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Transfer Pricing as an Instrument of Tax Avoidance in Multinational Corporations: Challenges in Law Enforcement and the Implementation of the Arm's Length Principle in Indonesia

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Abstract
The development of economic globalization has encouraged increased activity of multinational companies operating across jurisdictions, thus opening up opportunities for tax avoidance practices through transfer pricing mechanisms. This practice is often used to move profits from countries with high tax rates to countries with lower tax rates, which in the end can reduce state revenues and lead to injustice in the tax system. This research aims to analyze the legal enforcement mechanism for tax avoidance practices through transfer pricing in multinational companies based on Minister of Finance Regulation Number 172 of 2023 and identify the juridical obstacles faced by the Directorate GeneralTax in its application.The research method used is normative juridical legal research with a qualitative approach through literature study of statutory regulations, legal literature and related documents. The research results show that law enforcement against transfer pricing practices in Indonesia is carried out through administrative mechanisms which include the stages of monitoring at-risk taxpayers, examining transfer pricing, determining fiscal corrections, issuing Tax Assessment Letters, as well asdispute resolution through objections and appeals to the Tax Court.Even though regulations have been updated through PMK Number 172 of 2023 by adopting the arm's length principle in accordance with international standards, its implementation still faces legal obstacles such as limitations in harmonization of domestic regulations with international standards and structural complexitymultinational company.Therefore, it is necessary to strengthen regulations and institutional capacity to increase the effectiveness of supervision and enforcement of transfer pricing laws in Indonesia.

INTRODUCTION

The development of economic globalization has significantly increased the activities of multinational corporations operating across jurisdictions. The integration of international markets, technological advancements, and investment liberalization have enabled companies to move capital, production, and profits relatively easily between countries. This condition has important implications for national tax systems, particularly in determining taxing rights over corporate profits earned in more than one jurisdiction. A major issue arises when multinational corporations exploit differences in tax rates between countries to reduce their global tax burden through tax avoidance schemes. Such practices are often carried out through transfer pricing mechanisms, namely the determination of transaction prices between entities that have special relationships within the same corporate group.[1]

Transfer pricing is fundamentally a legitimate and necessary practice in multinational business operations, as transactions between entities within the same group are unavoidable. These transactions may include the sale of goods, provision of services, use of intangible assets, and financing arrangements. However, in practice, transfer pricing is frequently used as a tax planning instrument to shift profits from high-tax jurisdictions to low-tax jurisdictions. This situation leads to base erosion and profit shifting, which ultimately reduces government tax revenues.[2]

The phenomenon of tax avoidance through transfer pricing has become a global issue. The Organisation for Economic Co-operation and Development (OECD), through its Base Erosion and Profit Shifting (BEPS) project, emphasizes that profit-shifting practices by multinational corporations result in significant losses of potential tax revenues for countries, particularly developing nations. Developing countries are generally more vulnerable due to limited tax administrative capacity and their reliance on taxation as a primary source of state revenue. In this context, transfer pricing regulation becomes a crucial instrument in maintaining fiscal sovereignty and fairness.[3]

Indonesia, as a developing country with substantial foreign investment inflows, faces similar challenges. The realization of foreign direct investment (FDI) in Indonesia exceeded IDR 1,200 trillion in 2022, indicating the high level of multinational corporate activity across various economic sectors. While such investment has the potential to

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[1] Zikri, F. N., & Winarningsih, S. *"Pengaruh Beban Pajak, Mekanisme Bonus, dan Tunneling Incentive terhadap Keputusan Transfer Pricing."* Jurnal Penelitian Ilmu Manajemen, Vol. 8, No. 1, (2023), p. 45–56.

[2] Vasini, N. N., et al.*"Transfer Pricing from the Perspective of Tax Planning"*. E-Jurnal Akuntansi Universitas Udayana, Vol. 34, No. 2, (2024), p. 310–325.

[3]OECD. *"Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations"*.

increase the tax base, it also creates opportunities for tax avoidance through cross-border related-party transactions.[4]

One notable case in Indonesia involving tax avoidance through related-party transactions is the case of PT Adaro Energy Tbk. According to reports from international institutions, Adaro's subsidiary in Singapore was allegedly involved in acting as an intermediary in coal sales at prices lower than market value, thereby shifting profits that should have been taxed in Indonesia to a jurisdiction with lower tax rates. This practice was suspected to have caused significant losses in potential tax revenues over several years.[5]

This case illustrates that transfer pricing is not merely a theoretical issue but a real and pressing concern within Indonesia's tax system. The disputes arising from such cases reveal differences in interpretation between taxpayers and tax authorities regarding the application of the arm's length principle and transfer pricing documentation. This condition underscores the importance of legal certainty and the strengthening of regulations and oversight over cross-border related-party transactions.

