

Tax Reform in Indonesia: The viewpoint of Tax Law and Tax Administration

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Taxation, one of the oldest of government function has been divided into three major areas – policy, law and administration. First you decide on a policy then you cast it into the technical requirements of a law, and finally you drop the problem of bringing in the money into the lap of the tax administrator. In the relationship between these three functions, the tax policy provides the design of the legal structure, and the legal structure is the framework on which an effective tax administration must be built. We must recognized that the three phase are interdependent and that the achievement of an overall sound tax system requires greater awareness of this interdependent.

Tax administration face for a formidable number of challenges in many developing countries and that is why some developing countries need a tax administration reform simply to achieve macro economic stability. There is a need to established a tax administration that can respond to the demands of a growing market economy and the resulting increase in the number of taxpayers. Moreover, there is the need to established legitimacy of tax collection and modernizing the tax administration so that it can operate effectively in an increasingly global economy.

While the specific issues and goals of fiscal policy may well differ from country to country within the same country as development process evolves, many of the problems and goals of tax administration are similar the world over. Generally, a tax administrators set as his goal the efficient assessment, collection and enforcement legally due, without undue to the government or the taxpayers in term of money, time or convenience.

Keywords: Tax Law, Tax administration

1. Introduction

In the last decade, the governments of most developing countries including Indonesia play a major role in stimulating and guiding the economic and social development of their nations. This public activity is characterized by efforts to increase national productivity and to raise living standards by distributing the benefits of increased productivity as widely as possible among populations

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Major issues still arise concerning how goals are to be achieved, whether primarily by public endeavor, through increased action by private enterprise, or by some combination of public and private activity. In whatever light government may be viewed by a people, however, no real progress toward the attainment of economic and social development can be achieved without the mobilization of resources. The **tax system** is often identified as one of the powerful levers available to these governments to move their economics from their present to the distinctly happier positions which invariably characterize the final year of development plan.

2. Tax System

Historically we have always discussed tax policy, tax law and tax administration in that order. First you decide on a policy, then you cast it into the technical requirements of a tax law, and finally, you drop the problem of bringing in the money into the lap of the tax administrator. Tax administrators is not only last, but only too frequently an afterthought; a technical functionary whose job it is to collect the revenue.

A tax system is like a three legged chair- the legs being policy, law, administration. Unless the three legs are equal in length and equally strong, the chair will be unstable. If one is shorter, as administration has usually been, there is a structural weakness. When that leg becomes sufficiently weak the whole tax system topples. In the relationship between these three functions, tax policy provides the design of the legal structure, and the legal structure is the framework on which an effective tax administration must be built. Since the three overlap, by the very nature of the relationship, the administrative feasibility of any tax measure must be given consideration on an equal basis. Thus, the simple logic of this analysis requires that the tax administrator must not only work closely with the tax planners and legal experts, he should be involved in each of the progressive steps from the very outset of a tax concept.

The tax system of a nation should reflect the social, economic and political aims of the government, and the administrative machinery should be able to implement it equitably and efficiently.. As a nation's economic goal expand and its policy objectives change and its industry grows, diversifies, and shifts geographically, like Indonesia nowadays, tax policy alters.

Tax policy proposals originate at both the executive and the House of Representatives (dewan perwakilan rakyat) levels. At a executive level, a number of agencies are involved, depending on the nature of the proposal. Equity-oriented reforms of the tax structure are the primary responsibility of the Ministry of Finance. Since mid of the year 2010 administration proposal are prepared by Badan Kebijakan Fiskal (Fiscal Policy Unit) in Ministry of Finance. The work

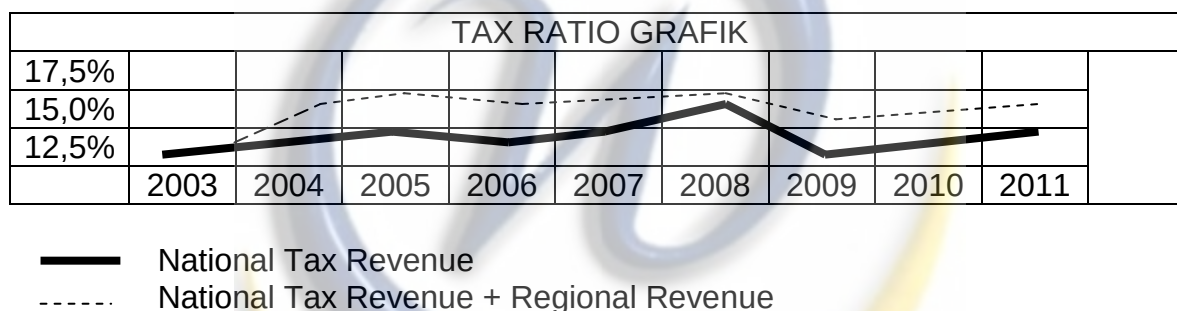
draws on a large staff of tax experts , economist and lawyers and it is a continuing process

Since 1984 up to now Indonesia change the tax system from official tax system to the self-assessment tax system, with some reason among others as follow:

- (1) To facilitate and encourage voluntary compliance with the requirements of the law;
- (2) To deter tax evasion and tax avoidance;
- (3) To maintain public confidence in the integrity of the tax system; and
- (4) To administer the tax legislation fairly, uniformly and impartially, as well as with diligence, firmness, courtesy and efficiency.

