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Project Finance 2024

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Indonesia: Law and Practice

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ABNR Counsellors at Law

INDONESIA

Law and Practice

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Contents

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ABNR Counsellors at Law

ABNR Counsellors at Law (ABNR) was founded in 1967 and is Indonesia's longest-established law firm, pioneering the development of international commercial law in the country following the reopening of its economy to foreign investment after a period of isolationism in the early 1960s. With around 120 partners and lawyers (including four foreign counsels), ABNR is the largest independent full-service law firm in Indonesia and one of the country's top three law firms by number of fee earners, giving it the scale needed to simultaneously handle large and complex transnational deals across a range of practice areas. The firm also has global reach as the exclusive Lex Mundi (LM) member firm for Indonesia since 1991. LM is the world's leading network of independent law firms, with members in more than 100 countries. ABNR's position as LM member firm for Indonesia was reconfirmed for a further six-year period in 2018.

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1. Project Finance Panorama

1.1 Sponsors and Lenders

Indonesian limited liability companies – including state-owned enterprises (SOEs) – typically act as local sponsors, whereas foreign legal entities or companies act as foreign sponsors. They then form a local subsidiary that will act as the project's investment vehicle.

Export credit agencies, multilateral agencies, commercial banks, and non-bank financial institutions (both local and foreign) typically act as lenders for project finance in Indonesia.

1.2 Public-Private Partnership Transactions

The main regulations concerning PPPs in Indonesia are:

- Presidential Regulation No 38 of 2015 dated 20 March 2015 on the Government Co-operation with Business Entities in the Procurement of Infrastructure (the "PR 38/2015");
- Presidential Regulation No 78/2010 on Infrastructure Guarantees in Public-Private Partnerships Provided Through Infrastructure Guarantee Entity (the "PR 78/2010");
- Minister of National Development Planning Regulation No 7 of 2023 on Implementation of Public Private Partnerships in Infrastructure Provision (the "Bappenas Regulation 7/2023"); and
- Minister of Finance Regulation No 260/PMK.011/2010 on Guidelines for Implementation of Infrastructure Guarantee in Partnership Project Between Government and Business Entity as amended by Minister of Finance Regulation No 8/2016 (the "MoF Regulation 260/2010").

Type of Infrastructure and Form of Co-operation

Types of infrastructure that can be developed with PPP schemes in Indonesia under PR 38/2015 are transportation infrastructure, road infrastructure, water resources and irrigation infrastructure, water supply infrastructure, centralised and local waste water management infrastructure systems, waste management infrastructure systems, telecommunications and informatics infrastructure, electricity infrastructure, oil and gas and renewable energy infrastructure, energy conservation infrastructure, urban facilities infrastructure, education facilities infrastructure, sports and arts facilities and infrastructure, zone infrastructure (eg, industrial zones), tourism infrastructure, health infrastructure, penitentiary infrastructure and public housing infrastructure.

PR 38/2015 also stipulates that PPPs may be conducted for infrastructure provision that comprises a combination of two or more types of infrastructure and may be partially financed by the government. Bappenas Regulation 7/2023 provides further elaboration on the combination of types of infrastructure projects in a PPP project as follows.

- PPPs can be a combination of two or more government contracting agencies (GCAs) for one type of infrastructure; or
- PPPs can be a combination of two or more GCAs for two or more types of infrastructure.

The GCAs of the relevant infrastructure that will be developed under a PPP scheme must sign a memorandum of understanding (MoU), which contains at least:

- an agreement on who will become the co-ordinator of the PPP project, as well as on

the decision-making mechanism of the PPP project;
- an agreement on the division of tasks and budget for preparation, transactions, and PPP management, including the rights and obligations of each GCA in the PPP agreement; and
- the implementation period of the PPP project, including the validity period of the MoU.

The MoU may also contain a dispute settlement mechanism.

The PPP scheme is conducted through a co-operation agreement (normally called a "PPP Agreement") entered into between the GCA – which can be the Minister/head of institution/head of regional government or an SOE/regional-owned enterprise as provider or administrator of the infrastructure, based on the laws and regulations – and the implementing business entity (IBE) appointed by the GCA through a tender process.

The PPP Agreement must specify, among other things, the project scope, the period of the partnership, an implementation/operation warranty, return of investment and the adjustment mechanism, rights and obligations (including risk allocation), performance standards, dispute resolution mechanism, and a supervision method. A PPP project can be identified, and the preparation of the project can be conducted, by either the GCA ("solicited project") or the private sector ("unsolicited project"). Nevertheless, the appointment of the IBE for both solicited and unsolicited PPP projects must be by way of public and transparent bidding or tender.

PPP Phases

In brief, PPP schemes in Indonesia consist of four phases.

Planning

This phase is only required for solicited PPP projects and is predominantly done by the GCA. The GCA will identify the viable project from a list of projects proposed by the Indonesian government, conduct preliminary study (which covers, among other things, the form, scheme and source of financing) and public consultation.

