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Matching cost against revenue at royalty expenses a tax court case in Indonesia

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ABSTRACT

The recording of royalty expenses must not only be consistent but also complied with the principle of matching costs against revenue, especially in calculating taxable income. If all accounting principles are not met in recording the royalty expense, the tax authority will correct it so that the royalty expenses cannot be deducted from taxable income. By using a case in a tax court in Indonesia, there is a taxpayer who does not meet the matching cost against revenue principle when recording royalty expenses. The taxpayer deducts these royalty expenses for the previous year in the current year because the amounts of these royalty expenses are known exactly in the current year. Even though the taxpayer's financial statements were audited and had an unqualified opinion, the Directorate General of Taxes (DGT) as the tax authority in Indonesia negated the royalty expenses as a deduction from taxable income. This paper finds that a net sales-based royalty fee scheme can be estimated at the end of the year and deducted from gross income without waiting for a certainty on the amount of royalty expense on invoices received in the coming year. The accounting records of the taxpayer are not proper so that some data or documents cannot be proven in the tax court. The method of recording in the financial statements with an unqualified opinion does not guarantee that the recording follows tax regulations, especially following Generally Accepted Accounting Principles (GAAP).

ABSTRAK

Pencatatan beban royalty tidak hanya harus konsisten tetapi juga harus sesuai dengan prinsip matching cost against revenue, terutama dalam menghitung penghasilan kena pajak. Jika semua prinsip akuntansi tidak terpenuhi dalam pencatatan beban royalti, otoritas pajak akan mengoreksi sehingga beban royalty tidak dapat dikurangkan dari penghasilan kena pajak. Dengan menggunakan kasus di pengadilan pajak di Indonesia, terdapat wajib pajak yang tidak memenuhi prinsip matching cost against revenue saat mencatat beban royalti. Wajib pajak mengurangkan beban royalty tahun sebelumnya di tahun berjalan karena jumlah beban royalty ini diketahui secara pasti pada tahun berjalan. Meskipun laporan keuangan Wajib Pajak telah diaudit dan memiliki opini WajarTanpa Pengecualian, Direktorat Jenderal Pajak (DJP) sebagai otoritas perpajakan di Indonesia mengkoreksi beban royalty sebagai pengurangan penghasilan kena pajak. Penelitian ini menemukan bahwa skema beban royalty berbasis penjualan bersih dapat diperkirakan pada akhir tahun dan dikurangkan dari pendapatan kotor tanpa menunggu kepastian jumlah biaya royalty atas tagihan yang diterima di tahun mendatang. Pembukuan wajib pajak tidak rapi, sehingga beberapa data atau dokumen tidak dapat dibuktikan di pengadilan pajak. Metode pencatatan dalam laporan keuangan dengan opini Wajar Tanpa Pengecualian tidak menjamin pencatatan tersebut mengikuti ketentuan perpajakan, terutama mengikuti Prinsip Akuntansi yang Dapat Diterima SecaraU mum (GAAP).

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1. INTRODUCTION

To earn income, a company will incur expenses related to it. One of the expenses is a royalty expense. Article 6 paragraph (1) letter a point 3 of the Income Tax Law (Pemerintah Republik Indonesia 2008) states that royalties can be deducted from gross income as long as this royalty expense is to obtain, collect, and maintain taxable incomes. The royalty expenses concerned by the DGT are the royalty expenses arising from transactions with related parties such as shareholders. The main problem from this royalty expense is the fairness of the transactions such as whether or not there are real royalty expenses and the fair value of the royalty expenses (Kementerian Keuangan 2013). The DGT has not made any specific rules regarding the accounting method of royalty expenses. As long as the recording is complied with the generally accepted accounting principle (GAAP), the royalty expenses can be deducted from gross income.

In 2017, based on the results of the tax audit, the DGT determined that the royalty expenses recording of the taxpayer, PT International Paint Indonesia, in 2015 was not under GAAP. Some royalty expenses could not be charged in 2015. This DGT stipulation is to be a dispute between the DGT and the taxpayer. The Tax Court finally determined this dispute with decision number PUT-009690.15/2018/PP/M.VIA in 2020 (Pajak 2020). This decision explains that the recording of royalty expenses must comply with all existing accounting principles, not only partially. The taxpayer argues that the recording of the royalty expenses is consistent because the financial statements have been audited by an independent public accountant and given an unqualified opinion. In such a condition, other principles, such as matching costs against revenue, are considered to be fulfilled. The taxpayer explained that the recording method implemented was not aimed at moving income to a different year and reducing taxable income. The DGT argued that the principle of matching cost against revenue should be applied so that the recognition of royalty expenses was recorded concerning the income earned. This tax court decision also explained a difference in understanding regarding the application of the principle of matching cost against revenue between the DGT and the taxpayer. The panel of judges disagreed with the method of recording the royalty expenses carried out by the taxpayer even though the method was carried out consistently and there was no indication of tax evasion.

