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Evaluation of The Role of Internal Compliance Unit on The Effectiveness of Internal Control

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ABSTRACT

This study aims to evaluate the second line roles in supporting the effectiveness of internal control based on its principles. In the Directorate General of Taxes (DGT), the Internal Compliance Unit serves as its second line of defense. The present study was conducted at the Internal Compliance Sub-directorate which is the Internal Compliance Unit Echelon I level at DGT. A descriptive qualitative research applying a deductive approach with a case study method was carried out to answer the research problems. The criteria used to evaluate the second line roles on the effectiveness of internal control refer to the publication of the Committee of Sponsoring Organization of Treadway Commission (COSO) in collaboration with the Institute of Internal Auditors (IIA) in July 2015 entitled "Leveraging COSO Across the Three Lines of Defense". The results of the study shows that the operation of UKI in supporting the effectiveness of internal control is quite satisfactory. However, several principles have not been implemented optimally.

INTRODUCTION

The economic growth rate of Indonesia cannot be separated from the role of taxes which have become the vital aspect of state finances. Taxes have an increasingly crucial contribution to the state revenue. According to Szarowska, (2014), the main purpose of taxation is to transfer resources from one group to another in order to achieve certain development goals without jeopardizing economic goals. Lapatinas, Kyriakou, & Garas (2019) argued that there are various tax policies in each country, leading to different capacities to produce and export better products. For developing countries, large amounts of tax revenue are needed to enforce the smooth and efficient functioning of the state, both at the national and regional levels (Neog & Gaur, 2020). Meanwhile, Vo et al. (2019) stated that unequal state income is a consequence of economic development. In the 2019 State Revenue and Expenditure Budget (APBN) posture, revenue from the tax sector accounts for more than 70% of total revenue (Ministry of Finance, 2019).

The Directorate General of Taxes (DGT) is an Echelon I unit of the Ministry of Finance whose task is to collect state revenues through taxes. DGT has an extremely vital role in the government as the achievement of tax revenue depends on its performance in exploring and seeking tax potential. Furthermore, all the financing needed by the government to run and provide access to basic services for the community is dependent heavily on tax revenues. As the only tax authority in Indonesia, it DGT is highly expected to carry out its duties in optimally collecting state revenues. According to Savic et al. (2015), tax policy and administration is the most important part of any tax system. The power of the tax authorities can affect both tax compliance (public trust to pay taxes) and tax avoidance (Hartl et al.,2015). To ensure high tax compliance among all citizens, the tax authorities then rely on two main measures, i.e. audits and fines, as well as certain steps to realize fair procedures (Gangl et al. 2015). Meanwhile, the estimation of tax revenue can be calculated in various forms and measures, such as simple trend model, time series forecasting, simulations, regression model, expert judgment forecasting, and consensus forecasting (Tibulca, 2021).

Comparison of Target and Realization of the State Budget (in Millions IDR)

Note	2015	2016	2017	2018	2019
Target	1.294,26	1.355,57	1.283,57	1.424,00	1.577,56
Realization	1.061	1.105,73	1.151,03	1.315,51	1.332,06
Achievement	81,96%	81,59%	89,67%	92,93%	84,44%

Source: DGT Performance Report, 2015-2019

The table above presents a comparison of the target and realization of the 2015 - 2019 APBN tax revenues. In those five years, the percentage of tax revenue achievement has always been consistently above 80%. In other words, the achievement of tax revenues shows an increasing trend, with the highest achievement in 2018, reaching more than 90%. Although the achievement does experience a decrease in 2019, the percentage is still higher than that of 2015 and 2016.

The vision, mission, and objectives of DGT, however, are not only measured from the achievement of tax revenue targets but also from the aspects of ethics and integrity. One of the missions of DGT is to develop digital-based core business processes that are supported by an adaptive and collaborative organizational culture and tax officials who have the best integrity, professionalism, and strong motivation. In this regard, DGT faces a cultural risk in the form of unethical behavior of its members which then affects the reputation and values of this organization in public. For financial companies, cultural risk is the key element of corporate culture that has an effect on the image of the organization (Ring et al., 2016).

