

# Global Transfer Pricing Landscape

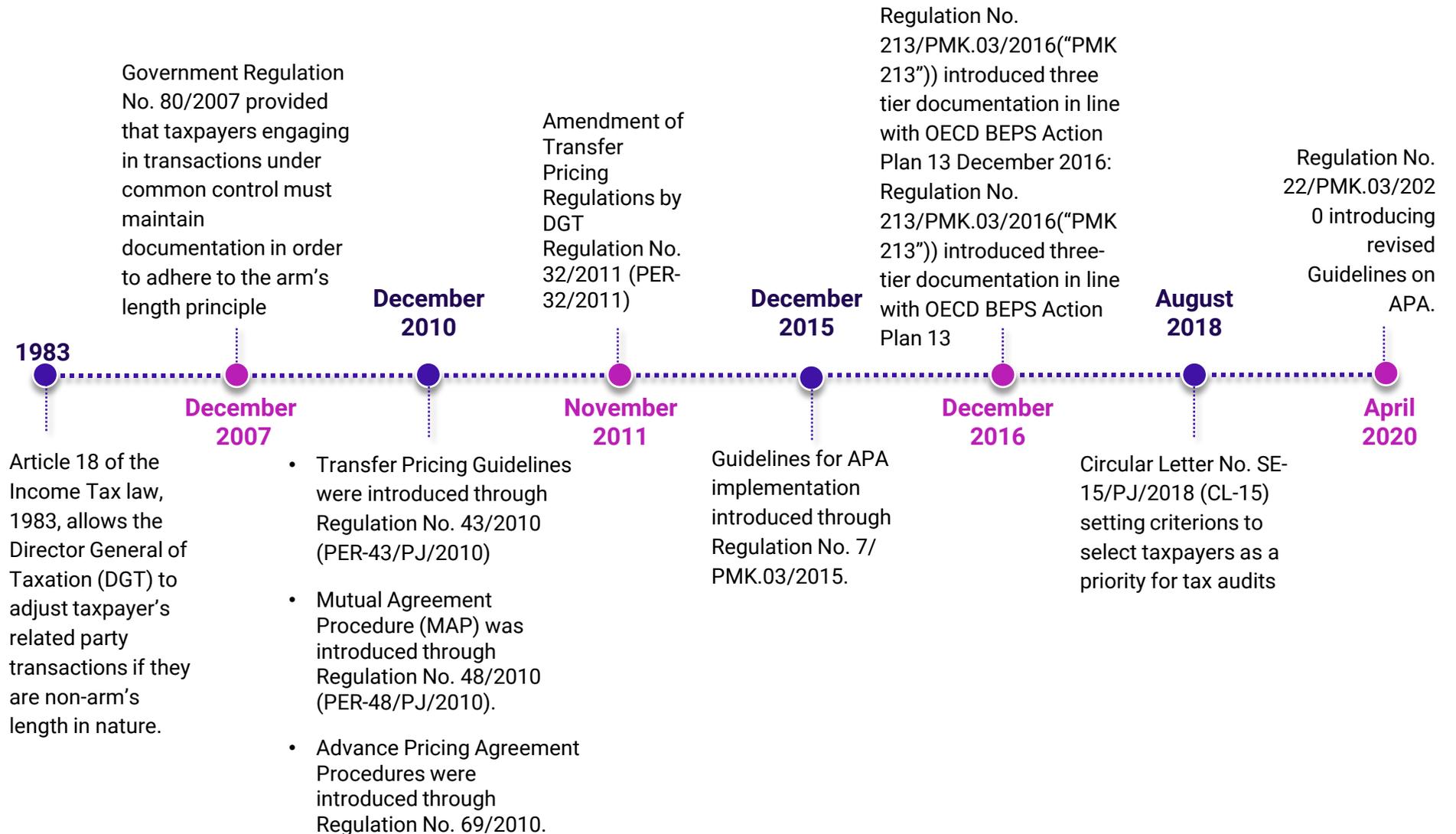
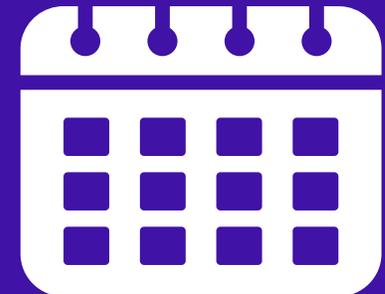
## Indonesia

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# Highlights



## Introduction

Article 18(3) empowers the DGT to re-determine the amount of taxable income and deductible expenditures for transactions between taxpayers where a 'special relation' exists.

