Does Audit Quality Reduce Tax Avoidance?

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ABSTRACT: This study aims to provide empirical evidence on the influence of thin capitalization, transfer pricing, and audit quality on tax avoidance. The dependent variable in this study is tax avoidance using Effective Tax Rate (ETR) proxies and dummy tax haven categories. Meanwhile, the independent variables in this study are thin capitalization with MAD ratio proxies and transfer pricing measured using related party receivables proxies. Furthermore, this study also uses a moderation variable, namely audit quality. Audit quality is measured using Big Four KAP proxies and dummy auditors industry specialization. This research uses a sample of 250 manufacturing company listed on the Indonesia Stock Exchange in 2018-2022. The results of this study show that transfer pricing affects tax avoidance, and audit quality can mitigate the influence of thin capitalization and transfer pricing affects tax avoidance.

KEYWORDS: Tax Avoidance, Thin Capitalization, Transfer Pricing, Audit Quality, and Auditor Industry Specialization.

I. INTRODUCTION

Taxes are one of the crucial sectors of state-owned revenue, with contributions to the state amounting to 74% to 80% of total state-owned revenue. The tax sector gets essential attention from the state and many other parties. In addition, taxes are one of the most important financial instruments contributing to national development, namely as a budget or supporting revenue for the state with an estimated large enough amount. The government makes taxes the mainstay of the source of funds used to mark the State Budget (APBN). Therefore, achieving the target tax revenue is quite crucial for the government. The following table shows the target and realization of the amount of tax the government has set for the last five years.

Year	2018	2019	2020	2021	2022
Target	1,618	1,786	1,404	1,444	1,783
Realization	1,518	1,546	1,285	1,547	2,034
Achievement (%)	93,86	86,55	91,50	107,15	114,05

Source: Processing data on Central Government Financial Statements (2018-2022)

The table above shows that the amount of realization of Indonesia's tax revenue target that has been set indirectly continues to increase. However, not significantly, and several times, it has yet reached the annual mark the Indonesian government set. Furthermore, the tax ratio in Indonesia is relatively stagnant in the range of 8% to 12%, namely from 2018 to 2022. The tax ratio itself is one of the benchmarks used to see and assess the ability of the government to manage state revenues, especially in the field of taxation. So, the greater the income derived from taxes, the greater the country's tax ratio rate.

Tax Justine Network (2020) reports that Indonesia has lost potential income from taxes with an amount of Rp. 68.7 trillion each year as a result of tax avoidance practices. The Ministry of Finance has targeted tax revenue of Rp. 1,198 T in 2020, but based on data from the Tax Justice Network shows that there is tax avoidance with an estimated 5.7% of the target. If this tax avoidance practice continues, it can cause losses to the state. In addition, based on data submitted by the Tax Justice Network, Indonesia ranks fourth in tax avoidance cases in Asia after China, India, and Japan. Taxes are one of the crucial sectors of state-owned revenue, with contributions to the state amounting to 74% to 80% of total state-owned revenue. The tax sector gets essential attention from the state and many other parties. In addition, taxes are one of the most important financial instruments contributing to national development, namely as a budget or supporting revenue for the state with an estimated large enough amount. The government makes taxes the mainstay of the source of funds used to mark the State Budget (APBN). Therefore, achieving the target tax revenue is quite crucial for the government. The following table shows the target and

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realization of the amount of tax the government has set for the last five years.

Tax avoidance practices often carried out are scenarios of transferring profits to countries included in the tax haven category (Indonesian Tax Forum, 2015). In addition to sharing profits, multinational companies use many techniques in several ways as a form of tax avoidance. One is thin capitalization (Buettner, Overesch, and Wamser, 2018), and the other is unreal transfer pricing (Hebous and Johannesen, 2021). They do it to reduce the burden on the company.

Kurniawan (2015) explained that thin capitalization is an abnormal comparison of the company's debt and capital structure. The practice formed a capital structure where the ratio of debt owned by the company is more significant when compared to the capital owned by the company. Some affiliated companies deliberately create this structure and tend to choose funding in the form of debt because the return from debt in the condition of interest can reduce the calculation of corporate tax. While returns derived from share capital cannot reduce tax calculations, they become attractive after-tax provisions that allow interest payments to reduce taxes, but dividends cannot.

