

IN THIS ISSUE:

▪ Locking the door on tax audits

Filing a qualifying AITR may enable you to lock the door on a tax audit. It is not a guarantee that the DGT will not reopen your books; however it may help you sleep better at night.

▪ Final income tax regime is back

Construction service businesses may need to revisit their books given that the final income tax regime for 2008 contracts applies retroactively from 1 January 2008. The same regime will be applicable for all types of land and building right transfers starting from 1 January 2009.

Locking the door on tax audits

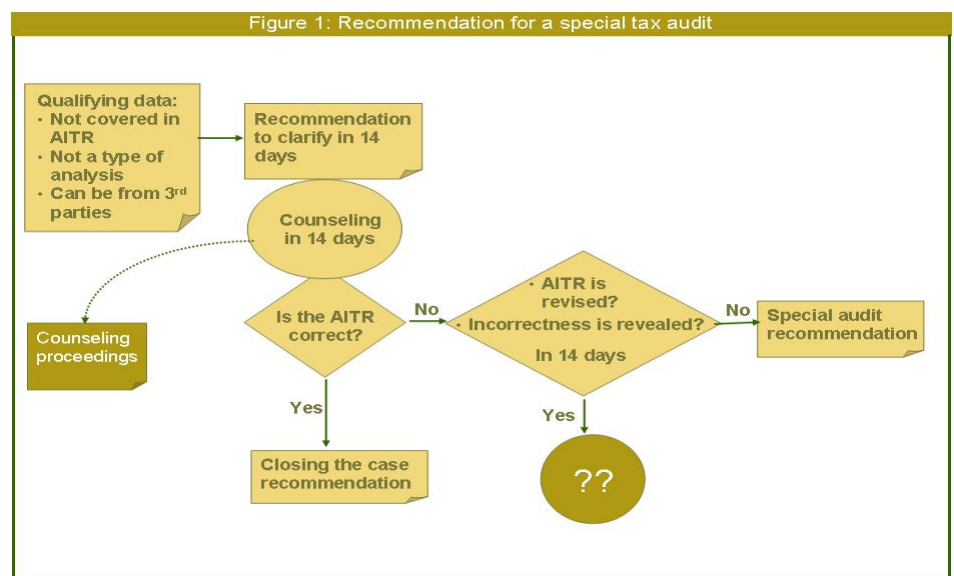
The Sunset Policy is good news for businesses and individuals. It is a one-off opportunity to escape interest on underpaid tax due under an annual income tax return (AITR) filed under the scheme. The Director General of Tax (DGT) has also pledged that it will not audit qualifying AITRs (unless they are found to be incorrect for some reason). Nor will the DGT use the data therein as a basis to issue assessments of any other taxes. Even an on-going tax audit for a particular year may be stopped by filing a qualifying AITR for that year.

Some people have worried that the policy may be too good to be true. There are particular concerns about the condition that must be met for the DGT to forgo tax audits ie, that the AITR must be correct. There are concerns that a simple mistake, which does not necessarily affect the tax calculation, could still mean a qualifying AITR is incorrect, and thereby trigger a tax audit.