3. Tax ratio

The ratio between tax revenue and gross domestic products of my country in the last ten years is as follow:



As you have seen, the “taxation potential “ of my country –the proportion of its gross domestic product that can be diverted to public purposes without setting up intolerable political and social pressures-is around 11 – 13% from Gross Domestic Product, generally lower, and in many cases appreciably lower than that of asean country, like singapore, malaysia, thailand etc.

The taxation potential of a country is obviously greatly dependent on:

- a. real income per head;
- b. the degree of inequality in the distribution of income;
- c. the sectoral distribution of the national income and the social and institutional setting in which the output of particular sectors is procured;
- d. **the administrative competence** (and so forth) of the tax-gathering organs of the government.

It would be more correct to say, therefore, that the taxation potential of the country depends **on the excess of the actual consumption over the minimum essential consumption of the population** and of its investment with serves the needs of future luxury consumption. In practise, however “the minimum essential consumption “of a community can not be defined or measured; it is not just a

matter of biological requirements of subsistence (which themselves vary greatly with climate and location) but of social conventions and habits and the actual standard of living to which bulk of population of any particular community has become accustomed. Since governments ultimately depend on the concern of the people whom they govern, it is impossible as a matter of policy to compress, by means of taxation, the actual standard of living of the mass of population outside fairly narrow limits, though in a progressive country, with a rising income per head, it is always possible to raise the taxation potential over a period by slowing down the rate of increase in consumption.

While optimal taxation depends on the trade-off between “efficiency” and “fairness”. However the use of these concepts in optimal tax theory does not always correspond closely to lay usage. In the context of optimal tax theory; a fair tax, is one that guarantees a socially desirable distribution of the tax burden; an efficient tax is one with small excess burden. In public discussion, on the other hand, a fair tax is one that imposes equal liabilities on people who have the same ability to pay, and an efficient tax system is one that keeps down administrative and compliance expenses. These alternative notions of fairness and efficiency in taxation are the subject of the administrative competence

Along with the tax reform, the more important is that Directorate General of Taxes (DGT) must increase coefficient of utilization of tax potential. The low coefficient of utilization of that potential – due to **bad tax laws, bad tax administration**, or both – which in turn is only partly to be explained by lack of knowledge, understanding, or of administrative competence: it is also the result of resistance by powerful pressure groups who block the way to effective tax reform.

4. Tax Revision and Tax Reform

The task of improving the tax system is a constant one. The system must be kept up to date and its working considered against the changes constantly occurring in business structure and activities, in family patterns of organization and asset holding, in the economic and social objectives of our society. Alongside this work of modernization, of keeping the tax system responsive to current conditions and activities, is the work of correcting past mistakes. Efforts at improvement are often styled “**tax revision**” or “**tax reform**”.

The major concern of tax reformers has been the need to improve the equity of the tax structure so as to make it comply more nearly with prevailing view of what constitutes a fair distribution of the tax burden and with the effects of taxation upon the functioning of the economy. The administrative machinery must change with it, or the policy changes are not effectuated.

The prime objective of income tax reform is to achieve greater fairness in the tax system. This confidence has been seriously diminished. What we know and read about public attitudes indicates a lack of trust in the tax system, a belief that there are privileged groups escaping taxes, unilateral and bilateral tax evasion, including Corruption, Collusion and Nepotism. This view of the tax system, and in particular the income tax, is unfortunately – justified by the actual facts.

A second objective of income tax reform is to restore efficiency and economy in the expenditure of Government funds. To talk of these expenditure goals in the context of tax reform may appear strange at first. The usual image of tax reform focuses upon the persons and individuals escaping payment of their proper share of the tax burden and the steps required to correct that situation.

Since 1984, The Indonesian Government has been attempting to restructure our National Tax Law as follows:

1. Law of The Republic of Indonesia Number 6 of 1983 which was amended several times lastly by the Law Number 28 of 2007 Concerning General Provisions and Tax Procedures;
2. Law of The Republic of Indonesia Number 7 of 1983 which was amended several times lastly by the Law Number 36 of 2008 Concerning Income Tax;
3. Law of The Republic of Indonesia Number 8 of 1983 which was amended several times lastly by the Law Number 42 of 2009 Concerning Value Added Tax on Goods and Services and Sales on Luxury Goods;
4. Law of The Republic of Indonesia Number 12 of 1985 which was amended lastly by the Law Number 12 of 1994 Concerning Land & Building Tax;
5. Law of The Republic of Indonesia Number 13 of 1985 Concerning Stamp Duty;
6. Law of The Republic of Indonesia Number 18 of 1997 which was amended several times lastly by the Law Number 28 of 2009 Concerning Regional Tax and Retribution;
7. Law of The Republic of Indonesia Number 19 of 1997 which was amended several times lastly by the Law Number 19 of 2000 Concerning Tax Collection with Coerce Warrants;
8. Law of The Republic of Indonesia Number 21 of 1997 which was amended lastly by the Law Number 20 of 2000 Concerning Acquisition Duty of Right on Land & Building;
9. Law of The Republic of Indonesia Number 14 of 2002 Concerning Tax Court.