Such unethical behaviors have appeared multiple times at DGT, with the most infamous example being the two mega corruption and money laundering cases which involve former DGT employees Gayus Tambunan and Dhana Widyatmika (CNN Indonesia, 2016). A similar case occurred in 2018, this time involving the former Head of the Tax Service Office (KPP Pratama) of Ambon City who was arrested by the Corruption Eradication Commission or KPK (Republika, 2018). Corruption is not the only unethical act committed by members of DGT. In 2020, there was a bribery case involving the former Head of the Office and the Functional Team of the Tax Auditor for Foreign Investment (CNN Indonesia, 2020). The latest one is the bribery case related to tax audits in 2021, where the perpetrator was an Echelon II DGT official who ironically had served as Director

of Audit and Collection (CNN Indonesia, 2021). According to Naher, Hoque, Hassan, Balabanova, Adams, & Ahmed (2020), corruption itself is a common consequence of poor governance triggered by a lack of transparency, weak accountability and inefficiency, and less participation of the citizens. Corruption is the main enemy of all mankind which can damage the country and infect every level of the government (Pertiwi, 2018; Sihombing, 2018). With high integrity and transparency from all members of the organization, cases of corruption and bribery can be prevented effectively (Chizema & Pogrebna, 2019).

Institutional integrity is an important indicator of the performance of DGT which can even affect the achievement of tax revenue targets. Integrity is a must for tax officials. Corruption is something that should never be in the mind of any tax officer as it definitely destroys the pillars of the national economy and creates public distrust. Building a good image of an institution as big as DGT is not easy, while corruption can effortlessly push back the positive foundations that have been built through all difficulties. The number of corruption cases that have occurred at DGT indicates that integrity is a vital aspect that must always be upheld by its members to realize the tax reform in Indonesia. This integrity must include an attitude of anti-corruption, honesty, and accountability (Huberts, 2018).

The enforcement of integrity is a part of internal control. According to the Committee of Sponsoring Organization of the Treadway Commission (COSO) (2013), internal control is a process carried out by the supervisory board, management, and other personnel designed to provide sufficient confidence on the achievement of objectives related to operations, reporting, and compliance. In other words, internal control must be implemented by an organization so as to provide reasonable assurance on the reliability of its financial statements, operational effectiveness and efficiency, as well as its compliance with applicable policies, procedures, laws, and regulations (Moeller, 2016). Internal control is instituted by different organizational actors from the micro level to implement a good system that not only measures a simple compliance but also provides added values to the organization (Henk, 2020).

Based on the aforementioned explanations, it can be said that internal control is not only related

to financial and accounting issues but also covers all aspects of the organization. Therefore, internal control can run well if there is strong belief that the organization has achieved its vision, mission, goals, and objectives by following applicable ethics, producing reliable and trustworthy financial statements, and complying with official regulations.

The establishment of achieving the effectiveness of internal control is closely related to the functions of the second line of defense formulated by the IIA. The second line functions include specific skills such as risk management, information security, financial control, physical security, inspection, compliance, legal, and the other functions which may vary depending on the specific needs of the organization (COSO & The IIA, 2013).

In DGT, there is a section within the organization that carries out duties and functions aimed at supporting the effectiveness of internal control and internalization of organizational culture, namely the Sub-Directorate of Internal Compliance, commonly called the Internal Compliance Unit (hereinafter referred to as UKI) at the Echelon I level. UKI serves as the second line of defense of DGT. PMK 217/PMK.01/2018 concerning Organization and Working Procedure of Ministry of Finance explains that UKI has the following roles:

1. preparing materials for strategies and designs, as well as implementing the internalization of compliance;
2. implementing and preparing reports of internal compliance tests; and
3. preparing materials for strategies, designs, and implementation of quality assurance concept development trials.

The importance of the role of UKI and the previous scandalous cases involving the internal parties of DGT have shown that a careful and in-depth evaluation of the roles of UKI must be carried out. There are still no specific organizational functions to assess the suitability of the implementation of UKI's tasks and duties. Several previous studies have been done to analyze the factors that influence the audit quality of UKI (Cahyadi, 2016), the perceptions of the roles of UKI and its effects on employee performance (Wika, 2017), and the effects of internal compliance monitoring on employee performance (Nazuwir, 2018). Therefore, it is necessary to conduct further

studies on the effectiveness of the implementation of UKI's duties based on the principles of internal control.

This study was conducted at the Sub-Directorate of Internal Compliance (UKI at the Echelon I level at DGT office), which serves as the second line at DGT. The criteria used to evaluate the second line roles on the effectiveness of internal control refer to the publication of COSO in collaboration with the Institute of Internal Auditors (IIA) in July 2015 entitled "Leveraging COSO Across the Three Lines of Defense". This publication describes the roles of each line of defense against the seventeen principles of internal control codified in the 2013 COSO framework.

LITERATURE REVIEW

Internal Control System

Every organization or entity must have certain goals to be achieved and these goals are then described in its vision, mission, and strategies. Organizational goals can be set by aligning the goals of each personnel, as well as each unit or division within the organization, with the goals of the organization or company (goal congruence). This alignment can work effectively if it is supported by a good control system, which is a system that can ensure the success of this alignment so that the main goals of the organization can be achieved ultimately. The objective of the control system itself is to achieve or maintain an expected condition.

