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## The Effect of Foreign Ownership, Bonuses, and Company Size on Transfer Pricing

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### Abstract

This study aims to analyze the influence of foreign ownership, bonuses, and company size on a company's decision to use transfer pricing. The research was conducted on 185 manufacturing companies listed on the Indonesia Stock Exchange during the 2019–2023 period. The approach used is a quantitative descriptive method. The results show that bonuses have a negative effect on performance, with a negative coefficient value of -0.003. This indicates that providing bonuses may reduce a company's tendency to use transfer pricing as a strategy. Meanwhile, foreign ownership also has a small negative impact on transfer pricing decisions, with a coefficient value of -0.006 and a significance level of 0.482, indicating an insignificant effect. On the other hand, company size is found to have a significant positive impact on transfer pricing, with a coefficient value of 0.743 and a highly significant level of 0.000. This study provides insights that company size is the dominant factor influencing transfer pricing decisions, while the effects of bonuses and foreign ownership are relatively small and insignificant. These findings contribute to a better understanding of the factors influencing transfer pricing practices in manufacturing companies in Indonesia.

### Keywords

Foreign Ownership, Bonuses, Company Size, Transfer Pricing.

## 1. Introduction

The rapid growth of the global economy has contributed to the expansion of multinational corporations. In these companies, there is international commerce among the members of the company, such as the marketing of goods or services. This business commerce often involves companies that maintain a special relationship between them (Kurniasih et al., 2013; Ningsih et al., 2020). By moving income and profits to nations with lower tax rates, multinational corporations frequently employ tax management techniques like transfer pricing to optimize earnings (Pranatio & Sutrisno, 2024). Since taxes are the primary source of income for developing nations like example Indonesia, this practice has resulted in significant losses for such nations. As a result, the author's focus while investigating the motivations of businesses that engage in transfer pricing (Eden & Smith, 2001; Kiselbach & Albrecht, 2011; Anggraeni et al., 2023).

In practice, transfer pricing involves the adjustment of buying and selling prices between two or more companies, with the aim of shifting profits to a country at a lower tax cost (Prasetio & Mashuri, 2020). This is due to the special relationship that the two companies have, which allows them to negotiate the transfer price. This special relationship can result in prices, fees, or other rewards that are not fair in business dealings. Indonesia suffers losses of up to trillions of rupiah year as an effect of the implementation of the transfer pricing, which lowers state revenue (Scott, 2015; Saraswati & Sujana, 2017; Ridwan, 2023). The state lost IDR 1,750 trillion as the result of this implementation of transfer pricing in 2017 alone; this is less than the IDR 1,822 trillion in income from the year before. Since the corporation lacks a reference or tax base, it is exceedingly challenging to predict the possible loss of tax income resulting from the use of transfer pricing (Siallagan & Machfoedz, 2006; Susilawati et al., 2022; Wori et al., 2023).

The implementation is due to the determination of managerial provisions to carry out all management of company assets and also determine transfer prices for affiliated companies (Pambayun, 2021). Concentrated shareholding in certain entities or interests will reduce the power to regulate the business operations of the companies they control. Nowadays, there is a tendency for shareholdings in multinational companies to become more concentrated (Laeq, 2021; Shah, 2022). When foreign shareholders hold a large stake, it means that they have already investing significant amount of capital in that company. Naturally, they would expect a proportionate dividend from their investment. If the corporation must pay dividends to minority shareholders, the majority will prefer to utilize transfer pricing techniques rather than do so. This further demonstrates that transfer pricing is more likely to be used the larger the majority holder's shareholding level (Hartati et al., 2015; Putranti et al., 2020).

Multinational companies often have entities in various countries. This phenomenon leads to transfer pricing practices to allocate income and costs between these entities, foreign ownership may take advantage of tax rates differences between countries to globally optimize tax liabilities. Studies conducted on the influence of multinational companies on applying transfer pricing schemes, namely foreign ownership, as stated by Indrasti (2016) and Refgia et al. (2016). Foreign ownership often creates conflicts of interest among majority and minority shareholders when foreign shareholders retain control over the company and can also influence various company provisions, including pricing and transfer of intangible assets through transfer pricing schemes. The study presented by Mashuri (2020) says that foreign ownership has a positive impact on companies to carry out transfer pricing practices, while in the study presented by Hasibuan (2021) says that foreign ownership has a negative impact on companies that doing transfer pricing practices.

