

THE POLITICAL ECONOMY OF TRANSFER PRICING: ITS CONTRIBUTION TO TAX AVOIDANCE AND WEALTH RETENTIVENESS

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Abstract

This article examines transfer pricing not as a neutral technical mechanism for allocating costs and revenues, but as a strategic instrument used by multinational enterprises to engage in tax avoidance and consolidate wealth. Drawing on a critical accounting framework, it builds on Sikka and Willmott (2010), who show that intra-group pricing constitutes a politico-economic practice that enables the systematic shifting of profits to low-tax jurisdictions, thereby eroding the tax base of countries where real economic activity takes place. The analysis highlights how corporations mobilize technical legitimations such as claims of arm's length pricing to construct new "truths" about fair value that are difficult for tax authorities to contest, particularly in developing countries with limited regulatory and audit capacity. Through a Foucauldian lens, transfer pricing is interpreted as a technology of power that reinforces the dominance of global capital over nation-states by controlling profit flows, structuring asymmetric regulatory negotiations, and deepening fiscal inequalities. The article thus argues that transfer pricing is a practice deeply embedded in vested interests and power relations, with significant implications for tax justice, state fiscal capacity, and the distribution of wealth in the global economy.

Keywords: Transfer Pricing, Tax Avoidance, Profit Shifting, Political Economy

1. Introduction

Multinational enterprises (MNEs) function as major forces within the global economy. Their influence is evident not only in production and trade activities but also in their ability to shape the direction of public policy. Beebejaun (2019) illustrates this dominance through economic indicators showing that MNEs contribute approximately 10% of global GDP, generate sales approaching half of global GDP, and control around 60% of international trade through intra-group transactions. These figures indicate that MNEs are not merely economic actors but institutions with the capacity to shape the rules of the global economic order.

Transfer pricing functions as a form of power/knowledge, namely a mechanism through which corporations use technical expertise to construct and maintain dominant positions. Internal pricing, profit allocation, and the design of global value chains are not merely managerial decisions but accounting techniques that directly influence the capacity of states to collect taxes. Zhang and Chan (2025) demonstrate that tax avoidance practices through transfer pricing erode state legitimacy and weaken public trust.

The logic of global capitalism shapes corporate orientations toward maximizing profits. Taxes are viewed not as a social obligation but as a burden to be minimized. Transfer pricing thus serves as an instrument to achieve corporate defined efficiency, even when such efficiency translates into reduced tax contributions. According to Tanasi

et al. (2025) and Saragih et al. (2021), these strategies are framed as rational business practices, while Syromyatnikov et al. (2020) show that such framing often obscures the fundamental objective namely, the accumulation of profits by global corporations.

The construct that taxes are merely costs to be minimized does not emerge naturally; it is formed through corporate discourse that is continually reproduced. Tanasi et al. (2025) and Sebele-Mpofu et al. (2021) show that transfer pricing is often utilized as a systematic mechanism for reducing tax burdens. This practice ultimately weakens the state's capacity to provide public services (Mpofu & Wealth, 2022). The corporate production of tax efficiency discourse reflects the concept of governmentality, referring to the ways in which power operates by shaping the thinking of society and the state regarding what is considered logical, rational, and acceptable in tax practices.

Profit shifting through techniques such as mispricing, management fees, and income relocation illustrates how corporate power becomes distributed through global networks. Tørsløv et al. (2022) estimate that 36% of global MNE profits are shifted to tax havens, demonstrating the capacity of corporations to determine the jurisdictions in which they prefer to be taxed.

State policies shaped by neoliberal orientations tend to create greater space for corporations to expand their influence and pursue their interests. In the context of developing countries, the direct adoption of OECD (Organisation for Economic Co-operation and Development) standards without adjustments to local characteristics and regulatory capacity can generate new vulnerabilities. Sebele-Mpofu et al. (2022) show that these conditions make developing countries increasingly susceptible to exploitation through profit-shifting practices carried out by multinational enterprises. Similar findings are presented by Choi et al. (2020), who observe that transfer pricing regulations are often used as instruments of tax competition to attract foreign investment. However, such strategies frequently have adverse consequences, as they undermine the ability of states to generate revenue and weaken the fiscal capacity necessary to provide sustainable public services.