A Tax Justice Network report revealed thin capitalization practices entitled Ashes to Ashes in 2019. The report revealed that British American Tobacco (BAT) allegedly carried out tax avoidance practices through its subsidiary, PT Bentoel Internasional Investama Tbk, with an intercompany loan scheme. In addition, Bentoel also received a loan from a Dutch company. The company accounts used to show that some of the funds provided as loans to Bentoel were funds originating from companies located in the tax haven, namely Britain and Jersey. The Tax Justice Network also alleges that Indonesia loses $11 million in revenue annually. In addition to thin capitalization carried out in tax avoidance practices, there is another practice that multinational companies usually carry out: transfer pricing. According to Members of the National Management Board of the Indonesian Accounting Association (IAI), the procedure was carried out by the company to minimize the tax burden to be paid. Applying this practice is done through transfer price engineering that can be done between divisions or companies..

The practice of transfer pricing only sometimes occurs abroad. In Indonesia itself, the method is rife by multinational companies. As previously revealed by an online journal in 2013, quoted from the statement of the then Minister of Finance Agus Martowardojo, transfer pricing practices often occur in Indonesia, and it is estimated that there have been more than 4000 companies, including multinational companies that have not made payments on taxes for the last seven years.

Furthermore, a report from Global Witness entitled "Taxing Times for Adaro" was released in 2019. The report explains that Adaro has transferred profits from the domestically mined coal sector to its Singapore-based subsidiary, Coaltrade Services International Company. In addition, the coal sold by Adaro to its subsidiaries is alleged to have been sold at a relatively lower price when compared to the current market price; then, they passed the coal to other countries with a nominally higher fee than the market price. So, the income received is more significant, but the tax burden to be paid in Indonesia will amount to less. Through this transfer pricing practice, Adaro is estimated to have reduced the total tax bill in Indonesia by almost USD 14 million per year.

Research on the effect of thin capitalization and transfer pricing on tax avoidance has been conducted by several researchers. Melina & Ferry Irawan (2022) showed that thin capitalization and transfer pricing affect tax avoidance. The same results were obtained from research conducted by Falbo & Firmansyah (2018) and Nadhifah & Arif (2020). In addition, other studies have found that thin capitalization influences tax avoidance, as conducted by Siti & Dewi (2019) and Madita &Ngadiman (2021). Research also shows that transfer pricing affects tax avoidance, as operated by Royanul & Ari (2019). In addition, according to Waddock, Bodwell, and Graves (2002), the government is one of the stakeholders of taxation, and stakeholders have certain rights, including the right to be respected, treated with integrity, protected by standards, given transparency to be given accountability. For stakeholders themselves, one way to maintain these rights is to utilize independent parties who function as external parties, namely external auditors. Auditing is more complex than between shareholders and the company but affects many interested parties. Just like regulators who expect audits to be able to ensure that companies comply with applicable laws and regulations, especially laws in the taxation department.

This study uses audit quality as a moderation variable to determine whether it can mitigate the tendency of companies in Indonesia to carry out tax avoidance practices. Previous research conducted by (Richardson, Lanis, and Taylor, 2013; Gaaya, Lakhal, and Lakhal, 2017) stated that audit quality could reduce tax avoidance practices. In addition, research by Alzoubi (2018) also explains that audit quality has a role in minimizing a company's profit management. However, research that considers audit quality in reducing the tendency of tax avoidance practices still needs to be improved. Gaaya et al. (2017) explained that audit quality could reduce the tendency of family companies to carry out tax avoidance practices. Previous research has also shown that some multinational companies have superior performance and have a tendency to carry out tax avoidance practices in their domicile companies. However, whether these conditions can later be mitigated by audit quality has yet to be answered in previous studies.

