

Transfer Pricing As a Tool for Tax Avoidance by Multinational Enterprises in Developing Countries

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Abstract

The abuse of Transfer Pricing (TP) by Multinational Enterprises (MNEs) has become a global crisis. The abuse of TP results in a serious reduced tax basis, and shifting of large some of profits from countries with high tax rates to those with lower tax rates, thus bringing about tax evasion and avoidance. Based on the empirical evidence, most scholars argue that developing countries suffer the most when it comes to the negative impacts of transfer pricing. As such this research seeks to investigate the strategies used by MNEs to minimize their tax burdens in the developing world.

The research adopted a quantitative approach to analyses the primary data. Primary data was collected through a questionnaire survey that was distributed among the targeted participants of Zimbabwe. The respondents were made up of top managers and ordinary workers from the Multinational Enterprises on Zimbabwe, and they were selected through a non-probability sampling. Based on the results of this study, most respondents were aware of the types of transfer pricing and all the strategies used to manipulate transfer pricing. Analysis is based on the primary data and questionnaire survey conducted in Zimbabwe. The results indicate that there is a positive correlation among the types of transfer pricing, namely; cost based transfer method, market based transfer pricing, negotiated transfer pricing and arbitrary transfer pricing.

Keywords: Transfer Pricing, Mnes, Tax Avoidance, Tax Havens, Zimbabwe, Market Based Transfer Pricing

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I. INTRODUCTION

One of the distinguishing characteristics of today's enterprises is globalization. Companies have engaged on expansion and diversification endeavors that have taken their activities across borders in order to maintain a competitive and sustainable upper hand in the globalized village; therefore, the development and growth of Multinational Enterprises MNEs. MNEs play an essential role on the world stage.

1.1. RESEARCH BACKGROUND

Globalization has led to the concentration of economic activity within a small number of Multinational Enterprises. This development has made it more challenging for governments to raise revenue from corporate income tax, as MNEs can shift their profits across borders to reduce their tax bills. In recent years, policy-makers have become increasingly concerned about this issue as the extent of profit shifting has intensified (Zucman, 2014). A key instrument that MNEs use to shift profits is manipulating transfer prices they charge on transactions between related parties within the MNE group (transfer mispricing).

For example, to reduce its pre-tax profits (and hence corporate taxes), an MNE can charge a lower price when selling to a related party in a low-tax country. Tax based transfer mispricing can take place in trade in real goods as well as in services, and in particular in the form of royalty and licensing payments on intellectual property rights held a broad.

In the fourth industrial revolution and for more than four decades to date, large corporate dominated the global economy. For example, the combined total revenues of 2000 biggest companies in 2021 constitute approximately half of the world's gross domestic product (GDP) of around 78.63 USD trillion (World Bank, 2021). Most of these companies are multinational corporate with operating facilities across the whole world and selling their products all over the world. This enhances and rejuvenates the perception of the public, particularly academia and policy makers that multinational entities are involved in some forms of tax avoidance strategies.

The European Commissioner for Competition Margrethe Vestager, after finding that in 2014 Ireland granted Apples a meager corporate tax rate of 0.005%, on 30 August 2016 announced the decision by the

Commission that Ireland was liable to collect Corporate Income Taxes from Apple amounting to €13 billion (European Commission, 2016). The bases of the commission's point of contention were the bizarre action by the Irish government tantamount to illegal subsidizing of a company already earning billion a year.

Sikka (2019) described transfer pricing as the biggest tax avoidance scheme of all with 60% of world trade occurring internally among multinationals (MNEs). Juxtaposing annual US corporate tax revenues of 400 USD billion, in the case of OECD countries, revenues losses due to tax avoidance by MNEs average between USD 240 billion per annum, where tax evasion losses stood at 200 USD billion (Avi-Yonah, 2017). MNEs are very resourceful, providing them with unfair advantages over domestic firms. Revenue losses through abusive transfer pricing by MNEs has been estimated to be in excess of US\$160 billion a year in developing countries (Fuest and Riedel, 2019; Murphy, 2018) hence the need to emphasize the importance of understanding MNEs TP practices, as they impact on taxes and the ability of governments to provide public goods and services directly affecting social welfare.

MNEs and their linked firms are anticipated to account for a tenth of global GDP, while their sales are estimated to be half of global GDP, Beebeejaun (2019) states that their growth rate is quicker than the global economy's average GDP growth. Sixty percent of MNE trade is said to be transactions that take place within group arrangements. The prices of these transactions are always a subject of controversy; they cannot be verified in many circumstances and are mostly not at arm's length or not even based on market transactions.

The prices of these transactions are always a subject of debate; they cannot be verified in many instances and are mostly not at arm's length or not even based on market transactions. This is the greatest irony of free market economies: a substantial proportion of world trade (that occurring within MNEs) is not governed by prices set by the market (Sebele-Mpofu, 2021).

Mckinley (2003) and Kebwaro (2012) describes transfer price as the price charged between related parties in an inter-company transaction. This practice, which includes a multinational selling itself goods and services at an artificial high price, has been commonly utilized by multinational businesses to move earnings out of the nations where they operate and into tax havens. As a result, the Multinational Enterprises pay no tax in its home country and no tax in the place where it is destined.

According to Gaietal (2014), MNEs' dominance in intercompany trade in particular industries is prone to power abuse. MNEs tend to structure transactions and exchanges between their affiliates, parent, and subsidiaries in such a way that tax liability is avoided or minimized by moving profits and incomes from jurisdictions with high tax rates to jurisdictions with low tax rates when exercising market power and dominance.

Governments must comprehend transfer pricing (TP) abuse techniques in order to be fully prepared to prevent or offset their economic impact (Cooperetal, 2017). Domestic income mobilization is a critical responsibility for every government's functionality and existence, and tax collecting is a critical component of such efforts. Transfer pricing is argued to have a detrimental impact for developing countries, not only does it lead to BEPS problems, but it aids tax avoidance, robbing these countries of entitled tax revenues to fund economic development, infrastructure, health, education and poverty mitigation efforts.

This study is motivated by the need for equity and neutrality in pricing decisions so as to avoid distortions in income allocation and taxing rights. It is vital that taxing rights are rightful and fairly distributed because such decisions have impacts on multiple arenas. In addition, curbing Ilicit Financial Flows (IFFs) is a component of the Sustainable Development Goals (SDGs) target 16 for promoting peace and justice as well as building strong institutions. The need for fulfillment of this SDG by developing the heightened interest on TP by both developed and developing countries, the prominent featuring of the issue in development agendas and tax administration forms as well as the negative effect of tax evasion and avoidance on economies piqued the researchers' curiosity and concern on the TP strategies and possible ways to ameliorate the unfavorable outcomes, thus this study aims to make a contribution to policy and practice (Sebele-Mpofu 2021). As such this study seeks to add to the paucity in knowledge in relation to TP manipulation strategies and TP in general as the area is still in its ascent stages of development and remains underexplored.

