

Update on Tax Allowance Incentive

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On 13 November 2019, the Indonesian Government issued Government Regulation No 78/ 2019 ("GR-78"). GR-78 replaces GR No 18/2015 ("GR-18"), which was amended by GR No 9/2016 ("GR-9").

GR-78 provides an income tax incentive for capital investment in certain business sectors and/or in certain regions ("Tax Allowance Incentive"). The regulation states the purpose is to drive and encourage direct foreign investment activities, both for economic and business sector development as well as to provide legal certainty of a more conducive business environment, in priority sectors and/ or regions.

As under previous versions of this regulation, the incentives are available for particular sectors nationwide, while others are available for particular sectors only in certain geographic regions (typically in less economically developed regions). Under GR-78, most sectors previously eligible only in certain regions are now eligible for incentives in all parts of Indonesia - there are now only 17 sectors remaining on the list for specific regions.

This regulation also introduces the OSS system as the medium for applications for the Tax Allowance Incentive.

GR-78 will be effective on 12 December 2019.

A. Important definitions under GR-78

Important definitions under GR-78 are as follows:

1. Capital Investment is defined as any form of capital investment activities, both by local and foreign investors to conduct business in Indonesia.
2. Certain Business Sector is defined as economic business sectors that have been given high priority on the national scale.
3. Certain Business Sector and in Certain Region is defined as economic business sectors and in certain regions that have sufficient economic potential to be developed, which have been given high priority on the national scale.
4. Online Single Submission (OSS) is defined as business licensing issued by OSS Institution for and on behalf of ministers, head of institutions, governors, or mayors to businessmen through an integrated electronic system.
5. Main Business Activity is defined as business sector and production type/ service at the time a taxpayer files an application for Tax Allowance Incentive, as stated in its principle license, investment license, capital investment registration issued by the Capital Coordination Board ("BKPM")/ Provincial Capital Investment Agency and One-Stop Integrated Service/ District or City Capital Investment Agency and One-Stop Integrated Service; or business license issued by the OSS Institution for the taxpayer.

B. Eligible taxpayer

Eligible taxpayer that can obtain Tax Allowance Incentive is as follows:

1. Domestic corporate taxpayer that conducts Capital Investment in Main Business Activity, both for new Capital Investment and expansion on the existing business in Certain Business Sector and/ or in Certain Business Sector and in Certain Region as well as meeting certain criteria and conditions, can be given the Tax Allowance Incentive.
2. Detail of Certain Business Sectors and/ or Certain Business Sector and Certain Region as well as certain conditions to obtain the incentive are stated in the attachments of GR-78. Under the attachments of GR-78, there are 166 business sectors that are eligible for the Tax Allowance Incentive, where among the 166 business sectors, there are 109 industrial sectors. Additionally, 17 prescribed business sectors in certain areas and provinces qualify for the tax allowance incentives. Among the 17 prescribed business sectors in certain areas and provinces, there are 10 prescribed industrial business sectors.
3. Expansion on the existing business does not include machinery and/ or equipment replacement and/ or addition, within a production line that was already in commercial production.
4. General criteria of taxpayer's business that can obtain the incentive covers:
 - a) Has high investment value or export oriented;
 - b) Employ large workforce; or
 - c) Has high local content in its production.

C. Detail of Tax Allowance Incentive

The Tax Allowance Incentive provided to the qualified taxpayer covers:

1. Investment allowance of 30% (on top of normal tax depreciation) of the amount invested in tangible fixed assets including land, which are used in the Main Business Activity. This allowance may be claimed at the rate of 5% each year over a six-year period.
2. Accelerated depreciation for tangible fixed assets and amortization for non-tangible fixed assets, per the below tables - noting that these rates are approximately double the rate of the general rates:

| Category of tangible fixed asset | Accelerated useful life | Straight-line depreciation method | Declining balance depreciation method |
|----------------------------------|-------------------------|-----------------------------------|---------------------------------------|
| Non-buildings | | | |
| Category 1 | 2 years | 50% | 100% |
| Category 2 | 4 years | 25% | 50% |
| Category 3 | 8 years | 12.5% | 25% |
| Category 4 | 10 years | 10% | 20% |
| Buildings | | | |
| Permanent | 10 years | 10% | |
| Non-permanent | 5 years | 20% | |

| Category of non-tangible fixed asset | Accelerated useful life | Straight-line depreciation method | Declining balance depreciation method |
|--------------------------------------|-------------------------|-----------------------------------|---------------------------------------|
| Category 1 | 2 years | 50% | 100% |
| Category 2 | 4 years | 25% | 50% |
| Category 3 | 8 years | 12.5% | 25% |
| Category 4 | 10 years | 10% | 20% |

3. A reduced tax rate of 10% for dividend paid to non-residents (or the applicable tax treaty rate).
4. An extended period in relation to the carrying forward of tax losses, beyond the standard five years but not exceeding ten years:

| a) Additional of one year: | b) Additional of two years: |
|--|---|
| <ul style="list-style-type: none"> (i) For Capital Investment as stated in point B (1); (ii) For Capital Investment as stated in point B (1) that is conducted in industrial estate and/ or bonded zone; (iii) For Capital Investment as stated in point B (1) on the new and renewable energy business sectors; (iv) If the taxpayer disbursed at least IDR 10 billion for economic and/ or social infrastructure in the business location; (v) If the taxpayer used at least 70% of local material and/ or components no later than the second fiscal year; or (vi) If the taxpayer recruited at least 300 local employees and maintains that amount for four consecutive years. | <ul style="list-style-type: none"> (i) If the taxpayer recruited at least 600 local employees and maintains that amount for four consecutive years; (ii) If the taxpayer disbursed research and development expenses in Indonesia for at least 5% of the Capital Investment amount within 5 years, for product development or production efficiency; or (iii) For Capital Investment in Certain Business Sector conducted outside of bonded zone, if within one fiscal year at least 30% of the total sales value is exported. |

5. The regulation also sets out, for the various extensions for recoupment of losses, how to work out the loss years to which the extensions apply.

