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CONTENTS

- 140 Editorial
Chris Evans
- 144 Corruption, complexity and tax evasion
Vito Tanzi
- 161 Corruption, taxation, and tax evasion
James Alm and Yongzheng Liu
- 190 Corruption, taxes and compliance
Anja Baum, Sanjeev Gupta, Elijah Kimani and Sampawende Jules Tapsoba
- 217 The impact of corruption on tax revenues, tax compliance and economic development: Prevailing trends and mitigation actions in Africa
Bernd Schlenther
- 243 Causes and consequences of corruption in tax administration: An Indonesian case study
Christine Tjen and Chris Evans
- 262 Tax and corruption: Is sunlight the best disinfectant? A New Zealand case study
Lisa Marriott
- 290 Tax corruption and private sector development in Vietnam
Ngoc Anh Nguyen, Quang Hung Doan and Binh Tran-Nam
- 312 Applying foreign anti-corruption law in the Chinese tax context: Conceptual difficulties and challenges
Nolan Sharkey and James Fraser

CONTENTS CONTINUED

- 333** Morality associated with fraud, corruption and tax evasion in South Africa
Boela (AP) Swanepoel and Jacolize Meiring
- 359** Addressing aggressive tax planning through mandatory corporate tax disclosures: An exploratory case study
Heidi Zummo, Bronwyn McCredie and Kerrie Sadiq

Causes and consequences of corruption in tax administration: An Indonesian case study

Christine Tjen¹ and Chris Evans²

Abstract

This article uses an Indonesian case study (the Gayus case) to explore critical issues in the relationship between tax and corruption. More particularly, it considers the causes and impact of corruption at tax administrative levels in Indonesia, and identifies and evaluates strategies the Indonesian revenue authority (the Directorate General of Taxation, or DGT) has adopted, or can adopt, to ensure opportunities for such corrupt activity are mitigated or eliminated. The article adopts a qualitative approach, utilising archival analysis supplemented by interviews and correspondence with key parties involved. After a broad introduction which outlines the nature, types and impact of corruption in revenue authorities, the article identifies the principles that typically underpin anti-corruption strategies in revenue authorities in developing countries, together with examples of some of the anti-corruption strategies employed. It then considers the nature of the corrupt activity exemplified by the Gayus case in Indonesia, how it arose, and how it came to light. This is followed by a consideration of the impact upon the organisation, how the DGT dealt with it and what changes came about as a result in terms of anti-corruption strategies subsequently adopted and now operating in the DGT. The article concludes with a section on the lessons learned and prospects for the future, both in Indonesia and elsewhere in the Asia-Pacific region.

Keywords: tax, tax administration, corruption, compliance

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1. INTRODUCTION

No society is immune from corruption,³ and within any society taxation plays a pivotal role in relation to such activity – which can be both positive and negative. Positively the tax system can provide the kind of regulatory framework and institutional foundations which can help to eradicate or constrain corrupt practices. On the negative side, corruption reduces tax compliance.⁴ Even perceptions of corruption, whether ‘grand’ or ‘petty’, seriously undermine taxpayers’ intention to report actual income.⁵

The relationship between tax and corruption is complex and it is also critical, and nowhere is this more the case than in the role a revenue authority plays in its administration of the tax system. A revenue authority acting with integrity, effectively and transparently administering the many facets of the system from taxpayer registration through to final tax collection and acquittal, will underpin good governance in any society. Conversely, where the revenue authority is distrusted, fails to carry out its duties in an impartial manner, and does not follow legal and socially accepted norms, then the social, economic and legal fabric will be fragile at best. ‘No tax is better than its administration, so tax administration matters – a lot’.⁶ And an essential objective of tax administration is to ensure the maximum possible compliance by taxpayers of all types with their taxation obligations. Unfortunately, in many developing countries, tax administration is ‘usually weak and characterised by extensive evasion, corruption and coercion. In many cases overall tax levels are low, and large sectors of the informal economy escape the tax net entirely’.⁷

As noted by the International Monetary Fund (IMF), ‘defining corruption in a comprehensive way is difficult both because corrupt behaviour varies and because it is generally concealed from public view’.⁸ The generally accepted definition adopted by the IMF – ‘the abuse of public office for private gain’ – is entirely relevant for the focus of this article, involving corruption in a revenue authority. It emphasises the point made by Søreide that ‘at its core, corruption is trade in decisions that should not be for sale’.⁹ That ‘trade’ can take a variety of forms and encompass a ‘range of acts, allocations and bargains....[including] “extortion”, “bribery”, “collusion” and “negligence”’.¹⁰

³ Transparency International, ‘Corruption Perceptions Index 2015’ <<http://www.transparency.org/cpi2015>>

⁴ James Alm, Jorge Martinez-Vazquez and Chandler McClellan, ‘Corruption and Firm Tax Evasion’ (2016) 124 *Journal of Economic Behavior and Organization* 146, 146.

⁵ Arifin Rosid, Chris Evans and Binh Tran-Nam, ‘Do Perceptions of Corruption Influence Personal Income Taxpayer Reporting Behaviour? Evidence from Indonesia’ (2016) 14(2) *eJournal of Tax Research* 387.

⁶ Roy Bahl and Richard Bird, ‘Tax Policy in Developing Countries: Looking Back – and Forward’ (2008) 61(2) *National Tax Journal* 279, 296.

⁷ Deborah Brautigam, ‘Introduction: Taxation and State-Building in Developing Countries’ in Deborah Brautigam, Odd-Helge Fjeldstad and Mick Moore (eds), *Taxation and State-Building in Developing Countries: Capacity and Consent* (Cambridge University Press, 2008) 1, 3.

⁸ IMF, ‘Corruption: Costs and Mitigating Strategies’ (IMF Staff Discussion Note SDN/16/05, May 2016) 3.

⁹ Tina Søreide, *Corruption and Criminal Justice: Bridging Economic and Legal Perspectives* (Edward Elgar, 2016) 17.

¹⁰ *Ibid* 14.

