



What do we know about Cooperative Compliance? Insights from Literature Review in Transfer Pricing Supervision

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ABSTRACT: Cooperative compliance is often defined as a framework for trust-based relationships in which tax authorities and taxpayers work together to establish and uphold mutual understanding. The main reported areas of tax compliance risks and disputes in Indonesia include profit shifting and transfer pricing. Through a literature review, we attempt a stocktake of the cooperative compliance literature in this review about transfer pricing supervision. A comprehensive literature search identified 17 studies published between 2014 and 2023. Two key types of interventions were identified: cooperative compliance and transfer pricing supervision. According to the review's findings, cooperative compliance research should focus more on using cooperative compliance as a strategic tool in business than just on tax compliance. This evaluation concludes with recommendations for future cooperative compliance research.

Keywords: Cooperative Compliance, Transfer Pricing Supervision, Literature Review



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INTRODUCTION

Unresolved issues with tax collection performance have persisted for a long time, especially in developing nations that frequently experience low tax ratios, high compliance costs, inadequate revenue collection from personal income taxes, and slow digitalization. ([Eberhartinger & Zieser, 2021a](#)). Multinational enterprises (MNEs) carry out more than 60% of all international trade transactions, the majority of which are cross-border transactions within MNEs ([Dunning & Lundan, 2008](#)) ([Sun et al., 2012](#)). This demonstrates that transfer pricing models are becoming increasingly significant in establishing transfer prices across borders ([Bartelsman & Beetsma, 2003](#); [McMahon et al., 2013](#); [Nguyen et al., 2020](#)) ([Chen et al., 2015](#); [Löffler, 2019](#)).

Main reported areas of tax compliance risks in Indonesia include Profit Shifting/Transfer Pricing, Other Tax Avoidance Schemes, Value Added Tax Fraud, Unpaid Tax Debts and Non filing of Returns. ([Bank, 2016](#)). As of my last knowledge update in September 2021, tax compliance risks in Indonesia could vary and change over time due to evolving regulations and enforcement

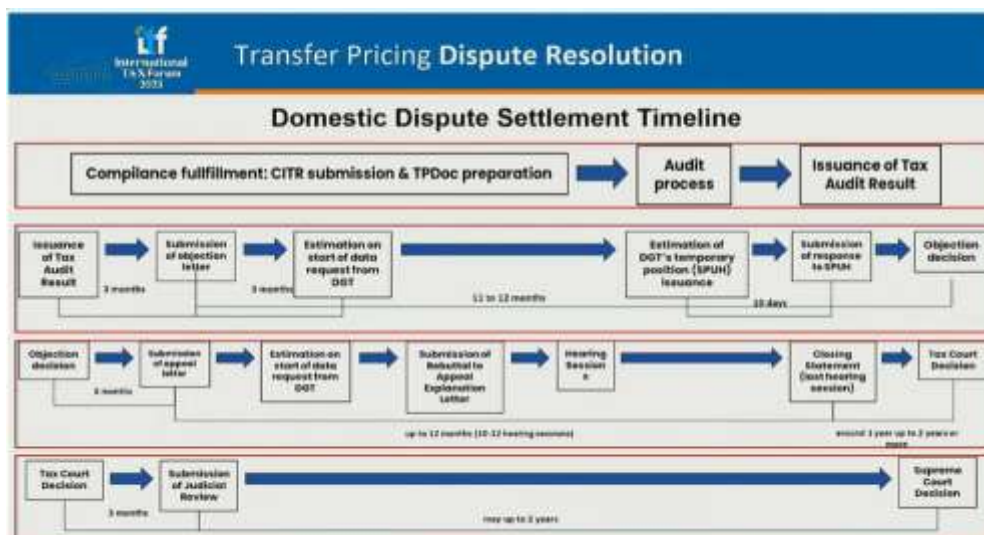
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priorities. However, some main reported areas of tax compliance risks in Indonesia. The number of transfer pricing conflicts has been rather high, and they are regarded as a significant problem in Indonesia's tax system (M. R. U. D. Tambunan, 2022). The findings from the hypothesis testing indicate a significant relationship between Transfer Pricing and Tax Planning Practices (E. W. Sari & Markhumah, 2023). According to our estimates, a company that prioritizes tax minimization has a GAAP effective tax rate that is 6.6 percentage points lower and, on average, saves around \$43 million more in taxes than a company that prioritizes tax compliance (Klassen, 2017)

