

Doing Business in Indonesia

2009



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1. Introduction

UHY is an international organisation providing accountancy, business management and consultancy services through financial business centres in over 70 countries throughout the world. Business partners work together through the network to conduct trans-national operations for clients as well as offering specialist knowledge and experience within their own national borders. Global specialists in various industry and market sectors are also available for consultation.

This detailed report providing key issues and information for investors considering business operations in Indonesia has been provided by the office of UHY representatives:

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Information in the following pages has been updated so that they are effective at the date shown, but inevitably they are both general and subject to change and should be used for guidance only. For specific matters, investors are strongly advised to obtain further information and take professional advice before making any decisions. This publication is current at June 2009.

We look forward to helping you do business in Indonesia.

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2. Business environment

Indonesia: A Brief Profile

Indonesia is located at the region of South East Asia dan Pacific with the income category “lower middle income”. It has a population with the amount: 225,630,065. GNI per capita (US\$): 1,650.

Indonesia is Southeast Asia’s largest economy. It has presented a high annual growth exceeding 6% in both 2007 and 2008. The expecting growth in 2009 is between 2% and 4.5%.

Indonesia has more than 237 million citizens, 50% of whom are under the age of 30.

The Indonesian GDP per person exceeds its Asian neighbours, such as the Philippines. Its GDP per person is three times than Vietnam. Indonesia is a group of democratic nations with significant regional autonomy. It is located on the world’s major trade routes and has extensive natural resources.

It is a top-ten market for U.S. agricultural products and within the top 30 overall markets for U.S. exports. Indonesia has ratified the Cape Town Treaty, which gives U.S. aircraft exporters access to financing through international protection and registration of financial interests.

Indonesia can be considered one of the richest countries on earth in terms of its biological diversity. The country is located between Asia and Australia, and comprises more than 17,000 islands that stretch 5,000 km from east to west. Because of its complex geographical make-up and unique bio-geographical position, Indonesia has enormous ecosystem diversity as well as a fascinating history and heritage.

In terms of human diversity, with more than 230 million inhabitants, the country ranks as the fourth most populous nation in the world and the third largest democracy. It is also the world’s largest Islamic nation, where a constitutional freedom to practice other religions sees major groups of Christians, Buddhists, Hindus and other faiths existing side by side. There are approximately 336 distinct recognised cultures that share more than 250 spoken languages. The lingua franca, Bahasa Indonesia, was adopted only 77 years ago and is now widely used throughout this vast land, serving as a means of communication and as a unifying factor.

Indonesia is diverse and is among the most culturally rich countries on earth. Add to this its enormous mineral, marine and natural resources and it is evident that it ranks as a major economic force in the region.

Following the economic and financial crisis that hit the country in 1997, the Indonesian government recognised the important role that foreign investment needed to play in the reconstruction of the Indonesian economy. During following years, successive governments enacted legal and regulatory reforms designed to make Indonesia a competitive destination for foreign direct investment.

Acceleration of Economic Growth and Trade

The Central Statistic Agency (BPS) announced that Indonesia's GDP grew 6.30% in 2007. Per capita income rose to IDR 17.6 million from IDR 15 million in 2007. Investment has increased from 35% in 2007 to 41% in first quarter of 2008. Meanwhile, net export increased by 14% in 2008 from 8% in 2007.

Batam Free Trade Zone (FTZ)

VAT and LST in Batam

For many years, there has been a particular treatment for Batam as a special BZ (bonded zone) with more VAT (value added tax) facilities than are awarded to ordinary BZs. The entire Batam area is still denominated as a special BZ. A company can only have a BZ status based on a specific MoF approval.

These Batam BZ companies are entitled to the same VAT (and customs) facilities as those granted BZ companies outside Batam. However, the VAT and LST (luxury of sales tax) in Batam are levied gradually on a selective basis on taxable goods and services purchased or consumed by Batam companies.

Currently, there are several taxable goods that has been imported and delivered in/to Batam companies and will attract VAT:

- Motor vehicles
- Cigarette and tobacco products
- Alcoholic drinks
- Electronic goods.

Since 1st January 2004, the utilization or consumption of foreign taxable services or foreign taxable intangible goods has been subjected to self-assessed VAT. Deliverances taxable services within or to Batam, as of 1st January 2006, have not yet attracted VAT.

The government decided against a proposal to turn the entire Batam Islands area into a single FTZ. Instead, it will specify bonded zones into which businesses can import goods duty free. The government also noted

that export businesses outside the bonded zones could still make use of bonded warehouses, as the status of the neighbouring Rempang and Galang Islands (the islands closest to Batam) has been decided by the government.

The Batam Authority, which governs Batam and has overseen its rapid economic development, argued that the bonded zone scheme would confuse investors and lead to local government workload. However, local authorities claimed that bonded zones would enable them to better govern Batam as mandated under Indonesia's decentralisation laws.

Legal System

Dutch Legal System plays an important role in influencing the history of Indonesian Legal System. The Nederland-Indies Government applies *concordantie* principle in the legal sector of Indonesian territory during colonial period. Based on this principle, literally every law that is passed by the Netherlands parliament would have some influence in the Indonesian territory a few years later if it is necessary with minor changes. When Indonesia became independent, its 1945 Constitution in Article II of the Transitory Provisions specifies that all laws and legislations existing under the Dutch colonial administration automatically became the laws and legislation of the Republic of Indonesia, until it is repealed, revoked, amended or found to be contradictory to the Constitution. As a result, the business regulations governing in Indonesia after independence remained the same as the legislation enacted in colonial times, such as parts of the Civil Code (*Burgerlijk Wetboek*), the Commercial Code (*Wetboek van Koophandel*) and the Bankruptcy Ordinance (*Faillissement Verordening*), until amended in by new laws introduced in 1960 -2004.

In the 1960s, the government of Indonesia ordained several laws intended to foster investment, such as the Basic Agrarian Law (Hukum Agraria) and the Foreign Investment Law (Hukum Penanaman Modal Asing). For the period of 1980 - 2000, the major overhaul of the laws governing Indonesian business practices resulted in the enactment of several more modern laws, such as the Mortgage Law, the Company Law, the Capital Market Law, the Bankruptcy Law, the Fiduciary Transfer Law, and the Arbitration Law as well as several Intellectual Property laws including laws on Copyrights, Patents, Marks, Industrial Designs, Integrated Circuits, and Plant Varieties.

Similarly, the rules governing commercial litigation procedures under Indonesian law are found in the Indonesian Civil Procedure Law derived from the Dutch colonial civil procedure codes (Herziene Indonesisch Reglement ("HIR") and Rechtsreglement Buitengewesten ("RBg")). The

Indonesian judicial system is organized into three levels. The lower court is the District Court (Pengadilan Negeri) established in all districts and municipalities (Kotamadya or Kabupaten) in Indonesia. The first appellate court is the High Court (Pengadilan Tinggi) established in all provinces in Indonesia. The highest court is the Supreme Court (Mahkamah Agung). Unlike common law systems, Indonesian civil law does not adhere to strict doctrines of precedent. Every case has to be determined on its own facts and merits. Meanwhile consideration is given to academic theories and prior decisions in similar cases, especially decisions of the Supreme Court.

Indonesia also has separate three-tiered structures or courts for handling disputes in administrative law, military law and Islamic family law. Since 1998, a number of specialized courts have been added to the Indonesian judicial system, including the Commercial Court, handling bankruptcy and intellectual property matters, the Anti-Corruption Court, the Human Rights Courts, and special tribunals for tax, labour, and fisheries disputes. Based on recent amendments to the Constitution, a Constitutional Court was established in 2003 and a Judicial Council is currently in formation. In 2004, The Indonesian Supreme Court has begun to implement a set of blueprints of comprehensive judicial reform and has been supported from the Indonesian public and the international community for this effort.

The court system does not provide effective recourse for resolving commercial disputes. The judiciary is nominally independent under the law; however, legal practitioners fear that irregular payments and other collusive practices often influence case preparation and the judicial ruling.

The government recognises the need for judicial reform but has not yet taken any action. In several instances the local courts accepted jurisdiction over commercial disputes despite contractual arbitration clauses calling for adjudication in foreign venues.

Indonesia is a signatory to the Convention on the Settlement of Investment.

