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Tax Alert

New Indonesia Singapore tax treaty

New double tax agreement signed by Indonesia and Singapore

On 4 February 2020, the Governments of Indonesia and Singapore signed a new double tax agreement[1] ("New DTA"), which will replace the DTA which has been in effect since 1992 ("Old DTA").

The New DTA will come into force once ratified by both countries. Most articles will then take effect and replace the existing treaty from 1 January of the year following the second country's ratification.

This Tax Alert summarises key changes under the New DTA, as compared with the existing treaty. The New DTA appears to reflect the positions taken by the countries under the OECD/G20 Multilateral Instrument ("MLI") signed in 2017, insofar as the 'matching' positions would have modified the Old DTA. Most notably, the over-arching principal purpose test ("PPT") will apply under Article 28.

However, the New DTA contains a number of other changes – many of which will be attractive to foreign investors investing in Indonesia. In particular, the improved capital gains protections for disposal of non-listed Indonesian shares by a Singapore resident. Overall, the New DTA may further strengthen the attractiveness of Singapore as a country from which to invest into Indonesia, and should be considered by any groups with, or considering, Indonesian investments.

Building a better working world

1 Agreement between the Government of the Republic of Singapore and the Government of the Republic of Indonesia for the elimination of double taxation with respect to taxes on income and the prevention of tax evasion and avoidance

New DTA (signed 2020)	Old DTA (Signed 1990)
1. Preamble The new preamble adopts the MLI text, including greater emphasis on combatting evasion and avoidance. *The Government of Republic of Singapore and the Government of the Republic of Indonesia, intending to conclude an Agreement for the elimination of double taxation with respect to taxes on income without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this Agreement for the indirect benefit of residents of third jurisdictions).* The above Preamble, and the PPT discussed below, create the potential for an interesting interaction with the question in Part V (11) of Form DGT regarding the purpose of a transaction which is to directly or indirectly obtain the benefit under the convention that is contrary to the object and purpose of the DTA.	*The Government of Republic of Indonesia and the Government of the Republic of Singapore, desiring to conclude an Agreement for the a voidance of double taxation and the prevention of fiscal evasion with respect to taxes on income.*
2. Fiscal domicile Definition of "a resident of a Contracting State" in Article 4(1) now states: *any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of incorporation, place of management or any other criterion of a similar nature, and also includes that State and any political subdivision, local authority or statutory body thereof*. The definition now excludes the exemption for permanent establishment (PE) of a foreign enterprise found in the Old DTA.	*For the purposes of this Agreement, the term "a resident of a Contracting State" means any person who is resident in a Contracting State for tax purposes of that Contracting State. This term shall not include a permanent establishment of a foreign enterprise which is treated as a resident for tax purposes - Article 4(1).*
3. Branch Profits Tax ("BPT") Reduction on branch profits tax (on the after-tax profit of a permanent establishment) to 10% - Article 10(6).	Previously 15% - Article 3 of the 1990 Protocol.
4. Most-favoured nation article on production sharing contracts ("PSC") The most favoured nation condition for Singapore resident taxpayers receiving PSC income has been removed – Article 10(7). The effect of PSC terms will remain unaltered by the DTA – e.g. the DTA cannot be used to reduce branch profits tax on a PSC permanent establishment.	*Nothing in this Article shall affect the provisions contained in any production sharing contracts relating to the exploitation and production of oil and natural gas which have been negotiated with the Government of Indonesia or the relevant state oil company of Indonesia, **provided that a company which is resident in Singapore deriving income from a production sharing contract shall not be less favourably treated with respect to tax than that levied on a company of any third state deriving income from a similar production sharing contract*** – Article 4(a) of the 1990 Protocol.

5. Dividends	
There is no change to the rate of dividend withholding tax ("WHT").	a) *10% of the gross amount of the dividends if the recipient is a company which owns directly at least 25% of the capital of the company paying the dividends;* b) *15% of the gross amount of the dividends in all other cases.*
The clause on the mode of application that should be settled by the competent authorities has been removed.	*The competent authorities of the Contracting States shall by mutual agreement settle the mode of application of these limitations.*
6. Interest	
There is no change to the rate of interest WHT.	*10% of the gross amount of interest.*
The interest WHT exemption on interest arising from Government bonds in a Contracting State and paid to resident of the other Contracting State has been removed.	Article 11(3) - *Notwithstanding the provisions of paragraph 2, interest arising in a Contracting State and paid to a resident of the other Contracting State shall be taxable only in that other State, if the interest is paid in respect of:* *(a) a bond, debenture or other similar obligation of the government of the first-mentioned State or a political subdivision or local authority thereof; or* *(b) a loan made, guaranteed or insured, or a credit extended, guaranteed or insured by the Monetary Authority of Singapore, or the "Bank Indonesia" (The Central Bank of Indonesia), or any other lending institution, as may be specified and agreed in letters exchanged between the competent authorities of the Contracting States.*
The list of government institutions exempt from interest WHT has been expanded to include sovereign wealth funds and their subsidiaries in Article 11(6), with a specific list provided.	
7. Royalties	
Reducing to 8% the Royalty WHT on payments for the use of, or the right to use, industrial, commercial or scientific equipment, or for information concerning industrial, commercial or scientific experience – Article 12(2)(b) Reducing to 10% the WHT rate on payments for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, or films or tapes used for radio or television broadcasting, any patent, trade mark, design or model, plan, secret formula or process – Article 12(2)(a)	15% withholding tax on all royalties.
The alienation of intellectual property rights is no longer regarded as a royalty.	*The provisions of paragraphs 1, 2 and 5 of this Article shall likewise apply to proceeds arising from the alienation of any copyright of scientific work any patent trade mark design or model plan or secret formula or process – Article 12(6)*

