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Original Research Article

Exploring the Opportunities for Tax Avoidance Through the Thin Capitalization, Transfer Pricing, and Foreign Ownership

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Abstract

This study examines the implications of Thin Capitalization, Transfer Pricing, and Foreign Ownership on Tax Avoidance within LQ45 companies during the period from 2019 to 2023. A purposive sampling method was employed to obtain a sample of 180 observations from a total of 225 companies. Panel data regression analysis was conducted utilizing Stata 18. The results indicate that Thin Capitalization exerts a negative influence on Tax Avoidance, whereas Transfer Pricing demonstrates a positive effect. Additionally, Foreign Ownership was found to have no significant impact on Tax Avoidance. This study offers a new insight into tax avoidance among Indonesian companies, highlighting how the corporate governance structure can influence tax strategies. It finds that the thin capitalization strategy and transfer pricing of a company are more influenced by management factors than by the structure of its shareholders. Investors should focus on the transparency of company tax policies, as managerial decisions have a greater impact on tax avoidance than ownership structure. Meanwhile, stricter oversight and clearer regulations are needed to prevent tax avoidance and profit shifting.

Keywords: Tax Avoidance, Thin Capitalization, Transfer Pricing, Foreign Ownership.

1. INTRODUCTION

Indonesia, as a developing country in Asia, relies on taxes as state revenue to finance the State Budget, which continues to increase every year. In 2023, the realization of tax revenue reached IDR1,916.34 trillion (94.81% of the target) with a growth of 3.64% (yoy). However, Indonesia's tax ratio to GDP was only 10.9% in 2021, down 1.4 points from 2007 to 2021, lower than the Asia-Pacific average of 19.8%, and the lowest in the region. This condition shows a significant challenge for the government in optimizing tax revenue for the State Budget.

Indonesia also faces global tax losses due to tax avoidance, with losses reaching $4.86 billion in 2020, mostly caused by multinational companies through transfer pricing schemes and inter-group loans. The OECD (2022) report shows that tax avoidance cases in Indonesia have been quite high and fluctuating in recent years, with many cases involving transactions between affiliated companies.

A tax avoidance case that has occurred in Indonesia is the case carried out by PT. Bentoel Internasional Investama, a subsidiary of British American Tobacco Ltd (UK). Bentoel diverted part of its income abroad through two main schemes, namely intra-company loans made in 2013-2015 and payments of royalties and other fees to affiliated companies in the UK. This scheme allowed the company to significantly reduce its taxable income and increase its pre-tax losses.

Thin capitalization, namely the excessive use of debt in a company's capital structure, is often used as a tax avoidance strategy because interest on debt can be deducted from fiscal profit, unlike dividends. Research conducted by Tarmizi *et al.,* (2023), Amni *et al.,* (2023), and Waluyo & Doktoralina (2018) on tax avoidance states that the practice of thin capitalization affects tax avoidance. Meanwhile, research conducted by Kundelis *et al.,* (2022), Tandayu *et al.,* (2023), and Rini *et al.,* (2022) found that thin capitalization practices did not affect tax avoidance.

Transfer pricing, which is a transaction price scheme set between companies in a group in different tax jurisdictions, is also a means of tax avoidance. Multinational companies use transfer pricing schemes to shift profits from high-tax countries to low-tax countries, thereby reducing their overall tax liabilities. Research conducted by Wier (2020), Beebeejaun (2019), and Herianti & Chairina, (2019) on transfer pricing states that transfer pricing practices affect tax avoidance. Meanwhile, research conducted by Wiharja & Sutandi (2023), Supriyanto *et al.,* (2022), and Khamisan & Astuti (2023) states that transfer pricing practices do not affect tax avoidance.

