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RESEARCH ARTICLE

State Revenue Receipt: A Legal Paradigm in Corporate Transfer Pricing

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ABSTRACT

This article aims to investigate the phenomenon of corporate transfer pricing that applies in Indonesia and is related to the implementation of tax system reforms from 1983 until now. Another objective is to analyze the implications for state revenue receipts and identify the latest developments in existing supervision and law enforcement efforts following the renewal of tax laws for corporations in increasing tax revenues for the state. The research method used in this research is normative legal research, a scientific research procedure to find the truth based on scientific logic from the normative side. The research specifications studied are related to the implementation of tax law and its application in Indonesia, especially in transfer pricing transactions. The main finding of this study is that understanding and applying transfer pricing principles following the arm's length principle is very important to maintain fairness in taxation. With a holistic approach that includes a legal paradigm in the tax system, Indonesia can optimize state revenue receipts from corporate transfer pricing transactions, supporting the country's fiscal sustainability.

INTRODUCTION

A growing issue today is corporate transfer pricing. National tax revenue and fiscal balance are affected by the pricing tactics of affiliated companies, especially in cross-border transactions (Taufiq & Tertiarto, 2018). Arham et al. (2020) stated that transfer pricing has been the subject of considerable debate in Indonesia, with questions being raised regarding tax equity and the importance of understanding and adhering to transfer pricing regulations (Arham et al., 2020)

. One of the most significant consequences of inequitable transfer pricing practices is the reduction in tax revenue received by the state. When multinational companies (MNCs) set below-market transfer prices for the export of products or services from subsidiaries in Indonesia to subsidiaries abroad, this can reduce taxable profits in Indonesia, thereby reducing the country's tax revenue (Rachmat, 2019). Companies may sometimes use transfer pricing practices to shift profits to jurisdictions with lower tax rates (W. A. Putri, 2017). Also, reduce the tax that must be paid in Indonesia and certainly reduce state tax revenues.

Transfer pricing practices can help MNCs optimize their tax structure. Appropriate and reasonable transfer pricing adjustments can legally reduce its tax liability, thereby increasing the profitability of the MNC (Kohlhase & Wielhouwer, 2023). Transfer pricing can help manage internal cash flows within MNCs in an efficient way to allocate resources more effectively between subsidiaries (Mashiri et al., 2021). Good transfer pricing practices can help MNCs make better business strategy decisions by comparing performance between subsidiaries and their products (Klassen et al., 2017). When transfer pricing practices are closely monitored and comply with the *arm's length principle*, the state can ensure that MNCs pay reasonable taxes and do not unlawfully avoid taxes. Transfer pricing that complies with the principle can maintain fairness in taxes. MNC companies are taxed in the same way as companies in general for MNCs abusing tax regulations (Huda et al., 2017). As a result, state tax revenue will increase.

The central concept in transfer pricing is the *Arm's Length Principle,* which states that the prices used in transactions between related entities in an MNC should be comparable to those used in transactions between unrelated parties. In other words, entities within the MNC should set the same transfer prices as they would set as unrelated parties. The goal is to prevent MNCs from unfair practices that may reduce tax liability in one tax jurisdiction while increasing tax liability in another (W. A. Putri, 2017). Another theory underlying the linkage of transfer pricing and taxation is the *National and* Fiscal *Interest Theory*. This theory emphasizes protecting a country's national and fiscal interests. In transfer pricing, the state seeks to ensure that tax revenues derived from MNC operations in the country are not tainted by unfair transfer pricing practices. Strict transfer pricing regulations can protect a country's tax revenue (Supriyati et al., 2021).

To address the negative impact of transfer pricing on tax revenue, the Indonesian government has taken various measures, including tax policy changes and tax system reforms, including transfer pricing regulations in Indonesia. Transfer pricing regulations in Indonesia are designed to prevent profit shifting and ensure that transactions between related entities are conducted within arm's length (Susanti & Firmansyah, 2018). Taxpayers conducting cross-border transactions must comply with transfer pricing rules and complete documentation related to the transfer pricing (Tampubolon & Al Farizi, 2018).

