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THE EFFECT OF ENVIRONMENTAL UNCERTAINTY AND TRANSFER PRICING ON TAX AVOIDANCE

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Abstract
The purpose of this study is to examine whether environmental uncertainty and transfer pricing affect manufacturing companies' tax avoidance on the Indonesia Stock Exchange (IDX). Using purposive sampling, 156 manufacturing companies from 2018 to 2021. Data are analyzed using linear regression using Eviews software version 12. The results of this study indicate that the average tax burden borne by the sample companies is low. In addition, this research finds that environmental damage has no impact on tax avoidance. Meanwhile, transfer pricing has a significant effect on tax avoidance. Most large companies, despite dealing with environmental issues, are relatively able to maintain their performance, resulting in consistent, solid earnings regardless of the amount of taxes they will incur.

INTRODUCTION

The competence of a country to enhance the nation can determine the prosperity of a country in its development. One of the factors that supports and builds a country is the national income. Adequate national income significantly contributes to the country, especially in the case of Indonesia, and is derived from taxes. Tax is the country's largest revenue source (Wijaya & Rahayu, 2021). According to the 2019 APBN, taxes contribute up to 82.5% of total state income, meaning that taxes are a crucial aspect that influences the government in providing important services to the community. According to UU No. 28 of 2007 concerning General Provisions and Tax Procedures, tax is an obligatory contribution to the government, owed by individuals or entities, and enforced by law. Taxpayers do not receive a direct reward, but their contributions are utilized for the country's needs and people's welfare. The following tax revenues are presented in table 1 below:

Table 1
Revenue Collection of the State Actualization for the Years 2018 – 2021 (in billion)

Year	Total Revenue		Tax Revenue		Non-Tax Revenue	
	Amount	%	Amount	%	Amount	%
2018	Rp 1,928,110	100%	Rp 1,518,790	78.77%	Rp 409,320	21.23%
2019	Rp 1,955,136	100%	Rp 1,546,142	79.08%	Rp 408,994	20.92%
2020	Rp 1,628,951	100%	Rp 1,285,136	78.89%	Rp 343,814	21.11%
2021	Rp 2,006,334	100%	Rp 1,547,841	77.15%	Rp 458,493	22.85%

Source: Badan Pusat Statistik (2023)

Table 1 provides insights into the significance of tax revenue, indicating that from 2018 to 2021, it consistently comprised approximately 77% to 79% of the total state revenue. This data underscores the pivotal role of taxes as the primary income source for the country, particularly in Indonesia. However, starting in 2019, coinciding with the onset of the Covid-19 pandemic, there has been a sustained decrease in tax revenue, mirroring the broader economic downturn. The impact of taxes is particularly felt by companies, as they are perceived as a burden capable of reducing net profits (Yuniarti et al., 2020). Consequently, in response to these challenges, companies are actively engaged in efforts to minimize their tax liabilities. One common strategy employed is tax avoidance, as businesses seek ways to reduce the overall amount of taxes paid. This complex interaction between economic factors and public sentiment underscores the complex relationship between taxation, economic performance, and corporate practices.

In the 2016 Panama Papers case, a notable term introduced is "shell company", a formally established entity operating to engage in fictitious activities or store assets, aiming to reduce tax burdens for the founder of the company or the company itself (O'Donovan et al., 2019). This case illustrates a tax avoidance phenomenon where companies, particularly large ones, strategically manage capital and fixed assets, leveraging optimal accounting methods to lower their overall effective tax rates (Fernández-Rodríguez & Martínez-Arias, 2012). Similarly, in Indonesia in 2014, foreign investment reached a total of IDR 463 trillion. Regrettably, a significant portion of foreign investors reported losses. According to records from the Directorate General of Taxes (DJP), only approximately 25% of the total foreign investment officially recorded losses, leaving the majority under suspicion of engaging in tax avoidance. Typically, these implicated companies operate in the manufacturing industry.

Tax avoidance can be described as one of the actions companies or taxpayers use to reduce their tax liability without violating the law or acting within legal boundaries (Anggraeni & Oktaviani, 2021). Tax avoidance is executed by capitalizing on loopholes in tax laws that have not yet been regulated, thus making it legal. The book "Taxation: A Very Short Introduction" by Stephen Smith discusses tax avoidance as a legitimate practice within legal limits. It is also explained that taxpayers have the right to manage their affairs to generate the lowest possible tax burden as long as they adhere to tax laws and do not engage in illegal activities. Not only because it is considered a corporate burden, but other motivating factors supporting tax avoidance efforts among taxpayers or companies include environmental uncertainty and transfer pricing activities.

