



# **THE INDONESIA ANTI-AVOIDANCE RULES: GAARs & SAARs**

By:

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# OUTLINE

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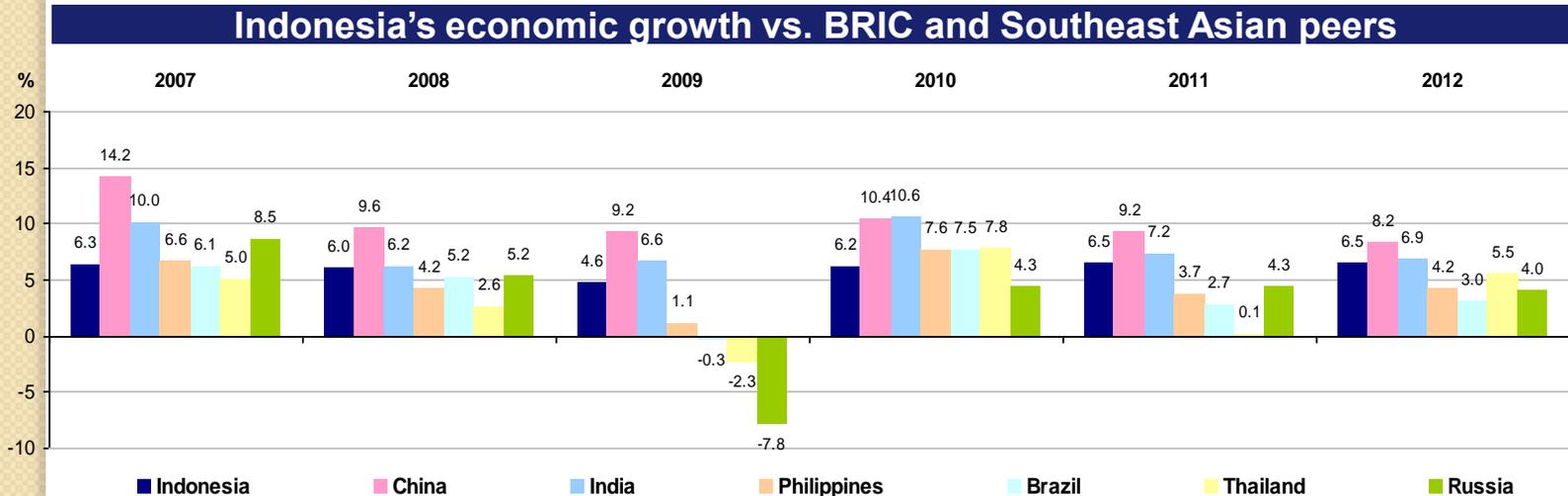
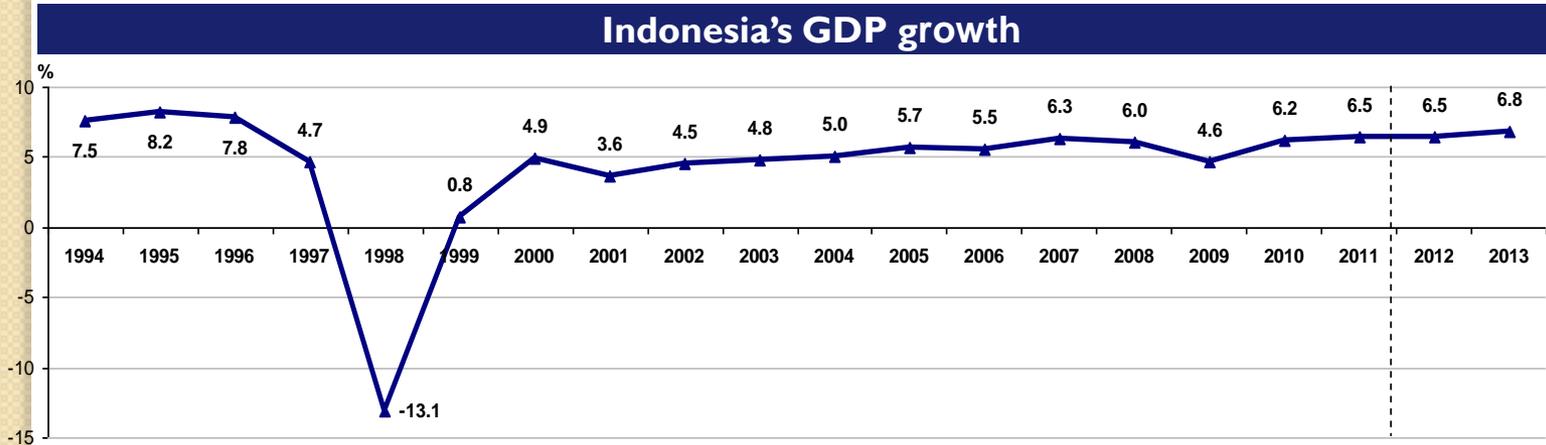
# **GAARs / SAARs in Indonesia : The Background**