Indonesia's taxation system is governed by several tax laws and regulations covering various types of taxes, such as income tax, value-added tax, import duties, excise tax, etc. The Directorate General of Taxes is responsible for enforcing various tax and taxation laws in Indonesia. Individuals and companies operating in Indonesia must understand and comply with these tax laws to fulfill their tax obligations and avoid penalties. Tax laws and regulations in Indonesia have changed over time through various amendments to the provisions of tax laws and regulations (Hardiyanto ., 2019)

Tax system reform in Indonesia relating to transfer pricing transactions is an effort to improve the transparency, fairness, and effectiveness of tax regulations related to transactions between tax-related entities, such as multinational companies (MNCs) and their subsidiaries in Indonesia. The aim is to ensure that the revenue the Indonesian government should earn from income tax is not constrained by unfair transfer pricing practices or abuse of tax regulations. Ideally, tax system reform in Indonesia related to transfer pricing can increase state revenue, but tax revenue to date has not met the target. Some factors that cause this are the complexity of transfer pricing, corporate non-compliance, corporate structures, the lack of tax authority resources, international challenges, and the economic crisis (Klassen et al., 2017).

The potential loss of state revenue due to corporate transfer pricing practices is related to several factors that allow companies to reduce their tax liabilities unlawfully. Such factors may include transfer pricing manipulation, profit shifting to jurisdictions with low tax rates, lack of transparency, lack of law enforcement, and complexity of business structures (Lianto, 2022; D. A. Putri & Najicha, 2021; Rachmat ., 2019)

This article investigates the corporate transfer pricing phenomenon prevailing in Indonesia concerning implementing tax system reform from 1983 until now. Another objective is to analyze its implications on state revenue receipts and identify recent developments in supervision and enforcement efforts by the tax law reform for corporations in increasing tax revenues for the state.

LITERATURE REVIEW

Definition and Concept of Transfer Pricing

Products, services, or intangible assets that occur between entities that have certain relationships are a matter of transfer pricing, this practice allocates income between affiliated parties. Such entities can be parent and subsidiary companies, corporate organisations, or controlled companies. In addition, transfer pricing is also used to optimise tax burden, manage cash flow and foreign exchange risk, and improve operational efficiency.

The OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administration states that there are principles regarding transfer pricing that should be made to reflect comparable transaction prices between independent parties. This is a fundamental concept in transfer pricing, namely the Arm's Length Principle. The principle is intended to prevent multinational companies from manipulating prices that may reduce tax liabilities in one jurisdiction while increasing them in another.

A range of experts have provided their perspectives on transfer pricing. Pratama (2020) defines it as a multinational company's strategy for managing tax liabilities through pricing transactions between affiliates. Tampubolon & Al Farizi (2018) emphasized transfer pricing as a pricing mechanism between companies with unique relationships. Meanwhile, Klassen, Lisowsky, & Mescall (2017) highlight the complexity of transfer pricing in international taxation, and Mashiri, Dzomira, & Canicio (2021) note the potential of transfer pricing as a tool for multinational companies to avoid or minimize taxes.

Transfer Pricing Method

Transfer pricing methods determine the fair value of transactions between related entities. There are five internationally recognized methods:

1. Comparable Uncontrolled Price (CUP). Comparing controlled transaction prices with comparable transaction prices between independent parties. This method is considered the most reliable, but it is difficult to apply due to the difficulty of finding comparable transactions. **OECD (2022)** states that CUP is the most direct method and is considered the most reliable if comparable data is available.

2. **Resale Price**. Determining the transfer price based on the resale price of goods or services to an independent party, less a reasonable profit margin. This method is generally used for distribution transactions. **Tampubolon & Al Farizi (2018)** explain that this method is suitable when a related entity acts as a distributor and resells goods to independent parties.

3. **Cost Plus**. Sets the transfer price based on the cost of producing the goods or services, plus a reasonable markup. This method is generally used for manufacturing transactions. **Klassen, Lisowsky, & Mescall (2017)** point out that the cost-plus method is often used in manufacturing transactions where one entity produces goods and the other distributes them.

4. **Profit Split**. Split the profit generated from transactions between related entities based on each entity's contribution. This method is generally used for intangible assets or highly integrated transactions. **Mashiri, Dzomira, & Canicio (2021)** explain that the profit split method is appropriate for transactions involving intangible assets because it is difficult to find independent comparable transactions.

