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Banking & Finance

Second Edition

Indonesia
ABNR Counsellors at Law

chambers.com

2019

Law and Practice

Contributed by ABNR Counsellors at Law

Contents

ABNR Counsellors at Law was established in Jakarta in 1967 as Ali Budiardjo, Nugroho, Reksodiputro. ABNR is one of the largest independent full-service law firms in Indonesia and its reputation is recognised globally. ABNR was selected, based on its integrity and professionalism, as the sole Indonesia member of the world's largest law firm association Lex Mundi. ABNR has played a major role in the financing of most of the significant Indonesian power projects. It has advised on project finance issues including financing structures involving BOT and BOO, and issues relating to government guarantees. ABNR has also advised on gold, copper, and coal mining projects, including the regulatory and licensing framework of these industries. ABNR also assists mining service companies with contracts and compliance in tender procedures.

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1. Loan Market Panorama

1.1 Impact of Regulatory Environment and Economic Cycles

Indonesian economic growth has been seen, amid global volatility, as relatively stable over the past several years. This stability has been mainly generated by government consumption, backed by domestic consumption despite a slow-down in foreign direct investment. Lending activity has grown over 2019 with much of it aimed at government or infrastructure projects. Bank Indonesia recently lowered its seven-day reverse repurchase rate in attempt to boost growth. However, generally there have not been any significant changes in the regulatory environment of the Indonesian loan market.

1.2 The High-yield Market

In economic conditions of stable growth, bond issuance is one of the primary means of continuously financing projects. Significant numbers of the issuers in the Indonesian high-yield market are existing issuers. The Indonesian market has also seen the emergence of asset securitisation.

1.3 Alternative Credit Providers

There has been no significant growth in alternative credit providers in Indonesia. Although peer-to-peer lending, and fintech in general, continues to grow and develop, it has not significantly affected the financing terms and structures in Indonesia.

1.4 Banking and Finance Techniques

Generally, in Indonesia there have been no significant changes to the "traditional" banking and financing techniques. However, non-bank lenders, including peer-to-peer platforms, are starting to grow in Indonesia and have begun to impact the SME and consumer finance markets.

1.5 Legal, Tax, Regulatory or Other Developments

There have been no recent legal, tax, regulatory or other developments that have had any significant impact on the loan market in Indonesia.

2. Authorisation

2.1 Authorisation to Provide Financing to a Company

Banks

In order to be able to provide financing to a company, a bank must have a written credit or financing policy, which shall, at least, mention all the aspects stipulated under the guidance on the preparation of the credit or financing policy of the bank. The credit and financing policy must be approved by the board of commissioners of the bank.

The credit or financing policy must, at least, contain the following main provisions:

- prudential principles in credit and financing;
- organisation and management in credit or financing;
- a policy on the approval of credit or financing;
- documentation and administration of the credit or financing;
- supervision of the credit or financing; and
- settlement of bad credit or financing.

Non-bank Financial Institution

To finance a company in Indonesia, a non-bank financial institution must have a policy and financing plan which is set out in an annual business plan by that institution.

The policy and financing plan must be both stipulated by the board of directors and disseminated to management and employees in the relevant working unit.

The institution must also nominate a working unit or an employee responsible for the following tasks and duties:

- administering marketing, knowing their customers, financial analysis, monitoring loan financing quality and billing and handling of debtor's complaints;
- arranging and applying operational and procedural standards for financing; and
- compiling and applying internal control systems and procedures to make sure that the process for granting financing is in accordance with the financing strategy and policy and does not violate the prevailing laws and regulations.

For the above-mentioned purpose, the non- bank financial institution must have an employee who has knowledge and experience in the financing sector.

Further, the institution must also mitigate the financing risk by implementing the following:

- risk transfer mechanisms through credit insurance in accordance with the prevailing laws and regulations;
- transferral of the risk on collateral from financing activities through appropriate insurance mechanisms; and/or
- the creation of fiduciary securities, mortgages, or hypothecs on the collateral of the financing activities.

There are also specific requirements that must be fulfilled depending on the type of business activities and the financing scheme.

3. Structuring and Documentation Considerations

3.1 Restrictions on Foreign Lenders Granting Loans

There are no specific restrictions on the granting of loans by foreign lenders to corporate borrowers. However, foreign lenders may be restricted from extending loans to microfinance institutions.

3.2 Restrictions on Granting Security to Foreign Lenders

There are no restrictions on the granting of security or guarantees to foreign lenders.

3.3 Restrictions and Controls on Foreign Currency Exchange

Indonesia has limited foreign exchange controls. The rupiah is, in general, freely convertible into other currencies within Indonesia. Bank Indonesia imposes a restriction on state-owned enterprises sourcing US dollars from Indonesian state-owned enterprise banks. Restrictions also apply on the transfer of the rupiah outside Indonesia to maintain the currency's stability and to prevent the utilisation of the rupiah for speculative purposes by non-residents. In addition, Bank Indonesia has the authority to request information and data concerning the foreign exchange activities of all persons and legal entities that are domiciled in Indonesia, or who plan to be domiciled in Indonesia for at least one year.

3.4 Restrictions on the Borrower's Use of Proceeds

The parties usually stipulate the provisions on the use of proceeds from loans or debt securities in their agreement. Generally, the use of proceeds shall be in accordance with its agreed allocation and the corporate benefit of the borrower.

Proceeds must not be used for money laundering purposes, as this is subject to criminal sanctions as stipulated under Law No 8 of 2010 on the Prevention and Eradication of Money Laundering.

