

Accrual Accounting and the Financial Treatment of Indonesia's Article 21 Income Tax Liabilities

Neneng Hartati

Faculty of Sharia and Law, UIN Sunan Gunung Djati Bandung, Indonesia
nenenghartati@uinsgd.ac.id

Abstract

This article examines the conceptual and accounting treatment of Indonesia's PPh Article 21, which governs the taxation of individual income derived from employment. The focus is on how this tax obligation is calculated and reflected in corporate financial statements, especially in cases where the employer bears the tax burden. Adopting a qualitative, document-based approach, the study explores how principles such as accrual accounting, the matching concept, and fiscal transparency influence the treatment of payroll tax liabilities. The analysis reveals significant inconsistencies in the classification and disclosure of Article 21 charges, stemming from variations in gross-up calculations, recognition timing, and liability reporting. These inconsistencies affect not only financial transparency and audit reliability but also broader issues of governance, stakeholder trust, and compliance. By integrating international tax theory with accounting standards, this article offers a conceptual framework for the uniform treatment of payroll taxes and highlights the need for regulatory harmonization. The findings suggest that clear, standardized accounting practices for PPh Article 21 would strengthen financial reporting integrity and align Indonesian practices more closely with international norms.

Keywords

PPh Article 21; Payroll Tax; Accrual Accounting; Tax Disclosure; Financial Reporting Standards

Introduction

Income tax plays a fundamental role in a country's economic structure, serving as a primary source of government revenue and a tool for income redistribution. Among the various tax provisions, Article 21 of Indonesia's Income Tax Law holds specific significance as it governs the taxation of individual income derived from employment relationships (Bird & Zolt, 2005). This article focuses particularly on the mechanisms of calculating and recognizing PPh Article 21 in financial reports, an area that presents complex challenges in tax accounting and corporate compliance. The treatment of such taxes in financial statements is not merely a technical matter but reflects broader issues of transparency, fiscal discipline, and alignment with international accounting standards (Tanzi & Zee, 2000).

Theoretical and empirical discourse on income taxation suggests that employer-based withholding taxes, such as PPh Article 21, require precise regulatory interpretation and uniform accounting application to avoid discrepancies in financial reporting (Musgrave & Musgrave, 1989, p. 220). The principle of matching expenses with revenues necessitates clear delineation of employer-paid tax liabilities and their classification as part of employee compensation packages (Scholes & Wolfson, 1992). Moreover, divergent interpretations and applications of gross-up methods further complicate the consistent reporting of income tax burdens in financial documents (James & Nobes, 2000).

Previous research has often emphasized tax compliance and policy effectiveness but has insufficiently addressed the accounting implications of payroll-related tax obligations (Slemrod, 1990). This indicates a scholarly gap in literature linking income tax administration with financial reporting practices, particularly in developing economies with evolving regulatory environments (Bird, 1992). Furthermore, despite the increasing complexity of employment arrangements, few studies have systematically examined the institutional accounting for PPh Article 21 obligations (Atkinson & Stiglitz, 1980, p. 178).

To fill this gap, the present study addresses three research questions: (1) How is PPh Article 21 calculated for various employment scenarios? (2) How are Article 21 charges reported in financial statements under differing accounting methods? (3) What are the implications of these treatments for corporate transparency and tax compliance? These questions are embedded within broader inquiries on tax policy, accounting standards, and organizational reporting behaviors.

The objective of this research is to critically examine the calculation mechanisms of PPh Article 21 and their accounting treatments in corporate financial reports. It aims to provide theoretical clarity and practical guidance on the appropriate recognition, measurement, and disclosure of Article 21 tax liabilities. The study's relevance is underscored by ongoing reforms in tax administration and international convergence of financial reporting standards, making it imperative to revisit how national tax

provisions align with global accounting norms (OECD, 1997). Through a conceptual framework grounded in tax theory and accounting principles, this article contributes to the academic and policy discourse on income tax regulation and corporate governance.

