

INDONESIA

INDUSTRIAL PROPERTY

INVESTMENT GUIDE





Jababeka Industrial Estate

WELCOME

We are very glad to release the first issue of Indonesia Industrial Property Investment Guide jointly with Tuah & Suparto Advocates and Solicitors and Cedar Strategi. We hope our industrial investment guide will be giving a great benefit to our foreign investor clients by guiding them to understand the property, legal and tax regulations in Indonesia on the industrial sector.

Despite the Covid-19 pandemic crisis since early 2020, the Indonesian government remains strongly committed to sustain growth by focusing on new infrastructure, human capital development and structural reforms to attract investment and fiscal support. Most importantly, the resilient industrial sector, particularly manufacturing, remains the key engine of economic growth recovery moving forward with positive spillover effects to other sectors, including property.

We hope that this first publication will continue to be a great benefit to our clients. Please do feel free to contact Knight Frank should we be able to assist you in your investment plan.



Willson Kalip
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It is an interesting time for Indonesia in terms of the growth of its regulatory framework, particularly over the latter part of this decade. We've seen an acceleration by the government towards greater legal certainty and transparency, whilst also embracing the evolution of bureaucracy by means of digitisation.

This trend, coupled with the country's existing attractive business opportunities, should rapidly proliferate Indonesia's reputation as an investment destination in the region, global pandemic economic fallout notwithstanding.

We're gratified and honoured to have collaborated with Knight Frank on the release of this essential publication which will provide a focused guide for foreign investors in their deliberations for Indonesia as an investment destination.



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**INDONESIA
PROPERTY**

INDONESIA PROPERTY

INDONESIA OVERVIEW



The world's largest archipelago of approximately **17,000 islands**



Over Half of all international shipping goes through Indonesian waters



The world's fourth most populous country of more than **260 million people**



The world's **14th-largest country** in terms of land area about 1,919,440 square kilometers



Established middle class consumers are forecast to grow from **26 million people in 2017** to **65 million people in 2030**



Indonesia has been rated by Sovereign Debt Rating Agencies as an **Investment Grade Country since 2017**, reflecting a positive outlook and confidence



2020 Infrastructure Budget increased to Rp419 Trillion, reflecting a strong commitment for connectivity to boost the economic growth



Manufacturing industry contributed **approximately 20% of the total GDP** in Q2-2020



Indonesia is forecast to be **the world's fourth largest economy at US\$10.5 Trillion by 2050**



Accounted for 58% in Q2-2020, private consumption or domestic demand has been the leading growth factor to the Indonesian economy.

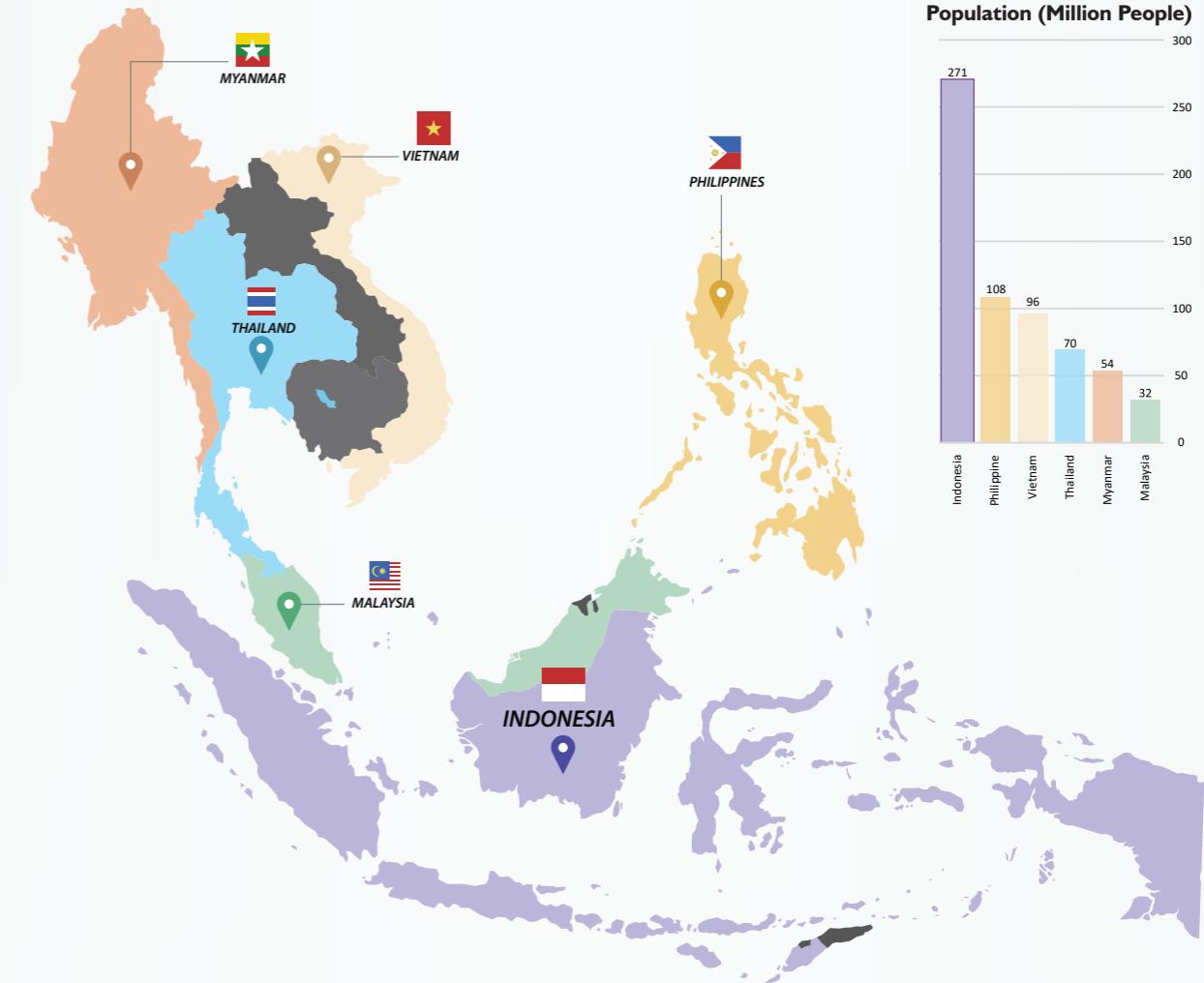


Indonesian High Networth Individuals (HNWIs) is forecast to **grow by 57% to 33,057 people in 2024**

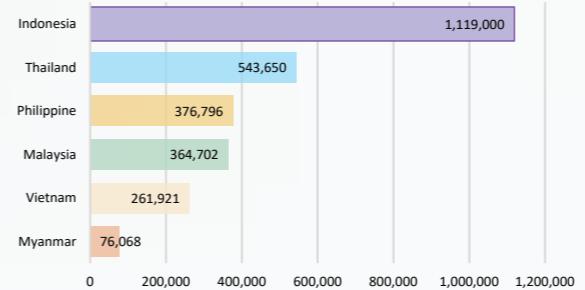


Indonesia's productive age group is forecast to reach **70 percent of the total population by 2030**

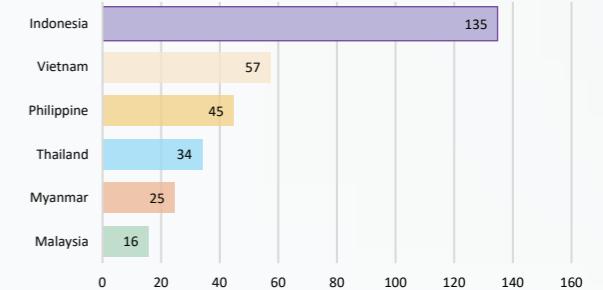
Regional Comparison



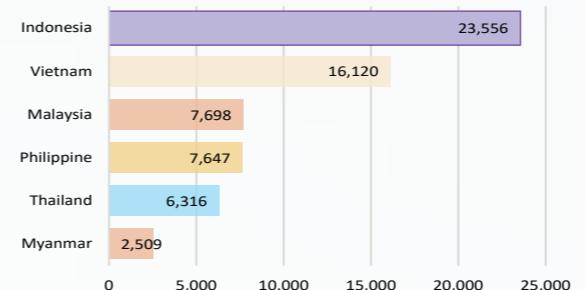
GDP (Billion US\$)



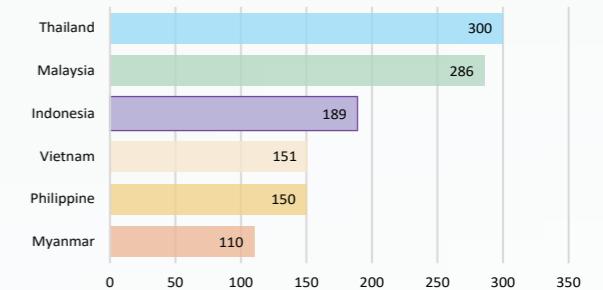
Workforce (Million People)



Flows of FDI (Million US\$)



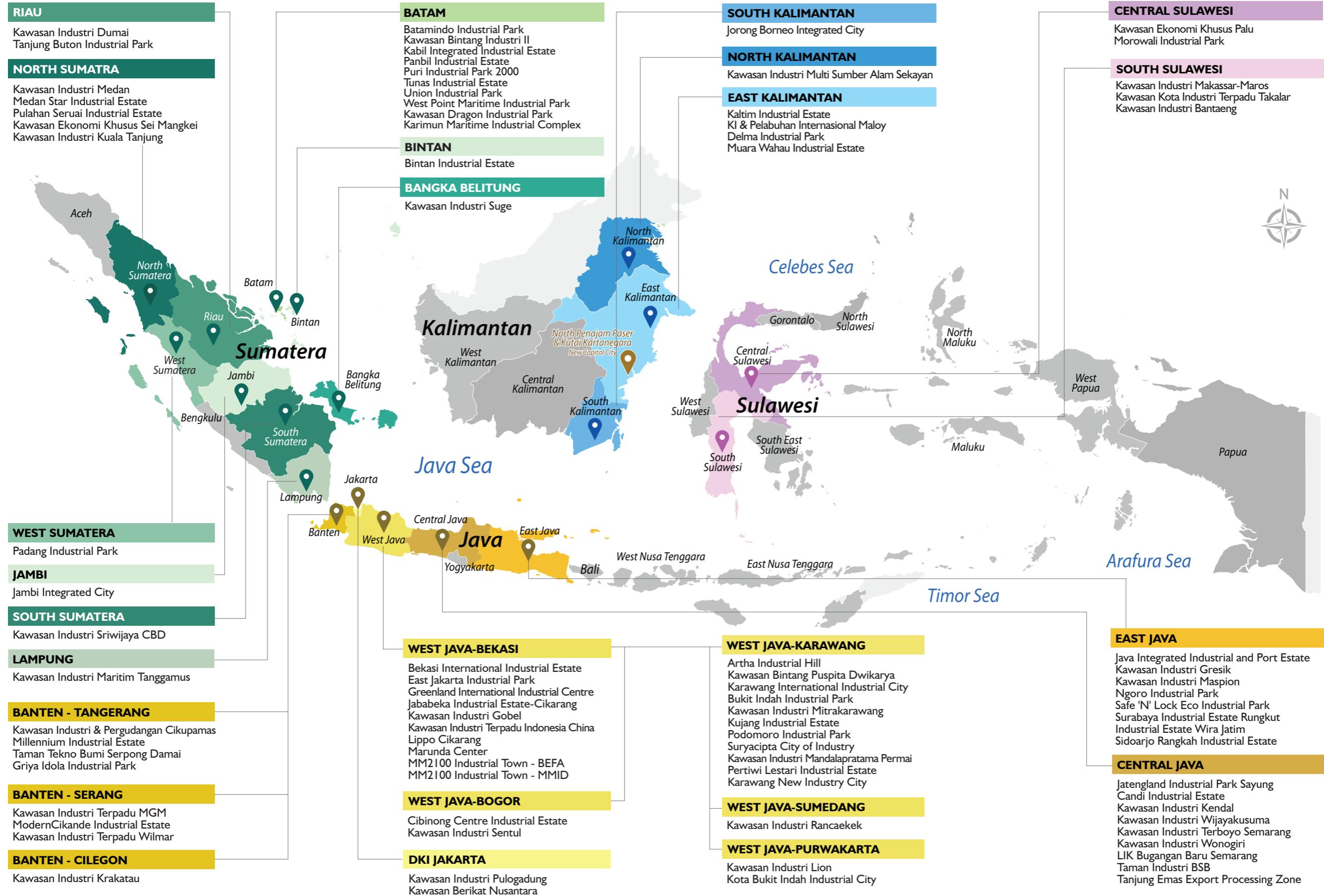
Average Minimum Wage (US\$/Month)



Source: Processed from Multiple Sources by Knight Frank / PT. Willson Properti Advisindo

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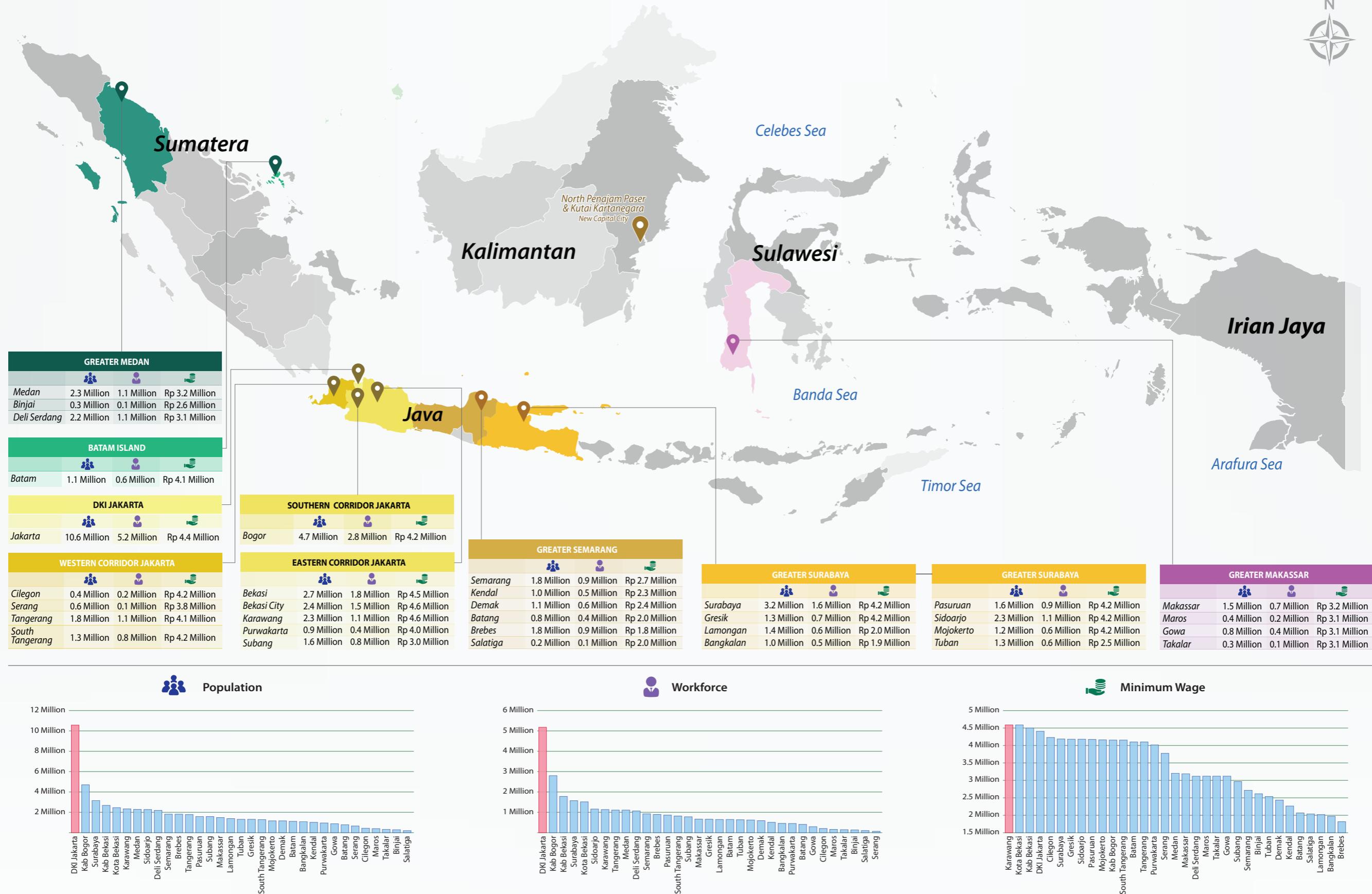
Map of Industrial Estates in Indonesia



