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THE IMPLEMENTATION OF AUTOMATIC EXCHANGE OF INFORMATION AS A TOOL TO TACKLE OFFSHORE TAX EVASION: AN EXPERIENCE FROM INDONESIA

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ABSTRACT

Cross-border tax evasion has been a central issue in international taxation in recent years. The use of Offshore Financial Centres (OFCs) and low tax jurisdictions to facilitate the wealth of high net worth individuals has led to offshore tax evasion and has eroded the tax bases of countries. Meanwhile, international tax cooperation is emerging with the aim of enhancing tax transparency. One way to reach tax transparency is with the implementation of the exchange of information for tax purposes. The tax authorities have already implemented the exchange of information on request; however, this method is ineffective to fight against offshore tax evasion. The tax authorities must already obtain the evidence of their suspicion over the taxpayers; otherwise, their request may be denied as a 'fishing expedition'. The demand for offshore financial information is obvious since it will enable tax authorities to oversee the level of offshore tax compliance. This study considers the importance of the Automatic Exchange of Information (AEOI) as a tool to access the resident's financial information of residents who kept their financial assets in other jurisdictions with a case study in Indonesia. The financial information from other jurisdictions is fundamental for Indonesia because it can be used for analysis and law enforcement of taxpayers, especially those who previously saved money abroad and have not reported or paid the correct amount of tax. This paper recognizes that despite the benefits of the AEOI, the implementation of the AEOI in Indonesia is still facing challenges, although it has been two years since its first implementation. This study will follow a qualitative methodological approach with a detailed literature review and real experience in Indonesia. Finally, this article explores the current stage of implementing the AEOI in Indonesia and the challenges faced by Indonesia with some proposed solutions for the Directorate General of Taxes for the effective implementation of the AEOI in Indonesia.

Keywords: AEOI, tax evasion, tax avoidance, offshore account, financial information

Penghindaran pajak lintas-batas telah menjadi isu sentral dalam perpajakan internasional dalam beberapa tahun terakhir. Penggunaan pusat-pusat keuangan di luar negeri dan yurisdiksi dengan tariff pajak yang rendah untuk memfasilitasi individu-individu kaya telah menyebabkan penggelapan pajak luar negeri dan telah mengikis basis pajak negara. Sementara itu, kerja sama di bidang perpajakan internasional muncul dengan tujuan untuk meningkatkan transparansi di bidang pajak. Salah satu cara untuk mencapai transparansi di bidang pajak adalah dengan penerapan pertukaran informasi untuk kepentingan perpajakan. Otoritas pajak telah menerapkan pertukaran informasi berdasarkan permintaan; namun, metode ini tidak efektif untuk memerangi penggelapan pajak luar negeri dikarenakan otoritas pajak harus memiliki bukti kecurigaan yang memadai dari wajib pajak; jika tidak, permintaan mereka dapat ditolak. Informasi keuangan yang berada di luar yurisdiksi akan memungkinkan otoritas pajak untuk mengawasi tingkat kepatuhan pajak luar negeri. Studi ini akan berfokus pada pentingnya Pertukaran Informasi Secara Otomatis (AEOI) sebagai alat untuk mengakses informasi keuangan yang berada di luar yurisdiksi dengan studi kasus di Indonesia. Informasi keuangan dari yurisdiksi lain sangat penting bagi Indonesia karena dapat digunakan untuk analisis dan penegakan hukum bagi wajib pajak, terutama bagi mereka yang sebelumnya menyimpan uang di luar negeri dan belum melaporkan atau membayar jumlah pajak yang benar. Artikel ini mengakui bahwa terlepas dari manfaat AEOI, penerapan AEOI di Indonesia masih menghadapi tantangan meskipun telah berlangsung dua tahun sejak pertama diimplementasikan. Studi ini akan menggunakan pendekatan metode kualitatif dengan tinjauan pustaka yang rinci dan pengalaman nyata di Indonesia. Terakhir, artikel ini membahas tahapan implementasi AEOI di Indonesia pada saat ini dan tantangan yang dihadapi oleh Indonesia dengan beberapa solusi yang diusulkan untuk Direktorat Jenderal Pajak untuk mewujudkan implementasi AEOI yang efektif di Indonesia.

1. INTRODUCTION

1.1 Latar Belakang

According to Victoria Perry (Saïd Business School, University of Oxford, 2017), corporate income tax plays a key role in developing and low-income countries. To effectively collect the tax revenue, tax authorities must have the ability to collect the data related to taxpayers' information; thus, the tax authorities can identify and analyse the non-compliant taxpayers (Darussalam, Kristiaji, and Deborah, 2014). Some of the most important information for the tax administration is related to the financial data of taxpayers. However, obtaining financial data is usually difficult since it will be related to bank secrecy, protected by domestic laws.

From the customers' perspective, bank secrecy is important, as the customers provide their confidential data, such as financial information, to the bank; thus, that bank must keep their data confidential (Darussalam et al., 2014). From the tax administration's perspective, bank secrecy can create the possibility that the taxpayers can hide their money in financial institutions to avoid tax payments (Actionaid, 2013). The high level of bank secrecy is also related to the financial sectors in low tax jurisdictions and Offshore Financial Centres (OFCs). The OFCs and tax havens provide safe places to launder money from illicit sources, such as the drug trade, corruption, and global crime, and facilitate tax avoidance or evasion (Actionaid, 2013). Thus, to prevent fraudulent activities and counter terrorism, tax authorities must have agreements to share information for tax purposes with each other (Bickers, Hopkins-Burns, Bennett, & Namay, 2015). However, these authors also added that there are main concerns about the possibility of misuse of data by the government, the accuracy of the information, the security of the data, and how the government will treat the received information.