3.5 Agent and Trust Concepts

The trust concept is not generally recognised in Indonesia, nor is it used in general lending activities. Under Indonesian law, a concept of *perwaliamanatan* – which may be similar to an English law trust concept – is used strictly in bond transactions. In Indonesia the agent acts specifically on behalf of the syndicate members in the administration (including in relation to security-interest related matters) and pursuant to the authorisations granted to it under an agency agreement, commonly incorporated in the loan agreement.

3.6 Loan Transfer Mechanisms

Loan transfer can be effected by:

- *Assignment (cessie)* – meaning the "sale and purchase of receivables", which is followed by delivery of the receivables – transfer of the claim/rights only – by way of an assignment. The assignment is made through an agreement between the previous lender and the new lender. The debtor must be notified, accept this in writing or acknowledge the assignment to be considered bound to pay the debt to the new lender. Without the acknowledgment, the debtor is entitled to continue paying the previous lender despite the assignment being complete between the previous lender and the new lender. This process, however, should not have any impact on the assignment between the previous lenders and the new lender. The transfer of the security interest due to an assignment is automatic. It is advisable that the transfer of the security interest be stipulated in an assignment agreement.
- *Novation* – where the previous lender agrees to transfer its receivables and obligations to the new lender. Consequently, the agreement between the previous lender and the debtor terminates and a new agreement between the new lender and the debtor is created immediately. Due to this characteristic, a novation agreement relating to a loan is entered into by the previous lender, the new lender and the debtor. The security interest does not automatically transfer in a novation and transferral must be expressly agreed to by the previous lender and the new lender. To evidence the agreement of the previous lender, the transfer of security must be clearly stipulated in the novation agreement.

To ensure preservation of the rights over the secured interests in favour of the new lender, the relevant entries in the register should be amended. In the case of a syndicated loan scenario, for as long as the security interests are registered in the name of the agent of the syndication, no amendment to the relevant register will be required except in the case of change of the agent. However, in the case of a land mortgage, the new lender must register its interest at the relevant authority before it can exercise its right under the security agreement, and must amend the mortgage certificates to ensure that the new lender will get the full benefit of the relevant security interest. This amendment is also required in cases where the mortgage certificate includes the names of the existing lenders in addition to the agent (as opposed to that of the agent only).

3.7 Debt Buy-back

Debt buy-back is unregulated in Indonesia. Parties are free to agree on restricting or permitting debt buy-back. If the parties agree to permit debt buy-back, the buy-back can be done pursuant to the relevant buy-back provision under the agreement. The application of lending limits for financial institutions needs to be considered when making debt buy-back.

3.8 Public Acquisition Finance

"Certain funds" rules are generally not recognised in Indonesian law. The regulations are silent on the requirement of certainty of financing for acquisitions. Instead, the rights and obligations of the parties to the transactions are, to the extent that the laws of Indonesia are or would be deemed applicable, subject to the principle of good faith (*iktikad baik*), which in principle governs the relationship between the parties to a contract and which, in certain circumstances, may limit or preclude the reliance on, or enforcement of, contractual terms and provisions.

4. Tax

4.1 Withholding Tax

Withholding tax – generally set at 20% – is applicable to interest and certain fees. If the recipient of interest benefits from the provisions of a tax treaty, the withholding tax rate may be reduced or eliminated. The borrower is normally requested to calculate the gross and indemnify any tax obligation that may be imposed upon the lender. The withholding tax upon the interest is to be collected by the borrower when it pays any interest to the lenders.

4.2 Other Taxes, Duties, Charges or Tax Considerations

Corporate taxpayers are subject to income tax (the generally rate is 25%) and value added tax (current general rate of 10%). Certain charges will apply to the registration of security, payable to the relevant security registration office.

4.3 Usury Laws

The application of an interest rate is either by agreement or as stipulated by law. Parties to a loan agreement may agree on an interest rate in excess of the statutory interest rate, unless it is forbidden by law. An interest rate charged otherwise can be considered as usury. In Indonesia a usury law (known as *woekerordonantie*) is still in force, allowing the court (among other things) to declare an agreement null and void in cases where the agreement indicates a disproportionate valuing of the obligations of the parties (including interest value), at the request of the disadvantaged party. However, its provisions are generally considered not to affect commercial loan agreements and facilities at present. It is important for the parties to a loan agreement to explicitly state the agreed interest rate applicable to the respective loan agreement.

5. Guarantees and Security

5.1 Assets and Forms of Security

In Indonesia, lenders would normally take security over all present and future assets of the debtor (including all movable, immovable, tangible and intangible assets). Creditors typically also wish to have a security interest over the shares of the Indonesian debtor and want to receive step-in rights. The point to be noted is that, due to the nature of security law in Indonesia, security over all assets and contractual obligations cannot be covered under one form of security or in one security document. This point is further elaborated in more detail below.

Security interests in Indonesia are limited to those prescribed by Indonesian law. The security interests available under Indonesian law are the mortgage, the fiduciary security, the pledge for in rem security interests and the guarantee for personal security (in personam) interests. Under strict legal interpretation in Indonesia, parties are not free to determine security interests contractually. Contracts may not generally be assigned for security purposes under Indonesian law. However, in practice, notwithstanding questions of validity, this is done, with a "contractual security". Contractual security in the form of contractual arrangements (such as a conditional assignment or novation of contractual rights and obligations for security purposes or powers of attorney), although untested, may be deemed invalid by Indonesian courts in that they may be considered a circumvention of the Indonesian security laws. In light of the foregoing, the creditors should obtain a collateral assignment of the main contracts under a common law system.

