THE INFLUENCE OF FOREIGN OWNERSHIP AND DEBT COVENANT ON TRANSFER PRICING: A STUDY OF CORPORATE GOVERNANCE

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How to cite this paper:
Hidayah, R., Suryandari, D., Yanto, H., Sa'dulloh, A., Suryarini, T., Wahyuningrum, I. F. S., Kayati, I. N., Hasna, S. I., & Nugraha, S. A. A. (2025). The influence of foreign ownership and debt covenant on transfer pricing: A study of corporate governance. *Journal of Governance & Regulation, 14*(2), 49–57.
https://doi.org/10.22495/jgrv14i2art5

ISSN Print: 2220-9352
ISSN Online: 2306-6784

Received: 15.03.2024
Revised: 28.06.2024; 19.03.2025
Accepted: 10.04.2025

JEL Classification: G41, M4, M16, M21
DOI: 10.22495/jgrv14i2art5

Abstract

The business world is developing very rapidly in countries. Transfer pricing (TP) is vital in multinational companies (Kumar et al., 2021). This study analyzes the influence of foreign ownership (FO) and debt covenants on TP with multinationality as a moderating variable. The research population is manufacturing companies listed on the Indonesia Stock Exchange (IDX). The sample used the purposive sampling method. This study uses the partial least squares structural equation modeling (PLS-SEM) method to test the research hypotheses. The results prove that FO does not affect TP and debt covenants have a significant positive effect on TP. Furthermore, multinationality can moderate by weakening the impact of debt covenants on TP. The novelty of this research gives new insight into corporate governance using multinationality as a moderating variable on the relationship between debt covenant, FO, and TP. Further research, may investigate the influence of environmental, social, and governance factors on TP. The study has implications for policymakers to establish clear regulations to ensure transparency and to prevent tax avoidance practices. Therefore, company management should pay more attention to the debt ratio. Then, investors have to consider how companies deal with tax risk.

Keywords: Foreign Ownership, Debt Covenant, Multinationality, Transfer Pricing

Authors' individual contribution: Conceptualization — R.H., D.S., and H.Y.; Methodology — D.S. and I.N.K.; Software — A.S.; Validation — R.H. and H.Y.; Formal Analysis — D.S. and I.F.S.W.; Investigation — T.S. and I.F.S.W.; Resources — A.S. and S.A.A.N.; Writing — R.H. and S.I.H.; Writing — Review & Editing — R.H., T.S., and S.I.H.; Project Administration — S.A.A.N.

Declaration of conflicting interests: The Authors declare that there is no conflict of interest.

Acknowledgements: The Authors appreciate the support of Research and Community Service, Universitas Negeri Semarang (14.26.2/UN37/PPK.10/2024) for all facilitates during the research.

1. INTRODUCTION

The emergence of economic globalization will have an impact on the economies of various countries. This requires every country to be more open in carrying out international trade, one of which is through cooperation. Firm size is an important factor for business sustainability (Hidayah et al., 2022). The larger the company size, the higher the tendency to have multinational subsidiaries. One form of openness in conducting international trade is the existence of multinational companies. Economic growth in Indonesia is caused by several factors, including global trade activities, which include import-export activities carried out by several multinational companies. One of the problems faced by multinational companies is transfer pricing (TP). TP issues are often encountered in mining and manufacturing multinational companies. Hence, this issue should be a higher priority for tax authorities in Indonesia and several other countries. TP is closely related to the pricing policy for goods, services, or intangible assets of a company which will later be transferred to related parties within the company or between companies, either within one country or between countries. This TP issue is one of the company's strategies for avoiding taxes (Sikka & Willmott, 2010; Wealth et al., 2023). Several experts state that TP activities are one of the company's strategies for obtaining high profits. TP could affect tax avoidance (Hidayah et al., 2022).

TP activities are not illegal because they stem from the company's goal of assessing and evaluating the performance of members both within one department and between departments (Melnychenko et al., 2017; Muhammadi et al., 2016) However, as time goes by, TP practices become illegal if they do not comply with applicable regulations and use unreasonable transaction prices. Companies take advantage of applicable regulatory loopholes to gain company profits through taxation. Indonesia's real form of handling TP issues is by establishing cooperation between countries and organizations that handle international taxation issues. Indonesia has also adopted several policies from the Organization for Economic Co-operation and Development (OECD) to deal with existing TP issues.