The costs of corruption are substantial. The IMF, noting that these costs are difficult to measure, nonetheless suggests that the annual costs of bribery alone¹¹ in developing and advanced economies are in the order of USD 1.5 trillion to 2 trillion (or roughly 2 per cent of GDP).¹² The same report goes on to note that corruption has a number of other manifest and direct implications for taxation. *Inter alia* it can: weaken the state's capacity to tax, leading to lower revenue collections; create disincentives for taxpayers to pay taxes; reduce the impetus for the state to collect taxes; and undermine spending programs.¹³

This article uses an Indonesian case study as a framework to explore critical issues in this relationship between tax and corruption. More particularly, it considers the causes and impact of corruption at tax administrative levels in Indonesia, and identifies and evaluates strategies the Indonesian revenue authority (the Directorate General of Taxation, or DGT) has adopted, or can adopt, to ensure opportunities for such corrupt activity are mitigated or eliminated. This is done in the context of an evaluation of a major tax office corruption scandal that has occurred in recent years in Indonesia: the Gayus case.¹⁴

The article adopts a qualitative approach, utilising archival analysis supplemented with interviews and correspondence with key players involved. After this introduction, section 2 identifies the principles that typically underpin anti-corruption strategies in revenue authorities in developing countries, together with examples of some of the anti-corruption strategies employed. The article then considers (section 3) the nature of the corrupt activity exemplified by the Gayus case in Indonesia, how it arose, and how it came to light. This is followed (in section 4) by a consideration of the impact upon the organisation, how the DGT dealt with it and what changes came about as a result in terms of anti-corruption strategies subsequently adopted and now operating in the DGT. The article concludes (section 5) with a section on the lessons learned and prospects for the future, both in Indonesia and elsewhere in the Asia-Pacific region.

2. PRINCIPLES AND STRATEGIES¹⁵

The integrity of its staff and systems is a vital component of any effective revenue administration, and yet – as Bahl and Bird point out – corruption and taxation have always been associated in history – and not just in developing countries.¹⁶ It would be naïve to believe that corruption is not a serious issue in most developing economies – indeed Uche and Ugwoke noted in 2003 in relation to Nigeria, for example, that '[t]he major threat to the effective administration of VAT in Nigeria ... is the widespread

¹¹ As noted earlier, bribery is only one aspect of the possible forms of corruption.

¹² IMF, 'Corruption: Costs and Mitigating Strategies', above n 8, 5.

¹³ Ibid 6-7.

¹⁴ Gayus Halomoan Partahanan Tambunan, a relatively low-ranking DGT official.

¹⁵ Parts of this section are based upon material originally contained in Margaret McKerchar and Chris Evans, 'Sustaining Growth in Developing Economies through Improved Taxpayer Compliance: Challenges for Policy Makers and Revenue Authorities' (2009) 7(2) *eJournal of Tax Research* 171.

¹⁶ Bahl and Bird, above n 6, 291, citing Carolyn Webber and Aaron Wildavsky, *A History of Taxation and Expenditure in the Western World* (Simon and Schuster, 1986).

corruption and indiscipline which are deeply entrenched in all aspects of the country's social and economic life'.¹⁷

Corruption may be systematic – involving groups of employees acting together in a corrupt fashion and often led by senior staff – or individual; and may or may not involve external 'clients'. Examples are not difficult to cite: charging for services that should be free; diverting cash; making false repayment claims; losing files; and receiving payments to complete tax returns or bribes to favourably settle audits. And corruption is not limited simply to tax activities – it can also include abuses of power such as theft or private use of goods like office equipment; fraudulent subsistence and travel allowance claims; and stealing time to pursue outside interests and/or employment.¹⁸

The consequences of corruption are obvious. It is a cancer that destroys the organisation itself and undermines all other aspects of society. It erodes confidence in the tax system and encourages evasion. It increases the costs of doing business and distorts the level playing field that should be available. And to the extent that there is a political limit as to the amount of tax that people will bear in developing countries (and that there is therefore a substitution effect between taxation and corruption), it reduces the amount of formal tax that can be collected.¹⁹

A comprehensive literature already exists on how to design and implement effective anti-corruption strategies in revenue authorities.²⁰ This section of the article merely highlights some key aspects from that literature in order to provide the context for the analysis of the Gayus case in Indonesia, explored in section 3. It begins by looking at a series of high level priorities and principles that the literature suggests are critical in attempting to tackle corruption in what Johnston terms 'fragile situations'.²¹ This is followed by a brief consideration of some of the key strategies that the literature has suggested may be appropriate (though they are very context-specific and are not always successful) in tackling corruption in revenue authorities.

¹⁷ Chibuike Uche and Onuora Ugwoke, 'The Law and Practice of Value Added Tax in Nigeria' (2003) 57(6) *Bulletin for International Taxation* 265, 272.

¹⁸ David Child, 'Key Steps to Address Corruption in Tax and Customs' (U4 Brief No. 15, Chr. Michelsen Institute, May 2008) <<https://www.cmi.no/publications/3041-key-steps-to-address-corruption-in-tax-and-customs>> accessed 4 April 2017.

¹⁹ Bahl and Bird, above n 6, 291.

²⁰ See, for example, Nick Devas, Simon Delay and Michael Hubbard, 'Revenue Authorities: Are They the Right Vehicle for Improved Tax Administration?' (2001) 21 *Public Administration and Development* 211; Anwar Shah (ed.), *Performance Accountability and Combating Corruption* (World Bank, 2007) (especially ch. 9: Mahesh Purohit, 'Corruption in Tax Administration', 285); Aminur Rahman, 'Tackling Corruption through Tax Administration Reform' (*In Practice* Business Taxation Note 48312, World Bank, April 2009); McKerchar and Evans, above n 15; OECD, *Bribery and Corruption Awareness Handbook for Tax Examiners and Tax Auditors* (2013); Maira Martini, 'Approaches to Curbing Corruption in Tax Administration in Africa' (U4 Anti-Corruption Resource Centre Expert Answer, Transparency International and Chr. Michelsen Institute, 25 June 2014); Richard Bird, 'Improving Tax Administration in Developing Countries' (2015) 1(1) *Journal of Tax Administration* 23; IMF, 'Corruption: Costs and Mitigating Strategies', above n 8.

²¹ Michael Johnston, 'First, Do No Harm – Then, Build Trust: Anti-Corruption Strategies in Fragile Situations' (World Development Report 2011 Background Paper, World Bank, September 2010).

2.1 Priorities and principles

Johnston identifies two key priorities that must underpin any form of anti-corruption strategy. The first is ‘do no harm’ and the second is ‘build trust’.²²

The first priority (‘Do no harm’) means avoiding premature or poorly thought-out reforms that can do more harm than good – notably steps that overwhelm a society’s capacity to absorb aid and put it to effective use, and that risk pushing fragile situations and societies into particular kinds of corruption that are severely disruptive. The second imperative (‘Build trust’) is essential if complex, collective-action problems are to be minimized, and if reform is to draw broad-based report.²³

These are sensible points, to which the IMF is able to add a number of other broad principles, as follows:²⁴

1. an effective strategy requires a holistic and multifaceted approach, albeit one that is appropriately prioritised and sequenced, depending upon country-specific circumstances. Hence an effective anti-corruption strategy is likely to involve not only credible sanctions but also a recognition that the kind of behavioural change sought must be grounded in a core system of social values. Moreover, any such approach is likely to entail short, medium and long term instruments and strategies;²⁵
2. perceptions and expectations (whether of internal or external stakeholders) must be carefully managed according to the implementation horizon of many anti-corruption reforms. Certain strategies, such as anti-corruption laws, can be very quickly implemented; but credibility, and sustainability, will only be achieved where they are supported, or appropriately enforced, by effective social values and institutions, which inevitably require more time to develop. In addition, and as noted by Johnston, where expectations are too low, essential support for reform and for the local leaders and groups that must undertake it will be absent or difficult to sustain. But conversely, high expectations can be equally problematic;²⁶
3. reforms of a preventative nature (as opposed to reforms directly addressing corrupt activity) can be equally effective. Hence reforms addressing transparency, or enhancing the rule of law – which will have an indirect effect on corruption – may be just as effective as more direct measures (such as setting up an anti-corruption commission); and
4. there are significant challenges to measuring corruption and the success of anti-corruption strategies.²⁷ But such challenges should not be a reason for inaction, merely a recognised impediment built into the process of reform.

