International Journal of Psychosocial Rehabilitation, Vol. 24, Issue 09, 2020
ISSN: 1475-7192

Hybrid Mismatch Arrangement: Does it endanger tax base?

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Abstract--- *Base erosion and profit shifting (BEPS) action plans issued by OECD and supported by G-20 have been partially adopted by Indonesia Tax Authority (ITA). So far, Indonesia has established regulation which addressed the Action Plans. There are various ways to avoid the tax. One of the common practice is hybrid mismatch arrangement. A group of companies can obtain benefits from this transaction by making use of tax regulation in different countries. The objective of this study is to elaborate how hybrid mismatch arrangement applied and why the tax authority concern about it. This study use case-study method. We analyze a state-owned enterprises case that applied hybrid mismatch arrangement. Thus, we found several decisive results. First, Company used hybrid mismatch arrangement scheme to shift profit abroad which implied to less tax payment in Indonesia. Second, the dispute is brought to the tax court and transfer pricing became the settlement of the scheme. This is happened because Indonesia faced legal basis to treat the scheme as a hybrid mismatch arrangement. These findings may give recommendation to Indonesia Tax Authority to establish the relevant rules.*

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Keywords--- *hybrid mismatch arrangement, Indonesia state-owned enterprise*

I. INTRODUCTION

Globalization makes the world as if there is no limit. Global Policy Forum defined globalization from various perspectives. First, people across the globe can communicate one to others and it occurred dramatically increased. Second. The interdependently among countries became higher. Lastly, the flow of money, technology, and raw materials are more ever more swiftly among countries. Globalization makes economic activities in the world integrated and continues developing. This is also supported by the rapid development of technology and information. International trade is easier and faster to facilitate trade and investment flows. In the era of globalization, there was a big question about the ability of tax regulations both domestically and internationally which could offset the pace of development of the globalization and economic digitalization of multinational companies. Globalization is able to erode developing country revenues and generate potential taxes through three channels, namely income lost due. There is competition for taxes, income or assets placed abroad, and transfer of profits (Dietsch & Rixen, 2014).

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International Journal of Psychosocial Rehabilitation, Vol. 24, Issue 07, 2020
ISSN: 1475-7192

The erosion of the state revenue tax can be done by multinational companies to obtain maximum profits by utilizing various state tax rates in tax planning. Multinational companies deliberately divert their taxes by diverting company profits to other countries by imposing lower taxes or not requiring taxes at all to increase the suitability of state taxes (Nanang Z, 2014). Aggressive tax planning (tax planning) strategies using divisions and differences in tax regulations of various countries are known as Base corrosion and profit shifting (BEPS), which is a big agenda for member countries of the Organization for Economic Co-operation and Development (OECD) and Twenty Groups (G20). The OECD and G20 declared action in 15 Action Plans on the BEPS issue in July 2013 to prevent tax evasion by multinational companies. Fifteenth Action Plan intended to establish international coherence on corporate taxation, improve international taxation standards by harmonizing taxation rights with economic substance. Also agreed to be approved immediately increased certainty and predictability of making multilateral instruments in response to BEPS and supporting the implementation of the BEPS Action Plan (Darussalam, 2014).

One of the issues discussed is hybrid mismatch arrangements. OECD defines hybrid mismatch arrangements as a scheme created by exploiting differences in the tax treatment of a particular instrument or entity between two or more countries (OECD Report, 2012). This scheme is one way that can be done for tax avoidance which causes the country to suffer losses due to the erosion of the tax base (Tambunan, 2016). The difference in tax treatment of an instrument may result in being taxed at a very low tariff or not taxed or even not taxed in the country involved (double non-taxation). Hybrid mismatch arrangements have some basic elements such as hybrid entites, that is, an entity that is treated as transparent for tax purposes in a country and non-transparent in another country. In addition, the hybrid instrument as another element in the form of financial instruments applied differently for tax purposes in two countries, generally as debt in a country and capital in other countries. Other elements can be in the form of hybrid instruments and dual resident entities that are also formed due to differences in treatment by two or more countries (OECD Report, 2012). Indonesia as a developing country that is also involved in global economic activities makes this scheme potentially carried out by companies in Indonesia.

AI. Literature Review

This research is based on several theories that are relevant to the studies carried out, including agency theory, signaling theory and several previous studies. Theory is needed to build a basic framework of research. While previous studies can help researchers in developing research hypotheses and research variables and indicators.

Agency Theory. The idea put forward by Jensen & Meckling (1976) states that companies are black boxes that are operated to achieve relevant conditions by considering inputs and outputs with the aim of maximizing profits. Furthermore, Jensen & Meckling explained that agency relations are contracts between one or more parties (as principals) with other parties (as agents) to provide services in the name of the principal by involving the authority to make decisions to agents. If both parties (agents and principals) maximize their respective utilities, then there are

strong reasons to believe that the agent does not always provide the best effort for the principal. Agency relationships arise between two or more parties consisting of principals and agents. The agent acts for and on behalf of the principal. (Ross, 1973). Furthermore, Ross explained that there is asymmetrical information between the principal and the agent. This causes the agent to have an incentive to act in the corporation if the information held by

the principal is not the same as that of the agent. Pareto efficiency can be achieved if each party contributes full information. However, the principal has difficulty in controlling the choice of the agent.

