



## RECONSTRUCTING THE VAT THRESHOLD IN INDONESIA: A LITERATURE REVIEW\*

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Article	Abstract
<p><b>Keywords:</b> taxable entrepreneur, threshold, VAT</p> <p><b>History of Article</b> Received: May 21, 2024; Reviewed: May 26, 2024; Accepted: June 15, 2024; Published: June 20, 2024</p> <p><b>DOI:</b> 10.56282/slr.v2i2.507</p>	<p>The high threshold to be confirmed as a taxable entrepreneur in Indonesia, which is the amount of gross turnover and/or gross income in a fiscal year of at least Rp 4.8 billion, has attracted criticism from several quarters, including the World Bank. There are even studies that argue the need to determine the ideal VAT threshold in a country, considering that a high threshold will reduce VAT revenue, while a low threshold will impose high compliance costs on small businesses. Based on a normative legal study, this study reaches two conclusions. First, the provisions governing the current VAT threshold in Indonesia have undergone several changes since the enactment of the 1984 VAT/PPnBM Law, with the latest provision stipulating that the amount of gross turnover and/or gross income in a fiscal year must be at least Rp. 4.8 billion. Second, the legal reconstruction of the VAT threshold in Indonesia needs to be carried out while still harmonising with other VAT policies, such as tariffs and the expansion of the VAT base, and taking into account benchmarking in several countries. It is recommended that there be a change in VAT policy on the threshold by not applying a threshold that is too high, taking into account the principle of neutrality, suggestions from competent world institutions such as the World Bank, and benchmarking with several developed countries that have a good VAT system and the imposition of VAT thresholds is not too high, such as Australia, Malaysia, Singapore, and Switzerland.</p>

### A. INTRODUCTION

Tax challenges in the digital age have led to sub-optimal tax performance. The Organisation for Economic Co-operation and Development (OECD) has made several proposals to address tax challenges in the digitalisation era. The first addressing effort was conducted by the OECD through Action Report 1 Base Erosion Profit Shifting (BEPS) in 2015, namely Addressing the Tax Challenges of the Digital Economy. The second handling effort was made through the OECD's Going Digital project since 2017,

to help policymakers better understand digital transformation and develop and implement a robust framework that promotes a positive and inclusive digital economy and society.<sup>1</sup>

Various efforts have been made by tax authorities to address tax challenges in the digital era, one of which is the challenge of sub-optimal tax performance. Indonesia is one of the countries whose tax performance is still not optimal, including the performance of Value Added Tax (VAT), although the tax legislation has undergone several changes since 1984, as it is necessary to re-regulate or amend the VAT law in Law No. 7 of 2021 on the Harmonisation of Tax Regulations (HPP Law). Some parties believe that the amount of the threshold or threshold of taxable entrepreneurs (PKP), which is currently IDR 4.8 billion per year, needs to be lowered in order to increase government revenue.<sup>2</sup> Even the World Bank, in its report titled "Indonesia Economic Prospects", suggested that Indonesia lower the threshold of PKP to IDR 600 million in order to increase the tax base, both from income tax (PPh) Article 25 deposits and VAT collection from corporations.<sup>3</sup>

Of course, the assessment of the size of the threshold for VAT in Indonesia needs to be studied philosophically and jurisprudentially in the context of the current digitalisation era, as the tax authority faces the challenge of aligning 'code is law' with the central insight of cyber law. The policy will only be achievable if the government is able to align VAT threshold policy with the borderless nature of digitalisation, including the many technologies that can be used by web-based sellers that are relevant to the transaction of goods or services by consumers over the web and the internet. Services in the digital age include applications, online games, e-books, streaming and downloadable media, cloud/web-based services, digital professional advice. This is also reinforced by the lack of studies or research on VAT thresholds, especially in Indonesia. For example, the results of Satyadini's study found empirical evidence in the form of a disproportionate distribution of taxpayers at the PKP threshold, which indicates the behaviour of taxpayers to place themselves at a point slightly below the PKP threshold.<sup>4</sup> This is an early indication of the practice of VAT avoidance, where taxpayers tend to report lower turnover in order not to exceed the PKP threshold.<sup>5</sup> However, these previous studies have not critically examined and answered what the VAT threshold should be in Indonesia. As for Satterthwaite, he found that in the context where (generally) small firms outnumber large firms, setting a higher threshold rather than a lower one can reduce competitive inequity by drawing an arbitrary line between similar firms.<sup>6</sup> Under these conditions, a higher registration threshold can improve VAT fairness and efficiency.<sup>7</sup> Furthermore, Minh argues that since VAT is one of the most important taxes in the revenue system, tax policy and tax

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<sup>1</sup> Organisation for Economic Co-operation and Development, Tax Challenges Arising from Digitalisation – Interim Report 2018: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project, Paris: OECD Publishing, 2018.

