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The Effect of Transfer Pricing, Earning Management, CSR and Firm Size in Tax Avoidance

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Abstract

This study aims to analyze the effect of Transfer Pricing, Earning Management and Corporate Social Responsibility on Tax Avoidance with Firm Size as a Moderating Variable. This quantitative study uses secondary data obtained and can be accessed through the Indonesia Stock Exchange website. The sample for this study consisted of 62 manufacturing companies. This study uses purposive sampling to select the desired sample. The analysis method of this study uses linear regression analysis and moderated regression analysis as analysis tools in Eviews. The study reveals that Transfer Pricing, Earning Management, and Corporate Social Responsibility significantly influence Tax Avoidance in manufacturing firms during 2018–2022. Firm Size strengthens the impact of Transfer Pricing and Corporate Social Responsibility on Tax Avoidance, acting as a moderating factor. However, it does not moderate the relationship between Earning Management and Tax Avoidance. This indicates that Firm Size plays a selective role in amplifying the effects of certain factors on Tax Avoidance but is ineffective in influencing others. These findings highlight the complexity of tax avoidance mechanisms and the varied roles played by organizational characteristics like Firm Size.

Keywords

Earning Management, Firm Size, Tax Avoidance Transfer Pricing.

1. Introduction

Tax is one of the main sources of state revenue that plays an important role in supporting national development. As the largest element in the structure of the State Budget (*Anggaran Pendapatan dan Belanja Negara*/APBN), tax has an essential budgetary function to finance various state expenditures (OECD, 2021). However, although the realization of tax revenue in Indonesia in 2017-2022 showed fluctuating achievements, this figure is still far from optimal. Indonesia's tax ratio of only 10.9% is still far below the average for Asia Pacific (19.8%) and OECD countries (34.3%) (OECD, 2023). This has an impact on obstacles in achieving national development targets, including reducing poverty, inequality, and unemployment (Indonesia, 2022). To overcome these obstacles, the Directorate General of Taxes (*Direktorat Jenderal Pajak*/DJP) has made various efforts to optimize tax revenues through the implementation of the Law on Harmonization of Tax Regulations (*Undang-Undang tentang Harmonisasi Peraturan Perpajakan*/UU HPP) and supervision of strategic sectors, one of which is the manufacturing sector. Based on data from the Central Statistics Agency (*Badan Pusat Statistik*/BPS), this sector is the largest contributor to Gross Domestic Product (GDP) with an average contribution of 18.34% in 2022 (BPS, 2022). However, the high tax burden on manufacturing companies often encourages tax avoidance practices, which have a negative impact on state revenues (Sriyono & Andesto, 2022).

Tax avoidance is a legal effort made by companies to reduce tax obligations by exploiting loopholes in tax regulations (Drake et al., 2019). In practice, companies use various strategies such as transfer pricing, earnings management, and disclosure of corporate social responsibility (CSR). Transfer pricing is often used by multinational companies to transfer profits between entities in different jurisdictions to take advantage of lower tax rates (Choi et al., 2020). Research shows that this strategy significantly contributes to tax avoidance in many countries (Flaaen, 2017; Amidu et al., 2019). In addition to transfer pricing, earnings management is another technique used by companies to minimize tax liabilities (Galingging, 2024). By utilizing the flexibility of accounting standards, management can manage company profits to reduce taxes payable (Siska et al., 2024).

CSR is often used as a strategy to improve a company's reputation while reducing the tax burden. Several studies have shown that CSR spending can be categorized as costs that reduce taxable profit (Chouaibi et al., 2022; Jiang et al., 2022). Company size or firm size plays an important role in tax strategy. Large companies tend to have higher operational complexity and access to resources to design more effective tax avoidance strategies (Wardani & Wijayanti, 2022). However, large companies are also under stricter supervision, which can limit their flexibility in practicing tax avoidance (Nurlis et al., 2021). Studies on the effect of transfer pricing, earnings management, and CSR on tax avoidance have been widely conducted. However, the results of the study still show inconsistencies such as previous studies that found a positive relationship between transfer pricing and tax avoidance (Amidu et al., 2019). Meanwhile, Mukhtar (2021) shows the opposite relationship between transfer pricing and tax avoidance. Likewise, the moderating role of firm size on these variables still requires further exploration to provide a more comprehensive picture (Abdullah et al., 2021; Komara et al., 2022).

