Executive summary

On 29 March 2018, Indonesia’s Minister of Finance (MOF) signed MOF Regulation No. 35/PMK.010/2018 (PMK-35) providing new regulations on tax holidays, as an incentive to conduct business in Indonesia. The regulations are effective as of 4 April 2018 and are intended to be more attractive than previous regulations. Corporate taxpayers making new capital investments in “pioneer industries” can apply for the incentives.

Under PMK-35, the definition of pioneer industry has been expanded to cover 17 sectors. The tax holidays provide more certainty as they provide for a 100% corporate tax exemption for years 5 through 20, depending on the amount of new capital investment.

This Alert summarizes key aspects of PMK-35.

Detailed discussion

General overview

A corporate taxpayer that makes a new capital investment under the pioneer industry category is eligible for a 100% tax holiday on its corporate income tax. This incentive is available from 5 to 20 years, depending on the size of the new capital investment, as follows:
An additional 50% corporate income tax reduction is offered for two years following the expiration of the above tax holidays.

To qualify for the tax holidays:
- A taxpayer must be an Indonesian legal entity with a new investment in a pioneer industry, with a minimum capital investment of IDR500 billion (US$36 million).
- It must be a new incentive.
- The taxpayer must comply with the Indonesian thin-capitalization rules (i.e., 4:1 debt-to-equity ratio).

### Pioneer industries
PMK-35 modified the existing list and has expanded the list of pioneer industries from 8 to 17 sectors. A pioneer industry is defined as an industry that has broad connection and/or linkage, provides value added and high positive economic consequences to surrounding areas, introduces new technology and provides strategic value for the national economy. The new list includes:

1. Upstream base metal industry
2. Oil and gas purification and or refinery industry
3. Petrochemical industry, based on petroleum, natural gas or coal
4. Inorganic base chemical industry
5. Organic base chemical industry
6. Pharmaceutical raw material industry
7. Manufacturing industry of semiconductors and other main computer components such as semiconductors wafer, backlight for liquid crystal display (LCD), electrical driver or LCD that is integrated with the computer manufacturing industry
8. Manufacturing industry of main components for communication equipment such as semiconductors wafer, backlight for LCD, electrical driver or LCD that is integrated with the smartphone manufacturing industry
9. Manufacturing industry of main components for medical equipment that is integrated with the manufacturing of irradiation equipment, electro medical or electrotherapy
10. Manufacturing industry of main components for industrial engines, such as electric motors or internal combustion motors that is integrated with the engine manufacturing industry
11. Manufacturing industry of main components for engines, such as pistons, cylinder heads, or cylinder blocks that is integrated with the vehicle manufacturing industry
12. Manufacturing industry of robotic components that is integrated with the engine manufacturing industry
13. Manufacturing industry of main components for ships that is integrated with the ship manufacturing industry
14. Manufacturing industry of main components for aircrafts, such as engines, propellers, rotors, or structure components that is integrated with the aircraft manufacturing industry
15. Manufacturing industry of main components for trains including engines or transmissions that is integrated with the train manufacturing industry
16. Power plant machineries industry, including the waste to energy plant machineries industry
17. Economic infrastructures

The new list seems to indicate that the Indonesian Government wants to expand the local economy beyond assembly to value added manufacturing in many sectors.

<table>
<thead>
<tr>
<th>Category</th>
<th>New Capital investment</th>
<th>Tax holiday period</th>
</tr>
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<tbody>
<tr>
<td>I</td>
<td>500 billion to less than 1 trillion</td>
<td>36 million to less than 72 million</td>
</tr>
<tr>
<td>II</td>
<td>1 trillion to less than 5 trillion</td>
<td>72 million to less than 360 million</td>
</tr>
<tr>
<td>III</td>
<td>5 trillion to less than 15 trillion</td>
<td>360 million to less than 1.1 billion</td>
</tr>
<tr>
<td>IV</td>
<td>15 trillion to less than 30 trillion</td>
<td>1.1 billion up to less than 2.1 billion</td>
</tr>
<tr>
<td>V</td>
<td>30 trillion and greater</td>
<td>2.1 billion and greater</td>
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</tbody>
</table>
A taxpayer may still qualify for a particular incentive even if it is engaged in a pioneer industry that is not specifically listed, if approved jointly by the MOF, other relevant Ministries and the Investment Coordinating Board.

**Procedure for the tax holiday application**

A taxpayer can submit the application to the Investment Coordinating Board either during the capital investment registration or within one year after the issuance of capital investment registration.

The taxpayer should receive a response from the MOF within five business days of a final decision made by the Investment Coordinating Board.³

**Tax audit and annual report requirements**

Under PMK-35, the tax holiday will start from the fiscal year when the taxpayer reaches the commercial operation stage (COS), i.e., the time when the taxpayer sells its product for the first time, or when the taxpayer uses its own products for further processing. PMK-35, upon the taxpayer’s submission of a COS request, requires the Indonesian Tax Authority to conduct a tax audit to determine whether the taxpayer’s COS determination is appropriate. In addition, if the taxpayer fails to satisfy its commitment such as committed capital investment, the actual activity is different from the proposed plan, or importing used capital goods for the investment, the Indonesian Tax Authority can recommend that the MOF terminate the tax holiday.

In addition, the taxpayer is required to submit an annual report to the Indonesian Tax Authority on: (i) the capital investment realization report starting from the issuance of MOF approval for the tax holiday until the COS; and (ii) the production realization report from the COS through the end of a fiscal year when the tax holiday expires. The report should be submitted within 30 days after the fiscal year end.

A taxpayer who obtains a tax holiday is not entitled to apply for another tax incentive but is allowed to apply for another incentive once the tax holiday period expires.

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**Endnotes**

1. The prior regulations provided only partial exemptions.
2. An example may be building shops and houses to accommodate people relocated to work on a factory/company.
3. Processing time by the Investment Coordinating Board is not specified.
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