1.2. PROBLEM STATEMENT

It has been proven that transfer pricing is an economic and legal tool used by business entities for their tax burden optimization (Menlychenko, 2017). The economic power of MNEs reached global scope by the end of the 20th century. They account for more than half the production of world GDP ,the total monetary reserves of MNEs are several times higher than the total foreign exchange reserves of all the central banks world-wide, moreover, multinational corporations are powerful employers. The most 500 powerful MNE's have a virtually unlimited power, some of their market capitalization are approximately USD 1 Trillion and their sales amount to approximately USD 2 trillion. These MNEs sale over 80% electronics and chemistry products 95%, Pharmaceuticals and 76% machinery equipment (Becker-Ritterspach, 2017 and World Bank, 2021). Using transfer pricing, MNEs are able to transfer revenues to foreign affiliates with lower corporate tax rates. As such

this research seeks to examine the role of transfer pricing using empirical evidence and primary as ways of tax reduction and avoidance methods.

1.3. SIGNIFICANCE OF THE STUDY

The significance of this study cannot be overemphasized. This study may provide a better understanding of transfer pricing and tax avoidance by MNEs and how this contributes to the profit distribution of MNEs and effect on the host country for MNEs.

- The authorities will seek to avoid any leakage of revenue through use of transfer pricing mechanisms that are likely to deny them of their revenue.
- Transfer pricing is racking serious havoc on most economies particularly those of developing countries, therefore this research will contribute to a large pool of literature.
- This study will also contribute recommendations to solve problems leading to tax avoidance associated with TP.

1.4. RESEARCH QUESTIONS

To achieve the research objectives, the following research questions are asked:

- What are the strategies used by MNEs to move large sums of profits from developing countries to developed countries?
- What can be done MNEs to avoid Transfer Pricing such that both governments and MNEs can benefit on these huge sums of money?
- What is it that Zimbabwe's government is doing that forces MNEs to prefer Transfer Pricing over paying taxes?
- What can be done by third world countries to reduce the magnitude of transfer pricing exploitation and abuse?

1.5. RESEARCH OBJECTIVES

The universal purpose of this study was to examine transfer pricing as a tool by MNEs for tax avoidance purposes and the degree by which transfer pricing may impact a firm's profit. In pursuit of the mentioned goal, the following research objectives guided the study:

- To investigate the strategies used by MNEs to minimize their tax burdens in the developing world.
- To investigate the strategies used by MNEs to move large sums of out to their mother land.
- To establish the effect of transfer pricing in aiding tax avoidance and evasion in Africa.
- To problematize weaknesses by tax authorities so that they should be aware of the need to publish documentation requirements concerning transfer pricing, with a view towards improving the ability of tax authorities to assess MNEs transfer pricing compliance.

1.6. INNOVATIONS

The main thrust of this study is to examine how Multinational Corporations (MNEs) use transfer pricing practices to reduce taxable profit with a view to recommend how such practices could be minimized, to strengthen the tax revenues of their host countries. This will be done empirically using various studies on transfer pricing, taxation and statistical sources such as World Bank, IMF, United Nations etc. The study will also look into various MNEs and how they take advantage of different tax rates charged in different jurisdictions to minimize the groups' tax liabilities through transfer pricing practices to shift profit from high-tax jurisdictions to low-tax jurisdictions. Multinational corporations as integrated entities capitilize on international differentials and generate integration economies by setting transfer prices that are unlikely to be the same prices arms' length parties would negotiate. Therefore this research seeks to critique this issue of Transfer Pricing and come to answer the question what is that the Zimbabwe's government and other African countries are doing that makes MNE's to prefer Transfer Pricing over paying taxes in host countries.

II. LITERATURE REVIEW

2.1. TRANSFER PRICING

Multinational firms have a number of tools to shift profits out of high into low tax regions. These include the option to finance an affiliate with debt or equity, the organizational form, or the payment of management fees or royalties between the parent company and its affiliates. When intrafirm trade crosses national borders, it is called international transfer pricing, or simply transfer pricing. The manipulation of transfer is another generally used instrument. International transfer prices make the already complex situation even more complex since more elements are added to the price-making decision. One complex and highly

discussed issue is when an internal cross-border transaction occurs, activities are undertaken in different tax jurisdictions which can have large effects on the pricing (Hjertbeg and Pettersson, 2010).

The economic rules propose that the highest transfer price would be market price and the lowest transfer price would be differential cost. Depending on the alternative available to the buyer and seller, some other transfer price might be chosen between these two extremes. Economic rules work best in a domestic business setting where both buyer and seller divisions are taxed at the same corporate rate, because the tax rates do not affect the outcome. While the economic principles work well for domestic transfer prices, they differ substantially from international rules. Each country legislates and implements its own transfer pricing laws. A multinational enterprise with foreign divisions must then comply with tax laws for each country in which one of its divisions is domiciled. Every transaction between company sub-units is subject to audit by two sets of tax authorities. Tax compliance places a heavy burden on MNEs and takes precedence over economic rules (Reimers, 2009).

Transfer pricing refers to the terms and conditions surrounding transactions within a multi-national entity. It concerns the prices charged between associated entities established in different countries for their inter-company transactions, i.e. transfer of goods and services. Since the prices are set by non-independent associates within the multi-national, it may be the prices do not show an independent market price. This is a major concern for tax authorities who worry that multi-national entities may set transfer prices on cross-border transactions to reduce taxable profits in their jurisdiction. This has led to the rise of transfer pricing regulations and enforcement, making transfer pricing a major tax compliance issue (Gałaszka, n.d).

A MNE has to manage its overseas transactions in a world characterized by different international tax rates, foreign exchange rates, governmental regulations, currency manipulation, and other economic and social problems. One of the most important things is to reduce the global income tax liability for the MNE and problem focus on double taxation (Hjertbeg and Pettersson, 2010).

An economic double taxation situation arises when the same income are taxed twice. For MNEs this transpires when there is a conflict of interest between the tax authorities in the countries involved in the transaction. The tax authority in each country wants to protect their tax base and gain as large income as possible. They can have laws and regulations that vary and raise claims at the same income. For example there can be differences in definitions on the requirements for unlimited tax obligations or in the definition of associated enterprises, what is considered to be the permanent place for the operation or different rules of what is considered to be incorrect pricing or transfer loss (Nguyen, 2009). It is widely accepted that companies seek to maximize profits. A multinational enterprise (MNE) can help achieve this goal by shifting profits from high-tax to low-tax jurisdictions (Gałaszka, n.d).

