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Synergy of Pancasila ethical principles and transfer pricing practices for economic sustainability

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Abstract

This study attempts to reconstruct the ethical principles of Pancasila with fair transfer pricing practices to create a set of guidelines that encourage economic sustainability in Indonesia, using a qualitative-critical approach. Data were obtained through in-depth interviews with tax authorities, tax consultants, and multinational companies, as well as document analysis using thematic techniques and NVivo 12 software. Findings suggest that although transfer pricing is legally permitted, the practice is often manipulated to suppress tax burdens, thereby reducing state revenues and exacerbating inequality. Integrating Pancasila values—such as fairness, transparency, and cooperation—into tax governance can encourage more ethical corporate behavior and strengthen regulatory compliance. The first, second, and fifth principles of Pancasila serve as important ethical foundations for regulating transfer pricing, promoting social justice, especially given the structural weaknesses in current regulations and enforcement. The study provides recommendations for strengthening the legal framework, increasing ethical awareness, and multilateral cooperation. Theoretically, it can enrich the literature by bridging local ethics and international tax policies, and provide practical implications for reforming transfer pricing governance that supports the country's fiscal resilience, social welfare, and sustainability.

Keywords: Economic sustainability, Multinational, Pancasila ethics, Transfer pricing.

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1. Introduction

Transfer pricing is the practice of determining prices in transactions between entities that have a special relationship. Although legally valid, this practice is often abused by multinational companies to shift profits to low-tax jurisdictions, which contributes to the erosion of the country's tax base and economic inequality [1, 2]. OECD data [3] shows that developing countries lose around USD 240 billion per year due to this practice. Unethical transfer pricing practices contradict the principles of fairness and transparency and hinder tax revenues needed for national development [4, 5]. Therefore, an approach is needed that is not only technical and legal but also based on ethics so that this practice is fairer and more responsible [6, 7]. This practice has a significant impact on state revenue, especially for developing countries like Indonesia, which rely on taxes as one of the main sources of state revenue [8, 9].

Indonesia, as a country with the ideology of Pancasila, prioritizes the values of social justice, shared prosperity, and economic sovereignty in business and tax governance [10]. This study looks at transfer pricing from a different angle by using Pancasila's moral and ethical values as a basis for making fair transfer pricing rules in Indonesia. Unlike previous studies that focus on technical aspects and international regulations such as the OECD Guidelines and BEPS Action Plan, this research emphasizes a philosophical and ethical approach based on national ideology to create a more just taxation system. A Pancasila-based ethical approach is expected to provide a holistic framework for managing transfer pricing. Values such as cooperation (gotong royong) and social justice foster synergy between corporate interests and national interests, creating a more harmonious relationship between businesses and the government (pajak.go.id). The integration of Pancasila principles into transfer pricing regulations can serve as a solution to ensure that such policies benefit corporations and contribute to economic sustainability. This study aims to reconstruct how the ethical principles of Pancasila can be synergized with fair transfer pricing practices to improve economic sustainability. Furthermore, this research offers policy recommendations to align taxation regulations more closely with Pancasila values.

2. Literature Review

Transfer pricing practices by multinational enterprises (MNEs) have become a critical issue in the global economy, especially due to their potential misuse for tax avoidance. These practices significantly impact developing countries, which are particularly vulnerable to the erosion of their tax base [11]. Aggressive transfer pricing not only undermines the tax base of source countries but also exacerbates global economic inequality [12-14].

In response to these challenges, the OECD has issued international guidelines to assist countries in tackling abusive transfer pricing and aggressive tax planning practices [3]. However, the implementation of these guidelines in developing countries faces numerous obstacles, such as limited tax administration infrastructure, lack of skilled human resources, insufficient access to relevant data, and the complex nature of multinational business structures [15, 16].

These conditions lead to weak protection of national tax bases and make developing countries particularly susceptible to tax avoidance by MNEs [17]. Transfer pricing manipulation is commonly found in high value-added industries such as electronics, pharmaceuticals, and digital services, where income shifting is facilitated by complex cross-border structures OECD [3]. Fu and Ghauri [12] emphasize that MNEs often set transfer prices that do not reflect market values, either excessively low or high, depending on tax optimization motives. Transfer pricing schemes involve not only mispriced transactions but also the use of shell companies, royalty agreements, and intra-group management fees that lack economic substance [18, 19]. These practices create substantial fiscal injustice, shifting the tax burden onto sectors like MSMEs and individual workers who lack access to sophisticated tax planning mechanisms [20, 21].