Preparation

For solicited PPP projects, the preparation phase covers the formulation of the pre-feasibility study, the GCA's implementation of supporting activities for the PPP project, and market sounding. The supporting activities that will be implemented by the GCA during this stage consist of, among others:

- the planning and implementation of land procurement;
- the submission of a proposal for government support to be approved by the Ministry of Finance;
- the submission of a proposal for government guarantee through *PT Penjaminan Infrastruktur Indonesia* (*Persero*) (or, in English, the Indonesia Infrastructure Guarantee Fund (IIGF)); and
- an application for final confirmation of availability payment.

For unsolicited PPP projects, the preparation phase covers:

- the submission of a PPP initiative by a private business entity;
- the evaluation and approval of the PPP initiative;
- the formulation of the feasibility study;
- public consultations and market sounding; and

- the evaluation and approval of the feasibility study.

Transaction

The transaction phase covers project location determination, procurement of an IBE, the signing of a PPP Agreement, and the financial close of the project.

Management

Once the PPP Agreement has been signed and the IBE has been financed, the construction of the project will commence.

Solicited Versus Unsolicited PPP Projects

There are two ways to initiate PPP projects in Indonesia: solicited and unsolicited PPP projects. In Indonesia, solicited PPP projects are more common, whereby the GCA initiates the provision of infrastructure in co-operation with a private business entity (thus making it a solicited PPP). Although not as common as solicited PPP projects, it is still possible for a business entity (the "Initiator") to propose a PPP initiative to the GCA (ie, an unsolicited PPP) for certain types of infrastructure, provided that such provision of infrastructure fulfils the following criteria:

- it is technically integrated with the master plan of the relevant sector;
- it is economically and financially feasible; and
- the Initiator has sufficient financial capability to finance the implementation of the project.

In an unsolicited PPP, the Initiator must first submit a letter of intent along with the relevant supporting documents for the project to the GCA for its evaluation. These supporting documents include:

- confirmation that the project aligns with the relevant sector's master plan, the government's plan, and regional spatial plans;
- evidence of the need for the provision of infrastructure;
- a preliminary study of the project;
- an overview of the Initiator's financial capabilities and technical experience; and
- early identification of the GCA institution responsible for managing the project.

The GCA will then assess the submitted documents within 15 business days and will make a decision within seven business days following the completion of the assessment period. If during the evaluation period another business entity also submits a proposal the same project to the GCA, the GCA may also evaluate their proposal and notify the Initiator in case additional time for evaluation is required and the reason therefor. Should the GCA approve the proposal, it will instruct the Initiator to proceed with preparation of the feasibility study.

After the Initiator completes its feasibility study, it will submit the documents (along with relevant supporting documents) to the GCA for assessment. In preparing the feasibility study, the Initiator may include an application for government support in accordance with the provision of applicable law. The GCA should then make its assessment of the submitted feasibility study documents based on several criteria, including whether the project should not necessitate government support in the form of financial contribution. In assessing the documents, the GCA will undertake a public consultation and market research to gather input on the proposed PPP project. This assessment should be completed within 30 business days (and is extendable for another 30 business days) as of receipt of the documents. If the feasibility study is approved

and the Initiator or the IBE has passed the qualification, the GCA will issue, among others:

- its approval of the feasibility study;
- its approval of the supporting documents;
- stipulation that the PPP project proposal is an unsolicited PPP project;
- stipulation that the Initiator has fulfilled the pre-qualification requirement of the PPP procurement;
- stipulation of the Initiator as the bid winner;
- stipulation of the compensation form; and
- statement that the feasibility study (together with the supporting documents) become the GCA's proprietary rights.

In addition to the foregoing, there are several benefits/privileges (compensation) that may be given to the Initiator, as follows:

- additional score of 10% in the tender process;
- a right to match against the best bidder in the tender process; or
- purchase of the PPP initiatives, including the related IP rights, by the GCA or the winning bidder.

The form of the above-mentioned compensation must be clearly set out in the GCA's approval.

Return of Investment for IBE

There are three types of return on investment (ROI) in PPP projects, which are:

- tariff;
- availability payment; and
- other types of ROI if they are not in contradiction with the applicable laws.

Benefit of PPP

The following benefits may be available for a PPP project.

- Government support is available in the form of viability support (also known as Viability Gap Fund (VGF)) and/or tax incentives as recommended by other Ministers, heads of agencies or heads of regional governments may be given to the PPP project.
- Project Development Facility (PDF) is one of the fiscal policies provided by the Minister of Finance to assist the GCA in preparing the pre-feasibility study and bidding documents and to assist the GCA in the PPP project transaction until the project reaches its financial close. The PDF may be sourced from the State Budget (*Anggaran Pendapatan dan Belanja Negara*, or APBN) or other legitimate sources.
- Government Guarantee is a financial compensation and/or other forms of compensation granted by the Minister of Finance to a business entity through a risk allocation scheme for a PPP project.