One of the very principle tax reform since 1984 is **the principle of self-assessment** is in no way a radical departure from several years tax practise (official assessment system) and the other significant changes in the income tax law is about a **tax rate and personal exemptions**.

5. Self-assessment

Self assessment is the sixth type of tax administration may be distinguished according to the degree of participation they require of the taxpayer or his agent, and the kind of response they elicit from the taxpayer. Under the self-assessment system, where the taxpayer is put under the greatest pressure, for he must supply all relevant information, the calculation of total income, the calculation of total tax free-income, the calculation of total taxable income, the calculation of tax due, and pay the tax, or some installment of it when he files his return. These function are the primary functions that are logically essential to the operation of income tax, while the other secondary functions that are not logically necessary for the operation of an income tax, but which are needed in practise as an aid to the primary functions: they are withholding of tax at source on some kinds of income, official assistant to taxpayers and checking and verification by the tax authorities of returns prepared by the taxpayer.

The Taxpayer also has ample opportunity to evade unilaterally by supplying false information or delaying payment, and opportunities, too, for bilateral evasion by corrupting assessors, auditors. or collector. The evasion rate in my country runs from 35 percent to possibly 50 percent. It is important, therefore, there must be a system for verification of taxpayer declaration, mistake – factual or legal, intentional or unintentional- are inevitable. Unless a tax system is guarded against intentional errors, they will inevitably increase, until the statute becomes unenforceable. Declaration must, therefore, be examined and verified, and when at fault, be corrected. When there is a recalcitrant taxpayer, the administrator must have a legal basis for proper investigation. The auditing of the taxpayers's book is the usual means whereby respect for the tax service in finding and punishing evasion is developed. On the effectiveness of this function hinges the percentage of tax evasion that my country will have and on the other hand, it is impossible to have enough agents to audit all tax returns. The actual money collected by my country tax service as a result of technical interpretation of laws, audit of returns per se, decision by tax lawyers, etc is a very small part of the total tax take. No country in the world including my country can afford an administrative system so large and costly that it could make every taxpayer to fill out the appropriate forms, assess himself the correct amount and voluntarily pay the taxes due, except we must develop of a climate of compliance (taxpayer conscience) in order to reach my country tax service philosophy. As you may know our Directorate General of Taxes philosophy, called "Tridarma Perpajakan", that is:

- a) Tax collection must cover all the tax subjects;
- b) Tax assessment must cover all the tax objects;
- c) Voluntary pay the taxes due.

6. Tax rate

Taxable Income is the basis for calculating the amount of income tax payable. In this Law, there are two classes of Taxpayer, namely resident Taxpayer and non-resident Taxpayer. For resident Taxpayer, there are basically two methods for determining the amount of Taxable income, namely the common calculation method and application of deemed profit method. In addition, there is a Special Deemed Profit which is applied to Certain Taxpayers based on the Minister of Finance Decree. For non-resident Taxpayer, the determination of Taxable Income can be differentiated between:

1. Non-resident Taxpayers conducting business or engaged in activities through a permanent establishment in Indonesia;
2. Other non-resident Taxpayer.

Article 17 Income Tax Law

(1) The tax rate applicable to each taxable income brackets is as follow:

a) Resident individual Taxpayer Taxable Income Brackets	Tax Rate Year	
	2008-2009	2010 - 2012
Up to Rp 50.000.000,00	5 %	5 %
Over Rp 50.000.000,00 up to Rp 250.000.000,00	15%	15%
Over Rp 250.000.000,00 up to Rp 500.000.000,00	25%	25%
Over Rp 500.000.000,00	30%	30%
b) Entities as a resident Taxpayer and permanent establishment	28%	25%

(2a) The tax rate as referred to in paragraph (1) subparagraph b becomes 25% (twenty five percent) which applies starting from the tax year of 2010.

(2b) Entity as a resident Taxpayer and public company whose at least 40% of their paid in capital are traded in the Indonesian stock exchange and meet other certain requirements can obtain a rate of 5% (five percent) lower than the tax rate as referred to in paragraph (1) subparagraph b and paragraph (2a), which is stipulated by or based on Government Regulation.

(2c) Tax rate applicable to dividend received by an individual resident Taxpayer is a maximum of 10% (ten percent) and final in nature.

(2d) Further regulation related to tax rate as referred to in paragraph (2c) shall be stipulated by the Government Regulation.

