



The Fundamental Taxation Design of Digital Transaction

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Abstract—This study aims to review how the efforts of the tax authorities to tax digital transactions to improve tax compliance. This research is a review of the provisions and regulations related to digital transactions. The review uses three approaches of historicity, rationality, and policy actuality based on the values of Pancasila as the source of all sources of law. The research results are divided into three levels of policy review. At the level of historicity, digital transactions with traditional transactions have the same tax obligations. At the level of rationality, digital transactions are transactions across jurisdictional borders, the aspect of income tax taxation requires criteria for determining permanent establishment. At the level of actuality, tax authorities are required to carry out unilateral measures and global consensus refers to the provisions of the OECD and the hierarchy of tax laws. The value of Pancasila justice is the foundation of the proposed tax policy that balances the obligations of foreign tax subjects with domestic tax subjects through the concept of significant economic presence. This research contributes practically to tax authorities in formulating digital transaction tax collection policies so that they can improve tax compliance.

Keywords—digital transaction; fairness; Pancasila values; tax compliance

I. INTRODUCTION

The impact of the pandemic for two years has changed the order of people's lives. Changes in social order affect people's consumption preferences. Acceleration of the use of technology follows changes in the social order and seeks to become a meeting point with people's consumption preferences. Businesses that utilize digital platforms thrive by involving foreign individuals and foreign entities. The characteristics of businesses that use digital platforms cross the jurisdictional boundaries of several countries, the implications of which affect the determination of their taxation rights.

Taxation rights have historically been regulated in the Income Tax Law which was last revised by the Tax

Harmonization Law. Article 2 of the Income Tax Law states that tax subjects consist of domestic tax subjects and foreign tax subjects [1]. Furthermore, Article 2 paragraph 4 explains the criteria for foreign tax subjects, but whether these criteria are still relevant to the growth of cross-border jurisdictions. In response to this, the tax authorities are required to review the determination of foreign tax subjects in local regulations or domestic laws as well as provisions in tax treaties with the contracting partner countries. [2], [3]. It should be remembered that in the hierarchy of legislation, it is mandatory to comply with the principle of *lex specialist derogate lex generalist* [4], [5]. In the context of tax collection, the tax authority is obliged to pay attention to this principle and must be based on the applicable provisions [6], [7].

Research on digital transaction taxation has previously been carried out, the perspective of digital transaction taxation in India, France, and Australia was carried out by [8], cross-jurisdictional digital transactions scrutinized by [3], and efforts to optimize taxation on the income tax aspect were investigated by [9]. These studies have not been based on the values of Pancasila as the foundation of digital transaction taxation policies. Especially focusing on the values of Pancasila on the criteria for determining whether foreign individuals and foreign entities are eligible as permanent establishments.

The problem in this study is how the tax authorities attempt to tax digital transactions. The focus of the research is on determining foreign individuals and foreign entities that have not been netted in determining a permanent establishment. The purpose of the study is to review how the tax authorities' efforts to tax digital transactions are to improve tax compliance. To answer the research questions, an analysis stage was carried out which was presented with the themes of historicity, rationality, and the actuality of Pancasila values. In the end, a proposal for the foundation of digital transaction taxation policies is presented as an effort to increase tax compliance. In the following description, a relevant theory review is presented which is used to formulate the foundation of digital transaction taxation policies.

II. THEORY REVIEW

A. Digital Transaction

Digital transactions grew rapidly at a time when the world was hit by a pandemic and in response to the development of society. The community is greatly helped by the various services that utilize digital platforms [10], [11]. The taxation aspect of digital transactions crosses the jurisdictional boundaries of a country. Another problem arises when questioning the taxation rights of a digital-based service. This is a concern Organization for Economic Co-Operation and Development (OECD).

The OECD proposes that physical presence should not be the main requirement in determining the taxation rights of digital transactions [12]. In principle, the OECD provides three guiding criteria in the event that a country applies the concept of significant economic presence [13]. The first is related to the income base which contains the types of transactions carried out, determining the income threshold level and other related administrations. Second, related to digital which includes local domain names, local digital platforms, and local payment options. Third, the user base is in the form of the number of final online contracts, the level of monthly active users, and the volume of digital content on a digital platform.