In international taxation, the arm’s length principle supported by the OECD says that transactions between related companies should have prices similar to those that unrelated companies would agree on in the same situation [3]. Unfortunately, the application of this principle in developing countries often encounters technical challenges, such as the lack of reliable comparables and limited analytical capacity within tax authorities [16, 22-24]. This principle, while technical, also has strong ethical dimensions in promoting fairness and equity in the tax system.Fiscal injustice becomes more pronounced when MNEs, backed by financial and legal power, exploit regulatory gaps and institutional weaknesses to minimize tax liabilities [12, 19]. If transfer prices are set fairly, tax burdens can be distributed more equitably, and government revenues would better reflect real economic activity [20, 25]. In contrast, manipulative transfer pricing creates imbalances in tax contributions across economic actors [26, 27].

This ultimately generates fiscal pressure on governments, hampering efforts to fund inclusive and sustainable development [21, 28]. Consequently, public services such as infrastructure, education, and healthcare suffer from underfunding [25]. Therefore, monitoring transfer pricing must be prioritized in the tax policy agenda of developing nations [29]. Such efforts should not only be technical but also ethically driven to ensure social justice [21, 30, 31]. Strengthening transfer pricing governance requires the integration of fairness principles, international standards, and moral values. Mehafdi [4] argues that ethics and social justice must underpin transfer pricing policies to build a just and sustainable system.

In Indonesia, transfer pricing has allowed MNEs to underreport profits in high-tax jurisdictions while inflating earnings in low-tax ones, often without real economic activities in the latter [8, 32]. As a developing country with significant foreign investment potential, Indonesia faces serious challenges in overseeing affiliated transactions that often do not reflect market values. To address this, the Indonesian government has enacted several key regulations. One is Minister of Finance Regulation number 172/PMK.03/2023, which requires taxpayers engaged in related-party transactions to prepare transfer pricing documentation (TP Doc) to justify the fairness of their prices during audits [33]. Another policy is Minister of Finance Regulation number 22/PMK.03/2020 on Advance Pricing Agreements (APAs) [34], which allows taxpayers and the tax authority to pre-agree on transfer pricing methods for future transactions, covering aspects like royalties, service fees, and transfer prices [35].

These policies aim to shift the tax authority’s role beyond enforcement to that of a collaborative partner, fostering voluntary compliance through transparency. Nevertheless, their effectiveness remains limited by several barriers. Among these are taxpayers’ lack of understanding, low integrity in policy implementation, and difficulties in verifying complex cross-border transactions [36-38]. In this context, MNEs with access to professional advisors can more easily exploit legal loopholes.

From an ethical economic perspective, transfer pricing is not merely an accounting or tax calculation issue—it embodies moral obligations in the economic relationship between corporations and the state. Ethical business practices demand transparency and fairness in financial decision-making, including pricing policies [4]. When transfer pricing strategies align with ethical standards and local values, they enhance public trust and institutional legitimacy, harmonizing corporate and national interests [39].

Institutional theory offers a useful framework to understand MNE behavior in developing countries' transfer pricing regimes. Firms are not just rational entities seeking efficiency and profit but also social actors embedded in institutional environments shaped by regulations, norms, cultural values, and social expectations [40]. Within this view, Rawls' theory of justice [41] underscores the need for fair distribution of economic benefits and burdens. Unjust transfer pricing strategies systematically undermine equity and disadvantage developing nations.

To bridge this implementation gap, tax governance must be grounded in value-based principles. Indonesia's state philosophy, Pancasila, offers relevant ethical foundations, including social justice, humanitarianism, and solidarity. These principles can guide economic relationships between corporations and governments toward more equitable outcomes. Therefore, the literature highlights that embedding local ethical values into global governance frameworks can promote more just and inclusive economic development.

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3. Methodology

The study looks at how Pancasila ethical values are applied in transfer pricing practices in Indonesia using a qualitative method and a critical paradigm. This approach was chosen because it allows for in-depth exploration of the dynamics of tax policies and transfer pricing practices that are not only viewed from technical and regulatory aspects but also from ethical and philosophical perspectives. We got first-hand information from semi-structured interviews with three main groups of stakeholders: tax authorities, tax consultants, and managers of multinational companies that were involved in the transfer pricing process. Informants were selected based on purposive sampling, a sample selection technique that considers the relevance and experience of informants to the research topic. People who gave information included people who worked for the Directorate General of Taxes (DJP) and were in charge of overseeing transfer pricing, tax consultants who had dealt with transfer pricing cases before, and financial managers from multinational companies who were interested in how transfer pricing policies and practices were used in Indonesia.

This study also uses secondary data, such as Indonesian tax rules 22/PMK.03/2020 on transfer pricing documentation and Advance Pricing Agreement, 172/PMK.03/2023, OECD guidelines on the arm's length principle, and different studies from journals that are indexed by Scopus and Web of Science. The data obtained were analyzed using thematic analysis techniques, with the following steps: The process involved (1) initial coding to identify patterns in informant answers, (2) categorizing data based on Pancasila principles related to transfer pricing practices, and (3) drawing conclusions by comparing empirical findings with relevant theories. To improve the accuracy and sharpness of the analysis, this study uses NVivo 12 software, which assists in the coding process and visualization of relationships between themes that emerge from interviews.