The Indonesian tax authority, Directorate of General of Taxes (DGT) has been increasingly focused on transfer pricing issues (Susanti & Firmansyah, 2018). Companies operating in Indonesia must ensure that their transfer pricing policies are in line with arm's length principles and are properly documented. (D. Sari et al., 2021). Aggressive transfer pricing is a reflection of actions that are designed specifically to evade paying corporation taxes. That Investigations were made to look into important factors that affect transfer price hostility in Indonesia, in particular the elements that facilitate transnational businesses to carry out those actions (Smolarski et al., 2019; Waworuntu & Hadisaputra, 2016).

The process of resolving transfer pricing requires significant resources, compliance costs, and a lengthy timeframe. It need more three years for transfer pricing dispute resolution, from audit process until supreme court decision. Process of resolving transfer pricing practices, from the submission of the Annual Tax Return and Transfer Pricing Documentation to the decision of a review, can be presented in the following diagram.



(Source: ITF 2023)

The proposed approach posits that through the integration of complementary investments in enforcement, facilitation and trust . Taxpayers submit Annual Report and TP Doc to report tax obligations and transfer pricing documentation. Furthermore, DGT supervises the SPT reporting before the inspection is carried out. Taxpayers who have undergone the audit, objection, appeal and reconsideration process are continued to undergo transfer pricing supervision. Reformers have the potential to enhance both enforced compliance and quasi-voluntary compliance, provide

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enduring political backing for reform and generate conditions that are more conducive to the construction of stronger fiscal contracts ([Prichard et al., 2019](#)).

Using communication, transparency requirements, transfer pricing documentation and penalties, it is possible to effectively encourage taxpayer compliance with transfer pricing policies. ([Cooper et al., 2017](#)). When imposing disclosure requirements, the tax authorities must: Consult taxpayers at the development stage to secure support from all stakeholders; Give taxpayers enough information (and training, if applicable) and prompt notification of any planned changes to encourage awareness and buy-in ([Cooper et al., 2017](#)).

Cooperative Compliance in transfer pricing supervision is a collaborative approach between tax authorities and multinational corporations to ensure compliance with transfer price rules ([Rossing, 2013](#)). The background of this approach can be explained as follows:

1. The complexity of transfer pricing ([Holtzman & Nagel, 2014](#)). Transfer pricing involves the internal pricing of transactions between subsidiaries or divisions within a multinational company. This can be very complex and requires proper assessment to avoid inequalities in income allocation that may lead to tax evasion.
2. Low Compliance ([Chan et al., 2006](#)) With increasing globalization and the complexity of international business, tax authorities often face difficulties in monitoring and ensuring compliance of multinationals with transfer pricing rules.
3. International cooperation ([Borkowski, 1997](#)) In an effort to address this problem, many countries are working together to develop international guidelines and standards related to transfer pricing.

Cooperative compliance is an approach in which multinationals are committed to working proactively with tax authorities in managing their transfer pricing ([Kumar, 2021](#)). It involves open communication, the provision of accurate information, and joint agreement on the right taxation approach.

Cooperative Compliance Benefits can benefit both sides. For companies, they can reduce tax uncertainty and the risk of expensive tax disputes. Developing a cooperation model: Several countries have developed a cooperative compliance model in which companies and tax authorities agree on a transparent and collaborative audit process. This creates confidence between both sides.

