

Indonesia

Eddy Marek Leks

Leks & Co

General

1 Legal system

How would you explain your jurisdiction's legal system to an investor?

Indonesia has a civil law system. Indonesia has the following hierarchy of laws and regulations, in descending order:

- the 1945 Constitution of the Republic of Indonesia;
- decrees of the People's Consultative Assembly;
- law or government regulations in lieu of law;
- government regulations;
- presidential regulations;
- provincial local regulations; and
- regency or municipality local regulations.

An injunction can only be obtained from the court, through a claim. Indonesian courts administer both law and equity. The parol evidence rule does not apply in Indonesia. If the words of agreement may be interpreted differently, the parties' intentions under the contract must be investigated. Generally, contracts can be made either orally or in writing. No formalities are required unless otherwise provided by law.

2 Land records

Does your jurisdiction have a system for registration or recording of ownership, leasehold and security interests in real estate? Must interests be registered or recorded?

Indonesia has a registration system for land, registering the ownership of land and its security interests (mortgage right). No registration for leaseholds is required except for the lease of a condominium unit or if it is for a foreign national's residential use. To date, large parts of the land in Indonesia are still unregistered. Since the land has not been registered, no certificate of land is issued by the National Land Agency (BPN).

Mortgage rights for land or buildings must be registered. The registration of a mortgage right will be followed by the creation of a book of land of the mortgage right. The mortgage right will be operative from the date the book of land of the mortgage right is made. A mortgage right certificate will be issued by the BPN and delivered to the mortgage rightsholder. This certificate has executable power and has the same effect as a final and binding court's decision. A building can be secured by fiduciary security. Fiduciary security must be made in a notarial deed and registered to the Fiduciary Registry Office. It comes into effect on the date of its recording in the Fiduciary Registry Book. A fiduciary security certificate is issued by the Fiduciary Registry Office. This certificate has executable power and has the same effect as a final and binding court decision.

3 Registration and recording

What are the legal requirements for registration or recording conveyances, leases and real estate security interests?

Every transfer of a land right and right of ownership of a condominium through sale and purchase, exchange, bequest or other legal action, except for a transfer of the right through auction, may only be registered if it is evidenced with a deed from a Land Deed Officer (PPAT). See question 2 for real estate security rights.

The following taxes or stamp duty apply to the acquisition of real estate in Indonesia:

- land and building acquisition levy of 5 per cent, paid by the purchaser, calculated on the transaction value or taxable object value, whichever is higher;
- income tax at 5 per cent, paid by the seller, calculated on the transaction value or taxable object value, whichever is higher;
- value added tax of 10 per cent, paid by the purchaser (VAT on the transfer of modest housing and modest condominiums is exempt);
- sales tax on luxury goods of 20 per cent, for a condominium or an apartment with a sale value of 5 billion rupiahs or with an area of 150 square metres (withheld upon signing of conditional sale and purchase agreement with the developer), whereas for land with a sale value of 5 billion rupiahs or with a building area of 400 square metres;
- land and building tax of up to 0.3 per cent calculated from the taxable object value, paid annually;
- stamp duty of 6,000 rupiahs;
- the PPAT's handling fees for land transfer, which are negotiable; and
- a state contribution revenue, which depends on the size of the land.

4 Foreign owners and tenants

What are the requirements for non-resident entities and individuals to own or lease real estate in your jurisdiction?

What other factors should a foreign investor take into account in considering an investment in your jurisdiction?

A foreign national or foreign legal entity can only obtain a right of use and right of lease with certain conditions. A foreign national whose presence is in the national interest may own a house that is built over a right of use of state land, or that is subject to an agreement with the holder of a land right, or own a condominium unit that is built over a right of use of state land. To obtain either a right of use or right of lease, each foreign national and foreign legal entity must be located in Indonesia.

To conduct real estate business, a foreign national or foreign legal entity must establish a limited liability company (PMA). At present, there is no restriction on a foreign national or foreign legal entity establishing a wholly foreign-owned company in the real estate sector. The investment in a PMA must be more than 10 billion rupiahs and the business plan or project of the PMA must be completed within three years.

5 Exchange control

If a non-resident invests in a property in your jurisdiction, are there exchange control issues?

