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THE SMES IN ORDER TO FACE THE AFTA AND GLOBALIZATION ERA**Gita Arasy Herwida**

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Abstract: *Small and medium enterprises (SMEs) have contributed much to the growth of the economy in Indonesia. Further, this sector is also famous for its survival during the economic crisis in the late 1990's or specifically the crisis began in the late 1997. The survival of the SMEs in Indonesia from that crisis has alerted the government and economic societies for not only concerning the economic development to the large enterprises as most of those large enterprises were collapsed during the crisis. Prior the crisis, the government focused on the development in capital tight industrial sectors in a big capital such as: in banking and manufacturing for mass production. Most of policies that were issued at that time enhanced the development of this sector such as: policies that eased inward investment in some particular business; policies to provide value added tax exemption in the bounded zone area, etc.*

If we look back to the crisis time, the collapse of the large enterprises was mainly caused by their lack of ability in paying their overseas debt, which was in US dollar currency. The SMEs could survive mainly because of two reasons. First, the SMEs' business is mostly export oriented. They gained advantage from the payment which was in US dollar. The foreign exchange of US dollar to Indonesian currency, Rupiah, during the crisis was increased amazingly more than four times from the previous value. Second, most of the SMEs did not have liability with the foreign banks or foreign parties. Thus, they did not have to pay any liabilities in US dollar. This was in contrast to the large enterprises which mostly had liability with the foreign banks or parties. They had responsibility to give payment in US dollar which meant that their liability amount rose parallel to the increasing of US dollar's value. The flexibility of the SMEs in their working capital side was one of their key factors in their survival from the crisis. The SMEs do not rely on their all working capital on foreign debt, they use their own capital or may have debt from local sources.

Actually the government has already established a new department in regard to the development of the SMEs. The department is under the Ministry of Cooperatives and Small Enterprises which was established in 1993. This department has also issued some policies and strategic programs for the development of the SMEs and the cooperatives sector in Indonesia. The core objective of the establishment of this department was to overcome the difficulties which were faced, either externally or internally. However, the crisis effectively encouraged the government to give more attention to the SMEs. This was in terms of giving them

more opportunity to grow further to become strong large entities, rather than merely remaining at the small and medium stage. Another fact is that the SMEs are able to provide wide job opportunities, which Indonesia requires to deal with the increasing number of unemployment.

Keywords: *Small and Medium Enterprises, foreign debt, working capital*

I. INTRODUCTION

Overview of Small and Medium Enterprises in Indonesia

Small and medium enterprises (SMEs) have contributed much to the growth of the economy in Indonesia. Further, this sector is also famous for its survival during the economic crisis in the late 1990's or specifically the crisis began in the late 1997. The survival of the SMEs in Indonesia from that crisis has alerted the government and economic societies for not only concerning the economic development to the large enterprises as most of those large enterprises were collapsed during the crisis. Prior the crisis, the government focused on the development in capital tight industrial sectors in a big capital such as: in banking and manufacturing for mass production. Most of policies that were issued at that time enhanced the development of this sector such as: policies that eased inward investment in some particular business; policies to provide value added tax exemption in the bounded zone area, etc.

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Since the establishment of this department, many policies have been introduced which emphasize the capital sufficiency using the soft debt policy and up skill management strategic programs for the SMEs entrepreneurs. Nevertheless, the SMEs have expressed disappointment. They especially doubt the willingness of the government in the implementation of the program. Furthermore, they doubt the government's seriousness in preparing the SMEs to face the globalization particularly the commencement of the ASEAN free trade area (AFTA).

The problems that have to be faced by the Small and Medium Enterprises (SMEs) in Indonesia may continue to worsen as the ASEAN Free Trade Area (AFTA) will be introduced completely in the near future. The SMEs will have to compete with foreign companies which invest in Indonesia. Their sales may not be as high as before. Considering that income tax could account for at least 10 % to 30% or 20% in average of their expenses the working capital for the following years will also be decreased. This essay will argue whether the existing tax concessions provided for the SMEs in Indonesia are sufficiently support the SMEs in order to face the AFTA and globalization era.

This article will analyze the Indonesian tax legislation which deal with the SMEs in Indonesia and will compare it to the Australian tax legislation for the SMEs. Each analysis of Indonesian and Australian tax legislation will be supported by some written opinion, evidences from journals and articles. In this article, the Australian tax legislation for SMEs is used for a role model which objective is to give an overview and comparison for Indonesia in providing tax legislation and tax concession for the SMEs.

