

THE REAL ESTATE M&A  
AND PRIVATE  
EQUITY REVIEW

FOURTH EDITION

**Editors**

Adam Emmerich and Robin Panovka

THE LAWREVIEWS

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# PREFACE

Publicly traded real estate companies and real estate investment trusts (REITs), with help from real estate private equity, have transformed the global real estate markets over the past 25 years. Their principal innovation, and secret sauce, is ‘liquid’ real estate. Unlike traditional property ownership, equity in publicly traded real estate vehicles is highly liquid, and can be bought and sold in large volumes, literally in minutes, on numerous global exchanges.

Publicly traded real estate vehicles have an aggregate market capitalisation of approximately US\$1.7 trillion globally, including over US\$1 trillion in the United States and approximately US\$200 billion in each of Europe and Asia. As public REITs and other vehicles have aggregated these properties and grown in scale and sophistication, so too have real estate-focused private equity funds, playing an important role catalysing hundreds of billions of dollars of REIT and real estate M&A transactions and IPOs.

However, despite the massive growth, the potential growth is far larger both in long-standing REIT markets and in newer REIT jurisdictions, where the trend is more nascent. With increasing development and urbanisation, the world is producing more and more institutional-grade properties, and a growing percentage of this expanding pool – an estimated US\$5 trillion and counting, so far – will inevitably seek the advantages of liquidity by migrating to the publicly traded markets. The growth is expected to be both local and cross-border, with approximately 40 countries already boasting REIT regimes.

REITs and other publicly traded vehicles for liquid real estate have grown because they are often a superior vehicle for stabilised assets. Greater liquidity and transparency – and often superior governance – are attractive to investors, resulting in a lower cost of capital and superior access to vast amounts and varieties of capital in the public markets. In addition to cheaper capital, REITs and other public vehicles benefit from efficiencies of scale, sophisticated management and efficient deal structures, to name just a few advantages. With these advantages, the global march of real estate to the public markets seems unstoppable.

This publication is a multinational guide for understanding and navigating the increasingly complex and dynamic world of liquid real estate and the transactions that mostly produce it. The sea change in the markets, sometimes called the ‘REIT Revolution’, has meant that major real estate transactions have migrated from ‘Main Street’ to ‘Wall Street’. They now often take the form of mergers, acquisitions, takeovers, spin-offs and other corporate transactions conducted in the public markets for both equity and debt. They have grown exponentially in complexity and sophistication, and increasingly represent cross-border multinational transactions fuelled by the now global real estate capital markets and M&A deal professionals. And they are often intermediated by international investment banks rather than local brokers, and financed with unsecured bonds or commercial mortgage-backed securities. In a fair number of cases they are catalysed by private equity firms or similar actors,

sometimes building portfolios to be taken public or sold to public real estate companies, and sometimes through buyouts of public real estate companies for repositioning or sale.

To create this publication, we have invited leading practitioners from around the globe to offer practical insights into what is going on around the conference tables and in the markets in their jurisdiction, with an eye to cross-border trends and transactions. As will quickly become evident, the process of liquefying real estate and the transactions involving public real estate companies require a melding of the legal principles, deal structures, cultures and financial models of traditional real estate, public company M&A and private equity. None of this, of course, happens in a vacuum, and transactions often require expertise in tax, corporate and real estate law, not to mention securities laws and global capital markets. Each of our distinguished authors touches on these disciplines.

We hope this compilation of insight from our remarkable multinational authors produces clarity and transparency into this exciting world of ‘liquid real estate’ and helps to further fuel the growth of the sector.

**Adam Emmerich and Robin Panovka**

Wachtell, Lipton, Rosen & Katz

New York

August 2019

# INDONESIA

*Emir Nurmansyah, Giffy Pardede and Gustaaf Reerink<sup>1</sup>*

## I OVERVIEW OF THE MARKET

To date, Indonesia's market for investment-grade real estate assets has been rather illiquid, showing very limited M&A and private equity activity. Many foreign investors consider Indonesia to be a risky place to do business. Until mid-2017, Indonesia's credit ratings were still below investment grade.<sup>2</sup> Furthermore, the legal framework is generally deemed to be unsupportive of cross-border transactions. Indonesia's investment law and land law impose restrictions on foreign investment. Banking and capital market legislation creates only limited room for creative financial structures. Creditors can establish security rights on land, shares and other assets, but in practice it may not always be easy to enforce these rights.

Being the world's fourth most populous country, with a fast-growing middle class, Indonesia has the potential to develop into a major market for real estate M&A and private equity. An increasing number of foreign investors, particularly from Japan, Korea and China, who already have some experience in doing business in Indonesia, recognise this potential and invest in the country's real estate market. Generally, the ASEAN market has an increased interest among foreign investors. Indonesia, perhaps together with Vietnam, Myanmar and Malaysia, is one of the countries that receives particular attention. Recent pro-foreign investment measures of the Jokowi administration, consisting of, inter alia, deregulation measures, a loosening of foreign investment restrictions, and tax and other incentives, contribute to this development.