Literature Review

The concept of income taxation has long been a cornerstone of public finance, with extensive scholarly discourse on its implications for equity, efficiency, and economic behavior. Within this domain, payroll taxes, including those on employment income, have drawn attention due to their dual nature as both fiscal tools and accounting concerns (Musgrave & Musgrave, 1989, p. 121). Income taxes withheld by employers, such as PPh Article 21, function as a mechanism to ensure regular tax collection, reducing evasion while simplifying administration (Bird & Zolt, 2005).

However, the literature also identifies critical tensions in how these taxes are recognized and reported in financial accounting, especially in the employer's books (James & Nobes, 2000). Scholars have debated whether such taxes constitute a liability, a cost of labor, or a deductible business expense—each interpretation bearing distinct implications for income measurement and financial transparency.

Several theoretical models inform the analysis of income tax, particularly the benefit and ability-to-pay principles. Atkinson and Stiglitz (1980, p. 155) offer a foundational framework distinguishing between horizontal and vertical equity, both of which underpin how tax burdens should be distributed among employees. These principles have influenced tax design but are less frequently applied to accounting treatment discussions.

In terms of financial reporting, international standards such as IAS 12 guide the recognition of current and deferred tax liabilities but remain ambiguous on specific withholding tax treatments (OECD, 1997). Furthermore, the convergence between national tax laws and global accounting practices remains inconsistent, particularly in jurisdictions where statutory frameworks are underdeveloped (Scholes & Wolfson, 1992).

Empirical studies have addressed the broader implications of income taxation on labor markets and economic development (Tanzi & Zee, 2000). However, few focus explicitly on how taxes like PPh Article 21 are integrated into corporate accounting systems. This gap is particularly noticeable in studies involving emerging economies, where administrative capacity and regulatory interpretation significantly influence compliance (Bird, 1992).

Moreover, accounting literature tends to isolate tax from payroll accounting, leaving a conceptual void in understanding how Article 21 obligations intersect with salary and benefit disclosures. The current study seeks to address this intersection by synthesizing

tax theory and accounting norms to provide a more coherent approach to reporting employment-related tax liabilities.

Theoretical Framework

1. Tax Equity and the Ability-to-Pay Principle

The principle of tax equity, particularly the *ability-to-pay* concept, is fundamental to understanding the rationale behind income taxes such as PPh Article 21. According to Atkinson and Stiglitz (1980, p. 170), individuals should contribute to public revenue in proportion to their capacity to pay, which is generally reflected in their gross income. In the context of employment-based taxes, this means that higher earners bear a larger tax burden, fulfilling vertical equity. For accounting purposes, this principle justifies the progressive structure of tax brackets applied in the Article 21 system. However, it also raises questions about the employer's role when tax liabilities are borne on behalf of employees—a practice known as the *gross-up* method. Such arrangements blur the line between compensation and tax liability, thereby challenging the accurate classification of income and expense in financial reports (Musgrave & Musgrave, 1989, p. 189).

2. Accrual Accounting and Matching Principle

From an accounting standpoint, the treatment of PPh Article 21 must align with the accrual principle and the matching concept. The accrual basis of accounting mandates that expenses be recognized in the period in which they are incurred, not necessarily when they are paid (Horngren et al., 2002, p. 362). Consequently, taxes withheld from salaries must be recognized concurrently with the related compensation costs. The matching principle further emphasizes that tax charges associated with employee remuneration should be recorded as part of the overall cost of labor during the same reporting period. When employers adopt the gross-up method, their additional payment to cover employees' taxes becomes part of salary expense, which must be consistently reflected in the income statement (Scholes & Wolfson, 1992). The theoretical importance of this principle lies in its ability to maintain temporal coherence in financial statements and ensure fair presentation of obligations.