<sup>2</sup> Enforce.com, "Apakah Ambang Batas Pengusaha Kena Pajak (PKP) Perlu Diturunkan? Ini Kata Pengamat", available at <https://enforce.com/taxnews/apakah-ambang-batas-pengusaha-kena-pajak-pkp-perlu-diturunkan-ini-kata-pengamat-1>, accessed on December 20, 2023.

<sup>3</sup> *Loc.cit.*

<sup>4</sup> A. Satyadini, VAT Threshold and Taxpayers' Behavioral Responses, *Simposium Nasional Keuangan Negara*, Vol. 1, No. 1, 2018, retrieved from <https://jurnal.bppk.kemenkeu.go.id/snkn/article/view/178>.

<sup>5</sup> *Loc.cit.*

<sup>6</sup> Emily Ann Satterthwaite, On The Threshold: Smallness and The Value-Added Tax, *Columbia Journal of Tax Law*, Vol.9, 2018, p. 177.

<sup>7</sup> *Loc.cit.*

administration units should develop their capacity to forecast VAT revenue, estimate compliance, and assess the revenue impact of proposed changes in tax laws and/or tax administration practices.<sup>8</sup> According to Minh, the existing VAT regime should achieve relatively greater efficiency improvements in VAT collection by increasing the existing compliance rate, even if this is possible through a combination of simplifying the VAT regime and improving the capacity of tax administration - rather than by raising the standard rate. This earlier study did not criticise the role of the VAT threshold in increasing VAT revenue and improving taxpayer compliance. Furthermore, Gebresilasse and Sow analysed the behaviour of manufacturing firms in Ethiopia when the government applied the VAT threshold after the introduction of VAT in 2003. The study found that there was clustering of firms around the threshold: marginal clustering firms successively lowered their reported turnover by 48,000 Birr to avoid registering at the 500,000 Birr (\$25,000) VAT threshold in 2003. This previous study did not explain how the VAT threshold compares across countries and did not argue for the ideal threshold in Ethiopia.<sup>9</sup>

Based on the background and novelty of this study, it is necessary to conduct a normative legal study that can answer the following two problems. First, what are the provisions of the VAT threshold in Indonesia? Second, what is the legal reconstruction of the VAT threshold in Indonesia.

## **B. ANALYSIS AND DISCUSSION**

### **1. VAT threshold regime and its changes in Indonesia**

Since the enactment of Law No. 8 Year 1983 on Value Added Tax and Sales Tax on Luxury Goods, the VAT threshold has undergone several changes. When the VAT/PPnBM Law came into effect in 1984, the government had regulated the provisions on the threshold of PKP based on the Minister of Finance Decree (KMK) No. 430/KMK.04/1984 on the Limit and Size of Small Entrepreneurs Not Subject to VAT 1984. KMK No. 430/KMK.04/1984 stipulates that small entrepreneurs are taxable entrepreneurs who supply taxable goods (BKP) or taxable services (JKP) with a total gross sales value of not more than IDR 60 million per year and use a business capital of not more than IDR 10 million. KMK No. 430/KMK.04/1984 revoked KMK No. 967/KMK.04/1983 on the Limits and Size of Small Enterprises Not Subject to VAT 1984, which stipulated that small enterprises are taxable persons for VAT purposes (PKP) with a gross turnover of not more than Rp. 24 million or taxable persons for VAT purposes with a capital of not more than Rp. 10 million. After KMK No. 430/KMK.04/1984, KMK No. 303/KMK.04/1989 concerning the limitation and size of small entrepreneurs for VAT purposes was issued. The KMK regulates several things concerning the threshold of VAT small entrepreneurs, including

- a. Individual entrepreneurs who supply taxable goods with a gross value not exceeding Rp 60 million in a tax year.
- b. Individual entrepreneurs who supply JKP with a gross value of not more than Rp. 30 million in a tax year.