Transfer pricing provisions apply to domestic transactions, only for the taxpayers that are subject to different tax rate regimes.

Furthermore, PER-43/PJ/2010, as (further amended by PER-32/2011) provides guidance on documentation requirements and insights on specific requirements with respect to the arm's length standard from an Indonesian transfer pricing perspective.

## OECD Guidelines

Indonesia is not a member of the Organization for Economic Co-operation and Development (OECD), although it has been granted 'enhanced participation' status. Indonesian transfer pricing guidelines reconfirm the basic transfer pricing concepts and principles of the OECD Guidelines.

## Related Party

According to the guidelines, a special relation is deemed to exist when:

- The taxpayer has a direct or indirect ownership of 25% or more capital in another taxpayer or two or more other taxpayers

- The taxpayer controls (directly/indirectly) another taxpayer or where two or more taxpayers are under common control
- Family relationship by blood or marriage.

## Arm's Length Principle

The arm's length principle can be implemented using the following steps:

- i. Perform a comparability analysis for identifying comparables ;-
- ii. Determine the most appropriate transfer pricing method;-
- iii. Apply the arm's length principle to the tested transaction based on the result of the comparability analysis and the selected transfer pricing method;-
- iv. Document each step of the process used to determine the arm's length price or profit.

## Transfer Pricing Documentation

### Exemptions and thresholds

Under the prevailing regulations governing transfer pricing, taxpayers were required to only maintain local transfer pricing documentation to establish the arm's length principle of the related party transactions.

The Minister of Finance (MoF) of the Republic of Indonesia issued PMK-213 dated and effective 30 December 2016 that requires the taxpayers to maintain three levels of documentation:

- A Master File;
- A Local File; and
- Country-by-Country Report (CbCR)

The regulations do not give preference to any specific method or methods and the taxpayers are independent to choose the most appropriate method out of the six transfer pricing methods.

Indonesia's Master File/Local File and Country-by-Country Reporting (CbCR) rules are consistent with OECD recommendations outlined in the final report on transfer pricing documentation and Country-by-Country Reporting–Action 13.

The said documents have to be submitted in the local language, i.e., Bahasa Indonesia. An exception is for the taxpayers having the approval to maintain their books in a foreign language and using a currency other than Rupiah who can maintain the documents in English accompanied by a translated version.

The regulation provides detailed guidance on who should prepare the document, what should be included and when such documentation should be made available.

This regulation is issued primarily in relation to the transfer pricing documentation requirements and does not override the existing transfer pricing regulations governing the application of the arm's length principle.

## Master File and Local File

The preparation of **Master File and Local File** is mandatory for taxpayers who have conducted related party transactions in the previous year and have:

- Annual gross operating revenue in the prior fiscal year that exceeds IDR 50 billion (approximately USD 3.7 million);-
- Transaction of tangible goods in the prior fiscal year that exceeds IDR 20 billion (approximately USD 1.5 million) or services, interest payments, royalties or other transactions exceeding IDR 5 billion (approximately USD 373,000);-
- Transactions with a related party that is domiciled in a country or jurisdiction with a corporate income tax rate that is less than the prevailing Indonesian corporate income tax rate (of 25%) in the current year.

**No separate thresholds for Local and Master File:** PMK-213 requires taxpayers to prepare the Local File and Master File if the above thresholds exceed.

Furthermore, PMK-213 does not require taxpayers to submit the Master File and Local File documentation along with the Corporate Income Tax Return (CITR), but only upon Directorate General of Taxation (DGT) request.

### Country-by-Country Report

DGT has issued the implementation regulation on CbCR, provides detailed guidance broadly on the following matters:

- a. Which business groups/multinational business groups are required to file the CbCR in Indonesia;
- b. What is required to be prepared and submitted as a part of the CbCR filing; and
- c. Timing for preparation and filing of the CbCR in Indonesia.

PER-29 is effective from 29 December 2017 and covers the Indonesian CbCR filing requirements from the fiscal year 2016 onwards.

Any local taxpayer with the following criteria shall be required to prepare and submit a CbCR in Indonesia:

- Taxpayers that are considered as the parent entity of a group of entities with a consolidated gross revenue in one tax year of at least IDR 11 trillion (approximately USD 818 million); or
- Taxpayers that are subsidiaries of one or more parent entities that is a tax resident in a jurisdiction which does not obligate CbCR does not have an exchange of information agreement with Indonesia, or does have an exchange of information agreement with Indonesia but a CbC report cannot be obtained by Indonesia from such jurisdiction.
- a CbCR cannot be obtained by Indonesia from such jurisdiction.