Source: Indonesia Investment Coordinating Board (BKPM) 2020

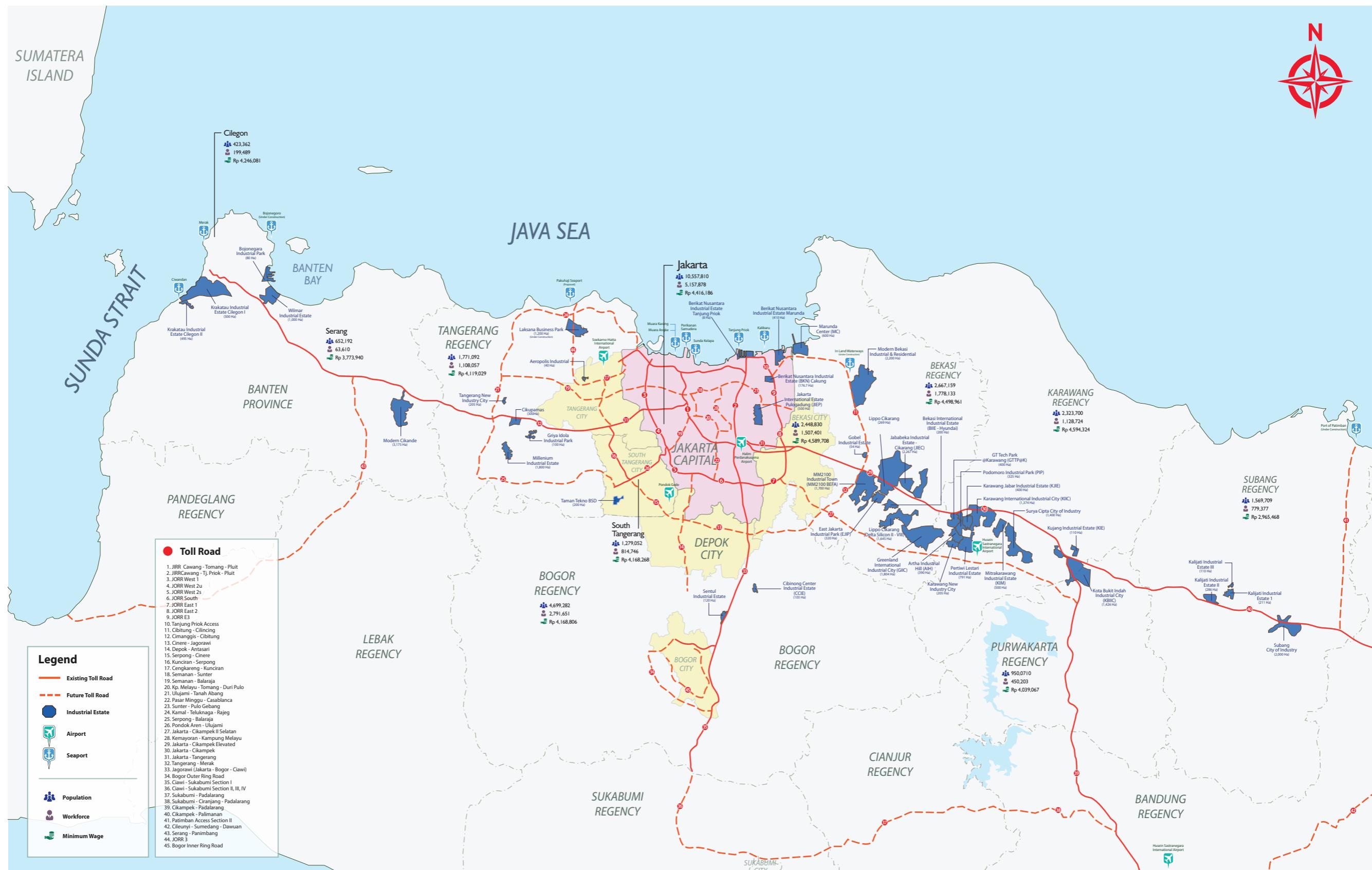
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Map of Population, Labor Force and Minimum Wage in Indonesia's Major Industrial Locations



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Map of Greater Jakarta Industrial Estates

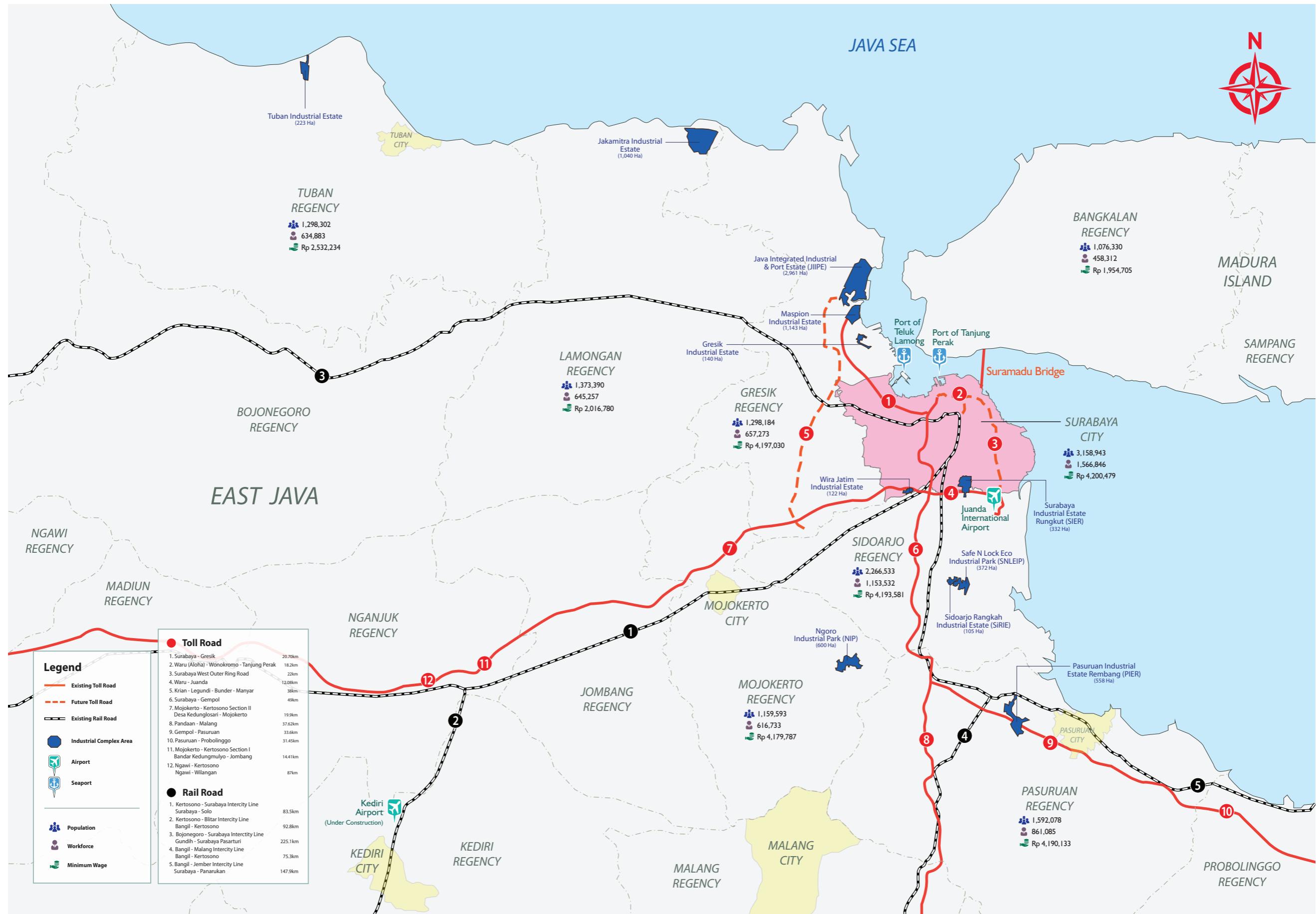


Source: Processed from Multiple Sources by Knight Frank / PT. Willson Properti Advisindo

Base Map : <https://kfmap.asia/>

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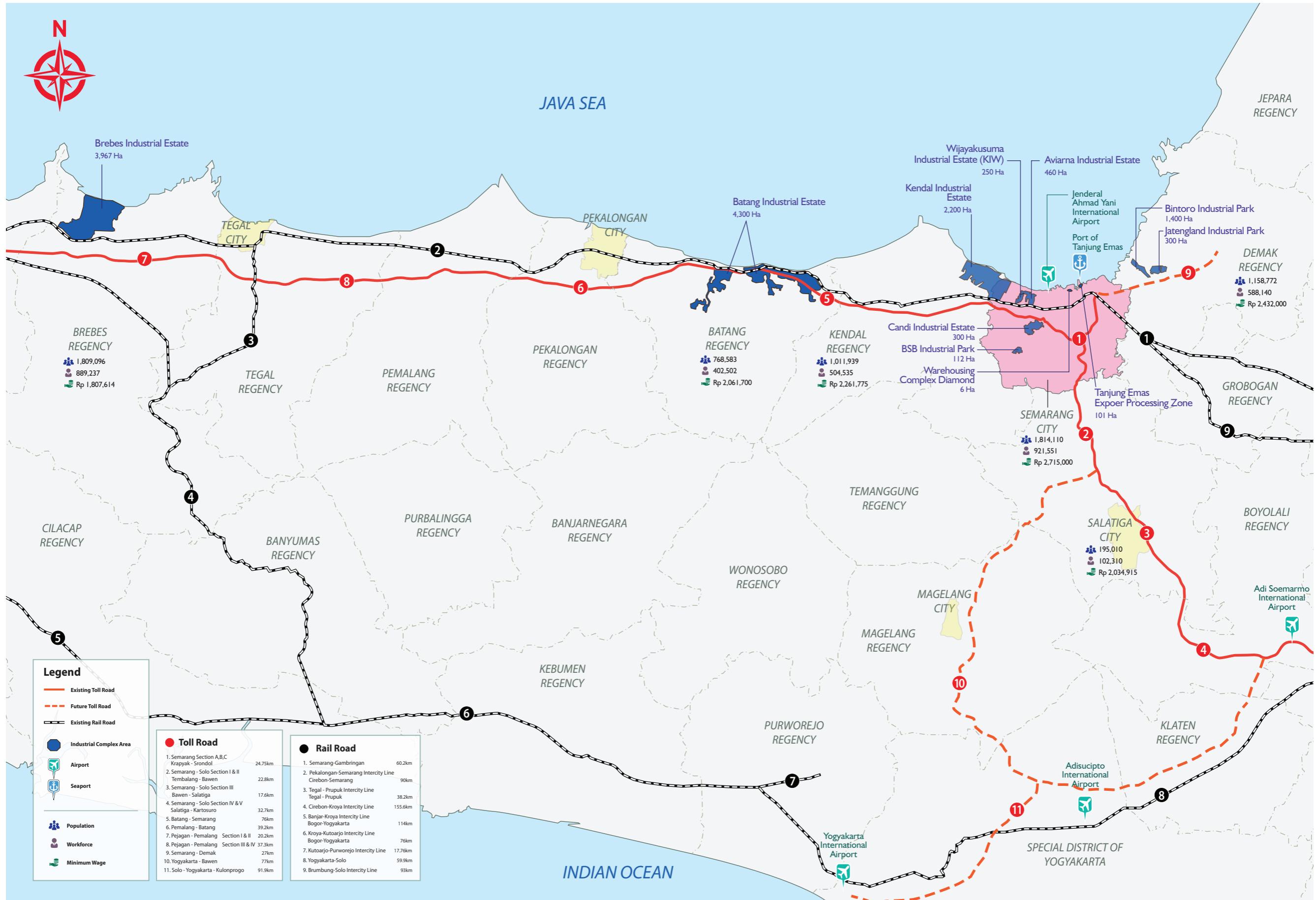
Map of Greater Surabaya Industrial Estates



Source: Processed from Multiple Sources by Knight Frank / PT. Willson Properti Advisindo
Base Map : <https://kfm.map.asia/>

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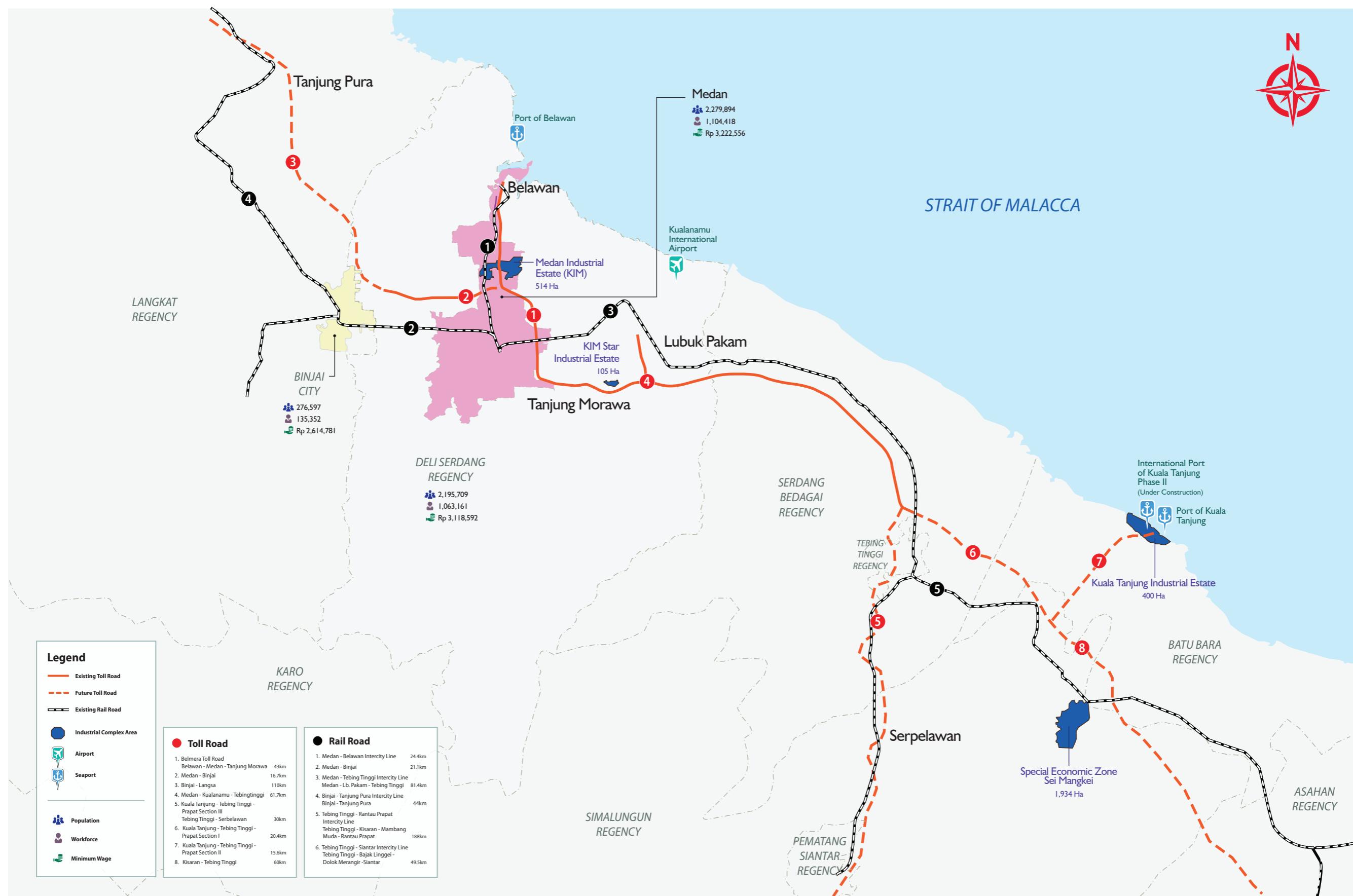
Map of Greater Semarang Industrial Estates