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<sup>8</sup> Tuan Le Minh, Estimating the VAT Base: Method and Application, *Tax Notes Int'l*, April 9, 2007, p. 203.

<sup>9</sup> *Loc.cit.*

Subsequently, KMK No. 1288/KMK.01/1991 on the limitation and size of small entrepreneurs for VAT purposes was issued, which was repealed by KMK No. 648/KMK.04/1994 on the limitation of small entrepreneurs for VAT purposes. KMK No. 648/KMK.04/1994 stipulates, inter alia, that a small entrepreneur is an entrepreneur who, in a fiscal year, supplies taxable goods with a gross turnover not exceeding Rp.240 million or taxable services with a gross turnover not exceeding Rp.120 million. Then, KMK No. 552/KMK.04/2000 on the limitation of small entrepreneurs for VAT was issued, which, among other things, stipulates that a small entrepreneur is an entrepreneur who, in one fiscal year, supplies taxable goods with a gross turnover of not more than Rp. 360 million or taxable services with a gross turnover of not more than Rp. 180 million. This KMK has been revoked and replaced by the Minister of Finance Regulation (PMK) No. 68/PMK.03/2020 concerning the limitation of small entrepreneurs for VAT. This PMK stipulates, among other things, that a small entrepreneur is an entrepreneur who provides taxable goods and/or services with a total gross turnover and/or gross income of not more than IDR 600 million in a fiscal year. In addition, as of 1 January 2014, the VAT threshold has been changed to the amount of gross turnover and/or gross receipts in one fiscal year of not less than IDR 4.8 billion, as set forth in MoF Regulation No. 197/PMK.03/2013 on the Amendment to the Regulation of the Minister of Finance No. 68/PMK.03/2020 on the Limitation of VAT for Small Entrepreneurs.

## **2. VAT Threshold and its Relationship with VAT in the Digitalisation Era**

There are 3 (three) changes in the substance of the VAT Material Tax Law through the regulation of other laws, namely the Government Regulation in Lieu of Law (Perpu) Number 1 of 2020, the Job Creation Law and the COGS Law. Perpu Number 1 of 2020 is the government's quick response in anticipation of the digitalisation era, including anticipation of the Covid-19 pandemic, which has an impact on the economic crisis and has the potential for a social crisis. Some of the most important contents of the VAT regulation are the tax treatment of commercial activities through electronic systems (PMSE) and the extension of the period for exercising rights and fulfilling tax obligations. The tax treatment of PMSE activities is a trade whose transactions are carried out through a series of electronic devices and procedures. The main points of the regulation are (a) the imposition of VAT on the use of intangible taxable goods and/or services from outside the customs territory within the customs territory by PMSE; (b) PMSE operators are natural persons or legal entities engaged in PMSE activities, consisting of foreign traders, foreign service providers, foreign PPMSEs and/or domestic PPMSEs; (c) the imposition of VAT on the use of intangible taxable goods and/or services from outside the customs territory within the customs territory by PMSE. (c) VAT imposed on the use of intangible taxable goods and/or services from outside the Customs Territory within the Customs Territory by PMSEs shall be collected, remitted and reported by PMSE Business Actors appointed by the Minister. (d) PMSE Business Actors appointed as PMSE VAT Collectors are those who have fulfilled certain criteria. (e) The VAT to be collected by the PMSE VAT Collector is 10% multiplied by the tax base. (f) The PMSE VAT Collector must remit the VAT collected for each tax period not later than the end of the month following the end of the tax period. (g) The PMSE VAT Collector must report the VAT collected and

remitted on a quarterly basis for a period of 3 (three) tax periods, at the latest by the end of the month following the end of the quarterly period. The limits of certain criteria to be appointed as a PMSE VAT Collector include: (i) the transaction value with buyers in Indonesia exceeds Rp 600 million in 1 (one) year or Rp 50 million in 1 (one) month; and/or (ii) the number of traffic or accessors in Indonesia exceeds 12 thousand in 1 (one) year or 1 thousand in 1 (one) month. The background of the provision of PMK-48/2020 is to create equal tax treatment (level playing field) between both conventional and digital economy operators, as well as between domestic and foreign digital economy operators, and to provide legal certainty for the collection of VAT on the use of intangible taxable goods and/or services from outside the customs territory into the customs territory by PMSE.