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II. THEORY AND METHODOLOGY

1. Agency Theory

Jensen & Meckling (1976) define agency theory as a cooperative relationship between principals (company owners) and agents (company managers). With the explanation, the company's owner delegates responsibility for decision-making and policy setting from the company to managers. Such separation can lead to agency conflicts. Agency theory has the concept of conflict of interest belonging to the principal and agent, where there is a cooperative relationship between the two parties, where each party has interrelated interests. The established relationship can occur when the company owner gives managers authority to run the company and make decisions. Furthermore, this causes a conflict of interest where the principal or owner is the party who has provided facilities and funds that managers will later use in carrying out various kinds of operational activities owned by the company and requires managers to take policies and act following the owner's wishes. However, on the other hand, this delegation of authority can lead to information asymmetry where a manager who is considered an agent can have more and broader knowledge and information compared to the company owner. Managers can then use this to act following their interests, namely manipulating the company's performance results to look good in the eyes of company owners so that they can get a good predicate. In manipulating company performance results, managers strive to maximize the profits obtained by carrying out various types of tax avoidance practices. The company can do this by planning tax; the manager can minimize the tax it will pay to the government by reducing its profits. Using this method is considered mutually beneficial for the principal and agent, where, in this way, they can achieve all the importance respectively.

2. Cost and Benefit Theory

Dreeze & Stren (1987) explain the purpose of cost and benefit analysis is to examine decisions related to consequences and profits used by firms. Tax avoidance transfers wealth from the government to shareholders (Francis et al., 2013). This method is the same as with other types of investors in multinational companies with foreign shareholders who want a high return on their investment (Vo, 2016). Investors with a high proportion of shares can enjoy more significant benefits that have been obtained from tax avoidance decisions, so that they are more motivated to interfere with managers' decisions related to taxation (Jiang, Zheng, and Wang, 2020). In addition, other risks they will face are the benefits obtained from tax avoidance practices (Vo, 2016). Long-term tax avoidance practices can lead to direct costs and indirect costs. This situation causes the majority shareholders to also pay more attention to the costs that will be incurred as a result of tax avoidance practices carried out by the company.

3. Methodology

This study used a population from companies in the manufacturing sector listed on the Indonesia Stock Exchange (IDX) from 2018 to 2022. In addition, the sampling method used in this study was purposive sampling. The following are the criteria that become the benchmark for sampling :

1. Manufacturing companies listed on the Indonesia Stock Exchange from 2018 to 2022.
2. Have published audited annual financial statements on the www.idx.com website
3. No losses according to commercial and fiscal financial reports from 2018 to 2022.
4. Manufacturing companies have related party receivables in the reporting year 2018 to 2022.

4. Operational Definition of Variables

The dependent variable is a variable that is the primary concern for every researcher, so the primary goal of researchers is to understand and explain these variables (Sekaran & Bougie, 2017). The dependent variable in this study is tax avoidance. Referring to Taylor & Richardson's (2013) research with several categories that have been adjusted, tax avoidance is also measured using ETR, referring to Taylor and Richardson (2013) with the following formula :

Effective Tax Rate $= $ Income tax expense / Profit before tax

The measurement of thin capitalization refers to Taylor & Richardson's (2013) research using the MAD Ratio. Calculating the amount of safe harbor debt amount (SHDA) by averaging total assets deducted by non-interest bearing liability (non-IBL) and multiplied by 80% and then calculating the maximum allowable debt (MAD) ratio by averaging total debt divided by SHDA.

$$SHDA = (\text{Average Total Asset} - \text{Non IBL}) \times 80\% \quad MAD\ Ratio = \text{Average Debt} / SHDA$$

Transfer pricing measurement in this study refers to research conducted by Tiwa et al. (2017) using proxy-related party transactions. This proxy aims to calculate company receivables derived from the value of sales transactions, which can simultaneously affect the company's profit assessment and reduce the obligation to make tax payments. The result of this measurement is that the greater the number obtained from the calculation, the greater the transfer pricing practice.

Transfer pricing $= $ Related Party Accounts Receivable / Total Assets

In this study, the moderation variable used was audit quality. Audit quality measurement refers to research conducted by Gaaya et al. (2017), namely by giving a score of 1 for companies audited by Big 4 Public Accountants and giving the opposite a score of 0. The following are local KAPs affiliated with Big 4 Public Accountants :

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1) KAP Purwanto, Sarwoko, and Sandraja affiliated with KAP Ernst and Young (E & Y)
2) KAP Tanudireja, Wibisana & Partners affiliated with KAP Pricewaterhouse Coopers (PwC)
3) KAP Osman Bing Satrio and Eny affiliated with KAP Deloitte Touche Thomatsu (DTT)
4) KAP Siddharta & Widjaja affiliated with KAP Klynveld Peat Marwick Goerdeler (KPMG)

In addition, other proxies are used in measuring audit quality, namely by using industry auditor specialization proxies. With the following calculation:

Auditor Industry Specialization = Total company asset / Total asset industry

Next, companies with a percentage of 30% or more will be given a value of 1, while a value of 0 for vice versa.