Considering the above, the types of security (both in rem and contractual) and the corresponding assets that the lenders in Indonesia normally take are as follows:

- mortgage over land and buildings and other fixtures above the land;
- fiduciary assignment over movable and immovable tangible assets (including buildings and other fixtures that cannot be secured by a mortgage), receivables, insurance proceeds, intellectual property;
- pledge over bank accounts, shares accompanied with additional contractual security in the form of power of attorney to manage bank accounts, power of attorney to vote and power of attorney to sell shares;
- contractual security in the form of conditional novation and power of attorney to exercise contractual rights over contractual arrangement of the debtor; and
- contractual security in the form of power of attorney to manage business over the licenses and other business of the debtor.

The mortgage, the pledge and the fiduciary security are in rem rights that are "absolute" and "exclusive" in the sense that the mortgagee, the pledgee and the fiduciary grantee may, in principle, exercise their powers with respect to the mortgaged, pledged or fiduciarily secured assets vis-à-vis all other persons, regardless of who (including the mortgagor, the pledgor or the fiduciary grantor) is using the mortgaged, pledged or fiduciarily secured property or has a contractual right to use it. Only a third party acting in good faith when

acquiring the mortgaged, pledged or fiduciarily secured asset may be protected against a concurrent claim of the mortgagee, the pledgee or the fiduciary transferee over the property.

Mortgages are established through a two-step procedure – ie, the signing of the mortgage deed before a land officer (PPAT) in Indonesian and registration of the mortgage deed at the relevant land registration office. The mortgage is established at the moment it is registered with the land book located at the Indonesian National Land Office (Badan Pertanahan Nasional Republik Indonesia (BPN)). As a result, certainty as to the moment of registration of the security interest is very important to the creditor or the lenders. The registration of the mortgage deed and the issuance of the mortgage certificate as evidence of registration can take between two weeks and six months although most commonly two and four weeks. There is a non-tax revenue that needs to be paid to the BPN for the registration of the mortgage whose amount depends on the amount secured under the mortgage deed.

A fiduciary security takes the form of a written agreement by which the fiduciary grantor transfers to the transferee its rights of ownership in respect of the transferred/assigned assets. Under the Fiduciary Law, the agreement must be in Indonesian and notarial deed form. Based on the fiduciary security agreement, the transferor transfers to the transferee its rights of ownership in respect of the assets for the time during which the debt under the agreement remains outstanding. "Possession" of the tangible assets remains with the transferor who is normally entitled to use or dispose of the assets in the ordinary course of business. Under the Fiduciary Law, a fiduciary security agreement must be registered, even if the assets over which a fiduciary security is granted are located outside of Indonesia (for assets in transit). The fiduciary security must be registered by the fiduciary grantee at the fiduciary registration office within 30 days as of the date of the fiduciary security agreement. If within 30 days the fiduciary security agreement is not submitted for registration in the fiduciary registration office, the parties must re-execute the agreement. The fiduciary security comes into effect on the date of registration in the fiduciary registration book kept by the fiduciary registration office (which is now done by online system). The fiduciary security must be registered by the notary within 30 days of the date of the security. Unlike mortgages, in practice, the amount secured in the security does not affect the notarial and registration fees. There is a prescribed notarial and registration fee for fiduciary securities which currently is still generally observed by notaries and the registration office.

There is no formal legal requirement to have a pledge agreement in writing. However, it is standard practice in Indonesia that pledges are embodied in a deed of pledge (notarised or executed privately), setting forth the particulars of the pledge. The deed of pledge does not need to be executed in Indonesian. In order to create a valid right of pledge over certain property, the following requirements must be complied with. In respect of tangible assets, the only constitutive requirement for the creation of a pledge is that the pledged asset is physically transferred out of the possession of the pledgor. The right of pledge will be discharged when the pledged asset is no longer kept under the control of the creditor. In respect of intangible movable assets, since the nature of intangible assets (such as receivables) is that there is no possession over such property, a notification must be made to whomever the assets/ receivables would have to be paid.

With respect to a pledge of shares, the pledge must be registered in the shareholders register of the company. To create a pledge on listed shares, both the company and the Stock Administration Bureau must be notified of the pledge, which will subsequently be recorded in the shareholders register held by the Stock Administration Bureau. For blocked shares kept in the custody of the Indonesian Central Securities Depository (PT Kustodian Sentral Efek Indonesia), a confirmation letter will be issued by them certifying that the shares are pledged.

There is no specific requirement for the execution of the pledge of a bank account. Although it can be privately executed by the pledgor and the pledgee, it is advisable that the pledge of bank account is executed in a notarial deed form before a notary because of the evidentiary weight in court.

The pledge of account created under the pledge of a bank account must be notified to the relevant bank and an acknowledgement of the pledge by that bank should be obtained. The acknowledgements also serve to evidence the bank's agreement to the provisions set out in the notice.

In practice, a pledge of a bank account is normally supported by the power of attorney to manage bank accounts. This power of attorney however does not create an in rem security interest.

5.2 Floating Charges or Other Universal or Similar Security Interests

Indonesian security law does not recognise the term "floating charges". Due to the restrictive nature of the prescribed Indonesian security interests, in practice, other "security documents" have developed in an attempt to cover all contingencies. These other forms of security mostly consist of powers of attorney or authorisations and other contractual arrangements (such as conditional assignment (and assumption) agreements and certain undertakings). However these contractual arrangements, unlike in rem security prescribed under Indonesian law, will not have any priority rights over other creditors and may not survive in the event of the insolvency of the debtor or borrower.

5.3 Downstream, Upstream and Cross-stream Guarantees

Under Indonesian law, there is uncertainty as to whether the issuance of a guarantee or a third-party security by a company to secure the fulfilment of obligations to a third party can be regarded as in the furtherance of the interests of that company (this is known as the "ultra vires doctrine"). Therefore, it is uncertain whether downstream, upstream and cross-stream guarantees may be voidable or unenforceable under the laws of the Republic of Indonesia.

