

Good Corporate Governance Mediates The Effect of Taxes on Transfer Pricing In Creating a GOLD Indonesia 2045

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Keywords:

Good Corporate Governance,
Transfer Pricing, Taxes

Abstract

Transfer pricing (TP) practices by multinational corporations (MNCs) are a crucial issue in tax administration that has the potential to reduce the domestic tax base, a significant threat to state revenue collection efforts needed to realize Indonesia Emas 2045. This study aims to examine the mediating role of Good Corporate Governance (GCG) in the relationship between taxes (proxied by tax rates) and corporate decisions to conduct transfer pricing. Based on Agency Theory, differences in interests between principals (owners/tax authorities) and agents (management) can encourage aggressive TP practices aimed at minimizing tax burdens. GCG, through principles such as transparency, accountability, and independence, is expected to act as an effective internal and external monitoring mechanism. The proposed research method is a quantitative approach with path analysis on data from MNC companies listed on the Indonesia Stock Exchange (IDX) during a certain period. The expected results are to prove that GCG not only weakens the tax incentives for aggressive TP (moderation role), but also forms a more responsible channel in determining transfer prices that is in line with the Arm's Length Principle. These findings will emphasize that the synergy between strict tax regulations and strong GCG implementation is key to ensuring sustainable tax compliance, creating a healthy investment climate, and supporting state financial accountability which is vital for achieving Indonesia's long-term development vision.

INTRODUCTION

Indonesia aspires to become a developed country with a per capita income equivalent to that of developed countries by 2045, known as Golden Indonesia 2045. To achieve this ambitious vision, the availability of large and stable financial resources through tax revenue is vital (Utomo, 2020). However, in the era of globalization and high capital mobility, Indonesia's tax base faces serious challenges, one of which is the practice of transfer pricing (TP) carried out by multinational companies (MNCs). Transfer pricing, namely the determination of transaction prices between parties with special relationships, is often abused to shift profits from jurisdictions with high tax rates (such as Indonesia) to tax haven jurisdictions or with lower tax rates. The Directorate General of Taxes (DGT) consistently highlights the potential tax losses resulting from this practice, which can significantly reduce the tax base (Indonesia, 2025).

Theoretically, high tax rates in a country will be a major incentive for MNCs to engage in aggressive transfer pricing practices (Kotler, 2008). Companies tend to look for loopholes or manipulate transfer prices to minimize their tax burdens legally (tax avoidance) or illegally (tax evasion). This phenomenon creates fiscal injustice and is detrimental to national development. Therefore, a mechanism is needed to neutralize or control this tax-based incentive, so that companies' decisions in determining transfer prices remain within the corridor of fairness (arm's length principle) and compliance (Philip, 2013).

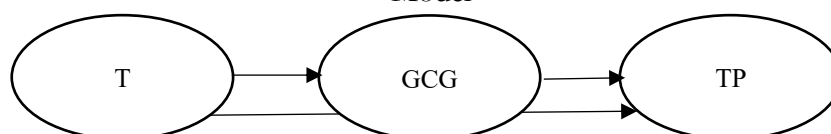
In this context, Good Corporate Governance (GCG) emerges as a crucial variable. GCG is a system that regulates and controls a company to create added value for all stakeholders, based on the principles of Transparency, Accountability, Responsibility, Independence, and Fairness (Ramadeni & Dewi, 2023). GCG is expected to act as an effective mediation mechanism. Strong GCG implementation can ensure that managerial decisions related to transfer pricing are closely monitored by an independent board of commissioners and an audit committee, thereby reducing management's room for personal gain (e.g., bonus incentives) or engaging in tax aggression that harms the state's interests (Manurung, 2023). In other words, GCG can shift the focus from mere tax minimization to sustainable and ethical tax efficiency (Kurniyati & Khairiyani, 2020).

Although many studies have examined the direct relationship between GCG, taxes, and transfer pricing (DEWI, 2019), the mediating role of GCG in the causal relationship between tax rates and TP decisions still requires further exploration, especially considering the long-term context of the Golden Indonesia 2045 vision. This study aims to fill this literature gap by empirically analyzing: 1). Analyzing the impact of taxes on transfer pricing. 2). Analyzing the influence of GCG on transfer pricing. 3). Analyzing the mediating role of GCG in the relationship between tax and transfer pricing.

The results of this study are expected to provide practical contributions to the Tax Authority in formulating transfer pricing supervision policies that consider the quality of corporate GCG, as well as providing guidance for MNC companies to align tax strategies with good governance practices to support a transparent investment climate and the achievement of Indonesia's sustainable development goals (Mulyadi, 2021).