Foreign ownership is considered an important factor in tax decision making in companies, because foreign owners often put pressure on management to maximize profits through various strategies including tax avoidance. Research conducted by Suranta *et al.,* (2020), Alkurdi & Mardini (2020) and Syukur & Jongsureyapart (2023) stated that foreign ownership has a positive effect on tax avoidance, which means that the greater the foreign ownership, the greater the potential for tax avoidance. Meanwhile, research conducted by Hasan *et al.,* (2022), Zagler (2023), and Amendolagine *et al.,* (2021) stated that foreign ownership does not affect tax avoidance practices.

Seeing this phenomenon, research was conducted to re-examine the effect of thin capitalization, transfer pricing, and foreign ownership on tax avoidance among LQ45 Companies during the period 2019-2023. It aims to address gaps in previous research by simultaneously analyzing these three factors in the context of LQ45 companies listed on the Indonesia Stock Exchange. The selection of LQ45 companies as research objects is based on their representation in the Indonesian capital market with large capitalization, high liquidity, and significant roles in contributing to state tax revenues. With this analysis, this study is expected to provide additional insights to the government in formulating tax regulations and for companies in managing tax strategies responsibly.

2. LITERATURE REVIEW

2.1. Agency Theory

Agency theory, as defined by Jensen and Meckling (1976), describes an agency relationship in which one or more individuals (the principals) hire another person (the agent) to perform a service or task on their behalf. This arrangement involves granting the agent decision-making authority. According to the literature, the relationship between agency theory and tax avoidance can be understood as follows: management is responsible for maintaining the company's financial performance while ensuring that shareholders receive benefits, primarily in the form of dividends. At the same time, managers must comply with government and tax regulations. Therefore, management needs to develop strategies and policies that balance these two different interests. From the perspective of management as an agent, it is reasonable to assume that they may engage in aggressive tax planning to help maximize shareholder wealth (Ullah *et al.,* 2021). Management has significant flexibility in implementing such strategies, which can influence how both principals and agents assess the company's performance and can lead to higher incentives, such as increased salaries and bonuses (Putri *et al.,* 2024).

2.2. Theory Planned Behaviours

The Theory of Planned Behavior, developed by Ajzen in 1991, posits that an individual's behavior or intention to act is influenced by their attitudes toward the behavior, subjective norms, and perceived behavioral control (Bensley & Fisher, 2003:8). The behavior of management in seeking to maximize shareholder interests is shaped by these three components.

2.3. Thin Capitalizations and Tax Avoidance

Thin Capitalization is a situation where a company's equity is financed with a relatively high level of debt compared to equity (OECD, 2019:1764) is often used as a tax avoidance strategy because interest on debt can be deducted from fiscal profit, unlike dividends. Multinational companies can structure their financing to maximize benefits, creating a tax-efficient mix of debt and equity while influencing the tax treatment of interest payments (OECD, 2012:3). The agency relationship in tax avoidance involves management balancing financial performance and shareholder benefits while complying with tax laws. Therefore, they must manage the debt-to-equity ratio effectively to maximize deductible costs and adhere to thin capitalization regulations. Management's belief that thin capitalization reduces tax burdens and enhances shareholder wealth, along with industry norms favoring debt financing and their ability to exploit tax loopholes, shapes their approach to tax avoidance. Research conducted by Tarmizi *et al.,* (2023), Amni *et al.,* (2023), and Waluyo & Doktoralina (2018) on tax avoidance states that the practice of thin capitalization affects tax avoidance. Meanwhile, research conducted by Kundelis *et al.,* (2022), Tandayu *et al.,* (2023), and Rini *et al.,* (2022) found that thin capitalization practices did not affect tax avoidance.