Source: Processed from Multiple Sources by Knight Frank / PT. Willson Properti Advisindo
Base Map : <https://kmap.asia/>

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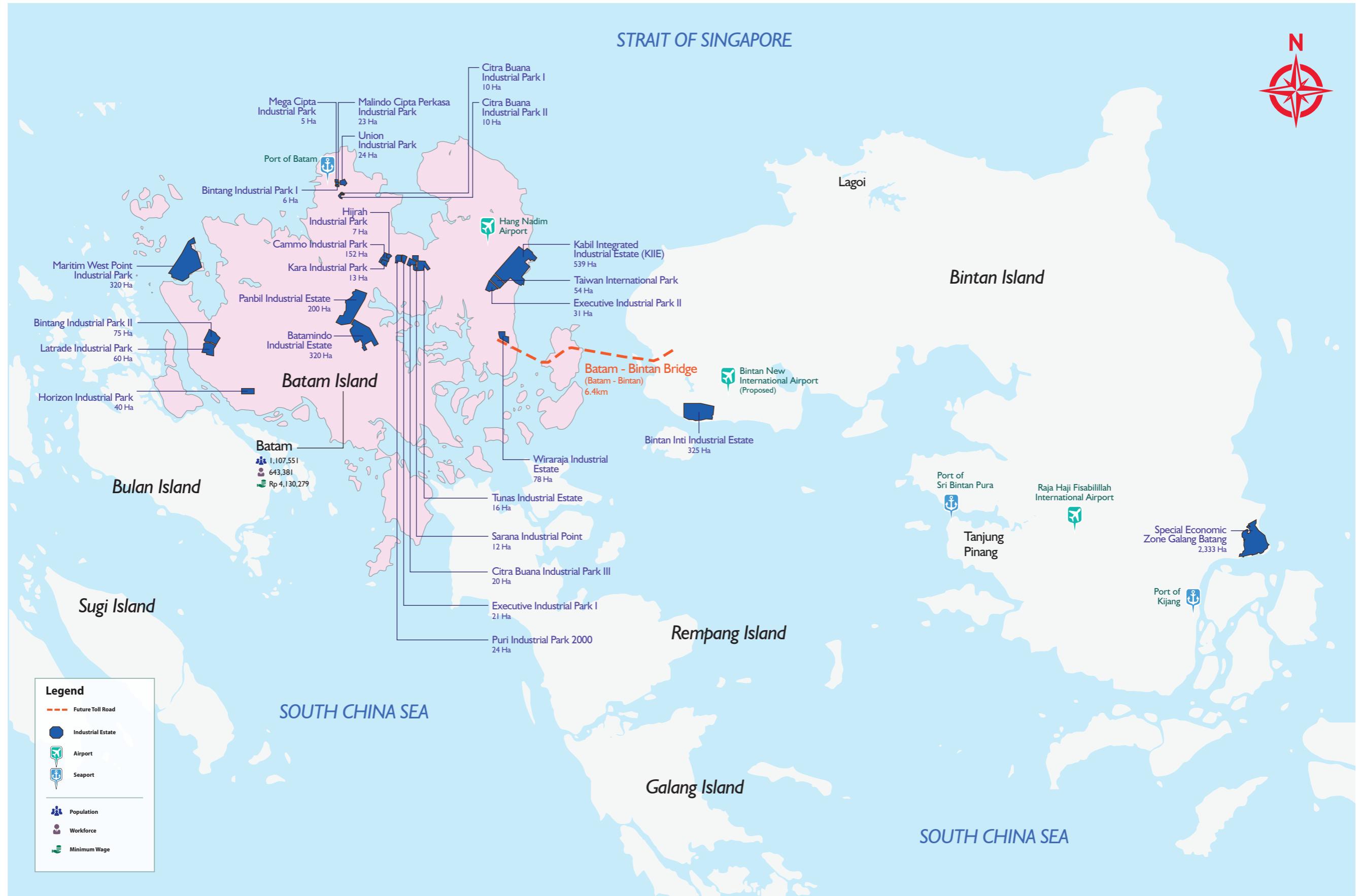


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Base Map : <https://kfmmap.asia/>

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Map of Greater Batam Industrial Estates

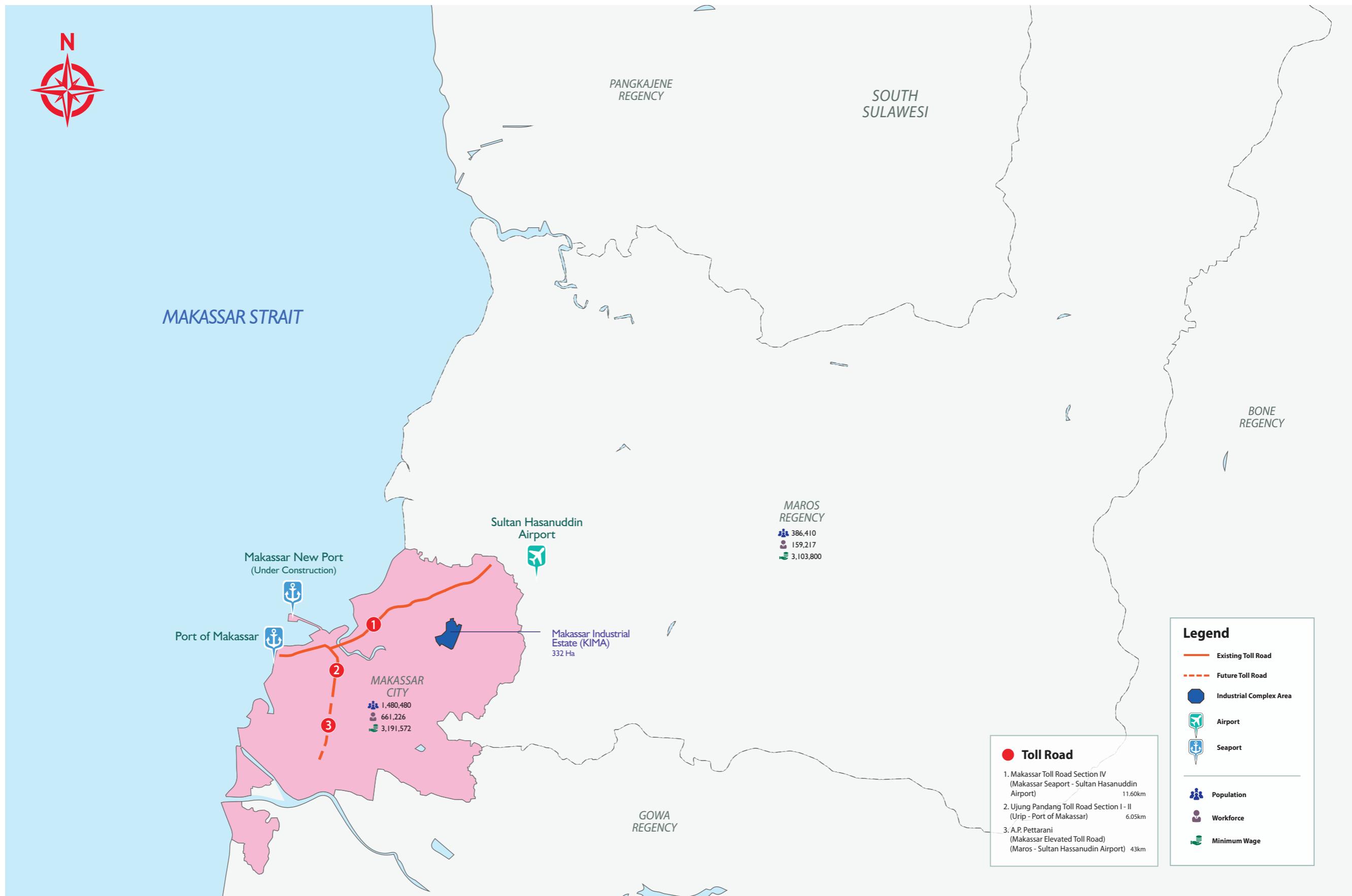


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Base Map : <https://kfmap.asia/>

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Map of Greater Makassar Industrial Estates

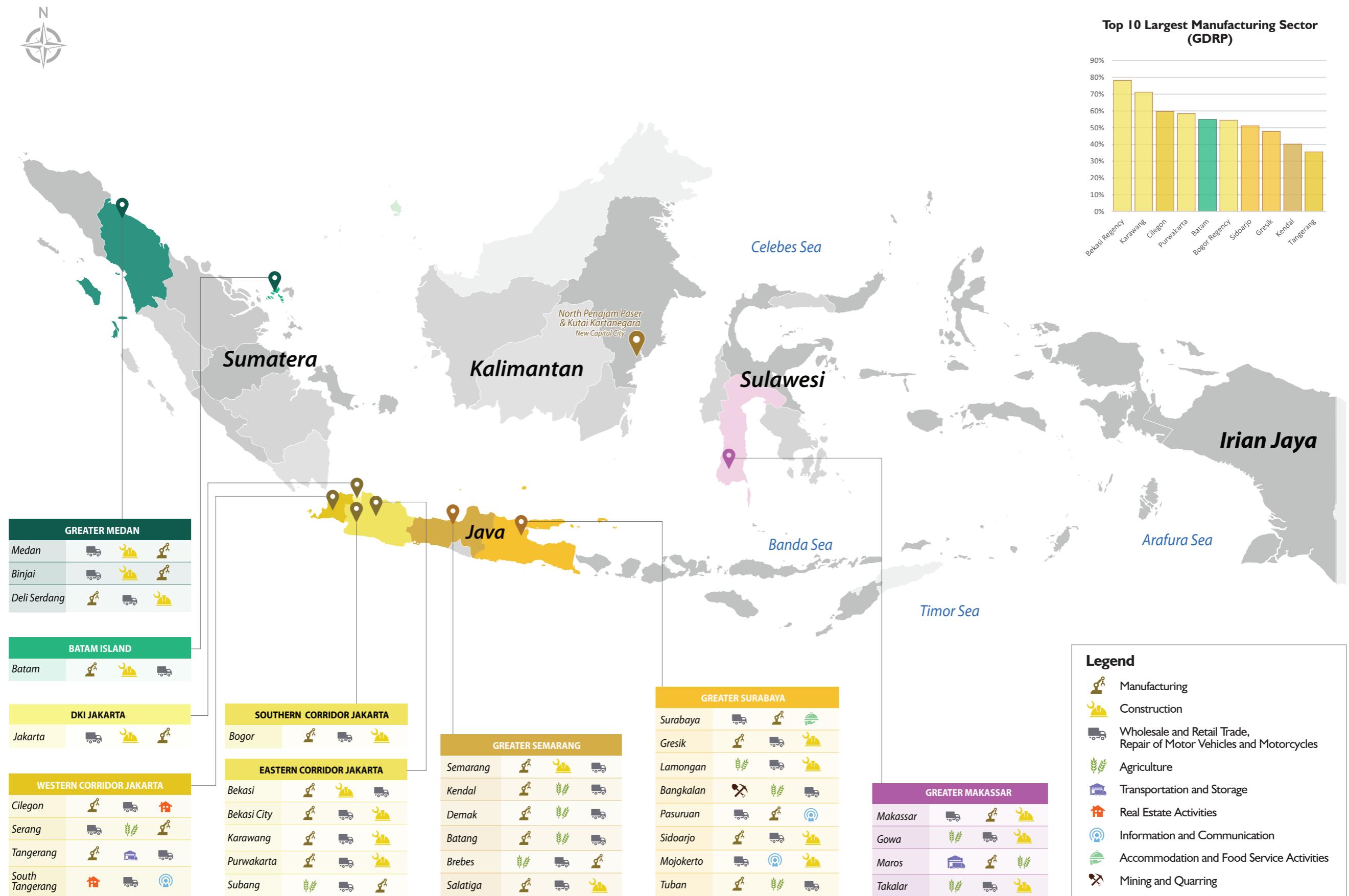


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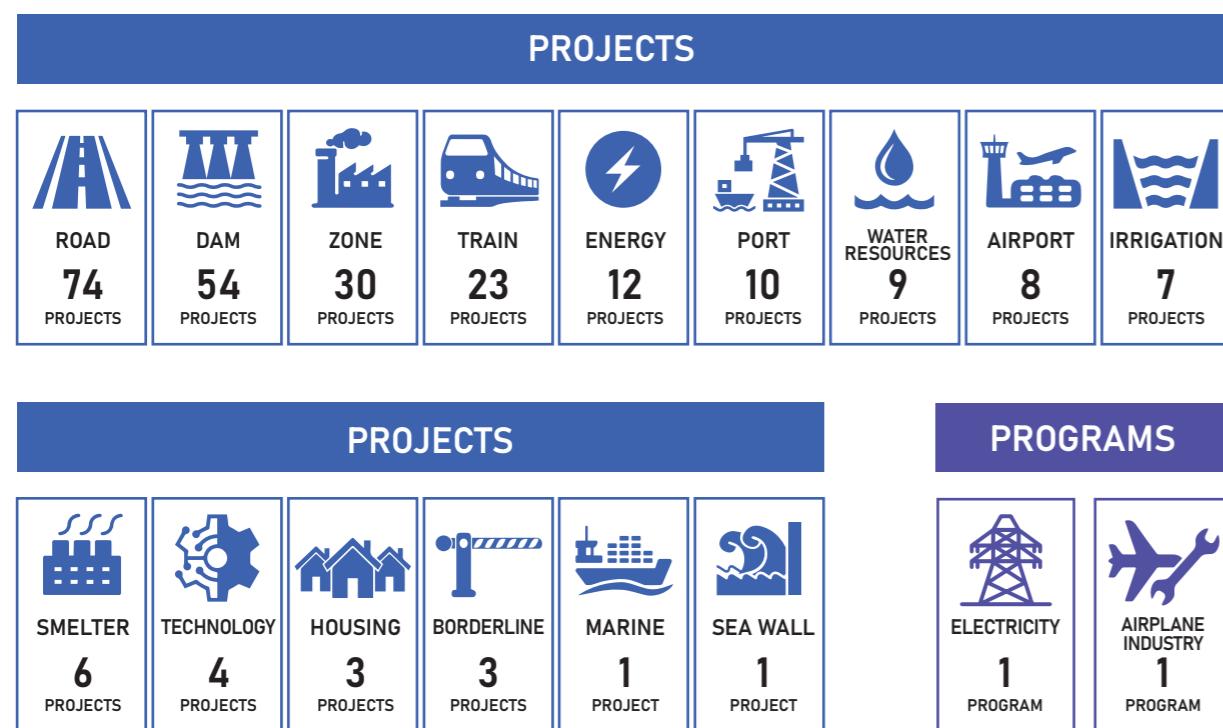
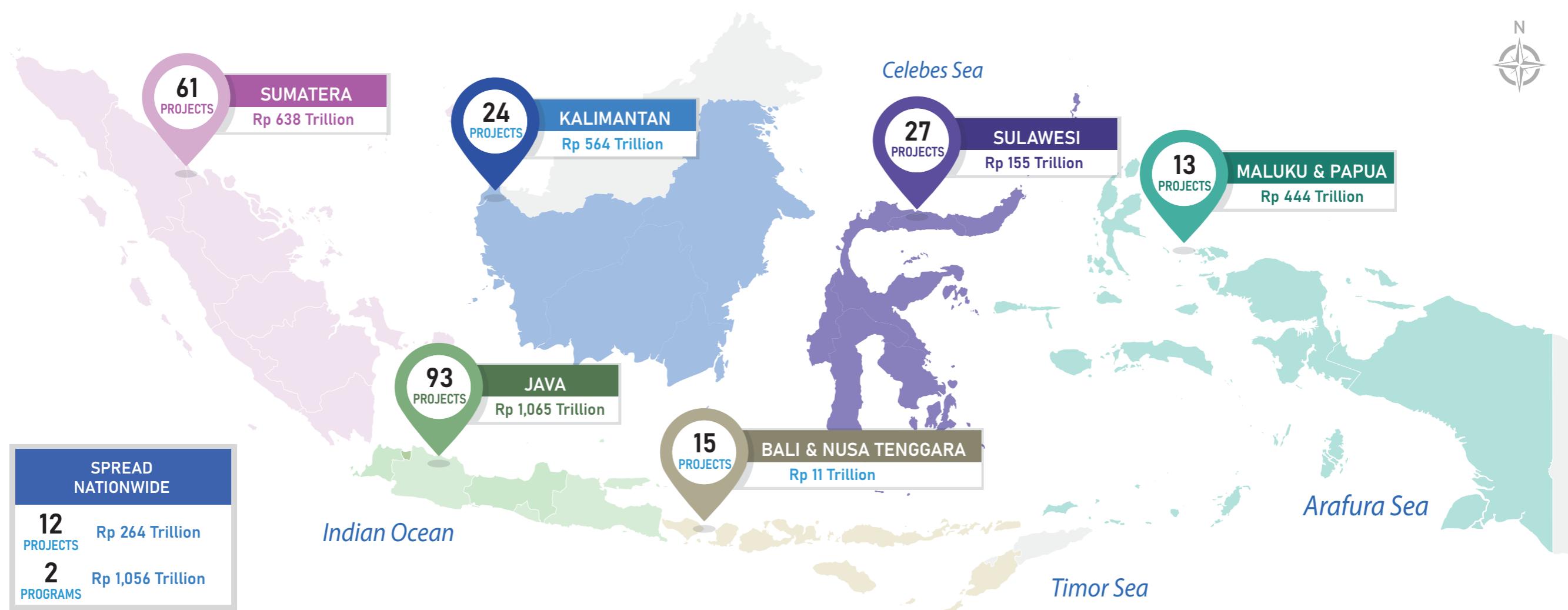
Map of Top Largest GDRP by Business Sector in Indonesia Major Industrial Estates Location