The determination of costs and revenues in intercompany transactions is, in reality, never fully objective. Tanasi et al. (2025) explain that internal prices can be adjusted without any corresponding change in actual economic activity, allowing firms considerable flexibility in manipulating the magnitude of costs or revenues reported in financial statements. Mechanisms such as management fees are often used as legal-formal channels for shifting profits from one entity to another within a corporate group (Sebele-Mpofu et al., 2021). This phenomenon demonstrates that accounting figures do not simply record economic conditions as they are; rather, they are constructions shaped by managerial decisions, corporate structures, and regulatory contexts. In other words, accounting information in intra-group transactions reflects a negotiated reality, not a truly objective representation of the underlying economic activity.

International initiatives such as the BEPS (Base Erosion and Profit Shifting) project and OECD guidelines function to establish global standards aimed at enhancing fairness and transparency in intercompany transactions. Instruments such as Advance Pricing Agreements (APAs) and safe harbours are designed to assist tax authorities in monitoring transfer pricing practices and minimizing opportunities for profit shifting (Tanasi et al., 2025). However, the effectiveness of these instruments is highly dependent on each country's institutional capacity.

Many developing countries face various obstacles, ranging from limited access to comparable data, weak administrative capacity, and inadequate legal support (Sebele-

Mpofu et al., 2022). These conditions place developing countries at a disadvantage when dealing with multinational enterprises that possess far greater resources and access to information. This situation reveals a clear asymmetry of power and knowledge between states and global corporations.

Tax law enforcement faces significant challenges due to the informational asymmetry between tax authorities and multinational enterprises. Research shows that even advanced economies must contend with lengthy, costly, and highly technical tax dispute processes (Zavaglia et al., 2025). The situation becomes even more complex for developing countries, which generally lack sufficient access to comparable data, transaction documentation, and cross-border information necessary to assess the arm's length nature of transfer prices. These constraints underscore that the power of multinational enterprises stems not only from their economic scale but also from their ability to control and manage information flows, while states rely solely on formal authority that is often limited in practice.

Tax havens play a central role as destinations for global profits shifted away from the countries where real economic activity actually occurs. Numerous studies show that low-tax jurisdictions provide high levels of secrecy, loose regulatory regimes, and legal structures specifically designed to attract multinational enterprises to move their profits into these jurisdictions (Tørsløv et al., 2022). This global architecture not only facilitates tax avoidance but also creates new forms of power by enabling corporations to choose legal environments that best serve their interests. Thus, corporate power is manifested not only through economic scale but also through the freedom to operate across jurisdictions and exploit regulatory differences between countries.

As a result of transfer pricing practices, states lose substantial tax revenues that should have been generated from economic activities occurring within their territories. Techniques such as mispricing, debt shifting, and income structuring allow companies to shift profits to low-tax jurisdictions, thereby reducing tax revenues (Tørsløv et al., 2022). This loss of revenue harms state finances and creates injustice, as compliant taxpayers both individuals and domestic businesses ultimately bear the burden of financing public services and development (Sebele-Mpofu et al., 2021). Therefore, transfer pricing is not merely a technical accounting issue. It is also a moral and political problem concerning who truly pays for the cost of national development and how large corporations are able to influence the distribution of that burden.

2. Theoretical Background

2.1 Transfer Pricing

Transfer pricing refers to the pricing of goods, services, and intangible assets transacted between related parties within multinational enterprise (MNE) groups. While transfer pricing is legitimate as an internal coordination and performance-measurement mechanism, recent studies show that it becomes a primary channel for shifting profits from high-tax to low-tax jurisdictions as part of tax avoidance strategies. Empirical and conceptual research in the past five years demonstrates that MNEs systematically manipulate transfer prices either by inflating intra-group charges in low-tax locations or lowering reported profits in high-tax jurisdictions to reduce their effective tax burden (Sebele-Mpofu et al., 2021; Rathke et al., 2020; Nguyen et al., 2020). Such practices erode the tax base of source countries and make tax authorities especially in developing economies with limited audit capacity more vulnerable to undetected profit shifting (Septiani et al., 2021). Collectively, this literature positions transfer pricing as a central

mechanism through which financial engineering and group ownership structures enable aggressive tax planning.

