Mazars Indonesia

Omnibus Law – Tax Breakthrough

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What is new?

The Indonesia's People's Representative Council passed the Omnibus bill into Law No. 11 Year 2020 ("Omnibus Law" or the "Law") concerning Job Creation on 5 October 2020 with enactment on 2 November 2020.

The Law is intended to attract investment and stimulate the economy by improving the ease and legal certainty of doing business in Indonesia including empowerment of cooperatives, SMEs as well as industries and national trades, thereby increasing job opportunities.

The tax breakthrough under the Omnibus Law is income tax law, value added tax law and general tax provisions and procedures ("KUP") law.

Some tax measures that were initially part of the Omnibus bill have already been addressed in Government Regulation in lieu of Law (Perppu) No. 1 Year 2020 which has been turned into Law No. 2 Year 2020 concerning the reduction of corporate income tax rate and taxation on e-commerce.

Taking into account the significant amendments on the tax laws, taxpayer is expected to address the impact against its business structure and revisit its tax treatment on transactions as to better utilize the changes.

Key highlights of Omnibus Tax Law

The tax reform under the Omnibus Law is outlined below.

Income tax law

- **Territorial tax system** – foreigners who are Indonesian tax residents will be taxed on Indonesia-source income including the income received outside Indonesia with regards to the activities conducted in Indonesia, to the extent one possesses certain skills[1]. The territorial basis is applicable for the first 4 (four) years upon being Indonesian tax resident. Nonetheless, the local regulation does not apply in the event of tax treaty relief claim. In the past, foreigners being Indonesian tax resident were taxed on worldwide income.
- **Indonesian citizen as foreign tax resident** – Indonesian citizen who resides outside Indonesia for more than 183 days within twelve months can be considered as foreign tax resident based on: permanent home, center of vital interest, habitual abode, tax resident status and/or other criteria which will be further determined by the Minister of Finance. In the past, Indonesian citizen was treated as foreign tax resident on the availability to present a valid identity being citizen of a jurisdiction, in addition to the 183 days threshold.
- **Dividend, net profit after tax of PE and other foreign-source earnings are income tax exempted**
  - **Local-source dividend** – is tax exempted in the hands of local individual tax resident and local entity, however restriction applies to individuals which dividend needs to be invested in Indonesia for a certain period. In the past, local-source dividend is subject to 10% withholding

[1] Definition of certain skills will be further regulated

tax (WHT) final for local individual and corporate income tax (CIT) for local entity, with income tax exemption for entity which holds at least 25% shares on its subsidiary and the dividend is taken from the retained earnings.

- **Foreign-source dividend and net profit after tax of PE** – derived from listed and non-listed entities including net profit after tax of a permanent establishment (PE), received by local individual and local entity, can enjoy income tax exemption to the extent the dividend is invested or utilized for other business in Indonesia within a certain period of time. Non-listed entities sourced dividend and PE's net profit after tax are non-taxable income by further requirements i.e., at least 30% of the net profit after tax is invested in Indonesia, and the investment shall take place prior to any issuance of tax assessment letter by the DGT due to CFC (controlled foreign corporation) rule. In the past, foreign source dividend and income were subject to individual income tax or corporate income tax with no exemption.
- **Foreign-source income** – incurred not under a PE which is received by local individual and local entity, is tax exempted provided that the income is invested in Indonesia within a certain period of time and satisfies the nature of active income derived from overseas business activities instead of overseas subsidiary. In the past, foreign source income was subject to income tax with no exemption.

  No claims of tax withheld nor claims of tax as expense with regards to the tax-exempted earnings mentioned above. Fail to execute the above-mentioned investment to Indonesia would result in all the income are taxable in Indonesia by the year the earnings incurred, taking into account the tax withheld in source country.