As a parameter to determine whether any such action is in furtherance of the interests of a company, it is important to take into account the provisions of the articles of association of that company and whether that company derives certain commercial benefits from the transaction in respect of which the guarantee and third-party security is issued.

Generally under Indonesian company law, the board of directors needs to obtain approval from a general meeting of shareholders to provide any guarantees that may result in more than 50% of the company's assets needing to be released or transferred to a third party in the event that the guarantee is enforced. Nevertheless in practice (especially for project finance), it is common for the lenders to require corporate approval from all the company's organs (ie, a general meeting of shareholders, the board of commissioners and the board of directors).

5.4 Restrictions on Target

There is no explicit restriction under Indonesian law on the target granting guarantees or security or financial assistance for the acquisition of its own shares. Therefore, it is uncertain whether that granting may be voidable under the laws of the Republic of Indonesia. The corporate benefit and the ultra vires doctrine are also applicable when the target grants guarantees or security or financial assistance for the acquisition of its own shares. All parties involved including each member of the board of directors, the board of commissioners and the shareholders themselves can be held personally liable under the piercing the corporate veil doctrine if the action of the target can reasonably be deemed as violating the corporate benefit principle and the ultra vires doctrine.

5.5 Other Restrictions

For private companies, other than the requirement to obtain approval from the general meeting of shareholders of the borrower or debtor, there is no other approval or consent required (especially from the authorities) for granting security or guarantees. Please note that if the borrower or debtor is a state-owned company, it cannot grant any security over its assets or provide any guarantee to the lenders due to restrictions under World Bank Negative Pledge and Indonesian regulation.

5.6 Release of Typical Forms of Security

The release of the in rem security would require certain formalities that need to be fulfilled by the borrower or the debtor. The lenders must issue a release letter, as a basis for requesting the release of the security, to the relevant authorities, namely to the BPN for the release of a mortgage, the fiduciary registration office for the release of a fiduciary assignment. For pledges of shares, normally the parties sign a termination of the pledge of shares agreement followed by the deletion of the record of the pledge of in the shareholder's register of the borrower or debtor.

5.7 Rules Governing the Priority of Competing Security Interests

A mortgagee, pledgee or fiduciary grantee is not only entitled to foreclose on the mortgaged, pledged or fiduciarily secured asset, but may also satisfy his or her claim out of the proceeds ahead of most other creditors seeking recourse on the mortgaged, pledged or fiduciarily secured asset, except for those whose claims are preferred by law (such as claims for costs of foreclosure, costs incurred to protect the mortgaged, pledged or fiduciarily secured asset from loss, and preferential claims of tax authorities).

Bankruptcy of the mortgagor, the pledgor and the fiduciary grantor does not, in principle, affect the security right of the mortgagee, pledgee and fiduciary grantee in that the assets in question are not regarded as being part of the bankruptcy estate.

Contractual security will be treated like any other contractual arrangement in the event of the bankruptcy of a borrower where the receiver has the right to determine the continuation of the contract and thus it may not survive the event of the bankruptcy. The Indonesian Civil Code also provides that a power of attorney, even if irrevocable, automatically terminates by operation of law upon bankruptcy of the grantor of the power of attorney. This rule is mandatory and a contractual provision to the contrary is invalid and ineffective

6. Enforcement

6.1 Enforcement of Collateral by Secured Lenders

The circumstances in which lenders can enforce its collateral are typically specified in the agreement between the secured lender and the borrower; usually being the events of default and of failure to pay the principal amount or interest when the loan is due. There are no compulsory requirements that lenders must satisfy before enforcing the collaterals.

Security interest can be enforced through public auction or private sale.

Since the security is given with executorial title, the secured lenders may sell the security in the absence of a court decision in the event of default. However, please note that in practice the state auction body still requires the presence of a court decision or order in order to proceed with a public auction. The state auction body even may refuse the application for a public auction sale if the party that wishes to execute the security cannot provide a court decision or order for the said auction.

The secured lenders will be prioritised ahead of the other common creditors when seeking payment from the execution of the collaterals. This right to be prioritised is not affected by bankruptcy or liquidation process of the borrower.

6.2 Foreign Law and Jurisdiction

The choice of a foreign law as the governing law of the contract will be upheld provided that:

- the chosen governing law does not violate public policy;
- the law is applicable only to the implementation and implications of the contract (the law shall not be applicable for determining the validity of the contract or the creation of the contract); and
- the chosen governing law does not deal with the material or substance of the law or in other words, not on the formality or procedural law.

6.3 A Judgment Given by a Foreign Court

In general, a foreign court decision is not enforceable within Indonesia. The judgement can be used as evidence in a retrial of the merits of the case but subject to the prevailing laws and regulations. Indonesia is not a party to any treaty, convention or bilateral agreement which recognises the enforcement of a foreign court judgment.

Under Indonesian arbitration law, a foreign arbitral award is enforceable within Indonesia. The award becomes enforceable after an Indonesian court validates the award by issuing a writ of *eksekuatur* (a court order).

6.4 A Foreign Lender's Ability to Enforce Its Rights

There are no restrictions applicable to foreign lenders specifically.

