



INDONESIAN TAX REFORMS POLICY ALTERNATIVES FOR HANDLING SHADOW ECONOMY

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ABSTRACT

The background of this study is that from 2022 to 2017, there was a significant burden increase in the Directorate General of Taxes (DGT)' system covering taxpayers, employees, and offices. To prevent more tax avoidance as one of the shadow economy activities, DGT should reform its human resources, information, and technology (IT), standard operating procedures (SOP), and tax policies. Using a multi-goal analysis framework, the author will choose the best reform policies by assessing service, easiness, modernness, and professionalism criteria. The author found that updating IT and SOP will improve the quality of taxpayers' services to aim for better compliance.

Latar belakang penelitian ini adalah sejak tahun 2022 hingga tahun 2017 terjadi peningkatan beban yang signifikan pada sistem Direktorat Jenderal Pajak (DJP) yang meliputi wajib pajak, pegawai, dan perkantoran. Untuk mencegah semakin maraknya penghindaran pajak sebagai salah satu kegiatan *shadow economy*, DJP perlu mereformasi sumber daya manusia, teknologi dan informasi (TI), *standard of procedures* (SoP), dan kebijakan perpajakan secara efektif dan efisien. Dengan menggunakan *multi-goal analysis framework*, penulis akan memilih kebijakan reformasi terbaik dengan menilai kriteria seperti pelayanan, kemudahan, kemodernan, dan profesionalisme. Penulis menemukan bahwa pemutakhiran TI dan SoP akan meningkatkan kualitas layanan wajib pajak untuk mencapai kepatuhan yang lebih baik.

1. INTRODUCTION

A shadow economy is an undetected economic activity in which the perpetrators only focus on personal gain by ignoring applicable laws (Wibowo and Indrayanti, 2020). Many governments use Gross Domestic Product (GDP) to estimate the severity of the shadow economy. In ASEAN, 2004-2015, the average percentage was 30% of the GDP. While among 24 selected Asian countries, from 2002-2015, the average percentage was 33.8%. Unfortunately, the GDP itself could not describe the whole economy's activities.

To reduce the amount and growth of the shadow economy, the government should improve its effectiveness through institutional reforms (Wibowo and Indrayanti, 2020). Indonesian Directorate General of Taxes (DGT) developed their tax system to solve tax avoidance and evasion as one of the shadow economy activities. Therefore, they are reforming their human resource, information and technology (IT), process business or Standard Operating Procedure (SOP), and policies. Unluckily, many goals should be accomplished with limited resources.

The question in this study is, "How can DGT run tax reform effectively and efficiently?" The author learned the importance of multiple streams (views) from Tunstall et al. (2016) to set an agenda (policy). Then, the author used the policy analysis method from Weimer and Vining (2017), covering problem and solution analysis by considering many goals and criteria. As a result, the author suggests that DGT prioritize the improvement of IT and SOP to improve taxpayers' service for better tax compliance.

2. LITERATURE REVIEW

Tax avoidance: A shadow economy activity

Smith (1994) in Wibowo and Indrayanti (2020) defines the Shadow economy as producing goods and services based on market prices legally and illegally but not recorded or reported in GDP calculation. People and businesses are more incentivized to avoid high taxes. Berdiev et al. (2015) emphasize that high capital tax rates may increase production costs in the formal sector, thereby incentivizing individuals to migrate to the informal one. Therefore, the tax burden leads to the cause of the shadow economy (Huynh and Nguyen, 2019).

Issue 1: Human resource

Berdiev et al. (2015) argued that economic development with a quality institution and human capital accumulation could reduce the size of the shadow economy. The improvement should be started with recruitment (Wibowo and Indrayanti, 2020) similarly argued for improving government effectiveness by recruiting the best human resources. This issue is relevant to Indonesia's vision to be a developed country in 2045 (Figure 1), requiring high-quality human resources aiming more productive economic structure to achieve a GDP of \$29,300

income per capita (Ministry of Finance of Indonesia, 2021).

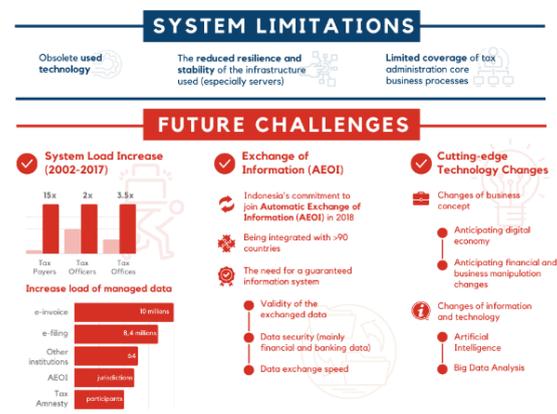
Figure 1 Indonesia 2045 Vision
Source: Ministry of Finance of Indonesia (2021)



Issue 2: Information and technology (IT)