Through this methodology, the research aims to formulate a transfer pricing model that is oriented towards tax compliance and based on Pancasila ethical values to support economic sustainability. Theoretically, this study adds to the body of knowledge by looking at transfer pricing from a different angle: how Pancasila ethics can be incorporated into tax laws. This study indicates that an approach based on local cultural values can be an alternative in overcoming transfer pricing manipulation in developing countries.

4. Result and Discussion

Transfer pricing refers to the pricing of transactions between affiliated entities, which, according to the OECD [3] can be misused by multinational enterprises to shift profits to low- or no-tax jurisdictions, thereby reducing tax revenues in source countries, especially in developing nations [20, 21]. In practice, these firms often set unfair prices for goods, services, royalties, or other costs to minimize reported profits in higher-tax countries—including those rich in labor and natural resources—leading to significant revenue losses, economic inequality, and weakened development capacity in developing countries [20, 25, 42].

Tax avoidance through transfer pricing is detrimental to developing countries, so that their tax revenues continue to decline, such as in Indonesia, which relies on tax as its main source of income [43]. Several studies have shown that developing countries experience significant tax losses due to transfer pricing manipulation, losing around USD 240 billion per year [3]. This kind of practice strengthens developing countries' dependence on debt and international aid, which can worsen long-term economic instability. The following are the results of interviews with multinational taxpayers:

> "…as a multinational company, we face pressure to maximize shareholder returns, including through tax management strategies. We acknowledge that we sometimes adjust transfer pricing to reduce tax burdens and shift profits to countries with lower tax rates. However, the company strives to follow established tax regulations to support responsibility to the country through transparent reporting…(DA)"

Here is an interview with another company employee:

> "… when setting the purchase price of raw materials from overseas affiliates, we consider various factors, including production costs, reasonable profit margins, and prevailing market prices. However, in some cases, the parent

> company provides specific instructions regarding the purchase price that we must comply with. Meanwhile, when setting the selling price for other affiliates, we usually conduct an analysis based on a comparison with market prices and benchmarking against similar companies. However, the parent company asked to keep the selling price in line with their global tax strategy, which sometimes makes it difficult for us to balance compliance with business interests…" (LI)

The following are opinions from tax consultants who help handle multinational company tax reporting and transfer pricing documents:

> "In carrying out our role as tax consultants, we always prioritize the principle of compliance with applicable regulations, including transfer pricing policies. We strive to ensure that our clients understand the importance of implementing transfer pricing according to the arm's length principle and are not involved in manipulation that can harm the country. As consultants, we also have an ethical responsibility to support transparency and honesty in tax practices, strengthening the company's reputation in the eyes of the public and government..." (WA)

The results of the interview with tax consultant EK are as follows:

> "… the limited understanding of transfer pricing is still quite large among multinational companies, especially in understanding the applicable regulations and their tax implications. Many companies still consider transfer pricing as merely an internal policy without understanding that Indonesian tax regulations require transparency and fairness of prices in affiliate transactions. This causes companies to often face tax corrections due to a lack of adequate documentation.…" (EK).

Transfer pricing guidelines were developed by the Organisation for Economic Co-operation and Development to promote fair tax practices among multinational enterprises. The OECD has supported multilateral agreements and encouraged countries to cooperate on tax issues to ensure a more uniform approach to transfer pricing and reduce the amount of double taxation that occurs [44]. Through the Base Erosion and Profit Shifting (BEPS) Action Plan, the OECD has tried to stop tax avoidance that isn't legal and make things more clear. However, the application of transfer pricing rules varies and remains inconsistent across different regions. Implementing these rules is still problematic because each country has different national interests, tax policies, and enforcement powers, making it difficult to apply consistent rules to profit shifting. Another problem is the various interpretations of fairness and reasonableness analysis standards, comparative complexity, and difficulties in determining the value of intangible assets [44]. MNEs are proactive in their home countries, but they do little to take sustainable action in the countries where they set up business, such as sourcing labor below wage levels and encouraging poor working conditions, taking advantage of lax social standards and environmental regulations, and engaging in aggressive tax avoidance activities [45].

4.1. Integration of Pancasila Ethics in Transfer Pricing Practices

Pancasila, as the basic ideology of the Indonesian state, contains ethical values that underlie economic governance [46]. The Pancasila principles give transfer pricing and tax manipulation a moral and ethical foundation. This is because Pancasila has values that aim to ensure social justice, unity, and prosperity for all Indonesians [46]. The principles of Pancasila provide a moral and ethical basis for transfer pricing and tax manipulation. Pancasila encourages the creation of a fair economic system, benefiting some parties and paying attention to the interests of society at large. The concepts of "cooperation" and "social justice" are important principles in ensuring that the country's wealth and resources are distributed fairly, creating a sustainable economic system [47]. This way of thinking about taxes is the same as the Pancasila philosophy. In Indonesia, tax collection must be able to show how the role of a way of life for society and the state requires that taxes be obeyed together in their real form, which is in the form of law [48]. So, people who pay their taxes must follow Pancasila's values, which are to be religious, humanistic, uniting, mutually cooperative, and working toward social justice [49].