Source: Indonesia Central Bureau of Statistics (BPS) 2020

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Map of National Strategic Projects



Infrastructure Development Plan (RPJMN 2020-2024)

Sector	National Development Budget (APBN)	Local Development Budget (APBD)	State-Owned Enterprises (SOE)	Private (BUMN)	Total (Trillion)
Roads	133.3	-	-	-	336.3
Railways	25.4	-	-	-	70.0
Sea Transports	7.2	-	-	-	143.0
Air Transports	7.7	-	-	-	7.7
Land Transports	-	-	-	-	-
Urban Transports	-	-	-	-	118.8
Electricity	1.1	-	-	-	1.1
Oil and Gas	5.2	-	18.8	19	743.8
Information and Communication Technology	45.2	-	-	-	483.2
Water Resources	77.9	15.6	-	-	123.4
Clean Water and Sewage	79.1	1.7	-	1	155.5
Public Housing	109.3	109.2	28.0	237.5	655.5
Urban Development	15.7	-	111.4	176	540.3
Total Infrastructure Spending	507.1	126.5	158.2	433.5	3,378.6

Source: The Committee for Acceleration of Priority Infrastructure Delivery (KPPID) 2020

Terms of Transaction

Industrial Land / Building Sales	
Sales Price	In Rupiah; It does not include 10% VAT, charges of maintenance, clean water consumption, waste water, connection fees of clean and waste water, electricity, telephone, building permit, transfer of title fee, applicable transaction taxes, levies and duties.
Down Payment	Up to 20%; Subject to negotiation.
Balance of Payment	Generally, within One Month from Down Payment; Subject to negotiation.
Handover and Construction	Allowed after 100% Payment and the Signing of the Binding Agreement for Sale and Purchase Agreement (SPA/AJB). Subject to negotiation.
Cost of the Deed of Sales & Purchase	Buyer is responsible.
Building Permit License	Buyer is responsible.
Any future expenses, utilities charges and fees in accordance with the prevailing Rules and Regulations	Buyer is responsible.

Service Charges, Operating Costs, Repairs and Insurance	
Service Charges, Operating Costs, Repairs and Insurance	Rupiah per sqm per month; Typically for premises within estate, service charge is quoted in Rupiah per square meter land size per month.
Utilities Payment	Electricity and Gas are separately metered. Clean water and waste water are charged separately.
Car Parking	No specific parking charges; Generally, free parking.
Internal Repairs	Tenant is responsible.
Repairs of Common Areas (Lobby, Lifts, Stairs)	Not applicable.
External/Structural Repairs	Landlord is responsible.
Building Insurance	Landlord is responsible.
Overtime Charges	Not applicable.

Disposal of Leases	
Tenant Subleasing and Assignment Rights	Subject to prior written notice and landlord's approval.
Tenant Early Termination Rights	Only by break clause (not common).
Tenant's Building Reinstatement Responsibilities at Lease End	Original condition, allowing for normal wear and tear.

Source: Knight Frank Indonesia/ PT. Willson Properti Advisindo

Single-Factory Building (SFB)

Rental Payments	
Base Rentals	In Rupiah/sq-m/month. Rents are usually quoted as net of service charges and other outgoings.
Typical Lease Terms	Minimum of 2 years.
Frequency of Rent Payable (In Advance)	Paid in advance, some annually.
Typical Rental Deposit	3 months gross rental (base rental) paid as Security.
Tenant Statutory Rights for Renewal	Can be accommodated as Option to Renew, subject to prior written notice to the Lessor and Lessor's approval.
Basis of Rental Increases or Rental Review	Unless an option to renew and renewal cap is agreed at the outset and specified in the lease, rental increment upon renewal will be based on prevailing market rents.
Frequency of Rental Increases or Rental Review	Open market rental venue or pre-agreed levels.
Basis of Service Charge Increases or Review	Government Regulations on changes of manpower costs, fuel prices and increment of other costs related to industrial estate operations.
Frequency of Service Charge Increases or Review	Normally on annual basis, but subject to changes of Government Regulations on costs related to industrial estate operations.
Tenant Improvements	SFB's are offered on as-is basis, typically equipped with small office on the mezzanine floor. Normally no tenant improvements are required.
Building Signages	Tenant is responsible.



Lippo Cikarang Industrial Estate



RELEVANT LEGAL AND REGULATORY FRAMEWORK

RELEVANT LEGAL AND REGULATORY FRAMEWORK

(A) Brave New World

Indonesia's Government has been increasingly robust in its attitude to attract foreign investments over the past decade. The country has been steadily rising in its ease-of-doing-business rankings in recent years as a result of changes to the country's infamous unending and unrelenting bureaucracy which has now been better streamlined and digitised.

There have also been calls from the business community for more public-private partnerships, particularly in the digital sector where regulatory framework and innovation may not always be synchronised. The Government's restructuring of its state-owned enterprises may thus be seen as an indication in realising its statement, though a clear direction has yet to be established. Nevertheless, the digital economy remains poised to be country's saving grace amidst the recession and the digital economy is expected to grow at a substantial rate moving forward, in particular during the "new normal era" and it is still expected to grow beyond that.

Historically, natural resources have always been central to Indonesia's economy, and given the current changes to the global sentiment on environmental practices, the Government have adjusted its practices and aims to develop other capabilities in both conventional industries and innovative technologies, with a particular focus on becoming a major manufacturing hub.

Whilst it's still a 'new day', the sheer potential of business opportunities in Indonesia cannot be ignored, and it is simply a matter of acquainting oneself to what may be Indonesia's entry into a new era in its desire to be an economic power in Asia.

(B) Legal and Regulatory Framework

This beautiful archipelago is still in its nascent stages of growth if examined from a global perspective. Revisions to the foreign investment regulatory framework have been and will foreseeably continue to be a careful balancing act, so as to manage protecting local businesses and assuaging socio-political and concerns.

On 5 October 2020, the Legislation Body of the House of Representatives of the Republic of Indonesia (DPR) and the Indonesian Government agreed to pass the Omnibus Bill on Job Creation ("Omnibus Law"). This has been officially signed by President Joko Widodo on 2 November 2020. Whilst the event has been heralded by its proponents to be a momentous achievement, the hitherto referred to balancing act shines through and the business community remains cautiously optimistic.

For the uninitiated, the Omnibus Law revises more than 70 existing laws and regulations and promises to simplify business permits and land acquisition processes as well as ease foreign ownership requirements, and would regulate many provisions in various industry sectors. It seeks to strengthen the economy of Indonesia by creating jobs, increasing competitiveness and making it easier to do business in Indonesia. This will also be covered below where various key takeaways relevant to the industry sector will be explored.

The Omnibus Law, whilst being the most recent, is not the only change that has occurred. Despite the many changes over this decade alone, the effects are only being seen and felt on a relatively moderate scale. Importantly, the conventions of past residual bureaucratic irregularities are still being felt, hindering certain due processes which would otherwise be relatively straightforward from the contemporary outlook. This is mostly felt in due diligence matters where physical attendance to searches are still required, and reliance on results may not be assumed without additional confirmation and/or verification. However, the changes that have occurred have mostly been positive and well received by the business community.

It may be pontificated that change is not without difficulties and challenges. It must be reiterated that Indonesia is in an interesting transitional stage where its evolution trajectory is yet to be determined and greatly subject to its various aptitudes, attitude and adaptability in realising its ambitions.

I. Introduction:

In President Joko Widodo's inauguration speech upon being elected for a 2nd term in 2019, the domestic and international community were informed of what to expect in the next 5 years. Strategic focus will be placed on the following which includes but not limited to (i) maintaining infrastructure development, (ii) developing human resources, (iii) simplification and reduction of bureaucracy, regulation and red tape, and (iv) wean off the country's extensive reliance on natural resources and transitioning to become a manufacturing hub complemented with accessibility to modern services.

It is worth noting that leading up to the unfortunate advent of the global pandemic, the country's manufacturing PMI was on an upward trajectory from October 2019 to hitting a record high in February 2020. Whilst there was a natural decline in the beginning of the second quarter of 2020, PMI figures from June 2020 onwards shows a recovery from April and May due to the relaxing of the PSBB/lockdown restrictions. Nevertheless, the current Government administration has maintained a staunch resolve for economic recovery by way of increased spending and various fiscal and tax incentives.

Apart from Governmental support, the regulatory framework for foreign investments in Indonesia has also made great strides in the past 5 years, culminating in a considerable increase in the world rankings for ease of doing business. With the passing and enactment of the Omnibus Law, this upward trend will likely be maintained, which should boost domestic economy productivity and encourage foreign investments.

Whilst the above backdrop provides for a relatively suitable environment for investments, it also important for foreign investors contemplating relocation or diversification of supply chains to possess, at the very least, a working understanding of the existing legal framework, and not simply from a checklist perspective of what is required. This would prove exceedingly advantageous in the medium-to-long term as the narrative, once immersed and rehearsed, shall unwrap perspectives of opportunities.

RELEVANT LEGAL AND REGULATORY FRAMEWORK

In addition to the political and legal considerations as mentioned above, there is also the social aspect which must be discussed. Being acquainted with the local culture and understanding social demographics enables practical solutions to be implemented by legal means, and prevent mismatch of expectations, unnecessary disputes, and avoidable hindrances.

The three cornerstones as laid out above shall be the focus of this article, where valuable insights, knowledge, and experience will be dispensed to readers to arm and equip them in setting up for success and to thrive in Indonesia.

Ia. The Omnibus Law – Relevant Outlook on Foreign Investments and Employment

The passing and enactment of the Omnibus Law has been a long-drawn battle for the President Joko Widodo's administration, and fulfils a promise made by the President at the start of his second term in office in 2019.

The Omnibus Law was originally scheduled to be passed in Q1 of 2020, though providence dictated otherwise with the regrettable events of the global Covid-19 pandemic. Despite the delays, the President remained determined that this new law is part of a much needed economic and social recovery, in particular to address the increasing unemployment figures in the country, and hence its namesake. This has led critics from various interest groups to question the thoroughness and true beneficial qualities. The business community are dumbfounded as to the absence of consultations, and unions felt threatened that the changes will result in a drastic disadvantage for them and their members. Regardless of one's view on the new laws, it is here to stay and ergo imperative to understand how it affects one's business.

We have compiled below a summary of some key aspects of the Omnibus Law structured to the relevancy of this publication.

(i) Foreign Investments

The Omnibus Law comprises of provisions for the relaxation of foreign investment regulations in Indonesia, as the President's administration had promised.

First and foremost being the revision of infamous "Negative List" within the next 3 months and it is expected to see more business sectors open to foreign investment. There shall also be the introduction of prioritised business sectors, where fiscal incentives and non-fiscal incentives may be provided. These should prove exciting for business sectors previously hindered by foreign ownership restrictions of various lines of businesses.

Market entry details shall be further expounded in Section 2 "Important Legal Aspects to Consider" of this publication.

Notwithstanding the above, the current Negative List does allow 100% ownership in most business sectors and we hope that after the aforementioned revision has been completed, more sectors will be open to 100% foreign ownership thus making Indonesia a more attractive investment destination.

(ii) Manpower

The revisions to Indonesian's Labour Law may be said to be the Omnibus Law's most controversial component, and have exposed the polarity within the existing sphere of industrial relations. The spirit of the revisions was founded on job creation, and as a corollary, make Indonesia's workforce more competitive against regional or global standards.

Various changes have been made, *inter alia*, the certainty of fixed-term employment, streamlining of compensation payments for termination of employment complemented with a less cumbersome process, and the extension of overtime hours allowed.

In the employment of foreign workers, it would seem that the Indonesian government have heard the strong sentiments of the foreign business community in the application of work visas. Under the provisions of the Omnibus Law, foreign shareholders of a company, members of the board of directors or board of commissioners of the company may be exempted from requiring an approval from the Ministry of Manpower for the utilisation of foreign workers.

(iii) Ease of Doing Business

Foreign businesses wishing to invest in Indonesia shall also be categorised according to risk levels, and be issued permits accordingly. Moreover, more permits will be designated under the ambit of the Online Single Submission system ("OSS") and issued electronically. This provides a higher degree of certainty with minimal human interaction. Meanwhile, various permits that were required prior to the Omnibus Law have also been made obsolete due to their antiquated purpose, with the Omnibus Law revoking the relevant regulations requiring such permits (e.g. revocation of 'Nuisance Permit').



RELEVANT LEGAL AND REGULATORY FRAMEWORK

2. Important Legal Aspects to Consider:

A. Establishing a Presence and Basic Compliance

Establishing a presence in Indonesia, whilst mainly procedural, requires a broad range of considerations within the parameters of the following which includes without limitation to Law No. 25 of Year 2007 on Capital Investment (“**Investment Law**”), Law No. 40 of Year 2007 on Limited Liability Company (“**Company Law**”), and Presidential Regulation No. 44 of Year 2016 (“**Negative List**”).

1. Limited Liability Company

Whilst there are other forms of legal entities available, foreign direct investments in Indonesia may only be in the form of a limited liability company (*Perseroan Terbatas Pananaman Modal Asing*, or a “PT PMA”). The **PT PMA** will require a minimum paid-up capital of IDR 2,500,000,000 (Rupiah Two Billion and Five Hundred Million), save for specific line of business which will require a higher amount as per statutory requirements. In addition, the PT PMA will also need to commit to an investment amount of more than IDR 10,000,000,000 (Rupiah Ten Billion) per line of business.

The Company Law requires a minimum of 2 shareholders, and have a dual board structure, namely the board of directors, and board of commissioners, where the former is executory in function, whilst the latter, supervisory in nature. Foreign nationals may populate the boards and there is no expressed requirement for an Indonesian board member unless the particular portfolio is HR related (say, HR director). However, and be that as it may, having a local Indonesian on the board of directors will help and ensure an efficient operation of matters in the event other directors are based overseas.

