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## Reconstruction of Indonesian Tax Law Based on The Principle Of Distributive Justice To Establish A Welfare State In The Framework of The Rule of Law

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**Abstract:** Amidst efforts to establish a welfare state, the current tax system actually creates economic injustice through the dominance of regressive indirect taxes, asymmetric law enforcement, and a transparency deficit that weakens public legitimacy. This study uses a dogmatic research method and deeply analyzes the vertical and horizontal consistency between legal norms and tax practices. The study was conducted using a textual and conceptual approach, as well as an assessment of the harmonization of various related regulations. The results show a disharmony between the constitutional mandate demanding distributive justice and consumption tax policies and weak enforcement against corporate tax avoidance. This phenomenon is exacerbated by limited transparency and accountability in the use of tax funds, leading to a crisis of public trust. The paper recommends a comprehensive reconstruction of the tax system, including strengthening progressive taxation, equal law enforcement, increasing fiscal transparency, harmonizing regulations, and adopting international practices, so that the tax system can function optimally as an instrument for redistributing welfare in accordance with the principles of the Pancasila rule of law.

**Keywords:** Tax Justice; Welfare State; Regressive Taxation; Law Enforcement; Fiscal Transparency

### INTRODUCTION

Taxation is a fundamental institution in the modern state system, serving beyond a mere technical fiscal instrument to serve as a mechanism for redistributing welfare and realizing the social contract between the state and its citizens. In the Indonesian context, the role of taxation has become increasingly strategic given the clear constitutional mandate to establish a welfare state *based* on the principle of distributive justice. However, findings on the ground indicate that serious tensions have emerged between the normative mandate of the constitution and the reality of tax policy implementation on the ground, creating a legitimacy crisis that threatens the foundations of Indonesia's rule of law. (Eiranda dkk., 2024)

At the normative level, the Preamble to the 1945 Constitution of the Republic of Indonesia firmly outlines that the purpose of the state is to "protect all the Indonesian people and all of Indonesia's native land, advance the general welfare, and improve the nation's life." This mandate is not merely a political ornament, but rather a material constitution containing the highest legal ideal, namely the implementation of social justice for all Indonesian people. Further elaboration of this principle is contained in Article 33 of the 1945 Constitution, specifically in paragraph (1) which states that "the economy is structured as a joint effort based on the principle of family," and paragraph (3) which mandates that "the land, water, and natural resources contained therein are controlled by the state and used for the greatest prosperity of the people." These articles indicate that Indonesia adheres to the concept of a material state of law which is not only tasked with upholding the supremacy of law in a formal sense, but also has a substantial responsibility to realize social justice through redistribution mechanisms and guarantees of economic welfare.(Hukumonline, 2024)

Indonesia adheres to a *hybrid conception* of a state based on the rule of law, combining elements of *the rule of law* and *the rule of law* within the framework of Pancasila as *its foundational norm*. Therefore, the Indonesian tax system must be designed and implemented with the principle of distributive justice as an integral part of the Pancasila *rule of law*.(Tiranda, 2017)

Economic analysis from the Indonesian Economic Research Institute (INDEF) further shows that the lower-middle class is the most impacted group. They face significant *pressure* because they do not receive benefits from social assistance programs (which are only provided to the bottom 40 percent) but also do not have sufficient income to absorb the increase in living costs caused by the 12% VAT. Therefore, the 12% VAT increase represents a policy choice that can be predicted *ex ante* to increase horizontal and vertical inequities in the distribution of the fiscal burden, contrary to the constitutional commitment to distributive justice.(Annur, 2024)

Alongside the issue of the regressiveness of indirect tax policies, a far more fundamental problem arises in the country's tax revenue sources: the widespread practice of corporate tax avoidance, *which* has resulted in significant losses to state revenue. According to data from *the Tax Justice Network* cited in a 2020 study, Indonesia loses approximately USD 4.78 billion (Rp 67.6 trillion) annually due to corporate tax avoidance practices.(Purendka dkk., 2025)

Further analysis of the *tax gap composition* shows that *the compliance gap* (the gap between taxes that should be paid and those actually paid) reaches 58 percent, far larger than *the policy gap*. In specific sectors such as pharmaceuticals, property, and real estate, the *tax avoidance rate* reaches an average of 25.36 percent, with some cases showing an *effective tax rate* (ETR) far below the nominal rate.(Sulistiyowati dkk., 2024)

While individual taxpayers face relatively significant audit risks and the real threat of penalties, companies engaging in aggressive *tax avoidance* rarely face proportionate legal consequences. This phenomenon creates what can be called "corporate tax impunity," where companies with strong financial and legal capacity can systematically reduce their tax burdens without significant risk of enforcement. This situation creates a fundamental distortion in the fairness function of tax law: the tax burden is borne disproportionately by weak tax groups (low- and middle-income taxpayers), while powerful tax groups (multinational corporations and *large corporate entities*) can avoid their obligations through weak legal provisions.(Suryana, 2023)