Signaling Theory Ross (1977) explained that signal theory was appointed based on asymmetric information (assimetric information) between managers who have adequate information and investors who do not get enough information. This theory is based on a concept that managers will convey good information to investors in order to increase the value of the company. However, investors may not be easy to be convinced of that information, because managers are parties who have interests in the corporation. So that corporations will try to do signaling on their financial policies that are costly and generally carried out by large companies. A signal is a process that has a cost in the form of deadweight costing which aims to convince investors about the value of the company. Ross provides one example of the level of leverage of a company where large companies will create incentives that encourage them to take high leverage. This smaller company cannot be followed, because they are relatively more vulnerable to going bankrupt.

Megginson et al., (2010) state that if managers know that their company is "strong" while investors for some reason do not know this, managers can pay dividends (or aggressively buy back shares) in the hope that the quality of their company's signals to the market . Signals effectively separate strong companies from weak companies (so that strong companies can provide their type signals to the market), it becomes expensive for a weak company to mimic the actions taken by strong companies. Meanwhile, Wolk et al. (2013) stated that the signals that can be given by the company are in the form of reliable financial information that can reduce uncertainty about the company's prospects in the future. Thus, signal theory explains why companies have the urge to provide financial statement information to external parties. The company's push to provide information is because there is information asymmetry between the company and outside parties because the company knows more about the company and future prospects than outside parties (especially investors and creditors). Signal theory suggests how companies should provide signals to users of financial statements. This signal is in the form of information about the condition of the company to the owner or other interested parties. The signal provided can be done through disclosure of accounting information such as financial statements, reports on what has been done by management to realize the wishes of the owner, or even in the form of promotions and other information stating that the company is better than other companies. Signal theory addresses problems regarding information asymmetry. This theory is based on the premise that managers and shareholders do not have access to the same company information. There is certain information that is only known by managers, while shareholders do not know the information. So, there is asymmetric information between managers and shareholders. As a result, when the company's capital structure changes, it can bring information to shareholders which will result in the company's value changing. In other words, there is a sign or signaling (signaling).

The study conducted by Richardson, et al. (2014) show that tax aggressiveness correlates with debt. Lanis, et al. (2018) examine the impact of corporate avoidance on the reputation of the board of directors and and the CEO. The test results show that when the company carries out tax avoidance the directors and CEOs get an increase in their reputation which is marked by the addition of the number of positions outside the board of directors. Tax avoidance is not only carried out by one company in one country but can also be carried out through a cross-border transaction mechanism. Tax avoidance is carried out by multinational companies through business groups in countries that apply different tax rates (Beuselinck & Deloof, 2014)

BI. DATA COLLECTION

This study used case study approach in order to obtain a deep understanding to address the hybrid mismatch arrangement. We used PT PLN. case as our main discussion. PT PLN is a state-owned enterprise. Moreover, the case is taken from Tax Court decision.

On October 3, 2006, PT PLN established Majapahit Holding BV (MHBV) in the Netherlands with total capital deposits and premium capital contributions of USD 2,528,745. Furthermore, MHBV seeks funding by issuing international bonds. On October 16, 2006, MHBV issued the first tranche of guaranteed international bonds of USD 1 billion. On June 28, 2007, MHBV issued a second tranche of guaranteed international bonds of USD 1 billion. MHBV's international debt obligations amounting to USD3,951,388,537 were included in Majapahit Finance BV (MFBV) in the Netherlands as capital and premium deposits at the end of 2009. Therefore, PT PLN has 100% direct ownership in MHBV and has 100% indirect ownership on MFBV established in the Netherlands. MHBV and MFBV are based on the Domicile Certificate (SKD) issued by the Tax Administration Amsterdam / Belastingients Amsterdam dated April 20, 2007 is a resident / Dutch resident.