By incorporating Pancasila values into economic policies like taxation and transfer pricing rules, bad business practices that hurt the country should be stopped. One example is when multinational companies use unfair transfer pricing to avoid paying taxes. Therefore, enforcing ethical transfer pricing regulations that are in line with Pancasila values will strengthen the tax system and support economic sustainability. The tax authorities in Indonesia are implementing regulations that aim to regulate transfer prices and provide guidelines for companies to determine fair prices in transactions between affiliated companies. These guidelines must be based on transparency and honesty in tax document reporting, also known as transfer pricing documentation, or TP Doc. Taxpayers who do business with multinational companies through affiliates must obey the rules in the TP Doc about using fair prices. These rules must be in line with other tax laws. To test tax compliance in the implementation of ALP, the tax authorities are required to supervise, inspect, and handle transfer pricing disputes. However, unfair transfer pricing practices still happen because of several issues, including people not understanding the rules, weak supervision and law enforcement, and the lack of up-to-date transfer pricing rules that are in line with how businesses work and change with new technology. Sukarno [38] highlights the ongoing need to address the issue of limited access to comparative data for both taxpayers and tax authorities. The following are the results of interviews with tax authorities:

> "… the unfairness occurs because multinational companies often have the resources and access to international tax consultants who help them design transfer pricing strategies that aggressively benefit them. Meanwhile, domestic companies do not have the same opportunities to do tax planning like this. As a result, domestic companies must pay full taxes, while multinational companies can reduce their taxes through certain schemes. In addition, tax avoidance

through transfer pricing also reduces state revenues that should be used for infrastructure development, education, and public health. This has a direct impact on public welfare…" (YG).

"As a tax authority, we see the synergy of Pancasila ethical principles and fair tax practices as an important foundation in ensuring optimal state revenues to support national development. Pancasila values, such as social justice and responsibility, provide moral guidance in our policies and supervision. We continue to strengthen transfer pricing regulations, such as requiring transparent transfer pricing documentation and expanding international cooperation to identify tax manipulation. We also encourage multinational companies to understand that paying taxes fairly is a real contribution to social justice and community welfare..." (DW).

4.2. Pancasila Ethics and Fair Transfer Pricing in Supporting Sustainable Tax Compliance

Tax compliance is a key component of a nation's economic sustainability. Through tax contributions, companies play a vital role in supporting public welfare. However, tax avoidance practices, particularly in transfer pricing, threaten this sustainability. Taxes contribute positively to society only when they are managed effectively for public benefit [50]. Tax payments uphold the social contract by funding infrastructure and preserving the justice system that underpins freedom and market stability [2]. In the Indonesian context, integrating Pancasila ethics into tax practices offers a strategic approach to promote legal compliance and enhance moral awareness among taxpayers. Pancasila values such as honesty, justice, and social responsibility encourage individuals and corporations to view taxes not merely as obligations but as real contributions to national development. By embedding these values into the tax system, paying taxes becomes a form of moral responsibility and a manifestation of national solidarity. As the philosophical and ethical foundation of Indonesia [51] Pancasila provides an ideal basis for rethinking tax compliance, aligning it with national identity and civic duty. Barus [48] emphasizes that Indonesia must frame tax compliance as a vital practice both for society and the government.

The misuse of transfer pricing—where profits are artificially shifted to low-tax jurisdictions—can significantly reduce national tax revenue. Integrating Pancasila ethics into transfer pricing policies can address these challenges. Values of cooperation and social justice embedded in Pancasila must be reflected in fiscal regulations, including in setting intercompany prices among multinationals. Applying the principle of social justice means that transfer prices must reflect arm's-length market values and must not be exploited to shift profits unfairly. This ethical framework fosters a more transparent and equitable tax environment, thereby increasing tax compliance and system integrity [3].

Each of the five Pancasila principles offers guidance for fair transfer pricing. The first principle, belief in the Almighty God, mandates that business practices, including taxation, must be grounded in moral and spiritual values. Transfer pricing, therefore, should not merely aim at minimizing tax liability but must also consider social responsibility. The second principle, Just and Civilized Humanity, upholds the economic rights of all parties and encourages transfer pricing practices that support national development. Unfair transfer pricing—which often results in base erosion—harms national revenue and hampers socio-economic progress [18].

