

## Conference Paper

# Application of Adam Smith's Four Canons in E-Commerce Tax Policy

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## Abstract

The e-commerce business has its own character. With the Internet network as the backbone, the transaction process can be done quickly and practically. Different characteristics from the conventional trade proved to be a problem in itself, namely, the difficulty of establishing clear and fair tax rules. There are at least two things that become the problem of taxation caused by e-commerce transactions. The e-commerce transactions according to the OECD which are then adopted into the Directorate General of Taxation No. 62/PJ/2013 (SE-62) can be grouped into four groups: online marketplace, online retail, classified ads, and daily deals. The purpose of this research is to explain and describe the tax policy in Indonesia in the e-commerce business activities and the fulfillment of four cannon Adam smith for e-commerce business activities. The results show that taxes should be neutral and fair to the forms of e-commerce transactions and between conventional transactions and forms of e-commerce transactions. Business decisions should be based on economic motivation rather than tax and taxpayer considerations in the same situation and carrying out the same transaction should be taxed at the same rate. Efficiency of compliance costs by taxpayers and administrative costs of the tax authorities should be minimized. The tax provisions should be clear and easily (Certainty and Simplicity) understandable so that taxpayers can anticipate the tax consequences in the development of transactions including knowing when, where and how the tax should be calculated or paid. Taxation should produce the correct amount of tax in the right time (Effectiveness and Fairness). The potential for tax avoidance and smuggling should be minimized by still trying to anticipate proportionately to the activity.

**Keywords:** tax, e-commerce, policy

## 1. Introduction

In the eighteenth century, Benjamin Franklin said, in this world, nothing is certain but death and taxes. However, the evolution of electronic commerce challenges this venerable adage through elaborate tax avoidance schemes across transnational borders.

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Most developed countries have implemented comprehensive tax regimes which levy income tax on all income earned within its borders. (Downer, Pauline, 2016. Taxation of Electronic Commerce (e-comm): Examination of Canadian Government Tax Policies and Directives Application of Adam Smith's Canons of Taxation, Journal of Financial Management & Analysis) [6].

Issues of cross-border shopping and mail order catalogs have long challenged administration of indirect taxes on a destination basis. However, rapid growth in online transactions and the expansion of digital products—such as video streaming, cloud-based storage, and smartphones—place new pressures on destination-based, subnational transaction taxes, like state and local retail sales and use taxes in the USA. For example, the location of both consumption and sale for digital products is difficult to define and imperfect enforcement capacity allows many remote transactions to effectively escape taxation because they are not taxed at origin or destination. New technologies and digital products challenge the design of decentralized commodity taxes in other countries as well. Canada operates a Goods and Services Tax (GST) with federal and provincial rates; value-added tax (VAT) rates vary within the European Union (EU); and India and Brazil levy state-level rates through their tax systems.

Even highly centralized tax systems are not immune to the pressures of e-commerce. For example, New Zealand's Prime Minister recently indicated that the country is losing significant revenue associated with online and digital transactions and efforts will be made to enhance enforcement. (David R. And William F. 2016, Taxes in an e-commerce generation, Int Tax Public Finance Springer Science Business Media New York 2016 Published on line) [7].

According to Gunadi, Fiscal justice is more aimed at the state of equity, in the sense equally equal sense of the distribution of the burden of state revenues (taxes) to be supported (paid by all citizens). Fairness (equity) in the tax system includes two aspects, namely horizontal and vertical. But in modern taxation systems, piracy justice is very relative and even seems pseudo and very rude. In practice, Gunadi added, preferences and ease of taxation are made available to certain groups of taxpayers or specific economic sectors. Likewise, the complexity of modern taxation provisions and inadequate quality, tax administration support systems inadvertently (effective) member opportunities avoidance or lack of taxation of some people and this is the cause of injustice. Nevertheless, taking into account such challenges and constraints, it is essential for the government to always seek justice in every tax policy