# 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.



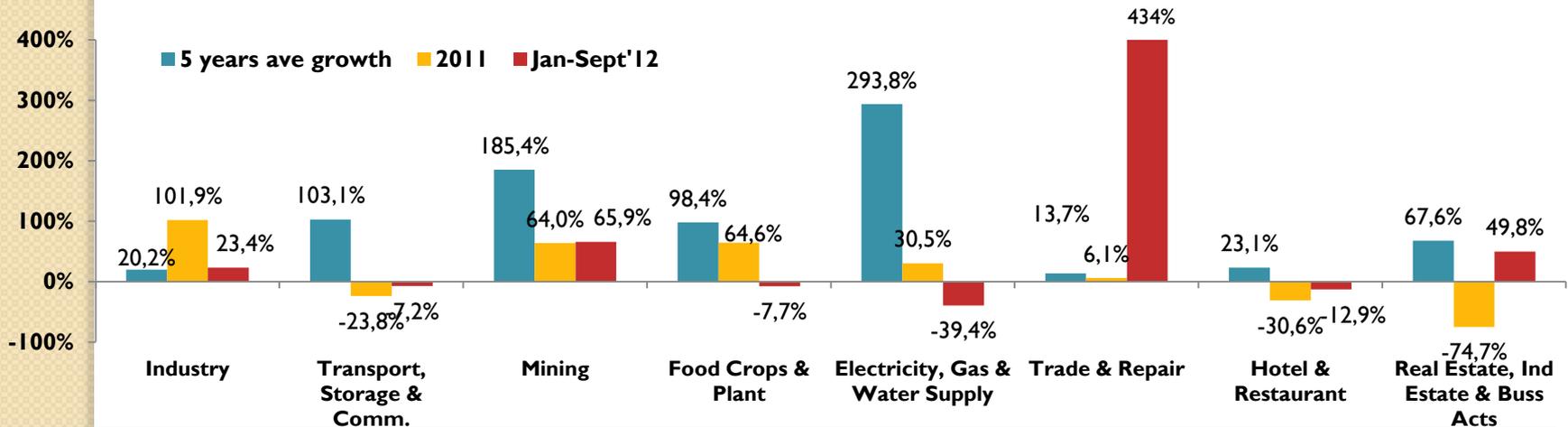
Source: MOF, IMF, World Economic Outlook



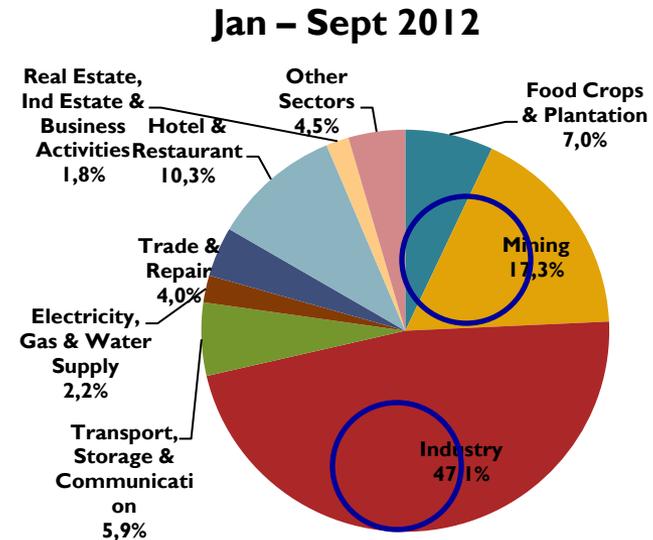
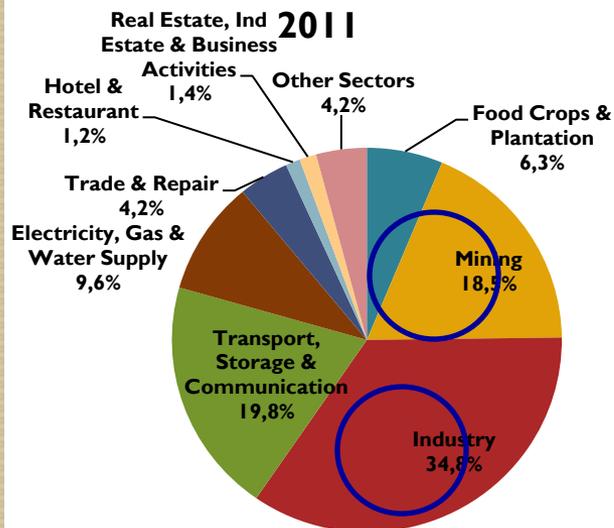
# FDI has been Growing Rapidly Across Sectors...



