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Legal Guide to Investment in Indonesia

July 2014

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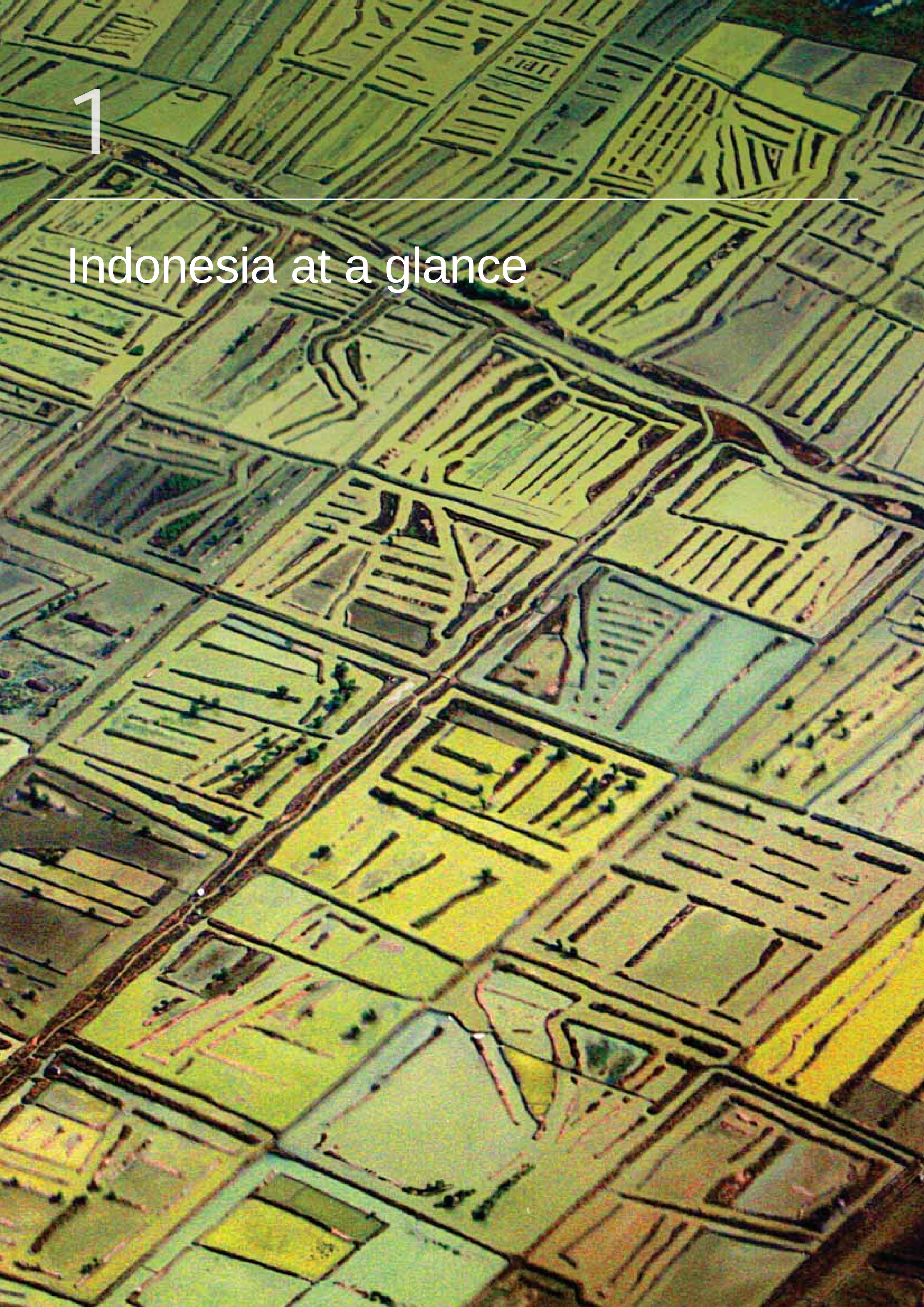
Indonesia at a glance



1.1 Investment environment

Indonesia, with its abundance of natural resources, access to global mobility through its strategic location along major sea lanes offers investors significant opportunities. Other influential factors include:

> it is the fourth most populous country in the world, with a population in 2013 of 251.1 million, according to the United States Census Bureau, and a projected population of 255.5 million in 2015, according to the BPS, Indonesia's official statistical organisation; and

> in 2013, its GDP was at $867.5 billion with an annual growth rate of 5.78%, compared to a GDP in 2012 of US$878 billion and an annual growth rate of 6.2%.

1.2 Economy

Since Indonesia gained independence nearly seven decades ago, its economy has moved from a traditionally agricultural-based one, to a more mixed economic base, with increased economic activity in the manufacturing and service industries. Currently, Indonesia ranks as the world's 17th largest economy.

Indonesia is a major producer of a broad range of commodities. It is the largest producer and exporter of palm oil in the world, and is the second largest producer of cocoa, tin and natural rubber. It provides 12 per cent of the world's nickel reserves and ranks seventh in the world's reserves of bauxite. It is also a large producer of steel, copper and fisheries.

Indonesia aims to be among the top 10 global economies by 2025. According to Indonesia's Master Plan Acceleration and Expansion of Indonesia Economic Development 2011-2025 (the ***MP3EI)***, Indonesia's economic transformation into a developed country will involve developing the regional economic potential in six economic corridors (Sumatra, Java, Kalimantan, Sulawesi, Bali – Nusa Tenggara and Papua – Maluku Islands), strengthening national connectivity locally and globally, and strengthening human resources capability, science and technology. Indonesia is focusing on developing eight key programs to reach its target by 2025. They are: agriculture, mining, energy, industrial, marine, tourism, telecommunication and the development of strategic areas. Following the issue of the MP3EI, the Indonesian Government has implemented, and continues to amend, key legislation, with a view to attracting more investment in these areas.

Japan was recognised as Indonesia's biggest investor in 2013, investing a total of US$4.7 billion, followed by Singapore (US$4.6 billion) and the US (US$2.4 billion). As one of the fastest growing economies in the world, Indonesia offers many business opportunities to foreign investors.

