

TAXATION STUDIES | RESEARCH ARTICLE

Analysis of Transfer Pricing Practices in Avoiding Tax Payments in Indonesia

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ABSTRACT

This study aims to analyze the transfer pricing practices by PT. XX in efforts to avoid tax payments in Indonesia and to identify the methods used to reduce tax burdens through profit shifting. The approach used is a qualitative method with a case study on PT. XX, supported by a review of literature and tax regulations, including the Minister of Finance Regulation No. 22/PMK.03/2020. Data were obtained from interviews with PT—XX employees, as well as an analysis of two contracts and relevant types of internal transactions. The results show that PT. XX's transfer pricing practices include strategies such as profit shifting, charging unreasonably high costs, and utilizing jurisdictions with lower tax rates. Regulatory gaps, the complexity of cross-border transactions, and weak supervision are factors driving these practices. Case studies of other companies, such as PT Adaro Energy Tbk, PT Toyota Motor Manufacturing Indonesia, and PT Toba Pulp Lestari, confirm the significant impact of these practices on the country's tax revenue. The study recommends strengthening regulations, enhancing the capacity of tax supervisory authorities, and harmonizing international standards related to transfer pricing. Additionally, companies are advised to implement Good Corporate Governance principles, and the government should improve its monitoring systems for affiliate transactions to reduce the risk of tax avoidance, particularly for specific products or services of PT. XX makes comparisons with other companies difficult, underscoring the need for further research on this issue.

Keywords: Transfer Pricing, Profit Shifting, Tax Avoidance, Tax Regulations, Good Corporate Governance.

JEL Code: E44, F31, F37, G15

I. Introduction

The importance of taxation as the backbone of national funding has become increasingly evident in the era of globalization and economic integration. Taxes are not only the primary source of government revenue but also a policy tool that can influence income distribution, economic stability, and national competitiveness. In Indonesia, the tax contribution to the State Budget (APBN) accounted for a very dominant share, exceeding 65% in 2024. This makes tax revenues a vital indicator of the country's fiscal health. Without adequate tax receipts, development programs in infrastructure, education, health, and social protection would be severely hindered. However, at the same time, the practices of tax avoidance and tax evasion pose serious challenges faced by almost all countries, including Indonesia. Transfer pricing, the practice of setting prices for transactions between entities within a multinational group, is often used to shift profits from

jurisdictions with high tax rates to those with lower rates. This leads to base erosion and profit shifting, collectively known as BEPS (Base Erosion and Profit Shifting). The OECD, together with G20 member countries, has responded to these challenges by launching a series of international guidelines, including the arm's length principle, which serves as a reference in determining transfer prices.

In Indonesia, the government regulates transfer pricing through the Income Tax Law, Minister of Finance Regulation No. 213/PMK.03/2016, and PMK No. 22/PMK.03/2020, which governs the documentation of transfer pricing. However, the implementation of these rules still faces challenges, particularly due to the limited availability of comparable data, the complexity of cross-border transactions, and the capacity of the tax authority's human resources. Therefore, research on transfer pricing becomes increasingly important, both to strengthen the scientific basis of tax supervision and to provide practical recommendations for regulators and business actors. This study holds high urgency, as PT XX is a multinational company that plays a crucial role in providing electricity infrastructure in Indonesia. With project values reaching hundreds of billions of rupiah and involving various affiliated entities abroad, PT XX's transfer pricing practices have a significant impact on state tax revenues. This case study is also expected to offer insights to other companies on the importance of implementing Good Corporate Governance (GCG) principles and complying with transfer pricing regulations. Academically, this research contributes to the literature by expanding the understanding of transfer pricing in Indonesia, particularly within the electricity infrastructure procurement sector, which is a relatively understudied area. It also fills knowledge gaps by presenting an in-depth analysis of how gross profit margins are allocated among affiliated entities, how risks are borne, and how tax implications are calculated. Thus, this research is anticipated to serve as a valuable reference for researchers, policymakers, and professionals in taxation and accounting, providing insight into the dynamics of transfer pricing and its impact on national revenue.

Taxation in Indonesia is a key pillar of the state's fiscal structure. By the end of 2024, tax revenue realization reached IDR 1,932 trillion, or 68% of the total 2024 State Budget (APBN) of IDR 2,842 trillion. This has encouraged the government to strive for optimal tax revenue as its primary source. Tax is a mandatory contribution from society or citizens that must be paid as state income. However, taxes paid by the public do not receive direct compensation because these funds are used for national needs aimed at maximizing public welfare (Ministry of Finance, 2022). As the primary source of state revenue, taxes are viewed not only from a revenue perspective but also from their broader role and function in the economy. Understanding the nature of tax as a compulsory contribution and a governmental instrument is crucial for illustrating how taxes impact various aspects of development and policy. Tax is a mandatory contribution from citizens and business entities to the state, as mandated by law, used to finance various government and development needs. The basic concept of tax encompasses its functions as a state revenue source, an income redistribution tool, an economic and social regulatory instrument, and an economic stabilizer (Halim, 2025). According to Kusuma (2016), tax is a public levy to the state treasury, based on a law that can be enforced without direct compensation, and is used to pay for public expenditures. From these definitions, tax functions as an income redistribution tool, an economic and social regulatory instrument, and a means of economic stabilization, although tax payments do not provide direct reciprocal services to the payer.

