Exploring The Arm’s Length Transfer Pricing Strategy for Taxation Purposes: An Ethnographic Study in a Manufacturing Enterprise

Alfa Rahmiati*, Resti Sandi*
*Universitas Airlangga

ABSTRACT

Practices of transfer pricing in among companies having “special relationship” (hubungan istimewa in Bahasa Indonesia, this study uses a term of ‘related party’) to others are very common nowadays. However, the complexity of transfer pricing strategy and practices in many companies made the use of individual level data become insufficient, therefore we conduct an ethnographic study to explore how taxpayer determines the reasonable transfer pricing based on five methods (i.e. Comparable uncontrolled Price/CUP, Resale Price/RPM, Cost Plus, Transactional Net Margin Method/TNMM and Profit Split Method/PSM). This research aims to execute a tax strategy based on those methods, which finally derive the amount of product price according to arm’s length transfer pricing rule. We collected the data through interviews, observation and literatures. They are based on several months of personal experience of field research in and around the manufacturing enterprise. The results showed that the tax expense could be reduced by using Cost Plus Method, but practically, the application of this method requires more in-depth analysis and a very reliable & comparative data so the company must spend a lot of cost and time to process it. The Transactional Net Profit Method is proved to be the best application for the enterprise to optimize tax expenses because the data used for the analysis were more accessible which saved time and costs.

1. Introduction

Indonesian economy experienced the slowest growth rate during 2014-2015. This condition has happened since 2009. According to World Bank’s quarterly report per July 2015; the growth is projected at 4.7% in 2015, down from a previous projection of 5.2% for real output growth. However, there were still positive developments stretching the manufacturing industry in the second quarter of 2015. Nikkei Indonesia mentioned Indonesia’s Performance Manufacturing Index (PMI) continued to increase compared to May and April during that year. In June 2015, PMI Indonesia was in a position of 47.8, an upward trend compared to May (47.1) and April (46.7).

This increasing number indicates that Indonesia's manufacturing industry performance is still contracting. The World Bank estimates that manufacturing industry in Indonesia will be increasing more in the future because of the demand for domestic consumption and high investment growth. In fact, the growth of manufacturing Indonesia is higher than China and India, and it is becoming a strong capital for Indonesia to enter the era of the ASEAN Economic Community (AEC) by 2015.

However, the rise of Indonesia's manufacturing industry does not necessarily make the exports become a significant increase. Press Release Central Bureau of Statistics reported that Indonesian exports in 2014 reached US $ 176.036 billion. This figure has decreased compared to exports value in 2013 amounted to USD 182.551 billion. Similarly, compared to the exports of 2012, the value of exports decreased by USD 190.020 billion. The decline of the exports is due to the fact that most Indonesian manufacturing company produces goods or services and sell it to the parent company abroad. Naturally, subsidiaries will conduct transactions with the parent company if they both have a special relationship.
There are many regulations about a “special relationship”. Indonesian Statement of Financial Accounting Standards (Pernyataan Standar Akuntansi Keuangan/PSAK) No. 7 states that a company may be considered to have a special relationship with other companies if one part has a significant influence to the other parties. Meanwhile, according to Indonesian tax regulation (Undang-undang No. 36 Year 2008, Fourth Amendment UU 7 of 1983 on Income Tax), one of the special relationship conditions is one of the company has an equity capital either directly and indirectly for at least 25% in other companies.

Obviously, the main objective of the company is making an optimal profit at a lowest cost, including costs associated with tax obligations. To do this, tax planning is an essential strategy undertaken by the company to minimize the tax burden without violating tax laws and regulations. Pohan (2013) states that it is human nature to think that, if you can not pay, why you should pay. If you can pay less, why you should pay more. But this should all be carried out in ways that do not violate the rules of taxation applicable in Indonesia.

