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Adopting BEPS Inclusive Framework in Indonesia:Taxation Issues and Challenges in a Digital Era

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Adopting BEPS Inclusive Framework in Indonesia:Taxation Issues and Challenges in a Digital Era

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Abstract. This research is intended to discuss the new framework of taxing a highly digitalized economy, known as Base Erosion and Profit Shifting (BEPS) Inclusive Framework. This research discusses challenges that will be faced by Indonesia while adopting that new framework into domestic jurisdiction despite its potential benefit for state revenue. Taxing a highly digitalized economy under the physical-presence concept has been considered obsolete and tends to encourage Multinational Enterprises to shift their profit into low tax jurisdiction. This research applies a qualitative approach and research method. The data collection was done through a literature review and expert interviews. Organization for Economic Cooperation and Development (OECD), with the support of G20 members, proposes the solution based on global consensus. The solution is to establish a nexus to allocate taxing rights and profit allocation to the market jurisdiction. Indonesia has formulated a domestic legal basis despite myriad challenges. The challenges include coverage of the establishment of technical legal implementing guidelines and the improvement of the tax authority to optimize its performance. Essentially, this study highlights the legislation and organizational capacity of the Indonesian context. The study finds the ability to establish the technical regulation is seems questionable and similarly to the organization's capability to implement the project.

Keywords: digitalized economy, taxing rights, profit allocation, international tax, global tax governance.

Abstrak. *Penelitian ini bertujuan untuk membahas kerangka baru atas pemajakan kegiatan ekonomi digital, yang dikenal oleh masyarakat perpajakan global sebagai Base Erosion and Profit Shifting (BEPS) Inclusive Framework. Penelitian ini juga membahas tantangan yang akan dihadapi oleh Indonesia ketika mengadopsi kerangka kerja baru tersebut terlepas dari potensinya meningkatkan penerimaan pajak domestik. Pemajakan kegiatan ekonomi digital dengan konsep kehadiran fisik telah dianggap usang dan cenderung mendorong perusahaan multinasional untuk menggeser laba perusahaannya ke negara lain yang memiliki tarif pajak lebih rendah. Penelitian ini menggunakan pendekatan dan metode penelitian kualitatif. Organization for Economic Cooperation and Development (OECD) dengan dukungan negara anggota G20 telah berupaya untuk menawarkan solusi untuk menghadapi tantangan pemajakan atas kegiatan ekonomi digital berdasarkan pada konsensus global. OECD mengusulkan adanya nexus atas hak perpajakan baru dan pendekatan baru terkait alokasi laba perusahaan multinational. Indonesia telah menyiapkan dasar hukum untuk pengimplementasiannya meskipun dengan berbagai tantangan. Tantangan yang dihadapi meliputi penyusunan ketentuan teknis pelaksanaan dan peningkatan kapasitas otoritas pajak untuk mengoptimalkan kinerjanya. Penelitian ini menyoroti perihal kapasitas legislasi dan kapasitas organisasi di Indonesia. Penelitian ini menyimpulkan bahwa kemampuan untuk memformulasikan ketentuan teknis dan kapasitas organisasi masih menjadi sesuatu yang diragukan.*

Kata kunci*: ekonomi digital, hak pemajakan, alokasi keuntungan, perpajakan internasional, pengaturan pajak global.*

INTRODUCTION

In the advent of technological advancement on economic activities, allocation of taxing rights based on physical presence becomes less relevant and less sufficient. However, taxing the digital economy with considerations to ensure fairness, certainty, and ease of policy is proven to be challenging due to the unilateral approach to tax towards an immaterial approach towards potential revenue (Petruzzi, 2018; Danon & Chand, 2019). Imposing tax based on 'out-of-date' policy such as based on physical presence would have potentially eroded the country's taxable base. Business entities with sophisticated and revolutionary technology would easily escape or move to more favorable tax treatment jurisdictions (Gianni, 2018).

In its essence, taxing rights should respect the territoriality of a country and follows the neutrality principle (Schon, 2015). International taxation warrants unique issues related to the multi-faceted interests of its actors, businesses, and countries, that are transacted within the boundaries of their own as well as each other's legal framework (Nizamev A., 2003). To respond to the challenge, the Organization for Economic Cooperation and Development (OECD) proposed to move forward by initiating an action plan on a consensus basis. Under this initiative, a new nexus rule to fairly tax those digital economic activities without the tendency to ring-fencing the global business was proposed (OECD, 2019). Thus, it has become the origination of Base Erosion and Profit Shifting (BEPS). Since the release of BEPS Project Action 1 in 2015 by OECD, this discussion has become a global agenda agreed by the member of G20 country without prejudice in 2017 with urgent consideration to set a tax basis with a global standard (OECD, 2018). Essentially, the Public Consultation Document released by the OECD emphasizes the relative merit of an alternative approach to allow the market jurisdiction to tax certain profit allocation (OECD, 2019). To ensure its application, several aspects need to be clarified. They are (a) new non-physical presence different from existing applied permanent establishment concept; (b) new concept of taxable income in the source jurisdiction and (c) interaction between the new concept and existing provision on the taxable presence on source jurisdiction, including the provision on the non-discriminatory rule.