The problem of corporate tax avoidance is directly linked to the phenomenon of intransparency in the management and use of public funds collected through taxes, a phenomenon that has created a crisis of public trust in tax institutions and the state in general. Fiscal transparency is a fundamental prerequisite for building public trust and healthy *tax morale*. When the public can clearly see how their taxes are used for the public good, they are

more willing to comply with their tax obligations voluntarily ( *voluntary compliance* ). Conversely, when there is *intransparency* in the management of public funds and suspicion of improper use of tax funds, public trust declines and gives rise to resistance to fiscal policies established by the government.(Supriyanto, 2024)

Studies show a significant gap between the tax burden paid by the public and the quality of public services received. Indonesia has a relatively high tax rate for a developing country, with the highest income tax rate reaching 35 percent. However, Indonesia's corruption ranking in the 2024 *Corruption Perceptions Index* (CPI) remains 99th out of 180 countries, far below developed countries with high *tax ratios* such as Denmark (ranked 1) or Singapore (ranked 3). This situation creates a public narrative that "high taxes but high corruption, public services remain low," a perception that is highly detrimental to tax morale.(Nafisyah, 2025)

A crisis of public trust has emerged, evident in the wave of protests and demonstrations that have erupted since August 2025 against the VAT increase policy. These protests are not solely a response to the VAT increase itself, but rather represent accumulated public frustration with a tax system perceived as unfair, non-transparent, and failing to provide a return commensurate with tax contributions paid. This phenomenon indicates that the constitutional legitimacy of Indonesia's tax system is in crisis—the public no longer views taxes as a form of mutual cooperation for the common good, but as a burden borne without any guarantee of responsible use.(Masputra, 2025)

This issue of public trust is also related to the fundamental issue of Indonesia's extremely narrow and continually contracting tax base. The latest data shows that out of Indonesia's 270 million population, only 19 million are required to file tax returns in 2023, and only 2.3 million actually pay taxes. Ironically, the number of taxpayers will actually decrease to just 1.7 million in 2024. This phenomenon indicates that not only corporate *tax avoidance* is detrimental to tax revenues, but also massive *tax evasion at the individual level and in the informal sector*, which is not covered by the formal tax system. Indonesia's *tax ratio* was only around 10.07 percent in 2024, far below the ASEAN average (14-15 percent) and OECD countries (34 percent), and has stagnated at around 9-12 percent for nearly the past two decades.(I. F. Budiman & Gumawang, 2025)

The government considers increasing the VAT rate to be one way to increase tax revenue without requiring a politically complex expansion of the tax base. However, this strategy ignores the reality that indirect taxes like VAT tend to be regressive and can exacerbate distributive inequities. Furthermore, the negative public response to the VAT increase suggests that efforts to increase tax revenue through rate increases erode voluntary tax compliance and the legitimacy of tax policy, rather than strengthening it.

Thus, Indonesia faces a fundamental legal paradox: the constitutional mandate clearly outlines that the tax system should function as a redistributive instrument to achieve social justice and public welfare. However, in practice, the tax system creates injustice across three dimensions: regressiveness in the indirect tax structure, asymmetry in law enforcement that grants impunity to corporate tax evaders, and a deficit in transparency and accountability in the use of tax funds that erodes public trust. This gap threatens the fundamental legitimacy of Indonesia's *rule of law*, as the legal system will ultimately only be considered *legitimate* when the public sees that the law is implemented in a fair and transparent manner and produces results consistent with constitutional objectives.

This situation demands a holistic reconstruction of Indonesian tax law that focuses not only on the technical aspects of increasing revenue, but also fundamentally integrates the principles of distributive justice, equal law enforcement, transparency and public accountability, and constitutional legitimacy as core principles in the design and implementation of tax policy. This reform must be able to address the misalignment between constitutional norms and empirical reality, while simultaneously rebuilding the social contract

between the state and its citizens through a tax system that is truly dedicated to achieving a welfare state as mandated by the Preamble and Article 33 of the 1945 Constitution within a true rule of law framework. (Hainorrahman & Futaki, 2024)

## METHOD

This study uses a normative (dogmatic) legal research method that focuses on normative textual analysis, the study of legal principles, and the consistency of laws and regulations in an effort to reconstruct Indonesian tax law based on the principle of distributive justice. The dogmatic approach was chosen because this study has the main objective of analyzing the internal structure of the Indonesian tax law system, namely the relationship between constitutional norms and the implementation of tax policies, as well as identifying normative inconsistencies that result in a legitimacy crisis. Dogmatic legal research is oriented towards an in-depth understanding of the meaning, content, and systematics of positive law as regulated in laws and regulations, relevant legal theories, and doctrines that have developed in the science of tax law and constitutional justice. (Smits, 2017)

The methodology specification of this research combines three main complementary approaches. First, the statute approach *is* carried out by carefully analyzing all laws and regulations relevant to the issue of tax law and distributive justice, starting from the 1945 Constitution of the Republic of Indonesia as the highest basic law, the Law on General Provisions and Tax Procedures (UU-KUP), the Income Tax Law, the Value Added Tax Law, to implementing regulations at the level of the Regulation of the Minister of Finance and the Directorate General of Taxes. This approach allows researchers to conduct an in-depth review of the normative hierarchy of laws and regulations, vertical consistency between the constitution and organic laws, and horizontal harmonization between various laws and regulations of equal standing and regulating the same field.