The Cooperative Compliance approach in transfer pricing oversight is a joint effort to create a more open and trustworthy environment in which companies and tax authorities work together to ensure compliance with transfer price rules, reduce the risk of tax disputes, and improve tax compliance ([Klassen, 2017](#)).

The purpose of this paper is to describe the application of Cooperative Compliance in a Transfer Pricing Supervision. We examine its theories, strengths and providing examples on content and context. We present the rationale for our design based on theoretical principles of Cooperative Compliance. We reflect on the pros and benefit of utilizing this type of cooperative approach and consider implications for future compliance.

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METHOD

The objective of this study is to assess the efficacy of implementing cooperative compliance practices within the Directorate General of Taxes of the Republic of Indonesia in transfer pricing supervision. The analytical techniques employed in this work encompass a comprehensive review of relevant literature and the application of descriptive statistical analysis based on secondary data and qualitative analysis.

The research approach used in this study, the findings indicate that there is a significant correlation between the variables being examined. The secondary data, which was collected from various sources, was subjected to qualitative analysis in order to gain a deeper understanding of the phenomenon under investigation. The results gained from this analysis provide evidence to support the existence of a strong relationship between the variables.

The methodology employed in this study is the utilization of literature review. The study employs a qualitative research approach characterized by inductive reasoning. The objective of researchers is to elucidate social phenomena by giving precedence to the social realities identified in their investigation. Thorough analysis and examination, it has been observed that In employing a qualitative methodology, the researcher aims to concentrate on the contextual factors that contribute to the development of a comprehensive comprehension of the subject at hand.

The research under consideration involves the examination and formulation of theoretical frameworks. Researchers aim to utilize inductive reasoning This paper aims to assess cooperative compliance implemented at the Directorate General of Taxes of the Republic of Indonesia and other countries.

Tabel 1. List of Literature Study

No	Name and Title	Methodology	Result
1	Cooperative Tax Compliance: from deterrence to defference (Kirchler et al., 2014)	Qualitative	This study discusses slippery-slope tax compliance, which integrates economic and psychological factors. Two variables that affect tax compliance are power and trust. The results consistently show the influence of the trust factor which is greater than the power
2	COOPERATIVE COMPLIANCE, TAX CONTROL FRAMEWORKS AND PERCEIVED CERTAINTY ABOUT THE	Quantitative	The results show that the need for certainty and the importance attached to tax compliance have positive effects on the quality of an

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	TAX POSITION IN LARGE ORGANISATIONS (Goslinga et al., 2021)		internal tax control framework. Moreover, both studies find the quality of a tax control framework has a positive effect on perceived certainty about the tax position.
3	Risk Management, Internal Control and Cooperative Compliance in Taxation (Ronald Russo, 2019)	Qualitative	CC faces big challenges and should continue to be developed. One area of development is providing more guidance by Tax Authorities on the TCF, for instance (but not limited to) in the points I mention in 14.2.3
4	Innovations in Tax Compliance Conceptual Framework (Prichard et al., 2019)	Policy Research Working Paper	A key challenge for governments lies in finding the right combination of these three measures-enforcement, facilitation, and trust-to achieve revenue and broader development goals.
5	Taxing Large Businesses: Cooperative Compliance in Action (Larsen & Oats, 2019)	Quantitative	A key ambition for the cooperative compliance measures has been to increase efficiency and effective use of resources for tax administration and many stakeholders demand 'proof' of efficient resource usage, especially the taxpayers themselves.
6	Pengaruh Digitalisasi Layanan Pajak dan Cooperative Compliance Terhadap Upaya Pencegahan Tax avoidance Dimoderasi Kebijakan Fiskal Di Masa Pandemi (Tambun et al., 2020)	Kuantitatif	Hasil penelitian membuktikan bahwa digitalisasi layanan pajak dan cooperative compliance berpengaruh terhadap upaya pencegahan tax avoidance. Selain itu kebijakan fiskal selama pandemi covid 19 mampu memoderasi pengaruh dari cooperative compliance terhadap upaya pencegahan tax avoidance.