The proposal to obtain a consensus for the new nexus rule on allocation of taxing rights and allocation of profit consists of two pillars (OECD, 2019). Pillar One focuses on the allocation of taxing rights and the measure to undertake the coherent review of the profit allocations and nexus rule. It substantially focuses on consumer-facing business. A consumer-facing business means a business that obtains revenue from supplying consumer products or providing digital services. These products are delivered to the consumer-facing element, therefore sectors such as extractive industry, commodities, financing must be carve-out (Erns & Young, 2019). Pillar Two, which is known as "Global Anti-Base Erosion" (hereafter is mentioned as GLoBE) focuses on the establishment of the coordinated rule to address the possibility of ongoing risk that enable multinational entities to shift their profit into favorable low tax jurisdiction. The effect of these proposals will establish two new aspects of the international mechanism, including (i) the platform of tax collaboration and (ii) the inclusive framework of BEPS.

Developing countries that support the creation of this new nexus to tax and the concept of this new allocation of profit, the challenges commensurate with the need for stronger capacity following this international coordinated tax avoidance prevention. Indonesia, a member of G20 countries, has voluntarily participated to support the establishment of a tax collaboration platform and to the implementation of the BEPS Inclusive Framework into their domestic tax provision. This participation was driven by the substantial loss suffered from the potential revenue that would have been earned from the highly digitalized business, added by the fact that Indonesia is one jurisdiction of big market users and source of income to digital MNEs (Gorbiano, 2019). The phenomenon co-exists with the enormous digital economic potential in the future (V.M. Rumata, et., al, 2020). The taxing regulatory framework will result in the potential loss on giant businesses' operating and generating income from Indonesia. A notorious example is the Google case whereby the Indonesian tax authority urged Google to pay its income tax from the revenue-generating from Indonesia.

In 2016, the Indonesian tax authority noted that the most proportion of Google revenue generated in the Asia Pacific region was contributed by Indonesia. The revenue then was shifted to its headquarter in Singapore. Indonesia tax authority imposed accrued Google tax liabilities for five years back, which equal to the amount of tax debt of more than USD 400 million accounted for 2015. The Indonesian government and Google reached a settlement where Google agreed to pay back taxes and fines (Reuters, 2016). The settlement was made through negotiation without any litigation process. It was led by the fact that the dispute has arisen due to the loopholes "facilitated" by the current Indonesian taxation regulatory framework. The tax authority is legally allowed to impose a tax on active income earned by the non-resident taxpayer if the non-resident business is physically present or through the creation of permanent establishment as mandated by the current prevailing income tax regulation mentioned in Income Tax Law Art. (2).

Following the survey conducted by Google and Temasek in 2019, it states that with these facts, similarly, Indonesia also has a big interest to ensure that tax base and potential revenue erosion should be minimized. As the practical move forward, the Indonesian tax authority has shown a supportive sign to implement the BEPS Inclusive Framework once the consensus is reached and officially announced into domestic jurisdiction (Gorbiano, 2019).

The Google case in Indonesia provides a precedent for the Indonesia Tax Authority to progress the initiative on taxing digital economies. Indonesia's internet economy growth is on high-speed which estimates to 40 billion USD in 2019 and potentially will reach 130 billion USD in 2025 (V.M. Rumata, et., al, 2020). The Indonesian government should gain considerable tax revenue following the massive increase of this digital economy growth. The interest on how to find the justifiable way to impose tax also lies on methods to fairly allocate the income of a highly digitalized economy among the jurisdiction where it operates, minimize the tax base, and potential revenue erosion. However, the Government of Indonesia needs to further examine the potential challenges of implementing this consensus appropriately into Indonesia's domestic tax provision.

The concept of the new nexus rule and profit allocation proposed by the OECD through Pillar One and Pillar Two is complex as it strives to fairly share the taxing rights into jurisdictions. The issues warrant a discussion on taxing rights, transfer pricing, and profit allocations about countries' presiding laws, tax treaties, and the implementation of mutually agreed procedures. This study focuses on the discussion of the general challenges to implementing the BEPS Inclusive Framework of Pillar One and Pillar Two, especially the general challenges potentially will be faced by the developing countries and the challenges that will be faced by Indonesia on its domestic tax provision. Further, this article is expected to deliver the input to the stakeholder to deal with the challenges. To the best of the Author's knowledge, publications related to the academic discourse on the issue are extremely scarce. The problems occur on the practical level, which produces segregated results and contextual-driven analysis. Thus, this research is exploratory and aims to provide findings from a context that applies to Indonesia, and by proxy, potentially applicable to other developing countries with the same context. Finally, the research should contribute to the early initiative of developing academic discourse on the topic. This study is aimed at exploring the challenges faced by Indonesia in establishing a technical legal framework and tax authority in adopting BEPS.

RESEARCH METHOD

The approach used in this study is qualitative. A qualitative approach is an approach in conducting research-oriented to natural phenomena because of its orientation, so it is naturalistic and fundamental and cannot be done in conventional laboratories but must go into the field.

