**UNIVERSITI TEKNOLOGI MARA**

# THE DYNAMICS OF TRANSFER PRICING OPTIMIZATION PRACTICE IN AN INDONESIAN MINING COMPANY: A REFLECTION OF BEHAVIOURAL VIEW ON THE ECONOMY, ENVIRONMENT, AND SOCIETY

**HANI WERDI APRIYANTI**

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# ABSTRACT

Most Multinationals Enterprises (MNEs) implement transfer pricing and maximize its usage for various management and tax-related objectives, particularly tax evasion. Cross-border transfer pricing is a problem that many countries are struggling to solve. Transfer pricing tax evasion can result in several economic and social issues, such as a reduction in tax revenue for the host country and a broader array of societal problems. Several transfer pricing policies have been developed in several nations, but many obstacles arise, such as transparency, human resources, and other ethical concerns. To overcome those problems, a multi-dimensional approach is strongly needed. Therefore, this study used a behavioural perspective, specifically the theory of planned behaviour (TPB), with three constructs, including the differential organizational perception of the benefit of transfer pricing optimization, the differential perception of transfer pricing regulation and business environment, and the differential perceived control over behaviour. The three research stages employed using three-layer unit analysis consist of MNEs or taxpayers, tax consultants, and tax authorities. The finding shows that transfer pricing is part of normal business activities aimed at managerial and taxation purposes. Indonesian MNEs are not aware of national and international regulations. They use tax consultants and utilize several internal and external factors to optimize their transfer pricing. This study enriches the literature on the role of behavioural aspects on transfer pricing optimization by Indonesian MNE, including an in-depth analysis of MNE, tax consultants, and tax authorities' perceptions of transfer pricing optimization behaviours. This study also gives practical implications, specifically the need for improvement, in transfer pricing guidance for the tax authorities to minimize abusive transfer pricing. The proposed framework and findings from the three-layer unit analysis were used to develop transfer pricing guidelines. The proposed model will be useful for monitoring and detecting transfer pricing optimizations that lead to tax avoidance.

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# CHAPTER 1
# INTRODUCTION

## 1.1 Research Background

Traditional economic theories guide corporate actions to exploit tax regulation loopholes to maximize profit. Tax planning, tax evasion, and tax avoidance are ways businesses try to maximize their earnings. Companies, organizations, or managers who engage in tax fraud are at significant risk of tax evasion. Therefore, most businesses prefer to engage in tax planning and tax avoidance rather than evading taxes. Most companies control their tax obligations to maximize profits. Among the popular strategies businesses find appealing to optimize profits are tax planning and tax avoidance (Tambunan, 2022).

Using related parties to transfer goods and services is one method of tax avoidance. Through related parties, companies can conduct transfer pricing following the agreement between their affiliates. Companies typically engage in price transfers with related parties or affiliates to boost their overall profit, often at the cost of other unit's tax payments (Rahmiati & Sandi, 2016). According to Kamilah (2019), MNEs (MNEs), as economic actors in economic globalization, engage in transfer pricing. Transfer pricing involves the distribution of profits from one entity to other entities within a group of companies. This practice is considered a normal thing in business activity.

MNEs use transfer pricing to shift the profit from high-tax jurisdictions to low-tax jurisdictions as well as to minimize tax obligations (Sari, D.K., 2020). Transfer pricing practices have increasingly developed over the past few years. MNEs commonly use the transfer pricing practice to minimize tax expenses by exploiting tax loopholes without violating any tax regulations (Sari, D.K., 2020). The other usefulness of transfer pricing is linked to tax evasion, resulting in numerous instances of transfer pricing litigation. In 2020, there were approximately 25 transfer pricing cases worldwide involving multinational companies such as Glencore Investment Pty in Australia, Cameco Corporation and Agra City Ltd. in Canada, Altera Corps in the United States, Business Norway AS and A/S Norske Shell in Norway, Prime Plastic Hem Nigeria Limited in Nigeria, Zinc Smelter B.V. in the Netherlands, Societal Italians Per Transalpine SPA in Italy, and others. One notable example of a transfer pricing case in