5. **The Transactional Net Margin Method (TNMM)** compares the operating net profit margin of a related entity with the operating net profit margin of a comparable independent entity. This method is considered the most flexible but is also prone to manipulation. **Pratama (2020)** found that the TNMM method is the most frequently used by multinational companies in Indonesia due to its flexibility.

While the OECD Transfer Pricing Guidelines provide general guidance, accurate transfer pricing is not a simple process. The selection of the appropriate method depends on the unique characteristics of each transaction, such as the type of goods or services traded, the complexity of the transaction, and the risks involved. Independent comparable data is crucial, especially for methods such as Comparable Uncontrolled Price (CUP) that rely on comparisons with similar transactions. In addition, the desired level of accuracy and efficiency considerations, such as cost and time required, also influence the method selection and decision-making process.

An empirical study on how multinational companies choose and apply transfer pricing methods was conducted by Klassen et al. (2017) on how companies choose the method with the lowest tax burden. Then Mashiri et al. (2021) examined using a game model approach to analyse the interaction between multinational companies and tax authorities in the context of transfer pricing, the results showed that stricter supervision and enforcement can increase compliance.

Factors Affecting Transfer Pricing

Internal and external factors influence transfer pricing decisions. The internal factors include the company's business strategy, organizational structure, and the transfer pricing policy applied. Pratama (2020) stated that *corporate governance* and offshore operational strategies affect transfer pricing practices in Indonesia's manufacturing companies. Then, in their research, Susanti & Firmansyah (2018) obtained findings in the form of determinants of transfer pricing decisions in manufacturing companies in Indonesia, namely *leverage*, profitability, and fixed asset intensity.

External factors also play an important role. Tax regulations establish a legal framework that restricts and directs transfer pricing practices at domestic and international levels. Supriyati, Murdiawti, & Prananjaya (2021) analyzed the determinants of transfer pricing decisions in manufacturing companies in Indonesia and found that tax regulations influence such decisions. Macroeconomic conditions, such as inflation, economic growth, and foreign exchange rates, can affect profitability and transfer pricing policies. Kohlhase & Wielhouwer (2023) describe how firms use transfer pricing to plan for taxes and tariffs in international trade, considering the role of headquarters and business units. Competition in the industry encourages firms to adjust transfer prices to maintain a competitive advantage.

Internal and external factors create complex dynamics in transfer pricing. Hummel et al. (2019) show that successfully integrating a tax-compliant transfer pricing system into the management control system depends on top management support, commitment to tax compliance, and availability of resources. Understanding these is crucial for multinational companies and tax authorities in formulating and implementing practical and fair transfer pricing policies.

Transfer Pricing Impact

Transfer pricing practices have a vast and complex impact on multinational corporations (MNCs), home countries, and destination countries. Transfer pricing can be an instrument to reduce the global tax burden and improve operational efficiency. However, transfer pricing practices can also trigger tax disputes with tax authorities and damage a company's reputation.

Then, there are differences in the impact of transfer pricing on the country of origin and the destination country of investment. In the home country, transfer pricing can reduce the tax base and result in a loss of tax revenue. However, transfer pricing can increase tax revenue and promote economic growth in the destination country. OECD (2022) highlights the potential consequences of disproportionate transfer pricing because it can cause losses in developing countries.

Hardiyanto's (2019) study shows that transfer pricing practices in Indonesia can potentially reduce state tax revenues. Huda et al. (2017) added that transfer pricing can hamper Indonesia's economic growth by reducing investment and job creation. Putri (2017) emphasized the importance of the fairness principle and adequate documentation in preventing transfer pricing fraud in Indonesia.

The impact of transfer pricing on capital flows and foreign direct investment is still debatable. Some studies show that transfer pricing can affect the investment decisions of multinational companies. Lianto (2022) analyzed the tax law and criminal law aspects of tax evasion in Indonesia, including transfer pricing abuse.

Data and statistics from various studies show the magnitude of the impact of transfer pricing on tax revenue and capital flows. Rachmat (2019) examined the relationship between taxes, bonus mechanisms, and transfer pricing in Indonesia, finding that transfer pricing can affect the effectiveness of the tax system.

Contemporary Issues in Transfer Pricing

The current dynamics of globalization affect the determination of increasingly complex transfer prices, such as the determination of transfer prices for intangible assets, such as intellectual property rights, *software*, and *know-how*. OECD (2022) guides the valuation and profit allocation of intangible assets, but the challenges in determining the fair market value and contribution of intangible assets to value creation are still considerable.