Past studies have examined the importance of information sharing for tax purposes. A study by Knobel and Meinzer (2014a) from the Tax Justice Network found that developing countries acknowledge the benefits of Automatic Exchange of Information (hereinafter: AEOI) and agree that sanctions could encourage tax havens to participate in the AEOI. However, Knobel and Meinzer (2014b) also criticised the standard of the AEOI as favouring developed countries and stated that entry barriers for developing countries should be lower. Knobel's (2017) survey of 30 countries found that the AEOI can be preferably used to tackle non-tax issues such as corruption and money laundering.

As a developing country and member of the G20, Indonesia has joined the Global Forum on Transparency and Exchange of Information for Tax Purposes. On 8 May 2017, the Government issued Government Regulation in Lieu of Law (Perppu) Number 1 of 2017 on Access to Financial Information for Tax Purposes as further enacted by Law Number 9 of 2017. This regulation is the primary legal basis for the Directorate General of Taxes (DGT) in obtaining the financial data of taxpayers from financial institutions. Further, the Minister of Finance issued Regulation of the Minister of Finance (PMK) No. 70/PMK.03/2017 as lastly amended by the Minister of Finance (PMK) No. 19/PMK.03/2018 regarding Technical Guidance on Implementation of Information Access for Tax Purposes as a secondary legal basis. The issuance of the regulations was an important milestone for Indonesia since it could now participate in the AEOI.

2. RESEARCH METHOD

This paper examines the importance of AEOI as a tool for combating offshore tax evasion with the case implementation in Indonesia. This research employs a qualitative method using a literature review and actual experience in Indonesia. The secondary data includes the relevant provisions of Indonesia Law for implementing the AEOI, the AEOI standard, pertinent guidance, government publications, reports, books, and relevant various articles.

3. TAX EVASION WITH CROSS BORDER TRANSACTION

Shifting assets from one jurisdiction to another has been facilitated by global development. The current era of globalisation is marked by the increase of capital mobility that is far exceeding the mobility of labour. Improvement in technology has been in great assistance for the increase as it enables the transfer of funds to and from all over the world. By its nature, the globalisation itself is a two-sided coin: it brings more flexibility in the economics on one side and creates some opportunities for tax avoidance on the other. The avoidance schemes vary from a small scale in which a company uses an offshore account to hide its assets, to a larger scale involving major corporations that use offshore holding companies to launder their profits.

Since the goal is to acquire as many profits possible, the activities are often hidden from authorities, more commonly known as the shadow economy. Some countries that facilitate this practice might argue that attracting the investors, which is also a part of the business competition strategy, is necessary to achieve resources. These so-called tax haven countries provide their services throughout globalised sectors, covering a wide range of businesses, from banking to finance to the weapon industry.The IMF identified that in 2003 there were more than 60 countries categorised as a tax havens, while estimated that as much as US$ 11 trillion in the total value of assets were kept in these countries, either with less-taxed or even untaxed (Christensen & Kapoor, 2004). In addition, tax haven countries, also known as low tax jurisdictions, such as Switzerland, Singapore, Hong Kong, and the Cayman Islands, manage some of the world’s most leading financial industries, which allegedly provide the opportunity to evade taxes for their foreign clients. The study by Zucman (2013) calculated that these jurisdictions retain around 8% of households' financial wealth. He also predicted that about 40% of foreign direct investments in the world are made through them. When this financial wealth or direct investment goes unrecorded, the source jurisdictions will suffer a loss. For example, under Indonesia’s domestic tax income laws, the income from money deposits in banks is subject to withholding tax of article 23. However, for some certain banks in Switzerland, this type of income is tax exempted. In addition, since there is no obligation for Switzerland to report this deposit to any jurisdiction, Indonesia not excluded – some Indonesian tax residents might prefer to keep their money in Switzerland.

This international tax evasion practice has raised several concerns from jurisdictions, particularly those heavily affected, i.e., developing countries. Among the concerns is the decline in government revenues and its impact on the fairness of the tax system. For instance, the imposition of personal income tax is quite challenging for developing countries than for advanced countries. Missing information on income generated from assets held in low tax jurisdictions is one of the key problems related to the enforcement of personal income tax.

The asymmetric information between tax authority and taxpayers often raises an opportunity for evading tax in the home country. Thus, tax authorities should work together to fight against tax evasion to maintain the integrity of the tax system. One of the most important policies to increase the detection of the threat of cross-border tax evasion is the exchange of information between tax authorities (Keen and Lighart, 2006).

Previous research of Johannesen and Zucman (2014), Casi, Spengel, and Stage (2018), and O'Reilly, Ramirez, and Stemmer (2019) have investigated the impact of the exchange of information on taxpayer's behaviour in their cross-border deposit. They found that the implementation of the exchange of information contributed to the decline of cross-border deposit numbers in OFCs. Subsequently, Johannesen and Zucman (2014), and Casi et al. (2018) also found that since the taxpayers are aware that the tax authority is now in the position of accessing their offshore assets information, there is a likelihood for the taxpayers to shift their assets from OFCs to other jurisdictions that have not implemented exchange of information.

4. TAX TRANSPARENCY

4.1 Bank Secrecy in Financial Industry

Bank secrecy, the term often used interchangeably with financial secrecy, financial privacy, or bank safety, is a condition in which any transactions between banks and their clients remain undisclosed and secure. It is one of the reasons as to why banks become the most popular place for people to keep their assets, either for protection or to hide it from the authority. Bank secrecy can be traced back to the 1700s when the Geneva bankers started the practice socially. Still, it was not until two centuries later that the bank's disclosure of clients' information without their consent is considered a crime, as stated in Switzerland's Banking Act of 1934.

