

## Conference Paper

# Analysis of Acceptable Tax Avoidance in Good Business Purpose at Indonesia

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## Abstract

The loss of the boundaries of a country in free trade and globalization promotes the flow of goods and services to be increased. It is also a result of the current financial integration. In addition to the factors of labor, natural resources, bureaucracy, tax issues also become one of the considerations for investors to invest. Many companies in the world do tax planning in order to minimize their tax liabilities. The Government of Indonesia, as one investment destination of foreign investment, should have a policy of anti-tax avoidance. This was done in addition to providing justice for all businesses and also providing legal certainty in order to enforce tax obligations. The anti-tax avoidance policies will shut down and deter the opportunities for aggressive tax avoidance. This study was conducted to discuss the anti-tax avoidance policies in good business practice in Indonesia. Referring to the theoretical perspectives, research paradigms are used, and the nature of this research is descriptive with qualitative analysis. The performance of the company in the context of acceptable tax planning that is transfer pricing, tax haven country utilization, thin capitalization, treaty shopping and Controlled Foreign Corporation. Efforts should be done by the government in addition to the importance of checks and improvement of regulations and making them effective in order to counteract tax avoidance practices and exchange of information on domestic and international level.

**Keywords:** investment, tax, tax avoidance

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## 1. Introduction

Taxation is one of the dynamic fiscal policy instruments, their application must always follow the dynamics of the economy, both domestically and internationally. Given the two functions inherent in the tax (BudgetAir and regulerend), then the tax collection is not only intended to maintain and increase the momentum of economic growth, is also pushing state revenue. Therefore, every year the Government is required to always

improve acceptance of the tax sector in line with increasing demand for development funds [21].

For more than two decades, revenues from the tax sector in Indonesia is experiencing an ever-increasing trend. Until now, not less than 80% of the budget revenue and expenditure (APBN) funded by receipts from the tax sector. As an inward-looking policy, tax receipts are expected to reduce dependence on foreign debt and be able to revive the confidence of the Indonesian nation. This is in harmony with the mission carried by the tax authorities as the competent tax authorities in the country, which collect revenues from taxes to support the independence of the state budget [12].

TABLE 1: Comparison of draft state budget 2014 and 2015 (in Trillion Rupiah).

No.	Commentary	APBN-P 2014	RAPBN 2015
1	Tax revenue	1.246	1.370
1	Domestic Tax	1.189	1.319
	(1) Income Tax	569.8	636
	(a) Oil and gas income tax	83.8	82.9
	(b) Non-oil income tax	485.9	553.12
	(2) VAT	475.58	524.97
	(3) United Nations	21.74	26.68
	(4) Excise	117.45	125.94
	(5) Other taxes	5.17	5.68
2	Tax International Trade	56.28	51.5
	(1) Import duty	35.67	37.2
	(2) The exit tax	20.6	14.2

Source: Nota Proposed Budget 2015.

Economic globalization has brought increased foreign investment between countries. There are several reasons that encourage investment from one country to another, namely: to spread the risk, because the domestic market conditions that are not supported or because of differences in the exchange rate as the outlook for growth and large (Easson: 2003: 17).

According to Hady (1998:5) in terms of its objectives, the investment can be classified into two types of investment. The first type of investment is a portfolio investment, that is, investments in financial assets such as stocks, bonds and other forms of other securities. The nature of movement in the investment portfolio and from all

corners of the world through the international money market relatively quickly. The second type of investment is a direct investment is investment substantially in the form of the establishment of the company, construction of the plant, the purchase of capital goods, land, raw materials. In this case the investor is directly involved in the management of companies and control the activities of the capital investment. Direct Investment usually begins with the establishment of subsidiaries or the purchase of a majority share of a domestic company. In the international context, this form of investment is usually conducted by a multinational company with general investment activities in manufacturing, the extraction and exploration of natural resources as well as the service industry.