International transfer pricing policies are generally set to extend the after-tax profitability of worldwide business transactions. The minimization of income tax liabilities for an MNEs has been considered as the most important factor or objective in designing transfer pricing policies in the foreign country, and consequently, if a transfer prices shifts profits from a country with high tax rates to a country with low tax rates, the global profits will be maximized. However, tax authorities are concerned that MNEs could use these transfer prices to shift profits between related parties through cost of goods (Gałaszka, n.d).

Tax avoidance and the unethical behavior of multinationals has become a major issue for governments around the world. Though crucial, tax avoidance by MNEs has been largely discussed with reference to the role played by low-tax jurisdictions or tax havens in facilitating transfer pricing manipulation (Taylor and Richardson, 2014). In order to take advantage of tax differentials in tax jurisdictions, MNEs also exploit the loopholes in the existing transfer pricing rules. Other scholars have discussed tax avoidance in the context of tax administration deficiencies, with the majority addressing this phenomenon as a matter between MNEs and the tax inspector (authority) (Mashiri, Dzomira and Canicio, 2017).

The role of multinational enterprises (MNEs) in world trade has continued to grow dramatically since the adoption of these Guidelines in 1995. This in part shows the increased pace of integration of national economies and technological progress, particularly in the area of communications. The growth of MNEs presents increasingly complex taxation issues for both tax administrations and the MNEs themselves since separate country rules for the taxation of MNEs cannot be viewed in isolation but must be addressed in a broad international context (OECD, 2017).

These issues occur primarily from the practical difficulty, for both MNEs and tax administrations, of determining the income and expenses of a company or a permanent establishment that is part of an MNE group that should be taken into account within a jurisdiction, particularly where the MNE group's operations are highly integrated (OECD, 2017).

In the case of MNEs, the need to conform to laws and administrative requirements that may differ from country to country creates additional problems. The differing requirements may lead to a greater burden on an MNE, and result in higher costs of compliance, than for a similar enterprise operating solely within a single tax jurisdiction (OECD, 2017).

In the case of tax administrations, specific problems emerge at both policy and practical levels. At the policy level, countries need to reconcile their legitimate right to tax the profits of a taxpayer based upon income and expenses that can reasonably be considered to emerge within their territory with the need to avoid the taxation of the same item of income by more than one tax jurisdiction. Such taxation can create an impediment to cross-border transactions in goods and services and the movement of capital. At a practical level, a country's determination of such income and expense allocation may be impeded by difficulties in obtaining pertinent data located outside its own jurisdiction (OECD, 2017).

At a primary level, the taxing rights that each country imposes depend on whether the country uses a system of taxation that is residence based, source-based, or both. In a residence-based tax system, a country will include in its tax base all or part of the income, including income from sources outside that country, of any person (including juridical persons such as corporations) who is perceived to be a resident in that jurisdiction. In a source based tax system, a country will include in its tax base income arising within its tax jurisdiction, irrespective of the residence of the taxpayer. As applied to MNEs, these two bases, often used in conjunction, generally treat each enterprise within the MNE group as a separate entity. OECD member countries have chosen this separate entity approach as the most reasonable means for achieving equitable results and minimizing the risk of unrelieved double taxation. Thus, each individual group member is subject to tax on the income arising to it (on a residence or source basis) (OECD, 2017).

In order to apply the separate companies' approach to intra-group transactions, individual group members must be taxed on the basis that they act at arm's length in their transactions with each other. However, the relationship among members of an MNE group may allow the group members to establish special conditions in their intra-group relations that differ from those that would have been established had the group members been acting as independent enterprises operating in open markets. To ensure the correct application of the separate entity approach, OECD member countries have adopted the arm's length principle, under which the effect of special conditions on the levels of profits should be eliminated (OECD, 2017).

These international taxation principles have been selected by OECD member countries as serving the dual objectives of securing the appropriate tax base in each jurisdiction and avoiding double taxation, thereby minimizing conflict between tax administrations and promoting international trade and investment. In a global economy, coordination among countries is better placed to obtain these goals than tax competition. The OECD, with its mission to contribute to the expansion of world trade on a multilateral, non-discriminatory basis and to obtain the highest sustainable economic growth in member countries, has continuously worked to build a consensus on international taxation principles, thereby avoiding unilateral responses to multilateral problems (OECD, 2017).

The foregoing principles concerning the taxation of MNEs are included in the OECD Model Tax Convention on Income and on Capital (OECD Model Tax Convention), which forms the basis of the extensive network of bilateral income tax treaties between OECD member countries and between OECD member and non-member countries. These principles also are included in the Model United Nations Double Taxation Convention between Developed and Developing Nations (OECD, 2017).

The main mechanisms for resolving issues that arise in the application of international tax principles to MNEs are contained in these bilateral treaties. The Articles that chiefly affect the taxation of MNEs are: Article 4, which defines residence; Articles 5 and 7, which determine the taxation of permanent establishments; Article 9, which relates to the taxation of the profits of associated enterprises and applies the arm's length principle; Articles 10, 11, and 12, which determine the taxation of dividends, interest, and royalties, respectively; and Articles 24, 25, and 26, which contain special provisions relating to non-discrimination, the resolution of disputes, and exchange of information (OECD, 2017).

The Committee on Fiscal Affairs, which is the main tax policy body of the OECD, has presented a number of reports relating to the application of these Articles to MNEs and to others. The Committee has recommended the acceptance of common interpretations of these Articles, thereby reducing the risk of inappropriate taxation and providing satisfactory means of resolving problems arising from the interaction of the laws and practices of different countries (OECD, 2017).

In applying the foregoing principles to the taxation of MNEs, one of the most challenging issues that has arisen is the establishment for tax purposes of appropriate transfer prices. Transfer prices are the prices at which an enterprise transfers physical goods and intangible property or provides services to associated entities. For purposes of these Guidelines, an "associated enterprise" is an enterprise that satisfies the conditions set forth in Article 9, sub-paragraphs 1a) and 1b) of the OECD Model Tax Convention. Under these conditions, two enterprises are associated if one of the enterprises participates directly or indirectly in the management, control, or capital of the other or if "the same persons participate directly or indirectly in the management, control, or capital" of both enterprises (that is; if both enterprises are under common control). The issues discussed in these Guidelines also arise in the treatment of permanent establishments as discussed in the Report on the Attribution of Profits to Permanent Establishments that was adopted by the OECD Council in July 2010, which supersedes

the OECD Report Model Tax Convention: Attribution of Income to Permanent Establishments (1994). Some relevant discussion may also be found in the OECD Report International Tax Avoidance and Evasion (1987) (OECD, 2017).

