Indonesian Tax Return Policy in the Perspective of Revenue, Equity, and Efficiency

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(Abstract)

The paper examines the tax return policies which have been implemented in Indonesia, after the introduction of self assessment system in 1984. Using a qualitative approach, the paper notes that the tax return policy swung from the equity perspective in 1984 to a more pragmatic policy in 1995, and finally it bounced back to the equity side in 2001. Furthermore, data reveals that the 2001 tax return policy, which obliges employee type individual taxpayers (EITs) to file tax returns, posted an obvious weakness from the efficiency side. In the period of 2001-2010, the number of individual tax returns increased significantly, but the individual tax revenues did not increase accordingly, and it was also marred by the occurrences of paradoxical situation in which number of tax returns had negative relation with tax revenues. However, in spite of its weakness, the 2001 tax return policy played crucial roles in promoting the equity in the tax system and increasing the tax awareness. Finally, the paper suggests several measures that may reduce the negative effects of the 2001 tax return policy.

Keywords: taxation, Indonesian tax return policy, tax return filing compliance, equity, cost efficiency, tax revenue

1. Introduction

It is reasonable that in collecting tax, the tax revenues earned have to be much bigger than the cost to collect them. Since so long, the need to implement more efficient tax system has risen in many jurisdictions, and numerous studies to promote more efficient tax systems have been conducted. Some tried to estimate the compliance cost, such as Slemrod (1984), Blazic (2004), and Moody (2005). The others analyzed the efficiency of tax administrations by comparing the administration costs, such as Ishi (2004). It is believed that the lower the collection cost per dollar of revenue earned, the more efficient the tax system is.

The tax collection cost is affected, for some extent, by almost all tax policies, and tax return policy is one of them. Nowadays, various tax return policies are implemented around the world. Based on tax return policies, countries can be grouped hypothetically into; 1) countries that require all of their taxpayers to submit tax returns, 2) countries that exclude certain group of taxpayers from the tax returns submitting obligation. For example, some countries exclude:

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a) taxpayers whose incomes are below a certain amount, b) taxpayers who are taxed through withholding mechanism.

Excessive tax return policies have taken parts in raising tax collection costs and creating unnecessary burden to society. These situations have triggered several studies on the possibility to reduce or even to abolish tax return filing obligation with varied results. For example, Leigh (2007) in Australia suggested that it would be beneficial to exempt most Australian taxpayers from tax returns filing obligation. On the other hand, Davidson (2009) argued differently; he pointed out the benefits of obliging people to file tax returns are greater than its costs. Meanwhile, study by Gale (2007) in the United States of America suggested that the idea to implement no-tax return systems would require considerable adjustments in self assessment tax regime.

In setting up an appropriate tax return policy, along with tax revenues, tax policy makers should consider the equity and efficiency aspects of tax revenues collection. Definitely, it is a big challenge. Equity and efficiency are as though two sides of one coin. If the efficiency is pushed to an extreme point, then the equity will be in precarious. On the other hand, if the equity is pushed to an extreme point then the tax system will be much more complicated. For example, in raising tax revenues, the head tax may be the most efficient tax as in such a system, every person would pay an equal lump-sum tax (Moody, 2005); thus, it does not need a complicated tax calculation. However, it has an obvious flaw that it neglects the ability to pay as one of the tax concepts in determining the existence of equity in taxation.

In the case of Indonesia, thus far, studies on tax return policies could not be found. Therefore, the present study through qualitative analysis attempts to provide an insight about Indonesian tax return policies from the perspective of equity and cost-efficiency of the tax system, and simultaneously investigates the impact of the tax return policies on the primary goal of taxation which is to raise tax revenues. Furthermore, the paper will center on individual annual income tax returns policies after the 1984 tax reform to the year of 2010.

The rest of paper is organized as follows. Section 2 elaborates the qualities of a sound tax system in particular the equity and efficiency of a tax system. Section 3 provides an overview about tax returns, and the development of tax return policy in Indonesia. Section 4 discuses the tax return policies in the perspective of the equity and efficiency, the statistic of tax returns, and the paradox of tax returns and revenues, and it also elaborates the positives and negatives of the 2001 tax return policy and policy implications. Section 5 contains conclusions.

2. The Qualities of a Sound Tax System

Scholars, tax experts, policy makers, and tax institutions for so long have come up with various concepts about qualities of ideal tax systems. For instance, Smith (1776) elaborated four qualities of a good tax system that were equity, transparency, convenience, and efficiency.

Stiglitz (1999) described five commonly accepted properties of a sound tax system which are: economic efficiency, administrative simplicity, flexibility, political responsibility, and fairness. In 2004, the European Commission-Common Consolidated Corporate Tax Base Working Group-issued a paper that elaborates eight general tax principles for the corporate income tax which are: 1) vertical equity, 2) horizontal equity, 3) efficiency/neutrality, 4) effectiveness, 5) simplicity, transparency, and certainty, 6) consistency & coherence, 7) flexibility, and 8) enforceability.

