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Good Corporate Governance in Mitigating Tax Avoidance: An Analysis of Transfer Pricing and Profitability in Indonesian Energy Companies

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Abstract

This research explores the factors that drive tax evasion, which remains a paramount fiscal challenge in Indonesia, especially among companies in the energy industry. Agency theory illustrates the conflict of interest existing between management and government in managing tax obligations. A quantitative methodology was used, drawing on 55 data points from 11 energy companies listed on the Indonesia Stock Exchange (IDX) from 2020 to 2024. The gathered data were examined using multiple linear regression and Moderation Regression Analysis (MRA). The results indicate that transfer pricing significantly boosts tax avoidance. Conversely, profitability and effective corporate governance (GCG), as measured by board size, have a significant negative impact on tax evasion. Additionally, GCG is found to significantly diminish the positive correlation between transfer pricing and tax avoidance. Consequently, it can be deduced that transfer pricing practices elevate tax avoidance, while enhanced profitability and robust corporate governance frameworks tend to decrease such practices. In this context, GCG plays a crucial role as a risk-mitigation mechanism against the adverse implications of transfer pricing practices.

Keywords: Good Corporate Governance, Tax Avoidance, Transfer Pricing.

INTRODUCTION

Taxation plays a strategic role as a primary pillar in fostering economic development and enhancing social welfare, given its status as the dominant and most

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sustainable source of government funding. The Indonesian government continues to initiate and implement a series of comprehensive tax policy reforms aimed at optimizing state revenue performance while expanding the tax base (Situmorang et al., 2025). A Systematic Literature Review by Ulfah et al. (2024), drawing upon data from the Ministry of Finance, reveals that Indonesia's total state revenue realization reached IDR 2,774.3 trillion. This achievement exceeded the 2023 State Budget (APBN) target by 112.6% and fulfilled 105.2% of the threshold stipulated in Presidential Regulation Number 75 of 2023, representing a 5.3% growth compared to the previous year. Within the state revenue structure, tax receipts were the main revenue stream, contributing IDR 2,155.4 trillion, while Non-Tax State Revenue (PNBP) accounted for IDR 605.9 trillion, and grant revenues totaled IDR 13 trillion. Cumulatively, these figures demonstrate that approximately 78% of total state revenue originated from the taxation sector.

Taxation serves as the primary source of revenue for Indonesia; however, tax compliance remains a significant challenge. Taxpayer non-compliance can foster tax avoidance practices, which ultimately diminishes state revenue (Eka et al., 2024). According to the *State of Tax Justice 2023* report, Indonesia incurs an estimated annual tax revenue loss of 0.27% of its Gross Domestic Product (GDP), equivalent to approximately USD 2.806 billion. This figure slightly exceeds the average for Asian countries, which is around 0.25% of GDP. This situation indicates a propensity among corporations to use tax avoidance to reduce fiscal liabilities and optimize profitability.

Tax avoidance can be conceptualized as a set of legally permissible mechanisms and schemes used by individuals and business entities to minimize tax liabilities by exploiting loopholes, exemptions, and incentives embedded in tax regulations (Junensie et al., 2020; Kusumawardani et al., 2025). Although operating within legal boundaries, this practice typically involves optimizing the technical and structural provisions of tax laws to reduce total compliance obligations. The primary orientation of tax avoidance is to strengthen a firm's fiscal position while enhancing its after-tax profitability. The implementation of such strategies varies in complexity, from leveraging legitimate tax deductions and credits to executing more sophisticated arrangements (Soemarsono et al., 2024). Despite remaining within a legal framework, tax avoidance is frequently perceived as inconsistent with ethical principles. It poses a risk of substantial fiscal losses, as it directly curtails state revenue generated from the taxation sector (Praystya & Anggrainie, 2024). In Indonesia, several corporations are known to engage in lawful tax liability reduction practices that ultimately negatively impact national revenue. This phenomenon is closely tied to corporate management, which holds the executive

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authority to formulate strategic policies to optimize resource utilization efficiency (Retnoningsih et al., 2024).