The method of recording the royalty expense implemented by PT International Paint Indonesia is a mixture of cash basis and accrual basis. This study finds that this mixed recording method is considered reasonable by independent public accountants so that the audit report issued provides an unqualified opinion. Based on tax regulations, the method of recording expenses must be an accrual method. If there is a difference in a recording like this, the taxpayer should make a fiscal correction on the calculation of taxable income. The taxpayer does not have to change the recording method as long as the recording is done consistently and in disclosure in the financial statements regarding the method used. This study also finds that in providing convenience and understanding financial statements, especially for the DGT, the taxpayer is not advised to record expenses using a mixed method like this. The taxpayer is better off choosing the accrual method in recording the expenses. This study also finds that the use of a recording method that is different from tax regulations and does not make fiscal corrections will cause a dispute with the DGT. The dispute will use resources that do not necessarily provide greater benefits for the taxpayer and the DGT.

In this case, there are 3 types of the disputed royalty expenses and all of them are related to affiliated companies. There is no dispute between the DGT and the taxpayer regarding the method of determining the amount of the royalty expenses and the royalty benefits for the taxpayer. The dispute is about when the royalty expenses can be deductible. For 2 types of royalty expenses, namely technologists & trademarks, and brands, the calculation is based on net sales. The taxpayer recorded this royalty expense as a deduction for gross profit when the values of these expenses were known exactly. The DGT did not approve this taxpayer's accounting method because there was a royalty expense that should have been charged in the previous year (2104) but was charged by the taxpayer in the current year (2015).

There are different interpretations regarding the condition when the certainty of the royalty expenses can be deducted from the gross income. The taxpayer argued that the certainty of this royalty expense amount occurs when there is a royalty expense invoice from the affiliate that has an intangible asset. The

invoice was received in the following year. The DGT argued that the taxpayer could estimate the royalty expense amount at the end of the year. When it was known the certainty of the royalty expense amount from the invoice, the taxpayer could make adjustments. For the third royalty type, namely SLA, the DGT corrected this expense because it was really a royalty expense from the previous year (2014) and it was only charged in 2015. There is no clear information on how to calculate this royalty expense. This SLA royalty is deducted from gross profit because the taxpayer received the invoice in 2015.

Besides differences in the recording method of royalty expenses, this research finds that the taxpayer cannot provide sufficient evidence to convince judges that the total royalty expense is IDR 14,260,441,642. Based on the facts in the tax court, there should be a positive fiscal correction to the royalty expenses of IDR 14,260,441,642. However, the tax audit results by the DGT have a positive correction to the royalty expense of IDR 7,939,424,300. The DGT should pay attention to this fact in determining policies. The discovery of new data at the hearing during an appeal can be used as material for the DGT to determine whether further action is needed on the income tax return reported by the taxpayer.

2. THEORITICAL FRAMEWORK AND HYPOTHESIS

One of the company's goals is for the shareholders' welfare (He and Kyaw 2018). For multinational companies, the companies included in the affiliation may have a role as a cost center or as a profit center (Merchant, Chow, and Wu 1995; Robinson, Sikes, and Weaver 2010). Determining which company is the profit center or the cost center depends on the overall multinational company strategy. If a country can become a profit center for a multinational company, they will have some strategies to move income from that country to another. One measure of the success or failure of a company's profit center is seen from the low effective tax rate or ETR (Robinson, Sikes, and Weaver 2010).

Indonesia is a fairly large market because of its largest population in ASEAN and a potential market for a multinational company to generate profits. With market considerations and corporate income tax rates, the international companies in Indonesia are trying to reduce tax payments or minimize the value of ETR. The corporate income tax rates in ASEAN countries in 2015 according to the tax year case in this paper are shown in Table 1. One way to reduce the tax payments is through royalty payments to affiliate companies abroad. One example is the case found in the Court Decision number PUT-115980.15/2014/PP/M.IIIA (Pajak 2018). In this Court Decision, a company in Indonesia used technology and paid royalties to a company abroad. The products produced by the Indonesian company were sold to royalty owners abroad. This case indicates that the foreign company can get a large income from Indonesia with a royalty payment scheme. The royalty expense in Indonesia can reduce tax payments.

By using manufacturing companies listed on the IDX from 2014 to 2017, the ETR and Cash ETR values are shown in Table 2. ETR is the ratio between income tax expense and GAAP profit before income tax. CashETR is the ratio between income tax payments and GAAP profit before income tax.

Table 2, explains that the mean value of ETR in 2014 and 2015 is greater than the income tax rate that is 25%. In 2016 and 2017, the mean ETR was less than 25%. It is estimated that in 2016 and 2017, most companies carried out aggressive tax planning due to the tax amnesty policy (Santoso 2020). Considering

Table 1
ASEAN States Corporate Income Tax Rates

No.	Country	Tariff (%)
1	Philippines	30
2	Indonesia	25
3	Malaysia	25
4	Singapore	22
5	Thailand	20
6	Vietnam	17

Source: Inside Tax Issue 321 June 2015

the mean value of CashETR, the manufacturing companies do not reduce tax payments. The strategy is taken not to reduce the tax payments but to increase the tax expenses. Most taxpayers do not carry out an aggressive tax planning strategy. The tax aggressive is carried out when there is an opportunity for taxpayers such as tax amnesty policy. This evidence is in line with the explanation byBayer, Oberhofer and Winner (2015). This fact explains that certain taxpayers carry out tax planning by reducing tax payments aggressively only.