This study analyzes how Transfer Pricing, Earnings Management, and Corporate Social Responsibility affect Tax Avoidance, with Firm Size as a moderating variable. This study examines whether Firm Size strengthens or weakens the relationship between these factors and Tax Avoidance. By examining this interaction, this study aims to provide insight into the role of organizational characteristics in influencing tax strategies, offering a deeper understanding of how these variables contribute to tax avoidance practices in companies.

2. Literature Review

According to Jensen & Meckling (1976), agency theory explains the conflict of interest between the principal (owner) and agent (company management) that occurs when both parties have different goals. In the context of taxation, the principal (government) expects the company to fulfil tax obligations according to regulations, while the agent tends to prioritize optimizing profits by minimizing the tax burden through strategies such as transfer pricing, earnings management, and firm size (Mpaata et al., 2022). Legitimacy theory, according to Deegan et al. (2002), argues that companies seek to gain social legitimacy through disclosure of information that is consistent with community norms and expectations. CSR is an important tool in increasing this legitimacy, although some studies show that CSR is also used as a strategy to reduce tax liabilities (Chouaibi et al. 2022; Sari & Meirina, 2023). Tax avoidance is a legal strategy to reduce tax liabilities by exploiting loopholes in tax regulations (Drake et al., 2019). This practice is often measured using proxies such as Effective Tax Rate (ETR), Cash ETR, or Book Tax Difference (BTD) (Barros & Sarmento, 2020). Tax avoidance is often the focus of studies because of its impact on state revenue and corporate legitimacy (OECD, 2021).

Transfer pricing is a strategy used by multinational companies to determine transaction prices between entities within a corporate group. Research by Adiguna & Ritonga (2024) and Rizki & Nugroho (2024), shows that transfer pricing is a primary tool in tax avoidance, especially when companies operate in jurisdictions with different tax rates. This strategy can shift profits to countries with low tax rates, thereby reducing tax liabilities. Earning management allows companies to organize financial statements to achieve certain goals, such as attracting investors or reducing the tax burden. Research by Siska et al. (2024) and Indriani & Ramli (2024), shows that earning management is often used to carry out tax avoidance, especially through accrual manipulation. CSR reflects the company's responsibility to society and the environment. Research by Chouaibi et al. (2022) and Sibarani & Tarmidi (2024), shows that CSR disclosure can affect the level of tax avoidance. In some cases, CSR is used as a tool to improve the company's image while minimizing taxes through cost allocation. Firm size describes the size of the company's scale based on total assets or revenue. Research by Wardani et al. (2021) and Nurlis et al., 2021) shows that large companies tend to have more resources to practice tax avoidance, but are also under stricter supervision from regulators.

Research by Amidu et al. (2019), shows that transfer pricing is a major strategy in moving profits to low-tax jurisdictions, which significantly reduces tax liabilities. Research by Maqsood et al. (2024), shows that companies involved in earnings management tend to use this strategy to reduce tax burdens while maintaining financial performance. CSR is often used to reduce taxable income through costs that can be categorized as operating expenses (Chouaibi et al., 2022; Jiang et al., 2022). Research by Komara et al. (2022), states that large companies with higher complexity tend to use transfer pricing to reduce taxes, although they are also under strict supervision. Research by Nurlis et al. (2021b), shows that large companies have higher flexibility to practice earnings management, but its effect may depend on regulatory pressure and public reputation. Abdullah et al. (2021), shows that large companies tend to use CSR as a tool to mitigate reputational risk, which can strengthen or weaken the relationship between CSR and tax avoidance depending on the context of the company's strategy.

H1: Transfer pricing has significant effect on tax avoidance.
H2: Earning management has significant effect on tax avoidance
H3: Corporate Social Responsibility has significant effect on tax avoidance.
H4: Firm size moderates the effect of transfer pricing on tax avoidance.

H5: Firm size moderates the effect of earnings management on tax avoidance.
H6: Firm size moderates the effect of CSR on tax avoidance.