Disputes between States and Nationals of Other States (ICSID)

So far only one American investment company has brought a case to the ICSID, which ruled in its favour. Indonesia's Arbitration Law recognises the right of parties to apply any rules of arbitration that they may mutually agree upon and provides default procedural rules if no other rules have been designated.

An Indonesian commercial arbitration board, BANI, is available if both parties agree. Companies have resorted to ad hoc arbitrations in Indonesia

using the United Nations Commission on International Trade Law (UNCITRAL) arbitration rules, as well as others. Other companies in Indonesia have used International Criminal Court (ICC) arbitrations.

On 12th August 1999, Indonesia's Parliament passed Arbitration Law Number 30, endowing the District Court of Central Jakarta with the power to enforce international arbitration awards. Before passage of the new arbitration law in 1999, enforcement lay with the Supreme Court, which was slow to act on decisions. Since 1999, Indonesian courts have swiftly enforced international arbitration awards— some have been executed within a month of the request for enforcement. The new law greatly reduces instances where district courts fail to apply the law, and legal practitioners predict that the process should improve as more judges educate themselves about arbitration.

Since 1981, when Indonesia joined the 1958 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York), fewer than two dozen foreign awards have registered with Indonesian courts (most of which have been enforced). The domestic and international press have widely publicised recent cases where those awards have not been enforced.

Right to Private Ownership and Establishment

Right of Ownership (Hak Milik)

A Hak Milik is the most entire right (land tenure) of ownership a person can own over land in Indonesia.

This right of ownership has several specific characteristics such as:

- It has no time limit
- It covers to all fixtures on the land
- Only Indonesian citizens and certain Indonesian legal entities (badan hukum) that may have a Hak Milik
- It can be transferred freely among Indonesian citizens and certain legal persons.

There is a possibility for having horizontal separation between the owner of the Hak Milik and the owner of a building on the land. The holder of this right of ownership can transfer the land to others.

In special condition, the Hak Milik has to be converted to other rights, such as a Right to Build, Right of Use, or Right of Cultivation if the holders are foreigners or PMA Companies.

Right to Build (Hak Guna Bangunan or "HGB")

A *Hak Guna Bangunan* is a right of leasehold for the period of 30 years or less and gives authorization to build and possess a building on land for the holder.

This Right to Build has several characters such as:

- There is a possibility that this *HGB* can be extended for an extra 20 years with the opportunity for renewal
- The title is granted by and registered at the Land Office
- Only Indonesian Citizens and Indonesian corporations incorporated in Indonesia and have their legal domiciles in Indonesia, also PMA Companies that may hold *HGB*
- It is intended for land utilization as the location for buildings or facilities
- This right to build can be transferred to the third parties during its existence
- A *HGB* is transferred by performing a Sale and Purchase Agreement (*Akta Jual Beli*) in the form of a notarial deed and it must be registered with the Land Office.

Generally, investors constructing industrial projects on industrial land in Indonesia look for a *HGB* title over the land.

The right to private ownership and establishment and rely on the private sector are assumed as the principal engine of economic growth in Indonesia.

State-owned Enterprises (*SOEs*) also play a dominant role in many sectors, including oil and gas retail and distribution, electric power generation and transmission, civil aviation, banking, and fertiliser production and wholesale distribution.

During these three years Indonesia has been promoted a competition in several sectors and reduced the privileges awarded to *SOEs*.

The State Ministry for *SOEs* is formed in 1998 by the Parliament. Privatisation plays an important role on its mandate but political opposition has effectively hindered such attempts. For the purpose of minimizing the loss and preparing themselves for privatisation, several provincial governments have made some improvement in their management and transparency of provincially owned firms (*BUMDs*).

Right to Cultivate (Hak Guna Usaha or "HGU")

The specific characteristics of Right to Cultivate are explained below:

- It is issued by State owned land specifically granted for estate or plantation activities
- Generally, its duration is limited for 25 and at most 35 years and it has the possibility of renewal
- It is granted and registered with the Land Office

- HGU is transferable to the third parties in terms of its existence by performing a Sale and Purchase Agreement (Akta Jual Beli) in the form of a notarial deed. It must be registered to the Land Office afterwards for the completion of transfer registration
- This HGU can be held by Indonesian individuals or legal entities, including PMA companies.

Right of Use (Hak Pakai)

- It is a right to use and/or collect produces from land administered by the State or it is owned by another person
- It is limited in duration by the contract or decree
- It is usually for a 25-year period with the renewal possibility and subjected to specific restrictions on the intended use of the land
- Indonesian citizens, Indonesian corporations, foreign residents and foreign corporations under the Basic Agrarian Law can carry a Hak Pakai
- It needs the permission of the relevant authorized officer for the transfer of a Hak Pakai over State land
- If it is accorded with the contract granting the right, the transfer of a Hak Pakai over land owned by private citizens.

Obtaining Land Titles by PMA Companies

There is one important procedure that has to be followed by a new prospective PMA company and needs land or real estate to perform its business in terms of land for the processing of the Location Permit.

A PMA company is allowed by The Location Permit to acquire the land that is needed for its operation. The Location Permit also functions as for the transfer of rights and for utilizing the land for its investment.

The Location Permit has to be obtained from the Regent (Camat) with jurisdiction where such land is located. The PMA company has to process to relinquish the land from its original land owners within 12 -36 months (depending the acreage of land) after the issuance of this Location Permit.

The company Permit needs to be carefully observed if it obtained a Location Permit previously, for example, the property purchase should be in conformance with it.

The investment license also needs to have a provision on the land. Thus, if the properties that have been purchased by the company have more than the acreage stated in its investment license, this action will not be permitted unless the company first submits an application with BKPM (Investment Coordinating Board) for a revision of its investment license to include a larger land area. It is expected for a company to use the land in

conformance with the terms of decree and its investment approval for those that has been obtained a decree granting its right in the land.

Protection of Property Rights

Foreign entities have no freehold rights to land ownership in Indonesia. Foreign investors' land holdings are usually obtained through long-term lease agreements (normally for 30 years) with the government or private parties. These lease holdings can be used as collateral. Government regulations allow mortgages to be registered against real property and seagoing vessels in their appropriate registries, as well as security interests in chattel, equipment, accounts receivable, and insurance proceeds. A search facility currently exists only for mortgages. The lack of transparency in Indonesia's courts means uncertainty whether security interests will be recognized and enforced. Foreign companies may also establish a limited company under Indonesian law that can legally obtain rights to land.

The court system does not provide effective recourse for settling property disputes. The new era government and Indonesia's decentralization process unleashed a flurry of new land claims by local residents against companies, often operating on government-granted concessions located in their communities. The problem of incomplete or inaccurate record keeping is compounded by an ineffective and corrupt enforcement system.

The US government in May 2003 again placed Indonesia on the Special 301 Priority Watch List for inadequate protection of Intellectual Property Rights (IPR), where Indonesia has been since the 1980s. The Indonesian government has steadily improved the regulatory and legal framework for the protection of IPR; however, enforcement continues to fall short. US businesses reported that Indonesia ranks as the third largest producer of pirated products. They maintain that 90 percent of all CDs (audio, video, and software) sold in Indonesia are pirated and estimate that industry suffered losses in 2002 of USD 253 million, a 33 percent increase over prior year.

Indonesia's new copyright law (Law 19/2002) takes effect on July 29, 2003. The new law increases fines up to Rp 500 million (USD 62,000) and provides for prison terms of up to five years for dealers of pirated materials. The law directs cases of alleged copyright violations to be tried in commercial courts, and for the rendering of judgments within 90 days. As part of the law's implementation, the Ministry of Industry and Trade plans to issue optical disc regulations that would enhance the government's ability to identify and prosecute producers of pirated products. In an effort to enhance interagency coordination on enforcement, Indonesia's Ministry of Justice recently formed an IPR task force made up

of the national police, customs, attorney general, judiciary, and members of the computer software and entertainment industries. The task force has already conducted a few high profile raids.

Indonesia is a member of the World Intellectual Property Organization, but has not yet ratified the related WIPO Performances and Phonograms Treaty (WPPT). The Ministry of Justice prepared a Presidential decree ratifying WPPT last year, and Justice officials expect the President to sign the decree sometime in 2003. Indonesia acceded to numerous international conventions on intellectual property rights, including the Paris Convention for the Protection of Intellectual Property; the Berne Convention for the Protection of Literary and Artistic Works (with a reservation on Article 33); the Patent Cooperation Treaty; Trademark Law Treaty; the Nice Agreement for the International Classification of Unclassified Goods and Services.