Indonesia is estimated to lose US $4.78 billion or if converted into IDR 67.6 trillion due to the tax avoidance actions of multinational companies (Hidayah et al., 2022). Apart from that, Indonesia will potentially lose tax revenues of 1,300 trillion due to TP activities that do not comply with regulations or are unreasonable (Larasati & Ariffitria, 2023). The director general of taxes stated that there were irregularities in the sales value and royalty payments of the Toyota Motor Manufacturing Indonesia (TMMI) company. Therefore, the TMMI company has to pay lower tax than what it should have paid, so that TMMI has to pay the tax shortfall of IDR 500 billion following the correction that has been submitted by the director general of taxes (Larasati & Ariffitria, 2023).

Studies about the relationship between debt covenant and foreign ownership (FO) on TP are still limited. Based on several previous research, one of the factors influencing TP practices is FO. FO and Debt covenants have a significant positive effect on TP (Hikmatin & Suryarini, 2019; Rohaeni et al., 2021; Sundari & Susanti, 2016). In addition, FO influences TP (Supriyati et al., 2021) contrary, researchers believe FO does not affect TP (Nofryanti & Arsjah, 2019; Rohaeni et al., 2021). Debt covenants significantly positively affect TP (Sari et al., 2022). However, the debt covenant is negative and significant to TP (Priyanti & Suryarini, 2021). In addition, debt covenants do not affect TP the variables of intangible assets and company size have a significant positive influence on TP (Taylor et al., 2015). Based on previous research, shows several elements influence TP, namely FO, independent commissioners, debt covenants, intangible assets, company size, and taxes (Ahn et al., 2018; Davies et al., 2018; Jayanti & Kusumawati, 2023; Larasati & Ariffitria, 2023; Nofryanti & Arsjah 2019; Priyanti & Suryarini, 2021; Sundari & Susanti, 2016).

This research uses *FO* and debt covenant (*DEBT*) variables as independent variables based on previous research. This variable was taken of course based on the inconsistent results of previous research and several limitations of previous research on similar topics. This research presents moderating variables. The aim is to find out whether other variables can strengthen or weaken the influence of independent variables on TP variables. This is based on the research gap that has been found, allowing researchers to come up with moderating variables. In this research, researchers used the multinationality (*MULTI*) variable as a moderating variable. *MULTI* is a strong variable, consistently having a significant positive effect on *TP* (Liana et al., 2020; Tayloret et al., 2015).

The remaining structure of this study is as follows. Section 2 provides a literature review and hypotheses development. Section 3 describes the research methodology including population and sample, measurement of variables, and data analyses. Section 4 presents the result. Section 5 show discusses the results. Section 6 describes the conclusions and suggestions.

2. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

2.1. Foreign ownership and transfer pricing

Theories that can describe the relationship between these variables and TP are agency theory and positive accounting theory. Agency theory describes the relationship between principal and agent where the principal is represented by the owner or shareholder and the agent is represented by company management (Alchian & Demsetz, 1975; Jensen & Meckling, 1976). If the agent does not fulfill orders or agreements with the principal, an agency conflict will occur. This conflict occurs because of differences in goals and information asymmetry between the principal and the agent, where the agent or company management tries to get the maximum profit possible by taking various methods, one of which is the TP policy. This agency theory is related to FO variables.

The relationship between agency theory and FO is shown when an agency conflict occurs, namely, because there are differences in interests between the principal and the agent, or other words, there are interests that take priority over other interests (Collien et al., 2023; Grove et al., 2023). This is shown when a foreign controlling shareholder carries out sales or purchasing activities for his/her company using unfair TP practices, this condition will benefit the foreign controlling shareholder.

Minority shareholders or non-controlling shareholders suffer losses due to these activities, the efforts made by foreign controlling shareholders are a form of maximizing the control rights obtained over share ownership.

