



New and Streamlined
Transfer Pricing (“TP”)
Rules ^{P1}

New and Streamlined Transfer Pricing (“TP”) Rules

On 29 December 2023, the Minister of Finance (“MoF”) issued regulation No.PMK-172¹ regarding an implementing guideline for the application of the Arm’s Length Principle (“ALP”) on Related-Party Transactions (“RPTs”).

This regulation serves as a one-stop source as a guideline for TP matters as follows:

- Definition of related party;
- Application of the ALP;
- TP documentation;
- Corresponding adjustments;
- Mutual Agreement Procedures (“MAPs”); and
- Advance Pricing Agreements (“APAs”).

PMK-172 revokes several MoF regulations, i.e. PMK-213², PMK-49³, PMK-22⁴; their contents are streamlined and elaborated into this PMK. In addition, some of the contents of PMK-172 are aligned with the Harmonisation of Tax Regulations (*Harmonisasi Peraturan Perpajakan/HPP*) Law which have also been accommodated under GR-50⁵ and GR-55⁶.

We highlight below the key changes in PMK-172 as follows.

Definition of Related Party

According to the Income Tax and Value-Added Tax (“VAT”) Law, a special relationship is deemed to exist based on ownership, control, and family relations that create a state of attachment and dependency.

¹ MoF Regulation No.172 Year 2023 (PMK-172) dated and effective from 29 December 2023

² MoF Regulation No.213/PMK.03/2016 (PMK-213) dated and effective from 30 December 2016 regarding TP Documentation

³ MoF Regulation No.49/PMK.03/2019 (PMK-49) dated and effective from 26 April 2019 regarding MAP

⁴ MoF Regulation No.22/PMK.03/2020 (PMK-22) dated and effective from 18 March 2020 regarding APA

⁵ Government Regulation No.50 Year 2022 (GR-50) dated and effective from 12 December 2022 regarding the implementation of General Tax Provisions (*Ketentuan Umum dan Tata Cara Perpajakan/ KUP*) Law

⁶ Government Regulation No.55 Year 2022 (GR-55) dated and effective from 20 December 2022 regarding the implementation of the Income Tax Law

PMK-172 further clarifies that the state of attachment and dependency is deemed to occur if one or more parties control the other, or if one or more parties are not independent. In addition, control is deemed to exist if:

- a) one party is controlling or controlled by another party, either directly or indirectly;
- b) two or more parties are under common control, either directly or indirectly;
- c) one party is controlling or controlled by another party through management or the use of technology;
- d) one individual has direct and/or indirect involvement or participation in managerial or operational decision-making at two or more parties;
- e) there are parties who are commercially or financially known or declare themselves to be in the same business group; or
- f) one party declares that it has a special relationship with another party.

The above requirements will require taxpayers to diligently assess their relationships with their transacting counterparties accordingly.

Application of the Arm's Length Principle

PMK-172 provides requirements for disclosures that were not previously covered under PMK-22, as follows:

1. Preliminary stage analyses for specific RPTs

PMK-172 regulates the requirement to undertake preliminary stage analyses for specific RPTs, including but not limited to analyses of the economic rationale and expected benefits from the transactions as follows:

- Service transactions;
- Financial transactions;
- Asset transfers;
- Business restructuring; and
- Cost contribution arrangements.

In addition to the above, PMK-172 has now added "other" financial transactions not mentioned above as a separate type of RPT, and similarly, elaborated the detailed preliminary stage that needs to be carried out for this type of transaction.

The preliminary stage analyses form an integral part of the overall robustness of the arm's length analysis and must be satisfied.

2. Shareholder activities

Specifically for the preliminary stage analysis for a service transaction with a related party, the taxpayer also needs to prove that the service provided does not represent shareholder activities.

