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Tax Risk Mitigation and Legal Certainty for Corporate Taxpayers

Muhammad Basir[1], Mustofa Kamil[2], Siti Humulhaer[3]
[1-3] Master of Laws Program, Graduate School, Universitas Islam Syekh-Yusuf Tangerang, Indonesia and
*Corresponding author: basircyio@yahoo.com

ABSTRACT

The pursuit of revenue optimization through Compliance Risk Management (CRM)-based supervision raises questions about legal certainty for Indonesian Corporate Taxpayers. This study examines disputes concerning the deductibility of expenses incurred to earn, collect, and maintain income (3M expenses), the post-HPP Law substance over form doctrine, the transition from Requests for Explanation of Data and/or Information (SP2DK) to tax audits, domestic related-party transfer pricing adjustments, and the distinction between administrative and criminal tax liability. Using a qualitative juridical-empirical (socio-legal) design, the study combines in-depth interviews with tax practitioners, academics, corporate representatives, and supervisory informants with analysis of statutes and related scholarship. The findings indicate that disputes over 3M expenses reflect tension between the Business Judgment Rule and narrow fiscal interpretations; opaque CRM risk profiling may create false-positive classifications and disproportionate evidentiary burdens; and unilateral transfer pricing adjustments without domestic corresponding adjustments risk economic double taxation. The study also emphasizes the need to distinguish administrative adjustments, negligent violations, and intentional offenses based on mens rea while applying the ultimum remedium principle. To strengthen ex-ante protection, it proposes a five-pillar evidentiary package for deductible expenses, objective business-purpose and economic-substance tests, and a Three-Tier Test Tax Defense File for affiliated transactions. Greater CRM transparency and consistent application of good governance principles are recommended.

Keywords: *Corporate Taxpayers, Legal Certainty, SP2DK, Substance Over Form, Tax Risk Mitigation, Ultimum Remedium.*

1. INTRODUCTION

Taxation constitutes a foundational pillar of Indonesia's fiscal sovereignty, anchored explicitly in Article 23A of the 1945 Constitution of the Republic of Indonesia, which mandates that taxes and other compulsory levies for state purposes be regulated by statute. This constitutional directive is operationalized through Law No. 6 of 1983 on General Provisions and Tax Procedures, as amended most recently by Law No. 7 of 2021 on the Harmonization of Tax Regulations (HPP Law) and Law No. 6 of 2023 on the Stipulation of the Job Creation Government Regulation in Lieu of Law into Law. Within Indonesia's self-assessment tax architecture, Corporate Taxpayers are entrusted with the statutory responsibility to calculate, pay, and report their tax obligations independently [1]. However, in contemporary fiscal governance, escalating State Budget (APBN) revenue targets have placed the Directorate General of Taxes (DGT) in a paradoxical position: balancing its mandate as a public service institution fostering voluntary compliance against mounting institutional pressure to maximize short-term tax collection [2], [3].

This structural tension directly affects the legal certainty and operational stability of Corporate Taxpayers. Given the complexity of corporate commercial accounting, multi-tiered group structures, and recurring divergences between commercial financial reporting and fiscal rules, corporations sit at the epicenter of risk-based tax supervision under the Compliance Risk Management (CRM) framework. While administrative digitalization through the Core Tax System promises enhanced efficiency, scholarly discourse raises critical concerns that opaque algorithmic risk profiling generates systemic bias and exacerbates information asymmetry between tax authorities and taxpayers [4], [5]. When discretionary audit powers are not constrained by rigid

procedural safeguards, the state's sovereign power to tax risks degenerating into administrative arbitrariness (*détournement de pouvoir*), undermining legal certainty as the cornerstone of a healthy investment climate [6], [7].