1.3 Geography

Indonesia is located in South-eastern Asia between the Indian Ocean and the Pacific Ocean, and occupies a total area of 1,904,569 square kilometres, making it the 15th largest country in the world. It is also the world's largest archipelago, with an east to west distance of 5,200 kilometres and a width of 1,870 kilometres. It has land borders with Timor-Leste (228 kilometres), Malaysia (1,782 kilometres) and Papua New Guinea (820 kilometres).

Indonesia has an abundance of natural resources, such as petroleum, tin, natural gas, nickel, timber, bauxite, copper, fertile soils, coal, gold and silver.

1.4 Indonesia's challenges

Although Indonesia's economic potential is strong, it continues to face a number of challenges. Corruption is a significant impediment to Indonesia's development. In 2013, Transparency International scored Indonesia 32 out of 100 on a scale from 0 (highly corrupt) to 100 (very clean), although this score has steadily improved in recent years. In addition, the overall ease of doing business in Indonesia in 2014 decreased by four points, from a ranking of 116 out of 189 economies to 120, according to the ranking given by the World Bank Group.

Bureaucracy is considered by many international investors to be a barrier to investing in Indonesia. Disharmony between regulations made by regulators at the central government and at the regional level is considered to be a key source of Indonesia's bureaucracy-related issues. The Government's regional autonomy policy has led to a proliferation of regional regulations that are not always consistent with the central legislation. In addition, officials in the relevant industry sector are given significant discretionary powers, which often leads to further regulatory uncertainty. Compounding this is general concern over the efficiency of contract enforcement. Clearer regulations, relaxation of restrictions affecting foreign investors and streamlining permit applications would certainly encourage increased participation from international investors. Given the archipelago nature of Indonesia, insufficient infrastructure is also seen as barrier to investing, particularly in the middle and eastern part of Indonesia. On the other hand, the insufficiencies of the infrastructure sector present great opportunities for foreign investors. A PPP model is increasingly popular among foreign investors, although the Indonesian Government has tended to promote a model that excludes support through the issue of government guarantees (see section 6 for more information).

Other key challenges that are characteristic of the Indonesian legal system include that:

- it is not uncommon to find conflicting laws from different authorities and it is often unclear which regulations are applicable. There is also often a time lag in passing implementing regulations;
- there is no reliable central source of obtaining comprehensive sets of relevant laws and regulations. It is not unusual, therefore, for Indonesian legal opinions to be caveated to reflect this;
- court proceedings are generally lengthy and cumbersome and are likely to take many months, or even years, to complete (see section 12 on dispute resolution for more information); and
- judges are given a high level of discretion in deciding matters. Combined with a lack of sophistication, particularly in some regional courts, this can lead to inconsistency in judicial interpretation.

1.5 Political system

Indonesia is the third largest democracy in the world after India and the United States. Since the late 1990s, Indonesia has experienced an extended period of political stability, consolidated democratisation and economic growth.

Executive and legislative branches

Indonesia is a unitary state. The executive branch is headed by a President and Vice President, who are directly elected for a five-year term by popular vote. The President and Vice President govern with the assistance of an appointed Cabinet. The People's Consultative Assembly, or the *Majelis Permusyawaratan* Rakyat (***MPR***), a 692-member parliament, has the authority to amend and stipulate the Constitution, and inaugurate the elected President and Vice President. The MPR comprises two lower houses:

- a 560-member House of Representatives (***DPR***), elected by proportional representation, with the authority to make legislation, determine the national budget and oversee the implementation of legislation by the Cabinet; and
- a 132-member advisory body called the House of Regional Representatives (***DPD***), with four representatives from each of Indonesia's 33 provinces.

Administrative divisions

Indonesia consists of 33 provinces, five of which have special status. Each province has its own political legislature and governor. The provinces are subdivided into regencies (*kabupaten*) and municipal cities (*kota*), which are further subdivided into subdistricts (*kecamatan*), and again, into a village level (either *desa* or *kelurahan*). The provinces of Aceh, Jakarta, Yogyakarta, Papua and West Papua have special status, which gives them greater legislative privileges and a higher degree of autonomy from the central government. For example, the Achenese Government has the right to establish an independent legal system; in 2003, it instituted a form of Sharia (Islamic law).

Judicial branch

The Indonesian judicial system comprises several types of courts under the oversight of the Supreme Court (*Mahkamah Agung*). The Indonesian President appoints judges to the bench of the Supreme Court. At first instance, civil disputes are heard at a State Court. The next tier of appeal is the High Court and then, ultimately, the Supreme Court. The Commercial Court deals primarily with bankruptcy and insolvency matters, although its jurisdiction can also extend to broader commercial matters. Appeals from the Commercial Court proceed directly to the Supreme Court. There is also a State Administrative Court (*Pengadilan Tata Usaha Negara*), which hears administrative law cases filed against the Government of Indonesia. Religious Courts hear disputes between Muslim citizens relating to marriage, inheritance and property donated for religious purposes.

Political parties

Key Indonesian political parties include:

- Golkar (leading party of the Suharto era);
- Indonesian Democratic Party of Struggle (***PDI-P***);
- Greater Indonesia Movement Party (***Gerindra***);
- National Awakening Party (***PKB***);
- United Development Party (***PPP***);
- National Mandate Party (***PAN***);
- Prosperous Justice Party (***PKS***); and
- Democrat Party (***PD***, a leading party of Yudhoyono era).

1.6 Structure of the laws

Indonesian's commercial legal system is influenced by civil law traditions and customary (*adat*) law. Dutch presence in, and colonial occupation of, Indonesia for 350 years has left a legacy of Dutch colonial law, which is reflected in the Indonesian Civil Code, Indonesian Commercial Code and Indonesian Criminal Code. Following independence in 1945, the nation started to establish its own modern Indonesian law, modifying existing Dutch legal principles and drawing from the customary law that existed before Dutch colonisation. In common with other civil law jurisdictions, judges in Indonesia are not bound by precedent, trusts are generally not recognised and contracts are subject to the principle of good faith.