The third principle, Unity of Indonesia, emphasizes national solidarity. This calls for close collaboration between the government and the private sector to develop and implement fair transfer pricing policies. Such cooperation ensures long-term economic resilience and minimizes exploitative practices. The fourth principle, Democracy Led by Fischer [52] supports participatory policy-making. Inclusive dialogue involving businesses, policymakers, and civil society will ensure that regulations serve the common good, not just particular interests. Finally, the fifth principle, Social Justice for All Indonesians, emphasizes equitable economic distribution. Fair transfer pricing in this context ensures that the economic value generated within Indonesia remains in the country and contributes meaningfully to development.

Applying these principles will foster a culture of fairness and accountability in taxation. Companies are encouraged to prioritize not only profit but also their broader contribution to society. When transfer pricing reflects ethical considerations, it ensures that businesses fulfill their tax obligations in a way that supports education, health care, and infrastructure—core elements of public welfare. To operationalize this ethical approach, awareness must be raised regarding the importance of fair contribution, as mandated by social justice. Moreover, dialogue among companies, regulators, and the public can result in more effective tax policies aimed at reducing avoidance. The principle of mutual cooperation should also guide corporate behavior, encouraging businesses to collaborate with the government in building an equitable economy. In this sense, cooperation involves more than legal compliance—it includes a shared commitment to national welfare through transparent and just tax practices.

Ultimately, Pancasila ethics can guide companies to balance their pursuit of profit with the nation's long-term sustainability. By embedding ethical considerations into transfer pricing strategies, Indonesia can reduce tax evasion risks, improve public trust, and create a tax system that promotes justice and economic inclusivity [7, 46].

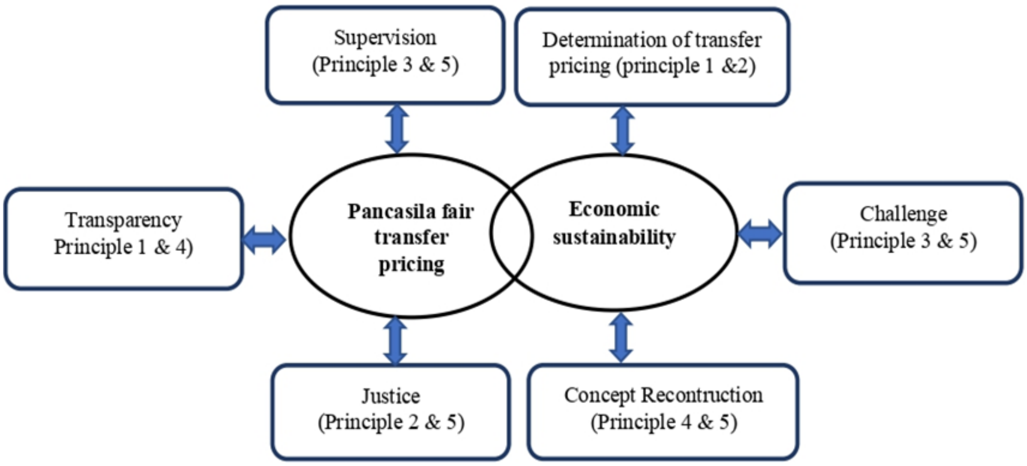

Figure 1.
Integration of Pancasila-based transfer pricing practices and economic sustainability.

Figure 1 illustrates the integration of Pancasila principles in fair transfer pricing practices to support economic sustainability. "Pancasila Fair Transfer Pricing" is at the center of the diagram as the main framework that connects various important elements, such as transparency, fairness, supervision, transfer pricing, challenges, and conceptual reconstruction. This approach aims to ensure that transfer pricing practices by multinational companies not only comply with regulations but are also in line with the moral and ethical values contained in Pancasila. This practice supports fair tax contributions to fund national development, which is critical for the stability and sustainability of the country's economy.

Each element in the diagram is associated with the principles of Pancasila. Transparency (Principles 1 & 4) underlines the importance of honest and accountable financial reporting, reflecting integrity and democratic participation in the tax system. Justice (Principles 2 & 5) affirms the fair distribution of economic benefits to support social welfare. Supervision (Principles 3 and 5) shows how important it is for tax authorities to make sure that rules are followed and that transfer pricing practices are not manipulated. On the other hand, Transfer Pricing (Principles 1 & 2) stresses the importance of being fair and honest when setting transfer prices, in line with business practices and ethical standards [3]. Lastly, the Concept Reconstruction part (Principles 4 and 5) calls for a new way of thinking about policy that is in line with international standards. The goal is to make sure that transfer pricing rules stay useful and flexible as the world faces new problems. It also links transfer pricing practices with corporate social responsibility, ensuring that tax contributions reflect a commitment to social justice and national development. The first, second, and fifth principles of Pancasila serve as an essential ethical foundation for regulating transfer pricing and promoting social justice, particularly in light of structural weaknesses in current regulations and law enforcement, as these principles emphasize the values of divinity, humanity, and social justice, which can encourage ethical, transparent, and socially responsible transfer pricing practices in addressing inequality stemming from regulatory and oversight gaps. By incorporating Pancasila values into transfer pricing practices, this framework helps keep the tax system honest and promotes economic growth for everyone. This approach creates synergies between business sustainability and national welfare.