PMK-172 updates the nature of the costs that relate to shareholder activities to include:

- the parent entity's administration, such as costs of shareholder meetings;
- the parent entity's reporting obligations, including the preparation of the parent entity's financial statements, audit reports and consolidation reports;
- raising funds or capital used for ownership acquisition by the parent entity;
- the compliance of the parent entity;
- protection of the parent entity's capital ownership in a subsidiary; and
- the overall business group governance.

3. Selection of TP method

PMK-172 continues to emphasise the following TP methods in determining the ALP, as follows:

- comparable uncontrolled price (“CUP”) method;
- resale price method (“RPM”);
- cost plus method (“CPM”); or
- other methods, such as:
 - i. profit split method (“PSM”);
 - ii. transactional net margin method (“TNMM”);
 - iii. comparable uncontrolled transaction (“CUT”) method;
 - iv. tangible asset and intangible asset valuation method; or
 - v. business valuation method.

In the event that the CUP or the CUT method can be used with equivalent reliability, these methods shall take precedence over other methods.

Specifically, for the profit split method, PMK-172 provides more detail on the application of the profit split method, specifically for transactions between parties having unique and valuable contributions to the RPT. This regulation also clarifies the definition of a unique and valuable contribution as a contribution that is more significant than the contribution from an independent party under comparable conditions and that is the main source of the actual or potential economic benefit in the business activity.

In addition, PMK-172 provides more detailed guidelines on the mechanism of applying the profit split method, such as the financial statement items, the formula, the analysis approaches, and the criteria of items to be used in the calculation. PMK-172 also explicitly provides an avenue for the application of the profit split method based on gross profit or net operating profit levels.

4. Price Indicator

Whilst the median continues to be one of the indicators considered, a price indicator of an arm’s length price can be in the form of an arm’s length point or range. PMK-172 elaborates that the price indicator shall be established based on a single-year’s comparable data, however multiple-year comparable data can be used as long as it can increase comparability.

The use of single or multiple-year comparable data shall be based on the data that is available and closely comparable at the time the transfer price is determined and/or when the transaction occurs. Furthermore, PMK-172 stipulates that, in the spirit of increasing comparability, in the event that more than one external comparable is available with the same comparability and reliability level, external comparables originating from the same country or jurisdiction as the tested party shall be selected and used as comparables.

TP Documentation

Whilst generally the requirements for TP documentation remain consistent, additional emphasis is placed on the following matters:

1. Country-by-Country Report (“CbCR”)

PMK-172 now stipulates that specifically for domestic taxpayers, a CbCR is required if the taxpayer is a parent entity of a business group whose consolidated gross turnover is amounting to at least IDR 11 trillion in the Fiscal Year (“FY”) prior to the reported FY. Previously, PMK-213 stipulated that the requirement for a general taxpayer above the IDR 11 trillion threshold would be based on the current FY. In addition, the parent entity definition is now based on ownership, whilst previously it was based on control.

Additionally, in the event that there is an error in the submission of the CbCR, PMK-172 clarifies that a rectification to the CbCR may be resubmitted accordingly.

PMK-172 has also modified the formula for calculating gross turnover, stipulating that it shall be inclusive of income received and/or obtained from business activities and from outside business activities after deducting sales returns and deductions and cash discounts. Previously, PMK-213 used gross sales before deducting discounts/rebates/other deductions.

2. Obligation to provide TP Documentation

The Directorate General of Taxes (“DGT”) is authorised to request TP documentation and the taxpayer must provide it within one month of the request. This is applicable not only during a tax audit, but also during compliance monitoring processes. A taxpayer who does not fulfil the obligation to provide TP documentation shall be subject to sanctions in accordance with the provisions of taxation laws and regulations.

Compliance assessment for TP

PMK-172 provides guidance on the compliance assessment with respect to the taxpayer’s application of the arm’s length principle.

a. Mechanism

The DGT is allowed to perform compliance assessment on the TP documentation fulfilment and the application of the ALP. Such assessment will include an assessment of the formality of RPT disclosures, minimum information disclosure requirements for Local File (“LF”) and Master File (“MF”), and a timeline for the submission of TP documentation for compliance monitoring and/or tax audit processes.