Second, a conceptual approach *is* applied to analyze the fundamental concepts underlying the Indonesian tax system, including the concepts of distributive justice, welfare state, rule of law in the context of Pancasila, *rechtsstaat*, and universally recognized tax law principles such as equality, certainty, convenience of payment, efficiency, and the ability-to-pay principle. Through this approach, researchers conduct a critical dialogue between the views and legal doctrines developed in constitutional law, tax law, and state science with the provisions of applicable laws and regulations, to verify whether there is harmony between the conceptual spirit underlying a norm and the way the norm is formulated and implemented. (Handayani & Arwanto, 2025)

Third, a synchronization and harmonization analysis approach is used to identify normative inconsistencies and conflicts within the Indonesian tax system. Vertical synchronization is conducted to test the consistency between constitutional mandates (specifically Article 1 paragraph 3, Article 23A, and Article 33 of the 1945 Constitution) and lower-level tax laws, to ensure that more concrete tax policies do not conflict with higher constitutional principles. Horizontal synchronization is applied to compare the consistency between various equivalent laws and regulations governing the taxation sector, for example, the relationship between the Income Tax Law and the Value Added Tax Law in embodying the principle of distributive justice, or the relationship between tax provisions and various laws granting incentives or tax breaks to certain corporations.

This research uses primary legal materials that include all laws and regulations relevant to the research theme, especially the 1945 Constitution and its amendments, laws in the field of taxation (UU-KUP, UU PPh, UU PPN, UU PBB), government regulations, regulations of the Minister of Finance, and circulars of the Director General of Taxation that regulate the implementation of tax policies. Secondary legal materials include books on constitutional law, tax law, theories of justice, international and national scientific journals that discuss tax justice,

legal dogmatics, and the welfare state, as well as decisions of the Constitutional Court and the Tax Court that provide judicial interpretations of tax provisions. Tertiary legal materials that are supporting include legal dictionaries, encyclopedias, and other academic sources that support methodological and conceptual understanding.(S. Budiman dkk., 2020)

The data analysis in this study is qualitative and produces in-depth analytical descriptions. Data collected through literature review were subjected to logical testing to verify internal consistency between various norms, identify logical gaps and normative inconsistencies, and systematically interpret the normative meaning of each provision within the broader context of the legal ecosystem. This study does not aim to test a specific hypothesis but rather to provide a holistic picture of the normative and factual status of the Indonesian tax system, as well as to identify dissonance between *das sollen* (what should be) according to the constitution and *das sein* (what exists) in the implementation of tax policy. With this dogmatic approach, the study is able to produce recommendations for normative reconstruction based on the internal logic of the law and consistency with the fundamental principles adopted by the Indonesian rule of law.(Budianto, 2022)

## RESULTS AND DISCUSSION

### Results

Through a vertical synchronization approach to the prevailing laws and regulations, it becomes clear that there is a fundamental inconsistency between the provisions of Article 33 paragraph (3) of the 1945 Constitution and Article 23A of the 1945 Constitution as the constitutional basis for tax collection, with the concrete policy of increasing Value Added Tax to 12 percent which has been in effect since January 1, 2025. Article 23A of the 1945 Constitution expressly states that “Taxes and other mandatory levies for the benefit of the state must be regulated by law,” and must be directed towards “state interests” which are not only fiscal but also distributional in the broad sense. This article must be read in harmony with Article 33 paragraph (3) which states that the land, water, and natural resources contained therein “are controlled by the state and used for the greatest prosperity of the people.” This means that fiscal policy, including tax policy, must be designed to produce a fair distribution of welfare and not exacerbate economic injustice.(Ruslina, 2012)

Law Number 8 of 1983 concerning Value Added Tax on Goods and Services, as most recently amended by Law Number 7 of 2021 concerning Harmonization of Tax Regulations, demonstrates that, from a normative design perspective, VAT is a tax that is neutral to the taxpayer's economic base, as it is imposed at the sales stage upon consumption of goods and services without considering the financial capacity of individual buyers. In modern tax theory, as outlined in the Handbook of Comparative Taxation, consumption taxes such as VAT are inherently regressive, as low-income households allocate a much larger proportion of their income to the consumption of goods and services than high-income households, who are able to allocate more to savings and investment. This phenomenon is known as the "*marginal propensity to consume*," which is inversely proportional to income level.(Asmarani, 2021)

The increase in VAT from 11 percent to 12 percent has a distributive impact that is clearly detrimental to low-income groups. Data from Celios (Center of Economic and Law Studies) conducted through *simulation models* shows that the poor will experience an increase in monthly expenses of Rp101,880 or Rp1,222,566 per year, while the vulnerable poor will suffer an additional burden of Rp153,871 per month or Rp1,846,455 per year. Simultaneously, an analysis of the impact on the lower middle class shows significant limitations, as this demographic group does not benefit from government social assistance programs and also does not have sufficient financial resources to cope with the rising costs of basic necessities such as education and healthcare without sacrificing access to these vital services.(Aulia dkk., 2025)