Multifaceted tax concepts brought by the scholars may seem bewildering. However, some ideas appear to have similarities even though the scholars addressed them in different ways and terminologies. Based on their relative positions to the pole of taxpayer's interest or to the pole of state's interest, the concepts can be put into two groups. The concepts of equity, certainty, and convenience are relatively closer to the taxpayers' interest rather than the state' s interest. It is because he or she, as a person who, bears the tax that a taxpayer would likely put significant concern on the fairness of the tax burden sharing, the certainty of the amount of tax, and convenience in paying taxes. On the other hand, the concepts of cost efficiency, economic efficiency, flexibility, political responsibility, effectiveness, enforceability have the inclination to the interest of states rather than the interest of taxpayers.

Among the many principles of a sound tax system, equity and efficiency have become the bywords among executives, legislatives, and public in striving for a sound tax system. Generally, equity principle is viewed from how fair tax burdens are shared among people. Furthermore, it is widely accepted that people with similar economic level should pay a similar amount of tax (horizontal equity) and people with higher economic level should pay higher tax (vertical equity). These equities refer to "ability-to-pay" concept as elaborated by Smith (1776) in his book The Wealth of Nations. He said, "The subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state."

However, tax burden can also be viewed from another perspective; from the formal aspect of taxation, not from the amount of taxes which each taxpayer has to pay. It is because taxation can afflict people not only from the amount of taxes that they should pay, but also from the tax procedures that they have to undergo in order to pay the taxes. From this point of view, a tax system is deemed to be fair if there is equality in tax procedures for all taxpayers no matter what the sources of incomes are. Businessmen, professionals, employees and others, as long as they receive a similar amount of incomes, shall be treated similarly.

Another issue in taxation is efficiency in collecting taxes. Most literatures define efficiency in two different ways. First, efficiency is defined as economic efficiency. It means that the tax system should be neutral to ensure that investment decisions take into account the best location from an economic perspective, Stiglitz (1999).

Second, efficiency is defined as cost efficiency. It means that tax should be collected at low cost as possible. Smith (1776) mentioned "Every tax ought to be so contrived, as both to take out and to keep out of the pockets of the people as little as possible, over and above what it brings into the public treasury of the state." Tax collection cost refers to all costs above tax payments that are incurred by both taxpayers (compliance costs) and tax offices (administration cost), in order to fulfill the requirements stated on tax regulations and to administer the tax itself. The tax collection cost efficiency can be improved by reducing costs that incurred in taxpayers' side, in tax offices' side or the both sides. In taxpayers' side, compliance costs cover expenses such as stationery, printing, copying, stamp, transportation, and non monetary aspects such as time spent, anxiety, opportunity costs. In tax offices' side, administration costs covers all costs and expenses for running in tax offices such as facilities, employees' expenses, utility expenses, compliance checking expenses, and other expenses.

3. Tax Returns, Taxpayers, and Tax Returns Policies in Indonesia

3.1. Tax returns

Indonesian general provisions tax law defines an income tax return as a form used to report tax calculations, tax payments, taxable objects or non taxable objects, assets, and liabilities in accordance with tax provisions[1]. There are two types of tax returns: interim tax returns and annual tax returns. Interim tax returns have to be submitted on a monthly basis; however, for eligible small businesses and taxpayers in remote areas, they may submit a combining interim tax return[2]. Meanwhile, annual income tax returns have to be submitted once a year. For individual taxpayers, annual tax returns have to be submitted no later than 3 months after the end of the tax year (March 31).

In the tax year 2010, three different forms of annual income tax returns were available for individual taxpayers:

a. Form 1770. For individual taxpayers who earn a) incomes from businesses or professional services, b) incomes from employments, c) incomes that are taxed with final withholding mechanism, or d) incomes from other sources.
b. Form 1770 S (simple tax return). For individual taxpayers who earn a) incomes from employments, b) incomes from other domestic sourced, or c) incomes that are taxed with final withholding mechanism.
c. Form 1770 SS (very simple tax return). For individual taxpayers who earn incomes solely from one employer; less than Rp60 million and they do not have other incomes except interest incomes from banks or cooperatives.

3.2. Taxpayers

Indonesian income tax is imposed on four groups of taxpayer: 1) an individual, 2) an undivided inheritance in lieu of the beneficiaries, 3) an entity and 4) a permanent establishment. Individual taxpayers cover Indonesian citizens and foreigners who earn incomes from Indonesia.

Individual taxpayers can be classified into several categories. For instance, they can be categorized as resident taxpayers or nonresident taxpayers. The income tax law defines resident taxpayers as; 1) any individual who lives in Indonesia, 2) any individual who is present in Indonesia for more than 183 days within any 12 months period, or 3) any individual who intends to reside in Indonesia. Meanwhile, nonresident taxpayers are: 1) any individual who does not reside in Indonesia, or 2) any individual who is present in Indonesia for not more than 183 days within any 12 month period, who receives or earns income from Indonesia.

