



EX ANTE AND EX POST APPROACHES IN TRANSFER PRICING DOCUMENTATION: A REVIEW OF PMK 172 OF 2023 AND EXAMINATION PRACTICES BY THE TAX OFFICERS

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Abstract

This article examines the mismatch between ex ante and ex post approaches in the preparation of transfer pricing documentation in Indonesia. While Ministry of Finance Regulation No. 172/2023 clearly mandates the use of the ex ante approach—where documentation is prepared based on information available at or before the time of the transaction—tax auditors often apply the ex post approach during audits by assessing actual outcomes. This inconsistency creates legal uncertainty and may discourage voluntary compliance among taxpayers. Using a normative-qualitative method and literature review, this study explores the issue from the perspective of regulations, audit practices, and international guidelines. A case study is included to illustrate how ex post adjustments can lead to disputes despite compliance with regulatory expectations. The article calls for harmonization between policy and enforcement practices to foster a more consistent, fair, and predictable tax system in Indonesia.

Keywords: Ex ante, Ex post, Legal certainty, Tax audit, TP documentation, Transfer pricing

INTRODUCTION

Transfer pricing has long been an important issue in the world of international taxation. For developing countries such as Indonesia, supervision of affiliated transactions carried out by multinational companies is becoming increasingly crucial, given the potential for profit shifting that can erode the national tax base (Mardiana & Badjuri, 2023). Determining transfer prices in accordance with the *arm's length principle* is the main foundation for maintaining the integrity of the tax system (Challoumis, 2023).

The issue of transfer pricing is not current issue in international taxation discipline (Sihombing et al., 2024). It has become a major highlight, especially in developing countries including Indonesia. At the national level, data from the Directorate General of Taxes (2023) shows the handling of *mutual agreement procedure* (MAP) cases. The balance of cases as of January 1, 2023 was 42. Furthermore, the submission of cases up to December 31, 2023 was 25. Furthermore, the number of cases resolved up to December 31, 2023 was 21. Some of the MAP cases were related to transfer pricing.

Transfer pricing documentation has a strategic role in this context. Transfer pricing documentation is an instrument regulated in laws and regulations to justify whether related - party transactions carried out by taxpayers have met arm's length principles (Irfan et al., 2021). However, the reality in the field shows a difference between the approach regulated in the regulations and the audit practices carried out by the tax authorities. PMK 172 of 2023 explicitly requires the preparation of documentation based on the ex ante approach, namely based on data and information available before or at the time the transaction is carried out. On the other hand, in audit practice, the tax authorities tend to assess the fairness of transactions using the ex post approach, which is based on the actual results that occur after the transaction.

The gap between what transfer pricing regulations require and how tax audits are actually carried out creates more than just technical challenges—it also leaves taxpayers uncertain about where they truly stand. When the rules say one thing but audits apply another, it becomes harder for businesses to plan with confidence or feel secure that their compliance efforts will be recognized. This lack of clarity can weaken trust in the tax system itself. This



study explores that disconnect, asking why it happens and what it means for both taxpayers and tax authorities. Through this analysis, it aims to offer practical insights that can help bring regulations and audit practices into closer alignment, so that the rules are not only clear on paper but also consistently applied in the real world.

LITERATURE REVIEW

Tax compliance constitutes a fundamental pillar of any effective tax system, as it reflects the degree to which taxpayers fulfill their fiscal responsibilities either voluntarily or as a result of enforcement measures instituted by tax authorities (James & Alley, 2002). Within the specific domain of transfer pricing, compliance transcends mere administrative functions such as the submission of reports and documentation. Rather, it encompasses a broader behavioral dimension—namely, how the consistency, clarity, and perceived fairness of both regulatory frameworks and their implementation in practice influence taxpayer attitudes, risk perceptions, and decision-making processes. As such, transfer pricing compliance cannot be fully understood without examining the dynamic interplay between formal rules and the manner in which they are enforced on the ground.