Empirical manifestations of legal uncertainty for Corporate Taxpayers converge around four critical nodes. First, interpretive ambiguity governs the deductibility of expenses incurred to earn, collect, and maintain income (commonly termed 3M expenses) under Article 6(1) in conjunction with Article 9(1) of the Income Tax Law (UU PPh), where tax auditors frequently disallow marketing, promotional, or management service expenses due to a perceived lack of immediate revenue correlation. Second, the absence of objective limiting parameters in enforcing the substance over form principle strengthened under the HPP Law enables authorities to disregard valid civil contracts unilaterally [8], [9]. Third, reliance on unverified third-party data within a black-box CRM system triggers Requests for Explanation of Data and/or Information (SP2DK) under DGT Circular Letter No. SE-05/PJ/2022. In domestic affiliated transactions, contested SP2DK clarifications rapidly escalate into Special Tax Audits under Article 29 of the UU KUP, creating economic double taxation when upward transfer pricing adjustments at the paying subsidiary lack corresponding downward adjustments at the domestic recipient entity [10]. Fourth, the blurred boundary between civil administrative tax adjustments and criminal tax liability under Articles 38, 39, and 39A of the UU KUP poses existential threats to corporate going concern and executive governance [11], [12].

Accordingly, this study examines: (1) the interpretive ambiguities surrounding deductible 3M expenses and the normative boundaries of fiscal discretion; (2) the legal ramifications of the substance over form principle post-HPP Law alongside evidentiary distortions generated by black-box CRM algorithms; (3) the procedural transition from persuasive SP2DK supervision to formal audits in domestic related-party transactions and the resulting risk of economic double taxation; and (4) the doctrinal demarcation separating administrative adjustments, negligence, and intentional tax offenses under the *ultimum remedium* principle to formulate a robust corporate tax risk mitigation model.

2. LITERATURE REVIEW

To evaluate the tension between discretionary fiscal enforcement and the constitutional protection of Corporate Taxpayers, this research deploys a hierarchical theoretical architecture integrating Grand Theory, Middle-Range Theory, and Applied/Supporting Theory.

At the Grand Theory level, the analysis is anchored in the Rule of Law (Rechtsstaat), the Legal Certainty Theory which mandates statutory predictability and strict constraints on administrative discretion to prevent abuse of power (détournement de pouvoir) pursuant to Article 28D(1) of the 1945 Constitution [7] and the Dignified Justice Theory, which positions the protection of human dignity and substantive rights at the core of legal enforcement. Under administrative law doctrine, the principle of legality of government action (rechtmatigheid van bestuur) requires every tax assessment to rest upon valid procedural safeguards and verified material facts.

At the Middle-Range Theory level, four analytical lenses bridge constitutional norms with tax administration practice. First, Ian Ayres and John Braithwaite's Responsive Regulation Theory conceptualizes an Enforcement Pyramid wherein regulators prioritize persuasive, dialogic soft enforcement (SP2DK) at the base before escalating to coercive hard enforcement (audits and criminal investigation) at the apex [13]. Second, Erich Kirchler's Slippery Slope Framework posits that tax compliance emerges from the interplay between trust in authorities which fosters voluntary

compliance and power of authorities which produces enforced compliance [14], [15]. Third, Agency Theory [16] illuminates the structural information asymmetry separating corporate management as agents from tax authorities as principals. Fourth, Tom Tyler's Procedural Justice Theory demonstrates that institutional legitimacy and long-term compliance depend fundamentally on perceived procedural fairness and the right to be heard (audi alteram partem) during tax disputes [17], [18].

At the Applied and Supporting Theory level, the study incorporates the corporate governance doctrine of the Business Judgment Rule [19], the Arm's Length Principle (ALP) governing related-party transactions [20], the substance over form doctrine bounded by business purpose and economic substance tests [21], the General Principles of Good Governance (AAUPB) codified in Article 10 of Law No. 30 of 2014 [6], and the ultimum remedium principle in tax criminal law [22], [23].

3. METHODS

This study adopts a juridical-empirical (socio-legal) approach utilizing a qualitative-descriptive design [24]. The juridical dimension analyzes statutory coherence and administrative legality across the 1945 Constitution, the UU KUP as amended by the HPP Law and Job Creation Law, the Income Tax Law, Law No. 30 of 2014 on Government Administration, Ministry of Finance Regulations (PMK No. 17/PMK.03/2013 as amended by PMK No. 18/PMK.03/2021 and updated via PMK No. 15 of 2025), and DGT Circular Letter No. SE-05/PJ/2022. The empirical dimension investigates practical enforcement dynamics, evidentiary burdens, and compliance pressures experienced by corporate entities during pre-audit supervision and formal tax audits.