3. Methods

This study investigates tax avoidance among manufacturing companies listed on the Indonesia Stock Exchange (IDX) from 2018 to 2022, using purposive sampling (Gozali & Nasehudin, 2019). A total of 62 companies over five years generated 310 observations. The data, obtained from annual financial reports on the IDX website (www.idx.co.id), were analyzed using EViews software. Tax avoidance was measured by the Effective Tax Rate (ETR), calculated as the ratio of tax paid to the tax burden before tax. Transfer pricing was assessed using the ratio of affiliated accounts receivable to total receivables, earnings management through Discretionary Accruals with the Modified Jones model, and Corporate Social Responsibility (CSR) using the CSR Index (GRI Standards). Firm size, the moderating variable, was measured by the natural logarithm of total assets. The analysis began with descriptive statistics to understand the data distribution, including mean, standard deviation, and range. Panel regression analysis was then employed to examine the effects of transfer pricing, earnings management, and CSR on tax avoidance. The appropriate regression model was determined using the Chow and Hausman tests to select between the Common Effect Model (CEM), Fixed Effect Model (FEM), and Random Effect Model (REM). The Moderated Regression Analysis (MRA) method assessed how firm size interacts with independent variables to influence tax avoidance. Hypotheses were tested using t-tests for individual variables and F-tests for their combined effects. The moderated regression results evaluated the moderating role of firm size in the relationship between transfer pricing, earnings management, CSR, and tax avoidance. This comprehensive approach provided insights into the dynamics of tax policy and company characteristics in shaping corporate tax strategies.

4. Results

Descriptive analysis is used to provide an overview of the research data. Based on the results of descriptive analysis in this study using data from 62 manufacturing companies listed on the Indonesia Stock Exchange (IDX) during the period 2018-2022. The dependent variable, Tax Avoidance, measured by the Effective Tax Rate (ETR), shows the variation in the level of tax avoidance among companies, with the average reflecting a moderate level of tax avoidance.

Table 1. Descriptive Statistical Analysis

Variables	N	Minimum	Maximum	Mean	Std. Dev.
TP	310	0.012	0.994	0.533	0.2277286
ERM	310	- 9.985.741	9.596.579	- 29.693	4.636.277
CSR	310	0.257	0.838	0.506	0.1161064
SIZE	310	20.619	33.655	29.065	2.0248358
TA	310	- 0.417	1.352	0.465	0.510448

Based on the Table 1, the independent variable Transfer Pricing, measured by the ratio of sales to related parties to total sales, shows an average Transfer Pricing value of 0.533, meaning that the proportion of related party receivables to total receivables is around 53.3% in the companies in the sample with a standard deviation of 0.2277286 indicating a variation in transfer pricing policies among the companies in this sample. The Earning Management variable, measured using discretionary accruals (Modified Jones Model), shows a negative average earnings management value (-29.693) indicating a tendency to reduce profits in most companies in the

sample and a standard deviation of 4,636.277 indicating a very high variation between companies in earnings management practices. Meanwhile, the Corporate Social Responsibility (CSR) variable, which is measured based on the GRI (Global Reporting Initiative) disclosure index, the average CSR value of 0.506 indicates that the level of company compliance with corporate social responsibility practices is around 50.6% and the standard deviation is 0.1161064, the level of corporate social responsibility commitment varies quite a lot between companies. The moderation variable Firm Size, which is measured using the natural logarithm of the company's total assets, shows an average of 29.065 indicating that most companies in the sample have relatively large asset sizes with a standard deviation of 2.0248358 indicating that company sizes vary quite a lot in the sample, but remain within the limits of large company sizes.

From the results of the regression of the selection of the estimation model, the approach used was FEM, where the results show:

Table 2. Fixed Effect Model

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-6.550322	0.989139	-6.622249	0.0000
TP	-0.408425	0.121781	-3.353766	0.0009
EM	-0.003145	0.000603	-5.217887	0.0000
CSR	-1.158015	0.275711	-4.200105	0.0000
SIZE	0.259176	0.034628	7.484516	0.0000

Based on the Table 2, the results of the analysis using the Fixed Effect Model show that all variables in the model are statistically significant at the 95% confidence level (p-value <0.05). The constant (C) has a coefficient of -6.550322, which indicates that when all independent variables are zero, the value of the dependent variable is -6.550322. The TP variable has a coefficient of -0.408425, which means that every increase in one unit of TP will decrease the dependent variable by 0.408425. The EM variable also has a negative effect with a coefficient of -0.003145, indicating a decrease in the dependent variable by 0.003145 for every increase in one unit of EM. Likewise, the CSR variable has a negative effect with a coefficient of -1.158015, while the SIZE variable shows a positive relationship with the dependent variable, with a coefficient of 0.259176. Thus, the TP, EM, and CSR variables have a negative effect, while SIZE has a positive effect on the dependent variable in this model.

