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UNMASKING TAX STRATEGIES: THE ROLE OF TRANSFER PRICING AND CAPITAL INTENSITY IN INDONESIA'S MINING SECTOR

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Abstract

Research related to Tax Avoidance is still an interesting topic to research, especially in Indonesia, which is trying to minimize tax avoidance practices. This research aims to examine the influence of transfer pricing and capital intensity on tax avoidance. The measurement of each variable is using the effective tax rate/ETR (for the tax avoidance variable), the amount of receivables from related parties (for the transfer pricing variable), and the ratio of fixed assets divided by total assets (for the capital intensity variable). For this research, the Author used a purposively selected sample, namely mining sector companies. The model was tested using multiple linear regression. The test results prove that transfer pricing has no influence, and capital intensity has a positive influence on tax avoidance. The research results can provide input for developing regulations related to tax avoidance practices.

Keywords: *Transfer Pricing, Capital Intensity, Tax Avoidance.*

1. Introduction

Transfer pricing has become a global concern due to its potential for enabling multinational corporations to shift profits across borders, often to jurisdictions with lower tax rate. This practice, while legal under certain conditions, poses significant challenges to tax authorities worldwide in their efforts to ensure fair and effective taxation. Organizations such as the OECD have taken steps to address these issues through the Base Erosion and Profit Shifting (BEPS) initiative, aimed at closing gaps in international tax rules.

In developing countries like Indonesia, the implications of aggressive transfer pricing are even more critical. Indonesia relies heavily on tax revenues to support national

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development goals. Consequently, practices that erode the tax base, including the misuse of transfer pricing, undermine fiscal sustainability. Despite regulatory measures such as the arm's length principle, mandatory documentation, and Country-by Country Reporting (CbCR), the enforcement and effectiveness of these policies continue to face limitations, especially in capital-intensive sectors like mining where cross-border transactions are more prevalent.

One of the main challenges in monitoring transfer pricing practices in Indonesia is limited information and gaps in access to financial data between jurisdictions. Although there are regulations governing transfer pricing documentation, such as PMK No. 172 of 2023 concerning the Application of Fairness Principles and Business Customs in Transactions Affected by Special Relationships, many companies still take advantage of legal loopholes to minimize their tax obligations.

Empirical research to examine transfer pricing in influencing companies' tendency to carry out tax avoidance has been widely carried out. This research, among other things, provides support for the positive relationship between transfer pricing and tax avoidance (H. A. Aristyatama & Bandiyono, 2021; Dharmawan et al., 2024; Kolondam & Permatasari, 2024a; Mohammed et al., 2019; Rizky Nurdiansyah & Masripah, 2023; Utami & Irawan, 2022). Other empirical research shows a negative relationship (Nadhifah & Arif, 2020)) and no effect (Ardillah & Vanesa, 2022; Iriyadi et al., 2024; Manik & Fitriana, 2023; Oktaviani et al., 2023).

The tax avoidance strategy carried out can also be in the form of using capital intensity, namely the company's strategy of investing in fixed assets to generate large depreciation costs, so that the taxes paid are lower. Previous research confirms the positive relationship between capital intensity ratio and tax avoidance (Darsani & Sukartha, 2021; Widyastuti et al., 2022). However, research conducted by (2020a) shows a negative relationship, and research by (2021)shows there is no relationship between the capital intensity ratio and tax avoidance.

Prior research has presented mixed findings on the relationship between transfer pricing, capital intensity, and tax avoidance. Some studies suggest a significant positive relationship between these variables, while others report either a negative association or no significant link. Additionally, many studies have employed broad industry samples, leaving sector-specific dynamics underexplored.

This research addresses this gap by focusing specifically on the mining sector in Indonesia-a strategically important, capital-intensive, and high-risk industry in terms of tax compliance. By examining ow transfer pricing and capital intensity affect tax avoidance within this context, the study aims to provide empirical evidence that can inform tax policy and caproate governance practices. The objectives of this study are to analyze the influence of transfer pricing on tax avoidance in Indonesian mining companies, and to assess the impact of capital intensity on tax avoidance. By concentrating

on these aspects, the research seeks to contribute to the academic discourse and support the formulation of more effective tax regulations.

2. Literature Review

2.1 Agency Theory

Agency Theory (Jensen & Meckling, 1976) provides the basis for understanding conflict of interest between company owners (principals) and managers (agents). Managers may pursue tax avoidance strategies, such as manipulating transfer pricing or investing in capital assets, to reduce tax obligations and enhance reported profitability, thereby increasing personal compensation and perceived performance.