Another important point to take note of is the Negative List, which regulates foreign the shareholding limitations (if any) according to the business activities of the PT PMA. Under the current Negative List, foreign shareholding is not restricted (i.e. 100% foreign owned allowed) for activities such as but not limited to, property development, manufacturing and trading. It cannot be stressed enough that choosing the right business activities with reference to the Negative List is of paramount importance to foreign investors.

However, as mentioned in the aforementioned section on the Omnibus Law, substantial changes are expected to be implemented by way of a Presidential Regulation in Q1 of 2021. No doubt foreign investors, existing and potential, await with bated breath.

2. Representative Office

Given the substantial fiscal commitment required for a PT PMA, many foreign investors consider establishing a Foreign Representative Office (“**RO**”) to get acquainted with the Indonesian market and explore opportunities, as the establishment of a RO does not require any capital injection.

However, as a RO is simply an ‘extension’ of its parent company, it is itself not a legal entity and as such is prohibited from generating revenue and may only conduct marketing and promotional activities of the trade or services of its parent company. Nevertheless, the RO option is the most economically efficient way to establish a presence in Indonesia without the need to commit to the various investment and paid-up capital amounts that are applicable to the PT PMA as raised above.

3. Procedures in setting up a PT PMA or a RO in Indonesia

The procedure in establishing a presence in Indonesia has never been simpler. The new approach taken by the Indonesian government focuses on enabling foreign investment companies to be provided with the core company documents such as the Deed of Establishment (incorporating the Articles of Association) (“DOE”), company tax documentation, and business licences as soon as possible. This would take around 1 week to complete, barring any unforeseen circumstances.

Apart from the DOE, most permits and licences are now obtained via the integrated OSS, which generally issues licences within 24 hours, barring any unforeseen circumstances.

4. Post-Incorporation Compliance

Indonesia is heading towards greater corporate governance, and as such foreign investors will need to pay greater attention in adhering to basic compliance matters such as, inter alia, monthly and annual tax filings, mandatory manpower and facilities reports, investment activities report, and registration of the national insurance programmes for employee welfare and healthcare.

For easy reference, the above may be easily compartmentalised into three categories, namely Core, Fringe, and Specific:

Core:

In connection with your legal entity, such as tax compliance, business identification, business licence, and import licence.

Fringe:

Certificates for employee welfare and healthcare insurance, environmental permit, manpower and facilities reports.

Specific:

Technical licences/permits and allows and enables the legal entity to undertake or perform a specific activity and/or is required due to the sector/industry. These include applicable regional licences.

In addition, it is worth paying attention to certification requirements from secondary authorities in relation to machinery certificate, structural approvals etc.

Whilst the above may seem somewhat cumbersome, familiarisation of the same from the outset will provide a cleaner understanding of the basic compliance activities required.

RELEVANT LEGAL AND REGULATORY FRAMEWORK

5. Joint-Ventures (“JV”)

It may at times be advantageous to have a partner (local or otherwise) in Indonesia, though it is vitally important who your partner is. This may sound somewhat obvious but experience has constantly shown that this needs to be further emphasised and underscored to new foreign investors.

The importance of the quality of documentation securing and regulating the relationship between the partners should not be in any way diminished. One of the most common excuses that have been bandied by foreign investors is that commercial relationships may be affected, where a ‘lack of trust’ is implied. From a professional perspective, clarity, precision, and lucidity are the key markers to commencing a promising JV relationship that would minimise risk of future disputes and consequently, hefty legal fees.

Conducting due diligence (“DD”) of your potential part should therefore be pursued as one of the first (if not the first) courses of action in forming a JV. Meanwhile, it is not absolutely necessary on every occasion to conduct a comprehensive and exhaustive DD on your potential partner. The extent of the DD will depend on subjective variables unique to each case, and nevertheless to be further assured and relied upon by formalised representations and warranties if required. Other legal considerations would include repatriation of funds and issues pertaining to majority/minority circumstances.

All good things will come to end at a specific stage, as the proverb goes, and as such it is also essential to contemplate exit mechanisms prior to entering into a JV with your potential partner. Far from being a prophecy of doom or a show of bad faith, the clarity and certainty manages expectations and enables for assurances to be provided, if necessary and within reason.

6. Acquisition of, or Subscription of Shares in a PT Company

Naturally, this option does not promise the comforts of total control that is available when incorporating a new company. However, it does have some benefits in that the foreign investor will, as it were, ‘hit the ground running’, so long as the foreign investor is cognisant of the facts and have accepted the state of affairs of the target company at the time of transaction.

Again, conducting DD is an absolute necessity, though extent of which could be tailored to the foreign investor’s requirements, be they positive or negative, so that a commercial decision can then be made with all the facts known.

In the acquisition exercise, there are several legal considerations to take note of. As there will evidently be a change in control of the target company, this will trigger various manpower implications under the law, in addition to addressing claims from existing creditors, if any. On the assumption of satisfactory DD and no prevalent issues on the any fronts, the sale and purchase documents will need examining, particularly a Conditional Sale and Purchase Agreement (**PPJB**) where condition precedents to be fulfilled may be explicitly listed. Completion, on assumption of satisfying of all necessary conditions, may be formalised in a notarised Sale and Purchase Deed (**AJB**) in accordance with the Company Law.

For the subscription of shares process, this could be perceived as a ‘JV-with-extra-steps’, where the foreign investor will need to take note of the various matters raised above and to prepare an acquisition plan in accordance with the requirements under the Company Law. This process will reduce tax exposure for the existing shareholders in the target company which may be a key factor in the commercial realm.

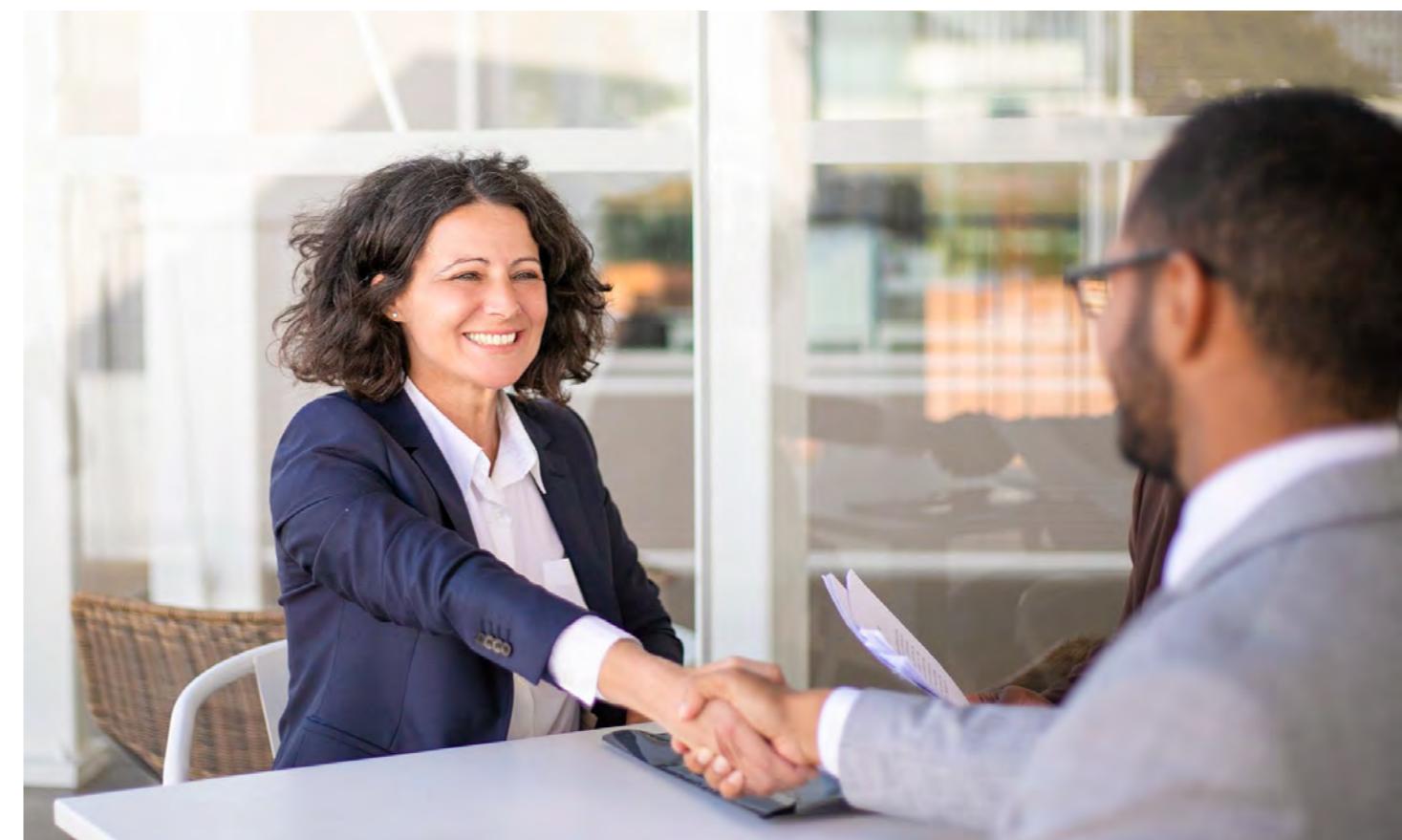
7. Alternatives to Consider

Depending on the nature of operations and objectives of the foreign investor, direct investment by way of a PT PMA or establishing a RO may not be applicable. As such the foreign investor may consider shifting source materials to Indonesia for cost efficiency.

Key points to take note of under such a structure would be the various documentation governing the cross-border relationship between the foreign company and its Indonesian OEM. Language, governing law, and dispute resolution being the most prevalent aspects to consider in this cross-border transaction.

In addition to the above, it is pertinent to take note of the various intellectual properties (“IP”) in the OEM transaction and ensure that proper and prudent steps are taken to protect the same under the law. To protect such IPs, it is not necessary for a foreign company to have a subsidiary in Indonesia as the said entity can be apply for registration of IPs with the Indonesian Directorate General of Intellectual Properties under the current regulatory framework.

Moreover, apart from registration of the IPs, it is worth to consider putting in place various OEM documentation which includes license agreement to further protect the interest of the foreign investor.



RELEVANT LEGAL AND REGULATORY FRAMEWORK

B. Acquisition or Leasing of Real Estate

From an objective perspective, there are no clear advantages either way in acquiring a plot of land or leasing from a land owner or industrial estate. The subjective commercial objectives of the foreign investor will determine which of the aforementioned option would be most suitable. In acquiring or leasing, there will be obstacles to circumvent and hurdles to negotiate.

Whilst Indonesia has taken significant strides in terms of digitising bureaucratic procedures, not all facets have been graced with such change. DD processes involving searching of land titles or court searches on corporations or individuals are still done by way of manual submission to the relevant authorities covering a specific jurisdiction at this point in time hence it is therefore with little surprise that general feedback mainly points to a regrettable compromise in time and cost efficiency by foreign investors. Nevertheless, Indonesia's predicted rise to prominence in the digital economy by 2025 and the digitization efforts undertaken by the current administration may prove to be of some comfort. Moreover, the enactment of the Omnibus Law includes the digitalisation of the spatial/-zoning maps to ensure a smooth and hassle-free DD process in due course.

Land title ownership in Indonesia is regulated under Law No. 5 of Year 1960 ("Agrarian Law"), with various implementing regulations, including but not limited to Government Regulation No. 40 of Year 1996, and Government Regulation No. 24 of Year 1997.

Principally, under the Agrarian Law, the highest level of title is the Freehold Ownership Right, or *Hak Milik* ("HM") title, which may only be held by Indonesian nationals. Other land titles includes but are not limited to Right to Cultivate (*Hak Guna Usaha*, or "HGU"), Right to Build (*Hak Guna Bagunan*, or "HGB"), and Right to Use (*Hak Pakai*, or "HP"), which can be directly or indirectly owned by foreign individuals. Each land title, with the exception of HM, has a definitive period of validity and renewal mechanisms and durations.

Once the land title of the target asset has been ascertained and confirmed, the foreign investor and their legal counsels will have a clearer line of sight of the path ahead and course of action to pursue. This would entail, inter alia, a DD process ensuring that the target asset is free from encumbrances, ascertaining the remaining validity period of the title, and preparation of documents for completion.

The leasing of real estate for operations of PT PMA will also require some extent of DD insofar as ascertaining the land usage designation (by the Indonesian Government), ownership of the land and property, including potential encumbrances and the remaining validity of the land title. As previously mentioned, certain DD process will require a level of cooperation from the lessors which is rarely unreasonably withheld. Naturally, the lease documentation be sans ambiguity and compliant under Indonesian law.

Foreign investors who wish to relocate or diversify their supply chains may also wish to obtain more information on Free Trade Zones, Special Economic Zones and other incentives in relation to land acquisition or leasing for factories and operations.

Meanwhile, foreign nationals may also be interested to learn that the Omnibus Law provides greater clarity and certainty when acquiring Strata Title property(ies) in Indonesia, insofar as previous 'restrictions' on applicable ownership title having been amended. However, ownership over HM titles (for landed property(ies)) are still unavailable to foreign nationals at this point in time.

C. Manpower Law & General Compliance

Having a sound understanding of Indonesian manpower law is one of the strategical advantages to operating smoothly in Indonesia, where cultural divides may be bridged and negate potential mismatch of expectations. It also allows the foreign investor to consider various courses of action to pursue, whether in incentivising or penalising members of the Indonesian operations.

The primary point to be raised in this section is that foreign nationals in the PT PMA are prohibited from holding portfolios/offices relating to HR (e.g. HR Director). In the event a foreign national will be based and working in Indonesia, he/she will first require a work visa and a stay permit ("KITAS") and must have an Indonesian employee present and the foreign national take on a "passive or observer" role. Note that the application for a KITAS will require local employees to fulfil certain requirements as prescribed under the law.

In particular for labour-intensive industries, having a competent HR executive in Indonesia is strongly recommended insofar as achieving and maintaining a healthy level in an intercultural performance target metric.



RELEVANT LEGAL AND REGULATORY FRAMEWORK

Whilst Indonesian manpower law does explicitly list the minimum provisions to be stated in employment agreements, it is strongly recommended that other provisions included are clear and detailed to ensure parties to the agreement have a shared understanding to avoid potential disputes arising out of misunderstandings. Additionally, there must also be a translation of the employment agreement in the Indonesian language, and governed by Indonesian laws.

Apart from the above, there is a mandatory social security program (BPJS Ketenagakerjaan and Kesehatan) in which the PT PMA will need to enrol its employees thereto. In addition, all employees will need to be reported to the Indonesian manpower office via the mandatory manpower/WLK report.

If there are 10 or more employees, the PT PMA will need to issue a company handbook which will need to be registered with the Indonesian manpower office as well.

With regards to general corporate compliance, the PT PMA will need to file 4 investment activities (LKPM) reports every year to BKPM, in addition to the various technical reports which needs to be filed to the relevant and various Government Institutions, in particular those at the Regional Government level.

Such reports are administrative in nature and although the contents can be technical in nature, it should be a straightforward and easy process. In particular that in light of digitalisation efforts, some reports can be submitted online and we expect more Institutions to adopt this approach in the near future.

Environmental protection is one of the priorities of the current administration hence it is vital for the PT PMA to secure the environment permits as prescribed under Law No. 23 of Year 2009 which includes without limitation to (i) AMDAL (environmental impact analysis), (ii) UKL-UPL permit and (iii) Izin Lingkungan permit.

The Omnibus Law does streamline the application process for the aforementioned environmental permits to provide certainty to the foreign investors.



3. Incentives from the Indonesian Government

As the Indonesian government is unwavering in its assertion of the Archipelago as an attractive investment hub in South-East Asia, there is a veritable assortment of incentives available to foreign investors.

Industrial-specific incentives are available in special economic zones, with facilities such as Bonded Zone (“**BZ**”) (Minister of Finance Regulation No. 131/PMK.04/2018 and Director General of Customs and Excise Regulation No. PER-19/BC/2018), including a multitude of concessions in the realm of taxation such as tax holiday, tax allowances, VAT waivers, and postponement of import duties. Labour-intensive investments have also been categorised to enjoy net income reductions.