Companies with foreign parties usually face asymmetry information due to policy, language, and geographic limitations. These barriers will make companies provide information openly and voluntarily to foreign parties who need company information. The policy decisions taken by the company are based on existing FO. The higher the FO of the company, the stronger the voting rights of investors in determining company policy. This policy will of course benefit foreign parties or foreign shareholders. This statement is further strengthened by previous research. FO has a significant positive effect on TP (Fathi & ElBannan, 2017; Setiawan et al., 2021). In addition, FO has a significant influence on TP practices.

H1: Foreign ownership has a significant positive effect on transfer pricing.

2.2. Debt covenant and transfer pricing

A debt covenant or debt agreement contract is a form of agreement issued by creditors to debtors to limit company activities that could potentially damage the value of the company's loans. Companies will show their best performance to be able to convince creditors that the company can pay off its loans, this happens if the company's loan level tends to be high (Watts & Zimmerman, 1986). This statement follows the accounting theory presented if a company shows a level of debt that tends to be significant, then the financial statements published do not reflect accounting conservatism (Watts & Zimmerman, 1986). This is because company management tends to manipulate profits and assets by increasing them to reduce the risk of renegotiating company debt. The company will show its best performance to lenders by increasing profits and the value of the company's assets as high as possible. One way companies take this is by using TP practices.

There is a significant positive relationship between debt covenants and TP. This condition occurs because the higher the company's debt level, the closer the company is to the debt agreement limits. This will increase the risk of deviations from the agreed agreements and the costs incurred. In addition, debt covenants positively affect TP practices (Kristina & Muhyarsyah, 2023). One of the ways companies deal with this condition is by implementing TP practices, namely increasing company profits and loosening credit limits.

H2: Debt covenants have a significant positive effect on transfer pricing.

2.3. Multinationality, foreign ownership, and transfer pricing

Ownership is an important factor in determining company policy. The company will invest in countries that have their advantages. The company's new market expansion is a factor influencing FO. Multinational companies carry out TP practices using the existence of subsidiaries to carry out unfair transactions (Pratama, 2020). In addition, multinational companies that have a high portion of foreign share ownership have a significant positive effect on TP practices (Richardson et al., 2013). This is in line with agency theory where if foreign controlling shareholders have a high portion of shares, this will have an impact on company decisions, one of which is when carrying out transactions involving overseas subsidiaries in expanding the company's market share. Multinationality can strengthen the relationship between FO and TP. This condition is caused by multinational companies taking advantage of gaps in differences in tax rates encountered by subsidiaries. Multinationality can influence company decisions in carrying out TP practices. In implementing TP, companies must pay attention to factors encountered by subsidiaries in various countries, such as language differences, tax regulations, and company policies. Several research references show that multinational companies that have a high portion of foreign share ownership influence TP practices.

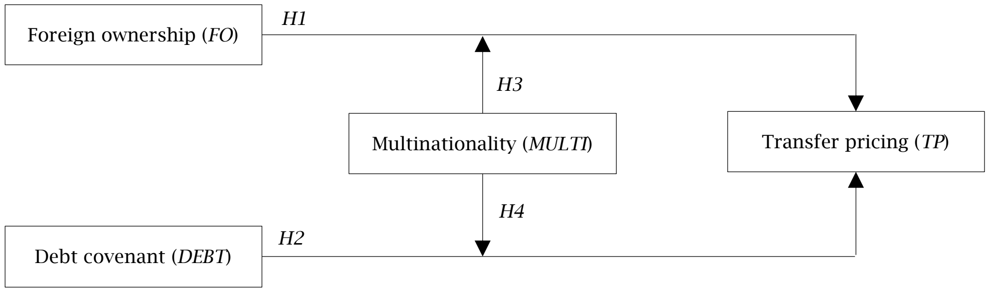
H3: Multinationality can moderate by strengthening foreign ownership of transfer pricing.