In the domestic context, various empirical studies indicate that transfer pricing is often associated with corporate tax avoidance practices. Research on manufacturing companies and other sectors in Indonesia shows that transfer pricing is used as a strategy to shift profits and reduce tax burdens. This strengthens the indication that related-party transactions are not always conducted based on the arm's length principle but are also influenced by tax-saving motives.[6]

Tax avoidance through transfer pricing has serious implications for state revenue. Taxation is the primary source of funding for national development; thus, profit-shifting practices can undermine the government's ability to provide public services. Moreover, such practices create horizontal inequity in the tax system, as multinational corporations may pay lower taxes compared to domestic firms that lack cross-border networks. This condition may also lead to distortions in market competition.[7]

From a tax law perspective, tax avoidance must be distinguished from tax evasion. Tax avoidance refers to efforts to reduce tax liabilities by exploiting loopholes or weaknesses in tax regulations without directly violating the law. In contrast, tax evasion involves illegal and manipulative actions that breach legal provisions and may result in

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[4] Rolnmuch, T. P. N. A., & Astuti, Y. *"Analysis of FDI into Indonesia"*. (2024).
[5] Global Witness, *"Adaro's Off-shore Coals Profits"* (2019)
[6] Anggriani, E. P., & Dalimunthe, H. *"Pengaruh Pajak dan Mekanisme Bonus terhadap Transfer Pricing pada Perusahaan Manufaktur."* Jurnal Riset Perpajakan dan Keuangan Publik, Vol. 2, No. 1, (2024), p. 112–124.
[7] Jumliana, M., et al. "Transfer Pricing dan Praktik Penghindaran Pajak pada Perusahaan Multinasional." Jurnal Pabean dan Perpajakan, Vol. 6, No. 2, 2024, p. 87–101.

criminal sanctions. In practice, transfer pricing often falls within a gray area between these two concepts, thereby requiring strict regulation and supervision.[8]

Indonesia's Income Tax Law stipulates that a special relationship may arise due to share ownership, management control, or family ties. Under such conditions, tax authorities are authorized to re-determine income and expenses in accordance with the arm's length principle. This principle requires that transactions between related parties be treated as if they were conducted between independent parties under comparable circumstances.[9]

The arm's length principle is an international standard applied in transfer pricing regulation. In Indonesia, this principle is governed by various regulations, including PER-22/PJ/2013, PER-43/PJ/2010 as amended by PER-32/PJ/2011, and transfer pricing documentation requirements under PMK-213/2016. These regulations govern methods for determining fair prices, documentation obligations, and audit procedures by the Directorate General of Taxes.[10]

The methods used to determine arm's length prices in transfer pricing include:

1. Comparable Uncontrolled Price (CUP)
2. Resale Price Method (RPM)
3. Cost Plus Method (CPM)
4. Transactional Net Margin Method (TNMM)
5. Profit Split Method (PSM)

These methods are intended to ensure that related-party transaction prices reflect those that would prevail in an open market.[11]

However, in practice, the application of the arm's length principle is not always straightforward. The main challenges include the availability of comparable data, the complexity of multinational corporate structures, and the valuation of intangible assets, which are often difficult to assess objectively. These factors make transfer pricing disputes among the most complex and frequently occurring tax disputes worldwide, including in Indonesia.[12]

To strengthen oversight of transfer pricing practices, the Indonesian government issued Minister of Finance Regulation No. 172 of 2023. This regulation aims to provide

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[8] Mardiasmo. "*Perpajakan*". Yogyakarta. (2019)
[9] Pasal 18 Ayat (4) Undang-Undang Nomor 7 Tahun 2021 tentang Pajak Penghasilan.
[10] Peraturan Direktorat Jenderal Pajak 22 Tahun 2013 tentang pedoman Pemeriksaan Terhadap Wajib Pajak yang Mempunyai Hubungan Istimewa.
[11] OECD. "Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations".
[12] Vasini, N. N., et al. *"Transfer Pricing from the Perspective of Tax Planning."* E-Jurnal Akuntansi Universitas Udayana, Vol. 34, No. 2, (2024), p. 310–325.

legal certainty, fairness, and ease in the implementation of taxpayers' rights and obligations, particularly concerning related-party transactions. It also reinforces transfer pricing documentation requirements as a means of proving compliance with the arm's length principle.[13]

Minister of Finance Regulation No. 172 of 2023 is part of Indonesia's effort to harmonize its tax policies with international standards, particularly the OECD's BEPS recommendations. One of its key focuses is enhancing transparency through mandatory transfer pricing documentation, including the master file, local file, and country-by-country report. This policy is expected to strengthen the capacity of the Directorate General of Taxes in detecting profit-shifting practices.[14]

Nevertheless, prior studies indicate that transfer pricing practices are still frequently associated with tax avoidance efforts. Empirical studies on manufacturing firms and other sectors in Indonesia show that related-party transactions are often utilized to shift profits and reduce tax burdens. However, most of these studies tend to focus on empirical and quantitative aspects, such as the impact of transfer pricing on tax avoidance, without thoroughly examining the normative aspects related to regulatory effectiveness and enforcement mechanisms.