2.2 Tax Avoidance

Tax avoidance encompasses legal strategies to minimize tax liabilities. According to Yahya et al., (2023) tax avoidance can be viewed along a spectrum ranging from benign tax planning to aggressive schemes bordering on evasion. This study focuses on acceptable avoidance strategies that exploit legal provisions to reduce tax burdens without engaging in outright fraud. Tax avoidance refers to efforts to efficiently pay taxes by avoiding the imposition of taxes based on applicable tax provisions. Tax avoidance is divided into 2 (Kessler, 2004), namely:

a. Acceptable tax avoidance
   Tax avoidance is permitted only if it has a good purpose, is not to avoid tax, and is not a fictitious transaction.
b. Unacceptable tax avoidance
   Tax evasion is not permitted, with the characteristics of not having a good purpose and creating fictitious transactions.

2.3 Transfer Pricing

Transfer pricing involves setting prices for intercompany transactions. While aligned with legitimate business objectives, it can be manipulated to shift profits to low-tax jurisdictions (Legenchuk et al., 2021). Empirical studies by H. Aristyatama & Bandiyono (2021); Kolondam & Permatasari (2024); Mohammed et al. (2019) indicate that aggressive transfer pricing correlates with higher levels of tax avoidance. However, other studies Alexander (2024); Ardillah & Vanesa (2022); Iriyadi et al. (2024); Manik & Fitriana (2023); Nadhifah & Arif (2020) no such relationship, highlighting inconsistencies possibly due to sector-specific factors. Transfer pricing is a company policy in determining transfer prices between divisions within one company or between companies that have a special relationship (Mardiasmo, 2011). Based on PMK No.22/PMK.03/2020 Special relationships can arise due to the following things:

a) Special relationship due to ownership
   This relationship arises due to ownership control in the form of capital participation of 25% or more, either directly or indirectly.

b) A special relationship because of mastery
   This relationship arises due to control either through management or the use of technology. This relationship can arise even though there is no ownership relationship.
c) A special relationship because of family ties
   This relationship arises because of the existence of family relationships, both by blood and by marriage, in a straight and/or sideways lineage of one degree or another.

Transfer pricing is often used as a strategy to reduce the tax burden and shift profits. Transfer pricing behavior is a logical consequence of the company group's strategy to create competitive advantage (Tambunan et al., 2022). The Indonesian government has made various efforts to minimize tax avoidance originating from transfer pricing transactions. These efforts include, among other things, issuing Regulation of the Minister of Finance of the Republic of Indonesia No. 172 year 2023 concerning Application of the Principles of Fairness and Business Normalcy in Transactions Affected by Special Relationships.

2.4 Capital Intensity

Capital intensity describes how a company invests in fixed assets (Monika & Noviari, 2021). The use of fixed assets in the company's business operations will impact the resulting high depreciation expense. This could be an alternative strategy for companies to minimize corporate taxes because the profits generated will also be lower, so taxes will also be lower (Sunday et al., 2024). Capital intensity is a crucial factor in this context, as companies with higher fixed asset investments can leverage depreciation to reduce their taxable income(Harefa & Margie, 2024). This relationship emphasizes the importance of capital intensity in tax planning strategies for firms. (Suciarti et al., 2020b)Consequently, understanding the dynamics of capital intensity and its implications for tax avoidance can helps firms optimize their tax strategies and enchance financial performance (Hendayana et al., 2024).

Firms should carefully evelate their capital investments to balance operational efficiency with effective tax planning, as the interplay between these factors can significantly influence overall financial outcomes (OLANISEBE et al., 2023). Ultimately, companies must navigate the complexities of capital intensity and tax regulations to ensure sustainable growth while fulfilling their tax obligations. This necessitates a thorough analysis of how capital intensiy affects not only tax liabilities but also long-term investnment strategies and operational efficiecncy in the competitive lanscapae.

2.5 The Relationship between Transfer Pricing and Tax Avoidance

Transfer pricing can be one of the strategies used by companies to avoid tax, especially multinational companies. Transfer pricing is carried out, among other things, by setting prices for transactions between entities that are still within the same business group. Even though transfer pricing is a legal and common practice in business activities, this practice also has great potential to be used as a tool in tax avoidance strategies, especially when price determination is not in accordance with the arm's length principle.