Patents: The current patent law dates from 2001, which amended and consolidated in a single text all previous legislation. In 1997, Indonesian law extended the term of patent protection to 20 years from 14 years, and maintained the provision for a two-year patent extension. The amendment allows for the patenting of plant and animals. However, some of the weaknesses of the old law persist. Chief among these flaws is the requirement that an inventor must produce a product or utilize a value-added process in Indonesia in order to obtain patent protection for the product or process. Inventions that are contrary to Indonesian laws and regulations are excluded from patent ability, and the standard for excluding inventions without domestic content appears to be inconsistent with TRIPS requirements.

Patents

As per 1 August 2001, Indonesia ordains a Patents Law (Law Number 14 of 2001).

There is a difference between local and foreign applicants. The local patent applicants may apply patent through the Directorate General of Intellectual Property Rights ("DGIPR"), the Department of Law and Human Rights. Meanwhile, the foreigners have to submit an application through a patent consultant in Indonesia. DGIPR acknowledges an international application entering the national phase (PCT application). The invention must meet each criteria: novelty, inventive step and industrial applicability in order to get a patent.

There are two types of patents in Patents Law Patents:

- Standard Patent-

Protects an invention with claim comprises of process/manufacture, machine/apparatus, product, composition of matter (including chemical compound and microorganism). This has 20 years protection from the filing date and non renewable.

- Simple Patent- Gives some protection to the invention of new apparatus, equipment or product that has value because of its shape, configuration, construction or composition. It has 10 years protection from the filing date and no extension.

Trademarks:

Indonesia enacted its new trademark law on August 1st 2001. Like the new patent law, the latest version consolidated into one text a series of trademark laws enacted over the past 20 years. The new law raised the maximum fine for trademark violations to Rp 1 billion (USD 95,000) and slightly reduced the maximum possible prison term. The government justified this move by claiming that financial penalties were a greater deterrent to IPR violators than imprisonment. Foreign rights holders, arguing that most IPR cases never result in the maximum sentence, had pushed for minimum sentencing guidelines rather than higher fines.

The trademark law provides for the determination of trademark rights by priority of registration, rather than by priority of commercial use. The law also provides for the protection of well-known marks, but offers no administrative procedures or legal ground under which legitimate owners of well-known marks can cancel pre-existing registrations. Currently, the only avenue for challenging existing trademark registrations in Indonesia is through the commercial courts, which generally have issued decisions within three months upholding legitimate trademarks.

The Law Number 15 of 2001 is the law that regulates the marks for goods and services. This Marks Law acquires a first-to-file principle where the State grants the right of mark to a person who has registered his or her mark at DGIPR.

For several reasons explain below, a mark cannot be registered:

- The applicant has a bad faith;
- The mark is in the contrary to public order, morality and the existing law;
- There are no differences;
- The mark has been in a public domain;
- The mark is a description to the goods or services;

- The mark has a similarity in principle or in its entirety to the other registered mark for the same goods;
- The mark has likeness in principle or in its entirety with a well-known mark for the same of goods;
- The mark has a similarity in principle or in its entirety to a well-known geographical indication;
- It is the name of a famous person;
- The mark is similar to the name or abbreviation, flag, logo, symbol of the state or national institution or international institution; and
- The mark is similar to the sign or stamp or official stamp used by of the state or government institution.

Registration Procedure

For the application of mark registration, it has to be submitted in the Indonesian language to DGIPR with enclosed the required documents such as a Power of Attorney, a Declaration of Ownership and 25 labels of the mark concerned.

The application must be registered through the Indonesian proxy by way of a power of attorney for applicant who domiciles outside Indonesia. For applications which do not satisfy all of the formal requirements, it will be returned for completion and/or remedial actions, for which a remedial period of 2 months (or 3 months for applications with a priority right) in principle is granted.

Applications that are complete and meet all of the formal requirements will be examined by DGIPR for their approval or rejection. Its process should not take longer than 9 months. Upon the issuance of the registration approval by DGIPR, the application is published in the Official Marks Gazette (Berita Resmi Merek) for 3 months. When the application for mark is being rejected then the applicant may submit an objection or a response to DGIPR within 30 days as of the date of the rejection letter. A mark is registered for 10 years from the filing date.

3. Foreign investment

The Law Number 1 of 1967 is governed direct foreign investment in Indonesia. It is amended by Law Number 11 of 1970 (“Foreign Investment Law”) and the last amendment was Law Number 25 of 2007.

These laws explain that Indonesian Government demands foreign investors who want to perform operation in Indonesia to form a limited liability company. Generally, it refers to foreign investment company or PMA (Penanaman Modal Asing) company.

The Indonesian government agency which issues investment licenses is The Investment Coordinating Board (commonly referred to as “BKPM”, Badan Koordinasi Penanaman Modal). There are also other Indonesian government agencies that issue import licenses and permits to employ non-Indonesian workers. BKPM does not issue licenses for investments in banking, financial institutions, insurance, and oil and gas. Instead, these are issued by other government agencies under separate legislation. For instance, the Department of Finance governs the foreign investment in banking, insurance and stock broking and the Department of Mines and Energy has a role to approve the foreign investment in the oil and gas sector.

Since the bulk of foreign direct investment in Indonesia is regulated by the Foreign Investment Law, the following focuses on the rules and regulations that most investors will encounter under this law. Investment through acquiring shares in a listed company will also be discussed briefly at the close of this section. An important feature of the Foreign Investment Law is the guarantee that the Indonesian government will not nationalize a foreign investment or revoke the investor’s rights to control a foreign investment, except where it is declared under Indonesian law to be in the national interest to do so and then only upon payment of mutually agreeable compensation determined in accordance with principles of international law. This guarantee is accompanied by assurances that the foreign investor will have the authority to appoint the management of the foreign investment company and the right to repatriate capital in the form of after-tax profits, reimbursements of expatriate manpower expenses, depreciation of fixed assets, and other reasons. The Foreign Investment Law also provides for arbitration of investment disputes that may emerge between investors and the government, allowing for such disputes to be submitted to international arbitration under rules of the International Convention for Settlement of Investment Disputes (“ICSID”).

Business Activities Open for Foreign Investment

Although the Foreign Investment Law is intended to encourage foreign direct investment in Indonesia, it requires that the Indonesian government must regulate the fields of business activity that are open to foreign investment and set the priorities and any special conditions to be placed on foreign investments. The Foreign Investment Law also allows the Indonesian government to determine that certain areas are closed to further investment. It also stipulates that industries relating to national defence are to remain totally closed to foreign investment and that certain sectors that are important to the State and affect the livelihood of the Indonesian population cannot be undertaken by foreign investors alone (i.e., without local participation).

These sectors are:

- harbours
- production, transmission and distribution of electric power to the public
- telecommunications
- shipping
- aviation
- drinking water
- public railway
- atomic reactors
- mass media.

For years, the Indonesian government has been issued a list of desired investments and fields of business activity which are closed to further foreign investment in accordance with the provisions of the Foreign Investment Law. This list is called the Negative List for Investment (Daftar Negatif Investasi).

There has been a conjunctive effort in preparation of the Negative List to hold the number of restricted sectors at a minimum and to remove numerous conditions that previously had been imposed. Foreign investors are very welcomed with this approach. It has significantly opened many sectors of business activity to new investments, both foreign and domestic. The most recent Negative List was issued in 2008.

It presents the willingness of the Indonesian government for attracting more foreign investments, after the substantial decrease in investment that followed the financial crisis that hit Indonesia and Asia in general in the late 90s. The process of recovery gradually gave some improvement in general public security, and other actions directed to make Indonesia more attractive for foreign investment. It gives some contribution to an increasing trend of foreign investment into Indonesia.

All business sectors are open to foreign direct investment because of recent liberalization in the investment sector, with the following exceptions:

- Business sectors that are closed to foreign investment
- Activity field, referred to as "strategic activities", which are significant for the State and subject to a maximum foreign shareholding of 95%, including:
 - public harbours and shipping
 - transmission and distribution of electric power for public use
 - telecommunications
 - aviation, public drinking water
 - public railways
 - nuclear power generation, etc.