(2) The amount of taxable income bracket as referred to in paragraph (1) subparagraph a may be adjusted by the Minister of Finance Decree.

7. Tax incentives

Problems of taxation, in connection with economic development are generally discussed from two different points of view which involve quite distinct and often conflicting consideration: the point of view of **incentives** and the point of view of **resources**. Those who believe that it is the lack of adequate incentives which is mainly responsible for insufficient growth and investment are mainly concern with improving the tax system from an incentive point of view through the granting of additional concessions of various kinds, with less regard to the unfavorable effects on the public revenue. Those who believe that insufficient growth and investment is mainly a consequence of a lack of resources are chiefly concerned with increasing the resources available for investment through additional taxation, even at the cost of worsening its incentive effects.

Article 31A

- (1) Taxpayer who invest capital in certain sectors and/or certain regions that are high priority in the national scale, may be given tax facilities in the form of:
 - a. up to 30% (thirty percent) investment allowance;
 - b. accelerated depreciation and amortization;
 - c. extended loss carried forward but shall not exceed 10 (ten) years; and
 - d. the imposition of Income Tax on dividend as referred to in Article 26 of 10% (ten percent), unless the tax rate under the relevant tax treaty is lower.
- (2) Further regulations concerning certain sectors and/or certain regions that are high priority in the national scale as well as the tax facilities as referred to in paragraph (1) shall be stipulated by the Government Regulation.

Article 31E

- (1) Resident entity taxpayer with gross income of Rp50.000.000.000, 00 (fifty billion rupiah) receives facilities in the form of reduction of the rate by 50% (fifty percent) of the rate as referred to in paragraph (1) subparagraph b and (2a) of Article 17 imposed on taxable Income from the part of the gross revenue of Rp4.800.000.000, 00 (four billion, eight hundred million rupiah).
- (2) The amount of the gross revenue as referred to in paragraph (1) can be increased with the Minister of Finance Regulation.

Another tax incentives that have been issued are as follow;

1	Tax incentives on investment in certain sectors and or in certain regions	A taxpayer who invest in certain sectors and or certain regions may be granted tax incentives in the form of: a. Up to 30% investment allowance b. Accelerated depreciation and amortization c. Extended loss carried forward but shall not exceed 10 years, and d. Ten percent tax on dividends referred to in Article 26, unless the tax rate is lower under the relevant tax treaty
2	Integrated	Starting from the first of Januari 2001, a taxpayer who

	Economic Developing Area	undertakes business in an integrated economic development area may be granted income tax incentives as follows: a. Up to 30% investment allowance b. Choice of implementing of accelerated depreciation and or amortization c. Loss carried forward not exceed 10 years starting from the subsequent taxable year d. Income tax on dividend paid to non-resident at 10% or a lower tax rate in accordance with tax treaty.
3	Income tax borne by government on grand and foreign loan	Income tax payable on income received or accrued by contractor, consultant and main supplier who execute government project financed by foreign grant and or foreign loan shall be borne by government.
4	The exemption of foreign departure tax for an individual who departs abroad.	The exemption of foreign departure tax for an individual who departs abroad. a. Non resident who is present in Indonesia with tourist visa, transit visa, social culture visa, business visit visa and is present in Indonesia for not more than 183 days within 12 months period b. Foreign labors who work in Batam Island, Bintan Island and Karimun Island as far as employment tax of their salaries has been withheld by their employer c. Non resident who receives or accrues income in Indonesia and who does not reside or is present in Indonesia for not more than 183 days within 12 months period as far as their income has been taxed by their employer
5	Permanent establishment who reinvest its profit in Indonesia shall be exempted from 20% from branch profit tax referred to article 26	The profits of a permanent establishment shall not be subject to branch profit tax if the profit is reinvested in Indonesia subject to certain conditions as follows: a. The reinvestment is undertaken on whole profits after tax in the form of equity participation in a newly established company in Indonesia as a founder. b. The reinvestment shall be undertaken in the current year or not later than the subsequent year of the taxable year in which the profits is received or accrued. c. The equity is not transferred within at least 2 years after the company in which the permanent establishment has invested, starts a commercial production
6	Income tax article 22 on import of capital goods are not levied in bonded area	For a conductor of bonded area and for a business person conducted there in , government of Indonesia provide tax free on income tax article 22 on: a. Imports on capital goods and tools for building, constructing an developing the bonded area, and office equipments which are used only in the bonded area by the conductor of bonded area b. Imports of capital goods and other tools which have direct relation with production activities of a business person in the bonded area. c. Imports of goods and materials for processing in bonded area.