### Secondary Filing Mechanism

PER-29 limits the CbCR filing requirements under the secondary filing mechanism and is only applicable to those local taxpayers where certain specific criteria of parent and constituent entity are met. The criteria are provided below:

### Criteria for Parent Entity

A parent entity having consolidated gross turnover in the relevant fiscal year (based on the consolidated financial report) of at least:

1. Equal to EUR 750 million (according to the functional currency exchange rate of the parent entity as of 1 January 2015) if the parent entity's country/jurisdiction does not require the filing of CbCR); or
2. The threshold of the consolidated gross turnover set by the jurisdiction where such parent entity is located which serves as the basis for determining the requirement to submit CbCR.

### Criteria for Constituent Entity

- a. Every separate business entity that is a member of a multinational business group and is included in the consolidated financial statements of the parent entity or is excluded merely due to business scale or materiality considerations; and/or
- b. Every Permanent Establishment(PE) of the business entity above having separate financial statements.

### Exemptions

- An exemption to a local taxpayer with an overseas parent entity is provided to file CbCR in Indonesia if the parent entity assigns a surrogate parent entity and fulfills the following conditions:
- The local taxpayer submits a notification on the surrogate parent entity to the DGT; and

- The country/jurisdiction in which the surrogate parent entity is domiciled requires the filing of CbCR and has a Qualifying Competent Authority Agreement (QCAA) and CbCR that can be obtained by the Government of Indonesia.

The CbCR must be available within 12 months after the end of the fiscal year of the local taxpayer. Both the notification form as well as the CbCR should be filed simultaneously within the following period:

- 16 months after the end of the fiscal year for the fiscal year 2016;
- 12 months after the end of the fiscal year for the fiscal year 2017 and thereafter.

PER-29 also notes that in cases where the CbCR cannot be obtained by the government of Indonesia, the local taxpayer should submit the CbCR within three months after the DGT's announcement (in its website) of the list of countries/ jurisdictions with which the DGT has QCAA but CbCR cannot be obtained. After three months, if the local taxpayer fails to submit the CbCR, a formal request letter will be issued by the DGT with the filing deadline of 30 days after the date of the letter.

PER-29 introduces a filing of notification to the DGT through a CbCR notification form. The form generally requires the local taxpayers to provide a statement on whether or not it has an obligation to submit a CbCR.

PER-29 does not specifically clarify the penalties or consequences that may arise

due to a failure in submitting the relevant submissions for CbCR documentation requirements within the required timeline.

However, not attaching the required receipt of filing of notification and/or the filing of CbCR to the CITR may trigger a case where the CITR may be considered incomplete and therefore the taxpayer may be subject to a fine of IDR 1,000,000 or up to 50% of any unpaid tax, whichever is higher.

## Contents of Master File, Local File and CbCR

**Master File** – The contents of the Master File provided in PMK-213 are largely consistent with those contained in Action Plan 13. It describes the global business group and includes the following:

- Structure of ownership and countries or jurisdictions of each constituent entity;
- Business activities performed;
- Intangible property owned;
- Financial activities and financing;
- Consolidated financial statements of the parent company and information on taxation pertaining to the related party transactions.

The Master File needs to be in Bahasa Indonesia.

**Local File** – The Local File is focused on sharing information on the local taxpayer. The contents of Local File are therefore broader than the contents of Master File as outlined in Action Plan 13. Local File needs to have details on:

- Identity and business activities being performed;
- Information on related party transactions and independent transactions performed;
- Implementation of arm’s length principle;
- Financial information;
- Non-financial events/occurrence/facts which influence the formation of price or profit level.

In summary it is consistent with the OECD but additional details such as the independent transactions are required to be disclosed; commodity transactions require extensive data/information; ex-ante approach must be adopted. The detailed list of contents of the Local File is provided in PMK-213.

**CbCR** – The format is aligned with Action Plan 13, where information on the list of members of Multinational Enterprises (MNE) and their business activities per jurisdiction, allocation of income, and taxes paid the per jurisdiction of MNE members both local and foreign is disclosed.

An additional requirement in the form of working (referring to Appendix E of PMK-213) which requires information per tax ID number of the group entities.

## Submission of documentation

**Master File and Local File:** Per PMK-213 Master File and Local File must be available no later than four months after the fiscal year end of the taxpayer and submitted to DGT based on the timeline stipulated in the regulation.