The Banking and Foreign Exchange System

Exchange rates are issued by the Central Bank on a daily basis for commercial banking purposes. However, for tax purposes (in calculating the Indonesian income tax liability on foreign currency income) the exchange rates are issued on a weekly basis by the Indonesian Ministry of Finance. Foreign exchange controls do not exist currently in Indonesia, however transfers of funds exceeding USD 10,000 from and within Indonesia should be reported to the Central Bank.

Openness to Foreign Investment

Indonesia encourages private sector-led growth and foreign investment. Foreign investment approvals in 2007 increased to USD 10 billion, from USD 6 billion in 2006. The biggest foreign investments are by Singapore investors (\$ 130.2million) and are followed by England (\$ 9.6 million), Belgium (\$6.4million), and South Korea (\$ 5.7 million). Investment approvals for Indonesian firms trended even more steeply upward, amounting in 2007 to USD 3.9 billion, from USD 2.7 billion in 2006.

Investment Law

On March 29th 2007, Parliament passed a new Investment law aimed at improving Indonesia's investment climate and attracting greater foreign investment into Indonesia. Law Number 25 of 2007 was signed by the President on April 26th, 2007. The law establishes basic investment protections including the following:

- Equal treatment for domestic and foreign investors. However, equal treatment is not applicable to investors from countries which obtain, "special rights based in an agreement with Indonesia."

- The Government of Indonesia (GOI) will not undertake any nationalization action, unless by law. In the event that the GOI “takes action to nationalize,” it will grant compensation with specified amount based on the market value or arbitration if the two parties do not agree.
- Investors may freely transfer assets to other parties, as long as assets are not determined (by law) to be state assets.
- Investors may transfer and repatriate capital, profits, royalties, income from asset sales, and other sources, in foreign currency, in accordance prevailing laws and regulations. However, this does not restrict the right of the GOI to receive taxes or royalties or implement laws and regulations requiring reporting of the transfer of funds. The GOI may also implement laws to protect the rights of creditors and to avoid losses to the State.
- Investments disputes between the Government and Investors may be settled through international arbitration based upon prior agreement between the parties.
- The new law appears to increase the authority of the Investment Coordinating Board (BKPM) in both implementing and proposing investment policy. The BKPM’s duties under the law include coordinating and implementing one door integrated services, developing an investor roadmap, provide consultation to investors seeking capital investments, and others. Although the law contains no provision authorizing BKPM to approve investments, BKPM approval is needed in order for investors to receive immigration facilities or investment incentives.

The Role of the BKPM

Foreign direct investment in the manufacturing, industrial or non-financial services sectors is licensed by BKPM. Investment in the areas of banking, insurance, general mining, oil and natural exploration, production and related activities are licensed by other regulatory bodies.

Sector Restrictions

Restrictions on foreign investment have been regulated by Regulation of The President of The Republic Indonesia No. 77 of 2007 concerning list of business fields that are closed to investments and business fields that are conditionally open for investments. Every sector has limitations of foreign capital ownership. These include limitations up to 95 % of foreign capital ownership in some Energy & minerals resources sectors.

An environmental impact study may be required, therefore the Articles of Association of corporate shareholders, or passports of individuals, should

be attached. The BKPM aims to process applications within one month. In practice, approvals may be faster.

Investment Application

The process of foreign investment begins with the submission of a formal application to the BKPM. The application must include a description of the project including names of participants, total capital required, employment details, production process description, power requirements and environmental issues

Capital Requirements

There is minimum capital requirement based on Law No. 40/2007 concerning Limited Liability Companies. They should prepare IDR 50 million for minimum capital and 25% of capital should be issued and paid up at the time of incorporation. The BKPM will grant approval based on its assessment of the need of the project. Share capital should be paid up in cash or in kind in the form of either tangible or intangible assets. Assets other than cash should be independently appraised. The BKPM can provide a range of facilities including import duty exemptions based on the submission of a 'master list', investment repatriation guarantees and possible tax holidays.

4. Setting up a Business

Legal Entities

There is a collection of recognised legal entities for setting up a business in Indonesia, which is as follows:

- Persekutuan Perdata (PP). A partnership between two or more people in one agreement to make a profit.
- Firma (Fa). A partnership between two or more people in one agreement to make a collective name to deal with third parties in making a profit.
- Persekutuan Komanditer (Commanditaire Vennootschap - CV). A partnership between two or more people in one agreement to make a profit. One partner is allowed to invest money into the partnership without having to manage the company.

However, the above business types apply only to local citizens. The types of legal entities that apply to foreign investors are:

Representative Office

As the time goes by, the global economic activity has experienced some growth. There are a large number of companies which have been expanded their business operations by including operations and offices in foreign countries.

Many companies have their own representative office in other countries although they may not have production facilities located in those countries in order to maintain the close supervision with the management of foreign business activities.

A representative office in Indonesia

In Indonesia, a representative office may not own or maintain production facilities or operational activities, and therefore, cannot accept orders, participate in tenders, sign contracts or engage in the importation of goods.

A representative office in Indonesia can be an Indonesian company, an Indonesian individual, or an expatriate individual. However, a work permit for the representative has to be applied together with the application for the representative office license if the representative office is to be headed by an expatriate.

To establish a Representative Office with permission from the Ministry of Industry and Trade, the company's head office needs to issue three letters:

- i. Letter of Intent stating the intention of the company to establish a representative office.
- ii. Letter of Appointment -stating the appointment of the chief representative.
- iii. Letter of Statement -stating that the Chief Representative will follow Indonesian regulations.

The three letters must be stamped by a notary public and approved by the Indonesian Embassy in the home country of the firm. Upon approval, the Indonesian Embassy will issue a Letter of Notification (Surat Keterangan). Upon completion of the four letters the process can continue to the related government ministry in Jakarta, to incorporate a fixed license for 2 years.

Other ministries require different types of letters.

Limited Liability Co or Perusahaan Terbatas (PT)

Foreign Direct Investment, most often referred to by its Indonesian abbreviation -PMA, is governed primarily by the Foreign Capital Investment Law No. 1 of 1967, and amended by Law No. 25 of 2007. As a legal basis, the law is fairly accommodative to various deregulatory policies and measures to date, and those that will be taken by the government in the foreseeable future.

In addition to Investment Law No. 1/1967, PMA companies as well as other companies, in their business operations are still subject to sector/industrial policies as required by corresponding ministries.

Establishing a Company

Investment Approval Process

The life of foreign investment companies has been extended by allowing the renewal of the fixed operating license (IUT) for an additional 30 years. In other words, the initial licenses are valid for 3 years (SPPP BKPM), plus 2 x 30 years, for a total of 63 years.

The process of incorporation of a new foreign direct investment company:
Initial License (valid for 3 years)

Step 1. Prepare and send the application with required documentation, compiled according to the investment plan.

Set up a joint venture agreement if investors plan to make the investment with Indonesian partners.

Step 2. Obtain the Initial License (SPPP BKPM), valid for 3 years.

Step 3. Incorporation of SPPP BKPM

- a. Establish Articles of Association with a Public Notary detailing proof of capital investment, and send it to the Ministry of Justice for approval and issuance of State Gazette.
- b. Registration of company address with local council (domicile).
- c. IRD registration (NPWP + PKP)

Registration with the Department of Industry and Trade (TDP)

Step 4. Key expatriate positions (work permits).

Fixed Operating License (30 years)

Step 5. Prepare and send the 6-month report (LKPM) to the provincial BKPM office as well as UUG (HO) nuisance act to the regional office of BKPM.

Step 6. Incorporate facilities - Master list/APIT or property ownership.

Step 7. Provincial approval for Fixed Licenses (BAP).

Step 8. Fixed License (IUT) for 30 years is issued.

A Limited Liability company is established either under foreign shareholders or through a joint venture with Indonesians or wholly owned by Indonesian shareholders and must be approved by the Ministry of Justice. It doesn't matter who is the owner of an Indonesian Limited Liability company, they must comply with Indonesian law and are considered an Indonesian company and the company can subsequently be changed or sold to the shareholders, foreign or Indonesian.

To get license of Change of Capital and Change of Owner the applications should be submitted to BKPM. According to BKPM, there's no charge to arrange licences.

Offshore Incorporation

In some situations, it may be to an investor's advantage to incorporate their firm offshore, while operations are carried out in Indonesia.