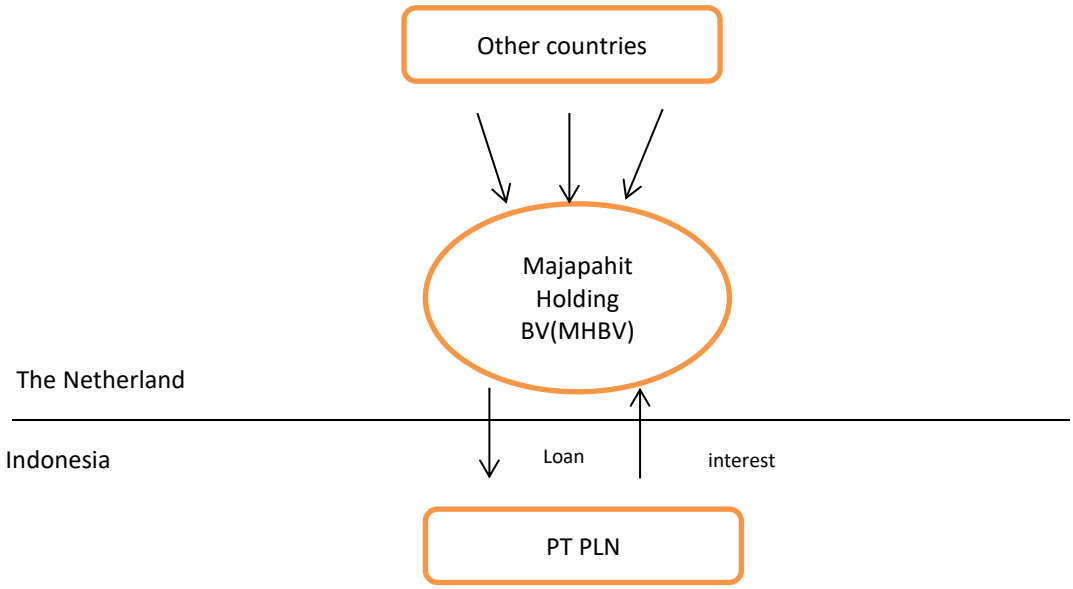
MFBV provided a loan to PT PLN for the amount stated in the intercompany loan agreement amounting to USD3,959,523,087 at the end of 2009 as well. related to the loan, PT PLN paid interest to MFBV in the amount of Rp.2,215,792,885,936. The interest has been taxed in the Netherlands and has not been deducted from Article 26 of Income Tax. PT PLN pays interest to MFBV for the duration of the debt with the details of the repayment due as follows:

a. October 16, 2006 - October 16, 2011;
b. 16 October 2006 - 16 October 2016;
c. 28 June 2007 - 28 June 2017;
d. June 28, 2007 - June 28, 2037;
e. 7 August 2009 - 7 August 2019;
f. January 20, 2010 - January 20, 2020.

In 2009, MFBV's profit amounted to USD234,886,540 and as much as USD150,875,000 of the profit was distributed as dividends to MHBV. On the other hand, MHBV reported 2009 profit from MFBV of USD234,886,540 which included dividend income from MFBV of USD150,875,000. In 2011, a tax assessment

underpayment (SKPKB) was issued for income tax (PPh) Article 26 The tax period from January to December 2009 of PT PLN for interest paid to MHBV (supposedly MFBV) with calculation of taxable income / tax base of Rp 2,237,865,809,450. The amount of Article 26 Income Tax payable is Rp.447,573,161,890. Article 26 of Income Tax that can be credited is Rp. 628,332,446, so that the tax that is not / less is paid in the amount of Rp.446,944,829,444. PT PLN is subject to interest sanctions Article 13 (2) of the General Provisions and Tax Procedures Act (UU KUP) for the amount of tax underpayment in the Underpayment Tax Assessment Letter amounting to Rp.196,655,724,955 so that the amount of tax payable is Rp .643,600,554,399. The amount approved by PT PLN in the Audit Result Final Discussion is Rp.5,452,203,250.

Scheme 1 – Transaction Path based on Tax Audit



PT PLN recognizes that its international bond interest is only Rp.22,072,923,514. After being examined by the Tax Auditing Team, there was a positive correction of the interest amounting to Rp.2,215,792,885,936 so that the value became Rp.2,237,865,809,450. Positive correction is made by the Tax Auditing Team based on the equalization of the interest of international bonds paid by PT PLN as the object of Article 26 Income Tax. Article 26 Paragraph (1) of the Income Tax Law (PPh Act) states that:

For income below, by name and in any form, which is paid or owed by government agencies, subjects of domestic taxes, organizers of activities, permanent establishments or representatives of other foreign companies to foreign taxpayers other than permanent establishment in Indonesia, withholding tax of 20% (twenty percent) of the gross amount by the party that is obliged to pay:

a. dividend;
b. interest includes: premiums, discounts, SWAP premiums, and rewards in connection with debt recovery guarantees;
c. royalties, rent and other income related to the use of assets;
d. rewards in connection with services, jobs and activities;
e. prizes and awards;
f. pension and other periodic payments.