In this context, tax avoidance refers to a company's efforts to minimize the tax burden it bears, either through legal strategies such as tax avoidance or strategies that approach legal violations such as tax evasion. Therefore, the higher the transfer pricing practice, the higher the company's tendency to practice tax avoidance (H. A. Aristyatama & Bandiyono, 2021; Dharmawan et al., 2024; Kolondam & Permatasari, 2024a; Mohammed et al., 2019; Rizky Nurdiansyah & Masripah, 2023; Utami & Irawan, 2022). Proposed hypothesis:

H1: There is a positive influence between transfer pricing and tax avoidance

2.6 The relationship between Capital Intensity and Tax Avoidance

Ownership of fixed assets that a company uses in managing its business activities is a natural thing. However, in some companies, a large fixed asset ratio can be used as a means to minimize taxes paid (Monika & Noviari, 2021). The use of fixed assets in the company's business operations will have an impact on the resulting high depreciation expense. This could be an alternative strategy for companies to minimize corporate taxes because the profits generated will also be lower, so taxes will also be lower (Suciarti et al., 2020a). Proposed hypothesis:

H2: There is a positive influence between capital intensity and tax avoidance

The research model is described as follows:

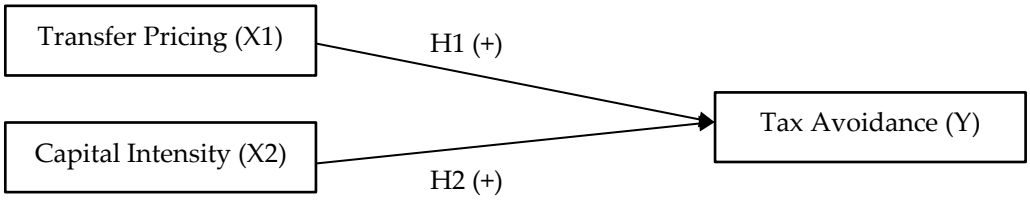

Figure 1. Research Model

3. Research Methods

This research uses a descriptive quantitative approach. Quantitative data is processed using the SPSS statistical application, and then the results are described according to the hypothesis test results obtained. The research uses secondary data in the form of financial reports accessed from the Indonesia Stock Exchange website.

The population in this research is all companies listed on the Indonesia Stock Exchange from 2019 to 2023. The sample was selected using a purposive sampling technique, namely companies operating in the mining sector with a final total sample of 16 companies and a total of 78 observations.

Operational Definition and Variable Measurement

Variabel	Definisi	Pengukuran
Tax Avoidance (Y)	Tax avoidance refers to efforts to efficiently pay taxes by avoiding the	Effective Tax Rate (ETR) $ETR = \frac{Tax\ Rate}{Earning\ Before\ Tax}$ (Ardillah & Vanesa, 2022)

	imposition of taxes based on applicable tax provisions.	
Transfer Pricing (X1)	Transfer pricing is a method of determining prices for transactions related to parties who have a special relationship.	$Transfer\ Pricing = \frac{Related\ Party\ Receivables}{Total\ Receivables}$ (Iriyadi et al., 2024)
Capital Intensity	Capital intensity describes how a company invests in the form of fixed assets in the company.	$Capital\ Intensity = \frac{Net\ of\ Fixed\ Asset}{Total\ asset}$ (Darsani & Sukartha, 2021)

Regression formula equation:

Description:

a : Constant

b : Independent Variable regression coefficient

TA : Tax Avoidance

TP : *Transfer Pricing*

CI : *Capital Intensity*

It : Company i, year t

e : error

The data in this study were analyzed using SPSS through a series of statistical procedures to ensure reliable and reproducible results. First, descriptive statistical analysis was conducted observe the basic characteristics of each research variable, including minimum, maximum, mean, and standard deviation values. Next, a multicollinearity test was performed using the Variance Inflation Factor (VIF) to ensure that there was no high linear correlation among the independent variable that could distort the validity of the regression results. Multiple linear regression analysis was then used to test the research hypotheses. The model's overall fit was assessed using the F-test to determine whether the independent variables jointly influence the dependent variable. Additionally, t-test were carried out to examine the partial effects of each independent variable on tax avoidance. Finally, the adjusted R-square value was used to evaluate the proportion of variance in tax avoidance that could be explained by the independent variables. These analytical steps enhance the transparency and robustness of the study's findings.