On the contrary, there is opportunistic management that is too aggressive in implementing tax planning by reducing tax payments to get incentives. This tax payments reduction will generate more cash and will be done by opportunistic management for personal benefit (Desai and Dharmapala 2009; Jensen 1986). Management has the discretion to choose the accounting method applied in the company and this can benefit management but harm shareholders (Aubert and Grudnitski 2014). The application of the Sarbanes-Oxley Act (SOX) in the USA can protect shareholders (Aubert and Grudnitski 2014). Another study explains that work meaningfulness is theoretically and empirically related to company performance (Kubiak 2020). Work meaningfulness is influenced by 3 psychological needs, namely, having the ability to choose tasks in the organization (autonomy), feeling that their work is valuable or useful (competence), and having a desire to relate to other people (relatedness). Therefore, there are several ways to reduce opportunistic management, including improving corporate governance as described in SOX and influencing the psychology of human resources in companies.

In another case, the parties with an interest in the company are not only shareholders, but also the tax authority as a corporate stakeholder has an interest in the company profits (Fontaine, Haarman, and Schmid 2006; Smith 2003). In addition, the tax authority is also interested in whether the taxes paid by the company are under its financial statements that are reported to investors and the tax authority (Caballé and Dumitrescu 2020).The tax authority’s interests are related to stakeholder theory (Freeman 2004; Freeman et al. 2010). Stakeholders are parties who have an interest in the company and can influence and be influenced by the company’s business. Tax planning carried out by the company will affect the tax authorities. This condition can be seen by the existence of a tax authority policy in the form of the Tax Cuts and Jobs Act (TCJA) which changes taxation in the USA because tax planning is in the form of a reduction in the tax burden carried out by taxpayers for a long time (Drake, Hamilton, and Lusch 2020).

Tax authority as a stakeholder also has an interest in the company’s accounting records to measure performance and, therefore, the tax authority pays attention to the accounting methods used by the company (Hörisch, Schaltegger, and Freeman 2020). In making decisions such as the selection of an accounting method, the company must pay attention to the interests of various stakeholders (de Gooyert et al. 2017). The tax authority has the authority to conduct tax audits on companies. One of the purposes of this tax audit is to find out how much tax must be paid by the taxpayer. The amount of tax paid is one of the interests of the tax authorities to the company. The tax audit conducted by the tax authority also can serve as a monitoring tool for shareholders on policies implemented by management. Due to the tax audit, the management will be more conservative in implementing its tax policies (Brushwood, Johnston, and Lusch 2018)”ISSN ”:”08826110”,”abstract”:”We examine whether firms respond to settlements of their uncertain tax benefits (UTBs.

Table 2
ETR and Cash ETR Description

	2014	2015	2016	2017
ETR:				
Mean	0.257	0.284	0.124	0.125
Median	0.247	0.248	0.248	0.242
CashETR:				
Mean	0.477	0.339	0.305	0.668
Median	0.266	0.258	0.243	0.249

Source: IDX

Due to the incentives provided being based on profits from financial statements, they prepared it based on GAAP informing a minimum tax payment (Armstrong, Blouin, and Larcker 2012). Then, there could be a significant difference between profit in the financial statements based on GAAP and taxable income in the Annual Corporate Income Tax Return. The GAAP financial statements may report a profit and the corporate income tax return declare a loss. The difference in these two reports is due to accounting engineering (Purwanti et al. 2015). With its legality, the tax authority can carry out tax audits to ensure that the company's income tax returns are under applicable regulations. The DGT as the tax authority in Indonesia determines the tax audit criteria and procedures to test whether the income tax returns comply with the regulations, and one of the criteria is a taxpayer who declares an overpayment of taxes (Indonesia 2015).

The royalty payment strategy to foreign affiliated companies can be a deduction from gross income to determine taxable income if it meets several requirements (Direktorat Jendral Pajak 2011). Based on the tax regulations in Indonesia, the requirements are as follows (Kementerian Keuangan 2013):

a. There are intangible assets that contribute to the success of the product in the market.
b. It can be identified which party contributed to the formation of the intangible asset.
c. It is evident that intangible assets have been transferred to the party using them.
d. It can be ensured that the compensation for the use of intangible assets is fair.

There are two royalty payment schemes, namely per-unit royalty and ad valorem (San Martín and Saracho 2010). Another article explains that there are 3 royalty payment schemes, namely fixed fees, per unit royalty, and ad valorem royalties (Bousquet et al. 1998). Per-unit royalty is a fixed royalty payment based on the number of tangible tax assets used. Ad valorem is a royalty payment based on a certain percentage of the proceeds from the use of royalties, for example from sales. A fixed fee is the amount of royalty that is paid by agreement between the owner and user of the royalty property regardless of how much tangible assets are used and how much output is generated from the use of these intangible assets. In its application, the royalty payment scheme may be a combination of these two or three payment patterns. These royalty payment schemes can affect the total production of companies that use these intangible assets. The ad valorem scheme will result in higher prices and lower total production units (San Martín and Saracho 2010).

