Scrutinizing The Change in Basic Rate Policy of Value-Added Tax in Indonesia

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ABSTRACT
The change in the VAT rate in Indonesia is a government initiative aimed at implementing tax reform. The primary objective of this policy is to increase state revenue and support economic recovery. However, public response to this policy has generally been negative. This study seeks to analyze the policy-making process behind the VAT rate change. Using a qualitative approach, the research employs literature review as its primary data collection technique. The findings suggest that increasing the VAT rate presents an opportunity for the state to optimize its revenue. Additionally, the implementation of an alternative VAT value scheme has the potential to reduce distortions caused by the provision of inappropriate VAT facilities.
Keywords: Value added tax, policy formulation.

INTRODUCTION

Value Added Tax (VAT) is the second largest contributor to tax revenue after Income Tax (PPh), contributing around 30% of total tax revenue. Historically, the VAT rate in Indonesia has undergone several significant changes. At the beginning of the implementation of the Sales Tax (PPn) system in 1950, the general rate was set at 10%. Then, in 1974, the rate was divided into three categories: 0% for tax-free goods, 5% for certain goods such as paper and cardboard, and 10% for other goods.

Table 1 Realization of State Revenue from Taxes 2021-2023

Source of Receipt	State Revenue Realization (Billion Rupiah)		
	2021	**2022**	**2023**
Income tax	696.676,60	998.213,80	1.040.798,40
Value Added Tax and Sales Tax on Luxury Goods	**551.900,50**	**687.609,50**	**742.264,50**
Land and Building Tax	18.924,80	23.264,70	25.462,70
Land and Building Acquisition Duty	-	-	-
Excise	195.517,80	226.880,80	227.210,00
Other Taxes	11.126,00	7.686,10	9.714,40
International Trade Taxes	73.695,40	90.897,60	72.898,00

Source: Central Bureau of Statistics

In 1983, Law No. 8 of 1983 introduced a VAT system with a flat rate of 10%, which lasted until March 2021. From 1 April 2022, this rate increases to 11% in accordance with the Harmonization of Tax Regulations Act (HPP Act). Based on Article 7 paragraph (2) of Chapter 4 of the HPP Law, this rate is planned to increase again to 12% in 2025. VAT is an indirect tax imposed on the consumption of goods and services regardless of their type. The main characteristics of VAT include its general, indirect, consumption-based, and multi-stage and non-cumulative nature. This tax is applied at each stage of production and distribution only on its added value.

However, the plan to increase the VAT rate has caused debate. Some are concerned about its impact on people's purchasing power and potential inflation, which could slow economic growth and increase unemployment. On the other hand, the government views this increase as an effort to increase state revenue, reduce dependence on debt, and align with international standards. According to the government,

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this tariff increase could generate additional revenue of up to IDR 75 trillion. Various studies support and criticize this move. A study by Ormaechae & Morozumi (2021) highlights the adverse impact of the multitariff system on the economy. Meanwhile, Putri (2024) notes that while a tariff increase can broaden the tax base, its negative effects such as a decrease in purchasing power should be anticipated by diversifying tax sources, such as carbon taxes. Another study, by Novianto et al. (2023), emphasized the importance of implementing VAT based on the principle of fairness, especially amid the post-pandemic economic situation. Agasi & Zubaedah (2022) assessed the VAT rate increase policy as a step to support economic recovery by prioritizing national interests.

The application of this new rate is also regulated in more detail in the Minister of Finance Regulation (PMK) Number 131 of 2024. This PMK explains the 12% tariff mechanism, including the application of the 11/12 coefficient as the tax imposition base (DPP) for almost all taxable goods and services. In addition, this regulation provides a one-month transition period for businesses to adjust their tax administration. While the government is optimistic about the positive impact of the VAT rate increase, public concerns regarding the socio-economic impact demand that this policy be evaluated and implemented judiciously to ensure its sustainability.

Hypotheses Development

Tax is one of the main sources of income in Indonesia in addition to oil and natural gas sources which play a very important role in the survival of the Indonesian nation. Tax from an economic perspective is understood as the transfer of resources from the private sector to the public sector. Meanwhile, the understanding of tax from a legal perspective is an obligation that arises because of the existence of a law that causes the obligation of citizens to deposit a certain amount of income to the state, the state has the power to force and the tax money must be used for government administration. From this legal approach, it shows that taxes as tax collectors and taxpayers as taxpayers.

Value Added Tax (VAT) is a tax that directly affects the Indonesian people, because Value Added Tax directly concerns the production of goods and services used by the people, regardless of rich or poor. Thus, people are very sensitive to Value Added Tax. To be able to understand the meaning of VAT, we first need to know the meaning of Value Added Tax, Judisseno (2004: 128), states the definition of Value Added Tax is the amount between the costs incurred and the expected profit level in a production process.