4. Results and Discussion

4.1 Result

4.1.1 Descriptive Statistics

The results of descriptive statistical tests on the data used in the research are presented in Table 1 below:

Table 1. Descriptive Statistic

Variabel	Min	Max	Mean	Std. Dev
TA	-0,2217	0,8680	0,2203	0,2104
TP	0,0013	0,9993	0,3499	0,3370
CI	0,0057	0,8938	0,3670	0,2274
N	78			

Source: Data processed by the Author

The Tax Avoidance variable has a value range between -0.2217 and 0.8680, with an average of 0.2203 and a standard deviation of 0.2104. The average of 0.2203 indicates that the average tax burden presented is 22.03% of profit before tax. The Transfer Pricing variable has a value range between 0.0013 and 0.9993, with an average of 0.3499 and a standard deviation of 0.3370. The average receivables from special parties in the sample companies is 34.99%. The Capital Intensity variable has a value range between 0.0057 and 0.8938, with an average of 0.3670 and a standard deviation of 0.2274. Sample companies have fixed assets on average of 36.70% of the total assets owned.

4.1.2 Regression Analysis Results

Table 2. Test Results

Variable	Coefficient	t-stat
Intercept	0,332	6,653
TP	-0,068	-0,985
CI	-0,238	-2,235**
Adj. R^2	0,055	
F-Statistic	3,258**	

***, **, * respectively significant at α 0.01, 0.05 and 0.1

Source: Data processed by the Author

Based on Tabel 2, the following regression equation is derived:

Y=0,332 - 0,68TP - 0,238CI

From this equation, we observe a constant value of 0,332. This indicates that if both Transfer Pricing (TP) and Capital Intensity (CI) are at zero (or held constant at their baseline), the dependent variable, Tax Avoidance (Y), would have an average value of 0,332. In essence, this is the baseline value of Y in the absence of any influence from the TP and CI variables.

The regression coefficient for Transfer Pricing (TP) is -0.068. This suggests that for every one-unit increase in Transfer Pricing, the dependent variable Y is expected to decrease by an average of 0.068 units, assuming Capital Intensity (CI) remains constant. The negative sign signifies an inverse relationship between Transfer Pricing and Y, meaning higher TP values are associated with lower Y values. However, it's important to note that in prior analyses, this particular influence was not found to be statistically significant.

Similarly, the regression coefficient for Capital Intensity (CI) is -0.238. This implies that for every one-unit increase in Capital Intensity, the dependent variable Y is expected to decrease by an average of 0.238 units, assuming Transfer Pricing (TP) remains constant. The negative sign here also indicates an inverse relationship between CI and Y; thus, higher CI values lead to lower Y values. Crucially, this specific influence was found to be statistically significant. Overall, this equation illustrates how changes in Transfer Pricing and Capital Intensity simultaneously affect the Tax Avoidance variable, taking into account the direction and magnitude of their respective impacts.

The regression equation model influences the independent variable on the dependent variable as shown by the adjusted R2 value of 0.055 or 5.5%. This means that the transfer pricing and capital intensity variables have an influence on the dependent variable tax avoidance by 5.5%, and the other 94.5% is influenced by other variables that are not tested in the research model equation.

4.1.3 F-Test (Model Test)

Table 3. F-Test

Model	Sum of Squares	df	Mean Square	F	Sig
Regression	,273	2	,136	3,258	,044
Residual	3,137	75	,042		
Total	3,410	77			

Source: Data processed by the Author

The F-test is employed to assess the overall significance of the regression model. The results of the regression model test indicate a significance value of 0.044, which is less than the conventional significance level of 0.05. Therefore, the regression model is deemed appropriate for use. This implies that at least one of the independent variables significantly influences the dependent variable. In other words, this model is suitable for predicting the dependent variable.

4.1.4 T-Test (Partial Test)

Tabel 4. T-test

Model	Coefficients	t	Sig	Summary
Constant	0,332	6,653	0,000	
Transfer Pricing (X1)	-,068	-,985	,328	Rejected
Capital Intensity (X2)	-,238	-2,325	,023	Accepted

Source: Data processed by the Author

The partial test results to examine the effect of Transfer Pricing on the effective tax rate (ETR) show a coefficient result with a negative value of -0.068 and a significance value of 0.328 (more than 0.05). This means that the Transfer Pricing variable does not affect ETR. Therefore, the first hypothesis, which states "there is a positive influence between Transfer Pricing and Tax Avoidance," is rejected or not accepted. The partial test results to test the effect of Capital Intensity on the effective tax rate (ETR) show a coefficient result with a negative value of -0.238 and a significance value of 0.023 (smaller than 0.05). The negative influence has the effect that the higher the Capital Intensity, the lower the ETR value, which means that the tendency to avoid taxes is higher. Therefore, the second hypothesis states "there is a positive influence between Capital intensity and Tax Avoidance " accepted.