There are no exchange control issues for foreign investors at present. Indonesia applies the national treatment principle, where the government gives all investors investing capital in Indonesia the same treatment no matter where they originate from, except for investors from a country that has privileges under a treaty with Indonesia. Investors are granted the right to transfer and repatriate the following in foreign currency, among others:

- capital;
- profits, bank interest, dividends, and other income;
- funds necessary for the purchase of raw and auxiliary materials, semi-processed goods, or processed goods, or the replacement of capital goods in order to protect the survival of the investment;

- additional funds necessary for financing capital investment;
- funds for the repayment of loans;
- royalties or fees payable;
- income of an individual foreign citizen working in a foreign investment company;
- proceeds from the sale or liquidation of the investment;
- compensation for losses;
- compensation for expropriation;
- payments made for technical aid, fees payable for technical and management services, payments made under project contracts, and intellectual property payments; and
- proceeds from the sale of assets.

Nevertheless, under the latest regulations from Bank Indonesia, all parties are obligated to use rupiah on transactions conducted within the territory of the Republic of Indonesia, applicable for cash or non-cash transactions. The transactions comprise any transaction with an intent of payment, settlement of other obligation using money and other financial transactions. The mandatory use of rupiah is exempted on certain transactions for the implementation of state budgeting, donation or granting from or to overseas, international trade transactions, bank savings or international financing transactions.

6 Legal liability

What types of liability does an owner or tenant of, or a lender on, real estate face? Is there a standard of strict liability and can there be liability to subsequent owners and tenants including foreclosing lenders? What about tort liability?

Generally, an owner of real estate is obligated to maintain the land, not abandon the land, pay property tax, and be ready if the land right is revoked in the national interest with proper compensation. In respect of condominiums, an owner will be liable for maintenance charges (eg, service charges and the sinking fund) and insurance.

An owner may be liable in tort for loss, damage, injury or death suffered by persons on the property.

7 Protection against liability

How can owners protect themselves from liability and what types of insurance can they obtain?

Owners of properties usually take out insurance to cover risks such as damage or destruction to property and public liability. Specifically for hotels, offices, malls and apartments, the owner of that type of building is obliged to insure the building against building failure, natural disaster, fire or riots.

8 Choice of law

How is the governing law of a transaction involving properties in two jurisdictions chosen? What are the conflict of laws rules in your jurisdiction? Are contractual choice of law provisions enforceable?

Generally, the Indonesian legal system allows parties to choose the governing law that will apply to a contract. Nevertheless, some contracts such as a franchise agreement and construction services contract must be governed under Indonesian law.

There is an international private law doctrine called *lex rei sitae*, meaning 'the law where the property is situated'. Even though there is no strict prohibition under land law to use Indonesian law in a real estate transaction, it is clear that, under *lex rei sitae*, transactions in respect of properties in Indonesia should be governed by Indonesian law.

Where a transaction involves properties in two or more jurisdictions, it would be practicable for the parties to enter into separate contracts for the sale of the properties in each jurisdiction and for each contract to be governed by the law of that respective jurisdiction.

9 Jurisdiction

Which courts or other tribunals have subject-matter jurisdiction over real estate disputes? Which parties must be joined to a claim before it can proceed? What is required for out-of-jurisdiction service? Must a party be qualified to do business in your jurisdiction to enforce remedies in your jurisdiction?

Real estate disputes may arise from the relationship between a government body and a landowner or between private parties. Thus, real estate disputes may only involve private parties or may incorporate government bodies, particularly the BPN. If the dispute is between a government body and private party, the claim should be submitted to an administrative court. If the dispute is between private parties, due to a breach of contract or an unlawful act, the claim should be submitted to a district court.

In the rare event the real estate dispute involves an error in the issuance of a certificate of land or a deed of sale and purchase by a PPAT, the BPN and the PPAT will also be brought in as co-defendants in the claim. In many real estate disputes, the BPN will most probably be included since it is the sole authority managing real estate registration in Indonesia. Even if the BPN or PPAT is not included as co-defendant, the claim will nonetheless be examined. However, the court may rule that the claim is unacceptable due to a lack of parties.

Real estate disputes can be referred to courts or an arbitration tribunal, as agreed by the parties in their arbitration agreement.

If a party is entitled to remedies in an action instituted in Indonesia, it may enforce these remedies even if it is not qualified to do business in Indonesia.

10 Commercial versus residential property

How do the laws in your jurisdiction regarding real estate ownership, tenancy and financing, or the enforcement of those interests in real estate, differ between commercial and residential properties?

Fundamentally, there is no difference on the provisions between commercial and residential properties. Each commercial and residential property is subject to the same set of regulations.

11 Planning and land use

How does your jurisdiction control or limit development, construction, or use of real estate or protect existing structures? Is there a planning process or zoning regime in place for real estate?

The applicable regulation is clear that prior to the development or use of land, parties must obtain a spatial utilisation licence. Spatial utilisation licences are given to guarantee that spatial use is in accordance with spatial planning and zoning regulations, and to prevent any negative impact from spatial utilisation and to protect the public interest.

