CHAPTER I

INTRODUCTION

1.1 Background of Study

In this globalization era, the development of information technology, communication creates opportunities for companies to develop and innovate. This was triggered by advances in technology whose impact has had a direct effect on the transformation of the taxation landscape internationally or indirectly through globalization. Especially in these pandemic eras where the economy in the world is getting worse but the country needs to keep financing their expenditures and one of the sources of income received by the state is taxes. Taxes have a very important role in the state, especially in the implementation of development because taxes are a source of state revenue to finance all expenditures including development expenditures. Government income derived from taxes in 2017 was recorded at 85.6% of total revenue (Ministry of Finance Republic of Indonesia, 2017). This is proof that taxes are the largest revenue contributor to the government, however for tax companies is a burden that can reduce profits. Additionally, during times of economic downturn, countries around the world have established related legislation to control corporate tax evasion in order to avoid eroding tax revenue. Since tax authorities are becoming more protective of tax revenue, foreign tax planning is becoming highly scrutinized, and businesses that engage in non-compliant tax avoidance are more likely to face tax penalties and regulatory intervention. One of the taxation issues that imposes taxation obligations is taxation. As part of any company strategic plan, the tax plan should be evaluated to assess the tax burden on various plan alternatives, the difference in dirty profits, and the outcome of implementing the tax plan on expenditure.

A tax plan is one of the management factors that indirectly provides the organization with a purpose and direction, and determines when to do it, when to do it, and who to do it. The tax plan is the pressure on the control of all transactions in the tax consequences, the coordination of tax potential. High tax burden can motivate companies to conduct transfer of profits by means of transfer pricing. Taxes come from an individual or an organization, neither individual nor organization have their own legal law in the state starting from the tax objects, subjects and also the tariff of the tax. Different states will have different rules since then it can cause tax problems where the taxpayer does not want to pay double tax for an organization like the multinational companies. They also will face the problem of tariff differences and the applicable taxes in each country. A multinational company is a large company that is usually established in developed countries and then has subsidiaries in various countries including developing countries. However, not all multinational companies were first established in developed countries. Many companies that start out doing business in developing countries then eventually go global. Companies that have gone global have a very high role in political and social aspects. As the name implies, namely multinational, the company has run its business in various countries by having subsidiaries in other countries. The phenomenon of multinational companies in their expansion tends to operate their business in a decentralized manner and implement the concept of cost revenue profit and corporate profit center concepts, which can be measured and assess the performance and motivation of each division / unit concerned in order to achieve company goals. To achieve these goals between others use a transfer pricing system or transfer pricing transactions. The topic of transfer pricing is one that is very important and sensitive in the world of business and the economy at large, especially in the area of taxation. Multinational corporations transfer pricing practices would have an effect on state revenue, both directly and indirectly, in terms of taxes.

Transfer pricing is a company policy in determining prices transfer of a transaction whether in goods, services, intangible assets or transactions company finances. There are two groups of transactions in transfer pricing, namely: intra-company and inter-company transfer pricing. Intra-company Transfer pricing is transfer pricing between divisions within one company. Meanwhile, inter-company transfer pricing is a transfer pricing between two related companies. The transaction itself can be done in one country (domestic transfer pricing), or in different countries (international transfer pricing). very often the term transfer pricing is connoted with something that is not good, namely a transfer or shift of income from a company in a country with a higher tax rate to other companies in the same group in countries with lower tax rates thereby reducing the total tax burden the company group. There is also the term transfer pricing manipulation, namely the activities of that increase costs or lower bills with the aim of minimizing amount of tax payable. Usually the price manipulation that is done is one of them at the sale price. Transfer pricing is done by calculating the amount of profits generated by each business concerned, as well as the income tax collected in the exporting and importing countries. There are rules regulating the tax treatment of transactions between parties that have a special relationship in almost every tax law. This law is the legal framework for tax authorities to correct transactions that arise between parties that have a special relationship, and it is thought to be a rule that can address transfer pricing issues. In the past, corporations used transfer pricing primarily to measure the efficiency of members or business branches, but times have changed, and many companies now use transfer pricing to reduce tax payments.