Recent theoretical and empirical contributions also highlight tax-motivated transfer pricing as a key determinant of how MNEs design their global production structures and intra-group financial flows. Sandonis and Yermukanova (2024) show that MNEs optimize transfer prices by balancing global tax minimization with domestic production incentives, making tax avoidance an integral part of vertical integration decisions. Complementing this, Kohlhase and Wielhouwer (2023) provide evidence that headquarters and subsidiary units adjust internal prices in response to cross-country tax differentials and import tariffs to minimize overall tax liabilities. Although global initiatives such as the OECD's arm's length principle and BEPS Action Plan aim to curb abuse, recent findings still reveal persistent opportunities for price manipulation, particularly in jurisdictions with weaker regulatory capacity (Sebele-Mpofu et al., 2021; Septiani et al., 2021). Thus, contemporary scholarship consistently affirms that transfer pricing remains a strategic and sophisticated tool for tax avoidance within multinational groups.

2.2 Tax Avoidance

Tax avoidance is commonly defined as the use of legal tax-planning strategies to reduce a firm's tax burden by exploiting loopholes, gaps, or mismatches in tax rules, often pushing the boundary between acceptable planning and aggressive base erosion. Recent studies emphasize that modern corporate tax avoidance is increasingly international in nature, relying on profit shifting from high-tax to low-tax or offshore jurisdictions, which erodes domestic tax bases and undermines governments' fiscal capacity, especially in countries with limited enforcement and audit resources (Tørslov et al., 2023; Nerudová et al., 2023; Nguyen et al., 2020).

Within this broader perspective, transfer pricing is theorized as a key mechanism through which tax avoidance is implemented in multinational groups. Empirical evidence over the past five years shows that multinational enterprises strategically set intra-group prices for goods, services, and intangibles to reallocate taxable income toward low-tax affiliates, thereby lowering their effective tax rates while formally complying with arm's-length rules (Irawan et al., 2020; Sebele-Mpofu et al., 2021; Rathke & Rezende, 2020). Research also indicates that stricter transfer pricing regulations, documentation requirements, and penalty regimes can reduce tax-motivated transfer pricing and curb profit shifting, confirming the central role of transfer pricing in contemporary debates on tax avoidance (Sari et al., 2020; Nguyen et al., 2020).

2.3 Profit Shifting

Profit shifting is generally understood as the deliberate relocation of taxable profits from high-tax to low-tax jurisdictions within a multinational enterprise (MNE) group, without a corresponding movement of real economic activity (Tørslov, Wier, & Zucman, 2023). In theory, profit shifting exploits differences in tax rates, rules, and enforcement across countries: firms design financial structures, intra-group transactions, and the location of intangibles so that more income is recognized where it is taxed lightly, while costs are booked where tax rates are higher (Ferrari et al., 2023; Gabanatlhong et al., 2024). This behavior erodes the tax base of higher-tax countries and can undermine the perceived fairness and sustainability of corporate tax systems, even when companies remain formally within the boundaries of the law (Tørslov et al., 2023).

Within this framework, transfer pricing is one of the primary mechanisms through which profit shifting is implemented. By setting intra-group prices for goods, services, financial transactions, and intangibles at levels that deviate from what independent parties would agree (the arm's length principle), MNEs can systematically shift reported profits toward affiliates in low-tax or preferential regimes and away from entities located in high-tax jurisdictions (Sandonis & Yermukanova, 2024). In practice, profit shifting via transfer pricing is especially prominent for hard to value intangibles and complex services, where there is wide discretion in determining comparable market prices (OECD, 2022). Thus, theoretical discussions of profit shifting almost always place transfer pricing at the centre, treating it as a key tax-planning tool that links multinational group structures to patterns of international tax base erosion (Sebele-Mpofu et al., 2021).