The following different forms of spatial utilisation licences are all issued by the local government:

- in-principle licence: a licence issued by the local government allowing, in principle, a certain activity. This type of licence may be in the form of a land utilisation appointment letter;
- location licence: a licence permitting the applicant to obtain the required space to perform their activities. This licence is required for the relinquishment of a land right. Local regulations may require a location licence to be based on an in-principle licence;
- land utilisation usage licence: this licence is required to apply for a building construction licence; and
- building construction licence: this licence is required to construct buildings (additional types of licences may be required by provincial or regency local regulations).

12 Government appropriation of real estate

Does your jurisdiction have a legal regime for compulsory purchase or condemnation of real estate? Do owners, tenants and lenders receive compensation for a compulsory appropriation?

The Land Acquisition Law was promulgated in January 2012. This law aims to provide for the procurement of land for national development. The land-owner must relinquish their land in the public interest, after being given fair and proper compensation or after a final and binding court decision.

Compensation will be granted for land, the space above and below the land, buildings, plant, goods related to land, and damages due to loss of business or work, relocation expenses, alteration of profession and remaining property value. Compensation may be in the form of money, substitute land, transfer of residency or ownership of shares, or their combination as agreed by the parties.

13 Forfeiture

Are there any circumstances when real estate can be forfeited to or seized by the government for illegal activities or for any other legal reason without compensation?

If the property is suspected of being obtained from crime or as a result of crime, the government has the right to seize it. The seized property is returned if:

- it is no longer needed in the investigation and prosecution;
- the legal case is dropped as a result of a lack of evidence or if the action was not defined as a crime;
- the legal case is waived in the public interest or annulled by law, unless the property was obtained as a result of a crime or is used for performing a crime; and
- the property will not be returned if the court rules that the property was taken from the state.

14 Bankruptcy and insolvency

Briefly describe the bankruptcy and insolvency system in your jurisdiction.

Under Indonesian law, if a debtor is bankrupt, it does not automatically entail that the debtor is insolvent. A debtor that has more than two creditors may be considered bankrupt if the debtor does not fully pay at least one loan that is due and payable. Thus, a bankrupt state does not indicate that one is unable to pay. On the other hand, insolvent means the inability to pay. Insolvency will be effective if there is no settlement proposal submitted by the debtor, the settlement proposal is rejected, or the legalisation of settlement is overruled by the court decision that is already final and binding.

Automatic stays apply to lenders holding a pledge, fiduciary security, mortgage right, hypothec, or other form of securities and third parties for 90 days from the date the court decision is issued. The automatic stay will expire under the law when the bankruptcy is terminated early or upon insolvency.

Investment vehicles**15 Investment entities**

What legal forms can investment entities take in your jurisdiction? Which entities are not required to pay tax for transactions that pass through them (pass-through entities) and what entities best shield ultimate owners from liability?

The limited partnership (CV) and PMA are common investment entities in Indonesia. Part of the profits made by members of a CV, association, partnership or firm, including a collective investment contract where the capital is not divided into shares, are excluded from taxation.

The recommended form for investment entities, either domestic or foreign, to shield owners from liability is a limited liability company. In a limited liability company, the shareholders' responsibilities are limited to the amount of capital or shares that have been deposited in the company, unless they violate certain conditions as set out in company law (in which case their liability will be unlimited).

16 Foreign investors

What form of entities do foreign investors customarily use in your jurisdiction?

Under investment law, any foreign investment in Indonesia will be in the form of a limited liability company. See question 4.

17 Organisational formalities

What are the organisational formalities for creating the above entities? What requirements does your jurisdiction impose on a foreign entity? What are the tax consequences for a foreign investor in the use of any particular type of entity, and which type is most advantageous?

Generally, a constitutive document (eg, partnership agreement and deed of establishment) will be prepared. The entities may need to be incorporated, registered or legalised by the relevant authorities.

To establish a PMA, a foreign investor has to apply for an approval licence to the Investment Coordinating Board in accordance with the standard industrial classification and negative investment list. After obtaining an approval licence, the foreign investor then executes the deed of establishment of a PMA before a notary.

The government provides a facility to the PMA that fulfils certain criteria. That facility may take the form of:

- income tax relief through a reduction of net income up to a certain amount of the investment made over a specified time period;
- import duty relief or exemptions on imports of capital goods, machinery or equipment which cannot yet be produced domestically for the purposes of production;
- import duty relief or exemptions on imports of raw or auxiliary materials for the purposes of production for a certain period and on certain conditions;
- exemptions or postponement of value added tax on imports of capital goods, machinery or equipment which cannot yet be produced domestically for the purpose of production;
- accelerated depreciation or amortisation; and
- relief on land and building tax for certain business sectors in certain regions, areas or zones.