1.3 Structuring the Deal

Non-recourse or limited recourse debt financing are predominantly opted for in project finance in Indonesia. The projects are typically financed by a combination of debt and equity (paid-up capital or shareholder loans). Debt-to-equity ratios vary depending on the sectors being financed, but it is typically at a ratio of 75:25. The debt portion is mostly funded by bank loans (offshore or onshore). Corporate bonds, project bonds, and securitisation of existing projects' revenues are increasingly used to fund new infrastructure projects – for example, through the issuance of green bonds to fund sustainable projects.

1.4 Active Industries and Sectors

The infrastructure, energy and industry sectors (such as smelting, electric cars, and batteries) are expected to continue to be more active in Indonesia in the coming year.

2. Guarantees and Security

2.1 Assets Available as Collateral to Lenders

Type of Security Interest

Security interests in Indonesia are generally limited to those prescribed by Indonesian law. The form of security interests available under Indonesian law are:

- mortgage, fiduciary security and pledge for in rem security interests; and
- (corporate and personal) guarantees for personal security interests.

In rem security interests are security interests that create preferential rights for the holder of the security even in bankruptcy.

According to strict legal interpretation in Indonesia, security interests under Indonesian law are limited to those described under the following laws and regulations:

- the Indonesian Civil Code;
- the Mortgage Law (for land, property and other immovable assets); and
- the Fiduciary Law (for any other movable assets that cannot be encumbered under the Mortgage Law).

There are no other (contractually crafted) instruments that can function as security; thus, parties do not have complete freedom to determine security interests contractually. However, notwithstanding questions of validity, this "contractual security" is documented in practice. 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) may be deemed invalid by Indonesian courts in that they may be considered a circumvention of Indonesian security laws.

Assets Typically Subject to a Security Interest and the Corresponding Security Interest

The assets of an Indonesian debtor typically requested by creditors to be part of the security package and the respective security interest that can and would normally be taken over each asset are:

- land, plant and other fixtures – mortgage (or *hak tanggungan*), provided that the land has a specific land title permitted to be subject to mortgage (please see separate discussion on mortgages), as otherwise these assets may be subject to a fiducia security or an undertaking to obtain land title and to provide security;
- movable and immovable tangible assets – not able to be subject to mortgage, therefore secured by a fiducia security;
- receivables – fiducia security over receivable;
- insurance proceeds – fiducia security over insurance proceeds;
- IP – fiducia security over intellectual property and power of attorney to exercise IP;
- bank accounts – pledge of bank accounts and power of attorney to manage bank accounts;
- shares – pledge of shares, power of attorney to sell shares, and power of attorney to vote;
- contractual arrangements – conditional assignment and assumption agreement and

power of attorney to exercise contractual rights; and
- licences and other businesses – power of attorney to manage business.

Creation and Perfection of Security Interest

The following summarises the creation and perfection process of in rem security interests in Indonesia.

Land mortgage (hak tanggungan)

A land mortgage is established through the signing of a mortgage deed in the Indonesian language before a land deed official where the land is located in Indonesia and registration with the E-Mortgage Deed Registration System. The land mortgage will be established and finalised once the electronic mortgage certificate (E-Certificate) is issued and the electronic land title certificate has reflected the mortgage creation. The E-Certificate will be sent to the mortgagee via email.

Under the E-Mortgage regime, each lender or creditor must initially register itself in the E-Mortgage Party Registration System prior to the registration of the mortgage deed in the E-Mortgage Deed Registration System. The online mortgage registration system is only written in Bahasa Indonesia. Registration of lenders or creditors with the system may be burdensome for offshore creditors or lenders and may take a significant amount of time to complete.

Generally, no regulatory approval or consent is required to establish a mortgage. However, in the event that the land title held by the project company is granted upon land with management rights held by the government, the establishment of a mortgage may require approval from the relevant government institution – depending on the underlying arrangement for the land cooperation or utilisation agreement entered into between the project company and the relevant government institution as the basis to apply for the land title.

Fiducia security

A fiducia security is established by entering into a written agreement and is signed before a notary to be made into a notarial deed form in the Indonesian language. The concept of a fiducia security results in a transfer of legal title from the transferor to the transferee under the condition that the legal title will automatically return to the transferor upon full repayment of the relevant debt of the transferor or debtor. The transferee's ownership of the fiduciary secured assets lasts as long as the relevant debt of the transferor or debtor to the transferee remains outstanding. The parties may also agree that actual re-transfer by the transferee to the transferor will only take place upon full payment of the relevant debt.

The fiducia security agreement must be registered (online) at the Fiducia Registration Office within 30 days of the date of the fiduciary transfer agreement. The fiducia security becomes effective on the date of registration and, upon acceptance of the registration application, the fiduciary transferee will receive a fiduciary certificate issued by the Fiduciary Registration Office.