PT PLN disagrees with the results of the inspection conducted by the Tax Auditing Team so that PT PLN submits an Application for Objection on December 27, 2011, but is rejected entirely with the following details:
Decision of Objection is stated in DGT Decision Number KEP-661/WPJ.19 /2012

Description	Previously amount (Rp)	Adjustment (Rp)	Final amount (Rp)
Tax Base	2.237.865.809.450	0	2.237.865.809.450
Income tax payable	447.573.161.890	0	447.573.161.890
Tax credit (Article 26 remitted)	628.332.446	0	628.332.446
Underpayment	446.944.829.444	0	446.944.829.444
Administration sanction	196.655.724.955	0	196.655.724.955
Total income tax should be paid	643.600.554.399	0	643.600.554.399

According to the Objection Review, based on MHBV data and facts it is not as beneficial owner (BO) of the interest. The real owner is an international bond holder spread in several countries. This shows that the MHBV is only a special purpose company or often referred to as special purpose vehicles (SPV). In addition, these international bonds have been listed on the Singapore Stock Exchange. Bondholders can at any time trade the bonds they hold so that the corrected interest costs must still be deducted from Article 26 of Income Tax.
PT PLN still disagrees with the Objection Decision so that it submits an Appeal to the Tax Court. The subject of the dispute is the difference in interest on international bonds amounting to Rp.2,215,792,885,936. According to PT PLN, it pays interest to MFBV instead of MHBV. The inspection team stated that the recipients of interest payments were MHBV because according to the data contained in the PT PLN interest report, the interest was paid to MHBV and did not mention MFBV at all. In addition, according to PT PLN the reason for the Objection Study is that MFBV is not a BO of interest paid by PT PLN not based on the correct facts. PT PLN assumes that the beneficial owner is an international tax language so that it becomes inappropriate if the term that is not given a definition then

refers to domestic law so that it cannot be defined unilaterally by the Indonesian government alone. Such an assumption refers to the opinions of experts, namely:

a. according to Edwardes-Ker, the term "beneficial owner" is an international tax language. Therefore, the interpretation must apply the autonomous approach (du Toit, p. 173);
b. at the International Fiscal Association Congress in 1998, delegates from Switzerland argued as follows:
   "... The beneficial ownership should be a treaty concept. The application of Article 3 (2), in the other words, the application of the given rules in the field of domestic law could be in my view of the undermine treaty solution and could also lead to some kind of treaty override. I think that since one benefit benefits from one way of treatment one should also say under what circumstances such benefits will be denied. And this should not be done based on domestic law but on treaty provisions. "
c. the above opinion was also supported by delegates from the Netherlands, France and Sweden who held that the interpretation of the "beneficial owner" must be in the treaty framework;

d. the opinions above are also in accordance with Lang's opinion as follows:
   According to Article 3 (2), a contextual meaning overrides a domestic law meaning if the context so requires. Thus, even though the starting point of Article 3 (2) is the lex fori approach, the context may require a universal meaning to prevail. Therefore, the fact how to phrase, context requiring, is interpreted is of relevance. The choice between two differing meanings of domestic context law on treaty context depends on how broad the terms context must require a meaning differing from domestic law meaning in order for contextual meaning to be used (Lang, 2001, p. 86);
e. Prokisch strongly supports the notion of the importance of "international tax language" to prevent misinterpretations so that each party has the same understanding (du Toit, p. 182);
f. Du toit (p. 183) argues that "beneficial owner" falls into the category of "international tax language", which is a term that is not defined in domestic law. Furthermore, Du Toit asked the question whether a term that is not defined in a P3B must be interpreted as other terms in the OECD Model which are not defined. Du Toit quoted Vogel's opinion in answering the question (du Toit, p. 183), as follows:
   Where OECD member states include tax treaties following the text of the Model Convention, it is presumed that states want the treatment to be meaningful by the Model Convention and its Commentary, as long as no particular circumstances indicate to the contrary;
g. Vogel argues that BO must be given meaning in the context of the international tax language meaning and not obtained from the domestic provisions of the country from the country that implements the treaty. Vogel (p. 562) states that:

> "*The first and foremost reason why the term cannot be interpreted by reference to the domestik law of the State applying the treaty is that none of the national tax systems in question offer a precise definition of the terms 'beneficial owner'. The terms must, therefore, be interpreted with reference to the context of the treaty and particularly with a view to the purpose pursued by the restriction".*

In addition, PT PLN also stated that MFBV had substance because of the large amount of capital deposit / deposit of shareholders. MFBV's capital deposit in 2007 amounted to USD 2,005,184,549. Companies that are categorized as "conduit" or "paper box" or "pass through" usually have a relatively small amount of capital deposits with a small risk intention from shareholders. In fact, MHBV, MFBV and Deutche International Trust Company N.V. has the same address namely herengracht 450, 1017CA Amsterdam. Research using Google Map as of July 2009 for this address shows that there is no signboard for MHBV and MFBV. The signboard written by Deutche Bank at that address. Regarding dividend payments, MFBV has directly paid dividends to shareholders (MHBV) in 2007 and continued in 2008. Details of the net income received by MFBV and dividends paid are as follows:

Table 1 – Net revenues received and dividend paid by MFBV

	Year 2007	**Year 2008**	**Year 2009**
Net income	129.410.775	170.915.752	234.886.540
Dividend payment			
Current year	(96.315.500)	(150.875.000)	-
End-of year	(33.095.275)	(20.040.752)	(234.886.540)
Retained earnings	-	-	-