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characteristics from the conventional trade proved to be a problem in itself, namely the difficulty of establishing clear and fair tax rules. There are at least two things that become the problem of taxation caused by e-commerce transactions. The e-commerce transactions according to the OECD which are then adopted into the Directorate General of Taxation No. 62/PJ/2013 (SE-62) can be grouped into four groups: online marketplace, online retail, classified ads, and daily deals. The Circular Letter-62, which is primarily binding only to the Directorate General of Taxation and not to taxpayers, has not regulated the issue of inter-state taxation for e-commerce that can be used for online booking, app stores, cloud computing, participative networked platforms, high speed trading or Even car and hotel booking services arranged centrally outside of Indonesia. Globalization or loss of trade barriers in the world leads to an increase in world trade volume. Increased trade not only drives the technology transfer process, but also accelerates the flow of goods and services. Along with the integration of world trade is also happening process of world financial integration.

Indonesia is one of the countries with the highest economic growth in the world and the largest middle class growth in Southeast Asia. This condition makes Indonesia a fertile ground for business players, especially retail business. The large population (250 million) with per capita income of 3,475 USD is a fat market for these businesses. In addition, traffic conditions in almost all major cities in Indonesia are jammed to make the Indonesian market a belle for foreign business e-commerce. E-commerce is a business transaction that is done electronically so that transactions between buyers and traders can make any sale and purchase transactions, whenever, and wherever. Such flexibility makes e-commerce commerce favored by the modern society of internet use. Although there has been no empirical research, the growth of e-commerce trade is directly proportional to the decline in congestion rates in major cities in Indonesia. Internet penetration in Indonesia to the community has reached approximately 35% of the total population. According to market research institute e-Marketer, the population of Internet users in 2014 reached 83.7 million people. With this number, Indonesia ranks sixth in the world in terms of Internet users. The figure will continue to grow, estimated by 2017 to reach 117 million netizens. While the population of internet users more than 3 (three) hours per day (netizen) based on Markplus Insight is amounted to 36 million people. The amount is an open market for e-commerce traders.

The e-commerce business has its own character. With the Internet network as the backbone, then the transaction process can be done quickly and practically. Different characteristics from the conventional trade proved to be a problem in itself, namely the difficulty of establishing clear and fair tax rules. At least there are two things that

become the problem of taxation caused by e-commerce transactions, namely direct taxes and indirect taxes.

Indirect tax is a tax imposed on consumer goods as well as on value added tax (VAT). The difficulty of determining indirect taxes is caused by the development of the world of information technology, so has added new types of digital products or software (software) that can be traded online. This is certainly different from the conventional trade of goods or products can be viewed physically. The sale and purchase transaction of digital products is done online which only involves two parties, without being noticed at all by the state or both countries from the buyer and seller. The second problem that becomes obstacle in applying of e-commerce tax is effort how to detect transaction of goods in the form of digital so that it can be subject to the application of tax compliance, especially the process of digital goods transactions that occur across the country. It is probable that the potential tax is lost when the transaction cannot be known by the tax authorities in both the seller and buyer origin countries.

For tax on income in direct or direct tax, it was found several obstacles and problems caused by the character of e-commerce business. The first problem is the occurrence of doubt in determining the form of permanent establishment (BUT). Usually in conducting conventional trading business, an overseas company wishing to open a branch in Indonesia, it will be taxed on all its business activities. However, with the character and nature of the e-commerce business, the need to open branches is no longer necessary. While the overseas business actor is free to market their products in various countries including Indonesia.

The second tax problem that arises in e-commerce is the difficulty of determining which countries are entitled to assign and levy taxes on income derived from e-commerce transactions. This is one of them because it is very difficult to track the identity of companies or individuals who play a major role in business. Moreover, trade in the form of electronic digital products. The research question is how the tax policy in Indonesia in the e-commerce business activities and the fulfillment of four canons Adam Smith for e-commerce activities in Indonesia. The purpose of this research is to explain and describe the tax policy in Indonesia in the e-commerce business activities and to explain the fulfillment of four canons of Adam Smith for the e-commerce business activities in Indonesia.