Early this year the government promulgated a regulation on the facility of income tax for certain business sectors, which obtains high priority on a national scale or on certain regions that have potential to be developed. The facility of income tax consists of:

- reduction of net income totalling 30 per cent of the total investment amount in the form of fixed tangible assets, including land that is used for main business activity, spread for six years, each for 5 per cent per annum since the company started commercial production;
- accelerated depreciation on tangible assets and accelerated amortisation of intangible assets;
- income tax charged over dividends paid to foreign taxpayers other than permanent establishments in Indonesia of 10 per cent or lower; and
- compensation of losses for more than five years but not more than 10 years if certain requirements are met.

Acquisitions and leases**18 Ownership and occupancy**

Describe the various categories of legal ownership, leasehold or other occupancy interests in real estate customarily used and recognised in your jurisdiction.

The following are the type of land rights under Indonesia law:

- Right of ownership: this inherited land right is the strongest and fullest that can be owned by a party. Only an Indonesian citizen, and some legal entities determined by the government, can obtain right of ownership.
- Right to build: the right to build and own buildings over another party's land for a term of up to 30 years, which can be extended for a further 20 years and can be renewed. An Indonesian citizen or Indonesian legal entity can obtain this right. The right to build can be granted over state land, a right of management and a right of ownership.

- Right to cultivate: the right to cultivate land controlled by the state for farming, fisheries or animal husbandry. The right to cultivate is granted for a term of up to 25 years, or up to 35 years if granted to a company, and can be extended for up to 25 years. An Indonesian citizen or Indonesian legal entity can obtain this right.
- Right of use: the right to use and take the fruits of, or simply take the fruits of, land that is directly controlled by the state, or of another party's land. Right of use can be granted for a definite term or indefinitely so long as the land is used for a specific purpose. An Indonesian citizen, a foreign national domiciled in Indonesia, an Indonesian legal entity, or a foreign legal entity with a representative office in Indonesia can obtain this right. Rights of use are granted for up to 25 years and can be extended for up to 20 years.
- Right of lease: the right to use another party's land for building purposes by paying the owner a sum of money as rent. An Indonesian citizen, a foreign national domiciled in Indonesia, an Indonesian legal entity or a foreign legal entity with its representative office in Indonesia can obtain this right.

Specifically for condominium units, a certificate of right of ownership of a condominium will be issued. This type of certificate will follow its underlying right (eg, right of ownership, right to build or right of use). A condominium may be built over a right of ownership, a right to build or a right of use over state land, and a right to build or a right of use over right of management. If the construction of the condominium unit is performed on a right to build or a right of use over right of management, the developer must obtain the right to build or right of use over right of management status before selling the condominiums.

19 Pre-contract

Is it customary in your jurisdiction to execute a form of non-binding agreement before the execution of a binding contract of sale? Will the courts in your jurisdiction enforce a non-binding agreement or will the courts confirm that a non-binding agreement is not a binding contract? Is it customary in your jurisdiction to negotiate and agree on a term sheet rather than a letter of intent? Is it customary to take the property off the market while the negotiation of a contract is ongoing?

It is not common to sign a non-binding agreement prior to executing a binding sale and purchase agreement. In Indonesia, before signing a sale and purchase agreement, the parties usually enter into a conditional sale and purchase agreement (CSPA) setting out terms and conditions, including conditions precedent that have to be fulfilled prior to closing. A CSPA is regulated under current condominium law as a binding agreement and must be made before a notary. It is not unusual to take the property off the market, unless there is a down payment given to the seller, or the CSPA or a similar agreement is signed for the respective property.

20 Contract of sale

What are typical provisions in a contract of sale?

The CSPA must clearly identify the parties and the subject property, and also set out the consideration. Other provisions in the contract include the deposit amount payable by the purchaser when the contract of sale is signed; conditions precedent; representation and warranties; the completion date of the transaction; and whether the contract is subject to due diligence by the purchaser. The deposit amount is typically 10 per cent, although for some transactions, the deposit amount may be much more than that.

For real estate developers, a CSPA that is signed with their customers is bound to a definitive regulation. For example, for the sale of condominium units, the CSPA has to contain information or provisions on:

- the name or building number and reserved condominium unit;
- the floor number and type of condominium unit;
- the area of the condominium unit;
- the sale price;
- the terms of the down payments;
- the building specification;
- the completion date;
- repairing the condominium unit within 100 days after delivery;
- becoming a temporary condominium property manager; and
- insuring the construction work during construction.