There are many types of tax plannings to minimize tax burden. For frequent subsidiary sales transactions with its parent, the tax planning that is often used is the one involving transfer pricing. In general, the definition of the transfer pricing is a set of transaction price occurs between the divisions that exist in a company. According to Plesner, Rossing and Rohde (2014), transfer pricing has a significant role in today’s business. Darussalam et al. (2013) mentions that the transfer pricing can be viewed and applied from three different perspectives, namely company law, managerial accounting, and taxation. In terms of company law, the transfer pricing can be used as a tool to improve the efficiency and synergy between the company and its shareholders. However, the transfer pricing policy which should protect the creditors and minority shareholders of treatment is often unfair. In terms of managerial accounting, transfer pricing can be used to maximize the profits of an enterprise through the pricing of goods or services by an organizational unit of a company to the other organizational units within the same company. In the perspective of taxation, transfer pricing is a pricing policy in the transactions carried out by related parties.

There are some interesting phenomena about the application of transfer pricing; particularly for some companies that conduct transactions with other companies and they are related parties (i.e. hubungan istimewa - in Indonesian Tax Law). This can often be indicated by the tax authorities as the shape-shifting of the tax burden, which may lead to an avoidance of tax burden that should be paid to the state treasury. Darussalam et al. (2013) call it as a “pejorative”, namely the transfer of the taxable income of a company within a group of multinational companies to other companies in the same group of multinational companies in the country with lower tax rate. The practice of transfer pricing that are often used by employers is to set up subsidiaries in certain countries which have lower tax rates or do not even tax at all. These countries are referred to as Tax Haven Country. These countries become a haven for entrepreneurs who want to hide from the tax obligation.

For preventing the tax avoidance by transfer pricing method, DGT (Directorate General of Taxation), which is the Indonesian taxation authority issues a regulation PER-43/PJ/2010, which last amended as PER-32/PJ/2011. It stipulates the application of Arm’s Length Principle (ALP). This principle contains transfers mechanism with reasonable price for companies when they make transactions with a related party and non related party. This prices are applied to the companies having related parties and is compared to companies that do not have related parties. The result should be the same or comparable. Article 1 paragraph 5 sets clearly on the application of this principle.

As noted by the regulation, the application of transfer pricing become very crucial nowadays, thus this study aims to assess qualitatively the extent to which the application of transfer pricing in accordance with tax provisions in Indonesia. Moreover the understanding of international transfer pricing in Indonesia practically remains limited. Therefore this study is necessary to be done. Meanwhile, there is an increasing tax regulatory pressure in Asia on multinational enterprises (Anonymous, 2011) which need inter-disciplinary approach to implement.

Transfer pricing should be seen in a holistic view. People must recognize multi-roles and consider some different methods. As tax research in Indonesia has not been integrated, there might be a flaw leverage synergies of combined research approach. With this reason, transfer pricing issue is a challenging topic to be researched, as it involves inter-company transfer, interact with several aspects in an organisation, and related to resource allocations, performance evaluation, tax management and business strategy. Hence this research is expected to serve as an integrated empirical evidence in Indonesia.

This study uses a case study of PT ABC, a manufacturing company which is located in Sidoarjo. PT ABC is chosen because it conducts transactions with overseas related party. This company is one of multinational enterprise that practice transfer pricing, and is scrutinized by the tax authority in Indonesia. The condition in PT ABC makes transfer pricing issues become more complex. This research will show how tax planning, especially on transactions involving transfer pricing issues in order to minimize the tax burden according to Indonesian Tax Laws.

The main contribution of this study is threefold. First, this paper provides an empirical evidence of a manufacturing company from a case study in Indonesia which performs transaction with overseas related party to show directly how transfer pricing is implemented. Second, the conclusion of this study has a practical implication for manufacturing companies in general and tax policy makers; the results of this study can be used as a reference of transfer pricing implementation. The outcome of transfer pricing method also serves as
references for practitioners to see the performance of transfer pricing system, which finally could provide directions for the refinement of current transfer pricing system. Third, the results of this study are expected to provide a reference for further researches on tax planning for transfer pricing.

2. Literature Review

2.1. Some Definitions of Special Relationship (Related Parties/Enterprise/Hubungan Istimewa)

PSAK No. 7 Year 2009 has several definitions of related parties: “The parties are said to have a special relationship if a) one of the parties has the authority and ability to control the other party or has significant influence in the decision making process in both financial and operational companies, b) Any transactions that occur between parties who have a special relationship is a transfer of resources or obligations between the parties and they did not see the importance of price calculation, c) The parties can have a control to the other parties if it has a direct ownership through subsidiaries with more than half of the voting rights and has the power to direct the company's policy with regard to financial and operating companies under the agreement that has been agreed, d) One party is said to have a significant influence in the company if they have a stake in the decision making for the company’s financial and operation, but not for controlling those policies, for example to formulate a company policy, conduct transactions with parties and exchange the managerial employees or reliance on technical information.