Some measures that should specifically boost the Indonesian real estate sector are the relaxing by the Indonesian Central Bank (Bank Indonesia) of the macro-prudential policy by raising the loan-to-value ratio, or financing-to-value ratio, for property loans. The policy should not only benefit individual home owners, but also developers, who can now provide a lower guarantee when taking out a loan from the bank. The Jokowi administration, which following the President's re-election in April 2019 will be in office for another five years, has also relaxed foreign ownership in residential property, albeit with limited short-term benefits expected. Finally, the Minister of Finance and the Indonesian Financial Services Authority

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1 Emir Nurmansyah and Giffy Pardede are partners and Gustaaf Reerink is foreign counsel at Ali Budiardjo, Nugroho, Reksodiputro. The authors would like to thank Craig Williams and Anton Sitorus of Savills Indonesia for their valuable input on current developments in Indonesia's real estate market as well as Linda Purnomo and Chaterine Tanuwijaya of Purnomo Consult for their comments on the tax implications of the real estate transactions discussed in this chapter.

2 Standard & Poor's was the last of the three major credit rating agencies to raise Indonesia's credit rating to investment grade on 19 May 2017. Recently, the three credit rating agencies increased Indonesia's credit rating even further.

(OJK) have taken several measures to make the use of real estate investment funds in the form of a collective investment contract (DIRE) – the Indonesian equivalent of real estate investment trusts (REITs) – more attractive.

There are generally four types of foreign investors active in Indonesia's real estate market:

- a* public real estate companies;
- b* DIREs or REITs;
- c* sovereign wealth funds; and
- d* private equity.

Foreign investors will need to invest through an Indonesian limited liability company with foreign investment status, a PMA company (as discussed in Section IV) or with a public listing. There are currently around 75 public real estate companies listed at the Indonesian Stock Exchange (IDX). Many of these companies have foreign participation. Well-known names with a strong presence are Agung Podomoro, Ciputra, Summarecon, Lippo and Sinar Mas. Most of the public real estate companies in Indonesia are traditionally developers, but some are trying to diversify their income streams, for instance, by investing in REITs, as discussed in further detail in Section III.

Foreign investors generally invest in four categories of real estate in Indonesia:

- a* commercial buildings for offices, hotels or retail;
- b* residential buildings;
- c* hospitals and healthcare; and
- d* land for development.

Most of the investments are for the long term, but particularly the investments in commercial buildings and residential buildings are sometimes only made to support development, after which individual units or parts of the property are sold.

In addition, some foreign conglomerates whose core business is not necessarily real estate are becoming active on Indonesia's real estate market. This also applies to certain financial institutions and insurance companies. These companies are often investing in commercial real estate for their own domestic occupation, for instance, for foreign employees who need to be housed in Indonesia.

In terms of transaction structure, the investments are generally still rather conventional. Most acquisitions consist of plain vanilla sale and purchase of direct property, and sometimes involve the sale and purchase of shares in local real estate companies, either directly or through the IDX. Again, the legal framework puts limitations on the creation of more sophisticated structures. Often, foreign investors create a joint venture with local partners, which indeed may be a requirement under Indonesian investment legislation.

In terms of deal value, the investments may sometimes be significant, but generally not as large as in countries with a more developed real estate market.

## **II RECENT MARKET ACTIVITY**

### **i M&A transactions**

M&A activity on Indonesia's real estate market is limited, but increasing. Recent transactions include the acquisition in May 2018 by PT Waskita Karya Realty of shares in PT Mitra Mega Development from PT Green Orchid Berkah Madani. PT Mitra Mega Development is developing a project called Logios Apartments, which consists of apartments and three

towers totalling 1,640 units, on an 8,149 square metres plot in Depok. PT Waskita Karya Realty financed the transaction by the issuance of Medium-Term Notes. The total deal value was 880 billion rupiah.<sup>3</sup> In May 2018, the Singapore listed company Perennial Real Estate Holdings acquired 100 per cent interest in Sanctuary City Pte. Ltd, which in turn holds a 60 per cent interest in PT Bhakti Bangun Harmoni. The remaining 40 per cent of the shares in PT Bhakti Bangun Harmoni are held by PT Cipta Harmoni Lestari. PT Bhakti Bangun Harmoni is the owner of 246,982 square metres of land in Sentul, Bogor. The company is developing Sanctuary City, a residential real estate project comprising houses and condominiums totalling 1,700 units. The consideration for the acquisition of Sanctuary City Pte. Ltd was US\$15.6 million. The total development costs of the project are over 1.6 trillion rupiah, funded through residential sales, external borrowings and internal funds.<sup>4</sup> In December 2018, Thailand based Strategic Hospitality Extendable Freehold and Leasehold Real Estate Investment Trust (SH-Trust) acquired from PT Agung Podomoro Land Tbk shares in PT Griya Pancaloka, a company that has the rights to develop and use the land to operate Sofitel Bali Nusa Dua Beach Resort, a five-star hotel with 398 guestrooms, 17 villas and facilities. Upon closing of the transaction, the REIT's subsidiary, PT Griya Pancaloka, entered into a master lease agreement with PT Central Pesona Palace, the master lessee of Sofitel Bali Nusa Dua Beach Resort. The total investment amount was around 1.653 trillion rupiah.<sup>5</sup>