The choice of a royalty payment scheme depends on the information obtained by the owners of intangible assets against those who use intangible assets, namely information on demand and costs for goods or services produced (Bousquet et al. 1998). When the information regarding the demand is uncertain (cost information is known), the ad valorem royalty payment pattern is better for the parties making the royalty contract. When information regarding costs is uncertain, several alternative payment schemes may arise. The use of this payment scheme depends on certain conditions such as the level of risk in the license contract. For companies using intangible assets from affiliated companies, the owners of intangible assets have information about costs and uncertainty of information on demand for goods. Therefore, it is preferable to charge royalties based on the ad valorem scheme.

Based on the income recognition principle (IAI 2017), royalty income is recognized when or as long as the entity fulfills its performance obligations by transferring promised goods or services (i.e. assets) to customers. Assets are transferred when (or during) the customer obtains control of the asset. The recognition of income from royalties is recognized over time. One definition of over-time recognition is that royalty users simultaneously receive and consume the benefits of the royalty provided by the owner of the intangible asset.

Based on the principle of matching cost against revenue, the royalty expense can be used as a deduction for income when there is income from the use of the intangible asset. Based on the accounting period principle, there is an equal period time between royalty income and expenses due to the use of intangible assets. In general, the timeframe used is the calendar year starting from January 1 and ending on December 31. From this accounting principle, it is possible to estimate the amount of income or expense as of December 31, even though there is no certainty about the amount of revenue and expenses that are determined from the bills or invoices issued. If the determination of royalty expense is ad valorem, which is based

on total sales, and then the royalty expenses can be determined as of December 31, because as of December 31, the sales value can be known with certainty.

The use of intangible assets is intended to increase the success of product sales in the market (Kementerian Keuangan 2013). In multinational companies, the intangible assets may come from the affiliated companies and sales to affiliated companies. There may be a role for the parent company to coerce the company using this intangible asset to sell its products to affiliated companies. In such conditions, have there been any successful sales of the product created by using this intangible asset? Can the royalty expense be used as a deduction to calculate taxable profit and net income? To ensure the fairness of transactions between related parties with transfer pricing transactions, it is necessary to carry out tests in the form of comparability analysis (Nations 2013; OECD 2010), namely characteristics of property or services, functional analysis, contractual terms, economic circumstances, and business strategies.

3. RESEARCH METHOD

This study uses a case study derived from a tax court ruling in Indonesia, namely the tax court decision number PUT-009690.15/2018/PP/M.VIA in 2020 (Pajak 2020). This decision can be downloaded from the website of the *Sekretariat Pengadilan Pajak, Kementerian Keuangan*, whose address is http://www.setpp.kemenkeu.go.id/risalah/IndexPutusan. This paper analyzed a selected tax court case using related kinds of literature. The analysis was carried out by desk-based.

The case discussed is a dispute case between the DGT and a taxpayer, namely PT International Paint Indonesia. The DGT conducted an audit of the 2015 Corporate Income Tax Return and completed it in 2017. The DGT stipulates that the taxpayer must pay corporate income taxes due to additional incomes and deduction of some expenses so that the taxable income increases. One of the expenses that the DGT corrected was the royalty expense. The royalty expenses occur because the taxpayer used intangible assets owned by affiliated companies. Regarding the fairness of the related party transactions, in this case, it is not the DGT's concern. The DGT sees that the recording method for the taxpayer royalty expenses is not under GAAP, so there is a correction.

This study discusses how to record royalty expenses according to the taxpayer and the DGT, and provides an overview of recording royalty expenses by considering the tax court's decision. The stage of the discussion of this case study begins with explaining a glimpse of information about the taxpayer. The next discussion in order is to explain the facts in court regarding the recording of royalty expenses, explain the dispute over royalty expenses, and discuss the proper recording of royalty expenses following the tax court's decision.

Taxpayer Information

PT International Paint Indonesia (PT. IPI) is an overseas investment company that has been doing business in Indonesia since 1992. All of PT IPI's companies are owned by Akzo Nobel, which is headquartered in the Netherlands. PT IPI's main products and markets include as the following (Iskandar 2008):

a. Marine coatings, namely ship protection specialists. Products sold include anti-corrosive and anti-fooling.
b. Protective coatings, namely protection of hard materials against chemical corrosion. Sales areas are to the oil and gas industry, paper and pulp industries.
c. Coil coatings, namely protection against steel coils.
d. Powder coatings, namely powder coatings for the industry in general, automotive components, and architecture.

Facts in Tax Court

Details of the royalty expenses corrected by the DGT are shown in Table 3.

The royalty expenses were corrected because they were the expenses for 2014 and could not be used as the deductions from gross income for 2015.

The taxpayer explained that the method of collecting royalty expenses was as follows (Pajak 2020:10):

a. The royalty expense invoices based on actual net sales for the January - June period would be billed for the period September in the same year;
b. The royalty expense invoices based on actual net sales for the July - September period plus the net sales forecast for the October - December period would be billed in the November period; and

Table 3
Details of the Royalty Expense Corrections

No	Information	Amount (IDR)
1	Technology & Trademark Account: Royalties-Intercompany	2.389.060.862
2	Brand Account: Internalcst-Other	242.713.053
3	SLA Account: Other Adj Inside	5.307.650.385
	Total the Royalty Expenses	7.939.424.300

Source: Processed Data

c. The royalty expenses deficiency invoices based on the difference between forecast and actual net sales for the October - December period would be billed in the following tax year.