Environmental uncertainty is characterized by a situation in which a company requires assistance in acquiring current and proficient information about its internal and external operational surroundings. As research indicates, the advancement of increasingly sophisticated and evolving information technology is one of the driving factors of environmental uncertainty in the business world (Seviana & Kristanto, 2020). The COVID-19 pandemic has adversely affected the country's economy, such as decreased company productivity, many employees being terminated due to companies' inability to pay their wages, and more (Barid & Wulandari, 2021). The COVID-19 pandemic has led to an environment of uncertainty, one of the causes of financial difficulties companies face. Business environments like these lead to situations where a company cannot provide certainty about the potential profits it will generate. It is also why companies are more likely to engage in tax management, namely tax avoidance and tax evasion, due to the obligations of each company as a taxpayer to pay taxes (Purnomo & Eriandani, 2023). The emergence of the COVID-19 pandemic in March 2020 in Indonesia led to a decrease in tax revenue, which was directly proportional to the slow and negative economic performance. Based on data from the Directorate General of Taxes, at the close of the first quarter of 2020, revenue from taxes had decreased by about 2.47% compared to the previous year. Environmental uncertainty, such as the COVID-19 pandemic, makes companies consider engaging in tax avoidance.

Transfer pricing is one of the techniques firms apply to achieve lower tax rates while still gaining significant benefits (Dwianika & Ahmad, 2021). It is done by setting low transfer prices to related parties sold at higher prices. (Farkhah Elfa et al., 2022) In practice, transfer pricing is consistently interpreted as one of the efforts to minimize the tax liability or expense that needs to be set by channeling profits to companies within the same group. (*Is This What a 'Golden Taxpayer' Looks like? Indonesian Coal Company and Its Investors Feel the Heat | Global Witness*, n.d.) Adaro Energy Tbk. (ADRO) is a mining company suspected of engaging in tax avoidance practices in 2019. The tax avoidance was conducted through transfer pricing activities or schemes, meaning that significant profits were transferred from Indonesia to companies in other countries with lower or even tax-free tax rates since 2017. As a result, the company managed to minimize the tax costs paid, amounting to more than Rp 1.75 trillion less than what should have been paid.

There is still limited research discussing the influence of environmental uncertainty and transfer pricing on tax avoidance, this study examines the absence and presence of the impact of these variables on tax avoidance. This research aims to analyze the impact of environmental uncertainty and transfer pricing on tax avoidance of manufacturing companies listed on IDX during 2018 until 2021. Additionally, this research is beneficial for the government, with the expectation that the government gains a better understanding of the activities or factors undertaken by companies to reduce the taxation costs they will incur.

HYPOTESIS DEVELOPMENT

It is known that managers who face more significant environmental uncertainty tend to be more involved in efforts or activities of tax avoidance, reflected in lower effective tax rates or unrecognized higher tax benefits (Huang et al., 2017). According to Asroel in 2016, in the study by (Pradita et al., 2019), environmental uncertainty is one of the environmental factors faced by organizations, which has the potential to disrupt organizational performance if the organization fails to adapt well to the rate of change and dynamics. Environmental uncertainty encompasses the level of regulatory change, the rate of technological change, competition, and market changes. In the context of agency theory, when managers are entrusted with the responsibility of managing shareholder assets, especially in conditions of high uncertainty, they may be incentivized to engage in legal means of tax management, such as tax avoidance (Purnomo & Eriandani, 2023). Research by (Huang et al., 2017) investigates the correlation between environmental uncertainty and the practice of tax avoidance. The result indicates a significant impact of environmental uncertainty on efforts to avoid tax. As the environmental uncertainty increases, the extent of tax avoidance also rises. Intensified competition in the business arena marked by swift market and technological shifts renders corporate administration intricate and challenging. Conversely, shareholder anticipations persist at elevated levels, demanding that managers consistently enhance wealth and optimize profits. Such circumstances drive managers to exercise judgment in resorting to earnings manipulation, tax manipulation, tax strategizing, and tax evasion. Based on previous research, the first hypothesis formulated in the study is:

H_1: Environmental uncertainty has a significant influence on tax avoidance.