Source: Decision of the Tax Court No.Put.59998 / PP / M.IIB / 13/2015

Based on these data, the interest received by MFBV is directly passed through MHBV in the form of dividend payments without waiting for the end of the financial year. This is not reasonable because dividend distribution is based on retained earnings or after the book value ends. On the side of costs, the interest paid by MHBV to bondholders is the cost of the largest portion compared to other costs, which is 90%. This shows that almost all revenues received by MHBV will be given to bondholders in the form of interest payments. From this fact it can be concluded that the interest income received by MFBV from PT PLN will be passed / passed through to MHBV, then the MHBV will pass through the bondholders in the form of interest payments. In other words, MHBV and MFBV

are pass through entities or conduit companies or the like. Pass through entity or conduit company or the like is not the beneficial owner. This is based on Indonesian legal provisions, namely:

a. Director General of Tax Circular Number SE-04 / PJ.34 / 2005 dated July 7, 2005 concerning Implementation Guidelines for Criteria for Beneficial Owner As Listed in the Director General of Taxes Circular Number SE-03 / PJ.03 / 2008 dated August 22, 2008 concerning Determination of Status The Beneficial Owner as referred to in the Indonesia Double Tax Avoidance Agreement with Partners is explained that:
   1) Beneficial owner is the actual owner of income in the form of dividends, interest and / or royalties that are fully entitled to directly enjoy the benefits of such income.
   2) Therefore, special purpose vehicles in the form of conduit companies, paper box companies, pass-through companies and other types are not included in the meaning of beneficial owner.

b. Director General of Tax Regulation Number PER-62 / PJ / 2009 dated November 5, 2009 concerning Abuse of Double Tax Avoidance Agreements jo. Regulation of Amendment to Director General of Taxes Regulation Number PER-62 / PJ / 2009 dated November 5, 2009 concerning Abuse of Double Tax Avoidance Agreements explained that Beneficial owner is the actual owner of the economic benefits of income, namely the income recipient who:
   1) acting not as an agent;
   2) acting not as a nominee; and
   3) not a conduit company.

Judging from the funds obtained by MHBV from the bonds issued, they are immediately channeled to MFBV and the interest income received is continued with an amount that is almost the same from MFBV to MHBV. MHBV has almost the same amount of interest income and interest expense. This can be seen from:

MHBV (*in USD*) 2009	
Loan to parent	3.962.383.687,00
Bonds outstanding	3.959.523.087,00
Interest income	235.915.811,00
Interest expense	192.872.841,00
MFBV (*in USD*) 2009	
Loans to ultimate parent	3.959.523.087,00
Share premium	3.951.388.537,00
Interest income on loans	235.676.193,00
Result before tax	234.886.540,00

Therefore, even though it is formally seen that MHBV and MFBV are the owners of these income, in practice they do not really enjoy the income. In another sense, MHBV and MFBV are not BOs. Another fact also shows that MHBV and MFBV are not BOs, namely:

1. MHBV and MFBV only have financial assets with the largest element in the form of long term loans while physical assets such as buildings, office equipment, vehicles and so on do not exist;
2. MHBV and MFBV also do not have employees so there are no remuneration costs for employees and do not have the burden of social securities; and
3. There is the signing of the same Financial Report Management Report for MHBV and MFBV, namely Member A (Mr.A.Hakam) and Member B (Deuthsche International Trust Company N.V). Based on other research, Mr.A.Hakam turned out to be an employee of PT PLN.

The recipient of interest income paid by PT PLN is not a BO so that the taxation rights are in Indonesia in accordance with Article 26 of the Income Tax Law. The legal basis is Article 11 paragraph (2) and (4) Indonesian-Dutch P3B. Article 11 paragraph (2) stipulates that:

1) Indonesia has the right to impose a tax on interest in accordance with statutory provisions in Indonesia, where Indonesia can impose a tax rate of 20% according to Article 26 of the Income Tax Law.
2) However, if the beneficial owner is a Dutch resident, the tax imposed may not exceed 10% of the gross amount of the interest.

Article 11 paragraph (4) clearly regulates the conditions that must be met so that interest income cannot be taxed in Indonesia, namely:

1) the beneficial owner is a Dutch resident; and
2) paid interest originates from loans made for a period of more than 2 (two) years or related to credit sales of commercial industrial or scientific equipment.

It is very clear Article 11 paragraph (2) and (4) regulate Indonesia's taxation rights for the interest payments. If the recipient of interest is not a party that substantially obviously is a BO, then Indonesia may impose Income Tax Article 26.

