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**Transfer Pricing, Thin Capitalization, and Tax Haven Strategies:  
Do They Still Drive Tax Avoidance in the Post-AEOI Era?**

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**ABSTRACT**

This study examines the effect of transfer pricing, thin capitalization, firm size, and tax haven country utilization on tax avoidance in manufacturing companies listed on the Indonesia Stock Exchange during 2020–2024 after the implementation of AEOI. The research uses a quantitative approach with a causal design and secondary data from financial reports. Multiple regression analysis is applied to test the relationship between variables. The results show that transfer pricing, firm size, and tax haven utilization have a significant effect on tax avoidance but in the opposite direction of the initial expectation, indicating lower tax avoidance. Meanwhile, thin capitalization shows a significant effect consistent with the hypothesis, where higher leverage increases tax avoidance. These findings suggest that tax behavior is influenced not only by company characteristics but also by regulatory pressure and transparency. Overall, the study provides evidence that stricter tax regulations have reduced aggressive tax practices.

*Tax Avoidance, Transfer Pricing, Thin Capitalization, Firm Size, Tax Haven*

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**INTRODUCTION**

Taxes remain one of the most important sources of government revenue, especially in a developing country like Indonesia where public spending continues to expand. They are mandatory contributions regulated by law and used to support national development and public welfare. In practice, tax revenue reflects how independent a country is in financing its own needs. Recent data also shows that Indonesia still needs to optimize its tax collection, as realization has not fully reached the national target. This condition highlights the urgency of improving compliance and strengthening the tax system (Undang-Undang No. 28 Tahun 2007; Kementerian Keuangan RI, 2024).

The manufacturing sector holds a strategic position in this context because it contributes the largest share of tax revenue compared to other sectors. Its large-scale production and broad operational network make it a major driver of

economic activity. At the same time, this complexity creates room for companies to arrange their financial strategies, including tax planning. As a result, the contribution from this sector is significant, but it also carries a higher risk of tax inefficiency due to various corporate strategies (Klikpajak, 2024).

One of the main challenges faced by tax authorities is the persistence of tax avoidance practices. Tax avoidance refers to legal efforts by companies to minimize their tax obligations by utilizing gaps within existing regulations. Even though it does not violate the law, it can reduce government revenue and create inequality in the tax system. Evidence from corporate financial reports shows that many firms report effective tax rates below the official statutory rate. This indicates that tax avoidance is not only present but also carried out in a structured and continuous manner (Dyrenge et al., 2008). Further studies also confirm that companies actively manage their tax burden through various planning strategies (Hanlon & Heitzman, 2010). From a conceptual perspective, tax avoidance is still considered legal because it relies on regulatory loopholes rather than violations (James & Nobes, 2014).

To address these issues, the Indonesian government has introduced several policies, including the Automatic Exchange of Information (AEOI). This system enables countries to exchange financial information across borders, making it harder for companies to hide income or shift profits abroad. In theory, this should increase transparency and reduce tax avoidance opportunities. However, in reality, companies with multinational operations and complex structures still have the ability to manage their tax obligations efficiently. This suggests that while AEOI improves transparency, it does not completely eliminate tax avoidance practices (OECD, 2021). In addition, the tax authority has also highlighted that companies with cross-border transactions tend to have higher risks of profit shifting (Direktorat Jenderal Pajak, 2023).

Several factors are often associated with tax avoidance behavior. Transfer pricing is one of the most widely discussed strategies, where companies determine transaction prices between related entities in different countries. This allows profits to be shifted to jurisdictions with lower tax rates (OECD, 2022). Another important factor is thin capitalization, which occurs when companies rely more on debt than equity financing. Since interest expenses can reduce taxable income, this strategy becomes attractive for minimizing tax payments (OECD, 2012). Firm size is also considered an influential factor in tax behavior. Larger companies generally have more resources, better access to expertise, and more complex operations, allowing them to design more advanced tax planning strategies (Chen et al., 2010). However, they are also more visible to regulators and the public, which may limit aggressive tax practices due to reputational

concerns (Watts & Zimmerman, 1986). This creates mixed findings in previous research regarding whether firm size increases or reduces tax avoidance.

Another factor that cannot be ignored is the use of tax haven countries. Many multinational companies establish subsidiaries in low-tax jurisdictions to shift profits and reduce their overall tax burden. Globally, a significant portion of financial wealth is stored in these jurisdictions, showing how relevant this issue remains (Zucman, 2014). In Indonesia, some companies are also reported to have connections with tax haven entities. Previous studies show that the use of tax havens can increase tax avoidance (Putri & Wibowo, 2022), although other findings suggest that its effect may weaken after the implementation of AEOI (OECD, 2021). Therefore, this study aims to re-examine how transfer pricing, thin capitalization, firm size, and tax haven utilization influence tax avoidance in manufacturing companies after AEOI implementation.