21 Environmental clean-up

Who takes responsibility for a future environmental clean-up? Are clauses regarding long-term environmental liability and indemnity that survive the term of a contract common? What are typical general covenants? What remedies do the seller and buyer have for breach?

Under the law, the party that causes environmental contamination is liable for the environmental clean-up. They must also perform countermeasures and ensure environmental recovery. Additionally, the party responsible for the business and its activities is obliged to recover contaminated land from hazardous and toxic material waste (B3). The recovery procedure for contaminated land consists of a contaminated land survey, determining a source location to obtain a contaminated land sample and recovery of the contaminated land.

It is not customary to stipulate a long-term environmental liability and indemnity that survives the term of a contract. Nevertheless, under representation and warranties, environmental issues are occasionally stipulated, particularly for industrial properties.

Specific remedies on breaches of environmental issues are rarely provided under the contract. However, since environmental issues are covered under representation and warranties, the aggrieved party may file a claim against the defaulting party on a breach of contract or unlawful act to recover the damages they have suffered.

22 Lease covenants and representation

What are typical representations made by sellers of property regarding existing leases? What are typical covenants made by sellers of property concerning leases between contract date and closing date? Do they cover brokerage agreements and do they survive after property sale is completed? Are estoppel certificates from tenants customarily required as a condition to the obligation of the buyer to close under a contract of sale?

Purchasers may request representations concerning leases, such as:

- that the seller has delivered to the purchaser complete copies of all of the leases;
- that an accurate rent roll for the property is attached;
- that the leases are in full force and effect;
- that there has been no default by either the landlord or tenant under the leases;
- that all brokerage commissions with regard to the leases have been paid; and
- that the seller (as landlord) has completed all tenant improvements required by the landlord under the leases and the tenants have accepted such tenant improvements as complete.

Some sellers agree to covenants not to amend or terminate existing leases or enter into new leases between the contract date and the closing date without the purchaser's consent. Whether the covenants and representations survive the completion of the sale depends on the commercial agreement between the parties.

Estoppel certificates from tenants are not recognised under Indonesian law. Even though it may be stipulated in the lease agreement, it is not common for a tenant to issue an estoppel certificate.

23 Leases and real estate security instruments

Is a lease generally subordinate to a security instrument pursuant to the provisions of the lease? What are the legal consequences of a lease being superior in priority to a security instrument upon foreclosure? Do lenders typically require subordination and non-disturbance agreements from tenants? Are ground (or head) leases treated differently from other commercial leases?

It is unusual to stipulate that a lease is subordinate to a security instrument. However, a mortgagee may stipulate in the deed of granting a mortgage to limit the authority of the mortgagor to rent the property or determine or amend the rental period or receive a down payment in advance, except with the prior written consent of the mortgagee.

If the lease is superior to a security instrument, the lease will prevail even though the property has been sold to a third party. This is a basic provision under the law.

Lenders do not typically require subordination and non-disturbance agreements from tenants since the lenders do not have any control over existing lease agreements.

Ground leases will be subject to the same set of laws on commercial leases.

24 Delivery of security deposits

What steps are taken to ensure delivery of tenant security deposits to a buyer? How common are security deposits under a lease? Do leases customarily have periodic rent resets or reviews?

Security deposits are vastly typical under residential and commercial leases. The landlord normally requires a payment of the security deposit on or before signing the formal lease. The security deposit is normally provided in cash, containing three-month rental charges and three-month service charges. Leases of a shorter duration, such as three years or less, tend to have fixed rents throughout the lease terms. Leases of a longer duration may provide for rent revisions, which may be subject to a cap or be pegged to a prevailing market rental rate or even an increase in the consumer price index.

25 Due diligence

What is the typical method of title searches and are they customary? How and to what extent may acquirers protect themselves against bad title? Discuss the priority among the various interests in the estate.

A title search has to be officially performed by a PPAT before a deed of sale and purchase is made and executed. If not done through the PPAT, every prospective buyer has the right to request a letter of information on land registration from the land office. The title search is performed through the land office.

The acquirers may protect themselves against bad title through due diligence (title search, reviewing the historical transactions, and requesting information from the relevant courts as well as an arbitration body), representation and warranties, and indemnity funds for a certain period.

Title insurance for property transactions and legal opinions on title are not common in Indonesia.

26 Structural and environmental reviews

Is it customary to arrange an engineering or environmental review? What are the typical requirements of such reviews? Is it customary to get representations or an indemnity? Is environmental insurance available? Is it customary to obtain a zoning report or legal opinion?

It is not customary to arrange an engineering or environmental review for a property. Purchasers will most likely examine the existing environmental documents. Representations or indemnities are more common even though it is not always stipulated under the contract. See question 21.