This issue suggests that transfer pricing regulation requires not only clear normative rules but also effective law enforcement mechanisms. Law enforcement in this context includes tax audits, fiscal adjustments, objections, and dispute resolution before the Tax Court. Each of these stages requires a strong legal foundation and adequate institutional capacity. Although Minister of Finance Regulation No. 172 of 2023 governs the application of the arm's length principle in related-party transactions, particularly transfer pricing in Indonesia, existing legal studies remain largely limited to analyses of regulations prior to the latest policy reforms.[15] As a result, they do not fully reflect the current development of positive law. On the other hand, studies on the implementation of the arm's length principle in enforcement practices remain partial and have not comprehensively integrated an analysis of the juridical challenges faced by tax authorities.

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[13]Niang, L. S., & Arsjah, R. J. *"Pengaruh Transaksi Hubungan Istimewa terhadap Kewajiban Dokumentasi Transfer Pricing Berdasarkan PMK 172 Tahun 2023."* Jurnal Riset Lembaga Administrasi Bisnis, Vol. 5, No. 1, (2024), p. 15–28..
[14] OECD. BEPS Action 13: "Transfer Pricing Documentation and Country-by-Country Reporting"
[15] Kementerian Keuangan Republik Indonesia. Peraturan Menteri Keuangan Nomor 172/PMK.03/2023 "*tentang Penerapan Prinsip Kewajaran dan Kelaziman Usaha dalam Transaksi yang Dipengaruhi Hubungan Istimewa*".

Based on the foregoing discussion, there is a significant research gap, namely the absence of comprehensive studies analyzing the effectiveness of law enforcement against transfer pricing practices under Minister of Finance Regulation No. 172 of 2023, particularly from a normative legal perspective. In addition, there is still limited research that systematically examines the juridical challenges faced by the Directorate General of Taxes in applying the arm's length principle to multinational corporations in Indonesia.

This issue indicates that the existence of adequate regulations does not necessarily guarantee effective implementation. Law enforcement in the context of transfer pricing depends not only on the clarity of legal norms but also on institutional capacity, the availability of comparable data, and the harmonization between national law and international standards.

Therefore, this study is important as it focuses on a normative analysis of transfer pricing law enforcement mechanisms based on Minister of Finance Regulation No. 172 of 2023. It also aims to identify and analyze the juridical challenges encountered in the implementation of the arm's length principle. Accordingly, this research is expected to contribute academically to the development of tax law and to serve as an evaluative reference for the effectiveness of tax policies in addressing tax avoidance practices in Indonesia.

METHODS

This study constitutes normative juridical legal research employing a qualitative approach. The normative juridical method is applied because this research focuses on examining the norms of positive law governing tax avoidance practices through transfer pricing mechanisms, particularly within the framework of Indonesia's tax regulations.[16] Normative legal research positions law as a system of norms; therefore, its primary objects of analysis are legal rules, legal principles, and legal doctrines relevant to the issue under study. The approaches used in this research include the statute approach, the conceptual approach, and the case approach. The statute approach is conducted by reviewing various regulations related to transfer pricing and tax avoidance, such as the Income Tax Law and its implementing regulations. The conceptual approach is employed to examine legal concepts such as tax avoidance, the arm's length principle, and related-party relationships based on the views of legal scholars. Meanwhile, the case approach is

[16] Johnny Ibrahim, *Teori dan Metodologi Penelitian Hukum Normatif,* (Malang: Bayumedia Publishing, 2022), p. 46.

carried out by analyzing concrete cases related to transfer pricing practices in order to understand the application of legal norms in practice.