The taxpayer explained that:

a. The Technology & Trademark royalty expenses, corrected by the DGT IDR 2,389,060,862, were the royalty expenses calculated based on the difference between forecast and actual net sales for the period October - December 2014 and invoiced in 2015.
b. The Brand royalty expenses, corrected by DGT IDR 242,713,053 were the royalty expenses calculated based on the difference between forecast and actual net sales for the period October - December 2014 and invoiced in 2015.
c. The SLA royalty expenses, corrected by the DGT IDR 5,307,650,385, were expenses for 2014 and were charged in 2015 because the calculation was only completed after the end of 2014 and was invoiced in 2015.

By using Article 28 paragraph (5) of the Law General Provisions and Taxation procedures (*Ketentuan Umum dan Tata Cara Perpajakan* or KUP) (Pemerintah Republik Indonesia 2007), the taxpayer explained that this recording method had obeyed with the accrual system or cash system. Obeying the principle was done to prevent a shift in profit or loss. An accrual system is a method of calculating an income and an expense, where an income is recognized when it is earned and an expense is recognized when it is payable, regardless of when the income is received and when the expense is paid in cash. The taxpayer deducted these royalty expenses when the expenses were payable or could be ascertained the amount through invoices. Because the taxpayer did this method strictly under the principle, the taxpayer argued that the royalty expenses were corrected by the DGT IDR 7,939,424,300 were not expenses in 2014, but expenses in 2015.

The DGT explained that the taxpayer should be able to estimate these royalty expenses by the end of 2014. If there is still a shortage of these royalty expenses, the taxpayer can adjust the journal and charge these royalty expenses in the year concerned. There is no information on what year it is concerned. This paper assumes that the year in question is 2015 because 2014 has closed the book.

The results of evidence in Tax Court on this dispute are as follow:

a. The 2015 royalty expenses are IDR 40,870,358,690. The details are in Table 4.
b. The royalty expenses that are positively corrected by the DGT are IDR 7,939,424,300 because of the expenses in 2014.
c. Evidence showed by the taxpayer in Tax Court against the royalty expenses of IDR 25,870,699,218 relate to parties with a special relationship (Akzonobel and International Paint Limited). From these royalty expenses, IDR 2,631,773,914 is for 2014 and the invoice proven by the taxpayer in Tax Court for this royalty expenses are only IDR 2,378,518,476. (Difference of IDR 253,255,438.).
d. The taxpayer cannot provide supporting evidence at the Tax Court hearing of the estimated royalty expenses of IDR 14,260,441,642.

The taxpayer explained that the royalty expenses paid to Akzo Nobel Coating International BV were 5% of the total net coating sales. The procedure for paying the royalty expenses was only 2 times per year, namely September and November. The November invoices were not all actual costs and some were estimated sales value of coatings. The difference between the estimate and the actual was collected in the following year. Based on the facts at the Tax Court and the principle of matching cost against revenue,

the panel of judges decided that the DGT fiscal corrections were maintained and rejected the taxpayer's appeal.

The transactions on intangible assets are the related party transactions. The audits conducted by the independent public auditor and the DGT have the same opinion, that these transactions are arm-length transactions. The DGT did not question the requirements that must be met so that these royalty expenses can be used as a deduction from gross income following applicable regulations (Kementerian Keuangan 2013). These related party transactions are reasonable according to the agreed criteria and applicable regulations (Nations 2013; OECD 2010).

Dispute

The royalty expenses in dispute are divided into 3 types of royalties, namely:

a. Technology & Trademark.
b. Brand

SLA

The three royalties in this dispute are related party transactions. The Royalty Technology& Trademark and the Brand become a dispute because the taxpayer charges these royalty expenses awaiting the certainty of the amount as seen from the invoices. Even though there is a cost estimate (from sales forecast for October to December), it was not adjusted at the end of December 2015. The calculation presented by the taxpayer in the Tax Court was without the royalty expenses based on net sales in December 2015. There is no basic information on assigning SLAs. The taxpayer argued that a certain amount of SLA expenses obtained after an invoice was received. Because the invoices of SLA royalty expenses were received in 2015 for sales of 2014, these expenses were charged in 2015. The DGT corrected all SLA royalty expenses related to sales in 2014.

4. DATA ANALYSIS AND DISCUSSION

Technology & Trademark

Based on facts in the tax court, the total royalty expenses on the Technology & Trademarks charged by the taxpayer in 2015 was IDR 23,466,332,995, consisting of the expenses for 2014 paid in 2015 amounting to IDR 2,400,083,006 and the expenses for 2015 paid in 2015 amounting to IDR 21,066,249,989 (Pajak 2020:57). The 2015 royalty expenses paid in 2016 were likely to be charged in 2016. The DGT corrections to this royalty expense amounted to IDR 2,389,060,862. There is a difference between the 2014 royalty expense proven in the Tax Court and the DGT correction of IDR 11,022,144 (IDR 2,400,083,006 - IDR 2,389,060,862). There is no further information on this difference.

Proof in Tax Court against the calculation of the royalty expenses of IDR 23,466,332,995 is as follows (Pajak 2020:57) (Table 5 and Table 6).