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7	Model Cooperative Compliance terhadap Kepercayaan Wajib Pajak dan Kepatuhan Wajib Pajak (Haniv, 2020)	Kuantitatif	Cooperative Compliance merupakan suatu paradigma hubungan otoritas pajak dengan WP, keduanya saling menaruh kepercayaan satu sama lain dan memiliki keinginan saling
8	The Effects of Cooperative Compliance on Firms' Tax Risk, Tax Risk Management and Compliance Costs (Eberhartinger & Zieser, 2021b)	Quantitative	Results show that horizontal monitoring firms perceive a significantly higher increase in tax certainty, which is associated with significant relative decreases in tax risk and compliance costs. Furthermore, while the quality of tax risk management upon entering the pilot project appears significantly higher for horizontal monitoring firms, they do not report greater improvement in tax risk management compared to the control group. These results are relevant for the development of cooperative compliance programs and the decision to participate in them.
9	COOPERATIVE COMPLIANCE PROGRAMMES: WHO PARTICIPATES AND WHY? (Goslinga et al., 2021)	Quantitative	We conclude that large organisations may benefit from CCP participation in terms of gaining more certainty about their tax position, whereas the tax authority may benefit because the organisation displays greater transparency. Both parties may benefit from the development of a better working relationship, but it appears that both parties need to continuously invest time and effort into the programme in order to actively maintain the cooperative relationship.

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10	Cooperative Compliance: SWOT Analysis for the Brazilian CONFIA Program (Martinez, 2021)	Quantitative	Cooperation between taxpayers and tax administration should be based on the responsibility of both, supported by mutual trust, which does not tolerate opportunistic behavior on both sides of the tax relationship.
11	KETERTERAPAN KONSEP COOPERATIVE COMPLIANCE PADA AKTIVITAS PENGAWASAN WAJIB PAJAK (Maulana & Abbas, 2021)	Kualitatif	Hasil penelitian ini menunjukkan bahwa pilar cooperative compliance belum diterapkan sepenuhnya karena beberapa hambatan. Pengaturan lebih lanjut mengenai komitmen, pengungkapan dan transparansi informasi, mekanisme pemberian kepastian, dan keterbukaan mengenai pendekatan manajemen risiko diperlukan untuk penerapan cooperative compliance secara optimal.
12	Developing a Cooperative Compliance Model for Developing Economies (Flanagan, 2018)	Qualitative	the implementation of cooperative compliance is still evolving and will need to adapt to the changing landscape of taxation and business. Thus, to sustain it in the long run, tax authorities must preserve the essence of cooperative compliance through continuous adaptations and prioritize trust as the basis for exchanging transparency with certainty to taxpayers.
13	Pelaksanaan Konsep Cooperative Compliance di Beberapa Negara OECD: Australia, Italia, Belanda dan Amerika Serikat. Bagaimana di Indonesia? (M. Tambunan, n.d.)	Kualitatif	cooperative compliance adalah mendorong adanya kepatuhan yang berkualitas; ditandai dengan pembayaran utang pajak dan penyampaian segala

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		jenis dokumen dengan cara yang efektif dan efisien
14	Nudges, Boosts, and Sludge: Using New Behavioral Approaches to Improve Tax Compliance (James Alm, Lilith Burgstaller, Arrita Domi, Amanda März and Matthias Kasper, 2023)	Qualitative Closer cooperation between administrators and academics should thus be facilitated and encouraged.
15	Cooperative versus adversarial tax audits: Implications of transparency for tax compliance and financial reporting quality (Adams & Bauer, 2023)	Quantitative We also compare the potential for an externality of higher financial reporting quality. Our findings support cooperation: firms under cooperative audits i) have lower differences between their effective tax rate and their size-industry peers and ii) display a modest spillover benefit in terms of a lower risk of subsequent financial. we design our study with this specific comparison in mind to better understand which of cooperative and adversarial audits have better outcomes. In that sense, we have a strong test of these audit options, bolstered by our consideration of endogenous treatment. Overall, our study generates important insights on the benefits of cooperative audits for corporate tax compliance and the potential, albeit modest, spillover to non-tax objectives.