The type of data used in this research is secondary data, consisting of primary legal materials, secondary legal materials, and tertiary legal materials. Primary legal materials include statutory regulations, such as the Income Tax Law and regulations related to transfer pricing, including Minister of Finance Regulation No. 172 of 2023. Secondary legal materials comprise legal literature, books, academic journals, and previous research findings relevant to the research topic. Tertiary legal materials include legal dictionaries, encyclopedias, and other sources used to support the understanding of legal terms and concepts applied in this study.[17]

The technique for collecting legal materials is conducted through library research, namely by identifying, gathering, and examining various legal sources relevant to the research problem. This process is carried out systematically to obtain comprehensive data that supports the legal analysis undertaken.[18] Furthermore, the collected legal materials are analyzed using qualitative analysis methods. The analysis is conducted by classifying, examining, and interpreting the legal materials in a systematic, logical, and argumentative manner.[19] This analytical process aims to identify the relationship between applicable legal norms and the issues under study, as well as to evaluate the effectiveness of the implementation of legal provisions related to transfer pricing in practice. The results of the analysis are then presented in a descriptive-analytical form to produce conclusions that are aligned with the objectives of the research.[20]

RESULT AND DISCUSSION

1. Law Enforcement Mechanisms Against Tax Avoidance Practices Through Transfer Pricing Based On Minister Of Finance Regulation No. 172 Of 2023

Law enforcement against tax avoidance practices through transfer pricing in Indonesia is essentially part of tax administrative law enforcement. This system is based on the self-assessment principle, as stipulated in Article 3 paragraph (1) of the Income Tax Law, as amended (most recently by Law No. 36 of 2008), under which taxpayers are

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[17] Zainal Asikin dan Amiruddin, *Pengantar Metode Penelitian Hukum,* (Depok: RajaGrafindo Persada, 2023), p. 21.
[18] Dyah Ochtorina Susanti dan A'an Efendi, *Penelitian Hukum (Legal Research),* (Jakarta: Sinar Grafika, 2022), p. 54.
[19] Irwansyah, *Penelitian Hukum: Pilihan Metode dan Praktik Penulisan Artikel*, (Yogyakarta: Mirra Buana Media, 2021), p. 67.
[20] Achmad Ali, *"Menguak Metode Penelitian Hukum Normatif,"* Jurnal Hukum dan Peradilan, Vol. 11 No. 2 (2023), p. 189.

entrusted to calculate, pay, and report their own taxes, while remaining subject to supervision by the Directorate General of Taxes.[21]

The legal basis for transfer pricing regulation is found in Article 18 paragraph (3) of the Income Tax Law, which grants tax authorities the power to re-determine income, deductions, and tax liabilities for taxpayers with related-party relationships, in accordance with the arm's length principle.

This provision is further elaborated in Minister of Finance Regulation No. 172 of 2023 concerning the Application of the Arm's Length Principle in Transactions Influenced by Related-Party Relationships. This regulation serves as the latest technical framework governing monitoring, auditing, and adjustments of transfer pricing transactions, and represents the implementation of the arm's length principle in line with OECD international standards.[22]

In general, the law enforcement mechanism against transfer pricing practices in Indonesia can be divided into five main stages as follows:

a. Monitoring of Taxpayers with Transfer Pricing Risk

The first stage in law enforcement is the monitoring of taxpayers who are considered to have transfer pricing risks. This supervision is carried out by tax authorities through profiling and risk analysis. Article 5 of Minister of Finance Regulation No. 172 of 2023 provides the legal basis for such supervision, including the analysis of the fairness of prices or profits in related-party transactions.[23]

The monitoring process includes:

1) Taxpayer Profiling

Tax authorities conduct profiling of taxpayers suspected of having related-party relationships. This includes analysis of shareholding structures, control relationships, and transactions among entities within the same group. Profiling is essential because

[21] Silmi Latifah, U. *"Pengaruh Kepatuhan Pembayaran Pajak dengan Sistem Self Assessment pada Masyarakat Indonesia."* Jurnal Hukum Lex Generalis, Vol. 6, No. 8, 2025. https://doi.org/10.56370/jhlg.v6i4.1149

[22] Kementerian Keuangan Republik Indonesia. Peraturan Menteri Keuangan Nomor 172/PMK.03/2023 tentang *Penerapan Prinsip Kewajaran dan Kelaziman Usaha dalam Transaksi yang Dipengaruhi Hubungan Istimewa.*

[23] Paor, Hilarius Oswaldo, dan Hartono. *"Implementasi Kebijakan PMK 172/2023 tentang Dokumentasi Transfer Pricing dalam Meningkatkan Transparansi Pelaporan Pajak dan Kepatuhan Wajib Pajak di Indonesia."* Jurnal Reformasi Administrasi 12, no. 1 (2025).

multinational corporations typically operate through complex networks across multiple jurisdictions.[24]