Based on these descriptions, it can be concluded that BO has a meaning that is not based on the definition of formal law, but contains economic meaning that looks at the substance. This is in accordance with the principles of Indonesian taxation legislation that adheres to material principles or "substance over form", where facts

or substance must actually be seen and not merely matters of formal legality. Finally, for the appeal submitted by PT PLN, the Tax Court rejected all of them so that the amount of Article 26 income tax of the January to December 2009 Tax Period accrued as follows:

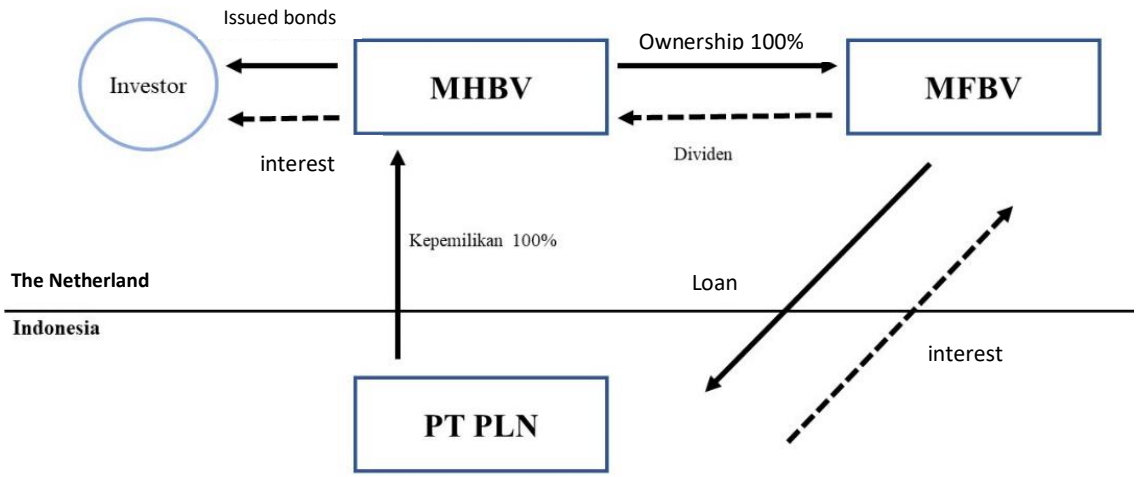
Tax Base Article 26 Income Tax	Rp. 2,237,865,809,450
Article 26 Income Tax payable	Rp. 447,573,161,890
Article 26 Income Tax Credit	Rp. 628,332,446
Article 26 of Income Tax is less (more) paid	Rp. 446,944,829,444
Administrative Sanctions	
Interest Article 13 (2) UU KUP	Rp. 196,655,724,955
Increase in Article 13 (3) UU KUP	Rp. 0
Amount of Income Tax Article 26 should be (more) is paid	Rp. 643,600,554,399

IV. DATA ANALYSIS

Based on the Tax Court Decision number Put 59998 / PP / M.IIB / 13/2015 on the Appeal submitted by PT PLN, the scheme carried out by PT PLN is as follows: First. PT PLN establishes MHBV in the Netherlands and a Domicile Certificate (SKD) is issued by the Tax Administration Amsterdam / Belastingients Amsterdam. Second, MHBV seeks funding by issuing international bonds. Third, MHBV international bond debt is entered into MFBV in the Netherlands as a capital deposit so that PT PLN has 100% direct ownership in MHBV and has 100% indirect ownership in MFBV in other words PT PLN, MHBV and MFBV have a special relationship. Fourth, MFBV provides a loan to PT PLN for money in the intercompany loan agreement in a period of more than two years. Fifth, PT PLN pays interest to MFBV for the loan. Sixth, the interest is taxed in the Netherlands and not deducted from Article 26 of Income Tax in Indonesia. Seventh, MFBV earnings are distributed as dividends to MHBV. Eight, the total profit of MHBV is equal to the profit earned by MFBV including dividends received.

International Journal of Psychosocial Rehabilitation, Vol. 24, Issue 07, 2020
ISSN: 1475-7192

Scheme 2 – Transactions conducted by PT PLN



Under the scheme carried out by PT PLN, it can be seen that PT PLN intentionally made MHBV and MFBV for tax purposes. From the scheme, PT PLN obtains benefits that should not have been obtained from the Indonesia-Netherlands P3B in the form of interest arising in Indonesia, only to be taxed in the Netherlands if the beneficial owner of the interest is a resident of the Netherlands and if the interest is paid for the debt more than 2 (two) years or paid in connection with the sale of industrial, commercial or scientific equipment credit (Indonesian-Dutch Tax Treaty Article 11 Paragraph (4)).