The first section will provide various definitions of the SMEs in Indonesia. The second section will discuss the role of the SMEs in Indonesia's economic development. The third section will discuss the AFTA, and identify problems that will arise for the SMEs. The fourth section will discuss whether or not Indonesia provides adequate tax concession for the SMEs. The writer will provide some existing tax regulations and policies that are related to the SMEs, and evaluate the effectiveness of the existing policies. The fourth section will confer some tax concessions provided by two developed countries, Australia and the UK, as a comparison model. The fifth section will identify the appropriate tax concessions for the SMEs in Indonesia. This section will also argue that Indonesia should adopt some tax concession from other countries with some adjustments.

What are the SMEs?

The SMEs have several definitions; every government department provides a different definition of SMEs. The definition of SMEs states at the Law no.9 of 1995 are small enterprises which are owned by Indonesian citizens, independent or not affiliated with other enterprises (subsidiary or branch) with or without legal licensing. Furthermore the classification of SMEs in term of assets and annual sales are as shown in Table 1 below:

Table 1. The Definition of SMEs in Indonesia Due to The Amount of Assets and Annual Sales

SMEs are defined as:		
<u>Small</u>	With assets of < Rp 20 million	Annual sales
<u>Enterprise</u>	(excluding land and building)	volume not more than Rp.1 billion
<u>Medium</u>	With assets > Rp 20 million	Annual sales
<u>Enterprise</u>	(excluding land and building) but < Rp.10 billion(US\$1.176 million)	volume is > Rp.1 billion

Source: *SME Profile* in '<http://www.actetsme.org/indo/indo2000.htm>' (2005)

According to Table 1, the categorization of the SMEs from the annual sales amount is less than 1 billion rupiah for the small enterprises, and more than Rp 1 billion rupiah for the medium enterprises. In accordance with the amount of assets, an entity will be part of small enterprises if it has assets amounting to less than 20 million rupiah. For the medium enterprises, the assets should be more than 20 Million rupiah, but less than 10 billion rupiah. Land and buildings are excluded from the distinguishing of the SME's assets.

The Ministry of Cooperatives and Small Enterprises provides a similar definition. It states that small enterprises must be owned by Indonesian citizens; and must be not affiliated with other medium or large entities either as branches or subsidiaries, in a direct or indirect relationship. Further, their net assets must be not more than 200 million rupiah excluding land and buildings, or their annual sales must be not more than 1 billion Rupiah per year. Medium enterprises are: entities with assets between 200 million rupiah and 10 million rupiah excluding land and buildings, owned by Indonesian citizens, independent and not affiliated with large enterprises, either branches or subsidiaries, in a direct or indirect ways. The same definition of SMEs in the Ministry of Cooperatives and Small Enterprises is also used by the Indonesian Bank (BI). The Ministry of Industry defines SMEs as entities which have assets less than 600 million Rupiah.

The Indonesian Industry and Trade Room (KADIN) categorizes SMEs according to the number of workers, the amount of assets, and the amount of annual sales. SMEs must not have more than 300 workers, the assets are not more than 250 million rupiah, and the annual sales amount should be under 100 million rupiah. Moreover, the Ministry of Trade stated that SMEs are entities which have not more than 25 million Rupiah in capital. The Indonesian Bureau of Statistics determines SMEs from the amount of workers. There should be from 5 to 19 workers for the small enterprises, and 20 to 99 workers for the medium enterprises. Furthermore, the Indonesian General Directorate of Taxation only provides the definition of small entrepreneurs, not the enterprises, in the Value Added Tax Legislation.

The differences in the definitions of SMEs cause a difficulty in setting an appropriate policy for the SMEs. In addition, the SMEs may also be confused as to which regulation they should follow. What happens in Indonesia is that each department has their own objectives, due to its indicator, and they may make different policies and should reach their objectives as well (cite). The uniformity of criteria of SMEs is required to simplify the policy for SMEs. The uniformity may also reflect the coordination within the department and an integrated and comprehensive SMEs policy should be developed. Once the certain definition is made, the policy that will be made should follow.

II. THE ROLE OF SMEs IN INDONESIA

The SMEs play an important role in economic field of Indonesia. The SMEs occupy 99.95 percent of the total amount of entities in Indonesia. The employment of small enterprises was 89 percent of total employment, while medium enterprises were 10.55 percent in the year of 2000. On the other hand the contribution of the small enterprises for the Gross Domestic Product (GDP) was only 41 percent and the medium enterprises were 16 percent. From the percentage of the employment and the percentage amount of the total entities in Indonesia, it is shown that the SMEs provide employment fields as the unemployment rate in Indonesia is very high. Furthermore, the high percentage of SMEs from the total amount of entities is proof that the SMEs should not be undermined anymore.