2) Identification of Related-Party Transactions

Following profiling, tax authorities identify transactions between related parties, such as the sale of goods, provision of services, royalty payments, and intra-group loans. These transactions may be used as mechanisms for shifting profits to lower-tax jurisdictions.[25]

3) Financial Statement Analysis

Tax authorities analyze the taxpayer's financial statements to assess profit levels, cost structures, and comparisons with similar industries. This analysis aims to detect anomalies in financial performance.[26]

4) Financial Ratio Analysis

In addition to financial statements, tax authorities evaluate financial ratios such as gross profit margin, operating margin, and return on assets. If these ratios fall significantly below industry standards, the taxpayer may be classified as high risk for transfer pricing practices.[27]

According to OECD reports, profit-shifting practices result in global tax losses of USD 100–240 billion annually, or approximately 4–10% of global corporate tax revenues. This figure remains widely cited as a global benchmark, highlighting the importance of monitoring as a crucial stage in transfer pricing enforcement.[28]

b. Transfer Pricing Audit (Tax Audit)

Pursuant to Articles 10–20 of Minister of Finance Regulation No. 172 of 2023, if monitoring indicates potential irregularities, tax authorities will conduct a tax audit. The

[24] Ardiansyah & Muhammad Ichsan,*"Analisis Penyelesaian Sengketa Pajak Terkait Perhitungan Transfer Pricing (Studi Kasus antara Direktorat Jenderal Pajak dan Perusahaan Multinasional)"* IBLAM Law Review, Vol. 4, No. 2, 2024. p. 1-14

[25] Zefanya, A., & Kennedy, P. S. J., *"Tinjauan Regulasi Hubungan Istimewa dan Prinsip Kewajaran dan Kelaziman Usaha dalam Penerapan Dokumen Transfer Pricing dari Sudut Pandang Perpajakan,"* Jurnal Manajemen, Vol 11, No 3, Tahun 2024, hal 45–60.

[26] Ginanjar, Achmad, & Wibowo, Agung Septia, *"Data Mining to Detect Fraud Patterns in a Taxpayer's Financial Statement,"* Scientax: Jurnal Kajian Ilmiah Perpajakan Indonesia, Vol 6, No 2, 2025, hal 135–150.

[27] Suhermanto, Putri Amanda, & Mardjono, Enny Susilowati, *"Penghindaran Pajak Dilihat dari Sisi Transfer Pricing, Return on Asset, dan Ukuran Perusahaan,"* CURRENT: Jurnal Kajian Akuntansi dan Bisnis Terkini, Vol 6, No 1, 2025, p. 1–13.

[28] Organisation for Economic Co-operation and Development (OECD). *"A Decade of the BEPS Initiative: An Inclusive Framework Stocktake Report to G20 Finance Ministers and Central Bank Governors"*. OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris. 2025

purpose of a transfer pricing audit is to assess whether the pricing or profit in related-party transactions complies with the arm's length principle.[29]

The audit process includes:

1) Analysis of Related-Party Relationships

Tax authorities first verify the existence of a related-party relationship, as regulated under Article 18 of the Income Tax Law and Minister of Finance Regulation No. 172 of 2023.[30] Such relationships may arise from share ownership, management control, or family ties.

2) Functional, Asset, and Risk Analysis (FAR Analysis)

FAR analysis is a key method in transfer pricing audits. It evaluates the functions performed by each entity, the assets utilized, and the risks assumed. The objective is to determine the economic position of each party involved in the transaction.[31]

3) Testing the Arm's Length Nature of Transfer Prices

Tax authorities assess whether the applied transfer prices are reasonable by comparing them with prices between independent parties, industry margins, and available comparable data.

4) Selection of Transfer Pricing Method

Article 12 paragraph (1) of Minister of Finance Regulation No. 172 of 2023 stipulates the acceptable transfer pricing methods, including:

a) Comparable Uncontrolled Price (CUP)
b) Resale Price Method (RPM)
c) Cost Plus Method (CPM)
d) Transactional Net Margin Method (TNMM)
e) Profit Split Method (PSM)

The method selection must follow the most appropriate method principle, meaning the method chosen must best reflect the characteristics of the transaction, the functions and risks of the parties, and the availability and reliability of comparable data.

[29] Tambunan, Maria R. U. D., *"A Note to Transfer Pricing Audit Performance by Indonesia's Tax Administration Based on Tax Court Decision 2015-2019 on Manufacturing Industry,"* Jurnal Akuntansi dan Auditing Indonesia, Vol. 24, No. 2, 2025. p. 86-96.