2.3 Political Background

Political economy is commonly understood as an interdisciplinary field that studies how political power, institutions, and ideas shape economic structures, and how economic interests, in turn, influence political decision-making and social outcomes. Recent work highlights political economy as the analysis of "structures and objectives at the systemic level," emphasizing how states, markets, and social actors interact to determine the distribution of resources, opportunities, and risks in capitalism. International political economy further stresses the tensions between globalization and its critics, showing how competing coalitions use institutions, regulations, and narratives to steer globalization in ways that reflect their interests and values (Martinez-Bravo & Wantchekon, 2023).

Within this perspective, contemporary political economy pays growing attention to taxation, public finance, and corporate behavior as arenas where power and distributional conflicts become visible. A critical political economy of taxation, for example, examines how tax systems reflect and reproduce power relations whose income is taxed, at what rates, and with what scope for avoidance rather than being neutral technical arrangements. This lens is particularly relevant for analyzing international tax avoidance, profit shifting, and transfer pricing by multinational enterprises, where legal rules, lobbying, international organizations (such as the OECD), and domestic political bargains collectively determine the extent to which global capital is taxed or allowed to minimize its contribution to public revenues.

3. Methods

The research method employed in this article is a qualitative approach using a critical literature review design grounded in the framework of critical accounting and Foucault's concepts of power, knowledge, and governmentality. The study relies entirely on secondary sources, including international journal articles, reports from international organizations, tax policy documents, and documented transfer pricing cases from various countries such as Zimbabwe, Mauritius, Vietnam, Indonesia, the United States, and the United Kingdom. These materials were purposively selected because they represent prominent instances of profit shifting practices and tax disputes.

These sources were analyzed interpretively to trace how discourses of tax efficiency, the arm's length principle, and international regulations are produced, negotiated, and utilized by multinational corporations, with a focus on the power relations between MNEs, developed countries, and developing countries, as well as their implications for fiscal justice and state fiscal capacity.

4. Results and Discussion

Transfer pricing can no longer be viewed as a purely technical accounting tool used solely to allocate costs and revenues within corporate groups. The practice has evolved into a strategic instrument employed by multinational enterprises to maximize profits and minimize tax burdens through various forms of cross-jurisdictional profit shifting (Sikka & Willmott, 2010). Research from the past five years affirms that such strategies align with the logic of capitalism oriented toward profit accumulation, in which taxes are regarded as costs to be reduced rather than social contributions to the state and society (Sebele-Mpofu et al., 2021). Developing countries such as Zimbabwe, Ghana, Vietnam, Indonesia, and many other African nations are disproportionately harmed due to limited administrative capacity, weak domestic regulations, and the dominant role of multinational enterprises in their economic structures (Nguyen et al., 2020).

Various mechanisms such as transfer mispricing, management fees, debt shifting, and the use of tax havens have been shown to systematically reduce potential tax revenues (Tørslov et al., 2022). Although international initiatives such as the OECD–G20 BEPS project and the UN Transfer Pricing Manual have been introduced, their effectiveness remains limited due to structural global inequalities, tax competition among countries, regulatory arbitrage opportunities, and significant information asymmetry between corporations and tax authorities (OECD, 2020). Thus, the problem of transfer pricing cannot be understood merely as a technical matter; it constitutes a global political-economic issue that shapes fiscal justice, state development capacity, and the distribution of wealth across countries (Rossing & Pearson, 2022).

Some Evidence on Transfer Pricing Practices and Tax Avoidance. This section presents several pieces of evidence regarding the use of transfer pricing practices in both developing and developed countries.

4.1 Developing and Transition Economies

Zimbabwe, as a developing country highly dependent on tax revenues from key sectors such as mining and agriculture, is particularly vulnerable to transfer pricing practices when multinational enterprises shift profits to low-tax jurisdictions rather than reporting them where real economic activity occurs (Sebele-Mpofu et al., 2022). Cases such as the alleged transfer pricing by Econet Wireless in 2017 illustrate how inflated intra-group charges can significantly reduce taxable income. In the mining sector, mispricing of mineral exports, intra-group management fees, and under-/over-invoicing have contributed to illicit financial flows. Although the government has strengthened its regulatory framework through the 2019 Transfer Pricing Documentation Regulations, enforcement challenges persist due to limited administrative capacity.