B. Permanent Establishment

Determination of the subject of foreign individuals and foreign entities to become a permanent establishment is regulated in the Regulation of the Minister of Finance no. 35 of 2019 regarding the determination of permanent establishment [14]. In Law no. 2 of article 6 paragraph 6 the criteria for significant economic presence are an additional provision for determining a permanent establishment other than physical presence [15]. Through a press release by the Directorate General of Taxes, it was determined that the tax imposition on Google Asia Pacific Pte. Ltd. is domiciled in Singapore [16]. Until this review article was compiled, there were ten press releases with a total number of value-added tax collectors as many as 73 business entities [17]. This stipulation is still limited to the collection of value-added tax that has not been able to tax aspects of income tax which is constrained by the determination of the criteria for a permanent establishment [9].

C. Tax Fairness

The aspect of justice in the preparation of taxation policies is of concern to the tax authorities, considering that one of the principles of tax collection is equality and equity [18]. Justice in taxation is divided into horizontal justice and vertical justice [19]. Fairness in taxation policies affects taxpayers' trust in tax authorities which leads to the intention to fulfill tax obligations [20]–[22].

Justice in the values of Pancasila is contained in the fifth precept, the fifth precept is imbued with the first to the fourth precepts [23]–[25]. Justice cannot apply to all levels of taxpayers, but justice that applies to most taxpayers is sought. In this article review, the aspect of justice is not seen from

vertical or horizontal justice, but rather on the justice of domestic tax subjects with foreign tax subjects. It can be said, the value of unity is important as unifying equality of domestic taxpayers in fulfilling tax obligations.

D. Tax Compliance

Research related to tax compliance never stops if there are legal loopholes that can be exploited by taxpayers. Thus, policies that are fair and provide legal certainty need to be considered considering one of the factors that can increase compliance [26]–[29]. The tax administration modernization reform in the form of digital-based services is an effort to accelerate compliance improvement. The use of the population identification number as the main number of the taxpayer as mandated in article 2 of the Harmonization of Tax Regulations Law [30], which is a form of tax administration policy reform.

The review of all laws, Decrees of the Minister of Finance, and their implementing regulations are only limited to domestic policies or unilateral measures. Improving tax compliance for cross-jurisdictional transactions requires a review at the tax treaty level with each treaty partner country. This is in line with the view [31] which uses a regulatory impact analysis approach that the policy review must be comprehensive on the provisions and their implementing regulations. In addition to reviewing domestic policies with unilateral measures, a global consensus is needed under the coordination of the OECD [2]. The next description is related to the research method used to achieve the research objectives starting with the presentation of the research object.

III. RESEARCH METHODS

A. Research Object

The object of this research is the provisions governing the taxation of digital transactions. The provisions governing digital transaction taxation are in the form of domestic provisions, tax treaties, and provisions from the OECD. Law no. 2 of 2020, Law no. 7 of 2021, the Regulation of the Minister of Finance no. 35 of 2019 is the object of research in the form of domestic provisions. The object of research is in the form of a tax treaty that uses the agreement between Indonesia and Singapore for the 2020 agreement which takes effect in 2021 [32].

B. Review

The stages of reviewing the digital transaction taxation policy using Yudi Latif's thinking consist of historicity, rationality, and the actuality of Pancasila values [24]. This thinking is very appropriate to use considering that all sources of law are the values of Pancasila. This method has been used in several tax policy reviews, such as the tax amnesty policy [33], [34] and as a foundation for individual taxpayer compliance [28], [35], [36].

The review stage begins with the historicity stage, this stage traces the historical development of digital transactions. The rationality review stage is a review of the rationalization of digital transaction taxation aspects. The actuality review stage is in the form of the tax authority's actuation to review

domestic policies and agreements with treaty partner countries on digital transaction taxation. At the end of the stages of historicity, rationality, and actuality in the form of a proposal for the foundation of a digital transaction taxation policy based on the values of Pancasila. Further, the results and discussion of the research are presented, starting with a historical review.

IV. RESULTS AND DISCUSSION

A. *Historicity*

Historically, this research has only traced post-pandemic technological developments. The impact of two years of the pandemic has changed the social order by accelerating oneself to use of technology in everyday life. Naturally, business grows by taking advantage of the conditions of society and its development always precedes its taxation policy. People's consumption pattern preferences have changed from offline to online, even after the pandemic some of these preferences are still more comfortable online.