There are two distinctive tax treatments applied to each category above. First, resident taxpayers pay income taxes on a worldwide income basis which means that they have to pay taxes not only on Indonesia sourced incomes but also incomes from abroad, while nonresident taxpayers only pay taxes on Indonesia sourced incomes. Second, resident taxpayers have to submit annual tax returns, while nonresident taxpayers do not.

Furthermore, individual taxpayers can also be categorized based on their main active incomes:

a. The employee type individual taxpayers (EITs)

   The EITs are individuals who earn incomes through employment, for example, civil servants, private companies' employees, labors, part-time workers and outsourcing workers. They may earn incomes from one employer or multiple employers. Based on this, the EITs are grouped further into a) the EITs who receive incomes solely from one employer (EIT-OEs) and b) the EITs who receive incomes from more than one employer or other sources (EIT-MEs).

b. The self employed type individual taxpayers (SEITs)

   The SEITs are individuals who earn incomes from conducting businesses and professional activities. It includes sole proprietor businessmen, farmers, and professionals such as doctors, notaries, actuaries, accountants, engineers and lawyers.

The main difference of the EITs and the SEITs lies on the tax payment fulfillment method. In monthly basis, the EITs' employment incomes are taxed through withholding mechanism while the SEITs incomes are taxed through self assessment system, though not without exception, several SEITs' incomes such as professional services are taxed by the combination of withholding and self assessment system.

3.3. The Development of Indonesian Tax Returns Policies

In year 1984, Indonesia embarked in a significant change of its tax system. At that time, a self assessment tax system was introduced which partly aimed to increase people's awareness and participation in taxation[3]. Since then, in terms of tax registration policies, Indonesian taxation can be divided into three periods: a) 1984-1994, b) 1995-2000, and c) 2001-2010 (the current state).

Table 1 shows that, in the first period (1984 to 1994), the 1984 tax return policy regulated that all taxpayers including the EIT-OEs have to file annual income tax returns. In the second period (1995 to 2000), the 1995 tax return policy regulated that all taxpayers have to file tax returns, except for a) individual taxpayers whose incomes are equal or less than the amount of personal exemption and b) individual taxpayers who receive income solely from one employer (EIT-OEs). In the third period (2001 to 2010), similar with the 1995 tax return policy, the 2001 tax return policy regulates that all taxpayers have to file tax returns, but it only exclude one segment of taxpayers which is the individual taxpayers whose incomes are equal or less than the amount of personal exemption. Unlike the 1995 tax return policy, the 2001 tax return policy requires the EIT-OEs to file tax returns.

Table 1 : Tax Returns Filing Policies during 1984-2010

Year 1984 to 1994	Year 1995 to 2000	Year 2001 - 2010 (the current state)
All taxpayers have to file tax returns.	All taxpayers have to file tax returns, except for: • Individual taxpayers whose incomes are equal or less than the amount of personal exemption. • Individual taxpayers who receive income solely from one employer.	All taxpayers have to file tax returns, except for Individual taxpayers whose incomes are equal or less than the amount of personal exemption.

Source: article 3 of the Law of the Republic of Indonesia Number 6 of 1983, article 3 of the Law of the Republic of Indonesia Number 9 of 1994, and article 3 of the Law of the Republic of Indonesia Number 16 of 2000.

From the three tax policies above, it can be seen that the main difference in the 1984, 1995, and 2001 tax return policies lied on the issue of whether an employee who works merely for one employer (EIT-OE) has to file annual income tax return or not.

4. Discussions on the Tax Return Policies

4.1. Tax Returns Policies in the Perspective of the Equity and the Efficiency

The three tax return policies mentioned previously have different implication on the balance of equity and efficiency aspects of Indonesian tax system. To begin with, the 1984 tax return policy emphasize more on the equity (fairness) as it treated all taxpayers in the same way; all of them have to submit annual tax returns. However, it had a main weakness on the efficiency issue (tax collection cost).

Under the 1984 tax return policy, theoretically, the percentage of the total tax collection costs to total tax revenues would be relatively high as it obliged all taxpayers to file tax returns, no matter how big or small their incomes. As an illustration, taxpayer ABC who is liable for only Rp100,000 may have to spent a bigger amount of money in order to submit his/her tax return. For instance, he/she has to spent Rp200,000 for stationery, printing, copying, stamp, and transportation expenses. If the tax offices spent Rp1 administration expense for each taxpayer, then the total collection cost will be Rp200,001. This simple illustration shows that the compliance cost plus administration cost are higher than the tax revenues, a condition that should be avoided by a sound tax system.