Meanwhile, Undang-Undang (Law) Number 36 Year 2008 article 18 paragraph 4 Fourth Amendment of Law Number 7 of 1983 on Income Tax states special relationship condition. It referred to paragraph (3) and (3a), Article 18 paragraph (4), Article 9 paragraph (1) letter f, and Article 10 paragraph (1), which considered; there is a special relationship if taxpayer has equity participation, directly or indirectly at least 25% in the other taxpayer, or the relationship between the taxpayer involves at least 25% participation of two or more taxpayer which above all can affect the price, when the possibility of reduced rates are lower than the market price. In such case, the tax base is a fair market price prevailing on the free market.

2.2. The Concept of Transfer Pricing

According to Indonesian taxation regulation, transfer pricing must be implemented based on law of Directorate General of Taxation (DGT) number PER-43/PJ/2010 which was last amended as PER-32/PJ/2011. This law explains that transfer pricing between the parties which have a special relationship are required to apply the principles of fairness and prevalence Enterprises (Arm’s Length Principle). Specified price/income/earnings of a company dealing with those who do not have a special relationship is considered into a comparison or used as a measure of the fairness of the price level. This price or income comparison is called reasonable price or a reasonable profit.

As mentioned in article 3 of the regulation; there are several steps to implement the principles of fairness and the prevalence of this business. The first step is to conduct a functional analysis, the second step is to do comparative analysis and then determine the most appropriate methods of transfer pricing based on previous analysis. A functional analysis (according to PER-43/PJ/2010 which was last amended as PER-32/PJ/2011, Article 7) is a process to identify and compare the significant economic activity and the primary responsibility is taken by those who have a special relationship with parties who are not involved as a special related party. Comparative analysis (according to PER-43/PJ/2010 which was last amended as PER-32/PJ/2011 chapter 4) is an analysis conducted to compare the degree of comparative transactions that occur among enterprises having a special relationship and between a company with those who do not have a special relationship. There is no difference in the material that may affect the price or profit of the comparable transactions. In fact there are some differences in condition but it can still be adjusted to remove the material or other influences which could make differences in price and profit.

2.3. Methods of Determining Transfer Pricing

Based on PER-43/PJ/2010 which was last amended as PER-32/PJ/2011, there are five methods to determine a transfer pricing, namely:

a. Comparable uncontrolled Price (CUP) is a price comparison method between parties that do not have any special relationship;

b. Resale Price Method (RPM) is a method that compares the price of the transactions between parties that have a special relationship with the product resale price after deduction of gross profit to those who do not have any special relationship.

c. Methods Cost-Plus (Cost Plus Method) is a method of adding a reasonable level of gross profit obtained by the same company from transactions with parties who are not having special relationship or a reasonable rate of gross profit obtained by other companies of comparable transactions with parties who are not having special relationship to the cost of goods sold

d. Transactional Net Margin Method (TNMM) is a method that compares the percentage of net income of the...
components that contribute to the transactions of related parties with the percentage of net income of the
components that contribute in comparable transactions carried out by the nonrelated parties.

e. Profit Split Method (PSM) is a method that determines the allocation of profits by related parties to the
nonrelated parties.

3. Research Method

This study is a qualitative research, which particularly applies an ethnographic design as proposed by
James P Spradley (McCurdy et al., 2004). This study aims to determine the most suitable transfer pricing
method for a company. This method needs some in-depth understanding of a company’s daily life so that they
properly generate product and services, as well as the business policies. Ethnographic design fits the goal of
this study, as this design was to learn the culture or day-to-day life of the community to discover what one need
to know in order to react like the people who lived in the company. The second author of this paper is the
person who collected the data comprehensively as she worked as the tax consultant of PT ABC, thus she could
articulate the whole pictures of company’s daily activity. Ghony and Almanshur (2012) mentions four stages of
ethnographic data analysis (as presented in Table 1):

- Domain Analysis
  Domain analysis is performed to obtain a general and comprehensive picture of the object under
  research or social background. Domain analysis is only used to get a general idea of research focus.