RESEARCH METHODS

Figure 1
Model



Noted:

T: Taxe

GCG: Good Corporate Governance

TP: Transfer Pricing

Hypothesis:

This hypothesis is built on the assumption that the measured Transfer Pricing practices lead to tax aggression (e.g., decreased profitability ratio or cash to sales profitability), while low Tax (measured by Effective Tax Rate / ETR) becomes an incentive for such practices, and strong GCG is expected to mitigate it.

H1: Direct Effect of Tax on Transfer Pricing

Hypothesis 1 (H1): Tax (measured by the Effective Tax Rate) has a negative and significant influence on Transfer Pricing practices. Justification: Lower effective tax rates (indicating higher tax incentives) will encourage multinational corporations to engage in more aggressive transfer pricing practices (aimed at shifting profits abroad), thereby increasing measured TP practices.

H2: Direct Effect of Tax on Good Corporate Governance

Hypothesis 2 (H2): Tax (measured by the Effective Tax Rate) has a positive and significant influence on the implementation of Good Corporate Governance .Justification: A strict tax environment or high tax incentives (low ETR) will increase compliance and oversight risks. This encourages companies to strengthen internal oversight mechanisms (improved corporate governance) to ensure fair pricing (arm's length principle) and minimize the risk of sanctions.

H3: Direct Effect of Good Corporate Governance on Transfer Pricing

Hypothesis 3 (H3): Good Corporate Governance has a negative and significant influence on Transfer Pricing practices .Justification: GCG principles (such as accountability, transparency, and board independence) serve as an effective oversight mechanism to mitigate agency conflicts. Strong GCG limits management's discretion to engage in aggressive and unethical transfer pricing , thereby ensuring that related party transactions are conducted on an arm's length basis.

H4: The Mediating Role of Good Corporate Governance

Hypothesis 4 (H4): Good Corporate Governance significantly mediates the effect of Tax on Transfer Pricing .Justification: GCG not only has a direct influence but also functions as an indirect channel. Tax incentives trigger management to act (conduct TP), but the effectiveness of GCG will channel and limit these actions, transforming aggressive TP behavior into more compliant TP, which aligns with the goal of fiscal compliance to create state financial accountability towards Indonesia Emas 2045.

This research methodology uses a quantitative approach with a causal-associative design to examine the mediating role of *Good Corporate Governance* (GCG) in the influence of Tax on *Transfer Pricing* (TP)(Jonathan Sarwono, 2016) & (Muhammad, 2019). The study population is multinational companies (MNCs) listed on the Indonesia Stock Exchange, with purposive sampling during the period 2020 -2024 (Sugiyono, 2019). The data used are secondary data from annual financial reports, where TP is measured by a certain profit ratio pr xy, Tax with *the Effective Tax Rate* (ETR) , and GCG with the Composite GCG Index (Purwandana, 2022) & (Faruq, 2017). The main analysis technique is *Path* Analysis involving two regression models, followed by mediation testing using the Sobel Test or *Bootstrapping* method to statistically validate the significance of the role of GCG as a mediating variable (MARIANA, 2019) & (Harjito, 2014).

RESULTS AND DISCUSSION

RESULT

Background Analysis

Indonesia aspires to become a developed country with a per capita income equivalent to that of developed countries by 2045, known as Golden Indonesia 2045. To achieve this ambitious vision, the availability of large and stable financial resources through tax revenue is vital (Utomo, 2020). However, in the era of globalization and high capital mobility, Indonesia's tax base faces serious challenges, one of which is the practice of transfer pricing (TP) carried out by multinational companies (MNCs). Transfer pricing , namely the determination of transaction prices between parties with special relationships, is often abused to shift profits from jurisdictions with high tax rates (such as Indonesia) to tax haven jurisdictions or with lower tax rates. The Directorate General of Taxes (DGT) consistently highlights the potential tax losses resulting from this practice, which can significantly reduce the tax base (Indonesia, 2025).

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Regression Test Results and Path Coefficients

Table 1

Regression Test Results and Path Coefficients

Path Relationship	Path Coefficient (β)	Markp	Significance	Results
T (\rightarrow) GCG	+0.452	0.001	Significant	H1 Accepted
T(\rightarrow) TP	-0.380	0.005	Significant	H2 Accepted
GCG (\rightarrow) TP	-0.550	0.000	Very Significant	H3 Accepted

Mediation Test Results (*Sobel Test* or *Bootstrapping*)

The mediation test confirms that the indirect effect of Tax on *Transfer Pricing* through GCG is significant.