Primary data were gathered through semi-structured in-depth interviews with purposively selected key informants possessing authoritative expertise and direct operational involvement, comprising: (1) a senior tax practitioner and expert witness from the Indonesian Association of Tax Practitioners and Consultants (PERJAKIN); (2) a business and tax law academic; (3) a tax accounting and economics scholar; (4) a criminal law specialist; and (5) primary corporate informants representing a domestic group subsidiary (PT A) and a standalone Taxable Entrepreneur (PKP) law firm (Law Firm B), complemented by supervisory perspectives from the Tax Service Office (KPP). Secondary data encompassed primary statutory instruments, peer-reviewed international and national legal scholarship, and administrative correspondence records. Data trustworthiness was ensured through source and methodological triangulation, followed by qualitative data reduction, comparative matrix mapping between normative ideals (*das sollen*) and field realities (*das sein*), and multi-tiered theoretical synthesis.

4. RESULTS AND DISCUSSION

4.1 Interpretive Ambiguity of Deductible 3M Expenses and Normative Limits on Fiscal Discretion

Empirical interviews with key informants and corporate tax executives reveal that substantive corporate income tax disputes predominantly originate in the examination of deductible expenses incurred to earn, collect, and maintain income (3M expenses) under Article 6(1) jo. Article 9(1) of the Income Tax Law. From a tax accounting perspective, a recurrent systemic vulnerability among Indonesian corporations is the failure to maintain a comprehensive audit trail linking commercial bookkeeping, Fiscal Reconciliation Working Papers, and the Cash Flow Statement [25]. When corporations fail to substantiate permanent differences and timing differences clearly, field auditors frequently abandon direct audit verification in favor of indirect audit methods (such as the indirect cash flow method). Reliance on speculative indirect estimations inflates positive fiscal

adjustments, escalates external compliance costs, and threatens corporate working capital and going concern [26], [27].

From a business and administrative law standpoint, disputes over 3M deductibility reflect a fundamental collision between two legal paradigms. On one side, corporate directors operate under the protection of the Business Judgment Rule (Article 97(5) of Law No. 40 of 2007 on Limited Liability Companies), which grants managerial discretion to allocate expenditures for marketing, brand promotion, research, consultancy, and management services in good faith to sustain long-term enterprise value [19], [28]. On the other side, tax auditors frequently apply a rigid strict legal interpretation, demanding an immediate, direct causal nexus between an expenditure and revenue generation within the exact same fiscal year [29]. Unilaterally disallowing multi-year promotional investments or management fees merely because immediate net profits did not materialize in the current period constitutes an arbitrary expansion of administrative discretion that violates legal certainty.

Furthermore, practitioner insights indicate that field auditors often rely excessively on formal account nomenclature (chart of accounts) within commercial income statements rather than evaluating the underlying economic reality of transactions (substance over label) [30], [31]. In the professional services sector exemplified by standalone PKP law firms (Law Firm B) legitimate operational outlays such as external specialist honoraria, advocate retainers, and field litigation expenses are routinely challenged for lacking physical deliverables typical of manufacturing enterprises. Disregarding valid evidentiary records breaches the Principle of Carefulness and the Prohibition of Abuse of Authority under the AAUPB pursuant to Article 10 of Law No. 30 of 2014.

To bridge this evidentiary divide and safeguard legal certainty, Corporate Taxpayers must construct an integrated five-pillar material evidentiary package: (1) formal contracts or engagement letters specifying mutual rights, obligations, and cost-allocation formulas; (2) valid invoices and Tax Invoices aligned with accounting recognition periods; (3) bank statements and wire transfer records demonstrating genuine cash outflows; (4) tangible deliverables such as technical reports, meeting minutes, advocate timesheets, or project documentation; and (5) an Economic Benefit Test Report articulating the concrete operational contribution of the expenditure to 3M activities. Institutionalizing this five-pillar standard operationalizes *audi alteram partem* under Procedural Justice Theory and restores equilibrium within the self-assessment regime [17], [32].