Several other M&A transactions in recent months involved property acquisitions. In July 2018, Singapore based UOL Group Limited, the parent company of Pan Pacific Hotel Group Limited, acquired 180 units at tower one of Thamrin Nine, a new property that is currently being constructed on a 5.4 hectares plot at Jalan Thamrin, the main corridor from Central to South Jakarta. Being 333.5 meters high and with 70 floors, tower one is said to become the highest building in Indonesia. UOL Group Limited will also manage 200 rooms of Parkroyal Hotel, a new hotel in the second tower of Thamrin Nine. The deal value was US\$56.8 million.<sup>6</sup> In September 2018, PT OUE Pengembangan Property, which is a subsidiary of Singapore real estate developer OUE Pte. Ltd., which is again part of the Indonesian conglomerate PT Lippo Karawaci Tbk, acquired around 8,000 square metres of land at Jalan Sudirman, South Jakarta's main corridor and Central Business District, from local property developer Asia Tower Sudirman. The purchase price, which amounted to 1.63 trillion rupiah, was paid in the form of promissory notes.<sup>7</sup> Another Singapore property

3 See <https://www.jpnn.com/news/waskita-karya-realty-kembangkan-bisnis-apartemen-di-depok>; <https://finance.detik.com/properti/d-4003448/anak-usaha-waskita-karya-beli-proyek-apartemen-rp-880-miliar>; [https://www.waskita.co.id/img/report\\_manager/files/447611c9f1974130c08173bb937a75ce.pdf](https://www.waskita.co.id/img/report_manager/files/447611c9f1974130c08173bb937a75ce.pdf).

4 See <https://industri.kontan.co.id/news/gandeng-pengembang-singapura-harita-group-garap-bisnis-properti-di-sentul-city>; <https://rumahhokie.com/beritaproperti/pengembang-singapura-akan-bangun-1-700-unit-hunian-di-sentul/>; [http://perennialrealestate.listedcompany.com/newsroom/20180531\\_171628\\_40S\\_ANFEF4R49029FN2H.1.pdf](http://perennialrealestate.listedcompany.com/newsroom/20180531_171628_40S_ANFEF4R49029FN2H.1.pdf).

5 See [http://www.sh-reit.com/storage/ir/shareholder-meeting/egsquare metres018/20180731-shreit-egsquare metres018-enc08-en.pdf](http://www.sh-reit.com/storage/ir/shareholder-meeting/egsquare%20metres018/20180731-shreit-egsquare%20metres018-enc08-en.pdf).

6 See <https://properti.kompas.com/read/2018/07/16/184618821/putragaya-wahana-raup-rp-816-miliar-dari-penjualan-apartemen-servis?page=all>; <https://properti.kompas.com/read/2013/07/18/1937131/Thamrin.Nine.Akan.Miliki.Gedung.Tertinggi.di.Indonesia>; <https://properti.kompas.com/read/2018/07/17/210821721/2020-indonesia-punya-pencakar-langit-70-lantai>.

7 See <https://theinsiderstories.com/unit-of-lippo-karawaci-buys-land-in-jakarta-for-us112m/>; [http://disclosure.bursamalaysia.com/FileAccess/apbursaweb/download?id=87084&name=EA\\_GA\\_ATTACHMENTS](http://disclosure.bursamalaysia.com/FileAccess/apbursaweb/download?id=87084&name=EA_GA_ATTACHMENTS).

developer, Keppel Land Limited, through its Indonesian subsidiary PT Sukses Manis Tangguh, acquired 7,700 square metres of land at Jalan Sudirman from PT Central Bank Indonesia Tbk. The land will be used to realise 400 luxury apartments. To total investment is estimated at 1.6 billion rupiah.<sup>8</sup> In November 2018, Indonesian listed company PT M Cash Integrasi Tbk acquired from PT Kencana Graha Optima 1,663.59 square metres of office space at Mangkuluhur City-Office Tower One in South Jakarta. The purchase price amounted to 108.13 billion rupiah.<sup>9</sup> In December 2018, PT Waskita Karya Realty, a subsidiary of PT Waskita Karya Tbk, acquired from PT Graha Ekatama 6.672 square meters of land in Serpong, South Tangerang. The total value of the transaction was 127.85 billion rupiah.<sup>10</sup>

There is also a significant number of new projects on Indonesia's real estate market. Most of these projects involve investment from foreign corporations through joint ventures with local companies. For example, Malaysia based developer Matrix Concepts Holdings Bhd, together with an Indonesian consortium comprising PT Bangun Kosambi Sukses (BKS), which is jointly owned by Agung Sedayu Group and Salim Group, and PT Nikko Sekuritas Indonesia (NSI), an investment bank, through their joint venture company, PT Fin Centerindo Satu, are developing an Islamic financial district in Pantai Indah Kapuk 2, not far from Soekarno Hatta Airport.<sup>11</sup> The aforementioned company PT Cipta Harmoni Lestari, through its subsidiary PT Serpong Bangun Cipta, is also developing a housing project Serpong Banara in South Tangerang.<sup>12</sup> In May 2019, real estate developer Sinar Mas Land announced its plans to develop Kazumi, a 2.8 hectares cluster of luxury housing that forms part of a 19 hectares estate called The Zora, in BSD City. The development is realised through Sinar Mas Land's company PT BSD Diamond Development in collaboration with a Japanese consortium led by Mitsubishi Corporation.<sup>13</sup> In May 2019, CFLD International (Indonesia), a subsidiary of the Chinese Industrial city developer CFLD, and the Singapore based Samanea Group, announced their plans to develop Tangerang New Industry City, a trading centre on a 7.6 hectares plot, in Tangerang District.<sup>14</sup>