In contrast, the fact that the SMEs only contribute a low percentage for the GDP should be carefully examined. Because the small amount of the SMEs contribution in the GDP, it does not mean that they should be ignored. The success of the SMEs depends on their productivity in carrying on their business. Productivity is related to the quality of the human resources, something that most SMEs in Indonesia struggle with. Therefore, referring to the huge number of the SMEs in Indonesia and considering the SMEs will give more job opportunities, the improvement of the SMEs in productivity, the government should develop appropriate policies related to the development of the SMEs in Indonesia. The awareness of the government to the SMEs can be seen from the policies they make, and, furthermore, the attention should be integrated from all elements of the government to ensure that the policies do not overlap, or even worse, contradict each other. The Table 2 shows the changing of the SMEs and large enterprises in Indonesia from 1997 to 2002, as reported by the Central Agency for Statistic in 2003.

From the table below, small enterprises lead in the number of enterprises in Indonesia, as this sector occupy more than 99% of total enterprises. In 1998, while the huge economic crisis hit Indonesia, the number of small enterprises decreased. However, compared to they experienced a smaller reduction. From 1997 to 1998, the amount of small enterprises decreased 7.4%, while medium enterprises and large enterprises decreased by 14.1% and 12.68%. Respectively as Indonesia started to recover from the crisis, the enterprises started to increase. It is shown in Table 2 that the number of all enterprises increased.

The leading position is still occupied by small enterprises, followed by medium enterprises and finally large enterprises.

Table 2. The Growth of Business Distribution in Indonesia by The Size of Business Entities from 1997 to 2002

Year	Small	Medium	Large	Total
1997	39,704,661 (99.843)	60,449 (0.152)	2,097 (0.005)	39,767,207 (100)
1998	36,761,689 (99.854)	51,889 (0.141)	1,831 (0.005)	36,815,409 (100)
1999	37,859,509 (99.857)	52,114 (0.138)	1,885 (0.005)	37,913,608 (100)
2000	38,669,355 (99.854)	54,632 (0.141)	1,973 (0.005)	38,725,960 (100)
2001	39,869,505 (99.850)	57,681 (0.145)	2,084 (0.005)	39,929,270 (100)
2002	41,301,263 (99.847)	61,052 (0.148)	2,198 (0.005)	41,364,513 (100)

Source: *SME Profile* in '<http://www.actetsme.org/indo/indo2000.htm>' (2005)

III. THE ASEAN FREE TRADE AREA (AFTA)

In January 1992, the Association of South East Asian Nations (ASEAN) declared their new agreement in the trading field called ASEAN Free Trade Area (AFTA). AFTA is a program of regional the trading objective of which is the comprehensive regional tariff reduction. The agreement also includes the liberalization of trading within ASEAN countries. This includes: the agreement in determining product certification standard; simplification the procedure in customs; and the elimination of zero tariff barriers.

The first agreement was signed by the original six members of the ASEAN, which are: Malaysia; Thailand; Philippine; Singapore; Brunei Darussalam; and Indonesia. The members of the ASEAN changed as Vietnam entered the organization in 1995, followed by Laos and Myanmar in 1997, and the youngest member Cambodia in 1999.

Currently, the ASEAN has Common Effective Preferential Tariff (CEPT) as the tariff for trading transaction within the ASEAN countries. The CEPT was reduced to 0-5% by the year 2002/2003 for the original six members. It will be

reduced by 2006 for Vietnam, 2008 for Laos and Myanmar, and 2010 for Cambodia. As the crisis hit the ASEAN region in 1998, the original six members of the ASEAN agreed to quicken the pace of tariff cuts in one year. The ten members of the ASEAN started to reduce their tariffs for the majority of goods to the range of 0–5% in 2003. Finally the complete commencement of CEPT was planned to be started in 2007 for the original six members of the ASEAN and 2012 for the four new comers.

However the trading between them has growth very slow, and the AFTA has not provided many benefits for Indonesia. Under the AFTA and its implementation of tariff reduction and simplification of customs system, all products from the ASEAN region will be more easily to be traded cross the borders of member countries. Further, the investor countries will be more likely to invest in more than one country in the ASEAN region. In 2002, one year before the tariff reduction begun, Indonesia already experienced the negative effects of the AFTA, as the manufacture of 'Toyota Soluna' cars moved their assembling company to Thailand, and Indonesia started to import cars from Thailand. The SMEs will also suffer loss from the relocation of some multinational companies from Indonesia to other countries. Because being a sub contractor of a multinational company is one of the methods that the SMEs employ in the business competition in Indonesia. Multinational companies sub contract some parts of their production process to the SMEs, where the business has a relation to the multinational company's product. For example, a multinational company which produces of shoes will sub contract the making of the shoe soles to the SMEs. Results in employees are losing their jobs and money going out from the country.