Bonuses that are given to management is often based on the financial performance of the company. This phenomenon can affect transfer pricing policies because management may be motivated to set transfer prices to maximize visible profits, Performance-based bonuses can encourage certain practices in financial reporting and allocation of income between entities in the corporate group. Similar studies also indicate that if the provision of bonuses has an impact on the company's provisions related to transfer pricing, this is because when lowering bonuses for directors, company owners want to evaluate the performance of directors in managing the company. Like the study proposed by Sudarmanto et al. (2024) said bonuses have a positive impact on the practice of companies implementing transfer pricing practices, in the study developed by Mineri & Paramitha (2021) said bonuses have a negative impact on companies implementing transfer pricing practices.

The size of a company is determined by the scale of the company, oftentimes measured by the total number of assets that the company owned. Company size can affect the extent to which transfer pricing is implemented by a company. Larger companies have more resources and higher operational complexity, which can affect transfer pricing practices, companies that are relatively larger in size tend to exercise greater transparency and vigilance in reporting their financial conditions because their performance is monitored by the public. On the other hand, smaller companies have a tendency to practice transfer pricing in order to appear to have better work performance, company size can affect the company's ability and policy in setting transfer prices, both for operational and strategic purposes. While the study suggested by Nurwati et al. (2021) claimed that variable of a company size has a negative influence on companies applying transfer pricing, research by Adilah et al. (2022) found that the size of a company has an impactful benefits on the transfer pricing implementation.

## **2. Literature Review**

One type of compensation that permanent employees may earn on an irregular basis is a bonus. Employees of commercial entities receive bonuses as part of their income when a company makes a net profit, Bonuses are a portion of the profits distributed to directors by shareholders. Giving management some bonuses can be a useful strategy to encourage directors or management to raise the performance of the company. Moreover, Business's post-tax profit' percentage determining the Commissioner's calculations. Grants and gratuities are mentioned in the circular letter's highlights in relation to incentive distribution. Bonuses are dependent on work position and are decided by the CEO of the firm, according to Mineri & Paramitha (2021). As example, the bonuses given for the company's directors or managements usually in the form of commissions, various allowances, compensations for intense sales results, and other various incentives. Board members received the bonuses after being figured in the General Meeting of Shareholders (GMS) held each year (Hanggiani et al., 2024).

Generally, the most popular method employed by a company to compensate directors and managers is profit-based incentives, Transfer pricing is regarded as a strategy that can be applied to raise expected profits. If bonuses are tied to business profitability and are calculated using the Index of Net Income Trend (ITRENDLB), managers will increase their net income and enhance their income reporting (Syarifah & Hersugondo, 2024). Modifying the structure of transactions between related parties is a strategic method that directors or management can use to manipulate earnings, thereby maximizing their bonus income, especially when it is tied to profit levels.

**H1:** Bonus has a positive effect on the implementation of transfer pricing scheme in the company.

These foreign controlling shareholders can sell products from a business they own to a connected business at a price that may be significantly less than market value by employing transfer pricing techniques (Hanggiani et al., 2024). These foreign controlling shareholders do so in order to gain personal benefits, which in turn can be detrimental to foreign and local non-controlling shareholders. Larger stakes held by foreign controlling shareholders will give them more sway over decisions pertaining to the company, such as volume and pricing rules in transfer pricing transactions. Foreign ownership percentage affects transfer pricing practices within company's decision. When foreign shareholder owns a larger percentage of shares in a company, they have greater influence over many choices, including policies of pricing and transfer pricing (Ramadhan et al., 2024).

**H2:** Foreign ownership has a positive effect on the implementation of transfer pricing scheme in the company.

Assessing the size of a company is a measure of a company's heft and reach, often gauged by its financial clout, workforce, or annual turnover. Company size means the scale of the company that can be measured by the total number of assets it has. Company size can affect the extent to which transfer pricing is implemented by the company. Larger companies tend to have greater transparency and vigilance when reporting their financial condition because their performance is monitored by the public (Ridwan, 2023). On the other hand, large companies with several segments, divisions, and subsidiaries will encourage the implementation of transfer pricing practice policies to transfer services or goods between divisions, segments, and subsidiaries. Transfer pricing decisions are made to optimize the company's profits. Companies of all sizes, large and small, can use transfer pricing procedures with management considerations that benefit the organization.