## 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)

REALIZATION	2010	2011	2012	2013	$\Delta$
FDI	147.9 T	175.3 T	221.0 T	272.6 T	23.3 %
DDI	60.6 T	76.0 T	92.2 T	117.7 T	27.6 %
TOTAL	208.5 T	251.3 T	313.2 T	390.3 T	24.6 %

Source: The Indonesian Investment Coordinating Board

Notes:

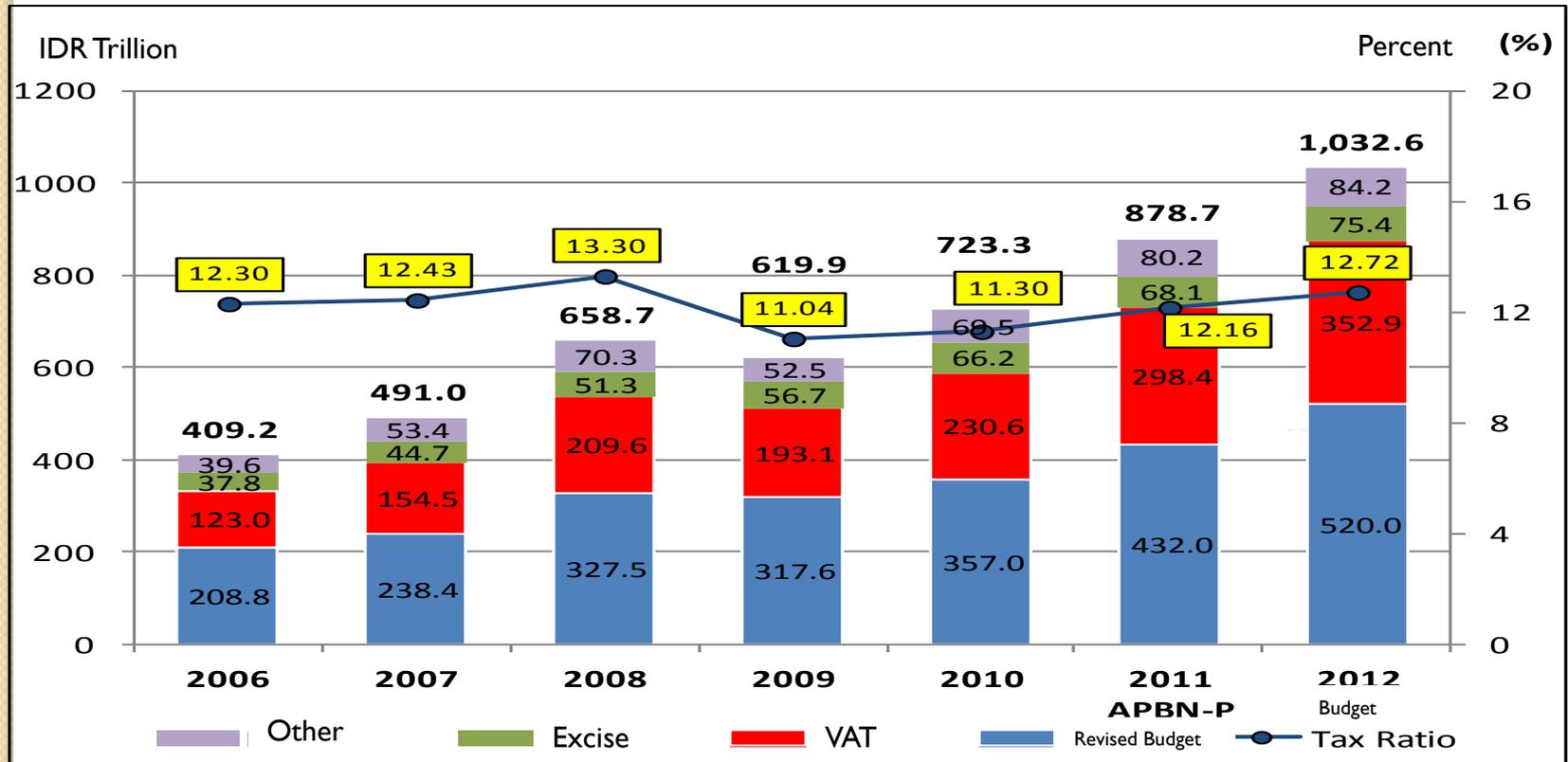
2010-2012: Investment realization

2013: Investment target as Strategic Planning BKPM 2010-2014

$\Delta$  : Investment realization target of 2013 to investment realization performance of 2012