This injustice reflects a violation of the fundamental principles that should be the operative principle of the Indonesian tax system. Article 55 of Law Number 8 of 1997 concerning Company Documents mandates that "tax collection shall be conducted based on certain principles," including the principle of *ability-to-pay* and the principles of horizontal and vertical equity. The principle of *ability-to-pay* contains the norm that a taxpayer's financial capacity to pay taxes should be the primary measure in determining the tax burden imposed; the higher the financial capacity, the higher the tax burden that can be imposed, and vice versa. This principle is based on the basic understanding that a fair tax system is one that allocates income according to each individual's economic capacity, not one that threatens the economic foundations of survival for the most vulnerable groups in society.(Abdullah dkk., 2025)

Furthermore, when the 12% VAT is imposed, there is a violation of the principle of vertical equity, which states that individuals with different economic capabilities should bear different tax burdens proportionally according to their ability to pay. In a flat rate Value Added Tax (VAT) system, all expenditures in rupiah are taxed at a uniform rate (12%), regardless of the entity making the expenditure. This shows that an individual with an income of IDR 5 million per month who allocates all of his income to consumption has a relatively higher effective tax rate (ETR) compared to an individual with an income of IDR 50 million per month who allocates 60 percent of his income to consumption and sets aside 40 percent for savings, thus only paying VAT on 60 percent of his income.(Safruddin, 2023)

The implementation of a 12% value-added tax (VAT) reflects a significant normative inconsistency within Indonesia's legislative hierarchy. In accordance with the fundamental principle of constitutional law that lower-level regulatory documents must not contradict higher-level regulations in the hierarchical structure, it can be argued that the Value Added Tax (VAT) Law, which sets a 12% rate, contradicts Article 33 of the 1945 Constitution. This article sets out the primary objective of ensuring the highest possible welfare for the people, and the fourth paragraph of the Preamble affirms the commitment to realizing social justice for all Indonesian citizens. Article 23A of the 1945 Constitution grants legislators the authority to determine tax rates through law. However, this authority is not an unlimited mandate; rather, it must be exercised within the framework of a "proportionality review" that ensures that specific tax policies remain in line with the constitution's core values of social justice and the people's welfare.(Ruslina, 2012)

The phenomenon of tax law enforcement shows inconsistency in the application of legal principles, which is characterized by a disproportionate focus on individual taxpayers while showing leniency towards tax avoidance strategies implemented by large corporations and multinational entities. This phenomenon is a fundamental violation of the principle of equality before the law, as guaranteed in Article 27 paragraph (1) of the 1945 Constitution and Article 1 paragraph (3) of the 1945 Constitution, which states that Indonesia is a state based on law (*rechtsstaat*). (Oktavira, 2022)

From a dogmatic perspective, this imbalance in law enforcement creates what can be described as a "two-tier justice system" in Indonesian taxation. Data analysis shows that audit rates for individual taxpayers (WPOP) who earn income from certain sources reach significant levels. This is due to rigorous risk assessments and a high probability of detection of violations. Conversely, for corporate taxpayers (WPB) engaged in aggressive tax avoidance practices, law enforcement mechanisms are less stringent and often disproportionate to the amount of tax evasion achieved.(Hidayat, 2019)

This imbalance lies in the legal mechanisms used. Law Number 8 of 1997 concerning Company Documents integrates various sophisticated anti-avoidance provisions, including Transfer Pricing Regulations (Article 18 of the Income Tax Law, which has been amended multiple times), Thin Capitalization Rules, Controlled Foreign Corporation (CFC) Rules, and the General Anti-Avoidance Rule (GAAR) stipulated in Law Number 7 of 2021 concerning

Harmonization of Tax Regulations. Formally, these provisions grant the Directorate General of Taxes broad authority to correct and re-impose taxes on transactions deemed to be conducted solely for tax avoidance purposes.(Anindya, 2025)

However, in practice, enforcement of these anti-tax avoidance rules faces significant structural and procedural barriers. First, the burden of proof rests with the tax authorities to prove the intent and substance of a transaction, while well-resourced corporate taxpayers can prepare sophisticated documentation and hire expensive tax advisors to argue that their transactions have a legitimate business purpose beyond tax avoidance. In Indonesia, the technical capacity of the Director General of Taxes is relatively limited compared to that of private tax professionals working for multinational corporations. This imbalance creates a significant information asymmetry, a situation that tends to favor corporate entities.(Khifni dkk., 2025)

Second, the limited resources available to the Director General of Taxes to conduct comprehensive audits, particularly of complex transactions involving transfer pricing or foreign tax credits, reinforce the impunity enjoyed by corporate tax evaders. According to recent data, of the Rp1,300 trillion annual tax deficit, only a small portion can be addressed through effective law enforcement measures. Much of this tax gap remains unresolved due to limited capacity and a mismatch between the sophistication of tax evasion schemes and the sophistication of audit mechanisms available to the relevant authorities.(Andriyani, 2025)