If within 30 days the fiducia security agreement is not registered, the parties must re-execute the fiducia security agreement. Other specific formalities (ie, notices and acknowledgements) are relevant for fiduciary security over receivables and fiduciary security over insurance proceeds.

Pledge

A pledge is established by a deed of pledge setting forth the particulars of the pledge, which can be executed in a notarial deed form or privately.

With regard to tangible assets, the requirement for the establishment 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. As regards intangible movable assets, a notification must be made to whomever the assets or receivables would have to be paid.

With regard to a pledge of shares, the pledge must be registered in the shareholder 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. This will be recorded in the shareholder register held by the Stock Administration Bureau. For blocked shares kept in the custody of the Indonesian Central Securities Depository (*Kustodian Sentral Efek Indonesia*, or KSEI), a confirmation letter will be issued by them certifying that the shares are pledged.

With regard to a pledge of a bank account, the relevant bank must be notified of and acknowledge the pledge. The acknowledgement also serves 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.

Contractual security

For contractual security in the form of conditional assignment and assumption agreement, the assignor is required to notify and obtain acknowledgement from the counterparties under the relevant contracts.

Security Agent

A security agent is authorised to sign security documents, manage the secured assets and enforce security on behalf of the lenders. However, there are differing views in terms of land mortgage, as the law does not expressly acknowledge the taking of security by lenders as represented by security agent. Therefore, it is recommended that each lender be listed and registered as a mortgagee as well.

2.2 Charges or Interest Over All Present and Future Assets of a Company

Indonesian security law does not recognise "floating charges" or other universal or similar security interest. In Indonesia, specific assets must be secured by a specific type of security.

Indonesian security can secure present and future assets of a company except for land mortgage. For fiducia security, however, the fiducia secured objects registered at the Fiducia Registration Office must be updated at the Fiduciary Registration Office.

2.3 Registering Collateral Security Interests

Generally, registering collateral security interests such as fiducia security and land mortgage is associated with registration fees or charges and Non-Tax State Revenue (*Penerimaan Negara Bukan Pajak*, or PNBP) paid to the government. The PNBP tariff is subject to change from time to time.

2.4 Granting a Valid Security Interest

The secured assets must be properly identified and listed in the security documents.

2.5 Restrictions on the Grant of Security or Guarantees

A company's articles of association typically provides for the necessary internal approval(s) required to be obtained before the company can grant any security or guarantee. In the context of a third-party security or guarantee, however, the validity of any legal act performed by an Indonesian company may be contested for the want of corporate benefit and compliance with its objects and the purposes of its articles of association. There is uncertainty as to whether the issuance of a third-party guarantee or security by a company to secure the fulfilment of obligations of a third party can be regarded to be in furtherance of the objectives of the company (ultra vires doctrine) and, consequently, whether such guarantee or third-party security may be voidable or unenforceable under Indonesian law.

In determining whether the issuance of a third-party guarantee or security is in furtherance of the objectives of a third-party guarantor, it is important to consider the provisions of the articles of association of that third-party guarantor and whether that third-party guarantor derives certain commercial benefit from the transaction in respect of which the third-party guarantee is issued. Based on the ultra vires doctrine, the validity or enforceability can in principle only be challenged by that third-party guarantor itself – ie, arguably through:

- the shareholders of that third-party guarantor;
- the board of directors of that third-party guarantor; or
- the board of commissioners of that third-party guarantor, or by a receiver or trustee in bankruptcy.

By obtaining the written consent of all of the shareholders, the board of directors, and the commissioners of the third-party guarantor authorising that third-party guarantor to enter into a third-party guarantee or security and confirming that such transaction is in the interests of that third-party guarantor, those parties should not be able to successfully challenge the validity or enforceability of that third-party guarantee or security on the basis of the ultra vires doctrine.

In addition, it should be noted that:

- under Presidential Decree No 59 of 1972, state-owned entities and regional-owned entities are not permitted to grant security and/or guarantee to secure the repayment of offshore loans received by state-owned entities, regional-owned entities and private companies; and
- the granting of security or guarantee by a sponsor/project company is caught by the World Bank Negative Pledge where the sponsor/project company is controlled and owned by the government of Indonesia.

2.6 Absence of Other Liens

For fiducia security, the lender could check for other liens on their collateral via the online website of the Fiducia Registration Office – noting that this is only possible for fiducia registration done after 5 March 2013, when the manual registration transitioned to online registration. For fiducia registration prior to 5 March 2013, manual checking is possible in theory but not in practice.

For land mortgage, the lender (with the company's and notary's assistance) could check through the relevant land office and obtain a statement letter confirming the land status.

No public registry is available for pledge of shares in a private company. Pledge of shares in

a private company is recorded in the shareholder register of the relevant company and the lender typically asks for the latest shareholder register to confirm this. For pledge of shares in a public company, the lender could confirm this through the Stock Administration Bureau.

For pledge of bank accounts, no public registry is available.