This research was conducted in 2020, several months after the BEPS Inclusive Framework Pillar One and Pillar Two concepts were publicly discussed in the Public Consultation event organized by OECD. This exploratory study will elaborate on the understanding, challenges, and how the challenges became part of the Indonesian domestic tax legal and practical provisions. Data collection was done through literature studies and in-depth interviews. Primary data consists of interviews with experts such as OECD Adviser, The Head of Global Tax Policy Centre Vienna University of Business and Economics, and virtual discussions with research associates of Global Tax Policy Centre Vienna University of Business and Economics. The secondary data comes from various publication information by Indonesian tax authorities, tax consultants, and mass media. The discussion was recorded and the researcher made interview notes on the important points of the discussion. The data analysis was done manually due to the size of the informants. The interview notes are analyzed based on themes and memos.

RESULT AND DISCUSSION

Fundamental Aspects of BEPS Inclusive Framework on Taxing Digital Economic (Unified Approach-Pillar One and Global Anti-Base Erosion Proposal "GloBE" Pillar Two)

The Interim Report released by the OECD Secretariat explained and described the change of business models due to the rapid enhancement of technology. For certain highly digitalized businesses, it identified three important characteristics of that business. Those characteristics are "scale without mass", "heavy reliance on intangible assets", and the "importance of data, user participation and their synergies with intangible assets" (OECD, 2019). There are some technical issues raised from stakeholders under Program of Work (PoW), which was grouped into three building blocks (OECD, 2019):

(a)The different approach to ascertain the amount of generated profit should be subjected to the new taxing rights and how that profit should be allocated among the countries/jurisdiction appropriately.(b)The design of the new nexus rule sufficiently captures the novel concept of business presence in market jurisdiction. The new nexus rule is expected able to reflect the transformation of global-scale business activities which must not be constrained by the physical presence prerequisite; and (c)The availability of new instruments to ensure and ascertain the appropriate implementation of new nexus rule, to enable efficient tax administration to apply the new taxing rights and the availability of effective elimination of double taxation and tax disputes resolution.

Indeed, the new taxing rights will require a method to fairly quantify the amount of generated profit to be allocated among the market jurisdiction and how that profit should be allocated to the jurisdiction following their entitled new taxing rights. OECD has taken the role in international tax law-making on a consensus basis.

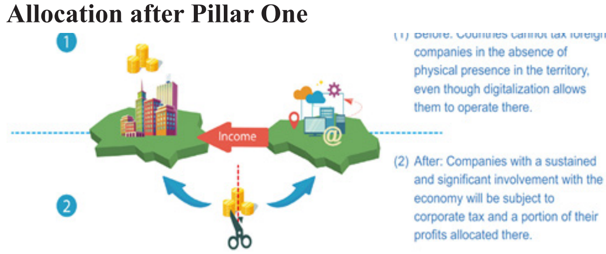
In simple terms, it could be said that OECD addresses two concerns. The first concern is that current rules required a physical presence to create a "nexus" between the operating firm and market jurisdiction. Pillar One is intended to address this concern by revising the nexus and profit allocation rules. The second concern is that even though the effort has been made to deal with the profit shifting, the possibility of MNEs shifting the profit into low tax jurisdiction might exist. Pillar Two is intended to address the second concern through global anti-base erosion (GloBE), which introduces a global minimum tax system (Doherty & Verghese, 2019).

Pillar One – Unified Approach

Pillar One, known as a unified approach is intended to redefine the new taxing rights and allocation of profit. The following figure 1 describes the issue that is addressed by Pillar One.

Under Pillar One, to fairly distribute the profit into market jurisdiction under the new nexus rule, the OECD has established three proposals that have been articulated to develop a consensus-based solution. The allocation of taxing rights and profit allocation generated from cross-border activities refers to – namely, the "user participation" proposal, the "marketing

Figure 1. Illustration of Taxing Rights and Profit Allocation after Pillar One



Source: World Economic Forum, (2019)

intangibles" proposal, and the "significant economic presence" proposal. Under Pillar One, it covers the following:

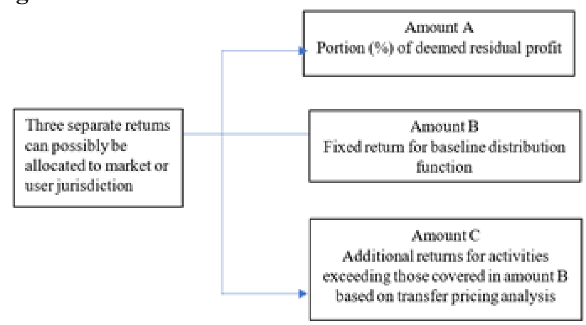
(1)Scope. The proposal pays serious attention to MNEs running highly digital business models. This proposal aims to cover broader business models including consumer-facing businesses with further work to be carried out on scope and carve-outs. With this determined scope of a business, the extractive industry is assumed to exclude from the scope. (2) New Nexus. For the type of business entities counted on this scope, it has considered creating a new nexus which is not formed due to the existence of physical presence but due to the performance of sales within a jurisdiction. The new nexus can be having a certain amount of threshold, including a proportion of the country-specific total of sales. This aims to ensure that each country must benefit from the economic activities including small market jurisdiction. Consequently, it might affect the design of new self-standing treaty provisions. (3)New Profit Allocation Rule going beyond the Arm's Length Principle. The new nexus subsequently will create a new profit allocation rule that this rule will be applied to the taxpayer counted on the scope. The new allocation applicable to taxpayers or business entities within the scope respectively will be allocated whether those business entities have an in-country marketing or distribution presence (through the form of a permanent establishment or separated entities acting as a subsidiary) or performing the sale via unrelated distributors. For the applicability of this new profit allocation, it retains the arm's length principle with the formula-based solution as a compliment. This combination of the rule is expected enable to reduce the tension of profit allocation among jurisdictions to cope with the taxing right in the current high digitalized era. (4)Increased Tax Certainty delivered via a Three-Tier Mechanism. This approach objective is to increase the tax certainty for both business entities as taxpayers and tax authorities. Therefore, for the practical aspect, it administers a three-tier profit allocation mechanism, as follows:

(1)Amount A – a share of deemed residual profit, allocated to market jurisdictions using a formulaic approach, i.e. the new taxing rights; (2)Amount B – a fixed remuneration for baseline marketing and distribution functions that take place in the market jurisdiction; and (3)Amount C – binding and effective dispute prevention and resolution mechanisms relating to all elements of the proposal, including any additional profit where in-country functions exceed the baseline activity compensated under Amount B.

For simplification, the three-tier is shown in figure 2.

With this intertwined formulaic-based approach and arm's length principle, the Program of Work (PoW) of OECD has strived to create the solution on the issues related to residual and non-residual profit fairly. It also exploits the profit-split method to bifurcate the total generated profit of MNEs into

Figure 2. Model-Based on Three-tier Mechanism



Source: OECD Public Consultation Meeting on 21-22 November 2019

routine and routine-component. Thus, this will require a simple approach to quantify the component of routine and non-routine as a mode of application of the proportion of newly introduced taxing rights. This approach was established by assessing the relative merit of the following aspect: (a) The adaptation and adjustment of the current transfer pricing rules with taking into account the issues raised (b) The use of a proxy-based on the expenditures have been capitalized by the group of an MNEs. This approach would include several consideration such as (i) how the cost bared relating to the activities and assets in and out of the scope of the new taxing right should be identified precisely; (ii) how the "useful lives" of different categories of expenditure and/or related to an investment to the development of product or services generated benefit should be determined and applied; and (iii) how concerns that cost may not always be an appropriate indicator of value could be addressed.

While establishing the new taxing rights and the new allocation of profit, the POW under Pillar One has several significant commonalities that need to emphasize (OECD, 2019):

(a)Although several proposals on creating an approach to address the taxing digital economy issue, to the extent that highly digitalized businesses can operate remotely, and/or are highly profitable, all proposals would reallocate taxing rights in favor of the user/market jurisdiction; (b)all the proposals envisage a new nexus rule that would not depend on physical presence in the user/market jurisdiction; (c)they all go beyond the arm's length principle and depart from the separate entity principle; and (d)they all search for simplicity, stabilization of the tax system, and increased tax certainty in the implementation

Pillar Two - Global Anti-Base Erosion Proposal "GloBE"

A move forward of the proposal on taxing a high digitalized business is that it needs to tackle the remaining BEPS challenges through the establishment of two inter-related rules:

(a)an income inclusion rule that is intended to tax the income generated from the dependent entity (foreign branch), if that income is subjected to an effective tax rate lower compared to a minimum tax rate; and (b)a tax on base eroding payments that would operate by way of a denial of or avoidance of a deduction or imposition of source-based taxation (including withholding tax), together with any necessary amendment to double tax treaties, for the certain transaction unless that transaction has been properly subjected to the effective rate more than a minimum rate.

The global tax system would pass a new architect into a new different landscape due to the application of Pillar One and Pillar Two. The following figure 3 will describe the different situations after the implementation of Pillar Two.

Figure 3. Illustration of Different Propensity of Business Behaviour after Pillar Two

Source: World Economic Forum, (2019)

The OECD seeks to create a way of enforcing the consensus of new nexus rules and a new allocation of profit. The issuance of Pillar Two is expected as a means of applying an inclusive framework of new nexus and profit allocation on taxing high digitalized businesses with relevant quantification methods in a parallel manner (OECD, 2019).

The program of Work (PoW) on Pillar Two concern the following three aspects:

(a)The use of financial accounts as a starting point for determining the tax base under the GloBE proposal as well as a different mechanism to address timing differences (b)The extent to which an MNE can combine high-tax and low-tax income from different sources taking into account the relevant taxes on such income in determining the effective (blended) tax rate on such income; and (c)Stakeholders' experience with, and views on, carve-outs and thresholds that may be considered as part of the GloBE proposal.

To effectively apply this new proposal, it would change the current domestic tax provision and double tax treaty agreement. Further, it also needs a platform of collaboration and coordination to avoid the possibility of double taxation of income earned by MNEs in more than one jurisdiction. Thus, the application of this new approach would work under a standardized structure or arrangement. Following the proposal, the income inclusion would be performed under a minimum tax, thus the shareholders of an MNE must bring into account a proportionate share of income if the income generated in a particular jurisdiction is not subjected to an effective tax rate above a minimum tax rate. Therefore, the implementation of the CFC rule will support this approach as a supplement for reinforcement. By enforcing that way, the income inclusion proposal might be fulfilling its objective to protect tax base on the home jurisdiction or other host jurisdictions where a group of MNE has operated. This approach is also expected to minimize the propensity of tax planning structure such as unreasonable intra-financing group; thin capitalization or other modes of profit shifting.