Transfer prices are important for both taxpayers and tax administrations because they determine in large part the income and expenses, and therefore taxable profits, of associated enterprises in different tax jurisdictions. Transfer pricing issues originally arose in transactions between associated enterprises operating within the same tax jurisdiction. The domestic issues are not included in these Guidelines, which focus on the international aspects of transfer pricing. These international issues are more difficult to deal with because they involve more than one tax jurisdiction and therefore any adjustment to the transfer price in one jurisdiction implies that a corresponding change in another jurisdiction is appropriate. However, if the other jurisdiction does not agree to make a corresponding adjustment the MNE group will be taxed twice on this part of its profits. In order to reduce the risk of such double taxation, an international consensus is required on how to establish for tax purposes transfer prices on cross-border transactions (OECD, 2017).

Traditional transaction methods are the comparable uncontrolled price method or CUP method, the resale price method, and the cost plus method. Transactional profit methods are the transactional net margin method and the transactional profit split method. The selection of a transfer pricing method always aims at finding the most appropriate method for a particular case. Traditional transaction methods are regarded as the most direct means of establishing whether conditions in the commercial and financial relations between associated enterprises are arm's length. This is because any difference in the price of a controlled transaction from the price in a comparable uncontrolled transaction can normally be traced directly to the commercial and financial relations made or imposed between the enterprises, and the arm's length conditions can be established by directly substituting the price in the comparable uncontrolled transaction for the price of the controlled transaction (OECD, 2017).

The comparable uncontrolled price method compares the price charged for property or services transferred in a controlled transaction to the price charged for property or services transferred in a comparable uncontrolled transaction in comparable circumstances. If there is any difference between the two prices, this may indicate that the conditions of the commercial and financial relations of the associated enterprises are not arm's length, and that the price in the uncontrolled transaction may need to be substituted for the price in the controlled transaction (OECD, 2017).

Under the comparable uncontrolled price method, the arm's length price for commodity transactions may be determined by reference to comparable uncontrolled transactions and by reference to comparable uncontrolled arrangements represented by the quoted price. Quoted commodity prices generally reflect the agreement between independent buyers and sellers in the market on the price for a specific type and amount of commodity, traded under specific conditions at a certain point in time. A relevant factor in determining the appropriateness of using the quoted price for a specific commodity is the extent to which the quoted price is widely and routinely used in the ordinary course of business in the industry to negotiate prices for uncontrolled transactions comparable to the controlled transaction. Accordingly, depending on the facts and circumstances of each case, quoted prices can be considered as a reference for pricing commodity transactions between associated enterprises. Taxpayers and tax administrations should be consistent in their application of the appropriately selected quoted price (OECD, 2017).

For the comparable uncontrolled price method to be reliably applied to commodity transactions, the economically relevant characteristics of the controlled transaction and the uncontrolled transactions or the uncontrolled arrangements represented by the quoted price need to be comparable. For commodities, the economically relevant characteristics include, among others, the physical features and quality of the commodity; the contractual terms of the controlled transaction, such as volumes traded, period of the arrangements, the timing and terms of delivery, transportation, insurance, and foreign currency terms. For some commodities, certain economically relevant characteristics may lead to a premium or a discount. If the quoted price is used as a reference for determining the arm's length price or price range, the standardized contracts which stipulate specifications on the basis of which commodities are traded on the exchange and which result in a quoted price for the commodity may be relevant. Where there are differences between the conditions of the controlled transaction and the conditions of the uncontrolled transactions or the conditions determining the quoted price for the commodity that materially affect the price of the commodity transactions being examined, reasonably accurate adjustments should be made to ensure that the economically relevant characteristics of the transactions are comparable. Contributions made in the form of functions performed, assets used and risks assumed by other entities in the supply chain should be compensated (OECD, 2017).

In order to assist tax administrations in conducting an informed examination of the taxpayer's transfer pricing practices, taxpayers should provide reliable evidence and document, as part of their transfer pricing documentation, the price-setting policy for commodity transactions, the information needed to justify price adjustments based on the comparable uncontrolled transactions or comparable uncontrolled arrangements

represented by the quoted price and any other relevant information, such as pricing formulas used, third party end-customer agreements, discounts applied, pricing date, supply chain information, and information prepared for non-tax purposes (OECD, 2017).

A particularly relevant factor for commodity transactions determined by reference to the quoted price is the pricing date, which refers to the specific time, date or time period (e.g. a specified range of dates over which an average price is determined) selected by the parties to determine the price for commodity transactions. Where the taxpayer can provide reliable evidence of the pricing date agreed by the associated enterprises in the controlled commodity transaction at the time the transaction was entered into (for example, proposals and acceptances, contracts or registered contracts, or other documents setting out the terms of the arrangements may constitute reliable evidence) and this is consistent with the actual conduct of the parties. If the pricing date specified in any written agreement between the associated enterprises is inconsistent with the actual conduct of the parties or with other facts of the case, tax administrations may determine a different pricing date consistent with those other facts of the case and what independent enterprises would have agreed in comparable circumstances (taking into considerations industry practices). When the taxpayer does not provide reliable evidence of the pricing date agreed by the associated enterprises in the controlled transaction and the tax administration cannot otherwise determine a different pricing date (OECD, 2017).

Tax administrations may deem the pricing date for the commodity transaction on the basis of the evidence available to the tax administration; this may be the date of shipment as evidenced by the bill of lading or equivalent document depending on the means of transport. This would mean that the price for the commodities being transacted would be determined by reference to the average quoted price on the shipment date, subject to any appropriate comparability adjustments based on the information available to the tax administration. It would be important to permit resolution of cases of double taxation arising from application of the deemed pricing date through access to the mutual agreement procedure under the applicable Treaty (OECD, 2017).

2.2. INTERNATIONAL TRANSFER PRICING

Transfers within an international group will often be cross-border, between divisions in different countries. With the advent of multinational corporations and their growth, they have added more complicated dimension to transfer pricing. In setting an international transfer price, a multinational company will usually concentrate on satisfying a single objective which is sole on the minimisation of taxation (ICAN, 2009). The other broad objectives of transfer pricing are considered secondary. By minimising income taxes through transfer pricing, the company's profit after tax will increase. However, national tax authorities (i.e. the home and host country of the multinational corporations) are now taking a very close look at whether the international transfer price constitutes an "arm length price". Arm's length price is the price two parties would have agreed to transact business if they had not been related.

Benke and Edwards (1980) recognised some other issues that merit consideration in the setting of transfer pricing by the multinational corporations. These considerations include import duty minimisation, adjusting for currency fluctuations, avoiding economic restrictions and presenting a favourable financial picture for a foreign affiliate in order to enhance borrowing opportunity or provide a temporary competitive edge. Similarly, Lucey (2003) stressed that the level of the transfer price can also affect the amount of import duties to be paid and is a way of repatriating dividends. In fact some countries place restrictions on the amount of dividend that can be paid from the branches of multinational corporations in their country. Where these restrictions exist, it may be partially avoided by charging a high transfer price in the particular country. In his opinion, Adeniyi (2008) posit that multinational corporation can take advantage of different tax rates charged in different jurisdictions to minimise the group's total tax liability. Ways of doing this include the use of transfer pricing to reduce the profitability of subsidiaries in high-tax countries and increase the profitability of its subsidiaries in low-tax countries. He also noted that changes in the transfer price can redistribute the pre-tax profit between subsidiaries, but the total pre-tax profit will be the same. However, if more pre-tax profit is earned in low-tax countries and less profit is earned in high-tax countries, the total tax bill will be decreased.