- Taxonomy Analysis
  Taxonomy analysis is the next step of the domain analysis. The objective is to make observations and
  interviews in line with the previous focus chosen by the researchers. Unlike the domain analysis, this
  analysis is performed on a particular domain in order to explain the research focus.

- Component Analysis
  In this analysis, researchers are looking for a difference and contrast by doing an observation,
  interviews and document study. Researchers look for differences between the elements in the domain
  being studied.

- Theme Analysis
  When analyzing the themes, the researchers attempt to find relations and important points that
  integrate the domains studied.

<table>
<thead>
<tr>
<th>Table 1</th>
<th>The Analysis Stages</th>
<th>Details of Analysis</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domain analysis</td>
<td>1. Identifying any special relationship between the parent company (PT FG) and the subsidiary (PT ABC).</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2. Identifying internal sales transactions that occur between PT FG and PT ABC.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>3. Identifying transfer pricing and its implementation.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>4. Identifying the tax burden</td>
<td></td>
</tr>
<tr>
<td></td>
<td>5. Identifying the proper tax planning for companies that set transfer pricing.</td>
<td></td>
</tr>
<tr>
<td>Taxonomy Analysis</td>
<td>1. Conducting interviews with accounting and tax staff of PT ABC about the special relationship between PT ABC and PT FG related to the internal sales transactions between them.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2. Conducting interviews with the manager of Tax Consultants Office; regarding the selection of the most appropriate tax planning method.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>3. Conducting an interview with Directorate General of Customs and Excise staff about issues related to transfer pricing.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>4. Conducting an interview with some members of Tax Office “GH” examiner team regarding a tax audit or examination for taxpayers who apply some transfer pricing transactions.</td>
<td></td>
</tr>
<tr>
<td>Component Analysis</td>
<td>1. Performing a functional analysis to identify the functions within an enterprise.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2. Performing a comparative analysis of the five methods in determining transfer pricing.</td>
<td></td>
</tr>
<tr>
<td>Theme Analysis</td>
<td>Choosing one of the most appropriate transfer pricing methods in the tax laws, which can contribute the lowest tax cost.</td>
<td></td>
</tr>
</tbody>
</table>

Sources: data processed (2016)

4. Analysis and Discussion

The subject of this research is PT. ABC, which is engaged in manufacturing and trading company located
in Sidoarjo, East Java. This company manufactures and exports shoes. The object of research is the sales
transactions between PT ABC and PT. FG (the parent company of PT. ABC). The transactions were classified
as a transaction involving special relationship parties because PT FG has more than 25% equity participation in
PT ABC. So PT ABC should implements a transfer pricing when conducting sales transactions with PT FG. The
price agreed by both companies is usually below the market price. However, according to the tax regulation, this kind of price is one of tax evasion form to minimize the burden of the company tax.

As mentioned earlier, PT. ABC is located in Indonesia and PT. FG is based in Taiwan. Companies that are located in two different countries automatically have different tax regulations, especially in terms of tax rates. In this case, tax rates refer to the corporate income tax rates. These tax rates are charged to the company. The target of PT. ABC to minimize the tax burden would be achieved if the corporate tax rate applicable in Taiwan is lower than Indonesia. During this research period, tax rate in Taiwan is 17%, which is lower than tax rate in Indonesia (25%).

4.1. Domain Analysis and Taxonomy Analysis

At the early stage of analysis, a special relationship between PT FG as the parent company and the ABC Company as a subsidiary is identified. According to article 18 of Law No. 36 Year 2008 and regarding Fourth Amendment of Law No. 7 of 1983 on Income Tax, "A party is said to have a special relationship with another party if the taxpayer has equity participation, directly or indirectly at least 25% in the other taxpayer, or the relationship between the taxpayer at least 25% participation in two Taxpayers or more ... " and the special relationship can affect the price i.e. at a price that is determined at a lower value than the market price. Based on the company documents provided during observation, PT.FG had direct equity participation with PT ABC as 51.1%. This is consistent with the definition of related parties in accordance with Statement of Financial Accounting Standards (SFAS) and Law 36 Year 2008 regarding Fourth Amendment of Law No. 7 of 1983 on Income Tax (directly at least 25% equity participation in the other tax payer).