Environmental pollution insurance is available. Any company that manages B3 is legally required to have insurance.

Zoning reports are obligatory under the law prior to the commencement of construction.

27 Review of leases

Do lawyers usually review leases or are they reviewed on the business side? What are the lease issues you point out to your clients?

In-house or external lawyers usually review the legal aspect of leases. Lease issues that need to be pointed out are:

- rental and terms of payment;
- use of rental space;
- rent review;
- option to renew; and
- default and its consequences.

It is unusual for the lender to require that a management agreement be subordinated to a mortgage.

28 Other agreements

What other agreements does a lawyer customarily review?

Lawyers will usually review the title documents (including deed of sale and purchase), building operational licences, brokerage agreements, service contracts, management agreements and one set of mortgage right documents (deed of granting a mortgage right, certificate of mortgage right and the loan agreement).

29 Closing preparations

How does a lawyer customarily prepare for a closing of an acquisition, leasing or financing?

Every set of actions on closing is stipulated under the contract. Deliverables will vary depending on the type of property that is transferred. Deliverables should include original title documents (including deed of sale and purchase), building licences, leases, keys, other property-related contracts, evidence of payment of income tax (for the seller), acquisition levy on land building (for the buyer), property taxes, service charges and utility charges.

There is no specified timing between the contract and closing. In Indonesia, for real estate asset acquisition, upon closing, the parties will execute the deed of sale and purchase before a PPAT. Prior to the execution, the seller has to pay income tax of 5 per cent, while the buyer has to pay an acquisition levy on land and building of 5 per cent. If the seller is a taxable entrepreneur, the buyer has to bear a VAT of 10 per cent of the purchase price.

30 Closing formalities

Is the closing of the transfer, leasing or financing done in person with all parties present? Is it necessary for any agency or representative of the government or specially licensed agent to be in attendance to approve or verify and confirm the transaction?

A PPAT, as a public official, must be present for each transfer of property. With regard to leasing or financing, the agreement can be signed privately by the parties or before a notary. There is no stipulation on the location of the transfer. In Indonesia, it is common for all parties to attend the closing.

31 Contract breach

What are the remedies for breach of a contract to sell or finance real estate?

Breach of contract is regulated under the provisions of contract law and the Indonesian Civil Code. Essentially, the seller must guarantee the safe control over the property and declare the existence of any hidden defect. If a hidden defect occurs, the buyer has the option to return the property by seeking a refund of the purchase price or to keep the property by seeking a partial refund, as determined by the judge, after hearing the opinions of experts. For other breaches, the consequences are normally set out in the contract. Under the Indonesian Civil Code, damages and expected profits that can be foreseen by the time the agreement is effective may be claimed against the defaulting party.

For a financing contract, the financier will probably request security in the form of a mortgage. If the borrower breaches the financing agreement, the lender is able to execute its mortgage right either through public auction or public court.

32 Breach of lease terms

What remedies are available to tenants and landlords for breach of the terms of the lease? Is there a customary procedure to evict a defaulting tenant and can a tenant claim damages from a landlord? Do general contract or special real estate rules apply?

Remedies for landlords against tenants that breach the lease terms are not strictly regulated under the law. Therefore, the terms and conditions of default and its consequences are specified under the contract.

Evictions are initially performed by the landlord's property manager, using the lease agreement as a basis, and are usually witnessed by the police. If the initial eviction attempt is unsuccessful, the landlord may request the housing division of the local authority to evict the tenants with the assistance of the police. This is only applicable for commercial and not residential properties.

Financing

33 Secured lending

Discuss the types of real estate security instruments available to lenders in your jurisdiction.

Under Indonesian law, a mortgage right is the only security instrument granted over land with or without other properties forming an integral part of the land for the payment of certain debts. For buildings, a fiduciary guarantee is also applicable. See question 2. Further, real estate is usually established on the right over the land (right of ownership, right to build, and right of use over state land) which can only be encumbered with a mortgage right.

34 Leasehold financing

Is financing available for ground (or head) leases in your jurisdiction? How does the financing differ from financing for land ownership transactions?

There is no restriction for financing of ground leases in Indonesia. The financier may categorise the financing either for investment or ownership. Ground lease finance may be categorised as investment finance, whereas purchase of a property may be categorised as ownership finance.

35 Form of security

What is the method of creating and perfecting a security interest in real estate?

A mortgage right is granted by a deed made before a PPAT. The form of the deed has been specified by the prevailing regulations. Subsequently, the deed must be registered to the land office within seven days after the signing of the deed. See question 2.

36 Valuation

Are third-party real estate appraisals required by lenders for their underwriting of loans? Must appraisers have specific qualifications?