2.3. MNEs IN AFRICA

Every year African countries lose at least \$50 billion in taxes — more than the amount of foreign development aid. So where is it all going and how can Multinational Enterprises be held to account? NGOs continue to raise the alarm. African countries are being swindled out of billions in tax revenues mainly by large foreign companies in the energy and resource sectors, but also increasingly by small and medium-sized enterprises, such as safari organizers in countries such as Kenya, Tanzania, South Africa and even Egypt.

According to the Organization for Economic Cooperation and Development (2021) (OECD), the annual losses of up to \$50 billion (€44 billion) have actually exceeded the amount of development aid given to Africa in the same amount of time. Meanwhile, the United Nations Economic Commission for Africa (UNECA)

puts the approximation much higher at \$100 billion. Particularly concerning is the fact that this money remains urgently missing from the affected countries, says Lisa Grossmann of the German-based Netzwerk Steuergerechtigkeit (NWSG), a network of NGO's working to tackle tax evasion and shadow economies worldwide. The lack of tax revenue has a negative impact, especially in the poorest countries starting with non-existent transport infrastructure, missing schools or hospitals and a non-functioning public service (DW, 2021). Sub-Saharan Africa is approximated to possess 30 percent of global mineral reserves, representing a major opportunity for the region. Despite the high level of private investment in this critical sector, new analysis finds that many Multinational Enterprises are avoiding paying their taxes. To get a sense of the scale of the investment that companies are making in the region's mining sector consider the case of Guinea. One multinational entity has invested five times more in a single bauxite mine (as a percent of GDP) than the government has spent in total public investment since 2018.

According to IMF (2021) governments in sub-Saharan Africa now under tremendous pressure to raise public spending in response to the pandemic are losing between USD450 and USD730 million per year in corporate income tax revenues as the result of profit shifting by Multinational Enterprises in the mining sector. Targeted policy actions to reduce tax avoidance could help governments regain some of this badly needed tax revenue to aid with the recovery and meet Sustainable Development Goals.

The importance of mining to economies in the region is clear. The mining sector provides about 10 percent to GDP across 15 resource intensive sub-Saharan African countries. In most of these countries, mining exports represent 50 percent of total exports on average and is the main source of foreign direct investment. However, for the 15 resource-intensive economies in the region, revenue from mining accounts for just 2 percent of GDP on average. There are concerns that this level of revenue does not represent a "fair" sharing of the benefits.

Research found that revenues are being reduced in two ways. First, countries try to attract inbound investment by lowering taxes, which has stoked unhealthy regional tax competition. Second, international profit shifting by Multinational Enterprises has reduced the tax base in producing countries.

According to the UN's Economic Commission for Africa's Report on the High Level Panel on Illicit Financial Flows from Africa, there was a US\$40 billion outflow from Africa due to trade mispricing in 2010. With corporate tax rates averaging out at 28 per cent in Africa this equates to nearly \$US11 billion in lost tax revenues. Given that companies and investors from G7 countries are responsible for more than half of the foreign direct investment in Sub-Saharan Africa, companies from G7 countries may be responsible for robbing African governments of around \$6 billion every year from just one tax trick alone. Developing countries lose estimated US\$100billion a year as a result of one set of tax avoidance schemes involving tax havens.

2.4. MARKET BASED TRANSFER PRICE

Under this approach, the relevant transfer price to charge between the selling and buying divisional managers will constitute the prevailing market price within the market as at the date of the transaction. This signifies that both the selling and buying divisional managers are expected to operate at arm's length. A major plus for using this approach is that it ensures divisional autonomy and allows for divisional managers to use their initiative in the pricing decision, which in the long run allows for performance evaluation among the managers. Its disadvantage is that, because of its market nature, it is prone to market fluctuations and will complicate the process of stock valuation as a result of the need to eliminate the unrealised profit on stock.

III. RESEARCH METHODOLOGY

Research is understood as the process of collecting, analyzing, and interpreting data in order to understand a phenomenon (Leedy and Ormrod, 2001). As a process, research is systematic in nature; in that it defines the objective of the study, manages the data, and communicates the findings within the established frameworks and in accordance with existing guidelines.

3.1. RESEARCH APPROACH

There are three main approaches to research, namely; quantitative, qualitative and mixed research (Kothari, 2004). The current research adopted a quantitative approach to collect and analyse data. A quantitative approach is specific in nature, and it builds upon the existing theories (Leedy and Ormrod, 2001). In quantitative research, the intent is to; establish, confirm, or validate relationships and to develop generalizations that contribute to theory (Leedy and Ormrod, 2001; Creswell, 2003). Accordingly, this approach was adopted to validate the correlations among the types of transfer pricing, and to assess the effect of transfer of pricing on tax avoidance.

3.2. RESEARCH DESIGN

A research design is the conceptual structure within which research is conducted; it entails the blueprint for the collection, measurement and analysis of data. As such, the design includes an outline of what the researcher will do from writing the hypothesis and its operational implications to the final analysis of data. More explicitly, the design decisions happen to be in respect of:

- What is the study about?
- Why is the study being made?
- Where will the study be carried out?
- What type of data is required?
- Where the required data can be obtained?
- What periods of time will the study include?
- What will be the sample design?
- What techniques of data collection will be used?
- How will the data be analysed?
- In what style will the report be prepared?

Source: (Kothari, 2004; 32)

In this research, the investigator adopted a quantitative approach to analyse the primary data which was obtained through a questionnaire survey that was distributed to the targeted participants who work in Multinational Enterprises on Zimbabwe. To collect data from the respondents, the research relied on an online survey that was developed on Google forms and then distributed via LinkedIn and email addresses. The targeted participants were selected through a non-probability sampling. Data entry and analysis was then conducted on a Statistical Package for Social Sciences (SPSS Version 20). SPSS software was also used for Descriptive Statistical Analysis, Pearson Correlation Analysis and for Simple Linear Regression.

3.3. DISTRIBUTION FRAME

Table 1: Distribution Frame

Category	Sample Frame	Targeted Sample	Actual Sample
Top Managers	189	84	63
Ordinary Workers	3078	335	316
Total	3267	419	379

Based on table 1, the sample frame was made up of 189 top managers, and 3078 ordinary workers. The researcher targeted 84 top managers and 335 ordinary workers. Out of the targeted sample of 419 participants, 63 top managers responded as well as 316 ordinary workers, making a total of 379 respondents.