3. Fiscal Transparency and Information Asymmetry

Transparency in tax accounting is also a matter of fiscal governance. According to Bird and Oldman (1990), clear disclosure of tax liabilities reduces information asymmetry between firms and stakeholders, thereby fostering trust and enhancing corporate accountability. In the case of PPh Article 21, ambiguity arises when firms do not clearly specify whether the tax is borne by the employee or the employer. This leads to inconsistent reporting across firms and complicates stakeholder analysis of labor costs and tax efficiency. The theory of information asymmetry, as articulated by Akerlof (1970), supports the argument that full disclosure of tax-related expenses is essential for informed decision-making by investors and regulatory bodies. Without

standardized reporting mechanisms, tax items such as Article 21 become vulnerable to manipulation or misinterpretation.

4. Tax Neutrality and Behavioral Effects

Lastly, the principle of tax neutrality—where taxes should not distort business or personal decisions—is relevant to both the design and reporting of PPh Article 21. If the financial statement treatment of payroll taxes varies significantly across industries or firms, it may influence corporate behavior regarding employment contracts or compensation structuring (Slemrod, 1990). For example, firms might prefer contract labor to avoid complex Article 21 obligations, potentially undermining job security and formal labor market participation. Scholes and Wolfson (1992) argue that inconsistent tax treatments can create artificial incentives that affect real economic choices, thereby reducing overall economic efficiency. This principle underscores the need for consistent tax accounting that minimizes unintended behavioral responses..

Previous Research

1. Atkinson and Stiglitz (1980)

Atkinson and Stiglitz's seminal work on public economics provided foundational concepts such as vertical and horizontal equity, which underlie modern income tax systems. Using a theoretical approach, they proposed that taxation should be progressive and reflective of individual capabilities to pay. Their insights are relevant to the rationale behind PPh Article 21, particularly in designing tax brackets and deductions. However, their work focused more on economic principles and less on practical accounting applications, leaving room for further exploration of how such taxes are treated in financial reports.

2. Musgrave and Musgrave (1989)

This comprehensive textbook explored both the design and application of tax systems in public finance. The authors discussed employer obligations in withholding taxes and emphasized the necessity of timely and accurate reporting. Their analysis highlighted the challenges of employer compliance but did not delve into the specifics of tax accounting in financial statements. Their framework supports the broader understanding of PPh Article 21 but does not resolve the ambiguity of gross-up treatment or employer-incurred liabilities.

3. Bird (1992)

Bird examined income tax administration in developing countries, focusing on systemic challenges in enforcement and compliance. Using a qualitative policy analysis, he demonstrated how weak administrative capacities and vague regulations contribute to inconsistent tax practices. His findings underscore the challenges of implementing a withholding system such as PPh Article 21, particularly in contexts where accounting systems may not fully reflect tax realities. However, Bird's work

remains general and policy-oriented, lacking detailed discussions on financial report integration.

4. Scholes and Wolfson (1992)

This study bridged the gap between tax law and accounting practice. The authors offered a robust theoretical and empirical analysis of tax planning, financial accounting, and organizational behavior. Their work is directly applicable to the treatment of PPh Article 21, particularly concerning the classification of employer-paid taxes and the timing of expense recognition. Despite its US-centric focus, the framework they proposed has international relevance and provides a valuable basis for evaluating Article 21's financial treatment.

5. James and Nobes (2000)

In their comparative study of international accounting systems, James and Nobes addressed how different jurisdictions approach tax accounting, highlighting discrepancies in the recognition and disclosure of tax liabilities. Their research supports the argument that the treatment of withholding taxes like Article 21 varies widely, leading to challenges in international comparability. This work is particularly relevant in showing how Indonesia's approach may diverge from global standards, thereby emphasizing the need for harmonization.