Real estate appraisals may be conducted by an internal or public appraiser engaged in the field of property appraisal services. However, in order to grant a loan, there is no obligation that lenders require third-party appraisal. The appraisal is typically used by lenders to obtain an opinion in relation to the market value of the security instrument. The appraiser must have specific qualifications, including:

- a public appraiser licence;
- a minimum of a bachelor's degree;
- they must have passed the appraiser certification test; and
- have a minimum of three years' experience.

37 Legal requirements

What would be the ramifications of a lender from another jurisdiction making a loan secured by collateral in your jurisdiction? What is the form of lien documents in your jurisdiction? What other issues would you note for your clients?

Generally, it is not necessary for a lender to be licensed, qualified or otherwise entitled to carry on business in Indonesia for a lender to enforce its rights under a mortgage over a property in Indonesia. Any foreign individual or foreign entity may engage in credit transactions in Indonesia. Nevertheless, foreign lenders in the form of a foreign legal entity must file a report to Bank Indonesia with regard to its loan to a local party.

The lien document of property would be a mortgage right.

Mortgage rights are assignable. A mortgage right is derived from an accessory agreement. Therefore, if the loan is assigned, the security right must follow through. The assignment of a mortgage right must be registered to a land office by the new creditor. The land office will then record

Update and trends

Discussion to give more flexibility to the foreigner on real property is increasing. One of the intentions is to increase the liquidity of the real estate market. This is also due to request from real estate developers. The government is preparing the proposed amendment of the current government regulation. One of the ideas is to provide indefinite right of use for foreigners, provided that it is only applicable to upscale condominium units. Further, under the government of President Jokowi, the Ministry of Public Housing has merged with Ministry of Public Work, and a new ministry, the Ministry of Agrarian and Spatial Planning has been formed, which also acts as chairman of the National Land Agency.

the assignment in the book of land and the book of land of mortgage rights as well as in the certificates of mortgage rights. The record date is the seventh day after receipt of complete documents for the assignment of mortgage rights, where it also applies as an effective date for the third party.

38 Loan interest rates

How are interest rates on commercial and high-value property loans commonly set (with reference to LIBOR, central bank rates, etc)? What rate of interest is unreasonably high in your jurisdiction and what are the consequences if a loan exceeds the reasonable rate?

The prime corporate lending rate is around 2.5 to 3 per cent above the central bank rate. The prime lending rate for consumer, retail and real estate purchases is higher than that.

Other than the prevailing bank rates, the interest rate that is applicable for a loan is 6 per cent. If a loan agreement regulates a much higher interest rate than what is applicable under the law and the prevailing bank rates, the loan agreement may be considered as violating the lawful cause of an agreement. As a result, it may be deemed null and void.

39 Loan default and enforcement

How are remedies against a debtor in default enforced in your jurisdiction? Is one action sufficient to realise all types of collateral? What is the time frame for foreclosure and in what circumstances can a lender bring a foreclosure proceeding? Are there restrictions on the types of legal actions that may be brought by lenders?

Creditors' remedies are either selling the security through public auction or through a private sale to obtain the highest price that will benefit both parties. The sale of security can be performed directly through a public auction or execution through a court.

There is no prohibition to execute all types of collateral altogether. The creditor nonetheless has to be aware that it would be technically difficult since each type of collateral has its own execution procedure. It is, however, normal for the bank to compile all secured assets (property) and offer them altogether through a public auction.

There are no restrictions on legal actions that may be brought against the lenders, even though it would not be easy if the claim or contest has no credible grounds.

40 Loan deficiency claims

Are lenders entitled to recover a money judgment against the borrower or guarantor for any deficiency between the outstanding loan balance and the amount recovered in the foreclosure? Are there any limitations on the amount or method of calculation of the deficiency?

Principally, under the Indonesian Civil Code, it is a general rule that every moveable and immovable good owned by a borrower is used as collateral against the payment of a borrower's debts. Therefore, if there is a deficiency between the outstanding loan balance and the recovered amount, the lender may file a claim requesting the confiscation of a borrower's or guarantor's assets. There are no general limitations on the amount or method of calculation of the deficiency.

41 Protection of collateral

What actions can a lender take to protect its collateral until it has possession of the property?

Under the current mortgage law, a lender is not allowed to take possession of the property. However, the mortgagee is allowed to purchase the object of the mortgage through a public auction.

If the borrower is in default, the lender has the option either to sell the mortgage object through a public auction or execute the executable title stated in the certificate of mortgage right. If the mortgagor is bankrupt, the mortgagee is authorised to execute all rights under the mortgage right.