## **RESEARCH METHODE**

### **Research Type and Data Sources**

This study applies a quantitative method with a causal associative approach to examine the influence of transfer pricing, thin capitalization, firm size, and tax haven country utilization on tax avoidance. A quantitative approach is appropriate because it allows relationships between variables to be measured objectively using numerical data and statistical analysis (Creswell & Creswell, 2023). The causal design is used to identify whether changes in independent variables lead to changes in the dependent variable, while controlling other relevant factors (Neuman, 2022). The study relies on secondary data obtained from audited financial statements and official company reports, ensuring objectivity and reliability in measuring taxation variables (Ghozali, 2021). Data sources include annual reports, sustainability reports, regulatory documents from the OECD and tax authorities, and relevant academic studies. The observation period covers 2020–2024 to reflect stable implementation of AEOI and to support consistent panel data analysis.

### **Population and Sample**

This study focuses on manufacturing companies listed on the Indonesia Stock Exchange during 2020–2024, totaling 195 firms. The population includes all entities that meet the relevant characteristics for the research objectives (Creswell & Creswell, 2023). The sample is selected using purposive sampling to ensure data suitability and completeness. Criteria include firms consistently listed during the observation period, having complete financial data, and providing all required variables, regardless of whether pre-tax income is positive or negative. A five-year period is chosen to improve data stability and

reduce bias, allowing more reliable panel regression analysis and consistent observation of relationships between variables (Hair et al., 2019).

### **Operational Definitions**

This study operationalizes five main variables to examine their influence on tax avoidance. Tax avoidance is measured using the Effective Tax Rate (ETR), calculated as income tax expense divided by pre-tax income, reflecting how companies manage their tax burden (Frank et al., 2009; Utami & Irawan, 2022). Transfer pricing is proxied by the proportion of affiliated cross-border transactions to total sales, indicating the extent of profit-shifting practices (Pratama & Firmansyah, 2020; Utami & Irawan, 2022). Thin capitalization is measured using the Debt-to-Equity Ratio (DER), which shows the company's reliance on debt financing to gain tax benefits from interest expenses (Ramadhan, 2023; Utami & Irawan, 2022).

Firm size is measured using the natural logarithm of total assets, representing the scale and operational complexity of the company (Fahmi & Yanti, 2024; Rochmaniati & Dewi, 2024). Meanwhile, tax haven country utilization is measured using a dummy variable, where a value of 1 indicates that a company has subsidiaries in tax haven jurisdictions, and 0 otherwise (Widodo, 2023; Putri & Wibowo, 2022). These measurements allow for consistent and objective quantification of each variable, enabling a more reliable analysis of their relationship with tax avoidance.

### **Data Analysis Methods**

This study measures each variable using clear and consistent indicators so that the relationship between variables can be tested properly. Tax avoidance is measured using the Effective Tax Rate (ETR), which compares income tax expense to profit before tax. A lower ETR indicates that a company is paying less tax relative to its income, which may reflect tax avoidance behavior (Frank et al., 2009; Utami & Irawan, 2022). Transfer pricing is calculated by comparing the value of related-party transactions abroad to total sales, showing how much the company is involved in cross-border affiliated transactions (Pratama & Firmansyah, 2020; Utami & Irawan, 2022). Thin capitalization is measured using the Debt-to-Equity Ratio, which reflects how much a company relies on debt financing (Ramadhan, 2023; Utami & Irawan, 2022).

Firm size is measured using the natural logarithm of total assets to represent the scale of the company (Fahmi & Yanti, 2024; Rochmaniati & Dewi, 2024). Meanwhile, tax haven utilization is measured using a dummy variable, where companies with subsidiaries in tax haven countries are coded as one, and others as zero (Widodo, 2023; Putri & Wibowo, 2022). These measurements

allow the data to be processed statistically and support regression analysis in explaining tax avoidance behavior (Ghozali, 2021).

## RESULT AND DISCUSSION

### Descriptive Statistics

The descriptive statistics give a clear picture of how the data is distributed across all variables. The average Effective Tax Rate (ETR) is around 0.2335, which means that, on average, companies pay about 23.35% of their profit as tax. Since ETR moves in the opposite direction of tax avoidance, this level shows that some firms still manage to reduce their tax burden. The variation in ETR values also shows that not all companies behave the same way. Some firms report much lower values, which suggests stronger tax avoidance, while others show higher values that reflect more compliance.