Little is known about the jurisdiction or country recognised as the first OFCs, but it was this law, along with stable currency, which then made Switzerland gain its world reputation in the financial industry, mainly for protecting clients' savings and information. Hence, as the popularity increased, foreigners with "pocket full of cash" came from around the globe to save their money there. In the 1940s, many banks adopted this practice, which was later considered the basis for bank secrecy as we know these modern days.

Although banks or financial services are common and can be found practically in all parts of the world, only a few financial centres are attractive to foreign customers. These jurisdictions share some common characteristics, which later are summarised by Zoromé (2007) into some categories. Four of these are (1) Primary orientation towards non-residents; (2) Favourable regulatory environment; (3) Low or zero-taxation scheme; (4) Disproportion between the size of the financial sector and the domestic financing needs. In addition, the paper contains a list of 46 countries regarded as OFCs. The IMF paper (2000) stated that one of the OFCs' major attributes is the centres which provide some or all of the following services: low or zero taxation, moderate or light financial regulation, and banking secrecy and anonymity. A more practical definition of OFCs also provided by this paper:

as centers where the bulk of financial sector transactions on both sides of the balance sheet are with individuals or companies that are not residents of OFCs, where the transactions are initiated elsewhere, and where the majority of the institutions involved are controlled by non-residents.

4.2 The Importance of Tax Transparency

The effect of globalisation, along with the growing number of OFCs in the 1970s and 1980s, has made the movement of capital through the transfer of funds to and from all over the world easier and therefore increasing rapidly. The global trade system has eventually encouraged multinational corporations to seek the best countries or jurisdictions that would provide them investment facilities and allow them to gain more profit. As a result, countries are in some kind of competition to attract corporations and individuals to invest, of which one way to win is by providing tax facilities.

The offered facilities might vary from a very loose tax administration to a low or even non-taxed income. These facilities allow companies or individuals to re-route their financial transactions via offshore centres providing them the opportunity to evade more taxes. Such practices were revealed in a recent leak of the Panama Papers[1].

These tax evasion practices have been harmful to some countries, particularly developing ones. The study of Baker and Nordin (2004) argued that developing countries suffered a loss of nearly US$500 billion of money every year. An even more massive impact follows after. Since revenue is fundamental for developing countries, a lack of resources leaves these countries no option but to incur debts from financial markets, which are costly, not only in terms of high payment due to high interest but also in terms of the nation’s dignity.

An even massive of impact is following after, since revenue is fundamental for developing countries, lacking in resources leave these countries no option but incurring debt from financial markets, which of course is costly, not just in term of payments, due to high interest, but also in the term of nation’s dignity. The hard-dependencies on creditors might be risky for countries as they can be very easily exposed to any interest from their creditors. In the same vein, the recent event of the Panama

[1] The Panama Papers: A giant leak of more than 11.5 million financial and legal records that shows how a global industry of law firms and big banks sells financial secrecy to politicians, fraudsters, and drug traffickers as well as billionaires, celebrities and sports stars. The documents were created by and taken from a powerful law firm based in Panama, Mossack Fonseca. The leaked records revealed information on more than 214,000 offshore companies connected to people in more than 200 countries and territories. Available at: https://www.icij.org/investigations/panama-papers/pages/panama-papers-about-the-investigation/

Papers revealed that since the 1970s, some big names from elite politics to world athletes, drug traffickers to celebrities from all over the world have been hiding their assets from the authorities by using facilities given by OFCs. This revelation sheds light on the long-lasting debate on whether the information held by financial institutions (e.g., banks) should be disclosed to authority for tax matters. In no coincidence, the revelation occurred just one year before commencing the exchanges of account information on an automatic basis for the first time in 2017, the occasion of which signalled the end of bank secrecy and the beginning of a new regime of tax transparency.

5. INTERNATIONAL TAX COOPERATION

5.1 Unilateral

In 2014, the US enforced the Foreign Account Tax Compliance Act (FATCA), which required non-US financial institutions to report financial information of US residents to the Internal Revenue Service (IRS) (Miller & Oats, 2016). FATCA was part of President Obama's campaign to crack down on foreign tax evasion (Panayi, 2016). Moreover, FATCA was a response to the UBS offshore banking scandal, which revealed that many US citizens have Swiss bank accounts without reporting and paying the tax to the IRS (Vermeiren and Lips, 2016). The US will impose a 30% withholding tax on any payments made to foreign financial institutions from the US if the foreign financial institutions fail to supply the right financial information of the US residents to IRS (IRS, 2018). In addition, foreign financial institutions will be expected to apply a 30% withholding tax on behalf of the IRS on payments to the account holders that do not provide identity information (Miller and Oats, 2016). From this point, it can be seen that FATCA is a unilateral action by the US forces foreign financial institutions to comply with their rules.

At first, FATCA was criticized because of the coercive action from the US towards foreign financial institutions. On the one hand, FATCA will increase the cost of compliance for foreign financial institutions (Miller and Oats, 2016) since they must provide adequate resources, particularly for creating IT systems. On the other hand, FATCA has inspired the emergence of similar actions, such as the OECD's Common Reporting Standard (CRS), which also targets the compliance of foreign financial institutions.

5.2 Bilateral

Bilateral coordination usually uses tax treaties. Tax treaties do not address the double taxation; instead, they will shift the burden of taxation from the source country to the residence country (Avi-Yonah, 2007). Bilateral tax treaties also constitute a limit in that the information that needs to be exchanged is reciprocal (Keen and Ligthart, 2006). Because of the different interests in the information needed, In addition, a bilateral treaty is a less powerful form of cooperation than its multilateral counterpart, as it requires voluntary approval of the two countries. Therefore, if a country found no interest toward the other, the bilateral treaty might not be concluded, leading to a condition that could create a loss to one side.