Transfer pricing is the price of goods, services or intangible assets 3 which are transferred between divisions within a company or within that company have a special relationship or a multinational corporation. The main purpose of transfer pricing is to evaluate and measure financial performance of a company, but often also transfer pricing used by multinational corporations to minimize the amount of its tax paid through engineering prices transferred between divisions. The main success of transfer pricing from a tax perspective is due to the transaction special relationship. Transfer pricing is a policy regulated by a company to determine the transfer price for a transaction, whether the price for goods, services, intangible assets, or financial transactions carried out by the company. Transfer pricing can also be interpreted as the amount of price charged by an individual business unit to a multi-unit company for transactions that occur between them. Transfer pricing has become a very interesting issue with developments in technology, communication and transportation that play an active role in supporting life manufacturing companies.the tax burden.

Tax expense is a tax that is borne by taxpayers personal or corporate taxpayers that are required to be paid to the state as one of the state revenues. Decision making for transfer pricing will cause tax payments to be lower. Every company expects to reduce the tax burden, so that it can be a trigger for a company to make transfers pricing. The bonus mechanism has an impact on the choice to transfer price.

The tax is one of the reasons corporations use transfer pricing. Normally, businesses try to avoid paying hefty taxes. Transfer pricing is one method used by firms to cut profits by declaring lower profits on their financial accounts. Companies should utilize the fair price principle to decrease liabilities taxes, but they are more likely to employ transfer pricing, which can lead to agency conflict between principal and agent.

The bonus mechanism is an additional compensation or award given to employees for the successful achievement of the goals targeted by the company. The profit-based bonus mechanism is the method most often used by companies in giving awards to directors or managers. In carrying out their duties, directors tend to show good performance to company owners to get bonuses in managing the company. This is supported by the opinion of (Hartati et al., 2015) which states that the compensation (bonus) of directors is seen from the performance of various divisions or teams in one organization. The greater the overall company profit generated, the better the image of the directors in the eyes of the company owner. Therefore, the board of directors was able to raise profits in the expected year by selling inventories to inter-group companies in multinational companies at below market prices. This will affect the company's revenue and increase profits for the year. Bonus is a reward granted by the RUPS to members of the Board of Directors when the firm makes a profit.

So the title proposed in this research " **The Impact of Income Tax and Bonus Mechanism toward Income Shifting with Transfer Pricing Decision of Consumer Goods Listed in Indonesia Stock Exchange**"

1.2. Problem Limitation

Problem limitation of this study will be three variables which are Income Tax (X_1), Bonus Mechanism (X_2), toward the dependent variable, which is Income Shifting with Transfer Pricing Decision (Y) and the data to be used is limited to the financial statement of Consumer Goods Companies that are listed in Indonesia Stock Exchange 2017 – 2020. Problem limitation aims to get a clear boundary and to avoid any distorted results due to broad problems.

1.3. Problem Formulation

Based on the background of the problem that has been described, the problems are as follows:

1. Does Income Tax have significant impact towards Income Shifting with Transfer Pricing Decision in the Indonesia Stock Exchange ?
2. Does Bonus Mechanism have significant impact towards Income Shifting with Transfer Pricing Decision Consumer Goods Companies in the Indonesia Stock Exchange?

3. Do Income Tax and Bonus Mechanism simultaneously have an impact toward Income Shifting with Transfer Pricing Decision in Consumer Goods Companies in the Indonesia Stock Exchange

1.4. Objective of the Research

Based on the above problem formulation, the objectives of this study are as follows:

1. The impact of Income Tax towards Income Shifting with Transfer Pricing Decision in Consumer Goods Companies listed on Indonesia Stock Exchange
2. The impact of Bonus Mechanism towards Income Shifting with Transfer Pricing Decision in Consumer Goods Companies listed on Indonesia Stock Exchange
3. The impact of Income Tax and Bonus Mechanism toward Income Shifting with Transfer Pricing Decision in Consumer Goods Companies listed on Indonesia Stock Exchange

1.5. Benefit of the Research

The benefit of the research can be separated into two kinds of benefit, which are:

1.5.1. Theoretical Benefit

Theoretically, the research is expected to add understanding and to add knowledge for various parties related to the research topics in the field of taxation and as a reference for further research as well.

1.5.2. Practical Benefit

Based on the research objective, the research is expected to generate practical benefits as follows:

1. For author

   By doing this thesis it can improve writers' knowledge and learn more deeply regarding the income tax and bonus mechanism toward income shifting of transfer pricing and also the general transfer pricing in multinational companies.

2. For reader

   The findings of this study will be utilized as comparison material, as well as literature and references for future researchers on income tax, and bonus mechanism, as well as a reference for researchers.

3. For company

   This research helps the consumer goods companies in solving the problems that will be faced related to Income Tax and Bonus Mechanism affect the Income Shifting with Transfer Pricing Decision.