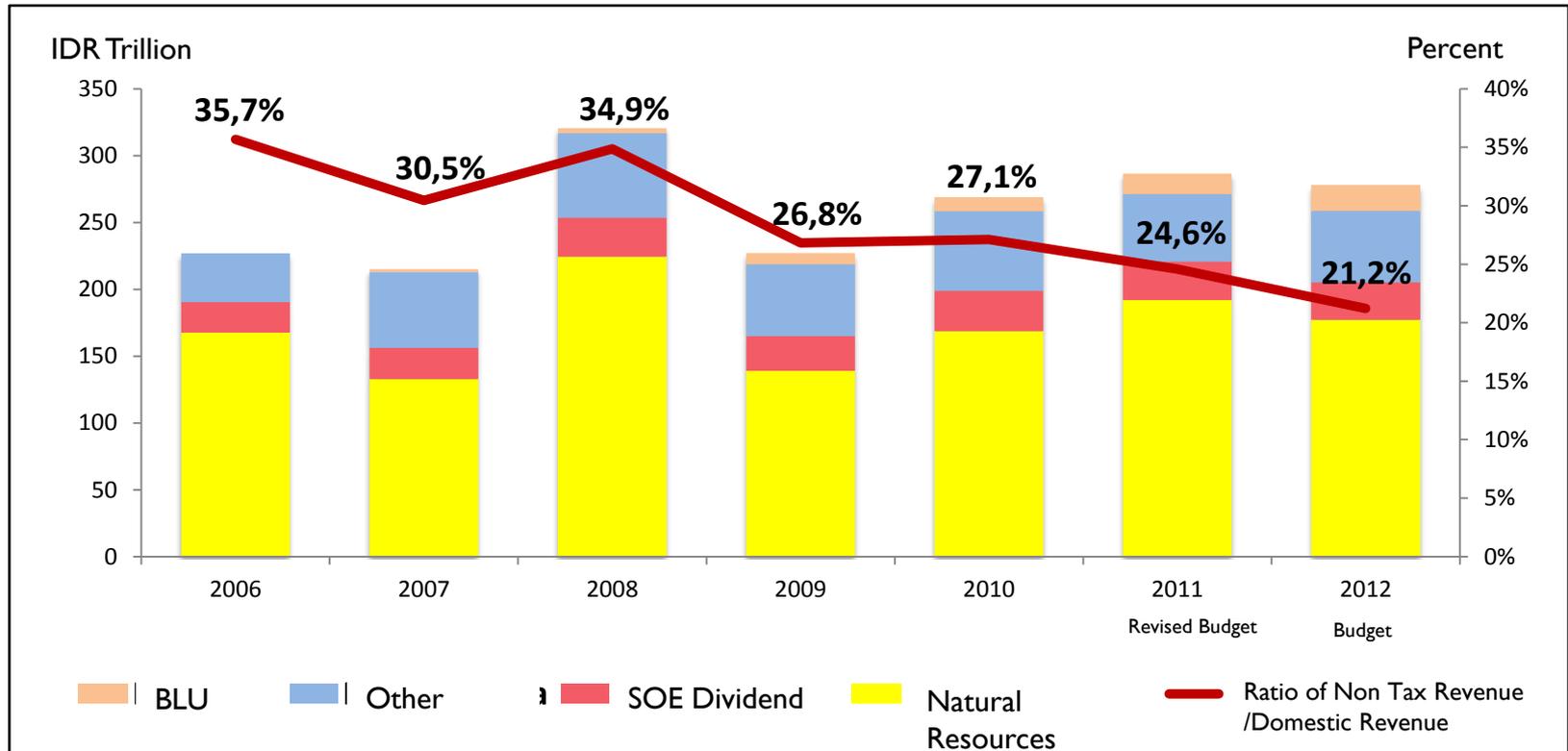
# Tax Revenue Growth (2006 - 2012)



- 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%.