The process of identification of internal sales transactions between PT FG and PT ABC was conducted by interviewing some people working at PT ABC. From the interviews, it is identified that the sales made by PT ABC is not only with other companies but also with PT FG which is the parent company. It happens due to a consideration that selling products to the parent company is a form of cost efficiency. This phenomenon is confirmed by the results of interviews with an employee of a Tax Consultant:

"... sah-sah saja kalau perusahaan jual ke induk (perusahaan). Salah satu tujuannya ya untuk efisiensi biaya...." (Interview with the general manager of A Tax Consultants, April 4, 2014)

In one year, the sales volume of PT ABC to PT FG is much larger than the sales of PT ABC to other companies. The total sales of PT ABC to PT FG are considered reasonable because there is a special relationship and market conditions also affect the level of sales. The similar view is also expressed by the Accounting Staff as follows:

"Sebenarnya keadaan market pada tahun yang bersangkutan menjadi penentu tinggi rendahnya penjualan itu. Kalau market-nya bagus ya jual kesana (induk perusahaan yaitu PT.FG) terus. Kalau market-nya lesu ya bisa jual ke tempat lain."

"Actually, the state of the market during the year is a determinant of sales volume. If there is a good market, then the company will keep selling the product to parent company. But if the market is worse, then PT ABC will sell products to other places. "(Interview with Accounting and Tax staff of PT.ABC, April 4, 2014)

The next analysis is identifying the opportunities of transfer pricing. The special relationship between PT. ABC and PT FG provides a great opportunity for the application of transfer pricing. Transfer pricing is the price made by the agreement between the two parties that have a special relationship. The general purpose of transfer pricing application is to streamline the corporate tax burden but not to avoid taxes. As the taxonomic analysis phase, the argument is strengthened through an interview with a Tax Consultant

"Harga transfer adalah harga yang terjadi di antara dua belah pihak yang punya hubungan istimewa untuk efisiensi pajak tapi bukan menghindari pajak lho. Kalau menghindari pajak ya kita nggak bayar sama sekali tapi kita "kan bayar pajak namun lebih efisien karena ada perencanan pajak untuk penerapan harga transfer itu tadi."

Transfer pricing is the price that exists between two parties that have special relationship for tax efficiency, but not for evading taxes. If we evade the taxes, means we do not pay at all. However, we do pay the tax; but in more efficient way. It is because there is a tax planning for the implementation of the transfer pricing. "(Interview with an Officer of Tax Consultants, April 4, 2014)

Other taxonomic analysis is performed by the Directorate General of Customs and Excise (DGCE), known as body that monitors and assigns certain sizes in the customs value. It plays an important role in the application of transfer pricing that occurs in existing companies in Indonesia. DGCE has certain standards in applying the customs value based on PMK 160/2010 on the customs value. The price listed in the database is
taken from the price that goes through the import transaction. However, for the export or foreign sales, the DGCE does not have certain standards in monitoring export prices. It is because the export activities are encouraged by the government. A staff of DGCE said:


“We set customs value based PMK 160/2010. But only the value of imports, because the export is encouraged by government to inject income to our country. We actually have a database price but it is not published. The database was compiled based on the prices of goods which entered Indonesia and prices can change at any time.” (Interview with a staff of DGCE, 15 April 2014)

To identify the appropriate tax planning for companies that implement a transfer pricing, a comparative analysis is conducted. When we perform the comparative analysis, the company must make a comparison as the basis for selecting the method of transfer pricing for the company. Comparative analysis is done only to compare transactions between PT. ABC and PT. FG as having a special relationship and also to compare transactions conducted by PT. ABC with independent parties.