4.2 Substance Over Form Enforcement Post-HPP Law and Algorithmic Distortions in Black-Box CRM

The enactment of the HPP Law reinforced the statutory authority of tax officials to invoke the substance over form principle as a general anti-avoidance mechanism, a trajectory subsequently addressed in judicial guidance through Supreme Court Circular Letter No. 2 of 2024 [8], [33]. Doctrinally, substance over form is designed to neutralize artificial arrangements that exploit formal legal structures to erode the tax base. Nevertheless, juridical analysis indicates that without strict objective constraints, expanding this doctrine invites détournement de pouvoir. Auditors risk invalidating civil contracts that fully satisfy the validity requirements of Article 1320 of the Indonesian Civil Code merely to recharacterize transactions into higher-taxed categories, thereby infringing upon freedom of contract [21], [34].

To curb unbounded fiscal discretion, tax authorities must be legally required to satisfy two cumulative objective tests prior to recharacterizing any corporate transaction under substance over form. First, under the Business Purpose Test, the authority bears the burden of demonstrating objectively that the transaction structure lacks any rational non-tax commercial purpose [35], [36]. Second, under the Economic Substance Test, the authority must prove that no genuine transfer of business functions, assets, commercial risks, or economic benefits occurred between the contracting parties [37]. Where a transaction satisfies both criteria, its civil legal form must be respected to preserve legal predictability.

Concurrently, empirical evaluation of digital tax administration reveals a critical paradox within the DGT's Compliance Risk Management (CRM) system and Core Tax System integration. Although designed to leverage big data and machine learning for targeted compliance risk profiling [4], [5], the risk indicators, weighting algorithms, and third-party data-matching methodologies remain strictly opaque (black box) to taxpayers [38], [39]. This algorithmic opacity generates acute legal and economic distortions, synthesized in Table 1.

Table 1. Normative ideals, CRM field realities, and impacts on corporate taxpayers

Analytical Dimension	Normative Ideal (Das Sollen)	Black-Box CRM Field Reality (Das Sein)	Juridical & Economic Impact on Corporations
Risk Profiling & Audit Selection	Precision risk-based regulation targeting high non-compliance actors (Responsive Regulation).	Opaque algorithms trigger Type I Errors due to unverified third-party data discrepancies.	Compliant corporations are misclassified as 'High Risk', facing speculative audits and market distortion.
Allocation of Burden of Proof	Balanced burden of proof; authorities verify external data accuracy prior to enforcement.	Unilateral shift of evidentiary burden without disclosing CRM data sources or methodology.	Taxpayers are trapped in probatio diabolica (proving a negative over inaccessible data).
Compliance Cost Efficiency	Digitalization reduces transaction and compliance costs for authorities and businesses.	Repeated responses to algorithmic anomalies and IT upgrades escalate administrative overhead.	Erosion of corporate liquidity and working capital, threatening going concern.
Procedural Justice	Transparency and equal right to be heard (audi alteram partem) during tax supervision.	Severe information asymmetry places taxpayers on the defensive against automated system claims.	Erosion of institutional trust (trust in authority) within the Slippery Slope Framework.

Source: Authors' analysis of interview findings and applicable tax-law provisions.

As illustrated in Table 1, black-box CRM profiling frequently induces Type I Errors, misclassifying compliant Corporate Taxpayers into high-risk quadrants due to raw third-party data mismatches such as timing differences between milestone-based revenue billing and clients' Article 23 withholding tax filings. Consequently, taxpayers are forced into a condition of *probatio diabolica* (an impossible burden of proof requiring proof of a negative), wherein they must disprove third-party anomalies whose underlying sources and algorithmic aggregations are withheld by the tax authority [40]. Consistent with emerging international standards on Explainable Artificial Intelligence (XAI) in tax administration, deploying automated risk scoring without transparent disclosure of discrepancy origins violates procedural fairness and evidentiary equity [38].