Based on previous studies, the control variables used in this study include company size, profitability ratio, solvency ratio, and government ownership. Company size is measured by the natural logarithm (ln) of the company's assets based on previous research that found an influence between company size and tax avoidance. Furthermore, the profitability ratio (ROA) is measured by calculating the amount of profit after tax divided by the number of company assets by previous research that found an influence between ROA and tax avoidance (Taylor & Richardson, 2012 & Gaaya et al. (2017). The solvency ratio (leverage) is calculated by the number of long-term liabilities (non-current liabilities) divided by the number of assets based on previous research that found an influence between leverage and tax avoidance (Taylor & Richardson, 2012 & Gaaya et al. (2017).Foreign ownership (fown) is measured by a dummy variable, namely the value of 1 if foreign investors own the company with a proportion exceeding 20%, and 0 for vice versa. The presentation of the significance of this study follows PSAK 15, which explains that investors are considered to have a significant influence on a company if they have 20% or more voting rights.

III. RESULT AND DISCUSSION

1. Descriptive Statistic

Descriptive statistics is the first step of a statistical process that will be used to describe data that has been collected, such as data centers, data distribution, and forms of data distribution (Cooper and Schindler, 2014).

Manufacturing companies listed on IDX	**165**
Manufacturing companies listed on IDX in the year of observation.	(44)
Companies that publish audited annual financial statements.	(4)
Companies that did not incur losses according to the fiscal financial statements in the year of observation	(49)
Companies that have related party receivables in the year of observation.	(18)
Number of companies meeting criteria (n)	50
Number of observation periods (i)	5
Final number of research samples (n x i)	250

Source: data processing result (2023)

Variables	Average	Standar Deviation	Minimum Score	Maximum Score
ETR	0,2466	0,1004	0,0097	0,8374
Thin Cap	0,4400	0,2342	0.0487	1,1802
Trans Pric	0,0441	0,0752	0,0051	0,3787
KA	0,4440	0,4978	0,0000	1,0000
Size	21,9864	5,6408	12,7314	30,9357
RoA	0,0960	0,0994	0,0005	0.9571
Leverage	0,1238	0,1115	0.0005	0.5403
Fown	0,2800	0,4499	0,0000	1,0000

ETR : Tax Avoidance, Thin Cap : Thin Capitalization, Trans Pric : Transfer Pricing, KA : Audit Quality. Size : Ln Asset. RoA : Profitability Ratio, Leverage : Solvency Ratio, Fown : Foreign Ownership.
**Source:** Data processing results (2023)

The results of the descriptive statistics above show that the average tax avoidance using ETR proxies is 24.66%. This percentage is below the corporate income tax rate applicable in Indonesia, which is 25%, which has been determined since 2010. This percentage can also be influenced by tax audits conducted by DGT and obtaining an Underpayment Tax Assessment Letter (SKPKB) for Income Tax or Overpaid Tax Assessment Letter (SKPLB). SKPKB can cause the amount of tax paid to increase, while SKPLB can reduce the amount of tax paid. An example is what happened to PT Hanjaya Mandala Sampoerna in 2018, who received a refund for a tax overpayment so that the amount of tax paid was reduced.

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Next is thin capitalization, which ranges from 4.8% to 118%. PT Tembaga Mulia Semanan, Tbk, has the highest level of thin capitalization. At the same time, PT Industri Jamu & Farmasi Sido Muncul Tbk has the lowest level of thin capitalization. Then, the average owned by the thin capitalization variable is 44%, with a standard deviation of 23%. Then, for variable transfer pricing has a level that ranges from 5.1% to 37.87%. The highest level, with a percentage of 37.87%, belongs to PT Wilmar Cahaya Indonesia, Tbk. At the same time, the lowest level is owned by PT Indospring, Tbk, with a percentage of 5.1%. This is also accompanied by the average value for the variable of 4.41% and the standard deviation of 7.52%.