7	Tax free on withholding income tax by other parties	Tax payer have the right to propose exemption on withholding income tax by other parties to the Direktorat General of taxes if: - In a current taxable year the Tax Payer can proof that the business is not going to have tax liabilities due to fiscal loss, or - Tax Payer have right to compensate his fiscal loss as long as the amount of loss is bigger than net income projected for the taxable year, or - Income tax paid is bigger than projected income tax
8	VAT and Sales Tax on Luxury Goods are not levied.	VAT and Sales Tax on Luxury Goods liable since April 1st 1995 on: - Import of taxable goods - The use of taxable service from outside of Indonesian Custom area. - The use of intangible goods from outside of Indonesian Custom area. - Transfer of taxable goods and/or taxable services by main contractor In accordance with government projects funded by grant or foreign loan, is not levied only on part of government projects funded by the grant or foreign loan
9	VAT and Sales Tax on Luxury Goods are not levied	- VAT and Sales Tax on Luxury Goods are not levied on: - Goods or imported materials shipping to bonded area - transfer of local goods to the bonded area - VAT and Sales Tax on Luxury Goods are levied on transferred price of imported goods transferred from Tempat Penimbunan Berikat (TPB) with the imported purpose to be used as long as the transfer is not for parties which have custom and duty free or deferred facilities for imports. - A deferred of VAT and Sales Tax on Luxury Goods payments as guarantee transfer to Treasury of Direktorat General of Custom and Duty which control the bonded area, transfer of machines and tools plant for repair/maintenance purposes. Repair/maintenance is permitted at the latest 12 months from the date of machines and/or tools plant transfer out from the bonded area. Bonded Area. ○ Free on VAT and Sales Tax on Luxury Goods on import capital goods and tools for building/constructing/developing the bonded area and office equipments which are used only in the bonded area by the conductor of bonded area which already have permission Bonded Warehouse ○ Free on VAT and Sales Tax on Luxury Goods on import capital goods and tools for building/constructing the warehouse which already have permission Entrepot for exhibition purposes ○ Free on VAT and Sales Tax on Luxury Goods on import

		capital goods and tools for building/constructing the Entrepot for exhibition purposes which already have permission
10	VAT and Sales Tax on Luxury Goods are not levied	VAT and Sales Tax on Luxury Goods are not levied on: 1. Import of Goods and or materials to be proceeded. assambled and or attached on another goods for the export purpose 2. Proceeded goods which raw materials originated from import transfered to the bonded area. Free on VAT and Sales Tax on Luxury Goods is counducted by the head of Bapeksta Keuangan or the head of Kantor Pelayanan Kemudahan Ekspor Regional (KPKER) on behalf of Ministry of Finance.
11	Deffered payment of VAT and Sales Tax on Luxury Goods	On rendering of Taxable Services to firm, like PERTAMINA (National Oil & Gas Mining Enterprise), Joint Operation Contract, and the owner of geogthermal exploration and ecploitation license, that have not procedure yet in exploration and exploitation of geothermal resource, payment of VAT is deferred up to starting producing and the payment is made for ministry of finance account in Bank Indonesia.
12	VAT and Sales Tax on Luxury Goods not collected	VAT and Sales Tax on Luxury Goods have a facility not to be collected on the Firm in bonded area and/or firm in bonded area in KAPET region, for: a. Importation of capital goods or equipment for development/construction/expansion of bonded area and office device that merely used by bonded area. b. Importation of capital goods or other equipment that directly related to production activity of firm in bonded area. c. Importation of goods and/or material to process in firm in bonded area. d. Entering of taxable goods from other Indonesia Customs area to firm in bonded area to process e. Sending the product of firm in bonded area to other firm in bonded area for next porocessing f. Exportation of goods and/or material from firm in bonded area to firm in other Customs area or other firm in bonded area in case of subcontract. g. Transfer of taxable goods resulted by subcontractor in other Indonesia Customs area or other firm in bonded area to the origin firm in bonded area. h. Action of borrowing machine and/or other factory equipment in case of subcontract from firm in bonded area to firm in other Indonesia Customs area, or other firm in bonded area and then turn back to the origin firm in bonded area. For the firm doing business as firm of bonded area in KAPET region, VAT and Sales Tax on Luxury Goods have a facility not to be collected on importation of capital goods or equipment for development/construction/expansion of bonded

		area and office device that merely used by related firm of bonded area.
13	Accelerated Income Tax and VAT Refund	For Tax Payer that meet certain criteria can get tax refund of: a. IncomeTax within 3 (three) months b. VAT within 1 (one) month
14	Agreement of the avoidance of double taxation	Until now, Indonesia has an agreement of the avoidance of double taxation with 54 countries

8. Personal exemptions

(1) The amount of personal exemptions is as follows:

- a) Rp15.840.000,00 (fifteen million eight hundred and forty thousand rupiah) for an individual Taxpayer; (up to year 2008 – Rp 2.880.000,00);
- b) additional Rp1.320.000,00 (one million three hundred and twenty thousand rupiah) for a married Taxpayer; (up to year 2008 – Rp 1.440.000,00);
- c) additional Rp15.840.000,00 (fifteen million eight hundred and forty thousand rupiah) for married Taxpayers' spouse provided they file a joint tax return as referred to in paragraph (1) of article 8;(up to year 2008 – Rp 2.880.000,00);
- d) additional Rp1.320.000,00 (one million three hundred and twenty thousand rupiah) for each dependent family member related by blood and by marriage in a direct lineage, and an adopted child with a maximum of three dependents; (up to year 2008 – Rp 1.440.000,00 for each dependent).