Input Tax paid by Taxable Entrepreneurs is actually on the tax invoice that he receives from the seller. And when the Taxable Entrepreneur sells the goods, he collects Value Added Tax from the buyer of 10% of the price of the goods. Before Taxable Goods and Taxable Services are consumed at the consumer level, VAT has been collected at each link in the production chain and distribution chain. Collection at each level does not cause a double effect because of the tax credit age. Therefore, the tax burden by consumers remains the same, regardless of the length or shortness of the distribution chain. Based on the background above, the main problem of this research is How is the Implementation of Value Added Tax on Goods and Services at PT. Acacia IT Service Indonesia?

METHOD

This study uses the post-positivism paradigm with a main focus on descriptive research, which aims to describe a review of the VAT rate change policy in Indonesia. The data collection method is done by using research gap, documentation study and literature study. Therefore, this study is conducted by collecting various literature sources in the form of books, journals, documents, articles, and other types of sources that will be used as references to analyze the data that has been collected.

RESULTS AND DISCUSSION

Pros and Cons of VAT Rate Increase

Taxes play an important role in a country, including in Indonesia, as tax revenue contributes most significantly to the country's income. In Indonesia, the source of tax revenue comes from Income Tax, VAT and STLG, Land and Building Tax (PBB), and other taxes. VAT revenue is the second largest contributor to total national tax revenue.

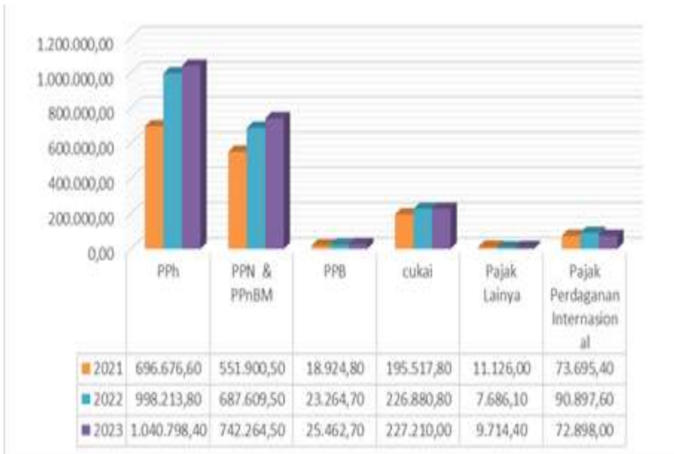

Figure 1. Tax Revenue Realisation
(Source: Processed Company Data)

The realization of VAT revenue in Indonesia from 2021 to 2023 has shown consistent growth, highlighting its crucial role in national economic development (BPS, 2023). According to Wijaya and Arsini (2021), VAT revenue remains substantial compared to other taxes, prompting the government to explore new ways to enhance collections, including expanding the taxpayer base, adjusting VAT facilities, and increasing VAT rates (Fajar et al., 2022). Indonesia's VAT Law has undergone four revisions, with the latest in 2021 under the Tax Regulation Harmonization Law (UU HPP), which introduced a VAT rate increase from 10% to 11% in 2022 and a planned rise to 12% in 2025 (UU HPP, 2021). Historically, VAT rates have evolved since the introduction of a sales tax in 1950, reflecting economic adjustments over the decades. The VAT increase aims to bolster government revenue, reduce reliance on foreign debt, and align Indonesia’s tax standards with global benchmarks, where the average VAT rate in OECD countries stands at 15% (Tempo, 2024). While the government underscores the fiscal benefits, critics argue that higher VAT may lead to reduced household spending and business activity, potentially impacting economic stability (Rosdiana, 2024; Ramadhan, 2022). Despite these concerns, Finance Minister Sri Mulyani asserts that Indonesia's VAT rate remains moderate in the global context, even though it exceeds rates in ASEAN nations (Kompas.com, 2024). However, declining consumer confidence and reduced purchasing power pose challenges that the government must address to balance tax revenue goals with economic resilience..