2.7 Releasing Forms of Security

Under Indonesian law, a security interest is accessory in nature and when the underlying claim is paid, expired or deemed null and void, the security interest also ceases to exist. However, typically, an Indonesian law release agreement is entered between the security agent and the obligors on the pay-off date. The release agreement would also set out additional steps that will be required to effect the release and discharge of the Indonesian security documents as follows.

- Land mortgage – release and discharge through the land office or E-Mortgage Deed Registration System, as applicable, with land deed official's assistance. The security agent is to provide power of attorney to the land deed official, as well as provide the release application and release statement.
- Fiducia security – release and discharge through the Fiducia Registration Office with notary's assistance. Security agent is to provide power of attorney to the land deed official, as well as provide the release application and release statement.
- Pledge of shares – deletion of pledge annotation from the company's shareholder register and return of original share certificate to the shareholders for pledge of shares in a private company. For pledge of shares in a listed company, the security agent needs to:
  (a) instruct the share registrar to de-register the pledge;
  (b) make a request to the custodian to unblock the securities account;
  (c) ask the custodian to request that the KSEI issue a confirmation that the Securities Sub-Account in C-BEST is unblocked; and
  (d) ask the custodian to transfer the shares to the pledgor's securities account immediately after the KSEI issue the unblocking confirmation.
- Pledge of bank account – notice of release to the account bank.

3. Enforcement

3.1 Enforcement of Collateral by Secured Lender

A secured lender can enforce its collateral upon an event of default based on the underlying agreement. Security interest in Indonesia can be enforced by way of public auction or private sale. In the event of default, theoretically, secured lenders may sell the secured assets without any court decision. However, in practice, the state auction body sometimes still requires a court decision or order to be provided before it will proceed with a public auction. The state auction body may even refuse the application of a public auction sale if the party that wishes to execute the security could not provide a court decision or order for said auction.

For a pledge of shares, the enforcement may be subject to the following restrictions. The sale of pledged shares through enforcement of the pledge will be subject to restriction of the articles of association of the company whose shares have been pledged. The articles of association may stipulate that the sale of shares is subject to

other shareholders' right of first refusal or to prior approval of a general meeting of shareholders. In some cases, licences of the company may include restrictions on changes of control of the licence holders and thus these provisions must also be observed.

It should be possible for the security agent to directly enforce and obtain proceeds of the fiducia security over receivables, the fiducia security over insurance proceeds, the fiducia security over reinsurance proceeds, and the pledge of bank account.

3.2 Foreign Law

A choice of a foreign law as the governing law of the contract and the submission to a foreign jurisdiction will be upheld in Indonesia except:

- where it is manifestly incompatible with the public policy of Indonesia; or
- where the Indonesian court may give effect to mandatory rules of the laws of another jurisdiction with which the situation has a close connection, if – and in so far as – under the laws of that other jurisdiction those rules must be applied, whatever the chosen law.

3.3 Judgments of Foreign Courts

Foreign arbitral awards are enforceable under Indonesian law without re-examination of the merits and re-litigation of the matters to the extent that they are issued by an arbitrator or arbitral tribunal in a country that is also a party to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (the "New York Convention"). The award needs to be registered at Central Jakarta District, with a writ of execution (known as an exequatur) from the chair of the Central Jakarta District Court or, where the award involves the government of Indonesia as one of the parties to the dispute, from the Supreme Court of Indonesia (through the Central Jakarta District Court).

Foreign court decisions are not enforceable within Indonesia. The judgment can be used as evidence in a retrial of the merits of the case – albeit subject to the prevailing laws and regulations. Indonesia is not a party to any treaty, convention or bilateral agreement that recognises the enforcement of a foreign court judgment.

3.4 A Foreign Lender's Ability to Enforce

In general, there are no other matters that might impact a foreign lender's ability to enforce its rights under a loan or security agreement. Previously, the Minister of Finance Regulation 213/PMK.06/2020 (the "MOF Regulation 213/2020") requires a lender holding security that wishes to sell the assets by way of public auction (via Auction Service Office (*Kantor Pelayanan Kekayaan Negara dan Lelang*, or KPKNL), Auction House or Class II Auction Official Office) to obtain an Indonesian Tax Identification Number (*Nomor Pokok Wajib Pajak*, or NPWP).

However, such requirement has been revoked by the Minister of Finance Regulation 122/2023 on Auction Guidance ("MOF Regulation 122/2023") and, as of 1 January 2024, an NPWP is only required for sellers who are required under Indonesian law to obtain an NPWP (ie, taxpayers under Indonesian law, which does not include foreign creditors or lenders). Nonetheless, in practice, the authors understand that – even though an NPWP is not required for foreign creditors or lenders – these creditors and lenders will need to obtain a statement letter from the tax office confirming that they are not taxpayers under Indonesian law.