## 2. Literature Review

This study discusses how the fulfillment of the four principles of Adam Smith's fulfillment of e-commerce taxation policy in Indonesia. The first research base used is that of three researchers from different universities in China; Dong-sheng Liu College of Computer Science & Information Engineering Zhejiang Gongshang University Hangzhou, Wei Chen College of Computer Science & Information Engineering Zhejiang Gongshang University of Hangzhou, Shi-wen Gao College of Mechanical and Electrical Engineering, Nanjing University of Aeronautics and Astronautics, China Aerospace of Science and Technology Corporation, Beijing, China under the title Gradual Tax Policies for China's E-commerce Based on Mode Classification presented in 2009 in the International Joint Conference on Artificial Intelligence. This study focuses on the rapid development of the internet, a very sharp increase in e-commerce trading. Furthermore, should tax be levied on the e-commerce transaction and how the tax policy on e-commerce transactions.

The results of this study determined that China made a stage in taxation on e-commerce transactions. Many things are involved in the tax policy on the e-commerce. China should consider the different stages of e-commerce models and adopt a phased tax policy based on classification mode in order to encourage a larger tax base as e-commerce challenges the basic principles of taxation-justice and efficiency. China, has taken a considerable proportion in overall trading volume. The tax base decreases, which has a deadly impact on fiscal revenues. Tax authorities should charge tax on e-commerce. Currently China combines online with offline and trading mode by not getting rid of traditional mode. Therefore, the tax authorities can collaborate with banks and build electronic tax payment systems. It can achieve tax objectives in time and even real-time taxation by controlling capital flows.

Currently, e-commerce in China uses a relatively small proportion. With more and more traditional companies using e-commerce, legal tax avoidance utilizing e-commerce makes fiscal losses more open. With this, the tax authorities should enact laws and regulations as soon as possible and impose the added tax value on real products traded through the Internet.

Further research conducted by Priyanka Meharia under the title e-commerce and taxation: Past, Present and Future, Assistant Professor, Eastern Michigan University, Ypsilanti, MI, USA In The IUP Journal of Accounting Research and Audit Practices. Vol XI No.4 year 2012. This research focuses on several problems. First, illustrate how past and current history of the sales tax policy on e-commerce transactions. Second, examine the effect of e-commerce on taxation and tax implications on the imposition or not

on e-commerce transactions and other tax potential. Third, calculate tax revenue from on-line sales. Fourth, analyze how sales tax by providing a background of the past.

The results of his research include (a) Any solution for Internet taxation will not be easy. Tax laws should be simple and neutral, and should not be a burden for anyone to comply with the rules. Probably the most difficult resolution to enforce would be a permanent ban on all specific e-commerce and internet taxes. This will avoid the harmful competition effects created by competitive tax rates designed to attract foreign investment. Again, however, such a tax policy filing must be agreed upon by every nation by making the right theory, but in fact, it is highly unlikely to be the same tax policy worldwide. (b) Chen and Smekal (2009) temporarily recognize that the main problem with e-commerce along the international line is that it is a 'sovereignty issue'. Buyer countries, in general, have no power to force sellers to collect and provide tax revenues to tax authorities. They also cite 'technical issues' in monitoring e-commerce. In most cases, it is just impractical to expect the importing country of e-commerce to be able to follow and control all phases and traces of transactions. Basu (2007) points out some of the more important points to consider when attempting to collect taxes on e-commerce, which include: (1) Determining the types of taxes to be collected; (2) The ability of vendors to collect taxes; (3) Determine the jurisdiction in which the tax should be applied; (4) Verify the place of consumption; (5) Determine the correct tax treatment of the packaged product; (6) Maintain data; (7) and Comply with audit requirements.

Research conducted by David R. Agrawal and William F. Fox under the title Taxes in an e-commerce generation published in *Int. Tax Public Finance Springer Science Business Media New York 2016* Published on line 1 September 2016. This research focuses on rapid growth in e-commerce has changed the ability of jurisdictions to enforce commodity tax appropriately. This leads to various effective tax rates that depend on the manner in which the goods and services are purchased and the characteristics of both the product and the seller.