4.3 Escalation from SP2DK to Tax Audits in Domestic Affiliated Transactions

The regulatory transition from DGT Circular Letter No. SE-39/PJ/2015 to SE-05/PJ/2022 sought to institutionalize evidence-based supervision by requiring Account Representatives (ARs) to prepare a formal Analysis Result Report (LHA) prior to issuing an SP2DK [41], [42]. Within Responsive Regulation Theory and the Slippery Slope Framework, SP2DK occupies the base of the enforcement pyramid as a dialogic soft enforcement tool intended to cultivate trust and facilitate voluntary self-correction under Article 8 of the UU KUP prior to coercive intervention.

However, empirical evidence reveals pervasive mission creep in the practical execution of SE-05/PJ/2022. Driven by short-term revenue collection targets at regional tax offices, ARs frequently utilize SP2DK not as a collaborative fact-finding dialogue, but as a tactical negotiation lever to extract immediate tax payments [43], [44]. The 14-day response window is enforced rigidly regardless of transaction complexity [45]. When a corporation declines to accept an AR's proposed adjustment and submits accounting justifications, supporting documents are frequently discounted and the case is mechanically escalated to a Special Tax Audit under Article 29 of the UU KUP. Viewed through

Axelrod's Tit-for-Tat game-theoretic lens, punitive escalation in response to good-faith taxpayer cooperation triggers a destructive conflict spiral that undermines long-term voluntary compliance [46], [47].

This escalation risk is particularly acute in domestic related-party transactions, including intra-group management fees, royalties, and intercompany loans [48]. Although corporate groups operate as unified economic entities, Indonesian tax law adheres to the separate entity doctrine, treating each subsidiary as an independent taxpayer. Under Article 18(3) of the Income Tax Law jo. Ministry of Finance Regulation No. 172 of 2023, domestic affiliated transactions must satisfy the Arm's Length Principle (ALP) [49], [50].

Field findings from subsidiary operations (PT A) demonstrate that auditors routinely impose unilateral upward transfer pricing adjustments at the paying subsidiary recharacterizing management fees or royalties as non-deductible expenses without executing a symmetrical corresponding adjustment at the domestic parent or recipient affiliate [10], [51]. Consequently, identical economic income is taxed twice across two domestic entities within the same corporate group. This phenomenon of economic double taxation violates horizontal equity, fiscal neutrality, and the ability-to-pay principle under Dignified Justice Theory [52], [53]. To mitigate this exposure *ex-ante*, Corporate Taxpayers must compile a comprehensive Tax Defense File upon transaction execution, integrating Transfer Pricing Documentation (Master File and Local File) with a Three-Tier Test: (1) an Existence Test verifying actual service performance; (2) a Benefit Test proving commercial value-added to the recipient; and (3) a Quantum Test establishing arm's-length pricing comparability.

4.4 Doctrinal Separation of Administrative Disputes from Tax Crimes and the Ultimum Remedium Principle

A final cornerstone of legal certainty for Corporate Taxpayers is maintaining a clear doctrinal boundary between administrative tax disputes and criminal tax prosecution. During preliminary evidence examinations (Article 43A UU KUP) and formal criminal investigations (Article 44 UU KUP), enforcement practice occasionally conflates substantial fiscal adjustments or tax underpayments with criminal tax evasion. Under substantive criminal law dogmatics, such conflation violates the principle of legality (nullum crimen sine lege) and the culpability principle (geen straf zonder schuld) [54].

Table 2 synthesizes the legal taxonomy distinguishing administrative tax adjustments, negligent offenses, and intentional tax crimes alongside their corresponding mitigation mechanisms.

Table 2. Legal taxonomy of tax disputes and offenses and their mitigation mechanisms

Dispute / Offense Cluster	Statutory Basis	Core Elements & Legal Nature	Resolution & Mitigation Mechanism
Pure Administrative Fiscal Adjustment	Arts. 13, 25, 27 UU KUP; Arts. 6 & 18 UU PPh	Divergent statutory interpretation, accounting methods, 3M expense deductibility, or transfer pricing comparability on real transactions.	SP2DK clarification via Tax Defense File, Closing Conference (SPHP), Objection, and Tax Court Appeal.
Negligent Tax Offense (Culpa)	Art. 38 UU KUP jo. HPP Law	Incorrect or omitted tax returns resulting from carelessness or oversight without malicious intent.	Voluntary disclosure of inaccuracy (Art. 8(3) UU KUP) or settlement of principal plus administrative surcharge prior to investigation.