2.4. Multinationality, debt covenants, and transfer pricing

Multinational companies always maintain their existence in the international world by paying attention to internationalization or diversion. This is shown by how many foreign subsidiaries the company has. To maintain its existence, the company will strengthen its finances by increasing company profits through TP practices. Apart from that, it is also to fulfill the requirements issued by creditors regarding debt covenants. The debt covenant hypothesis in positive accounting theory predicts that companies manage earnings in order to avoid possible future debt covenant violations (Watts & Zimmerman, 1986). The higher the company's debt-to-equity ratio (DER), the more company management tends to choose accounting policies that can increase company profits. The way companies take to increase profits is by shifting profit recognition from the next period to the current period. This condition has an impact on the company's small leverage ratio and will increase the level of creditors' trust in the company. This is because financial conditions tend to be stable with minimal risk of bankruptcy. Multinationality and debt covenants simultaneously influence TP in manufacturing companies. Multinational companies increase company profits by using TP practices to strengthen company finances and avoid regulations related to debt covenants issued by creditors. This method is used by companies to maintain the involvement and trust of multinational companies with international markets and creditors. This condition is reflected in a diversion in the form of branch subsidiaries abroad.

H4: Multinationality can moderate by strengthening the debt covenant on transfer pricing.

Figure 1. Theoretical framework



3. RESEARCH METHODOLOGY

3.1. Population and sample size

This research uses a deductive quantitative approach involving numerical data that is statistically analyzed to verify, develop, and discover knowledge (Hair et al., 2016). The research design used is a hypotheses testing study, which empirically builds the hypotheses that have been proposed and tests the influence between the variables hypothesized in the research. This research uses panel secondary data from annual and financial reports of manufacturing companies listed on the Indonesia Stock Exchange (IDX) from 2019 to 2021. The secondary data was obtained from the official IDX website (https://www.idx.co.id/id). The sampling technique in this research used purposive sampling. There are 25 companies as research samples with three years of observation, so there are 75 units of analysis. Table 1 displays information regarding sampling.

Table 1. Research sampling

No.	*Criteria*	*Total*
1	Manufacturing companies listed on the IDX for the 2019–2021 period	215
2	Manufacturing companies that do not publish annual reports consistently and completely from 2019 to 2021	45
3	Manufacturing companies that do not have complete data regarding research variables	145
Number of sample companies (*i*)		25
Number of years (*t*)		3
The final number of research analysis units ($i \times t$)		75

3.2. Measurement of variable

This research uses the dependent variable, namely *TP*. The independent variables consist of *FO* and *DEBT*. This research adds *MULTI* as a variable that moderates the relationship between *FO* and *DEBTs* on *TP* practices. This research does not use a control variable because of two reasons. Firstly, this research aims to capture the real condition of manufacturing companies listed on the IDX without any special treatment. Secondly, to achieve comprehensive research related to domestic market power. An overall summary of the operational definitions of the variables used in this research is presented in Table 2.

Table 2. Operational definition of variables

No.	*Variable*	*Definition*	*Measurement*
Dependent variable			
1	Transfer pricing (*TP*)	*TP* is a price policy determined in a transaction between divisions in a multinational company where the price is determined by the related parties based on reasonable limits. However, it is still possible for these prices to deviate.	*TP* = (receivables from related parties) / (total company receivables) × 100% (Supriyati et al., 2021)
Independent variable			
1	Foreign ownership (*FO*)	*FO* is the portion of ownership of a company's outstanding shares that is owned by parties outside the company, whether individuals, agencies, or legal entities with overseas status.	*FO* = (foreign share ownership) / number of outstanding shares) (Pratama, 2020)
2	Debt covenant (*DEBT*)	A *DEBT* is a debt agreement contract issued by a creditor or lender to a debtor or related company to limit company activities that could damage the value of the loan and/or the value of its recovery (Supriyati et al., 2021).	*DEBT* = (total debt) / (total capital) (Sari et al., 2022)
Moderating variable			
1	Multinationality (*MULTI*)	Multinational companies, generally known as multinational corporations, carry out business activities in various countries through affiliated subsidiaries such as exports and imports.	*MULTI* = (number of foreign subsidiaries) / (total number of subsidiaries) (Richardson et al., 2013)

3.3. Analytical methods

The data analysis consisted of descriptive statistical analysis and inferential statistical analysis. Descriptive statistical analysis is a method to find out the existing problem based on the data. Then, inferential statistical analysis is a systematic step to draw certain conclusions based on a sample or subset of data. This research uses partial least squares structural equation modeling (PLS-SEM) (Hair et al., 2016).

4. RESEARCH RESULTS

4.1. Descriptive statistics

The results of the descriptive analysis regarding *TP*, *FO*, *DEBTs*, and *MULTI* are seen in Table 3.