If the compliance assessment of TP documentation is fulfilled, the testing is carried out by comparing the TP documentation with the actual condition.

However, if the taxpayer:

- does not apply the ALP;
- does not apply the ALP correctly;
- cannot prove that specific RPTs have satisfied the preliminary stage analysis; or
- the transfer price determination does not fulfil the ALP,

the DGT is authorised to perform a TP adjustment by determining the transfer price based on the ALP and consider the taxpayer’s approach in applying the ALP.

b. Deemed dividends

PMK-172 stipulates that TP adjustments made by the DGT are considered as indirect profit repatriations to the affiliated party, which are treated as taxable dividends that are subject to tax upon the payment date or when they are available to be paid or when they are due.

However, it is also regulated in PMK-172 that a TP adjustment will not be considered as a dividend if there is an addition/deduction of cash (or cash equivalent) in the amount of the TP adjustment prior to the issuance of the Tax Assessment Letter (*Surat Ketetapan Pajak/SKP*) and/or the taxpayer has agreed to the transfer price determined by the DGT.

This “deemed” dividend rule is applicable on all types of RPTs, either local or cross-border transactions. For cross-border transactions, PMK-172 confirms that the taxpayer can use the applicable tax treaty relief.

c. TP adjustments and VAT implications

PMK-172 stipulates that the DGT is authorised to adjust the VAT tax base based on the arm’s length market price if the selling price to the related party is lower than the arm’s length market price.

Furthermore, PMK-172 highlights that any form of TP adjustment performed by the DGT can be allocated to each transaction of delivery of taxable goods and/or taxable services.

However, such correction will not result in any additional creditable Input VAT to the buyer, and any creditable Input VAT will still refer to the pre-adjustment price as stated in the original VAT Invoice.

Corresponding Adjustments

If a TP adjustment is imposed by the DGT during a tax audit or by a Treaty Partner’s tax authority on a foreign tax subject that results in double taxation, the domestic taxpayer who is the counterparty to the transaction may carry out a corresponding adjustment.

If the TP adjustment is imposed by the DGT on a transaction between two domestic taxpayers, the domestic counterparty of the adjusted taxpayer can request a corresponding adjustment if the adjusted taxpayer agrees with the TP adjustment and does not file any legal action.

Under this condition, the corresponding adjustment shall be carried out through:

- a. An amendment to the Annual Tax Return by taking into account the transfer price determined by the DGT, if the domestic counterparty has not been tax audited;
- b. An issuance of SKP by the DGT that takes into account the transfer price determined by the DGT if the domestic counterpart is being tax audited;
- c. An amendment to the SKP by the DGT on an *ex-officio* basis that takes into account the transfer price determined by the DGT if the domestic counterparty has been issued an SKP and did not file legal action.

If the TP adjustment is imposed by a Treaty Partner’s tax authority for a local taxpayer’s transaction with a foreign tax subject, the corresponding adjustment is carried out through MAP.

Mutual Agreement Procedures and Advance Pricing Agreements

The administrative procedures of MAPs and APAs stipulated in PMK-49 and PMK-22, respectively, mostly remain the same, but there is now more detailed elaboration in PMK-172. For example, when a taxpayer applies for MAP or APA to the DGT, the DGT must issue a written notification letter within one month to inform the taxpayer whether or not the application can proceed. PMK-172 now stipulates that if such notification letter is not issued within one month, the application is deemed to have been approved to proceed and the DGT must issue a notification letter on this.

The key changes other than the administrative procedures are set out below.