One of the tax offices in Indonesia reported that in 2018, approximately 28% of multinational corporations evaded taxes by declaring losses. It included around 3,918 companies reporting losses for one to two years and 1,150 for three to five years. Despite this, the companies continued to operate and even expand their businesses. It is indicated that there is a positive relationship between transfer pricing aggressiveness and tax avoidance (Wijaya & Rahayu, 2021). This phenomenon is not limited to foreign companies, as transfer pricing can also occur among domestic companies by taking advantage of differences in tax rates between them. According to agency theory, principals engage in various forms of accountability transfers to make decisions necessary for the institution's operation (Jensen & Meckling, 1976) . One of the methods used for accountability transfer is transfer pricing. Transfer pricing refers to the price or value of a product or service that has a special relationship between departments among the affiliated entities that share a special relationship (Herianti & Chairina, 2019).

Numerous studies or research have explored the impact of transfer pricing on tax avoidance and their results are inconsistent. Companies employ transfer pricing strategies to minimize tax burdens by concealing the company's wealth (Putri & Mulyani, 2020). Manufacturing companies listed on the Indonesia Stock Exchange from 2012 to 2017 demonstrated that transfer pricing significantly correlates with tax avoidance activities (Herianti & Chairina, 2019). The research conducted by (Dwianika & Ahmad, 2021) also sought to assess the impact of transfer pricing on the adoption of tax avoidance strategies, and their findings indicated that transfer pricing does exert a noteworthy effect on tax avoidance practices. The studies by (Putri & Mulyani, 2020; Stephanie et al., 2017) also indicated a relationship between transfer pricing and tax avoidance. Transfer pricing activities are every day across countries because each country has unique regulations that can be utilized to minimize tax payments (Panjalusman et al., 2018). However, different research results are presented by (Fadillah & Lingga, 2021; Napitupulu et al., 2020; Widiyantoro & Sitorus, 2019), who found that transfer pricing and tax avoidance have no relationship. One of them is caused by the change in the government system, which has resulted in many new policies. From the statement stated, the second hypothesis in this research is:

H_2: Transfer pricing has a significant influence on tax avoidance.

METHOD

Sample

The research objects were selected using the purposive sampling method, which involves determining samples based on specific criteria relevant to the research. The requirements for the research samples are:

1. Manufacturing companies listed on the Indonesia Stock Exchange in 2018. Based on the Central Statistics Agency (BPS) in 2021, the business sector that contributed the most to the national GDP is the manufacturing industry, with a total value of Rp3.27 quadrillion or about 19.25% from the total of national GDP, which shows that manufacturing sector holds considerable importance in the economy.
2. Companies with complete reports from the period 2018 to 2021.
3. Companies with income tax expenses or payments. A total of 156 companies and 624 observations that met the requirements of the research object were selected as research samples.

Operational Definition and Measurement of Variables

Tax Avoidance

Tax avoidance is the dependent variable in this research. Tax avoidance seeks to reduce the tax obligation or tax rates to a minimum that is still within the limits of tax laws (Tanujaya & Vaustine, 2023). This study uses ETR (Effective Tax Rate) to measure tax avoidance. The measurement of ETR aims to provide a comprehensive view of the income tax burden on the company's pre-tax profits as presented in the financial statements. ETR is calculated using the following formula (Dyreng et al., 2010):

$$ETR = \frac{Tax\ Expense}{Profit\ before\ Tax} \quad \text{.....1}$$

Environmental Uncertainty

Environmental uncertainty and transfer pricing are the independent variables in this research. Environmental uncertainty represents the external environment influencing management's business strategy decisions (Arieftiara et al., 2017). This research measures the environmental uncertainty variable using Sales volatility. Sales volatility can be understood as fluctuating sales volume from one period to another (Saptiani & Fakhroni, 2020). Sales volatility can be measured using standard deviation, with the formula as follows:

$$Environmental\ Uncertainty = \frac{Standard\ Deviation\ of\ Sales}{Total\ Asset} \quad \ldots\ldots\ldots\ldots\ldots\ldots..2$$

Transfer Pricing

Transfer Pricing is a determination made by corporations in contracts to establish the pricing for transactions encompassing products, services, intangible assets, and financial dealings conducted by a corporation (Nugroho, 2022). Based on the book titled "Current Taxation Issues" written by Bunyamin in 2019, in a study conducted by (Nugroho, 2022), the foundation of transfer pricing, in field cases, is often accomplished by increasing purchase prices and reducing sales prices between companies within a group during transactions, aiming to direct profits to divisions located in a country with relatively lower tax rates compared to the parent company's domicile. Transfer pricing can be measured with the formula below (Maxentia Tiwa et al., 2017) :

$$Transfer\ Pricing = \frac{Receivables\ from\ Related\ Parties}{Total\ Receivable} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots3$$

Data Analysis

This research analyzes data using multiple linear regression analysis using statistical tools, namely EVIEWs.