The next policy was the 1995 tax return policy. In the perspective of cost efficiency, the total tax collection cost under the 1995 tax return policy would be theoretically lower than the 1984 tax return policy. Because, different from the 1984 tax return policy, the 1995 tax return policy excluded two segments of taxpayers from tax returns filing obligation. One of them is the low income taxpayers, and the other is the employee type taxpayers who received income solely from one employment (EIT-OEs). There are several reasons to exclude the two segments of taxpayers from the tax return filing obligations. First, under the income tax law, taxpayers who earn incomes below the personal exemption do not have to pay taxes. Second, the EIT-OEs' employment incomes are taxed through withholding mechanism. Thus, generally, there are no additional tax dues that they have to pay and should report in annual income tax returns. Therefore, excluding the low income taxpayers and the EIT-OEs would lower the tax collection costs as it minimized the number of the zero or low payment tax returns.

However, the 1995 tax return policy also had several problems. One problem in implementing the 1995 tax return policy was in identifying whether an employee is an EIT-OE or an EIT-ME. This obscurity hampered tax offices in taking necessary actions if employee type taxpayers did not file tax returns. Another one, the 1995 tax return policy might reduce the EIT-OE' s tax awareness. For instance, Mr. A is an employee of XYZ Company. He usually only earns salaries, therefore, as an EIT-OE, by the regulation Mr. A does not have to submit tax returns. These situations run for many years that may make him does not aware about the tax return filing regulations in details. Therefore, when, for a certain year, he occasionally received other incomes such as incomes from an informal sector, he might be not aware that he has to submit a tax return. In a worse scenario, Mr. A does aware about his tax obligation, but he intentionally tries to evade paying taxes by pretending as though he is still an EIT-OE who does not have an obligation to submit a tax return.

If an employee type taxpayer (EIT) does not submit a tax return, unless there are data, tax offices will face difficulty in determining whether he/she is an EIT-OE or an EIT-ME. It was an obstacle in upholding the 1995 tax return policy. For example, the General Provisions Tax Law regulates that tax offices can issue the reprimand letters if taxpayers failed to submit tax returns[4]. However, since there are uncertainties in identifying whether a taxpayer has an obligation to submit a tax return or not, then the process to issue a reprimand letter could be delay or if it is issued, there is a possibility that the tax offices may issue it mistakenly.

The last is the 2001 tax return policy (the current tax policy). It revoked the tax treatment privilege that EIT-OEs have enjoyed during the 1995-2000. The 2001 tax return policy only excludes one segment of taxpayers from the tax return filing obligation which is the low income taxpayers. As a consequence, all EITs whether they are EIT-OEs or EIT-MEs are treated similarly. All of them have to submit tax returns. Therefore, in the term of tax equity, the 2001 tax return policy is closer to the equity side than the 1995 tax return policy.

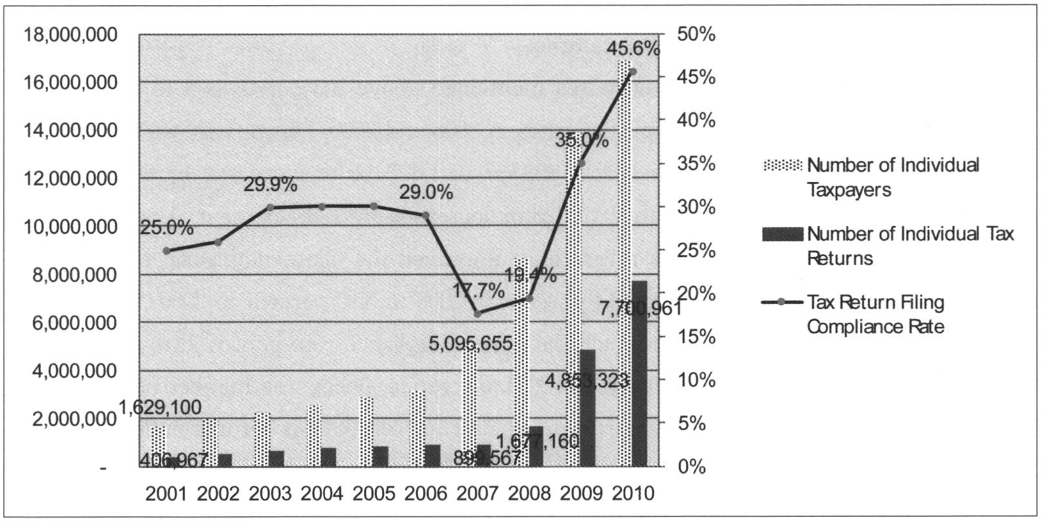
In conclusion, the three tax return policies elaborated above have their own advantages and disadvantages. From equity and efficiency perspective of a tax system, they show that Indonesian tax system has shifted from emphasizing on equity in the 1984 tax return policy to a more pragmatic way which focused on efficiency in the 1995 tax return policy, and finally in 2001 tax return policy it moved once again to equity side.

4.2. Tax Returns Filing Compliance Rate

Tax return filing compliance rate is the ratio of the number of tax returns divided by the number of taxpayers. It measures the level of taxpayers' obedience in submitting tax returns. As aforementioned, Indonesian taxation period can be divided, based on its tax return policy, into three periods: a) 1984-1994, b) 1995-2000, and c) 2001-2010 (the current state). In the last period, the 2001 tax return policy regulates that all taxpayers have to file tax returns except for individual taxpayers whose incomes are equal or less than the amount of personal exemption.