On the other hand, the competition will significantly increase as all products can are competing each other more easily. The readiness of enterprises in Indonesia is still questionable, in particular is the SMEs. The SMEs, however, are still struggling in their availability of capital, and their problem in preparing the competitive human resources. The government has already issued some policies to encourage the improvement of the SMEs performance. This has involved departments such as: the Ministry of Trade; the Ministry of Cooperative and Small and Medium Enterprises; and the Ministry of Industry. However, the involvement of the Taxation General Directorate has been minimal and it is difficult to find easily the policies in the taxation field which are particular to the SMEs. The discussion about the taxation legislation for the SMEs will be provided in section four.

Faisal Basri, an economist, believes that Indonesia has suffered more since the commencement of AFTA, because according to Indonesia's economic condition, the country has not ready yet for the open market, which also means open competition. Not many of the entities in Indonesia are ready to face the free market as there are weaknesses in management, marketing, productivity, and competitive advantage. Basri believes that Indonesia may survive facing the AFTA if the trading agreement also involves other countries such as China and Japan. The enlargement of trading will give an opportunity to Indonesia to expand its target market. There is a trading agreement between the AFTA and Chinese economic and trade ministers, who already consented to have a Free Trade Area (FTA) in 2010 for the six original members, and 2015 for Vietnam, Myanmar, Laos, and Cambodia. Nevertheless, Indonesia do not have any choice to avoid the commencement of AFTA or resist the global free trade. The Indonesian

government should take a smart, fast action to face the free trade by giving and applying the appropriate legislation in all aspects of industrial element. The especially important is for the SMEs because Indonesia's economy heavily relies on the SMEs sector. Taxation may take part on it. Concessions for the SMEs may help the SMEs to minimize their expenses and maximize their profit. Therefore they could continue to carry on their business. Otherwise, Indonesia will only become a target market for other ASEAN countries, and the SMEs in Indonesia will be more likely unstable than in the previous crisis to collapse.

IV. THE EXISTING INDONESIAN TAX CONCESSION FOR THE SMEs

It is not easy to find the term of 'SMEs' in the Indonesian taxation legislation 2000. However we can still find the term "small entrepreneur" and "medium entrepreneur". But the definition of "small entrepreneur" can only be found in the Indonesian Value Added Tax Legislation No. 18 2000. We can not find term of the "small enterprises" or "medium enterprises" in the Indonesian taxation legislation.

The Indonesian Income Tax Legislation No.17 2000 (ITL)

As mentioned above, the term of SMEs can not be found in the ITL. Therefore, it is likely that the Income Tax legislation does not provide any legislation particularly for the SMEs. The definition of the SMEs can not be found anywhere in its legislation. However, there are some articles in the ITL that have a relation with the SMEs. This is even though they do not necessarily give many contributions to the concession to the SMEs for income tax purposes.

Division III article (3) point (a) (2)

The first article is in division III article (3) of the ITL. This concerns the exemption income for income tax purposes. Point (a) (2) states that, the given assets that are obtained by: family who has one degree relationships; religion community; education entities; or social enterprises; or small entrepreneurs including cooperatives that are determined by the Ministry of Finance, as long as they are not associated in the purpose of business, works, or proprietary between those two parties, will be exempted as tax object for the income tax purposes. The article does not mention the SMEs, but, the terms of small entrepreneur and medium entrepreneur may be interpreted as the owner of the SMEs. So, if the small or medium entrepreneur receives assets from the other parties, who do not have any relation to the enterprises, the assets will not be imposed of the income tax. This is beneficial for the SMEs because the SMEs have an opportunity to exercise the assets, in order to enhance their productivity if the assets that are given are worth enough to be used for this purpose. In reality, the activity of giving assets to business entities is very rare, compared to other parties which are mentioned in that article such as entities in religion, education, or social enterprises. Therefore, even though this article is only useful for the SMEs which obtained assets in the way that is stated in this article.

Division III article (3) point (k)

The second article is an article in the ITL which mentions the SMEs in relation to venture capital. However, the favor of the article is for companies who

have a venture capital with the SMEs. As states in the division III article (3) of the ITL, in regard to the exemption income for the income tax purposes, point (k) states that the income that is acquired by the venture capital company, as the profit allocation from its partner company, which carries on business in Indonesia, is exempted from taxation. The partner companies, which are mentioned in this point are small companies, medium companies or any companies which operate in the business sectors that are determined by the Ministry of Finance. Furthermore, the shares of the partner company are not traded in the stock exchange market in Indonesia. This article, however, does not support the SMEs in regard to income tax purposes. The favor of this article which is given to the venture capital company, aims to support the government policy for the growth of the SMEs, from the availability of capital. This article exists in order to encourage large enterprises to take part in the government program for the SMEs, through the venture capital company.

