THE INDONESIA ANTI-AVOIDANCE RULES:
GAARs & SAARs

By:
Astera Primanto Bhakti
Director of Center for State Revenue Policy,
Fiscal Policy Agency, Ministry of Finance of The Republic of Indonesia

on the event of:
4th IMGF-Japan High Level Tax Conference Program
TOKYO, April 2013
1. Background of GAARs/SAARs in Indonesia
2. The Indonesian GAARs
3. The Indonesian SAARs
4. GAARs/SAARs: Some Consideration for Its Effectiveness
5. Conclusion
GAARs / SAARs in Indonesia: The Background
Indonesia’s Economic Growth: High and Stable

- Indonesia has achieved continuous high economic growth since 2000, 6.5% real GDP growth in 2011.
- Maintaining growth in line with capacity, 6.5% expected for full year 2012 and 6.8% projected for 2013.
- Consistently outpacing its most BRIC and South-East Asian peers.

**Indonesia’s GDP growth**

**Indonesia’s economic growth vs. BRIC and Southeast Asian peers**

Source: MOF, IMF, World Economic Outlook
FDI has been Growing Rapidly Across Sectors...

FDI Growth by Sectors (%YoY)

Industry and Mining Continue to be the Two Largest Invested Sectors (2011 Compared to 2012)

Source: BKPM, processed
Note: Data excludes oil & gas and banking
### Investment Growth in Indonesia

#### The Investment Realization of the year 2010-2012 (& Target for the year 2013)

<table>
<thead>
<tr>
<th>REALIZATION</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>Δ</th>
</tr>
</thead>
<tbody>
<tr>
<td>FDI</td>
<td>147.9 T</td>
<td>175.3 T</td>
<td>221.0 T</td>
<td>272.6 T</td>
<td>23.3 %</td>
</tr>
<tr>
<td>DDI</td>
<td>60.6 T</td>
<td>76.0 T</td>
<td>92.2 T</td>
<td>117.7 T</td>
<td>27.6 %</td>
</tr>
<tr>
<td>TOTAL</td>
<td>208.5 T</td>
<td>251.3 T</td>
<td>313.2 T</td>
<td>390.3 T</td>
<td>24.6 %</td>
</tr>
</tbody>
</table>

Source: The Indonesian Investment Coordinating Board

Notes:
- **2010-2012**: Investment realization
- **2013**: Investment target as Strategic Planning BKPM 2010-2014
- Δ: Investment realization target of 2013 to investment realization performance of 2012
• **2006-2012:** Tax Revenue increased by 2.5 times, from IDR 409,2 T (2006) to IDR 1,019.2 T (2012).

  Average growth is 17% annually.

• **2011–2012:** Tax revenue increased by 17.5%; Non-oil tax revenue increased by 22.2%.
During the period of 2006-2012, Non Tax Revenue increased by 6% annually.

Natural Resources, particularly the Oil and Gas, have been the primary sources of non tax revenue.
TAX AVOIDANCE/EVASION?

Legal Tax Planning

TAX AVOIDANCE

Illegal Tax Planning

LEGAL or NOT?

Based on FACT & SUBSTANCE
Which of the followings are considered as tax avoidance?

1. Company Reporting Losses / No Income in its Tax Return for several years, but the business remains exist
2. Not reporting income earned abroad (interest, dividends, and capital gains)
3. Shifting debt to high-tax jurisdiction; vise versa, shifting of profit and income into low-tax jurisdiction
4. Preference of debt to equity as financing source for its tax benefit
5. Setting up shell corporations and trusts in foreign haven countries to channel funds
GENERAL ANTI-AVOIDANCE RULES (GAARs)
GAARs IN INDONESIA

LEGAL BASES:
Indonesian Income Tax Law (IITL), (as lastly amended by Law No.36 year 2008)

a. **Substance Over Form rule**
   ie. Article 4, 23, 26 of IITL (Income Determination)

   **Definition of Income:**
   “Any increase in economics capacity received by or accrued by a taxpayer from Indonesia as well as from offshore, which may be utilized for consumption or increasing the taxpayer’s wealth, **in whatever name and form**, including .......”