Another emerging issue is the transfer pricing of financial services, including loans, guarantees, and cash management services. The complexity of financial instruments and the volatility of financial markets add to the difficulty in determining the fair price of financial services transactions. The development of digital technology also raises new challenges in the transfer pricing of digital transactions, such as *e-commerce*, *cloud computing*, and *big data*. Uncertainty about digital business models and profit allocation between jurisdictions demands a new approach to determining the fair value of digital transactions.

Developments in international tax regulations, such as the OECD BEPS initiative and pillars 1 and 2 of the OECD/G20 Inclusive Framework on BEPS, significantly impact transfer pricing practices. Stricter transfer pricing documentation obligations and more comprehensive anti-tax avoidance regulations require multinational companies to improve compliance and transparency in cross-border transactions.

Tax authorities face various challenges in monitoring and auditing transfer pricing in the era of globalization. Limited resources, technical expertise, and access to information are obstacles in assessing the transfer pricing compliance of multinational companies. International cooperation and information exchange between jurisdictions are increasingly important to improve the effectiveness of supervision and law enforcement in transfer pricing.

METHODOLOGY

The research method used in this research is normative legal research. Normative legal research is a scientific procedure that finds the truth based on scientific logic from the normative side. The normative side here is not limited to legislation alone. It emphasizes the search for data contained in the dynamics of the Directorate General of Taxes institution. In this study, research is carried out on applying the tax regulations in Indonesia, which are related to applicable laws and regulations. This research uses secondary data as supporting material that analyzes applicable laws and regulations concerning legal principles adopted and vertical and horizontal synchronization levels. The research specification is related to implementing and applying tax law in Indonesia, particularly on transfer pricing transactions.

The types and sources of data used are primary, secondary, and tertiary legal materials. Secondary data collection techniques in this research are carried out by paying attention to data sources, namely, those obtained from library materials, which include primary, secondary, and tertiary legal materials. The analysis is carried out by selecting materials related to the topic of this research, which will then be researched with a systematic and normative thinking pattern. The research results are poured into writing, arranged systematically, and descriptively analytically described.

RESULTS

Tax system reform in Indonesia related to transfer pricing has undergone a long journey, starting in 1983 with the enactment of Law Number 6 Year 1983 on General Provisions and Tax Procedures. Then, it was strengthened by other transfer pricing regulations, namely Law Number 9 the Year 1994, Government Regulation Number 213 the Year 2016, and Government Regulation Number 94 the Year 2017. In addition, in line with the development of international tax regulations, Indonesia also actively participates in efforts to prevent *base erosion and profit shifting* (BEPS) by signing the *Multilateral Competent Authority Agreement* (MCAAT) to exchange tax information with other countries automatically.

The tax reforms show that Indonesia is committed to creating a fair, effective, and transparent tax system, especially in addressing transfer pricing challenges. Tampubolon & Al Farizi (2018) stated that taxpayers conducting cross-border transactions must comply with transfer pricing rules and complete related documentation. That shows the importance of understanding and complying with evolving transfer pricing regulations. Hardiyanto (2019) states that tax laws and regulations in Indonesia have undergone significant changes over time. Tax system reform is expected to increase taxpayer compliance and optimize state revenue.

The following are some of the laws and regulations that become references in the reform:

1. 1. Law Number 6 Year 1983 on General Provisions and Tax Procedures (KUP). This law regulates the basic principles of taxation in Indonesia. Along with transfer pricing reform, KUP has undergone several amendments to cover transfer pricing regulations.

2. Law Number 9 the Year 1994, on the amendment of Law Number 6 the Year 1983, on General Provisions and Tax Procedures

3. , Government Regulation Number 213, the Year 2016, on the Application of the Double Taxation Avoidance Agreement (DTAA), and Government Regulation Number 94 the Year 2017 on the Amendment of Government Regulation Number 46 the Year 2013 on Types and Rates of Income Taxes that are Final and/or Withheld by Tax Collectors. These regulations regulate double *taxation agreements* (*DTAs*), including transfer pricing and information exchange provisions.

4. Director General of Taxes Regulation No. PER-43/PJ/2010 on Guidelines for Financial Reporting in the Framework of Transfer Pricing. This regulation regulates financial reporting procedures related to transfer pricing, including documentation requirements that companies must comply with when reporting transfer pricing transactions.