According to the Committee of Sponsoring Organization of Treadway Commission (COSO) Internal Control (2013), the objectives of internal control include (1) operating objectives, (2) reporting objectives, and (3) compliance objectives. Meanwhile, the components of internal control according to COSO Internal Control (2013) are (1) control environment, (2) risk assessment, (3) control activities, (4) information and communication, and (5) monitoring activities. In addition, COSO Internal Control (2013) also lists several limitations of internal control, such as: (1) the incompatibility of the objectives set as the basis for setting up internal control; (2) the fact that someone's opinion in making a decision can also be inaccurate; (3) disturbances caused by human error, (4) management's ability to override internal control; (5) the ability of the management, other

personnel, and/or third parties to avoid control through collusion, and; (6) external incidents beyond the control of the organization.

The Three Lines of Defense Model and the Second Line of Defense

The Institute of Internal Auditors (IIA) published a position paper in 2013 entitled "The Three Lines of Defense in Effective Risk Management and Control", stating that this model is adapted from the Federation of European Risk Management Associations (FERMA). According to the IIA, the governing bodies and senior management are the main stakeholders of the three lines of defense model; both are responsible for setting goals, determining strategies to achieve those goals, and establishing the best governance structures and processes to manage risks in achieving the goals. According to the IIA's three lines of defense, an organization consists of: (1) the first line: functions that own and manage risks, namely operational managers; (2) the second line: functions that oversee risks, such as risk management functions, compliance functions, and controllership functions; and (3) the third line: the function that provides independent assessment, namely the internal audit function. The IIA also states that all lines must be present in every organization, regardless of size or complexity. However, under certain conditions, certain lines of defense can be combined if necessary. This can happen especially in small organizations.

In 2015, COSO recommended the use of the three lines of defense model to implement its internal control framework published in 2013. This recommendation can be seen from its publication in July 2015 entitled "Leveraging COSO Across the Three Lines of Defense", in which COSO collaborates with the IIA as one of its supporting organizations. This publication describes the role of each line of defense as well as the role of the governing bodies and senior management in the seventeen principles of internal control codified in the 2013 COSO framework. Specifically, the second line assists the first line in implementing strategies, providing insight into risks, helping to manage the risks, performing control based on existing policies and procedures, as well as obtaining information and reporting to the board of directors regarding the overall risk conditions. Although not completely independent, the second line can participate in

determining, implementing, and developing the process of risk management and internal control. In some organizations or entities, the second line can even take part in certain decision-making processes (ipaca.id, 2020).

The second line functions may vary greatly, depending on the size of the organization. In large, publicly-traded, complex, and/or highly regulated organizations, all of these functions may be separated and distinct. On the other hand, in smaller, privately-owned, and less complex organizations, some second-line functions may be combined or even absent. For example, some organizations may combine legal and compliance functions into one department or combine health and safety departments with environmental functions. The second line monitoring is adjusted to the organization's specific needs, generally separated from day-to-day operations. In many organizations, monitoring activities are spread across the organization. However, in some cases, the monitoring function may be limited to one or a few areas. Second line functions may directly develop, implement, and/or modify the internal control and risk systems of the organization. These functions may also take on decision-making roles for certain operational activities.

Ethics and Integrity

A government system that is clean and free from Collusion, Corruption, and Nepotism (KKN) is the main prerequisite for growing public trust (Ismail, 2017). A country will be more well-developed and its people will be more prosperous if it is supported by a good government that is clean and free from corruption. Ethics and integrity are two crucial keys to realize good governance. According to Ismail (2017), government's ethics is a teaching to behave properly and correctly based on benevolent values related to human nature. Meanwhile, Indonesia Dictionary defines integrity as the qualities, characteristics, and circumstances that describe something in its entirety, so that it has the potential and ability to radiate authority and honesty.

RESEARCH METHODS

Approach, Methods, Data Analysis

This study applies a descriptive qualitative approach consisting of a series of interpretive

techniques that aim at describing, decoding, and translating phenomena that occur naturally in the social world in order to gain a deeper understanding of a situation (Cooper & Schindler, 2014). According to Cooper & Schindler (2014), descriptive study attempts to seek answers to who, what, when, where, and sometimes how questions, thus having the task of describing or defining the subject, often profiling a group of problems or events. In addition, this study uses a case study method applying a deductive approach to conduct the data analysis. The deductive approach is an approach that is based on something that has been identified about a particular domain as well as the theoretical considerations concerning that domain (Bryman, 2012). This approach begins with a formal theoretical understanding and field observations.