The ease and speed of transactions enable global companies to compete across various sectors. This development is driven by advances in the economy, technology, transportation, and information, which have transformed business patterns and the behavior of business owners. The growth of companies from a national scale to multinational operations with branches abroad is also influenced by differences in tax rates between countries, which encourage the practice of transfer pricing (Pondrinal, Sari, and Putri, 2023). Transfer pricing refers to the prices of products or services transferred between divisions within a company or between related companies. A related party relationship occurs when one party can control or influence the decisions of another party (PSAK No. 7 Year 2010). According to the Organisation for Economic Co-operation and Development (OECD), transfer prices are the prices set for transactions of goods and services between members of a group within multinational companies that deviate from fair market value. These prices are

established based on the arm's length principle and apply only to transactions of goods and services between related parties (Sarah Ginting & Nera Marinda Machdar, 2023).

The definition of transfer pricing, as the price arising from the transfer of goods, services, and intangible assets, mentioned above, is a neutral one. However, transfer pricing practices are often used for tax avoidance. This occurs due to the misuse of transfer pricing by multinational companies as taxpayers, which allows them to manipulate the prices transferred to their affiliated companies. This practice aims to minimize or avoid paying tax altogether to the government (Adiningsih, 2023). Case studies indicate that many assets are held abroad to avoid domestic taxes, often due to low tax rates, with the majority being held in countries with similarly low tax rates. Case studies indicate that many assets are stored overseas to avoid domestic taxation due to low tax collection rates (Adelia & Asalam, 2024).

Minister of Finance Regulation No. 22/PMK.03/2020 states several transfer pricing methods that can be used, namely:

- a. Comparable Uncontrolled Price (CUP) method: a method that compares the price of goods and services in transactions between affiliated parties with transactions conducted with independent parties.
- b. Resale Price Method (RPM): a method comparing the gross profit earned from transactions between affiliated parties with the gross profit earned by the company from transactions conducted with independent parties.
- c. Cost Plus (C+) method: a method comparing the mark-up on costs in transactions between affiliated parties with the mark-up on costs charged in independent transactions.
- d. Profit Split Method (PSM): a method that attempts to measure the fairness of compensation (in this case, profit) received by a company for its contribution within a multinational group.
- e. Transactional Net Margin Method (TNMM): a method comparing the operating profit margin earned from transactions with independent parties to those in transactions between affiliated parties.

Companies naturally aim to maximize profits while minimizing tax payments. One strategy companies may employ to reduce their tax burden is tax avoidance. Typically, companies report lower profits in their financial statements to lower the amount of tax payable. A standard method used by multinational companies to report lower profits is through the use of transfer pricing. According to Kurniawan (2015), multinational companies use transfer pricing to shift taxable income to countries with lower tax rates, thereby reducing the overall tax burden borne by the corporate group. Kurniawan (2015) also explains that one frequent transaction indicating transfer pricing is sales to related parties. The use of transfer pricing in related-party sales transactions is often aimed at optimizing tax liabilities by deliberately reducing sales revenue, thus lowering corporate income (Rahayu, 2010). Therefore, it can be concluded that the higher a country's tax rate and the greater the tax burden faced by a company, the more likely the company will engage in tax avoidance through transfer pricing.

As transfer pricing cases have increased domestically and internationally, several companies have been suspected of engaging in such practices. PT Adaro Energy, through its subsidiary in Singapore, reportedly paid over USD 125 million less in taxes between 2009 and 2017 by shifting profits to offshore locations. PT Toyota Motor Manufacturing Indonesia, together with its Singapore business unit, allegedly lowered sales prices, resulting in a tax revenue loss of IDR 1.22 trillion from 2005 to 2008. PT Toba Pulp Lestari was recorded as exporting pulp at below-market prices to its affiliate in Macau, resulting in a tax loss of IDR 1.07 trillion from 2007 to 2016. The Corruption Eradication Commission's task force uncovered suspicious illegal exports of 5 million tons of nickel to China since 2020, despite the government's ban on nickel exports. The Coca-Cola Company was reported to have underpaid taxes by USD 6.1 billion during the period 2007-2009 due to improper profit allocation to its foreign subsidiaries. Chevron Australia lost a case involving

intercompany loans with unreasonable interest rates. Google was suspected of shifting royalties to subsidiaries in the Netherlands and Bermuda to avoid taxes amounting to USD 22.7 billion.