**CbCR:** The CbCR must be available no later than 12 months after the fiscal year end and must be filed with CITR of the following fiscal year.

The taxpayer is required to indicate if they have prepared the transfer pricing documentation while filing CITRs.

Taxpayers are not required to submit documentation on an annual basis. However, it needs to be submitted to the tax authorities within seven days of the request, though the regulation provides for time up to 30 days from the day of request.

## Selection of comparables

Pan-Asian comparables are also accepted, if adequate domestic comparables are not available.

## Certain Specific Transactions

### Intra-group services

Taxpayers need to apply for the ‘Benefit Test’ to substantiate that intra-group services are actually received, and the quantum of service charge is commensurate with the benefits derived.

## Royalty

Taxpayers need to justify the existence of the intellectual property, its value in the generation of profits to the licensee, the ownership of the intellectual property with the licensor and the arm's length nature of the royalty rate.

The DGT generally challenges the arm's length nature of the royalty paid by the deeming licensee to be contract manufacturers.

## Financial transactions

Thin capitalization regulation is applicable (effective fiscal year 2016) through Regulation No. PMK 169/PMK-010/2015. The rules state that the maximum debt to equity ratio should be 4:1, and in the event of a taxpayer having zero balance of equity or less than zero, the entire costs of the loan (i.e., interest expense) would not be deductible for tax purposes.

## Reporting and Compliance

### Corporate Income tax return

A CITR (along with special attachment forms 3A, 3A-1, 3A-2) needs to be filed within four months from the end of the fiscal year. The details of a related party transaction such as the type of transaction, value of the transaction, a related party, transfer pricing method applied, the reason for the application of the method, whether transfer pricing documentation is prepared, etc. must be disclosed with the annual corporate tax return.

If the taxpayer fails to disclose such information, there may be an increased attention by the ITO, with the ultimate outcome being the need to submit the documentation.

Based on PMK-213, the taxpayers are additionally required to file details on whether Master File and Local File have been prepared and also state the dates when they were prepared in additional summary form along with the CITR.

## Transfer pricing audit/assessment

The taxpayer is selected for assessments based on risk indicators, such as:

- Application of tax refund;
- A large number of related party transactions;
- Oil and gas and coal mining industry;
- Continuous operating losses;
- Related parties in tax havens;
- Significant related party transactions;
- An increase in gross revenue/receipts but no change in net profit;
- Reporting low profit compared to the industry average or that of other similar enterprises.

## APA, MAP and Safe Harbour provisions

No safe harbour provisions are available.

### APA and covered period

Unilateral and bilateral APAs are available. Domestic transactions are also covered as per the new APA Guidelines. An APA is valid for five years for both Unilateral and Bilateral APAs (as compared to the previous three years for unilateral and four years for bilateral APAs).

### Timelines

The application must be submitted 6 to 12 months prior to the start of the proposed APA period. An Unilateral APA must be concluded within twelve months, and a Bilateral APA must be concluded within twenty-four months from the commencement of negotiation.

### Roll-back Provisions

The roll-back provision is also now available for a maximum period of five years (previously only for one year) if that relevant year is not under assessment or appeal. However, a taxpayer can only apply for a roll-back period in cases where

- Facts and circumstances do not materially differ;
- Statute of limitations is not yet passed;
- Corporate Income Tax Assessment letter for the subject year has not been issued;
- The taxpayer is not charged or is not under any investigation for a tax crime.

Taxpayers must also be privy to the fact that submitting an application for an APA might trigger a tax audit if the related party transactions have not been assessed in the previous three years.

### Who can apply?

The following taxpayers can request for an APA:

- Indonesian entities that have operated for at least three years;
- A PE that has operated for at least three years in Indonesia;
- Foreign taxpayers that reside in tax treaty countries (through the respective country's competent authority).

### Other important pre-requisites:

- The taxpayers have filed CIT return for the previous three fiscal years prior to an APA application,
- The taxpayer has prepared and maintained Local File and Master File for three previous years prior to making an application as well filed CIT returns for the previous three years,
- The taxpayer is not under tax crime investigation or is not charged with a tax crime,
- Related party transactions and related parties proposed to form part of the APA application have been declared by taxpayer in its Annual CIT for the previous three fiscal years prior to the APA application,

- The proposed transfer pricing is based on the arm's length principle and doesn't lead to a reduction in the operating profit of the taxpayer as compared to profits declared in Annual CIT for the previous three fiscal years prior to the APA application.