5. Director General of Taxes Regulation Number PER-22/PJ/2013 on Procedures for

Determining Transfer Prices and Procedures for Providing Data and/or Information in the Framework of Transfer Price Determination. This regulation provides more detailed guidelines on how transfer prices should be determined and how companies should provide data and information to tax authorities regarding transfer price assessment.

6. Regulation of the Director General of Taxes Number PER-32/PJ/2011 on Procedures for Reporting Data and/or Information Required in the Framework of Transfer Pricing in Multinational Companies and/or Business Entities with Special Relationships. This regulation explains the procedures for reporting data and information required by multinational companies or business entities with unique relationships to assess compliance with transfer pricing.

7. The signing of the Multilateral Convention on Mutual Administrative Assistance in Tax Matters (CMAAT). The Indonesian government has also signed the CMAAT, which allows for the automatic exchange of tax information with other countries and assists in the fight against tax evasion and abusive transfer pricing practices.

Law Number 6 Year 1983 became the first milestone of tax reform in Indonesia, marking a paradigm shift in the Indonesian tax system from *an official assessment system* to a *self-assessment system*. In this system, taxpayers are given the trust to calculate, pay, and report their taxes. This trust requires high understanding and compliance from taxpayers to the applicable tax regulations, including transfer pricing. As stated by Nuryanah et al. (2023), for a tax regulation to be fair, it must fulfill four main requirements: equality, certainty, *convenience* of payment, and *economy of* collection. The principle of *equality* requires that all taxpayers, including multinational companies involved in transfer pricing, are taxed fairly and equally. The transfer price must reflect the fair market price used in transactions between non-related parties. The *certainty* principle requires that taxation rules, including transfer pricing rules, be formulated clearly and easily understood by all related parties. It is important to avoid differences in interpretation and tax disputes that can harm taxpayers and the state. The *convenience of payment* principle emphasizes the need for tax systems and procedures that make it easier for taxpayers to fulfill their obligations. Finally, the principle *of economy of collection* requires the government to manage tax administration efficiently and effectively, so that the cost of tax collection can be kept as low as possible without compromising state revenue.

The principle of equality in taxation requires that all taxpayers, including MCNs involved in transfer pricing practices, be taxed similarly. Transfer prices between related entities should reflect fair market prices, as would transactions between independent parties. Special or discriminatory treatment of MNCs violates this principle (Resmi, 2017). In the context of transfer pricing, transfer prices between related entities should reflect fair market prices as they would be used in transactions between unrelated parties. If transfer pricing practices result in special or discriminatory treatment of MNCs, this may violate the equivalence principle.

The principle of tax *certainty* demands that the rules related to transfer pricing should be clear and understandable to all parties involved, including MNCs. Also, there are rules governing how transfer prices should be determined, as well as reporting and auditing procedures. This certainty prevents tax disputes due to ambiguous rules (Mardiasmo, 2009). This certainty is important to avoid tax disputes that can arise if the rules are unclear.

The *convenience of tax payment* also applies to transfer pricing practices. Transfer pricing tax reporting and payment guidelines should be clear and practical (Soemitro, 1996). Transfer pricing-related regulations and guidelines should be designed so that MNCs can understand and comply with these rules quickly. This ease of payment can be a clear and practical guideline on how transfer pricing should be reported and how transfer pricing-related tax payments can be made smoothly.

Finally, the principle of *economy of collection* is also relevant in monitoring transfer pricing practices. Tax authorities should be efficient in *transfer pricing* audits. The audit process should maximize results at minimal cost (Devano & Rahayu, 2015). Tax authorities must transfer pricing audits efficiently, using available resources wisely. The transfer pricing audit process should be designed to achieve maximum results with minimum cost.

The Indonesian government has been reforming the taxation system since 1983 through the National Taxation System Reform (PSPN). This reform considered three important elements: policy, law, and tax administration (Pohan, 2003). The direction of tax reform in 1994 was to accommodate domestic investment policies to attract foreign investment companies (PMA) to invest in Indonesia. Members of the public were still given the trust to be able to do nationally in the system of calculating, paying, and reporting their taxes (*self-assessment*) so that through this system, taxation is expected to be implemented neatly, controlled, simple, and easily understood by the public. The 1997 Tax Reform was part of the 1994 tax reform, so the basic principles and objectives were the same as the 1994 tax reform. The 1994 reform accommodated domestic investment policies to attract Foreign Direct Investment (FDI). A *self-assessment* system was introduced, making it easier for people to calculate, pay, and report taxes (Soemitro, 1996).