(2) The application of paragraph (1) is based on the facts and circumstances at the beginning of a taxable year or fraction of a taxable year;

(3) The Minister of Finance, after consultation with the House of Representatives, shall stipulate the adjustment of personal exemptions.

Elucidation of:

Article 7

Paragraph (1)

In determining the taxable income of an individual resident Taxpayer, personal exemption is deducted from the net income. In spite of personal exemption for a Taxpayer himself, an additional amount of personal exemption is available to a married Taxpayer. A Taxpayer whose wife receives or derives income which is combined with his own income is given an additional personal exemption in respect of his wife amounting to Rp15.840.000,00 (fifteen million eight hundred and forty thousand rupiahs). A Taxpayer whose relatives through blood or marriage in direct lineage are fully dependent on the Taxpayer, such as parents, parents-in-law, children or adopted children, is granted an additional personal exemption for up to a maximum of 3 (three) people. Family members who are

fully dependent means family members who have no income and whose entire living expenses are borne by the Taxpayer.

Example:

Taxpayer "A" has a wife and 4 (four) dependent children. If his wife has income from an employer who has withheld income tax under Article 21 and the employment has no relationship to the business of her husband or other members of the family, the non-taxable income of Taxpayer "A" is Rp21,120,000.00 {Rp15,840,000.00 + Rp1,320,000.00 + (3 Rp1,320,000.00)}. As for the wife, at the time of Article 21 tax withheld by her employer, there is a personal exemption of Rp15,840,000.00. If the wife's income is combined with that of her husband, the non-taxable income granted to Taxpayer "A" would be Rp36,960,000.00 i.e. Rp21,120,000.00 + Rp15,840,000.00.

Paragraph (2)

The computation of personal exemption under paragraph (1) is determined by the status of the Taxpayer at the beginning of a taxable year or at the beginning of part of a taxable year. For instance, on January 1, 2009, Taxpayer "B" is married and has 1 (one) child. If a second child is born after January 1, 2009, the personal exemption of Taxpayer "B" for taxable year 2001 remains based on the marital status with 1 (one) child.

Paragraph (3)

Under this provision, the Minister of Finance is given an authority to adjust the personal exemption as described in paragraph (1) after consultations with the House of Representatives and by taking into consideration economic and monetary developments as well as developments in the annual cost of living index.

9. Modernizing the Tax Administration

The law or law administered are the very basis of the Directorate General of Taxes (Direktorat Jenderal Pajak) existence. They reflect the tax policy as well as other social and economic policies of the Government. The DGT does not set those policies, but it has the responsibility to administer, to make work, the laws passed by Legislative to carry them into effect. The Directorate General of Taxes, is not the "prima donna" in fiscal matters, but it has a fundamentally important role in making the tax system work, as well as in achieving the objective of certain other non-tax policies.

For the most part, however, the collection of taxes and contribution is the final direct purposes of all DGT activities. Both the scope and nature of these activities are governed by short and long term considerations. For the short term, we must concern ourselves with the application of current laws to current income and with the efficient operation of system to collect and account for the resulting taxes and contributions. For the longer term, we must concern ourselves with creating a

climate of public trust in the fairness, impartiality and firmness of our administration.

In year 1989, DGT has improved its tax administration by restructuring the organizational structure that gave priority to serve taxpayers. The improvement was done by splitting the District Tax Office into (1) Tax Service District Office (2) Tax Service District Office on Land & Building (3) Tax Audit and Investigation Office. The main function of Tax Service District Office is to serve taxpayer's right and obligation, while the Tax Audit and Investigation Office conduct examination and investigation the taxpayers in order to proof the taxpayer's compliance. By restructuring the Tax Service District Office that was based on type of tax, DGT failed to improve the performance of DGT, since there are still have job duplication, inefficiency, unilateral and bilateral tax evasion, and the taxpayer's difficulties in fulfilling their tax obligation.

In line with the increasing tax revenue, the DGT has proclaimed integrated and continuous work program as follows:

Year	Work program
2001	Internal Consolidation and Canvassing
2002	Knowing your Taxpayers
2003	Law enforcement
2004	National Data Base and Single Identification Number
2005	Toward Indonesia Sinergy
2006	Indonesia Sinergy
2007	Self sufficient Government Budget
2008	Legal certainty increase sistematically
2009	Collusion, corruption, and nepotism decrease sistematically
2010	Society welfare increase systemacally

Four strategig policies that have been supported by International Monetary Fund (IMF), World Bank and other international funds are:

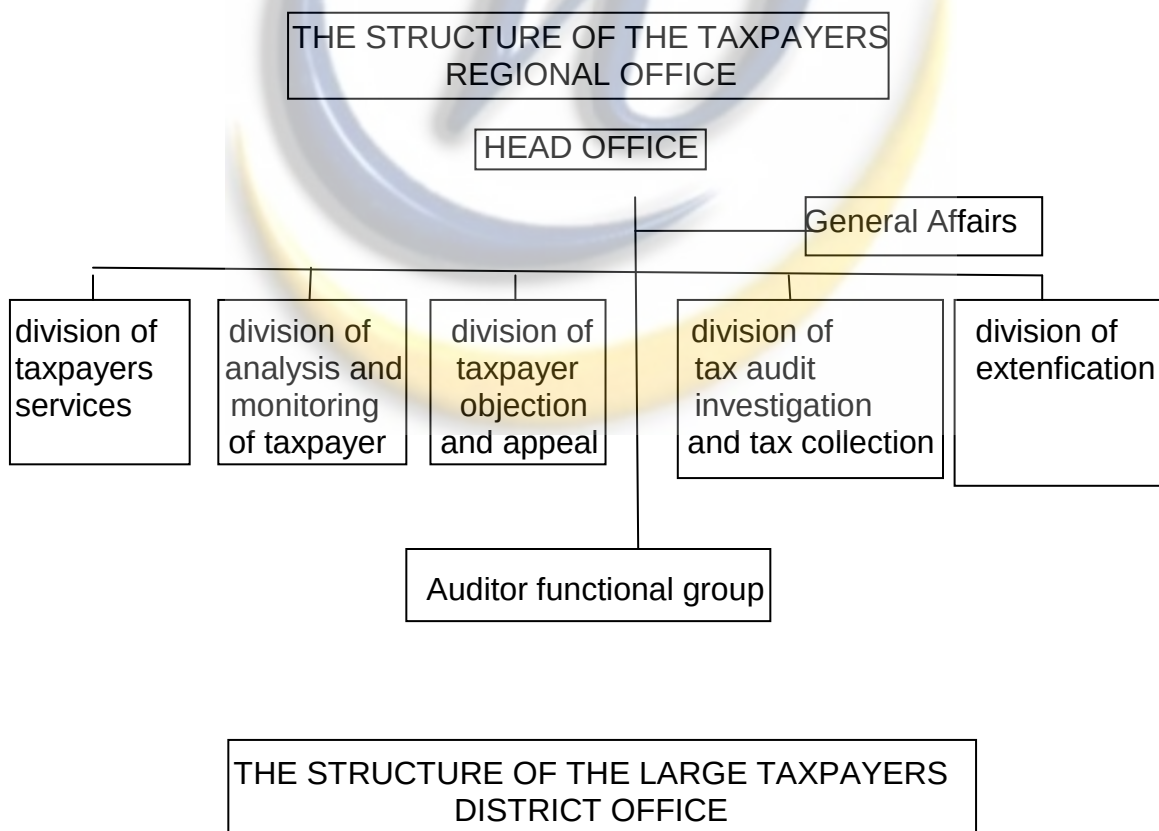
1. Creating Large Taxpayer Regional Tax Office and Large Taxpayers District Office under Direktorat General of Taxes that adiministrate certain Taxpayers who contribute large tax revenue;
2. Designing new automation system that integrates Direktorat of Budget for tax payment and tax return confirmation process;
3. Developing national audit plan concerning type and number of taxpayers that should be audit, amount to 15% (fifteen percent) of large and medium taxpayers based on data from other institutions, such as Directoret General of Customs (DGC) The DGC will send peridecally and using electronic media to DGT all acurate and up to date information of PEB, PIB, Income Tax Article 22, VAT and Sales Tax on Luxury Goods and others information for improving audit activities;

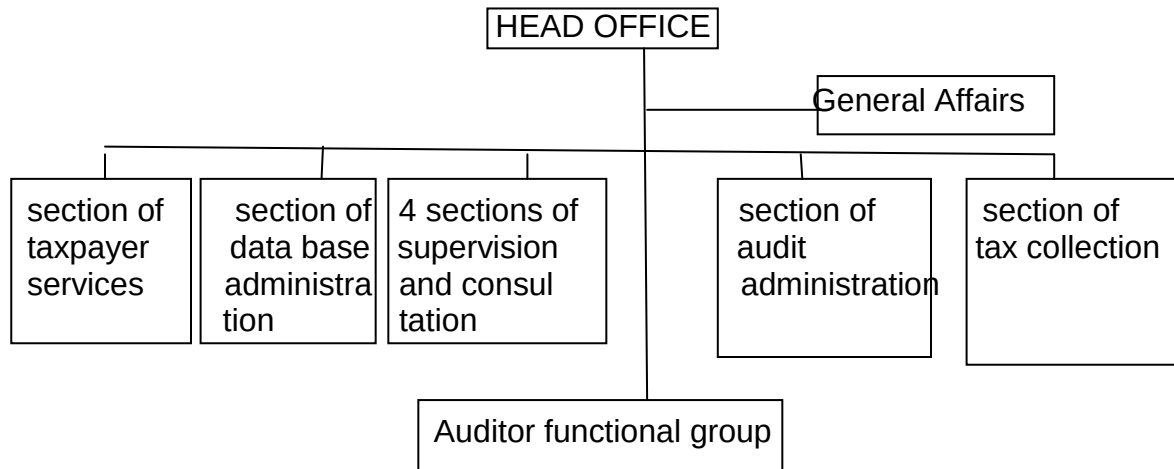
4. It plans to do tax arrears payment to cut the number of taxpayers who have tax arrears 25% of total tax arrears in year 2002.