Division III article (14) point (1) and (2)

The third article, which probably can be considered as the legislation that has a relation with the SMEs, concerns the taxation calculation method for the individual tax payers, which have a turnover of less than 600 million Rupiah. ITL provides two tax calculation methods for the individual tax payers. This is likely a concession for the SMEs as individual tax payers. The calculation methods are stated in article 16 of the ITL. The first method is book keeping which must be prepared according to the Indonesian Accounting Standard Board (IASB), with some adjustment for taxation purposes. The adjustment can either be the method that must be used for the calculation of: depreciation; inventory; book value of assets; and the allowable expenses which is in article 6(1)(2), 7(1), and 9(1 (c),(d), and (e)). Tax payers whose annual turnover more than 600 million Rupiah, are obliged to calculate their income tax by using this method.

The second method is using the norm calculation method, which concerns the taxable income from multiplying the gross income with the norm percentage, which is stated in article 14 of the ITL. This method is allowable for individual tax payers, where turnover is not more than 600 million Rupiah. The norm percentage will be determined in the decree issued by the Ministry of Finance and also stated in the article 15 of the ITL. For the SMEs which carry on the business of the individual tax payers, and which have an annual turnover of less than 600 million Rupiah, may apply to use the data recording method instead of the book keeping method. This does not have a direct impact on the amount of income tax that they should pay, but this method will simplify their works. Especially for the SMEs which do not have competent human resources to comply with the accounting methods, using the data recording method for recording their transactions and calculating the amount of the gross profit will be easier for them.

Division VII article 31A point (1) and (2)

Article 31A point (1) and (2) state that tax payers who are investing in some particulars business or in some particular regions in Indonesia which are regulated by the decree of The Indonesian government will get some tax incentives as shown below:

1. Reduction of the net income with maximum of 30% from the investing amount. The reduction is for 6 years with allocation of 5% reduction per year

2. Acceleration of depreciation and amortization
3. Retain a longer compensation of financial loss but not more than 10 years
4. 10 % tax rate for dividend in regard to article 26 of ITL; for non-resident tax payers; unless tax treaties agreement determines lower tariff.

The objective of this article is to enhance the increasing of a direct investment to Indonesia through foreign capital investment or domestic capital investment for some particular business such as: export oriented industry and industry in the rural area of Indonesia in order to achieve the equal distribution of Indonesian development. This article can be used for any possibilities for any agreements with other countries in trading, investment, etc. Indirectly, we could say that this article is mainly for the favor for those who have invested in a big value of money.

This article is beneficial for those who invest their money to those which are regulated in the decree of the Indonesian government. The SMEs seem taking an important part in the achievement of equal development distribution in rural area but it is more likely that the SMEs are not included in this article.

Income Tax Rates for Annual Assessable Income

In the ITL, income tax rates for annual assessable income are divided into three different rates. The first is income tax rates for the resident individual tax payers, which is regulated in article 17(a) of the ITL. The second is tax rates for resident companies and entities, which is stated in article 17(b) of the ITL. The third is tax rates for non-residents either individual or entities, which is in article 26 of the ITL. However, there is no tax rate distinguish for the SMEs tax rate. All tax rates apply to all tax payers, and the distinguishing factor is the level of income which tax payers earn in the current tax year.

The Indonesian Value Added Tax legislation (VATL)

The VATL more effectively recognizes the term of small entrepreneurs than the ITL even though the term of small enterprises is still very difficult to find. The limitations for small entrepreneurs are for entrepreneurs stated in the decree of the Ministry of Finance No. 552/KMK.04/2000 which was amended by No. 572/KMK.03/2003. The small entrepreneurs are for those who in one income year deliver tax goods or tax services, or either tax good and tax services for which the gross amount of delivery is not more than 600 million rupiah. There will be exempted from the liability of paying and lodging the Value Added Tax (VAT) return. In addition they are not required to register their business as Tax Entrepreneurs. This decree was commenced from 1 January 2004. The deputy of the Ministry of Finance, Mr. I Gde Erata, stated that the commencement of this decree has offered favor of the administration cost efficiency both for the small entrepreneurs and the General Directorate of Taxation. The meaning of administration cost is the cost that arises in purpose of completing the obligation in the value added tax, such as paying, filling and lodging monthly VAT tax return.

However, the gross amount for the circumscription of small enterprises which is 600 million rupiah for tax goods and tax services, are too small. This opinion has been reinforced by the Director of Cooperatives Board Wahab As'ary, commenting to the commencement of the decree of the Ministry of Finance No. 572/KMK.03/2003 in January 2004. According to Wahab As'ary, the amount of 600 million rupiah is too small in this current time as there are many small

enterprises which can achieve that amount. The entities that have a gross amount beyond the allowable amount will face difficulty to handle their status as tax entrepreneurs. This is because they have to have a tax file number, as they also have to be able to fill in other tax returns. He added that considering the current circumstances the reasonable amount of gross turnover is 5 billion rupiah per year.