Several previous studies indicate that transfer pricing is often used for tax avoidance to reduce tax payments. Herman (2023). Revealed that transfer pricing exploits gaps or loopholes in tax laws by shifting company profits to other entities within the same group in different countries, thereby lowering the company's overall tax burden. Anggraini (2024) also concluded that when prices set do not reflect market conditions, transfer pricing can be used as a tool for tax avoidance. However, some studies argue that transfer pricing is not always directly related to tax avoidance. For example, Hidayanto (2024) noted that companies do not primarily use transfer pricing to avoid taxes, possibly due to strict regulations and supervision. Additionally, Adiningsih (2023) found that transfer pricing and profitability have no significant effect on tax avoidance.

II. Research Method

In this study, the researcher uses a qualitative research method with an exploratory phenomenological approach. According to Putri (2025), this qualitative phenomenological research emphasizes understanding through in-depth interviews, observations, and document analysis. This is why the author chooses this approach to deeply explore the transactions and swift income conducted by PT XX through its affiliated companies located abroad. Through detailed research, interviews, and document analysis, it is expected to determine whether PT XX engages in tax abuse through transfer pricing or, more specifically, the swift income method. PT XX is a multinational company operating in the high-voltage electricity procurement sector. The research subjects are selected purposively, using the following criteria:

- a. The subject is a multinational company.
- b. The subject has transactions with related parties.
- c. The company's financial reports related to transfer pricing.
- d. The budget required for projects related to transfer pricing.
- e. Target informants include financial/accounting managers, tax managers, project financial controllers, and tax consultants.

The selection of interviewees among the targeted informants was based on their direct involvement in preparing financial reports, supervising project financial activities, and responsibility for tax-related matters. Each party's role is detailed as follows: the finance manager is responsible for the company's financial reporting, which includes preparations for both external audits and other external stakeholders; the tax manager oversees all company tax matters, ranging from income tax and VAT reporting to handling tax audits; the project financial controller manages the project from contract approval through to the administration of expenditures, receipts, and project budgeting; meanwhile, the tax consultant, as an external party, provides expert advice concerning transfer pricing regulations and taxation practices in Indonesia.

III. Results and Discussion

2.1. Tax Avoidance

Tax planning refers to the taxpayer's ability to organize financial activities in a manner that minimizes tax expenses by exploiting weaknesses or gaps within tax laws and regulations, utilizing specific methods and characteristics (Rioni, 2019). The primary objective of tax planning is to strategically design the taxpayer's operations to minimize the tax burden as much as possible by taking advantage of existing tax loopholes. This is done to maximize post-tax profits, recognizing that taxes represent a deduction from earnings (Gula & Mulyani, 2020). Within this context, transfer pricing practices are often utilized as part of a company's tax

planning strategy to minimize tax liabilities. This is achieved by manipulating prices in transactions between related entities within the same corporate group (Simanjuntak, 2017). A related party relationship exists when a taxpayer is in a position that could potentially influence decision-making in an unreasonable or non-arm's-length manner. By leveraging such related-party transactions, companies attempt to reduce taxable income in high-tax jurisdictions and shift profits to jurisdictions with lower tax rates, thus optimizing their overall tax burden.

2.2. Transfer Pricing

Companies naturally aim to maximize their profits while minimizing the amount of taxes they have to pay. One common strategy employed to achieve tax minimization is tax avoidance. Typically, companies report lower profits in their financial statements to reduce their taxable income and thereby lessen the tax burden. Among the various tactics frequently used by multinational corporations to report lower profits is transfer pricing. According to Pricewaterhouse, as cited by Yuniasih et al., experts acknowledge that transfer pricing can be a legitimate method to avoid double taxation; however, it also presents opportunities for misuse (Jarkoni & Juniyati, 2023). This misuse often involves shifting profits from countries with higher tax rates to those with lower tax rates. Transfer pricing practices usually involve inflating purchase prices and deflating sales prices between companies within the same corporate group or related parties. In doing so, profits are transferred to affiliated companies located in low-tax jurisdictions, thereby reducing the overall tax liability of the multinational corporate group (Aulia Astri, 2021). Transfer pricing is frequently perceived negatively, commonly referred to as "abuse of transfer pricing," which entails the deliberate shifting of taxable income from a multinational company's entity in a high-tax country to affiliates in countries with lower tax rates. This practice aims to minimize the total tax burden borne by the multinational group (Rosad et al., 2020). While transfer pricing can serve legitimate business purposes, its instrumental use for tax avoidance raises significant regulatory and ethical concerns.