## ii Private equity transactions

Private equity activity on Indonesia's real estate market is very limited. A noteworthy transaction dates from a few years ago, i.e. the creation of joint venture company PT Nirvana Wastu Pratama (NWP Retail) by subsidiaries of Warburg Pincus LLC and the Indonesian public real estate company PT City Retail Developments Tbk (formerly called: PT Nirvana Development Tbk) in 2015. PT City Retail Developments Tbk specialises in

8 See <https://www.cnnindonesia.com/ekonomi/20170919174310-92-242779/keppel-land-borong-lahan-bca-senilai-rp586-miliar>.

9 See [https://www.idx.co.id/StaticData/NewsAndAnnouncement/ANNOUNCEMENTSTOCK/From\\_EREP/201811/6316051a60\\_8370692bc3.pdf](https://www.idx.co.id/StaticData/NewsAndAnnouncement/ANNOUNCEMENTSTOCK/From_EREP/201811/6316051a60_8370692bc3.pdf).

10 See <https://industri.kontan.co.id/news/waskita-karya-realty-tambah-land-bank-seluas-6672-meter-persegi>.

11 See <https://www.theedgemarkets.com/article/matrix-concepts-indonesian-consortium-jointly-develop-jakarta-financial-district>.

12 See: <https://industri.kontan.co.id/news/gandeng-pengembang-singapura-harita-group-garap-bisnis-properti-di-sentul-city>.

13 See <http://www.sinarmasland.com/news-media/media-releases/sinar-mas-land-luncurkan-kazumi-cluster-ketiga-dari-the-zora-yang-menghadirkan-elemen-berkualitas-ti>.

14 See <https://properti.kompas.com/read/2019/05/08/082818721/cfld-international-dan-samanea-kerja-sama-kembangkan-tnic>; <https://industri.kontan.co.id/news/cfld-kerjasama-dengan-samanea-bangun-pusat-perbelanjaan-di-tangerang>.

the development of hypermarket anchored retail centres in emerging cities across the country. As part of the investment, the private equity firm committed US\$125 million, with the option to invest up to an additional US\$75 million.<sup>15</sup> In February 2019, NWP Retail raised another US\$200 million from Warburg Pincus LLC as well as the Korean Teachers' Credit Union and Citic Securities One-Belt-One-Road Fund. NWP Retail currently has 33 developments in Java, Kalimantan, Sumatera, Sulawesi, and Papua.<sup>16</sup>

### III REAL ESTATE COMPANIES AND FIRMS

#### i Publicly traded REITs and REOCs – structure and role in the market

As briefly touched upon above, there is currently no legal basis in Indonesia for the establishment of REITs. Instead investors who wish to invest in income-producing real estate in Indonesia can do so through DIREs. In contrast to REITs, DIREs are not legal entities, but are based on collective investment contracts (KIKs). DIREs are regulated by the OJK. In December 2017, the OJK issued a new regulation on DIREs.<sup>17</sup> Furthermore, in July 2016, it issued a regulation regarding DIREs based on shariah principles.<sup>18</sup>

A DIRE scheme involves a custodian bank and an investment manager who makes a collective investment in, inter alia, real estate and assets that are related to real estate (i.e., securities of real estate companies that are listed on the IDX or issued by real estate companies, or both). The 2017 OJK regulation introduced a new restriction that, of the DIRE portfolio's net assets, at least 80 per cent must be real estate assets, while assets that are related to real estate may only be a maximum of 20 per cent. It is not possible for a DIRE to invest in vacant land. However, the 2017 OJK regulation now permits a DIRE scheme to invest in real estate that is under development as long as it generates revenue within six months of its ownership being transferred to the DIRE. Several restrictions apply in such case, including that the investments cannot amount to more than 10 per cent of the DIRE net value, there must not be any significant dilution of the DIRE's revenue (i.e., 20 per cent of revenue or more) during the period of construction, and there must be no construction issues relating to the construction not being completed. It would also be possible for a DIRE to invest in a special purpose company (in the form of an Indonesian limited liability company), established solely to invest in real estate assets. If a special purpose company is used, the DIRE must own at least 99.9 per cent of the issued shares of the special purpose company.

Unresolved matters include how a DIRE can directly invest in real estate or own shares in a special purpose company, considering that a DIRE is not a legal entity, while under the Indonesian Agrarian Law, only Indonesian individuals and certain legal entities can have title to land in Indonesia, and under the Indonesian Company Law, shares in an Indonesian limited liability company can only be held by legal entities or individuals.