4.3. Economic Sustainability through Fair Transfer Pricing Practices

The sustainability of a country's economy depends on stable and fair tax revenues. Sustainability and fairness are interrelated issues in the tax system because achieving tax fairness will increase the degree of sustainability in the tax system and the economic sustainability of a country [53]. A just and equitable tax structure not only supports the government in generating reliable revenue but also promotes social trust and economic stability over time. Fairness in taxation ensures that taxpayers, including multinational companies, contribute proportionally to the economies in which they operate.

Business ethics are needed to maintain sustainability in a business system so that if ethics in international cooperation are not implemented, it can damage relations between countries [46]. The absence of ethical considerations in cross-border transactions can lead to conflicts, unfair competition, and a breakdown of trust between nations. Sustainability, business ethics, and corporate social responsibility (CSR) are all important parts of doing business internationally. These three elements are interconnected and function collectively to ensure that companies act responsibly, operate sustainably, and provide benefits to both society and the environment [54]. Ethical practices help align corporate strategies with global sustainability goals while respecting the legal and cultural frameworks of host countries.

Public financial sustainability also relies on several key components, such as fiscal responsibility, long-term planning, balanced budgets, social inclusion and equity, green investment, debt management, resilience to economic shocks, transparency and accountability, revenue diversification, technology and innovation, and continued economic growth and development [55]. A government’s ability to manage its finances wisely ensures the availability of public goods and services, economic stability, and the fulfillment of its social contract with citizens.

Pancasila business ethics incorporates the organization’s values and principles into its operations so that companies can run in a responsible, fair, and culturally appropriate way [56]. These ethics help companies not only survive but thrive in a manner that respects Indonesian cultural and moral foundations. Integrating Pancasila ethics into transfer pricing policies will increase state revenues and create a fairer and more sustainable business ecosystem. The value of justice in Pancasila, in particular, can serve as the foundation for policies that ensure companies pay taxes according to their real economic activities in Indonesia.

Taxes play a crucial role in implementing the Pancasila values. One of the key goals is to achieve social justice for all Indonesians, as enshrined in the fifth principle. Taxes are a practical tool for realizing not only this principle but also the noble values embedded in all Pancasila principles. The principle of social justice, when applied to corporate taxation, can reduce the gap between company profits and their contributions to national development [57]. This aligns corporate behavior with national interests and societal needs. In a fair tax system, fair transfer pricing plays a strategic role in ensuring that multinational companies pay taxes in accordance with their economic contribution to the countries where they operate. Table 1 illustrates six interrelated key aspects that facilitate the realization of fair transfer pricing and contribute to a country's economic sustainability. One of the most important aspects is fair tax revenue, which ensures that companies pay taxes based on the fair market value of their affiliated transactions. When tax revenues are proportionally received, governments can allocate them to infrastructure, health, and education, ultimately improving public welfare [3].

Table 1.
Fair Transfer Pricing and Economic Sustainability.

Aspect	Explanation	Impact on Economic Sustainability
Fair Tax Revenue	Fair transfer pricing requires companies to pay taxes in accordance with fair market value, according to the income earned from activities in Indonesia.	The stability of state tax revenues is a major source of income for infrastructure development, education, health, and social welfare.
Tax Avoidance and Profit Shifting	Manipulating transfer prices to shift profits to countries with lower tax rates reduces tax revenues in the countries where the company operates.	Tax avoidance practices harm a country's economy by reducing funds available for socio-economic development and exacerbating economic inequality.
Tax Transparency and Compliance	Transparent and fair transfer pricing practices increase voluntary tax compliance from companies because taxes are considered a fair obligation and commensurate with the benefits received by the company and the country.	Increasing tax compliance helps increase state revenue and reduces the burden of supervision by tax authorities. Public trust in the tax system increases.
Social Justice	The principle of social justice in Pancasila requires companies to pay taxes according to the income earned, not based on countries with low tax rates.	The goal is to reduce social and economic inequality. By minimizing tax evasion, countries have more funds to allocate to sectors that reduce inequality.
Mutual Cooperation and Collaboration	There is a collaboration between the government and the private sector in formulating fair transfer pricing policies based on the principles of Pancasila.	Creating a sustainable system by involving various parties in decision-making. This synergy strengthens economic stability and increases investment.
Economic Sovereignty	The implementation of fair transfer pricing supports the economic sovereignty of countries by ensuring that companies do not avoid their tax obligations through manipulative transfer pricing structures.	With maintained economic sovereignty, Indonesia can maintain control over its economic resources and utilize tax revenues for more equitable and sustainable development.
Long Term Investment	Fair transfer pricing practices can create a more stable investment climate because investors will be more attracted to countries with transparent and fair tax systems.	Increasing the flow of foreign investment that funds infrastructure projects and other strategic sectors, supporting sustainable long-term economic growth.