The phenomenon of tax avoidance among energy sector corporations was highlighted in a PwC (2021) publication titled *Mine 2021: Great Expectations, Seizing Tomorrow*, which asserted that energy companies employ transfer pricing schemes to minimize tax payments to the state. The report further revealed that approximately 70% of 40 major mining entities failed to disclose tax transparency reports. The mining sector is particularly susceptible to tax avoidance due to its high profitability, extensive related-party transactions, and complex cross-border operations (Syarif & Koerniawan, 2025). The case of PT Adaro Energy Tbk, a major mining enterprise, serves as a prominent example of disclosed corporate tax avoidance. The company reportedly utilized transfer pricing mechanisms, a method frequently observed in comparable corporate tax disputes. Consequently, this practice resulted in a substantial reduction of the firm's tax liabilities in Indonesia, estimated at USD 125 million (approximately IDR 1.75 trillion) below the statutory amount due (Fitriani & Widaryanti, 2024).

A multitude of factors influence tax avoidance; specifically, this study examines transfer pricing practices, corporate profitability, and the implementation of Good Corporate Governance (GCG), as reflected in the role of the board of directors. Transfer pricing is a strategic mechanism corporations use to minimize tax burdens. In practice, firms with high profitability levels may adjust inter-entity transfer prices to reduce reported taxable income, taking into account pre-tax earnings conditions (Ekasari et al., 2025). Transfer pricing in Indonesia remains a critical issue, particularly for enterprises engaging in cross-border operations. Ambiguity or complexity in determining transfer prices for individual transactions may indicate potential tax avoidance, especially when pricing fails to adhere to the arm's length principle (Budiman & Bandi, 2022). Prior empirical literature examining the linkage between transfer pricing and tax avoidance has yielded mixed conclusions. The findings of Alexander (2024) indicate that transfer pricing is not significantly related to tax avoidance. However, these results contrast with empirical evidence from Widyasari et al. (2024) and Iriyadi et al. (2024), which demonstrate that transfer pricing significantly influences tax avoidance, with both positive and negative effects.

Another crucial factor is profitability. Corporations generally endeavor to increase profit through operational efficiency to enhance firm value. Profit, defined as the net difference between revenues and expenses, reflects a firm's productivity level and serves as a benchmark of managerial performance for shareholders. Because net

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income is realized after tax deductions, managing tax expenses becomes vital to optimizing overall earnings efficiency (Oktafiani et al., 2023). A company's ability to generate earnings from its operations is reflected in its profitability metrics. Higher profitability is typically accompanied by an increased potential tax liability, given that earnings constitute the primary baseline for corporate income tax assessment (Harnovinsah et al., 2025). In this study, profitability is measured using Return on Assets (ROA), an indicator used to evaluate financial performance based on a firm's ability to generate earnings relative to its total assets. A higher ROA signifies superior corporate performance. Additionally, ROA is intrinsically linked to net earnings and the magnitude of corporate income tax liabilities (Suryatimur et al., 2020). Under these circumstances, firms tend to adopt tax planning strategies – including tax avoidance within statutory boundaries – to optimize tax burdens and preserve after-tax earnings efficiency (Widyastuti et al., 2022). Empirical studies examining the impact of profitability on tax avoidance, such as those conducted by Harnovinsah et al. (2025) and Andriawan et al. (2024), demonstrate both positive and negative effects. Conversely, empirical findings from Lestari and Kholid (2024) indicate that profitability has no significant effect on tax avoidance practices.

The subsequent factor is GCG. Corporate governance plays a vital role in influencing tax avoidance levels through its monitoring and control functions over executive management. This mechanism aims to curb managerial opportunistic behavior that may prioritize self-interest over shareholder value. Through effective supervision, the operational leeway for management to engage in tax avoidance practices becomes constrained, thereby repressing the extent of tax avoidance (Syura et al., 2020). In this study, GCG is proxied by board size. Board size is a critical corporate governance mechanism for mitigating agency problems between principals and agents, thereby ensuring alignment of interests between the parties (Kalbuana et al., 2023; Luwihono et al., 2021). Prior literature examining GCG proxied by board size has yielded inconclusive results. Empirical evidence provided by Kalbuana et al. (2023) and Susanto et al. (2024) indicates that GCG can be both positively and negatively associated with tax avoidance practices. Conversely, Widijaya and Putra (2025) concluded that GCG has no significant effect on tax avoidance. In this study, GCG serves a dual analytical role: first, as an independent variable to examine its direct impact on tax avoidance, and second, as a moderating variable to test whether GCG strengthens or weakens the effect of transfer pricing on tax avoidance. According to Baron and Kenny (1986), a moderating variable is conceptually treated similarly to an independent variable because

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it alters the direction or strength of the relationship between the independent and dependent variables. Drawing upon the aforementioned prior studies, GCG has been widely tested as an independent variable. Consequently, both conceptually and empirically, GCG fulfills the criteria to be positioned as a moderating variable in this investigation.

