H, 2021)

The bonus mechanism is a component of calculating bonuses through the GMS to members of the board of directors, the amount of the bonus is given by owners or shareholders who have good performance every year and if the company makes a profit. The mechanism can be used as a measure if a company has a profit. The bonus mechanism based on the amount of profit will make directors try to manipulate profits and even manipulate net profits with the aim of maximizing the bonuses they receive. This bonus mechanism can also lead to fraud that is personally beneficial (Indriaswari, 2017).

Good Corporate Governance

Good Corporate Governance(GCG) is a series of mechanisms, processes and relationships used by various parties to direct and control a company. GCG aims to ensure

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transparency, accountability, responsibility, independence and fairness in company management, which ultimately improves the company's performance and reputation. Jensen and Meckling focus on agency problems in the context of GCG. They explain that conflicts of interest between managers (agents) and shareholders (principals) can be minimized through effective governance mechanisms, such as appropriate incentive structures, close supervision by the board of directors, and information disclosure.(Melzatia et al., 2019)And(INDRIASWARI, 2017)And(NPWA Putri et al., 2022)

METHODOLOGY

This research design uses a literature review study, namely identifying, evaluating and synthesizing research results and thoughts produced by researchers and practitioners. The results of research and thoughts are usually published through various sources such as journals, books, the internet and other libraries.

Search for published articles via Google search with keywordsTransfer Pricing, Tax Minization, Tunneling Incentive, Deb Covenant, Bonus Mechanisms, and Good Corporate Governance. Articles or journals that match the criteria are then downloaded for further analysis. This Literature Review uses literature published up to 2023 which can be accessed in full text in pdf and scholarly format (peer reviewed journals).

In compiling a literature review, the author followed four stages of activities as explained by Ramdhani et al. (2014), namely (1) selecting the topic to be reviewed, (2) tracking and selecting suitable (relevant) articles, (3) conducting literature analysis and synthesis and (4) organizing the writing of the review. Regarding literature analysis and synthesis, the author does this by analyzing articles that are relevant to the topic to be reviewed. This means discussing articles by making identification and classification based on the elements that will be reviewed from several articles discussing almost the same topic. Next, integrate the analysis results and make conclusions based on the similarities and differences of each article.

The following is a sample of the articles used:

Table 1 Research Sample

Publication	Writer	Title/sub Title
LLC "Consulting Publish-ing Company "Business Perspectives"	(Quoc Thinh & Thi Hai An, 2023)	***The influence of income tax rate, tunneling incentives, and return on equity on transfer pricing be-havior of foreign direct investment enterprises in Vietnam***

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European Journal Of Business and Management Research	(Handayani, 2021)	*Tax Minization as a Moderator on the Effect of Tunneling Incentive and Bonus Mechanism on Transfer Pricing Provisions*
JATA (American Accounting Association)	(Lo et al., 2010)	***Tax, Financial Reporting, and Tunneling Incentives for Income Shifting: An Empirical Analysis of the Transfer Pricing Behavior of Chinese-Listed Companies***
Journal of Accounting, Finance and Auditing	(Fuadah & Nazihah, 2019)	*The Effect Of Tax, Tunneling Incentive, Bonus Ecchanisms, And Firm Size On Transfer Pricing (Indonesian Evidence)*
Ekombis Review Journal – Scientific Journal of Economics and Business	(Azzuhriyyah & Kurnia, 2023)	**The Influence of Tunneling Incentives, Intangible Assets, and Debt Covenants on Transfer Pricing Decisions with Tax Minimization as a Moderating Variable (Empirical Study of Manufacturing Companies Listed on the Indonesian Stock Exchange 2015-2021)**
PERMANA: Journal of Taxation, Management and Accounting	*(Khoirunisa & Wahyudin, 2022)*	**Analysis of the Effect of Thin Capitalization, Debt Covenant, and Tunneling Incentive on Transfer Pricing with the Audit Committee as a Moderating Variable**
Journal of Applied Business, Volume 05 Number 01 (June, 2021) 57 – 72	*(Marfuah et al., 2021)*	**The Effect Of Tax Minimization, Bonus Mechanism, Foreign Ownership, Exchange Rate, Audit Quality On Transfer Pricing Decisions**
JASa (Journal of Accounting, Auditing and Accounting Information Systems)	*(Mamay Komarudin, Naufal Affandi, Ende, Nugrahini*	**The Effect Of Taxes And Bonus Mechanisms In Moderating Profitability On Transfer Pricing**