Figure 1 shows that, in the period of 2001-2007, the 2001 tax returns policy has increased the number of tax returns, but at slow paces. In 2001-2007, the number of tax returns increased 1.21 times from 406,967 at the end of 2001 to 899,567 at the end of 2007, but the number of registered individual taxpayers increased higher. It increased 2.13 times from 1,629,100 in 2001 to 5,095,655 in 2007. As the result, even though the number of tax returns increased, the filing compliance rates remained low. They fluctuated around 17.7 percent to 29.9 percent. The low levels of filing compliance rate point out that huge number of individual taxpayers did not care about the filing obligation. For example, in 2006 and 2007, around 71.0 percent and 82.3 percent taxpayers did not file tax returns respectively. The low levels of filing compliance rate may also indicate that there were problems on 1) the taxpayer's obedience toward tax laws, 2) the law enforcement, or 3) the 2001 tax return policy itself.

Figure 1: The Individual Tax Return Filing Compliance Rates 2001-2010



Source: Writer's calculations.
Notes:
a) The number of individual taxpayers data are from:
- 2001-2008 from the tax handbook in numbers 2001-2009 -DGT (2010),
- 2009-2010 from the directorate general of taxes' annual report 2010-DGT (2011).

b) The number of individual tax returns data are from:
- 2001-2009 from the tax handbook in numbers 2001-2009 -DGT (2010),
- 2010 from unpublished raw data-DGT (2012).

Furthermore, in order to increase taxpayers' compliance rate, in 2008, a program name "sunset policy" was launched. The sunset policy offered administration sanctions deduction or removal for those of taxpayers who submits the unreported tax returns or the amended tax returns during the sunset policy period: January, 1 2008 to March 31, 2009. The sunset policy also guaranteed that there will be no tax audit on the taxpayers, unless there are data that show the submitted tax returns are incorrect[5].

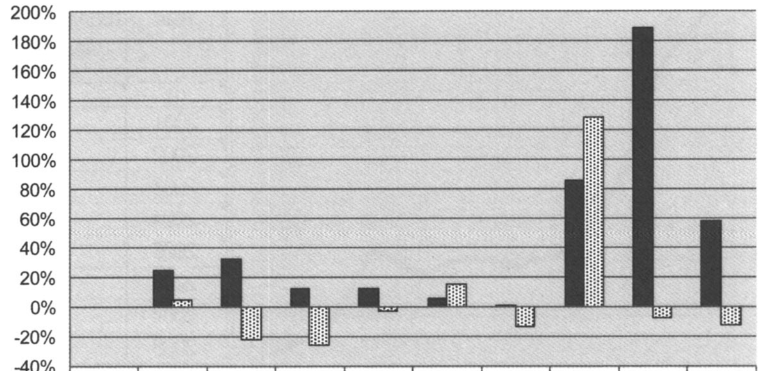
Besides the sunset policy, several other measures may influence the tax return filing compliance such as the 2002-2008 tax administration reform, simpler tax return forms, and the "drop box" program. The drop box program, implemented firstly for the 2008 tax returns, aims to make tax return submitting process easier. Normally, taxpayers have to go to a tax office to hand in their tax returns which may make them have to spend some times and disburse some in order to submit the tax returns. In addition, in the tax office, they have to spend some more times waiting the tax officers doing their business such as, checking the completeness and formal aspects of the tax returns. For busy taxpayers, it is a problem because they do not have much spare time, and for low income taxpayers, it is a problem because they have to spend some money in submitting tax returns. To minimize these hassles, during peak seasons (in March for individual taxpayers), tax offices set up "drop boxes" in the shopping malls, business centers, office buildings, factories, and other busy places. At the drop boxes, the tax return receiving processes are relatively faster as tax officers do not do details checking as in the tax offices. Thus, taxpayers will spend shorter times, and they can choose any location that is most convenience to them in submitting tax returns.

The sunset policy and other measures mentioned above have managed to increase the number of tax returns and the compliance rates in 2008 and 2009. Figure 1 shows that, in 2008, the number of tax returns increased from 899,567 to 1,677,160 or increased by 86.44 percent. Furthermore, in 2009, it increased to 4,853,323 or increased by 189.4 percent. Along with that, the increases on the number of tax return have improved the filing compliance rates. The filing compliance rates increased from 19.4 percent in 2008 to 35.0 percent in 2009. This increasing trend continued in year 2010 in which the filing compliance rate improved to 45.6 percent. Thereupon, after the implementation of the 2001 tax return policy, the number of tax returns increased 17.92 times from 406,967 tax returns in 2001 to 7,700,961 tax returns in 2010.