Third, the legal structure itself exhibits normative ambiguity. Unlike the clear illegality of tax avoidance, which is subject to legal sanctions, borderline tax avoidance occupies a gray area between legal and illegal, with no clear threshold at which tax planning practices become unacceptable. This phenomenon creates a situation where many companies can engage in aggressive tax planning with little concern about significant legal consequences. The legal uncertainty that dominates this environment facilitates the possibility of denial, which can be used to mitigate the potential consequences of such tax strategies.(Anindya, 2025)

Fourth, this corporate impunity is also relevant in relation to criminal liability. Despite provisions in Law Number 8 of 1997 concerning Tax Crimes that regulate criminal prosecution for significant tax evasion, criminal prosecutions of corporate entities and their directors remain rare in practice. The trial process in these cases often takes a long time in the judicial system. In contrast, enforcement of tax non-compliance by low- and middle-income taxpayers (WPOP) is carried out more quickly through administrative collection mechanisms and seizure orders that can be executed directly without lengthy judicial proceedings.(Hidayat, 2019)

This phenomenon creates a highly detrimental paradox from a legal and justice perspective. Under prevailing norms, the principle of equality before the law stipulates that all taxpayers, both individuals and corporations, must be subject to uniform legal standards and enforcement mechanisms. This principle is reinforced by the obligation to ensure that economic status or the ability to afford expensive legal counsel does not become a discriminatory factor. However, analysis of existing data indicates that unequal enforcement of tax regulations results in a disproportionate burden of compliance being borne by individual taxpayers with limited financial resources. Conversely, large corporate taxpayers are able to evade their tax obligations with a high degree of freedom. This violates the principle of equality before the law, which is the foundation of the law's legitimacy.(Hasan, 2020)

The third dimension of the most fundamental problem is a crisis of legal legitimacy arising from a combination of opaque use of tax funds and a lack of public accountability. This occurs alongside uneven enforcement of laws against corporate tax evasion. This crisis goes beyond technical failures in public financial management; it affects the fundamental basis of the social contract between the state and its citizens, which in turn affects the legitimacy of the legal system itself.(Aditama, 2025)

From the perspective of constitutional law theory, legal legitimacy in a modern state, according to Max Weber, depends on three grounds: legal-rational authority (i.e., compliance with the law because society believes that the applicable rules have been made through legitimate procedures and are applied consistently), traditional authority (compliance based on custom and tradition), and charismatic authority (compliance with figures considered to have charisma). In the context of a modern state based on the rule of law, the primary source of legitimacy is legal-rational authority, namely that society obeys the law because they believe that the law is just, applied consistently, and designed for the public interest.(Appiah dkk., 2024)

However, when public trust in government institutions is eroded by the perception that tax funds collected from the public are not being used transparently, responsibly, or effectively for the public good, the rational basis for legal compliance will gradually collapse. At this point, society may shift from voluntary compliance to coercive compliance (compliance due to fear of punishment). This, in turn, requires increased law enforcement resources and creates ongoing tensions between the state and society.(Dagan, 2024)

Tax opacity is reflected in several concrete dimensions. First, although the government publishes an Annual Tax Expenditure Report and is recognized internationally as one of the highest in the Global Tax Expenditure Transparency Index, transparency at this level remains aggregate and macro, with no breakdown of how specific tax revenues are used in implementation programs on the ground. Ordinary taxpayers, despite contributing to the state treasury, often lack clarity on how their contributions are allocated to the specific public services they use.(Nafisyah, 2025)

Second, there is a significant information gap between the government and the public regarding tax compliance and enforcement. Government agencies possess extensive data on audit results, enforcement actions, and revenue collected; however, this information is not regularly and easily communicated to the public in a format that is easily understood and actionable. A glaring lack of transparent communication dominates this issue, leaving the public uncertain about the extent to which tax evasion is detected, the amount of fines imposed, and the use of revenues recovered from tax enforcement. This information gap raises public doubts about the rigor in reporting and addressing corporate tax evasion.(Suryantara, 2024)

Third, and this is the most critical dimension from the perspective of *rule of law* and legitimacy, is the public perception that tax-funded public services suffer from significant corruption and inefficiency, while corporate tax avoiders are allowed to evade their tax obligations without significant consequences. Data from the Corruption Perceptions Index shows that Indonesia has a corruption ranking of 99 out of 180 countries, far below developed countries with high tax ratios such as Denmark (ranked 1), Finland (ranked 2), or Singapore (ranked 3). This creates *cognitive dissonance* for the public: they are asked to pay taxes for the public good, yet they note that tax-funded public services are often inadequate, public infrastructure is damaged, and corruption occurs at various levels of the bureaucracy that is supposed to manage these funds.(Simanjuntak, 2025)

Furthermore, this perception is reinforced by a clear imbalance in law enforcement. While small-scale tax violations by ordinary citizens are swiftly prosecuted, large-scale tax evasion by large corporations and powerful individuals is ignored or dealt with half-heartedly. This undermines the fundamental assumptions of the social contract: that the law applies equally to all and that paying taxes is a justified sacrifice for the common good. The legitimacy of the tax system as a whole is eroded when ordinary citizens perceive themselves as obligated to pay their taxes in full while powerful corporate entities can avoid paying them, and when the government uses tax funds in a non-transparent and unaccountable manner.(Nafisyah, 2025)