42 Recourse

May security documents provide for recourse to all of the assets of the borrower? Is recourse typically limited to the collateral and does that have significance in a bankruptcy or insolvency filing? Is personal recourse to guarantors limited to actions such as bankruptcy filing, sale of the mortgaged or hypothecated property or additional financing encumbering the mortgaged or hypothecated property or ownership interests in the borrower?

Security documents, other than loan agreements, do not normally stipulate that there will be a recourse against all borrower's assets. If the repayment of a loan is not sufficient, the lender has the right to file bankruptcy or a postponement of debt payment obligations through a commercial court. The recourse to guarantors would rely on the provisions in the security documents.

A guarantor is essentially unable to be subject to heavier terms and conditions than the borrower. Further, since the law provides certain special rights to guarantors (eg, a guarantor's obligation to pay the debt commences after the lender has seized and sold the borrower's assets; a guarantor may contest the lender's rights and request the lender to firstly determine the secured amount borne by the guarantor against the borrower's debt), it is customary to waive those rights.

43 Cash management and reserves

Is it typical to require cash management system and do lenders typically take reserves? For what purposes are reserves usually required?

A cash management system (a lock box) is not commonly used on real estate transactions in Indonesia.

44 Credit enhancements

What other types of credit enhancements are common? What about forms of guarantee?

The lenders may request additional guarantees to secure the payment of all outstanding sums. Moreover, requesting a completion guarantee from a holding company, a sponsor or a shareholder of the mortgagor is normal. This completion guarantee may also include certain payment or covenant guarantees; for example, payment for a shortfall in interest, an obligation to top up any shortfall in the loan-to-value ratio or an obligation to fund cost overruns, and an obligation to provide subordinated loans to cover future investment costs. This commitment may be in the form of letter of comfort, letter of intent or even a corporate guarantee.

45 Loan covenants

What covenants are commonly required by the lender in loan documents? What is the difference depending on asset classes?

Covenants generally include obligations to maintain the property, use the proceed in accordance with the loan's objective, submit quarterly financial report, pay all property taxes assessed against the property, comply with all laws and provisions of agreement, maintain the insurance required under the loan documents, comply with environmental obligations, obtain the lender's consent to leases within certain pro forma requirements and obtain the lender's consent to a transfer of the property or ownership interests in the borrower or the addition of further mortgage debt. If the loan is a construction loan, there will be covenants to complete construction. If the loan concerns an office building or retail centre, the lender will require that borrowers comply with all obligations under leases and obtain consent of the lender to new leases or the modification or termination of existing leases.

46 Financial covenants

What are typical financial covenants required by lenders?

Many single asset loans contain requirements that borrowers maintain a required debt-service ratio, although this is not a requirement in many other transactions. Loans may also contain an obligation to comply with loan-to-value covenants. Many loans, however, do not contain such requirements. If a loan is made to an operating entity, the operating company may be subject to covenants regarding overall debt, restricted payments, debt-to-leverage ratios, fundamental changes, limits on capital expenditures, EBITDA, and so on.



Eddy Marek Leks

eddy.leks@lekslawyer.com

Menara Palma 10th Floor, Suite 10-03
Jalan HR Rasuna Said
Blok X2 Kav 6
Jakarta 12950
Indonesia

Tel: +62 21 5795 7550
Fax: +62 21 5795 7551
www.lekslawyer.com

47 Secured moveable (personal) property

What are the requirements for creation and perfection of a security interest in moveable (personal) property? Is a 'control' agreement necessary to perfect a security interest and, if so, what is required?

There are two methods for the creation and perfection of a security toward moveable property (either tangible or intangible), that is, through fiduciary security or a pledge. For a pledge, the secured property must be delivered to the pledgee. For a fiduciary security, the secured property is not delivered to the fiduciary security holder, but held by the fiduciary security grantor. There is no legal requirement stipulating that a pledge has to be made in writing. Yet, it is a common practice, whether in a notarial or private deed form. Regarding the shares of a limited liability company, in order to be valid, the pledge must be registered in the shareholder register. See question 2 concerning the creation and perfection of a fiduciary security.

48 Single purpose entity (SPE)

Do lenders require that each borrower be an SPE? What are the requirements to create and maintain an SPE? Is there a concept of an independent director of SPEs and, if so, what is the purpose? If the independent director is in place to prevent a bankruptcy or insolvency filing, has the concept been upheld?

Lenders in Indonesia do not require an SPE for each borrower. The Indonesian legal system does not recognise an SPE. Each SPE is formed in accordance with the limited liability company law. Further, since SPEs are not recognised under Indonesian law, there is no independent director of SPEs.

However, having and establishing a separate legal entity for a specific project is the current trend among entrepreneurs in Indonesia.