Empirical evidence from prior literature yields inconsistent results regarding the aforementioned factors influencing tax avoidance. Such discrepancies suggest that the interrelationships among these variables warrant a more comprehensive explanation and re-examination across different empirical contexts. Consequently, these mixed findings provide the primary rationale and motivation for conducting further investigation to gain a deeper understanding of the determinants of tax avoidance.

LITERATURE REVIEW

Agency Theory

Agency theory explains tax avoidance practices through the lens of the principal-agent relationship. Within this framework, the principal delegates authority to the agent to manage the firm and execute strategic decisions concerning corporate interests (Jensen & Meckling, 1976). Agency theory posits that individuals naturally tend to prioritize self-interest over organizational objectives. In an agency relationship, the principal strives to maximize firm profitability by deploying resources through the agent. Conversely, agents, as corporate managers, harbor distinct interests in securing greater compensation or performance-based incentives (Fahri & Fahria, 2023).

In the context of this study, agency problems arise from fundamental goal incongruence between the government and corporations regarding tax administration. The government, as the responsible fiscal authority, possesses a strong incentive to maximize national tax revenues. Conversely, corporate management, acting as an agent, is motivated to maximize net profits by managing and minimizing tax liabilities. This divergence of interests inherently creates a conflict that drives corporations toward tax-avoidance strategies to reduce fiscal obligations and pursue higher profitability. According to Antari and Setiawan (2020), in practicing tax avoidance, management seeks to optimize earnings in alignment with corporate goals, including adjusting pre-tax income by exploiting loopholes in existing tax regulations.

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HYPOTHESIS DEVELOPMENT

The Effect of Transfer Pricing on Tax Avoidance

High profit targets imposed by principals can inflate corporate tax liabilities, as the magnitude of reported earnings directly determines the tax obligations due. Under such circumstances, management, acting as an agent, is incentivized to deploy strategic measures to manage tax burdens more efficiently. One prominent strategy is transfer pricing, which is leveraged to reduce tax liabilities without directly violating statutory regulations (Fahri & Fahria, 2023). This practice shifts profit recognition to jurisdictions with lower tax rates than high-tax countries, thereby concentrating reported earnings within entities subject to lighter tax obligations. Domestically, this mechanism is executed by adjusting transaction prices among affiliated entities or business units within a corporate group, which ultimately influences the magnitude of profits reported by each respective entity.

Firms engaging in transfer pricing typically establish agreements to set transaction prices that, under certain circumstances, may involve manipulating transaction reporting, thereby distorting reported tax liabilities (Rezeki et al., 2021). Empirical evidence from studies by Aristyatama and Bandiyono (2021) and Budiman and Bandi (2022) consistently indicates a significant positive correlation between the intensity of transfer pricing practices and the degree of tax avoidance. These findings suggest that the more aggressively a firm engages in inter-affiliate transfer pricing, the higher its likelihood of engaging in tax-avoidance activities to minimize fiscal liabilities.

H1: Transfer pricing positively affects tax avoidance.

The Effect of Profitability on Tax Avoidance

According to Susilowati et al. (2024), as corporate financial performance improves, corporate income tax liabilities tend to increase correspondingly. This condition may incentivize firms to deploy tax management strategies to curb the growth of such tax burdens. Conversely, shareholders anticipate higher dividend payouts in tandem with rising corporate earnings. Consequently, tax avoidance practices may be employed to preserve optimal after-tax profitability, thereby meeting investor expectations. Aligned with the findings of Oktaviana and Kholis (2021), an increase in corporate earnings inevitably leads to higher tax liabilities. Such circumstances can motivate management to pursue specific strategies to alleviate fiscal pressure, including tax avoidance.