Generally, a bilateral treaty sets the rules for the exchange of information between countries. Both the OECD and the UN models of tax treaties have provisions regarding the exchange of information.

5.3 Multilateral

The Global Forum on Transparency and Exchange of Information for Tax Purposes (the Global Forum) is the continuation of a multilateral forum created in 2000 by the OECD (OECD, 2020c). The Global Forum was restructured in September 2009, adding members from non-OECD countries and endorsed by the G20, with the aim to improve transparency and exchange of information for tax purposes (OECD, 2020c). As of September 2020, the Global Forum had 160 members with equal voting rights (OECD, 2020a). Since 2009, the Global Forum has been actively driving and monitoring global commitments for implementing the standards of the AEOI as well as encouraging the participation of developing countries for the AEOI. The nature of multilateral allows it to impose any sanctions on countries unwilling to cooperate. As such, it is a powerful and and much more efficient treaty compared to both unilateral and bilateral treaties.

6. AUTOMATIC EXCHANGE OF INFORMATION

6.1 Background of Automatic

Following the FATCA, several countries in Europe, including the UK, Germany, Italy, Spain, and France, have initiated a multilateral agreement which allow them to share financial information automatically (Panayi, 2016). There is an international debate regarding whether the AEOI is actually a duplication of FATCA, or the AEOI, like FATCA, is used to prevent the unilateral actions by countries (Miller and Oats, 2016). Vermeiren and Lips (2016) argued that FATCA is the precedent for the OECD to make an international standard on the AEOI.

In September 2013, the G20 Leader's Summit declared their support for the OECD in developing a legal framework standard for the AEOI that could be applied globally. In February 2014, the G20 ministers of finance endorsed the CRS as the global standard for the AEOI. The CRS is an intergovernmental project to improve the effective sharing of information for tax purposes. As of May 2020, 157 countries have already committed to implementing the AEOI (OECD, 2020b).

6.2 Legal Basis for Automatic

The legal instruments that permit AEOI include (OECD, 2018a):

1. Article 26 of the OECD Double Tax Agreements;
2. Article 6 of the Multilateral Convention

on Mutual Administrative Assistance in Tax Matters which specifically provides for the optional use of automatic exchange; and
3. Tax Information Exchange Agreements (TIEA) that provides for the automatic exchange of information.

In addition to the legal basis for exchange, Competent Authorities are allowed to enter a bilateral reciprocal agreement using The Model Competent Authority (CAA). This CAA will allow them to set out the details regarding how and when the information will be exchanged. However, several jurisdictions can enter multilateral CAA to reduce the cost of negotiating with every jurisdiction. The Multilateral CAA provides solutions to implement the AEOI sooner compared to a single agreement. Since the negotiation is conducted simultaneously with several jurisdictions, the duration will significantly be reduced.

6.3. How Automatic Exchange of Information Works

The AEOI process begins with the tax authority of each participating jurisdiction collecting the vast amount of financial data from the financial industry. The data will then be combined and identified to which country residence it belongs. After the information is ready, i.e., sorted and encrypted, it will be sent to the country of residence using secure electronic transmission called Common Transmission System (CTS), developed by the OECD. The country of residence will process the information received for tax purposes (OECD, 2012).

6.4 Challenges of the Implementation

Implementing the AEOI might pose some challenges, especially in developing countries, according to The World Bank Group report in the OECD (2014). The challenges involve the low awareness regarding the importance of the AEOI, high cost of IT systems, lack of human resources for analysis, and the use of the received data in the legal frameworks, which all are aimed to ensure the confidentiality and data safeguard.

Furthermore, there is also an issue of human rights related to the privacy of the account holders. The tax authority has to guarantee that the account holders' information remains confidential and used only for tax purposes. The cost to implement the CRS will vary depending on each country's readiness and will be borne both by the tax authority and financial institutions. The OECD (2014) stated that the costliest investment is the IT systems, followed by human resources. Also included in the cost is the political cost to amend domestic regulations, which would give the tax authority the power to access financial information.

6.5 Expected Benefit from Automatic Exchange of Information

Under the residence principle, taxes will be levied on the income that arises from both domestic and foreign sources. Miller and Oats (2016) stated that the residence principle is the 'right to tax its residents on their worldwide income and gains.' To work effectively, the residence principle requires that the tax authority have full information about the foreign income of their residents (Bacchetta and Espinosa, 1995). However, offshore data will be difficult to obtain if the tax authorities do not have adequate resources. Currently, the method for obtaining the offshore data is by using Exchange of Information on Request included in bilateral tax treaties.

The AEOI will complement the use of Exchange of Information on Request with four main benefits for developing countries: (1) Detection of tax evasion and offshore wealth; (2) Deterrence from future non-compliance; (3) Supporting domestic synergies; and (4) Enhancing reputation (OECD, 2014). The detection of tax evasion is critical for countries. The AEOI, therefore, will facilitate the detection of non-compliant taxpayers, even if the tax authority did not have any suspicion in the first place. Furthermore, since the financial institutions will report their account holders' information, including their balances, directly to the tax authority, the taxpayers will be educated to report all of their income. Thus, AEOI will create a deterrence from future non-compliance (OECD, 2014).