The case study method is divided into a series of detailed and in-depth scientific activities carried out intensively and about a program, event, and activity, either at individual, group of people, institution, or organization level, which aims to gain comprehensive knowledge (Rahardjo, 2017). According to Yin (2003), a case study is a method used to examine various types of data sources such as documents, artifacts, interviews, and observations. Therefore, the case study is seen as a powerful research method for obtaining multiple perspectives from a single organization, state or situation, event, or process at a point in time or over a certain period (Cooper & Schindler, 2014). The collected data were analyzed using descriptive account and content analysis, with the main research object being the Directorate General of Taxes (Direktorat Jendral Pajak/DGT), especially the Sub-Directorate of Internal Compliance Unit (Sub-direktorat Kepatuhan Internal/SKI).

Data Collection Techniques

The data are collected through two stages, namely: (1) the collection of the primary data, which are obtained directly from the Head of the Sub-Directorate of Internal Compliance Unit, Head of the Compliance Testing Section, Head of Quality Assurance Section, Head of Compliance Internalization Section, and UKI Echelon I officers, as well as other employees involved in the preparation of the internalization program of organizational values/culture, and; (2) the collection of the secondary data in the form of the 2018-

2020 DGT Performance Report, 2018-2020 DGT Annual Report, 2020-2024 DGT Strategic Plan, as well as relevant regulations, journals, information from printed and online media, books, and other supporting documents.

Research Instruments

Data collection is carried out using several instruments such as semi-structured interviews and documentation taken from important notes from institutions or organizations as well as individuals in the form of DGT Performance Reports; DGT Annual Reports; DGT Strategic Planning documents; documents from all sections of UKI in carrying out their duties and functions; documents from the Compliance Internalization Section at the Sub-Directorate of Internal Compliance Unit in carrying out their duties and functions; as well as other relevant information to answer the research problems related regulations, journals, news from printed and online media, books, and other documents.

RESULTS AND DISCUSSION

Evaluation of the Role of the Internal Compliance Unit (UKI) on the Effectiveness of Internal Control Based on the Principles of Internal Control

1st Principle of Internal Control: Organization Demonstrates Commitment to Integrity and Ethical Values

The first roles and responsibilities of the second line of defense include testing compliance, investigating potential violations of the rules, and carrying out other specific tasks related to integrity and ethical values. The results of the interviews and documentations prove that the Sub-Directorate of Internal Compliance (UKI) has carried out the aforementioned roles and responsibilities based on certain programs that have been previously prepared. The activities initiated by UKI are (1) preparing the code of ethics and code of conduct for the employees of the Directorate General of Taxes (DGT), (2) strengthening anti-corruption culture, (3) monitoring the implementation of the code of ethics and code of conduct for the employees, (4) establishing an integrity zone towards a corruption-free area (ZI-WBK) and a

clean-serving bureaucratic area (ZI-WBBM), (5) preparing the implementation of the measurement of the organizational integrity index, and (6) acting as the whistle-blowing system (WBS).

2nd Principle of Internal Control: The Supervisory Board Demonstrates Independence from Management and Exercises Oversight on the Development and Implementation of Internal Control

Normatively, the effectiveness of supervision carried out by the supervisory board is supported by the structures and processes established by management at the business execution level. The DGT Supervisory Board consists of internal party, which is the Inspectorate General of the Ministry of Finance and several external parties such as the Audit Board of the Republic of Indonesia (BPK), the Financial and Development Supervisory Agency (BPKP), and the Taxation Supervisory Committee. In relation to this first principle, the communication pattern between UKI and the supervisory board needs to be explored more deeply. In carrying out its duties, UKI is responsible to the head of each work unit as well as to the UKI leaders at higher levels. Based on the interviews, it is known that for each monitoring and compliance testing conducted by UKI, a report on the results is submitted to the Echelon II level, which is the Director of Internal Compliance and Transformation of Apparatus Resources (hereinafter referred to as KITSDA). Besides the Director of KITSDA, the report is also submitted to the third line, which is the Inspectorate General of the Ministry of Finance. The testing results reported by UKI can be used as evaluation material by the Leaders and the Inspector General as the Supervisory Apparatus to develop the implementation of internal control at DGT in particular, and at the Ministry of Finance in general.

In addition to submitting reports, the communication between UKI and the supervisory board is also done through regular monitoring and evaluation meetings conducted both online and offline. Routine meetings are held at both sub-directorate and directorate levels, as well as with the supervisors of the Inspectorate General of UKI. These meetings usually discuss the implementation of performance achievements and obstacles that occur during the work programs. Figure 1

below presents a tiered scheme of UKI's internal responsibilities within DGT.