The Tax authorities have certain standards in determining whether or not a reasonable transfer pricing applied by a company. The standard is obtained through benchmarking in several similar companies. If a reasonable transfer price could not be identified, the tax authorities may approve the transfer pricing used by the taxpayer in question. The Taxonomy analysis of this issue is an interview with a tax officer as follows:

“...kita benchmarking dulu kalau masih belum ketemu juga harga real nya, ya kita pakai harga yang dipakai oleh Wajib Pajak....”

“... first we will do a benchmarking. If we still cannot detect its real price, we use the prices used by the taxpayer ....” (interviews with team members of Tax Office examiner “GH”, June 4, 2014)

4.2. Component Analysis

The component analysis consists of two stages: 1) functional analysis and 2) comparative analysis. The functional analysis is performed in much kind of analyses. The first analysis is related to the functioning of the company. PT ABC is a company that acquires raw materials and processes them into finished goods as well as storing and subsequently distributing the finished goods to their consumers. In short, the most dominant function in PT. ABC is a manufacturing function.

The second functional analysis is an risk analysis. As mentioned earlier, the function of PT ABC is a manufacturing company which have some risk in its, manufacturing activities such as the risk of scarcity of raw materials, failed products, production capacity risks, marketing risks that cause the goods are not sold in the market, the risk of currency and exchange rate fluctuation, and the risks caused by a riot outside the company that may occur due to strike action by workers who ask for a raise.

The third functional analysis is related to the assets of the company. The main assets consist of fixed assets. The fixed assets owned by PT ABC are related to manufacturing function. It consists of some machines used for processing the raw materials and the machines used for sorting products that will be sold to consumers. Besides the machine, there is also a factory building used as a place for company operations ranging from sorting of raw materials to finished goods storage (warehouse). Vehicle is also one of the tangible fixed assets owned by the company which is used as a means of transportation for taking and delivering the raw materials to the finished good available for sale.

The next step is performing comparative analysis. The comparative analysis for Comparable uncontrolled Price (CUP) method is conducted by focusing on two transaction price: 1) transaction price between PT. ABC and PT. FG and 2) the transaction price agreed by PT. ABC with independent companies (companies that do not have a special relationship) namely PT. "CBA". Meanwhile, the comparative analysis for Resale Price Method (RPM) is occurs when PT. ABC sells merchandise to PT. FG (there is a special relationship) for USD 8.5, then PT. FG resells the merchandise that has been purchased from PT. ABC to PT. "DEF" at USD 14.5 (there is no special relationship between PT. FG and PT. "DEF"). The expected profit rate is 20%. Thus the reasonable selling price is obtained by the following calculation: Reasonable price = USD 14.5 - (20% x USD 14.5) = USD 11.6

Comparative analysis on Cost Plus Method is done by adding the rate of gross profit earned by the company when dealing with those who have a special relationship with the gross profit earned by the company from transactions carried out by an independent company. In other words, if companies choose this method, PT. ABC determines first what percentage of the level of margin to be added to the cost of which will be a fair selling price.
Comparative analysis on Transactional Net Margin Method (TNMM) is performed by using net income as the main data in the analysis process. This method compares the net profit earned by the company when conducting a transaction with a related party and independent company. PT. "PMM" is chosen as a comparison.