Mauritius, a small island nation with highly competitive tax rates, frequently serves as a financial hub for treaty shopping and profit-shifting structures. Investigations show how firms such as Illovo and MTN routed profits to shell entities in Mauritius with no real economic activity, enabling substantial reductions in tax liabilities in African countries where operations actually take place (Beebejaun, 2019). These cases highlight Mauritius's role as a key node in global tax avoidance architecture, often to the detriment of developing economies.

In Vietnam, transfer pricing is widespread among foreign direct investment (FDI) firms, which play a dominant role in the manufacturing sector. The government faces significant difficulties in determining whether reported losses are genuine or the result of profit shifting due to limited comparable data and complex pricing methods (Nguyen et

al., 2020). Many FDI firms continue to expand operations while repeatedly reporting losses, suggesting patterns of mispricing that reduce state revenue and hinder development financing.

In Indonesia, transfer pricing has long been identified as a major concern because it erodes potential tax revenues (Septiani et al., 2021). The Asian Agri case is one of the most prominent examples: the company was found to have manipulated prices and fabricated costs across 14 affiliated entities to shift profits to jurisdictions such as Singapore and Hong Kong, resulting in losses exceeding IDR 1 trillion to the state (Margareta, 2024). The Supreme Court imposed criminal fines amounting to approximately IDR 2.5 trillion, making the case a landmark illustration of how intra-group price manipulation can systematically reduce tax obligations.

4.2 Developed and Developing Economies

Multinational enterprises (MNEs) exert significant influence over the global economy and public policy, controlling large shares of global GDP, sales, and trade (Beebejaun, 2019). Transfer pricing functions as a form of corporate power, enabling firms to structure intra-group transactions that shift profits and erode tax bases while being framed as rational business behavior within capitalist systems (Zhang & Chan, 2025; Tanasi et al., 2025). Corporate narratives further legitimize tax minimization, allowing transfer pricing to systematically reduce state revenues and relocate profits to tax havens an estimated 36% of global MNE profits (Tørslov et al., 2022). These practices highlight the constructed nature of accounting numbers and the role of managerial discretion in shaping reported income (Sebele-Mpofu et al., 2021).

Despite global initiatives such as BEPS and APAs, enforcement effectiveness remains constrained by institutional capacity, especially in developing countries, which face information asymmetry and weak administrative systems (Sebele-Mpofu et al., 2022). Tax havens exacerbate these challenges by providing secrecy and permissive regulation, amplifying revenue losses and raising ethical concerns about fiscal fairness (Tørslov et al., 2022). Evidence from Zimbabwe, Mauritius, Vietnam, and Indonesia illustrates how mispricing, shell entities, and fictitious transactions enable significant profit shifting, resulting in substantial public revenue losses (Beebejaun, 2019; Nguyen et al., 2020; Margareta, 2024). Advanced economies face similar issues: the United States handles large-scale transfer pricing disputes such as the ConocoPhillips–Louisiana case (Zavaglia et al., 2024), while the United Kingdom has addressed aggressive tax avoidance through measures like the Diverted Profits Tax, exemplified by the Starbucks case (Rossing & Pearson, 2022).

The findings of this article open an important discussion on how transfer pricing should be understood within the context of the global neoliberal economy. The dominance of multinational enterprises in international trade creates asymmetrical power relations in which states, while highly dependent on foreign investment flows, simultaneously lose control over their tax bases. In this context, transfer pricing becomes a primary channel through which multinational enterprises shift profits via complex yet formally legal schemes. This produces a paradox: states demand tax revenues to support development and public welfare, yet the very policy frameworks they adopt create spaces for significant reductions in tax collections (Beebejaun, 2019).