- **Other non-taxable income** – surplus income distributed to member of cooperatives, deposits received, and income derived from the fund management with regards to Hajj administration; and surplus income incurred by social and religion institutions are income tax exempted. In the past, those income were taxable in the hands of recipients.
- **Reduction of withholding tax due to interest and the likes** – would be further regulated. In the past, payment of interest expense and the likes were subject to 20% WHT or reduced rate under the relevant tax treaty upon the satisfaction of local tax treaty relief requirements.

Value added tax law

- **Consignment arrangement and in-kind contribution by assets *inbreng* between VATable entrepreneurs are non-VATable transactions** – In the past, both transactions were subject to 10% VAT.
- **Coal is VATable goods** – In the past, coal prior to being processed to briquette was non-VATable goods.
- **Creditability of input VAT**
  - **Prior to being VATable entrepreneur** – input VAT including self-assessed VAT is creditable at 80% of output VAT. In the past, input VAT incurred prior to being VATable entrepreneur was not allowed to be credited against the output VAT.
  - **Pre-production stage** – input VAT, to the extent relates to the main business activities and satisfies the formality requirements of VAT invoice, are creditable. Claim of VAT refund is at

year end. In the past, only input VAT that related to capital goods was creditable and VAT overpayment was claimable on monthly basis.

- **Input VAT not claimed in VAT return and/or assessed during tax audit** – are creditable to the extent it relates to main business activities and satisfies the formality requirements of VAT invoice. In the past, such tax credits were not applicable.
- **Input VAT collected under tax assessment letter** – is creditable at the principal amount to the extent the tax assessment letter is paid and there are no legal efforts as well as satisfies the requirements for crediting the input VAT.

- **Time limits for claiming input VAT** – input VAT is creditable within three months upon its issuance to the extent it is not expensed nor capitalized. Nevertheless, input VAT not reported in VAT returns and/or found during tax audit remains creditable. In the past, the three months threshold was applicable however prior to tax audit took place.
  - **Pre-production stage** - In the event there is no delivery of goods/services within three years (can be more under particular business sectors) since the first time the input VAT was credited, the VAT overpayment balance is unable to be carried forward and any VAT already refunded to taxpayer and/or credited are to be paid back to the state treasury. In the past, the time limit was three years and extendable for another two years.
  - **VATable entrepreneur deregistration due to business dissolution, by request or ex officio deregistration** - Similar limitation of input VAT credit as that applies to pre-production stage, the balance of VAT overpayment is unable to be carried forward and any VAT already refunded to taxpayer and/or credited are to be paid back to the state treasury. There is no such provision in the past.
- **VAT invoice without tax identification number (NPWP)** - however identity number (NIK – Nomor Induk Kependudukan) for local customers or passport number for foreign customers are required. In the past, NPWP was required.

KUP law

- **Introducing the use of reference rate determined by the Minister of Finance with and without uplift factor as an interest penalty with 24 (twenty-four) months cap** - the reference rate is as determined by the Minister of Finance on monthly basis plus an uplift factor at 5%, 10% and 15% on certain conditions. In the past, a 2% fixed per month of interest rate is applicable with no time limits for particular types of penalties.
  - **No uplift** – applicable to late payment of tax assessment letter; tax installment; and tax short payment due to an extension of annual income tax return (ATR). No uplift for interest rewarded to taxpayers.
  - **A 5% uplift** – appliable to amendment of ATR and monthly tax return (MTR); late payment of MTR and ATR; and tax under payment including typo and miscomputation which is collected through tax collection notice.
  - **A 10% uplift** – applicable to voluntary disclosure of incorrect tax return during tax audit.
  - **A 15% uplift** – applicable to tax audit result; tax underpayment due to ex officio grants of tax identification number (NPWP) and/or VATable entrepreneur identity; and claw back of input

VAT already refunded or claimed with regards to the excess of three years' time limit of pre-production period.