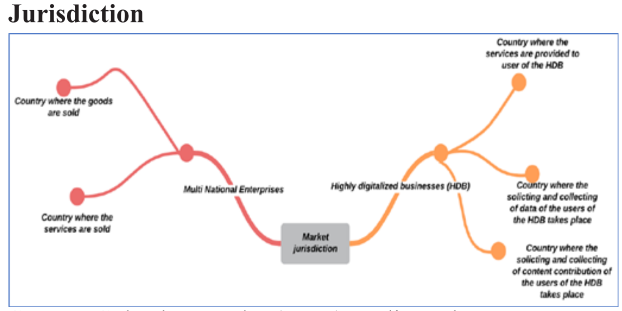
Assessing Indonesia Tax Policy Landscape toward BEPS Inclusive Framework on Taxing Digital Economic (Unified Approach-Pillar One and Global Anti-Base Erosion Proposal "GloBE" Pillar Two)

The Discussion of Adopting BEPS Inclusive Framework Pillar One and Pillar Two in Developing Countries

The introduction to the two Pillar similarly has redefined the definition of "market jurisdiction" as an element of taxing rights. This redefining concept has enabled the amount of income to be segregated into three elements known as amount A, B, and C being applied under the new regime. The extent of each amount to be applied under the proposed Pillar One is described in the following part. Figure 4 represents the new scope of market jurisdiction.

This figure sounds positive shows that there will be an environment where the sale of intangible goods or services could be used as a proxy to market jurisdiction. The redefinition of market jurisdiction as a proxy to taxing rights would be such a positive sign for developing countries to get the profit allocation, which is subject to tax. It may be due to their role as a market to the goods and services (Abu M.M. et., al, 2020) regardless of the critics posed by the United Nations BEPS Monitoring Group (BMG) this newly invented proposal will only give tiny benefit for the developing countries (UN, 2020). Thus, as a practical consequence, the following highly digitalized business, with their types of business will be subject to tax, which formerly has possibly not been taxed under the physical-presence rule. Seeing the current proposal to be agreed upon, the government of each state would see this step as a global move forward due to an establishment of international coordination. On the other hand, to the new nexus rule and new profit allocation proposal, it is important to emphasize the following remarks about Pillar One (Hearson, 2019).:

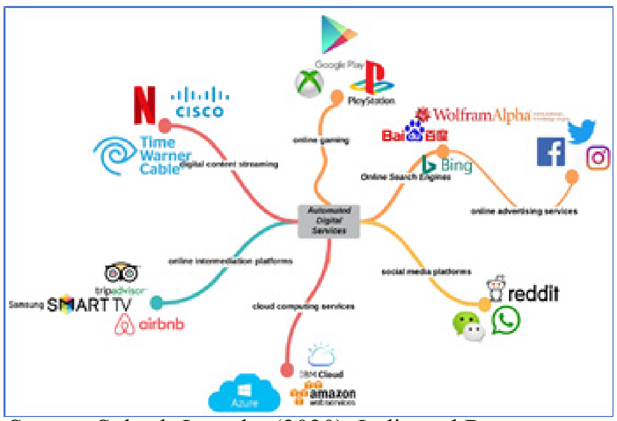
Figure 4. Simplification of Redefining Market Jurisdiction



Source: Subash Jangala, (2020), India and Recent Updates on the OECD/G20 Inclusive Framework's Two Pillar Approach, South View No. 1919, South Centre

(1)Amount A; or commonly called residual profit or non-routine profit, the existence of amount A of Pillar One is a breakthrough on the omits of taxing right due to non-physical presence. The developing countries would get the pie share of income allocation since this new nexus rule will enable the government to mobilize the revenue even though in the absence of physical presence in their jurisdiction. The amount A refers to the percentage of MNE's worldwide consolidated residual profit. The residual profit will take a large proportion of total income since it refers to the profit due to non-routine activities. The appropriate formulaic method to deal with this problem must be on the attention of the developing countries to ensure this amount must be fairly shared with the developing countries (Cobham et., al, 2020). The activities outside the home office could substantially affect the sustainability of the business, therefore the profit of non-residual activities may be generated from that non-home office activities. From the perspective of the UN BEPS Monitoring Group, this proposal is a result of quite radical thinking on international tax rules. (2) Amount B; commonly know as non-residual profit or routine profit; an approach to align the allocation of profit due to marketing and distribution function – that is assumed as a routine activity within a jurisdiction. This possibly uses a formula for remuneration where a physical presence will be a proxy. This might be interesting for developing countries because it considers value creation on a particular jurisdiction on local/domestic function. By applying this proxy, for a value creation contributed in developing countries will be counted on relatively a bit fair remuneration by applying transfer pricing concept, particularly the transaction net margin method (TNMM). (3)Amount C; a mechanism whereby a country can challenge the amount of profit allocation distributed into its jurisdiction under Amount A and Amount B. Amount C will serve as a mode of dispute prevention.