Research and Development, and human resource skills development have also recently been granted eligibility for various incentives viz. gross income reduction, though naturally certain criteria have to be fulfilled, such as for example, assessments by the government of the R&D activities to determine if they are advancing the national economy, pioneer industries or technologies, or the transfer of innovative technologies that is foreign to local businesses.

For export-oriented industries, the BZ facility is an attractive option as it provides the following benefits to an investor, (i) suspension of import duties and waiver of VAT levies, (ii) waiver of levies on sales tax for luxury products, (iii) waiver of excise on the import of specific goods or raw materials and/or machines used in the manufacturing process.

For foreign investors who intend to implement an assembling line of business, an incentive similar to the BZ will be that of the facility of Ease of Imports for Export Purposes (“**KITE**”). Unlike the BZ facility where importation of semi-finished goods or raw materials are not allowed, this will be allowed under the KITE facility in addition to the waiver of excise on the import of machines used in the assembling process.

4. Understanding the Local Culture

Most foreign nationals who have been to Indonesia in seeking adventure or restful introspection have often discovered that Indonesians are generally heart-warmingly welcoming. It has also been said that there is a strong sense of communal sentiment thriving within Indonesian society, be it on the beachfronts or deep in the jungles.

Foreign investors can find Indonesia to be rather frustrating, if they are superimposing and are unable to acquaint and adapt to the local culture. In commercial settings and human resource management, the communal sentiment is also ever present and pervades through the rich fabric of cultivating relationships. Bridging the cultural divide is of utmost importance in running a smooth and orderly operations in Indonesia.

Confrontational approaches should be avoided, though it may be necessary in certain circumstances with the involvement of an intermediary, if possible. In the Indonesian context, commercial disputes should always, in the first instance, be resolved amicably and driven by the principles of good faith, which is also enshrined in Article 1338 of the Indonesian Civil Code.

RELEVANT LEGAL AND REGULATORY FRAMEWORK

The presence of legal counsel for disputes in Indonesia may, more often than not, be construed as a declaration of hostilities, and may be difficult (though not impossible) to backtrack for an amicable conclusion. That is not to say that one should not consult with an Indonesian legal professional, for it is certainly useful to be advised on not only the law but the various approaches to be adopted in obtaining a win-win scenario.

Whilst Indonesia has the largest Muslim population in the world, it is also a multi-religious society and foreign investors are advised to be considerate and respectful of the different belief systems prevalent in society.

5. Common Pitfalls to Avoid

This closing segment will highlight several common pitfalls to avoid based on the collective experience of foreign investors in Indonesia. Whilst some of these may seem trivial or under the purview of common sense, it is strongly advisable to review these again when contemplating investing in Indonesia.

(i) Best Market Practice vs The Law

Indonesia's gradual proliferation as an investment destination has resulted in an undesirable vortex caused by its reputation for leniency in days of yesteryear, and the shift towards good corporate governance and compliance that are also echoed on a global scale.

As a result, there are competing voices with more or less equal credibility and validity, which causes a great deal of confusion for foreign investors who are new to Indonesia. Nevertheless, it is strongly advised that foreign investors obtain independent legal advice to ensure that they are fully apprised of the relevant laws and regulations prior to making any major decisions.

(ii) Avoiding Mismatch of Expectations

Very often, there lies a gap of understanding between parties, especially if the terms are negotiated verbally and agreed upon based on a 'promised' or handshake. Definitive agreements are strongly advised and recommended to be put in place from the outset to formally record the understanding of agreed terms between parties to avoid any misunderstandings that will most likely have a detrimental effect.

(iii) Importance of IP Protection

IP registrations in Indonesia may require a substantial time to obtain and the Indonesian IP registration system adopts a "first to file" concept. As stated in above paragraphs, a foreign company may register an IP without having a legal entity in Indonesia and it is advisable to do so if such IPs will be used in the Indonesian transaction.

(iv) Nominees and Trust Structures

Nominees and trust structures are unilaterally prohibited and not recognised under Indonesian law, even though there may be underlying documents such as a declaration of trust, as these will be rendered void and unenforceable.

Article 33 of the Law No. 25 of Year 2007 on Investments also prohibits the entering into of agreements or statements which assert that share ownership in a limited liability company is for and on behalf of another person. Such agreements are void and unenforceable.

(v) Language of Indonesian Agreements

It is required under Law No. 24 of Year 2009 on the National Flag, Language, Emblem and Anthem for all agreements in Indonesia to be in the Indonesian language. In the event a foreign entity is party to an agreement, a translation of the foreign language may be included. The recent issuance of Presidential Regulation No. 63 of Year 2019 ("PR 63/2019") allows for the governing language of agreements to be at the discretion of contractual parties so long as a foreign party is involved, though the definition or extent of involvement by the foreign party is not expatiated in the aforementioned law and regulation. Therefore, it is possible for parties to agree on which language will prevail to the extent that the law is silent on the same.

(vi) Use of Rupiah Currency

In general, Bank Indonesia Regulation No. 17/3/PBI/2015 stipulates that the Rupiah currency must be used to settle most commercial transactions, save for exceptions in transactions such as international commercial trade (i.e. purchase of goods/services directly from a foreign vendor or service provider).

In the event parties require the inclusion of a foreign currency, say for example, nominal value of shares in a JV company between a foreign entity and a local Indonesian entity, the exchange rate has to be stated in the definitive agreements and the constitutional documents of the JV company at the time of incorporation.



RELEVANT LEGAL AND REGULATORY FRAMEWORK

(vi) Spousal Consent

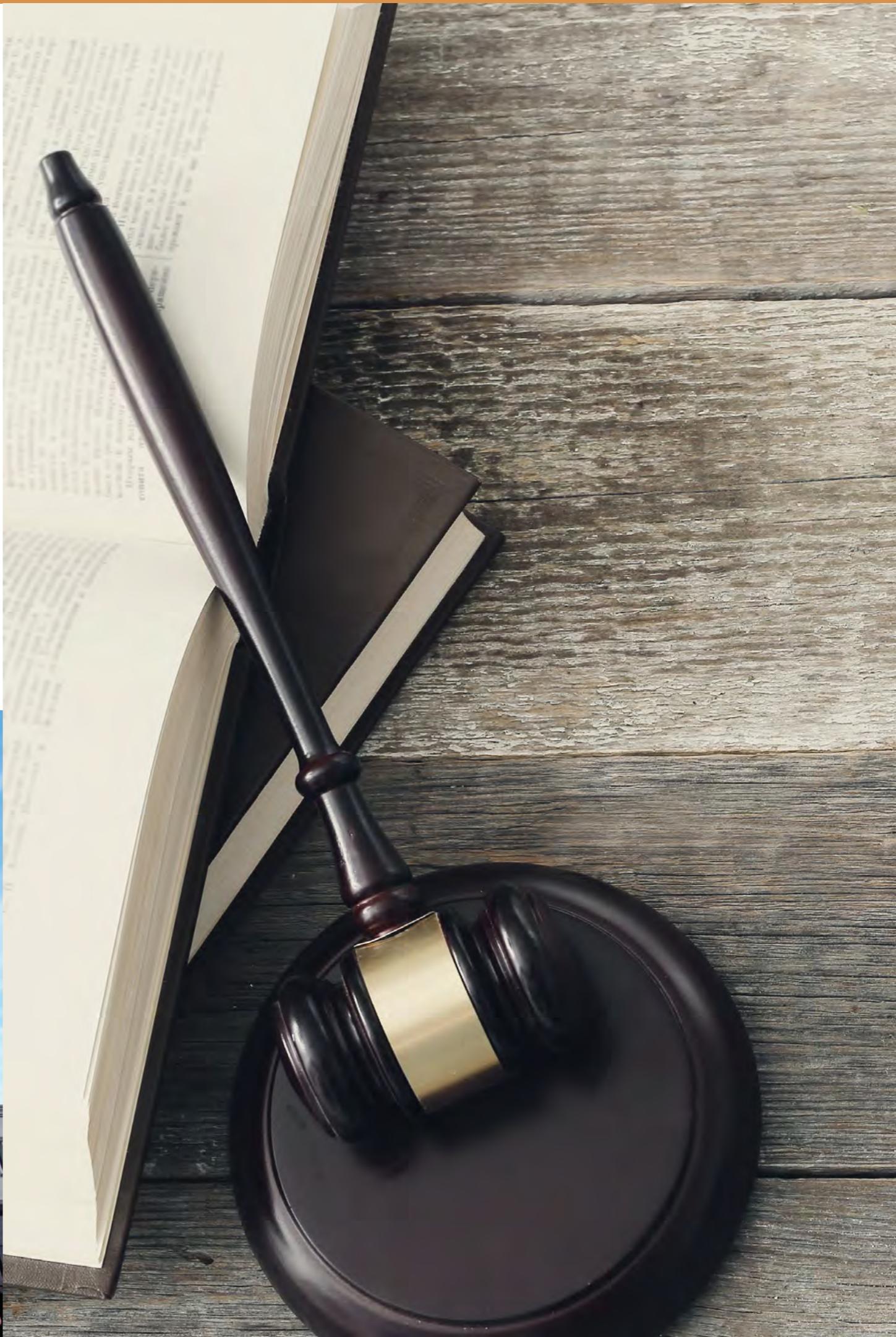
Under the rule of communal property under Law No. I of Year 1974, spousal consent will be required for most transactional documents, including (without limitation) lease agreements, sale & purchase agreement, deed of transfer, mortgage, pledge and personal guarantee if the signatory is a natural person and is legally married in accordance with the law.

The DD process, as mentioned above, will in most cases ascertain the marital status of contracting party(ies). In the event spousal consent is not obtained where required, the transaction may be challenged. A general rule of thumb is to first ascertain the nature of transaction and if such transactions necessitates spousal consent by contracting party(ies).

6. Closing

This a crucial period of transition for Indonesia in its ambitions to become a manufacturing power and a digital hub in Asia. The Indonesian government has clearly outlined its targets and executed various actions to safeguard and improve the country's 'soft' and 'hard' infrastructure.

Indonesia certainly abounds in opportunities for foreign investors, though the experience of their investment sojourn in this beautiful Archipelago will be defined and shaped by their understanding of the local laws and cultures in establishing an agreeable equilibrium with the existing ecosystem.





**TAX
INFORMATION**

BASIC GUIDE TO INDONESIAN TAXATION

No.	Topic	Content
1	Overview of tax system and types of taxes in Indonesia	Understand the overall tax system in Indonesia including its legal basis and types of taxes relevant to Indonesia
2	Withholding tax system in Indonesia and common pitfalls to avoid	Understand withholding tax obligations as the system is unique compared to regional peers
3	Mitigate tax risk - understand the basic tax compliance obligations in Indonesia	Description of basic tax compliance requirements in Indonesia including initial registration, monthly and annual tax compliance
4	Customs duties and taxes	Understand the customs system in Indonesia and types of taxes payable on importation
5	Tax incentives in Indonesia and focus sectors	<ul style="list-style-type: none"> • Tax incentives currently available in Indonesia, their scope and criteria, and mechanism for application • Highlight sectors that which are the key object for tax incentives
6	Expatriate tax compliance and planning	<ul style="list-style-type: none"> • Description on scope of income taxable for expatriates working or residing in Indonesia, rates, personal reliefs available and opportunities for tax planning
7	Establish tax efficient structure for shareholding and financing	<ul style="list-style-type: none"> • Understand key tax considerations for setting up tax efficient structure • Options for offshore holding company
8	Highlights of international tax issues in Indonesia	<ul style="list-style-type: none"> • A series of international tax issues that are relevant for MNCs or investors conducting cross-border transactions
9	Key tax reforms and impacts brought by Omnibus Law on Job Creation	<ul style="list-style-type: none"> • Discuss key changes brought upon by Omnibus Law on Job Creation to current tax laws and system

Overview of Indonesian Tax System and Types of Taxes

I.I Introduction

Since the time of the silk road trade, Indonesia has been the centre of exchange for goods, cultures and ideas. Indonesia has thrived owing to its strategic location on the equator with access to Indian peninsula, China, South East Asia as well as Australia. With abundance of crops and minerals both inland as well as in the territorial waters surrounding the vast number of islands, Indonesia has always been blessed with resources.

A relatively stable political environment coupled with a large workforce of young and technically capable citizen makes it a very lucrative proposition. The consumer demand has been increasing consistently over the years with a sustained urbanization and higher purchasing power than ever. Through its vast land and a large domestic market, Indonesia offers significant opportunities to the foreign investors.

The tax system here is unique and despite sounding more complex than some of the neighbouring countries, has been able to attract foreign investment consistently over the years.

Whilst Indonesia's tax-to-GDP ratio has been sitting at low point – lower than the marks of its South East Asia neighbours, such as Singapore, Malaysia and Thailand, the government of Indonesia has been granting incentives, lowering tax rates and improving its tax system to make it more attractive to foreign investors.

During the first half year of 2020, whilst the pandemic had just began to hit the country socially and economically, the government of Indonesia pushed forward and passed the law for reduction of corporate income tax rate – the corporate income tax rate was reduced from 25% to 22% and eventually 20% from 2022 onwards. A series of tax incentives were also introduced by the government to help businesses including foreign-owned corporates to cope with the impacts of the pandemic.

Indonesia offers numerous tax incentives to foreign investors, from tax holidays to tax allowances, to super tax deduction, and geography specific zones aiming at export-oriented businesses. The government is currently working on expanding these incentives further and consolidate them to provide more convenience and greater legal certainty to foreign investors.

On 2nd November 2020, the President of Indonesian signed the long-awaited Omnibus Law on Job Creation, marking a new chapter of Indonesian legal system reform. The reform involves amendments to several tax laws. With the purpose to promote investment, provide justice and equality to foreign investors, and encourage voluntary compliance, the tax cluster of Omnibus Law is viewed and appraised widely as it opens a new era for foreign investment and the country's economy.

Amid the rapid societal changes, coupled with the Omnibus Law enactment, Indonesia's tax system is set to evolve quicker than ever, as it seeks to streamline certain bureaucratic process and operate in a more efficient manner. With a raft of legislative, regulatory, and administrative changes currently under way to reform the existing tax system, Indonesia is ready to welcome more foreign investors to step foot into this archipelago of opportunities. Investors looking to set up a business presence in Indonesia are encouraged to understand the tax system here, its potential upcoming changes, assess the tax implications and opportunities available to them and optimise various models at both investment and operating level to realise growth, seize efficiencies and control risks.

1.2 Indonesia Tax System

In general, Indonesia tax system is on self-assessment basis - taxpayers are given responsibilities to calculate, pay, and report their own taxes in accordance with prevailing tax laws and regulations, and the tax authority - **Directorate General of Taxation (DGT)** act more as an auditor and controller. Self-assessment system applies to mainstream taxes which are regulated centrally by the government such as income tax and Value Added Tax (VAT).

Official assessment system whereby the taxpayers' payment would entirely depend upon assessment by the Tax Office, also exist - but it applies to local level taxes such as Land and Building Tax (*Pajak Bumi dan Bangunan / PBB*), Duty on the Acquisition of Land and Buildings (*Bea Perolehan Hak atas Tanah dan Bangunan / BPHTB*) and Vehicle Tax (*Pajak Kendaraan Bermotor / PKB*).

Indonesia implements a **withholding tax system** as its mechanism to collect income tax revenue - various activities and transactions of payments are subject to withholding tax in Indonesia whereby third parties are required to deduct or collect taxes from payees and deposit them to the tax authority.

The fundamental pillars of Indonesia tax system are built under (i) Income Tax Law, (ii) VAT Law, (iii) General Tax Provisions and Procedures (*Ketentuan Umum dan Tatacara Perpajakan /KUP*) Law, (iv) Stamp Duty Law, and (v) Regional Taxes and Retribution (*Pajak Daerah dan Retribusi Daerah / PDRD*) Law.