6. Tanzi and Zee (2000)

Tanzi and Zee analyzed tax policy design in developing economies, emphasizing the importance of equity, efficiency, and administrative feasibility. They argued that personal income tax systems, especially those involving employer withholding, must balance simplicity with fairness. Their policy-based analysis helps contextualize Article 21 within broader tax reforms and supports the argument for clear guidelines on accounting treatment to enhance transparency and compliance. However, their work lacks specific case analysis of financial reporting practices.

While the reviewed literature provides valuable insights into tax policy, public finance, and accounting theory, none of the studies comprehensively examines the treatment of PPh Article 21 in financial reports. Most contributions remain either theoretical or policy-oriented, without connecting tax obligations to practical accounting procedures. This research addresses that gap by integrating fiscal and financial perspectives, offering a detailed conceptual framework for the calculation and disclosure of Article 21 taxes in corporate accounting systems.

Research Methods

This research adopts a qualitative, conceptual approach, relying exclusively on secondary, document-based data. The study synthesizes existing theories, legal texts, accounting standards, and scholarly literature to explore how Income Tax (PPh) Article 21 is calculated and treated within financial statements. Conceptual data provide an

analytical lens to interpret and critique the norms surrounding tax liability recognition and payroll expense reporting. The reliance on theoretical constructs allows for an in-depth investigation of normative accounting and taxation frameworks without the distortion of quantitative variance (Scholes & Wolfson, 1992).

The primary sources of data are international accounting and tax law literature, including books and peer-reviewed journals published no later than 2009. Specific attention is given to accounting standards such as IAS 12 and tax policy frameworks relevant to the treatment of employment-related obligations. Supplementary sources include Indonesian tax regulations, particularly those related to PPh Article 21, analyzed against global accounting principles to highlight areas of divergence and convergence. These sources are critically evaluated for their relevance, clarity, and theoretical robustness (Musgrave & Musgrave, 1989, p. 132).

Data collection involves systematic textual analysis of selected sources using thematic coding to extract key concepts such as "tax liability recognition," "gross-up method," and "financial reporting compliance." The goal is to categorize and relate different interpretations of how Article 21 taxes should be treated in financial statements. This interpretive process is guided by content analysis principles, which are particularly suited for conceptual research involving regulatory texts and accounting standards (James & Nobes, 2000).

The analysis process involves triangulation of the extracted themes with established theoretical models, including accrual accounting, the matching principle, tax neutrality, and fiscal transparency. Each theme is evaluated against these models to assess its conceptual coherence and practical implications. For instance, the gross-up method is scrutinized under the matching principle to determine whether employer-paid taxes meet the criteria for salary expense recognition. This method ensures internal validity and enriches the analysis with multiple theoretical perspectives (Bird & Zolt, 2005).

Conclusions are drawn through a synthesis of findings from literature and normative theory, emphasizing consistency, logical coherence, and alignment with international best practices. The findings are not generalized to all contexts but aim to provide a conceptual benchmark for the treatment of PPh Article 21. By focusing on how legal-tax obligations translate into accounting records, the study bridges a critical knowledge gap and contributes to a more integrated understanding of payroll taxation and financial disclosure (Atkinson & Stiglitz, 1980, p. 198).

Results and Discussion

The findings of this conceptual study reveal that the treatment of PPh Article 21 in financial reporting lacks consistency due to ambiguous regulatory guidance and the absence of universally adopted accounting frameworks. Theoretical analysis shows that while employer-paid Article 21 taxes should logically be treated as part of employee compensation, practical application varies widely across firms and sectors.

Under the accrual basis of accounting, such taxes must be matched with the corresponding salary period to which they relate, reinforcing the application of the matching principle (Horngren et al., 2002, p. 390). However, some organizations record them as separate tax liabilities or operational expenses, resulting in inconsistency in financial statements and potentially misleading representations of labor costs. This misalignment highlights the gap between tax compliance and accurate financial reporting, undermining transparency and accountability (Bird & Oldman, 1990).