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	Kusumawati, Siti Fatonah, 2023)	
Advances in Economics, Business and Management Research, volume 142 5th Sriwijaya Economics, Accounting, and Business Conference(SEABC 2019)	*(Tjandrakirana & Ermadiani, 2020)*	**Factors That Influence Companies to Transfer Pricing**
ATTESTATION: SCIENTIFIC JOURNAL OF ACCOUNTING	*(Herlina & Murniati, 2023)*	**Effect of Effective Tax Rate, Tunneling Incentive, and Bonus Mechanism on Transfer Pricing Decision**
ICE-BEES 2019 International Conference on Economics, Business and Economic Education 2019 Volume 2020		**The Effect of Tunneling Incentive to Transfer Pricing Decision with Tax Minimization As a Moderating Variable**
Journal of Accounting and Taxation Analysis, Volume 5, Number 1, March 2021, Pages 35-44	*(Mineri & Paramitha, 2021)*	**THE EFFECT OF TAXES, TUNNELING INCENTIVES, BONUS MECHANISMS AND PROFITABILITY ON TRANSFER PRICING**
https://ejournal.uin-suska.ac.id/	(Mutia, et al 2021)	**The Influence of Taxes, Bonus Mechanisms, Foreign Ownership, Tunneling Incentives and Exchange Rates on Company Decisions to Conduct Transfer Pricing**
Accounting Analysis Journal 9(2) (2020) 110-115	*(Devi & Suryarini, 2020)*	**The Effect of Tax Minimization and Exchange Rate on Transfer Pricing Decisions with Leverage as Moderating**
SCIENTIFIC JOURNAL OF REFLECTION: Economics, Accounting, Management and Business	*(WC Putri & Lindawati, 2023)*	**The Influence of Tax Minimization, Exchange Rate and Tunneling Incentive on Transfer Pricing Decisions**

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(JIMEA) MEA Scientific Journal (Management, Economics and Accounting)	*(Lingga et al., 2022)*	**Corporate governance, Bonus mechanism and Tunneling incentives' influence on transfer pricing practices**
Trisakti Accounting Journal Volume. 8 No. February 1 2021 : 23-40 ISSN : 2339-0832 (Online)	*(Aryati & H, 2021)*	**The Relationship Between Tunneling Incentive, Bonus Mechanism and Debt Covenant on Transfer Pricing Decisions with Tax Minimization as Moderation**

RESEARCH AND RESULTS

The literature review process was tested empirically by testing 17 articles with various findings. Some of them try to directly test Transfer Pricing, Tax Minization, Tunneling Incentive, Deb Covenant, Bonus Mechanisms, and Good Corporate Governance.

The Effect of Tax Minization on Transfer Pricing

OECD BEPS Action Plan (2013) Tax minimization has a significant influence on transfer pricing practices. Tax minimization is a strategy used by companies to reduce tax burdens in a legal way, including through transfer pricing practices. The OECD launched the BEPS Action Plan in response to aggressive tax minimization practices through transfer pricing. BEPS aims to ensure that profits are taxed where economic value is actually created. This includes tightening transfer pricing rules to prevent tax base erosion and unfair profit shifting. States that companies use transfer pricing as the main tool to reduce the tax burden by allocating profits to jurisdictions with low tax rates and costs to jurisdictions with high tax rates. However, this practice faces stringent regulatory challenges and significant compliance risks. This theory is supported by research(Handayani, 2021),(Fuadah & Nazihah, 2019),(Azzuhriyyah & Kurnia, 2023),(Marfuah et al., 2021),(Mamay Komarudin, Naufal Affandi, Ende, Nugrahini Kusumawati, Siti Fatonah, 2023),(Tjandrakirana & Ermadiani, 2020),(Herlina & Murniati, 2023),(Aryati & H, 2021)