The advantages and disadvantages of offshore usually focus on the facilities offered by tax havens in nations like Mauritius and the Cayman Islands. Your management consultant can assist you in making this important decision.

5. Labour

Visas

Indonesia issues a range of different classes of visa depending on the purpose of a foreigner's visit. Short visit visas valid for 60 days may be issued on arrival at an official entry point to passport holders from most developed and neighbouring countries. The passport's validity should be at least six months.

Business visas may be issued for business visits not including work. Business visas are issued by Indonesian embassies overseas, based on a letter of invitation from the party to be visited. Business visas may be renewed, once in the country, for up to a maximum of six months. Foreigners intending to take up employment in Indonesia, together with any foreign dependents, should apply for a KITAS or semi-permanent residence visa. While much of the preparatory work is done in Indonesia, the visas are issued by embassies overseas based on a temporary stay visa, or 'VITAS', issued by the immigration authorities in Jakarta. A KITAS visa is issued for a year, but may be renewed for up to four years after which a fresh application is required.

Work permits

All foreigners planning to work in Indonesia must obtain a work permit in addition to a KITAS visa. Work permits are issued by the Department of Manpower approximately concurrently with the VITAS visa. Employment of foreigners must be in the context of an approved manpower plan. Many expatriates are employed as technical advisers. The BKPM will approve a certain number of positions for expatriates as contained in the investment application.

Other requirements

All foreign residents must also hold a 'police pass'. Work permit holders must pay in advance an annual training levy of USD 1,200 before issue or renewal of the work permit. All foreigners holding a KITAS visa require a valid exit/re-entry visa to leave and return to Indonesia. A final 'exit permit only' is required when a work permit is to be cancelled or will not be renewed.

The development of Indonesian employment regulations is progressive and further changes are expected in the coming years. Due to the active

involvement of various NGOs, the awareness of Indonesian laborers has also increased during the last 10 years.

Employment Agreements

Employment agreements in Indonesia are categorized into:

- Employment Agreements for a definite period in which an employment relationship has a definite term or based on the completion of a certain job (e.g., employment between a company and an interim worker; or a contract in which a company employs someone to set-up a computer network)
- Employment Agreements for an indefinite period in which the employment agreement does not have specific term or require a completion of a certain job.

6. Taxation

Tax system

LAW OF THE REPUBLIC OF INDONESIA NO. 28 OF 2007 ABOUT THE THIRD AMENDMENT OF LAW OF THE REPUBLIC OF INDONESIA NO 6 OF 1983 ABOUT TAX ADMINISTRATION LAW .

This law governs the tax system in Indonesia.

New laws

The current framework of Indonesia's tax laws dates from 1983 with subsequent revisions, most recently in 2007. There are separate laws covering income tax, value added tax (VAT) and sales tax on luxury goods. Other tax laws include the law on the taxing of land and buildings and the law on stamp duty. Individual articles contained in the laws may be supported by implementing regulations and decrees, government regulations and decrees of the Directorate General of Taxation. The government is committed to a greater intensification of tax collection including increasing the number of registered taxpayers.

Income tax

Income tax is applied to resident corporations and individuals on most sources of increase in economic wealth. A company is treated as a resident of Indonesia for tax by virtue of its establishment or its place of management in Indonesia. A foreign company carrying out business activities through a permanent establishment (PE) in Indonesia will generally have to assume the same tax obligations as a resident taxpayer. Resident taxpayers and Indonesian PEs of foreign companies have to settle their tax liabilities either by direct payments, by withholding by third parties, or a combination of both. Foreign companies that do not have a PE in Indonesia are to settle their tax liabilities in respect of their Indonesian-sourced income by way of the Indonesian party paying the income withholding the tax.

Income tax shall be imposed on any taxpayer in respect of income during a taxable year. Thus, the imposing of income tax has to carry out that there are tax person and tax object i.e. the income. A taxable year is a certain period for imposing the income tax. The taxable year is the calendar year.

The Income Tax Law governs income tax imposition on Taxpayer related with income received or accrued in a taxable year. The taxpayer is subjected to tax if that person receives or accrues income. A Taxpayer who receives income is called a Taxpayer under this law. A Taxpayer is taxed

on the income received or accrued during a taxable year or a fraction of a taxable year, if the tax obligations commence or end in a taxable year.

Taxpayer

Taxpayers consist of resident and non resident tax persons. The resident taxpayer is an individual and an entity. The non resident taxpayer is a Permanent Establishment (PE) and Non PE. The resident taxpayer and PE must file the annual tax return. The individual resident taxpayer is an individual who resides in Indonesia or present in Indonesia for more than 183 (one hundred and eighty-three) days within any 12 (twelve) month period, or an individual who in particular taxable year is present and intends to reside in Indonesia. The entity resident taxpayer is an entity established or domiciled in Indonesia.

The non resident taxpayer means:

An individual who resides in Indonesia or is present in Indonesia for more than 183 (one hundred and eighty-three) days within any 12 (twelve) month period, or an individual who in that particular taxable year is present in the country and intends to reside in Indonesia.

An individual who does not domicile in Indonesia or is present in Indonesia for not more than 183 (one hundred and eighty-three) days within any 12 (twelve) month period. An entity which is not established or domiciled in Indonesia deriving income from Indonesia other than from conducting business or carrying out activities through a permanent establishment.

The significant difference between a resident taxpayer and a non-resident taxpayer is that a resident taxpayer is taxed on his/her income originating from Indonesia and/or from abroad, however a non-resident taxpayer is taxed on his/her income derived only from Indonesia. Therefore, any individual reside in Indonesia or any individual stay in Indonesia for more than 183 days within a period of 12 months, or any individual who, within a fiscal year, stays in Indonesia and intend to reside in Indonesia, is taxed on his/her worldwide income under any name and form whatsoever.

Taxable Object

The Taxable Object is income. Increasing in economic benefit derived by a taxpayer and may be used for consumption or increase the wealth of the taxpayer concerned, under any name and form whatsoever, including:

Any remuneration / compensation related with work, services, or activities, gained from employment or independent profession, including: wages, salary, honoraria, doctor's fees, actuarial fees, accountant's fees, lawyer's fees

- Any income or compensation from any business or activity
- Any income from capital include from movable and immovable assets, such as reward and gain from loan condonation (“haircuts”), etc.

Withholding Taxes

Withholding taxes is a main system by which Indonesian income tax has been gathered. Whenever specific income item is subject to withholding tax, the tax payer has the responsibility to withhold or collect the tax.

The rates of withholding tax vary according to the nature of the income source. Rates for domestic payments extend up to 15%. Payments made overseas on certain sources of income may be liable to withholding tax of up to 20%. Applicable tax treaties may reduce the rate of withholding tax.

Generally, the payer is held responsible for withholding or collecting the tax. These withholding taxes are referred to use the relevant article of the Income Tax (PPh) Law, as follows.

(i) Article 21, income tax

Taxable income is calculated from the gross revenue less occupation cost (biaya jabatan), pension contributions, including contributions Old Age Saving.

The regulation of director General of Tax for per 31/PJ/2009 about the technical guidelines of withholding, payment and filing of Article 21 Income Tax and / or Article 26 Income Tax related to the work, services and tax payer activity.

Employers are needed to withhold Article 21 income tax from the salaries payable to their employees and pay the tax to the State Treasury on their behalf. The same withholding tax is applicable to other payments to non-employee individuals (e.g., fees payable to individual consultants or service providers). Resident individual taxpayers that don't have an NPWP (Tax ID Number) are subject to a surcharge of 20% in addition to the standard withholding tax.

(ii) Article 22 income tax

Article 22 income tax is applicable to the following:

The import of goods;

The sale of goods to the government requiring payment from the State Treasury, the State Budget General Directorate, or certain state-owned companies;

The sale/purchasing of automotives, steel, cement, cigarettes, and paper products; and

The sale/purchasing of luxury goods.

The tax rates for these are as follows:

	Tax Rate	Tax Base
1. The import of goods – using an Importer Identification (API)	2.5%	Import value, i.e., CIF value plus duties payable
2. The import of goods – without an API	7.5%	Import value, i.e., CIF-value plus duties payable
3. The sale of goods to the government and required payment from the State Treasury and certain state-owned companies	1.5%	Selling prices
4. The purchasing of steel products	0.30%	Selling prices
5. The purchasing of automotive products	0.45%	Selling prices
6. The purchasing of paper products	0.10%	Selling prices
7. The purchasing of cement	0.25%	Selling prices
8. The purchasing of luxury goods	5%	Selling prices

Taxpayers without an NPWP are subject to a surcharge of 100% in addition to the standard tax rate.