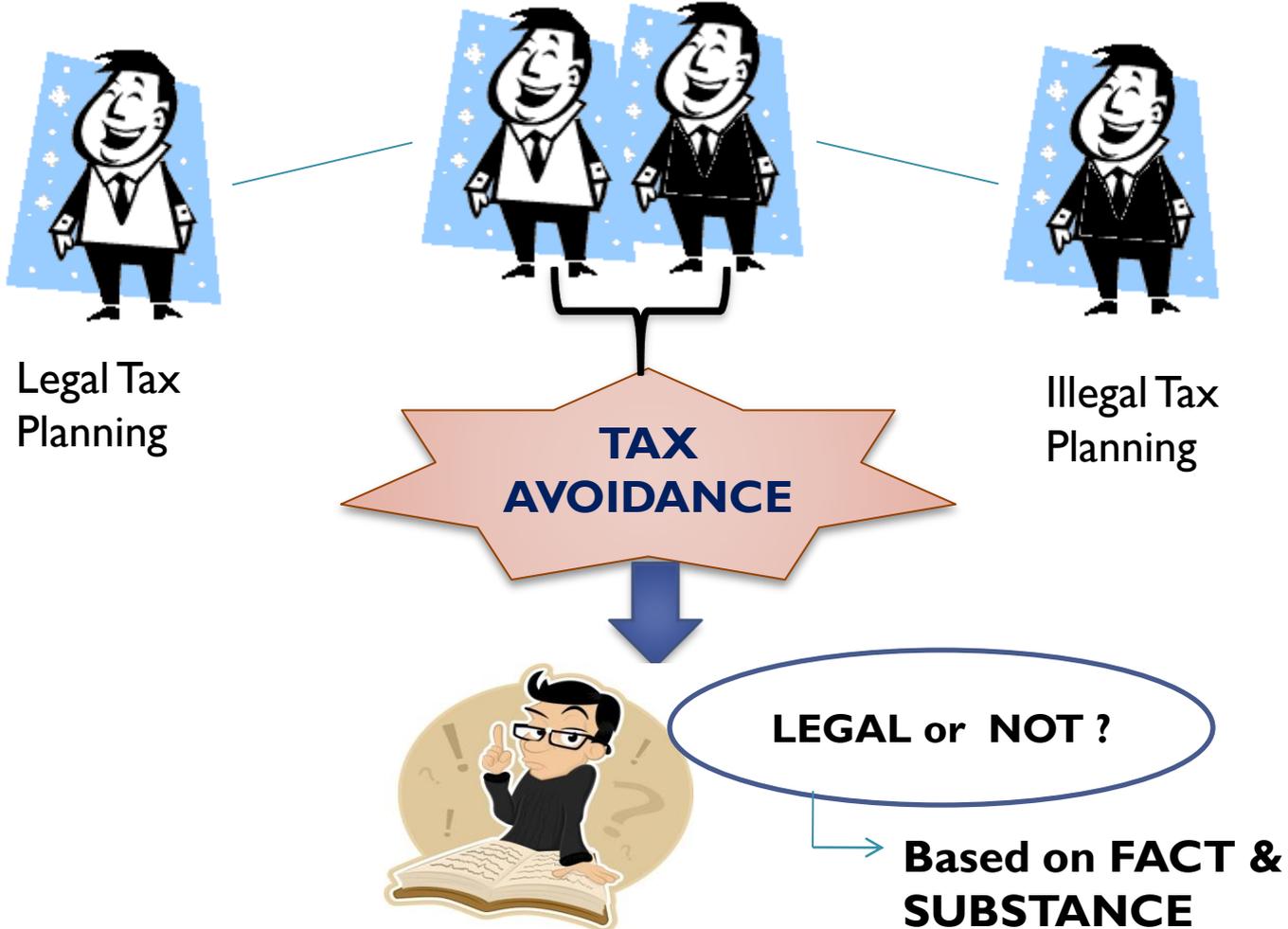
# Non Tax Revenue (2006 - 2012)



- 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 ?





# TAX AVOIDANCE : Some Stylist Facts



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.



