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Indonesia and Singapore Governments Sign Amendment of the Indonesia-Singapore Tax Treaty

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Recent Development

The governments of Indonesia and Singapore recently reached an agreement to update the Indonesia-Singapore tax treaty. The amendment introduces some changes to the tax rate for certain types of income, such as royalty and branch profit tax, and also regulates certain aspects that were not regulated in the previous tax treaty, such as capital gains and tax avoidance.

The Indonesian tax authority indicated that the amendment was made to adjust with the current landscape of international taxation and the latest economic developments.

What the Regulation Says

The amendment of the Indonesia-Singapore tax treaty was signed on 4 February, five years after the initial negotiation started. The tax treaty amendment has not been ratified by the government yet, so it is not in force. But we understand that the Indonesian tax authority hopes that the ratification process can be completed soon, so that the amendment can be immediately implemented.

Below is a comparison of certain items that have changed significantly between the current and the amended version of the Indonesia-Singapore tax treaty:

Clause	Current Indonesia-Singapore Tax Treaty	Amended Indonesia-Singapore Tax Treaty
Government exemption	Interest received by the government of a contracting state from the other contracting state is exempted from tax in the other contracting state.	Interest received by the government of a contracting state from the other contracting state is exempted from tax in the other contracting state, <u>including interest received by a sovereign wealth fund and its subsidiaries</u>.

Clause	Current Indonesia-Singapore Tax Treaty	Amended Indonesia-Singapore Tax Treaty
Source-state exemption for government-issued bonds or debentures	The tax treaty provides a tax exemption	The tax treaty does not provide a tax exemption.
Royalty	15%	• 8% for payment of royalty on the use, the right to use or information on, industrial, commercial or scientific experience • 10% for other types of payment of royalties
Branch profit tax	15%	10%
Exception on Production Sharing Contract	There is a requirement that the tax treatment received by a Singapore taxpayer must not be less favorable than any third state ("most favored nation").	The "most favored nation" requirement is removed.
Capital gains	There is no provision on capital gains.	• It refers to the OECD Model. • There is a provision on indirect transfer of assets. • Indonesia has the right to impose tax on transfers of shares in the Indonesia Stock Exchange. • Capital gains on transfers of shares, other than shares traded on an approved stock exchange, deriving more than 50% of their value directly or indirectly from immovable property situated in the other country may be taxed in that other country if the seller owns at least 50% of the total issued shares of the company whose shares are sold. It does not apply to gains derived from the transfer of shares deriving

Clause	Current Indonesia-Singapore Tax Treaty	Amended Indonesia-Singapore Tax Treaty
		value from immovable property used by the company to carry on its business and to gains derived from the alienation of shares alienated or exchanged in the framework of a reorganization of a company, a merger, a scission or a similar operation.
Exchange of Information	OECD Model 1977	OECD Model 2017

The clause on the most favored nation for branch profit tax is eliminated. As a result, under the amended tax treaty, branch profit tax of 20% will apply for permanent establishments in any production sharing contract related to oil and gas and contracts of work for other mining sectors, as set out in the Indonesian tax law.

The addition related to the capital gains includes the following:

- Gains from the sale of unlisted shares where (i) more than 50% of the value of the shares is directly or indirectly derived from immovable property situated in the other country, and (ii) the seller owns at least 50% of the total issued shares of the company whose shares are being sold, may be subject to tax in the country where the immovable property is situated.

- Gains from the sale of listed shares of an Indonesian company that are traded on the Indonesia stock exchange may be taxed in Indonesia.

The amended tax treaty includes anti-tax avoidance provisions in the preamble and in the new provision of Article 28. The objective of including the anti-tax avoidance provisions in the preamble is to eliminate double taxation but also not to create opportunities for a non-taxation or tax reduction situation. Under the new provision on anti-tax avoidance, if the intention of a transaction is merely to take benefits from certain provisions in the tax treaty or to create a tax avoidance situation, the benefits under the tax treaty may not be available to be enjoyed.

Actions to Consider

The new provisions under the amended tax treaty may be a positive development in the landscape of capital investment from investors. The capital gain provision under the amended tax treaty in particular may be beneficial for investors to contemplate or to revisit their exit strategy as it offers a certain levels of protection from taxation of capital gains.

In addition, a taxpayer may also benefit from the reduction of the withholding tax rate on royalty, which was 15%, to either 10% or 8%, which may affect the existing Intellectual Property arrangement adopted by multinational companies in Indonesia.

Please note, however, taxpayers that would like to enjoy the benefits of the Indonesia-Singapore tax treaty amendment should ensure that they meet the requirements to implement the tax treaty as set out under the prevailing tax regulation.

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