(iii) Article 4 (2) – final income tax

Resident companies, PEs, representatives of foreign companies, organisations, and particular individuals are required to withhold final tax from the following gross payments to resident taxpayers and PEs:

Description	Tax Rate
1. Rental of land and/or buildings	10%

Description	Tax Rate
2. Proceeds from transfers of land and building rights	5% or 1% (for transfers of simple houses and apartments conducted by taxpayers engaged in a property development business)
3. Fees for construction work performance	<p>2% for small qualification service provider) or 3% (for other qualification service provider) or 4% (for non-qualification service provider).</p> <p>Notes:</p> <p>For contracts signed before 1 January 2008, applies :</p> <p>The new tax rates as mentioned above for payment contracts or part of the contracts as of 31 December 2008 and onwards.</p> <p>The previous tax rates for those contracts which are signed before January 1, 2008.</p>
4. Fees for construction work planning	4% (for qualification service provider) or 6% (for non-qualification service provider)
5. Fees for construction work supervision	4% (for qualification service provider) or 6% (for non-qualification service provider)
6. Interest on time or saving deposits and on Bank Indonesia Certificates (SBIs) other than that payable to banks operating in Indonesia and to government-approved pension funds	20%
7. Interest on bonds other than that payable to banks operating in Indonesia and government-approved pension funds	15% or if the recipient is a mutual fund registered with the Capital Market Supervisory Board (BAPEPAM), the tax rate is 0% for 2009-2010, 5% for 2010-2013 and 15% thereafter. If the recipient is a non-resident taxpayer, the tax rate is 20% or a lower rate in accordance with

Description	Tax Rate
	the relevant tax treaty
<p data-bbox="379 398 938 427">8. Sale of shares on Indonesian stock exchanges</p> <p data-bbox="352 461 965 584">Founder shareholders may opt to pay tax at 0.5% of the market price of their shares upon listing. If they do</p> <p data-bbox="352 618 965 707">not opt for this, gains on subsequent sales are taxed under normal rules</p>	0.1%
9. Income from lottery prizes	25%
10. Forward contract derivatives	2.5% applicable to the initial margin

(iv) Article 23 income tax

THE REGULATION MINISTRY OF FINANCE NO. 244/PMK.03/2008
Income Tax Article 23.

Certain types of income paid or payable to resident taxpayers are subject to Article 23 income tax at a rate of either 15% or 2% of the gross amounts:

Article 23 income tax is due at a rate of 15% of the gross amounts on the following:

- Dividends
- Interest, including premiums, discounts, and loan guarantee fees
- Royalties
- Prizes and awards.

b. Article 23 income tax is due at a rate of 2% for gross amounts on the fees of the following:

1. Rentals of assets other than land and buildings
2. Technical services
3. Management services
4. Consulting services
5. Appraisal services
6. Actuary services

7. Accounting services
8. Design services
9. Drilling services for oil and gas mining except for those performed by a PE
10. Support services for oil and gas mining
11. Mining services other than oil and gas support
12. Flight and airport support services
13. Forest felling services
14. Waste processing services
15. Labour supply/outsourcing services
16. Intermediary/agency services
17. Custodianship and storage services except for those performed by stock exchanges KSEI, and KPEI
18. Sound dubbing services
19. Film mixing services
20. Computer and software-related services
21. Installation services (for example, of electricity, machinery, or telephone equipment) except for those rendered by qualifying construction companies
22. Maintenance and improvement services (for example, for electricity, machinery, or telephone equipment) except for those rendered by licensed construction companies
23. Manufacturing services (Maklon)
24. Investigation and security services
25. Event organisation services
26. Packaging services
27. Provision of space and/or time for the dissemination of information
28. Pest eradication services

29. Cleaning services

30. Catering services.

(v) Article 26 – Non-residents

Resident taxpayers, organisations, and representatives of foreign companies are required to withhold tax at a rate of 20% from the following payments to non-residents:

- a. On gross amounts :
1. Dividends
 2. Interest, including premiums, discounts (interest), swap premiums, and guarantee fees;
 3. Royalties, rents and payments for the use of assets;
 4. Fees for services, work, and activities;
 5. Prizes and awards;
 6. Pensions and any other periodic payments;
 7. After-tax profits of a branch or PE.
- b. On Estimated Net Income (ENI), being a specified percentage of the gross amount:

	ENI	Effective Tax Rate
Insurance premiums paid to non-resident insurance companies:		
by the insured	50%	10%
by Indonesian insurance companies	10%	2%
by Indonesian reinsurance companies	5%	1%
Sale of non-listed Indonesian company shares by	25%	5%

	ENI	Effective Tax Rate
non-residents		
Sale by non-residents of a conduit company where this company serves as an intermediary for the holding of Indonesian company shares or a PE	25%	5%

Where the recipient is resident in a country which has a tax treaty with Indonesia, the withholding tax rates may be reduced or exempted.

Period of Tax Payment and Tax Return Filing

Monthly Tax Obligations

Type of Tax	Deadline for a Tax Payment	Deadline for a Tax Return
1. Article 21/26 Income Tax	The 10 th of the following month	The 20 th of the following month
2. Article 23/26 Income Tax	The 10 th of the following month	The 20 th of the following month
3. Article 25 Income Tax	The 15 th of the following month	The 20 th of the following month
4. Article 22 Income Tax – Tax Collector	The 10 th of the following month	The 20 th of the following month
5. Article 4(2) Income Tax	The 10 th of the following month	The 20 th of the following month
6. VAT and LST – Taxable Enterprise	The 15 th of the following month	The 20 th of the following month
7. VAT and LST – Taxable Collector	The 15 th of the following month	The 20 th of the following month

Annual Tax Obligations

Type of Tax	Deadline for a Tax Payment	Deadline for a Tax Return
1. Corporate Income Tax	The ending of the fourth month after the book year end before filing the tax return	The ending of the fourth month after the book year end
2. Individual Income Tax	The ending of the third month after the book year end before filing	The ending of the third month after the book year end

Type of Tax	Deadline for a Tax Payment	Deadline for a Tax Return
	the tax return	
3. Land and Building (L&B) tax	Six months after the receipt of a Tax Due Notification Letter (SPPT) from DGT Office	N/A
4. Duties on the acquisitions of L& B Rights	On the date of acquisition	N/A

EXTENDED FILING DEADLINE

In terms of annual income tax return, there is a possibility for taxpayers to extend their filing deadline up to two months. It can be performed by filing a written notification to the DGT before the deadline and attaching a tentative tax calculation. Based on the tentative calculation, the tax due have to be settled before submitting the extension notification.

A 2% of interest penalty per month is applicable to the difference until the shortfall is paid whenever the actual tax due according to the final tax calculation is higher than the tentative calculation.

TAX RATES

CORPORATE INCOME TAX RATES

The applicable corporate tax rate in 2009 is a flat rate 28%. It will be decreased up to 25% in 2010. There is a 5% tax discount of the standard rate for public companies that meet a minimum listing requirement of 40% and other conditions. It will provide an effective tax rate of 23% in 2009 and 20% in 2010.

Tax Cut for public companies

Starting from 1 January 2008, a 5% corporate tax discount is awarded to public companies who meet the following conditions:

- There is at least 40% publicly owned of their paid shares
- The companies must comprise 300 individuals to the lowest degree. Each individual hold less than five percent of their paid-in shares
- Those two considerations must be fulfilled for at least six months (183 days) in a tax year.

However, these services will not be applicable for those years where either or both of the conditions are not fulfilled.

Small enterprises are entitled to a tax discount of 50% of the standard rate for a taxable income up to Rp. 4.8 billion.

The term of small enterprises is a corporate taxpayer that has an annual turnover of not more than Rp. 50 billion.

Tax cut for small enterprises

PT Y turnover in 2009 is Rp4.5 billion with taxable income of Rp500

million. Calculations of income tax payable: $50\% \times 28\% \times \text{Rp}500 \text{ million} = \text{Rp}70 \text{ million}$.

PT X turnover in 2009 is Rp30 billion with taxable income of Rp3 billion.