Based on Table 3, shows the results of descriptive statistical tests. The *TP* variable has a mean value of 0.21586. This means that the average level of *TP* in multinational companies in the manufacturing sector in Indonesia in 2019–2021 was 21.6%. The minimum value of 0.00003 indicates that the company with the lowest level of risk of carrying out *TP* practices was PT Argha Karya Prima Industry Tbk (AKPI) in 2019. Furthermore, the maximum value of 0.98863 was owned by PT Bumi Teknokultura Unggul Tbk (BTEK) in 2020. This shows that the BTEK company carries out quite a lot of transactions with related parties. This gives a signal that this company's *TP* practices tend to be higher than other sample companies.

The *FO* variable has a minimum value of 0.00124. This value was owned by PT Kimia Farma Tbk (KAEF) in 2019. This shows that KAEF has a lower amount of *FO* than other sample companies. This condition is because KAEF is a state-owned company whose capital is mostly owned by the government. Furthermore, the maximum value of the *FO* variable is 0.83886 owned by PT Japfa Comfeed Indonesia Tbk (JPFA) in 2021. This can be interpreted as 83% of the shares owned by JPFA being owned by foreign parties. The higher the share ownership held by foreign parties, the higher the indication that the company is carrying out *TP* practices with related parties. In other words, this company has a special relationship with foreign parties abroad. In addition, the average value of the *FO* variable is 0.24481 or 24.48%, which shows the average value of *FO* in manufacturing companies in Indonesia is 24.48% from 2019 to 2021.

The *DEBT* variable has a mean value of 1.37324. This indicates the average level of capital ownership structure and company assets financed by debt in multinational companies in the manufacturing sector in Indonesia in 2019–2021. The minimum value of 0.13118 is owned by PT Ekadharma International Tbk (EKAD) in 2021. This shows that the EKAD company has a fairly weak capital ownership structure compared to other sample companies in this study. Meanwhile, the maximum value of 17.21064 was owned by PT Central Proteina Prima Tbk (CPRO) in 2019. This means that the CPRO company has a strong capital ownership structure and the EKAD company has assets financed by debt which is quite high. Hence, the risk of the company carrying out *TP* practices tends to be higher than other sample companies.

The *MULTI* variable has a maximum value of 1.00000 owned by AKPI in 2019–2021. This means that the AKPI company has a balanced comparison between the number of foreign subsidiaries and the total subsidiaries owned. The minimum value of the *MULTI* variable is 0.01111 owned by Indomobil Sukses Internasional Tbk (IMAS) in 2021. This shows that foreign subsidiaries owned by IMAS have the smallest proportion compared to other sample companies. In conclusion, the possibility of *TP* practices is higher when a company has many foreign subsidiaries.

Furthermore, the *MULTI* variable has a value of 0.29765. This condition indicates that multinational companies in the manufacturing sector in Indonesia have a low number of foreign subsidiaries, only 29.76%. In conclusion, manufacturing sector multinational companies listed on the IDX still have low ownership of subsidiaries in other countries.

Table 3. Results of descriptive statistical analysis

Indicator	*N*	*Mean*	*Min*	*Max*	*Std. dev.*
FO	75	0.24481	0.00124	0.83886	0.25217
DEBT	75	1.37324	0.13118	17.21064	2.18567
MULTI	75	0.29765	0.01111	1.00000	0.22293
TP	75	0.21586	0.00003	0.98863	0.25332

4.2. Inferential statistics

4.2.1. Convergent validity test and colinearity test

Based on Table 4, it can be seen that all research variables have a value outer loading of 1.00. Hence, the research variables are declared valid.

Table 4. Convergent validity test

Variable	*FO*	*DEBT*	*TP*	*MULTI*	*MULTI * FO*	*MULTI * DEBT*
FO	1.000	0.000	0.000	0.000	0.000	0.000
DEBT	0.000	1.000	0.000	0.000	0.000	0.000
TP	0.000	0.000	1.000	0.000	0.000	0.000
MULTI	0.000	0.000	0.000	1.000	0.000	0.000
MULTI * FO	0.000	0.000	0.000	0.000	1.000	0.000
MULTI * DEBT	0.000	0.000	0.000	0.000	0.000	1.000

Going more depth, the colinearity test is a test that aims to find out how far a construct is truly different from other constructs (Hair et al., 2016). The variance inflation factor (VIF) value for each variable shows a value of less than five, so there are no symptoms of multicollinearity in this model.