**Table 1.**  
**Descriptive Statistics**

Variables	N	Minimum	Maximum	Mean	Std. Deviation
Tax Avoidance	170	0.1300	0.3400	0.2335	0.04109
Transfer Pricing	170	0.0100	0.6400	0.2656	0.15217
Thin Capitalization	170	0.1000	2.5669	0.9758	0.30536
Firm Size	170	26.0700	31.4700	28.9862	1.13735
Tax Haven	170	0.0000	1.0000	0.4353	0.49726

Other variables also show quite wide differences between companies. Transfer pricing ranges from very small to quite large proportions, indicating that some firms rely heavily on related-party transactions, while others barely use them. Thin capitalization also varies, showing that some companies depend more on debt than others. Firm size differs across the sample, reflecting both small and large companies with different levels of resources. Meanwhile, the tax haven variable shows that not all firms have foreign affiliates in low-tax countries. These differences highlight that each company has its own financial structure and tax approach, which later affects how they manage their tax obligations.

### Classical Assumption Test Results

Before testing the hypotheses, the regression model was first examined using classical assumption tests to ensure the results are reliable and free from bias. The normality test shows that the residuals are normally distributed, meaning the model can be interpreted properly. The multicollinearity test indicates no strong correlation between independent variables, as seen from tolerance values above 0.10 and VIF below 10. The heteroskedasticity test also

shows no issue, with significance values above 0.05. In addition, the Durbin-Watson value of 1.991 confirms no autocorrelation. Overall, the model meets the required criteria and is suitable for further analysis.

### Hypothesis Test Results

The regression results show that the model used in this study is reliable and suitable for analysis. The F value of 192.169 with a significance level of 0.000 indicates that the model fits the data well. This means that transfer pricing, thin capitalization, firm size, and tax haven utilization together are able to explain changes in tax avoidance. The coefficient of determination also supports this result. The Adjusted R Square value of 0.819 shows that 81.9% of the variation in tax avoidance can be explained by the variables in the model, while the remaining 18.1% is influenced by other factors outside the study. This result shows that the model has strong explanatory power in describing tax behavior among manufacturing companies.

**Table 2.**  
**Hypothesis Test Results**

Model	B	Std. Error	Beta	t	Sig.
(Constant)	0.183	0.036			
Transfer pricing	0.149	0.009	0.511	16.752	0.000
Thin capitalization	-0.079	0.004	-0.588	-17.737	0.000
Firm size	0.003	0.001	0.074	2.274	0.026
Tax haven	0.025	0.003	0.305	9.205	0.000

The regression coefficients provide a clearer picture of how each variable affects tax avoidance. Transfer pricing has a positive and significant effect on ETR, which means higher transfer pricing is associated with lower tax avoidance. Thin capitalization shows a negative effect on ETR, indicating that higher debt levels lead to higher tax avoidance. Firm size has a positive effect, suggesting that larger firms tend to be more compliant. Tax haven utilization also has a positive effect on ETR, meaning firms with tax haven connections do not necessarily engage in higher tax avoidance. These findings show that company characteristics influence tax strategies in different ways and reflect real conditions in corporate tax management.

### The Effect of Transfer Pricing on Tax Avoidance

The results show that transfer pricing has a significant positive effect on ETR. This means that when related-party transactions increase, the ETR also rises. Since ETR moves in the opposite direction of tax avoidance, this finding indicates that higher transfer pricing activity is linked to lower tax avoidance. In other words, transfer pricing in this case is not being used to reduce tax

payments. This result does not support the initial expectation that transfer pricing increases tax avoidance (Richardson et al., 2013). It suggests that the presence of related-party transactions alone is not enough to explain tax behavior, especially when companies operate under tighter supervision.

From a theoretical view, transfer pricing can be used to shift profits across countries with different tax rates (Hines & Rice, 1994). However, stricter rules and stronger monitoring have reduced this flexibility. Companies are now required to follow documentation rules and apply the arm's length principle, which limits aggressive practices (OECD, 2017). In Indonesia, these rules are reinforced through specific regulations that push firms to be more transparent. As a result, many related-party transactions are simply part of normal business operations, not tax strategies. This finding is in line with Taylor and Richardson (2014), but differs from studies that found the opposite effect (Klassen & Laplante, 2012; Pratama & Firmansyah, 2020).

#### **The Effect of Thin Capitalization on Tax Avoidance**

The results indicate that thin capitalization has a significant effect on ETR with a negative coefficient. This means that when a company's level of debt increases, the ETR tends to decrease. Since ETR moves in the opposite direction of tax avoidance, a lower ETR reflects a higher level of tax avoidance. This finding supports the assumption that companies with higher leverage are more likely to reduce their tax burden. The use of debt allows firms to record interest expenses, which can be deducted from taxable income, leading to lower tax payments. This shows that financing decisions are closely related to how companies manage their tax obligations (Modigliani & Miller, 1963; Graham, 2003).