PMK-48/2020 basically does not set the VAT threshold applicable in Indonesia, as it only regulates the limitations of certain criteria to be appointed as a PMSE VAT collector. By being appointed as a PMSE VAT collector, the collector immediately collects VAT, regardless of whether the collector is a PKP or not. Of course, this treatment is not the same as the traditional output and input tax collection mechanism, which still takes into account the VAT threshold to be confirmed or not as a PKP. The government should set an ideal and consistent VAT threshold in today's digital era, as the registration threshold, which is usually measured on the basis of annual turnover, determines which businesses remain exempt from registering and collecting VAT on their sales.<sup>10</sup> This means that more studies are needed to determine the VAT threshold, as the main challenge in implementing VAT is to set an appropriate turnover threshold at which businesses are required to register for the tax.<sup>11</sup> because a high threshold will reduce tax revenue, while a low threshold will impose high compliance costs on small businesses.<sup>12</sup>

### 3. Comparison of VAT Threshold in Different Countries

There is a broad consensus among VAT economists on the setting of the VAT threshold. Some argue that the economic efficiency of VAT is improved by setting a higher threshold rather than a lower one (so that more businesses are exempted).<sup>13</sup> While there is a consensus among experts in favour of a high threshold, actual thresholds vary widely and tend to be low, even in OECD and European countries.<sup>14</sup> In addition, most countries also allow traders not to register as taxable persons as long as they are below the VAT threshold.<sup>15</sup> This is not only because of compliance costs, but also in the commercial interest of those who sell to registered taxable persons, as registered taxable persons allow them to recover the tax on their inputs, and the tax that would otherwise be charged on their outputs is recovered by registered traders.

It is necessary to make a policy comparison of the VAT threshold in some countries that have introduced indirect taxes on electronic services to consumers.

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<sup>10</sup> Emily Ann Satterthwaite, *Ibid.*

<sup>11</sup> Mesay M. Gebresilasse and Soule Sow, *Ibid.*

<sup>12</sup> *Loc.cit.*

<sup>13</sup> *Loc.cit.*

<sup>14</sup> *Loc.cit.*

<sup>15</sup> Liam P. Ebrill, Michael Keen, Jean-Paul Bodin and Victoria Summers, *The Modern VAT*, Washington: International Monetary Fund, 2001, p. 116.

By benchmarking or comparing with other countries and analysing them,<sup>16</sup> a comprehensive understanding of the ideal VAT threshold policy in the digitalisation era in Indonesia can be obtained in the future. The following table provides a brief overview of the thresholds and VAT rates applied in various countries.<sup>17</sup>

Table 1. a brief overview of the thresholds and VAT rates applied in various countries

Countries	Rate	Date	Threshold	IDR
Australia	10%	Jul 2017	AUD \$75,000 (Exchange rate on 3 May 2024 @Rp.10,584)	793.800.000,-
China	6%-13%	N/a	Nil	0
India	18%	Jul 2017	-	0
Indonesia	11%	Aug 2020	IDR 4,8 billion	4.800.000.000
Japan	10%	Oct 2015	JPY 10 million (Exchange rate on 22 April 2024 @Rp.104.82)	1.048.200.000
Malaysia	8%	Jan 2020	RM500,000 (Exchange rate on 22 April 2024 @Rp.3,398.32)	1.700.000.000
New Zealand	15%	Oct 2016	NZD 60,000 (Exchange rate on 22 April 2024 @Rp.9,585.66)	575.139.600
Philippines	12%	Jan 2024	P 3million (Exchange rate on 22 April 2024 @Rp.282.35)	847.050.000
Singapore	9%	Jan 2020	S\$100,000 (Exchange rate on 22 April 2024 @Rp.11,910.35)	1.200.000.000
Switzerland			CHF100,000 (Kurs tanggal 22 April 2024 @Rp.10.440,15)	1.044.015.000
South Korea	10%	Jul 2015	Nil	0
Taiwan	5%	May 2017	NTD 480,000 (approx \$15,250) (Exchange rate on 22 April 2024 @Rp.496.94)	238.531.200

<sup>16</sup> Kusumaningtuti SS, *Peranan Hukum dalam Penyelesaian Krisis Perbankan di Indonesia*, Jakarta: Rajawali Pers, 2009.