²² Ibid 2-3.

²³ Ibid 1.

²⁴ IMF, ‘Corruption: Costs and Mitigating Strategies’, above n 8, 15.

²⁵ Rahman, above n 20, 2-3.

²⁶ Johnston, above n 21, 6-7.

²⁷ See, for example, Fredrik Galtung, ‘Measuring the Immeasurable: Boundaries and Functions of (Macro) Corruption Indices’ in Charles Sampford, Arthur Shacklock, Carmel Connors and Fredrik Galtung (eds), *Measuring Corruption* (Ashgate, 2006) 101; Francisco-Javier Urra, ‘Assessing Corruption: An Analytical

2.2 Key strategies

Tax corruption depends, ultimately, on the willingness of tax officials on the one hand, and taxpayers or their intermediaries on the other, to engage in corrupt activity. As noted by Rahman, the key drivers of tax corruption are often based upon opportunities afforded by tax officials.²⁸ For example, in many countries, offering a bribe is the only way to make progress with tax matters (as in obtaining relevant documentation or progressing an appeal) or avoid harassment from tax officials. Rahman further notes that the underlying factors that can facilitate this willingness to engage in corrupt behaviour by tax officials include: complex and unclear tax laws and procedures; non-transparent hiring and reward mechanisms; a low level of skills; a lack of professional ethics and integrity; low pay and a lack of incentives; conflicts of interest; the ‘get-rich-quick’ syndrome; and insufficient checks and balances within the administration.²⁹ But the willingness of tax officials to act corruptly is often simply a response to an opportunity proffered by the taxpayer or agent. For example, businesses are often willing to pay a bribe if it reduces the tax cost and/or saves time in tax disputes.

Obviously, therefore, any strategies which directly impact upon the opportunity or willingness of the parties to engage in corrupt activities will be worthy of consideration. Many such strategies are now briefly considered.

2.2.1 Corruption risk mapping

The preparation of ‘Corruption Risk Maps’, designed to guide procedural changes to reduce opportunities of corruption, is a useful starting point for any revenue agency determined to tackle problems of corruption. In Columbia this strategy was successfully employed, based upon an initial systematic study of important business processes, to address the vulnerable points in the systems and identify optimal strategies for dealing with each.³⁰

2.2.2 Human resource management

The development and implementation of a transparent, fair and effective human resource management policy, involving all aspects of recruitment, performance appraisal, career development and remuneration is a vital aspect of any medium to long term reform process.³¹ Staff need to be carefully recruited on merit-based selection principles, and remunerated at levels which are at least broadly comparable to equivalent positions in banking and the accounting profession, have access to carefully developed in-house and external training possibilities and have realistic opportunities for career and income progression.

Review of Corruption Measurement and Its Problems: Perception, Error and Utility’ (Edmund A Walsh School of Foreign Service, Georgetown University, Washington, DC, May 2007); Carmen R Apaza, ‘Measuring Governance and Corruption through the Worldwide Governance Indicators: Critiques, Responses, and Ongoing Scholarly Discussion’ (2009) 42(1) *PS: Political Science & Politics* 139.

²⁸ Rahman, above n 20, 2.

²⁹ Ibid.

³⁰ Jit Gill, ‘The Nuts and Bolts of Revenue Administration Reform’ (World Bank, January 2003) 13 <<http://siteresources.worldbank.org/INTTPA/Resources/NutsBolts.pdf>> accessed 4 April 2017.

³¹ Rahman, above n 20, 3.

2.2.3 *Ethical policies and practices*

Staff must be aware of the importance of integrity at both the personal and organisational levels, and policy and practice must reflect this. It is not sufficient merely to introduce ethical 'Codes of Conduct', sets of internal disciplinary rules and instruments such as 'Taxpayers' Charters'; they also need to be shown to be 'living' documents that inform everyday activity and decision-making. Other practical measures include asset declarations for all staff, and the availability of avenues for whistleblowing (including protection from disclosure after the event). Collier et al., in an Indonesian context, identified that the establishment of peer learning groups in the workplace considerably enhanced and reinforced ethical behaviour and reduced corruption in a revenue authority when allied to internal training on the topic. The groups comprised a small number of trainees who maintained contact and reinforced communities of ethical practice in a variety of ways, including face to face meetings, and SMS and email groups, during and after the delivery of the training.³²

2.2.4 *Internal controls and deterrence*

Strong internal controls are an essential part of any strategy designed to address corruption in a revenue authority. Child notes that managers must be proactive and conduct desk and office inspections, and design procedures and systems that deter integrity lapses and make them easier to spot.³³ Other examples include restricting access by taxpayers to designated taxpayer service areas so that they cannot access other revenue authority work spaces; restricting access by employees to scanned copies of original records to prevent tampering; creating audit trails of administrative decisions and changes made to taxpayer current accounts; and separating the functions of assessing and collection in order to reduce opportunities for corruption and collusion.³⁴

In addition, an effective internal investigation force, combined with severe penalties (including dismissal and prosecution) for malfeasance and a strong likelihood of detection, will inevitably reduce the incidence of corruption. 'To the extent corruption follows an economic calculus, the expected value of the outcome of taking a bribe may be heavily influenced by the chances of getting caught and being heavily penalized'.³⁵

2.2.5 *Statutory changes*

Statutory changes to increase transparency, remove discretion and simplify the law can make a significant contribution to the enhancement of the integrity of the operation of the revenue authority. Where the structure of a particular tax is as transparent as possible, and obligations and liabilities are clearly stated, taxpayers will be less likely to be cheated. Bahl and Bird note that '[n]othing good can come of a situation in which tax administrators and tax payers negotiate over how large the tax liability should be. One problem in the practice of income taxation in developing

³² Kate Collier, Ali Rokhman, Sherria Ayuandini and Panca Kurniawan, 'Using "Workplace Learning Groups" - A Peer-Learning Approach — in the Indonesian Tax Office to Encourage Workplace Learning and Support Cultural Change within the Organisation' (Paper presented at the *Researching Work and Learning Conference 5*, Cape Town, South Africa, December 2007).