The researcher also discusses the argument for the principle of purpose as a place to be taxed as appropriate for consumption taxes in cross-border trade. Furthermore researchers also analyzed recent reforms for value added tax in the EU in response to e-commerce. Then examine various policy options in the United States, maintain the status quo, or change the new rules of the country to adopt information reporting, as well as national reforms that require companies to pay taxes regardless of physical presence and link it to recent European reforms.

His research finds that advances in digital and economic technologies that facilitate long-distance transactions raises new and important policy questions in federation with tax-decentralized commodities, including US retail sales tax and value added tax and Goods and Services tax in some countries. Similar issues can also arise for international transactions. Both the United States and the European Union seek to collect consumption taxes as a basic objective. The optimal tax theory, even when expanded to include administration and compliance, shows that identical tax rates are the best policies for local and long-distance transactions in local markets, although sufficient empirical research is needed before definite conclusions can be reached. However, the inability to enforce objective taxation effectively across open borders has resulted in a favorable tariff (at least in some cases) for e-commerce transactions. In the United States, most of the reforms have been bottom up from the state and are intended for the purpose of improving tax enforcement. However, the US State believes that it is burdened with a standard of physical presence for the seller of collection and remittance of the tax, which is inconsistent with the consumption tax on digital transactions. Furthermore, state-level policy solutions make very different practices throughout the country and are likely to make significant compliance costs, especially when including buyer compliance. Reform at the national level either through Congress (such as the Fair Marketplace Act) or the court system appears to be an important next step that can ultimately reduce compliance costs to effectively enforce goals of a series of state sales taxes. We prefer Congressional laws that better reduce uncertainty and improve appropriate compliance and compliance across countries. Top-down national reform is needed given the rapid pressure of changes on Internet technology on the state tax system. Furthermore, the United States can learn from the EU's top-down reform of e-commerce taxation. Recognizing that tax collection in some countries has the potential to create administrative complexity for many companies, the EU simplifies compliance for digital products through cooperative administration, despite the ability to enforce rules in the US context and new margin effects created by oversimplified simplifications. Researchers also recommend further research on commodity tax reform in countries other than the United States; As a country that changed their treatment of digital products. Researchers believe other countries can learn from the effects of these reforms given that e-commerce poses challenges for all tax systems.

Further research conducted by Pauline Downer C.A., M.B.A., Ph.D. Associate Professor, Faculty of Business Administration Memorial University of Newfoundland: St. John's Newfoundland, Canada published in the Journal of Financial Management & Analysis, 29 (1): 2016; 1-14. Under the title Taxation of Electronic Commerce (e-comm):

Examination of Canadian Government Tax Policies and Directive Application of Adam Smith's Canons of Taxation.

His research focuses that technological advances have changed the way in which business is done. This new-age business can put pressure on traditional principles governing taxation of transnational transactions. This article discusses policy directives enforced by most countries and considers whether traditional policies can or should be applied. The purpose of this study is to examine advanced taxation models in various developed and developing worlds, the Tax Policy will also be reviewed to determine whether the current trend toward electronic commerce taxation is so congruent with the tax base. A review of Canada's taxation system on revenues and the application of traditional concepts to the taxation of electronic commerce in terms of domestic and international perspectives. The trend appears in the international trade taxation in the international front is also checked. In order to ensure a fundamentally electronic tax-trading system, a review of the methods currently being applied to build this system is essential to ensure that the government is taking the right steps.

The results of his research as follows; There are many potential developments that will impact on the issue of electronic commerce taxation in the future. The tax case will provide some clues, however, this will only develop after the government has rationalized their policy on electronic commerce and its taxation. In terms of acting rules that must be applied in the information age, the theoretical aspects of tax policy seem to have been overshadowed. Instead of returning to the essence of taxation policies, legislators have attempted to open to implement the rules developed for e-commerce transactions as mortars to electronic activity occurring in cyberspace. E-commerce is a very different mode of business, consequently, it is not appropriate to apply the standards developed for traditional business activities to this new way of doing business.