The size of the manufacturing company has an average asset of Rp. 2,198,640 billion. The company's profitability has a percentage value ranging from 0.05% to 95.71%. Furthermore, the percentage value of solvency ranges from 0.05% to 54.03%. Again, based on the figure below, 44% of the companies sampled in this study have been audited by external auditors from the Big 4 Public Accountants. Besides that, it can also be seen that foreign investors own 28% of the companies sampled in this study.
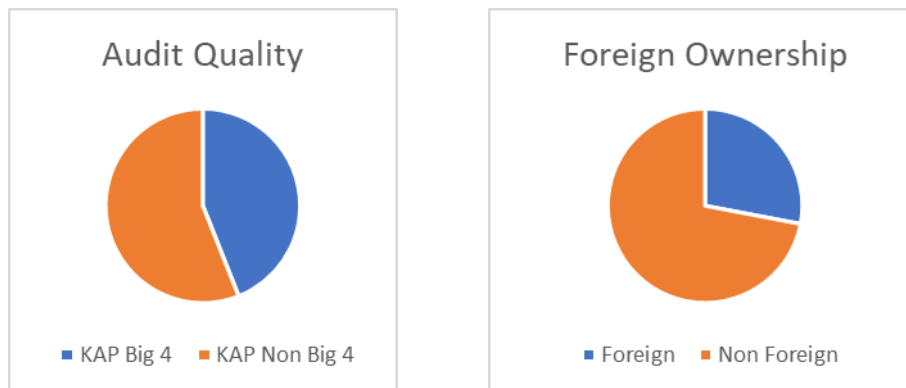
1.1 Classical Assumption Test

The classic assumption test in this study consists of normality, multicollinearity, heteroskedasticity, and autocorrelation tests. This classical assumption test was carried out on research model 1 with the specification of additional analysis with proxy changes in moderation variables.

1.1.1 Normality Test

Model	JB Score	Probability	Result	Conclusion
1a	1513,29	0,000	α > probability	Regression equations are not normally distributed
1b	1534,59	0,000	α > probability	Regression equations are not normally distributed

Source: data processing result (2023)

The normality test in this study was tested using the Jarque-Bera (JB) test. Based on the test results in the table above, the resulting probability level is below the specified alpha. Thus, the regression equation in this model is not normally distributed. Furthermore, the procedure performed for normality problems in this study is to use robustness regression estimation S and MM to test H1 and H2, as suggested by Leone, Minutti-Meza, and Wasley (2019).

1.1.2 Multicolinearity Test

Variabel	VIF	Result	Conclusion
Model (1a)			
TC	2,89	VIF < 10	No multicholinerity
TP	2,10	VIF < 10	No multicholinerity
KA	5,30	VIF < 10	No multicholinerity
SIZE	1,20	VIF < 10	No multicholinerity
ROA	1,21	VIF < 10	No multicholinerity
LEV	1,55	VIF < 10	No multicholinerity
FOWN	1,46	VIF < 10	No multicholinerity
Model (1b)			
TC	1,64	VIF < 10	No multicholinerity
TP	1,34	VIF < 10	No multicholinerity
SA	6,29	VIF < 10	No multicholinerity
SIZE	1,29	VIF < 10	No multicholinerity

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ROA	1,14	VIF < 10	No multicholinerity
LEV	1,62	VIF < 10	No multicholinerity
FOWN	1,32	VIF < 10	No multicholinerity

Source: data processing result (2023)

This study identified mutcholinearity using the variance inflation factor (VIF). Based on the table above, the highest VIF value is owned by the audit quality variable using an industry auditor specialization proxy of 6.29. Overall, all independent variables have a VIF value of less than 10, so it can be concluded that there is no multicollinearity between independent variables.

1.1.3 Heterokesdasticity Test

Model	BP Score	Probability	Result	Conclusion
1a	17,55	0,040	α > probability	There is heterokedasticity
1b	10,44	0,315	α < probability	No heterokedasticity

Source: data processing result (2023)

Next is the heteroskedasticity test, which is detected using the Breusch-Pagan (BP) test. Based on the test results in research models (1a) and (1b), it can be concluded that research model 1a has a probability level below the predetermined alpha so that heteroskedasticity is tightened. As for the research model, 1b has a higher probability level than the predetermined alpha, so there is no heteroskedasticity.