4.3. Tax Returns and Revenues Paradox

The soaring numbers of tax returns has raised a question on "how did they affect the tax revenues?". Intuitively, if the number of tax returns increases, the tax revenue will increase, as well, but it does not always be like that. Figure 2 shows these phenomena. In year 2002, 2006, and 2008, the increase on the number of tax returns had positive relations with the increase on tax revenues. For instance, in 2006, the number of tax returns increased by 5.5 percent, and it positively affected the tax revenues. Tax revenues increased with a higher percentage, 15.6 percent. Similarly, in 2008 the number of tax returns increased by 86.4 percent, and it also increased the tax revenues. Tax revenues increased by 129.1 percent.

Figure 2: The Comparison of the Percentage Change of Number of Individual Tax Returns and Individual Income Tax Revenues 2001-2010



	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
∆ Tax Returns		24.8%	32.4%	12.6%	12.5%	5.5%	0.2%	86.4%	189.4%	58.7%
∆ Revenues		4.7%	-21.7%	-25.8%	-2.6%	15.6%	-13.2%	129.1%	-7.2%	-12.3%

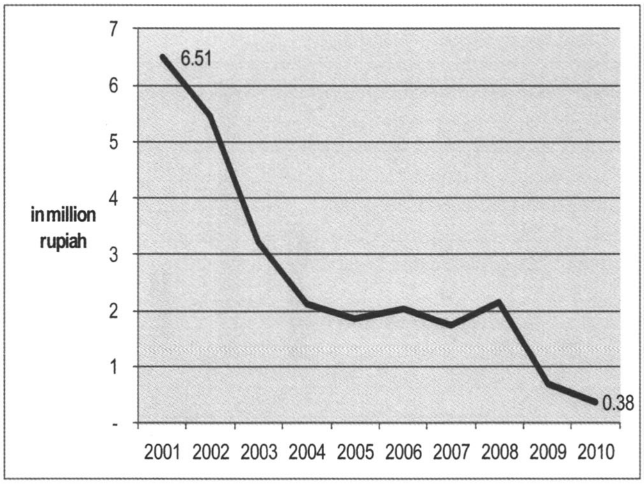
Source: Writer's calculations.
Notes:
a) The number of individual tax returns data are from:
- 2001-2009 from the tax handbook in numbers 2001-2009 -DGT (2010),
- 2010 from unpublished raw data-DGT (2012).

b) The individual income tax revenues data are from:
- 2001-2009 from the directorate general of taxes' tax revenues statistic –DGT (2010),
- 2010 from the central government financial report 2010.

However, the positive relations between the number of tax return and the tax revenues do not always occur. Figure 2 shows that paradoxical conditions occurred in year 2003, 2004, 2005, 2007, 2009, and 2010. At those years, the numbers of individual tax returns increased, but they could not generate higher tax revenues. On a contrary, tax revenues drop to lower amounts. The phenomena became especially clear in 2009 and 2010. In 2009, the number of tax return increased significantly by 189.4 percent, but tax revenues decreased by minus 7.2 percent. Similarly, in year 2010, the number of tax return increased by 58.7 percent, but once again tax revenues down by minus 12.3 percent.

Besides the paradoxical conditions, another issue on the relationship between the number of tax returns and tax revenues is about the tax returns' ability to bring revenues. After the 2001 tax return policy implemented, the tax returns' ability to bring revenues, in average, have plunged. Figure 3 shows that the average tax revenues per an individual tax return in 2001-2010 were in a decreasing trend. In 2001, individual tax returns in average generated Rp6.18 million tax revenues; however, it was decline ever since. In the last three years, the average tax payables reported by individual taxpayers in their annual tax returns have plummeted significantly. The average tax payables reported in 2008, 2009, and 2010 tax returns were Rp2.15 million, Rp0.69 million, and Rp0.38 million. Thus, the average tax payables reported in the 2010 tax returns has dropped 17.07 times compared to those reported in the year 2001 tax returns.

Figure 3: The Average Tax Revenues per an Individual Tax Return 2001-2010



Year	Number of Individual Tax Returns	Individual Income Tax Revenues in billion Rp
(1)	(2)	(3)
2001	406,967	2,648
2002	507,965	2,773
2003	672,370	2,172
2004	756,864	1,612
2005	851,190	1,570
2006	898,036	1,815
2007	899,567	1,575
2008	1,677,160	3,608
2009	4,853,323	3,347
2010	7,700,961	2,935

Source: Writer's calculations.
Notes:
a) The number of individual tax returns data are from:
· 2001-2009 from the tax handbook in numbers 2001-2009 -DGT (2010),
· 2010 from unpublished raw data-DGT (2012).
b) The individual income tax revenues data are from:
· 2001-2009 from the directorate general of taxes' tax revenues statistic -DGT (2010),
· 2010 from the central government financial report 2010.

