Signing of Re-Negotiated Indonesia-Singapore Tax Treaty

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On 4 February 2020, Indonesia and Singapore signed a renegotiated tax treaty that both amends and updates provisions of the original tax treaty that was signed on 8 May 1990. The revisions to the original tax treaty reflect the current international tax landscape with regard to anti-abuse, information sharing and mutual agreement procedures, and improves relief for taxation of intangibles and some capital gains.

WHEN ARE THE CHANGES EFFECTIVE?

The re-negotiated tax treaty ("the Tax Treaty") is not yet effective.

The Tax Treaty will enter into force after Indonesia and Singapore have each ratified the re-negotiated tax treaty and notified each other that they have completed their ratification procedures. Once the Tax Treaty enters into the force, then it shall be effective as follows (per Article 29 of the Tax Treaty):

For Indonesia:

a. In respect of taxes withheld at source: 1 January of the following year;

b. In respect of other taxes: for any tax year commencing on or after 1 January of the following year; and

c. In respect of Article 26 (Exchange of Information): immediately apply.

For Singapore:

a. With regard to taxes withheld at source: 1 January of the following year;

b. With regard to taxes chargeable (other than taxes withheld at source): 1 January of the second calendar year following the year the Tax Treaty enters into force; and

c. In respect of Article 26 (Exchange of Information): immediately apply.

Therefore, for Indonesia, the changes for taxes will be effective from 1 January 2021 provided the Tax Treaty enters into force by 31 December 2020.

WHAT ARE THE MAJOR CHANGES?

There are no changes to the rates of withholding tax applicable to payments of interest and dividends. These remain:

Interest	10%
Dividends (corporate shareholder owning at least 25% of the share capital)	10%
Dividends (all other cases)	15%

The tables below summarize some of the major amendments and updates:

Article 5: Permanent Establishment		
Clause	Existing Tax Treaty	Re-negotiated Tax Treaty
Definition of Permanent Establishment in Article 5 paragraph 2 item (h)	A building site or construction, installation or assembly project which exists for more than 183 days	A building site or construction, installation or assembly project which exists for more than 183 days. **It is understood that a time limit of 3 months shall apply to an assembly or installation project performed by a person other than the main contractor.** (This was previously in the Protocol to the existing tax treaty; now moved into the body of the tax treaty)

Article 9: Associated Enterprises		
Clause	Existing Tax Treaty	Re-negotiated Tax Treaty
Clarification regarding corresponding adjustments for transfer pricing	Not regulated	Regulated under Article 9 item 2 & 3

Article 10: Dividends		
Clause	Existing Tax Treaty	Re-negotiated Tax Treaty
Reduction to rate of with-holding tax	-	As noted above, there is no change to the general rates of withholding tax
Branch profits tax	15% (as stated in the Protocol)	10% (Article 10(6))
Tax treatment for oil and gas production sharing contract ("PSC")	A company resident in Singapore deriving income from a PSC shall not be less favorably treated compared to a company resident in another country deriving income from a similar PSC (as stated in the Protocol)	This provision is replaced by a general statement that Article 10(6) of the Tax Treaty does not over-ride any terms (re: branch profits tax) in a PSC or mining contract of work (Article 10(7))

Article 11: Interest		
Clause	Existing Tax Treaty	Re-negotiated Tax Treaty
Who is entitled to relief	The recipient who is the beneficial owner of the interest	Reference to "recipient" is removed. Relief is available to the beneficial owner of the interest, provided it is paid
Exemption from tax for interest earned by government institutions	Exemption from tax for interest earned by government institutions (Article 11(3))	The list of government institutions subject to the exemption is expanded to include special purpose investment funds and to specifically include the BPJS funds and specific investment entities owned by the Singapore Government (Article 11(4))
Exemption from taxation for government-issued bonds or debentures	Regulated under Article 11(3)	Omitted – now taxable unless otherwise exempt under Article 11(3)
Penalty charges for late payment not regarded as interest	Not regulated	The definition of interest specifically excludes penalty charges for late payment

Article 12: Royalties		
Clause	Existing Tax Treaty	Re-negotiated Tax Treaty
Who is entitled to relief	The recipient who is the beneficial owner of the interest	Reference to "recipient" is removed. Relief is available to the beneficial owner of the interest, provided it is paid
Reduction to rate of with-holding tax	15% of the gross of the amount of royalties	• 8% for the use of, or the right to use, industrial, commercial or scientific equipment, or for information concerning industrial, commercial or scientific experience • 10% for the use of or the right to use copyrights, patents, trade marks, designs, models, plans, secret formulas or processes
Taxation of alienation (sale) of IP	Specifically included as taxable, but subject to 15% rate of withholding tax	This clause is deleted. The alienation of IP is no longer classified as a royalty. Taxation will depend on other provisions in the Tax Treaty

Article 13: Capital Gains		
Clause	**Existing Tax Treaty**	**Re-negotiated Tax Treaty**
Capital Gains	Not regulated – in general most gains were taxable	• Gains from the alienation of movable property related to a PE in the other contracting state may be taxed in that other state • Exception for gains from the alienation of ships or aircraft operated in international traffic, or movable property pertaining to the operation of such ships and aircraft • Gains from selling of shares are taxable if more than 50% of the share value directly or indirectly derives from immovable property, the alienator owned at least 50% of the total issued shares, and the shares are not traded on an approved stock exchange. An exemption applies for alienation of shares in the framework of a reorganization of a company (i.e. merger, a scission or similar operation) or for gains deriving value from immovable property in which the company carries on its business • Indonesia retains the right to tax gains from the alienation of shares in a company that is an Indonesian resident and traded on the Indonesian Stock Exchange. Currently the tax rate for the sale of shares in a company traded on the Indonesian Stock Exchange is 0.1% from the selling price • Other gains are now only taxable in the contracting state where the alienator is a resident