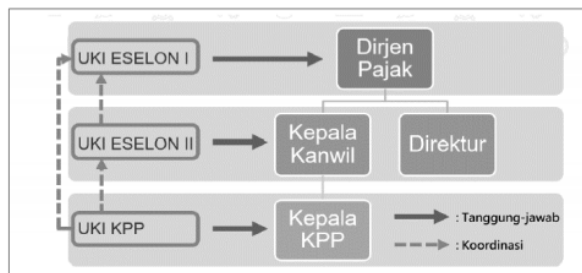


Figure 1. The scheme of UKI's responsibilities in stages

Apart from the internal parties, several external parties also conduct supervision/inspection of DGT, such as the Audit Board of the Republic of Indonesia (BPK), the Inspectorate General of the Ministry of Finance, and the Financial and Development Supervisory Agency (BPKP), as well as a non-structural committee, namely the Taxation Supervisory Committee.

3rd Principle of Internal Control: Under the Supervision of the Board of Commissioners (or Board of Supervisors), Management Establishes Organizational Structure, Reporting Lines, and Appropriate Authorities and Responsibilities following the Set Objectives

The second line, together with the management, carries out its authorities and responsibilities according to certain duties and functions. Based on the Minister of Finance Regulation (PMK) Number 87/PMK.01/2019 dated 11 June 2019 concerning Amendments to PMK Number 217/PMK.01/2018 on Organization and Work Procedures of the Ministry of Finance and to PMK Number 210/PMK.01/2017 dated 29 December 2017 on Organization and Work Procedures of DGT Vertical Agencies, the Sub-Directorate of Internal Compliance is one of the sub directorates of the Directorate of KITSDA whose function is to formulate strategies and design for the implementations of internal compliance systems and quality assurance concept development trials.

4th Principle of Internal Control: Organization Demonstrates Commitment in Recruiting, Developing, and Retaining Competent Individuals following the Defined Goals

The second line must ensure that employees and their activities are in line with the performance

indicators provided by the management and oversee the management in placing its employees according to their competencies. In DGT, the achievement of employee performance indicators is handled by the Sub-Directorate of Personnel Management Development (PMK) and the Bureau of Organization and Administration (Organta). However, UKI also carries out tests related to the achievements of the Key Performance Indicators (KPI) which are based on certain themes and business processes. In addition to conducting tests related to the achievements of KPIs, the second line needs to make sure that business processes related to human resources (such as recruitment, promotion, transfer, and many others) run well. Based on the results of the interview, there has been no compliance test done on the business processes regarding Human Resources (HR). The reasons for this include the focus of compliance tests which concentrate only on the main business processes of DGT, the limited number of second line functions, and the absence of special competencies possessed by the test executors related to HR business processes. This shows that UKI has not played an optimal role in supporting the effectiveness of internal control in the 4th principle.

5th Principle of Internal Control: Organization Provides Support to Individuals Responsible for the Implementation of Internal Controls following the Defined Goals

In the fifth principle of internal control, the second line monitors and reports on the fulfillment of certain internal control responsibilities. In DGT, there is Internal Control Monitoring (PPI) whose activities are carried out on business processes and activities in the implementation of DGT's duties by monitoring the main controls to assess the quality of the internal control system from time to time. This monitoring aims to ensure that the established main controls have been running in accordance with the systems, procedures, laws, and regulations. The activities of PPI include reviewing, evaluating, and/or conducting compliance testing on the entire process of functions, activities, and work units within DGT. These activities can be done daily, weekly, or monthly. Meanwhile, the results of the interview point out some factors that must be taken into consideration, namely: (1) risk factors of work unit; (2) geographical factors of work unit, and (3) high-risk business processes. Monitoring is also

performed on the follow-up to recommendations which are in the form of the improvement of business processes, policies, and/or procedures that can ultimately provide added value and assist the organization in achieving its goals as well as the efficiency and effectiveness of organizational governance.

6th Principle of Internal Control: Organization Sets Clear Objectives for the Identification and Assessment of Risks Related to These Objectives

Under the 6th principle of internal control, the second line is not responsible for setting or approving overall entity-level objectives. However, the second line may need to develop, implement, monitor, and report on objectives or sub-goals related to specific areas of expertise, such as compliance or quality assurance. Regarding this principle, UKI functions as a risk manager in accordance with KEP-702/PJ/2019 concerning Guidelines for the Implementation of Risk Management in the Directorate General of Taxes. UKI formulates KEP-702/PJ/2019 as the implementation of its tasks UKI task in the 6th principle of internal control. In addition, UKI acts as a risk management reviewer as stipulated in PER 05 of 2020 regarding the Implementation of the Duties of the Internal Compliance Unit within the DGT.