1.1.4 Autocorrelation Test

Model	BG Score	Probability	Result	Conclusion
1a	29,40	0,000	α > probability	There is autocorrelation
1b	21,37	0,000	α > probability	There is autocorrelation

Source: data processing result (2023)

The autocorrelation test in this study was detected using the Breusch-Godfrey (BG) method. Based on the results of autocorrelation tests on research models 1a and 1b presented in the table above, the probability level of the two models is below the predetermined alpha. Thus, there is an autocorrelation in the regression model of the study.

1.2 Robustness Regression

Hypothesis testing in models 1, 1a, and 1b should use the one least square regression method. However, based on the test results, the classical assumption of regression must be replaced with a robustness regression model. This is due to the results of the classical assumption test, which states that the model is not normally distributed, and there has been heteroskedasticity and autocorrelation. In model 1, the dependent variable tax avoidance is measured using the Effective Tax Rate proxy. The independent variables in this study are thin capitalization and transfer pricing. Thin capitalization is calculated using the MAD Ratio proxy, and transfer pricing is measured using the related receivables proxy. Furthermore, the moderation variable, audit quality, is computed using two representatives. This audit quality proxy distinguishes research models 1a and 1b, wherein in research model 1a, audit quality variables use four significant representatives; in research model 1b, dummy proxies specializing in industry auditors are used.

1.2.1 Test on model 1a

Variables	Prediction	Coef	Probability
Dependent Variables = *TA*			
TC	+	-0,002	0.875
TP	+	-0,087	0,079
TC x KA	+	0,022	0,081
TP x KA	+	0,067	0,335
SIZE		1,688	0,001
ROA	-0,005		0,839
LEV	0,060		0,031
FOWN	0,010		0,120

Source: data processing result (2023)

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Based on the table above, the TP coefficient shows a value of -0.087 with a smaller probability level when compared to the predetermined significance level of 10% (p = 0.079, α = 0.1). The result shows that transfer pricing affects tax avoidance. Furthermore, the variable coefficient TC x KA shows a value of 0.022 with a smaller level of probability when compared to the predetermined significance level, which is 10% (p = 0.081, α = 0.1). It means that external auditors from Big 4 Public Accountants can reduce the tendency of transfer pricing on tax avoidance.

Control variables that affect tax avoidance are Size and Leverage. The company's size (Size) has a probability level lower than the predetermined alpha of 5% (p = 0.001, α = 0.005). It means that the larger the company, the less likely it is to engage in risky tax avoidance practices. In addition, the ratio of liabilities (leverage) also has a lower probability when compared to a predetermined alpha of 10% (p = 0.031, α = 0.1).

1.2.2 Test on 1b model

Variables	Prediction	Coef	Probability
Dependent Variables = *TA*			
TC	+	0,010	0,410
TP	+	-0,058	0,137
TC x SA	+	-0,049	0,004
TP x SA	+	0,231	0,031
SIZE		1,211	0,016
ROA		0,002	0,934
LEV		0,079	0,006
FOWN		0,017	0,007

Source: data processing result (2023)

Based on the table above, the TC x SA coefficient has a value of -2.82 with a smaller probability level when compared to the predetermined significance level of 5% (p = 0.004, α = 0.005). This shows that external auditors who have special industry specialization are able to mitigate the effect of thin capitalization on tax avoidance. Furthermore, the TP x SA coefficient has a value of 2.14 with a smaller level of probability when compared to the predetermined significance value of 10% (p = 0.031, α = 0.1).Control variables that affect tax avoidance in this research model are Size, Leverage, and Fown. The company's size has a lower probability value when compared to a predetermined significance value (p = 0.016, α = 0.1). Then solvency ratios and foreign ownership also get similar values, namely lower probability values when compared to predetermined significance values (Lev p = 0.006, α = 0.1; Fown p = 0.007, α = 0.1).