To better understand what drives taxpayers to comply, the 'slippery slope framework' developed by Kirchler and colleagues (Muehlbacher et al., 2011) offers a helpful perspective. The idea is simple but powerful: people are more likely to comply with tax rules when they trust the authorities and also recognize their ability to enforce the law. It's about finding the right balance between credibility and fairness. But when tax authorities use an approach that doesn't align with what the rules say—such as relying on ex post audits even though the taxpayer has followed the ex ante documentation requirements—this balance can be thrown off. Trust begins to erode, and compliance may no longer come from a sense of responsibility, but rather from fear of being penalized. In the long run, this kind of forced compliance is harder to sustain and can weaken the overall effectiveness of the tax system.

The Theory of Planned Behavior also offers insight into how inconsistencies in tax policy and enforcement can affect taxpayer behavior. This theory suggests that people are more likely to comply when they feel confident in their ability to predict outcomes and manage risks. But when taxpayers follow the rules and still face uncertainty—perhaps because audits apply different standards than the regulations—they may start to feel that their efforts don't matter. This loss of control over the process can weaken their willingness to comply voluntarily. Instead of being driven by trust or a sense of responsibility, their behavior may shift toward caution or even avoidance, especially if they begin to see the system as unpredictable or unfair (Taing & Chang, 2020).

The theory of economic deterrence also helps explain taxpayer behavior by focusing on cost-benefit thinking. In this view, people tend to comply with tax rules when the benefits—like certainty, reduced risk, and peace of mind—clearly outweigh the potential costs. But if taxpayers who have followed the rules still face the risk of being penalized or having their reports challenged, the value of being compliant starts to fade. The effort and uncertainty involved may no longer seem worth it. When seen alongside the slippery slope framework and the theory of planned behavior, a consistent message emerges: gaps between what the rules say and how they are applied in practice create confusion and discourage honest taxpayers. To strengthen voluntary compliance, authorities need to ensure that policy and enforcement go hand in hand. A system that is clear, fair, and predictable is more likely to build trust and encourage long-term cooperation from taxpayers (Ya'u et al., 2023).



METHODS

This research applies a normative-qualitative approach, using descriptive and analytical methods to explore the topic. The main sources of data include key regulatory documents such as Minister of Finance Regulation No. 172 of 2023 (PMK 172/2023), Directorate General of Taxes Regulation No. PER-22/PJ/2013, Circular Letter No. SE-50/PJ/2013, and the 2022 OECD Transfer Pricing Guidelines. These primary sources are complemented by a range of secondary materials, including academic journal articles, professional reports, and policy papers. The study begins by examining the core differences between the ex ante and ex post approaches to transfer pricing documentation, with a focus on how these differences affect legal certainty and taxpayer compliance. To bring the issue closer to practice, a simple case study is included to show how inconsistencies between the rules and their application can lead to real challenges for taxpayers in the field.

RESULTS AND DISCUSSION

The ideas of ex ante and ex post are clearly discussed in the 2022 edition of the OECD Transfer Pricing Guidelines. These concepts help guide how tax authorities and taxpayers assess whether related-party transactions follow the arm's length principle. One important reference appears in Paragraph 3.69, which highlights that transfer pricing should be evaluated based on information that was reasonably available at the time the transaction took place. This reflects the OECD's emphasis on an ex ante perspective—focusing on what the parties knew or could have known at the time—rather than judging transactions only by their outcomes after the fact.

First, Paragraph 3.69.

In some cases, taxpayers establish transfer pricing documentation to demonstrate that they have made reasonable efforts to comply with the arm's length principle at the time their intra-group transactions were undertaken, ie on an ex ante basis (hereinafter “the arm's length price-setting” approach), based on information that was reasonably available to them at that point. Such information includes not only information on comparable transactions from previous years, but also information on economic and market changes that may have occurred between those previous years and the year of the controlled transaction. In effect, independent parties in comparable circumstances would not base their pricing decisions on historical data alone.

Second, Paragraph 3.70.

In other instances, taxpayers might test the actual outcome of their controlled transactions to demonstrate that the conditions of these transactions were consistent with the arm's length principle, i.e. on an ex post basis (hereinafter “the arm's length outcome-testing” approach). Such a test typically takes place as part of the process for establishing the tax return at year-end.

Third, Paragraph 3.71.