Source: Previous Research

This study explores slippery-slope tax compliance ([Kirchler et al., 2008](#)), a complex process involving economic and psychological factors. It reveals that trust is a more influential factor than power in determining tax compliance. The need for certainty and the importance of tax compliance positively affect the quality of an internal tax control framework. The study also highlights the importance of cooperative compliance measures, which aim to increase efficiency and effective use of resources for tax administration. Horizontal monitoring firms perceive a higher increase in tax certainty, which is associated with significant decreases in tax risk and compliance costs.

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However, they do not report greater improvement in tax risk management compared to the control group.

The study concludes that large organizations may benefit from cooperative compliance participation in terms of gaining more certainty about their tax position, while tax authorities may benefit from greater transparency. Both parties need to continuously invest time and effort into the program to actively maintain the cooperative relationship. The study also highlights the potential for higher financial reporting quality through cooperative audits.

RESULTS AND DISCUSSIONS

There are four pillars that taxpayers must follow in order to increase tax compliance: registration, filing, reporting and payment ([Sub-group, 2004](#)). Cooperative compliance can be implemented before an inspection through transfer pricing risk analysis is conducted, that is, during transfer pricing monitoring ([Rossing, 2013](#)). A letter asking for an explanation of data and information about risks and non-compliance with transfer pricing policies may be given to taxpayers who face transfer pricing risks.

The findings of this study suggest that the implementation of cooperative compliance is not yet fully realised in various aspects, including business awareness, openness through disclosure and transparency, responsiveness, and disclosure and transparency by taxpayers ([Maulana & Abbas, 2021](#)). Finding the ideal mix of these three strategies—enforcement, facilitation, and trust—to generate income and advance more general development objectives is a major problem for government ([Prichard et al., 2019](#)).

Cooperative compliance programs were developed as a result of the search for new and efficient means of enhancing taxpayers' compliance behavior and risk management techniques. taxing bodies. OECD is an acronym for the Organisation for Economic Co-operation and Development. prominent proponent of cooperative compliance initiatives and a catalyst for the growth of these programs on a global scale ([Colon & Swagerman, 2015](#)).

The theory of cooperative compliance is a framework that describes how cooperation between tax authorities and taxpayers (companies or individuals) can improve tax compliance. This theory encompasses the concept that by encouraging collaboration, communication, and transparency between the two sides, the level of fiscal compliance can be enhanced without having to rely on severe sanctions or punishment. Here are some theories underlying cooperative compliance:

1. Trust Theory: This theory argues that a good collaboration between tax authorities and taxpayers can build trust. By having trust, taxable persons are more likely to comply with tax rules voluntarily, and taxation authorities will be more confident that the information provided by the taxpayer is accurate.
2. Social Norms Compliance Theory: This theory focuses on how social norms and expectations can influence tax behavior. In the framework of cooperative compliance, collaboration

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between tax authorities and taxpayers can help build social standards that promote tax compliance.

3. **Transaction Cost Theory:** Cooperative compliance reduces transaction costs in tax surveillance and enforcement. By sharing information and mutual understanding, both sides can avoid the costs associated with costly disputes and litigation.
4. **Voluntary Compliance Theory:** This theory states that when taxpayers feel that the tax system is fair and that they have the ability to understand and obey tax rules, they are more likely to obey voluntarily. Cooperative compliance seeks to create an environment in which taxation is considered more fair and understandable.
5. **Positive Incentive Theory:** Cooperative compliance can provide a positive incentive for taxpayers to comply with tax rules. The theories above help explain why cooperative compliance is seen as an approach that can enhance tax compliance in a more efficient and effective way. It also emphasizes the importance of building mutually beneficial cooperation between tax authorities and taxpayers to better tax goals.