In year 2002, a new type of Tax Service District Office was created based on function and professional in order to eliminate those above problems and was launched for the first time the Large Taxpayer Office (LTO) in Jakarta. This organization selects only around 300 taxpayers based on revenue, the amount of tax payment, and the amount of tax arrears. The purposes of establishment this Large Taxpayers Office, among others are:

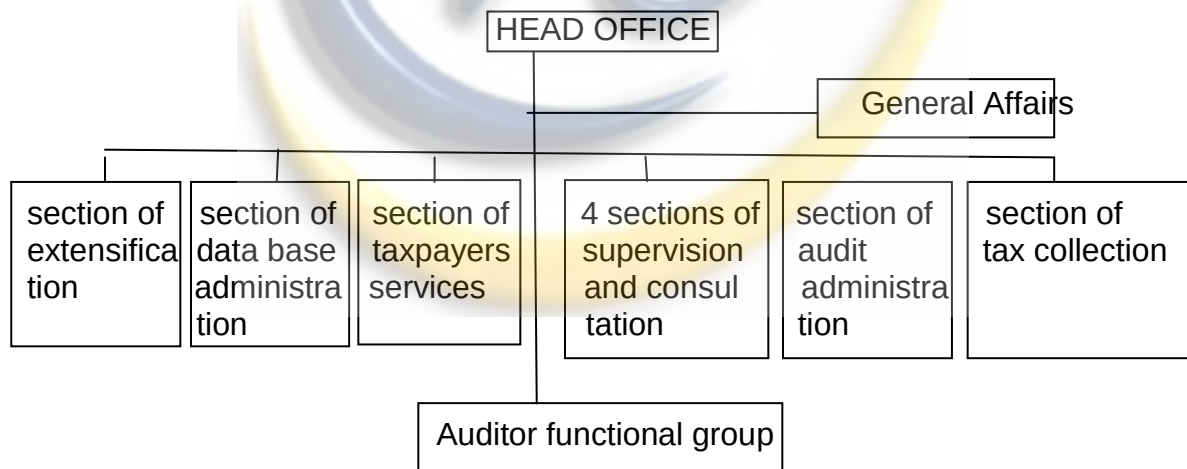
1. To change the tax administration becomes a modern tax administration;
2. To provide excellent services for the taxpayers;
3. Because of the small amount of taxpayers, controlling on each taxpayers become more accurate and simple;
4. To improve the image of Direktorat General of Taxes becomes better.

Following the establishment of Large Tax Office, there are changes on structure organization become modern structure organization and administration system as follows:





THE STRUCTURE OF THE MEDIUM AND SMALL TAXPAYERS DISTRICT OFFICE



10. Conclusions:

Two aspect of tax policy need to be considered. One is the formulation of tax laws and the other is all-important matter of tax administration. First you decide on a policy, then you cast it into the technical requirements of a tax law, and finally, you drop the problem of bringing in the money into the lap of the tax administrator.

If tax administration is effective, policy makers in government are permitted a wider range of action patterns and combinations. If administration is inadequate, the policy must of itself be inadequate, in that only the less sophisticated alternatives are practically available. If administration is so poor that the evasion rate is extremely high, policy decisions become basically an exercise in futility. The government then must depend on “charitable” contributions rather than on predetermined payments according to an economic plan. Tax administration, therefore, is the key to effective tax policy, rather than the reverse.

The term “tax reform” should be taken to refer not only to the establishment of new and heavier taxes – an interpretation prevalent today among quite a number of technical experts as well as the general public – but also to a true reconstruction of the tax system, which may involve new taxes but may at the same time imply the elimination or reduction of others. As one of the instruments of fiscal designed to expedite economic development and implement specific social principles, the tax system may lend itself to the furtherance of that policy’s objectives, but it cannot safeguard its efficiency by dissociating itself from the political and institutional environment. Consequently, efficient fiscal and administrative technique must be combined with sound political judgment if a tax reform is to be anything more than a mental exercise.

But, on the other side, in today’s world those traditional paradigms based on a compliance-oriented paradigm is an anachronism. Most taxpayers do not need to learn/know to generate tax information. Instead, they must learn to assess the reliability of tax information generated by tax specialists. And to use tax information to make good business decisions. This reflects the fundamental conceptual approach and emphasis on the role of taxes in the decision-making process. That is why, the task of improving the tax system is a constant one. The system must be kept up to date and its working considered against the changes constantly occurring in business structure and activities, in family patterns of organization and asset holding, in the economic and social objectives of our society.

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