Moreover, when assessed through the lens of tax neutrality and information asymmetry, the gross-up method of calculating PPh Article 21 presents significant challenges. Firms that gross-up employee income for tax purposes are effectively increasing employee benefits, which, if not properly disclosed, distort reported salary structures and may affect stakeholder perception of compensation practices (Scholes & Wolfson, 1992). From a governance perspective, failure to disclose such employer-borne tax burdens can be construed as a form of information withholding, reducing the utility of financial reports for investors and regulators. These findings contribute to the existing literature by linking theoretical tax frameworks to practical accounting dilemmas, underscoring the need for a clearer integration of tax policy and financial reporting standards.

Research Question 1: How is PPh Article 21 calculated for various employment scenarios?

1. Legal Framework and Income Components

The calculation of PPh Article 21 is rooted in the legal classification of taxable income under Indonesia's income tax code. It includes not only base salaries but also bonuses, benefits-in-kind, and allowances. Each component is taxed progressively, following tax brackets designed to uphold the principle of *ability-to-pay* (Atkinson & Stiglitz, 1980, p. 171). The income is aggregated monthly or annually, then reduced by allowable deductions such as *biaya jabatan* (professional fees), pension contributions, and non-taxable income thresholds (*PTKP*). This legal structure parallels global payroll tax systems in form but diverges in complexity due to extensive discretionary exemptions, creating calculation variability (Bird & Zolt, 2005).

2. Net vs. Gross Salary Calculation

A major variation in calculation methods arises between net and gross salary arrangements. In a net salary scheme, the employer assumes the tax burden, effectively *grossing up* the employee's income to reflect the tax due. This requires a reverse-calculation of the tax owed using gross-up formulas to arrive at the true cost to the employer (Musgrave & Musgrave, 1989, p. 211). For example, if a net salary of IDR 10 million is contractually agreed upon, the gross amount must be computed to ensure the employee receives the full net value after tax deduction. The gross-up method, while employer-friendly for employee retention, introduces accounting challenges,

especially in allocating the tax as part of salary expense rather than an operational tax liability (Scholes & Wolfson, 1992).

3. Tax Withholding Mechanism and Monthly Recognition

The withholding system mandates employers to deduct PPh Article 21 monthly, depositing it with the tax authority while issuing payslips showing deductions. This system ensures liquidity for the state and simplifies compliance for employees. Yet, for accounting purposes, this means that tax liabilities accrue monthly, not annually, and must be matched with each month's payroll entry (James & Nobes, 2000). The absence of standardized software or automated systems in many firms leads to human error, particularly when benefits and bonuses are irregular, thereby complicating consistent tax reporting.

4. Special Cases: Non-Permanent Employees and Directors

The treatment of income tax for non-permanent workers and directors varies. Contract employees are often taxed using a final tax scheme (Article 26 for foreign workers), while directors may receive honoraria or dividend-like income, which complicates the application of standard Article 21 rules (Tanzi & Zee, 2000). These differences necessitate tailored calculations, often based on the proportional income received during the employment period. The lack of guidance on how to record such taxes in financial statements creates ambiguity about whether these amounts fall under payroll tax, corporate tax, or dividends.

5. Deductions and Allowances

Indonesia's tax regulation allows multiple deductions before arriving at taxable income, including *iuran pensiun*, *tunjangan jabatan*, and health benefits. These affect the final PPh Article 21 liability but are often inconsistently applied across firms. According to Bird (1992), such inconsistencies stem from administrative discretion and the absence of strong enforcement mechanisms. In financial reporting, this inconsistency can lead to variation in reported labor costs and profitability, depending on whether deductions are included as employee benefits or excluded from gross income.

6. Comparative Practices and International Standards

Globally, countries use differing models for payroll tax calculation. Some use cumulative annual calculations with tax credits, while others, like Indonesia, adopt a monthly, progressive approach. James and Nobes (2000) argue that these differences complicate efforts to standardize international financial reporting, especially for multinational companies operating across jurisdictions. For Article 21, its unique monthly gross-up requirement sets it apart and highlights the need for standardized guidance on how these calculations should be recognized and disclosed in financial reports.