7. Bankruptcy and Insolvency

7.1 Company Rescue or Reorganisation Procedures Outside of Insolvency

The court-sanctioned insolvency proceedings are governed by Law No 37 of 2004 on Bankruptcy and Suspension of Payments (Bankruptcy Law). There are two types of court-sanctioned insolvency proceeding applicable to Indonesian limited liability companies:

Bankruptcy Proceedings

Bankruptcy proceedings aim at liquidation, but are often used for the reorganisation of a business by way of restart (if a composition plan is accepted by the creditors under a voting mechanism and ratified by the Commercial Court). The bankruptcy proceedings are initiated by the filing of the bankruptcy petition, by either the creditor (either unsecured or secured) or the debtor itself, which contains the receiver nomination. If the bankruptcy petition is granted, the Commercial Court will declare the debtor bankrupt, appoint receiver(s) and a supervisory judge. The court-appointed receiver will handle the affairs of a bankrupt debtor during the bankruptcy process. A bankrupt debtor can still reorganise if the composition plan that the debtor offers is approved by the affirmative votes of more than half of the unsecured creditors, who are present or represented at the voting meeting, whose rights are acknowledged or provisionally acknowledged; and who represent at least two-thirds of the total amount of the unsecured claims of the unsecured creditors present or represented at the meeting, whose rights are acknowledged or provisionally acknowledged.

Otherwise, the bankrupt debtor will be declared insolvent (see definition of insolvency) and the receiver will liquidate the bankrupt debtor.

Suspension of Payment Proceedings

Suspension of payment (PKPU) proceedings aim at continuation of the business, but may result in liquidation (if the composition plan is rejected by the creditors under a voting mechanism or fails to secure the Commercial Court's ratification). The PKPU proceedings are initiated by the filing of the PKPU petition by either the creditor or the debtor itself, which contains the administrator nomination. If the PKPU petition is granted, the Commercial Court will grant the debtor a provisional PKPU, appoint administrator(s) and a supervisory judge. The court-appointed administrator will, jointly with the debtor's director(s), handle the affairs of a corporate debtor. A debtor in a PKPU can reorganise if the composition plan that the debtor offers is approved by the affirmative cumulative votes of:

- more than half of the unsecured creditors, who are present or represented at the meeting, whose rights are acknowledged or provisionally acknowledged; and who represent at least two-thirds of the total amount of the unsecured claims of the unsecured creditors present or represented at the meeting, whose rights are acknowledged or provisionally acknowledged; and
- more than half of the secured creditors, who are present or represented at the meeting; and who represent at least two-thirds of the total amount of the secured claims of the secured creditors present or represented at the meeting.

Otherwise, the bankrupt debtor will be declared bankrupt and insolvent (see definition of insolvency). The receiver(s) thereafter will be appointed to liquidate the bankrupt debtor.

The two types of proceedings are not principally opposed and can be used as needed by the situation at hand.

There is also a proceeding recognised by Indonesian law that is not technically an insolvency proceeding: dissolution and liquidation under Law No 40 of 2007 on Limited Liability Companies (Company Law). This is a company/shareholder driven, irreversible process that is used only for limited liability companies; it does not cater for the possibility of the debtor's restructuring and has no creditor vote.

Definition of Insolvency

Insolvency as used in the Bankruptcy Law has a meaning that differs from that in many other legal systems. It does not constitute the test for bankruptcy declaration, but refers to the specific concept of "the state of being insolvent at law", which occurs when:

- no composition plan is submitted in the creditors' meeting for the verification of claims;
- the composition plan is rejected in the voting process by the creditors;
- the composition plan is approved by the creditors but not ratified by the Commercial Court;
- no composition plan is ratified by the Commercial Court during the suspension of payments period (causing the debtor to be declared bankrupt and insolvent at the same time); or
- the final and binding ratified composition plan is nullified by the Commercial Court due to the fact that the debtor is negligent in performing its obligations under the ratified composition plan.

7.2 Impact of Insolvency Processes

If the secured creditors attempt to enforce their security after the restructuring and insolvency proceedings have commenced, they may not be able to do so since their right to enforce their security is subject to a stay, for a maximum period of 90 days as of the rendering of a bankruptcy declaration, and during the entire period of the suspension of payments, which can reach up to a maximum of 270 days, as of the granting of a suspension of payments decision.

7.3 The Order Creditors Are Paid on Insolvency

Free Assets and Encumbered Assets

- The outstanding wages (excluding severance payments and other rights) of the employees of the bankrupt debtor would rank higher than any claims. Outstanding rights of the employees of the bankrupt debtor other than outstanding wages would rank below the secured creditors. (Article 95, paragraph 4 of the Labour Law in connection to the Decision of the Constitutional Court No. 67/PUU-XI/2013, dated 11 September 2014.
- Specific expenses stipulated by the Tax Law:
  (a) legal expenses arising solely from a court order to auction movable and or immovable goods;
  (b) expenses incurred for securing the goods; and
  (c) legal expenses, arising solely from the auction and settlement of inheritance.
- Preferred creditors ranked above the secured creditors:
  (a) tax claims;
  (b) court charges which specifically result from the disposal of a movable or immovable asset (these must be paid from the proceeds of the sale of the assets over all other priority debts, and even over a pledge or mortgage); and
  (c) those legal charges exclusively caused by the sale and saving of the estate (these will have priority over pledges and mortgages).
- Encumbered Assets;
- Receiver's fee;
- secured creditors; and
- the remains (if any) will go to the free assets.

Free Assets

- Bankruptcy estate creditors – claims against the bankruptcy estate such as:
  (a) the fee of the receiver;
  (b) the costs of liquidating the bankruptcy estate (fees of an appraiser, an accountant, etc);
  (c) new financing;
  (d) the lease costs for the bankrupt's house or offices as of the date of the declaration of bankruptcy; and
  (e) the wages (excluding severance payments) of the employees of the bankrupt debtor as of the date of the declaration of bankruptcy (Article 39 paragraph 2 of the Indonesian Bankruptcy Law (IBL)).
- Preferred creditors consisting of:
  (a) specific, statutorily preferred creditors whose preference relates only to specific assets (1139 Indonesian Civil Code); and
  (b) general, statutorily preferred creditors (for example, revenue authorities, etc), which should include those owed severance payments (1149 Indonesian Civil Code and the Labour Law).
- Unsecured creditors.