RESULT AND DISCUSSION

Below is a Table regarding the sample criteria selected in this study:

Table 2
Data Sampling

Description	Total
Manufacturing companies listed on IDX	165
Companies that do not met the criteria	9
Companies that selected as samples	156
Samples data	624
Outlier	48
Total data	576

Source: Processed Data (2023)

Descriptive Statistics

The analysis of this research begins with descriptive statistics. Descriptive statistic summarizes the subject of an investigation by utilizing data from a sample or the entire population.

Table 3
Descriptive Statistics

	N	Min.	Max.	Mean	Std. Dev
Tax Avoidance	624	-8.03	16.25	-0.1396	0.97845
Environmental Uncertainty	624	0.00	1.77	0.1961	0.20313
Transfer Pricing	624	0.0000	0.9999	0.1966	0.29104

Source: Eviews Processed Data (2023)

Descriptive statistical analysis in Table 3 reveals that the value of TA (Tax Avoidance), measured using ETR (Effective Tax Rate), has a maximum value of 16.25 for PT Surya Toto Indonesia Tbk. in 2020. It indicates that PT Surya Toto Indonesia Tbk. is relatively compliant with tax payments. The minimum value of TA is in PT Prima Alloy Steel Universal Tbk., which is -8.03, indicating that the company is less compliant in tax payments and has a high level of tax avoidance. The average value of TA is -0.1396, this suggests that the companies in the sample carry a comparatively light average tax burden, at only 13.96%.

EU (Environmental Uncertainty) which measured using sales volatility, has a maximum value of 1.77 for PT. Panasia Indo Resources Tbk. in 2021. It suggests that the company has good performance and high earnings persistence. Meanwhile, the minimum value of EU is 0.00, observed in PT. Inti Agri Resources Tbk. in 2019, indicating that the company is not performing well enough to maintain its performance and does not have persistent earnings. The average value of the EU variable is 0.1961, which generally suggests that the manufacturing companies listed on the Indonesia Stock Exchange (BEI) are relatively good at maintaining their performance, resulting in high earnings persistence.

TP (Transfer Pricing) which measured by the ratio of related party receivables to total receivables, has a maximum value of 0.9999 for PT Keramika Indonesia Asosiasi Tbk. in 2019. It indicates that PT Keramika Indonesia Asosiasi conducts transfer pricing. The minimum value of TP is 0.0000 for companies including PT Indah Kiat Pulp and Paper Tbk., PT Trias Sentosa Tbk., PT Multistrada Arah Sarana Tbk., and PT Pelat Timah Nusantara Tbk. in 2018. This trend continued for certain companies in subsequent years. The average value of transfer pricing is 0.1966, indicating that there is an indication of transfer pricing or related-party transactions amounting to 19.66% of the sample companies. The standard deviation is 0.29104, which describes the data spread of the transfer pricing variable among the 624 data points.

Panel Regression Analysis

This research utilized panel data and conducted tests to determine the best model. There are three approaches in this study, namely the Fixed Effects Model (FEM), Common Effects Model (CEM), and Random Effects Model (REM). The research findings that the best model for this study is the Fixed Effects Model (FEM).

Table 4
Coefficient of Determination

Dependent Variable	R^2	Adjusted R^2
TA	0.589	0.435

Source: Eviews Processed Data (2023)

Based on Table 4, it is stated that the coefficient of determination R^2 essentially gauges the model's effectiveness in elucidating the fluctuations observed in the dependent variable. R^2 represents the coefficient of determination, signifying the collective impact of the independent variables on the dependent variable. Table 4 displays the results of the coefficient of determination test. The coefficient of determination assessment findings suggests that the study's dependent variable, TA (Tax Avoidance), produces an Adjusted R Square value of 0.435. It reveals that the independent variables in the study could explain the dependent variable of the study by 43.5%. Meanwhile, 56.5% of the variation in the dependent variable is explained by other factors outside the research model.