Panayi (2016) explained the advantages of implementing AEOI for the resident country, stating that the tax authority will obtain financial data in a timely manner. In addition, implementing the AEOI will also help tax authorities detect illicit activities, such as money laundering and therefore can support domestic systems (OECD, 2014). Participation in the AEOI also demonstrates the commitment to enhancing tax transparency, thus improving the reputation of developing countries (OECD, 2014).

Despite several challenges faced by developing countries, the AEOI is still a favourable solution for obtaining financial information from other jurisdictions to address offshore tax evasion. As discussed by Ring (2014), developing countries have serious barriers for securing the needed information compared to developed countries, as they often have several domestic constraints and difficulties obtaining information from other jurisdictions. Since the previous data concluded that a huge amount of wealth of the developing countries' citizens is held in OFCs, the tax authority in developing countries have to implement AEOI for the best solution in obtaining the financial data. Even though Grinberg (2013) indicated that there is no guarantee that the AEOI would provide tax revenue for the resident country, developing countries need to develop the political will to take action for tax compliance nevertheless, including the action for offshore accounts.

7. THE IMPLEMENTATION OF AUTOMATIC EXCHANGE OF INFORMATION IN INDONESIA

7.1 Bank Secrecy in Indonesia

Almost all financial industries across countries around the world apply bank secrecy for the reason that it is crucial to protect the privacy of the account holders. As a financial industry, banks' services lie in the trust of their customers; thus it is an obligation for them to protect their customers' information. As access to this information becomes limited, banks earn trust from customers, making them the popular place to save money. Bank secrecy, in short, is a fundamental element in the financial industry. As for Indonesia, the provisions of bank secrecy or customer confidentiality are stipulated in several regulations as follows:

1. Article 40 and Article 41 of the Law Number 7 of 1992 concerning Banking as amended to the Law Number 10 of 1998;
2. Article 47 of the Law Number 8 of 1995 concerning Capital Market;
3. Article 17, Article 27, and Article 55 of the Law Number 32 of 1997 concerning Commodities Futures Trading as amended by the Law Number 10 of 2011; and
4. Article 41 and Article 42 of the Law Number 21 of 2008 concerning Sharia Banking.

The financial industry has the obligation to keep the customer's information from outside parties, including the governments or tax authorities. From another point of view, it can also be seen that the banking industry provides facilities for taxpayers to hide their assets. If the DGT does not have access to taxpayers' financial information, it will eventually lead to taxpayers' non-compliance activities. These activities include deliberately keeping their money in the banking industry in order to evade tax, or worst, launder money. Thus, if such condition continues to exist, the tax base will be eroded and cause a massive loss to the tax revenue.

As Indonesia's tax authority, the DGT can access the financial information held by the banks or other financial industries. However, it is limited to specific taxpayers and information, following a certain procedure. The process requires the DGT to make special request to the bank/ financial industry where the financial information is knowingly kept. It is less efficient because it took a long time and the information that could be obtained is minimal. Article 41 of Law Number 7 of 1992 concerning Banking as amended by the Law Number 10 of 1998 states that for tax purpose, the Head Office of Central Bank (Bank Indonesia), based on the request from the Minister of Finance, has the authority to issue written order to the bank to provide information or written evidence to the tax authority (DGT). The bank is then obliged to provide customer's information to the DGT based on the request from the Minister of Finance. However, this regulation only gives provision for specific customers and specific information of taxpayers. In addition, the process for obtaining financial information takes longer times because of the amount of the red tape process for obtaining financial information takes longer times because of the amount of the red tape involved. From tax authority's perspective, this condition is unfavourable because the longer the financial information is obtained by the DGT, the longer chance for taxpayers to keep their money and use it for illegal activities.

The Government of Republic of Indonesia has implemented tax amnesty programme between July 2016 and March 2017 as a transition period to the transparency era in which bank secrecy no longer applies. The programme enabled taxpayers to report their previously unreported assets without sanction from the DGT and it was designed to encourage the voluntary disclosure by taxpayers through assets repatriation or assets declaration, including offshore assets such as bank account, deposit, and investment securities. The implementation of the AEOI after the programme was over marked the beginning of the transparency era in Indonesia. Based on the tax amnesty data (DGT, 2017), the top five countries where the declaration of foreign assets originated from are Singapore, the British Virgin Islands, Hong Kong, the Cayman Island and Australia. This data provides preliminary evidence that there are Indonesia's tax residents' assets kept abroad. It can also be assumed that the Government of Republic Indonesia might have suffered a loss on its tax revenue for years because of the untaxed assets kept abroad and furthermore, there might have been capital fleeing Indonesia.

From the fact that a huge amount of assets, especially financial ones, are kept abroad, the DGT has a valid reason to obtain financial information from other jurisdictions. In line with this fact, Indonesia has joined the international cooperation to promote tax transparency. One of these is the Global Forum on Transparency and Exchange of Information for Tax Purposes (the Global Forum), which aims to enhance tax transparency from the use of exchange of information within its members. In April 2009, the G20 Leaders' Summit in London declared that the bank secrecy era was over. The Indonesian government signed the Multilateral Convention on Mutual Administrative Assistance in Tax Matters (MAC) in November 2011, within which Article 6 set the implementation of the AEOI. The commitment to support the AEOI came to existence when in November 2014, the G20 Leaders' Summit in Brisbane declared their approval for the implementation of the AEOI on a reciprocal basis based on Global Standard of the AEOI, Common Reporting Standard (CRS), starting on the year 2017 or year 2018. As the legal basis for implementing the AEOI, the Government of the Republic of Indonesia signed the Multilateral Competent Authority Agreement (MCAA) in June 2015, within which the Annex F set the commitment of Indonesia to implement the AEOI in September 2018.