The mechanism for the government to implement nation-wide tax laws is primarily through issuance of Government Regulations, Ministry of Finance (MoF) regulations, and the DGT regulations and/or circular letters, whereas PDRD is implemented through issuance of local regulations (*Peraturan Daerah*)/(PERDA) by regional and local governments.

1.3 Main Types of Taxes

1.3.1 Income Taxes (*Pajak Penghasilan/PPh*)

- Income tax is levied in Indonesia based on central government law, i.e. no provincial or local taxes on income is applicable in Indonesia.
- Unlisted entities¹ are subject to a flat **Corporate Income Tax (CIT) rate of 22%** rate on their taxable income². The rate of 22% was freshly reduced in 2020 - prior to this, the CIT rate was 25%. The CIT rate will be further reduced to 20% from 2022 onward.
- Small and Medium Enterprises (SME) with annual turnover of no more than IDR 4.8 billion are subject to final income tax at 0.5% rate of gross turnover for the first three years since incorporation.
- Concessionary tax rate is available for SME in general with annual turnover of less than IDR 50 billion. that is, in the form of a 50% discount on standard CIT rate on taxable income in proportionate to the part of gross turnover up to IDR 4.8 billion.
- Income derived from certain business activities or transaction, such as, construction, shipping, and rental or transfer of land and/or building, is **subject to final income tax** at different rates as stipulated by the regulation.
- Entities in certain fields are subject to special CIT regime such as oil and gas contractor, and foreign drilling companies.
- The individual income tax rate in Indonesia is on progressive basis ranging from 5% to 30% depending on the individual's income bracket – please refer to Section 6 of this guide .

- Income tax in Indonesia is primarily collected through a withholding tax mechanism - please refer to Section 2 of this guide.

1.3.2 VAT (*Pertambahan Pajak Nilai or PPN*)

VAT is a form of indirect tax, imposed generally **at the rate of 10%**, on delivery of taxable goods and services by VAT registered enterprises (*Pengusaha Kena Pajak / PKP*).

Registration as a PKP is mandatory if the taxpayer derives an annual taxable turnover of more than **IDR4.8 billion**. Taxpayers that do not meet such annual turnover threshold can also choose to register as a PKP on voluntary basis. PKP will need to impose VAT for its delivery of taxable goods and/ or services whilst it can claim VAT incurred for purchase of goods and/or services for business purposes.

The reverse charge mechanism of VAT ("Self-Assessed VAT" or "Offshore VAT") is applicable in Indonesia on payment to overseas services provider. Entities in Indonesia are required to pay and report the Offshore VAT, regardless of whether they are PKP or non-PKP.

1.3.3 Luxury Sales Goods / Sales Tax on Luxury Goods (*Pajak Penjualan atas Barang Mewah or PPnBM*)

PPnBM is a Sales Tax imposed on luxury goods - it is levied **in addition to VAT** and imposed on goods classified as luxury either manufactured in or imported into Indonesia.

PPnBM rates are currently ranging **between 10% to 125%**. The scope of objects that are subject to PPnBM primarily comprise **motor vehicles, luxury residences, aircrafts, and luxury cruises**.

1.3.4 Regional and Local Taxes

Regional and local tax are divided into two groups: (i) tax collected by province, such as motor vehicle tax, motor vehicle fuel tax, cigarette tax, and (ii) tax collected by city or district, such as hotel tax, restaurant tax, entertainment tax, advertisement tax, street lighting tax. Most of these taxes are considered consumption taxes and not creditable.

2. Withholding Tax (WHT) System and Common Pitfalls to Avoid

As described above, WHT is essentially a mechanism used by the DGT to collect income taxes. In implementing the WHT system, **Indonesian government appoints all registered taxpayers** to withhold tax for making certain payments to either resident or non-resident of Indonesia ("Tax Withholder").

Taxpayers new to Indonesia may often neglect such obligations due to lack of knowledge regarding WHT and ending up having to pay income tax on behalf of their vendors (due to not deducting the WHT from the payments made) and subject to additional penalties (due to late payment and filing). Therefore, investors having entity or business establishment in Indonesia is encouraged to seek tax consultation for WHT implication before making any payments to the vendors.

¹ Including group of persons and/or capitals constituting a single unit whether carrying on business or not, including limited liability company, limited partnership, other company, state-owned enterprise or regional government-owned enterprise in any name and form whatsoever, firm, commercial partnership, cooperative, pension fund, partnership, organization, foundation, mass organization, social-political organization, or other organizations, institution, and other forms of entity, including collective investment contract and permanent establishment.

² All expenses related to obtaining, maintaining and collecting the income, are treated as deductible expenses when calculating taxable income.

The WHT system are governed under the Income Tax Law and comprise the following in general:

2.1 Article 21 WHT (PPh 21)

The PPh 21 is applicable when companies make **salary payment and other compensation to their employees, or other services related payments to non-employee individuals**, who are Indonesian tax resident.

The PPh 21 rate conforms with individual income tax rate. The rate will be **20% higher** if the individual does not have an Tax Identification Number (*Nomor Pokok Wajib Pajak / NPWP*).

2.2 Article 22 WHT (PPh 22)

PPh 22 is triggered by **importation of goods and local purchase of certain commodities and goods** by certain buyers (e.g. the purchase of oil fuel by private gas stations, the purchase of cement by local distributors).

PPh 22 rate on importation of goods is in general at 2.5% if the importer has an Importer Identification Number (*Angka Pengenal Import / API*) or 7.5% without the API. The PPh 22 collected generally constitute as **prepayment** for the taxpayer's current year income tax liability.

2.3 Article 23 WHT (PPh 23) & Article 26 WHT / (PPh 26)

PPh 23 is WHT applicable for payments made to **Indonesian tax resident**, whereas PPh 26 is applicable for payments made to **non-tax resident of Indonesia**. Almost all types of payments except for purchase of goods, are subject to PPh 23 / PPh 26.

The WHT rate under PPh 23 is either at 2% or 15% depending on the nature of the payments. The rate will be **100% higher** if the income tax recipient does not have NPWP.

The WHT rate under PPh 26 is in general at 20% on gross transaction amount. However, there are certain transactions where the WHT rate is applied based on Estimated Net Income (ENI). For example, transfer of shares in an Indonesian non-listed entity will be subject to withholding tax at 20% on the ENI which is deemed to be at 25% of the sales amount – in this respect, the effective PPh 26 rate is therefore 5% (20% x 25%) of the gross transaction amount.

If the payment recipient is a tax resident in a jurisdiction / country which has a tax treaty with Indonesia, the withholding tax rates **may be reduced or exempted**.

2.4 Article 4(2) WHT (PPh 4(2))

Certain types of payments to / income derived by Indonesian resident taxpayers are subject to final income tax under PPh 4(2), such as transactions relating to land and/or building and construction services.

The PPh 4(2) rate for rental of land and/or building is at 10%, and transfer of land and/or building is at 2.5%. Construction services attracts WHT ranging from 2% to 6% depending on nature of the construction services and the contractor's qualification.

3. Tax registration, administration, and compliance obligations in Indonesia

3.1 Initial Registrations and Set-Up

Every taxpayer (regardless individual or corporate) in Indonesia is identified through their NPWP (Tax ID), registered with the DGT. Once a taxpayer has obtained NPWP, he/she needs to apply for the E-FIN(Electronic Filing Identification Number) in order to set up the online tax portal to conduct tax filing obligations and access to various digital tax services. In entities' cases, digital certificate is also required in order to conduct VAT compliance and PPh 23 filing.

Taxpayers having annual turnover exceeding IDR 4.8 billion are compulsory to register as a VAT-able Entrepreneur, i.e. *Pengusaha Kena Pajak / PKP*, with the DGT.

3.2 Indonesian tax compliance requirement, payment and reporting timeline

The routine Indonesian tax compliance primarily involves **monthly and annual compliance** comprising three categories of tax obligations:

(1) Withholding Tax, (2) VAT, and (3) Corporate Income Tax.

Transfer Pricing compliance requirements³ shall also be observed by corporate taxpayers conducting related party transaction or are part of a multinational corporation.

In general, the relevant timeline regarding tax payment and reporting which shall be fulfilled by entity taxpayer in Indonesia, can be summarised as follows:

Type of Tax	Deadline	
	Tax Payment	Tax Reporting
Monthly		
Art. 21		
Art. 23	By 10th of the following month	By 20 days of the following month
Art. 26		
Art. 4(2)		
Art. 25 ⁴	By 15 days of the following month	By 20 days of the following month
VAT	Before the deadline of reporting	By the end of the following month
Self-Assess VAT	By 15 days of the following month	By the end of the following month
Annual		
Art. 21	N/A	By end of the first month following the fiscal year end
CIT	Before the deadline of reporting	By 4 th month after the end of the fiscal year (e.g. for companies with financial year ended on 31 December, the deadline for CIT reporting falls on 30 April)
CbCr Notification	N/A	By end of the following fiscal year
TP Documentation	N/A	By the time of CIT Return filing (the summary of Master File and Local file shall be attached to CIT Return filing)

³ In the form of preparation of transfer pricing documentations comprising Local File, Master File and Country by Country Reporting (CbCr) reporting

⁴ Article 25 is monthly tax instalment that entity taxpayers need to prepay based on their prior year's income tax liability



Late payment or late filing penalties

- Interest penalties** will be imposed at **2% per month on the amount of underpaid tax**, capped at 48% (24 months) in the event of late payment⁵. Partial month, for example a single day will be considered a full month.
- One-off administrative penalty for late filing** include: IDR500,000 for monthly VAT return, IDR 100,000 for other monthly tax return, and IDRI,000,000 for CIT return.
- Failure to file a tax return by the relevant deadline may also result in the DGT to issue a **warning letter** to the taxpayer.
- The warning letter will typically require the taxpayer to file the tax return **within 30 days** of the warning letter date. Ignoring such a letter can prompt the DGT to **issue an official tax assessment** along with an administrative penalty of **50% of the assessed tax**.

3.3 Other general administration notes

Generally, books and records, including those on computers should be maintained in Rupiah and in the Indonesian language, and kept for a period of 10 years in Indonesia. PMA companies that prepare their financial statements in United States Dollar as the functional currency in accordance with Indonesian Accounting Standards may maintain English Language and US Dollar bookkeeping, subject to approval from Ministry of Finance.

For tax purposes, there is no statutory requirement for an audit of a taxpayer's accounts by a public accountant. However, if taxpayers do have an audited account, the Tax Office requires them to be submitted upon annual tax filing.

4. Customs Duties and Taxes

In general, importation of goods (whether capital or non-capital goods) into Indonesian customs area is subject to three types duties and taxes: (i) Import Duty, (ii) VAT, and (iii) WHT Art. 22 (PPh 22):

(i) Import Duty

- Import duty is calculated using **tariff rate multiplied by Customs Value** - Customs Value is the agreed price to be paid or will be paid by the buyer to the seller – the components include cost plus freight plus insurance. Tariff is based on Harmonized System Code as stipulated in the Indonesian Import Duty Tariff Book, generally ranging from 0%-15%.
- Import duty is considered a non-creditable / one-off cost for importers or buyers.
- The Indonesian government offers import duty relief, exemption, and/or deferral concessions to investors in order to promote the development of local and export-oriented industries. Please refer to later for relevant tax incentive brief.

(ii) VAT

- VAT is calculated using standard VAT rate of 10% multiplied by Import Value - Import Value is the Customs Value plus import duty.
- VAT on importation can be **treated as input VAT** (receivable / claimable), creditable against the output VAT by importer in Indonesia, if it is registered as a PKP.

(iii) PPh 22

- As described in Section 2 above, PPh 22 is payable upon importation as prepaid income tax of which taxpayers can claim it as credit upon filing of CIT return at the year end. Accordingly, similar to VAT, PPh 22 generally represents a cash flow issue for taxpayer rather than actual expenses incurred.
- Tax concession is available on exemption of PPh 22, if a company is subject to final income tax regime or it is suffering from commercial losses. Application to the DGT is required to obtain the exemption.

5. Tax Incentives in Indonesia and Focus of Sectors

Tax incentives in Indonesia can be broadly categorized into two types:

- Statutory incentives:** incentives which are stipulated under prevailing Income Tax Laws and can be obtained on self-assessment basis with no approval from government required, such as the SME incentive.
- Discretionary incentives:** incentives which are stipulated through issuance of Government Regulations with evaluation and review from BKPM and/or DGT, and approval from MoF required.

The discretionary incentives can be summarised into the following categories:

Income Tax related:

Type of Tax	Applicability	Benefits	Application
Tax Holiday Incentive	Investor who makes an investment with the minimum value of Rp100 billion in a pioneer industry ⁶	CIT reduction of 50% or 100% for 5 to 20 years, depending on the investment value	Apply to Ministry of Finance through OSS system for approval
Tax Allowance Incentive	Companies that invest in certain business sectors and/or regions ⁷ - 166 designated sectors and 17 categories of investment in designated sectors and also in designated regions are regulated as eligible	<ul style="list-style-type: none"> Reduction in net income of up to 30% of the amount invested, prorated at 5% for six years of the commercial production, provided that the assets invested are not transferred out within six years; Accelerated depreciation and/or amortisation deductions; Extension of tax losses carry-forward for up to ten years; A reduction of the withholding tax rate on dividends paid to non-residents to 10% (or lower if treaty relief is available). 	Apply to BKPM via OSS system for approval
Super Deduction Tax	<ol style="list-style-type: none"> Corporate taxpayers who provide internship or vocation training; Corporate taxpayers who conduct Research and Development ("R&D") activities in Indonesia; and Corporate taxpayers who are operating in labour-intensive industry 	<ul style="list-style-type: none"> Cost deduction up to 200% for vocational education Cost deduction up to 300% for R&D conducted in Indonesia Reduction in net income of 60% of the amount invested in the form of tangible fixed assets for labour-intensive industry 	Apply to DGT via OSS system for approval

⁶ Currently applicable to 18 pioneer industries with specific Standard Classification of Business Field (Klasifikasi Baku Lapangan Usaha/KBLI). Businesses outside the scope of KBLI can also apply through separate channel.

⁷ Certain industries, e.g., forestry, low rank coal for local consumption, geothermal power producer, oil refinery, chemical producer (limited to certain products), machinery and equipment producer, etc.
Certain industries in certain areas, e.g., fruit processing outside Jakarta, nickel processing companies building smelters located outside Java island, copper processing companies building smelters located outside Java island etc.

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(ii) Others:

Types	Scope	Benefits	Application
Geographic Area Specific Incentives and facilities	Integrated Economic Development Zones (Kawasan Pengembangan Ekonomi Terpadu/KAPET)	<ul style="list-style-type: none"> Non-collection of VAT and LST on importation of certain goods; Non-collection of Article 22 Income Tax on importation of certain goods; 	Apply to the specific regional government
	Bonded Stock Piling Area (Tempat Penimbunan Berikat/TPB) ⁸	<ul style="list-style-type: none"> Postponement of import duty on certain goods; 	
	Free Trade Zones (FTZs)	<ul style="list-style-type: none"> Exemption of excise on importation of certain goods; and 	
	Special Economic Zones (KEKs) ⁹	<ul style="list-style-type: none"> Non-collection of VAT and LST on the domestic purchases of certain goods. 	
	Industrial Zones (Kawasan Industri/KIs)		
Import Tax and Duties Facilities	Importers fulfilled certain criteria set under regulations	<ul style="list-style-type: none"> WHT import exemption Import duty exemption Non-collection of VAT / exemption on strategic goods Temporary Imported Goods BKPM Masterlist facility 	Apply to DGT or BKPM

Further, there are Tax Exemption and Drawback Facilities for Export Tax facilities under the scheme of ease of imports for the production of goods to be fully exported (*Kemudahan Impor Tujuan Eksport/KITE*) which comprise the following:

- KITE Exemption** - This exemption facility allows for most raw materials and sample goods to be imported without payment of import duty, provided that the finished products are exported. The VAT and/or PPnBM on such importations are not-collected either.
- KITE SME** - Further incentives are also available for small to medium enterprises, whereby the operational requirements are less stringent. The import duty, VAT and/or PPnBM exemptions are available on the importation of raw materials, sample goods, and machinery.
- KITE Drawback** - This drawback facility allows for the recovery of import duty paid on imported raw materials that are incorporated into finished products which are subsequently exported.