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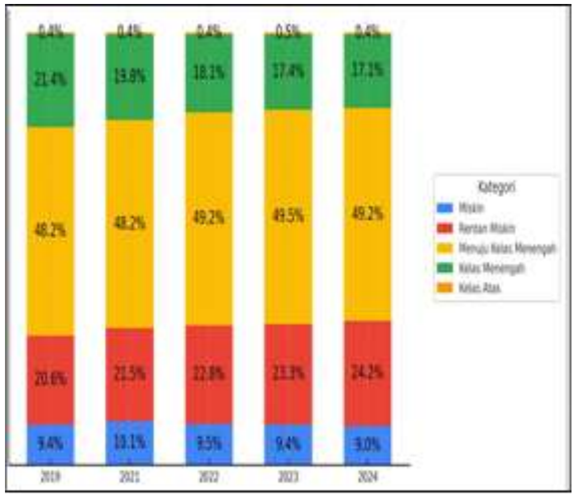

Figure 2. Proportion of the population
(Source: Processed Company Data)

Indonesia's middle-class population has declined, with BPS data indicating a drop from 21.45% in 2019 to 17.13% in 2024, equating to around 9.48 million people. In 2022, food inflation reached 5.8% following the VAT increase from 10% to 11%, and the upcoming rise to 12% is expected to push inflation up by approximately 1.4% per month. Economist Bhima Yudhisthira argues that this VAT hike could lead to higher electricity tariffs, fuel prices, and interest rate adjustments, consequently increasing production costs and limiting consumer purchasing power (Putri, 2024).

According to Junianto and Suharno (2023), inflation in the food sector reduces household consumption, affecting business performance and employment rates (Ardin et al., 2022). Studies suggest a 1% VAT increase could lower household spending by 0.32% to 0.51% and reduce economic growth by 0.02% (Junianto et al., 2023; Gunawan et al., 2022). Rohman (2024) highlights a concerning inflation trend in late 2023, fueling fears about the broader economic impact of the planned 2025 VAT adjustment.

Lower consumer spending would negatively affect businesses by reducing sales, potentially leading to production cuts and job losses. Public protests reflect concerns over these consequences, urging the government to reconsider the policy. In response, Indonesia issued Minister of Finance Regulation No. 131/2024, effective January 1, 2025, detailing VAT mechanisms, including the "alternative value" approach to tax calculation for taxable goods and services, ensuring a smoother transition (PMK 131/2024)..

VAT Policy Conceptualization

The policy formulation process involves recognizing and addressing public concerns to ensure effective solutions (Winarno, 2012). The VAT rate adjustment aims to optimize tax revenues and support economic recovery, yet public resistance stems from fears of price hikes and reduced consumption. Indonesia's VAT system follows a negative list principle, allowing selective exemptions. While this mitigates broad price increases, underlying production costs can still escalate due to VAT-related input expenses (Khawaja & Yassine, 2019). The Indonesian Chamber of Commerce warns that rising VAT rates may reduce sales volumes, leading to business losses (Kencana, 2021). To maintain fairness, PMK 131/2024 introduces tiered VAT rates: luxury goods face higher taxes, while essential goods remain at lower rates. This differentiation aims to address economic disparities and minimize distortion caused by previous VAT exemptions. The challenge remains in balancing revenue generation with consumer affordability to ensure sustainable economic growth while mitigating inflationary pressures.

In The alternative value scheme has the potential to shift consumer preferences due to price differences, impacting specific businesses depending on purchasing behaviors. Research by Agha and Haughton (Iswahyudi, 2018) indicates that this scheme negatively affects taxpayer compliance, mainly due to the complexities it introduces in VAT collection, which leads to higher compliance costs. For taxable entrepreneurs (PKP), managing VAT becomes increasingly burdensome, particularly in handling input tax (PM) and output tax (PK). Variations in VAT rates can create difficulties in tax calculations, increasing the likelihood of errors in invoice issuance, even with a single-rate system. This complexity also raises administrative costs for the Directorate General of Taxes (DJP), complicating enforcement and potentially leading to tax disputes.

An effective tax administration system is necessary to ensure smooth implementation. The government must convince the public that the VAT adjustment is designed to enhance revenue without harming livelihoods, while also reducing distortions caused by misallocated VAT facilities. Public support is essential for the success of tax policies, particularly in optimizing national tax revenue. Collaboration between society and the government in tax compliance is key to achieving successful VAT policy implementation and economic stability.

CONCLUSION

Changes in VAT rates have sparked debate among the public, considering that VAT is an almost inseparable element of economic activity. In the process of formulating the policy, the Indonesian government was faced with opportunities and obstacles to achieve the main goal, namely maximizing state revenue through VAT revenue. In the midst of public debate, the government through the Ministry of Finance issued PMK 131 Year 2024 as an answer and created an opportunity. The opportunity that arises from the formulation of the VAT rate change policy is the possibility of increasing state revenue through an increase in the VAT rate. In addition, there is a possibility to reduce distortions resulting from the provision of inappropriate VAT facilities by applying another value scheme. With this opportunity, there are also hurdles that must be faced. These hurdles include the amount of preparation required by the government to deal with the various problems arising from the policy, both from the impact caused by the increase in the VAT rate, the increase in taxpayer compliance costs, and administrative costs, as well as how to get support from the public.

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