Several additional conditions have been further imposed on the aforementioned pre-existing conditions like-

- The APA should not be disadvantageous to the tax administration in the form of lower operating profits,
- The taxpayer must not be associated with any tax crime or should not be under any investigation for the same, and the transactions to be covered under APA must be declared in the annual CIT Return for three previous years.
- The Guidelines also covers in detail the operational procedures regarding the withdrawal of APA, implementation, and renewal of APA, as well as evaluation and judicial investigation of APA. The taxpayers must be mindful that submitting false information can lead to adverse consequences, including the cancellation of an existing APA.
- Guidelines also lay down the situations where the tax authorities are entitled to carry out transfer pricing adjustments in case of inaccurate furnishing of information, non-submission of the necessary information, etc.
- A taxpayer may also apply for a Mutual Agreement Procedure (MAP) within the time limit as may be applicable as per the relevant tax treaty.

## Penalties and Other Consequences of Non-compliance

Inappropriate disclosure of information pertaining to related party transactions by a taxpayer in a CITR could lead to an administrative penalty of up to 400% of the unpaid tax and three months to six years of imprisonment if criminal activity is involved.

A penalty of 2% per month up to 48% shall be imposed on the underpayment of tax arising from adjustments to related party transactions based on the assessment.

If taxpayers have not prepared Master File and Local File prior to the submission of CITR, then the return may be considered as incomplete and, in such cases, penalties may be levied by DGT on any unpaid tax of up to 200%, as well as other criminal actions.

Taxpayers are required to pay only an amount agreed with tax auditors during the tax audit's closing conference. If the taxpayer does not agree with any of their corrections, it need not pay anything at this point.

Taxpayers need to ensure in deciding how much to pay, since an adverse DGT decision on its objection may result in an administrative penalty of 50% of the underpaid tax. Further, this penalty increases to 100% if an appeal is lodged, and the decision is not in favor of the taxpayer.

## Time limits to complete an assessment

There is no separate statute of limitation for transfer pricing, but an assessment must be concluded within five years from the tax year end filing date.

In case of any transfer pricing assessment, the taxpayer can object to such assessment and further appeal the unfavorable decision in a similar manner as with any tax assessment.

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# Summary of Transfer Pricing Requirements

## Effective from

December 2010

## Compliance Requirements

- The taxpayers to maintain three levels of documentation, which contains Master File, Local File and CbCR. Indonesia's Master File/Local File and CbCR rules are consistent with OECD recommendations outlined in the final report on transfer pricing documentation and CbCR– Action 13.
- The formal regulations for adoption of BEPS and CbCR are in place as DGT has issued DGT Regulation No. 29/PJ/2017 (PER-29) regarding 'Procedures for the Management of CbCR,' following the release of the CbCR requirements in early 2017 through Minister of Finance (MoF) Regulation No. 213/PMK.03/2016

## Penalties

No specific transfer pricing penalties, however, inappropriate disclosure may lead to an administrative penalty of up to 400% of the unpaid tax and three months to six years of imprisonment in case of criminal actions.

A penalty of 2% per month up to 48% shall be imposed on the

underpayment of tax arising from adjustments to related party transactions based on the assessment.

If taxpayers have not prepared Master File and Local File prior to submission of CITR, then the return may be considered as incomplete and in such cases, penalties may be levied by DGT on any unpaid tax of up to 200%, as well as other criminal actions.

## Method and Preference for Comparable

- Five methods as defined by the OECD without any hierarchy.
- Pan-Asian comparables are also accepted, if adequate domestic comparables are not available.

## Peculiar Features

Comparable uncontrolled price (CUP) is considered to be the preferred method by the tax authorities.

## Safe Harbour and APA

No safe harbour provisions available. Unilateral (valid for three years) and Bilateral APA (valid for four years) are available. Roll-back provision is available only for up to five years, and only if that relevant year is not under assessment or appeal.

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Our cross-functional teams serve a wide range of industries, with a specific focus on healthcare, food processing, and banking and financial services. Over the last decade, we have built and leveraged capabilities across key global markets to provide transnational support to numerous clients.

We provide an array of solutions encompassing Consulting, Business Services, and Professional Services. Our solutions help businesses navigate challenges across all stages of their life-cycle. Through our direct operations in USA, India, and UAE, we serve a diverse range of clients, spanning multinationals, listed companies, privately owned companies, and family-owned businesses from over 50 countries.

Our team provides you with solutions for tomorrow; we help you *Think Next*.

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