

TaxFlash



Withholding Tax and Tax Treaties: Christmas comes early!

On 15 December 2009, the Director General of Taxation (DGT) issued a circular letter, SE-114/PJ/2009, providing more detailed information about how taxpayers can comply with new regulations 61 and 62 (the subject of previous PwC Tax Flashes 2009/11 and 2009/12).

Prior to the circular, there were significant concerns about how taxpayers could comply with the rules, and there were particular concerns about whether foreign tax authorities would provide a certificate of residency or domicile in the form required by the DGT.

In this issue:

- The new forms
- Refund mechanism
- Transaction between two foreign taxpayers

In very welcome news, the DGT has released new DGT 1 and DGT 2 forms and, significantly, it is now clear that foreign tax offices will only be required to provide sign-off on residency issues for the foreign taxpayer claiming treaty protection without involving the financial side of the transactions themselves. Therefore we would not anticipate major issues in getting foreign tax offices to provide the certification required. However, one concern remains: the number of forms (either DGT 1 or DGT 2) that foreign taxpayers have to provide depends on the number of Indonesian payers with whom they have transactions.

However, foreign taxpayers who are seeking to rely on treaties, will still need to provide themselves the significant financial and other information as outlined in our earlier Tax Flashes.

The other welcome news is that, in some circumstances, a certificate of residency or domicile can now be used by a taxpayer for up to a year. Previously it was feared that a new certificate may be required for each payment for which treaty relief was sought. The DGT circular explains the circumstances in which a certificate may remain valid for up to 12 months, as including where:

- The foreign taxpayer conducts transactions with the same Indonesian payer, and
- The name and address of the foreign taxpayer does not change during the entire 12 months.

The new forms

The previous forms issued in November (DGT 1 and DGT 2) have been replaced by new forms. They are almost identical and therefore taxpayers still need to exercise a due care in completing them.

Page 1 of the DGT form 1 can remain valid for up to 12 months, as noted above. It requires the taxpayer to provide details of the foreign income recipient and the Indonesian income payer, a declaration by the foreign taxpayer that the relevant information is true, and include the sign-off of foreign residency by the foreign tax authority.

Page 2 of the DGT form 1 must be completed wherever income subject to withholding tax is paid to a foreign taxpayer. Importantly, the page 2 information only needs to be signed off on by the foreign taxpayer receiving the Indonesian source income.

Foreign corporate taxpayers who are not listed are still allowed to seek the treaty relief as long as the entire requirements are fulfilled. The complete list of requirements are itemized in Article 4 of DGT's regulation No. Per - 62/PJ/2009. For such eligible corporations, they would be required to check "yes" for questions number 7, 8, 9, 10, 11 and 12 on page 2, part V of DGT form 1.

Question number 12 of page 2, part V of DGT form 1 is posed to determine if the foreign corporate taxpayer who receives the income from Indonesian payer is actually a pass through entity or serves as a conduit for other entity. The foreign corporate taxpayer claiming the treaty relief should not use more than 50% of its Indonesian source income to fulfil its obligations to other parties in form of interests, royalties, services or other payments.

The new DGT form 2 applies only to foreign banks, and income arising from share and bond trading transactions conducted through the Indonesian stock exchange. In further good news, the form can be copied and reused by different Indonesian payers, subject to ratification by the Tax Office where the Indonesian payer is registered.

Refund mechanism

The circular letter also confirms that foreign taxpayers will be allowed to claim refunds of withholding tax paid at higher rates where they can subsequently demonstrate that lower rates of tax under tax treaty provisions should have applied. Until the new regulation for refund mechanism in connection with these new forms is issued, we believe that the current regulations should prevail.

Transaction between two foreign taxpayers

In some situations, an Indonesian withholding tax obligation can arise in respect of transactions between two different foreign taxpayers (*e.g.*, a transfer of shares subject to the 5% transfer tax). In these cases, the DGT has confirmed that a foreign taxpayer purchaser (which may have a withholding tax liability, but subject to treaty relief) can obtain proof of tax residency of the seller by reference to a certificate of domicile issued by the seller's home tax office in its usual form (*i.e.*, the Indonesian DGT will not insist that the DGT form 1 be used).

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