Table 5. Colinearity test

Factor	*FO*	*DEBT*	*TP*	*MULTI*	*MULTI * FO*	*MULTI * DEBT*
Composite reliability	1.000	1.000	1.000	1.000	1.000	1.000
Cronbach's alpha	1.000	1.000	1.000	1.000	1.000	1.000
AVE	1.000	1.000	1.000	1.000	1.000	1.000
Full collinearity VIF	1.348	1.218	1.119	1.379	2.334	1.877

Note: AVE — average variance extracted.

Based on Table 5, shows that each indicator block of research variables has a cross-loading value of the latent construct that is greater than the value of the other constructs. Therefore, all variables have met the criteria for discriminant validity.

4.2.2. Q^2 predictive relevance

The Q^2 predictive relevance test is used to measure how good the model's observation values are. Table 6 shows the Q^2 value is greater than zero, so this research model is appropriate.

Table 6. Q^2 predictive relevance

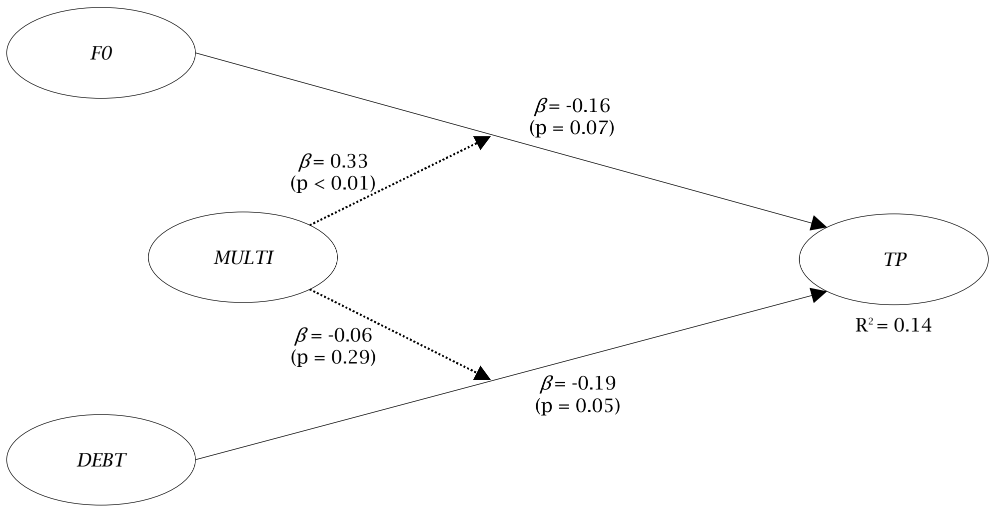
Factor	*FO*	*DEBT*	*TP*	*MULTI*	*MULTI * FO*	*MULTI * DEBT*
Composite reliability	1.000	1.000	1.000	1.000	1.000	1.000
Cronbach's alpha	1.000	1.000	1.000	1.000	1.000	1.000
AVE	1.000	1.000	1.000	1.000	1.000	1.000
Full collinearity VIF	1.348	1.218	1.119	1.379	2.334	1.877
Q-squared	0.139					

Based on Table 7, shows a p-value of 0.075 with a path coefficient of -0.160, so the *H1* is rejected. The *H2* shows a p-value < 0.05 with a path coefficient value of -0.19. Hence, *H2* is accepted. Furthermore, the p-values in *H3* show a p-value < 0.001 with a path coefficient of 0.334. Hence, *H3* is accepted. Finally, the p-value in *H4* shows 0.29 with a path coefficient value of -0.063. Therefore, *H4* is rejected.