1. Mutual Agreement Procedures

a. Lawsuit and judicial review (“JRs”)

Under the existing rule, the MAP process can be carried out simultaneously with certain domestic dispute resolution processes. PMK-172 has included lawsuits and JRs as domestic dispute resolution processes that may be carried out simultaneously with the MAP. Under this rule, the DGT may terminate the MAP negotiation if a lawsuit decision has been issued with an order to cancel the SKP with items currently covered in the MAP process.

b. MAP does not postpone refunds of tax overpayment

On top of not postponing the tax payment and tax collection process, PMK-172 has now added that MAP requests also do not postpone refunds of tax overpayment.

c. Written notification on the result of negotiations and agreements

PMK-172 stipulates that the DGT will issue written notifications regarding the results of negotiations containing MAP agreements. As part of the notification, the DGT can request the taxpayer to submit additional documents, listed as follows:

- statement letter of not applying for dispute resolution outside the MAP; or
- statement letter of revocation or adjustment accompanied with a written approval from the Tax Court or the Supreme Court regarding the revocation or adjustment of the dispute.

If the taxpayer does not fulfil the request from the DGT within the specified timeline, the DGT will submit a written notification to the Treaty Partner’s tax authority stating that the MAP cannot be implemented.

d. Additional requirement for MAP process after an appeal or JR decision

Under the HPP Law, if a MAP process has not reached agreement by the time of the announcement of a Tax Court or JR decision, the DGT may use the appeal/JR decision to take a position or to stop negotiations if the content of the decision is related to the MAP case. PMK-172 has now added that if no JR request is submitted on the appeal decision, then the DGT will use the appeal decision as the consideration for the MAP negotiation, or to stop the negotiation.

e. Mutual Agreement Decision Letter issued after domestic remedy decision

In general, PMK-172 stipulates that if a Mutual Agreement Decision Letter (*Surat Keputusan Persetujuan Bersama*) is issued after the issuance of a domestic remedy decision, the tax payable in the Mutual Agreement Decision Letter must be recalculated according to the domestic remedy decision.

2. Advance Pricing Agreements

a. Additional conditions for taxpayers applying for APA

In the event that domestic taxpayers decide to apply for an APA, PMK-172 has added an additional requirement whereby this can be done provided that the domestic taxpayer is not subject to a preliminary evidence examination, criminal investigation in taxation matters, prosecution for

taxation criminal acts, taxation criminal proceedings, or criminal sentencing in taxation matters.

b. Taxpayers experiencing negative business cycle

In the event that an APA application is submitted by a taxpayer whose business is negatively affected by a national disaster declared by the Central Government, the profit level in the projected financial statements shall be the profit level resulting from adjustments to normal conditions.

c. Elimination of sanctions related to APA implementation

In the event that in the APA Period and/or Roll-back there are administrative sanctions arising as a result of:

- Amendment of the Annual Tax Return if the taxpayer has not been tax audited;
- Issuance of SKP by the DGT under a tax audit; or
- Amendment of the SKP by the DGT on an *ex-officio* basis after an SKP has been issued,

the DGT nullifies the administrative sanctions according to the KUP Law.

d. Implementation of Bilateral and Multilateral APA based on mutual agreement

In the event that the Bilateral/Multilateral APA results in a mutual agreement, the DGT shall issue an APA decision letter within one month from:

- the date of the receipt of the written notification from the Treaty Partner's tax authority stating that the APA can be implemented; and
- the date of the delivery of the written notification to the Treaty Partner's tax authority stating that the APA can be implemented.

Transitional provisions

As PMK-172 comes into effect, transitional provisions are regulated as follows:

- Any ongoing MAP process carried out based on PMK-49 and the decision letter that has not been issued shall be followed up based on PMK-172;
- Any ongoing APA process carried out based on PMK-22 and the decision letter (for implementation, amendment, or cancellation) that has not been issued shall be followed up based on PMK-172; and
- The obligation to prepare, maintain, and submit TP documentation for FY 2024 and beyond shall be carried out based on PMK-172.

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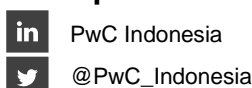
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