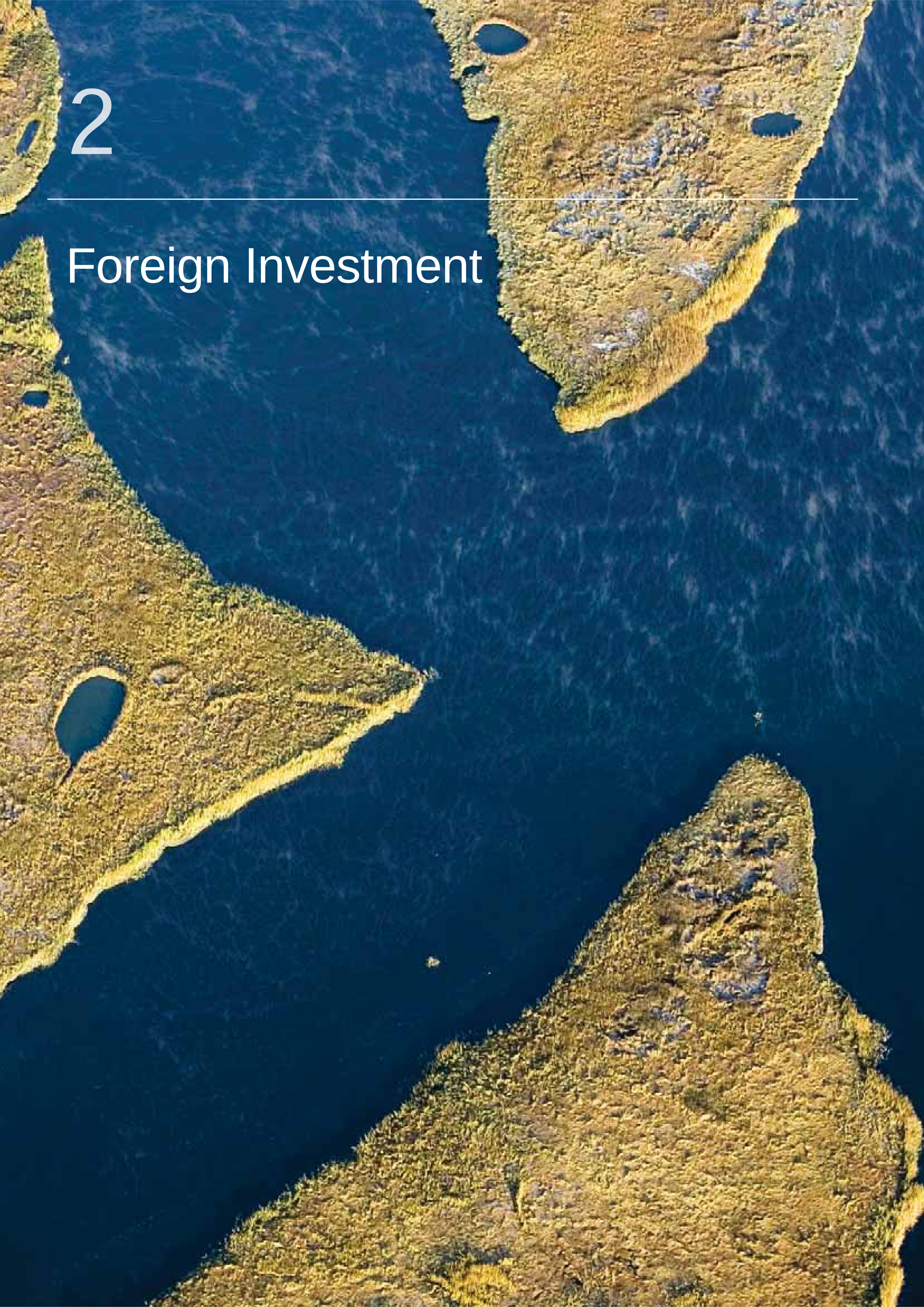
The hierarchy of rules and regulations in Indonesia is outlined under Article 7 of Law No. 10 of 2004 on the Formulation of Law and Regulations:

1. 1945 Constitution (*Undang-Undang Dasar 1945* or ***UUD'45***);
2. Law (*Undang-Undang* or ***UU***) and Government Regulation in Lieu of Law (*Peraturan Pemerintah Pengganti Undang-Undang* or ***Perpu***);
3. Government Regulation (*Peraturan Pemerintah* or ***PP)***;
4. Presidential Regulation (*Peraturan Presiden* or ***Perpres***); and
5. Regional Regulation (*Peraturan Daerah* or ***Perda***).

In addition to the legal instruments above, there are Presidential Instructions or Decrees, Ministerial Decrees and Circulation Letters, which add further detail to Laws and Government Regulations. Importantly, as Indonesia does not adopt a precedent-based legal system, judges applying these laws and regulations are not obliged to apply previous rulings/decrees on similar matters.

1.7 International treaties

Indonesia is also party to a large number of international treaties. Under Indonesian law, international treaties take precedence over domestic legislation. To the extent of any inconsistency, international treaties apply.



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Foreign Investment

2.1 Overview

There are two key common forms of foreign investment in Indonesia:

> direct investment – where the investor invests capital in a new or existing company, in order to establish a business or business presence in Indonesia and participate in the management of the investee company; and

> although this is not defined in the Investment Law, this is generally understood to be portfolio investment – where the investor invests through the purchase of securities in the capital markets, such as equity, debt or a combination of both, and is less interested in participating directly in the management or control of the investee company.

The Investment Law (as defined below) only regulates direct foreign investment.

2.2 Direct foreign investment

(a) Form of investment

In Indonesia, direct foreign investment is regulated by Law No. 25 of 2007 regarding investment and its implementing regulations (the ***Investment Law***). Under the Investment Law, any form of direct foreign investment in Indonesia must be in the form of a limited liability company. The investment must be by way of the foreign investor holding shares in the company. A company established with foreign investment capital is known as a '**PMA Company**'; while an investment company established with no foreign investors is known as a '**PMDN Company**'. In general, all Indonesian incorporated companies are subject to the Indonesian Company Law (Law No 40 of 2007 regarding Limited Liability Companies); while PMA and PMDN Companies are also governed by the Investment Law. Note that a PMA Company itself is also regarded as a foreign investor from the Investment Law perspective.

Importantly, the Investment Law protects investors by stating that the Indonesian Government is not allowed to take away the ownership rights of any investor, including foreign investors, without paying such an investor a market-based compensation.