Table 7. Hypotheses test

Hypothesis	*Correlation*	*Path coefficient*	*p-values*	*Explanation*
H1	*FO → TP*	-0.160	0.075	Rejected
H2	*DEBT → TP*	-0.19	0.046	Accepted
H3	*MULTI * FO → TP*	0.334	< 0.001	Accepted
H4	*MULTI * DEBT → TP*	-0.063	0.29	Rejected

Figure 1. The output of PLS-SEM



5. DISCUSSION

5.1. The effect of foreign ownership on transfer pricing

In Table 7, the influence of the *FO* variable on *TP* has a negative path coefficient value of -0.160 with a p-value of 0.075 which means the significance of the p-values is greater than 0.05 (5%). This condition shows that *FO* does not have a significant influence on *TP*. Therefore, empirically *H1* is rejected.

Foreign controlling share ownership in manufacturing companies in this study does not exercise control rights. When making decisions, do not interfere in carrying out TP practices. Another reason *H1* was rejected was that manufacturing companies emphasized caution in conducting transactions with related parties. Furthermore, collaborate with other countries' fiscal authorities to determine and agree on transfer prices with related parties or those with special relationships.

The results of this research are not in line with agency theory, which states that agency conflicts occur because of differences in interests between the principal and the agent. This agency theory should be able to support *H2* because foreign controlling shareholders can use their control rights to make purchases or sales to their companies using TP practices. In addition, foreign share ownership can transfer assets aimed at reducing expenses which will have an impact on reducing company profits. This is done by foreign controlling shareholders to maximize personal welfare and has an impact on non-controlling shareholders who feel disadvantaged by maximizing their control rights. Moreover, foreign controlling shareholders have greater access to company information than non-controlling shareholders. Easy access to information by foreign companies will provide opportunities for companies to carry out TP practices. However, this statement was not proven in this research.

This research is in line with previous research that the FO variable does not influence the TP variable (Pratama, 2020; Jayanti & Kusumawati, 2023). This condition occurs because foreign controlling shareholders do not carry out TP practices with the aim of expropriation. In this research, all decisions taken by the company must be approved by the board of directors. This is irrelevant if the foreign controlling shareholder wants to carry out a takeover or expropriation.

5.2. The effect of debt covenant on transfer pricing

The test results are presented in Table 7. The influence of the *DEBT* variable on *TP* has a positive path coefficient value of -0.19 with a p-value of 0.046 which means that the significance of the p-values is not bigger than 0.05 (5%). This condition shows *DEBTs* have a significant positive influence on *TP*. Hence, empirically *H2* is accepted.

DEBTs have a significant positive influence on *TP*. This is due to the tendency of companies to use debt covenants as a way to increase company profits. When a company has a fairly high level of debt, the company will be closer to the debt agreement limits. This is supported by the debt ratio of manufacturing companies in this study which is quite high, namely 137.32% as measured by the DER. Therefore, the higher the company's debt level, the greater the company's possibility of carrying out TP practices. This will also have the impact of increasing the risk of the company making deviations from the agreed debt agreements and the costs incurred. The company's solution to overcome this is to implement TP by increasing company profits and loosening credit limits.

This research is in line with positive accounting theory by Watts and Zimmerman (1986) that if a company shows a level of debt that tends to be significant, then the financial reports published do not reflect accounting conservatism. This is because company management tends to manipulate profits and assets by increasing them. The aim is to reduce the risk of renegotiation of company debt. The company will show its best performance to lenders through the highest possible profits and company asset value. Therefore, one of the methods taken by companies is to use TP practices.

The results of this research are supported by several studies that debt covenants have a positive effect on TP (Sundari & Susanti, 2016; Sari et al., 2022; Kristina & Muhyarsyah, 2023). Companies tend to choose accounting methods that are indicated to be able to manipulate income according to the company's needs. One way to do this is by reducing the tax cost and increasing the interest cost through debt loans. This condition has an impact on increasing company profits by using TP practices. The higher the profits obtained by the company, the higher the creditor's level of trust in the debtor. Debt covenants have a positively significant influence on company decisions in carrying out TP practices. A high percentage of the company's debt ratio causes the company to get closer to the debt covenant. Moreover, debt covenants have a significant positive influence on TP practices (Ramdhany & Andriana, 2022). The higher the company's debt ratio, the higher the indication that the company is carrying out TP practices.