One of the indicators of high-quality human resources can utilize IT. However, based on the World Economic Forum's study, Indonesia needs to improve its competitiveness due to weak technology development policies to increase productivity (Wibowo and Indrayanti, 2020). In the DGT case, the tax officer should manage enormous amounts of taxpayer data. From 2002 to 2017, there was a 15 times increase in the number of taxpayers. Unfortunately, the current DGT systems are outdated, and the process business is unintegrated. Moreover, there are taxpayers' offshore assets that made DGT should collaborate with other tax authorities. Luckily, since 2018, DGT and other tax authorities have been facilitated by G20-Global Forum to exchange tax information. This initiative aims to prevent technological crime activities that cause severe threats to organizations, including the public sector (Remeikiene et al., 2018)

Figure 2 DGT's System Challenges
Source: Ministry of Finance of Indonesia (2021)



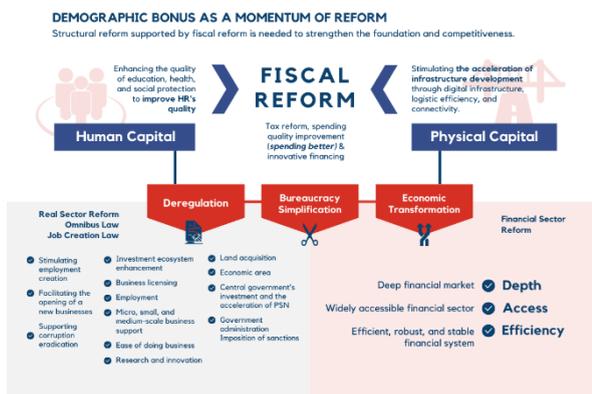
Issue 3: Business processes

IT and business processes cannot be separated. DGT aimed to use the Commercial Off The Shelf system to improve internal applications for better service, including registration, payment, assistance, and supervision and based on the Minister of Finance Decree No. 360/KMK.03/2017 concerning Tax Reforms,

reforming business processes is the initial solution before making new regulations. Moreover, bureaucracy simplification and deregulation as part of the fiscal reformation are essential for better collecting and redistributing revenues among citizens. Figure 3 shows that both are expected to increase employment, improve business efficiency, combat corruption, and maintain good governance.

Figure 3 Fiscal Reform

Source: Ministry of Finance of Indonesia (2021)



Issue 4: Regulations

The collaboration between the government and the people should be maintained before the violation of the legal norms, such as tax avoidance or evasion, happen to earn economic benefits (Remeikiene et al., 2018). Because of that, the author analyzes the most effective and efficient way for DGT to reform the tax system to keep taxpayers compliant by analyzing available alternative policy alternatives considering human resources, IT, business processes, and regulations.

Multiple stream theory

Tunstall et al. (2016) explained that the multiple streams theory of policy alternatives covers three conceptual streams. The first one identifies the policy actors, focusing on events that attract public attention and evaluation from existing programs. In this study, the policy actor is DGT, who wants to improve the tax compliance of taxpayers, which decreases because of their tax avoidance or evasion. Meanwhile, the current system cannot solve the problem, showing ineffective and inefficient public services.

Then the second is recognizing the policy stream that focuses on the technical feasibility of the policies that can be implemented. There are many considerations here, such as whether the policy can achieve the goal and whether the resources are available. Every DGT's tax reform policies covering human resources, IT, business processes, and regulations have each consequence of supporting tax compliance. Therefore, policy prioritizing is the research method in this study.

Last, the political stream will complement whole streams because it contains the degree of support or resistance to the policies. Every political thing is about maintaining the interests. DGT should collect revenue for the state budget; meanwhile, taxpayers want to

keep their income. For this reason, the tax reform will improve the effectiveness and efficiency of DGT in helping taxpayers to fulfill their obligations.

3. RESEARCH METHOD

When it was started in early 2022, the data for this study was the facts of DGT's reform preparation covering the reform background, goals, policies, regulations, team, and benefits. The author learned multiple goals and policies as the challenges in running a tax reform in multi years. To holistically see the tax reform policy, the author referred to Weimer and Vining's two-step policy analysis (2017), covering the problem and solution analyses. The problem analysis covers assessing the symptoms, framing and modeling the problem, and choosing the goals and a solution method. Meanwhile, the solution analysis covers choosing the impact categories for goals, valuing policy alternatives, assessing, and recommending.

4. ANALYSIS

Problem analysis

Assessing symptoms is about determining the empirical basis. DGT's data stated that the 2002-2017 system burden increased, including 150% of taxpayers, 200% of employees, and 350% of offices. With more taxpayers, more potential tax avoidance should be handled. Meanwhile, tax officers need more valid taxpayer data to analyze their fulfillment of tax obligations. The current system is not suitable anymore to pursue voluntary compliance.

This case is framed as a government failure in bureaucracy and needs a reform agenda. Currently, DGT needs more effective and efficient resources to perform better. Therefore, DGT's tax reform focuses on improving human resources, IT, business processes, and policies. The more complicated the tax avoidance or evasion as shadow economy activities, the more complex the tax reform should be. On the other hand, DGT has limited resources in people, budget, and technology to run the reform.