**H3:** Company size has a positive effect on the implementation of transfer pricing scheme in the company.

### 3. Methods

This study in financial economics adopts a quantitative approach, utilizing secondary data from the annual financial statements of manufacturing companies listed on the Indonesia Stock Exchange (IDX) for the 2019–2023 period, accessed via Bloomberg. The population consists of 465 manufacturing companies that consistently published their annual reports on the IDX during this period. The sample was selected based on specific criteria: (1) companies must be listed and publish annual reports on the IDX; (2) financial reports must include comprehensive data for the 2019–2023 period; (3) companies must not report losses during the study period; and (4) shareholding must be predominantly controlled by foreign parties. These criteria ensure that the data used is relevant and reliable for financial analysis. This study aims to understand various financial dynamics influencing corporate strategies, such as transfer pricing policies, management bonuses, foreign ownership, and company size. By focusing on verified and up-to-date data, this research contributes to insights into financial management and corporate behavior in the manufacturing sector, particularly regarding foreign investor involvement and the management of corporate assets.

### 4. Results

This study examines four variables: Transfer Pricing, defined as a company's policy for determining transaction prices between affiliated entities; Bonus, which represents the rewards allocated to management or board members based on success

as determined in the General Meeting of Shareholders, calculated as net profit divided by net profit from the prior period; Foreign Ownership, which measures the proportion of a company’s capital owned by foreign individuals or entities, calculated as the ratio of foreign ownership to total shares; and Company Size, which indicates the scale of the company as reflected by its total assets, expressed in logarithmic form (Log of Total Assets). These variables are essential for analyzing the financial dynamics and corporate strategies in the study.

**Table 1. Model Fit**

		Iteration History <sup>a,b,c,d</sup>				
		-2 Log likelihood	Coefficients			
Iteration			Constant	Bonus	Company Size	Foreign Ownership
1	Step 1	162.239	-7.589	-.002	.316	-.003
	2	151.824	-14.518	-.003	.577	-.005
	3	150.451	-18.251	-.003	.716	-.006
	4	150.415	-18.972	-.003	.742	-.006
	5	150.415	-18.994	-.003	.743	-.006
	6	150.415	-18.994	-.003	.743	-.006

a. Method: Enter  
 b. Constant is included in the model.  
 c. Initial -2 Log Likelihood: 185.149  
 d. Estimation terminated at iteration number 6 because parameter estimates changed by less than .001.

According to the above table, the -2LL value decreases by 10.415 from its beginning value of 162.239 to its final value of 151.824 after the independent variables are entered. A good regression model or a hypothesized model that fits the data is indicated by this drop in the -2LL score.

**Table 2. Goodness of Fit Test**

Hosmer and Lemeshow Test			
Step	Chi-square	df	Sig.
1	6.823	8	.556

As indicated in the table, chi-square is 6.823, with a significance level of 0.556 > alpha 0.05. This indicates that the model and the data match.

**Table 3. Multiple Linear Regression Variables in the Equation**

		B	S.E.	Wald	df	Sig.	Exp (B)	95% C.I. for EXP(B)	
Step								Lower	Upper
1 <sup>a</sup>	Bonus	-.003	.003	1.556	1	.212	.997	.992	1.002
	Company Size	.743	.161	21.370	1	.000	2.103	1.534	2.881
	Foreign Ownership	-.006	.009	.494	1	.482	.994	.977	1.011
	Constant	-18.994	4.503	17.790	1	.000			

a. Variable(s) entered on step 1: Bonus, Ukuran Perusahaan, Kepemilikan Asing.

As can be seen in the Table 3, variable of bonus which has a negative coefficient value, is on -0.003, with a significant value of 0.212 > alpha 0.05. This suggests that H1 is disproved. Therefore, the bonus has a negligible and detrimental impact on the company's ability to implement transfer pricing. As depicted, the company size variable, calculated based on the total asset’s algorithm, has a positive coefficient value of 0.743. This indicates a significant positive relationship with performance, because the p-value is below the 0.05 threshold for significance. As can be seen in the Table 3, variable of Foreign Ownership has a negative coefficient value of -0.006 and a significant value of 0.482 > alpha 0.05. This suggests that H3 is disproved.

Therefore, foreign ownership has a negligible and detrimental impact on the company's ability to use transfer pricing.

## 5. Conclusion

Objective of this study is aimed to analyze how bonuses, firm size, and foreign ownership affect transfer pricing decisions within the period of 2019 to 2023. It is possible to draw the following conclusions from the data analysis and discussion outcomes using a sample of 37 companies and 185 observation data: With a significant value of  $0.482 < \alpha 0.05$  and a negative coefficient value of  $-0.006$ , the variable of foreign ownership has a negative impact on the company's ability to do transfer pricing. With a significant value of  $0.212 < \alpha 0.05$  and a negative coefficient value of  $-0.003$ , the bonus variable has a negative impact on the business that uses transfer pricing. With a significant value of  $0.000 < \alpha 0.05$  and a positive coefficient value of  $0.743$ , the company size variable positively affects businesses that use transfer pricing.

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