(b) Authorities responsible for managing foreign investment

Regencies and cities generally organise investment in their respective regions through a regional investment service agency called the Regional Investment Coordinating Board. However, where the investment is associated with foreign investment, the investment must be approved by the Indonesian Government, through the Investment Coordinating Board (*Badan Koordinasi Penanaman Modal* – ***BKPM***). Generally, BKPM is responsible for approving all foreign investment, except investment in: (a) the banking and financial services sector (where approval is granted by Indonesia's Financial Service Authority); (b) the upstream oil and gas sector (which is regulated through production sharing contracts with the oil and gas contracting agency *Satuan Kerja Khusus Kegiatan Usaha Hulu Minyak dan Gas Bumi* (***SKK Migas***)); and (c) a portfolio investment through the purchase of securities in the capital markets.

Foreign investors must submit to BKPM periodic investor activity reports summarising investment progress and any obstacles to their investment activities.

(c) Principal Licence and establishing a PMA Company

The Principal Licence of investment is required as an initial government approval that must be obtained before conducting investment in Indonesia and establishing a PMA Company. After BKPM has granted approval for the proposed investment, the process of incorporating a PMA Company may commence. This process broadly involves:

> execution by the founders of the company of the Deed of Establishment containing the articles of association of the company before a notary public in Indonesia; and

> submission of the Deed of Establishment of the company to the Ministry of Laws and Human Rights, for approval of the articles of association of the company. One of the prerequisites to obtaining approval is proof of payment of 100 per cent of the issued capital.

(d) Investment licences – fiscal and non-fiscal

Applying for the relevant licences and fiscal allowances may commence once the PMA Company is established.

The licences and fiscal allowances usually required include the following:

> Producer Importer Identification Number (API-P): Required if the PMA Company wishes to import goods that will be used by the company as capital goods and raw materials.

> Facility for Import Duty Exemption on Machinery: Required if the PMA Company wishes to obtain the benefit of the import duty exemption on machinery, goods and materials imported in particular service industries (eg tourism, public transport, public health, mining, construction, telecommunications and seaports). The exemption is usually granted for two years.

> Facility for Corporate Income Tax (PPh Badan): This may be in the form of a Tax Allowance or a Tax Holiday.

- The Tax Allowance is granted in accordance with Government Regulation No. 1 of 2007 on the Income Tax Facility for Investment in Several Business Sectors and/or in Several Regions as last amended by Government Regulation 52 of 2011 (***GR 1/2007***). There are four kinds of facilities that may be granted for Corporate Income Tax: (i) the reduction of net income in the total amount of 30 per cent, prorated at 5 per cent for six years; (ii) acceleration of depreciation and amortization deductions; (iii) a reduction of the withholding tax rate on dividends paid to non-residents to 10 per cent or the applicable reduced double taxation avoidance treaty rate; and (iv) the right to carry forward tax losses for up to 10 years.
- The Tax Holiday facility, granted by the Government in accordance with Minister of Finance Regulation No. 130/PMK.01/2011 (***PMK 130***), is corporate income tax cuts for five industrial sectors where the value of the investment is at least IDR 1 trillion (approximately AUD$93 million), 10 per cent of the investment value is placed into banks in Indonesia, and the entity has been duly established at least 12 months before the enactment of PMK 130. An application for a Tax Holiday may only be made until 15 August 2014.

> Regional Licences: A general licence to conduct business (SIUP), issued by the regional government where the project or business is located, and required to acquire land for the business, manpower-related licences and licences for any other matter that falls under the authority of the regional governments (eg nuisance permit).

> Operation Permit: Issued by the Ministry relevant to the field of business and required for the technical aspects of the business field.

> Business Licence: Issued by BKPM and required to be obtained in order to commence production and operational activities to produce goods or services.

(e) Investing in existing PMDN or PMA Companies

A PMDN Company must obtain prior approval from BKPM to transfer all or some of its shares in the company to a foreign individual or entity. Such shares may only be acquired if the business field is open to investment (see the discussion on limitations on foreign investment in section 2.4). BKPM's prior approval is also required for changes to the shareholding composition of an existing PMA Company.

(f) Representative office

As an alternative to establishing a PMA Company or investing in an existing PMDN or PMA Company, foreign investors are permitted to open a representative office in Indonesia. There are three main types of representative office: a representative office under the control of the Department of Trade, a representative office under the control of the Department of Public Works, and a regional representative office.

A representative office licensed by the Department of Trade is the most common form of representative office. However, the range of activities that may be conducted by such a representative office is quite narrow. In particular, it may not undertake trading activities, own production facilities or undertake operational business activities and, therefore, cannot accept orders, participate in tenders, sign contracts or engage in the import, export or distribution of goods. The types of activities that may be conducted by such a representative office include marketing and promotional activities and information gathering for the foreign company.

A representative office under the control of the Department of Public Works is established for the specific purpose of entering into a joint operation agreement with an Indonesian entity to engage in construction and construction consulting services.

A regional representative office may be established by a multinational company in one of Indonesia's main cities to manage the operations of such company in the ASEAN region. The activity of a regional representative office is limited to supervising and co-ordinating the business of its company within the region. This office is not allowed to engage in transactions with companies or persons in Indonesia, either for export or import or domestic trading.

2.3 Indirect foreign investment

The primary form of indirect foreign investment into Indonesia is through the country's stock exchange, which is regulated by the Financial Service Authority, or *Otoritas Jasa Keuangan* (***OJK***), whose main function is to regulate capital market activities. Because the Investment Law states that it does not apply to indirect or portfolio investments, it is unclear whether public companies deals fall within the jurisdiction of BKPM and require pre-approval. In 2013, Indonesia introduced Regulation 5/2013, which had the effect of subjecting public companies to the authority of BKPM, depending on whether the 'controlling' shareholder of the public company was a foreign investor. Some of these provisions were subsequently revoked, and so, at the time of writing this guide, it is unclear what regulation applies to foreign investments in public companies. As such, obtaining further advice on this issue is strongly recommended.

2.4 Limitations on foreign investment

(a) Banned sectors

Not all business fields are 'open' to foreign investment. Under Presidential Regulation No.39 of 2014 the 'Investment Negative List' (the ***Negative List***), which was last revised on 23 April 2014, business sectors are either completely 'closed to' investment or 'conditionally open' (meaning that they are subject to foreign ownership limits or require special arrangements and permits). The Negative List prohibits any investment activities from being conducted in those fields, whether by the PMA Company itself or by subsidiaries of the company. Decisions to close business fields to foreign investment are based on health, moral, cultural, environmental, national defence and security concerns, and other national interests. (See the table below for more information.)