³³ Child, above n 18.

³⁴ Gill, above n 30, 13.

³⁵ Bahl and Bird, above n 6, 291.

countries is that, apart from withheld taxes, tax liabilities are, in fact, often negotiated'.³⁶ In similar vein, Awasthi and Bayraktur have produced empirical findings which support the existence of a significant link between measures of tax corruption and tax simplicity, such that a less complex tax system is shown to be associated with lower corruption in tax administration.³⁷

2.2.6 *Autonomous revenue authorities*

In recent years many developing countries have established their tax departments into autonomous or semi-autonomous revenue authorities ('ARAs'). It has been a noticeable worldwide trend, with some suggestions that the World Bank has, upon occasions, 'been a persuasive salesman'.³⁸ The defining feature of an ARA is some degree of autonomy whereby the revenue collection function is removed, either partly or wholly, from the Ministry of Finance. The management of the ARA therefore has significant independence in financial, personnel and operational matters, but is accountable for delivering agreed results, with continuation of appointment and renewal of contract for top management dependent upon revenue administration performance.³⁹ These independent revenue agencies, it is argued, are thus more able to provide better pay and other incentives to their staff while also imposing greater accountability for performance and reducing opportunities for corruption.⁴⁰ Taliencio argues that if one compares the pre- and post- reform state of affairs in countries where ARAs have been introduced, there is improvement in most cases along most dimensions of performance.⁴¹

Others are more circumspect. Gallagher notes that the jury is still out,⁴² while Fjeldstad and Moore suggest that many of the perceived advantages may have been short term and identify a number of conceptual and practical problems with ARAs that suggest they are not always the panacea that the World Bank may have suggested.⁴³ Whatever the true overall picture, it is certainly the case, as argued by Rahman, that 'autonomy minimizes the chances of the administration's involvement in political corruption and client favouritism'.⁴⁴

2.2.7 *Organisational options*

Regardless of whether the revenue authority is constituted as an autonomous or semi-autonomous body, the way in which it is internally organised can have a significant impact upon the effectiveness of the tax administration and its capacity to combat corruption.⁴⁵ Traditionally, three separate models for the organisation of revenue

³⁶ Ibid.

³⁷ Rajul Awasthi and Nihal Bayraktur, 'Can Tax Simplification Help Lower Tax Corruption?' (World Bank Policy Research Working Paper 6988, July 2014).

³⁸ Odd-Helge Fjeldstad and Michael Moore, 'Tax Reform and State-Building in a Globalised World' in Deborah Brautigam, Odd-Helge Fjeldstad and Michael Moore (eds), *Taxation and State-Building in Developing Countries: Capacity and Consent* (Cambridge University Press, 2008) 235, 249.

³⁹ Gill, above n 30.

⁴⁰ Mark Gallagher, 'Benchmarking Tax Systems' (2005) 25(2) *Public Administration and Development* 125, 130.

⁴¹ Robert Taliencio, 'Designing Performance: The Semi-Autonomous Revenue Authority Model in Africa and Latin America' (World Bank Policy Research Working Paper 3423, October 2004).

⁴² Gallagher, above n 40, 133.

⁴³ Fjeldstad and Moore, 'Tax Reform and State-Building in a Globalised World', above n 38, 249-255.

⁴⁴ Rahman, above n 20, 4.

⁴⁵ Charles Vehorn and John Brondolo, 'Organizational Options for Tax Administration' (Paper presented at the 1999 Institute of Public Finance Conference, Zagreb, June 1999).

authorities have been suggested both in the broader organisational theory literature⁴⁶ and in more specific literature relating to tax administration.⁴⁷

1. product-based, relating to the type of tax (income tax, VAT, etc.) administered by the revenue authority;
2. functional, relating to the different administrative functions performed by revenue authorities such as processing tax returns, or auditing, or collecting taxes; and
3. client-based, relating to the different types of taxpayer according to criteria such as scale of operation (large, small, etc.), form of ownership or industrial/economic sector.

Developing countries have tended to move away from product-based structures built upon different types of tax to those which are based upon function, although often with elements of a client-based market segmentation approach also in evidence (for example, the introduction of large taxpayers units focusing upon the large companies which are often responsible for a disproportionate amount of revenue collections; or the introduction of industry-based organisational structures).⁴⁸ In this way they have been able to secure the advantages of improved accountability and control, enhanced compliance, better administrative efficiency, reduced corruption and more customised taxpayer service.

2.2.8 *Minimise taxpayer/revenue agency interaction*

The higher the level of contact and interaction between tax officials and taxpayers, the greater the scope for corruption and collusion. Therefore minimising that contact through the use of self-assessment, withholding taxes and the like can be an effective strategy. Gill identifies examples from Latvia and Russia where work processes were modified to reduce interaction between tax officials and taxpayers,⁴⁹ and Bahl and Bird note that VAT and payroll taxes tend to score relatively highly in this respect.⁵⁰

2.2.9 *Reduce compliance costs*

Compliance costs for taxpayers in developing countries are four to five times higher than those in developed countries.⁵¹ This therefore suggests that reducing compliance costs 'lowers the amount of bribe a (rational) taxpayer might be willing to pay to avoid the declaration and payment process'.⁵²

2.2.10 *Other strategies*

Other strategies mentioned by Rahman include greater institutional use of e-services and automation; simplified and standardised procedures; and taxpayer outreach and

⁴⁶ For example, B J Hodge, William Anthony and Lawrence Gales, *Organization Theory: A Strategic Approach* (Prentice Hall, 5th ed., 1996).

⁴⁷ Vehorn and Brondolo, above n 45.

⁴⁸ Ibid 21; Gallagher, above n 40, 133; Fjeldstad and Moore, 'Tax Reform and State-Building in a Globalised World', above n 38, 248.

⁴⁹ Gill, above n 30, 13.

⁵⁰ Bahl and Bird, above n 6, 291.

⁵¹ Chris Evans, 'Studying the Studies: An Overview of Recent Research into Taxation Operating Costs' (2003) 1(1) *eJournal of Tax Research* 64.

⁵² Bahl and Bird, above n 6, 291.

education.⁵³ One strategy that does not appear to have been successful in combating corruption is the privatisation or outsourcing of the tax collection function. Tax farming (the process where the right to collect tax is auctioned off to a private agent in exchange for a fixed sum payable in advance) and tax sharing (whereby private agents collect taxes, with the right to keep a share of the total collection) have often been introduced with the objective of reducing administrative costs and increasing the level and reliability of collections.⁵⁴ The examples of outsourcing of some local authority tax collection in Tanzania and Uganda suggest that they may sometimes have succeeded in increasing revenue collections, but that the levels of corruption have also increased.⁵⁵

3. THE GAYUS CASE

The Gayus case stands out – in terms of media coverage and organisational impact – as one of the more infamous and significant tax corruption cases in Indonesia in recent years. Gayus Tambunan was an official in the Indonesian DGT in the period up to 2009, where his role was Tax Objection and Appeal Reviewer.⁵⁶ As a civil servant Group IIIA, his net income in the year ended 31 December 2009 was IDR 9,263,600 per month (AUD 926.36); it was subsequently established that he had around IDR 28 billion (AUD 2,800,000) in his bank accounts in that year.