4. Foreign Investment

4.1 Restrictions on Foreign Lenders Granting Loans

In general, foreign lenders are not restricted from granting loans. However, foreign lenders are restricted from granting loans to Indonesian entities if such loans require security from the Indonesian government or the Bank Indonesia (or other state-owned banks) and result in any liabilities of the Indonesian government.

4.2 Restrictions on the Granting of Security or Guarantees to Foreign Lenders

In general, the granting of security or guarantees to foreign lenders is not restricted or impeded. However, as mentioned in **2.5 Restrictions on the Grant of Security or Guarantees**, it should be noted that:

- under Presidential Decree No 59 of 1972, state-owned entities and regional-owned entities are not permitted to grant security and/or guarantee to secure the repayment of offshore loans received by state-owned entities, regional-owned entities and private companies; and
- the granting of security or guarantee by an Indonesian entity is caught by the World Bank Negative Pledge where the Indonesian entity is controlled and owned by the government of Indonesia.

4.3 Foreign Investment Regime

Foreign direct investment is subject to restrictions or requirements that vary based on the line of business of the company – for example:

- limited foreign shareholding;
- minimum capital contribution; or
- certain co-operation with microenterprises or SMEs.

4.4 Restrictions on Payments Abroad or Repatriation of Capital

There are no restrictions on payments abroad or repatriation of capital by foreign investors. However, any transfer of foreign exchange to and from abroad by such person is subject to the reporting obligation to Bank Indonesia as regulated by Bank Indonesia regulations concerning the monitoring of the flow of foreign exchange activities and the reporting of foreign exchange activities other than offshore loans, as may be amended from time to time. Certain transactions of Indonesian rupiah have been restricted by the Bank Indonesia Regulation on the Money Market and Foreign Exchange Market, as may be amended from time to time, and its implementing regulation. Violation of these regulations is subject to administrative sanctions.

4.5 Offshore Foreign Currency Accounts

A project company may establish and maintain offshore foreign currency accounts.

5. Structuring and Documentation Considerations

5.1 Registering or Filing Financing of Project Agreements

The financing agreement is subject to the company's report to:

- Bank Indonesia, in respect of offshore loans, foreign exchange flows, and the fulfilment of offshore loan prudential principles; and
- the Minister of Finance in respect of offshore loans.

The timing of such report is subject to the relevant regulations.

The financing or project agreements need to be prepared and signed in the Indonesian language (in addition to the foreign language) for compliance with the Indonesian language regulations and to ensure the validity and enforceability of such agreements.

5.2 Licence Requirements

Ownership of land requires a title over such land evidenced by the relevant title certificate. The different types of land title are:

- right of ownership;
- right to build;
- right to cultivate; and
- right of use.

Only right of use can be granted to foreigners, as well as foreign legal entities having a representative in Indonesia.

Natural resources cannot be owned by a private entity as they are controlled by the state -although such private entity may use natural resources based on the relevant permit. By way of example, a company may explore and exploit geothermal resources based on a geothermal business licence issued by the Minister of Energy and Mineral Resources.

Undertaking the business of ownership or operation of such assets requires licence(s) under the relevant regulations. It is not possible for a foreign entity to hold such a licence; it would need to be done through the establishment of a foreign investment company in Indonesia, which would apply for and be granted such licence.

5.3 Agent and Trust Concepts

The concept of security trust is not recognised in Indonesia. The common arrangement used in Indonesia is the concept of security agent as an alternative to security trust.

5.4 Competing Security Interests

Methods of Subordination

The following methods of subordination are used.

- Contractual subordination is possible and common. It can be achieved by an intercreditor arrangement between the lenders or an individual subordination deed (commonly used in a shareholders' loan).
- Structural subordination is not common.
- Intercreditor arrangements are common. The parties to an intercreditor agreement usually include lenders, borrowers and obligors. The agreement is used to set out various lien positions, the rights and obligations of each lender, and their impact on other lenders.

The priority will be applicable in the insolvency/bankruptcy proceeding. Creditors that hold in rem security interest will have higher ranking than creditors that do not hold any in rem security interest. Generally, mortgages, pledges and fiduciary transfers or assignments are in rem security interests that are absolute and exclusive. They create preferential rights to the holder.

5.5 Local Law Requirements

Typically, the project sponsors establish a special purpose vehicle – often in the form of an Indonesian limited liability company – to oversee the development and operation of the project. This is known as the project company.

6. Bankruptcy and Insolvency

6.1 Company Reorganisation Procedures

Typically, when it comes to debt restructuring, parties can engage in private negotiations regarding the unpaid debt as long as the company has not been officially declared bankrupt by a court. Nevertheless, the Indonesian Bankruptcy Law does offer a formal mechanism for corporate rescue known as the "suspension of payments" process. This process is applicable to all individuals and businesses with their registered address or place of operation in Indonesia.