Business sectors that are not mentioned in the Negative List are, in theory, considered completely open to investment from non-Indonesian investors but this is not necessarily the case in practice. Article 3 of the Negative List confirms that business sectors that are not specifically mentioned are unconditionally open for investment. However, we consider that it would be prudent to re-confirm with BKPM (as the government institution that administers the enforcement of the foreign ownership limitations provided in the Negative List other than those in the banking, finance and mining sectors) that there is no unwritten policy in place, or condition imposed, that restricts foreign investment into business lines that are not listed in the Negative List. Where new business sectors have been introduced, although a new foreign ownership limit may now apply where previously there was no formal restriction, investors at least have some certainty as to what restriction or condition applies.

LIST OF BUSINESS FIELDS CLOSED TO INVESTMENT	
Sector	**Business field**
Agriculture	Marijuana cultivation
Forestry	1. Capturing of Fish Species as listed in Appendix *I Convention on International Trade in Endangered Species of Wild Fauna and Flora*. (***CITES***) 2. The use (removal) of coral/atoll from nature for construction material/lime/calcium and souvenir/jewellery, also live or dead coral (recently dead coral) from nature.
Industry	1. Manufacture of Alcoholic Beverages (Hard Liquor, Wine, and Malt Containing Beverages) 2. Manufacture of chemicals that can damage the environment: a. Mercury processed Chlorine Alkali b. Manufacture of active ingredients of pesticides c. Industrial chemicals: Polychlorinated Biphenyl (***PCB***), Hexachlorobenzene d. Manufacture of the ozone depleting substances listed in President Regulation No.39/2014 3. Chemical Material Industry Schedule 1 Chemical Weapons Convention (Sarin, Soman, Tabun Mustard, Levisite, Ricine, Saxitoxin, VX, etc)
Transportation	1. Providing and Implementation of Land Terminals 2. Implementation and Operation of Weight Stations 3. Implementation of Motor Vehicle Type Tests 4. Implementation of Motor Vehicle Periodic Tests 5. Telecommunication/Supporting Facility of Shipping Navigation 6. Vessel Traffic Information System (***VTIS***) 7. Air Traffic Guiding Service
Communication and Informatics	Management and Implementation of Radio Frequency and Satellite Orbit Spectrum Monitoring Stations
Culture and Tourism	1. Government Museums 2. Historical and Ancient Heritage (temple, castle, epigraphy, remains, ancient buildings, etc) 3. Gambling/Casinos

Source: President Regulation No.39/2014 on List of Business Fields Closed to Investment and Business Fields Open, with Conditions, to Investment. The Negative List was last updated in April 2014.

(b) Foreign ownership caps and other conditions

Foreign investors are able to hold up to 100 per cent ownership in some industries under Presidential Decree No. 39 of 2014, while in other sectors the maximum amount of foreign ownership is capped at a figure between 20 and 95 per cent. There are several further sectors that are subject to specific regulations, such as banking and horticulture, where the foreign ownership may be capped as low as 20 per cent. To the extent that 100 per cent foreign ownership in the relevant business sector is not permitted, the PMA Company must be a joint venture between foreign investors and Indonesian participants.

The following table outlines some of the business fields for which the cap on foreign ownership has either been tightened, relaxed or clarified since the new Negative List was published in April 2014. This table is intended to give an overview of some of the sectors that were affected by the changes to the Negative Investment List in April 2014 and does not cover all lines of business subject to foreign investment caps.

Recent changes to caps on foreign investment in Indonesia

Business field	Cap
Energy and mineral resources	
Electrical power installation services	Closed to foreign investment (before 24 April 2014, it was open for up to 95% foreign capital).
Large-scale power plants (capacity of >10MW)	Foreign investment limit for power plant projects carried out in a public-private partnership is 100%. Under the partnership terms, a foreign investor can wholly own the power plant during the concession period, after which some equity must transfer to the Government. (Before 24 April 2014, it was subject to a 95% limit).
Small-scale power plants (capacity of 1-10MW)	Subject to foreign ownership limit of 49% (before 24 April 2014, small-scale electricity generation could be carried out in partnership with local businesses with no express restriction on foreign capital).
Land drilling services	Closed to foreign investment (before 24 April 2014, it was open for up to 95% foreign capital).
Offshore drilling services	Subject to a foreign ownership limit of 75% (before 24 April 2014, it was subject to a 95% limit).
Certain oil and gas support services	Closed to foreign investment (before 24 April 2014, it was open for up to 95% of foreign capital).
Certain oil and gas construction services	Either closed to foreign investment or subject to limits ranging from 49% to 75% (before 24 April 2014, these services were not mentioned in the Negative List).

Business field	Cap
Communications and informatics	
Advertising	Open to investment by ASEAN member countries subject to a foreign ownership limit of 51% (before 24 April 2014, it was entirely closed to foreign investment).
Broadcasting	Open to 20% foreign ownership in existing radio or television broadcasting companies by way of new capital injection by foreign investors. This was not, strictly speaking, a new rule, since the 2002 Broadcasting Law already provided that a foreign investor may participate in the capital of an existing broadcasting company for its business expansion. It is possible that this change to the Negative List was made to harmonise the regulations.
Fixed telecommunication network provider services (includes the operation, maintenance or provision of network access for facilities used for voice, data, text, sound and video transmission using wired telecommunications infrastructure)	Subject to foreign ownership limit of 65% (before 24 April 2014, it was subject to a 49% limit).
Provision of content services (eg ring tone, premium SMS), call centres, data communication system services and internet services	Subject to foreign ownership limit of 49% (before 24 April 2014, these businesses could only be conducted in partnership with local partners and there was no express limit on the foreign ownership).
Healthcare	
Sub-specialised hospital services, specialised medical clinics, specialised dental clinics and specialised nursing treatment services	Open to investment by ASEAN member countries subject to a foreign ownership limit of 70% in certain regions of Eastern Indonesia, and 67% in the rest of the country. (Before 24 April 2014, the limits were tighter).
Pharmaceuticals (manufacture of drugs, raw pharmaceutical materials and finished drugs)	Subject to foreign ownership limit of 85% (before 24 April 2014, it was subject to a 75% limit).
Transportation	
Construction of land terminals (eg passenger land transport terminals and general cargo terminals)	Subject to foreign ownership limit of 49% (before 24 April 2014, this line of business was not covered under the Negative List, so the revised list now clarifies what limit applies).
Periodical motor vehicles testing services	Subject to foreign ownership limit of 49% (before 24 April 2014, this line of business was not covered under the Negative List, so the revised list now clarifies what limit applies).
Provisions of port facilities	Subject to foreign ownership limit of 95% for port provision services in a public–private partnership scheme (before 24 April 2014, it was subject to a 49% limit).