7.2 Core Requirement of the Implementation of Automatic

In order to implement the AEOI, a jurisdiction needs to meet the four core requirements necessary to implement the CRS. According to OECD (2018a), the four core requirements are (1) Translating the reporting and due diligence rules into domestic law, including rules to ensure their effective implementation; (2) Selecting the legal basis for the AEOI; (3) Putting in place information technology and administrative infrastructure and resources; (4) Protecting the confidentiality and safeguarding data.

7.2.1 Translating the Reporting and Due Diligence Rules into Domestic Law

The signing of the MCAA marked Indonesia's commitment to implement AEOI in June 2015, and it was expected to be ready for the first exchange of the financial account information by September 2018. This means that the domestic legal framework, which obligates the financial institutions to collect and report the financial account information to the DGT, should be made available immediately. Failing to meet the criteria of the availability of domestic regulations for the AEOI would categorize Indonesia as failing to meet its commitment. As such, it would not be able to receive any information but still be obliged to supply information to other countries. Indonesia's reputation in international cooperation for tax transparency campaign would also suffer. The chance to obtain financial account information from abroad would be lost, despite its importance for Indonesia in verifying its taxpayers' compliance.

Anticipating the above possibility, Indonesia passed the Government Regulation in lieu of Law of the Republic of Indonesia Number 1 of 2017 (Perppu 1/2017) concerning Access to Financial Information for Tax Purposes, as later enacted into law by Law Number 9 of 2017. It revokes certain secrecy provisions in financial institutions and grants the DGT access to financial information for tax purposes. This regulation is the primary legal basis for Indonesia to implement the AEOI, while the secondary one is created through the stipulation of Ministry of Finance Regulation Number 70/PMK.03/2017 concerning Technical Guidance on Access to Financial Information for Tax Purposes, as lastly amended by Ministry of Finance Regulation Number 19/PMK.03/2018. Further, the technical guidance for registration of financial institutions and reporting of reports containing financial information is regulated with the issuance of Director General of Taxes Regulation Number 04/PJ/2018.

7.2.2 Selecting the Legal Basis for the Automatic Exchange of Information

Once the domestic regulation is in place, the DGT will be able to get financial account information, which will then be exchanged with other jurisdictions'. The exchange process needs a legal basis for both countries so that they can exchange the data. Indonesia's exchange of information network as a legal basis consists of as follows:

1. Double Tax Agreements/ Tax Treaties containing the Article about the exchange of information.
2. The Multilateral Convention on Mutual Administrative Assistance in Tax Matters (MAC), within which Article 6 regulates the optional use of AEOI.
3. Tax Information Exchange Agreements (TIEA) that provide provision for AEOI.

In line with MAC, Indonesia also signed the Multilateral Competent Authority Agreement (MCAA) on 3 June 2015 in Paris. As of April 2019, 105 countries already signed the MCAA to implement the AEOI on financial account information (OECD, 2020d). In addition, Indonesia also signed Bilateral Competent Authority Agreement (BCAA) for the AEOI on financial account information on a reciprocal basis with Hong Kong on 16 June 2017. Further, Indonesia also signed a joint declaration with Switzerland to implement the AEOI on financial account information on a reciprocal basis on 4 July 2017 for the taxable period that begins in January 2018.

7.2.3 Putting in Place Information Technology and Administrative Infrastructure and Resource

The two basic channels utilised by the DGT for the AEOI are as follows:
1.The systems used by financial institutions to report the financial account information they hold to the DGT. An online system developed by the Financial Service Authority (Otoritas Jasa Keuangan/OJK), called Sistem Penyampaian Informasi Nasabah Asing (SiPINA), is used by financial institutions under the supervision of OJK such as banks, capital markets, and insurance companies. For those not supervised by OJK, such as commodities future trading companies, the reporting is facilitated by an online system developed by the DGT called Portal EOI.
2. The system used to exchange financial account information with other jurisdictions. Indonesia uses Common Transmission System (CTS) developed by the OECD for exchanging data with other jurisdictions. The CTS is a platform that facilitates the exchange of tax information between Competent Authorities around the world securely and efficiently.

7.2.4 Protecting Confidentiality and Safeguarding Data

The confidentiality of taxpayers' data is a fundamental aspect of the AEOI. Confidentiality and data safeguard must be covered both in the domestic legal framework and the system and procedures of data exchange. The domestic legal framework in Indonesia already has the provision for protecting the privacy of the financial account information data, including the sanction for the parties who breach the confidentiality rules. The international agreements for the AEOI also provide the provision of confidentiality and data safeguards. Special audit procedures are also applied to ensure that the confidentiality and data safeguards for tax information remain intact. The OECD and the Global Forum set a high standard for this matter. As protecting the tax information is related the human rights of taxpayers, Indonesia's level of protecting confidentiality and safeguarding data was assessed prior to joining the AEOI. It was only Indonesia passed the assessment that it was ready to implement the AEOI.

7.3 Build the Awareness of the Importance of Automatic Exchange of Information in Indonesia

The AEOI is one of the fundamental tools for developing countries to tackle illicit financial flows kept in OFCs or in low tax jurisdictions. If Indonesia could not provide a domestic legal framework for the AEOI by the end of June 2017, it would fail to meet its commitment. Realising this, the Indonesian government was encouraged to accelerate the process of approval and ratifying the domestic regulations in accordance with the AEOI rules. However, this process was not an easy task. Therefore, in order to build awareness of the importance of the AEOI in Indonesia, DGT involved other authorities early on the legislation process. This included Financial Authority Service (OJK), Coordinating Ministry for Economic Affairs, Ministry of Law and Human Rights, Ministry of State Secretariat, and the Indonesia Financial Transaction Reports and Analysis Centre (PPATK). Their early involvement was necessary as DGT was able to receive many inputs from different points of view. For instance, the implementation of the AEOI will affect the financial institutions directly; this is the field where the Financial Service Authority has the most reliable experiences.