For the 2015 period, the December 2015 net sales estimate was not taken into account, whereas based on the taxpayer's explanation, the December 2015 net sales forecast was calculated to determine the amount of the 2015 royalty expense (Pajak 2020:10). This fact proves that the taxpayer is inconsistent in providing evidence and arguments in Tax Court.

Table 4
Details of Royalty Expenses

Account No	Description Account	Balance as of 31 Dec 2015 (IDR)	Correction of DGT (IDR)
C5512500	Royalties based to 3rd Sales Based	55.028.946	0
C7819000	Internalcst-Other	2.349.337.266	242.713.053
C7811100	Royalties-Intercompany	23.466.333.006	2.389.060.862
C7832000	Other Adj Outside	739.217.830	0
C7853000	Other Adj Inside	14.260.441.642	5.307.650.385
	Total	40.870.358.690	7.939.424.300

Further analysis shows that:
Royalties based to 3rd Sales Based is Nippon Royalty.
Internalst-Other is Corporate Brand Royalty.
Royalties-Intercompany is a Technology & Trademark Royalty.
Other Adj Outside and Other Adj Inside are SLAs.
Source: Processed Data

Table 5
Proof in Tax Court (2014 Period)

2014 period:	
Net Sales value for January-December 2014	IDR 466.547.550.566
Royalty rate for Technology & Trademark	5%
Royalty expenses payable	IDR 23.327.377.528
Royalty expenses paid in 2014	IDR 20.939.316.667
Royalty expenses from 2014 paid and charged in 2015	IDR 2.389.060.862

Source: Processed Data

Table 6
Proof in Tax Court (2015 Period)

2015 period:	
Net Sales value for January – September 2015	IDR 344.719.958.046
Forecast Net Sales October – November 2015	IDR 76.604.435.121
The number of Net Sales for the royalty expenses invoices	IDR 421.324.393.167
Royalty rate for Technology & Trademark	5%
Royalty Expenses for 2015	IDR 21.066.219.658

Source: Processed Data

The taxpayer's calculation and recognition of royalty technology & trademark expenses use a combination of cash basis and accrual basis. There was an expense incurred in 2014 but was charged in 2015 because the royalty expense was paid in 2015. There is an expense in 2015 (October - November) charged in 2015 even though the royalty expense was paid in 2016. This treatment is different from the income recognition principle (IAI 2017).

As an agent of principal, management has the flexibility to choose the method of recording in measuring its performance (Aubert and Grudnitski 2014). However, it should be noted whether the selection of this recording method could interfere with the interests of all parties, not only shareholders but also stakeholders. This recording does not appear to be a problem for shareholder interests but is a problem with DGT as a stakeholder. This is proven by the results of the independent public accountants audit report, which provided an unqualified opinion. This public accountant's opinion is also used by the taxpayer as an excuse in court hearings to maintain the recording method used. The DGT as a stakeholder does not agree with the mixed methods used by the taxpayer. The taxpayer should pay attention that the interests of stakeholders in the company are various (de Gooyert et al. 2017). Especially for the interests of the DGT, the taxpayer must pay attention to several tax regulations in recording this royalty expense.

This royalty payment scheme is ad valorem using a certain percentage of sales (Bousquet et al. 1998; San Martín and Saracho 2010). The ad valorem scheme can be optimally used if the cost of goods manufactured is known and the demand data are uncertain. This requirement is under the conditions of the taxpayer. Sales of taxpayer products are made to independent third parties, so the demand for their products is uncertain.

There are two in the value of this royalty expense, IDR 23,466,332,995 and IDR 23,455,310,851, both of which come from the taxpayer itself. The explanations are as follow:

a. Details of the royalty expenses submitted by the taxpayer explaining the Technology & Trademark royalty expense of IDR 23,466,332,995 (IDR 2,400,083,006 + IDR 21,066,249,989)
b. The calculation of the royalty expense per tax year is IDR 23,455,310,851 (IDR 2,389,060,862 + IDR 21,066,219,658).
c. There is a difference of IDR 11,022,144 (IDR 23,466,332,995 - IDR 23,455,310,851).

There is no information on this difference. From this fact, it can be assumed that the taxpayer is less thorough and inaccurate in providing proof of calculation.

The evidence in court explained that the taxpayer was also inaccurate in providing documents as evidence in court. It appears that the accounting books and records implemented by the taxpayer were not proper and orderly.

The existence of this fatal error is an indication that there is opportunistic management. This is following Desai and Dharmapala's (2009) explanation. Two reports must be submitted, one to shareholders and the second to the DGT due to different interests. Consequently, the reports must be completed with neat documents so that the reconciliation process to meet these interests can be correct.

The taxpayer's net sales reported in the 2015 corporate income tax return was IDR 511,950,488,597 (Pajak 2020:36). The taxpayer could already know how much the 2015 royalty expenses were because the taxpayer already knew the total net sales from the annual tax return. There is a question why the taxpayer should wait for an invoice from the intangible asset owner to deduct the royalty expenses in the income statement. The reason why the taxpayer did not use an estimate of the royalty expenses based on the net sales from the annual tax return is also a question.

It is estimated that the postponement of the imposition of royalty expenses is a management strategy. This strategy is used to regulate how much profit is desired (earning management). With the consistent reason that this method is carried out every year, independent public accountants can provide an unqualified opinion. This treatment carried out by management can improve company performance as explained by Kubiak (2020) as long as the selection of this method is valuable for the organization as a whole. Because it is different from tax regulations, management should reconcile this royalty expense when calculating taxable income.

