

Indonesia-Singapore tax treaty

Amendment agreed pending ratification

Indonesia and Singapore finally agreed after five years of negotiations to a package of revisions to the existing double tax agreement (DTA) which has been in force for 29 years. Both States' finance ministers signed the new DTA on 4 February 2020 in Bogor Indonesia, three months after Indonesia ratified the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI Convention) to which Singapore is a party.

General changes

The revision brings about several changes in the taxation at source of dividends and branch profit tax, interest, royalties, and capital gains. Branch profit tax (BPT), provided under the provision of Business Profit in the current DTA and moved to the provision of Dividends in the new DTA, is reduced from 15% to 10%. The new DTA retains the exception applicable for income arising from production sharing contracts in oil and gas and contract of works for other mining sectors. However, while the current DTA calls for a most favored nation condition for the exception to apply, the new DTA removes the condition. Dividend tax remains at 10% if the dividends pertain to shareholding of at least 25% and 15% for all other cases.

Interest is still taxed at source at 10%, the same rate as that under the current DTA. However, the tax exemption currently available for both States' residents in respect of interest derived from Government bonds or debentures is gone in the new DTA leaving the Governments of both States as the only parties entitled to the exemption benefit. It also asserts that a penalty charge for a late payment is beyond the scope of the interest definition.

Royalties currently taxed at source at a single rate of 15% are divided into two categories in the new DTA based on the types of intangibles right to which the royalties belong: (1) right to copyright, patent, trademark, design or model, plan, secret formula or process; and (2) right to industrial, commercial or scientific equipment or information concerning industrial, commercial or scientific experience. Royalties of the first category is taxed at 10% while those of the second category at 8%.

An article is added in the new DTA to deal specifically with capital gains. For gains arising from the alienation of immovable property, the new DTA allows the State in which the immovable property is located to tax the gains in line with the OECD and UN Model Tax Conventions. The rule extends to the alienation of shares other than those traded on approved stock exchange deriving more than 50% of their value directly or indirectly from immovable property. However, it does not apply for alienation of shares carried out in the framework of a reorganization of a company, a merger, a scission or a similar operation.

Alignment with the MLI Convention

The new DTA appears to have been aligned with the provisions of the MLI Convention intended to modify the global network of more than 3000 tax treaties and in particular the MLI position of Indonesia and Singapore. It states in the preamble the Convention-asserted objective of a DTA: elimination of double taxation without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty shopping arrangements). This is supported by an article added to the new DTA which states that a treaty benefit in respect of an item of income shall be denied if one of the principal purposes of the transaction or arrangement giving rise to the income is obtaining that treaty benefit.

The provision on Associated Enterprises has been reworded to include a paragraph calling for a corresponding adjustment from a State pursuant to a primary (transfer pricing) adjustment made by the other State in respect of profits related to cross-border transactions between associated enterprises. However, the corresponding adjustment requirement should not apply if based on the final ruling of judicial or legal proceedings over the actions giving rise to the primary adjustment one of the enterprises concerned is liable to penalty for fraud, gross negligence or willful default.

Entry into force

The entry into force of the new DTA is subject to the exchange of ratification instruments between Indonesia and Singapore neither of which has announced any timeline for this. If both can complete their respective ratification and exchange the ratification instruments in 2020, you can expect the new DTA will enter into force on 1 January 2021.

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