Some concessions for some particular business also provided by the value added tax legislation through the decree of the Ministry of Finance especially for transaction in the bounded zone area, for example: Batam island and some other places in Indonesia. Those tax incentives will be useful for the SMEs who trade with companies located in the bounded zone area, especially for export purposes.

The Bill of Taxation Legislation

In response to the critics from many social elements in the society about the weaknesses of the existing tax legislation in general, and the lack of awareness of the taxation policy with the growth of the SMEs, the government has arranged new bill for taxation legislation in regards of reformation in taxation sector. The bill is still in the process of being discussed in the Indonesian Parliament. The bill includes tax reform policies for the general tax legislation, the income tax (IT), value added tax (VAT), and other tax regulations. In July 2007, the government passed the Law no. 28/2007 about the General Tax Legislation which will replace the existing General Tax Legislation namely Law no.16/2000, this new Law will be commenced for the 2008 tax year. We are still waiting for the Income Tax and Value Added Tax bill to be passed and commenced. At the meantime, this paper will examine the content of the new law and the bills regarding its influence to the development of SMEs in Indonesia.

The current tax rates are progressive tax rates for both individual and corporate tax rates, which are stated in the article 17 of the ITL 2000. In the new bill, there will be new tax rates for the individual and corporate tax payer. Firstly, tax rates for the individual tax payers will still be progressive tax rates but the rate's layer reduced from 5 to 4 layers by eliminated the 10% tariff. Moreover, the highest tax rate will be gradually reduced to 33% for 2007 tax year and 30% from 2010 tax year. Also, the amount of income which will be imposed with the lowest tax rate will increase from 25 million Rupiah to 50 Million Rupiah. In sum, the new tax rates is likely give favor for the individual tax payers especially or those whose income between 25 million to 50 million Rupiah which previously were imposed by two tax rate's layers, 5% and 10%. Furthermore, for the SMEs which business is as individual business, the new rates especially the gradually reduced rates may also give an opportunity for them to make an increasing earning after tax forecast, thus, indirectly will influence its business performance.

However, a grey cloud may occur for corporation tax payers as the bill is about to impose single or flat rate which is 30% or in other word is the same with the current highest corporate rate. The bill stated that the rate will be gradually reduced to 28% fro the 2007 tax year and 25% from 2010 tax year, it will be faster for listed go public entities. If the Parliament agrees with this one, it is likely will trigger a negative sentiment from the business society as well as from the public. This is because the effect of the single tax rate implementation will not merely be in the amount of its profit after tax but may also influence other aspect such as labor salary, the price of goods, and may increasing the tension in the

business competition. Indeed, this high tax rate will give a significant shock influence for SMEs which included as corporate tax payers.

The taxation policies will play an important role for the SMEs. The amount of tax, whether income tax, value added tax, or any other taxes, will influence the profit achievement of the entities. As mentioned in the first section, income tax will comprise at least 10% to 30% of the expenses; it depends on the level of gross profit retained by the entities.

Moreover, the income tax bill still does not mention the existing of SMEs or at least recognize SMEs as a type of business entities, even it is likely hidden in the article which explains about the income criteria for those who are entitled of using conventional book keeping and not oblige to make an appropriate book keeping as mention in Indonesia Financial Accounting Standard (PSAK). The article stated that for tax payers whose income are not exceeded from 1,8 billion Rupiah in one tax year are entitle in using conventional book keeping and to use a percentage norms; which will be regulated by the decree of the Ministry of Finance; in calculating its tax payable.

Compared to other countries in Asia, such as Thailand and Taiwan, our tax legislation (both the current legislation and the bill) awareness of SMEs is still very little. Those both countries provide a low flat income tax rate for their SMEs which are 4 per cent in Thailand, and 2 per cent in Taiwan. Value-added tax (VAT), on the other hand, will influence the selling price of the goods or services and the competitive advantage of the product in the global market.

V. AN OVERVIEW OF TAX CONCESSION FOR THE SMEs IN AUSTRALIA AND THE UK

Australia and the United Kingdom (UK) are good examples for Indonesia of a positive way to treat SMEs for taxation purposes. Both countries are developed countries, which are economically, politically, and socially strong compared to Indonesia. Both of them have a high rating in the development of industry and technology. However, they are still aware of the development of the populist base economy, including the SMEs. They provide considerable tax concession for the SMEs. The concessions provided are not merely income tax concessions they include incentives in the Capital Gain Tax (CGT), Goods and Services Tax (GST), and concessions of tax in state level. This section will resent an overview of the tax concessions for the SMEs in Australia and the UK, as developed countries. They are good models for Indonesia which is a developing country and is still trying to reform its tax legislation. It is also the process of increasing their awareness level for the existence and development of the SMEs.