This phenomenon has been empirically demonstrated by the massive wave of protests that have erupted since August 2025 in response to the increase in the value-added tax (VAT) to 12 percent. Interestingly, official sources often analyze the intensity of these protests as simply a rejection of the tax increase. However, a deeper analysis reveals that the underlying grievance is not simply about the tax increase, but rather about the breakdown of the social contract itself—the belief that the state deserves the sacrifices demanded. The public is saying: “Why should we pay higher taxes if we don’t believe the funds are being used for the public good and see corporate elites evading taxes freely?”(Dagan, 2024)

From the perspective of *the rule of law*, this represents a fundamental crisis. According to Lord Bingham and the International Commission of Jurists, *the rule of law* encompasses the following principles: the law must be clear and accessible; government power must be limited by law; all people must be equal before the law; and government institutions must be transparent, accountable, and possess integrity. The lack of transparency in public financial management, coupled with the unequal enforcement of laws that favor those in power, violates all of these legal principles and erodes the foundation of the legal system's legitimacy.(Hasan, 2020)

There are fundamental weaknesses in the normative consistency of Indonesia's tax system. The regressive nature of the 12% VAT violates the principle of distributive justice enshrined in the constitution; unequal law enforcement violates the principle of equality before the law; and the lack of transparency violates the social contract that underpins the legitimacy of the legal system. These three factors together have created a situation in which Indonesia's tax system has deviated significantly from its constitutional mandate to realize a welfare state based on social justice within a legal framework.(Hasan, 2020)

To change this situation, we need a fundamental reconstruction of tax law that goes beyond technical reforms in rates or anti-avoidance rules. We need substantial reform of the structural design of the tax system itself. This reform must reintegrate the principles of distributive justice, equality before the law, and transparent governance as operational principles. These principles must not be merely decorative principles enshrined in the Constitution but neglected in practical implementation.(Dagan, 2024)

## Discussion

To reconstruct Indonesia's tax system to be consistent with the constitutional mandate of distributive justice and the welfare state, the first and most fundamental step is to restructure the tax base by maintaining and strengthening the progressive nature of the income tax while simultaneously reducing reliance on regressive indirect taxes such as VAT. The theoretical principle underlying this approach is that, in a truly progressive and distributively just tax system, each taxpayer's fiscal contribution should be proportional to their economic ability to pay, not based on their consumption. Progressive taxes, particularly income taxes with increasing rates according to income brackets, have been empirically proven across various countries to be the most effective tool for achieving significant redistribution and reducing economic inequality.(Syahril & Hasan, 2024)

Tax-to-revenue ratio reform requires increasing revenue from progressive income taxes while simultaneously reducing the burden of regressive value-added taxes. As OECD data shows, in established welfare states such as Denmark, Finland, Sweden, and other Nordic countries, direct taxes (income taxes) account for 50-60% of total tax revenues, while indirect taxes (e.g., VAT) account for 20-30%. In contrast, Indonesia has a different structure, with Value Added Tax (VAT) accounting for over 30% of total tax revenues, while Corporate Income Tax (PPH Badan), which plays a key role in progressive redistribution, accounts for around 25%. This adjustment requires increasing the effective collection of corporate income tax through broadening the tax base and improving compliance, along with a potential

reduction in the VAT rate from 12 percent back to a more sustainable level or a progressive differentiation in VAT rates, applying a lower rate to basic goods and a higher rate to luxury goods consumed primarily by high-income households. (Diamond & Saez, 2011)

To address this issue, the proposed reforms should include a progressive restructuring of income tax brackets. This restructuring should include increasing marginal tax rates for high-income individuals and corporations. It is important to consider increasing the corporate tax rate, currently at 25 percent. This rate could be raised to 30-32 percent, in line with similar countries in the region. This increase would have a significant impact on tax revenues without unduly burdening middle- and low-income taxpayers. According to simulation studies, increasing the income tax rate for the highest income group, namely those with annual incomes above IDR 5 billion, from 35 percent to 40-45 percent, coupled with increasing the corporate tax rate to 32 percent and closing significant tax avoidance loopholes, could increase tax revenues by 4-5 percent of GDP. This increase would offset the reduction in the VAT rate and ensure an overall increase in fiscal revenues. (Rahmawati, 2024)

Furthermore, comprehensive tax structure reform is urgently needed to integrate progressive asset taxes and wealth taxes, which are currently largely absent from the Indonesian tax system. Many countries implement a combination of property taxes, inheritance taxes, and capital gains taxes as part of their progressive tax architecture to achieve equitable distribution goals. In Indonesia, the property tax currently amounts to only 0.08 percent of GDP, well below the international standard of 1-1.5 percent. However, this could be a significant source of additional revenue, both progressive and efficient, especially if designed with a progressive rate structure that imposes higher rates on high-value properties and secondary properties used for investment purposes. (Ardian dkk., 2025)