The normality test aims to test whether in the regression model, the confounding variables or residuals have a normal distribution or not. Here are the results of the normality test:

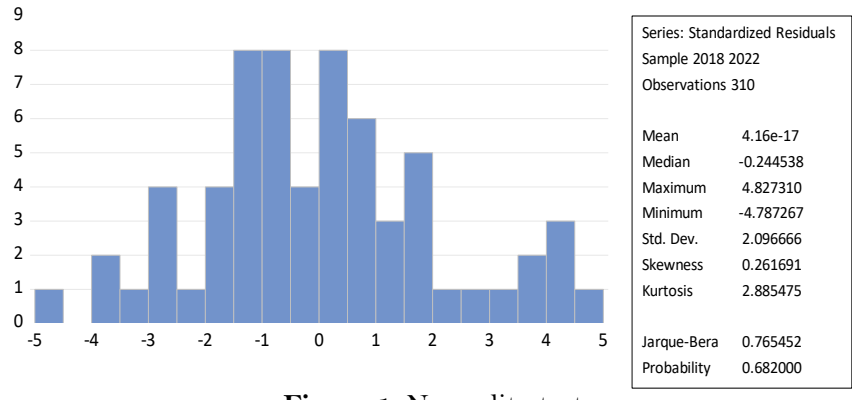

Figure 1. Normality test

Based on the Figure 1, the Jarque-Bera (J-B) value is 0.765452 with a probability value of 0.682000. This value indicates a probability of acceptance of 0.682000 greater than the significance level (0.682000> 0.05), so it can be concluded that the data is normally distributed.

The multicollinearity test aims to test whether a high or perfect correlation is found in the regression model between independent variables. The following is the multicollinearity test:

Table 3. Multicollinearity test

Variables	TP	EM	CSR	SIZE
TP	1.000000	0.134520	0.099616	0.023129
EM	0.134520	1.000000	0.047833	0.055348
CSR	0.099616	0.047833	1.000000	0.132429
SIZE	0.023129	0.055348	0.132429	1.000000

Based on the Table 3, the multicollinearity test with correlation values between the variables TP, EM, CSR, and SIZE. Based on these results, all VIF (Variance Inflation Factor) values for each variable are below 10, which is a commonly used threshold to detect multicollinearity problems. Multicollinearity occurs when there is a very strong linear relationship between independent variables, which can interfere with parameter estimation in the regression model. Since the VIF values of all variables are within reasonable limits (<10), it can be concluded that there is no multicollinearity problem in this data. This indicates that each independent variable can make a unique contribution to the model without significantly influencing each other.

The autocorrelation test aims to test whether in the linear regression model there is a correlation between the residual error in period t with the error in period t-1 (previous). Here is the autocorrelation test:

Table 4. Autocorrelation test results

Test	Value
dl	1.52318
4-dl	2.47682
du	1.65605
4-du	2.34395
dw	2.179611

Based on the Table 4, the results of the autocorrelation test using the Durbin-Watson test show that the Durbin-Watson (dw) value of 2.179611 is within the upper limit (du) range of 1.65605 and its complementary value (4-du) of 2.34395. This indicates that there is no autocorrelation, either positive or negative, in the regression model being tested. In addition, the dw value is also not in the uncertainty zone, which is between the lower limit (dl) of 1.52318 and the upper limit (du). Thus, it can be concluded that the classical assumptions of regression related to residual independence have been met in the model.

The determination coefficient test (R^2 Test) is used to determine the closeness or relationship between the dependent variable and the independent variable. This study uses the R2 value with a range of values between 0 and 1. Simultaneous test hypothesis testing is used to see whether the independent variables have an overall effect on the dependent variable.