Tax Concession in Australia

Australia provides four tax concessions for the SMEs. The tax concessions are: simplified tax system (STS); CGT concessions; pay-as-you-go (PAYG) concessions; GST concessions; research and development (R&D) tax offset; state tax concession and some other concessions. All SMEs are entitled to obtain those concessions. However, there are some tests, which may be different for each concession, which should be satisfied by the SMEs.

Simplified Tax System (STS)

The simplified tax system (STS) is the newest integrated taxation concession system for the SMEs, designed for the purposes of income tax. The STS can be called integrated because this system does not merely provide a single concession from one point of view. This system tries to integrate many aspects in accountancy with taxation implications. This system also can be recognized as the most complete tax concession system compared to other concessions. The objective of the STS is to provide a simple operation according to the calculation system in three areas in accountancy. They are cash accounting, depreciation, and trading stock. Cash accounting and depreciation are compulsory, while trading stock is optional for SMEs that are eligible to be registered as STS tax payers. Not all of the SMEs are eligible to become STS tax payers, there are some criteria that should be satisfied by the SMEs. To be eligible the SMEs must carry on business in the income year, have average turnover for the last 3 or 4 years less than AUS \$ 1 million, and have depreciating assets up to AUS \$ 3 million.

Cash accounting in the STS is the basis that is used for the STS tax payers, in order to recognize income and expenses. The operations of cash accounting in general adopt the general accounting principles for income tax purposes, unless for the recognition of expenses. Under the general accounting principles for income tax purposes, which is developed by case law and practice, expenses are not always recognized on the payment action. Expenses under the STS must be recognized by the time the entities make cash out action. The income will only be recognized at the time that the SMEs receive the payment from the transaction. The STS tax payers may experience losses from strict cash basis expenses recognition, because they can not recognize their accrued expenses in the financial statement.

Depreciation in the STS does not require a depreciation calculation for individual assets. Under the STS, there will be two groups of assets. The first group is assets which have cost acquisition, excluding GST, of less than AUS \$ 1,000.00. Assets in this group will be written off instantly. The second group is assets which have a cost acquisition amounting for more than AUS \$ 1,000.00. The second group is divided to two groups group A and group B, according to the asset's lifetime. Group A is for assets for which the lifetime is less than 25 years. The depreciation rate for group A is 30%. Group B is for assets which have a lifetime of more than 25 years, and which obtain a 5% depreciation rate.

The trading stock value under the STS is taken from value at the year-end, compared to the value at the opening of trading stock. The treatment is either adding the increasing value in the calculation of assessable income, or claiming the decreasing value for deduction. The increasing or the decreasing value will only be treated for income tax purposes if the amount is more than AUS \$ 5,000.00. Payne argues that the entities which apply this system constantly experience more gain than others that are not constant.

CGT Concession

CGT concession is stated in the division 152 of Income Tax Assessment Act (ITAA) 1997. This concession offers four types of concessions. The first type is 15 year held assets retirement exemption. The second is 50% gain reduction from transactions under CGT events. The third type is retirement exemption (life time limit), and the fourth is replacement assets roll-over.

Other Concessions

Other concessions are: R&D tax offset which aims to encourage the SMEs to develop their productivity; state concessions which are made by the state government; GST concessions which give option for SMEs which have a turnover under the limit for not registering and also provide advantages in cash flow; Pooled Development Funds (PDFs), concessions that are presented for registered investment companies which have investment in SMEs.

Tax Concession in The UK

The SMEs in the UK The type of tax concessions for the SMEs in the UK has similarity with the Australian tax concessions. The UK concessions also provide a simplification of calculation and accounting method for the SMEs. The UK has a financial reporting standard for small entities (FRSSE) which has simplification of calculating and reporting accounting system. The SMEs also retain more deduction for the research and development (R&D) expenses than non-SMEs companies if their R&D expenses are more than AUS \$ 10,000.00. SMEs are entitled to receive 50% additional deduction for the R&D expenses, besides, large companies are only entitled for 25% additional deduction. Further, the SMEs are allowable to deduct their salary and benefit expenses of the entity's owner as long as the amount does not exceed the rate which is stated in National Insurance Contributions (NICs). There is also concession for SMEs who are doing capital investment in machinery and plant by receiving 25% higher rate than other entities. There are also shares investment incentives, and employee share system which aim to enhance high quality managers eager to run SMEs. Accordingly SMEs will be handled by the capable manager who can maintain the SMEs.

The Similarity and The Effectiveness of Tax Concession for SMEs in Australia and The UK

There are some similarities from the Australian and the UK tax concession of the SMEs. Firstly, both of them provide concession in a type of giving simplification in calculation and recording of accounting method for the SMEs even though in a different way. Secondly, the SMEs are entitled for some deductions which are not allowable for non-SMEs, R&D expense is one examples of it. Thirdly, both countries offer concession for companies who invest in the SMEs, which objective is to encourage the establishment of new SMEs rather than to maintain them.