[30] Liem Sien Niang & Arsjah, Regina Jansen, *"Pengaruh Transaksi Hubungan Istimewa, Transfer Pricing terhadap Kepatuhan Wajib Pajak dengan PMK172/2023 sebagai Pemoderasi,"* Jurnal Lentera Bisnis, Vol. 14, No. 2, 2025. p. 2123-2137

[31] Sugondo, Winarto; Dewi, Iryani; & Setiawan, Puguh Aji Hari, *"Transfer Pricing dalam Hukum Bisnis Indonesia: Mewujudkan Keadilan pada Transaksi Pihak Berelasi,"* Jurnal Kertha Semaya, Vol. 13, No. 10, (2025), p. 2200–2213.

c. Determination of Transfer Pricing Adjustments

Under Article 25 of Minister of Finance Regulation No. 172 of 2023, if the audit concludes that transfer prices are not at arm's length, tax authorities are authorized to make fiscal adjustments.

These adjustments may include:

1) Increase in Income

Tax authorities increase the taxpayer's income if sales to related parties are undervalued.

2) Adjustment of Gross Profit

If the cost of goods sold is inflated due to related-party transactions, the gross profit may be adjusted.

3) Adjustment of Operating Margin

Tax authorities may adjust the operating margin to align with industry standards.[32]

These adjustments aim to restore the taxpayer's profit position as if the transactions had been conducted with independent parties. Studies indicate that most transfer pricing disputes in Indonesia arise from disagreements over operating margin adjustments.

d. Issuance of Tax Assessment Letter (SKP)

Following the adjustments, tax authorities issue a Tax Assessment Letter (Surat Ketetapan Pajak/SKP) as an administrative legal instrument.

Common types of SKP in transfer pricing cases include:

1) SKPKB (Underpaid Tax Assessment Letter)

Issued when there is a tax underpayment resulting from transfer pricing adjustments.

2) SKPKBT (Additional Underpaid Tax Assessment Letter)

Issued when new data reveals additional tax liabilities.

Articles 13–14 of the General Provisions and Tax Procedures Law provide the legal basis for the state to collect unpaid taxes.[33]

e. Legal Remedies Available to Taxpayers

Since transfer pricing enforcement is administrative in nature, taxpayers are granted the right to pursue legal remedies.

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[32] Sugondo, Winarto; Dewi, Iryani; & Setiawan, Puguh Aji Hari, *"Transfer Pricing dalam Hukum Bisnis Indonesia: Mewujudkan Keadilan pada Transaksi Pihak Berelasi*

[33] Mundhofar, Abdul; Utama, Deaby Anugrah; Mursidah, Ita; Soelistyono, Nico E.; & Purwadi, Windyo. *"Permasalahan Surat Ketetapan Pajak Kurang Bayar (SKPKB) terhadap Pajak Penghasilan (Kajian Putusan Pengadilan Pajak Nomor: PUT-013567.99/2020/PP/M.VIIIA Tahun 2022),"* Jurnal IKAMAKUM, Vol. 3, No. 1, 2021. p. 587-598.

These include:

1) Objection

Taxpayers may file an objection with the Directorate General of Taxes against the SKP.

2) Appeal to the Tax Court

If the objection is rejected, taxpayers may file an appeal with the Tax Court.

3) Judicial Review to the Supreme Court

Decisions of the Tax Court may be challenged through a judicial review before the Supreme Court.[34]

This mechanism demonstrates that tax law enforcement primarily emphasizes an administrative approach as the main instrument for ensuring taxpayer compliance. Under the self-assessment system, the state entrusts taxpayers with the responsibility to calculate, pay, and report their tax obligations. Therefore, in cases of non-compliance, the initial response by tax authorities generally involves administrative measures, such as tax audits, issuance of tax assessments, imposition of administrative sanctions in the form of interest or fines, and active collection measures.

This administrative approach reflects the corrective and restorative nature of tax law, which aims to recover state revenue losses and encourage voluntary compliance, rather than merely to punish. Accordingly, tax law enforcement is not automatically directed toward criminalization of every violation but instead considers proportionality and the degree of taxpayer fault.

However, if during supervision or audit there is evidence of criminal elements—such as intentional concealment of income, falsification of documents, or manipulation of transactions to evade taxes—law enforcement may escalate into the realm of criminal tax law. In such cases, tax authorities may conduct investigations and bring the matter before criminal courts. In other words, criminal tax law functions as an ultimum remedium, or a last resort, applied only when administrative mechanisms are insufficient or when the violation clearly constitutes a serious tax offense.