In every reform, many stakeholders' views should be considered. Taxpayers got full attention as the main DGT stakeholder in the current tax reform. DGT aims to maintain taxpayers' trust and increase compliance through a more reliable tax system. Besides, the reform can boost tax officers' integrity and strengthen coordination with other institutions.

Because of those goals, the fittest method to decide the best recommendation to prioritize tax reform policies is using multiple-goal analysis. As mentioned earlier in the research method, there are impact categories to analyze whether the reform policies can pursue the goals. More technical ways will be in the solution analysis.

Solution analysis

First, to measure whether the current tax reform is on track to pursuing its goals, the author determined some impact categories with each concern:

1. Service: How could the reform policy alternatives be helpful for taxpayers?
2. Easiness: How could the reform policy alternatives make taxpayers comfortable fulfilling tax obligations?
3. Modernness: How could the reform policy alternatives could update the tax system?
4. Professionalism: How could the reform policy alternatives maintain tax officers' skills and integrity?

Then, because the reform policy alternatives should be mutually exclusive, the author determined these alternatives:

1. Providing training for tax officers
2. Updating the IT system
3. Advancing the SOP
4. Formalizing new regulations

The author gathered the goals, impacts, and policy alternatives in the multiple-goal framework in the Appendix. There are qualitative assessments to assess each policy alternative with grades "Low," "Medium," "High," and "Very High" with relevant analysis. For instance, the grade of service criteria for the training improvement policy is medium; meanwhile, the IT update policy is high. It is because the IT update policy is directly improving taxpayer service. On the other hand, the knowledge tax officers get from training should be adjusted to the current situation and depend on their position.

Policy recommendations

Based on the result of the multiple-goal framework, DGT is on track to pay attention to updating the IT policy because it got the most grade of "Very High." As mentioned earlier, IT issues covering outdated systems and unintegrated process businesses are the leading cause of tax reform. If DGT can solve both, they can manage and analyze big taxpayer data more effectively and efficiently.

Because updating the IT requires a high budget, advancing the SOP can be an alternative. This policy can create a more streamlined process to help tax officers monitor taxpayers' rights and obligations. A system called Compliance Risk Management will track compliance based on risk priority. Therefore, not only voluntary compliance but also tax fairness will happen among taxpayers.

Technically, DGT continues to run the tax reform with a dedicated team as planned in the regulation. Then, DGT should ensure the benchmarked global IT system can fit the local practice significantly to improve internal applications. Furthermore, DGT can utilize the new system to improve tax officers' skills by doing comparative studies with global tax authorities. Last, besides updating the IT system, DGT can keep advancing SOP by regularly evaluating it.

5. CONCLUSION

In this study, the author reviewed many goals of current tax reform to handle tax avoidance and evasion

as shadow economy activities. The author found that the success key to running the tax reform is prioritizing the policies to achieve mandated goals. The reform policies of updating the IT system and advancing the SOP got the most "Very High" grade, meaning these policies hit the impact categories of reform goals satisfactorily.

Those policies cannot stand alone without tax officers who implement them and taxpayers who fulfill their obligations. Therefore, it is essential to improve tax officers' skills and integrity to give better taxpayers service by fulfilling their rights to comply and formalizing proper regulations affecting them.

The limitation of this study is that the data is very limited in the preparation phase of current tax reform. The author plans to continue this study in the near time, especially to dig deep into the part of SOP with more room for improvement than IT with its modernness. Since we know which business process should be prioritized to get pay attention like this study, DGT can implement the result of tax reform more effectively and efficiently.

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APPENDIX

Policy Alternatives Assessment

Goals	Criteria	Policy Alternatives			
		Providing training for tax officers	Updating the IT system	Advancing the SOP	Formalizing new regulations
Maintaining taxpayers' trust	Service	<u>Medium</u> The skillful officers can assist taxpayers manually	<u>High</u> IT will run SOP more efficiently	<u>Very High</u> Specific processes will make taxpayers want to fulfill their obligation	<u>Low</u> Taxpayers need time and assistance to implement the new regulations.
Increasing taxpayers' compliance	Easiness	<u>Medium</u> Knowledgeable tax officers can remind taxpayers' obligation	<u>Very High</u> Online services will help taxpayers easier in fulfilling their obligation	<u>High</u> The streamlined SOP will keep taxpayers' rights and obligations in the right place.	<u>Low</u> New regulations potentially cause tax avoidance if they are rigid.
Making a more reliable tax system	Modernness	<u>High</u> An updated tax system needs well-trained tax officers	<u>Very High</u> An updated tax system will be more capable of gathering and analyzing big data.	<u>Medium</u> A better tax system will prevent wrong input, process, and output.	<u>Low</u> New regulations can directly or indirectly impact modernizing the tax system.
Boosting tax officers' skills and integrity	Professionalism	<u>Very High</u> Knowledgeable tax officers can be better at decision making	<u>Medium</u> A better human resource system can track tax officers' performance, working history, and relevant data for development purposes.	<u>High</u> Clear SOP will prevent tax officers from any fraud	<u>Low</u> Most tax regulations affect taxpayers, not the tax officers.