3.4. POPULATION AND SAMPLING

In this research, the investigator adopted a quantitative approach to analyze the primary data which was obtained through a questionnaire survey that was distributed to targeted participants who work in Multinational Enterprises in Zimbabwe. The targeted participants were selected through a non-probability sampling.

3.5. PROPOSED MODEL

In his opinion, Adeniyi (2008) entails that multinational corporation can take advantage of different tax rates charged in different jurisdictions to minimize the group's total tax liability. Ways of doing this involve the use of transfer pricing to reduce the profitability of subsidiaries in high-tax countries and increase the profitability of its subsidiaries in low-tax countries. He also noted that changes in the transfer price can redistribute the pre-tax profit between subsidiaries, but the total pre-tax profit will remain the same. If more pre-tax profit is earned in low-tax countries and less profit is earned in high-tax countries, the total tax bill will be reduced. Transfer pricing is arguably a tool or an instrument that is employed by Multinational Enterprises to reduce their overall tax liabilities, which resultantly reduces the tax revenues accruing to government of countries where such companies carry out their business operations. Owing to different types of transfer pricing, it has become increasingly difficult for national tax authorities to assess the income of multinational corporations (Onyeukwu, 2010; Augustine, 2011, Eden, 2001). As such, the following model was developed:

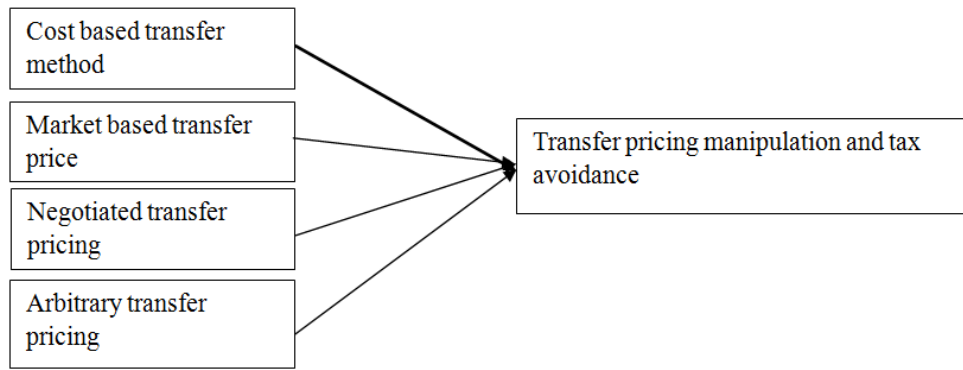


Figure 5: Proposed Model

Based on the proposed model, the following hypotheses were developed:

Hypothesis 1: Cost based transfer method has a positive effect on transfer pricing manipulation and tax avoidance.

Hypothesis 2: Market based transfer pricing has a positive effect on transfer pricing manipulation and tax avoidance.

Hypothesis 3: Negotiated transfer pricing has a positive effect on transfer pricing manipulation and tax avoidance.

Hypothesis 4: Arbitrary transfer pricing has a positive effect on transfer pricing manipulation and tax avoidance.

3.6. REGRESSION MODEL

Different types of transfer pricing have long been used as tools for tax avoidance by multinationals. These involve cost based transfer method, market based transfer price, negotiated transfer pricing, arbitrary transfer pricing (Lucey, 2003; Adeseye, n.d). As such, the independent variables of this study are: cost based transfer method, market based transfer price, negotiated transfer pricing and arbitrary transfer pricing, while transfer pricing manipulation and tax avoidance has been treated as a dependent variable. The independent variables of this study were thus regressed on transfer pricing manipulation and tax avoidance as follows:

$$TPMTA = f(CBTM, MBTP, NTP, ATP)$$

The model was expanded into a linear mathematical relationship as follows:

$$TPMTA = \beta_0 + \beta_1 CBTM + \beta_2 MBTP + \beta_3 NTP + \beta_4 ATP + \epsilon$$

Where,

TPMTA = Transfer Pricing Manipulation and Tax Avoidance

CBTM = Cost Based Transfer Method

MBTP = Market Based Transfer Price

NTP = Negotiated Transfer Pricing

To test the model, a Simple Linear Regression was utilized, and the Pearson correlation analysis was conducted on SPSS Version 20.

IV. DATA ANALYSIS

4.1. DESCRIPTIVE STATISTICS

The survey questionnaires were distributed among the targeted sample of 419 workers from the Multinational Enterprises in Zimbabwe. Out of 419, 379 participants responded. Hence there was 90.45% response rate.

Table 2: Gender of participants

	Gender	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Male	203	53.6	53.6	53.6
	Female	176	46.4	46.4	100
	Total	379	100	100	

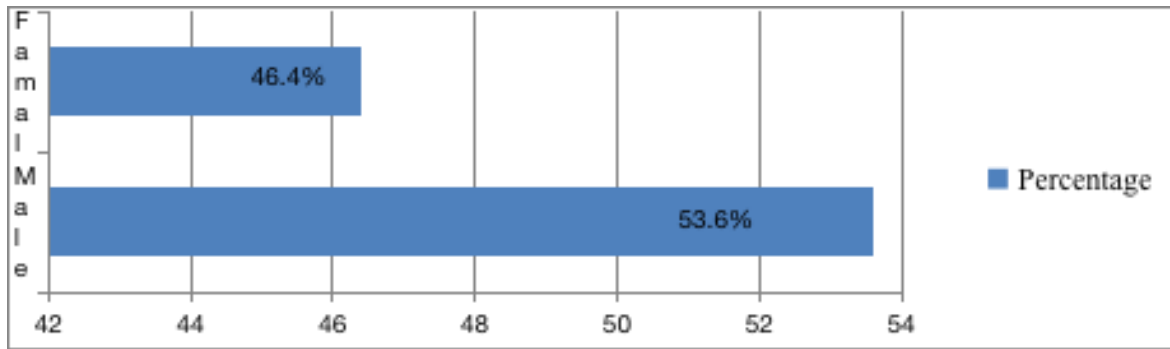


Figure 6: Gender of participants

Out of 379 participants who responded, 203 (53.6%) were males, while 176 (46.4%) were females.