1.3 Logit Logistic Regression

The study also used additional analyses assumed through model 2. In this model 2, a proxy change is used for the dependent variable, namely by using a dummy derived from a category included in the list of tax haven countries (www.cncb.com). Countries included in the list of tax havens in this study are Panama Islands, South Dakota, Florida, Delaware, Texas, Nevada, British Virgin Islands, Chanel Islands, Jersey Islands, Guernsey, Isle of Man, Cayman, Bermuda, Virgin England Islands, Turks, Caicos, Gibraltar, Hongkong, Singapore, Bahama Islands, Bahrain, Dubai, Benelux Belgium, Netherlands, Luxembourg, Ireland, Switzerland, Liechtenstein. Test the hypothesis in this model using logistic logit regression. The results ofprocessing regression data are presented in the following table :

1.3.1 Test on 2a model

Variables	Prediction	Coef	Probability
Dependent Variables = *TA*			
TC	+	2,361	0,101
TP	+	8,068	0,004
TC x KA	+	-6,018	0,001
TP x KA	+	-11,638	0,049
SIZE		4,799	0,882
ROA		2,770	0,160
LEV		8,813	0,000
FOWN		0,852	0,062

Source: data processing result (2023)

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Based on the table above, the coefficient value for the transfer pricing variable shows a value of 8.068 with a probability level more minor than the predetermined significance level of 5% (p = 0.004, α = 0.05). So, it can be concluded that transfer pricing affects tax avoidance. Furthermore, the value of the coefficient for TC x KA shows a value of -6.018 with a smaller level of probability when compared to the predetermined significance level of 5% (p = 0.001, α = 0.05). It shows that audit quality can mitigate the effect of transfer pricing on tax avoidance. Furthermore, the control variables are influential in this research model are leverage and fown variables. The ratio of solvency and foreign ownership has a lower probability value when compared to the significance level predetermined for this regression model (Lev p = 0.000, α = 0.05; Fown p = 0.062, α = 0.1).

1.3.2   Test on 2b model

Variables	Prediction	Coef	Probability
Dependent Variables = *TA*			
TC	+	-0,741	0,476
TP	+	5,222	0,026
TC x SA	+	1,365	0,474
TP x SA	+	-1,522	0,789
SIZE		3,411	0,350
ROA		0,715	0,668
LEV		7,103	0,000
FOWN	0,449		0,304

Source: data processing result (2023)

Based on the table above, the coefficient value for the transfer pricing variable is 5.22, accompanied by a smaller probability value when compared to the predetermined significance value of 10% (p = 0.026, α = 0.1). It shows that transfer pricing has a positive effect on tax avoidance. Furthermore, the leverage control variable has a coefficient value of 7.103 with a smaller probability value when compared to the predetermined significance value of 5% (p = 0.000, α = 0.05).

1.3.3   Goodness Fit Model

The test is carried out to assess whether the model used in the study can be categorized as good or not. The following are the results of the model feasibility test (goodness fit model) for research models 2a and 2b :

Model	H-L Statistic	Prob Chi Square
2a	8,918	0,349
2b	10,438	0,235

Source: data processing result (2023)

The table above shows the results of the model feasibility test for model 2a, which has a probability value of 0.349, which exceeds the predetermined significant value of 0.05. This is also the case for model 2b, where the resulting probability value is 0.235, which exceeds the predetermined considerable value. From these results, the two models used in this study are appropriate and feasible to explain the relationship of variables in this study.

IV. CONCLUSION

A. *Thin capitalization* and *tax avoidance*

The results of testing H1 with ETR as the dependent variable are presented in the table above. The probability level in the variable TC or thin capitalization is 0.875. The value is more significant when compared to the predetermined significance level of 10% (p = 0.875, α = 0.1). This result is also supported by the test results in model 2, where the dependent variable proxy is converted into a dummy tax haven category in the model. The probability value generated with the model is 0.410. The results were also more significant when compared to predetermined significance levels (p = 0.410, α = 0.1). From these results, it can be concluded that thin capitalization does not affect tax avoidance. This study's results align with research conducted by Nirmalasari & Endah (2021) and Moeljono (2020). This can happen because companies in the manufacturing sector do not use the funding structure that originates and is dominated by the use of debt that exceeds the provisions of the laws and regulations in Indonesia. The use of debt by the company is assumed to be more widely used for the company's operational activities. Thus, H1 in this study was not empirically supported, or H1 was rejected.