The second dimension of tax system reconstruction is eliminating asymmetries in tax law enforcement, which currently grant impunity to corporate tax evaders while imposing harsh enforcement measures on individual taxpayers. From a legal and constitutional justice perspective, unfair enforcement against different categories of taxpayers constitutes a fundamental violation of the principle of equality before the law. To reverse this, the government must implement comprehensive institutional strengthening of the tax administration's capacity, particularly the Large Taxpayers Office (LTO), which handles audits and enforcement against large and multinational corporations. (Djarmiko & Dharmasetya, 2025)

This institutional capacity reform requires a multifaceted approach. First, a significant increase in resource allocation for labor, training, and technological infrastructure in tax administration, particularly for Large Taxpayer Units, which are currently understaffed compared to the complexities of corporate taxation issues and international transactions involving transfer pricing, thin capitalization, and profit shifting schemes. According to data from the International Survey of Revenue Administration (ISORA), coordinated by the OECD, the tax per employee ratio in Indonesia reached IDR 9.47 billion per employee, significantly higher than the OECD average of IDR 4 billion, indicating severe staffing shortages and capacity constraints. (Muttaqien & Purwati, 2025)

Second, stronger and clearer anti-tax avoidance regulations need to be strengthened and consistently applied. Indonesia has adopted the General Anti-Tax Avoidance Rule (GAAR) in the 2021 Tax Harmonization Law, but its implementation and enforcement are far from optimal. An effective GAAR must comprehensively adopt the principle of substance over form, allowing tax authorities to deny tax benefits from transactions that are technically compliant but lack a legitimate business purpose beyond tax reduction. Judicial interpretation of the GAAR also needs to be strengthened through the development of consistent jurisprudence that establishes clear standards regarding when the GAAR can be applied and when taxpayers can expect legal protection. (Cowx & Kerr, 2024)

Third, Indonesia must accelerate the implementation of international tax cooperation standards agreed upon in the OECD/G20 BEPS Inclusive Framework, particularly Pillar Two, which introduces a 15 percent global minimum tax for multinational enterprises. With consistent adoption and implementation of this global minimum tax standard, Indonesia will be able to eliminate extreme forms of profit shifting and tax base erosion that currently cause significant revenue losses. Coordination with foreign tax authorities through automatic information exchange and review of transfer pricing documentation will significantly improve the effectiveness of law enforcement on international transactions.(Aprilia, 2025)

Fourth, and this is a crucial dimension, imbalances in law enforcement can be reduced by establishing equal probabilities of detection and similar enforcement consequences for individual and corporate taxpayers. This means that the level of criminal prosecution for corporate tax evasion must be increased to be proportional to the level of criminal law enforcement for individual tax evasion. Currently, criminal prosecutions for tax crimes largely target individual taxpayers, while corporate entities and their executives are often subject to only relatively light administrative sanctions. To achieve true equality before the law, institutional reforms will require allocating significant resources to criminal investigation units specialized in corporate tax crimes and capable of addressing the complexities of corporate structures, holding companies, and transfer pricing arrangements.(Adiyanta, 2025)

The third dimension of reconstruction is establishing a comprehensive fiscal transparency framework and strengthening public accountability mechanisms in the management and utilization of public funds collected through taxes. The basic principle behind this dimension is that the legitimacy of the tax system depends on public confidence that the taxes they pay will be used responsibly, transparently, and for the true public good. If this social contract collapses, that is, when the public believes that tax revenues are being used irresponsibly or corruptly, then even from a purely fiscal perspective, the system becomes counterproductive as voluntary compliance declines and enforcement costs increase dramatically.(Closs-Davies dkk., 2024)

To create meaningful fiscal transparency beyond simply publishing aggregate data, the government needs to establish a detailed, accessible, and user-friendly public portal that explicitly shows how each category of tax revenue is used for specific programs, services, and infrastructure investments. This goes beyond the current Tax Expenditure Report, which is openly aggregated and *top-down*. Transparency must be granular; for example, residents of North Jakarta should be able to see what proportion of their taxes goes to their local public services, how much to national defense, how much to education, and so on. Technologies such as advanced data visualization, mobile apps, and citizen-friendly dashboards can significantly improve public accessibility and understanding of the fiscal picture.(Firstiyanendro & Utomo, 2025)

More importantly, participatory budgeting mechanisms must be institutionalized at all levels of government. Participatory budgeting, which has been successfully implemented in various countries and several Indonesian cities such as Surabaya and Banyuwangi, allows citizens to actively participate in public budget planning and allocation, not only in a consultative role but also in the actual decision-making process regarding resource allocation. Research shows that participatory budgeting significantly improves fiscal transparency, reduces the risk of corruption, and most importantly, restores public trust because citizens directly see that their voices are taken into account in the use of public funds.(Mariani & Kiswara, 2020)

Institutional accountability mechanisms also need to be strengthened. The Supreme Audit Agency (BPK), as the government's external auditor, should be given broader authority and resources to conduct comprehensive audits not only on the use of public funds, but also on the effectiveness of tax administration and compliance with constitutional requirements

regarding distributive justice. The BPK's independence must be strictly protected from political interference to ensure the credibility of its findings and recommendations. Currently, the BPK cannot provide an unqualified opinion on government financial reports due to the limited scope of its audits, which are related to the inaccessibility of tax administration data. This situation itself represents a lack of transparency.(IMF, t.t.)