Cooperative compliance is an approach to tax administration that encourages collaboration and transparency between taxpayers and tax authorities. This approach has several strengths, including:

1. **Enhanced Taxpayer Compliance:** Cooperative compliance fosters a culture of voluntary compliance by promoting open communication and trust between taxpayers and tax authorities. This can lead to increased compliance and reduced tax evasion.
2. **Efficiency:** The cooperative compliance model reduces the need for extensive audits and investigations, which can be time-consuming and resource-intensive for tax authorities. This leads to greater efficiency in tax administration.
3. **Predictability:** Taxpayers benefit from greater predictability in tax matters. They can have a clearer understanding of how their tax obligations are determined, reducing uncertainty and the risk of disputes.
4. **Cost Savings:** Both taxpayers and tax authorities can save money by avoiding the costs associated with lengthy tax disputes, audits, and litigation. This makes more resources available for other essential government services.
5. **Fairness and Consistency:** Cooperative compliance promotes fairness and consistency in tax administration. It helps ensure that taxpayers with similar circumstances are treated similarly, reducing the likelihood of arbitrary or unfair assessments.
6. **Improved Tax Authority Capabilities:** Tax authorities benefit from a more detailed understanding of the industries and sectors they regulate. This information can be used to better target their enforcement efforts and adapt tax policy as needed.
7. **Risk Mitigation:** For businesses, cooperative compliance provides a proactive way to identify and manage tax risks. By working closely with tax authorities, they can reduce the likelihood of costly surprises in the form of unexpected tax liabilities.

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8. Reputation and Trust: Engaging in cooperative compliance can help build a positive reputation for businesses and foster trust between taxpayers and tax authorities. This can be valuable in business relationships and public perception.

While cooperative compliance has several strengths, it also requires a high degree of transparency, mutual trust, and communication between taxpayers and tax authorities. Its success depends on the commitment of both parties to work together for the common goal of achieving a fair and efficient tax system.

Once the data from the field has been obtained. Researchers engage in the process of gathering and analyzing literature as a means to accomplish this task. Examples of sources commonly used in academic research include books, scholarly journals, scientific publications, newspaper stories, legislative documents, governmental regulations, and the act of doing searches. The acquisition of pertinent knowledge pertaining to design through electronic mass media, specifically television and internet news sources, is being sought.

This paper examines the management of compliance risk in the specific setting of tax audits within the Directorate General of Taxes. The user's text is not provided. Please provide the text that needs to be rewritten in Data are utilized to supplement data obtained from field studies in order to enhance the understanding of ideas pertinent to the research issue. Researchers have demonstrated a comprehensive understanding of the subject matter prior to doing fieldwork, starting with the initial stages of the research process. As one of the instruments employed in the analysis of data derived from field research.

CONCLUSION

The Directorate General of Taxes through Transfer Pricing Supervision has been able to improve taxpayer compliance and tax revenue and reduce collection costs in cooperative compliance program. There are three things that must be promoted with cooperative compliance in transfer pricing supervision in Indonesia. The cooperative compliance theory suggests that collaboration between tax authorities and taxpayers can enhance tax compliance without severe sanctions or punishments, promoting communication and transparency. Cooperative compliance in transfer pricing supervision is an approach to tax administration that encourages collaboration and transparency between taxpayers and tax authorities.

In the future, DGT is expected to regulate transfer pricing supervision dan expand the database with tax control framework tools. Cooperating with authorities that affect taxpayers such as tax consultants, legal consultants, etc. In this way, it is hoped that the plan to accelerate the core tax system can be implemented and have an impact at the level of taxpayer confidence in the tax authorities, and result in high taxpayer compliance.

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