Gayus' name first emerged into the public spotlight in July 2009 when he was mentioned as a potential money laundering suspect by police involved in the investigation of the so-called judicial mafia. This suspicion had come from the Center for Financial Transaction Reporting and Analysis (PPATK), which had identified substantial bank accounts belonging to Gayus in Bank Panin and Bank BCA. The police then conducted an investigation into the case and on 7 October 2009, investigators from the Criminal Police Headquarters sent a Notice of Commencement of Investigation to Gayus, formally identifying him as a suspect. In the file sent by police investigators to the prosecutor's office, Gayus was alleged to be involved in corruption, money laundering, and embezzlement. His assets were initially frozen, but surprisingly unfrozen in November 2009. Even more surprisingly he was initially cleared by a local court of various charges laid against him in March 2010.

Later in 2010, however, fresh charges were laid, and Gayus was indicted on the following counts:

⁵³ Rahman, above n 20, 2-3.

⁵⁴ Anuradha Joshi and Joseph Ayee, 'Associational Taxation: A Pathway into the Informal Sector' in Deborah Brautigam, Odd-Helge Fjeldstad and Michael Moore (eds), *Taxation and State-Building in Developing Countries: Capacity and Consent* (Cambridge University Press, 2008) 183, 190.

⁵⁵ Godfrey Bahiigwa, Frank Ellis, Odd-Helge Fjeldstad and Vegard Iversen, 'Uganda Rural Taxation Study', Report commissioned by Department for International Development (UK) Uganda, Economic Policy Research Centre, Kampala, 2004; Daniel Kobb, 'Corruption in Tanzania: An Application of Tax Farming' (Mimeo, Tanga Tanzania and KKonsult USA, 2004).

⁵⁶ The literature refers to him variously as a 'fairly low level tax official' (Howard Dick, 'Statistics, Half-Truths and Anti-Corruption Strategies' in Tim Lindsey and Helen Pausacker (eds), *Is Indonesia as Corrupt as Most People Believe and Is It Getting Worse?* (Centre for Indonesian Law, Islam and Society Policy Paper, Melbourne Law School, 2013) 5, 13), a 'relatively low ranking tax official' (Ross H McLeod, 'Survey of Recent Developments' (2011) 47(1) *Bulletin of Indonesian Economic Studies* 7, 8), and 'a middle level [of] DGT official' (Yustinus Prastowo, 'New Perspectives of Comprehensive Reform: Integrating Corruption Eradication and Tax Optimization Agenda' (Paper presented at the Tax and Corruption Symposium, Sydney, 12 and 13 April 2017) 3).

1. *first*, that Gayus, as a Reviewer in the Objections and Appeals Directorate of the DGT, together with four other DGT officials (a fellow Reviewer from the same Directorate, the Head of Section and the Deputy Director of the Tax Reduction and Objection Division and the Director of the Objection and Appeal Division) committed or participated in an unlawful act, to enrich themselves or another person or a corporation, detrimental to the country's finances, in handling a tax objection filed by a small corporate taxpayer related to that taxpayer's tax liabilities;
2. *second*, that Gayus, together with another person, at various times between August 2009 and November 2009, attempted to bribe investigators from the Civil Service Criminal Investigation Police Headquarters to persuade them to use their positions of power and authority to cease their investigation of his financial transactions;
3. *third*, that Gayus attempted to bribe a judge with the intention of influencing his trial case, so that he would escape a prison sentence or so that his sentence would be reduced; and
4. *fourth*, that Gayus in September 2009 at the office of the Criminal Investigation Police Headquarters and Manhattan Hotel (South Jakarta) gave false information in relation to the ongoing investigation.

Based on the above indictments, Gayus was found guilty and sentenced to seven years in prison, together with a fine of IDR 300 million. In addition, and unsurprisingly, Gayus was served with a dishonourable discharge from his DGT employment on the basis that he had violated the employment code of conduct.

There are a number of rather unsettling and somewhat unsavoury aspects of the Gayus case. The corrupt activity in the case appears to have been corruption by greed rather than corruption by need, particularly given that the Ministry of Finance of the Republic of Indonesia had increased the salary rates for their staff compared to other civil servants in years prior to 2009. Furthermore, the Gayus case became a major issue in Indonesia because, at that time, the DGT was in a period of modernisation and was particularly trying to increase the level of trust from taxpayers. This case, according to interviews with key personnel from the DGT,⁵⁷ had an adverse impact upon that process and, because of the heightened media interest,⁵⁸ significantly decreased the level of trust from taxpayers and reduced the ability of the DGT to achieve tax revenue targets that had been set for it.

It is also disturbing that Gayus was apparently able to leave prison on scores of occasions, on at least one of which he had travelled overseas on a false passport.⁵⁹ Moreover, he testified that he had received millions of dollars in bribes and fees from over 150 individual and corporate taxpayers, including three large companies

⁵⁷ Harry Gumelar, Director of Internal Compliance and Apparatus Transformation Directorate, interviewed 25 January 2017.

⁵⁸ See, for example, articles in the *Jakarta Globe*, 19 January 2011, 20 January 2011 and 5 February 2011; and in the *Jakarta Post*, 29 January 2011.

⁵⁹ It is noted, for example, that he 'bribed his way out of prison for short trips to Singapore, Kula Lumpur, Macau and famously to watch the tennis in Bali': Dick, above n 56, 13, citing Alice Budisatrijo 'Indonesian Taxman Gayus Tambunan Jailed for Corruption', *BBC News*, 19 January 2011 < <http://www.bbc.com/news/world-asia-pacific-12224782>>.

associated with the Golkar party chief, Aburizal Bakrie (though subsequently he recanted this aspect of his testimony).⁶⁰

But perhaps the most worrying aspect of the Gayus case is that the nature of the case, and the manner in which it unfolded, played directly into a narrative that has led the Indonesian public to suspect that there is a very large gap between policy rhetoric and action, and that the much-vaunted anti-corruption campaign being conducted in Indonesia at the time was largely ineffective and its impact overstated.⁶¹ Gayus was a relatively 'small fish' so far as corrupt activity was concerned, and the monetary penalty imposed was a very small proportion (only around 1 per cent) of the amount of bribes that were apparently extracted. Despite the very obvious involvement of powerful and wealthy taxpayers who had been involved in the corrupt activity, as well as very high ranking police officers and members of the judiciary, none of these 'big fish' involved in the same web of corruption as Gayus were ever prosecuted or sanctioned.⁶²