Suspension of Payments

The process of suspension of payments begins when either the debtor or their creditors file a petition with the Commercial Court. This petition includes a proposal to repay some or all of the debt to both secured and unsecured creditors. The primary aim is to provide the debtor with an opportunity to reorganise the company, with the hope that it can continue operating and eventually satisfy the claims of its creditors. Following the submission of the petition, the Commercial Court grants the debtor provisional suspension of payments and appoints two key figures – namely, an administrator and a supervisory judge. These individuals work alongside the debtor to oversee its financial affairs.

During this suspension period, the debtor retains the ability to manage and dispose of its assets, but always in collaboration with the appointed administrator. Importantly, the debtor is not obligated to make payments to unsecured creditors during this time, and secured creditors cannot enforce their security interests without the court's approval. Additionally, the debtor has the option to present a proposed composition plan to all of its creditors.

First Creditors' Meeting

Within 45 days of the provisional suspension of payments being granted, it is mandatory to convene a meeting of the creditors. During this meeting, secured and unsecured creditors have two options – namely, either to:

- give their approval to a composition plan if one was presented to the Commercial Court; or
- reach an agreement to extend the provisional suspension of payments, converting it into a more extended period of up to 270 days from the initial grant of provisional suspension.

In the event that the creditors do not reach an agreement, the debtor will be officially declared bankrupt.

Composition Plan Ratification

If the creditors give their approval to the plan, a written report must be submitted by the supervisory judge to the Commercial Court. The court then evaluates this report and listens to input from the administrator and creditors, who may have objections. The court is required to reject the plan if:

- the value of the debtor's assets significantly exceeds the amount specified in the plan;
- there is insufficient certainty that the plan will be successful;
- the plan was reached through fraudulent transactions, unfair preferences given to one or more creditors, or other unethical means – regardless of whether the debtor or any other party was involved in this misconduct; or
- the fees and expenses incurred by the administrator or other professionals engaged have not been paid or adequately secured.

Once ratified, the composition plan becomes legally binding for all secured and unsecured creditors, except for those secured creditors who dissented. Dissenting secured creditors have the right to receive compensation from the debtor, calculated at the lower of either:

- the value of their collateral, with the option to choose between the value specified in the security documents or the value determined by an appraiser appointed by the supervisory judge; or
- the amount of their outstanding secured claims.

Post-ratification

After the plan is approved, the temporary suspension of payments comes to an end, and the administrator or receiver (as relevant) is released from their duties. The control of the debtor's business and assets is then returned to the debtor, with any specific terms outlined in the plan still in effect.

6.2 Impact of Insolvency Process

A bankruptcy proceeding may affect the ability to enforce security during the "stay period". The stay period is 90 days from the rendering of a bankruptcy declaration, and a maximum of 270 days from the rendering of a suspension of payments decision.

Preferential creditors would have a higher ranking with regard to proceeds arising from the bankruptcy asset's liquidation, even though the assets might be part of a secured claim of a creditor. Claims for costs of foreclosure, costs incurred to protect the bankruptcy assets, claims from the government (including tax), and employees' claims all have a higher ranking than a secured claim.

No entity is excluded from bankruptcy proceedings. However, certain financial institutions can only be the subject of a bankruptcy petition made by a relevant government institution. By way of example, insurance companies can only be petitioned by the Indonesian Financial Services Authority. The legislation applicable to them is Law No 40 of 2014 on Insurance.

Based on Law No 37 of 2004 on Bankruptcy and Suspension of Payments (the "Bankruptcy Law"), there are two types of court-sanctioned insolvency proceedings applicable to Indonesian limited liability companies: bankruptcy proceedings and suspension of payment proceedings.

6.3 Priority of Creditors

When a bankruptcy estate is declared to be in a state of insolvency and the receiver decides to liquidate the bankruptcy estate for distribution to the creditors of the bankrupt debtor, a ranking will need to be applied.

The general rule on distributing the proceeds of a bankruptcy estate to unsecured creditors is one of equality, subject to the statutory priority rights of certain categories of creditors. Shareholders rank behind all creditors in the distribution of the proceeds of the bankrupt estate. Secured creditors may enforce their security rights as if there were no bankruptcy, subject to any applicable stay of enforcement. However, upon the request of the receiver or the preferred creditor having rank higher than the secured creditors, the relevant secured creditor must grant its portion from the proceeds of the enforcement of in rem security for the same amount as such preferred creditor's claim.

In descending order, the ranking order of creditors under the bankruptcy is:

- outstanding wages (excluding severance payments and other rights) of the employees of the bankrupt debtor – these would rank higher than any claims and the outstanding rights of the employees of the bankrupt debtor other than outstanding wages would rank below those of the secured creditors;
- specific expenses stipulated by the Tax Law, such as:
  (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, such as:
  (a) tax claim;
  (b) court charges that 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) legal charges, exclusively caused by sale and saving of the estate (these will have priority over pledges and mortgages);
- bankruptcy estate creditors (ie, claims against 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 debtor'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;
- secured creditors, which under Indonesian law consist of:
  (a) mortgage (for land);
  (b) pledge (over movable intangible assets);
  (c) fiduciary transfer (over movable and intangible assets); and
  (d) hypothec (for aircraft and ships of more than 20 cubic metres);
- specific statutorily preferred creditors whose preference relates only to specific assets;
- general statutorily preferred creditors (eg, revenue authorities), which should include the severance payments.
- unsecured creditors receive their pro rata share of any of the remaining proceeds – the cost of the bankruptcy is shared pro rata among the statutorily preferred creditors and the unsecured creditors; and
- shareholders.