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The relationship between profitability and tax avoidance is further supported by the empirical findings of Wirianata et al. (2024), which demonstrate a positive effect of profitability on the propensity to engage in tax avoidance practices. From an agency theory perspective, the role of managers as agents centers not only on enhancing firm operational performance but also on optimizing net after-tax earnings through effective tax strategies. Although high profitability reflects managerial success in executing corporate operations, a simultaneous increase in pre-tax earnings amplifies the firm's fiscal liabilities. This condition ultimately drives management to manage taxes more efficiently.

H2: Profitability positively affects tax avoidance.

The Effect of Good Corporate Governance on Tax Avoidance

In the context of agency conflicts, the implementation of robust corporate governance is crucial for mitigating goal divergence between owners and management. Effective governance aligns managerial behavior with shareholder preferences, including determining the optimal level of tax avoidance practices. Conversely, weak governance creates leeway for managers to make decisions that do not fully reflect the owners' interests (Kovermann & Velte, 2019). As corporate taxpayers, firms are subject to statutory provisions and principles inherent in GCG implementation, thereby incentivizing them to fulfill their tax obligations in a compliant and transparent manner. Nevertheless, the dynamics of GCG implementation can also shape the trajectory of a firm's tax policies. Under certain circumstances, decision-making flexibility within this governance framework still affords firms opportunities to pursue tax-avoidance strategies, provided they remain within existing regulatory boundaries.

The implementation of GCG within a firm is directed toward fostering compliance with statutory provisions, including the fulfillment of tax obligations. Effective GCG implementation is expected to reinforce corporate transparency, accountability, and regulatory tax compliance (Chandra & Cintya, 2021). Optimally executed corporate governance also plays a pivotal role in curbing tax avoidance while enhancing firm value, thereby bolstering market confidence and attracting external investors. Empirical findings from Noviari and Suaryana (2019) confirm that GCG implementation is negatively associated with tax avoidance, indicating that higher governance quality is associated with lower levels of corporate tax avoidance. Furthermore, empirical evidence from Chandra and Cintya (2021) supports the conclusion that a consistently

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applied GCG system effectively minimizes the potential for tax avoidance within corporate structures.

H3: Good Corporate Governance negatively affects tax avoidance.

The Moderating Role of Good Corporate Governance in the Effect of Transfer Pricing on Tax Avoidance

Corporate transfer pricing practices may indicate tax-avoidance efforts, particularly when firms operate extensive cross-border business networks. Such suspicions typically arise when transactions among affiliated entities are executed using pricing schemes that fail to reflect the arm's length principle. Before the establishment of stringent international regulations restricting non-arm's-length transactions, GCG served as the primary control mechanism to ensure that corporate operations adhered to ethical standards and addressed stakeholder interests. Through an optimally operating control system, GCG suppresses tax avoidance practices executed via transfer pricing while preventing management from taking actions that deviate from fairness and regulatory compliance (Fasita et al., 2022). Empirical findings by Dharmawan et al. (2024) state that GCG implementation plays a moderating role in weakening the effect of transfer pricing on tax avoidance practices. Through effective oversight and control mechanisms, GCG incentivizes management to act in accordance with applicable statutory provisions while proportionally safeguarding the interests of all stakeholders.

H4: Good Corporate Governance weakens the effect of transfer pricing on tax avoidance.

RESEARCH METHODOLOGY

This study employs a quantitative approach using purposive sampling to select the research sample. As a non-probability sampling method, sample selection was guided by specific criteria aligned with the study's objectives. The selection criteria were applied to energy sector companies listed on the Indonesia Stock Exchange (IDX) during the 2020 – 2024 period. Specifically, eligible firms had to satisfy the following requirements: (1) actively listed on the IDX throughout the entire research period, (2) incurred no operating losses during the observation window, and (3) published complete and consistently presented financial or annual reports. Of the 91 energy sector companies listed on the IDX, 11 firms met all specified criteria. With a five-year observation period, the final dataset yielded 55 firm-year observations.