   The above provisions forms the principles in determining taxable income, and it operates as one of the measures to counter tax avoidance and/or evasion.
b. Article 18(1) : Debt and Equity

⇒ Determine the Debt to Equity ratio of companies for tax calculation purposes

c. Article 18(4) : Control / Ownership

“Related Taxpayer” shall be deemed to exist in the case of:

⇒ A taxpayer who owns directly or indirectly at least 25% of equity of other Taxpayers;

A relationship between taxpayer through ownership of at least 25% of equity of two or more taxpayer, as well as relationship between two or more taxpayers concerned;

⇒ A Taxpayer who controls other Taxpayer; or two or more Taxpayers are directly or indirectly under the same control;

⇒ A family relationship either through blood or through marriage within one degree of direct or indirect lineage.

General Applicability of the provisions ⇒ GAARs
INDONESIAN GAARs on Tax Treaty

Legal Base:

a. Article 26 (1a) of Law of The Republic of Indonesia Number 36 of 2008 concerning Fourth Amendment of Law Number 7 of 1983 concerning Income Tax


DTA abuse occurs in case of:

a. transaction that has no economic substance, which is done by using the structure /scheme in such a way with a view solely to obtain tax treaty benefits.

b. transaction with a structure / scheme where legal form differs from economic substance, in such a way with a view solely to obtain tax treaty benefits

c. income recipient is not the beneficial owner
Beneficial Owner is defined as income recipient who is:

a. Not acting as Agent;

b. Not Acting as Nominee; and

c. Not a Conduit Company

In the case of misuse of DTA:

a. DTA does not apply; and
   
   Apply regular taxation rules in accordance with Indonesian Income Tax Law.

b. In the case of difference between the legal form of a structure / scheme with their economic substance (economic substance), the tax treatment will be based on their economic substance (substance over form).
SPECIFIC (TARGETED)
ANTI AVOIDANCE RULES (SAARs)
LEGAL BASES:
Indonesian Income Tax Law No.36 year 2008:

a. Article 18(2): Controlled Foreign Companies (CFC)
   ➔ Minister of Finance is authorized to determine when a dividend is
deemed to be derived by a resident Taxpayer on participation in
an offshore company other than public companies, where:
   ✓ Taxpayer owns at least 50% of the paid in capital of the
company; or
   ✓ Taxpayer together with other resident Taxpayer own at least
50% of the paid-in-capital of the company

b. Article 18(3,3a,3b,3c,3d): Related Party + SPV/SPC related
Transactions
   ➔ Transactions between related parties should be carried out in a
   “Commercially Justifiable Way” and on Arm’s Length Basis.
SAARs IN INDONESIA

18(3): Interest Stripping
- DGT is authorized to reallocate income and deductions between related parties and to characterize debt as equity, aiming to properly reflect the transaction between “independent party”
- Resale Price, Cost-Plus, or other methods

18(3a): Advance Pricing Agreement (APA)
DGT is authorized to conclude agreement with a Taxpayer and with Tax Authority from other countries on Transfer Pricing method between related Taxpayer

18 (3b): SPV/SPC Related Transaction
Taxpayer who purchases shares or assets of other entity through a special purpose company (SPC) can be deemed as the real party who conducts the transaction, provided that such taxpayer is the affiliation of the SPC and the price of the transaction is unfairly settled.
18 (3c): SPV/SPC related transaction
The sale or transfer of shares of a conduit company or SPC which is:
- established (or domiciled) in tax haven countries; or
- affiliated with company/PE established (or domiciled) in Indonesia
could be deemed as the sale or transfer of shares of an entity that is
established (or domiciled) in Indonesia or PE in Indonesia.