However, the implementation of a fair tax system still faces significant challenges, particularly in the form of profit shifting and tax avoidance. Multinational companies often shift profits to low-tax jurisdictions to reduce their tax liabilities, which undermines state revenues and exacerbates economic inequality [2]. To address this issue, tax transparency and compliance are crucial to reinforcing the national tax system. Transparency in reporting transfer pricing transactions enables tax authorities to detect manipulative practices. Strengthened oversight and international cooperation through information exchange reduce the space for aggressive tax avoidance. The principle of social justice in Pancasila also underlines the need for equitable tax distribution. When multinational companies avoid taxes, the burden often shifts to MSMEs and individual workers who lack access to complex tax planning [48]. This further deepens social and economic inequality. Stricter regulations in transfer pricing ensure companies contribute fairly based on their actual economic activities. The Starbucks case in the UK illustrates this point: despite global profitability, the company reported losses domestically to reduce taxes. Public and regulatory pressure eventually led Starbucks to pay more taxes, confirming that strong, transparent policies can improve tax justice [21].

Moreover, fair tax revenue is closely linked to economic sovereignty. When companies pay taxes proportionally, states can fund development, invest in infrastructure, and reduce dependence on foreign debt [25]. Conversely, continued tax avoidance weakens national fiscal capacity and increases reliance on external loans [1]. Therefore, collaboration between government and the private sector is essential. Through transparent transfer pricing guidelines, enhanced oversight, and compliance incentives, tax systems can be more effective and equitable [3].

Ultimately, implementing fairer transfer pricing strengthens economic sovereignty and supports social justice. Table 1 shows that improved transparency fosters compliance and revenue, realizing the Pancasila principles and positioning tax not only as a fiscal tool but also as a driver of equality and sustainable development. Fair transfer pricing practices can significantly enhance state tax revenues by ensuring that multinational companies pay taxes commensurate with the income they generate in Indonesia. Transparent and fair transfer pricing also fosters public trust in the tax system, which is essential for voluntary compliance and encouraging greater private sector contributions to national development. Table 1 illustrates six interrelated key aspects that facilitate the realization of fair transfer pricing and contribute to a country's economic sustainability. Applying Pancasila principles to transfer pricing governance can therefore strengthen Indonesia's tax system and economic resilience.

Globally, the shift toward sustainable economic practices opens new opportunities. Transfer pricing, if aligned with sustainability goals, can reward companies that contribute to environmental protection and penalize those externalizing environmental costs [45]. By incorporating sustainable goals into core business operations, companies not only contribute to the UN SDGs but also bring positive social and environmental change, especially in developing countries where they operate. The principle of economic justice must underpin profit allocation, aligning with the fairness principle that reflects true value creation [45].

Aggressive transfer pricing undermines development by reducing tax revenues and limiting government capacity to invest in education, health, and infrastructure [58]. In contrast, companies that fulfill tax obligations ethically support long-term economic sustainability. Therefore, integrating the ethical foundations of Pancasila with transfer pricing policy is crucial. Several policy steps can help operationalize this synergy: First, increasing socialization and education; the government should intensify awareness campaigns and educational programs to emphasize the importance of transparent transfer pricing. Enhancing understanding among business actors will reduce manipulation and improve compliance. Second, Strengthening Oversight: Monitoring mechanisms must be reinforced to prevent practices that harm state revenues. The tax authority should be proactive in audits and use data analytics to detect irregularities. Third, Government–Business Collaboration

Applying the 3rd principle of Pancasila, mutual cooperation, the government should engage the private sector in shaping fairer tax policies. Transparent dialogue ensures that policies are practical and fair.

The involvement of taxpayers, tax consultants, and tax authorities is vital. Taxpayers, particularly multinational companies, are expected to demonstrate integrity and transparency in line with Pancasila's 1st principle: Belief in One Almighty God. Their transfer pricing practices must reflect the arm's length principle and avoid manipulation. Ethical compliance is not just a legal responsibility but a moral one. Tax consultants have a strategic role in ensuring that companies comply with regulations ethically. Reflecting the 2nd principle—Just and Civilized Humanity—they must balance corporate interests with the public good and advise clients with integrity, helping to build a transparent tax system. Tax authorities, as enforcers of fiscal policy, must ensure fairness and uphold the 5th principle—Social Justice for All Indonesian People. Their responsibilities include administering taxes equitably and using revenues for the common welfare. They must also educate stakeholders and strengthen supervision to deter abuse.

