



In general, cloud computing may be defined as the delivery of computing as a service, rather than a good, whereby shared resources, software and information are provided to computers and other devices over a network. Cloud computing provides computation, software applications, data access, data management and storage resources without requiring cloud service users ("CSU"s) to know the locations and other details of the computing infrastructure. Data are stored on servers at remote locations. The main objectives for utilizing these computing services are cost saving considerations, process centralization, improved performance and updated software.

In Indonesia there is no specific tax regulation stipulating the tax treatment of cyber businesses including cloud computing. Thus the tax treatment of cloud computing activities requires interpreting the current tax regulations.

## **PUBLIC CLOUDS**

An independent cloud service provider ("CSP") offers a range of services to unrelated parties. Applications, storage and other resources are made available to the general public in competition with other independent CSPs in the market place.

### **Onshore CSPs**

To establish and provide cloud computing services in Indonesia, a CSP must obtain permission from various government units, including the Indonesian Investment Board ("BKPM"), to obtain the principal license, and the Minister of Communication and Information.

### **Withholding Taxes**

Income received by an onshore CSP (including a permanent establishment ("PE")) is subject to withholding tax if paid by an Indonesian CSU which are mostly corporate taxpayers, including government agencies.

Payments to an onshore CSP are deemed as royalty payments if the cloud services provided include the following:

1. the use or right to use copyrights in the fields of literature, arts, scientific work, patents, design or modeling, formulas or secret processes, trademarks or intellectual /industrial property rights or other similar rights;
2. the use or right to use industrial, commercial or scientific equipment/tools; or
3. waiver of rights, entirely or partly, related to the use or granting of intellectual /industrial property rights or other rights.

Royalty payments are subject to a 15% withholding tax which is a prepaid corporate income tax for the onshore CSP.

Otherwise, payments are considered for general services, subject to a withholding tax of 2%.

### **Value Added Tax (VAT)**

An onshore CSP must register as a VAT-able company (except if its annual gross revenue is less than IDR 4.8 billion) and impose 10% VAT on all fees billed to both onshore and offshore CSUs.

VAT charged by onshore CSPs can be claimed by the onshore CSUs against their VAT output/payable if the onshore CSUs are VAT able companies.

### **Offshore CSPs**

#### **Withholding Taxes**

Indonesia tax laws require that, subject to a Tax Treaty between Indonesia and the country of residence of an offshore CSP, income received by an offshore CSP for cloud computing services from an onshore CSU is subject to a withholding tax of 20% that must be withheld and paid by the onshore CSU. This rule does not apply if the service is provided by a Permanent Establishment of a non-resident service provider/offshore CSP.

#### **Value Added Tax (VAT)**

A non-resident cannot register for VAT purposes in Indonesia.

The utilization of offshore services is therefore subject to self-assessed 10% VAT and CSU's obligation to comply with this requirement, which applies to all payments made to an offshore CSP.

The 10% self-assessed VAT is creditable against the CSU's VAT output/payable (except if the onshore CSU is a non-VATable company).

### **Permanent Establishments ("PEs")**

Non-resident CSPs can be deemed as PEs if the services are furnished by an employee or any other persons in Indonesia for more than 60 days in a period of 12 months

## **PRIVATE CLOUDS**

A group which has many subsidiaries/branches may establish its own internal CSP which only provides services to group companies. This can be done by establishing a separate entity or using an established entity to provide the services.

The establishment of an internal group CSP has different objectives than those of an independent CSP.

Most group level internal CSPs are established to provide standardized processes and single data storage to create efficiencies in operation processes. Internal CSPs can also be utilized for other functions, e.g., help desks, security operations, security management, service support, technology information management and service quality control, among others.

VAT and Withholding Tax obligations are similar as explained above, if the CSP and CSUs are different legal entities.

### **Corporate Income Taxes**

*Please note that currently it is not possible for a CSP to establish a branch in Indonesia from a legal and licensing perspective. The following information on Indonesian corporate tax relates to a PE.*

Basically, a PE constitutes a unit of its Head Office, so payments made by a PE to its Head Office or its other offshore branches are considered to be movement of funds within one entity. Therefore, payments made by a PE to its Head Office or its offshore branches for royalties or other services provided are not deductible expenses for Indonesian Corporate Income Tax purposes. Please note that any such payments made by a PE to its Head Office can be categorized as a remittance of profits (dividends) which are subject to 20% withholding tax, unless the Tax Treaty between Indonesia and the country of residence of the Head Office specifies otherwise.

However, if the charges for cloud computing activities are included in the Head Office's administrative costs allocated back to its Indonesian PE, then they can be deductible for Corporate Income Tax purposes, subject to certain requirements.

For corporate taxpayers, group charges for cloud computing are normally deductible, but this is subject to review of the reasonableness of the charges. Please see Transfer Pricing section below

## **TAX TREATIES**

The application of a reduced withholding tax rate and PE requirements are subject to the availability of tax treaty relief, and the eligibility of the recipient to apply for such

relief. If a tax treaty is applied, withholding tax can be reduced from 20% to 10% or 15%, depending on tax treaty provisions.

In order to apply tax treaty provisions, a valid certificate of domicile/residency ("COD") using a standard form issued by the Indonesian Tax Authority, called Form DGT-1, must be available. The COD needs to be completed by the offshore income recipient, validated by its local competent tax authority and furnished to the resident withholding tax agent, normally the CSU. Without the availability of this form, the standard domestic withholding tax rate of 20% applies and the CSUs have the obligation to withhold and pay this withholding tax payable.

Tax treaty benefits will be denied in the event of treaty abuse, indicated by transactions not having economic substance.

## **TRANSFER PRICING**

The transfer pricing environment in Indonesia is changing rapidly and the latest transfer pricing regulations are now mostly in line with the OECD Guidelines. These regulations also stipulate that for domestic transactions (i.e., onshore CSPs) no transfer pricing documentation is required, unless the CSP and CSU are subject to different tax rates. This could become more pertinent as the new tax holiday regime takes off. However, the Indonesian Tax Office ("ITO") can still question domestic related party transactions, even if no documentation is required. And adjustments do not lead to corresponding adjustments on the other side of the transaction, in particular when both taxpayers fall under the jurisdiction of different tax offices.

Transfer pricing documentation is only required if the total transactions with the CSP exceed IDR 10 billion (less than USD 1 million under the current exchange rate).

The ITO is extremely wary of service transactions involving related parties and often scrutinizes these transactions during a tax audit. Proof that the services have been rendered and that they benefited the Indonesian CSU are required. In some cases evidence of the cost base has also been requested. To best defend against these ITO challenges, taxpayers should maintain robust transfer pricing documentation.

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