

Private acquisitions in Indonesia: market analysis overview

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MARKET OVERVIEW

1. What are the current major trends in the private M&A market?

The private M&A market in Indonesia is dominated by transactions conducted by existing business players who want to expand their business activities. There are many private equity deals but most of them are of quite small value. Most are primary buy-outs, limited to small and medium-size businesses. The main buyers in M&A transactions are Chinese, Japanese, Korean or South East Asian companies and venture capitalists. Most deals involve financial investors rather than strategic investors.

In May 2016, the Indonesian Government enacted a new Investment Negative List under Presidential Regulation No. 44 of 2016 (Negative List) that is, a list of business sectors in Indonesia that foreign investors are not allowed to invest in). The new Negative List has opened up certain of business sectors that were previously closed for foreign investors, for example e-commerce, rubber production, healthcare, financial services, logistics, oil and gas and power plants. These sectors can now attract foreign investors to invest and build their businesses in Indonesia. Most recent M&A transactions in Indonesia are due to the impact of the new Negative List.

In addition, as of 1 July 2016, the government enacted Law No. 11 of 2016 on Tax Amnesty, in which the government will allow the taxpayer to write off their outstanding and payable tax obligations, after the taxpayer has first disclosed their assets and pay certain ransom fees, which are determined based on certain percentage of the total assets and are payable to the government. The enactment of the Law on Tax Amnesty also affects M&A transactions in Indonesia.

2. What has been the level of private M&A activity in the previous year?

The value of M&A transactions in 2015/16 exceeded US\$500 million. The most notable transactions included:

- Investments made by KKR & Co, Warburg Pincus, Farallon Capital Management and Capital Group Private Markets in Go-Jek of Indonesia.
- Alibaba's acquisition of Lazada Group in South East Asia.
- PT Elang Mahkota Teknologi Tbk (Emtek, IDX EMTK) licensing transaction with BlackBerry Limited (NASDAQ: BBRY; TSX: BB) which led to the development of BlackBerry messenger in Indonesia for six years.

DEAL STRUCTURES

3. What are the current trends in the structuring of private M&A transactions?

The structure of a private M&A transaction depends on the intention of the seller, that is, whether the seller plans to exit the target company or develop the target company further. Usually, M&A transactions are a combination of the above purposes.

In practice, the seller will receive cash from the sale through a:

- Sale of the existing shares.
- Transfer of assets listed in the name of the seller to the target company.

The remaining consideration will be subscribed by the buyer by issuing new shares in the target company.

Acquisitions through distressed asset and bad debts are also common.

Private equity investors tend to invest heavily in private M&A transactions, by building a portfolio of multiple similar operating companies which can create scale and synergy.

The total price of the transaction is agreed in a memorandum of understanding or term sheet signed by the seller and buyer. However, a price adjustment mechanism is set under the memorandum of understanding or term sheet, which will apply on completion of the due diligence relating to the target company.

Generally, the calculation of the price uses the target's earnings before interest, taxes, depreciation, and amortisation (EBITDA) as the reference. A sales multiply method that is, a forecast of the target's future sales is also quite commonly used.

The size of the deposit reserves is the main criterion relevant to price calculations in mining/oil and gas transactions.

4. What are the current trends in the terms and documentation of private M&A transactions?

Direct participation through a conditional share sale purchase agreement or conditional share subscription agreements is common in Indonesia. Most documents in M&A transactions include the following provisions:

- Conditions precedent and conditions subsequent.
- Representation, warranties, covenants and undertakings from the seller.
- Indemnification and indemnity procedure.
- Price adjustment mechanism.

In practice, indemnification is limited to the total consideration paid by the buyer to the seller. In some cases, subject to the deal, limitation of liability also applies.

Recently, convertible notes (or loans and warrants) have been commonly used, in M&A transactions relating to small, medium size businesses and businesses that are restricted under the Negative List.

5. What are the current trends in how private M&A transactions are conducted?

Most M&A transactions in Indonesia are negotiated sales. An auction sale is only used if the shares of the target company are pledged as security and sold by the lender when it enforces its security, due to the target being unable to pay its debt. A buy-out of distressed assets is an alternative if the target cannot pay its debt.

CROSS-BORDER LITIGATION AND ARBITRATION

6. Is it common market practice for a share purchase agreement to provide for a foreign governing law and/or jurisdiction? If so, in what circumstances does this occur and which governing law and/or jurisdiction are common choices?

It is common for a share purchase agreement to provide for a foreign governing law and jurisdiction. English law is usually the governing law and the courts of Singapore or Hong Kong usually have jurisdiction.

7. Is it market practice for an arbitration provision to be included in private M&A documents? Are arbitration clauses enforceable in your jurisdiction? Do local courts respect the choice of jurisdiction in an arbitration clause?

Generally, an arbitration provision is included in private M&A documents. A foreign or international arbitral award can be recognised and enforced under the UN Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (New York Convention), which was ratified by Indonesia by Presidential Decision No. 34 of 1981. The procedures for recognition and enforcement of foreign arbitral awards are further regulated by Law No. 30 of 1999 on Arbitration and Alternative Dispute Resolution.

RECENT DEVELOPMENTS AND PROPOSALS FOR REFORM

8. Have there been any significant recent or proposed legal developments affecting the market that could impact on transactions?

The government has issued 13 economic packages to attract foreign investors to invest in Indonesia. Further, the authors understand from press releases that to attract more foreign investors and boost M&A transactions in Indonesia, the government is planning to:

- Decrease corporate tax rates.
- Provide more facilities for investors.
- Revise the Negative List further.

9. What will be the main factors affecting the market next year, and how do you expect the market to develop?

The government programme to build some 35,000 megawatt power plants will create and increase M&A transactions in the energy industry, which will significantly boost infrastructure and the real estate industry.

In addition, the authors think that the Tax Amnesty Law will play an important role next year, as it offers lower redemption rates for Indonesian taxpayers who repatriate their offshore assets to Indonesia.

Practical Law Contributor profiles

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Publications

- *Getting the Deal Trough: Acquisition Finance.*
- *LexisNexis Merger and Acquisition Law Guide.*
- *The International Comparative Legal Guide to: Mining Law.*
- *The International Comparative Legal Guide to: Securitization.*
- *The International Comparative Legal Guide to: Project Finance.*
- *The International Comparative Legal Guide to: Corporate Tax*
- *Getting the Deal Trough – Tax on Inbound Investment*
- *Jurisdiction Correspondences International Tax Review*
- *Editorial Board Derivative and Financial Instrument Bulletin IBFD.*
- *The Littler Mendelson Guide to International Employment and Labour Law.*
- *Transfer Pricing and Tax Avoidance, Thomson Reuters.*
- *Tax Litigation Global Guide, Thomson Reuters.*

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