Jakarta, 27 March 2019

To:

1. **His Excellency Dr. Robert Pakpahan**
   Director General of Taxation
   Ministry of Finance, Republic of Indonesia

2. **His Excellency Dr. Ir. Mohammad Rudy Salahuddin, MEM**
   Deputy IV (Creative Economy, Entrepreneurship, and SME & Cooperative Competitiveness)
   Coordinating Ministry of Economic Affairs, Republic of Indonesia

Subject: Industry Submission and recommendations on Indonesia E-Commerce tax

On behalf of the Asia Internet Coalition (AIC) and its members, we thank you for the opportunity to offer our inputs on regulatory developments in Indonesia's e-commerce sector, particularly on regulation No. 210/PMK.010/2018 regarding the Tax Treatment of E-Commerce ("MOF Regulation 210").

AIC is an industry association comprised of leading Internet and technology companies in the Asia Pacific region with an objective to promote the understanding and resolution of Internet and ICT policy issues. Our current members are AirBnB, Amazon, Apple, Booking.com. Expedia Group, Facebook, Google, LinkedIn, LINE, Rakuten, Twitter and Yahoo (Oath).

We commend the government on formulating the regulation, with an aim to stimulate the e-commerce sector in the country. These efforts and direction are critical, particularly at a time when cross-border trade and data flows has taken a centre stage in Indonesia's digital economy development. However, MOF Regulation 210 may be one way to increase revenues in the short term, we believe that having a short sighted tax structure can potentially harm e-commerce and SMEs in the long run. **Considerably, the potential impact of regulation on e-commerce raises significant concerns, as explained below:**

a. **Impact on MSMEs**

   80% of SMEs in the ASEAN bloc see e-commerce as an opportunity for their business. Indonesian e-commerce market is projected to rise from US$8 billion to as much as US$65 billion by 2022, and much of this growth will be generated from MSME's integration in the digital economy. However, MOF Regulation 210, is more likely to bring regulatory hurdles and discourage aspiring entrepreneurs from selling online. The regulation may hamper the development of micro-, small-, and medium-sized businesses and cooperations ("UMKM"). Given that many UMKM are still struggling to establish their business models, MOF Regulation 210 may prove to be more of an obstacle than the tool to ease the fulfilment of tax obligations it was intended to be and restrict consumer choices for goods at lower costs, especially in rural areas. A research by McKinsey shows that consumers outside of larger cities in Indonesia see greater cost savings from participating in e-commerce. Consumers in non-Java regions save 11% to 25% by shopping online compared to traditional offline retail. It is also observed that at least 30% of online commerce spending is new consumption, capturing previously untapped needs.

   The regulation could unintentionally damage the continued growth of both e-commerce and trade, international implications of which may hinder the ability of small business to compete globally and ultimately slow the potential growth of e-commerce. This could further stifle the growth of MSMEs in Indonesia. We argue that while the premise of the e-commerce tax is welcome, the authority should postpone its implementation to fine-tune the regulations, which remain vague.

b. Excessive barriers to entry

E-commerce when looked holistically brings various benefits to multiple stakeholders in the value chain. Low barriers to entry and ease of scalability allows new entrepreneurs to test their wares with little to no overheads. A study by Bain & Company found that retail SMEs who use e-commerce saw around 15% sales increase on average. The study also found that 40% of retail SMEs cite the low cost of setting up an online store as being a key benefit, among others. In support, a recent IMF study shows that participation in online commerce is associated with more than a 30% increase in total factor productivity for firms in the Asia region. With such benefits, a unilateral taxation regime could restrict e-commerce platforms to promote digital inclusivity and social equality.

One of the regulation requirements is that all sellers or merchants on online platforms must have a tax payer number (NPWP). Further, sellers with profits under IDR 4.8 billion (US$339,000) per year are subjected to a 0.5% tax. Those whose profits are higher will be designated as taxable entrepreneurs (PKP) and will have to follow valued-added tax (VAT) rules. It is important to note that, 80% of 1,765 e-commerce sellers in 18 Indonesian cities are categorised as micro businesses with profits below IDR 300 million (US$21,226) per year, while 15% of sellers are categorised as small businesses. Only 5% of them are medium-sized. Therefore, a good 80% of sellers on e-commerce platforms are still struggling and in the process of refining their business models before they can grow their business.