By using the data on net sales in the annual tax return, the Technology & Trademark royalty expenses in 2015 can be estimated and the calculation is as follows (Table 7).

The taxpayer can make an adjustment entry for this unbilled royalty expense, IDR 4,531,304,772 at the end of the year. The entries for these royalty expenses are as follow:

a. September 2015
   Net Sales value for January – September 2015 is IDR 344.719.958.046. The royalty expenses are IDR 17.235.997.902 (IDR 344.719.958.046 x 5%) (Appendix 1).
b. November 2015
   Forecast Net Sales October – November 2015 are IDR 76.604.435.121. The royalty expenses are IDR 3.830.221.756 (IDR 76.604.435.121 x 5%) (Appendix 2).
c. December 2015
   Based on the annual tax return, total Royalty Technology & Trademark Expenses for the 2015 are IDR 25.597.524.430 (IDR 511.950.488.597 x 5%). The adjusted entry as of December 31, 2015 for this royalty expenses are amounted to IDR 4,531,304,772 (IDR 25,597,524,430 - IDR 17,235,997,902 - IDR 3,830,221,756) (Appendix 3).
d. September 2016
   When the invoice and payment are made in September 2016 (the following year), the entry made is adjusted to the actual invoice amount. If the amount of the royalty expenses in the invoice equals the estimate in the adjusted entry (Appendix 4)

If the amount in the invoice is smaller than that of the estimated adjusted entry, for example, IDR 4,500,000,000 (Appendix 5).

If the amount in the invoice is bigger than that of the estimated adjusted entry, for example, IDR 4,600,000,000 (Appendix 6).

This method is similar to that recommended by the DGT. By using this method, the principle of matching cost against revenue can be fulfilled in calculating taxable income. Based on the revenue recognition principle, a measuring tool for the amount of revenue is the amount of cash or its equivalent obtained from all sales transactions with independent parties. By using this principle, the amount of the royalty expenses that are deducted from gross income should not have to wait for the invoice.

Table 7
The Technology & Trademark Royalty Expenses in 2015

	2015	
Net sales based on the 2015 annual tax return	IDR	511.950.488.597
The Royalty expenses rate for Technology & Trademark	5%	
The Royalty Expenses 2015	IDR	25.597.524.430
The Royalty expenses invoiced and paid for the period 2015	IDR	21.066.219.658
The remaining royalty expenses have not been invoiced	IDR	4.531.304.772

Source: Processed Data

Brand

Proofing in the Tax Court, the royalty expenses on Brand (CoBrand) charged by the taxpayer in 2015 was IDR 2,349,337,266 consisting of the expenses for 2014 paid in 2015 amounting to IDR 242,715,300 and the expenses for 2015 paid in 2015 amounting to IDR 2,106,621,966. (Pajak 2020:57). The DGT corrected these royalty expenses amounting to IDR 242,713,053 because it was the expenses in 2014. There is a difference in the 2014 royalty expense that was charged in 2015 between the taxpayer explanation in the court and the DGT correction of IDR 2,247 (IDR 242,715,300 - IDR 242,713,053).

The calculation of these royalty expenses of IDR 2,349,337,266 is as follows (Pajak 2020:57) (Table 8 and Table 9).

There is no calculation of the CoBrand royalty expenses based on sales in December 2015. In Tax Court, the taxpayer explained that the December 2015 net sales were also calculated to determine the amount of the 2015 royalty expenses (Pajak 2020:10). It means that the taxpayer is inconsistent in arguments in the Tax Court.

The calculation and recognition of the CoBrand royalty expenses are the same as the recognition of the technology & trademark royalty expenses, which use a combination of cash basis and accrual basis. This treatment is different from the income recognition principle (IAI 2017). This mixed method of charging royalties can be an indication that there is opportunistic management within the company (Desai and Dharmapala 2009). The discretion possessed by management in choosing an appropriate accounting method should pay attention to the interests of all various stakeholders (de Gooyert et al. 2017). For the interest of the tax authority as one of the stakeholders, management should pay attention to existing tax regulations. Unlike the existing regulations, it can lead to disputes that result in the use of resources without adding value to the company.

The CoBrand royalty payment scheme is the same as the technology & trademark royalty payment scheme, namely ad valorem (Bousquet et al. 1998; San Martín and Saracho 2010). In addition to optimizing the utilization of this royalty, using an ad valorem scheme is easier in determining royalty expenses because the number of sales can be known at the end of the year with certainty. This payment scheme is the best because the owner of the royalty is an affiliated party, the shareholder, that knows well the information on the costs charged by users of the intangible assets (Bousquet et al. 1998).

The net sales reported by the taxpayers on the 2015 corporate income tax return amounted to IDR 511,950,488,597 (Pajak 2020:36). By calculating the same as the royalty expenses on the Technology & Trademarks royalty, recording this royalty expense is not under the principle of matching cost against revenue. The taxpayer can make bookkeeping according to accounting principles.