Fixed business rules have evolved over time and can be easily applied in the conventional tax system that has developed in most countries both in the application of domestic and international tax laws. These rules are developed to ensure a fair and neutral tax system that allows the most efficient allocation of resources in the economy. The business rules have not been easily adapted in the new e-commerce era. The application of this rule produces systems that influence the behavior of taxpayers to behave in ways that are not characteristic of a fair and neutral tax system. If the tax system is fair and neutral. If a fair and neutral tax system is ideal, attempts to make old rules and regulations work in a dramatically altered environment are acceptable.



### 3. Research Methods

To find out how the fulfillment of four canons of tax (four cannons Adam Smith) on the policy of e-commerce taxation in Indonesia is in accordance with the points of problem formulation, objectives, and benefits of research, then used the paradigm of this research approach is post positivism with data collection techniques through deep interview. The reasons for using post positivism paradigm are among others because researchers will rely on theory in order to provide precise initial guidance and to be analyzed according to the research context.

The data collection of this research using qualitative data collection techniques, with some consideration that is because with this method the data obtained will be more complete, more deeply, credible, and meaningful so that the purpose of research can be achieved. According to Irawan in qualitative research, the methodology used has unique characteristics. These characteristics stem from research issues that start from broad and general questions, flexible, open and qualitative data collection, as well as inferential findings that are inductive and not generalize.

Determination of the type of research is often associated with the objectives to be achieved from the research undertaken. This study aims to provide a description or description of a situation. So that the type of research used is a qualitative descriptive method that is carried out on the fulfillment of the principles of taxation on the policy of e-commerce taxation in Indonesia.

Qualitative data analysis is an analysis performed on non-numeric data such as interviews or reading reports from books, articles, and including non-writings such as photographs, drawings or films, in order to find a common pattern in the form of word-words. Referring to the analysis of qualitative data proposed by Neuman, the data analysis used in this study is the analysis of qualitative data with narrative method. Collected field data will be classified and categorized. Furthermore, the classification of data is related to the existing theme in the theory used to obtain the pattern of e-commerce policy based on the results of in-depth interviews. The data obtained will be triangulated data. Triangulation of this data is done by comparing the primary data and secondary data ever done ago compared with the theory used in this study.

### 4. Analysis and Discussion

Electronic commerce (e-commerce), although widely known as one of trade alternative that has advantages but many are still vague understanding in this regard.

Both beginners and conventional entrepreneurs also want to participate but have little knowledge of e-commerce. Electronic commerce is actually an electronic commerce. Conventional trading and e-commerce both occur because of the transaction between suppliers with consumers, only in e-commerce digitization of information flow, goods and money.

For tax purposes it is necessary to clarify the types of products transacted through e-commerce. Differences in definition of services and intangible goods will create legal certainty in the tax treatment of supplies made by companies abroad. The difference also has the potential to avoid tax evasion and smuggling. The similarity with regard to product definition of e-commerce products will make it easier for taxpayers to comply with tax obligations and will support the e-commerce development efforts themselves. E-commerce adds an entirely new dimension to the already complex world of taxation, along with its enforceability [1]. In particular, the existing problem is territorial jurisdiction. According to Basu, "the disconnection between the geographical basics of the modern tax system on the one hand and the character of the e-commerce region on the other, is at the heart of the challenge that e-commerce provides a new face for taxation."

Basu also added that throughout history, cross-border transaction issues have always proven to be the most problematic. Any discussion of global e-commerce taxation should start with inherent difficulty of effectively verifying the location, identity and residence of the seller or buyer over the Internet. Difficult issues involving jurisdiction begin to emerge when The world's tax system is starting to clash with global e-commerce

In order to fully appreciate the impact of taxes on e-commerce, we need to consider why countries levy taxes and the goals of taxation. The objective of any tax system is to transfer resources from the private sector to the public sector, influence behavior and redistribute the wealth of a nation. Another objective cited by many countries in the development of general tax policy is to ensure that the policy developed emulates policy that has been entrenched in other areas. The goal has been to maintain neutrality, fairness and simplicity as this serves to advance desirable economic activity. Most countries have developed tax policy using a framework developed by the celebrated economist Adam Smith in 1776 and explained in his Treatise. The Wealth of Nations. The four attributes of policy identified by Adam Smith were equality, certainty, and convenience of payment and economy in collection. Each of these is subsequently examined and applied to the taxation of electronic commerce (Downer, Pauline, 2016. Taxation of Electronic Commerce (e-comm): Examination of Canadian Government Tax

Policies and Directives Application of Adam Smith's Canons of Taxation, Journal of Financial Management & Analysis) [4].