18 (3d): International Hiring-out of Labor
The amount of income that individual resident taxpayer has received from
an employer which is the affiliation of non residents entity may be
adjusted by tax authority, in case of the employer transfers the payment in
forms of expenses or other expenditures which is paid to his affiliation.
1. **Thin Capitalization Rule**: Currently is still under preparation.

2. **Controlled Foreign Company Rule**:
   a. [Minister of Finance (MOF) Regulation No. 256/PMK.03/2008] concerning the Determination of when dividend is accrued by a resident Taxpayer on participation in an offshore company other than public companies.
   b. [DGT Regulation no PER - 59/PJ/2010]
      Dividend is deemed to be derived in the:
      - 4th month following the deadline for filling the tax return in the offshore country; or
      - 7th month after the offshore company’s tax year ends (in case the country does not have a specific tax filling deadline)
3. **Related Party/Transfer Pricing Rules**:

   a. **[DGT Regulation no PER 43/2010 as amended by PER-32/2011]**
      
      Application of the fairness and the prevalence principles for transactions with related party
      ✓ “Commercially Justifiable Way” and on Arm’s Length Basis.

   b. **[DGT Regulation no 69/PJ/2010 Advance Pricing Agreement]**
      ✓ Agreement between Tax Competent Authorities and Tax Payer concerning Pre-defined Transaction Price
      ✓ The agreed price shall be in effect for maximum 3 consecutive tax years commencing from the tax year the price was agreed.

   c. **[DGT Regulation no 48/PJ/2010 Mutual Agreement Procedure]**
      ✓ Optional way for taxpayer to solve problems due to misapplication of DTA clauses.
ANTI AVOIDANCE RULES: 
THE OPERATIONAL REGULATIONS

4. **SPV/SPC Related Transaction:**
   a. **MOF Regulation No. 140/PMK.03/2010** concerning Determination of Taxpayer who genuinely purchases shares or assets of other entity through a special purpose company that is a related party and the price is unfairly settled.

   [Anti Stepping Rules for Paragraph (3b) of Article 18 of IITL]

   b. **MOF Regulation No 258/PMK.03/2008** concerning Article 26 Withholding on Income from Sales or Alienation of Shares as referred to Paragraph (3c) of Article 18 of Income Tax law which is received or accrued by Non-Resident Taxpayer

5. **International Hiring Out Labor**

   **MOF Regulation No 139/PMK.03/2010** concerning Reallocation of the amount of income that individual resident taxpayer has received from an employer which is the affiliation of non-residents entity

   [rule for Paragraph (3d) Article 18 of IITL]
GAARs & SAARs: Some Considerations

Some of the issues that need to be anticipated to clear the way towards the GAARs/SAAARs implementation:

1. Taxpayer/Business refusal
   - public hearing and consultation might be a way to avoid this

2. Lower investment, particularly the inbound investment
   - require profound and comprehensive analysis

3. Politics and others

4. Court Decision
   - Indonesia: Court makes references to the existing laws and regulations
ANTI AVOIDANCE RULE: STRIKING THE BALANCE

Return

Risks

Prudence
Administration
Enforcement and Compliance

RISK

RETURN

Investment Economic Growth

International Obligation Domestic Needs

POLITICS
Conclusion

1. The fast development in business sophistication has resulted in enhanced complexity of transactions. The tax planning involving the complex transactions may entangle tax avoidance scheme.

2. The existence of anti avoidance rule is important as a mean to obtain proper base for the implementation of domestic tax regulation.
   - The Indonesian GAARs/SAARs were introduced as part of the measures to prevent and counter abusive tax planning (tax avoidance/evasion) from taxpayer.
   - Overall, the Indonesia Anti Avoidance Rule applies the **Substance Over Form** approach in line with International standard/approach.
   - When deciding on cases, court refers to the laws and regulations in Indonesia

3. In order to have an optimal result, the formulation of anti avoidance rules should consider all relevant aspects/factors for both Government and Taxpayers sides, ie : Risk vs Return ; Prudence vs Flexibility
THANK YOU