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Data analysis was conducted using multiple linear regression to test the direct relationships between the independent and dependent variables, and Moderated Regression Analysis (MRA) to evaluate the moderating variable and interaction effects. All data processing procedures were performed using SPSS. Before hypothesis testing, a series of classical assumption tests was performed to ensure that the regression model satisfied statistical prerequisites, namely residual normality, the absence of severe multicollinearity, the absence of autocorrelation, and homoscedasticity (absence of heteroscedasticity). Once all classical assumptions were fulfilled, hypothesis testing was conducted to determine the statistical significance and direction of relationships among the variables in accordance with the theoretical framework. The empirical regression model specification in this study is formulated as follows:

$$TA = \alpha + \beta1(TP) + \beta2(ROA) + \beta3(GCG) + \beta4(TP) * (GCG) + e$$

Operational Definitions and Measurement of Variables

Tax Avoidance

Tax avoidance is conceptualized as a legally permissible endeavor by taxpayers to minimize tax liabilities by exploiting interpretative ambiguities and statutory concessions embedded in tax regulations. In this study, the degree of tax avoidance is proxied using the Effective Tax Rate (ETR) indicator. An ETR exceeding the statutory tax rate suggests that the firm has not fully optimized available tax incentives or relief. Conversely, an ETR below the statutory tax rate reflects the firm's capacity to manage its tax liabilities more efficiently by leveraging existing tax provisions, resulting in a relatively lower proportion of tax paid relative to commercial earnings (Pamungkas & Fachrurrozie, 2021).

$$ETR = \frac{Tax\ Burden}{Pre - Tax\ Income}$$

Transfer Pricing

Transfer pricing is the process of establishing transaction values for goods, services, or intangible assets exchanged between entities. This process encompasses internal transfers across units within a single corporation as well as transactions between related entities (bound by affiliated or special ownership relationships) within a global enterprise group. Its primary objective is to govern pricing mechanisms in such related-

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party transactions, thereby ensuring the appropriate allocation of revenues and expenses across divisions or subsidiaries (Arifin et al., 2020). In this study, transfer pricing is proxied by the ratio of related-party receivables to total corporate receivables. This ratio reflects the proportion of transactions executed with affiliated entities relative to the firm's total aggregate receivables (Merle et al., 2019).

$$TP = \frac{Receivables\ from\ Related\ Parties}{Total\ Receivables}$$

Profitability

ROA serves as an essential financial metric, expressed as a percentage, that evaluates corporate operational efficiency. Specifically, this ratio measures an entity's capacity to convert its aggregate asset base into net after-tax earnings over a given accounting period, thereby reflecting managerial effectiveness in leveraging asset investments to generate profits. The ROA value is computed as the ratio of net income after tax to total firm assets (Chen et al., 2010).

$$ROA = \frac{Net\ Income\ After\ Taxes}{Total\ Assets}$$

Good Corporate Governance (GCG)

The Board of Directors holds the primary responsibility for managing and representing the firm across all operational activities. Meanwhile, the Board of Commissioners provides strategic guidance and exercises oversight over the executive duties of the Board of Directors. However, an excessively large board size may diminish the effectiveness of coordination and oversight, thereby adversely affecting managerial performance. In corporate governance literature, board size is commonly measured by the total number of board members within a firm (Kalbuana et al., 2023). In this study, the GCG variable is positioned not only as an independent variable but also as a moderator within the empirical framework.

$$\text{Board Size} = \text{Total Number of Board Members}$$

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RESULTS AND DISCUSSIONS

Classical Assumption Tests

Classical assumption tests were conducted prior to the regression analysis to ensure that the dataset and the empirical model met all necessary statistical prerequisites.

Normality Test

Data normality in this study was evaluated using the One-Sample Kolmogorov-Smirnov (K-S) test based on the regression model residuals. The objective of this procedure is to assess whether the residuals follow a normal distribution. The normality assumption is deemed satisfied if the significance level (*p-value*) exceeds 0.05. The results of the normality test are presented in Table 1.

Table 1. Normality Test Results

One-Sample Kolmogorov-Smirnov Test		Description
N	55	The data is not normally distributed
Asymp. Sig. (2-tailed)	0,019	

Source: Processed Data, 2026

Initial normality test results indicated that the dataset was not normally distributed, as evidenced by a significance value (*p-value*) below 0.05. In parametric statistical analysis, satisfying the normality assumption is essential for minimizing potential bias and enhancing the reliability of estimates. Consequently, this study identified and treated outliers to improve data distribution and fulfill the required statistical assumptions.