America is the first country establishing e-commerce tax policies. In December 1995, Electronic Commerce Tax Study Group was established and began to study relative tax policies. From 1996, zero tax policy on domestic trade and zero tariff policy on international trade has been carried out with measured strokes. On July 1, 1997, US government issued Framework for Global Electronic Commerce, which points out that all governments should manage to encourage and help companies apply Internet into business and meanwhile advises internet free zone. (Dong, Wei and Shi, 2009, Gradual Tax Policies for China's E-commerce Based on Mode Classification, International Joint Conference on Artificial Intelligence) [5].

In June 1998, EU issued a report that how to guarantee revenue from value added tax and promote e-commerce, which requires 20% value added tax on e-commerce, paid by consumers. On July 1, 2003, implementation of value added tax, which prescribe that companies have rights to choose places to pay taxes, the countries where they are registered or the countries where companies sell products. It makes companies transfer to low-tax countries out of tax evasion. On December 4, 2007, EU issued a new value added tax act requiring tax paying in the countries where transactions occur, which avoids that companies conducting e-commerce establish offices in low-tax member states for reducing tax burden. (Op.cit. Dong, Wei and Shi, 2009) [5].

In 1998, Indian government issued laws and regulations to promote e-commerce, and finally got some achievements. However, tax problems caused by e-commerce are increasingly serious. In order to protect benefits, in 1999, India issued the standpoints and policies on taxing e-commerce: payments for goods from Indian companies to American companies through oversea computer systems are regarded as Royalties from India and accordingly withholding tax should be imposed in India. (Op.cit. 2009)

Comparing tax policies in US, EU and India, there exists an agreement of insisting taxation neutral principle although three categories of tax policies are different. This principle has two meanings: one is that taxation should avoid impacting or disturbing production, investment decision-making and consumption choices of tax payers. Market mechanism exerts the role of resource allocation. The other is that taxation doesn't cause other economic losses or additional burdens except for capital loss directly because of taxes. Taxation neutral principle that taxation cannot hinder e-commerce becomes consensus when governments all over the world make tax policies on e-commerce. (Loc. Cit. Dong, Wei and Shi, 2009) [5].

The OECD developed countries in October 1998 have pioneered a discussion of the taxation aspect of e-commerce by holding the OECD Intercultural Conference or the 'Ministerial Conference on Electronic Commerce' in Ottawa Canada. Through its working group with its work program the Committee of Fiscal Affairs (CFA's) group of OECD tax experts. The conference has produced several agendas, among others: (1) Taxpayer Services; (2) Tax Administration, identification and information needs; (3) Tax Collection and Control; (4) Consumption Tax; (5) Tax Arrangement and Co-operation The work program of the Committee of Fiscal Affairs is one of them is trying to clarify about the tax aspects of e-commerce and has resulted in Taxation Framework Conditions include:

1. The principles of taxation applied to conventional trading should also be treated against e-commerce transactions.
2. The CFA (Committee of Fiscal Affairs) believes that existing taxation provisions can implement these principles.
3. The application of these principles to e-commerce should be drawn up to safeguard fiscal authority by a country, and to achieve equitable distribution of tax bases between countries, and to avoid the imposition of double taxation or non-taxable potential.
4. The process of implementing these principles should involve intensive dialogue between OECD countries with business and non-member countries.