Please however note that the above order of priority may not always be upheld strictly.

7.4 Concept of Equitable Subordination

There is no concept of equitable subordination under Indonesian law.

7.5 Risk Areas for Lenders

A transaction that is entered into by the debtor within a specific period before the declaration of the debtor's bankruptcy

may be nullified by the Commercial Court upon a claim submitted by the receiver in accordance with the provisions of the IBL. This legal remedy is known as an actio pauliana suit.

The nullification of a legal action or transaction made by the debtor may be granted by the Commercial Court upon the lawsuit of the receiver if the receiver can prove the following requirements:

- the legal action being challenged was performed by the debtor before the bankruptcy declaration was rendered;
- the debtor was not obliged by contract or law to perform the legal action being challenged, or in other words the legal action was voluntarily conducted by the debtor;
- the legal action being challenged prejudices the creditors' interests; and
- the debtor, and the other party with whom the debtor conducted the legal action being challenged, knew or should have known that the legal action would cause damages for the creditors.

With respect to the last requirement, both the debtor and the third party with whom the legal action being challenged was performed are deemed to know that such a transaction will be detrimental to the creditors (unless it can be proven otherwise) in the event that:

- the legal actions or transactions being challenged were conducted within the period of one year before the debtor's bankruptcy, the transaction was not mandatory for the debtor and belongs to one of the following three categories:
  (a) a transaction in which the consideration that the debtor received was substantially less than the estimated value of the consideration given;
  (b) a payment or granting of security for debts which are not yet due; or
  (c) a transaction entered into by an individual debtor with a certain relative or related parties.

The nullification of the payment of a debt that has become payable can only be granted if it can be proven that:

- the recipient of payment (ie, the lender) know that the petition of bankruptcy against the debtor had been registered; or
- in the event that the payment was made due to a conspiracy between the debtor and the creditor(s), in order to provide the said creditor(s) with greater privilege than the other creditors.

The effect of a successful challenge is the nullification of the legal action or transaction in question (some court decisions have deemed such actions as unlawful acts) and therefore the restoration of the conditions obtaining prior to the execution of those actions or transactions.

The IBL specifically provides for the following consequences of a successful challenge:

- any persons receiving properties or goods that constitute part of those assets of the debtor which are covered by the legal action being nullified must return them to the receiver and this should be reported to the supervisory judge, if that person is not able to return the relevant goods or property in the same condition as they were, they will pay compensation to the bankruptcy estate; and
- the right of any third parties over the properties or goods, which are obtained in good faith and not free of charge, (including the holder of the security rights being imposed on them) should be protected.

For goods being received by the debtor under the legal actions being nullified, the receiver should return them or their value to the other party with whom the debtor conducts the legal action, to the extent that the bankruptcy estate is not jeopardised. If there is an outstanding difference that needs to be returned to the other party with whom the debtor conducts the legal action, that party may verify such difference as an unsecured claim.

8. Project Finance

8.1 Introduction to Project Finance

Project finance in Indonesia was introduced to finance the (first) Independent Power Producer (IPP) project in the 1990s. Nowadays infrastructure projects in Indonesia rely on project finance, on a non-recourse or limited-recourse basis, from offshore commercial banks, bilateral or multilateral financial institutions and export credit agencies. The involvement of state-owned banks and financial institutions in project finance in Indonesia is slowly increasing. From the banking-and-finance-regulation perspective, project finance is subject to the same requirements as any other type of loan (eg, the obligation to comply with the prudent banking principles of meeting certain minimum credit ratings, hedging and liquidity ratios).

The Government of the Republic of Indonesia, through the Minister of Finance (MOF), provides certain types of guarantee for infrastructure projects. These have included, for example, the business viability guarantee letter (BVGL) in the power sector to cover the payment obligations of PT Perusahaan Listrik Negara (Persero) (PLN) as the offtaker in a power purchase agreement and infrastructure guarantees covering the financial obligations of the government contracting agency in charge of the partnership project in public-private partnership (PPP) projects. In PPP projects, there is a guarantee provided by the Indonesia Investment Guarantee Fund (IIGF). The benefit of these guarantees can be extended to the lenders in project finance.

8.2 Overview of Public-Private Partnership Transactions

The mechanisms for establishing public-private partnerships between the government and the business sector for the development of infrastructure are generally set out in the Presidential Regulation No 38 of 2015 on Government Co-operation with Business Entities in the Procurement of Infrastructure (PR 38/2015).

This type of co-operation was introduced as an alternative to the conventional bureaucratic "business licensing" to entice investors by providing a sense of greater equality between the parties since the private investor is deemed as the government's counter-party. Under Indonesian law, contracts are considered as law and bind those who enter into them. This means that the government is legally bound to honour the contract, thus giving greater certainty compared to business licensing.

The procurement of an infrastructure project that will be developed with a PPP scheme is prepared by the minister/head of institution/head of region. However private business entities can initiate a PPP project and bring it to the government if the proposed infrastructure project and the procurement fulfil the following criteria:

- being technically integrated to the master plan for the relevant sector;
- being economically or financially feasible; and
- the private business entity is capable of financing, or procuring financing for, the implementation of the project.