Table 5
F Test

Dependent Variable	F-Statistic	Prob(F-statistic)
TA	3.842	0.000

Source: Eviews Processed Data (2023)

The f test aims to determine whether independent variables impact the dependent variable. Table 5 displays the results of the F test. The result of the F test yields a probability value of 0.000, which is < 0.05. It implies that the variables EU (environmental uncertainty) and TP (transfer pricing), taken together, significantly influence tax avoidance.

Table 6
t-test

Variable	Coefficient	t-Statistic	Prob.
(Constant)	-0.159	-7.881	0.000
Environmental Uncertainty	0.096	1.216	0.225
Transfer Pricing	-0.141	-2.550	0.011

Source: Eviews Processed Data (2023)

The t-test aims to determine the individual influence of each independent variable on the dependent variable simultaneously. Table 6 displays the results of the t-test. The results of the initial hypothesis test concerning the impact of environmental uncertainty on tax avoidance show a probability value > 0.05, precisely 0.225. This result can be interpreted as environmental uncertainty not significantly impacting tax avoidance, whereas the first hypothesis stated that environmental uncertainty affects tax avoidance. The inconsistency between the formulated hypothesis and the test results leads to the rejection of the first hypothesis. Meanwhile, the result of the second hypothesis test regarding the impact of transfer pricing on tax avoidance show a probability value below 0.05, precisely 0.011. This result can be interpreted as transfer pricing is significantly impacting tax avoidance; thus, the second hypothesis is accepted.

Discussion

The Effect of Environmental Uncertainty on Tax Avoidance

The absence of an effect from environmental uncertainty on tax avoidance can occur because, when facing environmental uncertainty, managers tend to preserve the value of the company's earnings. Managers typically engage in earnings management intending to boost company earnings that might otherwise be affected by environmental uncertainty. It is done to maintain a positive image for stakeholders despite the impact of environmental uncertainty. On the other hand, managers might not prioritize the increasing tax value the company would have to pay, which rises as earnings increase. The findings of this research are contradictory to studies carried out by (Arieftiara et al., 2020; Dwi Laksono & Firmansyah, 2020; Huang et al., 2017; Ratu & Siregar, 2019; Seviana & Kristanto, 2020; Syarendra & Kristanto, 2020), which implies a significant and positive impact between environmental uncertainty and tax avoidance. Meanwhile, this study aligns with the research by (Mawaddah & Darsono, 2022; McGuire et al., 2014), indicating that environmental uncertainty does not affect tax avoidance.

The Effect of Transfer Pricing on Tax Avoidance

The results of the test of hypothesis regarding the impact of transfer pricing on tax avoidance show a significance level below 0.05, specifically 0.011, with a coefficient of negative 0.141. It indicates that transfer pricing has a significant negative impact on tax avoidance activities. Thus, the second hypothesis related to transfer pricing has an influence on tax avoidance. The negative relation between transfer pricing and tax avoidance may due to government's new policy related to transfer pricing, thereby diminishing companies' incentives to engage in tax avoidance via transfer pricing practices (Dwianika & Ahmad, 2021). (Wijaya & Rahayu, 2021) Related-party transactions or transfer pricing occur outside the principles of fairness and arm's length. The purpose of these transactions for companies is to minimize the business cycle, consequently reducing tax liability. This findings align with studies conducted by (Anderson & Ismail, 2023; Barker et al., 2017; Dwianika & Ahmad, 2021; Farkhah Elfa et al., 2022; Herianti & Chairina, 2019; Septiani et al., 2021), all of which explain the impact of transfer pricing on tax avoidance.

CONCLUSION

Based on tests carried out on 156 manufacturing companies registered on the IDX from 2018 to 2021 regarding the influence of environmental lighting and transfer pricing on tax avoidance, it can be concluded that environmental lighting has no effect on tax avoidance. This can happen because when dealing with the environment, companies tend to ignore the value of the taxes they have to pay because they prioritize company performance. It is hoped that the implications of this research can be a consideration for policy makers to monitor each company in terms of tax avoidance.

Suggestions for future researchers include including additional methods to measure tax avoidance other than ETR (Effective Tax Rate) such as BTD (Book Tax Differences). Future researchers can also expand the research data sample taken from the Indonesian Stock Exchange, including adding company sectors and extending the observation period, with the hope that the results obtained can be maximized.

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