4.2 Discussion

4.2.1 The Effect of Transfer Pricing on Tax Avoidance

The regression analysis indicates that transfer pricing, as measured by related-party receivables, does not significantly influence tax avoidance ($p>0.05$). This suggests that the presence of related-party receivables may not directly reflect profit-shifting activities that affect effective tax rates in the mining sector. This means that whatever the value of transfer pricing carried out by the company will not affect the value of the effective tax rate (ETR). Therefore, because the ETR is not affected, the tax avoidance ratio also has no influence. Test results that are not significant require further evaluation regarding the use of the special party receivables ratio as a measurement of transfer pricing value. The use of special party receivables is not necessarily related to sales-related transactions that affect the company's tax burden.

Therefore, in future research, other proxies for measuring transfer pricing can be used, such as identifying whether the company owns and transacts with subsidiary companies located in tax heaven countries (Mohammed et al., 2019). The test results of this research are similar to those conducted by Ardillah & Vanesa (2022), Oktaviani et al., (2023), dan Manik & Fitriana (2023). However, the test results are not the same as those of Aristyatama & Bandiyono (2021), (2024), Kolondam & Permatasari (2024a), Mohammed et al., (2019), Rizky Nurdiansyah & Masripah (2023), and Utami & Irawan (2022). Although the result does not support Hypothesis 1, it provides valuable insight into how transfer pricing is manifested in the mining sector. The lack of significant findings may also reflect

the stricter regulatory scrutiny and transparency requirements imposed on resource-based companies, particularly in the wake of BEPS-related reforms.

4.2.2 The Effect of Capital Intensity on Tax Avoidance

The findings reveal a statistically significant negative relationships between capital intensity and the effective tax rate ($p<0.05$), indicating that higher investment in fixed assets corresponds with lower tax burdens. This supports Hypothesis 2 and aligns with agency theory, which suggests that management may utilize capital investments strategically to reduce taxable income through depreciation. The research results are similar to research conducted by Suciarti et al., (2020a) and different from the results obtained in research by Darsani & Sukartha (2021), Monika & Noviari (2021), and Widyatuti et al., (2022).

The results also imply that regulatory bodies should pay closer attention to the treatment and reporting of fixed assets in capital-heavy industries. Moreover, the findings contribute to the broader understanding of how operational characteristics like capital intensity influence corporate tax behavior. They also underscore the importance of sector-specific analysis, as industries with substantial asset bases may require tailored regulatory responses to mitigate tax avoidance risks. In sum, while transfer pricing did not show a direct effect in this study, capital intensity emerged as a significant factor in reducing effective tax rates. These outcomes highlight the complexity of tax avoidance behavior and the need for nuanced, context-sensitive policy frameworks.

5. Conclusions

This study investigates the impact of transfer pricing and capital intensity on tax avoidance in Indonesia's mining sector. The findings reveal that transfer pricing, as measured through related-party receivables, does not significantly influence tax avoidance behavior. In contrast, capital intensity shows a statistically significant negative association with effective tax rates, suggesting that firms with higher investments in fixed asset are more likely to engage in tax avoidance strategies via depreciation benefits. These results offer several important implications. Theoretically, the study supports agency theory by demonstrating how management may exploit capital structure to reduce tax burdens. Practically, the findings highlight the need for regulatory authorities to closely monitor fixed asset reporting and depreciation policies in capital-intensive industries. Moreover, the non-significance of transfer pricing underscores the need for improved proxies or methods to detect subtle tax avoidance behaviors.

The research, however, has limitations. The proxy used for transfer pricing may not fully capture all forms of related-party profit shifting. The relatively narrow sectoral focus, while a strength in contextual relevance, may limit generalizability to other industries. Future studies could enhance measurement techniques for transfer pricing, incorporate broader samples across sectors, and examine moderating variables such as caproate

governance or audit quality. In conclusion, this study contributes to a deeper understanding of tax avoidance mechanisms in the Indonesian mining industry. It underscores the influence of capital investment patterns on tax planning strategies and calls for more nuanced regulatory oversight to address evolving corporate tax behaviors.

Topics related to tax avoidance are still an interesting topic to research, especially in Indonesia, which is trying to minimize various tax avoidance efforts by taxpayers so that state revenues are in line with the expected targets. This research seeks to examine the influence of transfer pricing and capital intensity on the tendency for tax avoidance behavior. The research results show that transfer pricing does not influence tax avoidance practices, while capital intensity has a negative influence on tax avoidance. The test results for the transfer pricing variable, which are not significant, can be input for subsequent research to be able to use other transfer pricing variable proxies, such as identifying whether the company owns and transacts with subsidiaries (Mohammed et al., 2019).

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