In 2002-2008, tax reform focused on improving organizational governance, human resources, and tax business processes. Thousands of operational standards were prepared, and the modernization of tax service offices was carried out by establishing Large Tax Service Offices, Special Tax Service Offices, Madya Tax Service Offices, and Primary Tax Service Offices. In 2002, the Tax Administration Modernisation Team was formed, and its members are renewed every year. In 2008-2016 tax reform focused on enhancing the role of taxes in response to the global financial crisis. Taxes perform a revenue function and encourage economic growth and investment climate. Various tax incentives and facility policies were issued, such as reducing tariffs to encourage business activities and increasing non-taxable income (PTKP) to support people's purchasing power. *Tax amnesty* and tax data exchange to increase tax potential and compliance, as well as the start of the renewal of the tax IT system, were also carried out in 2016-2017.

Minister of Finance Decree (KMK) Number 360/KMK.03/2017 on Tax Reform Program affirmed that tax reform consists of five themes or pillars: organization, human resources, information technology system and database, business process, and laws and regulations. This legal basis is strengthened by Presidential Regulation No. 40/2018 on Tax Administration System Reform, followed by KMK No. 767/KMK.03/2018. It was first started with the issuance of Minister of Finance Decree (KMK) Number 885/KMK.03/2016 dated Dec 9, 2016, which was later updated with MKK Number 928/KMK.03/2016 on the Establishment of Tax Reform Team.

Transfer pricing is the taxpayer's price when selling, buying, or sharing resources with its affiliates. Affiliate practices aimed at *tax avoidance* will undoubtedly be detrimental to a country's tax revenue, because the potential tax revenue that should be obtained is lost. The Organisation for Economic Cooperation and Development (OECD) revealed that more than 60% of the world trade value is generated from transactions related to multinational companies using transfer pricing schemes. Usually, the scheme used by multinational companies that practice transfer pricing is by shifting corporate profits from countries with high tax rates to countries with lower tax rates. The OECD also noted that transfer pricing practices increased significantly by 20% in 2018 compared to the previous year (Kohlhase & Wielhouwer ., 2023)

By looking at the country's need to secure foreign exchange on state revenue from taxes, the study and implementation of tax system reform in terms of transfer pricing from 1983 to 2022 should be analyzed more deeply. That way, there are still many efforts that need to be adjusted by the government to increase state revenue in the tax sector.

When tax system reform related to transfer pricing is carried out to increase state revenue, but tax revenue has not met the expected target, it can be caused by several complex factors. Some common reasons why tax revenue has not reached the target in the context of transfer pricing reform in Indonesia include several factors. First is the complexity of transfer pricing with the assumption that transfer pricing practice is a very complex and technical field. A proper transfer pricing analysis requires an in-depth understanding of business operations, tax regulations, and market prices. Transfer pricing tax audits and enforcement can also take a long time. Therefore, implementing transfer pricing reforms can face technical barriers that slow the process. Next is MNCs' non-compliance with transfer pricing regulations properly or even trying to evade taxes by unfair practices. This non-compliance can challenge tax authorities to ensure that the transfer prices are reasonable "at arm's length" (Putri, 2017).

Next is the lack of human resources and technology by the tax authorities in Indonesia. These limitations may affect the ability to monitor and enforce transfer pricing regulations effectively. Another thing to observe is also the complexity of the corporate structure. Multinational companies often have complex corporate structures with many subsidiaries in various jurisdictions (Klassen et al., 2017). Monitoring the transactions between subsidiaries and the level of transfer pricing compliance can be complicated. Not to mention when it comes to international challenges. Here, multinational companies often have cross-border operations involving multiple countries. Coordination and cooperation between jurisdictions to address unfair transfer pricing can be difficult. In turn, changes in economic conditions, both globally and domestically, can affect companies' revenues and transactions, which can affect tax receipts from transfer pricing (Pratama, 2020). Finally, the Covid-19 pandemic has affected many aspects of the economy, including business activities and international trade. The impact of this pandemic also certainly has an impact on tax revenue from transfer pricing.