***H_1* : Thin Capitalization Has a Positive Effect on Tax Avoidance.**

2.4. Transfer Pricing and Tax Avoidance

Transfer pricing in taxation refers to the pricing policy used in transactions between related parties to determine profit distribution among entities (Darusalam *et al.,* 2022:9) is often used by multinational companies to minimize their tax burden by shifting profits from high-tax to low-tax jurisdictions. This practice can distort tax responsibilities and revenues if it doesn't reflect market conditions (OECD, 2022:30). According to agency theory, management (the agent) employs transfer pricing strategies to meet shareholder (the principal) expectations and optimize profits. Shareholders pressure management to take advantage of varying tax rates, encouraging profit shifting to lower-tax areas. This enhances reported net income and addresses competitive investment returns. Management aims to boost shareholder wealth by exploiting tax rate differences, a practice supported by industry norms. As other companies engage in similar strategies without consequences, management views this as acceptable. Moreover, the ability to find and exploit tax regulation loopholes influences management's approach to tax avoidance. Research conducted by Wier (2020), Beebeejaun (2019), Maulana *et al.,* (2018) and Herianti & Chairina, (2019) on transfer pricing states that transfer pricing practices affect tax avoidance. Meanwhile, research conducted by Wiharja & Sutandi (2023), Supriyanto *et al.,* (2022), and Khamisan & Astuti (2023) states that transfer pricing practices do not affect tax avoidance.

H_2 : Transfer Pricing Has a Positive Effect on Tax Avoidance.

2.5. Foreign Ownership and Tax Avoidance

Foreign ownership refers to the percentage of shares held by foreign investors in a company (Suranta *et al.,* 2020). Foreign ownership is considered an important factor in tax decision making in companies, because foreign owners often put pressure on management to maximize profits through various strategies including tax avoidance. Tax avoidance can manifest in any company, particularly multinationals. When ownership is primarily foreign, there is a tendency for increased tax avoidance. Research indicates that foreign ownership influences tax strategies through strengthened corporate governance. Foreign shareholders typically press management to maximize profits, which can lead to more aggressive tax management (Ullah *et al.,* 2021). The theory of planned behavior illustrates that foreign investors expect management to optimize financial efficiency, including tax management (belief). This expectation aligns with external stakeholders' norms, such as regulators, who advocate for tax efficiency as part of sound financial management (subjective norm). The expertise of foreign investors in global tax structures can empower management to adopt tax avoidance strategies with minimal perceived risk (perceived behavioral control). Research conducted by Suranta *et al.,* (2020), Alkurdi & Mardini (2020), Putri *et al.,* (2024) and Syukur & Jongsureyapart (2023) stated that foreign ownership has a positive effect on tax avoidance, which means that the greater the foreign ownership, the greater the potential for tax avoidance. Meanwhile, research conducted by Hasan *et al.,* (2022), Zagler (2023), and Amendolagine *et al.,* (2021) stated that foreign ownership does not affect tax avoidance practices.

H_3 : Foreign Ownership Has a Positive Effect on Tax Avoidance.

3. RESEARCH METHOD

This study uses a causal approach with a population of 45 companies included in the LQ45 index category on the Indonesia Stock Exchange (IDX) for the 2019–2023 period. The research sample consists of 180 observations obtained from LQ45 companies during that period. The sample selection was based on the consideration that companies in the LQ45 index have large market capitalization and high liquidity levels, as well as significant international exposure, so they are more likely to be exposed to the risk of Thin Capitalization and Transfer Pricing practices. In addition, these companies have a large contribution to state tax revenues, and analyzing their tax strategies is relevant to the formulation of national tax policies. The purposive sampling technique was used to determine the sample based on specific criteria previously determined by the researcher. All variables in this study are summarized and processed using specific indicators to present values on a predetermined scale.

3.1. Tax Avoidance

This study operationalizes the tax rate according to the income tax law (Statutory rate of tax) minus the effective tax rate (Effective Tax Rate) borne by the company (Effective Tax Rate). This measurement was chosen because the higher the difference between the ETR and STR values indicates the greater the level of tax avoidance carried out (Thomsen & Watrin, 2018).

$TA = STR - ETR$

3.2. Thin Calitalization

This study measures thin capitalization using the MAD Ratio or Maximum Amount Debt Ratio proxy. The MAD Ratio is calculated by calculating the safe harbor debt amount (SHDA) and then calculating the maximum allowable debt (MAD) ratio by dividing the average total debt by SHDA (Utami & Irawan, 2022).