5.3. The Influence of multinationality in moderating the relationship of foreign ownership to transfer pricing

Based on the test in Table 7, the influence of *MULTI* in moderating the relationship between *FO* and *TP* has a positive path coefficient value of 0.334 with a p-value of < 0.001. This shows the significance of p-values is smaller than 0.05 (5%). This condition shows that *MULTI* can strengthen the influence of *FO* on *TP*. Hence, empirically *H3* is accepted.

Multinationality is one of the factors that can influence a company's decision to carry out TP practices. This is as stated by Pratama (2020) in his research that multinational companies carry out TP practices using the existence of subsidiaries to carry out unfair transactions. The company's ownership structure, which is dominated by FO, is one of the factors that causes companies to carry out unreasonable TP practices.

The results of this research support agency theory. If foreign control has a high share of shares, it will have an impact on company decisions. One of them is when carrying out TP transactions involving overseas subsidiaries in expanding the company's market share. In line with previous research stated multinational companies that have a high portion of foreign share ownership have a significant positive effect on TP practices (Richardson et al., 2013; Taylor et al., 2015).

In agency theory, it is stated that company owners and management have different interests in determining transfer prices for their subsidiaries domiciled abroad. Where the owner seeks to maximize personal profits globally through TP while company management prioritizes company sustainability. This agency conflict of course results in agency costs that can be charged to the company. The resolution of this agency problem of course involves foreign controlling shareholders in determining decisions related to the company's TP practices.

5.4. The influence of multinationality in moderating the debt covenant relationship on transfer pricing

Based on Table 7 shows that the influence of *MULTI* in moderating the relationship between *DEBTs* and *TP* has a negative path coefficient value of -0.063 with a p-value of 0.29. This means that the significance of p-values is smaller than 0.05 (5%). This shows that *MULTI* can moderate by weakening the influence of *DEBTs* on *TP*. Therefore, empirically *H4* is rejected.

The existence of multinationals in manufacturing companies could weaken the relationship between debt covenants and TP. Hence, companies with subsidiaries in many countries could minimize the influence of debt covenants in TP practices involving subsidiaries located abroad. This condition can occur because multinational companies have flexibility in determining transfer prices involving subsidiaries located abroad. This is regardless of the regulations set by the creditor. This flexibility can be seen in the company's financial reports, especially the profit and loss report and balance sheet. When multinational companies play with transfer prices, it has an impact on the company's profit or loss. The company's efforts are to shift profits to subsidiaries. Apart from that, it can be seen from the company's balance sheet that when a company sets a transfer price that is relatively lower than the fair market price, it will have an impact on the company's assets which tend to be low.

This research is in line with Watts and Zimmerman (1986) that the debt covenant hypothesis in accounting theory is positive. The higher the company's DER, the more company management tends to choose accounting policies that can increase company profits. Companies increase profits by shifting profit recognition from the next period to the current period. This condition has an impact on the company's small leverage ratio, this situation increases the level of creditors' trust in the company. In this theory, credit covenants are used by creditors as a monitoring tool, so that companies maintain their financial stability. This condition will result in the company being able to pay off its obligations with a small risk of the company going bankrupt.

6. CONCLUSION

This research provides empirical support that FO does not influence TP. Debt covenants have a significant positive influence on TP. The originality of this study provides some new insights into the role of multinationality. First, multinationality can weaken the relationship between debt covenants and TP. Second, multinationality can strengthen the relationship between FO and TP. Hence, companies must consider the existence of subsidiaries in several countries which has different regulations.

The research findings have significant implications for companies. First, company management is expected to be more careful in implementing TP practices. Second, to reach effective performance, the management should avoid unreasonable TP practices. Third, companies must continue to comply with the regulations that apply to various overseas subsidiaries to avoid administrative sanctions. Furthermore, company management is expected to pay attention to the company's debt ratio to avoid financial risks. Then, this finding also gives insight for policymakers to establish strict regulations on TP to prevent tax avoidance.

This research is important for adding literature on TP, especially in the form of the role of multinationality in the relationship between debt covenant, FO, and TP. This research captures the emerging condition of TP. In addition, this research gives other perspectives to the government when assessing and evaluating the TP policies in multinational companies. However, this research only focuses on the domestic market. Therefore, future research is expected to expand the sample area. This research ignores the environmental and social elements. Thus, future studies may provide additional insights by investigating the impact of environmental, social, and governance factors on TP.

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