8. Capital gains	
The new Article 13 on Capital Gains will follow a standard OECD approach in respect of a) Disposals of immovable property in a jurisdiction being taxable in that jurisdiction b) Disposals of assets related to a permanent establishment or fixed place of independent services being taxable in that jurisdiction c) Disposal of ships or aircraft operated in international traffic, or movable property pertaining to the operation of such ships or aircraft shall be taxable only in the residency jurisdiction For disposal of shares, the New DTA will exempt gains on the sale of shares by reserving the taxing rights to the jurisdiction where the alienator is a resident and not the country of source under Article 13(6), except:	There is no Capital Gains Article in the Old DTA.
a) Listed entity carve-out under Paragraph (5) - Alienation of shares in a listed Indonesian company traded on the Indonesian Stock Exchange (“IDX”) where Indonesia retains the taxing rights; and b) Land-rich carve-out under Paragraph (4) - Alienation of shares in a company situated in the Other Contracting State deriving more than 50% of its value directly or indirectly from immovable property **AND ONLY IF** the alienator owned at least 50% of the total issued shares of such a company – in which case the Other Contracting State where the company is situated retains the taxing rights. However, this paragraph (4) does **NOT** apply to alienation of shares in such a company if: - that company carries on its business in the immovable property; or - the alienation of shares is done within the framework of a reorganization of a company, a merger, a scission or a similar operation.	There was previously some uncertainty as to the interaction of the capital gains regime for the disposal of Indonesian listed shares, which is resolved by the New DTA. Such transactions are typically taxed at a deemed rate of 0.1% of transaction value when crossed on the IDX. Given there was no previous capital gains protection, the disposal of non-listed Indonesian shares in the past was subject to Indonesian taxation on a deemed basis at 5% of the transaction value. The New DTA should provide shelter from this taxation for non-listed, non-land rich shares and for non-controlling (less than 50%) stakes in land rich companies. The interpretation of the exceptions for immovable property “in which the company carries on business” will require close analysis in each case.
9. Exchange of information	
Exchange of Information (“EoI”) under Article 26 now follows the OECD Model Tax Convention version 2017. This provides for more extensive coverage on all taxes and not just those covered by the DTA. Also, it does not permit a Contracting State to decline to supply information solely because the information is held by a bank, other financial institution, nominee or person acting in an agency or a fiduciary capacity or because it relates to ownership interests in a person.	The Old DTA follows the previous OECD Model 1977.

10. Entitlement to benefits - anti-tax avoidance	
Adoption of the Principal Purpose Test pursuant to the OECD/G20 BEPS process. *A benefit under the DTA shall not be granted in respect of an item of income if it is reasonable to conclude, having regard to all relevant facts and circumstances, that 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 the DTA* - Article 28.	No previous equivalent. However, similar concepts have been implemented via regulations to interpret the treaty abuse and 'beneficial owner' concepts in Indonesia. Article 22 of the Old DTA only imposed a limitation of relief, which required income from the country of source to be remitted into, or received in, the country of residence for the tax treaty to apply.

Our Values

Who we are:

At EY, everything starts with our people:

- People who demonstrate integrity, respect and teaming.
- People with energy, enthusiasm and the courage to lead.
- People who build relationships based on doing the right thing.

What we stand for:

Achieving Potential - Making A Difference

We are committed to helping our people, our clients and our wider communities achieve their potential.

Sectors we serve in Indonesia

- Banking & capital markets
- Asset management
- Insurance
- Power & utilities
- Mining & metal
- Oil & gas
- Media & entertainment
- Telecommunications
- Technology
- Public infrastructure
- Transportation
- Real estate
- Consumer products
- Pharmaceuticals
- Plantation
- Industrial & manufacturing
- Automotive
- Government & public sector
- Not-for-profit organizations

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