An outlier is an observation exhibiting extreme values – either abnormally high or low – thereby deviating significantly from the main distribution of the data. If such observations fail to represent true population conditions, they must be removed or adjusted to prevent biased analytical outcomes (Ghozali, 2018). A total of four observations were identified as outliers and excluded from the sample. Accordingly, the final dataset utilized for subsequent empirical analysis comprised 51 observations. A subsequent normality test was performed following the data adjustment process; the results are presented in Table 2.

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Table 2. Normality Test Results After Correction

One-Sample Kolmogorov-Smirnov Test		Description
N	51	Normally distributed data
Asymp. Sig. (2-tailed)	0,200	

Source: Processed Data, 2026

Based on the testing results, the empirical dataset was confirmed to satisfy the normality assumption. This is evidenced by a significance value (*p-value*) of 0.200, which exceeds the 0.05 threshold, thereby indicating that the data are normally distributed.

Autocorrelation Test

In the context of linear regression analysis, the autocorrelation test is a critical diagnostic procedure applied to ensure residual independence. Specifically, this test aims to verify the absence of serial correlation between error terms across adjacent time periods, which is essential for the validity of statistical inference. To detect potential autocorrelation in this study, the Durbin-Watson (DW) test was specifically implemented. The initial DW statistic of 1.493, which fell below the dU upper threshold of 1.721, confirmed the presence of autocorrelation. To address this issue and remediate the regression model, the Cochrane-Orcutt procedure was subsequently applied (Adrianto et al., 2023). Following correction via the Cochrane-Orcutt method, re-testing yielded a DW statistic of 1.940. Given that this value lies within the range between dU and 4 – dU (1.721 < 1.940 < 2.060), it can be concluded that the autocorrelation problem in the dataset has been successfully eliminated.

Multicollinearity Test

Table 3 shows the results of the multicollinearity test.

Table 3. Results of the Multicollinearity Test

Variabel	Tolerance	VIF	Description
LAG_TP	.644	1.553	There is no multicollinearity
LAG_ROA	.901	1.110	
LAG_GCG	.981	1.019	
LAG_TPxGCG	.659	1.518	

Source: Processed Data, 2026

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The diagnostic test indicates the absence of multicollinearity within the regression model, as evidenced by tolerance values exceeding 0.1 and Variance Inflation Factor (VIF) values remaining below 10.

Heteroscedasticity Test

Table 4 shows the results of the heteroscedasticity test using Glejser.

Table 4. Heteroscedasticity Test Results

Variabel	Sig.	Description
LAG_TP	.482	There is no heteroscedasticity
LAG_ROA	.100	
LAG_GCG	.510	
LAG_TPxGCG	.346	

Source: Processed Data, 2026

All variables are free of heteroscedasticity, with significance levels above 0.05.

Regression Test

Data analysis was performed utilizing multiple linear regression and Moderated Regression Analysis (MRA). In MRA, the regression equation incorporates an interaction term – derived from the product of the independent variable and the moderating variable – thereby enabling the evaluation of moderation effects. The regression estimation results of this study are presented as follows:

LAG_TA = 0,367 + 0,102LAG_TP – 0,009LAG_ROA – 0,049LAG_GCG – 0,069LAG_TP*GCG

Hypothesis Test

F Test

The F-test p-value of 0.000 ($p < 0.05$) indicates that the estimated model achieves a statistically significant goodness-of-fit. Simultaneously, these empirical results confirm that transfer pricing, profitability, and GCG exert a significant effect on tax avoidance.

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Test of the Coefficient of Determination (R^2)

With an Adjusted value of 0.94, it can be concluded that transfer pricing, profitability, and GCG collectively account for 94% of the variance in tax avoidance practices. The remaining 6% is attributable to other variables excluded from the empirical model.

t-Test

Table 5. Results of the t-Test

Variabel	Koefisien	t	Sig
LAG_TP	.102	3.680	.001
LAG_ROA	-.009	-7.264	.000
LAG_GCG	-.049	-2.038	.047
LAG_TPxGCG	-.069	-19.814	.000

Source: Processed Data, 2026

The -test results indicate that the first hypothesis (H_1) regarding transfer pricing is **supported**, showing a statistically significant positive effect ($p = 0.001 < 0.05$). Conversely, the second hypothesis (H_2) regarding profitability is **rejected**: although it yields a significance value of 0.000, the estimated coefficient is negative, contradicting the hypothesized positive relationship. Furthermore, the third hypothesis (H_3) concerning GCG is **supported**, showing a significance value of 0.047 in a positive direction. Finally, the fourth hypothesis (H_4), which examines the moderating role of GCG in attenuating the effect of transfer pricing on tax avoidance, yields a significance value of 0.000, thereby confirming that H_4 is **supported**.