Accountability also demands public reporting on specific enforcement actions in tax compliance. The Directorate General of Taxes should publish regular reports on: how many cases of tax evasion have been detected and corrected, how many fines have been imposed, how much revenue has been recovered, and how the recovered revenue has been used. This lack of information creates a vacuum that is often filled with speculation and rumors, further eroding public trust. Transparency in enforcement actions also serves as a deterrent—if potential tax evaders see that their tax evasion schemes have been detected and sanctions imposed, they will be more likely to comply with the regulations.(Nurakhmadi dkk., 2024)

The fourth dimension of reconstruction is constitutional and legislative reform that explicitly integrates distributive justice as a guiding principle in tax law. Currently, the Indonesian Constitution contains provisions on public welfare and social justice, but in practice, these provisions are aspirational and not legally binding, thus not compelling the courts or legislature to overturn or revise tax policies that conflict with these principles. To change this, amendments or clarifications to the 1945 Constitution and/or the Tax Administration Law could explicitly codify that the tax system must be designed in accordance with the principles of distributive justice, affordability, horizontal and vertical equality, and proportionality related to the constitutional welfare objective.

Legislative reforms should also adopt a “constitutional proportionality test” for tax policy, which would require courts to evaluate whether a particular tax policy is designed in a manner proportional to achieving constitutional objectives, or whether it imposes an excessive burden on certain groups that is not justified by the constitutional objectives. This approach has been used by constitutional courts in various countries, including the Turkish Constitutional Court and the South African Constitutional Court, and could be adopted by the Indonesian Constitutional Court to provide a framework for constitutional review of tax policies.(Suasa dkk., 2021)

Normative codification should also include an explicit recognition that in situations where existing tax policies or structures fail to achieve the goal of distributive justice and undermine public trust through opaqueness or unfair enforcement, there is a constitutional obligation for the government to reform. This would provide a basis for citizens or public interest groups to challenge tax policies in the Constitutional Court based on the principle of constitutional tax justice, creating an accountability mechanism that currently lacks one.(Mahpudin, 2024)

Finally, the reconstruction of Indonesia's tax system must be carried out within the context of international tax cooperation and the application of global best practices in tax design, administration, and enforcement. Indonesia has become a member of the OECD/G20 Inclusive Framework on BEPS and has committed to implementing various tax standards, including the Common Reporting Standard (CRS) for the automatic exchange of information and Pillar Two of the global minimum tax. These commitments need to be implemented seriously, not only formally but also substantively in administration and policy design.(Tambunan, 2021)

Furthermore, Indonesia can learn from international experiences with progressive tax systems in welfare states, particularly those of the Nordic countries, the Netherlands, and other continental European countries that have successfully combined high levels of tax redistribution with strong compliance and public acceptance. Institutional designs from these countries, such as independent tax ombudsmen, citizen advisory boards in tax policy

development, and multi-level governance in tax administration, can be adapted and implemented in the Indonesian context to enhance both the effectiveness and legitimacy of the tax system. (Rumasukun & Noch, 2023)

The most important aspect of this reconstruction is that the four dimensions—structural progress, symmetrical law enforcement, fiscal transparency, and the constitutional framework—are not separate but mutually reinforcing and supporting each other, creating a fundamentally fairer, more legitimate, and more effective system. If taxes are made more progressive but enforcement against corporate tax avoidance remains weak, the regressive nature of Value Added Tax (VAT) will persist, albeit at a more muted level. If law enforcement becomes symmetrical but there is no transparent framework to demonstrate how collected revenues are used, public trust will continue to erode. Reconstruction must be comprehensive and holistic, focusing on achieving mutual reinforcement among the various elements of reform to create a positive cycle that strengthens the legitimacy of tax laws and restores the social contract between the state and its citizens in a context consistent with the constitutional mandate for distributive justice and a welfare state within a genuine legal framework. (Wijayanto, 2015)

## CONCLUSION

This research has identified and analyzed a fundamental paradox in Indonesia's tax law system: the inconsistency between the constitutional mandate to realize *a welfare state* based on distributive justice and regressive tax policies, asymmetric enforcement, and a fiscal transparency deficit that erode public trust. The research shows that this normative inconsistency is not merely *a technical issue* but represents a fundamental crisis in the legitimacy of Indonesia's *rule of law*.

To overcome this crisis, a holistic and comprehensive reconstruction is needed that encompasses five interconnected elements: first, *rebalancing* the tax structure toward *progressivity* by reducing reliance on regressive indirect taxes and strengthening progressive income taxes; second, truly symmetrical law enforcement through institutional capacity building, strong anti-tax avoidance regulations, and equal detection probability for all categories of taxpayers; third, establishing a fiscal transparency framework and participatory budgeting mechanisms to strengthen the social contract; fourth, constitutional and legislative reforms that integrate distributive justice as an operational principle; and fifth, harmonization with *international best practices* and global tax standards. This reconstruction will not only improve revenue mobilization, but more importantly, will restore the constitutional legitimacy of the Indonesian tax system and strengthen the foundation of the Pancasila state law in realizing the noble goal of equitable prosperity for the people.

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