<table>
<thead>
<tr>
<th>No</th>
<th>Description</th>
<th>No Transfer Pricing</th>
<th>CUP</th>
<th>RPM</th>
<th>Cost Plus</th>
<th>TNMM</th>
<th>PSM</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Price per unit (USD)</td>
<td>8,50</td>
<td>10,50</td>
<td>11,60</td>
<td>10,28</td>
<td>10,46</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Exchange rate 31 Dec 2012</td>
<td>9.708,00</td>
<td>9.708,00</td>
<td>9.708,00</td>
<td>9.708,00</td>
<td>9.708,00</td>
<td>9.708,00</td>
</tr>
<tr>
<td></td>
<td>Price per unit (Rp)</td>
<td>82.518,00</td>
<td>101.934,00</td>
<td>112.612,80</td>
<td>99.798,24</td>
<td>101.545,68</td>
<td>-</td>
</tr>
<tr>
<td>2</td>
<td>Production (unit)</td>
<td>1.359.296</td>
<td>1.359.296</td>
<td>1.359.296</td>
<td>1.359.296</td>
<td>1.359.296</td>
<td>1.359.296</td>
</tr>
<tr>
<td>3</td>
<td>Total Sales</td>
<td>112.166.387,328</td>
<td>138.558.478,464</td>
<td>153.074.128,589</td>
<td>135.655.348,439</td>
<td>138.030.636,641</td>
<td>-</td>
</tr>
<tr>
<td>4</td>
<td>COGS</td>
<td>105.436.404,088</td>
<td>130.244.969,756</td>
<td>143.889.680,873</td>
<td>127.516.027,533</td>
<td>129.748.798,443</td>
<td>-</td>
</tr>
<tr>
<td>5</td>
<td>Gross Profit</td>
<td>6.729.983,240</td>
<td>8.313.508,708</td>
<td>9.184.447,715</td>
<td>8.139.320,906</td>
<td>8.281.838,198</td>
<td>-</td>
</tr>
<tr>
<td>6</td>
<td>Expenses</td>
<td>5.793.339,085</td>
<td>7.156.477,693</td>
<td>7.906.203,928</td>
<td>7.006.532,447</td>
<td>7.126.007,867</td>
<td>-</td>
</tr>
<tr>
<td>7</td>
<td>Profit before tax</td>
<td>936.644.155</td>
<td>1.157.031,014</td>
<td>1.278.243,787</td>
<td>1.132.788,460</td>
<td>1.155.830,332</td>
<td>-</td>
</tr>
<tr>
<td>8</td>
<td>Income Tax</td>
<td>234.161.039</td>
<td>289.257,754</td>
<td>319.560.947</td>
<td>283.197.115</td>
<td>288.957.583</td>
<td>-</td>
</tr>
<tr>
<td>9</td>
<td>Profit after tax</td>
<td>702.483.116</td>
<td>867.773,261</td>
<td>958.682.840</td>
<td>849.591.345</td>
<td>866.872,749</td>
<td>-</td>
</tr>
</tbody>
</table>

Source: The internal data of PT ABC, with additional process

Theme Analysis is performed using five methods in accordance to PER-43/PJ/2010 which was last amended as PER-32/PJ/2011. The comparison result is shown in Table 2. It shows that the most appropriate method to be applied for determining the transfer pricing is the Cost Plus Method; particularly in terms of the most efficient tax cost. However, it should be reviewed whether this method best suited to the company. The reason is Cost Plus Method is a traditional method that requires an ideal comparison. Moreover this method is very difficult to be implemented since the process of finding the appropriate comparison companies involves in-depth analyses, takes a lot of time and high cost.

Transactional Net Margin Method is in the second rank of most efficient tax expense. It serves as an alternative to Cost Plus Method. Gathering the data to perform this analysis using this method is not difficult with the help of a commercial database that is much more practical compared to Cost Plus Method analysis. Thus the most appropriate method to be applied by PT ABC is TNMM. From the four methods that have been tested, this method gives the most efficient tax expenses and the data needed is not complicated and does not need some in-depth analyses either.

5. Conclusion

To sum up, the proper tax planning strategy of transfer pricing at PT ABC is the Transactional Net Margin Method (TNMM). This is due to several reasons as follows:

- TNMM is able to reduce the corporate tax burden better than other methods. For example, if it is compared to RPM methods, PT ABC can save tax amounted Rp 30.603.364. With lower income tax amount, this method already fulfilled the Arms Length principle.

- Although TNMM is not the best method for tax saving, the application of TNMM is not too difficult. Applying first rank method (Cost plus) in practice can experience hurdles. Determining a mark-up cost through benchmarking analysis can be very complex, for example some companies record certain cost in their cost of good sold, while others may record in operating expenses. This inconsistency may create difficulties in determining the mark-up cost. In contrast, TNMM method is easier to be implemented because the net profit data is often available for public. Hence, TNMM provides better benefit in terms of saving time and expenses.

It should be noted that the conclusion above is based on restricted transactions. The result is based on observation and interviews of the researcher who worked in the company in a particular period and thus cannot be concluded for all transactions in PT ABC before nor after the researcher’s working period. Based on this limitation, future researchers can examine the implementation of transfer pricing in multi years period (this research only conducts a year study).
References