Table 3: Marital Status

	Marital S	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Married	284	74.9	74.9	74.9
	Single	95	25.1	25.1	100
Total		379	100	100	

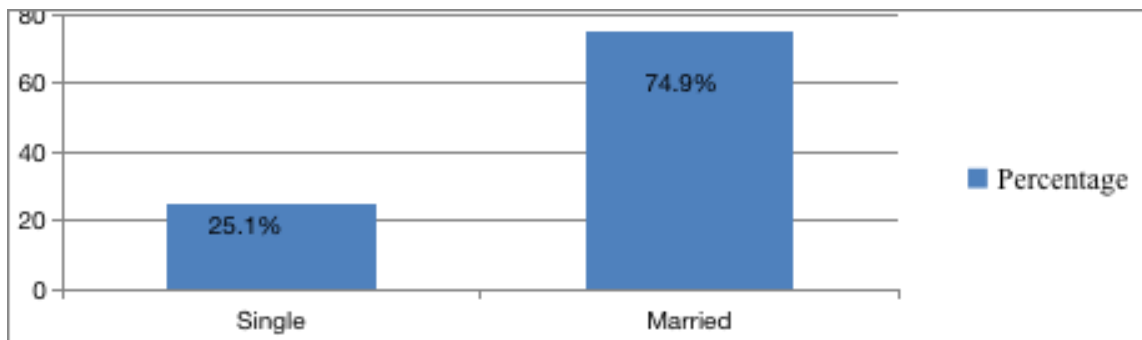


Figure 7: Marital Status

In terms of marital status, 284 (74.9%) respondents were married whereas 95 (25.1%) were single.

Table 4: Education Level

	Education L	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Diploma	173	45.6	45.6	45.6
	Bachelors	150	39.6	39.6	85.2
	Postgraduate	56	14.8	14.8	100
Total		379	100	100	

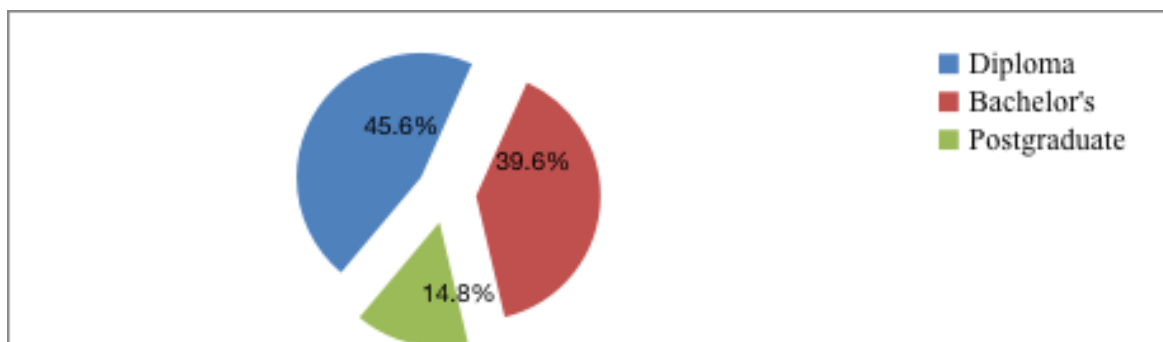


Figure 8: Education Level

In terms of education, 173 (45.6%) respondents were in possession of diplomas, while 150 (39.6%) were holding Bachelors, whereas 56 (14.8%) had reached a postgraduate level.

Table 5: Age of Participants

	Age	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	21 - 30	79	20.8	20.8	20.8
	31 - 40	179	47.2	47.2	68.1
	41 - 50	121	31.9	31.9	100
Total		379	100	100	

79 (20.8%) respondents were aged between 21 and 30, 179 (47.2%) were aged between 31 and 40, while 121 (31.9%) were aged between 41 and 50.

Table 6: Employment History

	Employment	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	5 & below	70	18.5	18.5	18.5
	6 to 10	292	77	77	95.5
	11 to 15	17	4.5	4.5	100
	Total	379	100	100	

Out of 379 respondents, 70 (18.5%) had less than 6 year of employment history, while 292 (77%) respondents had a range of 6 to 10 years of employment history. 17 (4.5%) respondents had a range of 11 to 15 years of employment history.

4.2. PEARSON CORRELATION

As shown in table 1 below, a Pearson Correlation analysis was performed to determine the relationship between the types of transfer pricing:

Table 7: Pearson Correlation

Correlations		CBTM	MBTP	NTP	ATP
CBTM	Pearson Correlation	1			
MBTP	Pearson Correlation	.632**	1		
NTP	Pearson Correlation	.512**	.512**	1	
ATP	Pearson Correlation	.671**	.776**	.592**	1

** Correlation is significant at the 0.01 level (2-tailed).

A significant correlation was found between market based transfer pricing and cost based transfer method at .632**. A significant correlation was found between negotiated transfer pricing and cost based transfer method at .512**. A significant correlation was also found between arbitrary transfer pricing and cost based transfer method at .671**. There is a positive correlation between negotiated transfer pricing and market based transfer pricing at .512**. In addition, there is a positive correlation between arbitrary transfer pricing and market based transfer pricing at .776**. A significant correlation was also obtained between arbitrary transfer pricing and negotiated transfer pricing at .592**. In other words, there is a positive correlation among all the types of transfer pricing that have been highlighted.

4.3. STRATEGIES USED TO MANIPULATE TRANSFER PRICING

Table 8: Strategies used to manipulate transfer pricing

	Strategies	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Tax havens	118	31.1	31.1	31.1
	Debt shifting	185	48.8	48.8	79.9
	Use of Tangibles	76	20.1	20.1	100

Total	379	100	100
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The respondents were asked to indicate the strategies that are used to manipulate transfer pricing, that they are familiar with, between tax havens, debt shifting and use of tangibles. 118 (31.1%) respondents selected tax havens, while 185 (48.8%) respondents selected debt shifting, whereas 76 (20.1%) respondents selected use of tangibles. In other words, most respondents were familiar with tax havens and debt shifting.

4.4. SIMPLE LINEAR REGRESSION

The effect of Cost Based Transfer Method on Transfer Pricing Manipulation and Tax Avoidance

Table 9: Model Summary

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.410a	0.168	0.166	0.65834

a Predictors: (Constant), Cost Based Transfer Method

Table 10: ANOVA

ANOVAa						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	33.027	1	33.027	76.202	.000b
	Residual	163.395	377	0.433		
Total		196.422	378			

a Dependent Variable: Transfer Pricing Manipulation and Tax Avoidance
b Predictors: (Constant), Cost Based Transfer Method

Table 11: Coefficients

Coefficientsa						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.723	0.194		14.014	0.00
	Cost BTM	0.380	0.044	0.41	8.729	0.00

a Dependent Variable: Transfer Pricing Manipulation and Tax Avoidance

Using a Simple Linear Regression, we obtained the R Square of 0.168 and a regression equation of Variable: Transfer Pricing Manipulation and Tax Avoidance = 2.723 + 0.380 (Cost BTM). The ANOVA resulted in F = 76.202 with 1 and 377 degrees of freedom. The F is significant at the level less than .001 level. A significant regression equation was found (F (1, 377) = 76.202, p < .001), with an R Square of 0.168. Hence, it can be concluded that the proposed hypothesis is significant.