From a theoretical perspective, this result aligns with Trade-Off Theory, where firms balance the benefits of tax savings from debt with potential financial risks. In Indonesia, the government has introduced thin capitalization rules to limit excessive use of debt, but the influence of leverage on tax behavior is still evident. High debt ratios are often used as an early signal in tax risk assessment by authorities. Even so, companies do not rely on debt solely for tax purposes, as it is also used for expansion and operational needs. This shows that tax avoidance through leverage is shaped by both financial strategy and regulatory pressure (OECD, 2015; Hanlon & Heitzman, 2010; Ramadhan, 2023)

#### **The Effect of Firm Size on Tax Avoidance**

The results show that firm size has a significant positive effect on ETR. This means that larger companies tend to report higher ETR, which indicates lower tax avoidance. In other words, big firms are less likely to engage in aggressive tax strategies compared to smaller firms. This finding does not

support the assumption that firm size increases tax avoidance. Although large companies have more resources and better access to tax experts, they also face higher exposure and stricter supervision. Their operations are more visible, and their financial reports are closely monitored by regulators, investors, and the public. As a result, they tend to manage their tax obligations more carefully and avoid actions that could raise concerns (Gupta & Newberry, 1997; Lanis & Richardson, 2012).

In the Indonesian context, large firms are often classified as key taxpayers and receive more intensive monitoring from tax authorities. This level of supervision pushes companies to maintain compliance and reduce the risk of tax disputes. In addition, large firms are more sensitive to reputational risk, which can affect investor trust and long-term performance. Strong corporate governance also plays a role, as larger firms usually have better internal controls and oversight mechanisms. These conditions encourage more transparent financial management and reduce the likelihood of aggressive tax planning. This finding is consistent with Lanis and Richardson (2012), but differs from Annisa et al. (2018), showing that the effect of firm size depends on the balance between capability and external pressure (Watts & Zimmerman, 1986; Lanis & Richardson, 2012).

#### **The Effect of Tax Haven Country Utilization on Tax Avoidance**

The results show that tax haven country utilization has a significant positive effect on ETR. This means that companies with affiliates in tax haven jurisdictions tend to report higher ETR, which reflects lower tax avoidance. In other words, the presence of tax haven entities does not automatically indicate aggressive tax behavior. This finding does not support the assumption that tax haven use increases tax avoidance. In some cases, these entities are established for operational reasons, such as managing international investments or supporting global business activities, rather than for shifting profits (Dyreng & Lindsey, 2009). Although tax haven countries are often associated with low tax rates and profit shifting strategies, their role in practice appears more complex (Hines & Rice, 1994).

Recent developments in global tax regulation have also reduced the effectiveness of tax haven strategies. Initiatives such as BEPS and the implementation of AEOI have increased transparency and strengthened information exchange between tax authorities. As a result, companies face greater pressure to ensure that their international structures can be justified. In Indonesia, firms with cross-border transactions must meet stricter reporting requirements, including transfer pricing documentation and disclosure of related-party activities. This makes it easier for tax authorities to monitor and

assess potential risks. The findings are consistent with Dyreng and Lindsey (2009), but differ from Hines and Rice (1994), showing that the impact of tax haven use depends on regulatory conditions and transparency levels (Hanlon & Heitzman, 2010; Dyreng et al., 2008).

## **CONCLUSION**

The results of this study show that tax avoidance behavior, which is reflected through the Effective Tax Rate (ETR), does not always follow the expected pattern. Transfer pricing is found to have a significant effect, but the direction is not in line with the initial assumption. Instead of lowering the tax burden, higher transfer pricing activity is associated with an increase in ETR, meaning that tax avoidance becomes lower. This condition suggests that transactions with related parties are not always used as a tool to shift profits, but may also be driven by operational needs and stricter regulatory control. In contrast, thin capitalization shows a consistent result. Companies with higher levels of debt tend to have lower ETR, which indicates a higher level of tax avoidance. This finding confirms that the use of debt financing still plays an important role in reducing taxable income through interest expenses.

Firm size and tax haven utilization also show significant effects, but again, the direction does not support the initial expectations. Larger companies tend to report higher ETR, which means they are less involved in aggressive tax avoidance. This can be explained by the higher level of scrutiny they face from regulators, investors, and the public, making them more cautious in their tax strategies. A similar pattern is found in companies that have subsidiaries in tax haven jurisdictions. Instead of lowering their tax burden, these companies show higher ETR, indicating reduced tax avoidance. This reflects the growing impact of global tax transparency and stricter international regulations, which limit the effectiveness of tax haven strategies. Overall, the findings highlight that tax avoidance is influenced by multiple factors and cannot be explained by a single approach alone.

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