Given the underlying provisions in the regulation and its net negative impact, we urge the government to reconsider the regulation, which in its current form not only harm existing sellers that fall into the micro-enterprise category by imposing burdensome requirements, but also instil a serious entry barrier to open a new business. Moreover, stricter rules for joining platforms could incentivise merchants to rely on informal online channels like social media to conduct sales, which is much riskier for both buyer and seller. Many SMEs may switch to social media if tax compliance remains focused on online marketplaces. When that happens, the government would suffer a loss of tax income due to the lack of monitoring on these platforms. Therefore, efforts should be made to limit the impact on value chains as much as possible and to avoid high barriers to entry for SMEs and start-ups.

c. Increase in compliance and operational costs

The regulation also forces marketplace platforms to become a tax deposit agent, which in effect makes them an extension of the Directorate General of Taxes with duties to collect, record, and deposit tax data for the government. We oppose this provision, as marketplace players are not fully equipped with the technical infrastructure to act as tax deposit agents. Importantly, such measures will not only be operationally challenging but also incur additional expenditures, cost of which could be significantly higher than the expected benefits the government aims to realize through such a regulation. We therefore suggest, the government to take a nuanced approach and prudently study the implications of – with a perspective of costs and benefits – the new tax regulation, to create a level playing field especially between the marketplace and social media. Importantly, Indonesia must first develop infrastructure that allows for more efficient tax collection and higher tax revenue. It is also recognised that there is a need to take a broader perspective which not only looks at the role marketplace platforms can play in the collection of tax but also takes a more holistic look at enforcement recognising the role of the various other actors in the supply chain such as shippers, importers, payment service providers and fulfilment houses.

d. Hinders the potential of e-commerce in Indonesia

The e-commerce industry in Indonesia is still very much in its nascent stage and has yet to fully penetrate and integrate itself in the region. E-commerce expenditure in Indonesia is still relatively low at 3% of total retail, as compared to 16% for China and 12% for US. Given e-commerce is still in early stage of development, burdensome regulations may halt the growth of the sector and diminish the aforementioned economic as well as social benefits. It could also add to inequality as burden of tax compliance will fall hardest on smaller entrepreneurs. It is critical to note that sellers are using e-commerce as ways to expand business, reach new customers, manage risks, rather than to avoid taxes. Tax burden such as the one proposed in Indonesia may push sellers to go back to informal channels, inhibiting their growth and hence potentially reduce future tax base.

Given the above-mentioned concerns and to achieve a fair and conducive ecosystem for e-commerce, we propose a pragmatic approach by taking into account the international best practices and multilateral frameworks. To this end, we recommend designing a new taxation regime for cross-border supplies of digital services, intangibles and tangible goods. Such a regime should be based on the guidelines issued by the OECD in the 2015 BEPS Action Paper 1 and subsequent reports. We also suggest referring to the latest report on "THE ROLE OF DIGITAL PLATFORMS IN THE COLLECTION OF VAT/GST ON ONLINE SALES" by OECD (published in March 2019), which include effective measures to make e-commerce marketplaces liable for the tax on sales made by online traders through their platforms, measures to facilitate data sharing and enhanced co-operation between tax authorities and online marketplaces.

As e-commerce cuts across borders, adopting a multilateral approach to taxing digital goods and services will help ensure regulatory harmonization, while encouraging the cross-border flow of e-commerce and the growth of the overall digital economy. We strongly encourage that the government considers adopting international best practices and frameworks such as the WTO E-Commerce Moratorium regarding zero customs duties on digital products, APEC Cross Border E-Commerce Facilitation Framework and the OECD Base Erosion Profit Sharing (BEPS) principles. We propose refraining from any unilateral undertakings, which are not long-term sustainable solutions, and most countries have expressed preference for an internationally agreed consensus on the taxation of profits. Hence, we would encourage that Indonesia endeavour to collaborate with the OECD to support the long-term, multilateral approach that various countries are working to develop.

A harmonized regional approach to e-commerce facilitation is the surest way to reap the full benefits of commerce, which includes connecting SMEs to global markets, enabling new startups, and provi consumers with a wide range of goods more efficiently and more cost effectively. In addition, redu barriers to the movement of goods and the secure transfer of
data will enable quicker, more inclusive growth.

Tax and regulations are important but the right sequencing and transition are the key. Given how e-commerce is delivering significant benefits to the society and that it is still in a nascent stage of development, it is best to err on the cautious side when it comes to tax imposition. For example, it might be better to provide a long adjustment period for merchants and conduct a small scale experiment to see the potential impact of such tax regulation first before implementing nationwide.

Considering there has been a lack of consultation on the MOF Regulation 210, as well as its perceived lack of fairness, we urge the government to expand their consultation period, for better preparedness. Finding this balance requires an in-depth study and consultation with expert stakeholders. AIC strongly suggest postponing and reviewing the implementation of MOF Regulation 210.

We suggest taking a measured approach by exercising caution, considering all options, and taking a long-term view. This will provide a stable environment for businesses to continue investing in and growing the local economy.

To that end, we greatly appreciate the opportunity to provide inputs and look forward to facilitate Indonesia's e-commerce landscape. It is our hope that as you continue this effort, we will be able to continue this dialogue and grow our partnership.

Should you have any questions or need clarification on any of the recommendations, please do not hesitate to contact our Secretariat Mr. Sarthak Luthra at Secretariat@aicasia.org or at +65 8739 1490. Importantly, we look forward to offer our inputs and insights on industry best practices, directly through meetings and discussions and help shape the dialogue for the advancement of e-commerce sector in Indonesia.

Sincerely,

Jeff Paine
Managing Director
Asia Internet Coalition (AIC)

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