2. Juridical Constraints Faced By The Directorate General Of Taxes In Addressing Transfer Pricing Practices

Law enforcement against transfer pricing practices in Indonesia is, in principle, supported by a relatively strong legal foundation within the national tax system. Transfer pricing is often utilized by multinational corporations to shift profits to jurisdictions with lower tax rates, thereby creating the potential for tax avoidance. Therefore, the

[34] Aulia, Ismiani & Machdar, Nera Marinda. "*Upaya Hukum dalam Penyelesaian Sengketa Pajak pada Pengadilan Pajak: Suatu Perspektif Keadilan,*" Jurnal Sinomika, Vol. 8, No. 2, 2023. p. 603-619.

government, through the tax authority, has established various legal provisions to ensure that transactions between related parties are conducted in accordance with the arm's length principle.

Normatively, the regulation of transfer pricing in Indonesia is primarily based on Law No. 7 of 1983 concerning Income Tax, as amended several times, most recently by Law No. 7 of 2021 on Tax Harmonization. Article 18 paragraph (3) of this law stipulates that the Director General of Taxes is authorized to re-determine the amount of income or expenses for taxpayers engaged in related-party transactions in accordance with the arm's length principle. This provision provides an attribution of authority to the Directorate General of Taxes to make fiscal adjustments to transactions that do not reflect fair market value.[35]

In addition, taxpayers' administrative obligations are governed by Law No. 6 of 1983 concerning General Provisions and Tax Procedures, as most recently amended by Law No. 7 of 2021 on Tax Harmonization. This law regulates taxpayer obligations related to registration, reporting, bookkeeping, as well as administrative and criminal sanctions for non-compliance. More technically, the implementation of the arm's length principle is regulated under Minister of Finance Regulation No. 172 of 2023, which governs transfer pricing methods, documentation requirements, and mechanisms for fiscal adjustments in related-party transactions.

Despite this comprehensive regulatory framework, in practice the Directorate General of Taxes still faces various juridical constraints in addressing transfer pricing practices. These constraints relate to regulatory harmonization, the complexity of evidentiary processes, and the existence of international tax treaties that influence the authority of tax officials to make fiscal adjustments. In general, these juridical constraints can be classified into several key aspects as follows.

Disharmony between Domestic Regulations and International Standards. One of the primary juridical constraints in enforcing transfer pricing rules is the lack of optimal harmonization between domestic tax regulations and international standards. In international practice, transfer pricing standards refer to the guidelines issued by the Organisation for Economic Co-operation and Development (OECD), namely the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations.[36]

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[35]Sugondo, Winarto, Dewi Iryani, dan Puguh Aji Hari Setiawan. "*Transfer Pricing dalam Hukum Bisnis Indonesia: Mewujudkan Keadilan pada Transaksi Pihak Berelasi.*" Kertha Semaya: Journal Ilmu Hukum, Vol 13, No. 10 (2025) p. 2200–2213.

[36] Sari, N. P., & Pratiwi, R.. Apakah transfer pricing documentation meningkatkan kepatuhan pajak? Jurnal Pajak dan Keuangan Negara, Vol 4, No 1, (2022), p. 245-252

These guidelines emphasize that transactions between related parties must adhere to the arm's length principle, meaning that prices should reflect those agreed upon between independent parties under comparable market conditions. This principle also highlights the importance of functional analysis, which evaluates the functions performed, assets used, and risks assumed by each party involved in the transaction.

Indonesia has essentially adopted these principles, particularly through Law No. 7 of 2021 on Tax Harmonization and Minister of Finance Regulation No. 172 of 2023. However, not all OECD approaches have been fully implemented. For example, Indonesia introduces safe harbor rules for certain transactions (such as distribution activities), whereas the OECD, as outlined in the 2022 Transfer Pricing Guidelines (Chapter IV, Section E, paragraphs 4.101–4.106), defines safe harbors as simplification measures primarily intended for low-risk transactions or small taxpayers to reduce administrative burdens. In addition, the OECD places significant emphasis on global minimum taxation (Pillar Two) through mechanisms such as the Qualified Domestic Minimum Top-up Tax (QDMTT). While the OECD stresses flexibility through the "most appropriate method" rule, Indonesia's PMK 172/2023, particularly Article 28, imposes more progressive sanctions for delays in transfer pricing documentation, compared to the OECD's more voluntary compliance-based approach.[37]

These differences in approach often lead to divergent interpretations between tax authorities and taxpayers, particularly multinational corporations that tend to rely on OECD standards in formulating their transfer pricing policies. Consequently, when the Directorate General of Taxes makes fiscal adjustments to related-party transactions, taxpayers frequently file objections or appeals based on broader interpretations of the OECD Guidelines. This situation ultimately increases the potential for tax disputes that must be resolved through objection procedures, appeals, or judicial review before the Tax Court.