The focus of this research is tax avoidance in the form of transfer pricing practices at PT. XX in Indonesia. This study aims to investigate the specific transfer pricing actions undertaken by PT. XX to reduce its tax liabilities, ensuring that the taxes imposed on the company comply with the applicable tax regulations in Indonesia. Through a detailed examination, the research seeks to uncover whether PT. XX deliberately reports a lower profit or maintains minimal profit margins compared to what would be expected under normal market conditions. Additionally, the study intends to compare PT. XX's profit margins with those of its affiliated entities located abroad to determine if there is a significant variance that indicates profit shifting through transfer pricing. By analyzing financial statements and related transactions, this research hopes to provide insights into the extent to which transfer pricing might be used as a tool for tax avoidance. The findings are expected to highlight whether PT. XX's reported profit and loss reflect its genuine economic performance, or if they have been strategically manipulated to minimize tax obligations. Ultimately, this study will contribute to a better understanding of the practical implications of transfer pricing regulations and their enforcement in Indonesia's corporate tax environment.

As a concrete example related to the subject of this research, there are two procurement contracts for substations involving PT. XX in several regions of Indonesia. These contracts reveal differences in the gross profit percentages of each affiliated company, both within Indonesia and abroad, which are highly relevant for analysis in the context of transfer pricing and tax avoidance. Specifically, PT XX is engaged in substation procurement contracts in East Java and Sumatra. The first contract involves the construction aimed at increasing electricity capacity in Paiton, East Java, with a value of IDR 176,243,696,649. Within the detailed cost breakdown of this contract, there are orders for products and expert services sourced from an internal company based in Hong Kong. Notably, Hong Kong applies a corporate income tax rate of 16.5%, which is lower compared to Indonesia's higher rate of 22%. The total margin earned by the group in this contract is 31%, with the Indonesian entity receiving a margin of only 15% and the Hong Kong entity obtaining a margin of 24%. The second contract involves the construction of an electrical substation in Muara Enim, valued at IDR

455,471,620,115. The contract cost details reveal orders for products and expert services to internal companies located in Singapore (IDR 15,096,442,178), Thailand (IDR 1,357,091,707), Vietnam (IDR 581,829,958), and Hong Kong (IDR 82,320,518,147). The total margin received by the group for this contract is 23%, with the individual country margins as follows: Indonesia at 17%, Singapore at 33%, Thailand at 37%, Vietnam at 29%, and Hong Kong at 27%. From the above data, it is evident that Indonesia receives the lowest margin among the involved countries, and Indonesia also has the highest corporate tax rate compared to the other four countries. The following table provides a detailed explanation of the profit margins and related figures for both contracts.

Table 1. Profit Margins

Contract	Desc.	Type of Transaction	Customer	Value	Total Cost	Gross Profit	% of Gross Profit	Corporate Tax Rate
I (Paiton)	Indonesia	Increase in Substation Power Capacity	Third Party	176,243,696,649	150,008,747,956	26,234,948,693	15%	22.00%
	Hong Kong	Product & Professional Service	PT XX	115,934,543,251	88,110,252,871	27,824,290,380	24%	16.50%
	Total			176,243,696,649		54,059,239,073	31%	
II (Muara Enim)	Indonesia	Electrical Substation Construction	Third Party	455,471,620,115	376,757,319,542	78,714,300,573	17%	22.00%
	Singapore	Product & Professional Service	PT XX	15,096,442,178	10,042,153,337	5,054,288,841	33%	17.00%
	Thailand	Professional Service	PT XX	1,357,091,707	849,132,281	507,959,426	37%	20.00%
	Vietnam	Professional Service	PT XX	581,829,958	413,215,636	168,614,322	29%	20.00%
	Hong Kong	Product & Professional Service	PT XX	82,320,518,147	60,258,619,283	22,061,898,864	27%	16.50%
	Total			455,471,620,115		106,507,062,026	23%	

From Table 1, it can be concluded that the company, as a group, prioritizes overall gross profit. Although Indonesia is the country receiving the project with the smallest gross profit percentage, this is not problematic because the group's total gross profit percentage remains relatively high. In terms of risk, PT XX in Indonesia bears the most significant risk, as it is responsible for maintaining good relationships with third parties and handling matters such as warranties and customer satisfaction with the project results. The subject of this research is focused on informants who can help present the research issues and other relevant matters to support the progress of this study. Informants are those who have comprehensive knowledge related to the research and hold positions critical to providing reliable information. These informants are directly involved in the fieldwork related to the study. The primary data sources used in this research consist of internal company data, which are obtained directly from relevant parties and considered primary data. Primary data are collected firsthand from the source without being processed by any other party. These documents include contract agreements, project budgeting and expenditure documents, purchase orders for products or labor, and budgeting data from each company, both domestic and foreign affiliates.