The implication is that various digital-based businesses are growing that take advantage of the existing marketplace. Various questions arise, whether the taxation aspect is the same as traditional transaction taxation. It can be concluded that the characteristics of the business are the same which distinguishes there is no direct meeting of sellers and buyers in a place or market.

The characteristics of traditional businesses that are the same as the characteristics of digital transactions give rise to the same aspects of taxation, both the subject and object of the tax. Regarding the tax object, both types of transactions are payable for value-added tax and income tax. However, the collection of income tax requires the determination of the tax subject in advance through the determination of the criteria for a permanent establishment. This has become a debate and has come to the attention of the OECD, so the OECD recommends the application of the concept of significant economic presence as an additional provision [13]. Historically, this is in line with the view of [37], those digital transactions as long as they meet the provisions of significant economic presence can be determined as permanent establishment tax subjects with income tax payable. The next review is in the form of a review of the rationality aspect of digital transaction taxation policies.

B. *Rationality*

Rationally, business actors take advantage of business opportunities during pandemic, during a pandemic several business fields have increased during an economic downturn. Businesses that thrive are digital-based both locally and internationally. What is most noticeable is the increasing use of online meeting applications, which until now have become a substitute for offline meetings if they experience certain problems.

The rationale of entrepreneurs, especially foreign individuals, and foreign entities, takes advantage of the shift in consumer preferences for various services, not limited to online entertainment services. The community is greatly helped by the existence of entertainment services during the pandemic without having to leave the house. This public

behavior continues until the time this review article is compiled, which means it becomes a new pattern of consumer preferences. But unfortunately, the taxation rights of a transaction across jurisdictional borders cannot be accelerated in proportion to the growth of businesses that prioritize rationality when there are business opportunities.

The rationality of business growth cannot be separated from the rationality in humans, this is in line with the view that humans always weigh the benefits and sacrifices of a business decision [38]–[40]. What about the rationality of the tax authorities, to review the digital transaction taxation policy? In addition to considering the provisions of the OECD, the tax authorities are obliged to consider the legal hierarchy and the fundamental basis of all policies are the values of Pancasila. The next description is a policy review from the aspect of the actuality of Pancasila values as the fundamental basis.

C. *Actuality*

The actuality stage is the final stage after the historicity and rationality stages before the proposed taxation design for digital transactions. The actuality stage is the stage of actualizing the values of Pancasila in the review of digital transaction taxation policies. The relevant values used as the foundation of digital transaction taxation policies are the values of unity and justice. The value of unity is imbued with divinity and humanity values that give confidence to domestic taxpayers in the importance of unity in building the nation through the fulfillment of tax obligations.

Foreign individuals and foreign entities referring to the Income Tax Law and Indonesia's Tax Treaty with Singapore must meet certain criteria before becoming a permanent establishment. Law no. 2 of 2020 in article 6 paragraph 6 states that there is a significant economic presence in Trading Operators Through Electronic Systems. This provision does not necessarily apply to the subject of foreign individuals and foreign entities that do not use the electronic system. The provisions of article 6 paragraph 6 of Law no. 2 of 2020 is an effort to apply the concept of significant economic presence as a criterion for determining a permanent establishment, but only limited to trading using an electronic system.

The agreement between Indonesia and Singapore to ratify the tax treaty does not contain provisions for the concept of significant economic presence in the determination of BUT. This means that justice between foreign tax subjects and foreign subjects has not been realized properly. Likewise, justice between foreign tax subjects who utilize the electronic system and other foreign tax subjects cannot be realized properly. We return to the proposal from the OECD for three additional criteria that can be used to determine a permanent establishment in the form of revenue, digital administration, and user aspects.

The proposal for the fundamental design of the digital transaction taxation policy begins with determining the tax subject of a permanent establishment. Considering that digital transactions are transactions that cross the jurisdictional limits of a country, the tax subjects are private foreigners and foreign entities. The value of Pancasila justice is applied to the criteria

for determining foreign and domestic tax subjects fairly. Foreign individuals and foreign entities as business actors who meet the criteria for significant economic presence are determined to be foreign tax subjects.

The prerequisite for the growth of the value of unity is the fulfillment of the aspect of justice between foreign tax subjects and domestic tax subjects. The value of unity is a value that unites domestic tax subjects to fulfill their tax obligations. The proposed fundamental design of the digital transaction taxation policy is presented in Chart 1.