# GAARs IN INDONESIA



## 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
- b. DGT Regulation no. 62/PJ./2009 as amended by no 25/PJ./2010 concerning The Prevention of Misuse of Double Taxation Avoidance (DTA) Agreement

## 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



# INDONESIAN GAARs on Tax Treaty



**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)**



# SAARs IN INDONESIA



## 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.



# SAARs IN INDONESIA



## → 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.



# ANTI AVOIDANCE RULES: THE OPERATIONAL REGULATIONS



## 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 :

- ✓ 4<sup>th</sup> month following the deadline for filling the tax return in the offshore country; or
- ✓ 7<sup>th</sup> month after the offshore company's tax year ends (in case the country does not have a specific tax filling deadline)



# ANTI AVOIDANCE RULES: THE OPERATIONAL REGULATIONS



## 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



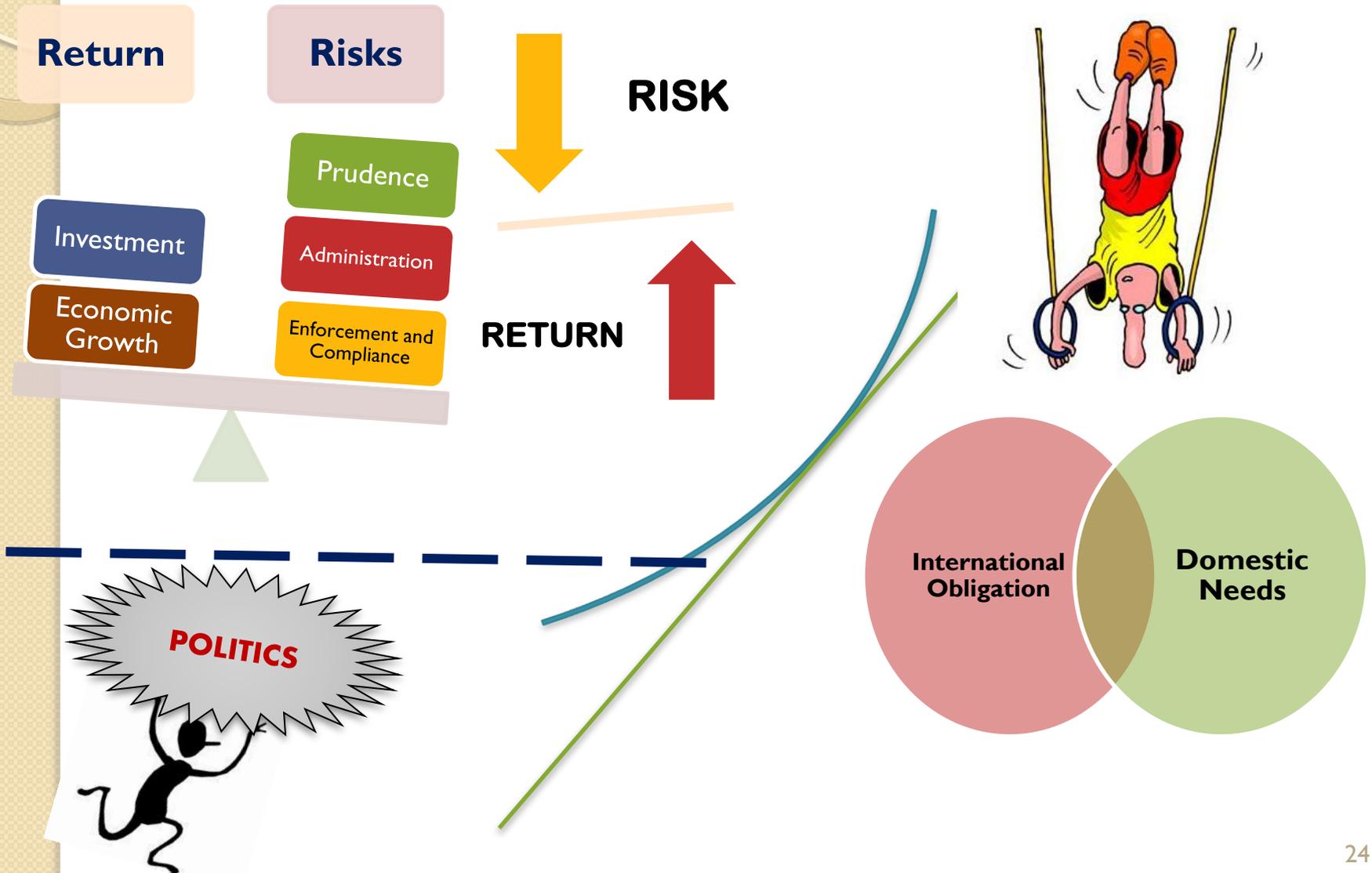
Some of the issues that need to be anticipated to clear the way towards the GAARs/SAARs implementation:

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





# 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**