Both the arm's length price-setting and the arm's length outcome-testing approaches, as well as combinations of these two approaches, are found among OECD member countries. The issue of double taxation may arise where a controlled transaction takes place between two associated enterprises where different approaches have been applied and lead to different outcomes, for example because of a discrepancy between market expectations taken into account in the arm's length price-setting approach and actual outcomes observed in the arm's length outcome-testing approach. See paragraphs 4.38 and 4.39. Competent authorities are encouraged to use their best efforts to resolve any double taxation issues that may arise from different approaches adopted by jurisdictions to year-end adjustments and that may be submitted to them under a mutual agreement procedure (Article 25 of the OECD Model Tax Convention).



See paragraphs 4.38 and 4.39. Competent authorities *are* encouraged to seek the best possible resolution of double taxation issues arising from differences in the approaches adopted by jurisdictions to year-end adjustments, in particular where such issues are submitted through the mutual agreement procedure *as* provided for in Article 25 of the OECD Model Tax Convention.

Fourth, Paragraph 6.194.

The first exemption means that, although the ex post evidence about financial outcomes provides relevant information for tax administrations to consider the appropriateness of the ex ante pricing arrangements, in circumstances where the taxpayer can satisfactorily demonstrate what was foreseeable at the time of the transaction and reflected in the pricing assumptions, and that the developments leading to the difference between projections and outcomes arose from unforeseeable events, tax administrations will not be entitled to make adjustments to the ex ante pricing arrangements based on ex post outcomes. For example, if the evidence of financial outcomes shows that sales of products exploiting the transferred intangible reached 1 000 a year, but the ex ante pricing arrangements were based on projections that considered sales reaching a maximum of only 100 a year, then the tax administration should consider the reasons for sales reaching such higher volumes. If the higher volumes were due to, for example, an exponentially higher demand for the products incorporating the intangible caused by a natural disaster or some other unexpected event that was clearly unforeseeable at the time of the transaction or appropriately given a very low probability of occurrence, then the ex ante pricing should be recognized as being at arm's length, unless there is evidence other than the ex post financial outcomes indicating that price setting did not take place on an arm's length basis.

The OECD Transfer Pricing Guidelines acknowledge that both the ex ante and ex post approaches have their place in assessing whether related-party transactions follow the arm's length principle. The ex ante approach, as explained in Paragraph 3.69, encourages taxpayers to base their pricing decisions on information reasonably available at the time of the transaction—including market trends and economic expectations. This forward-looking approach reflects how independent parties typically operate in real business settings.

On the other hand, Paragraph 3.70 describes the ex post approach, which involves checking whether the results of a transaction match what would be expected under arm's length conditions. This is usually done at the end of the year when preparing tax returns. While both approaches are used by tax authorities in different countries (Paragraph 3.71), they can sometimes lead to mismatched conclusions. For example, if one country focuses on what was expected at the time of the deal (ex ante), while another evaluates only what actually happened (ex post), the same transaction might be treated differently—causing the risk of double taxation. This is why the OECD encourages tax authorities to resolve such differences through mutual agreement procedures, as outlined in Article 25 of the OECD Model Tax Convention.

Importantly, the OECD also sets clear boundaries to prevent unfair treatment of taxpayers. Paragraph 6.194 reminds tax authorities not to rely solely on ex post outcomes when the original pricing was based on reasonable forecasts and the differences were caused by unforeseeable events. For instance, if a product unexpectedly becomes a huge success due to a natural disaster or another rare event, the original pricing may still be considered reasonable—as long as there's no evidence that it was manipulated. In short, these OECD guidelines highlight the need for balance, consistency, and fairness. By encouraging tax authorities to respect well-prepared documentation and to avoid making retroactive judgments without cause, the Guidelines aim to support a tax environment where compliant taxpayers are protected and trust in the system can grow.

Regulations regarding transfer pricing documentation are regulated in the Regulation of the Minister of Finance Number 172 of 2023 concerning the Application of the Principle of



Fairness and Business Custom in Transactions Influenced by Special Relationships. PMK 172 of 2023 does not explicitly mention *ex ante* or *ex post*. However, if observed implicitly, it is contained in several articles, including the following. First, in Article 17 paragraph (1), namely: "Transfer Pricing Documents as referred to in Article 16 paragraph (2) letters a and b, must be prepared based on data and information available at the time the Affiliate Transaction is carried out". This clause indicates that in preparing transfer pricing documentation for local documents (*local files*) and master documents (*master files*) using the *ex ante approach*.