According to Easson (2003: 18) Foreign Direct Investment (FDI) can be done in many forms, namely the purchase of assets in the country where the investment, transfer of assets to the countries where investments, reinvesting profits earned in the country of investment, including the acquisition of a majority stake or lending to subsidiaries or affiliates.

In order to manage the wealth of the company's profit and maximize the value of the company, the company's management will make a decision through a thorough consideration. One important component into consideration the company is a tax, therefore, the tax should be well planned. Efforts to minimize the tax burden carried by making tax planning. Simply put Spitz (1983) provides a definition of tax planning as follows: "Tax planning is arrangement of a person's business and/or private affairs in order to minimize tax liability." So simply tax planning is the efforts made by the taxpayer to minimize tax payable. The purpose of tax planning are things so that the tax burden as low as possible by utilizing the existing regulations.

This is in line with the opinion of Farid Ahmad was quoted as saying by Gunadi (2007: 16) which defines tax planning as follows:

*Tax planning is a series of processes or actions taken taxpayer to manipulate the sources of income and expenses as well as other transactions with the objective of minimizing, suspension or elimination of the tax burden which is well within the framework of the legislation. To reach this objective, employers should take advantage of every deduction, exclusion, exemption, convenience, and credit provided by the provisions and the tax administration.*

## 2. Main Problem

Conceptually tax planning includes both tax cuts permanent and the possibility of suspension. Tax savings can be obtained from tax planning involving several concepts such as: the use of tax exemption, reduction in overall tax rates, maximization of income reduction, acceleration of expenditure, delays to tax, transaction structuring taxable become taxable.

The purpose of international tax planning according to Spitz (1983) is to minimize or defer taxation legally in order to achieve the desired business, anticipating double taxation and gain the benefits of a relationship between two or more tax systems and the factors non-other taxes, Thus, the research problems can be formulated as follows:

1. How does the practice of tax planning undertaken by the company?
2. What is the government doing to make acceptable tax planning?

## 3. Objective

In accordance with the formulation of the aforementioned problem, the purpose of this study are as follows:

1. Know and explain the practice of tax planning undertaken by the company.
2. Know and explain the government's move to make acceptable tax planning.

## 4. Research Methods

In order to know the practice of acceptable tax planning companies and government steps in making acceptable tax planning in accordance with the grain of the formulation of the problem, objectives, then used a research approach using qualitative research methods. According to the qualitative Irawan in other research, the methodology used has unique characteristics. The characteristics of the problem stems from studies initiated broad and general questions, data collection is flexible, open and qualitative, as well as inductive inference and findings are not generalizable ([19]: 61).

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The qualitative method was also selected for the qualitative method can give details about the complex phenomenon difficult to express by quantitative methods ([3]: 5). Moreover this method also chosen because it has the same specific characteristics with the characteristics of qualitative research. A qualitative approach is expected to understand the social phenomena studied holistic overview of the report's views in detail and arranged in a scientific background.

This study aims to understand the social phenomenon that exists through a picture that is both deep and comprehensive (holistic). In other words, this study was conducted to understand the meaningful social action. This study aimed to get an overview and a deep understanding of the practice of acceptable tax planning companies and government steps in making acceptable tax planning.

This study aims to provide a description or picture of a situation. So that kind of research is a qualitative descriptive method performed on the Indonesian tax system. In conducting this research, collecting data from two sources, namely; the study of literature and documentary studies.

Qualitative data analysis is the analysis of the data of the non-numbers such as interviews or reports record readings from books, articles, and including non-writings with the aim of seeking a common pattern in the form of words description word ([19]: 99). Referring to the analysis of qualitative data presented by Neuman (2003: 448-449), the analysis of the data used in this study is qualitative data analysis with narrative method.

## 5. Discussion and Analysis

Tax planning made by the taxpayer included to minimize the tax payable can be done in various ways, whether they comply with the provisions of taxation (lawful) or who violate tax laws (unlawful). The term is often used is tax avoidance and tax evasion. Tax avoidance and tax evasion are aiming to reduce or minimize the tax payable. In this case the tax avoidance is done in ways that do not violate the applicable provisions namely by exploiting the weaknesses contained in the applicable regulations, while tax evasion is done in ways that are illegal (in violation of applicable regulations).