In contrast, secondary data comprises information provided indirectly to the data collectors, often through other people or documents. Secondary data sources are indirectly related to the research object but are considered supportive to the study, including books, articles, internet sources, and similar materials. This research is conducted and documented to explore various methods used to practice transfer pricing by shifting profits to countries with lower tax rates. This project involves countries such as Singapore, Hong Kong, Thailand, and Vietnam. The research findings were obtained through qualitative methods, using a case study approach supported by data collection through observation, interviews, and documentation. Previously, an external consultant conducted an audit of this project. The consultant analyzed the project by comparing it to similar companies where the average gross profit margin ranges from 3% to 5%. According to the table above, the margin achieved by PT XX exceeds 5%, indicating that PT XX's project and financial reports display

gross profit margins significantly higher than those of comparable companies. From the documentation of the two major contracts awarded to PT XX between 2022 and 2024, it was discovered that orders for goods and services were placed with affiliated entities overseas, specifically in Hong Kong, Singapore, Thailand, and Vietnam. Although the projects were carried out in Indonesia, the most significant profit margins were realized by the foreign entities operating in jurisdictions with lower tax rates. The researcher conducted interviews regarding the above projects with the finance manager, tax manager, project financial controller, and tax consultant. The researcher posed a series of questions broadly covering the following topics:

- a. Were you involved in the tender-winning team?
- b. In your opinion, is it necessary to involve more parties (such as tax and accounting teams) in determining the project value?
- c. Does PT XX have a minimum threshold for project value or margin that must be achieved?
- d. Why are the affiliate margins in other countries higher compared to Indonesia?
- e. Do external parties know the margin values in each country?
- f. Can transactions like these be classified as profit-shifting practices?
- g. Are these practices inconsistent with Good Corporate Governance (GCG) principles?
- h. Are these actions intended to avoid paying higher taxes in countries with higher tax rates? I. From the company's perspective, do you consider these actions reasonable and appropriate?
- i. To the tax consultant: What sanctions or penalties could be imposed on PT XX if this is proven to be profit shifting?

The responses from the interviewees did not always align, but these differences could be explained with reasonable arguments. In the interview with the Financial Manager ("FM"), after posing the above questions, he stated that "These practices do not constitute transfer pricing or profit shifting because each affiliated company in each country must consider other cost components not included in the Cost of Goods Sold (COGS), such as sales, marketing, and general and administrative expenses (indirect costs)." The FM explained that not all entities can set the same gross profit margin on a project. Therefore, for other affiliate countries such as Singapore, sales, marketing, and general and administrative expenses (indirect costs) may be higher than in Indonesia, including salaries and team member welfare-related costs, which are likely to be higher than in Indonesia. Consequently, to achieve an appropriate profit or margin, the affiliate in Singapore must have a higher gross profit margin than PT XX in Indonesia. For one project, the gross profit margin of the Singapore affiliate was 33%, higher than PT XX in Indonesia at 17%. Therefore, although the gross profit margin in Singapore is higher and the corporate tax rate there is lower, this cannot be classified as profit shifting to Singapore.

The Financial Manager (FM) confirmed that he was not involved in the tender process for the project and did not have detailed knowledge regarding why the gross profit margin was higher in Singapore. This issue has also never been a concern for external auditors. According to the external audit team, the supporting evidence typically presented is limited to purchase order documents issued by PT XX to its Singaporean affiliate. Based on the FM's statements, no special analysis has ever been conducted to compare the differences in non-COGS expenses among affiliates in different countries. Therefore, there is no clear understanding of what would constitute a fair margin difference between these affiliates. The FM believes that PT XX is still practicing Good Corporate Governance (GCG) by transparently implementing and reporting internal company data to external auditors and regulators. The FM also added that it would be beneficial to involve the finance teams from each country in the tender process. However, their current involvement may not be significant, as the Commercial Finance team from the Asia Pacific regional office handles this process.

In contrast, the Project Finance Controller (PFC) expressed the opinion that the situation falls under transfer pricing practices, more precisely, profit shifting. The PFC stated, "If the gross profit margin in Indonesia is lower compared to other countries, it can be considered an effort to transfer higher profits to countries with lower tax rates." This opinion is expressed notwithstanding the possibility that other cost components may be

higher in affiliated countries, such as Singapore and Hong Kong, unless the group company can present detailed data on these costs for each affiliated country. The PFC noted, "When this issue is raised with those involved in the tender process, they are unable to provide detailed answers or explain the differences with accurate data." Therefore, according to him, the process lacks transparency. Furthermore, the sales and tender teams focus solely on the total gross profit received by the project at the group level, as their targets are based on the overall gross profit generated for the entire corporate group, rather than the gross profit in each country. The team mentioned, "There are gross profit limits set for each country, but these limits are not the main targets." Typically, if PT XX's gross profit margin in Indonesia already exceeds 12%, the distribution of gross profit margins among the countries is not a priority. According to the PFC, as a company located in Indonesia, PT XX should ideally receive the largest allocation of gross profit. This opinion is based on several reasons:

- a. **Tax Contribution in Indonesia.** As a company operating within Indonesia, PT XX should provide the most significant tax contribution to the Indonesian government, demonstrating its responsibility and support for national development.
- b. **The Highest Risk Carried by PT XX.** PT XX bears the highest risk because it directly deals with third parties. The company has contractual obligations to complete the project in accordance with the terms of the agreement. It remains responsible until the warranty period ends, which typically lasts for two years after all products and services have been handed over to the project owner or customer.
- c. **Complex Warranty Responsibilities.** Although a warranty budget has been provisioned, actual warranty costs may exceed initial estimates. Projects usually involve both products and services. After the products arrive at the project site and are ready for use, a service phase is still required to ensure that all products and electrical flows function properly. This phase culminates in commissioning, which involves final testing, inspection, and verification of the system, facilities, or equipment to ensure it is fully operational.
- d. **Duration of Process and Warranty Period.** The time between product arrival at the project site and commissioning can be pretty lengthy. As a result, the product warranty may expire before the overall project warranty period even begins. In such cases, PT XX remains responsible for the project warranty, including products not manufactured by PT XX itself.