The potential loss of state revenue due to corporate transfer pricing practices is related to several factors allowing companies to reduce tax liabilities illegally. There are several reasons why this may occur. First, multinational corporations (MNCs) can manipulate transfer prices, which are prices for goods, services, or assets transferred between subsidiaries or related entities within the MNC. MNCs may set transfer prices below fair market value, reducing profits subject to tax in jurisdictions with high tax rates (Susanti & Firmansyah, 2018). Unfair transfer pricing practices may allow MNCs to shift their profits to jurisdictions with lower tax rates. MNCs may establish entities in low-tax countries or use jurisdictions with favorable tax rules to reduce liabilities.

Some countries such as Indonesia are alleged to lack transparency in reporting transfer pricing transactions or a lack of ability to monitor these practices (Hummel et al., 2019). MNCs often have more excellent resources and the ability to conduct more sophisticated transfer pricing analyses than the tax authorities in the country. As a result, MNCs often "negotiate" with tax authorities and complicate monitoring and enforcement efforts. Another issue is that MNCs' business structures are often complex, involving subsidiaries and entities operating in multiple jurisdictions. This issue can hinder tax authorities from properly tracking and analyzing transfer pricing transactions.

Not all transfer pricing practices are done to avoid taxes unlawfully. Some transfer pricing practices may be legal and done for risk management and business efficiency purposes. However, if transfer pricing is done unfairly and violates the *arm's length principle*, then this may result in the loss of tax revenue that the state should receive. The impact will be harmful to the country's fiscal and tax fairness. Therefore, the state needs to continue to reform its regulations and monitoring procedures to address this potential loss of tax revenue.

Stricter monitoring and enforcement of transfer pricing should be balanced with a strong understanding of transfer pricing rules and principles among companies (Hummel et al., 2019). In addition, transparency and cooperation between the government, companies, and the private sector can play an important role in achieving the goal of increasing transfer pricing-related tax revenue. The government can conduct awareness campaigns to increase the understanding of companies, especially multinational companies (MNCs), about the importance of transfer pricing compliance. Education and training can help companies understand the rules and *arm's length* principles. Tax authorities in Indonesia need to improve their ability to monitor and audit transfer pricing practices. Measures that can be taken include training tax staff in transfer pricing monitoring, using technology for data analysis, and increasing cooperation with tax authorities in other countries regarding information exchange. The situation can be solved by establishing a specialized team of transfer pricing experts to audit multinational companies with complex transfer pricing transactions. To provide an in-depth view of the company's transfer pricing practices and help determine whether the transfer prices determined are by the fair price principle. The government can also strengthen stricter taxation policies related to transfer pricing to ensure that tax regulations and transfer pricing guidelines are applied consistently.

In addition, active participation in international cooperation, such as tax information exchange, is important to address manipulative transfer pricing practices and prevent multinational companies' exploitation of international legal loopholes. Expansion and refinement of domestic regulations are also necessary to determine whether market prices are fair, and benchmarking methods

need to be re-analyzed to ensure compliance. Furthermore, establishing an independent arbitration panel can expedite and streamline the resolution of transfer pricing disputes and allocate adequate resources for tax technology to improve monitoring and enforcement efficiency. Also, collaboration with the private sector, such as audit firms and tax consultants, can improve understanding and compliance with transfer pricing regulations.

CONCLUSION

Based on the analysis that has been conducted regarding the exploration of the legal aspects of tax system reform in Indonesia related to transfer pricing transactions, it is found that the understanding and application of transfer pricing principles based on the *arm's length principle* is fundamental to maintain fairness in the implementation of taxation. This research shows the need for strict and transparent regulations and strict law enforcement in transfer pricing practices to ensure that multinational companies (MNCs) pay reasonable taxes and do not conduct tax avoidance that is not by applicable regulations. The results also show that cooperation between the government, tax authorities, and companies in understanding and complying with transfer pricing regulations needs to be enhanced to ensure that transfer pricing regulations and guidelines remain relevant and aligned with global business developments and changes

in international regulations. Taking a legal paradigm approach to the tax system, Indonesia can optimize state revenue from corporate transfer pricing transactions, support the country's fiscal sustainability, and encourage better investment.

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