DISCUSSION

The Effect of Transfer Pricing on Tax Avoidance

The empirical findings from hypothesis testing indicate that transfer pricing practices positively affect tax avoidance. This outcome aligns with prior research by Hidayat et al. (2024) and Iriyadi et al. (2024), which demonstrated a positive and significant association between the two variables. Consequently, a higher intensity of transfer pricing implementation is associated with a greater corporate propensity to engage in tax avoidance strategies. Transfer pricing practices refer to the systematic manipulation of transaction prices among related entities to depress corporate

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profitability artificially. The primary objective is to simulate reduced earnings or operational losses, thereby mitigating the tax liabilities remitted to the state. Although tax authorities enforce regulations to ensure that transactions between affiliated firms adhere to the arm's length principle, many enterprises continue to exploit transfer price manipulation to minimize their overall tax burden.

Findings by Adiguna and Ritonga (2024) demonstrate that business entities tend to implement transfer pricing strategies to reduce their global tax burden. This tendency is particularly pronounced and often serves as a primary strategic option, especially in environments with high corporate tax rates. Such practices represent a deliberate corporate maneuver to optimize fiscal liabilities across multiple jurisdictions. In line with agency theory, goal incongruence frequently arises between the government and corporate management. Leveraging information asymmetry, managers are incentivized to engage in opportunistic tax-avoidance behaviors, such as transfer pricing manipulation, to maximize corporate profitability. Consequently, while the government aims to optimize tax revenues for infrastructure development and public services, managerial opportunism erodes the national tax base and diminishes potential state revenues.

The Effect of Profitability on Tax Avoidance

The hypothesis-testing results indicate that profitability has a negative effect on tax avoidance. Although it diverges from initial expectations, this finding offers significant academic value by demonstrating a relational pattern that contrasts with the majority of prior studies, which predominantly reported a positive impact. Consequently, this study offers an alternative perspective that broadens the discourse on tax avoidance.

The findings of this study contrast with previous empirical research by Andriawan et al. (2024), Indriani (2023), and Wirianata et al. (2024), which reported that profitability positively affects tax avoidance, suggesting that firms with higher profitability tend to exhibit greater tax avoidance intensity. However, these results align with the findings of Oktaviana and Kholis (2021), who documented a negative relationship between profitability and tax avoidance practices. This outcome indicates that higher profitability is associated with a lower propensity for tax avoidance. An underlying explanation for this phenomenon is that highly profitable firms typically possess a more systematic tax management framework to achieve optimal tax efficiency, thereby constraining their inclination toward tax avoidance.

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The findings of this study contradict the core premise of agency theory. Under agency theory, heightened corporate profitability inherently yields more substantial net earnings. This financial condition subsequently motivates management to pursue profit maximization, which directly increases the corporate income tax burden. In response to these elevated tax liabilities, agency theory predicts that firms possess stronger incentives to engage in tax avoidance practices to minimize their overall fiscal burden (Rezki et al., 2020).

The Effect of Good Corporate Governance on Tax Avoidance

The hypothesis-testing results reveal that GCG, proxied by board size, has a negative effect on tax avoidance. This finding reinforces previous research by Susanto et al. (2024), which documented that a larger board size is associated with a reduced corporate propensity to engage in tax avoidance. This phenomenon indicates that a larger board, coupled with a diverse set of competencies, enhances corporate monitoring functions, thereby mitigating the inclination toward aggressive tax strategies. From a practical standpoint, these results underscore the vital role of corporate governance in shaping more responsible corporate tax policies. With more comprehensive oversight, the board of directors can foster stronger tax compliance by embedding principles of transparency, ethics, and regulatory compliance. In turn, this proactive and responsible tax management approach fosters strong trust among key stakeholders, including investors seeking market certainty and integrity, as well as tax authorities that emphasize fiscal compliance.