There were several factors that may explain why the paradox of tax returns and revenues occur. First, most of the individual taxpayers are employee type individual taxpayers (EITs). Perhaps, more than 80 percent of registered individual taxpayers in 2010 were EITs[6]. Hence, the biggest part of the individual tax returns was EITs' tax returns which did not generate sizeable additional tax revenues unless the EITs had substantial other non-employment incomes. As aforementioned, the EITs' incomes: salaries, wages, and other employment incomes are taxed through withholding mechanism in every paycheck they received. Therefore, at the end of the year, for the EIT-OEs, the tax dues will be zero; no additional tax payment should be made. However, for the EIT-MEs, certainly, they have to pay additional taxes on their other incomes.

Second, several tax policy changes have contributed to the lower amount of tax revenues, for instance, the changes on the personal exemption. During 2001-2010, the government has increased the amount of personal exemption three times: in 2005, 2006, and 2009. In 2005, there was a sharp increase in the personal exemption. For instance, the personal exemption for single taxpayers increased by more than 300 percent, from Rp2,888,000 to Rp12,000,000; for married with no child taxpayers, it increased 206 percent from Rp4,320,000 to Rp13,200,000[7]. Furthermore, in 2006 and 2009, the personal exemption for single taxpayers increased by 10 percent and 20 percent. Another policy change that affected the tax revenues was the change on income tax rates. In the tax year 2009, the government reduced the individual income tax rate;

the highest rate reduced from 35 percent to 30 percent, and the interval of income bracket for the lowest rate (5 percent) increased from Rp25,000,000 to Rp50,000,000.

Third, some taxpayers naturally try to minimize their taxes, or even avoid paying taxes especially if the possibility to be caught is low. This is also the case in Indonesia, though there is no complete data about the amount of tax avoidance, some wealthy taxpayers, including the EITs avoid paying taxes properly. It was a factor that made Indonesian tax ratio low. In 2010, the tax ratio was 11.06 percent , much lower than the 2010 OECD countries' average tax ratio, 33.8 percent (OECD, 2012).

4.4. The Positives and Negatives of the 2001 Tax Returns Filing Policy and Policy Implication

In self assessment tax system, the tax return is a fundamental document because a tax return is a legal document in which a taxpayer declares that he/she has reported all taxable incomes, tax calculation, and tax payments in accordance with tax laws and regulations. Thus, in a case there are unreported incomes or other irregularities detected by tax offices then tax offices will have a legal base to ask taxpayers' accountability.

Furthermore, obliging people to submit tax returns increase tax awareness. It encourages people to learn about many aspects of taxation, in particular that related with them such as how to fill a tax return properly, how to pay taxes, their tax rights and obligation, and many others. In contrary, if people are not obliged to submit tax returns, their concern about taxation may be lower as taxation is not a big issue for them. Thus, obliging people to submit tax returns is indispensable for a nation. It is not only increase people's consciousness on how government spent the tax money, but it also encourages people to exercise vigilance over government's performances which eventually will be beneficial in fostering good governance as a fundamental requirement for a country's prosperity.

The 2001 tax return policy provides several positives things. First, it promotes the equity in the tax system and increases tax awareness. By only excluding the low-income taxpayer, it puts all taxpayers including the EIT-OEs in the same tax treatment. Thus, the only thing that makes people treated differently in the obligation to submit tax returns is whether they earn incomes above the personal exemption or not. For instance, businessman who earns Rp10 million and an employee who earns the same amount of income will have the same obligation in submitting a tax return.

The significant increase on the number of tax return from 406,967 in 2001 to 7,700,961 in 2010 might reflect that the 2001 tax return policy, for some extent, succeeded in promoting equity as it distributed the tax burden to a bigger number of people, and it also managed to reduce the number of people who were able to eschew from the tax office administration nets.

Another one is that the 2001 tax return policy is relatively easier to be implemented compared to the 1995 tax return policy. As previously mentioned, under the 1995 tax return policy, there was a difficulty in determining whether a tax payer is an EIT-OE or an EIT-ME. The problem did not appear in the 2001 tax return policy. Under the 2001 tax return policy, the tax offices do not need to differentiate whether an employee is an EIT-OE or an EIT-ME. If an employee type taxpayer does not submit a tax return, tax offices can take further necessary actions as for sure that is a tax violation.

However, the 2001 tax return policy also has a couple of weaknesses. Its main drawback is in the tax collection cost-efficiency. First, there was a big gap between the increase on tax collection costs and the increase on tax revenues. By assuming that the tax collection cost increases proportionally with the increases on the number of tax returns, then, during 2001-2010, the tax collection cost might increase by about 17 times, similar with the increase on the number of tax returns. However, in fact, the tax revenues only increased by 0.2 times. Thus, it can be argued that the 2001 tax return policy is less efficient compared to the 1995 tax return policy.

Second, the quality of tax return decreased. In the last three years, the average tax payables reported by individual taxpayers in their annual tax returns have plummeted significantly. It decreased from Rp2.15 million in 2008 to Rp0.69 million in 2009, and to Rp0.38 million in 2010. In addition, the average tax payables reported in the 2010 tax returns has dropped significantly, 17.07 times, compared to those reported in 2001 tax returns.