Business field	Cap
Finance	
Venture capital	Subject to foreign ownership limit of 85% (before 24 April 2014, it was subject to an 80% limit).
Trade	
Small-scale retail business lines	Closed to foreign investment (before 24 April 2014, most retail business lines were, in practice, not open to foreign investment but the position has now been confirmed by the revised list).
Large-scale retail business lines	Not expressly mentioned in the Negative List, so in theory it would be considered open to foreign investment; however, there is no clarity on what would constitute 'large-scale' retail business.
Distribution, warehouse and cold storage (except cold storage in areas listed below)	Subject to foreign ownership limit of 33% (before 24 April 2014 they were entirely open to foreign investment).
Cold storage businesses in Kalimantan, Sulawesi, Nusa Tenggara, Maluku and Papua	Subject to foreign ownership limit of 67% (before 24 April 2014, they were entirely open to foreign investment).

Source: President Regulation No.39/2014 on List of Business Fields Closed to Investment and Business Fields Open, with Conditions, to Investment. The Negative List was last updated in April 2014.

Apart from limitations in terms of percentage of foreign shareholding, there are other conditions that attach to some of the remaining 'open' business fields. Certain subsectors of forestry, maritime and fishery, energy and mineral resources, industrial, defence, public work (eg construction for public buildings), trade, culture and tourism, transportation, communication and informatics, finance, banking, manpower and transmigration (eg labour service providers), education, health and security, have one or more of the following conditions:

> they are reserved for micro, small and medium enterprises and cooperatives (as defined in Law Number 20 of 2008 on Micro, Small, Medium Enterprises and Cooperatives);

> they require a partnership;

> they are required to be in a certain location; and

> they require a special licence from the relevant Minister.

Obtaining professional advice on how the business field of a particular proposed investment is categorised is strongly recommended, as navigating the various laws can be difficult.

3

Enterprises in Indonesia

3.1 Types of corporate enterprises

There are three main private limited liability company models recognised in Indonesia:

> general Indonesian companies (*Perseroan Terbatas Biasa* or ***PT Biasa***);
> domestic capital investment companies (*Perseroan Terbatas Penanaman Modal Dalam Negeri* or ***PT PMDN***); and
> foreign investment companies (*Perseroan Terbatas Penanaman Modal Asing* or ***PT PMA***).

Perseroan Terbatas or 'PT' is a limited liability company. Under a PT, shareholder liability is limited to the extent of the capital agreed to be contributed by shareholders.

Indonesian law divides PT into two classes: (1) PT Biasa and PT PDMN and; (2) PT PMA. The ownership of a PT Biasa or PT PDMN is limited to Indonesian citizens and/or Indonesian legal entities. A PMDN Company may enjoy certain regulatory or tax advantages that a PT Biasa is not eligible for.

Only a PT PMA can be used for foreign investment activities. Foreign investors may, however, acquire shares in PT PMDN or PT Biasa companies, provided that they comply with the Investment Law and Negative Investment List. The acquired PT Biasa/PT PMDN would also have to be converted into a PT PMA. It is possible to have 100 per cent foreign shareholding in a PT PMA where the industry sector so permits, provided it has a minimum of two shareholders either as foreign individuals or company entities.

The minimum capital requirement for company incorporation in Indonesia is IDR 50 million for PT Biasa, but higher amounts are required for PT PMDN or PT PMA. The Regulation 5/2013 requires that a minimum of IDR10 billion be invested in a new PT PMA, excluding the cost from the land and buildings. In addition to the minimum investment requirement, the Regulation 5/2013 also requires that each shareholder of a PT PMA holds shares with a nominal value of at least IDR 10 million. Furthermore, the Regulation 05/2013 states that the minimum equity to debt ratio permitted is 25 per cent. Although, in practice, there are cases of BKPM approving a 10 per cent equity to debt ratio, specifically in the property and plantation sectors.

3.2 Corporate governance

Indonesia's Law Number 40 of 2007 on Limited Liability Companies (the ***Company Law***) and implementing regulations establish a 'two-board' system of governance:

> the Board of Commissioners (*Dewan Komisaris*) that supervises the performance of the Board of Directors and policies made by the board, and provides advice to the board; and

> the Board of Directors (*Direksi*) that manages the company's operations and serves as the authorised organ and representative of the company in all matters, subject to compliance with the law, the company's rules and resolutions of the general meeting of shareholders.