- **Reduction on certain penalties**
  - **Fail to file tax return and voluntary disclosure of incorrect tax return during preliminary tax crime investigation** – are subject to 100% penalty of tax liability (reduced from 150% applicable in the past).
  - **Late issuance of VAT invoice and incomplete VAT invoice –** are subject to 1% penalty of transaction value (reduced from 2% applicable in the past).
  - **Output VAT which was reported in VAT return not of the month when that output VAT was issued –** is not subject to penalty. In the past, such lack of compliance was subject to 2% penalty of transaction value.
  - **Termination of tax crime investigation –** is subject to penalty at three times of tax liability (reduced from four times applicable in the past).
- **No overriding of tax penalty in the event of interest and increment penalties** – during tax audit due to VAT underpayment and defect input VAT that should not be credited, applies penalty whichever is higher. In the past, two penalties were imposed.
- **Time limitation for the issuance of tax collection notice –** applicable at five years upon tax dues. In the past, there is no time limit to issue tax collection notice.
- **Certainty on the statute of limitation –** the ATR and MTR filed become final in the case of no tax assessment letter issued within five years since the fiscal year/month ends, unless taxpayer conducts tax crime within the respective fiscal year/month. Criminal acts other than tax crime can no longer extend the statute of limitation. No tax underpayment assessment letter nor additional tax underpayment assessment letter can be issued beyond the expiration of statute of limitation. In the past, tax underpayment assessment letter and additional tax underpayment assessment letter can be issued despite the five-year statute of limitation is over in an event of tax crime or other criminal acts that could result in state loss by court's decision.
- **Tax audit for VATable entrepreneur that fails to render goods/services within the three years' time limit which input VAT already refunded or credited –** In the past, claw back was conducted under tax collection notice.
- **First time negligence as well as the increment penalty is removed –** Fail to file tax return or incorrect filing of tax return by negligence that potentially result in state loss is subject to at least one time and a maximum of two times penalty, or imprisonment for at least 3 months to a maximum of one year. In the past, first time negligence was subject to 200% increment.

Key notes

The tax breakthrough under the Omnibus Law is believed to improve the tax atmosphere in Indonesia as provides greater certainty of tax treatment and statute of limitations as well as minimizes tax leaks.

In light of income tax, the Law introduces (i) territorial tax system replaces the world wide tax regime; (ii) Indonesian citizen as foreign tax resident under certain criteria; (iii) dividend, net profit after tax of

PE and other foreign-source earnings are income tax exempted, (iv) other non-taxable income: surplus income distributed to member of cooperative, deposits received and income derived from the fund management with regards to Hajj administration, and surplus income incurred by social and religion institutions; and (v) reduction of withholding tax due to interest and the likes.

In light of VAT, the Law defines (i) consignment arrangement and in-kind contribution by assets *inbreng* between VATable entrepreneurs as non-VATable transaction, whilst coal is redefined as VATable goods; (ii) creditability of input VAT for certain conditions i.e. prior to being VATable entrepreneur, pre-production stage, input VAT not claimed in tax return and/or assessed during tax audit, and input VAT collected under tax assessment letter; (iii) time limits for claiming input VAT for pre-production phase and entities undergo business dissolution; and (iv) VAT invoice without tax identification number (NPWP).

In light of KUP, the Law introduces (i) the use of reference rate determined by the Minister of Finance with and without uplift factor as an interest penalty with 24 months cap; (ii) reduction on certain penalties; (iii) no overriding of tax penalty in the event of interest and increment penalties; (iv) time limitation for the issuance of tax collection notice; (v) certainty on the statute of limitation; (vi) tax audit for VATable entrepreneurs that fail to render goods/services within the three years' time limit which input VAT already refunded or credited; and (vii) remove the definition as well as increment penalty with regards to first time negligence.

Taking into account the significant amendments on the tax laws, taxpayer is expected to address the impact against its business structure and revisit its tax treatment on transactions as to better utilize the changes.

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The content of this newsletter is for the purpose of general guidance on matters of interest and is not meant as advice. The implementation and impact of laws/regulations can vary widely based on the specific facts involved. Readers are advised to consult their tax advisors before making any business decisions.

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