Third, the 2001 tax return policy has put a considerable operational burden to tax offices to handle the quick increases in the number of tax returns. From 2008 to 2010, the numbers of tax returns increased by 7.56 times or 6.8 million, but many of them, unfortunately, were the zero or low payment tax returns[9]. On the other hand, tax offices' capacity to handle them did not change as quickly as the increases on the number of tax returns. For instance, the number of employees only increased by 0.05 times from 31,269 in 2008 to 32,741 in 2010[10]. This condition might reduce the service quality of tax offices, and it also could reduce tax offices' ability to monitor a more potential taxpayers.

To this stage, the previous discussions show that all of the three tax policies that have been implemented in Indonesia have the positives and negatives. There was a dilemma in choosing the priority between equity and efficiency of a tax system. Obliging the EIT-OEs to file tax returns reduced the efficiency of the tax system, but it improved the tax system's equity and the tax awareness.

Therefore, considering the importance of the tax system equity, the invaluable of people's tax awareness, the practicality of the 2001 tax return policy, and the low level of Indonesian tax ratio, this paper suggests that it is better for the government to keep implementing the 2001 tax return policy. However, several measures should be taken to minimize its negative effects. For instance, setting up a special procedure to manage the EITs' tax returns, especially tax returns from the low incomes EITs, may reduce the tax offices' resources needed to manage them, so that the tax offices can make a better resources allocation in order to handle more potential taxpayers. Another one, promoting electronic filing may reduce the processing time in particular the key-in process. Furthermore, in order to increase the number of submitted tax returns; tax offices should simplify the EIT's tax return forms, and keep improving the tax returns submitting process. Lastly, in order to increase the individual tax revenues, tax offices should put more focus on assessing tax payment of the self employed individuals and medium to high wealth employees.

5. Conclusions

- After the implementation of self assessment tax system in 1984, Indonesia tax return policies can be divided into three periods: a) 1984 to 1994, b) 1995 to 2000, and c) 2001 to 2010 (the current state). Indonesian tax return policies swung from the equity perspective in 1984 to a more pragmatic policy in 1995, and finally it bounced back once again to the equity side in 2001.
- The main difference in 1984, 1995 and 2001 tax return policies lies on the issue of employee type individual taxpayers who earn incomes from one employer (EIT-OEs). In 1984 policy, EIT-OEs were obliged to submit tax returns, then in 1995 they were waived, and in 2001, they are once again obliged to submit tax returns.
- Data reveals that there is a big weakness on the effectiveness of the 2001 tax return policy (current tax return policy) in raising tax revenues. During 2001-2010, number of tax returns increased for about 17 times but individual tax revenues only increased by 0.2 times, and it also dotted by the occurrences of paradoxical situation in which number of tax returns had negative relation with tax revenues.
- However, despite its weakness on the efficiency side, the 2001 tax return plays crucial roles in promoting the equity in the tax system, increasing the tax awareness, and it is relatively easier to be implemented compared to the 1995 tax return policy. Considering all of these and the low level of Indonesia's tax ratio, the paper suggests that it is worth for the government to keep implementing the 2001 tax return policy, but several measures should be taken to minimize its negative effects.
- The dilemma in choosing between the equity of a tax system and efficiency in collecting tax from the EITs may also occur in countries which implement the self assessment tax system. Therefore, further researches in this area will be beneficial to enrich the understanding on how similar or different tax return policies are running in other tax jurisdictions that will be useful in reshaping tax return policies in the future.

Notes

[1] See article 1 point 11 of the Law of the Republic of Indonesia Number 6 of 1983 concerning General Provisions and Tax Procedures.

[2] See the Minister of Finance Regulation number 182/PMK.03/2007.

[3] See the Elucidation of the Law of the Republic of Indonesia Number 6 of 1983 concerning General Provisions and Tax Procedures.

[4] See article 13 paragraph (1) b of the Law of the Republic of Indonesia Number 9 of 1994 concerning the Amendment of the Law of General Provisions and Tax Procedures.

[5] See article 37A of the Law of the Republic of Indonesia Number 28 of 2007 concerning the Third Amendment of the Law of General Provisions and Tax Procedures and article 37A the Law of the Republic of Indonesia Number 16 of 2009 concerning the Fourth Amendment of the Law of General Provisions and Tax Procedures.

[6] The Director General of Taxes, in a press interview, mentioned "from January to September 2010 the new registered individual taxpayers were 2.8 million, of which 2.5 million"; 89 percent. <http://us.bisnis.vivanews.com/news/read/181824-2010--jumlah-wajib-pajak-bertambah-2-8-juta>.

[7] See Minister of Finance Regulation Number 564/KMK.03/2004.

[8] See the 2010 DGT Annual Report page 101.

[9] Director General of Taxes in a seminar. <http://www.republika.co.id/berita/ekonomi/keuangan/11/05/21/llj4uf-bukan-anda-kan-diperkirakan-50-juta-wajib-pajak-belum-tunaikan-kewajibannya>.

[10] See directorate general of taxes' 2008 and 2010 annual reports.

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