Based on these reasons, the Project Finance Controller (PFC) firmly asserted that PT XX rightfully deserves to earn a larger gross profit compared to other parties and that PT XX does not fully comply with Good Corporate Governance practices. During the interview with the Tax Manager (TM), when asked the same questions, the TM straightforwardly stated that "These practices fall under the category of profit shifting." The TM further emphasized, "It is important to identify which countries receive higher profits and whether those countries have higher corporate tax rates." The TM explained that he has never been involved in the tender process for any project and, therefore, does not have detailed knowledge of why PT XX's gross profit received is lower compared to other countries. The TM expressed willingness to be involved in the tender process in the future, so that he could provide input if any aspects do not comply with Indonesian tax regulations, thereby reducing risks of penalties or fines from tax authorities. Generally, the TM becomes involved during tax audits or reviews of transfer pricing documentation conducted by external consultants. During such audits, consultants establish a minimum gross profit margin threshold for companies in Indonesia, which is typically set at 5%. When conducting audits, consultants review all projects being undertaken by PT XX during the current year and examine the gross profit percentage of each project. If any project's gross profit margin falls below the minimum threshold, consultants conduct a detailed review of that project. This review includes scrutinizing any costs that exceed budgets and identifying abnormal expenses such as penalties. In the case of the two projects studied here, since both had gross profit margins above the minimum threshold, neither project was subject to detailed audit scrutiny. This exchange underscores the differing viewpoints within PT

XX's management regarding transfer pricing and profit shifting. While the PFC emphasizes the importance of fairness and the adequate allocation of profits in relation to risk and contribution, the TM stresses the need for adherence to regulatory thresholds and the role of external audits in ensuring compliance. The TM's desire for more involvement in the tender process indicates a willingness to strengthen internal controls and mitigate tax risks, which aligns with principles of Good Corporate Governance and regulatory compliance.

During regulatory examinations, tax audits typically do not conduct a detailed scrutiny of the gross profit margins of each affiliated country. Regulators typically review supporting cost documents, such as invoices from suppliers and purchase orders sent to them. However, from these supporting documents alone, the gross profit of the respective affiliated companies cannot be determined. The Tax Manager (TM) believes that while such practices pose risks, proving them is very challenging. From the company's perspective, it cannot be definitively stated whether these practices are acceptable or not because clear justifications for the differences in gross profit margins have not been provided. However, if these actions are indeed profit shifting, they would indeed violate Good Corporate Governance principles. On the other hand, from a global group perspective aimed at maximizing overall profits, such practices might be considered reasonable.

The final interview was conducted with the Tax Consultant (TC). Using relevant questions, the TCs stated that these transactions could be classified as profit-shifting practices. The TC's explanation closely aligns with the Tax Manager's opinion, emphasizing the need to assess which country has the higher gross profit and whether that country's corporate tax rate is lower. If an affiliate in a particular country has a higher gross profit margin while its tax rate is lower, this situation is indicative of profit shifting. In Indonesia, there is currently no official regulation that sets a minimum gross profit margin threshold for projects like these. However, tax regulators have the authority to examine and assess the appropriate margin values more thoroughly for such projects. Direct comparisons (apple-to-apple) are difficult due to differences in cost items, particularly salary or wage expenses. Nonetheless, these costs can be adjusted using specific methods to estimate a reasonable project value. The Tax Consultant considers these practices quite risky and, despite the difficulty in proving them, acknowledges that the risks remain. Profit shifting practices can result in sanctions, including fines or administrative penalties, as well as tax adjustments imposed by tax authorities. Specifically, violations related to profit shifting and transfer pricing in Indonesia are governed by Law Number 28 of 2007 concerning General Provisions and Tax Procedures (UU KUP). Additionally, Article 18 of the Income Tax Law (UU PPh) empowers the Directorate General of Taxes (DGT) to make corrections when transfer prices do not comply with the arm's length principle. Below is a summary of the interviews from the four informants:

Table 2. Interviews Result

Aspect	Finance Manager	Project Finance Controller	Tax Manager	Tax Consultant
View on practice	Does not consider it transfer pricing or profit shifting because non-COGS/indirect costs (sales, marketing, and general & admin expenses) are considered	Regarding it, it is a transfer pricing/profit shifting if Indonesia's gross profit is lower than that of other countries.	Identifies practice as profit shifting; emphasizes knowing which country has higher profits and whether its tax rate is higher.	Categorizes practice as profit shifting based on comparing gross profits and tax rates of affiliated countries.
Main Reasoning	Non-COGS expenses in other countries (e.g., Singapore) are higher; thus, the gross margin must be higher to align with pre-tax profit.	No detailed data on non-COGS expenses; tender process lacks transparency; tender team focuses on group profits, not country-level profits.	Not involved in tender, only during tax audits and transfer pricing documentation reviews	Challenging to do direct comparisons due to cost differences, but the risk remains; penalties can

Aspect	Finance Manager	Project Finance Controller	Tax Manager	Tax Consultant
				apply if profit shifting is proven.
Involvement in Tender Process	Not involved; Commercial Finance regional team handles tender.	Not involved; tender team focuses on group gross profit, not individual countries.	Not involved; willing to participate to ensure compliance with tax laws.	No direct mention of involvement in tender.
Involvement in Project Execution	Not directly involved, but can make corrections if errors in project financial reporting arise.	Directly involved, responsible for the project's financial position.	Not directly involved; acts as intermediary with tax authorities or consultants during audits.	Not directly involved; acts as intermediary with PT XX and tax authorities during audits.
Analysis of Costs and Gross Profit	No special analysis of non-COGS cost differences among affiliates.	No detailed non-COGS cost data is available; therefore, it is challenging to explain the gross profit differences.	The consultant sets a 5% minimum gross profit threshold; projects with higher margins are not audited in detail.	No official minimum gross profit threshold; regulators may conduct audits and adjustments.
View on Good Corporate Governance (GCG)	PT XX practices GCG transparently with data shared with external auditors and regulators.	Believes PT XX does not fully practice GCG due to a lack of transparency and unfair profit allocation.	If profit shifting violates GCG, it might be justified for the global group benefit.	Risky practice; proven profit shifting breaches GCG and incurs penalties.
Company Risks and Responsibilities	PT XX faces no significant risks due to transparency and fair profit allocation among countries.	PT XX faces the highest risks due to contractual obligations and complex warranty periods.	Aware of the risk of tax fines and penalties if non-compliant.	Risk of administrative sanctions and tax corrections if profit shifting is proven.
Recommendations	Local finance teams should be involved in tender processes despite their current limited role.	PT XX should receive the largest gross profit allocation due to tax contributions and risk exposure.	Willing to be involved in tenders to reduce tax and penalty risks.	Need strict supervision and compliance to avoid penalties from profit shifting practices.

Suppose a uniform gross profit percentage is applied across all countries without considering the differences in risks and market characteristics of each country. In that case, there will be a significant disparity in profits, particularly for projects undertaken in Indonesia. For example:

- a. The Paiton Project (Indonesia) should have generated a profit of IDR 32.6 billion, which is IDR 6.3 billion higher than the currently reported profit.
- b. The Muara Enim Project (Indonesia) should have generated a profit of IDR 87.46 billion, which is IDR 8.7 billion higher than the currently received or reported profit.

Table 3. Reported and Uniform Gross Profit Comparison by Country

Contract	Description	Contract/Order Value	Gross Profit (reported)	Gross Profit % (used)	Gross Profit (uniform% %)	Uniform Gross Profit %	Difference in Gross Profit (IDR)
I (Paiton)	Indonesia	176,243,696,649	26,234,948,693	15%	32,608,862,780	18.5%	6,373,914,087
	Hong Kong	115,934,543,251	27,824,290,380	24%	21,450,376,293	18.5%	
	Total	176,243,696,649	54,059,239,073	31%	54,059,239,073		
II (Muara Enim)	Indonesia	455,471,620,115	78,714,300,573	17%	87,434,281,664	19.2%	8,719,981,091
	Singapore	15,096,442,178	5,054,288,841	33%	2,897,977,655	19.2%	
	Thailand	1,357,091,707	507,959,426	37%	260,513,133	19.2%	
	Vietnam	581,829,958	168,614,322	29%	111,690,569	19.2%	
	Hong Kong	82,320,518,147	22,061,898,864	27%	15,802,599,004	19.2%	
	Total	455,471,620,115	106,507,062,026	23%	106,507,062,025		

Based on the above calculations, if a uniform gross profit rate were applied across all countries, PT XX should receive an additional profit of approximately IDR 6.4 billion from the Paiton project and IDR 8.7 billion from the Muara Enim project. Using the corporate income tax rate of 22%, this translates into underpaid corporate tax (PPh Badan) of:

- a. IDR 1,402,261,099 for the Paiton project
- b. IDR 1,918,395,840 for the Muara Enim project

This underpayment could trigger tax audit risks and adjustments by the Directorate General of Taxes (DGT). If PT XX is proven to engage in transfer pricing practices by shifting profits to countries with lower tax rates, potential sanctions include:

- a. **Transfer Pricing Adjustments (Additional Corporate Income Tax):** The DGT will adjust transaction prices among affiliated entities to reflect arm's length pricing. This adjustment increases taxable income in Indonesia, resulting in additional corporate income tax liability. Legal basis: Article 18 paragraph (3) of the Income Tax Law (UU PPh).
- b. **Interest on Underpayment:** The company must pay interest on the outstanding tax due to transfer pricing adjustments. Legal basis: Article 8 paragraph (2a) and Article 13 paragraph (2) of the General Tax Provisions and Procedures Law (UU KUP).
- c. **Administrative Penalties (Underpayment Tax Assessment Letter Fines):** If the tax adjustment results in an Underpayment Tax Assessment Letter (SKPKB), administrative fines will be imposed according to prevailing laws.
- d. **Penalties for Late Submission of Transfer Pricing Documentation:** Companies are required to prepare and submit transfer pricing documentation (Local File, Master File, and Country-by-Country Report). Failure to submit these documents on time is considered improper bookkeeping and may lead to automatic tax assessments and penalties of up to 50% of the tax owed.
- e. **Criminal Tax Sanctions:** If profit shifting is deemed illegal tax evasion (beyond tax avoidance), criminal penalties may be imposed under Articles 39 and 39A of UU KUP.

IV. Conclusion

Based on the research findings, it can be concluded that transfer pricing practices at PT XX have sparked debate among internal company parties regarding the fairness of distributing gross profits among entities. The differing opinions of the financial manager, project finance controller, tax manager, and tax consultant reflect the complexity of this issue. Some parties consider the margin differences to be reasonable, given the inclusion of non-COGS (indirect) expenses in each country. In contrast, others view them as indications of profit shifting that could potentially reduce Indonesia's tax contributions. From a public policy perspective, these findings highlight the importance of enhancing the supervisory capabilities of tax authorities. The tax government needs to enhance its cross-border data analysis capabilities, expand access to international comparable data, and reinforce cooperation for information exchange with tax authorities in other countries. This aligns with Indonesia's commitments within the OECD/G20 Inclusive Framework on BEPS, which promotes transparency and global tax fairness.

For companies, the findings emphasize the importance of complying with the arm's length principle and maintaining adequate transfer pricing documentation (Local File, Master File, and Country-by-Country Report). Proper documentation enables companies to mitigate risks of tax corrections, administrative fines, and criminal sanctions. Companies should also involve their tax and finance departments in the project planning phase to ensure transfer pricing decisions are commercial and legally justifiable. This research has broad practical implications. First, for regulators, the study offers inputs for developing more comprehensive policies, including the potential establishment of minimum gross profit margin thresholds for strategic projects. Second, for companies, it encourages the adoption of Good Corporate Governance (GCG) and transparency in profit reporting, thereby reducing reputational and litigation risks. Third, for academics, it opens up opportunities for further research with wider scopes, such as comparing transfer pricing practices across different industry sectors or analyzing the impacts on macroeconomic indicators, like the tax ratio.

As a limitation, this research focuses solely on two PT XX projects from 2022 to 2024 and relies on interview data and internal documents. Future studies could broaden the research scope to other projects or sectors, or utilize quantitative data and econometric methods to objectively measure the effects of transfer pricing on tax revenues, thereby providing a more comprehensive basis for policymaking. According to agency theory, information asymmetry can enable opportunistic behavior by management directed by headquarters. Oversight of transfer pricing practices continues to face challenges, particularly due to data limitations and difficulties in assessing inter-affiliate transactions. For multinational corporations, transfer pricing practices remain feasible, but proving them is very difficult, especially for external parties and regulators. Hence, stronger government oversight and regulations, along with corporate adherence to Good Corporate Governance principles, are essential to prevent the misuse of transfer pricing, commonly known as profit shifting. This research demonstrates that transfer pricing remains a significant challenge in tax supervision, particularly for Indonesian tax authorities. The PT XX case study suggests potential profit shifting, where profits are relocated to countries with lower tax rates, such as Hong Kong, Singapore, Thailand, and Vietnam. This is illustrated by disproportionate margin allocations, where foreign entities earn the highest gross profit margins despite projects being conducted in Indonesia and risks being borne by PT XX.

Based on interviews with four informants, it is concluded that the Project Finance Controller, Tax Manager, and Tax Consultant share similar views, suspecting profit shifting practices by PT XX. However, proving these practices is very difficult, especially for external parties. To date, detailed tax audits and transfer pricing documentation reviews have not been conducted because the projects' gross profit margins remain relatively high and no abnormal costs have been recorded. Meanwhile, the Financial Manager holds a different view, considering the margin differences acceptable because the corporate group factors in other expenses such as sales, marketing, and general administrative costs when determining each country's gross profit. However, the exact values of these costs are not precisely known.

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