Second, Article 17 paragraph (2) states: " The Transfer Pricing Determination Document as referred to in Article 16 paragraph (2) letter c must be prepared based on data and information available up to the end of the tax year. This clause indicates that in preparing country *-by-country reports*, it is possible to use an *ex-post approach*.

In practice, tax auditors in Indonesia often use an *ex post* approach—assessing related-party transactions based on their actual outcomes and comparing those results to current market benchmarks or profit margins. This approach is partly supported by Article 12 paragraph (3) of the General Provisions and Tax Procedures (KUP) Law. While it can be useful for detecting possible manipulation or unfair pricing after the fact, applying this method too rigidly can create problems. Many taxpayers have already prepared their transfer pricing documentation in good faith using the *ex ante* approach, based on the information available at the time the transaction took place. If auditors ignore the original business context and rely only on what happened afterward, they risk misunderstanding the taxpayer's intent or commercial rationale. As a result, even compliant taxpayers may face large, unexpected tax adjustments—not because they broke the rules, but because the rules are being applied differently at the audit stage.

Saragi (2024) highlights the growing importance of developing transfer pricing regulations in Indonesia, especially in ensuring that tax practices reflect fairness and align with how businesses typically operate. He stresses that transfer pricing documentation should be prepared contemporaneously—that is, at the time the transaction occurs—to show that the taxpayer is complying with the rules based on what was known at the time. This approach not only reflects good faith but also supports legal certainty. However, if tax authorities place more weight on evaluating outcomes after the fact—using an *ex post* approach—then the efforts made by taxpayers to comply in real time may be overlooked. This can lead to uncertainty and a sense of unfairness, as businesses that followed the rules in good faith may still face unexpected corrections or disputes during audits.

Building on this perspective, Black et al. (2022) explored how fairness is handled in the IRS's use of algorithmic models for tax audits in the United States. Their study highlights the importance of taking individual taxpayer circumstances into account when evaluating fairness in enforcement. They argue that audit models relying heavily on past data and final outcomes—without considering the specific context in which taxpayers made their decisions—can lead to unfair results. Such models risk placing a disproportionate audit burden on certain taxpayers, simply because the system overlooks the bigger picture. Moreover, when these models are not designed with strong principles of vertical fairness—that is, recognizing differences in taxpayers' economic positions—the risk of bias in audit selection and outcomes becomes even greater.

For this reason, it is essential that tax authorities find the right balance between using *ex ante* and *ex post* approaches when conducting audits. While looking at actual outcomes can help identify issues, those results should not be the only factor considered. A fair assessment must also take into account the information and assumptions the taxpayer had access to at the time the business decision was made. This includes recognizing transfer pricing documentation that was prepared in good faith and in accordance with the rules. When audits consider both what was known at the time and what eventually happened, the process becomes more balanced



and just. Such an approach not only promotes fairness and proportionality but also reinforces legal certainty—ensuring that taxpayers are treated consistently and that the tax system remains trustworthy and predictable.

This kind of contradiction can weaken the foundation of voluntary compliance. When taxpayers have taken the time and effort to prepare their transfer pricing documentation properly and in a timely manner—yet still face tax adjustments—they may begin to question the fairness of the system. Over time, this erodes trust in the tax authority and reduces the willingness to comply voluntarily. Instead of feeling that the system rewards transparency and good faith, taxpayers may feel punished despite doing the right thing. On top of that, the cost of compliance rises, as they are forced to revisit and defend past decisions using criteria that were not applicable at the time the transaction took place. This not only leads to unnecessary administrative burdens but also creates frustration and uncertainty that can discourage long-term compliance.