$MAD\ Ratio = Average\ Debt / SHDA$

$SHDA = (Average\ Total\ Assets – Non\ IBL) \times 80\%$

3.3. Transfer Pricing

This study measures transfer pricing using 5 item indices developed from three transfer pricing measurement factors as a proxy for measuring transfer pricing (Amidu *et al.,* 2019).

1) Having a subsidiary or company in a group domiciled in a jurisdiction with tax haven characteristics.
2) Carrying out financial transactions with a subsidiary or company in a group located in a tax haven jurisdiction in a certain fiscal year.
3) Having a parent company, subsidiary, or member of a business group operating in another country that has different tax rates, other than a tax haven jurisdiction.
4) Conducting transactions with affiliates located in countries that apply different tax rates in the observed period; and
5) Making royalty payments for the use of intangible assets to related parties in the relevant fiscal year.

Each indicator is given a score of 1 if met and a score of 0 if not met. The company's transfer pricing index is calculated by adding the five indicators, then dividing the result by five. A maximum score of five reflects a higher level of transfer pricing practices, while a score of zero indicates that the company does not manipulate transfer prices.

3.4. Foreign Ownership

This study measures foreign ownership using the formula of the number of foreign shares owned by foreign investors divided by the total number of shares outstanding (Solihin & Utami, 2022).

FO = Foreign Ownership / Total Shares

4. RESULTS AND DISCUSSION

4.1. Descriptive Statistics

Table 1: Descriptive Statistics

Variables	Mean	Maximum	Minimum	Std. Dev.	Observations
TA	0,00755	0,24055	-0,28889	0,07411	180
MAD	0,64493	1,71689	0,02216	0,37975	180
TP	0,49222	1,00000	0,20000	0,24687	180
FO	0,38688	0,95372	0,00580	0,28622	180

Referring to Table 1 of the statistical results, the minimum value of the tax avoidance variable indicates that some companies employ aggressive strategies to minimize their tax obligations. In contrast, the maximum value suggests the presence of companies that face a relatively high tax burden. The average (mean) tax avoidance value of 0.07% shows that, in general, LQ45 companies engage in tax avoidance practices to a moderate extent. This level of tax avoidance may be attributed to the stricter tax supervision imposed by regulators on these companies. Next, a model selection test is conducted to identify the most appropriate model for the analysis.

4.2. Model Selection Test

Table 2: Model Selection

Test Summary	Decision	Result	Best Model
Chow Test	Prob > F	0,7512	CEM
Hausman	Prob < Chi2	0,8647	REM
Lagrange Multiplier	Prob > Chi2	0,0561	CEM

Based on the results of the Chow test presented in Table 2, the Common Effect Model is determined to be more suitable than the Fixed Effect Model. Furthermore, the Hausman test results indicate that the Random Effect Model is preferable to the Fixed Effect Model. The LM test suggests that the Common Effect Model is also more appropriate than the Random Effect Model. Therefore, the best model for this study is the Common Effect Model (CEM). Data processing in the CEM is performed using the General Least Squares (GLS) approach, which ensures that the data is free from multicollinearity. To address heteroscedasticity, a test with Robust Standard Errors is applied. Once all classical assumption tests are satisfied, the analysis proceeds with multiple linear regression tests.