Calculations of income tax payable:

1. Taxable income of the turnover that enjoying facilities:
 $(\text{Rp}4.8 \text{ billion} : \text{Rp}30 \text{ billion}) \times \text{Rp}3 \text{ billion} = \text{Rp}480 \text{ million}$
2. Taxable income of the turnover that does not enjoying facilities:
 $\text{Rp}3 \text{ billion} - \text{Rp}480 \text{ million} = \text{Rp}2.52 \text{ billion}$

Income tax payable is:

- (50% x 28%) x Rp480 million	=	Rp	67.2	million
- 28% x Rp2.52 billion	=	Rp	705.6	million
Income tax payable	=	Rp	772.8	million

Individual Income Tax

Main Personal Relief

Annual non-taxable income (PTKP) for resident individuals is as follows:

	Rp.
Taxpayer	15,840,000

Spouse	1,320,000
Each dependent (max. of 3)	1,320,000
Occupational expenses (5% of gross income, max. Rp. 500,000/month)	6,000,000
Employee contribution to Jamsostek for old age security savings (2% of gross income)	Full amount
Pension maintenance expenses (5% of gross income, Max. Rp 200,000/month)	2,400,000

The rates of withholding tax vary according to the nature of the income source. Rates for domestic payments extend up to 15%. Payments made overseas on certain sources of income may be liable to withholding tax of up to 20%. Applicable tax treaties may reduce the rate of withholding tax.

Normal Tax Rates

The income tax is used to find how much yearly taxpayer income tax. Tax rate for resident individual taxpayer:

- I : 5% (five percent) for Rp. 0 - Rp. 50,000,000.00
- II: 15% (fifteen percent) for over Rp.50,000,000.00 - Rp. 250,000,000.00
- III: 25% (twenty five percent) for over Rp. 250,000,000.00 – Rp. 500,000,000.00
- IV : 30% (thirty percent) for over Rp. 500,000,000.00

Calculation of Individual Taxable Income

Taxable income is calculated after allowable deductions. For individuals there are income tax exclusions which are set at relatively low income levels. Individuals are broadly liable to income tax on cash income. Benefits in kind provided by employers to employees are not taxable to individuals but are non-deductible against corporate taxable income. Employers are required to withhold income tax from employees and paid to the State Treasury every month.

Employers prepare a consolidated annual tax return detailing each employee's individual tax calculation. The employee should then file a separate personal return. Tax returns should be filed by 31 March of the year following the year of assessment.

Taxable business profits are computed on the basis of normal accounting principles as modified by certain tax adjustments. Generally, a deduction

is allowed for all expenditure incurred to obtain, collect, and maintain taxable business profits. A timing difference may arise in respect of when an expenditure recorded as an expense for accounting can be claimed as a deduction for tax.

Corporate taxable income is calculated after the deduction of most normal business expenses. Rates of depreciation are regulated, although taxpayers may elect either the straight line or double declining method. Provisions that are not deductible are employee benefits in kind as mentioned above.

Companies may choose to be taxed on the basis of a financial year other than the calendar year. Books of account may be kept in English based on the DGT's approval. Foreign currency, i.e. US dollars, may be used as the reporting currency if appropriate approval is obtained. Annual filings should be lodged within three months of the financial year, though an extension may be obtained.

Payment of Taxes

Taxes are paid by monthly instalments on a current year basis. The regular instalment amount is based on the previous year's filings after taking credit for withholdings at source. Any shortfall should be settled by the 25th day of the third month following the end of the financial year. Overpayments of tax may be recovered, but only after a tax audit has been completed. The self-assessment principle, however, underpins Indonesian income tax law. A substantial part of individual income is collected by way of withholding by third parties.

Value Added Tax

Law of the Republic of Indonesia number 18 of 2000 the second amendment of the Law No 8 1983 about the Value Added Tax and Luxury Sales Tax.

VAT is applicable to the import and delivery of most goods and services. Insurance and banking are not subject to VAT. The VAT standard rate is 10%. The export of goods is zero-rated. Taxpayers are required to submit a tax return in the following month and shows details of all output and input VAT. The net output VAT is payable by the 20th of the following month. An excess of input VAT may be carried forward (compensated) to the following month or refunded. Suppliers who trade with so called 'VAT Collectors' will not collect VAT from their customers or clients. The VAT is then paid direct to the State Treasury. Such suppliers may be in a constant overpayment situation and may be forced to seek regular refunds.

According to Article 4 of the Indonesian VAT Law, VAT is the tax imposed on:

1. delivery of taxable goods within the custom Area
2. import of taxable goods
3. rendering of taxable service in the custom Area
4. intangible taxable goods utilization obtained from outside the customs area in the customs area
5. taxable service usage and obtained from outside the customs area of Indonesia within the customs Area
6. export of taxable goods.

Non Taxable Goods and Services

There are several kinds of goods which are excluded as taxable goods in Article 4A of Indonesian VAT Law. They are:

1. Products of mining and drilling that is extracted directly from the source, for example crude oil, natural gas, geothermal energy, sand and gravel, coal (before processing into coal briquettes), iron ore, tin ore, copper ore, gold ore, silver ore and bauxite ore;
2. Basic Commodities for public, for example rice, salt, corn, sago and soy beans;
3. Food and beverages served in hotel, restaurant, and such other places;
4. Money, gold, and valuable documents, securities.

Non Taxable Services

There are also several types of services that are also excluded as taxable services. They are the following:

1. medical health services
2. social welfare for example orphanages and funeral services
3. postal delivery
4. banking, insurance and financial leasing services
5. religious services
6. education

7. culture and entertainment which has been imposed under regional
8. entertainment tax
9. broadcasting services not include advertising
10. shipping and inland public transportation, international air
11. transport
12. manpower
13. rendering of services by the government in efforts to run the government in general
14. hotel services.

VAT Mechanism

In general, the taxpayers who provide taxable goods or perform taxable services have to impose the VAT to the buyer. The imposing VAT is performed by withholding 10% VAT rate of the tax base. VAT on the export of taxable goods is fixed at 0%. The effective VAT rate on deliveries and import of tobacco products is 8.5%.

The taxpayer has to make a tax invoice as evidence for this VAT withholding. The tax invoice is made when they sell and it is called output tax invoice. The VAT withheld is called output tax.

When taxpayers buy taxable goods or taxable services, they have to pay an additional payment of VAT which is withheld by their supplier. This VAT is called input tax and the withholding proof is called input tax invoice.

Taxpayers have to calculate how much they withhold in output tax and how much input tax they have in a month period. The output tax in a month is subtracted or credited by the input tax in a month. If the result is positive they have to pay to government account. On the contrary if the result is negative then they can ask restitution to government.

Value Added Tax (VAT) is typically due on events involving the transfer of taxable goods or the provision of taxable services in the Indonesian Customs Area. The taxable events are:

1. Deliveries of taxable goods in the Customs Area by an enterprise
2. Importation of taxable goods
3. Deliveries of taxable services in the Customs Area;

4. Use or consumption of taxable intangible goods originating from outside the Customs Area in the Customs Area
5. Use or consumption of taxable services originating from outside the Customs Area in the Customs Area
6. Exportation of taxable goods by an enterprise.

The delivery of taxable goods is defined very broadly; it includes the following:

1. Deliveries of a title to taxable goods according to an agreement
2. Transfers of taxable goods according to a leasing-with- option or a finance-lease agreement
3. Deliveries of taxable goods to an intermediary trader or an auction official
4. Own-use and/or free gift of taxable goods
5. Remaining taxable goods and certain assets, which were originally not for sale, at a company's dissolution
6. Deliveries of taxable goods within a company (e.g., between branches, or between the head office and its branches) unless the company, subject to the DGT's approval, centralises its VAT reporting
7. Deliveries of goods on consignment.

VAT reporting

Companies and individuals as taxable enterprises are required to report their business activities and settle the VAT liabilities on these every month. VAT is usually to be accounted for on a decentralisation basis. As a result, a company carrying out business activities through a number of business units (branches) in the working areas of different district tax service offices (KPP) must register each unit with the relevant KPP. It is in this context that internal deliveries of taxable goods within a company are subject to VAT.

Subject to DGT approval, a company may centralise its VAT reporting and so may exclude internal deliveries of taxable goods from the scope of VAT. To obtain DGT approval, a company must satisfy a number of conditions, including sales administration centralisation and the removal of the business units to be centralised from any deliveries of taxable goods. However, companies who file e-tax returns may choose to centralise their

VAT reporting without satisfying the other conditions; they simply need to submit written notification to the DGT.