Figure 5. Highly Digitalized Business Possibly Covered under Market Jurisdiction



Source: Subash Jangala, (2020), India and Recent Updates on the OECD/G20 Inclusive Framework's Two Pillar Approach, South View No. 1919, South Centre

The concern on these allocations ascertains that the impact of BEPS has not brought uniform and similar impact to each country due to the different stage of economic level (Peters C., 2015). Besides those concerns on the developing countries' side, the stakeholders and practitioners also gave comments on this proposal. The type of key point of public comments raised while the OECD organized public consultation are the following (Dalton, 2020):

(a)The principles underlying the establishment of a unified approach should be articulated clearly to the public rather than confined to the international level. (b)Practical challenges need a bold solution such as how to determine the profit allocation which politically and economically acceptable (c)The mandatory, multilateral, and binding arbitration on how to settle the dispute on an agreeable basis and to prevent the potential inconsistency interpretation.

The general public concern especially from the developing countries on these initiatives, specifically about Pillar One consists of (i) how to clearly define routine activities under Amount B – about fact and circumstance has to meet and the interpretation of the level of profit related to routine activities, (ii) the agreement on scale or amount of profit, the range of time on determination of profit and the threshold of profit, (iii) how to fairly treat the losses and importantly (iv) how this new initiative will interact with the prevailing existing provision (RSM Canada, 2019). About the distinction between 'routine' and 'residual profit', the economist categorized the profit into two categories; they are normal/ routine profit' – based on routine activities and 'residual profit/excessive profit' – refers to the opportunity based on the cost of capital. It could be earned through the specific innovation, establishment of market power. The percentage of the cost of capital could be different in each country (i.e. in 2016, US (11%), EU (6%), Japan (4%), emerging market (14%) (Cobham et., al, 2019). Even this "solution" still rise new homework to fix.

For Pillar Two, as a mode to ensure income inclusion and global anti-tax base erosion (GloBE), several practical issues were also raised from stakeholders. Further, these issues would be quite challenging with the current capacity. It needs to make a thorough observation of the difference of accounting standards applied in a different jurisdiction. It also needs to take a close a look at the recognition of expenses and income accrued, the different treatment on permanent and temporary difference to accrue the expenses, the treatment to depreciation, amortization, carry forward, and other items of calculations. It means that the countries still have to perform further homework on global accounting standards to feasibly apply this Pillar One and Pillar Two.

Cobham et., al (2019) suggested that to realize this new nexus of taxing rights and allocation of profit, it needs to refer to the Country-by-country reporting (CbcR) as a basis. Cobham et., al (2019) performed a simulation on how much the country would receive the additional corporate tax revenue given by the new nexus of taxing rights and profit allocation. The simulation was created based on country GDP, cost of capital, CbCR data, and amount of sales based on regional distribution. That research made a combination of the mode of allocation proposed by OECD, IMF, and Independent Commission for the Reform of International Corporate Taxation (ICRIT). The research revealed that reallocation of taxing rights and profit allocation will be beneficial to the non-OECD with little benefit. Indeed, even though with little benefit, it has contributed to the reduction of profit shifting of lower-income country. Cobham et., al (2019) also emphasized that as input based on their research, the global governance should reconsider occupy apportioned of multinational's employment as a proxy instead of solely based on the total value of sales in each jurisdiction. This more likely similar argument also proposed by the Indian government to take into account the number of employees, wages paid to employees, and assets deployed other than the volume of sales. Broaden element of nexus is expected to give the developing countries a larger share of the pie (Indian Tax Authority position).

On the other hand, to what extent this proposal brings a permutation to developing countries has not been precisely calculated. The lack of high-quality data made the modeling prediction could not accurate. This challenge will be faced by the government of developing countries while they strived to forecast how much additional revenue they will get and what technical aspects must be prepared (Hearson, 2019). Hearson (2019) highlighted the carve-out and threshold possibly reduce the utility of the Pillar One for developing countries:

(a)The business entities threshold. On the seminar held by International Fiscal Association (IFA) in September 2019, it was proposed that the turnover threshold could be no less than 750 million EUR. This means that only giant company which will include in this inclusive framework taxing the right allocation. (b)The revenue threshold. The Amount A of Pillar One will be distributed based on the volume of the sales/user until exceeding a certain amount. This means that there will be a possibility a particular country with a small market which will not get the revenue from the profit allocation. (c)The residual profit threshold. Amount A of Pillar One will apply to the company's residual profit. This cannot easily be tight to a specific part of business function since the amount of this profit is commonly quite high for digital businesses. (d)Carve-out. This new approach shall not apply to extractive, commodities, and financial industry. These types of businesses may have a high-value chain, but these are excluded from new taxing rights.

Indonesian Challenges toward Implementing BEPS Inclusive Framework Pillar One and Pillar Two

The size of Indonesia's digital economy has reached USD 40 billion in 2019. This is the largest proportion in Southeast Asia. With an average growth of 49% per year, it is predicted that the value of Indonesia's digital economy will reach up to USD 130 billion by 2025. Certainly, this figure shows an extraordinary market potential that Indonesia should be able to capitalize on. In several previous years, however, Indonesia has suffered from tax potential revenue from a highly digitalized economy. In 2017 that the aforementioned Google case versus the Government of Indonesia was settled with the amount of tax paid undisclosed to the public. This mode of the settlement was because no fundamental legal basis was available to enforce the non-presence business to pay the income tax from the income it actively generated from a particular jurisdiction.