4.3. Classical Assumptions Test

This study conducts several classical assumption tests, including tests for normality, multicollinearity, heteroscedasticity, and autocorrelation. The normality test, using the One Sample Kolmogorov-Smirnov method, yields a significance value of 0.0601 (greater than 0.05), indicating that the data distribution is normal. In the multicollinearity test, all variables have Variance Inflation Factor (VIF) values below 10, suggesting that there are no multicollinearity issues. The autocorrelation test shows a Chi-square probability value of 0.4924 (greater than 0.05), which means there is no autocorrelation in the model. However, the heteroscedasticity test, utilizing the Breusch-Pagan method, reveals the presence of heteroscedasticity in the regression model, as the probability value is 0.0000 (less than 0.05). To address this issue, the study employs regression estimation with robust standard errors. The results from this robust estimation indicate a Prob > F value of 0.0036, confirming that the overall regression model remains significant and valid, and is considered more reliable than the model without robust standard errors.

4.4. Hypothesis Test

Table 3: CEM Hypothesis Test Results

TA = 0, 2861 – 0,07463 MAD + 0,03326TP - 0,01492FO + e						
Variable		**Coefisien**	**t-stat**	**Prob t-stat**		**Result**
Tax Avoidance		0,02861				
Thin Capitalization		-0,07463	-3,20	0,002	***	Accepted
Transfer Pricing		0,03326	2,30	0,022	**	Accepted
Foreign Ownership		-0,01492	-0,75	0,452		Rejected
N	180					

Adj R-Square	0,0675					
Prob F	0,0016**					

The thin capitalization variable has a coefficient of -0.07463 with a significance level of 0.002 (< 0.05), indicating a significant negative relationship with tax avoidance at the 5% significance level. This suggests that a higher proportion of debt financing in the capital structure corresponds to a lower tendency for the company to engage in tax avoidance. This finding contradicts earlier studies by Amni *et al.,* (2023), Tarmizi *et al.,* (2023), and Waluyo & Doktoralina (2018), which concluded that debt-based funding structures actually increase the potential for tax avoidance through interest payments.

The coefficient for the transfer pricing variable is 0.03326 with a significance of 0.022 (< 0.05), indicating a significant positive effect on tax avoidance. This suggests that the more actively a company engages in transfer pricing transactions with its affiliates, the greater its likelihood of tax avoidance. This result aligns with previous studies conducted by Wier (2020), Beebeejaun (2019) and Maulana *et al.,* (2018), which assert that transfer pricing is often utilized by multinational companies as a key strategy for shifting profits to jurisdictions with lower tax rates.

Lastly, the foreign ownership variable has a coefficient of -0.01492 with a significance level of 0.452 (> 0.05), which implies that there is no statistically significant effect of foreign ownership on tax avoidance. This finding contrasts with the results of earlier studies by Suranta *et al.,* (2020), Alkurdi & Mardini (2020) and Putri *et al.,* (2024) which indicated a significant effect of foreign ownership on corporate tax avoidance practices.

4.5. The Effect of Thin Capitalization on Tax Avoidance

Thin capitalization negatively impacts tax avoidance. This means that increasing the use of debt in a company's capital structure actually leads to a reduction in the level of tax avoidance. This relationship can be understood by considering that companies with high levels of debt are often subject to strict oversight from creditors and regulators. Furthermore, in countries that have tax treaties (referred to as P3B), the tax rate on interest expenses is generally lower than the domestic tax rate of 20%. As a result, companies utilizing thin capitalization can achieve legal and optimal tax savings. This is because they benefit from the ability to deduct interest expenses and enjoy lower tax rates on cross-border interest payments.

Agency theory suggests that management has the responsibility of ensuring stable financial performance while also maintaining shareholder benefits, such as dividends. Effective management of the debt-to-equity ratio is crucial for maximizing the amount of interest expenses that can be deducted in tax reports. The management’s decision regarding thin capitalization significantly affects both the company's interest and tax expenses. According to Article 6, paragraph 1, letter a, number 3 of the Income Tax Law (UU PPh), when a company employs a significant amount of debt relative to equity for its operations involving obtaining, collecting, and maintaining (referred to as 3M activities), the interest expenses incurred can be tax-deductible. This provision allows companies to reduce their tax liabilities without needing to engage in additional tax avoidance strategies.