8. CHALLENGES FACED BY INDONESIA IN IMPLEMENTING AEOI AND SUGGESTIONS TO ADDRESS THEM

8.1 The Compliance Level of the Financial Institution

Following the implementation of the AEOI on financial account information in September 2018, DGT's next task is to monitor the compliance of the financial institutions to the Law Number 9 of 2017. Compliant to this law, the financial institutions are required to do the following: (1) performing due diligence procedures for account holders who want to open financial accounts; (2) registering as reporting or non-reporting financial institutions; (3) reporting the financial information to DGT.

DGT has to make sure that the financial institutions have performed due diligence in accordance with the CRS. In this procedure, determining the account holders' tax residence is critical. Some account holders may have several tax residences, while some others may not be residents of reportable jurisdictions. As Indonesia applies the wider approach, the financial institutions have to perform the due diligence on all account holders and collect all financial information of the account holders who are non-resident, regardless of whether their resident country is reportable jurisdictions or not. Another challenge faced by DGT is to ensure that Anti Money Laundering (AML) and Know Your Customers (KYC) principles are already applied.

Tax auditors performing the audit to financial institutions must be equipped with sufficient knowledge of AML and KYC, and the number of those possessing such knowledge is limited. One way to overcome this shortcoming is by involving auditors from OJK and PPATK in a joint audit. Deemed as experts who work for DGT, they are also bound by the confidentiality clause stipulated in the Article 34 of the Law Number 6 of 1983 concerning General Provisions and Tax Procedures as lastly amended by the Law Number 28 of 2007.

After performing due diligence, the financial institutions must register either as reporting or non-reporting institutions. Verifying this can be tough for DGT as it has to calculate the total population of financial institutions obliged to register, while some data might not be publicly available. DGT can accurately calculate the population of those under the supervision of OJK. However, the unreliable available data for some other financial institutions such as the cooperative (koperasi simpan pinjam) may force DGT to gather the information from local governments or local tax offices.

Reporting financial institutions have an obligation to report the financial account information of their account holders. The international standard stipulates that the reporting file be made only in Extensible Mark-up Language (XML) format. However, for convenience reasons, DGT allows the reports to be filed in either XML or Excel formats. The next challenge for DGT is to determine the filing accuracy of these reports in their respective formats. A collaboration between DGT and OJK may be effective in ensuring that financial institutions file their reports correctly. This is done in joint dissemination or other forms of assistance, including providing help desks and call centres for financial institutions. Next, the reports must be validated to determine their quality. OJK starts the process by validating the report's format, followed by validation on the content by DGT, which includes a follow-up function whenever one or more mistakes on the financial institutions' reporting file are found. The whole process is to assure that all the reporting files are of high quality.

8.2 The Quality of the Data Receiving and Sending

Almost 100 jurisdictions carried out the AEOI in 2019, resulting in their tax authorities to obtain data on 84 million financial accounts held offshore with a total asset of EUR 10 trillion (OECD, 2019a). Table 1 shows the rapid increase of AEOI from 2017 to 2019.

Table 1. Exchanges that took place in 2017, 2018, and 2019 under the AEOI Standard
Source: The Global Forum on Transparency and Exchange of Information for Tax Purposes (2020)

Year	Exchanging Jurisdictions	Exchange Relationships	Accounts (million)	Assets (EUR trillion)
2019	97	6,100	84	10
2018	96	4,500	47	4.9
2017	48	2,600	11	1.1

All jurisdictions involved in the AEOI expect that the information both sent and received is, at least, meets the minimum requirements. In the case Indonesia is a sender jurisdiction, data quality depends on the accuracy of financial information submitted by the reporting financial institutions due to the long and complex process explained above. DGT not only has a role in ensuring that the sent reporting files are of high quality, but it also has to make sure that the received information is of international standard by establishing good communication with partner countries so that any error in the received reporting files can be properly corrected promptly. In contrast, when Indonesia is the receiver jurisdiction, DGT has to make sure that the information it receives is in accordance with international standards and can be processed. Any inaccuracy found in the received information must immediately be communicated with the competent authority who sent the information, as set in the MCAA provision. Through the whole process, DGT must establish itself as the central figure for providing two-way communications both to financial institutions and partner countries and validating the sent and received reporting files.

8.3 Utilization of the Automatic Exchange of Information's Data from Other Jurisdictions

Based on the Global Forum data, Indonesia received financial information from 59 jurisdictions in 2018 and 66 jurisdictions in 2019 (OECD, 2019a). This massive flow of financial information expands its database. To make use of this information, DGT is required to apply the correct tools in processing and analysing the data and ensure that each procedure regarding the confidentiality and data safeguard is implemented properly. However, the completeness of data received may pose a challenge when matched with the DGT database. The information received may not contain a Tax Identity Number (TIN). This unique identity is quite reliable in determining the correct taxpayer, so its absence means an identification error. DGT will have to devise another identification strategy, including matching the name with the address or date/place of birth. This process of identification is vital to determine whether the received information can be analysed further, for example compared to the tax return of a certain taxpayer. A valid identification process is a must; otherwise, the information received will be unusable. Nevertheless, it requires a careful and complicated activity which unfortunately takes a lot of time. As a result, the impact of AEOI on tax compliance or, in particular, on recovered tax may not be readily observed.