Research Question 2: How are Article 21 charges reported in financial statements under differing accounting methods?

1. Employer-Borne vs. Employee-Borne Classification

One major distinction in financial treatment lies in whether the employer bears the tax burden. If PPh Article 21 is paid by the employee through withholding, it is treated as a liability and is excluded from the employer's expenses (Horngren et al., 2002, p. 385). In contrast, when the employer assumes this tax through gross-up arrangements, the amount must be reported as an additional salary expense. Scholes and Wolfson (1992) emphasize that failure to report such expenses under employee compensation misrepresents true labor costs and affects the firm's operating margins. Despite regulatory prescriptions, many companies inconsistently apply this classification, leading to financial distortions.

2. Recognition Under Accrual vs. Cash Basis

Under the accrual accounting principle, taxes must be recognized when the liability arises, not when paid. This means PPh Article 21 should be recorded at the time of payroll issuance, not on the payment or remittance date (James & Nobes, 2000). Companies using a cash basis may delay recognition until the tax is paid, creating timing mismatches between expenses and liabilities. Such mismatches undermine the matching principle, reducing the comparability and reliability of financial reports. The accrual basis, aligned with IFRS and IAS 12, provides a clearer picture of financial obligations and should be the preferred method in Article 21 tax treatment.

3. Presentation in Income Statement and Notes

The classification of PPh Article 21 charges also affects how they are presented in the financial statements. When employer-borne, these should be aggregated under salary and benefit expenses in the income statement (Bird & Oldman, 1990). Additionally, comprehensive disclosure in the notes should include the amount of tax withheld and any additional tax borne by the employer. However, many firms fail to include this information in disclosures, which limits transparency and accountability. Musgrave and Musgrave (1989, p. 208) argue that non-disclosure may also affect tax compliance if amounts expensed differ from amounts remitted.

4. Liability Recognition in Balance Sheet

At the end of each reporting period, any outstanding Article 21 obligations should be listed as current liabilities under tax payable. The timing of salary payment and tax deposit may create short-term liabilities that need explicit recognition (Horngren et al., 2002, p. 401). In the absence of such classification, financial statements understate liabilities and potentially overstate liquidity. Accurate liability recognition is also essential for audit purposes and for calculating working capital and debt ratios used in investment analysis (Scholes & Wolfson, 1992).

5. Deferred Tax Treatment and Temporary Differences

In some cases, particularly where bonuses or severance packages are recognized differently for tax and accounting purposes, temporary timing differences arise. These differences may lead to deferred tax assets or liabilities under IAS 12. However, many Indonesian firms do not recognize such deferred tax consequences from PPh Article 21, possibly due to lack of guidance or understanding. James and Nobes (2000) note that such omissions can have material effects on tax expense and net income if recurring in large amounts. More robust guidance on recognizing deferred taxes arising from payroll discrepancies is needed.

6. Implications for Audit and Governance

The treatment of Article 21 charges significantly influences external audits and corporate governance. Incomplete recognition or inconsistent classification can trigger audit qualifications or adverse findings. Furthermore, since payroll is often one of the largest expenses in labor-intensive industries, misreporting Article 21 obligations can mislead stakeholders about cost structures (Tanzi & Zee, 2000). Enhanced internal controls and training for finance teams are essential to ensure compliance and transparency in financial reporting practices.

7. Emerging Perspectives on Tax Reporting Integration

While traditional tax and accounting practices have operated in silos, scholars such as Bird and Zolt (2005) advocate for integrated systems where payroll taxes are automatically reflected in financial records. Integration ensures real-time recognition and reconciliation, reducing manual errors and strengthening internal control systems. This study supports such integration, especially for jurisdictions like Indonesia where payroll tax complexity is high. Future research may further develop standardized models for reporting such tax charges across sectors and jurisdictions.