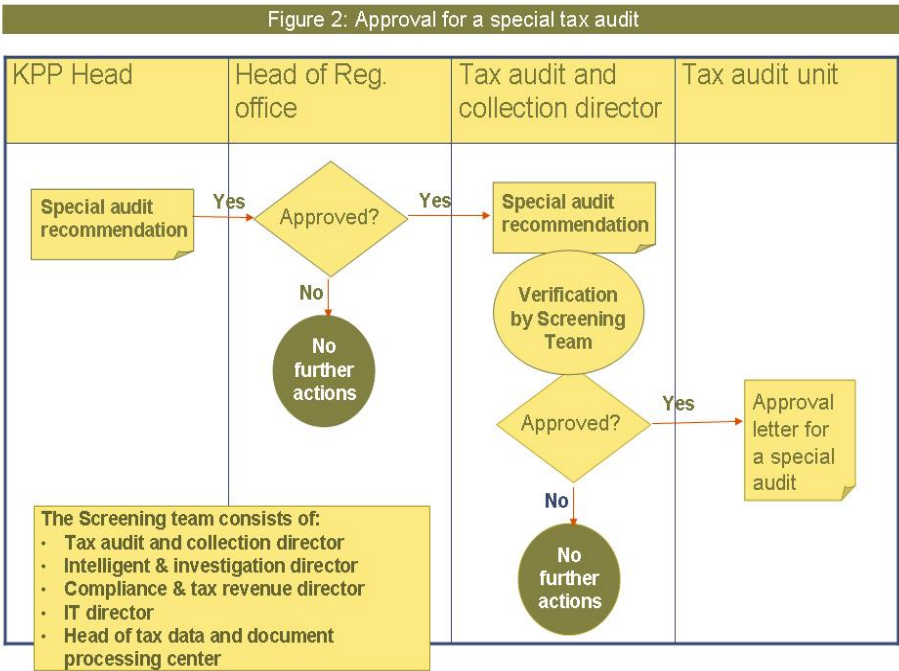
Robust decision process

In response to these concerns, the DGT issued SE-67/PJ/2008 (SE 67) on 2 December 2008 to clarify its stance on whether or not use of the Sunset Policy will provide tax audit protection. The DGT says a special audit on a qualifying AITR may only be performed after a robust decision making process involving senior officers of the DGT office.

Only data or information not covered in a qualifying AITR can be used as a starting point to pursue the need for a special tax audit (Refer to Figure 1). This must be stand-alone data or information which could be obtained from third parties such as a counter party in a transaction, government agencies, banks, or even disappointed employees.



The DGT office will then assess the quality of that data before it requests the taxpayer concerned to clarify it with a designated DGT official, within 14 days. A *counselling session* will be conducted between the taxpayer and the DGT official. This aims to determine the validity of the designated data and in particular whether or not the AITR, in light of the data, remains correct. The session must occur within a maximum period of 14 days. The results will be documented in official *counselling proceedings* to be signed by both parties.



Only in situations where an AITR is found incorrect and the taxpayer does not proceed to revise it in the next 14 days, will the DGT official write a recommendation to his superior, the head of a particular tax service office (KPP), for a special tax audit. The recommendation letter will then pass from the KPP head through the head of the regional office to the director of tax audit and collection (Ref. to Figure 2).

A final decision to conduct a special audit must be approved by a screening team consisting of four directors and the head of the tax data and document processing center of the DGT office.

Not a guarantee

SE 67 should give comfort to anyone who has doubts about whether the DGT's pledge not to conduct a tax audit is genuine. This is especially true for those who genuinely seek to present the truth in their AITRs. Hence, filing a qualifying AITR may enable those people to lock the door on tax audits and sleep better at night!

Although the sunset policy does not provide a blanket guarantee that the DGT will not reopen your books, it should only be in unusual situations, where the DGT comes into possession of relevant information from other sources, that any real risk of a tax audit will arise.

There are only a couple of weeks left to tidy up your AITRs if you want to use the Sunset Policy opportunity. Enough time is left to act now, especially if you have identified areas of concern which you would seek to rectify in your revised AITRs.

Final income tax regime is back

Starting from 1 January 2009, any transfers of land and buildings (L&B) rights will be subject to final income tax. In general, the tax rate is 5% of the higher of the transaction value or the *official value of the tax object* (NJOP). A special tax rate of 1% will apply for transfers of rights of simple houses and apartments. These rules are set out in government regulation (GR) 71/2008 issued on 4 November 2008 which serves as the third amendment of GR 48/1994.

Until 31 December 2008, such transfers are still governed by GR 48/1994 as amended by GR 27/1996 and GR 79/1999. Under these regulations, the withholding tax rate is 5% across the board. Only in cases where the transferors are individual taxpayers or foundations engaged in L&B right transfer businesses will the tax withheld be treated as final income tax. For other transactions, the tax withheld is to be treated as a prepayment of corporate income tax (PPh 25) for the company transferring the L&B rights.

The final income tax regime is also re-applied to construction service businesses by virtue of GR 51/2008 issued in July 2008. A further implementing regulation, Minister of Finance (MoF) Reg. 187/PMK.03/2008 was issued in November 2008. These regulations declared that for all contracts signed in 2008 the final income tax regime would be applied retroactively from 1 January 2008.

Any construction service contracts signed before 2008 may or may not be affected by the final income tax regime depending on whether there are still payments for these contracts beyond 2008. The tax treatment for all payments up to 31 December 2008 should be governed by the non-income tax regime. For all payments after 2008, the final income tax regime will apply.

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