6. Expatriates' Tax Compliance and Planning

6.1 Basis of Taxation and Rates

A foreign individual is regarded as a tax resident of Indonesia if he/she fulfils any of the following conditions:

- He/she resides in Indonesia; or
- He/she is present in Indonesia for more than 183 days in any 12-month period; or
- He/she is present in Indonesia during a fiscal year and intends to reside in Indonesia.

⁸ Consist of Bonded Zone; Bonded Warehouse; Bonded Exhibition Place; Duty Free Shop; Bonded Auction Place; Bonded Recycling Area; and Bonded Logistic Centre.

⁹ CIT reduction facility is also available for new taxpayer with new capital invested in the production chain of main activities in KEK. Taxpayers being rejected for the CIT Reduction facility and taxpayers carrying out other activities in KEK, may apply for similar Tax Allowance under the Income Tax Concessions.

Expatriates who work and reside in Indonesia with valid work permit are also required to obtain NPWP in order for the employer to pay and report their PPh 21. Upon obtaining NPWP, expatriates will be subject to income tax as Indonesian tax resident similar to the locals.

The income tax for individual resident in Indonesia is on progressive rate basis as follows:

Taxable income	Rate	Income Tax - IDR
Up to IDR 50,000,000	5%	2,500,000
Above IDR 50,000,000 up to 250,000,000	15%	30,000,000
Above IDR 250,000,000 up to IDR 500,000,000	25%	62,500,000
Above IDR 500,000,000	30%	30% of the relevant amount

In general, personal tax relief available to individual tax resident includes the following:

Types	Tax Relief - IDR
Taxpayer (for single taxpayer)	54,000,000
Spouse (if applicable)	4,500,000
Each dependent (up to three)	4,500,000
Position allowance / occupational expenses (5% of gross income, maximum at IDR 500,000 per month)	6,000,000

6.2 Employer's Withholding Tax Obligations

Individual income taxes are collected mostly through withholding tax mechanism as explained in Section 2. Employers are required to withhold Article 21 income tax on **monthly basis** for salaries and other compensation payable to their resident employees – including both local and foreigners with valid work permit. Resident employees **without NPWP** are subject to a **20% higher surcharge** of withholding tax.

Compensation or payment to non-tax resident individuals is subject to withholding tax under Article 26 whereby the withholding tax rate is stipulated at 20% final. If there is existing tax treaty, such withholding tax may be exempted upon fulfillment of certain conditions.

6.2 Employee's Tax Obligations

Expatriates registered with NPWP are required to file annual individual income tax return, due by 31 March following the calendar year in which income is derived. In order to file annual individual income tax return, employer will need to provide individuals with withholding tax slip at the beginning of the tax reporting year with details of income and withholding tax made.

As individual income tax return needs to be filed electronically via online tax portal, taxpayer who has never filed income tax return previously needs to obtain E-FIN first to activate the log-in to the online portal.

7. Tax considerations including pros and cons related to shareholding structure and company structure (capital structure)

7.1 Tax consideration on shareholding structure

In determining a company's shareholding structure, tax considerations need to be reviewed and analysed primarily concerning **how the shareholder should hold the shares** in subsidiaries and from **which jurisdiction should the holding company be located**.

Tax efficient shareholding structure may be contemplated in order to optimize the effect of tax upon repatriation of dividends and transfer of shares in Indonesian company, i.e. exit strategy.

Indonesia currently has over **70 tax treaties**, each tax treaty encompasses different terms with regards to allocation of taxing rights between treaty country and Indonesia. Whilst treaty shopping is generally prohibited under Indonesian anti-avoidance rules, investor can nonetheless leverage on Indonesia's treaty network to the extent that it is practical and not in violation against any anti-avoidance provisions.

Repatriation of profits through dividends

As discussed earlier, distribution of dividends by an Indonesian company to a non-resident parent entity will be subject to **20% final withholding tax** in general. The 20% withholding tax rate can be reduced under relevant tax treaty depending on the specific terms. Therefore, before deciding a holding company of Indonesia entity, it is important to assess if the country or jurisdiction where the holding company entity is located has an effective and favourable tax treaty with Indonesia in place so that a reduced withholding tax rate can be applied.

Transfer of shares in Indonesian company

As discussed above, transfer of shares by non-resident shareholder in an Indonesian company will be subject to 5% effective withholding tax on the gross value of transaction. Such withholding tax may be exempted if there is existing tax treaty between the shareholder's resident country and Indonesia – the exemption will depend on the treaty provision, i.e. whether there is an Article on Capital Gain Taxes that allocates the entire taxing rights to non-resident's country or jurisdiction.

In case there is tax treaty available in which there is specific clause stipulating the taxing rights on capital gains on transfer of shares, the withholding tax may be exempted unless Indonesia is allocated with the taxing rights.

7.2 Tax considerations on capital structure

Indonesia implements thin capitalization rules whereby **debt to equity ratio ("DER") at maximum of 4:1** is applicable for income tax calculation purposes. In this aspect, if the ratio exceeds 4:1, the excess interest would not qualify as deductible expenses. Thin capitalization rules, however, would not be applicable for certain taxpayers, such as banks, financial institutions, oil and gas and mining operations under the contract, companies subject to final tax and infrastructure projects.

8. Highlights of International Tax Issues

Multinational corporations having establishment or business activities in Indonesia need to be aware of several international tax issues in light of the tax authority's efforts to tackle tax avoidance and compete for fair share of tax revenue attributable to Indonesia.

8.1 Permanent Establishment ("PE") Risk

Foreign entities without legal establishment in Indonesia may constitute a PE in Indonesia if they undertake certain degree of activities (such as having employees physically presence in Indonesia for more than certain period of time), or have certain forms of presence (such as having workshop, office, factory, etc.). The definition of PE is stipulated under the Indonesian Income Tax Law.

Where the foreign company is a resident in a country that has a tax treaty with Indonesia, the definition of PE may be different - usually there is a longer 'time test' for certain activities performed in Indonesia.

A PE is obliged to register with the DGT, and also required to be assessed for VAT registration, i.e. become VAT-able. Having a PE presence can often result in adverse tax consequence for foreign entities due to the potential applicability of 'force of attraction' rules and requirement to pay additional Branch Profit Tax at 20%, on PE's net profit after tax. The Branch Profit Tax may be reduced based on the applicable tax treaty.

8.2 Transfer Pricing Issues

Related party transactions are subject to transfer pricing requirements, i.e. transactions shall be conducted in accordance with arm's length principle. The DGT requires Indonesian taxpayers carrying out related party transactions to prepare transfer pricing documentation including Master File, Local File and Country by Country Reporting (CbCr).

From Indonesian transfer pricing perspective, there is no safe harbour rule available.

Related party transactions involving payment for intragroup services and royalties as these transactions have become the primary target of the DGT's audits. To successfully defend the commercial substance of the related party transaction and in avoiding double taxes, it is of utmost importance that the Indonesian companies develop and maintain a robust set of documentations to satisfy the benefit and arm's length test.

8.3 Anti-Tax Treaty Abuse

Based on Indonesia tax laws and regulations, non-resident income recipient may claim tax treaty benefits only if it satisfies certain requirements. These requirements are regulated under DGT Regulation No. 25/PJ/2018 ("PER-25") which aims to tackle tax treaty abuse by foreign taxpayers.

Pursuant to PER-25, to claim treaty benefits, non-resident income recipient shall furnish DGT Form to declare certain facts, as well as submit proof that it is a tax resident of the jurisdiction / country that has effective tax treaty with Indonesia. Based on the contents of the declaration, non-resident would not be entitled to benefit from a tax treaty if it is not the beneficial owner of the income and / or the transaction does not have economic substance and / or the transaction was motivated by reasons of taking advantage of the tax treaty.

8.4 Multilateral Instrument (MLI)

MLI is a multilateral treaty issued by the Organization for Economic Cooperation and Development (“OECD”) to implement treaty related anti-tax avoidance measures under its Base Erosion and Profit Shifting (“BEPS”) Project. Being one of the most revolutionary aspect of the BEPS Project, the MLI allows for inclusion of treaty related anti-avoidance measures in the existing tax treaties of participating jurisdictions (signatories) without the need for renegotiating each of the bilateral tax treaty separately – it needs to be applied in parallel to existing tax treaties and serves as an addition (like a protocol).

Indonesia is one of the 94 jurisdictions that have signed up for MLI. Indonesia’s MLI was ratified in November 2019 through the Presidential Regulation Number 77 Year 2019 and deposited with the OECD in late April 2020. The MLI was considered entry into force from 1 August 2020.

The key impacts of the MLI will be restriction on claiming of tax treaty benefits as MLI introduces the mandatory adoption of ‘Principle Purpose Test’ whereby tax treaty benefits will be denied if it is reasonable to conclude that one of the principal purposes of a transaction or arrangement is to obtain tax treaty benefit.

Multinational firms and investors conducting cross-border transactions with Indonesia should assess the implications and potential risk of their existing business structure being targeted.

8.5 Taxation of Cross-Border Digital Transactions

Indonesia, being one of the developing economies with 4th largest population in the world, is positioned to be impacted tremendously from the effect of digitalisation – Indonesia’s plan for taxing digital economy was initially included under proposed Omnibus Law. Following the COVID-19, it expedited the introduction and enactment of digitalisation tax through Law Number 2 Year 2020 (“Law No. 2 / 2020”).

The approach under Law No. 2/2020 in taxing the digital economy is to exert both Direct Tax (income tax) and Indirect Tax (VAT) obligations on foreign sellers, service providers and foreign e-commerce platform (“foreign digital players”) sourcing revenue through digital transactions from Indonesian market. Subsequent to Law No. 2/2020, the DGT issued implementing regulations (effective from 1 July 2020) on the VAT obligation part which requires foreign digital players to be appointed as VAT collector and fulfill VAT obligations if they meet the transaction thresholds set.

Whilst Indonesia had also proposed mechanism with regards to income tax imposition, it has not yet issued any implementing regulations to bring the new rules into effect. It is envisaged that implementing regulations relating to income tax obligation will be issued after global consensus is reached and delivered by OECD by the end of 2020.

8.6 Other General and Specific Anti-Avoidance Rules

Indonesia also has a series of anti-avoidance rules in place, embedded as part of its domestic tax laws to tackle taxpayers participating in unlawful tax avoidance. Although the enforcement standard and procedures of these rules are relatively ambiguous and sometimes debatable, it is expected that more resources from the DGT will be allocated in the near future to ensure a proper implementation system.



9. Key Tax Reforms and Impacts brought upon by Omnibus Law on Job Creation

Previously, the Ministry of Finance, through its issuance of regulation No. 77/PMK.01/2020 concerning its Strategic Plan during 2020 to 2024 period (“PMK-77”), has confirmed the reformation of a series of tax law package as part of its 19 draft legal umbrellas. Among others, Omnibus Law Bill and the Stamp Duty Bill are targeted to be completed by 2020.

Despite encountering a wave of controversy, the government of Indonesia pushed forward to enact the Omnibus Law on Job Creation through Law No. 11 Year 2020 (“Law No. 11/2020”) as it was formally signed by President Joko Widodo on 2nd November 2020 and became effective on the date of the promulgation. Meanwhile, the Stamp Duty Bill is enacted through Law No. 10 Year 2020 which will start to take effect from January 2021.

Under Law No. 11/2020, the tax provisions are included in Chapter VI - Ease of Doing Business in Part 7. The tax provisions consists of 4 Articles, namely Articles 111 to 114 involving changes to the Income Tax Law, VAT Law, KUP Law and Regional Tax and Retribution Law.

Here is a summary of key changes brought upon by Law No. 11/2020 / Omnibus Law to the current tax system:

TAX INFORMATION

Concerning	Key Changes	Concerning	Key Changes
Income Tax	<ul style="list-style-type: none"> The definitions of tax resident and non-tax resident of Indonesia are reorganised and given more certainty. Indonesian citizens that reside abroad for more than 183 days will be treated as non-resident if they fulfil certain requirements. Expatriates with dual tax residency and who reside in Indonesia beyond the 183 days time test will be deemed as resident. However, only Indonesian-sourced income will be subject to income tax. Non-Indonesian sourced income will be non-taxable while the Indonesian citizen is regarded as non-resident. Expatriates who possess certain skills can be exempted from income tax for a period of 4-year since they become Indonesian tax object. Indonesian-sourced dividends received by resident corporate taxpayers will be exempt from income tax with no minimum shareholding condition, whereas dividends received by resident individuals will be exempted from income tax if they are reinvested in Indonesia within a certain period of time Dividends and after-tax income from a Permanent Establishment abroad can be exempted from the Indonesian income tax as long as they are invested or used to support other Indonesian business needs within a certain period and meet the requirements¹⁰. The PPh 26 at 20% currently applicable to interest payments due to foreign taxpayers, in connection with a debt repayment guarantee, can be reduced through further Government Regulation. 	Tax Administration and Procedures	<ul style="list-style-type: none"> Administrative sanction for late tax correction and deposit is amended from 2% per month to become benchmark interest rate of Bank Indonesia (BI) plus 5% divided by 12 months. The tax administrative sanctions due on improper issuance of VAT invoices, or for not registering as a VAT-able Entrepreneur, will be reduced to 1% of the tax base. Taxpayers are given interest compensation in the event that an objection, appeal, or request for reconsideration is granted partially or in full, causing an overpayment of tax. The termination of investigation may be carried out if taxpayer has paid the tax debt or underpayment added with a fine of 3 times (previously 4 times) the amount of unpaid or underpaid tax.
VAT	<ul style="list-style-type: none"> Delivery of taxable goods by consignment is no longer included under the definition (deleted) Coal mining products are now subject to VAT – it is no longer included in the list of goods exempted from VAT. Input VAT incurred on the utilisation of goods/services prior to the VAT-able Entrepreneur delivers their first taxable goods and/or services will be creditable as long as the input VAT meets the crediting requirement – previously, only input VAT incurred on capital goods are creditable. Input VAT incurred on the utilisation of goods/services prior to the PKP registration will be creditable¹¹. Input VAT discovered during a tax audit process will be creditable. Additional information or details are required to be shown on the VAT Invoice issuance, i.e. Faktur Pajak by VAT-able enterprise. Relaxation on information required on Faktur Pajak issued by retail merchant to end customers. 	Regional and Local Taxes	<ul style="list-style-type: none"> The central government can regulate regional tax rates and levies in accordance with national fiscal policies. The central government also conducts an evaluation of regional regulations related to PDRB to test the suitability of the provisions of higher laws and regulations and / or national fiscal policies. <i>(Greater harmonisation of the tax rules. is the apparent goal of this change which is hoped to create a better business environment, spur investment and job creation but still maintain the ability of the regional governments to collect tax revenue.)</i>

¹⁰ Requirements include that the reinvested fund is at least 30% of the after-tax income / dividends, and that the foreign entities from which Indonesian taxpayer receives dividends are not traded in Indonesian Stock Exchange.

¹¹ Input VAT will be creditable up to a level of 80% of entity's taxable delivery.



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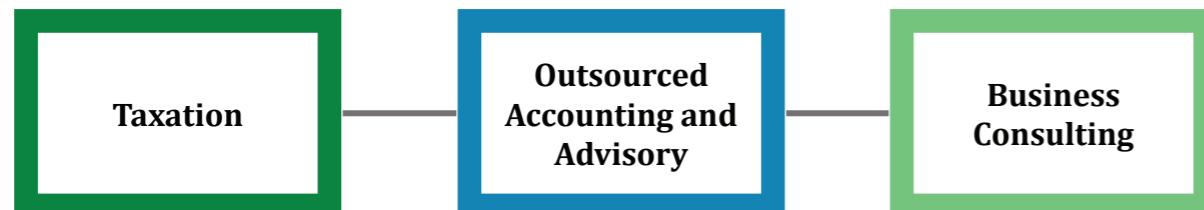
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