In the context of Planned Behavior Theory, management's perspective on debt in the capital structure is influenced by the belief that increased debt will yield benefits in the form of tax savings through an interest expense tax shield. However, if a company already carries a substantial debt burden, the tax advantages of additional debt may be maximized, thereby diminishing management's incentive to pursue other tax avoidance methods. Subjective norms also play a significant role, particularly when thin capitalization practices attract heightened scrutiny within the industry. Consequently, companies may prefer to adopt capital structure strategies that are considered appropriate and aligned with established norms. Additionally, perceived behavioral control is reflected in regulations such as PMK No. 169/2015, which sets limits on the debt-to-equity ratio. This regulation acts as an external constraint on management's ability to manipulate the capital structure for tax benefits. The combination of regulatory limitations and creditor oversight restricts management's ability to engage in tax avoidance through increasing debt.

4.6. The Effect of Transfer Pricing on Tax Avoidance

Transfer pricing positively influences tax avoidance, indicating that multinational companies view it as an effective strategy to compete globally while minimizing tax liabilities (Supriyati *et al.,* 2021). Both international and domestic tax regulations recognize transfer pricing as a significant risk for tax avoidance, leading to the implementation of various rules to monitor this practice. Article 18 of the Income Tax Law and PMK No. 172/2023 govern the oversight of inter-company transactions with foreign affiliates by applying the arm's length principle and a Substance Over Form approach. This is to ensure that every transfer pricing transaction reflects a fair market price and real economic substance, rather than serving merely as a tool for tax reduction through complex corporate structures.

According to the Theory of Planned Behavior, management's attitude towards transfer pricing is largely driven by the economic benefits gained, particularly in distributing profits to countries with lower tax rates to lessen the tax burden. Subjective norms influencing this decision include industry standards; if other sectors or multinational companies employ similar strategies without facing severe penalties, this encourages management to adopt transfer pricing strategies. The perception of behavioral control in transfer pricing pertains to the company's capability to design a pricing scheme that can evade tax authority scrutiny. Management often accesses information to develop intricate intergroup transfer pricing schemes and exploit gaps in tax regulations and arm's length standards, often with the aid of consultants or tax professionals. As long as management effectively handles the documentation and justification of their pricing scheme, the risk of audits or sanctions can be minimized, allowing the intended benefits of transfer pricing to be realized.

4.7. The Effect of Foreign Ownership on Tax Avoidance

In this study, foreign ownership did not significantly affect tax avoidance. This suggests that a high proportion of foreign shares in a company's ownership structure does not necessarily grant foreign shareholders substantial control over the company's tax policy. The average foreign ownership stands at 38.68%, indicating that foreign shareholders have limited influence on company policies, particularly concerning tax avoidance strategies (Supriyanto *et al.,* 2022). Additionally, foreign investors are often motivated by the attractive tax incentives offered for investment in Indonesia. However, they may not always benefit from tax avoidance, especially when it involves high costs and risks. Many companies find that tax avoidance strategies can be expensive and risky due to the complexities of regulations across different countries and the potential for penalties if detected.

According to agency theory, foreign shareholders typically pressure management to maximize profits to meet high expectations for investment returns. Consequently, the role of directors is crucial in leveraging tax facilities and incentives to encourage shareholder investment. On the other hand, the theory of planned behavior suggests that foreign shareholders' attitudes toward tax avoidance can vary based on the tax incentives in the destination country of investment. When foreign investors aim to maximize corporate profits legitimately, they may prefer utilizing tax facilities and incentives rather than engaging in tax avoidance. The subjective norm indicates that if a country has strong norms encouraging tax compliance, companies with foreign ownership will likely adhere to these standards and enhance their tax compliance. Perceived behavioral control relates to how much influence foreign investors can exert on management decisions regarding tax strategies, especially when their ownership stake is not substantial. With limited control, foreign investors may want to reduce taxes but cannot implement tangible actions, resulting in little change in the company's tax avoidance behavior.