The maximum percentage for DIRE schemes to borrow funds is 45 per cent of the total value of the real estate to be purchased. Additionally, the 2017 OJK regulation now permits DIRE schemes to borrow funds by way of issuing debt securities. However, such issuance may only be undertaken for the purpose of purchasing real estate assets that have already

15 See <https://www.pehub.com/2015/02/warburg-pincus-to-invest-125-mln-in-nirvana/>.

16 See [https://www.warburgpincus.com/content/uploads/2019/02/2019-02-11-NWP-Press-Release\\_vF-English\\_vF.pdf](https://www.warburgpincus.com/content/uploads/2019/02/2019-02-11-NWP-Press-Release_vF-English_vF.pdf).

17 OJK Regulation No. 64/POJK.04/2017 on DIREs in the form of KIKs.

18 OJK Regulation No. 30/POJK.04/2016 on Sharia DIREs in the form of KIKs.

generated revenue, and may only be worth 45 per cent of the total value of the real estate to be purchased. Just three DIREs are currently active in Indonesia. The first of these is DIRE Ciptadana Properti Ritel Indonesia, which has been listed on the IDX since 2013. It owns a shopping centre in Solo, Java. The second, DIRE Bowsprit Commercial & Infrastructure, was launched by Indonesian public real estate company PT Lippo Karawaci Tbk in early 2017 and has been listed on the IDX since March 2017. This DIRE's funds have been used to acquire office towers and a distribution centre currently managed by PT Lippo Karawaci Tbk (Berita Satu Plaza in South Jakarta at around US\$29 million, Menara Matahari in Tangerang at around US\$39 million, Menara Asia in Tangerang at around US\$29 million and Balaraja Distribution Centre at around US\$34 million). An amount of around US\$52 million has been used to participate in PT Mitra Wijaya Wisesa, which manages Life Tower in Kuningan, South Jakarta. The remainder, of around US\$1 million, has been allocated as working capital.<sup>19</sup> The third, DIRE Simas Plaza Indonesia, was listed by Fund manager PT Sinarmas Asset Management in July 2019. It has a total portfolio of 10.4 trillion rupiah (US\$736.02 million). Contrary to other DIREs, DIRE Simas Plaza Indonesia does not use buildings, but shares in property companies as underlying assets. The underlying assets include a 95.37 per cent shareholding in the listed company PT Plaza Indonesia Realty, which owns and manages Plaza Indonesia shopping mall. The Plaza office tower and Grand Hyatt Hotel, all located in Central Jakarta, as well as a 100% shareholding in PT Sarana Mitra Investama, the parent company of the owner and manager of fX Sudireman shopping center, located in South Jakarta.<sup>20</sup>

Apart from DIREs, some offshore REITs are active on the Indonesian real estate market. Two noteworthy examples are Lippo Malls Indonesian Retail Trust (LMIR Trust) and First REIT, both REITs listed on the Singapore Exchange Securities Trading Limited (SGX), sponsored by PT Lippo Karawaci Tbk. LMIR Trust has a diversified portfolio of 23 shopping centres and seven retail spaces across Indonesia.<sup>21</sup> First REIT has a portfolio of 12 hospitals, two integrated hospitals and malls, one integrated hospital and hotel and one hotel and country club in various cities in Indonesia, in addition to several assets in Singapore and South Korea.<sup>22</sup> In December 2017, LMIR Trust and First REIT announced their joint acquisition of an integrated development of hospital and shopping centre assets in Yogyakarta, Java.<sup>23</sup> In February 2019, LMIR Trust acquired from PT Mandiri Cipta Gemilang, Lippo Mall Puri in West Jakarta for 3.70 trillion rupiah. It is said to be LMIR Trust's largest transaction to date, resulting in an increase of its assets by 19 per cent from 19.51 trillion rupiah to 23.21 trillion rupiah. The transaction was financed with a combination of debt and equity financing.<sup>24</sup>

We can conclude that DIREs are not very popular among investors. A likely reason for the limited popularity of DIREs is the lack of corporate and financial transparency that these

19 See <https://www.bowsprit-am.com/>; <https://www.thejakartapost.com/news/2017/02/14/lippo-group-launches-its-first-reit-in-indonesia.html>.

20 See [https://www.thejakartapost.com/news/2019/07/08/sinarmas-pools-rp-10-4-trillion-from-local-reits-issuance.html?utm\\_campaign=os&utm\\_source=mobile&utm\\_medium=ios..](https://www.thejakartapost.com/news/2019/07/08/sinarmas-pools-rp-10-4-trillion-from-local-reits-issuance.html?utm_campaign=os&utm_source=mobile&utm_medium=ios..)

21 See <https://www.lmir-trust.com/our-portfolio.html>.

22 See <https://www.first-reit.com/about-overview.html>.

23 See <https://www.lmir-trust.com/newsroom.html> and [www.firstreit.listedcompany.com/newsroom.html](http://www.firstreit.listedcompany.com/newsroom.html).

24 See <https://www.businesstimes.com.sg/companies-markets/lmirt-to-buy-retail-mall-in-west-jakarta-for-37-t-rupiah>.



funds and Indonesian companies generally often show. It is unlikely that recent measures aimed at making the use of DIREs more attractive will change the generally negative sentiment among foreign investors regarding these funds.