Often in practice the line between tax avoidance practices with tax evasion is difficult to distinguish. Although it is legal tax avoidance and tax evasion can be distinguished, but economically good tax planning through tax avoidance and tax evasion are equally result in reduced tax revenue. According to Gunadi (2007) avoidance (avoidance) mainly involves the commercialization and effectively use the fiscal policy and deviate legitimate technical and ambiguities in laws and regulations. Meanwhile, smuggling or tax evasion, and the like (tax evasion) mainly occurs by omission or under-reporting of taxable income are sometimes supported by engineering the legal, accounting and other administrative.

Prasetyo (2008:44) cites the opinion of Prebble in his article mentioned that tax avoidance has several characteristics, among others: The transaction, often false, transactions carried out not have a meaning economically meaningful, the absence of the element of risk and their efforts to exploit loopholes in tax regulatory.

Furthermore, fiscal affairs committee of the OECD (Organization for Economic Cooperation and Development) adds that other characteristics of tax avoidance is that secrecy is a form of this scheme is generally the consultant showed how a tool or avoidance on condition Taxpayers maintain as confidential.

Rohatgi (2002) stated that in many countries differentiated tax evasion on tax evasion allowable (acceptable tax planning) and that is not allowed (unacceptable tax planning). That is, tax avoidance may be illegal if the transaction is carried out solely for the purpose of tax evasion or do not have a good business purpose (a bona fide business purpose). Between one country and another may have a different view about any scheme that can be categorized as acceptable or unacceptable tax planning tax planning. A transaction will be called as unacceptable tax planning or aggressive tax planning if they have these characteristics: does not have a goal attempt was good, solely to avoid taxes, not in accordance with the spirit and intention of parliament and the transactions that are engineered to cause charge fees or loss. Instead, a transaction is classified as acceptable tax planning if it meets the following characteristics: has a good business purpose and not solely to avoid taxes, in accordance with the spirit and intention of parliament and no transaction engineered.

In line with the aforementioned, Kessler (in [23]) states that the form of tax avoidance which is prohibited is when the action of taxpayers correctly according to the 'letter of the law' but incorrectly or not in accordance with the intent of lawmakers (spirit and intension of parliament). Based on the aforementioned, it can be said that the term of tax avoidance is more complex than the term tax evasion.

For many countries the problem of tax avoidance and tax evasion is a concern of government, because the practice is contrary to the principle of fairness in taxation, a serious impact on state revenue from taxes and distort international competition and capital flows. On that basis, the OECD (1998) (Organization for Economic Co-operation and Development) provide recommendations to its member states to anticipate practices of tax evasion as follows: First; strengthen the tax rules and tax assessment and investigation in an effort to detect and anticipate practices of tax evasion. Second; facilitate, improve and expand the exchange of information between tax administrations in order to combat international tax evasion practices. Third; exchange of experience on an ongoing basis on techniques to detect and anticipate practices of tax evasion and improve tax compliance.

In tax planning, multinational companies have many opportunities compared to domestic companies because they have the geographic flexibility in placing economic resources in accordance with the system of production and distribution. The flexibility of a variety of geographically to minimize the total tax burden of global companies. Shifting income and costs through internal engineering between members of multinational corporations has the potential to minimize the global tax burden.

From some international tax literature it is known that there are some tax avoidance schemes are often done by multinationals, namely:

1. Transfer Pricing. According to Gunadi (1994:184) Transfer pricing is the amount of the price on delivery (transfer) of goods or services in return for the delivery of which has been agreed by both parties in the business and financial transactions. In the context of transfer pricing taxation is used to manipulate the price of the imposition of a transaction between the companies related in order to minimize the burden of the tax due on the overall group of companies.