Article 13 (old)/14 (new): Independent Professional Services		
Clause	**Existing Tax Treaty**	**Re-negotiated Tax Treaty**
Criteria to be met so that income is taxable	If the professional exceeds the stated 90 days time period	If the professional has a fixed base regularly available, or if the professional exceeds the time test (revised to become 90 or more days in any period commencing or ending in the fiscal year concerned)

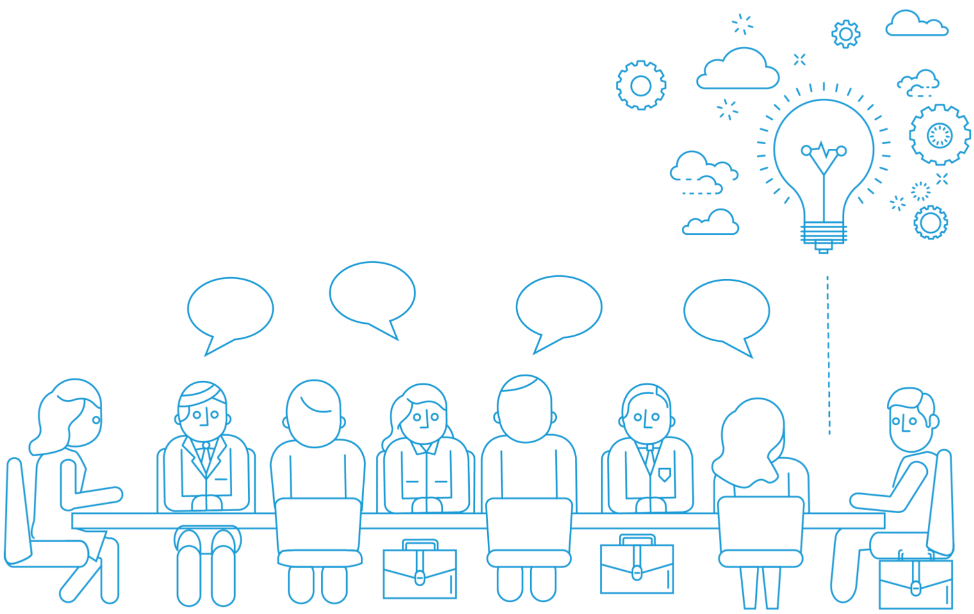
Article 14 (old)/15 (new): Dependent Personal Services		
Clause	**Existing Tax Treaty**	**Re-negotiated Tax Treaty**
Criteria to be met so that income is taxable	If the employee is present in the non-home country for more than 183 days in the calendar year	Period is no longer linked to a calendar year, but to any 12-months period Employer is not required to be tax resident in the "home" country

Article 15 (old)/16 (new): Directors Fees		
Clause	Existing Tax Treaty	Re-negotiated Tax Treaty
Right to tax	Only refers to directors' fees Income earned for managerial or technical services is subject to Article 14 (i.e. treated as employment income)	Now expanded to include "supervisory board" (i.e. commissioners) This paragraph no longer exists

Article 21 (old)/22 (new): Income Not Expressly Mentioned/Other Income		
Clause	Existing Tax Treaty	Re-negotiated Tax Treaty
Right to tax	Income not expressly mentioned in the Tax Treaty may be taxed in accordance with the laws of that country	Income not expressly mentioned in the Tax Treaty shall be taxed in the country of residence of the resident, except where the source is in the other country

Article 26: Exchange of Information		
Clause	Existing Tax Treaty	Re-negotiated Tax Treaty
Exchange of Information	In accordance with OECD Model Convention 1977	In accordance with OECD Model Convention 2017

Article 28: Anti- tax Avoidance		
Clause	Existing Tax Treaty	Re-negotiated Tax Treaty
Entitlement of Benefits	Not regulated	Regulated to emphasize the Principal Purpose Test (PPT)



IMPLICATIONS & ACTIONS:

⇒ Previously the sale by Singapore investors of shares held in Indonesian private companies were subject to 5% withholding tax based on the proceeds. In many cases, the Tax Treaty will now avoid this unless the company's value is mostly derived from immovable property. Any proposed sale or restructuring of a shareholding in an Indonesian company might benefit from delaying the execution until the Tax Treaty comes into effect.

⇒ The new protection from tax for capital gains from most share sales is similar to that provided by the Hong Kong-Indonesia Tax Treaty with the additional beneficial provision that protection is still available for the sale of shares in an immovable asset 'rich' company if the selling shareholder holds less than 50% of the issued capital. Therefore an investor from Singapore is no longer at a disadvantage to a Hong Kong investor when considering the exit taxes arising from an equity investment into an Indonesian private company.

⇒ The re-negotiated tax treaty specifically reflects certain provisions of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion & Profit Shifting ("MLI"). In particular it has adopted in the preamble that the tax treaty shall not create "opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements...)", and Article 28 includes the principle purpose test that prevents access to a tax treaty benefit if "obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Agreement."

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