For future anticipation of the quality of information exchanged and subsequently, ensuring the effectiveness of the received information, the DGT is demanded to work closely with the Global Forum to always maintain the standard of exchanged information. This can be done by reporting or providing inputs to the Global Forum regarding the quality of the information received from other jurisdictions. The report may serve as an assessment tool for AEOI implementation, which will determine of the jurisdiction's compliance rating. However, as Indonesia will also be assessed, DGT must also ensure that the information sent always follows the standard. In doing so, DGT is expected to conduct close cooperation with each financial institution by providing updated knowledge on standardized quality of information, which will then lead to better reporting by the financial institutions. Finally, the DGT is required to be actively involved in the international forums of AEOI in order to keep up with any development and be ready to implement it in AEOI practice and regulations.

Another challenge in exercising the received information is related to the sensitivity of the data itself. It is undeniable that financial information received from other jurisdictions contains some material which may call for extra treatment, e.g., the holder's identity and the value of an account. The DGT must ensure that this information is properly guarded by creating a secure and monitored access. Any leak would bring a fatal consequence: Indonesia would no longer be able to receive financial information from its partner jurisdictions, as had happened to a country in Europe.

Viewing from a wider perspective, the DGT receives financial information from some jurisdictions that are considered as OFCs or generally thought to be "the places where people hide their financial assets". On the one hand, this "newly-disclosed information" provides the DGT with a potential source of additional tax revenue. On the other hand, it also has the potential of backfiring when not managed appropriately. Due to its sensitivity, DGT must be convinced that the information has undergone a thorough database analysis ensuring no potential legal issue in the future, for instance, an accusation of defamation.

8.4 The Assessment of AEOI's Implementation

To be able to implement the AEOI, a jurisdiction has to conduct some efforts which, among others, include drafting the domestic regulations, making practice guidance and creating operational systems. To ensure the effectiveness of AEOI, the Global Forum has given the mandate to monitor and review the implementation of the AEOI through an assessment of each jurisdiction. The two areas where the assessment is going to be made are legal frameworks and effectiveness in practice (OECD, 2018b; 2019a). Each area will be assessed separately, and the combination of the assessments will be reflected in a jurisdiction overall determination that is expected to be issued in 2021 (OECD, 2019a). As for the time being, the assessment as to whether each jurisdiction already has the required legal frameworks is estimated to be ready by November 2020, and this will be followed by an assessment of effectiveness in practice (OECD, 2019a).

The overall rating of the assessment will determine to which degree a jurisdiction has complied with the AEOI Standard and measure how deep a jurisdiction understands the complicated implementation of the AEOI. To establish its role in the era of transparency and gain an international reputation, there is no other way for Indonesia but to put together all the required efforts to earn the highest rating as the expected result. To realise this expectation, DGT must have the commitment and consistency in carrying out AEOI's implementation. This commitment requires cooperation with all related stakeholders, not only within DGT but also external parties, including OJK, financial institution associations, and the financial institutions themselves. Committing to the AEOI Standard, building and maintaining a reliable system, continuous supervision on financial institutions' obligatory reports, and imposing sanctions where appropriate are just some of the elements that the DGT must consistently undertake in order to keep up with AEOI's implementation. Alternatively, AEOI, as an expected weapon in the long war against cross-border tax avoidance, would be just a meaningless campaign that has no impact on the ongoing fight or, even worse, provides no contribution to tax revenue at all.

9. CONCLUSION AND LIMITATION

9.1 Conclusion

It is almost irrefutable that most developing countries rely on tax revenue for financing their development. However, the amount of tax collected is still below their tax capacity due to the growing unacceptable tax practices by some high net worth individuals, such as keeping money in low tax jurisdictions or OFCs. Tax authorities worldwide have cooperated to exchange and obtain information held in offshore areas through the mechanism of The Exchange of Information on Request. However, this method is considerably less effective, particularly with regard to the financial data held by financial institutions, such as banks. The financial information of the taxpayers is often under bank secrecy domestic laws.

The Government of the Republic of Indonesia has enacted regulations regarding the access to financial information for tax purposes as the legal basis for Indonesia to join the AEOI. Indonesia has exchanged financial information based on the CRS with its partner jurisdictions since September 2018. Even after two years since its first implementation, the DGT recognizes that the implementation of AEOI still poses some challenges.

These challenges are manifested in 1) monitoring the compliance of financial institutions, which is a key for the DGT to obtain the high quality of financial information; 2) creating a secure and reliable system, which guarantees the confidentiality and data safeguard and optimizes the utilization of information received for tax intensification and extensification; and 3) establishing an AEOI implementation that follows the agreed standard, which will be rated later on through the ongoing ssessment of AEOI implementation.

Despite those challenges, the DGT is demanded to be consistently prepared with the correct tools and updated knowledge in order to implement the AEOI to the highest standard. Recognising that financial information is an important factor in analysing taxpayers' compliance, especially of those who hide their money abroad with the intention to neither report nor pay the correct amount of tax. The implementation of the AEOI is thus expected to increase the compliance level of taxpayers, which in turn, will result in significant additional tax revenue for the country.

9.2 Limitation

This research only conducts a literature review and a case study in Indonesia; hence it provides no comparison analysis with other developing countries that also implement AEOI. This comparison is necessary to widen the perspective regarding the challenges faced and steps taken by other tax authorities in implementing AEOI. There remains considerable scope in the AEOI area in terms of future research, not only to examine the ongoing development but also to extend the analysis to other regional groupings of developing countries. Since the goal is to bring additional tax revenue, and considering the exchange of financial accounts based on CRS in Indonesia has already been conducted twice, it would be interesting to investigate the effect of AEOI implementation on recovered tax using a quantitative approach.

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