7th Principle of Internal Control: Organization Identifies Risks for Achieving Overall Entity-level Goals and Implements Risk Analysis to Establish Risk Management

According to the 7th principle of internal control, the second line carries out the risk management function which is responsible for the risk management whose responsibilities. may be delegated significantly on the identification of risks and their controlling aspects. The scopes of the implementation of risk management activities carried out by UKI include: (a) updating regulations related to the application of risk management, namely Kepdirjen Number KEP-702/PJ/2019 regarding Guidelines for the Implementation of Risk Management within DGT, (b) providing risk management assistance in the form of technical guidance to the Risk Owner Unit (UPR) regarding the procedures for compiling reports on the implementation of risk management in accordance with the provisions, (c) analyzing the reports on the

implementation of risk management, to review and provide recommendations on the Risk Management Implementation Report (LPMR) prepared by UPR, (d) evaluating the implementation of risk management in vertical units to assess the Maturity Level of Risk Management Implementation (TKPMR) and determine efforts to improve the quality of the risk management implementation; and (e) preparing the List of Risks and Risk Mitigation Book for the DGT vertical units.



Figure 2. DGT's Risk Dictionary

8th Principle of Internal Control: Organization is Aware of the Potential Fraud in Conducting Risk Assessments on the Achievement of its Goals

In the 8th principle, the second line makes sure that risk assessment and control include the assessment of fraud risks. In this regard, the second line must establish an investigation unit that plays a vital role in preventing and detecting fraud. Besides, the second line is also assigned to developing and monitoring policies and procedures for all entities related to potential fraud. The Decree of the Director General of Taxes Number 702 of 2019 explains that potential fraud is included in the priority risk category; fraud risk is ranked 4th after state financial and assets, policy, and reputation risks. To prevent behavior that deviates from the code of ethics and code of conduct as well as to prevent fraud, UKI conducts sampling monitoring to the vertical units and directorates at the head office of DGT. The methods used by UKI include survey, observation, surveillance, inspection, team meetings, and other methods (PER-05). In addition to monitoring, UKI must uphold the anti-fraud principle through various internalization media, such as offline meetings, short messages through the logbook application (an application accessed by all DGT employees to report their attendances

online), as well as videos and posters containing messages about the prohibition of fraud.

9th Principle of Internal Control: Organization Identifies and Assesses Changes that May Have a Significant Influence on the Internal Control System

In the 9th principle, the second line assists the management in assessing the effects of changes on the internal control system, always proactively adapts to changes, and regularly monitors and considers rapid changes to the legal, regulatory, and compliance risks of the organization. At the beginning of 2019, UKI prepared the UKI Annual Monitoring Plan (RPT) at DGT and the main control monitoring was subsequently carried out monthly for the activities outlined in the RPT. Besides, UKI also issued a code of ethics monitoring plan during the COVID-19 prevention period and submitted inputs for the preparation of the 2020-2024 DGT Strategic Plans. These prove that UKI has done a reasonably good job in supporting the effectiveness of internal control in the 9th principle.

10th Principle of Internal Control: Organization Selects and Develops Control Activities that Contribute to Minimizing Risks on the Achievements of its Goals so as to Reach an Acceptable Level of Risk Tolerance

Under the 10th principle of internal control, the second line is generally responsible for monitoring controls over management's instructions and may also participate in the selection and development of those controls, but with the management remaining in charge of the internal control system. To minimize potential risks, UKI conducts several important activities, including the reinforcement to build a risk-aware culture for work units. The results of the interviews show that the development of a risk-aware culture can be quite tough at times. During the implementation of the risk management process, UKI also analyzes the risk management documents prepared by the Risk Owner Unit (UPR) at Echelon II level. Based on the analysis report, UKI will then determine which UPR should conduct Risk Management Monitoring and Evaluation which aims to assess the overall process and environment for implementing risk management at the UPR. Besides, UKI also selects which UPR to receive assistance on risk management. This analysis on the

risk management documents is conducted to assist UPR in implementing risk management in the next period. UPR can also request assistance from UKI, if needed. UKI plays a fairly good role in supporting the effectiveness of internal control on the tenth principle. This can be seen from the preparation of the Risk Dictionary, the Decree of Director General of Taxes (KEP) Number 702 which is formulated by UKI, containing the stages and processes of risk management, and the Periscope application to facilitate the vertical units in preventing and managing potential risks.