Transfer pricing is also a means of distributing profits among companies in the business group is determined by the discretion of the parent company, so that the tax liability between the companies can be arranged. Given these transactions take place between the parties related, are that the price tends not to be arm's length (reasonable price). In the end there was a shift in the tax base from one country to another.

The imposition of unreasonable price for transactions between companies that have a special relationship that ultimately resulted in profit-sharing between multinational companies operating in many of these countries becomes unnatural. Transfer pricing policy aimed at maximizing the efficiency of the group as a

totality and profitable business (investment) group of global companies. In this case the motivation of tax on transfer pricing practices implemented wherever possible to move income to countries with the lowest tax burden or minimal.

Transfer pricing between taxpayers (WPDN) with others who are abroad (transfer pricing transnational) is generally carried out for the purpose: to maximize income economic entities, securing competition subsidiaries or branches (market penetration), evaluates the performance of its subsidiaries or foreign branches, to avoid exchange rate fluctuations, mengatrol 'prestige' of the association, increase the share of joint venture profits, reduce financial risk, and securing cash flow of subsidiaries.

From the foregoing it is clear that in terms of multinational companies, transfer pricing is a tool to mobilize operating income for the purposes of its business. Meanwhile, from the state, transfer pricing practice protocols can result in distortion of state revenues from taxes.

To determine whether the transactions that occurred between the parties related are in accordance with the principle of arm's length, so to prevent the practice of transfer pricing method applied method to determine the arm's length. In the case of transfer pricing, pricing/fair value (arm's length price) is defined as the price that must be paid by parties who are not related to the same or similar goods.

In determining the price or the fair value of transactions which occur between the parties related, pricing or the fair value of transactions conducted using the base equivalent to that carried out by parties who are not related. A transaction can be considered equivalent if the differences existing in the comparable transaction did not have a significant impact or differences can be eliminated by making the necessary adjustment.

The principle of arm's length price is also applied in any double taxation avoidance agreement (tax treaty). Countries that make an agreement given the authority to apply the arm's length price of the transactions carried out by parties related. Definition of the term special relationship itself is usually not defined but refers to the domestic understanding of each country.

2. Utilization of tax haven country. International tax evasion through the use of tax haven countries are important and of concern to the majority of countries, particularly developed countries. According to Spitz (1983: 31-32) terminology refers to the tax haven jurisdictions where there is no tax, tax is only levied on



certain transaction and lower tariffs on profits derived from overseas or special treatment other types of transactions are taxable.

State tax havens cannot be clearly defined because it is relative, that depends on the provisions of each country in defining it. A country may be referred to as a tax haven by another country if that country provides an incentive in the economic activity in a particular area within that country. So, whether a country will be classified as a tax haven countries or by other countries depends on the definition of tax haven countries provided by the other country.

Since there is no formal definition of tax haven countries, to determine that a country can be classified as a tax haven country can be seen from the following criteria: First; do not collect taxes at all or if the tax levy, then the charge is low tax rates. Second; have strict regulations on bank secrecy and/or business confidential and will not disclose such confidentiality to anyone or any country, although it is possible disclosure by an international treaty. Third; available facilities of modern communication tools that enable communication across the world without any obstacles. Fourth; lax supervision of foreign exchange flows, including deposits coming from foreign countries, both individual and corporate. Fifth; the promotion and the belief that the tax haven countries a financial center is good and guaranteed ([15]: 328)

In addition to these things Kristanto (2007:39) add a that other characteristics of tax havens are: lack of exchange of information, lack of transparency, lack of activity is substantial and the ring fencing where the facility is valid only in the area concerned. Considering there is no formal definition of tax haven, then some countries define a country included in the category of tax havens if they meet the criteria set by the country concerned.

Thus it can be said that what is meant by the countries tax havens are countries that deliberately giving tax facility either in the form of taxation which is very low or not taxed at all to taxpayers in other countries so that income of a taxpayer other State transferred to country. Actions taken by the tax haven countries and countries that have a 'preferential tax regime' by taxing at low rates or even to apply tariffs of 0% by the OECD as 'Harmful tax competition'. These countries deemed to unfair competition, because it is not based on the 'level playing field'.