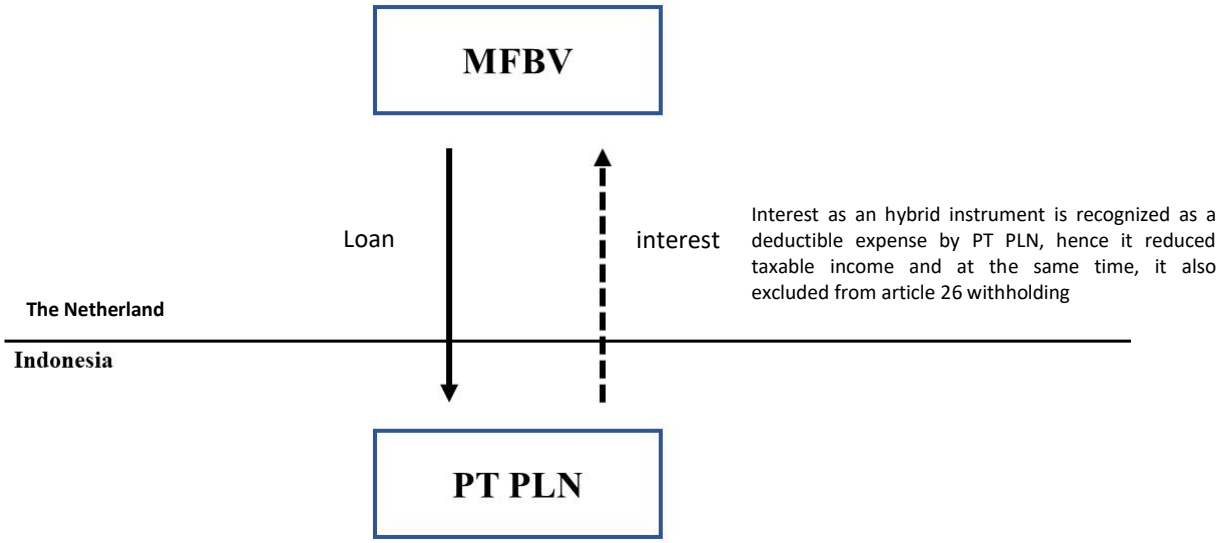
The two things mentioned in Article 11 Paragraph (4) of the Indonesian-Dutch P3B are conditions for interest to arise in Indonesia, only to be taxed in the Netherlands. In accordance with the definition of BO in general, MFBV can actually be said as BO for the interest payment if it is regulated by another party or carried out independently. However, in reality PT PLN itself holds power or control and on the other hand MHBV and MFBV do not have it. Regarding the debt period, the period has exceeded the requirement of more than two years (Decision of the Tax Court No.Put. 59998 / PP / M.IIB / 13/2015). PT PLN pays interest to MFBV for the term of the debt with the details of the return due as follows:

a. October 16, 2006 - October 16, 2011;
b. 16 October 2006 - 16 October 2016;
c. 28 June 2007 - 28 June 2017;
d. June 28, 2007 - June 28, 2037;
e. 7 August 2009 - 7 August 2019;
f. January 20, 2010 - January 20, 2020.

The scheme carried out by PT PLN can be classified in one of the hybrid mismatch arrangements conditions namely deduction / no inclusion (D / NI). D / NI causes the recognition of costs in a country and these costs are not income taxed in other countries. D / NI involves a hybrid instrument element, which is an instrument that is treated differently by the countries involved for tax purposes, more as debt in a country and as equity in another country (OECD Report, 2012).

Starting from the view that the hybrid transaction occurs because of the incompatibility of tax rules between the countries involved, not all of them cause mismatches because sometimes the results do not always lead to inconsistent results (Anggi, 2016). Like the scheme carried out by PT PLN which happened not because of differences in views between the rules of the Indonesian-Dutch tax regulations. The loan interest paid by PT PLN to MFBV is a hybrid instrument which is a cost (deductible of taxable income) of PT PLN and as MFBV interest income that is not subject to tax deductions in Indonesia which should be charged at 20%. This is the erosion of the tax base carried out by PT PLN in Indonesia by utilizing the Indonesia-Dutch Tax Treaty.

Scheme 3 – Hybrid Mismatch Arrangement conducted by PT PLN



As stated in the Tax Court Decision No.Put. 59998 / PP / M.IIB / 13/2015, the completion of the hybrid mismatch arrangements case conducted by PT PLN refers to the rules relating to transfer pricing. This happens because Indonesia does not yet have rules regarding hybrid mismatch arrangements. Even though PT PLN has a hybrid mismatch arrangements scheme, the principle of legality limits Indonesia to prove the BEPS scheme. Proving the tax base erosion carried out by PT PLN is done by proving that MFBV is not entitled to benefits from the Indonesia-Netherlands Tax Treaty in Article 11 Paragraph (4) and Article 26 Income Tax for interest on the loan to be imposed. Facts that prove in the Tax Court Decision No.Put. 59998 / PP / M.IIB / 13/2015. that is:

1. Company ownership PT PLN established MHBV in the Netherlands with 100% ownership. Then MHBV established MFBV also in the Netherlands with 100% ownership. Thus, MHBV and MFBV are directly and indirectly owned by PT PLN or in other words PLN controls MHBV and MFBV. The special relationship between PLN and MHBV and MFBV implies that the loan lending and interest payment schemes are regulated and determined. by PT PLN.