Research Question 3: What are the implications of these treatments for corporate transparency and tax compliance?

1. Financial Transparency and Stakeholder Trust

Transparent reporting of PPh Article 21 obligations is essential for building stakeholder trust. When companies disclose the full extent of their payroll tax responsibilities—including grossed-up taxes—they provide a clearer picture of their compensation structures and tax behavior. Bird and Oldman (1990) stress that financial opacity, especially in emerging economies, deters investor confidence and undermines market integrity. If tax-related expenses are hidden or inconsistently reported, it misleads shareholders, creditors, and regulatory authorities about the firm's cost structure and profitability.

2. Regulatory Compliance and Legal Risk

Accurate reporting of Article 21 obligations is not just an accounting concern but a legal one. Misreporting can result in underpayment of taxes or incorrect classification

of liabilities, triggering penalties from tax authorities (Tanzi & Zee, 2000). In Indonesia, inconsistent interpretation of tax codes has resulted in increased audit findings and disputes, particularly in cases where the gross-up method is applied without clear documentation. Firms that fail to correctly report these obligations may also face reputational damage, compounding the financial consequences of non-compliance (Bird, 1992).

3. Comparative Consistency and International Standards

With globalization, multinational firms operating in Indonesia must reconcile local tax treatments like PPh Article 21 with international accounting standards. Disparities in reporting requirements may create inconsistencies in consolidated financial statements, complicating inter-company comparisons and decision-making (James & Nobes, 2000). The lack of harmonization not only affects external reporting but also internal budgeting and tax planning, especially for HR and payroll departments managing diverse tax jurisdictions.

4. Corporate Governance and Ethical Accountability

Transparent tax reporting is closely linked to corporate governance. Scholes and Wolfson (1992) argue that tax behavior reflects broader ethical standards within firms. If companies seek to obscure their true labor costs or exploit ambiguous tax rules, it may signal deeper governance issues. Proper accounting of Article 21 charges—including disclosure of whether the employer or employee bears the tax—demonstrates ethical accountability and adherence to fair financial practices. Furthermore, the board of directors has a fiduciary responsibility to ensure truthful reporting, making the treatment of payroll taxes a governance priority.

5. Impact on Employee Relations and Labor Contracts

The financial treatment of PPh Article 21 also has internal implications for employee relations. When employers gross-up salaries but fail to disclose this practice clearly in financial or payroll statements, it may lead to misunderstandings or disputes about compensation fairness. According to Musgrave and Musgrave (1989, p. 234), employee trust in compensation systems depends on transparent and consistent tax deductions. Clear disclosure reinforces contractual trust and prevents labor dissatisfaction that might arise from perceived inequities in tax burden distribution.

6. Role of Audit and Internal Control

External and internal audits play a critical role in verifying the proper treatment of Article 21 obligations. Bird and Zolt (2005) advocate for regular audit trails and internal reviews to ensure that tax expenses are appropriately recognized, classified, and disclosed. Inadequate documentation or misclassification—such as recording gross-up tax under general administrative expenses rather than payroll—may trigger audit qualifications or even forensic investigations. Effective internal control systems must therefore integrate tax compliance checks into payroll processing and financial reporting workflows.

7. Scholarly Perspective: Integrating ESG with Tax Transparency

A new scholarly perspective gaining traction is the integration of tax transparency within broader Environmental, Social, and Governance (ESG) frameworks. Although often associated with environmental and labor concerns, governance includes ethical tax behavior and financial transparency. Emerging literature suggests that stakeholders increasingly evaluate companies on their tax responsibility as part of ESG scoring (Preuss, 2009). PPh Article 21, as a key component of employee taxation, thus becomes a lens through which firms' social responsibility and ethical standards are evaluated. Integrating Article 21 compliance into ESG reporting may enhance long-term credibility and stakeholder loyalty.