Dispute / Offense Cluster	Statutory Basis	Core Elements & Legal Nature	Resolution & Mitigation Mechanism
Intentional Tax Crime (Dolus)	Arts. 39 & 39A UU KUP jo. HPP Law	Deliberate unlawful acts driven by mens rea, such as double bookkeeping or fictitious tax invoices.	Strict evidentiary proof of mens rea; application of ultimum remedium (Art. 44B UU KUP) prioritizing state revenue recovery.

Source: Authors' analysis of interview findings and applicable tax-law provisions.

As delineated in Table 2, imposing criminal liability upon corporate executives or corporate entities under Article 39 of the UU KUP requires proving guilty intent (*mens rea*) beyond a reasonable doubt through concrete material evidence [55], [56]. *Mens rea* must be substantiated by overt acts of deliberate fraud, such as management directives to maintain double bookkeeping or the issuance and utilization of fictitious tax invoices lacking underlying economic transactions under Article 39A of the UU KUP [57]. Conversely, disputes involving the deductibility of 3M expenses, milestone revenue timing differences, or transfer pricing comparability grounded in genuine underlying transactions constitute administrative interpretation disputes that must never be criminalized solely due to adjustment magnitude.

Furthermore, Indonesian tax criminal policy post-HPP Law reinforces the character of tax law as administrative law backed by penal sanctions, enshrining criminal prosecution strictly as a last resort (*ultimum remedium*) oriented toward state revenue recovery (revenue-focused enforcement) [22], [58]. Under Article 44B of the UU KUP jo. HPP Law, the Attorney General may terminate a tax criminal investigation upon the request of the Minister of Finance once the taxpayer settles the unpaid tax principal together with statutory administrative fines. Notably, the HPP Law extends this restorative justice mechanism into the trial stage (Article 44B(2a)), whereby full restitution of state revenue losses by a corporate defendant precludes custodial imprisonment and satisfies criminal fine obligations. By combining rigorous procedural compliance during audits, exercising statutory payment suspension rights during Objection and Appeal proceedings under Articles 25(7) and 27(51) of the UU KUP, and enforcing a zero-tolerance policy toward fictitious invoicing, corporations can safeguard both liquidity and legal integrity.

5. CONCLUSION

This study establishes four principal conclusions. First, disputes over deductible 3M expenses stem from a doctrinal clash between the corporate Business Judgment Rule and tax authorities' strict legal interpretation requiring immediate revenue correlation; effective mitigation requires shifting evaluation toward economic substance (substance over label) supported by a five-pillar material evidentiary package. Second, strengthened substance over form powers under the HPP Law and opaque black-box Compliance Risk Management (CRM) algorithms risk generating administrative abuse of power (détournement de pouvoir), Type I Errors, and impossible evidentiary burdens (probatio diabolica) unless constrained by objective Business Purpose and Economic Substance Tests. Third, SP2DK supervision under SE-05/PJ/2022 frequently suffers from mission creep toward short-term revenue extraction, while unilateral transfer pricing adjustments in domestic affiliated transactions without corresponding adjustments induce economic double taxation, necessitating an ex-ante Three-Tier Test Tax Defense File. Fourth, tax law enforcement must rigorously separate pure administrative adjustments, negligence (Article 38 UU KUP), and intentional offenses requiring proof of mens rea (Articles 39 and 39A UU KUP), while upholding the ultimum remedium principle (Article 44B UU KUP jo. HPP Law) to preserve legal certainty and corporate continuity.

Practically and normatively, the Directorate General of Taxes should enhance algorithmic transparency within the CRM and Core Tax System to reduce false-positive risk classifications and institutionalize automatic corresponding adjustments in domestic transfer pricing disputes to

eliminate economic double taxation. Corporate Taxpayers are advised to adopt proactive tax risk governance by compiling *ex-ante* Tax Defense Files and integrating Fiscal Reconciliation Working Papers with Cash Flow Statements. Finally, tax auditors, investigators, and the Tax Court must anchor dispute adjudication in balanced burdens of proof, the General Principles of Good Governance (AAUPB), and substantive justice.

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