## **ii Real estate PE firms – footprint and structure**

As discussed above, private equity activity on Indonesia's real estate market is very limited. In the case of the aforementioned investment by Warburg Pincus LLC, a joint venture was created through an acquisition by Adventure Holdings BV, an affiliate of Warburg Pincus LLC, of 35 per cent of the shares in PT Nirvana Wastu Pratama, a subsidiary of PT Nirvana Development Tbk.<sup>25</sup>

## **IV TRANSACTIONS**

### **i Legal frameworks and deal structures**

As discussed above, investments in Indonesia's real estate sector are generally still rather conventional, consisting of plain vanilla sale and purchase of shares in local real estate companies, either directly or indirectly (i.e., through the IDX). A direct sale and purchase of shares in a local real estate company may be subject to foreign investment restrictions, for example, by imposing a cap on foreign ownership in Indonesian companies. Indonesia's 2007 Investment Law creates authority for the president to compile a list of business lines that are closed and conditionally open to foreign investment. A revised version of this 'Negative List' became effective in May 2016. A common business line for a real estate company in Indonesia would be '68110 – Real estate that is privately owned or rented'. This business line includes buying, selling, renting and operating of self-owned or leased real estate, such as apartment buildings, dwellings and non-residential buildings. As this business line is not included in the 2016 Negative List, a local real estate company with activities covered by this business line should in principle be 100 per cent open to foreign investment. If the real estate company is not only active in buying, selling, renting and operating of self-owned or leased real estate, but also other activities (e.g., the construction or operation of real estate), different business lines are relevant, which may be included in the Negative List and can therefore be closed or conditionally open to foreign investment.<sup>26</sup> In any event, from experience, although not explicitly listed as a business field that is closed or a business field that is conditionally open in the Negative List, certain business fields may in reality not be open to foreign investment. Furthermore, an Indonesian limited liability company (PT) should have at least two shareholders, so even if no foreign restrictions apply, it is common to have a local shareholder to hold part of the shares. There may also be commercial reasons to have local participation in the company.

Until recently, a foreign investor wishing to establish a real estate company or purchase shares in a local real estate company required a licence from the Indonesia Investment Coordinating Board (BKPM). However, as a result of a new regulation that was enacted by the government of Indonesia in 2018, investors who wish to start their business in Indonesia are

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25 See <https://www.reuters.com/article/indonesia-press-nirvana-dvlpmt-warburg-p-idUSL3N0WR0NL20150325>.

26 See also Section V on foreign investment restrictions to companies active in providing integrated services for the support of facilities as well as cleaning services for buildings.

no longer required to obtain a licence from the BKPM, but can instead register their business through the Online Single Submission (OSS) system and obtain a single identity number (NIB). This new approach also applies to any existing Indonesian company, whether a PMA company with foreign shareholders or a local company with only Indonesian shareholders, including a local company which intends to convert its status to become a PMA company as a result from a transfer of shares from an Indonesian shareholder to a foreign shareholder. This NIB will serve as an Investment Registration Number, Importer Identification Number, Number of Company Registration Certificate, Social Security for Manpower and Social Security for Health Number, and Custom Identity Number. Once the company has obtained an NIB, the company may apply for a business licence or commercial or operation licence through the OSS system, provided the company meets certain requirements as set out in the new regulation.

Until recently, the BKPM regulations made a distinction between foreign investment companies engaged in the development and management of different types of property. However, following the issuance of a new BKPM regulation on 22 July 2019, this distinction no longer exists. Basically, a foreign investor who wants to set up a foreign investment company that is engaged in the development and management of property should invest more than 10 billion rupiah, excluding land and buildings, and the foreign investment company's issued and paid-up capital should be at least 2.5 billion rupiah with a minimum share participation of 10 million rupiah.

Before the shares in the local real estate company with only Indonesian shareholders are transferred, it will generally be required to amend the articles of association of the company; for instance, to increase the issued and paid-up capital to at least 2.5 billion rupiah. This amendment shall be made in notary deed form and be approved by the Minister of Law and Human Rights. These documents should be uploaded to the OSS system to obtain an NIB. Since the BKPM regulations have not been revoked, each PMA Company still needs to meet the requirements as set out in these BKPM regulations, including but not limited to submitting quarterly activity reports, which are used by the BKPM to monitor the implementation of the investment plan. As soon as the investment plan has been realised and the company is ready for operation, a business licence can be obtained through the OSS system.

Foreign investment restrictions also do not apply to a venture capital company (PMV); any equity participation by a PMV would be deemed to be domestic investment rather than foreign investment – even if one or more shareholders of the PMV are foreign. A PMV can be established in the form of a limited liability company, cooperative or limited partnership (CV). The minimum capital requirement to establish a PMV in the form of a limited liability company is 50 million rupiah. A PMV in the form of a PT can be 85 per cent owned by a foreign entity or institution. However, the maximum direct capital participation in a PMV by a foreign entity as a shareholder is limited to the maximum amount of the entity's net equity. Business activities in which a PMV may be engaged are equity participation, quasi-equity participation or financing through purchase of securities issued by business partners. Business partners can be individuals or companies, including micro, small, medium businesses and corporations receiving equity participation based on a profit-sharing principle from the PMV and financing of productive business. A PMV may participate in a real estate company provided that the value of participation in one business partner (in this case, the real estate company) is a maximum of 25 per cent of the venture capital company's equity. Furthermore, this participation may only last for 10 years. After the lapse of this period, the

PMV must divest its shares in the real estate company as the purpose of a PMV is to help start-up companies. Parties wishing to establish a PMV must obtain a business licence from the OJK.