Despite this default VAT reporting basis, companies registered with certain tax service offices (KPP PMA, KPP Badora, KPP Go Public, LTO, and MTO tax offices) are required to centralise their VAT reporting.

VAT liabilities are typically settled by using an input-output mechanism. A vendor of taxable goods or a taxable service must typically charge VAT to the buyer. From the vendor's perspective, it is an output tax. The buyer has to pay the VAT to the vendor. From the buyer's perspective, it is an input tax. To the extent that the goods are necessary for running the buyer's business, the input tax can be credited against the buyer's own output tax. Similarly, the vendor can also offset the output tax against input tax on the acquisition of taxable goods or taxable services. If the accumulated output tax for a particular month exceeds the accumulated input tax for the same period, the taxpayer in question has to settle the difference by the 15th of the month following. If, however, the accumulated input tax for a particular month exceeds the accumulated output VAT, the taxpayer may ask for a monthly refund or carry over the overpaid VAT to the following months.

Import VAT on goods and self-assessed VAT on the consumption or use of foreign taxable services or intangible goods should be understood in the context of the standard input-output mechanism.

Because the non-resident vendor or service provider cannot charge VAT (cannot, in other words, issue tax invoices) to the Indonesian buyer/importer, the Indonesian buyer/importer has to pay the VAT for and on behalf of the non-resident vendor or service provider. To the degree that goods/services imported or procured are necessary for running the importer/service recipient's business, the input VAT (import VAT and self-assessed VAT) is claimable as a tax credit.

A deviation from the standard mechanism, however, is in force for deliveries of taxable goods and services to VAT collectors. The VAT Collector is currently either the State Treasury or PSC companies (including Pertamina).

Sales Tax on Luxury Goods

Sales taxes also include sales tax on luxury goods (PPnBM). This tax applies at the point of import or manufacture and is additional to VAT. It is a non-creditable one-off tax and applies to a wide range of goods. Rates range from 10% to 50%.

In addition to VAT, deliveries or imports of certain manufactured taxable goods may be subject to LST. A particular item will only attract LST once, i.e., tax will be charged either on importation of the good or on delivery by the (resident) manufacturer to another party.

LST must be accounted for every month together with VAT. The importer or the manufacturer of the goods is held responsible for the settlement of the LST.

To ascertain whether or not a particular item is subject to LST and to identify the LST rate, reference should be made to the Customs Book using the relevant harmonised system (HS) code.

Special Industry Rules

Certain industries, in particular production sharing contractors, mining companies under contracts of work and geothermal projects are subject to income tax in accordance with specialist rules. Rates of tax vary according to the generation of each respective contract.

Tax Treaties

There are currently 59 tax treaties in force with other countries. Provisions typically include reduced withholding tax rates on interest, dividends and royalties and a broader definition of the concept of permanent establishment compared with domestic law.

Sunset Policy

Following the enactment of the 2007 tax administration law, taxpayers are allowed to revise their annual corporate income tax returns (CITR) for years before 2007 without facing any interest penalties on the underpaid tax amounts. In the normal situation, an underpaid tax amount would trigger interest penalties at 2% per month. Apart from the interest exemption, there are other concessions:

- Any data declared in the revised CITR cannot be used as a basis to issue assessments on any other taxes
- The revised CITR will not be audited unless it claims an overpaid tax refund or proves to be incorrect
- Filing a revised CITR which calls for an additional tax payment may stop an on-going tax audit. This includes not only the audit of corporate income tax for which the revised CITR has been filed but also the audit of other taxes as long as the relevant tax returns do not claim tax overpayments.

The Director General of Tax (DGT) however, at his own discretion, may decide to continue the audit irrespective of the absence of overpaid tax returns. The concession is available only up to the end of 2008. Hence, to enjoy the concession, the revised CITR must be filed before 1 January 2009.

7. Accounting & reporting

The history of Indonesian Generally Accepted Accounting Principles began when the Indonesian Accountants Association (abbreviated to IAI), established in 1957, was appointed by the Government of Indonesia in 1984 to develop accounting standards in Indonesia to be used mostly for Limited Liability Partnership. IAI then established a committee to develop accounting standards in Indonesia. This committee, which is responsible for developing and implementing the accounting standards, is called Dewan Standar Akuntansi Keuangan (DSAK).

Over the years, IAI has developed many accounting standards for various types of business practices in Indonesia. In October 2004, DSAK developed Indonesian Generally Accepted Accounting Principles that consist of Accounting Methods and Procedures for Financial Statements, Accounting Methods and Procedures for Financial Statement of Islamic Banking, 59 Statements of Financial Accounting Standards, and seven Interpretations.

The Indonesian Statement of Financial Accounting Standards is mostly based on the International Accounting Standards (IAS), which was recently changed to International Financial Reporting Standards (IFRS).

The second major source of the Indonesian Statement of Financial Accounting Standards is the United States Generally Accepted Accounting Principles. In addition to the above two sources, the IAI also pronounces their own Statement of Financial Accounting Standards such as Accounting Standard for Indonesian Venture Capital, Accounting Standard for Mining Industry, and an Accounting Standard for Islamic Banking. The 59 Statements of Financial Accounting Standards consist of 43 General Statements, 15 statements for specific industries and one statement revised and merged with other General Statements.

Other than IAI, the Government of Indonesia also appointed BAPEPAM (Indonesian Securities Exchange Commission) to establish additional regulations, besides those established by IAI, designed specifically for publicly held corporations.

Presentation of Financial Statements

In compliance with government regulation, every limited liability Partnership in Indonesia should prepare its Financial Statements in accordance with the Financial Accounting Standards established by the Indonesian Accountants Association.

The Indonesian Financial Accounting Standards require that Financial Statements consist of an Income Statement, Balance Sheet, Statement of Equity, and a Note to the Financial Statement. With the exception of the Cash Flow Statement, Financial Statements must be prepared based on the accrual basis, and on the assumption that the company will remain in operation for the foreseeable future. Financial Statements should be prepared annually and audited by a registered public accounting firm if the company meets any one of the following criteria:

- The company is utilising public funds
- The company has issued obligations
- The company is a publicly held corporation.

The Audited Financial Statements of a company that meets one of the criteria above should then be verified and signed by the Board of Directors, and published in the local Indonesian newspaper.

Moreover, the Minister of Trade and Commerce requires the filing of the audited financial statements for every limited liability partnership that meets the following criteria:

- The entity is a publicly held corporation
- The entity is utilising public funds
- The entity has issued obligations or promissory note
- The entity has total assets exceeding IDR 50,000,000,000.

Accounting for Tax

For tax purposes, a company's books have to be maintained in conformance with the prevailing accounting standards unless the tax law is in the condition differently. The books must be presented in Rupiah, composed in Indonesian, and stored in Indonesia.

Foreign-investment (PMA) companies, PEs, and subsidiaries of foreign companies can keep their books in USD and compile them in English related to specific DGT approval. A collective investment contract (KIK) may permit the usage of USD accounting related that it issues USD-denominated investment funds. DGT approval application must be submitted with the DGT office no longer than three months before the start

of the USD accounting year. The DGT is required to decide on the application within a month. If no decision is made within that time, the application is automatically approved.

Companies that are regulated by a Production Sharing Contract (PSC) or a Contract of Work (CoW) with the government may bring into consideration to apply USD accounting in English by giving some notification the DGT in writing. This notification has to be submitted to the DGT office by no longer than a month before the beginning of the USD accounting year. A company can also compile its books in English but keep them in Rupiah. In this case, the company have to submit a written notification to the DGT no longer than three months after the beginning of the tax year in which the books are composed in English.

The usage of a foreign language other than English and a foreign currency other than USD in a company's books is not allowed. Irrespective of the currency and the language used, companies typically have to settle their tax liabilities in Rupiah (except for PSC companies) and file tax returns in Indonesian. For corporate income tax, the assertions must be presented in USD side by side with Rupiah in the annual corporate income tax returns.

A company that has obtained approval to maintain USD accounting may return to Rupiah accounting subject to DGT approval. Once approval is granted, the company may not re-apply for USD accounting approval during the five years after the cancellation of the USD accounting.

8. UHY firms in Indonesia

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