3. Thin Capitalization. According to Gunadi (2007: 279) Thin capitalization is the practice of finance branches or subsidiaries of larger interest debt rather than with equity. Roy Rohatgi (2002: 396) states that the thin capitalization is a disguised

capital through loans that exceed the limits of reasonableness. In the context of thin capitalization loan is a loan in the form of money or capital from shareholders or parties that have a special relationship with the borrower.

In general, interest paid to the lender who is not resident in the borrowing country can be used as a deduction on taxable income of the borrower, while the dividend cannot be used as a deduction. If a company decides to finance most of the company by way of a loan with interest to the parent company, the subsidiaries income tax liability can be reduced. This would be a great advantage if the tax payer subsidiary to a parent company subject to withholding tax rates are low.

According to Gunadi (2007:198), lending in the practice of thin capitalization can be done in several ways, namely: 1) direct loan, 2) back-to-back loan, and 3) a parallel loan. In direct loans (direct loans), investors (shareholders) WPLN directly provide loans to the child company. In connection with the utilization of the loan, the investor earns interest that the amount is generally determined by the investor. Meanwhile, on the approach back to back loan funds to the investor submit a mediator as a third party to immediately loaned to the subsidiary by giving rewards. To counteract the efforts of tax evasion by taxpayers through the thin capitalization, several countries have thin capitalization rules. Tax consequences arising on the application of the thin capitalization of the subsidiaries in the source country can be divided into three categories, namely: the classification of debt as capital, interest charges cannot be charged to subsidiaries and interest payment classification as a distribution of profit on capital.

4. Treaty Shopping. Tax treaty can be made the object to perform the activities of tax evasion, although the purpose of the tax treaty itself is to prevent tax evasion. The practice of treaty shopping by thuronyi made by a resident of a country that does not have a tax treaty established a subsidiary in the State which has a tax treaty and conduct investment activities through its subsidiaries, so that investors can enjoy low tax rate and the facilities other tax listed in the treaty tax.

The practice of treaty shopping to be done to take advantage of treaty benefits. In this case the facilities listed in the tax treaty (treaty benefits) can only be enjoyed by resident (subject to tax in the country) of both countries that the treaty. According Mansury (1999: 215) for the use of the facilities the relevant tax treaty two requirements must be met. The first requirement is a formal requirement (administrative requirement) which is proof that the person concerned is a resident of the state that the treaty was a 'Certificate of Resident (COR)' issued

by the competent authority in the country treaty partner. The second condition is the condition of the material (substantive requirement), namely that the taxpayer in the country treaty partner is actually resident (resident) in the partner country and not resident third country.

5. Controlled Foreign Corporation (CFC). In this case the practice of tax avoidance is done by delaying the recognition of capital income is sourced from abroad (especially in tax haven countries) to be taxed in the country. The practice of tax evasion through the CFC by setting up overseas entities where taxpayers (WPDN) has control.

According to Arnold (2002: 81) There are several ways to do tax avoidance in connection with the use of CFCs, among others: First; Taxes shall be able to divert revenues sourced from domestic to overseas entities it controls (controlled foreign entity) incorporated in tax haven countries. Second; Taxes shall be able to establish a subsidiary in a tax haven country to obtain a source of income abroad or to receive dividends or other distributions from subsidiaries outside the country.

WPDN effort to minimize the amount of taxes paid on investments made abroad is to secure the profits should be distributed to its shareholders. By utilizing a special relationship and a majority ownership stake, enterprises abroad can be controlled so that the dividend is not distributed/suspended. The aforementioned efforts will be more profitable for the company if the foreign business entity in the country was established in tax havens or low tax jurisdiction.