4.8. Expansion Test

The Expansion Test in this study was conducted by analyzing the Board of Directors (BOD) of each analysis unit annually. The analysis was divided into two sub-samples: one for units with a foreign BOD and another for those with only a domestic BOD. This additional analysis aimed to determine the role of a foreign BOD in relation to thin capitalization, transfer pricing, foreign ownership, and tax avoidance.

Table 4: Expansion Test Results

TA	Foreign BOD		Non- Foreign BOD	
	Coeff.	Prob.	Coeff.	Prob.
MAD	-0,11441	0.001**	-0,00251	0,948
TP	0,02077	0,360	0,04269	0,026
FO	-0,00565	0,815	-0,02034	0,589
N	88		92	
R-Square	0,1351		0,0606	
Prob F	0.0065**		0,1368	

The results of the expansion test reveal that in the sub-sample of companies with foreign directors, the Thin Capitalization coefficient becomes stronger. This indicates a growing negative influence on tax avoidance. In contrast, for companies without foreign directors, the Thin Capitalization coefficient approaches zero and is not significant, suggesting that in companies managed solely by local directors, the level of debt does not significantly impact tax avoidance. Conversely, the findings for Transfer Pricing differ. In companies without foreign directors, the transfer pricing coefficient increases and remains significant, demonstrating that transfer pricing practices strongly influence tax avoidance in domestic companies. However, in companies with foreign directors, the transfer pricing coefficient decreases and loses significance, indicating that transfer pricing strategies no longer have a significant effect on tax avoidance in firms with foreign boards of directors.

Foreign ownership consistently shows insignificance in both sub-samples and demonstrates a weakening negative coefficient. This trend suggests that the significant effects of thin capitalization and transfer pricing are contingent upon the presence or absence of foreign directors. Specifically, the influence of debt on tax avoidance appears primarily in companies with foreign management, while the impact of transfer pricing is more pronounced when management is entirely local. Statistically, the coefficient of determination in the sub-sample with foreign directors is significant and increases, while the model for the sub-sample without foreign directors is not significant. This indicates that in domestic companies, the three variables are less effective at explaining the variance in tax avoidance.

The results of this expanded analysis support the notion that in companies with foreign directors, the effects of oversight and discipline are stronger. In such cases, thin capitalization exhibits a significant negative impact: high debt levels actually reduce the intensity of tax avoidance strategies. The presence of foreign directors encourages the use of debt to the extent permitted by regulations to secure tax deductions on interest, while also pressuring managers not to exceed allowable limits. Conversely, in companies without foreign directors, the discipline regarding debt in tax strategies is looser. Local management may not prioritize the use of debt as a tool for tax planning, thus making thin capitalization play a negligible role.

Regarding transfer pricing, foreign directors ensure that the company's practices remain fair and compliant with international regulations, minimizing the risk of violations. On the other hand, in companies without foreign directors, the impact of transfer pricing is significant and greater. This is due to local majority owners potentially using transfer pricing to shift profits to other domestic entities they control, allowing them to take advantage of tax breaks or fiscal losses, thereby benefiting the owners.

5. CONCLUSIONS

Based on the discussion results, it was determined that thin capitalization has a significant effect only when foreign directors are present, while transfer pricing has a significant effect only in the absence of foreign directors. This indicates that a company's corporate governance structure can influence its tax strategy. Additionally, foreign ownership does not significantly impact tax avoidance, suggesting that decisions about tax avoidance rely more on managerial strategies and policies than on the ownership structure of shares.

This study advises investors to pay attention to the transparency of corporate tax policies, as tax avoidance strategies are more influenced by managerial decisions than by ownership structure. For the government, there is a need for stricter supervision of thin capitalization and transfer pricing, as well as clearer tax policies to close loopholes that allow for tax avoidance without hindering investment. Improving the transparency of financial reports and enhancing international cooperation are also essential to prevent profit shifting to low-tax jurisdictions.

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