Empirical research by Noviari and Suaryana (2019) corroborates agency theory, demonstrating that GCG implementation significantly enhances financial reporting transparency. As a core pillar of GCG, this transparency is essential for reducing information asymmetry by equalizing data availability among management, shareholders, and broader stakeholders. The availability of such high-quality information mitigates potential agency conflicts, including aggressive tax avoidance, by constraining managerial opportunities for opportunistic behavior and enabling more rigorous oversight.

The Moderating Role of Good Corporate Governance in the Effect of Transfer Pricing on Tax Avoidance

Hypothesis testing results demonstrate that GCG attenuates the positive effect of transfer pricing on tax avoidance. The interaction between corporate governance and

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transfer pricing activities reduces corporate inclination to pursue tax avoidance strategies. Corporate transfer pricing is frequently identified as a tax avoidance mechanism, particularly when transaction prices are set artificially or deviate from the arm's length principle. To address this issue, robust implementation of corporate governance is paramount. Corporate governance serves as a primary oversight mechanism, ensuring business operations remain ethical and aligned with stakeholder interests. Consequently, corporate governance mitigates tax avoidance practices stemming from transfer pricing by providing stringent monitoring over corporate activities and effectively deterring management from engaging in non-transparent or unethical practices (Fasita et al., 2022).

These findings are reinforced by Dharmawan et al. (2024), who similarly documented that GCG moderates and weakens the impact of transfer pricing on tax avoidance. In greater detail, their study indicated that related-party transactions, which often involve transfer pricing mechanisms, serve as a primary vehicle for corporate tax avoidance. Nevertheless, effective GCG implementation has been shown to constrain this tendency. GCG mitigates the tax avoidance risks associated with transfer pricing by guiding management toward strict compliance with legally binding regulations and safeguarding stakeholder rights. This outcome is facilitated by the GCG framework, which encompasses ethical principles, operational guidelines, and regulatory recommendations established by supervisory authorities such as the Financial Services Authority (OJK), serving as an internal control mechanism governing managerial decisions and actions.

From an agency-theory perspective, the link between transfer pricing practices and tax-avoidance efforts can be conceptualized. This association primarily stems from a lack of transparency or inadequate disclosures regarding related-party transactions within corporate financial statements. Such conditions directly induce information asymmetry between management and principals, most notably shareholders and tax authorities. Consequently, principals incur substantial costs, particularly monitoring costs to discern the extent of transfer pricing activities and to evaluate managerial performance and accountability accurately. In this context, the implementation of GCG is a critical governance mechanism for mitigating these information gaps. By adopting the GCG practice framework recommended by the Financial Services Authority (OJK), enterprises not only alleviate information asymmetry but also effectively safeguard stakeholder rights and enhance overall firm value.

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CONCLUSION

The empirical findings reveal that heightened transfer pricing practices exert a positive and statistically significant effect on tax avoidance. Conversely, profitability exhibits a significant negative relationship with the propensity for corporate tax avoidance. Furthermore, board size, serving as a proxy for GCG, has been shown to have a significant negative impact on tax avoidance practices. Most notably, the results indicate that GCG not only exerts a direct effect but also significantly attenuates the positive association between transfer pricing and tax avoidance, thereby underscoring its pivotal role as a crucial mitigating mechanism.

Several limitations of this study warrant consideration. First, the five-year observation period (2020–2024) is relatively brief, primarily due to data availability constraints, which precluded the adoption of a longer timeframe. Second, the dataset exhibited inherent distributional constraints, as evidenced by the necessity of data transformation to satisfy basic statistical assumptions before hypothesis testing.

Based on these findings, several recommendations for future research are proposed. First, subsequent studies are advised to employ an extended observation period to provide a more comprehensive framework of inter-variable relationships and yield more stable, representative findings. Additionally, a longer timeframe enables the examination of macroeconomic shifts and regulatory dynamics that could influence empirical outcomes. Second, future research should use higher-quality, more comprehensive datasets to minimize reliance on data transformation. Should data transformation remain necessary to satisfy statistical assumptions, scholars ought to explicitly delineate the specific transformation technique employed along with its underlying rationale. Alternatively, subsequent studies may consider adopting estimation methods that are robust to violations of assumptions, thereby preserving the validity of the findings even when the data structure does not strictly adhere to classical assumptions.

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