Table 5. Test of determination coefficient (R^2 Test) and F Test

Model	*Adjusted R-squared*	Prob(F-statistic)
Model 1	0.628526	0.000000

Model 2	0.748621	0.000000

Based on the Table 5, the Fixed Effect Model (FEM) model, the Adjusted R-squared value of model 1 is 0.628526 or 62.85%. This indicates that the independent variables of transfer pricing, earnings management, and corporate social responsibility on tax avoidance are 62.85%, while the remaining 37.15% is explained by other variables outside this study. The Adjusted R-squared value of Model 2 is obtained at 0.74751, which means that the contribution of the influence of the transfer pricing, earnings management, corporate social responsibility, firm size, and firm size moderation variables (TP_SIZE, EM_SIZE, CSR_SIZE, to tax avoidance is 74.75%. After entering the moderation variable, the influence of the independent variable on the dependent variable becomes stronger, which initially had an influence of 62.85% (before entering the moderation variable) to 74.75% (after entering the moderation variable). The results of the F test show that the significance value of model 1 is 0.0000 <0.05 and model 2 is 0.0000 <0.05, so transfer pricing, earnings management, corporate social responsibility, have a simultaneous effect. Likewise, model 2 shows that the transfer pricing, earnings management, corporate social responsibility variables, with firm size moderation simultaneously affect tax avoidance so that the model is declared 'fit' (the research regression model is said to be feasible to be carried out in hypothesis testing).

The heteroscedasticity test aims to test whether in the regression model there is inequality of variance from the residuals of one observation to another. The purpose of the t-test is to see the direct effect of the independent variable on the dependent variable partially. Moderation regression analysis is a regression analysis that involves moderating variables in building a model of its relationship.

Table 6. Heteroscedasticity and MRA Test

Test	Variable	Coeff.	Std. Error	t-Statistic	Prob.
Heteroscedasticity	C	0.082799	0.160461	0.516006	0.6063
	TP	0.011782	0.019756	0.596378	0.5515
	EM	-7.10E-05	9.78E-05	-0.726720	0.4681
	CSR	-0.079886	0.044727	-1.786085	0.0753
T	C	-6.550322	0.989139	-6.622249	0.0000
	TP	-0.408425	0.121781	-3.353766	0.0009
	EM	-0.003145	0.000603	-5.217887	0.0000
	CSR	-1.158015	0.275711	-4.200105	0.0000
MRA	C	-13.37421	2.042709	-6.547292	0.0000
	TP_SIZE	-0.319675	0.045040	-7.097637	0.0002
	EM_SIZE	-0.000870	0.000161	-5.397028	0.0621
	CSR_SIZE	-0.568963	0.107041	-5.315367	0.0000

Based on the Table 6, the results of the Heteroscedasticity test show that the constant (C) is 0.082799, meaning that if all independent variables are zero, then the average of the dependent variable is 0.082799. The TP variable has a coefficient of 0.011782, and EM is -7.10E-05, but both are not statistically significant (p-values of 0.5515 and 0.4681, respectively). The CSR variable has a coefficient of -0.079886, which indicates a negative effect on the dependent variable, with significance approaching the 10% confidence level (p-value 0.0753). Overall, only CSR is almost significant, while the other variables are not significant.

The T test, show the transfer pricing variable probability value of 0.0009 <0.05, so it can be concluded that transfer pricing has a significant effect on tax avoidance so that hypothesis 1 is accepted. The earning management variable shows a probability value of 0.0000 <0.05, so it can be concluded that earning management has a significant effect on Tax Avoidance, so that hypothesis 2 is accepted. The corporate social responsibility variable shows a probability value of 0.0000 <0.05, so it can be concluded that corporate social responsibility has a significant effect on tax avoidance, so that hypothesis 3 is accepted

The MRA test It is known that the regression coefficient value of the interaction of transfer pricing and tax avoidance is -0.319675 with a Prob value of 0.0002, where < with a significance level of 0.05. With the coefficient value indicating a decrease in the ETR value, which means that the moderation direction is strengthening. This means that hypothesis 4 is accepted. The results of the study prove that firm size is able to moderate the effect of transfer pricing on tax avoidance. It is known that the regression coefficient value of the interaction of earning management and tax avoidance is -0.000870 with a Prob value of 0.0621, where < with a significance level of 0.05. With the coefficient value indicating a negative direction (decrease in ETR). This means that Hypothesis 5 is rejected. The results of the study prove that firm size is not able to moderate the effect of earning management on tax avoidance. It is known that the regression coefficient value of the interaction of corporate social responsibility and tax avoidance is -0.568963 with a Prob value of 0.0000, where < with a significance level of 0.05. With the coefficient value indicating a decrease in

the ETR value, which means that the direction of moderation is strengthening. This means that Hypothesis 6 is accepted. The results of the study prove that firm size is able to moderate the effect of corporate social responsibility on tax avoidance