Constraints Related to International Tax Treaties. Another juridical constraint relates to the existence of international tax treaties concluded by Indonesia with its partner countries. These treaties, commonly known as Double Taxation Avoidance Agreements (DTAAs), aim to prevent double taxation and enhance cross-border tax cooperation.[38] For instance, Indonesia has entered into tax treaties with various countries, including Singapore, which regulate related-party relationships under provisions concerning

[37]*https://www.itrworldtax.com/NewsAndAnalysis/The-selection-of-the-best-transfer-pricing-method/Index/1960?utm_source.*

[38] Sambur, N. G., Siar, L., & Sarapun, R. M. S. *"Analisis terhadap Persetujuan Penghindaran Pajak Berganda (P3B) terhadap korporasi dalam sistem hukum di Indonesia"*. Jurnal Administratum, Vol 12, No, 5, (2023).

associated enterprises. These provisions generally allow tax authorities to adjust profits where transactions between related entities are not conducted in accordance with the arm's length principle.

However, such treaties also provide dispute resolution mechanisms through the Mutual Agreement Procedure (MAP) between the tax authorities of the contracting states. Provisions within tax treaties that have been ratified hold a lex specialis position over domestic law insofar as they regulate the same matters. This creates a particular challenge for the Directorate General of Taxes. When Indonesian tax authorities unilaterally apply transfer pricing adjustments, the treaty partner country may implement a corresponding adjustment or even reject the adjustment. If both countries fail to reach an agreement through the MAP process, there is a risk of double taxation, which may adversely affect taxpayers and, in turn, the investment climate.[39]

Furthermore, variations in arbitration clauses and dispute resolution mechanisms across different tax treaties require tax authorities to tailor their enforcement approaches to the specific provisions of each treaty. This adds further juridical complexity to the enforcement of transfer pricing rules, especially in cross-border transactions.[40]

Based on the above analysis, it can be concluded that the juridical constraints faced by the Directorate General of Taxes in addressing transfer pricing practices mainly involve several key aspects. First, the lack of optimal harmonization between domestic tax regulations and international standards leads to differing interpretations between tax authorities and taxpayers. Second, inconsistencies between tax laws and their implementing regulations create complexities in the exercise of fiscal adjustment authority. Third, the diversity of provisions within Double Taxation Avoidance Agreements increases the complexity of law enforcement in cross-border transactions.

From an academic perspective, these conditions indicate that although Indonesia has established a relatively strong legal framework for regulating transfer pricing, the effectiveness of law enforcement remains highly dependent on the consistency of regulatory harmonization and the clarity of applicable legal norms. Therefore, it is necessary to strengthen the synchronization between domestic regulations and international standards, as well as to enhance the institutional capacity of tax authorities, in order to ensure that transfer pricing enforcement can be carried out more effectively, fairly, and with greater legal certainty for all parties involved.

[39] Haritsyah, M. *"Hambatan penyelesaian sengketa transfer pricing melalui Mutual Agreement Procedure (MAP) di Indonesia"*. Educoretax, Vol 2, No 1, (2022), p. 20-34.
[40] Nugroho, A., & Sari, D. P.. Upaya meminimalisir transfer pricing pada hukum perpajakan. Jurnal Rechtidee, Vol 8, No 1, (2023)

CONCLUSION

The law enforcement mechanism against tax avoidance practices through transfer pricing in Indonesia, based on Minister of Finance Regulation No. 172 of 2023, is carried out through five main stages: monitoring high-risk taxpayers, conducting transfer pricing audits, determining fiscal adjustments, issuing Tax Assessment Letters, and providing administrative legal remedies in the form of objections, appeals, and judicial review. This mechanism demonstrates that Indonesia's tax law enforcement system is primarily administrative in nature, aiming to correct the fairness of profits rather than immediately imposing criminal sanctions on taxpayers, except where elements of tax evasion are identified.

Although Indonesia has established a strong legal framework to address transfer pricing practices through tax laws and implementing regulations such as Minister of Finance Regulation No. 172 of 2023, which adopts the arm's length principle, the Directorate General of Taxes still faces significant juridical challenges. These include the lack of harmonization between domestic regulations and the standards of the Organisation for Economic Co-operation and Development (OECD), as well as the complexity of double taxation avoidance agreements, which may lead to disputes and the risk of double taxation. Such challenges often complicate the processes of evidence gathering, fiscal adjustments, and the fair enforcement of tax laws against multinational corporations that tend to exploit regulatory gaps to shift profits. Ultimately, stronger regulatory harmonization and enhanced institutional capacity of tax authorities are required to ensure that transfer pricing enforcement becomes more effective and provides greater legal certainty for all parties involved.

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