4. IMPACT UPON THE DIRECTORATE GENERAL OF TAXATION

In general, corruption within the DGT is influenced by several factors, often relating to opportunity (as noted in section 2). More particularly, interviews and correspondence with a senior DGT official suggest that corrupt activity within the DGT is driven by:⁶³

1. the non-compliance of taxpayers in fulfilling their obligations as required by the provisions. As a result, when the Account Representative (the relevant tax official) asks them to pay their tax liability, the taxpayer instead seeks to negotiate a lower amount, usually also offering a bribe, rather than pay the full amount of tax due;
2. in the audit process, where under-declarations or evidence of other forms of evasion are established, then the taxpayer attempts to negotiate a lower tax liability, again by offering a bribe, than the amount of the true tax assessment; and
3. taxpayers negotiating (with proffered financial inducements) with tax collectors and bailiffs to postpone or cancel the impounding of their assets as a result of the tax collection process.

It is, perhaps, slightly surprising that corrupt activity within the DGT would still be driven by the first and the third of these points. They would certainly have been primary drivers in the periods prior to the modernisation of the DGT but it would be expected that they would be less prevalent in more recent times. In the case of the first point, this is partly because taxpayers under supervision of a particular Account Representative are regularly rotated by the DGT. Arguably, therefore, the risk would be 'too high' for a 'rational' tax officer to undertake such blatantly corrupt activity.

⁶⁰ McLeod, above n 56, 8.

⁶¹ Ibid 7.

⁶² Ibid 8.

⁶³ Harry Gumelar, Director of Internal Compliance and Apparatus Transformation Directorate, interviewed 25 January 2017, supplemented by private correspondence dated 31 March 2017.

With respect to the third point, it also appears somewhat unlikely that tax collectors and bailiffs would be capable of postponing or cancelling the seizure of assets without being detected given the implementation of new real time and comprehensive information systems such as the DGT Information System (Sistem Informasi Direktorat Jenderal Pajak or SIDJP). Nonetheless, it is clear from interviews and correspondence that the DGT sees all three areas as potential points of vulnerability.

The anti-corruption strategy in operation in relation to the Indonesian DGT has, in recent years, involved both external and internal monitoring and control. The principal external driving agency since 2003 has been the Corruption Eradication Commission (Komisi Pemberantasan Korupsi or KPK). Its main functions are to investigate alleged corruption and, if sufficient evidence exists, to prosecute those suspected of engaging in it.⁶⁴ Dick suggests that, since 2004, it has been ‘the brightest star in Indonesia’s anti-corruption firmament’, having been remarkably successful, investigating and prosecuting ‘big fish’ such as ministers, parliamentarians, senior public servants, provincial chiefs, district heads and mayors across the country.⁶⁵ He also notes, however, that this success may be chimerical: that the KPK’s activities have been in the nature of ‘sustainable harvesting’. ‘In other words, as one “big fish” is reeled in, another takes its place. Sustainable harvesting is a good thing environmentally but not as a corruption eradication strategy. It does not reduce the rate of harvesting’.⁶⁶

It is probably reasonable to conclude that a low-level official such as Gayus would have been ‘flying under the radar’ of the external monitoring agency (the KPK), notwithstanding allegations that ‘big fish’ were possibly involved. As a result, the Gayus case probably did not have any serious implications for the external monitoring of corruption within the DGT. The KPK was not, in any obvious way, impacted by the Gayus case, and has continued its strategy of pursuing the perpetrators of ‘grand corruption’ rather than turning its attention to corrupt activity in the lower levels of the DGT.⁶⁷

The Gayus case, and cases like it such as that involving Dhana Widyatmika, another tax official,⁶⁸ and many other tax officials,⁶⁹ may not have resulted in the prosecution of any of the bigger fish involved in corrupt activities, nor any significant change in the manner in which external monitoring of the DGT takes place by agencies such as the KPK. But it has certainly had an impact upon the manner in which anti-corruption activity has subsequently been conducted within the DGT.

⁶⁴ Simon Butt, ‘Indonesia’s Anti-Corruption Courts: Are They as Bad as Most People Say and Are They Getting Better?’ in Tim Lindsey and Helen Pausacker (eds), *Is Indonesia as Corrupt as Most People Believe and Is It Getting Worse?* (Centre for Indonesian Law, Islam and Society Policy Paper, Melbourne Law School, 2013) 17.

⁶⁵ Dick, above n 56, 12.

⁶⁶ Ibid.

⁶⁷ This is the case despite suggestions from commentators that the KPK should target its resources and efforts more strategically on the goal of consolidating islands of integrity within the state apparatus – and particularly the Supreme Court, the Attorney General’s Office, and the DGT: see Dick, above n 56, 12.

⁶⁸ See Joko Sriwido, ‘The Implementation of Gijzeling in Solving Tax Corruption Cases in Indonesia’ (2016) 4(1) *Scientific Research Journal* 50.

⁶⁹ See Yustinus Prastowo, ‘New Perspectives of Comprehensive Reform: Integrating Corruption Eradication and Tax Optimization Agenda’ (Paper presented at the Tax and Corruption Symposium, Sydney, 12 and 13 April 2017) for a list of other DGT officials involved in bribery and other forms of corruption in recent years.

Based on the information gathered from DGT, the organisation does not distinguish between different forms of corruption (such as 'large' and 'small'); all irregularities or violations that are related to corruption (fraud) involving DGT officials now receive a 'zero tolerance' approach. Thus, legal action will ensue, providing strict penalties up to and including formal dismissal and prosecution. The Government of Indonesia has set penalties for disciplinary offences committed by civil servants.⁷⁰ These regulations contain categories and classifications of punishment for various offences, with disciplinary outcomes based upon the impact of the offence upon the work unit, institution and/or country. The case of Gayus, as the final outcome attests, clearly fell at the more egregious end of the scale of offences.

As a result of the Gayus case, many internal changes have occurred since 2012. For the purposes of this article, two major changes are now considered: in the first place there has been a significant change in internal organisation related to internal corruption monitoring and control; and secondly there have been developments in broader anti-corruption strategies conducted within the DGT.

4.1 Optimising the role of the Directorate of Internal Compliance and Apparatus Transformation

One prime example of change since Gayus is the change in the role of the Directorate of Internal Compliance and Apparatus Transformation (DICAT) within the DGT's organisational structure. The role of the DICAT is to formulate and implement policies and technical standardisation in internal compliance and apparatus transformation. Since the Gayus case, the DGT has optimised the role of this Directorate, especially through its Internal Compliance and Internal Investigation Unit. This unit operates as a formidable line of defence in order to supervise the implementation of the Code of Conduct through a variety of techniques, including random surprise inspections, surveillance, and others.⁷¹

The DGT has established this internal compliance unit to carry out the following functions: internal control monitoring; risk management monitoring; monitoring the code of conduct and disciplinary compliance; monitoring the follow-up of internal control results; and formulating recommendations on business process improvement.