The appointment of the business entity that will execute the PPP project (business entity executor) can be by way of public tender or direct appointment. Under PR 38/2015 direct appointment is expressly permitted in the event of the following situations:

- development of infrastructure that has been built and/or operated previously by the same developer;
- the work can only be carried with new technologies and only one developer can provide that technology; or
- the developer controls most or all the land required to implement the PPP.

If the PPP project was initiated by a private business entity, that private business as the initiator may receive compensation or certain advantages in the form of an extra 10% added to its points score in the competitive tender, the right to match, or to sell the project's idea or plan (including any intellectual property rights) to the government or the tender winner.

The implementation of the PPP project will be based on the co-operation agreement signed between the government contracting agency (CA) and the business entity executor.

Under PR 38/2015, the business entity executor is required to obtain the financing for the PPP project within twelve months of the signing of the co-operation agreement. However, the CA can grant an extension from time to time (with each extension being for a maximum of six months) if the failure to obtain financing is not caused by negligence of the business entity executor.

8.3 Government Approvals, Taxes, Fees or Other Charges

Presidential Decree No 39 of 1991 on the Co-ordination of Management of Offshore Commercial Loans (PD 39/1991) requires companies which intend to obtain offshore commercial loans to seek approval from the Offshore Co-ordinating Loan Team (Pinjaman Komersial Luar Negeri (PKLN)) for the plan and to report on the implementation of the loans and the repayment. The offshore loans that are under the co-ordination of the PKLN team are:

- offshore commercial loans relating to construction projects whose financings have the following nature/characteristics:
  (a) non-recourse;
  (b) limited-recourse;
  (c) advance payments;
  (d) trustee borrowings;
  (e) leasing; and
- offshore commercial loans relating to development projects whose financing is based on the scheme of BOT (build, operate and transfer), B&T (build and transfer), etc.

In addition to the approval from the PKLN team, the borrower of any offshore loan must comply with reporting requirements on a recurring basis, as follows:

- a report on the foreign exchange flows specifically on the plan to conclude an offshore loan;
- a report on the disbursements, interest payments and repayments under the offshore loans;
- a report on the foreign exchange flows in regard to the realisation of an offshore loan; and
- a report on the implementation of prudent principles.

The transaction documents do not need to be registered with any governmental body. However upon the signing of the transaction documents, the borrower must report to the PKLN team and Bank Indonesia and must provide a copy of the main finance documents (eg, common terms agreement). There is no requirement under Indonesian law to have the finance documents governed by Indonesian law. Therefore it is common in Indonesia to have the finance documents governed by foreign laws (usually English law or New York Law).

In respect of taxes, fees and other charges please refer to **4. Tax**.

8.4 The Responsible Government Body

The responsible government body for the oil and gas, power and mining sectors is the Ministry of Energy and Mineral Resources. The oil and gas sector also involves the Special Task Force for Upstream Oil and Gas Business Activities Republic of Indonesia (SKK Migas) as the government agency under the Ministry of Energy and Mineral Resources that manages the upstream oil and gas business activities under co-operative contract (PSC). Meanwhile in the power sector, it also involves PLN, a state-owned company that acts as the offtaker or CA in any PPP power projects. The responsible government bodies for other sectors are as follows:

- for water and toll roads, the Ministry of Public Works and Housing;
- for transportation (eg, ports and airports), the Ministry of Transportation; and
- for telecommunication (eg, satellite), the Ministry of Communication and Information.

8.5 The Main Issues When Structuring Deals

Foreign direct investment in Indonesia is subject to Presidential Regulation No 44 of 2016 on Business Fields that are Closed and Conditionally Open for Investment (Regulation No 44/2016) also known as the "negative list". Under the negative list, certain lines of business are closed or subject to a maximum foreign shareholding that must be complied with by a foreign investment company (PMA Company) in Indonesia. If the project company or the borrower is a PMA Company, this may affect the structuring of the deals. The negative list can also affect the execution of a pledge of shares where it limits the sale of the shares to a foreign third-party buyer.

In the power sector, in particular for non-geothermal independent power projects (IPPs), in addition to the negative list, the transfer of shares prior to commercial operation date (COD) is also subject to restriction under Minister of Energy and Mineral Resources Regulation No 48 of 2017 on the Supervision of Business Activities in the Energy and Mineral Resources Sector (Regulation 48). Regulation 48 provides that prior to COD, non-geothermal IPPs may only transfer shares to affiliated parties whose shares are more than 90%-owned by an equity financier or sponsor. Further, the affiliate must be a party one level below the sponsor (a direct subsidiary of the sponsor). While Regulation 48 does not define the term "sponsor", the current view from the Ministry of Energy and Mineral Resources is that the term is intended to refer only to direct shareholders of the IPP. The effect of this, given the way in which the term "sponsor" is used in Regulation 48, appears to be that the share transfer restrictions described above only apply to transfers of shares in the IPP itself, and not to transfers of shares in (including share pledge enforcements over) its direct or indirect shareholders. While, so far, the restrictions seem intended only to apply to shares in the IPP itself, we can't exclude the possibility that the ministry may change its view in the future, as a literal reading of Regulation 48 is not free from doubt on this point.

8.6 Typical Financing Sources and Structures for Project Financings

The financing sources for project finance in Indonesia are typically bank financing, multilateral or bilateral financial institutions and export credit agencies. Project bonds are also a source of project finance although not used as often as bank or export credit agency financing. Recently Islamic financing has also been used in project financing in Indonesia.

The project sponsors will incorporate a special purpose vehicle in the form of limited liability company to develop and run the project (the project company). As in typical project financing, the project company will become the borrower and all of its assets will be secured for the benefit of the lenders. The sponsors are required to provide sponsor support in the form of a contractual undertaking (set out in a sponsor support agreement) to provide equity to the project company when necessary.