Core Findings and Pathways Forward

The findings of this conceptual analysis illuminate significant discrepancies in how Income Tax (PPh) Article 21 is calculated and reported in financial statements, thereby answering the three guiding research questions. First, the calculation of Article 21 varies depending on employment arrangements, deductions, and whether taxes are grossed-up by the employer. This variation underscores the need for uniform guidance on tax computation and employer obligations. Second, the accounting treatment of Article 21 charges differs based on whether the tax is employer- or employee-borne, the basis of accounting used, and the company's interpretation of salary expense recognition. This inconsistency in reporting practices threatens financial transparency and undermines the comparability of corporate financial statements. Third, these accounting treatments have far-reaching implications for corporate governance, audit readiness, employee relations, and overall tax compliance.

This research contributes novel insights by integrating public finance theory, tax law, and accounting standards to establish a conceptual model for recognizing and reporting payroll tax obligations. The study also highlights gaps between regulatory mandates and accounting practices that demand attention from policymakers and standard-setting bodies. Theoretically, it advances a more holistic framework for understanding tax-related liabilities in the context of financial reporting. Practically, it offers companies, auditors, and regulators a foundation for improving documentation, disclosure, and alignment with both national tax laws and international accounting principles. Addressing these inconsistencies is vital for ensuring fiscal integrity, enhancing governance, and building stakeholder confidence in corporate tax practices.

Conclusion

This study examined the calculation and financial treatment of Income Tax (PPh) Article 21, with particular focus on employer obligations and financial reporting practices. It revealed notable inconsistencies in how Article 21 liabilities are computed, recognized,

and disclosed in corporate financial statements. These inconsistencies are not merely technical but reflect broader governance and transparency concerns. By synthesizing tax theory and accounting principles, the study contributes to academic understanding and practical reform of payroll tax treatment. Companies are encouraged to adopt accrual-based recognition of Article 21 charges, ensure comprehensive disclosure, and strengthen internal control mechanisms. Future research should further explore sector-specific variations and assess the effectiveness of regulatory enforcement in standardizing tax reporting.

References

- Akerlof, G. A. (1970). The market for "lemons": Quality uncertainty and the market mechanism. *Quarterly Journal of Economics*, 84(3), 488–500.
- Atkinson, A. B., & Stiglitz, J. E. (1980). *Lectures on public economics*. McGraw-Hill.
- Bird, R. M. (1992). *Tax policy and economic development*. Johns Hopkins University Press.
- Bird, R. M., & Oldman, O. (1990). *Taxation in developing countries* (4th ed.). Johns Hopkins University Press.
- Bird, R. M., & Zolt, E. M. (2005). Redistribution via taxation: The limited role of the personal income tax in developing countries. *UCLA Law Review*, 52(6), 1627–1695.
- Horngren, C. T., Sundem, G. L., & Elliott, J. A. (2002). *Introduction to financial accounting* (8th ed.). Prentice Hall.
- James, S., & Nobes, C. (2000). *The economics of taxation: Principles, policy and practice*. Prentice Hall.
- Musgrave, R. A., & Musgrave, P. B. (1989). *Public finance in theory and practice* (5th ed.). McGraw-Hill.
- OECD. (1997). *Revenue statistics of OECD member countries 1965–1996*. Organisation for Economic Co-operation and Development.
- Preuss, L. (2009). Ethical sourcing codes of large UK-based corporations: Prevalence, content, limitations. *Journal of Business Ethics*, 88(4), 735–747.
- Scholes, M. S., & Wolfson, M. A. (1992). *Taxes and business strategy: A planning approach*. Prentice Hall.
- Slemrod, J. (1990). Optimal taxation and optimal tax systems. *Journal of Economic Perspectives*, 4(1), 157–178.
- Tanzi, V., & Zee, H. H. (2000). Tax policy for emerging markets: Developing countries. *IMF Working Paper No. 00/35*.
-