It would also be possible for a foreign investor to carry out an asset deal. However, asset deals are not very common in Indonesia, as the transfer of assets in general and land, buildings and fixtures in particular can be a rather complicated, time-consuming and costly process. If a foreign investor decides on an asset deal, it will be necessary to establish a PT first. This company should obtain its own licences to be active in the real estate sector, as licences can generally not be transferred under Indonesian law.

Irrespective of whether it has the status of a normal limited liability company or a foreign investment company, a PT cannot hold an ownership right on land; this right is strictly reserved for individuals with Indonesian nationality. However, a PT can hold three other types of land rights: right of cultivation, right to build and right of use. In practice, the right to build is the type of land right most commonly used by real estate companies. It is granted for a maximum initial period of 30 years and is extendable for another period of 20 years, with a possibility of renewal. On top of an ownership right, right to build and right of use, a right of ownership to a multi-storey unit can be established. This right can be issued to owners of residential, commercial or retail units in multi-storey buildings such as condominiums, strata-title office buildings or trade centres. The validity period depends on the expiry date of the land right on which the right of ownership to a multi-storey unit has been established. The ownership right, right to build, right of use, and of ownership to a multistorey unit can be sold, exchanged, transferred, bequeathed or mortgaged.

## **ii Acquisition agreements terms**

Given the illiquid character of the Indonesian real estate market, it is hard to provide a description of the typical terms of real estate M&A and PE transactions. However, it is common for parties to enter into a share purchase agreement for the acquisition of existing shares or a share subscription agreement for the subscription for new shares in a local real estate company.

Although in-kind contribution is also possible under the law, shares are normally acquired or subscribed for by payment of a cash consideration. The purchase price is often paid directly to the sellers or issuers of the shares (i.e., without the use of an escrow account). Price-adjustment mechanisms are sometimes used, normally in the form of closing accounts, rather than locked-box mechanisms.

Given that foreign investment is strictly regulated in Indonesia, parties in M&A and private equity transactions will normally need to agree on conditions precedent relating to regulatory approvals, in addition to corporate and third-party approvals that need to be obtained. As a result, it may take a relatively long time for a transaction to be closed. For this reason and also given the uncertainties in the market, material adverse change clauses are also commonly used and accepted by parties. Equally, it is common for parties to agree on a broad list of pre-closing covenants. The use of a long stop date for the fulfilment of the conditions precedent is also generally accepted. Break fees are sometimes used, but not very common.

Just like other companies, real estate companies in Indonesia often have compliance issues. For this reason, it is common and in any event advisable to conduct extensive legal, financial and tax due diligence on a target company. Warranties and specific indemnities are commonly agreed on to mitigate at least part of the potential liabilities. To the extent

these liabilities cannot be sufficiently mitigated, it may be advisable to do an asset deal, despite the fact that – as discussed above – the transfer of assets can be a rather complicated, time-consuming and costly process.

When foreign investors choose to create a joint venture with local partners for their real estate investment, parties often enter into an additional joint venture agreement or shareholder agreement. These agreements commonly create rights for certain shareholders to, *inter alia*:

- a* nominate members of the board of directors and board of commissioners of the company;
- b* list reserved matters at the level of the board of directors, board of commissioners or the general meeting of shareholders;
- c* set out a deadlock mechanism for when shareholders or their nominated directors or commissioners cannot agree on the reserved matters; and
- d* contain terms in business plans and reporting, financing of the company, the distribution of dividend, create restrictions on the transfer of shares.

Some of the provisions of the joint venture agreement or shareholders' agreement may also be covered by the articles of association of the company.

### **iii Hostile transactions**

There do not appear to have been any recent hostile transactions in Indonesia's real estate sector.

### **iv Financing considerations**

M&A and private equity transactions in Indonesia's real estate sector are typically financed by a combination of equity and debt. As discussed above, when a foreign investor wishes to purchase shares in a local real estate company, the company will need to have the status of a foreign investment company. This also implies that more than 10 billion rupiah should be invested; at least 2.5 billion rupiah of this amount should come in the form of equity.

Certain reporting requirements apply to a recipient of a foreign loan in Indonesia. Furthermore, when certain monetary thresholds are met, the conversion of Indonesian rupiah to foreign currencies or the purchase of foreign currency against Indonesian rupiah conducted by a bank and its customers must be based on an underlying transaction.

Under Indonesian law, lending obligations can be secured by various types of security. Rights to land as well as buildings and fixtures can be mortgaged. Shares in a PT can be pledged. Security on movable assets can be established in the form of a 'fiduciary transfer'. Other than in the case of a pledge, the creditor-transferee holding a security in the form of fiduciary transfer will normally not have physical control of the assets.

To be able to create security such as the above, generally, consent from existing creditors is needed. In addition to creditor consent, shareholder approval is also required. The Indonesian Company Law and the articles of association of an Indonesian company normally stipulate certain requirements to obtain corporate approval from the organs of the company (i.e., the board of commissioners or the general meeting of shareholders). Lack of corporate approval would legally affect the validity of the loan and pledge agreements and cause the board of directors to be held liable for any loss in relation thereto.