One of the primary responsibilities of any free market governance system is to ensure that the tax policy is simple, effective and enforceable. Inefficient taxes and the government's inability to enforce it, are likely to hamper any economic productivity. The fundamental principle of tax policy is that taxes must be economical, neutral and equitable. Taxes are neutral or efficient when not causing taxpayers to change their behavior in response to taxes. Market forces alone must determine the success or failure of methods in conducting commercial activities. Success or failure should be based on the merit of a business venture and not the fact that one way of doing business produces different tax liabilities on other approaches when the income earned from the activity is the same. The second characteristic of a good tax policy identified by Adam Smith is 'certainty'. All tax obligations must be confident and not arbitrary because it will cause the system to be managed the same done by all taxpayers.

Hellerstein concluded in his research that almost all experts and tax experts agree that the state tax must be convinced, uniform and administrable. A world of uncertainty

induces sub-optimal behavior, which can lead to reduced integrity of the current tax system worldwide.

The permanent establishment in the taxation system of Indonesia occupies a special position because in addition to taxation on the permanent establishment is somewhat different from the taxation of the taxpayer in general, also in connection with the tax treaty, the existence or absence of a permanent establishment is crucial. Whether or not a source country imposes a tax on the profits derived by a company domiciled abroad. The term permanent establishment (Permanent Establishment) is known among the worlds of the new Indonesian taxation following the enactment of Law No. 7 of 1983 on Income Taxes, on 1 January 1984.

The definition of a permanent establishment (BUT) pursuant to a P3B is a fixed place of business through which the enterprise is a business of wholly or partly carried on business. One of the main criteria of BUT is the existence of a fixed place which is used to conduct business. Such BUT is often referred to as BUT asset (asset type permanent establishment).

According to the Taxation Agreement The provisions concerning the permanent establishment in a taxation agreement are very important, in addition to determining whether there is a right of a source country to impose tax on business profits received or obtained by a resident company Its partners, also regulates the way of business profits (business profits) of a permanent establishment. The definition of a permanent establishment in the taxation agreement is subject to the understanding granted by the respective tax treaties, which may differ from one taxation agreement to another. Generally, in a permanent establishment agreement (Permanent Establishment) is defined or defined as a fixed place where all or some of the enterprises (overseas) business is run. The existence of a permanent establishment is required two conditions are: (1) The existence of a particular place of business. (2) In the place of business there are business activities (business activities) of a company (overseas) run, either partly or wholly. The taxation of BUT in Indonesia is determined based on the time period applicable in each P3B, as follows: (1) In the event that the term requirement for the existence of BUT in Indonesia is satisfied, it is taxable in Indonesia and subject to the withholding tax in accordance with prevailing regulations. (2) In the event that the term of the BUT is not met, in the case of remuneration, the tax cannot be taxed in Indonesia, the right of taxation is done by the treaty partner of the place of foreign WPA. A physical presence is an office or place of business, agent, or property within the state. A firm 'permanent establishment' decides based on where they are located, but based on the ecommerce 'permanent establishment' can be the location of the server.

At the time of the 'brick-and-mortar' business, a permanent establishment is where a company's store is located. It is identified by where the product is sold from. For example, Barnes and Noble who sell online also have storefronts in some countries, so they have a permanent establishment in each country. Amazon.com has no store and sells all its products online; Therefore, he has no permanent establishment at this time. If the business remains determined by the physical location of the company's servers, internet companies can avoid paying sales taxes by placing servers in countries with lower tax rates. In order to apply the rules of a permanent establishment to the seller, the state shall determine: (1) if the seller's Internet service provider is its agent; and (2) if the website hosting is in a state of creating a permanent establishment. Physical presence, 'standard nexus' is difficult for countries that want sales taxes because most of them have not established a physical presence in all of their states doing business.

In the implementation of ecommerce in Indonesia raises several issues and issues about the legal aspects of trade related to the use of the system formed online. Some of these problems include the traditional legal system has the principles of jurisdiction in a transaction, which concerns the place of transactions, contract law and so forth. E-commerce gives birth to the problem of applying the concept of jurisdiction in the transaction. Place of transactions and contract law must be established cross-border, both regionally and internationally, given the nature of cyberspace that is borderless or does not recognize the borders of a country.