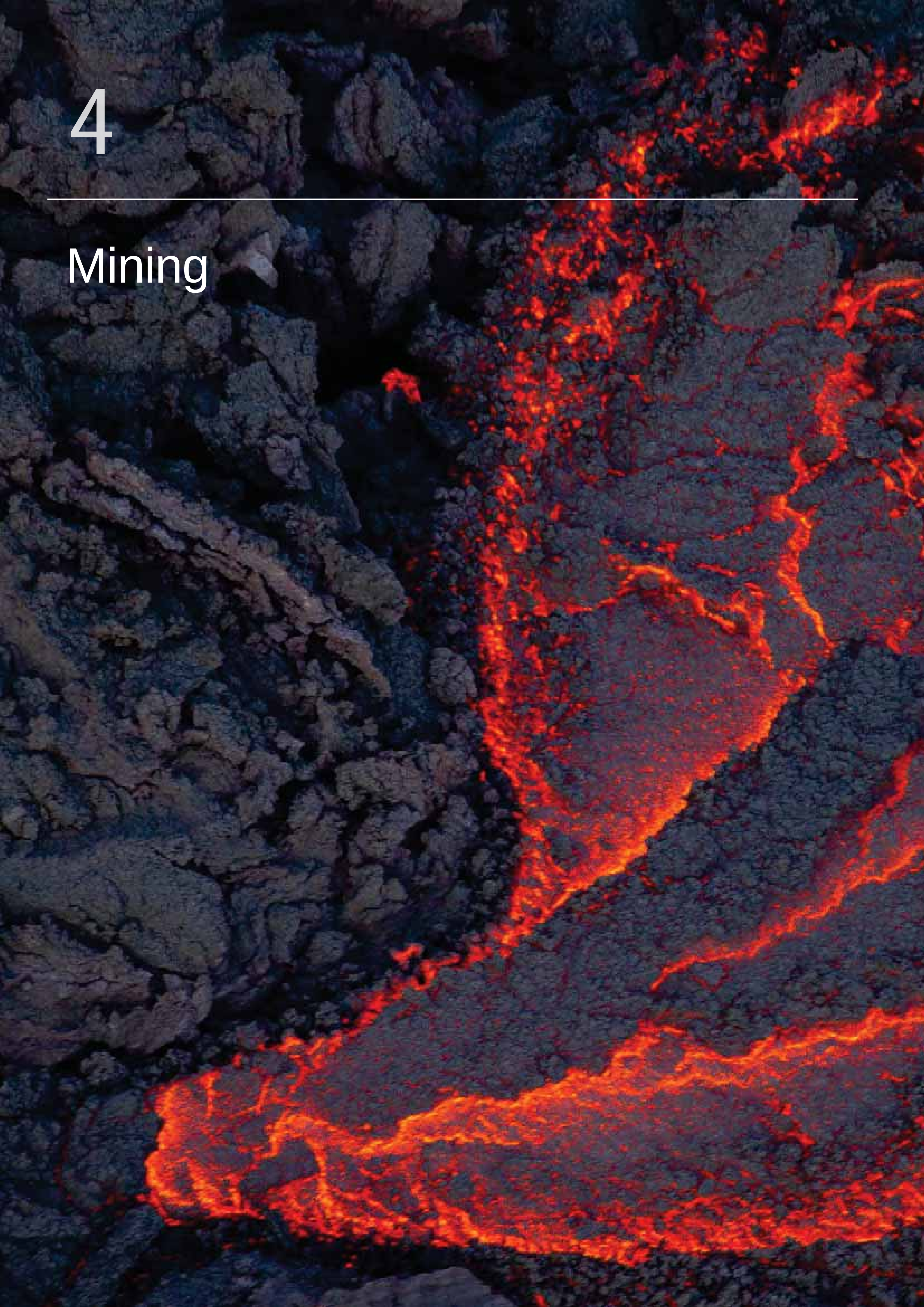
Indonesia's Company Law adopts the common law concept of fiduciary duties for each board in carrying out their respective role. While the two boards are separate, the Board of Commissioners may work together in conjunction with the directors to implement strategies of the company.

A director has a duty to manage the company in good faith and prudently for the benefit of the company and is personally liable for any loss suffered by the company for breach of this duty. Directors of Indonesian companies have similar responsibilities to directors of companies in common law countries and, among other things, must prepare an annual report to shareholders for approval and a business plan for the next financial year, manage the company's operations and represent the company in relation to external parties.

All of the directors and commissioners of a PMA Company, whether a 100 per cent foreign owned company or a JV Company, may be foreigners. However, the position of 'personnel director' (who need not be a member of the board) and positions of authority in a human resources capacity, cannot be occupied by foreigners. If there is an Indonesian shareholder in the PMA Company, BKPM may recommend that at least one of the directors is Indonesian.

4

Mining



4.1 Regulation

Mining is regulated under Indonesia's Law No.4 of 2009 on Minerals and Coal Mining (the ***Mining Law)***. This law came into effect in 2009 and introduced a licence-based system of regulation of mining. The Mining Law does not cover the Contract of Work System (***COWs***), which regulated the mining sector before the licencing framework, except that the Mining Law includes transitional provisions stating that existing COWs will be honoured.

Mining activities can only be carried out in areas that the Indonesian Government has classified as mining zones. The Government classifies areas that will be mining zones, based on determinations by regional governments in consultation with the National Parliament that an area has mineral and/or coal extractive potential.

Before obtaining a mining business permit, and except in respect of small-scale mining zones, a person must obtain a licence to conduct mining activities in a particular mining zone. The key stages are:

> obtain required licence to mine in a particular mining zone:
  - WIUP designated within a WUP mining zone; or
  - WIUPK designated within a WUPK mining area, which is a 'special mining area' originally reserved to the State for certain commodities and conservation but for which approval has been given by the National Parliament for commercialisation.

> obtain a mining business permit for exploration and production:
  - IPR (small-scale mining business permit granted for a small-scale mining area, but that is not available to foreign investors);
  - IUP (mining business permit required for a WUP area); or
  - IUPK (special mining business permit required for a WUPK area).

An IUP is obtained after obtaining a WIUP. The process for obtaining a WIUP differs depending on the type of mineral involved:

> metallic minerals and coal are granted by tender; and

> non-metallic minerals and rock/stone are granted by direct application.

An exploration IUP is granted upon application after obtaining a WIUP. Only the Minister (and not regional governments) has authority to issue IUPs to PMA Companies.

An IUPK is obtained after obtaining a WIUPK. State-owned and region-owned entities have priority for the grant of an IUPK, and the Minister must first offer WIUPKs to state-owned enterprises or region-owned enterprises on priority terms. Where State-owned enterprises or region-owned enterprises lack interest, a WIUPK can then be offered to private entities through a bidding process.

IUPs and IUPKs may be held directly or indirectly by foreign investors (subject to divestment obligations considered below). A key feature of the Mining Law is that each applicant may only be granted one IUP or IUPK; however, a public company may be granted more than one licence.

An IUP for exploration entitles the holder to undertake general inspection, exploration and feasibility studies for a specified maximum period, depending on the mineral or coal being mined, after which the permit can be extended as a production licence; whereas holders of exploration IUPKs have narrower rights because the mining zone is a 'special mining area'.

An IUP for operational production entitles the holder to conduct construction, mining, processing and purification, and transportation and sales activities.

4.2 Relinquishment and divestment requirements

The Government of Indonesia introduced new mining regulations in 2013. Regulation No. 27 of 2013 (***MEMR 27/2013***) was introduced to implement the divestment obligation under Government Regulation No. 23 on 2010 on the Implementation of Coal and Mineral Mining Business Activities (***GR 23/2010***), as amended by Government Regulation 24 of 2012 (***GR 24/2012***) and Indonesia's Mining Law. The MEMR 27/2013 overrides former divestment and pricing procedures under previous mining law.