However, both government of Australia and the UK still receive some critiques from some experts which mostly hit the effectiveness of the tax concessions. There is some mischief that found by them such as: the concessions are effective merely for the small size entities rather than the medium size and there is still no uniformity for the definition of SMEs. Especially for the UK, Freeman argues that mostly of the tax concessions can only be applied for the corporate SMEs rather than for both for corporate and unincorporated SMEs.

VI. SUGGESTION TO THE TAXATION POLICY FOR THE SMEs IN INDONESIA

From the overview of the current Indonesian tax legislation for the SMEs, identify the expected bill of Indonesian tax reform, and look at models from Australia and the UK. Indonesia has lack of taxation policies in particular for the SMEs compared to Australia and the UK. The tax policies for SMEs that are now commencing in Indonesia are mostly in the VAT which is similar to the GST concession provided in Australia. There are probably some articles in the ITL that have an indirect relation with the SMEs. However, those articles sometime are too broad or the objective is merely to enhance the growth of SMEs in terms of numbers rather than to maintain its productivity. Therefore, there should be more tax concessions for the SMEs for the income tax purposes. Tax concessions for SMEs in Australia and the UK may become a good models even though there will need some adjustment if Indonesia will use similar concessions.

Here are some ideas of having an appropriate tax concessions for the SMEs in Indonesia, which some of them are adapting from the Australia and the UK tax concession. The First, upon off all, there should be a certain criteria for the SMEs from different point of views such as: the amount capital; number of workers; annual turnover; and the amount of depreciation assets excluding land and buildings; that can be used for all parties in Indonesia which have interest to the SMEs whether from the government, investors, or entrepreneurs. The uniformity may prevent overlapping between policies and may avoid such parties which try to take advantage from the policies.

The second, the concessions should be divided to two groups due to its objective which are to encourage investment in SMEs and or establishment of new SMEs, and to maintain and enhance the existing SMEs to become more productive and well established. Concession for the investment in SMEs or establishment of new SMEs is like in the division III article (3) point (a) (2) of the ITL about the given assets and the division III article (3) point (k) about venture capital. However, as the numbers of SMEs are still occupying from total numbers of enterprises, tax concessions for maintaining purposes will be more important from tax concessions for establishment purposes. For maintaining purposes, some tax concessions that may be provided such as:

1. giving different income tax rate for the SMEs as stated in the bill of tax reform which may increase the performance of SMEs from the profit achievement side. 10% tariff seems reasonable even though some experts believe that this tariff is still high compared to our neighborhood countries in Asia.
2. giving a simplification of calculating and recording for the availability of financial statement purposes. Australia has the STS with the cash accounting basis and the UK has the FRSSE. Indonesia has article in the division III article (14) point (1) and (2) of the ITL which is provided only for individual tax payers without mention explicitly about this application to the SMEs. There should be a simplification of calculation method or system for SMEs which have legal form as corporate tax payers. Considering human resources in the SMEs mostly experience difficulty in applying the Indonesian general principle of accounting with some adjustment for taxation purposes. Furthermore, the method should be supported by the clear guidelines which are easy to follow, and the tax commissioner should welcome to explain clearly if there are queries from the SMEs in regard to the system.

With an appropriate design and an accurate implication of the simply calculation method, the SMEs may gain efficiency of time and administrative expenses. Besides, the different income tax may give the SMEs to retain bigger net profit than the net profit gain under the current income tax rates. It means that the SMEs may achieve bigger amount of working capital which can be used for their next operational. It may also help the SMEs for their existence and competitive advantage in the middle of AFTA and the world global free trade.

The third, there should be distinction between tax concessions for the small enterprises and for medium enterprises. Otherwise, the same problem of application will be faced as it is experienced by Australia. Considering the wide range of criteria between small enterprises and medium enterprises, the objective of tax concessions for the small entities are to expand their business to the medium level and for medium entities is to become larger and stronger entities.

The fourth, there should be coordination between the tax legislation made by the central government with tax legislation issued by the province, city, and district government. As the commencement of the Act No.22/1999 for the region autonomy, the local governments tend to maximize their revenue through some retribution or other local taxes.

In conclusion, Indonesian government should provide more tax concessions for the SMEs in order to strengthen the SMEs capability in facing the AFTA and globalization. The bill of tax reform which is still being discussed in the Indonesian Parliament may become a trigger for the government awareness to the importance of SMEs in Indonesia economy. Tax concessions which are provided by developed countries such as Australia and the UK may become good models for Indonesia. Indonesia may adapt some tax concessions with some adjustment in regards to condition in Indonesia.

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