Second, the article emphasizes that the application of the Arm's Length Principle (ALP) faces substantial challenges in developing countries. Limited access to comparable data, weak audit capacity, and the growing weight of intangible-asset-based economic

activities makes the principle difficult to implement effectively. These problems are compounded by the fact that international guidelines are largely developed in the context of advanced economies; when developing countries adopt them without adequate adaptation, the effectiveness of tax enforcement becomes severely constrained (Sebele-Mpofu et al., 2022).

Third, the analysis shows that transfer pricing operates as a structural mechanism within the neoliberal order, reinforcing uneven power relations between multinational enterprises and states. In many developing countries, governments become increasingly dependent on foreign investment while gradually relinquishing control over their tax bases. Recent studies indicate that transfer pricing serves as a key channel through which Multinational Enterprises (MNEs) shift profits using complex but formally legal arrangements, thereby intensifying the paradox whereby governments call for higher tax revenues even as their own policy regimes facilitate substantial tax reductions (Beebejaun, 2019).

Fourth, the article raises fundamental concerns about fiscal justice in the global tax architecture. On the one hand, developed countries act as the principal designers of international tax standards; on the other hand, many multinational corporations headquartered in these jurisdictions are among the main actors engaged in cross-border tax avoidance. This contradiction suggests that the global tax system is not neutral, but instead reflects asymmetric interests between developed and developing countries. Ultimately, developing countries bear a disproportionate burden through the loss of potential tax revenues, even though they rely heavily on fiscal resources to finance development agendas, including health care, education, and infrastructure for the wider population.

Fifth, from a critical accounting perspective, this article underscores the importance of qualitative approaches in deconstructing technocratic narratives that portray transfer pricing as an objective and neutral mechanism. Through qualitative inquiry, researchers can trace the social meanings embedded in pricing practices, uncover the power relations operating among states, corporations, and the accounting profession, and observe how rules and institutions are shaped and negotiated in practice. In this way, the study demonstrates that transfer pricing is not merely a matter of numerical calculation or the application of quantitative formulas, but a complex social, economic, and political phenomenon that requires interdisciplinary analysis involving legal, political, sociological, and public policy perspectives.

Transfer pricing is positioned by Sikka and Willmott (2010) as a central instrument of tax avoidance and a mechanism of wealth retention in the hands of multinational corporations. Within the critical accounting framework, they show that the pricing of intra-group transactions is not simply a technical procedure for allocating costs and revenues, but a political-economic strategy systematically used to shift profits to low-tax jurisdictions or tax havens. This practice not only reduces corporate tax liabilities but also erodes the tax base of countries where real economic value is created. The interpretation becomes even more pronounced when examined through a Foucauldian lens, in which transfer pricing can be understood as a technology of power that enables corporations to produce and impose “truths” about fair value, thereby negotiating and simultaneously challenging state authority in defining what is considered legitimate and equitable within tax regimes.

5. Conclusion

Through claims about the “arm’s length price” and other forms of technical legitimization, corporations construct “truths” about fair value that are, in practice, difficult for tax authorities to challenge particularly in developing countries where supervisory capacity and the quality of underlying data remain limited. In this context, transfer pricing operates as a technology of power that enables corporations to control profit flows and tax burdens across jurisdictions, to negotiate and even shape regulatory frameworks together with governments, and to reconfigure the distribution of fiscal revenues between states.

Consequently, transfer pricing contributes to the reproduction of structural inequalities between highly mobile global capital and nation-states that rely on tax revenues to finance public services such as education, health care, and infrastructure for their citizens. Through claims about the “arm’s length price” and other forms of technical legitimization, corporations construct “truths” about fair value that are, in practice, difficult for tax authorities to challenge particularly in developing countries where supervisory capacity and the quality of underlying data remain limited. In this context, transfer pricing operates as a technology of power that enables corporations to control profit flows and tax burdens across jurisdictions, to negotiate and even shape regulatory frameworks together with governments, and to reconfigure the distribution of fiscal revenues between states. Consequently, transfer pricing contributes to the reproduction of structural inequalities between highly mobile global capital and nation-states that rely on tax revenues to finance public services such as education, health care, and infrastructure for their citizens.

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