To counteract the practice of tax evasion are necessary to CFC Rule. In connection with the CFC Rules, Pinto (2003: 325) gives the following opinion:

*CFC legislation Applies to resident shareholders with regard to non-resident corporation directly or indirectly controlled by them. It taxes the undistributed profits of the CFC in the hands of the resident shareholder. Eventhough there are some differences in the ownership thresholds of the foreign entity for its application, a minimum degree of connection with the CFC at least sufficient to Confer A Certain decisional power on the domestic shareholders is Necessary to justify current taxation on the basis of Reviews their influence on the decision to repatriate its profits.*

In this case the CFC Rule apply to taxpayers who directly or indirectly controls the taxpayer abroad, which are taxed is CFC undistributed profits to its shareholders.

Besides ownership to taxpayers abroad must exceed the specified minimum. Thus the taxpayer in the country have the effect of delaying the distribution of profit.

In connection with the use of CFC Rules, Surahmat further confirm that basically CFC Rules are rules to prevent taxpayers of a country do the tax deferral on income, by carrying out transactions or investments in the Country, known as tax havens, because tax rates in countries the very low or no taxes at all. Generally the purpose of CFC Rules is that the taxpayer does not shift income out of the country by establishing a company in Country specific for taxation provisions are very loose.

In facing the practices of tax evasion committed by multinational companies is generally a state issue regulations prevention of tax avoidance are specific (Specific Anti Avoidance Rule/SAAR) regulated in domestic law, such as controlled foreign company, an arm's length rule, advance pricing agreement, and a debt to equity ratio. In practice in some countries, specific anti-avoidance rule to be effective in efforts to deter tax evasion practices and provide legal certainty for the taxpayer.

In addition to the provisions of a specific nature, in many countries also issued tax evasion prevention provisions of a general nature (General Anti Avoidance Rule/GAAR). The goal made the prevention of tax evasion provision of a general nature is to anticipate tax avoidance practices not covered under the provisions of a special nature or to counter tax avoidance actions which at the time made the regulations have not known. This is done on the grounds that there is a tendency of tax evasion practices from year to year more and more sophisticated and harder to detect and resisted only by relying on Specific Anti Avoidance Rule 62. In this case the tax planning undertaken by the taxpayer no longer defensive tax planning, but has more offensive is often known as aggressive tax planning ([30]: 192–193)

Furthermore Cooper (1997: 31) says that the General Anti Avoidance Rule shall contain a distinction between transactions that are categorized as acceptable tax planning and tax planning are classified as unacceptable because not all tax evasion is offensive. Makhfatih (2005) in his dissertation cites the opinion of Uppal and Reksohadiprodjo (1999) and Sour (2001: 3) states that the motivation to do the avoidance or evasion of tax in Indonesia is partly due karena<sup>64</sup>: lack of education, lack of supervision and law enforcement, government performance and external factors, namely: regulatory and market mechanisms.

In order to save the state revenues from taxes, the government can intervene, either directly (direct government involvement) or indirectly (government influence) that is through regulation. According to the effective regulation to achieve the public interest is an essential function of government. In an effort to anticipate error or

untruth taxpayer in tax reporting, tax systems must be equipped with the provisions regarding both research and examination of the reports submitted by the taxpayer. In addition to law enforcement efforts on the implementation of the tax obligations of taxpayers and tax authorities increased knowledge regarding tax matters is also an important thing to note.

## 6. Conclusions and Suggestions

The performance of the company in the context of acceptable tax planning that is transfer pricing, tax haven country utilization, thin capitalization, controlled treaty shopping and Foreign Corporation.

Efforts should be made the government is in addition to the importance of the examination and refinement of rules and regulations to effectively counteract tax evasion practices, also required the cooperation between tax administrations of both domestic and international information exchange. To counteract the practices of tax evasion (tax avoidance) government must make efforts, among others, as follows:

1. Improving the tax regulations.
2. supervision/inspection on the implementation of the tax obligations of taxpayers.
3. Improving education taxation for tax officials.
4. exchange of information both at domestic and international level.

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