## v Tax considerations

### *Share deals*

The proceeds from a sale of shares in an Indonesian company may be subject to capital gains tax, which, where the shares are not listed, is 25 per cent when the seller is a company and 30 per cent when the seller is an individual. The sale of shares listed on the IDX is subject to a tax of 0.1 per cent of the transaction value.

Object	Seller	Purchaser	Tax (applicable to seller) as gain on sale
Shares in listed company	Indonesian / foreign company / individual	Indonesian / foreign company / individual	0.1 per cent of the transaction value
Shares in Indonesian limited liability company	Indonesian company	Indonesian / foreign company / individual	25 per cent corporate income tax
	Indonesian individual	Indonesian / foreign company / individual	Up to 30 per cent (progressive rate for individual income tax)
	Foreign company / individual	Indonesian / foreign company / individual	20 per cent x 25 per cent = 5 per cent final tax To be withheld by the company which shares are being sold

Dividends received by a resident company from another Indonesian company are exempt from tax, provided the dividends come from retained earnings and the recipient company holds at least 25 per cent of the capital of the company distributing the dividend. If the recipient company holds less than 25 per cent of the shares, the received dividend is subject to 15 per cent withholding tax, which represents an advance payment of the company's tax liability. Dividends distributed to a non-resident are subject to 20 per cent withholding tax, unless the rate is reduced under a tax treaty. Dividend distributions to individual shareholders are subject to 10 per cent withholding tax.

Object	Recipient	Ownership	Tax
Dividend	Local company	less than 25 per cent	15 per cent withholding
		25 per cent or more	Exempt
	Local individual	Any per cent	Final tax 10 per cent (via withholding)
	Foreign company / individual	Refer to the applicable tax treaty	20 per cent without tax treaty May be reduced with applicable tax treaty rate

### *Asset deals (land and buildings)*

In the case of an asset deal, the sale of assets is subject to 10 per cent VAT. The transfer of land will trigger the obligation for the seller to pay income tax, which is 2.5 per cent of the purchase price of the land (unless the seller is foreign and the rate is reduced under a tax treaty), and the purchaser to pay an administrative fee for the transfer of land rights, which is approximately 5 per cent of the purchase price of the land.

Related tax	Rate	Notes
Value added tax	10 per cent	
Seller's Tax	2.5 per cent of transaction value	Final income tax for seller

Related tax	Rate	Notes
Buyer's duty	5 per cent	So called <i>Bea Perolehan Hak atas Tanah dan Bangunan</i> (BPHTB). Buyer must pay this fee to transfer the title in the land certificate
Income tax	None	Sale of land and/or building is subject to final tax only

Aside from the above-mentioned tax in relation to the transfer, there are other taxes applicable to owning land and buildings. Land and building tax (*Pajak Bumi dan Bangunan - PBB*) is payable each year on land, buildings and fixtures. This is a regional tax and the rate is determined by the regional governments and therefore the exact rate will depend on where the assets are located.

#### vi Cross-border complications and solutions

As discussed above, a direct sale and purchase of shares in a local real estate company may be subject to foreign investment restrictions. To circumvent foreign investment restrictions, foreign investors sometimes resort to an investment structure involving nominee arrangements, on the basis of which an Indonesian individual or entity holds the shares on behalf of the foreign shareholder. However, in Article 33 of the 2007 Investment Law, an express prohibition was introduced to the effect that: 'Domestic investors and foreign investors who make investments in the form of a limited liability company are prohibited from entering into an agreement or making a statement asserting that share ownership in a limited liability company is for and in the name of another person.' Such agreements are invalid and unenforceable. Article 33 of the Investment Law also provides for these agreements to be null and void.

In practice, there is still much uncertainty as regards the correct interpretation of the nominee prohibition. However, any element of the contractual arrangements that goes beyond a true financing arrangement runs the risk of running foul of the law. This means that in very broad terms these arrangements should best avoid powers of attorney to exercise ownership rights and of assignment of dividends and voting rights. However, a true financing arrangement (which could be strengthened and secured by a right of pledge) should be allowed under the law. Under Indonesian company law, the voting rights on shares must remain with the pledgor.

## V CORPORATE REAL ESTATE

There does not appear to be any trend in the Indonesian real estate market in separating corporate real estate from operating companies.

It is common in Indonesia to separate the ownership of real estate from building management. Building management activities could, for example, be covered by the following business lines: '81100 – Integrated services for the support of facilities, such as general interior cleaning, maintenance, waste disposal, guard and security, mail routing, reception, laundry and related services'; '81290 – Cleaning services for buildings'; and '81300 – Services for garden maintenance'.

Note that activities under business lines 81100 and 81300 may be, and 81290 are, closed to foreign investment.

## **VI OUTLOOK**

The prospects for Indonesia's real estate market are rather positive. Momentum is picking up. The effects of recent and ongoing pro-foreign investment measures by the Jokowi administration are already evident and are to likely have greater impact in the longer term. Having said that, it is likely that Indonesia's legal framework will have to improve further before the country's market for investment-grade real estate assets can achieve full potential.

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