However, it should be noted that the foregoing priority order may not always be upheld strictly for specified and unspecified reasons.

6.4 Risk Areas for Lenders

The Indonesian Bankruptcy Law regulates nullification of preferential transfer transactions conducted by a borrower before its bankruptcy, if such transaction were considered detrimental to the creditors by the receiver. The receiver may nullify such transfer if:

- the preferential transfer was performed by the borrower before it was declared bankrupt;
- the borrower was not obligated by contract (existing obligation) or by law to perform the preferential transfer;
- the preferential transfer was prejudicial to the creditors' interests; and
- the borrower and a third party had or should have had knowledge that the preferential

transfer would prejudice the creditors' interests.

If the preferential transfer transaction was carried out within one year prior to the borrower's bankruptcy, provided that the transaction was not mandatory for the borrower and unless it could be proven otherwise, both the borrower and the third party with whom the act was performed are deemed to have known that the transaction was detrimental to the creditors if the transaction falls into one of the following three categories:

- a transaction in which the consideration that the borrower received was substantially less than the estimated value of the consideration given;
- a payment or granting of security for debts that are not yet due; or
- a transaction entered into by the borrower with a certain relative or related parties.

There is no provision under the Indonesian Bankruptcy Law that stipulates a specific period in which the preferential transfer claim can be made. However, a request for the nullification of a preferential transfer must be made by the receiver. The claim can be made only if the borrower has a receiver.

If the creditors find borrower's assets that existed during the bankruptcy proceedings but are discovered only after the bankruptcy proceedings have been completed, the creditors may report such findings to the Commercial Court. The Commercial Court will then appoint a receiver to distribute such newly discovered assets to the creditors whose rights have not been satisfied in full.

6.5 Entities Excluded From Bankruptcy Proceedings

No entity is exempted from bankruptcy proceedings. Nonetheless, specific financial institutions can only be the target of a bankruptcy petition if initiated by a relevant government agency. By way of example, insurance companies can solely be petitioned by the Indonesian Financial Services Authority. The applicable legislation is Law No 40 of 2014 on Insurance.

7. Insurance

7.1 Restrictions, Controls, Fees and/or Taxes on Insurance Policies

There are no limitations imposed on insurance policies for project assets issued or guaranteed by foreign insurance companies. Nevertheless, the income tax in Indonesia – set at 20% – applies to the payment of insurance premiums received by these foreign insurance companies.

7.2 Foreign Creditors

If insurance policies for project assets are encumbered by a fiduciary security and the relevant insurance company acknowledges this security or assignment, then the payouts from these policies may be payable to foreign secured creditors. It is also typical for secured creditors to be listed as an insured through a banker's clause under the insurance policy.

8. Tax

8.1 Withholding Tax

Payments made by the company to lenders under the financing agreements are subject to withholding tax in Indonesia unless the recipient is an Indonesian bank and/or an Indonesian branch of a foreign bank. If the recipient is a tax

resident of a jurisdiction that has an effective tax treaty with Indonesia, it could get the benefit of a reduced withholding tax rate under the tax treaty.

8.2 Other Taxes, Duties, Charges

Other than the registration fee for the security interest, as stated in **2.3 Registering Collateral Security Interests**, all agreements entered in Indonesia or to be used in Indonesian territory are subject to Indonesian stamp duty. Currently, the nominal amount of Indonesian stamp duty is IDR10,000 for transactions of more than IDR5 million. Generally, stamp duty is due and payable at the time documents are executed.

8.3 Limits to the Amount of Interest Charged

Generally, parties can agree on the amount of interest that can be charged. In the absence of such agreement and to the extent Indonesian law applies, 6% per annum is the maximum interest rate that can be charged.

9. Applicable Law

9.1 Project Agreements

Usually, project agreements are governed by Indonesian law. However, certain project agreements – where the execution does not necessarily occur in Indonesia (ie, offshore supply contracts, offshore Engineering, Procurement or Construction (EPC) contracts or offshore or technical services agreements) – are typically governed by foreign law.

9.2 Financing Agreements

Financing agreements are generally governed by foreign law (commonly English or New York law), save for the Indonesian security documents, which must be governed by Indonesian law.

9.3 Domestic Laws

Indonesian security must be governed by Indonesian law. Specific project agreements, such as those for onshore construction, are legally mandated to be subject to Indonesian law.

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