8.7 The Acquisition and Export of Natural Resources

All energy and mineral natural resources found within the Indonesian jurisdiction are national assets of the Indonesian people and shall be controlled and utilised by the state for the maximum welfare of the people. Accordingly, the selling of energy and mineral natural resources is generally regulated and, to certain extent, subject to government approval. For instance, in the sector of mineral mining, a mining company is obliged to process and purify their minerals domestically before they can export the minerals. Selling minerals below certain purification levels is permitted provided that the mining company obtains approval from the Director General of Foreign Trade, at the Ministry of Trade which is issued based on a recommendation from the Director General of Mineral and Coal at the Ministry of Energy and Mineral Resources. As a result of this policy, in recent years, there have been a number of project financings in Indonesia for the development of processing and purifying facilities.

It should also be noted that pursuant to Government Regulation Number 1 of 2019 on Export Proceeds from Natural Resources Exploitation, Management, and/or Processing Activities, export proceeds from natural resources must be paid to an onshore bank account.

8.8 Environmental, Health and Safety Laws

Environmental matters in Indonesia are generally governed by Law No 32 of 2009 on Environmental Protection and

Management (Environmental Law). The Environmental Law was enacted for the purpose of protecting the Indonesian territory from environmental pollution and damage. In light of this, the Environmental Law requires any business activity conducted within Indonesia to comply with the requirement to prepare an environmental impact analysis documents that must be approved by the Minister of Environment and Forestry/Governor/Mayor/Regent (depending on the activities and coverage area of the project). The project company must also obtain an Environmental Permit issued by the Minister of Environment and Forestry/Governor/Mayor/Regent (as applicable). Normally the oil and gas, power and mining sectors are also subject to Government Regulation Number 101 of 2014 on Management of the Waste of Hazardous and Toxic Materials which requires that every company conducting business activities using and/or producing hazardous and toxic materials (locally known as "B3") to perform B3 waste reduction, B3 waste processing and/or B3 waste land-filling and obtain a B3 Waste Management Permit. In respect of health and safety, the project company must prepare occupational health and safety Guidelines pursuant to the Law No 1 of 1970 on Work Safety. Further, each industry sector also has its own safety regulations. However the general requirement is that every installation as well as all equipment and machinery used by a company must have certificates of worthiness.

In the context of infrastructure projects, the relevant government bodies that oversee environmental, health and safety in Indonesia are the relevant local government, the Ministry of Environment and Forestry, the Ministry of Energy and Mineral Resources and the Ministry of Manpower.

9. Islamic Finance

9.1 The Development of Islamic Finance

Indonesian banks and financial institutions are promoting *shari'a* financing products in Indonesia and *shari'a* financing is increasingly becoming a substantial part of the portfolios of Indonesian banks. This is in line with the Indonesian government's program which aims to increase the *shari'a* financing (and broader Islamic finance) market in Indonesia. In some cases, Indonesian banks and financial institutions offering *shari'a* products may offer more beneficial commercial terms to the borrower (in terms of pricing, etc) compared to the commercial terms under the conventional loan arrangement. The total of *shari'a* financial assets in Indonesia (excluding *shari'a* securities) is approximately USD94.44 billion, with 10.87% year-on-year growth per June 2019. The capitalisation of *shari'a* securities was estimated at IDR3,699.5 trillion (approximately USD260 billion) in June 2019. Currently, Indonesian banks and financial institutions offer various *shari'a* products, covering *murabaha*, *musharaka*, *mudaraba*, *ijara*, *qardh*, *istisnaa*. Variation of the products has also been introduced to the Indonesian market.

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9.2 Regulatory and Tax Framework

Shari'a financing is generally regulated under the auspices of the Financial Services Authority (Otoritas Jasa Keuangan) and performed within the constraints of the Shari'a Banking Law, along with regulations issued by the Financial Services Authority and fatwa issued by the Shariah National Board of the Indonesian Council of Ulama (Dewan Syariah Nasional Majelis Ulama Indonesia). Despite attempts to adopt *shari'a* principles into *shari'a* financing products in Indonesia, *shari'a* principles (such as ownership to portion of assets) are not entirely compatible with Indonesian laws and regulations. When such non-compatibility arises, practitioners rely on the guidelines issued by the Financial Services Authority (Otoritas Jasa Keuangan) and the Shariah National Board of the Indonesian Council of Ulama (Dewan Syariah Nasional Majelis Ulama Indonesia).

Accounting principles for *shari'a* financing have been introduced into Indonesia, which are substantially the same as conventional loan accounting treatment. Hence, there will be no difference in the accounting treatment for the parties' financial assets and liabilities under *shari'a* financing and they will be treated the same as customary conventional loan rights and liabilities in the respective parties' books and records. Tax treatment would also be the same as conventional loan structure.

9.3 Main Shari'a-compliant Products

Shari'a financing products can be issued by Indonesian banks and financial institutions licensed to conduct *shari'a* financing activities or that have a *shari'a* unit. Each bank and financial institution are required to have at least one director overseeing *shari'a* compliance and a dedicated *shari'a* supervisory board.

9.4 Claims of Sukuk Holders in Insolvency or Restructuring Proceedings

Sukuk is a debt instrument under Indonesian law and would be treated pari passu with all the issuers' other present or future unsecured and unsubordinated obligations.

9.5 Recent Notable Cases

Indonesian peer-to-peer financing practitioners have commenced development of *shari'a* -based financing products, in response to the increasing demands of the market. While it is still in its initial stages, the practice remains under scrutiny particularly due to the lack of *shari'a* -principles supervision in this sector.