Linear regression testing produces a constant value (α) with a negative value of 6.550322, which indicates that if the Transfer Pricing, Earning Management, Corporate Social Responsibility variables have a constant value, then the ETR is 6.550322. The TP regression coefficient (X1) is -0.408425. This can be interpreted that if the TP variable increases by one unit, the ETR level will decrease by -0.408425, which indicates positive tax avoidance. The EM regression coefficient (X2) is -0.003145. This can be interpreted that if the EM variable increases by one unit, the ETR level will decrease by -0.003145, which indicates positive tax avoidance. The CSR regression coefficient (X3) is -1.158015. This can be interpreted that if the CSR variable increases by one unit, the ETR level will decrease by -1.158015, which means positive tax avoidance.

5. Discussion

Transfer pricing has been shown to have a significant effect on tax avoidance. Companies use transfer pricing mechanisms to exploit loopholes in tax regulations, such as moving profits to jurisdictions with low tax rates, setting prices below fair market prices, or not charging interest on related receivables transactions. This strategy is in line with agency theory, which explains the conflict between agents (management) and principals (owners). Management has an incentive to reduce the tax burden in order to increase company profits, even though this can harm the interests of the tax authorities. This study is consistent with the findings of (Herianti & Chairina, 2019; Ramdhani et al., 2021). Earning management also shows a significant effect on tax avoidance. Profit manipulation is carried out by increasing accruals to reduce taxable profit, so that the taxes paid are lower. This practice is in line with agency theory, where management uses accounting discretion to achieve personal or corporate goals. This is in line with agency theory, where managers as agents use accounting discretion to achieve certain goals, including reducing tax liabilities. These results are in line with research by Irawan et al. (2020) and Sholikhah & Sari (2023), which shows that earnings management has a positive effect on tax avoidance.

CSR is proven to have a significant effect on tax avoidance. The higher the CSR disclosure, the greater the opportunity for companies to utilize CSR spending to reduce gross income and tax burdens. This is in accordance with the legitimacy theory, which states that companies utilize CSR to improve their reputation and gain legitimacy from the community, although it is often associated with tax avoidance strategies, and this study is consistent with the results of (Abdullah et al., 2021; Chouaibi et al., 2022). Firm size strengthens the effect of transfer pricing on tax avoidance. Large companies tend to be more flexible in utilizing transfer pricing strategies to minimize tax burdens. In the context of agency theory, large companies face higher agency costs because supervision is more difficult, thus providing greater opportunities for managers to utilize transfer pricing, and this finding supports the research of (Komara et al., 2022).

Firm size does not moderate the relationship between earnings management and tax avoidance. This shows that company size, both large and small, does not affect the effectiveness of earnings management in influencing tax avoidance. The homogeneity of the sample and strict supervision of large companies are likely the main reasons for this insignificance. This finding is consistent with Nurlis et al., (2021), that firm size does not moderate the relationship between earnings management and tax avoidance. Firm size strengthens the effect of CSR on tax avoidance. Large companies with more resources have a higher capacity to integrate CSR into tax strategies. This supports agency theory and legitimacy theory, where

large companies use CSR to maintain their reputation while reducing their tax burden and this result is consistent with research (Abdullah et al., 2021).

6. Conclusion

This study concludes that transfer pricing, earnings management, and CSR have a significant effect on tax avoidance in manufacturing companies listed on the IDX during the period 2018–2022. Firm size moderates the relationship between transfer pricing and CSR on tax avoidance, but does not moderate the relationship between earnings management and tax avoidance. The practical implication of this study is the need for stricter supervision of large companies, especially in monitoring transfer pricing practices and CSR spending to ensure tax compliance. Regulators also need to develop more specific tax policies to reduce loopholes that allow tax avoidance practices through transfer pricing, earnings management, and CSR. As a suggestion, future research can consider other moderating variables, such as corporate governance or regulatory influence, to provide a more comprehensive understanding of the dynamics of tax avoidance in the manufacturing sector.

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