<sup>17</sup> Jacinta Caragher, "Digital Services Taxes DST – global tracker", 11 April 2024, available at <https://www.vatcalc.com/global/digital-services-taxes-dst-global-tracker/>, accessed on April 12, 2024.

Thailand	7%	Sep 2021	THB 1.8million annum (approx. €46,000) (Exchange rate 22 April 2024 @Rp.438.52)	789.336.000
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#### 4. Critical Review of VAT Thresholds in Indonesia

Three-quarters of the world's population live in countries that levy VAT on the sale of goods and services,<sup>18</sup> with a variety of threshold treatments. Based on a comparison of thresholds in several countries, Indonesia has the highest VAT threshold, including when compared to Singapore, Australia, Switzerland and Malaysia. Some countries, such as China and South Korea, do not even use a threshold in their VAT. This shows that the choice of threshold is an important element in the design of the VAT law. Setting the threshold too low can seriously jeopardise the political and administrative feasibility of VAT. It will also increase the concentration of VAT in a small number of taxpayers.<sup>19</sup> In addition, the limited administrative capacity in many countries supports the setting of a relatively high threshold, but often the tax authorities in charge are not convinced of the benefits of such a relatively high threshold approach. Often without full justification, many argue and believe that high thresholds can significantly reduce tax revenues to the state as well as the perception of unfair competition among taxpayers.<sup>20</sup>

It is recognised that the debate on VAT in developing countries still lacks attention to the beneficial role of VAT threshold changes in the context of the neutrality principle.<sup>21</sup> Indeed, the policy of changing the VAT threshold should be able to offset the loss of VAT revenue due to changes in VAT rates, as the VAT threshold plays an important role in the design of revenue-neutral tax reforms.<sup>22</sup>

Given the potential importance of below-the-limit treatment in terms of VAT registration, for the development of compliance capacity, and the importance of considering the tax competitive position of taxpayers as well as between countries, a simple tax policy and VAT threshold should have an impact on VAT revenue without neglecting the principle of neutrality. The principle of neutrality in VAT refers to taxation that should be neutral unless there are compelling reasons for it to be so - for example, VAT is not intended to change the relative preference between two consumer goods and is not intended to change the relative value of marginal productivity between two inputs. With regard to the threshold in VAT, the threshold norm can be said to be quite neutral if, based on the invoicing system with the credit method in the VAT Act, the PKP must be actively involved and the administration has been carried out correctly, considering that the VAT paid by the PKP buyer is VAT that is calculated with the output tax with the credit mechanism. In addition, the ideal VAT threshold policy should also consider the possibility of tax administration focusing on significant core taxpayers.

<sup>18</sup> Emily Ann Satterthwaite, *Ibid.*

<sup>19</sup> Liam P. Ebrill, Michael Keen, Jean-Paul Bodin and Victoria Summers, *Op.cit.*, p. 123.

<sup>20</sup> *Loc.cit.*

<sup>21</sup> Lourenço S. Paz, The welfare impacts of a revenue-neutral switch from tariffs to VAT with intermediate inputs and a VAT threshold, *The Journal of International Trade & Economic Development*, Vol. 24, No. 4, 2015, pp. 465-498, DOI: 10.1080/09638199.2014.924652.

<sup>22</sup> *Loc.cit.*

### C. CONCLUSION

Based on the background, analysis and discussion, two conclusions are drawn. Firstly, the provisions governing the VAT threshold in Indonesia currently stipulate that the amount of gross turnover and/or gross income in a fiscal year must be at least IDR 4.8 billion. This provision has undergone several changes since the enactment of the 1984 VAT Law. Second, the legal reconstruction of the VAT threshold in Indonesia will be carried out while still aligning with other VAT policies, such as the principle of neutrality, VAT rates, expansion of the VAT base, and consideration of benchmarking in several countries whose VAT collection systems are not very different from Indonesia. an example is Australia. It is recommended that there be a change in VAT policy on the threshold by not applying a threshold that is too high, as the threshold in Indonesia is currently Rp. 4.8 billion, while the World Bank suggests that Indonesia lower the threshold of PKP to Rp. 600 million and several developed countries that have a good VAT system have applied a VAT threshold that is not too high, such as Australia at AUD \$75,000, Malaysia at RM500,000, Singapore at S\$100,000 and Switzerland at CHF100,000.

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