In addition to contract in in this case is a proof of agreement between both parties who make commercial transactions. The problem is that state law on conventional trading considers commercial transactions to be valid, full-strength, and unconditionally specific to be reduced to a written form or also known as paper-based transactions. While in E-commerce, the contract is made electronically and paperless transaction. Document used is a digital document, not a paper document. Actually oral consent is legal and strong enough in making transactions, but of course easy to attack and sought his weakness when faced with legal issues.

On transactions between private parties, invoices, cover letters, and other commercial documents are essentially unnecessary in writing. Nevertheless, tax authorities in many European countries require invoice and other accounting documents in written form. Computerized accounting records are accepted by tax authorities in certain countries, especially in countries where computer systems are capable of handling certain formal requirements specified by the tax administration. Until now still often debate issues of contractual legality in E-commerce transactions. Some opinions suggest the

need to improve the principles of law in conventional contracts, such as the time and place of contract agreement.

The issue of consumer protection is a major factor in the success of an E-commerce application. This is because consumers are parties that determine the viability of electronic commerce. Problems that occur in relation to consumer protection is a fraud that is often done by the seller considering its existence. Problems about the existence of this seller such as the seller is a virtual store or a fictitious on-line store. Another problem that occurs is the condition of the goods purchased, such as goods delivered in damaged condition, the delay of delivery or even goods that have been purchased not sent to the buyer. Not to mention if the problem arises because the purchase order or payment by the buyer is not acknowledged by the seller. Given the importance of the problems that occur then the government should have enacted a law on E-commerce that provides maximum protection to consumers.

In traditional transactions, people recognize signatures. The purpose of a signature in a document is to ensure the authenticity of the document. Electronic transactions also use digital signatures or known as digital signatures. Digital signatures are not actually a signature as it is known so far, which uses a different way of marking a document so that documents or data so as not only to identify from the sender, but also ensure the integrity of the document does not change during the transmission process. A digital signature is based on the content of the message itself. In the E-commerce transaction a digital signature is obtained through a cryptography process.

*Digital or electronic signature here does not mean the writings of signatures made digital images. Digital electronic is obtained by first creating a message digest or hash that is the mathematical summary of the document to be sent via cyberspace. The function of digital signatures is like a fingerprint that is a tool for identifying a sent message. The purpose is to ensure that the message is not sent by others, and as a legally strong proof that the content of the message sent by the sender has been approved by the sender*

During this digital signature is a method of security in the use of public networks as a means of data transfer is quite 'safe'. It is said to be safe because the digital signature forms from the assemblies of an algorithm that are very difficult to trace or break. But, very difficult does not mean cannot. Some forms of crime in counterfeiting digital signatures use software that can generate such digital signatures.

Adam Smith's four cannons principles that should be applied to electronic transactions (e-commerce) in Indonesia in cross-border transactions with other countries include:

1. Neutrality, taxes should be neutral and fair to forms of e-commerce transactions and between conventional transactions and other forms of e-commerce transactions. Business decisions should be based on economic motivation rather than tax and taxpayer considerations in the same situation and carrying out the same transaction should be taxed at the same rate.
2. Efficiency, compliance costs by taxpayers and administrative costs of the tax authorities should be minimized.
3. Certainty and Simplicity, tax provisions should be clear and easy to understand so that taxpayers can anticipate tax consequences in the development of transactions including knowing when, where and how the tax should be calculated/paid.
4. Effectiveness and Fairness, taxation should produce the correct amount of tax in the right time. The potential for tax avoidance and smuggling should be minimized by still trying to anticipate proportionately to the activity.
5. Flexibility, taxation system should be flexible and dynamic to support system that always follow technological development and trade transaction development.

## 5. Conclusion

Indonesia's tax policy on e-commerce is not yet supported by a comprehensive taxation system on tax systems, supervision, special units and prevention of tax evasion. Almost all other countries prepare well for taxation on e-commerce transactions. The fulfillment of the four principles of taxation Adam Smith remains the cornerstone that should be held by the government in applying it to e-commerce.

## 6. Suggestion

The Indonesian government needs to follow the example of other countries in anticipating e-commerce transactions and make a comprehensive policy move to support the application of e-commerce tax in accordance with the principles of taxation.



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