This internal compliance regime within the DGT consists of both a preventative system and a reactive system. The preventative system entails compliance examination, monitoring of the DGT's Employee Code of Conduct, administration of the whistleblowing system, the obligation to submit the Civil Servant Wealth Report, risk management, and a Corporate Value Internalisation Program. In contrast, the reactive part of the system is conducted by an Internal Investigation Sub Directorate and embraces the following actions:

1. collecting materials and information on complaints received;
2. making recommendations to immediate supervisors to examine the disciplinary offences committed by employees; and
3. conducting 'red-handed operations' if there is valid information that will

⁷⁰ The Discipline of Civil Servants, Indonesian Government Regulation No 53 Year 2010, 6 June 2010.

⁷¹ Directorate General of Taxation (DGT), *Annual Report 2015: The Guidance Year of Taxpayers' Compliance: Building a Culture of Tax Compliance* (2015).

occur in order to discipline violation transactions.

4.2 Developments in the anti-corruption strategy within the DGT

Great emphasis is now placed on the DGT Code of Conduct,⁷² which consists of nine key obligations for employees and eight prohibitions (see Table 1). To facilitate the understanding and implementation of the code, the DGT has issued the Director General of Taxes Circular Letter No SE-33/PJ/2007 regarding Guidelines for Implementing DGT Code of Conduct. Initially, the code of conduct is implemented by each employee signing a Statement Letter of Willingness to Comply with DGT Code of Conduct. Although this existed prior to the Gayus case, greater emphasis has been placed upon adherence to the code since 2010.

Table 1: Employee Code of Conduct

Employee Obligations
1. Respect other people's religions, faith, and cultures
2. Work in a professional, transparent, and accountable manner
3. Secure DGT data and information
4. Provide best service to taxpayers, fellow employees, or other stakeholders
5. Obey official orders
6. Be responsible in using DGT properties
7. Abide by official working hours and rules
8. Become a role model for the community in fulfilling tax obligations
9. Behave, dress, and speak in a polite manner
Employee Prohibitions
1. Act in a discriminatory way in performing tasks
2. Become an active member or partisan of political parties
3. Abuse power
4. Misuse office facilities
5. Accept any gift in any form, either directly or indirectly, from taxpayers, fellow employees, or other stakeholders, which leads to the employee being suspected of abusing power
6. Misuse tax data and information
7. Perform actions which may lead to data disruption, destruction or alteration in the DGT information system
8. Break the norms of decency that can damage public image and dignity of DGT

Source: DGT (2017)⁷³

The DGT has adopted a three-line defence concept to monitor the correct implementation and operation of its code of conduct. The first line of defence lies with workplace supervisors who are specifically obliged to ensure that their subordinates strictly adhere to the code of conduct. The second line comprises the work carried out by the Internal Compliance Unit (see section 4.1 above) through surprise inspection, surveillance, and other mechanisms. Finally, a last line of defence

⁷² Regulated by Minister of Finance Regulation No 1/PM.3/2007.

⁷³ Private correspondence with DGT dated 31 March 2017, supported with Minister of Finance Regulation No 1/PM.3/2007.

is provided by the Inspectorate General of the Ministry of Finance which is particularly responsible for identifying violations of the code of conduct where fraud is indicated.

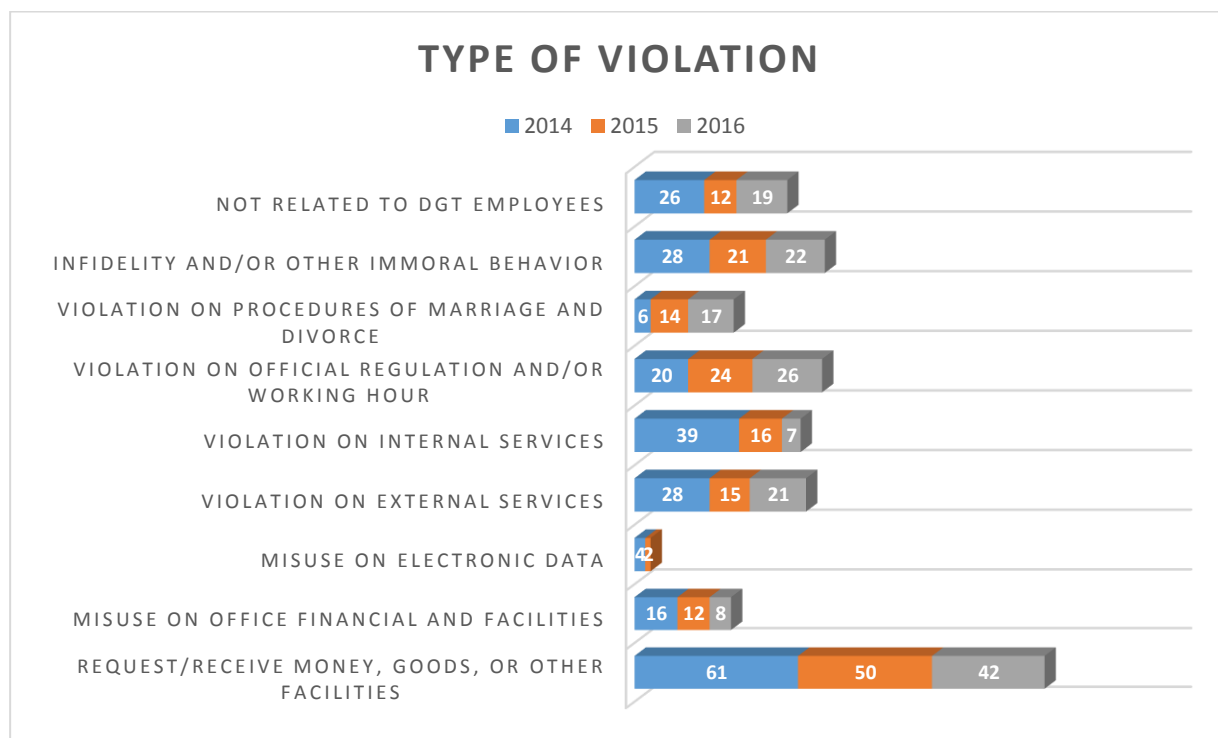
One further development since 2012 is the introduction of a comprehensive whistleblowing system to help provide early detection of violations of the code of conduct of employees. Currently, reports on the violation of the DGT code of conduct can be submitted in a variety of relatively easy and accessible ways, including through Help Desks and Call Centres, on a dedicated whistleblowing telephone hotline, and by fax, email and written letter. The number of violations reported in the period 2007 to 2016 is reported in Figure 1. It is interesting to note the spike in reports in the two years immediately following 2011, around the period when the Gayus case was receiving intense media publicity.