B. *Transfer pricing* and *tax avoidance*

The results of testing H2 with ETR as the dependent variable are presented in the table above. The probability value generated in

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the hypothesis test against model 1 is 0.079. The deal is smaller than the significance value of 10% (p = 0.079, α = 0.10). This result is also supported by the test results on research models 2a and 2b, with probability values of 0.004 and 0.026. The result is smaller when compared to the predetermined significance value of 5% (p = 0.004 & 0.026, α = 0.05). The results of this study are in line with Taylor and Richardson (2012), Dharmawan et al. (2017) and Annisa & Dudi (2018). This is due to the special relationship between related parties. The existence of this special relationship is used to make transactions that do not follow fairness to minimize the tax burden owned by the company. Thus, it can be concluded that unique relationships used unreasonably by related parties can open up opportunities for companies to carry out tax avoidance practices and maximize profits that the company can obtain. Thus, H2 in this study is empirically supported, or H2 is accepted.

C. *Thin capitalization,* audit quality, and *tax avoidance*

The results of H3 testing with research model 1, namely using ETR dependent variables and using big four proxy for the moderation variables and auditor industry specification, have probability values of 0.081 and 0.004. The value is smaller when compared to the previously determined significant values of 10% and 5% (p = 0.081, α = 0.1; p = 0.004, α = 0.05). This is also Supported by the test results in model 2 with the dependent variable dummy tax haven and the audit quality moderation variable, with a probability value 0.001. The value is also smaller when compared to the predetermined significant value of 5% (p = 0.001, α = 0.05). The results of this study show that audit quality moderation variables, both using Big Four proxies and auditor industry specialization are equally able to mitigate the relationship or effect of thin capitalization on tax avoidance. Indirectly, this is in line with research conducted by Gaaya et al. (2017), which states that external auditors can mitigate tax avoidance practices. This condition shows that companies with external auditors who come from the big four KAP and have special specialization and experience in the industry, primarily through thin capitalization practices, have the opportunity to do less tax avoidance. Thus, H3 in this study is empirically supported, or H3 is accepted.

D. *Transfer pricing,* audit quality, and *tax avoidance*

The results of H4 testing in research models 1 and 2 are the same. In research model 1, with the dependent variable ETR and moderation variable using industry-specialization proxies, the auditor showed a probability value of 0.031. The value is smaller when compared to the predetermined significance value of 10% (p = 0.031, α = 0.1). This aligns with the hypothesis test results in research model 2 with the dependent variable dummy tax haven and moderation variable using audit quality proxies. The results in model 2 show a probability value of 0.049. The value is smaller when compared to the predetermined significant value of 10% (p = 0.049, α = 0.1). The results of this study show that audit quality, both using Big Four proxies and auditor industry specialization, can mitigate the relationship or effect of transfer pricing on tax avoidance. In addition, this is also indirectly in line with research conducted by Gaaya et al. (2017), which states that audit quality can mitigate tax avoidance. This condition shows that companies with external auditors who come from the big four public accountants and have special specialization and experience in the industry, primarily through thin transfer pricing practices, have the opportunity to do less tax avoidance. Thus, H4 in this study is empirically supported, or H4 is accepted.

E. *Size, RoA, Leverage,* and *Fown*

In addition to examining the influence of independent and moderation variables on dependent variables, this study also examined the effect of control variables, namely company size, profitability ratio, solvency ratio, and foreign ownership, on both ETR proxies and dummy tax haven categories. Each of these tests shows that the solvency ratio, which in this case uses leverage proxies, is the most consistent control variable, showing its effect on tax avoidance. This condition indicates that companies with high debt levels tend to be tax-avoidant. It is assumed that the greater the debt burden and interest to be paid by the company, the more taxable income will be reduced.

V. LIMITATIONS

In the implementation of this study, several things could be improved. One of them is the relatively small and limited number of samples and the sample area that only uses companies located in Indonesia. This is because the criteria determined are strict. In addition, the proxies of some variables used in this study still need to be updated, and old references tend to be used. Therefore, researchers hope that future studies can use better and more diverse variable calculation proxies and use samples from various countries.

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