Table 8
Royalty Expenses (2014 Periode)

2014 period:	
Net Sales Value for the Period January-December 2014	IDR 466.547.550.566
Royalty rate for CoBrand	0,5%
Royalty expenses payable	IDR 2.332.737.753
Royalty expenses paid in 2014	IDR 2.090.024.700
Royalty expenses from 2014 paid and charged in 2015	IDR 242.713.053

Source: Processed Data

Table 9
Royalty Expenses (2015 Periode)

2015 period:	
Net Sales value for January – September 2015	IDR 344.719.958.046
Forecast Net Sales October – November 2015	IDR 76.604.435.121
The number of Net Sales for the royalty expenses invoices	IDR 421.324.393.167
Royalty rate for CoBrand	0,5%
Royalty Expenses for 2015	IDR 2.106.621.966

Source: Processed Data

SLA

There is no clear information on what is meant by the SLA royalty expenses. Data from this court decision explain that the SLA expenses were charged on the Other Adj Outside account of IDR 739,217,830 and Other Adj Inside accounts of IDR 14,260,441,642. During the trial, the taxpayer could not provide supporting evidence to convince the judge that the value of the SLA expenses from the Other Adj Inside account was IDR 14,260,441,642.

From the SLA value of IDR 14,260,441,642, the DGT had corrected with the amount of IDR 5,307,650,385 because it was an expense in 2014 and was charged by the taxpayer in 2015. These SLA royalty expenses are transactions with related parties. From the data, there was the SLA expense from Other Adj Inside of IDR 8,952,791,257 (IDR 14,260,441,642 - IDR 5,307,650,385), which was admitted by the DGT. In the Tax Court, the taxpayer could not provide sufficient evidence to this expense, IDR 8,952,791,257. This fact can be new data for the DGT that there is a burden that cannot be reduced as a deductible expense.

The unclear SLA royalty expenses, both on evidence and the type of intangible assets used must be a concern for DGT in making corrections. Since the SLA expenses are transactions with related parties, the fair value of these transactions must be carried out following the taxation provisions stipulated in the Minister of Finance Regulation number PER-22/PJ/2013 (Kementerian Keuangan 2013). The recording of the SLA expenses can indicate an opportunistic management due to unclear recording methods. From the independent public accountants report, it can be concluded that the SLA recording method is reasonable, while the results of the tax audit by the DGT have an unfair recording method. It is estimated that there is a tax planning that benefits management and is detrimental to shareholders (Desai and Dharmapala 2009).

5. CONCLUSION, IMPLICATION, SUGGESTION AND LIMITATION

Royalty expenses from intangible assets used to generate income can be deducted from both gross income and taxable income. The recording of these expenses must comply with all accounting principles. Although only one of these accounting principles is unfulfilled, the royalty expenses are nondeductible for the taxable income. If the principle of matching cost against revenue is not fulfilled when recording the royalty expenses, it will be detrimental to the taxpayer because the DGT corrects the expenses. The financial statements are audited and received an unqualified opinion by an independent public accountant. This does not guarantee that the recording method at one of its costs is following tax regulations. In this case, the DGT does not recognize the method of recording the royalty expenses by the taxpayer even though the method is deemed reasonable in the financial statements audited by an independent public accountant.

The determination of the royalty expenses based on the ad valorem schema such as from net sales value can be estimated at the end of the year. The net sales value also can be known at the end of the year. The imposition of royalty expenses does not have to wait for a certain amount from invoices received from owners of intangible assets. If there is a difference in the value of the royalty expense at the end of the year and the value of the invoice received in the following year, then this difference can be charged in the year the invoice is received. This recording method can meet the principle of matching cost against revenue.

The 2014 royalty expenses, however, charged in 2015, have been corrected by the DGT. There was no explanation about the 2015 royalty expenses that were charged in 2016. When the court ruling determined that the corrections made by the DGT are correct, there is a question, whether the taxpayer could revise the 2015 corporate annual income tax return by including the 2015 royalty expenses that had been charged in 2016. A further study is needed regarding the policy of whether or not taxpayers can revise the annual tax return due to a court decision. The revision of this annual income tax return of course must be done by paying attention to the expiration date of the annual income tax return, justice for taxpayers, and tax administration.

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Appendix 1.

Account	Debit	Credit
Royalty Technology& Trademark Expenses	17.235.997.902	
Royalty Expenses Payable		17.235.997.902
Royalty Expenses Payable	17.235.997.902	
Cash		17.235.997.902

Appendix 2.

Account	Debit	Credit
Royalty Technology& Trademark Expenses	3.830.221.756	
Royalty Expenses Payable		3.830.221.756
Royalty Expenses Payable	3.830.221.756	
Cash		3.830.221.756

Appendix 3.

Account	Debit	Credit
Royalty Technology& Trademark Expenses	4.531.304.772	
Royalty Expenses Payable		4.531.304.772

Appendix 4.

Account	Debit	Credit
Royalty Expenses Payable	4.531.304.772	
Cash		4.531.304.772

Appendix 5.

Account	Debit	Credit
Royalty Expenses Payable	4.531.304.772	
Royalty Technology & Trademark Expenses		31.304.772
Cash		4.500.000.000

Appendix 6.

Account	Debit	Credit
Royalty Expenses Payable	4.531.304.772	
Royalty Technology & Trademark Expenses	68.695.228	
Cash		4.600.000.000