11th Principle of Internal Control: Organization Selects and Develops General Control Activities over Technology to Support the Achievement of its Goals

In the 11th principle of internal control, the second line is assigned to monitor certain technological activities. Regarding technology monitoring, DGT includes the monitoring materials and methods in PER-05 of 2020, in which the monitoring of control over technology is termed Information and Communication Technology -Based Control Monitoring (PPTIK). PPTIK is carried out to monitor the main controls based on information and communication technology. PPTIK has a number of specific tasks in monitoring certain systems and control activities over business processes contained in an application. It is supported by applications embedded in information technology systems. One of the implementers of PPTIK mentioned in PER-05 is the Directorate of KITSDA (in this case, UKI). PER-05 also states that the planning, implementation, and reporting of PPTIK by UKI are set out in the RPT. UKI has not performed its role optimally in supporting the effectiveness of internal control in the 11th principle. This is indicated by the absence of instructions for implementing PPTIK as outlined in the RPT so that UKI has not carried out PPTIK activities as expected.

12th Principle of Internal Control: Organization Implements Control Activities through Specific Policies that Define Expectations through Procedures that Turn the Policies into Actions

In the 12th principle, the second line monitors compliance with specific policies and procedures established by the management,

assists the management in the development and communication of policies and procedures, and oversees the potential for risk appetite set by the organization. Regarding this principle, UKI has played a good role in supporting the effectiveness of internal control in the 12th principle by conducting compliance testing with specific policies and procedures established by the management, assisting the management in the development and communication of policies and procedures, and ensuring that potential risks related to the risk appetite set by the organization are well-monitored.

13th Principle of Internal Control: Organization Obtains or Generates as well as Uses Relevant and Quality Information to Support Other Components of Internal Control to Function Properly

In the 13th principle, the second line collects information from across the organization for use in monitoring activities. One of the information-gathering activities done by UKI is the establishment of supervision over the code of ethics and code of conduct. In this activity, UKI collects data from various relevant sources to see which work units require intensive internalization of compliance. Complaint data that enter the WBS channel is also used by UKI to determine which units need to be monitored. In addition to monitoring the code of ethics, an assessment regarding the activities that have the highest risks is also carried out during compliance testing activity. According to the respondents of this study, there is a process of collecting data and information used as material for consideration in selecting the monitored work units. This proves that UKI has played its role in supporting the effectiveness of internal control in the 13th principle.

14th Principle of Internal Control: Organization Communicates Information Internally, including the Information on the Objectives and Responsibilities of Internal Control to Support its Implementation

In the 14th principle, the second line monitors, collects information, and communicates the obtained information to the first and third lines as well as the supervisory board regarding compliance monitoring/testing activities. In addition, the second line is responsible for

monitoring communication/complaint channels such as the whistleblower hotline. Regarding the monitoring results, UKI will send the report to the Director of KITSDA. UKI will also compile a memorandum of recommendation for the vertical units, which is generally addressed to the heads of the vertical units. To report to and request data from the third line regarding the reports of monitoring activities conducted by UKI, all requested reports are prepared by UKI to be submitted to the third line of DGT, namely the Inspectorate General. By monitoring, collecting information, and communicating specific information to the first and third lines or the supervisory board regarding compliance monitoring/testing activities, UKI has played a role in supporting the effectiveness of internal control under the 14th principle.

15th Principle of Internal Control: Organization Maintains Communication with External Parties regarding Specific Matters that may Influence the Other Components of Internal Control

In the 15th principle of internal control, the second line contributes to the reporting of certain information needed by external parties related to the internal control of the organization. The external parties include the Functional Supervision Apparatus, namely the Audit Board of the Republic of Indonesia (BPK), the Inspectorate General of the Ministry of Finance, and the Financial and Development Supervisory Agency (BPKP), as well as a non-structural committee, namely the Taxation Supervisory Committee (DGT, 2019). Based on the recommendations from the results of the inspection by the Functional Supervision Apparatus, the Directorate of KITSDA submits a request for a follow-up, coordination, and assistance/supervision of the object being examined. Furthermore, based on the results of the assistance and follow-up activities submitted by the object, the Directorate of KITSDA will forward the follow-up documents to the Functional Supervision Apparatus for evaluation based on the work procedures and standards applicable in each agency. By reporting information needed by the external parties regarding the organization's internal control, UKI has a quite significant contribution in supporting the effectiveness of internal control in the 15th principle.

16th Principle of Internal Control: Organization Selects, Develops, and Carries Out Ongoing and Separate Evaluations to Ensure that Internal Control Components Are Existing and Functioning Optimally

In the 16th principle of internal control, the second line carries out continuous and separate evaluations to check if all components of the internal control system exist and function as expected. In PER-05, it is stated that ongoing monitoring is monitoring done by UKI on internal control inherent in the normal operating activities of an entity, which includes routine management and supervision activities as well as other actions taken by the owners of controls in carrying out their duties. Meanwhile, a separate evaluation is an assessment of the quality of internal control performance within a specific scope and frequency based on the risk assessment and the effectiveness of continuous monitoring procedures. Regarding this principle, UKI only contribute to the separate monitoring process. Meanwhile, the ongoing monitoring process is not carried out by UKI due to the absence of appropriate tools and other influencing factors.