The Need for Harmonization of Audit Regulations and Practices

A clear gap is emerging between what the rules say and how audits are carried out in practice—particularly in the area of transfer pricing. Regulations such as Minister of Finance Regulation No. 172/2023 emphasize the use of the ex ante approach, meaning taxpayers are expected to base their documentation on information available at the time of the transaction. However, in many audits, authorities still rely heavily on ex post evaluations that focus on actual results. This disconnect can leave taxpayers in a difficult position: even if they follow the rules in good faith, they may still face challenges or corrections during an audit. Over time, this creates uncertainty and weakens trust in the system. Harmonizing what the regulations require with how audits are performed is not just a technical fix—it’s essential for building fairness and consistency. When audit practices align with regulatory expectations, it becomes easier for businesses to comply, disputes are reduced, and the overall integrity of the tax system is strengthened.

Illustration

To better understand how inconsistencies between tax rules and audit practices can affect businesses, consider the case of PT XYZ Indonesia, a manufacturing subsidiary of a multinational group. In line with the requirements of Minister of Finance Regulation No. 172/2023, PT XYZ prepared its 2022 transfer pricing documentation in early 2023, at the same time it submitted its annual tax return. Because the documentation had to be based on information available at the time, PT XYZ used benchmarking data from 2021, the most recent year for which complete financial data from comparable companies was accessible. Based on this analysis, the company determined that a 7.5% operating margin was within the arm’s length range, and its actual margin fell comfortably within that threshold.

However, during a tax audit conducted in 2024, the tax authorities took a different view. Rather than relying on the ex ante information that was available at the time of the transaction, they used 2022 data—reflecting post-pandemic market recovery—and found that the updated market margin had risen to 9.8%. As a result, they concluded that PT XYZ’s profit was too low and issued a transfer pricing correction, increasing the company’s taxable income.

What’s striking about this case is that PT XYZ had followed the rules. It prepared its documentation on time, used the best data available, and acted in good faith. Yet, because the auditors judged the transaction based on how things turned out later—not how they looked at the time—the company was penalized. This raises serious questions about fairness and legal certainty, especially when taxpayers are doing their best to comply. Moreover, the audit forced PT XYZ to re-justify its past decisions using data and standards that weren’t even available when the transaction occurred. This added to their compliance burden and created a sense of unpredictability—one that can discourage voluntary compliance in the future.



This example shows how important it is to align audit practices with regulatory expectations. If taxpayers who follow the rules still face corrections based on hindsight, trust in the system will inevitably suffer. A balanced approach that respects both ex ante documentation and actual outcomes is essential to maintaining a fair, consistent, and trustworthy tax environment.

CONCLUSION

The gap between what the regulations say and how audits are conducted in practice poses serious legal risks for taxpayers. When ex ante and ex post approaches are applied inconsistently, it creates uncertainty about what counts as proper compliance. This not only makes it harder for businesses to plan and document their transactions with confidence, but also puts those who try to follow the rules in a vulnerable position. Over time, such inconsistencies can erode trust in the tax system and discourage voluntary compliance. To address this, it is essential that policymakers and tax authorities work toward greater harmony between regulation and enforcement. When the rules and their application are aligned, the transfer pricing system becomes more credible, and the broader goal of fair and predictable taxation can be more effectively realized.

Suggestion

Since this study is primarily conceptual—based on a normative analysis of existing regulations and audit practices in Indonesia—future research would benefit greatly from incorporating a more empirical approach. One way to do this is by collecting firsthand insights through surveys or in-depth interviews with relevant stakeholders, such as corporate taxpayers, tax consultants, and auditors. Hearing directly from those involved in the process would help reveal how the ex ante and ex post approaches are actually applied in practice, and what real-world challenges they encounter on the ground.

In addition, conducting comparative studies with other countries—especially those with more mature and established international tax systems—could provide broader insights. By examining how different jurisdictions apply transfer pricing rules and manage audit consistency, Indonesia can learn valuable lessons to help design policies that are clearer and more aligned with international standards.

Lastly, future research could also look more closely at the link between the audit approach used (ex ante or ex post) and the outcomes of tax disputes. Understanding whether one method leads to more frequent objections or longer resolution times would give policymakers a better sense of which direction to take in improving audit policies. In short, bringing together real-world data, international comparisons, and dispute outcomes can support the development of a more consistent, fair, and practical transfer pricing system in Indonesia.

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