

TaxFlash

In This Issue

- Protocol Amending the Indonesia-Malaysia Tax Treaty comes into force
- Can we use a Certificate of Domicile (CoD) issued by the tax authorities of a treaty partner country?
- New rules for non-residents in claiming refunds for withholding tax
- Redetermination of Expatriates Income



Protocol Amending the Indonesia-Malaysia Tax Treaty comes into force

The Director General of Tax (DGT) issued Circular Letter No : SE-86/PJ/2010 on 11 August 2010 announcing that the Protocol amending the Tax Treaty (and the existing protocol) between Indonesia and Malaysia (2010 Protocol) entered into force on 15 July 2010, and shall have effect for amounts paid or credited on or after 1 September 2010.

Key changes under the 2010 Protocol are:

- The maximum withholding tax on interest, dividends and royalties is reduced to 10% from 15%.
- The branch profit tax (BPT) rate reduction in the DTA does not apply to any production sharing contracts in the oil and gas sector with a resident of Malaysia. The previous Protocol also contained a similar exception, however with the condition that if Indonesia's other tax treaties provided for a lower BPT rate, then Malaysian residents were entitled to use that lower rate.
- Labuan offshore companies are not entitled to the DTA benefits.

Malaysian companies currently investing in Indonesia through a Labuan offshore company should review their holding structure to explore if they can enjoy the amended tax treaty benefits above by transferring the residency of the holding company to another location in Malaysia.

Can we use a Certificate of Domicile (CoD) issued by the tax authorities of a treaty partner country?

In our Tax Flash No. 5/2010 we mentioned that to claim tax treaty benefits the DGT will now allow foreign taxpayers to use a CoD form issued by Indonesia's tax treaty partner countries if the following conditions are met:

- The CoD is written in English;
- The CoD is issued on or after 1 January 2010;
- It is an original CoD or a photocopy authorised by the Tax Service Office in which the withholding tax agent is registered;
- The CoD clearly identifies the foreign taxpayer; and
- The CoD bears the name and signature of an authorised officer of the tax treaty partner's tax office.

Our recent experience shows that in practice this is not an automatic option. The DGT has indicated that where it has previously received a CoD issued by the tax authority of a particular treaty partner country in the Indonesian format (i.e. possibly from another taxpayer), it will not accept a CoD in that country's format. Accordingly, the CoD in the form of the treaty partner country will only be accepted if the tax authority of a treaty partner country refuses to certify the Indonesian Form DGT-1 for all of its taxpayers.



New rules for non-residents in claiming refunds for withholding tax

Since November 2009, the DGT has issued a number of regulations specifically related to combating tax treaty abuse. The DGT has now clarified the mechanism for foreign taxpayers to claim tax refunds, in DGT regulation No. 40/PJ/2010 dated 9 August 2010.

Foreign taxpayers may request a tax refund if there is an error in withholding or collecting tax which caused a greater amount of tax being withheld than was due, incorrect withholding on non tax objects, or the incorrect application of a tax treaty.

Foreign taxpayers that have a Permanent Establishment in Indonesia are not eligible to claim tax refund. For eligible taxpayers, the request must be made by the withholding agent under a power attorney from the foreign taxpayer.

A specific form must be used for the refund request (Form DGT-3) and the power of attorney in favor of the withholding agent should also use a form prescribed by the DGT (Form DGT-4).

Form DGT -3 should be supported by the following documents:

- CoD using Form DGT-5
- Original withholding tax slip
- Statement letter from the foreign taxpayer stating that the tax has not been credited and/or expensed by the foreign taxpayer.
- Documents related to the type of income to evidence the amount (e.g. for interest: loan agreement, accounting records for the income, bank statements).
- Other documents specific to the type of income or the amount of withholding (e.g. for the beneficial owner pursuant to a tax treaty) may also be required.

Instead of using Form DGT-1 or Form DGT-2, in claiming the tax refund, foreign taxpayers should use Form DGT-5. The Form DGT-5 must, among other things be certified by the tax office of the tax treaty partner country, or it may be replaced by a CoD in a form commonly authorised and issued by the tax treaty partner country, if that authority will not certify form DGT-5.

A refund request must be decided by the DGT within three months of receiving request letter.

Redetermination of Expatriates' Income

On 11 August 2010 the Minister of Finance (MoF) issued Regulation No. 139/PMK.03/2010 regarding redetermination of income received by an Indonesian tax resident individual from a local employer who has a 'special relationship' with a foreign company.

Under this regulation, should an expatriate employee receive income from a local employer, and the local employer reallocates part or all of the expatriate's income in the form of a payment (e.g. management fee, technical fee, or other service fees) to a related foreign company (of which the expatriate is also an employee), the DGT may redetermine/assess the off-shore payment as being the expatriate's Indonesian employment income. The Indonesian income of the expatriate will be regarded as the sum of the amount received locally and the amount paid as fees to the foreign company.

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