The Indonesian government has been increasingly aware of the rapid development of digital economics activities, including software provider and apps, game, video, and music streaming, film-related business, design, and design graphic auxiliary, broadcast and streaming service subscription, social media, and over the top services, that it needs to govern through a comprehensive rule especially about the tax provision related to the implementation of rights and obligations of each party, both the government and business like other business entities. Furthermore, the tax authority needs to emphasize the similar level playing field between a conventional business and a digital business. Until recently, as a response to the digital economy, the Indonesian government issued Presidential Regulation No. 74/2017. This regulation is a form of attention from the government to support the acceleration and development of electronic-based national trade systems (e-Commerce), start-ups, business development, and logistical acceleration by establishing an integrated Roadmap for Electronic-Based National Trade Systems (Road Map) e-Commerce). The e-commerce road map covers funding, taxation, consumer protection, education, and human resources, infrastructure, communication, logistics, cybersecurity, and the Formation of the 2017-2019 SPNBE (Sistem Perdagangan Nasional Berbasis Elektronik or national trade system by using electronic basis) Road Map Implementation Management.

Previously, the Ministry of Trade also has issued a provision of trade-related activities, which included e-commerce through Law No. 7 of 2014 concerning Trade. The provisions are intended to bring an understanding to the public that the public has the same concepts related to Trading through Electronic Systems (or Perdagangan Melalui Sistem Elektronik PMSE), providing protection, certainty to traders, holding PMSE, and consumers. The Trade Law defines PMSE as a trade whose transactions are carried out through a series of electronic devices and procedures. PMSE business types include traders (merchants), Electronic Commerce Organizers (PPSE) such as electronic communication providers, electronic advertisements, electronic offers, electronic transaction application system operators, service providers, and payment application systems and service providers and goods delivery application systems (tax.go.id, 2014).

However, governing the e-commerce activities without any government intervention to ensure each business generating income from Indonesia facing the same level playing field has not been considered adequate anymore. It needs to equally tax business which has 'tangible entities' located in Indonesia and 'intangible entities' located outside Indonesia while generating income or earning significant economic benefit from large market in Indonesia. With the current status quo of nontaxable income of business located outside of Indonesia, it will not be fair for the similar business compares to domestic nor will erode government tax potential revenue.

As a move forward measure, Indonesia as a member of G20 has also participated to succeed in the global consensus on taxing digital economics which has generated income in market jurisdiction without the physical presence. That commitment has been declared in Ministerial Meeting 2020 on the G20 Riyadh, Inclusive Framework on BEPS OECD/G20 (DDTC News, 2020) with other 130 countries (Sukardi & Jiaqian, 2020). It was also clearly understood by the Indonesian government that the realization of current tax revenue from the digital business could not reflect the large potential of transaction activities in Indonesia. It means, Indonesia still has a big opportunity to optimize its potential revenue knowing its role as a market jurisdiction. With this fact, Indonesia should actively participate in the public international arena to discuss how it should allocate the taxing rights into market jurisdiction, to what extent the factors affecting the income threshold in each jurisdiction should be considered, or how it should define the routine and non-routine scope as the fundamental basis to calculate the amount of tax be able to mobilize by the source income countries. On the other hand, to govern the tax treatment on digital service, the domestic provision mentions in Article 6 (1) of the Government Regulation in Lieu Law of the Republic of Indonesia (Perppu) No. 1 the year 2020 – then becomes Law No. 2 years 2020 that tax treatment in trading activities through electronic systems or Perdagangan Melalui Sistem Elektronik (PMSE) shall be done with the following:

(a)the imposition of Value Added Tax on the utilization of Intangible Taxable Goods and/or Taxable Services from outside the Customs Area within the Customs Area through Trade Through Electronic Systems (b)the imposition of Income Tax or electronic transaction tax on Electronic Trading (PMSE) activities carried out by foreign tax subjects who meet the provisions of significant economic presence.

Article 6 (1) above can be considered as a mode of legal basis to tax highly digitalized businesses. Specifically, on that Article 6(7) highlight the means of significant economic presences as one of or accumulated of the following form:
(a)gross circulation of the business group consolidation up to a certain amount; (b)sales in Indonesia up to the amount certain; and/or (c)active users of digital media in Indonesia until a certain amount.

This provision reflects the proposal of OECD as stated in its Proposal and Public Consultation Document. From the informant perspective, the formulation to this legal basis is considered as a step forward among the developing countries but it can effectively bring additional revenue if the tax authority has been able to calculate the volume of transaction made on its domestic market. The availability of this regulation has functioned as a new legal basis or the umbrella of the act to impose income tax once the global consensus has been reached. Until currently, the public international still discuss the Proposal and is expected to reach the consensus by mid-2021 (OECD, 2020). However, even in the presence of a legal basis to tax income generated by the nonresident digital business once the global consensus has been reached, Indonesia must face myriad numbers of challenges. For the legal aspect, the execution to levy tax can be done if it has sufficient technical regulation and guidelines. Further, the way business performed is in highly digitalized mode, which means the tax authority – Directorate General of Taxes also has to adopt the way of their organization run their activities into the way of business work. This also means that DGT as an organization should adopt to their external environment change.