The Effect of Tunneling Incentives on Transfer Pricing

Djankov, La Porta, Lopez-de-Silanes, and Shleifer (2008) Tunneling incentives have a significant influence on transfer pricing practices, it can be seen that majority

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shareholders or management often use transfer pricing as a tool to move profits and assets from the companies they control , often at the expense of minority shareholders. This practice occurs especially in environments with weak regulation and minimal legal protection for minority shareholders. To overcome this problem, strict transfer pricing regulations, strong legal protection and transparency in financial reports are needed. Effective supervision and strong law enforcement are also important to prevent transfer pricing abuse in the context of tunneling. This theory is supported by research(Quoc Thinh & Thi Hai An, 2023),(Handayani, 2021),(Lo et al., 2010),(Azzuhriyyah & Kurnia, 2023),(Herlina & Murniati, 2023),(Mineri & Paramitha, 2021),(Gupta & Goyal, 2023),(Wu et al., 2009),(Devi & Suryarini, 2020)

The Effect of Deb Covenant on Transfer Pricing

Armstrong, Guay, and Weber (2010)examines how debt covenants influence companies' transfer pricing decisions. They find that companies with tight covenants tend to be more conservative in setting transfer prices to ensure financial stability. For example, they may set a lower transfer price to reduce reported earnings in entities with stricter covenants in order to maintain required financial ratios. This theory is supported by research(Azzuhriyyah & Kurnia, 2023),(Aryati & H, 2021)

The Effect of Bonus Mechanism on Transfer Pricing

Armstrong, Guay, and Weber (2010)The bonus mechanism has a significant influence on transfer pricing practices within the company. It can be seen that managers and executives whose compensation is tied to financial performance metrics have an incentive to use transfer pricing as a tool to optimize financial results that affect their bonuses. Research shows that transfer price manipulation can be done to increase revenue or profits in a particular business unit, meet performance targets, and thereby increase bonuses. This can result in financial statements that do not reflect actual economic conditions and pose risks for the company, including potential audits and sanctions from tax authorities. Therefore, it is important for companies to have strict monitoring and regulatory mechanisms to ensure that transfer pricing is carried out in accordance with the arm's length principle and not just to manipulate management bonuses. This theory is supported by research(Fuadah & Nazihah, 2019),(Herlina & Murniati, 2023),(Lingga et al., 2022),

The Influence of Good Corporate Coverage on Transfer Pricing

Good corporate governancehas a significant influence on transfer pricing practices in companies. Experts show that companies with good governance tend to be

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more compliant with arm's length principles in setting transfer prices. This is because good governance encourages transparency, accountability and strong supervision from the board of directors and audit committee on financial decisions, including transfer pricing. By implementing good governance well, companies can minimize the risk of tax audits, maintain their reputation, and maintain the trust of shareholders and other stakeholders. Therefore, the integration of good corporate governance in transfer pricing strategies is crucial to achieving good compliance and maintaining the integrity of the company as a whole. Theories are supported by research(Rosa et al., 2017)

CONCLUSION

Based on empirical testing that Tax Minization, Tunneling Incentive, Deb Covenant, Bonus Mechanisms, and Good Corporate Governance have a significant influence on Transfer Pricing, it can be seen that theoretically there is an influence between these variables and is supported by research that has been carried out, but the Good variable It is not certain that Corporate Governance has a significant influence because there is not much research that supports this theory, so further research is needed to link Good Corporate Governance variables to Transfer Pricing

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