The effect of Market Based Transfer Pricing on Transfer Pricing Manipulation and Tax Avoidance

Table 12: Model Summary

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.316a	0.100	0.097	0.68491

a Predictors: (Constant), Market Based Transfer Pricing

Table 13: ANOVA

ANOVAa						
Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	19.573	1	19.573	41.725	.000b
	Residual	176.849	377	0.469		

Transfer Pricing As A Tool For Tax Avoidance By Multinational Enterprises In

Total	196.422	378
a Dependent Variable: Transfer Pricing Manipulation and Tax Avoidance		
b Predictors: (Constant), Market Based Transfer Pricing		

Table 14: Coefficients

Coefficients ^a						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	3.151	0.195		16.126	0.00
	Market BTP	0.286	0.044	0.316	6.46	0.00

a Dependent Variable: Transfer Pricing Manipulation and Tax Avoidance

Using a Simple Linear Regression, we obtained the R Square of 0.100 and a regression equation of Variable: Transfer Pricing Manipulation and Tax Avoidance = 3.151 + 0.286 (Market BTP). The ANOVA resulted in F = 41.725 with 1 and 377 degrees of freedom. The F is significant at the level less than .001 level. A significant regression equation was found (F (1, 377) = 41.725, p < .001), with an R Square of 0.100. Hence, it can be concluded that the proposed hypothesis is significant.

The effect of Negotiated Transfer Pricing on Transfer Pricing Manipulation and Tax Avoidance

Table 15: Model Summary

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.744a	0.554	0.553	0.48207

a Predictors: (Constant), Negotiated Transfer Pricing

Table 16: ANOVA

ANOVA ^a						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	108.81	1	108.81	468.213	.000b
	Residual	87.612	377	0.232		
	Total	196.422	378			

a Dependent Variable: Transfer Pricing Manipulation and Tax Avoidance

b Predictors: (Constant), Negotiated Transfer Pricing

Table 17: Coefficients

Coefficients ^a						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	0.770	0.169		4.546	0.00
	Negotiated TP	0.816	0.038	0.744	21.638	0.00

a Dependent Variable: Transfer Pricing Manipulation and Tax Avoidance

Using a Simple Linear Regression, we obtained the R Square of 0.554 and a regression equation of Variable: Transfer Pricing Manipulation and Tax Avoidance = 0.770 + 0.816 (Negotiated TP). The ANOVA resulted in F = 468.213 with 1 and 377 degrees of freedom. The F is significant at the level less than .001 level. A significant regression equation was found (F (1, 377) = 468.213, p < .001), with an R Square of 0.554. Hence, it can be concluded that the proposed hypothesis is significant.

The effect of Arbitrary Transfer Pricing on Transfer Pricing Manipulation and Tax Avoidance

Table 18: Model Summary

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.478a	0.229	0.227	0.63394

a Predictors: (Constant), Arbitrary Transfer Pricing

Table 19: ANOVA

ANOVAa						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	44.911	1	44.911	111.752	.000b
	Residual	151.511	377	0.402		
Total		196.422	378			

a Dependent Variable: Transfer Pricing Manipulation and Tax Avoidance
b Predictors: (Constant), Arbitrary Transfer Pricing

Table 20: Coefficients

Coefficientsa						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.512	0.181		13.888	0.00
	Arbitrary TP	0.431	0.041	0.478	10.571	0.00

a Dependent Variable: Transfer Pricing Manipulation and Tax Avoidance

Using a Simple Linear Regression, we obtained the R Square of 0.229 and a regression equation of Variable: Transfer Pricing Manipulation and Tax Avoidance = 2.512 + 0.431 (Arbitrary TP). The ANOVA resulted in F = 111.752 with 1 and 377 degrees of freedom. The F is significant at the level less than .001 level. A significant regression equation was found (F (1, 377) = 111.752, p < .001), with an R Square of 0.229. Hence, it can be concluded that the proposed hypothesis is significant.

V. CONCLUSION

5.1. RECOMMENDATIONS AND IMPLICATIONS

Although it is said to be unethical, transfer pricing should be embraced by MNEs because it helps in reducing duty costs by shipping goods into countries with high tariff rates through using low transfer prices so that the duty base of such transactions is lowered.

It also helps in reducing income and corporate taxes in high tax countries by overpricing goods that are transferred to countries with lower tax rates, and thereby assisting companies to obtain higher profit margins.

However, to some extent it should be discouraged because:

1. There can be conflicts within the divisions of an organization regarding the policies on pricing and transfer.
2. Lots of extra costs are incurred in terms of time and manpower required in executing transfer prices and maintaining a proper accounting system to support them. Transfer pricing is a very complicated and time-consuming methodology.
3. It gets difficult to establish prices for intangible items such as services rendered, which are not sold externally.
4. Sellers and buyers perform individual functions and, thus, assume different types of risks. For instance, the seller may refuse to provide a warranty for the product. But the price paid by the buyer would be affected by the difference.

5.2. LIMITATIONS

The focal point of the research is on the transfer pricing in Zimbabwe, and is limited to transfer pricing across borders transactions by MNEs, therefore Zimbabwe is representing other developing countries in this transfer

pricing issue. Tax avoidance was not considered in detail as there is a vast body of knowledge on this subject. The major limitation of this study was gaining access to participants willing to answer the questionnaires and participate in the study. From the questionnaires filled some participants were withholding information they thought by responding fully they would be exposing themselves to their competitors in the market. In some instances the employees did not understand the concept of transfer pricing.

5.3. CONCLUSIONS

Transfer pricing refers to the prices of goods and services that are exchanged between companies under common control. Enterprises under common control refer to those that are ultimately controlled by a single parent corporation. Multinational corporations use transfer pricing as a method of allocating profits (earnings before interest and taxes) among their various subsidiaries within the organization. Transfer pricing has been, and continues to be, the tool through which corporations are shifting their income to low-tax jurisdictions and in some cases to no-tax regions. As business develops, more and more complex business transactions are created, and the lack of current legislation to prevent these transactions, creates an opportunity for excessively aggressive tax avoidance.

Transfer pricing methods offer many advantages for a company from a taxation perspective, although regulatory authorities often frown upon the manipulation of transfer prices to avoid taxes. Effective but legal transfer pricing takes advantage of different tax regimes in different countries by raising transfer prices for goods and services produced in countries with lower tax rates.

In some cases, companies even lower their expenditure on interrelated transactions by avoiding tariffs on goods and services exchanged internationally. International tax laws are governed by the Organization for Economic Cooperation and Development (OECD) and the auditing firms under OECD review and audit the financial statements of MNEs accordingly.

Based on the results of the study, most respondents were aware of the types of transfer pricing and the strategies that are used to manipulate transfer pricing. The results indicate that there is a positive correlation among the types of transfer pricing.

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