2. Borrowing mechanism Viewed from the point of view of the utilization of the results of international bond issuance, those who obtain benefits or enjoy the proceeds or proceeds are PT PLN. Regarding loans, MFBV functions are unclear. The scheme is carried out for certain purposes. In essence, loan funds from the issuance of bonds by MHBV are modified through MFBV. Interest from the loan substantially the beneficiaries are holders of international bonds, not MHBV or MFBV. In addition, from the fact that the listing of international bond issuance is carried out in Singapore, there is no guarantee that the bondholders are Dutch citizens.
3. MHBV and MFBV are a pass through / conduit company

There are characteristics that MHBV and MFBV are a pass through / conduit company, namely:

a. MHBV and MFBV do not have employees who carry out company operations so there are no remuneration fees;
b. the signing of the same Financial Report Management Report for MHBV and MFBV, namely Member A (Mr.A.Hakam) and Member B (Deuthsche International Trust Company N.V). Based on other research, Mr.A.Hakam turned out to be an employee of PT PLN;
c. MHBV, MFBV and Deutche International Trust Company N.V. has the same address, Herengracht 450, 1017CA Amsterdam;
d. most of the funds obtained from the issuance of international bonds by MHBV are directly channeled to MFBV and the interest income received from PT PLN is continued with almost the same amount from MFBV to MHBV and MHBV will forward it to bondholders in the form of interest payments; and
e. the interest fee paid by MHBV to bondholders is the largest portion compared to other costs (90%).

V. Study Results, Summary And Contribution

Hybrid mismatch arrangements or hybrid transaction is a transaction that is categorized differently by two or more countries due to differences in the domestic provisions of each country resulting in inconsistent results that cause tax obligations to be very low or not taxed at all. Starting from this view, not all hybrid transactions cause mismatches because the results do not always cause inconsistencies. OECD does not provide a standard definition for hybrid mismatch arrrangements. There are three conditions that can occur from this scheme, namely: double deduction scheme (DD), deduction / no inclusion scheme (D / NI) and foreign tax credit generators (FTC generators). The scheme carried out by PT PLN can be categorized as D / NI. The loan interest paid by PT PLN to MFBV is a hybrid instrument which is a cost (deduction from taxable income) of PT PLN and becomes MFBV interest income that is not subject to tax deductions in Indonesia. This is the erosion of the tax base carried out by PT PLN in Indonesia by utilizing the Indonesia-Dutch Tax Treaty.

BEPS 2 Action Plan on Neutralise the Effects of hybrid mismatch arrangements has not been the focus of the Indonesian Government. Until now, the Indonesian tax regulations have not regulated the hybrid mismatch arrangements scheme. If there are cases that can be classified as hybrid mismatch arrangements, Indonesian tax regulations still deal with them with rules related to transfer pricing. The settlement of the hybrid mismatch arrangements carried out by PT PLN is resolved by referring to the rules relating to transfer pricing by proving that the recipient of interest payments (MHBV and MFBV) is not the beneficial owner (BO) of the income. After being proven, PT PLN is not entitled to use benefits from the Indonesia-Netherlands Tax Treaty Article 11 Paragraph (4) because 2 cumulative conditions based on the agreement are not fulfilled.

International Journal of Psychosocial Rehabilitation, Vol. 24, Issue 07, 2020
ISSN: 1475-7192

OECD and G20 provide recommendations to neutralize the hybrid mismatch arrangements scheme for members and also other countries in the world. This recommendation is expected to be applied in these countries, considering that BEPS is a very complex problem. Prevention of hybrid mismatch arrangements scheme has been carried out by several countries. The European Union has the latest rules, namely the Anti-Tax Avoidance Directive (ATAD), which contains anti-hybrid measures that follow the principles of the BEPS 2 Action Plan. In addition, the Swiss state has implemented certain anti-hybrid rules in its tax rules. The tax rules are enough to prevent hybrid structures. Other countries that already have rules regarding hybrid mismatch arrangements are Australia. Australia has a tax regulation system that adheres to the substance over form principle so that it can reject forms of tax avoidance and also to eradicate the tax base.

Indonesia as a developing country in the future will continue to face challenges from global economic developments. One of the biggest challenges is the issue of BEPS that arises because multinational companies want to get the maximum benefit supported by the uncoordinated tax regulations between countries. The hybrid mismatch arrangements scheme is one of the schemes of BEPS that has not been the focus of the Indonesian government. The practice of this scheme already exists in Indonesia. Even though it can still be handled by regulations related to transfer pricing, regulations are still needed regarding the future hybrid mismatch arrangements scheme to provide legal certainty. Given the legal system in Indonesia uses the principle of legality.

ACKNOWLEDGMENT

The authors would like to thank to Directorate General of Taxes of Republic of Indonesia for the discussion. Also, credit goes to Indonesian Tax Court for providing the case studies.

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