The synergy of ethical behavior from all three actors will create a taxation system that is fair, sustainable, and grounded in Pancasila. Such a system will enhance state revenues and public trust while supporting long-term national development. To enhance transparency and accountability in transfer pricing practices, the fourth principle of Pancasila—Democracy Led by Wisdom—can be used as the foundation for requiring greater corporate openness in reporting affiliate transactions. This can be achieved by tightening the requirements for Transfer Pricing Documentation (TP Doc), including Local Files, Master Files, and Country-by-Country Reports (CbCR). Furthermore, international cooperation with institutions such as the OECD and G20 must be strengthened to monitor cross-border transactions and detect tax avoidance schemes. The adoption of blockchain technology in the tax system can also provide immutable transaction records, enhancing both trust and accountability [3].

In line with the first principle—Belief in the One Almighty God—companies should be encouraged to cultivate moral awareness and voluntary compliance. This can be realized through the integration of ethics education for executives and tax professionals, as well as the implementation of tax-based Corporate Social Responsibility (CSR), where paying taxes is recognized as a direct contribution to national development. Providing incentives to companies that consistently demonstrate transparency and voluntary compliance will further promote ethical tax behavior.

To uphold the second principle—Just and Civilized Humanity—the state must reinforce sanctions against unfair transfer pricing practices and ensure equal treatment for all taxpayers. This includes the imposition of progressive fines proportional to the amount of tax avoided, establishing public tax compliance ratings to encourage responsible behavior, and expediting the resolution of disputes through Advance Pricing Agreements (APA) and Mutual Agreement Procedures (MAP), thereby reducing uncertainty in enforcement.

The third principle of Pancasila—Unity of Indonesia through mutual cooperation—can guide the fostering of stronger collaboration between the government and business sectors. Establishing multi-stakeholder tax policy forums involving government institutions, academic experts, and private sector representatives will ensure more balanced and inclusive policy-making. Business associations should also be encouraged to formulate ethical transfer pricing codes based on Pancasila values, and international cooperation—especially through bilateral and multilateral agreements for Automatic Exchange of Information (AEOI)—should be intensified to curb global tax avoidance.

Finally, to realize the fifth principle—Social Justice for All Indonesian People—transfer pricing policies must ensure fair distribution of economic benefits. This involves allocating revenues generated from transfer pricing taxation to sectors that directly improve public welfare, such as infrastructure, education, and health. In addition, the government should implement redistributive tax mechanisms by applying higher rates to corporations that gain significant profits from national resource exploitation while offering incentives to MSMEs that contribute to the people's economy. Oversight must also be strengthened to prevent economic exploitation by multinational companies that shift profits abroad while benefiting from local resources and labor. Embedding the principle of social justice in tax regulation ensures that tax policies support not only corporate interests but also provide tangible benefits to workers, SMEs, and society at large.

In summary, fair transfer pricing aligned with Pancasila can elevate Indonesia's fiscal sustainability, enhance equity, and support inclusive development. Transfer pricing policy must go beyond legal compliance to embody the nation's foundational values. Through collaborative governance, ethical enforcement, and value-based reforms, Indonesia can build a tax system that sustains both its economy and its national identity.

5. Conclusion

This study confirms that non-transparent transfer pricing practices can reduce state tax revenues and exacerbate economic inequality. Integrating Pancasila ethics into transfer pricing policy offers a normative foundation for building a fairer and more sustainable tax system. Principles such as social justice, transparency, and mutual cooperation provide a moral compass for companies to not only comply with tax regulations but also contribute to national development. However, implementation still faces challenges, including regulatory loopholes, low awareness, and weak oversight. To increase policy effectiveness, the government should close legal gaps that enable tax avoidance, enhance transparency through technologies like blockchain, and expand international cooperation in tax information exchange. Ethics education must also be strengthened through curricula and outreach, while incentives should be provided to companies that apply just and transparent transfer pricing practices. A Pancasila-based approach can thus improve compliance, restore public trust, and support inclusive economic growth.

Theoretically, this study enriches the tax literature by highlighting the underexplored link between Pancasila ethics and transfer pricing. Practically, it serves as a guideline for multinational firms to design more socially responsible tax policies. For policymakers, it offers concrete recommendations to strengthen regulation and enforcement, ensuring that transfer pricing aligns not only with OECD standards but also with national values and social welfare goals. Nonetheless, this study has limitations. It adopts a qualitative approach, relying on interviews and conceptual analysis, which limits its ability to quantify the impact of Pancasila values on tax compliance. Future research using quantitative or mixed methods would enhance the findings. Moreover, as this study focuses on Indonesia, generalizability to other contexts may be limited. Comparative studies across countries could offer broader insights. Finally, due to limited empirical data, future case studies from companies applying ethical transfer pricing principles would be valuable for validating and expanding the research outcomes.

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