D. Utilization of Tax Allowance Incentive

The Tax Allowance Incentive can be utilized from the time of:

1. Starting of commercial production for the 30% investment allowance;
2. The issuance of approval letter for the Tax Allowance Incentive for:
 - a) Accelerated depreciation on tangible fixed assets and accelerated amortization for non-tangible fixed assets;
 - b) A reduced tax rate of 10% for dividend paid to non-residents (or the applicable tax treaty rate);
 - c) Additional carry forward tax losses as stated in point C (4) (a) (i) and (ii).
3. The issuance of approval letter on additional carry forward tax losses for all conditions as stated in point C (4) except for conditions stated in C (4) (a) (i) and (ii).

E. Procedures to obtain Tax Allowance Incentive

The procedures to obtain Tax Allowance Incentive are as follows:

1. Taxpayer wanting to obtain Tax Allowance Incentive must submit an online application before the starting of commercial production through OSS system, which should be conducted:
 - a) Along with the registration to obtain Business Identification Number (*Nomor Induk Berusaha* - "NIB") for a new taxpayer; or
 - b) Within one year after the issuance of business license by OSS Institution for Capital Investment and/ or expansion.
2. The approval letter for obtaining Tax Allowance Incentive will be issued by the Minister of Finance ("MoF") after the application submitted to OSS is accurately and completely received.
3. In case OSS system is not available, the application can be submitted off-line.

F. Limitation on fixed assets utilization

There are limitations on the use of fixed assets that have been given Tax Allowance Incentive, which are as follows:

1. Tangible fixed assets that has obtained Tax Allowance Incentive are not allowed to be used other than for the purpose given under the incentive, or to be transferred, except the fixed assets are replaced by new tangible fixed assets, before the end of a period whichever is longer between:
 - a) Within six years since the starting of commercial production; or
 - b) The useful life of the tangible fixed assets as stated in the tangible fixed asset table in point C (2).
2. Non-tangible fixed assets that has obtained Tax Allowance Incentive are not allowed to be used other than for the purpose given under the incentive, or to be transferred, except the fixed assets are replaced by new non-tangible fixed assets, before the end of the useful life of the non-tangible fixed assets as stated in the non-tangible fixed asset table in point C (2).

G. Revocation of Tax Allowance Incentive

If the taxpayer that has obtained Tax Allowance Incentive no longer meets the conditions in obtaining Tax Allowance Incentive, that taxpayer is imposed with administrative sanctions as follows:

1. The revocation of Tax Allowance Incentive given under GR-78;
2. Imposition of tax and tax penalties in accordance with the prevailing tax regulations; and
3. The taxpayer can no longer obtain the Tax Allowance Incentive.

H. Tax Allowance Incentive vs other tax incentives

Tax Allowance Incentive can no longer be given to a taxpayer that has obtained:

1. Tax facilities for conducting business in the Integrated Economic Development Zone (*Kawasan Pengembangan Ekonomi Terpadu - KAPET*) under GR No 20/2000 as amended by GR No 147/2000;
2. Tax holiday incentive under GR No 94/2010 as amended by GR No 45/2019; and
3. Super deduction incentive for intensive labor industry under GR No 94/2010 as amended by GR No 45/2019.

I. Further implementing regulations

GR-78 empowers various ministries to issue implementing regulations on particular aspects of the regulation, including specific requirements for some sectors.

J. Transitional provisions

At the time GR-78 is enacted:

1. Taxpayer that has obtained tax facilities under GR No 1/2007 as lastly amended by GR No 52/2011 can still utilize the tax facilities until the end of the tax facility period;
2. Taxpayer that has obtained tax facilities under GR-18 as amended by GR-9 can still utilize the tax facilities until the end of the tax facility period;
3. On the proposal of tax facility provision under GR-18 as amended by GR-9 that has been submitted before the enactment of GR-78, it can still be processed under GR-18 as amended by GR-9;
4. For taxpayer that the principle license, investment license, Capital Investment registration has been issued by BKPM/ Provincial Capital Investment Agency and One-Stop Integrated Service/ District or City Capital Investment Agency and One-Stop Integrated Service after the application of GR-18 as amended by GR-9 up to before the enactment of GR-78, can be given tax facilities under GR-78 provided the taxpayer meets criteria and conditions stated in GR-78 and it has never received approval or rejection letter for Tax Allowance Incentive under GR-18 as amended by GR-9.
5. For taxpayer that the business license issued by OSS Institution before the enactment of GR-78 can be given tax facilities under GR-78 provided the taxpayer meets criteria and conditions stated in GR-78 and it has never received approval or rejection letter for Tax Allowance Incentive under GR-18 as amended by GR-9.
6. All the implementing regulations for GR-18 as amended by GR-9 are still valid provided they are not contradicting with provisions under GR-78.
7. GR-18 as amended by GR-9 is revoked and no longer valid.

K. Evaluation of GR-78

The implementation of GR-78 shall be evaluated no longer than two years after it is issued by the team determined by the Economic Coordinating Minister.

For further information of the above, please do not hesitate to contact our Tax Partners or engagement teams.

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