

# TaxFlash



## *New Controlled Foreign Company Rules*

The Ministry of Finance (MoF) has updated the Controlled Foreign Company (CFC) rules through the issuance of Regulation No.PMK-107/PMK.03/2017 (PMK-107) which is dated and effective 27 July 2017, and applicable starting fiscal year 2017. This regulation revokes PMK-256/PMK.03/2008 and also parts of KMK-164/KMK.03/2002 regarding Foreign Tax Credits (FTCs) which deals with the FTC calculation for dividends paid by a foreign CFC.

The updated CFC rules reflect some of the recommendations arising from the OECD/G20 Base Erosion Profit Shifting Action Plan No.3. The key changes are set out below.

### *Scope*

As in the previous regulations, the scope is limited to CFCs which are not listed on a stock exchange.

PMK-107 has expanded the scope of a CFC to include the following foreign companies:

1. *Directly owned CFCs* – being a foreign entity:
  - a) at least 50% owned by an Indonesian taxpayer; or
  - b) at least 50% collectively owned by Indonesian taxpayers
2. *Indirectly owned CFCs (new)* – being a foreign entity with a minimum ownership of 50% by another CFC, or collectively by Indonesian taxpayers CFCs, or collectively by a number of CFCs (including under the same or different Indonesian parent company).

The ownership threshold used to determine the CFC status is the ownership percentage at the end of the fiscal year of the Indonesian taxpayer, and is based on either percentage of paid up capital or paid up capital with voting rights.

For indirectly owned CFCs, the 50% threshold is determined based on the ownership of the indirectly owned CFC (not proportionally). For example, if Y Ltd is 60% owned by X Ltd which is 60% owned by PT A, Y Ltd is considered as being an indirectly owned CFC of PT A even though the effective ownership of PT A in Y Ltd is less than 50%, i.e. 36% (60% x 60%). This is because the ownership at Y Ltd level is more than 50%, i.e. 60% owned by X Ltd.

### **Transparent entities**

Ownership through trusts or similar arrangements is deemed as a “pass-through” and will be considered as ownership by the investor(s) in the trust or the similar entity.

### **Timing**

As with the previous regulation, the Indonesian taxpayer must recognise a deemed dividend from any CFC by the end of the fourth month after the deadline to submit the CFCs Corporate Income Tax Return (CITR), or the seventh month after the end of the fiscal year of the CFC if there is no CITR submission obligation.

### **Deemed Dividends calculation**

As with the previous regulation, the deemed dividend is calculated based on the effective ownership in the CFC multiplied by the commercial profit after tax. For example, the deemed dividend from Y Ltd at PT A level in the above example would be 36% of the commercial profit after tax of Y Ltd.

As a new provision to take note of, if an actual dividend is paid by the CFC, this amount can be offset (non-taxable) against previously reported deemed dividends but only if within the past five consecutive years. For example, a deemed dividend can offset an actual dividend paid in 2021 if the deemed dividend was reported any time between 2017 and 2021. If the actual dividends are higher than the deemed dividends within that period, the difference must be reported in the Indonesian taxpayer's CITR.

### **Foreign Tax Credits**

Taxes paid on the actual dividends can be credited in the Indonesian taxpayer's CITR in the year when the tax is paid or withheld, subject to limitations.

The allowable FTC amount limited by the lower of:

- a) the foreign income tax that should have been due under terms of an applicable tax treaty; *(new)*
- b) the foreign income tax actually paid or payable; or
- c) the limit calculated based on the proportion of the deemed dividend from the total taxable income (including the deemed dividend) multiplied by the total tax due in the CITR.

If actual dividends are paid from more than one country the allowable FTC calculation is based on per country limitation.

PMK-107 provides a prescribed format for the FTC calculation to be attached to the CITR. This document must be attached with the following documents of the directly owned CFC:

- a) financial statements;
- b) a copy of the CITR (if any obligation);
- c) a calculation or list of profits after tax for the past five years; and
- d) a tax payment or withholding tax slip on the actual dividend paid.

More detailed examples for the determination of CFC, deemed dividends calculation, and FTCs are available in the attachment of PMK-107.

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