Figure 1: Number of Violation Reports



Source: DGT (2017)

Figure 2 identifies the types of violation report for the years 2014 to 2016.

Figure 2: Type of Violation Reports

Source: DGT (2017)

It is noticeable in Figure 2 that ‘bribery’ (requests for money, goods or other) is by far the largest category in each of the three years, but also encouraging that the trend is positive over the period, with very nearly a one-third decline in such reports in 2016 compared to 2014. A similar positive trend, albeit on significantly lower absolute figures, is evident in relation to the abuse/misuse of office finances and other facilities.

5. LESSONS LEARNED AND FUTURE PROSPECTS

In part the positive trends identified in the preceding section may reflect the development of a culture within the DGT that is more resistant than has hitherto been the case to the temptations of corruption. To demonstrate resistance to any sort of corruption, collusion, and nepotism, and to build resilience, the DGT has held various activities to nurture and foster an anti-corruption culture and spirit among its employees. For example, the commemoration of World Anti-Corruption Day was conducted by organising an anti-corruption poster-making contest, an anti-corruption exhibition, and an Anti-Corruption and Integrity Initiative Appraisal (Penilaian Inisiatif Integritas dan Anti Korupsi/PIIAK) program. In addition, the DGT organised an anti-corruption talk show, featuring anti-corruption activists, with the theme ‘United in Delivering Corruption-Free Transformation’ as a highlight of World Anti-Corruption Day 2015. The theme was raised with the expectation that the DGT employees would be united in helping to foster the DGT as an institution free from negative influences such as corruption, so that its work for Indonesia could be optimised.

Interviews recently conducted with DGT officials and others with a close knowledge of the DGT certainly suggest that there may have been a cultural shift with a positive change in the behaviour of DGT officials.⁷⁴ Noticeably they suggest, on a purely anecdotal basis, that corrupt activity has tended to decrease. In part this may be because officials are afraid to engage in corrupt activities because there is stronger penalty enforcement undertaken by the triple line internal defence mentioned in section 4.2 above (immediate supervisors, the DGT Internal Compliance Unit and the Inspectorate General of the Ministry of Finance) as well as external monitoring and control exercised by the KPK (the Corruption Eradication Committee). In addition, however, and based on the interviews, there appears to be a change in corporate culture, such that, whereas in the past it used to be common to find examples of ‘collective corruption’, in contrast, nowadays, a person acting in a corrupt fashion would more likely to be seen as an outlier or ‘strange person’.⁷⁵

But there is also a recognition that this is an ongoing process where vigilance must be maintained. As noted by Dick, corruption in Indonesia is no small problem; among the G20 nations, Indonesia’s perceived level of corruption is the worst except for Russia.⁷⁶ As such, the DGT recognises that it must continue to implement a series of carefully designed internal compliance programs with the aim of building integrity and trust in the system. To this end it is currently undertaking three initiatives as follows:

The ‘know your employee’ initiative

The DGT intends to make an initiative to ‘Know Your Employee’ a critical part of its culture. Direct supervisors will be expected to have a good understanding of their subordinates, based upon their performance and activities during working hours, as well as their lifestyles away from the office.

The role model program

This program is designed to create a culture where DGT leaders become role models, in terms of commitment and implementation of the values of the Ministry of Finance and the Employee Code of Conduct. With the commitment and role models of leadership, it is expected to motivate employees to continue to uphold and implement the values of the Ministry of Finance and Employee Code of Conduct.

The DGT care initiative

This is the development of a culture that should be emphasised within the DGT where officials are expected always to have a caring attitude towards the image of the DGT by not hesitating to remind fellow employees to always uphold the DGT Employee Code of Conduct and Discipline of Civil Servants and report those employees who show indications of violations, either to their immediate supervisor or through the whistleblowing system. This is designed to encourage a cultural change to one where an attitude of ‘I will not let anyone spoil the DGT’ becomes part of the

⁷⁴ Interviews conducted with Harry Gumelar from the Directorate Internal Compliance and Human Resource Transformation of the DGT; and with Yohanes (Tax academic and consultant); and Darussalam (Tax consultant and member of the Tax Reform team), on 25 January 2017.

⁷⁵ Based on the interview with Yohanes. As a former DGT official he may be in a good position to compare the ‘old condition’ and the ‘current condition’ of the DGT.

⁷⁶ Dick, above n 56, 14.

implementation of the Finance Ministry Core Values, particularly values related to integrity and professionalism.

Such initiatives, of course, may be judged to be effective, in the longer term, in helping to eradicate or mitigate the worst ravages of corruption within the DGT and helping to build trust between the taxpaying population of Indonesia and its tax officials. But – useful as they may eventually prove to be – they can only ever be a small part of the overall anti-corruption strategy. Many other instruments/levers and policy prescriptions will also be required. For example, as suggested by one of the interviewees, simplification of tax regulations is desperately needed so that the number of tax disputes can be reduced.⁷⁷ A reduction in the number of tax disputes inevitably removes a key set of opportunities for corruption and collusion.

Providing certainty in outcomes under tax laws and avoiding discretion wherever possible is also absolutely vital in reducing opportunities for corrupt behaviour by tax officials, taxpayers and their intermediaries. Sadly, it is therefore disappointing to end this article on a negative note. According to a government regulation issued in 2010⁷⁸ business enterprises that can persuade the relevant tax official that they are ‘pioneers’ – defined as those having ‘extensive linkages, providing high value-added and externalities, introducing new technology and having strategic value to the economy’ – may be granted unspecified special (discretionary) income tax treatment.⁷⁹ Whilst ever such discretions exist, surrounded by ill-defined and nebulous concepts, opportunities for corrupt behaviour by tax officials will continue to flourish.

This combination of complex tax laws (particularly when it comes to the process of tax dispute resolution as in the Gayus case), the discretionary power of tax officials (as was evident in the more recent Handang Sukarno case⁸⁰) and a general lack of adequate monitoring and supervision (notwithstanding the improvements noted above) is a toxic mix that is not easily tackled. Until it is, it will, sadly, continue to promote corrupt activity and bedevil the operation of the Indonesian tax system, and the role of the DGT in that system, for many years to come.

⁷⁷ Darussalam (Tax consultant and member of the Tax Reform team), interviewed on 25 January 2017.

⁷⁸ Number 94/2010. Article 29 is particularly open to abuse.

⁷⁹ McLeod, above n 56, 18-19.

⁸⁰ Handang Sukarno was the Head of the Sub-Directorate of Preliminary Audit in the DGT who was recently the centre of a corruption scandal in Indonesia.