17th Principle of Internal Control: Organization Evaluates and Communicates Internal Control Weaknesses Timely to Responsible Parties, including Top Management and the Board of Commissioners (or Similar Oversight Boards), to Take Corrective Actions

In the 17th principle, the second line can obtain a delegation of responsibility for monitoring and reporting control weaknesses. PER-05 explains that the findings of the main control monitoring results must be submitted to the authorized parties to take corrective steps. Each finding should propose recommendations that can eliminate/minimize the causes of the finding. The provided recommendations must clearly state which parties are responsible for carrying out the follow-up. In identifying the responsible parties, it is necessary to pay attention to the authority of these parties to carry out the follow-up as expected. The findings of the main control monitoring results are submitted in the Main Control Monitoring Results Report (LHPPU). UKI submits LHPPU to the head of the work unit, namely the Director of KITSDA. UKI compiles a Quarterly Final Report for Echelon I

level based on the compilation of LHPPU of head office work units/Echelon II units of the head office.

Apart from LHPPU, there is also another type of report, namely the Immediate Finding Report (LTS). LTS is a report that needs to be followed up immediately because the main controls are often not implemented properly, thus having a huge impact on strategies/operational activities and/or on the interests of the stakeholders. UKI submits the LTS to the Director of KITSDA to be forwarded to the Director General of Taxes and/or other related parties that are capable of taking corrective actions. In this case, UKI has played a role in supporting the effectiveness of internal control under the 17th principle. This is shown by the implementation of monitoring in the form of PPU, EPITE, EKR by UKI which produces recommendations for improving business processes when weaknesses are found in the controlling system

CONCLUSION

Based on the results of the analysis, it can be concluded that the Internal Compliance Unit has been quite competent in performing its roles in supporting the effectiveness of internal control. However, some principles of internal control have not been implemented optimally by UKI, such as the 4th principle (organization demonstrates commitment in recruiting, developing, and retaining competent individuals following the defined goals); the 11th principle (organization selects and develops general control activities over technology to support the achievement of its goals); and the 16th principle (organization selects, develops, and carries out ongoing and separate evaluations to ensure that internal control components are existing and functioning optimally).

UKI has not contributed optimally in supporting the effectiveness of internal control in the 4th principle, as indicated by the absence of activities carried out by UKI related to compliance testing on management policies in the field of Human Resources (HR). This may increase the possibility of errors made by the management in placing and allocating employees. It is extremely crucial to control the placement of employees, especially in DGT strategic units, and to quickly identify problematic employees indicated to have violated UKI and have not performed their

roles optimally in supporting the effectiveness of internal control under the 11th principle and the Information and Communication Technology-Based Control Monitoring (PPTIK) as outlined in the Annual Monitoring Plan (RPT). Both actions need to be taken into consideration since DGT is currently building a large system called the Core Tax Administration System or the Update for the Tax Administration Core System (PSIAP). There should be good supervision in the system to support the effectiveness of internal control in the implementation of DGT's business processes. Regarding the 16th principle of internal control, UKI only takes part in the separate monitoring process, while the continuous/ongoing one is not carried out optimally due to the absence of adequate tools. This results in the early warning system not being implemented optimally because the control only focuses on the first line.

Recommendations

Based on the results and conclusions of this study, some suggestions can be proposed as follows:

1. To optimize the role of UKI in the 4th principle, it is recommended to: (a) register UKI employees to take part in education and training program on management policies regarding recruitment, development, and placement as well as the other HR-related policies; (b) hold internal meetings to discuss compliance test plans related to management policies on HR; and (c) make a monitoring plan related to management policies on HR.
2. To optimize the role of UKI in the 11th principle, it is suggested to: (a) propose to the HR manager to place one or two employees in the IP Sub-Directorate who have a good understanding of information and communication technology, (b) provide inputs to the application development team for the Core Tax Administration System Update (PSIAP) to build an information and monitoring menu that can be used by UKI to carry out the monitoring process, (c) conduct comparative studies with other agencies/companies on how to conduct PPTIK, (d) collaborate with the Directorate of Information and Communication Technology to build tools to implement PPTIK.
3. To optimize the role of UKI in the 16th principle, it is advisable to: (a) hold internal meetings to discuss the ongoing monitoring process; (b) implement PPTIK. The 11th and 16th principles are essentially interrelated since ongoing monitoring can be carried out if UKI has implemented PPTIK. Therefore, if UKI has succeeded in implementing PPTIK an effort has been made to optimize the role of UKI in these two principles.

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