For the technical aspect, similarly, with other developing countries, Indonesia may face the challenges to adjust the formula proposed by the global consensus and the possibly former different treatment on an accounting basis and taxation basis to ascertain the amount of income generated by a nonresident from Indonesia market. The difference in permanent and temporary expenses on the recording system may be the future challenges on ascertaining how much pie will be earned since the allocation of profit can be made after the business group consolidated its income – income inclusion from all of the jurisdiction (Deloitte, 2020). Further, each business also proposes different concerns on how it must recognize the activities determined as substantial value creation. For example, as reported by Ernst & Young (2020) for the digital business model, the company prefers the marketing intangible to recognized as the enterprise's residual profit that is related to the value creation of a jurisdiction where the MNE operates. Then, for a fast-moving consumer goods company, marketing and trade intangible contribute to the failure and sustainability of business thus it should consider the high value of the aforementioned activities. Further, for the pharmaceutical industry, it expresses apprehension on the process which determine system profit, routine return among other aspects. The business believes that the profit split method will cause dispute in the current environment when the arm's length standard is applied. It also proposes the use of a formulaic calculation to calculate local market profits, starting with a base rate and adjusting to the profit level for a country by using the three levers formula (Nayak, 2020).

However, apart from those different treatments of accounting basis, Indonesia future tax and accounting record system must be able to sufficiently categorize and justify the income generate from routine and non-routine activities, income generates from residual and routine profit, and value creation framework as a basis to allocate the profit among jurisdiction and as nexus to allocate the taxing rights. Indonesia also needs to improve the arm's length principle beyond the current traditional transfer pricing rule. The arm's length framework must be compatible with the digital business. Escalating the current transfer pricing arm's length rule which is commonly applied to manufacturing products must be improved to adequately apply into the highly digitalized business. With the currently available tax rule, these "basic regulation facilities" must be created. This discussion seemed absent from the taxation forum. The current taxation forum intensively discusses solely the imposition of value-added tax on digital products.

Importantly, to what extend the Indonesia government will get the pie, will depend on how reliable the Indonesian government could collect the database on how many entities of highly digitalized business has operated in Indonesia, how much they have earned from Indonesia, what they have prepared to enlarge their market in Indonesia, how much the volume of transaction in Indonesia. Certainly, the comprehensive data about their business entities and how significant they earned economic benefit from Indonesia would be the basis for the Indonesian tax administration to have the power to tax those businesses with a fair amount of pie.

As a response to the global challenge, the Directorate General of Taxes has established a new directorate, namely Directorate of Data Collection and Information and Directorate of Information Technology and Communication. Those additional new two directorates are sound positive to respond to the challenges. However, to what extent that new two directorates to be able to collect the data, to make the new reliable projection of additional revenue must be collected and to ensure Indonesia must have additional revenue fairly are another different thing, as it also has to set a mode to settle a dispute resolution. The DGT has still continuously expressed their problem related to the collection of data event though at the same time it also has claimed that the DGT has made effort to collect the data through several modes or program of data collection such as National Payment Gateway, (Sejati, 2020) Core Tax to record and to monitor taxpayer compliance (Prima, 2019). With the newly established directorate, the DGT is expected to establish better coordination with other government bodies which engage in digital business. The problem of coordination among government bodies should not become an everlasting problem.

CONCLUSION

The global consensus has proposed a step to move forward on taxing a highly digitalized economy other than the traditional physical-presence basis through BEPS Inclusive Framework Project. OECD/G20 proposed new nexus of taxing rights and a new approach on profit allocation into jurisdictions including the market jurisdictions. The allocation of profit is based on value creation, routine function, and other considerations before the sustainability of the business. This proposal will certainly affect Indonesia's tax revenue potential as a member of G20 and importantly as a big market jurisdiction. The commitment of Indonesia to support to conclude the proposal will bring an impact to the formulation of domestic provision to implement the adopted policy once it has concluded. Unfortunately, with Indonesia's current position, it has never published its position, commentary, or proposal to the global public arena.

Indonesia has formulated the legal basis to tax highly digitalized businesses. That legal basis ultimately refers to the OECD/G20 BEPS Inclusive Framework proposal. Certainly, this act is considered as a move forward to be ready into the international arena and as a measure the catch the opportunity. However, the Indonesian tax authority still has a list of homework needs to deal with. Firstly, it must be able to formulate appropriate legal implementing regulation and the technical guideline with the new complexity. Secondly, with the worldwide business, the business needs to consolidate its business activities report before the profit is allocated to each respective jurisdiction before the allocation of taxing rights, this work will become a new challenge to business and tax authority. The tax authority needs to enhance current basic taxation adaptable to the new calculation method of business activities reporting system. Thirdly, the tax authority needs to improve its capacity as an organization and individual to follow the dynamic change of its internal and external environment. Establishing a new directorate to enhance its function should be optimized following the aim of its creation. With this digital era, the tax authority should be able to handle the database system to ensure the potential tax revenue it should collect.

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