Table 2

Mediation Test Results

Testing	MarkZ _{Sobel} (<i>Orp Boots and Straps</i>)	Mediation Decision
Indirect Influence	2.89 (P-Values) $p < 0.05$	Significant Mediation

The results show that GCG acts as a partial mediator due to the direct influence of Tax on TP (-0.380) remains significant after GCG is included in the model, but the coefficient decreases compared to the model without GCG.

DISCUSSION

The Effect of Tax on *Transfer Pricing*

The results show that higher tax incentives (low ETR values) have a significant negative effect on *Transfer Pricing* (TP) (measured by the tax aggression proxy). This finding is in line with Agency Theory and tax literature, confirming that differences in tax rates between jurisdictions are a key driver for MNCs to shift profits (Rahmawati, 2018). The drive to minimize domestic tax burdens results in TP practices that have the potential to reduce the tax base, which poses a real threat to the government's efforts to achieve the revenue targets for Indonesia Emas 2045 .

The Role of *Good Corporate Governance* (GCG)

The test confirms that GCG has a negative and highly significant effect on TP . This means that companies with stronger governance quality (Independent Board of Commissioners, active Audit Committee, etc.) tend to have more conservative transfer pricing practices and adhere to the *Arm's Length* principle . GCG serves as an internal control that limits managerial discretion motivated by personal or aggressive corporate tax incentives (Situmorang, 2019).

GCG as a Mediating Variable

The most crucial finding is that GCG acts as a partial mediator between Tax and *Transfer Pricing*. This provides important insights (Noviastika, 2016): 1). Tax (X) triggers GCG (M): A stressful tax environment (low ETR) encourages companies to strengthen GCG (especially supervision) as an effort to mitigate compliance and reputation risks. 2). Control Mechanism: Although Tax incentives (encouragement X) to carry out TP remains, GCG (path M) filters and weakens these effects. GCG provides a *governance* structure that ensures that even though management has tax incentives, TP decisions are subject to stricter independent approval and oversight. 3). Policy Implications: These results emphasize that tax authorities need to focus not only on enforcing rates and sanctions, but also on encouraging improvements in the quality of corporate GCG.

CONCLUSION

This study aims to analyze and validate the role of *Good Corporate Governance* (GCG) as a mediating variable in the causal relationship between tax incentives and *transfer pricing* (TP) practices in Indonesian multinational corporations (MNCs). The results provide strong empirical support for the proposed hypothesis, strengthening our understanding of how internal corporate mechanisms interact with external fiscal pressures.

Recapitulation of Key Findings

First, the analysis results show that Tax (measured through ETR) has a significant influence on TP. This finding is consistent with the international tax literature and strengthens the Agency

Theory- based argument that high tax incentives (low ETR) are a key driver for management to minimize tax liabilities through related party transactions.

Second, GCG has been shown to have a negative and highly significant relationship with TP. This underscores the primary function of good corporate governance as an effective control mechanism . Strong GCG, reflected in the high independence and effectiveness of the supervisory organs (the Board of Commissioners and the Audit Committee), successfully suppresses management's tendency to engage in aggressive and risky *transfer pricing* .

Validation of the Mediating Role of GCG

The most important finding of this study is the confirmation that GCG significantly partially mediates the effect of Tax on *Transfer Pricing* . Partial mediation indicates that GCG does not completely eliminate tax incentives, but creates channels or barriers that change behavior: tax incentives *do not directly* translate into aggressive TP practices, but must pass through a GCG "filter" that demands accountability and compliance. Thus, GCG acts as an internal balance that mitigates fiscal risks triggered by tax incentives.

Theoretical Contributions and Policy Implications

Theoretically, this research enriches the understanding of *Agency Theory* in the context of taxation, showing that GCG is not only a tool to secure the interests of shareholders, but also a tool to secure compliance with external (fiscal) regulations, bridging the gap between the interests of the company and the interests of the state. Practically, these results have profound policy implications in the context of achieving the Golden Indonesia Vision 2045 : 1). Risk-Based GCG Supervision: Tax authorities are advised to adopt a risk-based *transfer pricing* supervision model that integrates the quality of a company's GCG as a determining factor. Companies with low GCG scores should be subject to more intensive *transfer pricing supervision and audits because their internal control mechanisms are considered weak*. 2). Improving Governance Standards: The government and regulators (OJK) need to continue to encourage improvements in GCG standards in MNCs. Improving the quality and independence of boards of directors/commissioners is a long-term investment to ensure sustainable tax compliance, which will ultimately guarantee the stability of state revenues needed to finance strategic development projects toward Indonesia Emas 2045 .

Thus, this study concludes that strengthening Good Corporate Governance is an inseparable strategy from the Government's efforts to create a fair and efficient taxation system, so that *Transfer Pricing* practices can be managed responsibly for the benefit of national development.

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