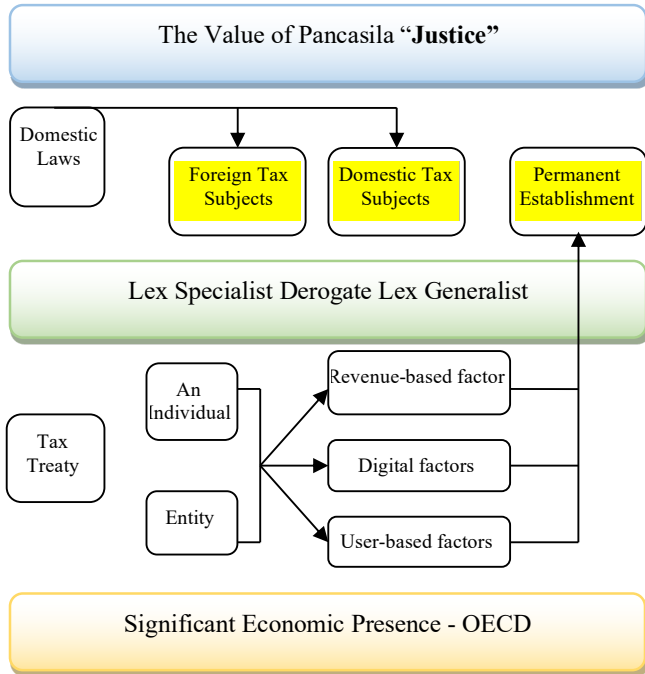


Chart 1. Taxation Design of Digital Transaction

Based on Chart 1. Taxation Design of Digital Transactions, the hierarchy of taxation principles are divided into two, domestic laws and tax treaties. Domestic law consists of Law no. 2 of 2020 and Law no. 7 of 2021. Considering that digital transactions are cross-jurisdictional transactions, the policy review is not limited to domestic laws, but also to tax treaties based on the principle of special provisions (tax treaties) which are superior to general provisions (domestic law).

Reviewing the tax treaty agreement by adopting the concept of significant economic presence from the OECD, the criteria for determining a permanent establishment are not only limited to physical presence. The three factors suggested by the OECD are revenue, digital, and users as criteria for significant economic presence. The value of Pancasila justice is the foundation of the digital transaction taxation policy in the sense that a permanent establishment has obligations equal to domestic tax subjects and foreign tax subjects based on domestic law.

The actual value of Pancasila, in this case, the value of justice, is illustrated in Chart 1. The final part of this policy review shows that the tax authorities face challenges when reviewing tax treaties with agreement partner countries. The

OECD concept can be applied but when cross jurisdictions require more persistent efforts, especially for treaty partner countries that have lost their tax potential. This reflects the rationality of partner country policymakers. Further, conclusions and suggestions for further research are presented.

V. CONCLUSION

This study aims to review how the efforts of the tax authorities to tax digital transactions to improve tax compliance. Historically, digital transactions with traditional transactions have the same characteristics thus, the tax obligations are also the same. The growth of a digital-based business is based on the rationality of considering the benefits and sacrifices. Taxation on the aspect of income tax requires criteria for determining fulfillment as a permanent establishment first. Tax authorities are required to review digital transaction taxation policies with the fulfillment of a sense of fairness of foreign tax subjects with domestic tax subjects.

The value of Pancasila justice in the review of digital transaction policies is translated as justice between foreign tax subjects and domestic tax subjects. When historically they have the same characteristics and the same tax obligations, they are rationally obliged to fulfill their tax obligations in the same way. The fundamental design of digital transaction taxation policies by considering the provisions of the OECD's significant economic presence and paying attention to the legal hierarchy between general principles and specific principles. The main foundation of the digital transaction taxation policy is the value of Pancasila justice, that it can increase the sense of belonging as a trigger for the intention to obey the implementation of the three precepts of unity.

This research is a review of digital transaction taxation policies, further research is needed at a more technical level. Further research is expected to be applied to a specific subject or object of certain digital transactions. It is hoped that this contribution of thought will become part of the slogan of a *Pajak Kita, Untuk Kita*.

ACKNOWLEDGMENT

The authors would like to express their sincerest gratitude to all participants involved in this study and Direktorat Sumber Daya, Direktorat Jenderal Pendidikan Tinggi, Kementerian Pendidikan Kebudayaan, Riset dan Teknologi as a funder of this study.

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