In Indonesia, there are requirements on holders of exploration IUPs or IUPKs to progressively relinquish parts of the area being explored. The extent of relinquishment varies depending on the mineral being mined. Eg holders of exploration IUPs or IUPKs for metallic minerals may retain a maximum of 50,000 hectares by the fourth year of the exploration phase; while by the eighth year of the exploration phase, or on expiry of the exploration IUP or IUPK (at the time of extension into a production IUP), a maximum of 25,000 hectares may be retained. Whereas, the maximum area that holders of exploration IUPs or IUPKs may retain for the exploration of coal by the fourth and eight year of the exploration phase is only 25,000 hectares and 15,000 hectares, respectively.

During the production stage, there is no mandatory obligation to relinquish any of the area being mined. However, holders of production IUPs and IUPKs whose shares are owned by foreign parties are required to divest a portion of their shares to the central government, regional governments, State-owned enterprises (***BUMNs***), region-owned enterprises (***BUMDs***) or national companies (any of the foregoing being categorised as ***Indonesian Participants***).

GR 23/2010, as amended by GR 24/2012, requires that a minimum 51 per cent shareholding be progressively divested to Indonesian Participants after five years, following the commencement of production as follows:

> 20 per cent in the sixth year;
> 30 per cent in the seventh year;
> 37 per cent in the eighth year;
> 44 per cent in the ninth year; and
> 51 per cent in the 10th year.

4.3 Divestment procedures

MEMR 27/2013 introduced mechanisms for the divestment procedure and for determining the share prices for divestment. The central government has the first priority in the divestment process, followed by the regional governments, BUMNs and BUMDs and national companies. MEMR 27/2013 specifies timeframes for the making of offers by IUP and IUPK holders and also the time frames within which Indonesian Participants must respond to such offers. Shares in an IUP or IUPK holder that are sold on the stock exchange will not satisfy the divestment obligation. In addition, IUP and IUPK holders and their affiliates are not permitted to lend funds to the Indonesian Participant for the purchase of the divested shares.

If an Indonesian Participant already holds not less than 51 per cent of the shares in an IUP or IUPK holder, the IUP or IUPK holder is not required to implement the priority divestment procedure.

4.4 Changes to investment structure

Changes to the investment structure of an IUP or IUPK holder, including changes to the investment and financing source, changes of status (from a PMDN to a PMA Company and vice versa), changes to the articles of association, changes to the directors and commissioners and changes to share ownership require the prior approval of the Minister, Government or Regent/Mayor in accordance with their respective authorities.

Foreign ownership of a PMDN that holds an exploration IUP or IUPK and wishes to convert to a PMA Company is limited to 75 per cent of the total issued shares. A change in share ownership of a PMA Company (including through share sale, merger, consolidation and acquisition) that holds an exploration IUP or IUPK can only be undertaken if foreign ownership is not more than 75 per cent of the total issued shares.

Foreign ownership of a PMDN Company that holds an operation production IUP or IUPK and wishes to convert to a PMA Company is limited to 49 per cent of the total issued shares. A change in share ownership of a PMA Company that holds an operation production IUP or IUPK can only be undertaken if foreign ownership is not more than 49 per cent of the total issued shares. In effect, a foreign miner could be reduced to 49 per cent on any change of shareholding in a PMA Company or on the conversion of a PMDN entity to a PMA Company (which must occur following the investment of a foreign investor in a PMDN Company).

4.5 Domestic processing and refining obligation, and export tax

In 2014, the Indonesian Government (through the Ministry of Energy and Mineral Resources (***MEMR***)) issued Regulation No. 1 of 2014 (***MEMR 1/2014***) to implement the in-country processing requirements under Government Regulation No. 23 of 2010 on the Implementation of Coal and Mineral Mining Business Activities, which have also been amended by Government Regulation 1 of 2014 (***GR 23/2010***) and Indonesia's Mining Law.

Under the Mining Law and GR 23/2010, holders of IUPs and IUPKs for production operation and COWs are required to add value for Indonesia by conducting in-country processing and refining. The Mining Law and GR 23/2010 require in-country processing and/or refining of minerals within five years of the effectiveness of such a law (ie from 12 January 2014) and therefore bans the export of ore after that date.

The new regulations are designed to implement the in-country processing requirements following the expiry of this five-year transition period.

Key features of the new regulations include:

> All mineral commodities (including metal minerals, non-metal minerals and rock/stone, but excluding coal) must be processed and/or refined in-country, according to the minimum processing and/or refining limits set out in MEMR 1/2014, before export.

> Nickel, bauxite, tin, gold, silver and chromium must be fully refined in-country, according to the minimum refining limits set out in MEMR 1/2014, before export.

> The holders of COWs and production operation IUPs may, for a period of not more than three years from the issuance of MEMR 1/2014 (ie until 12 January 2017), continue to export:

- semi-processed metal minerals in the form of: copper, iron, ilmenite, titanium, lead, zinc and manganese concentrates (provided the relevant minimum limits for the processing of such concentrates set out in the regulation are satisfied); and
- copper by-products in the form of: anode sludge and copper telluride (provided that further refinement of such products in-country cannot yet be undertaken).

> The right to export such semi-processed minerals and copper by-products is dependent upon the COW or IUP holder obtaining a recommendation from the Director General in the MEMR's name. Each recommendation is valid for a period of six months. In order to obtain such a recommendation, the COW or IUP holder must, in the case of export of semi-processed minerals, demonstrate:

- that it has sufficient funds to undertake processing and refining in-country using its own facilities or based on a cooperation with another party;
- its seriousness to develop refining facilities directly or in cooperation with another party with a plan for the development of such facilities; and
- good environmental management performance.

For the export of copper by-products, only the latter two criteria must be satisfied in order to obtain a recommendation.

The Ministry of Finance also issued a new regulation, Regulation No. 6/PMK.011 of 2014, which imposes export taxes on the export of copper, iron, ilmenite, titanium, manganese, lead and zinc concentrates. This regulation is designed to disincentivise COW and IUP holders from exporting semi-processed products. Export taxes are imposed progressively, commencing at a rate of 20 per cent (25 per cent for copper concentrate) in 2014 and increasing to 60 per cent by 2016.

5

Land

5.1 Introduction

The legal framework for land ownership in Indonesia was established under Law No.5 of 1960 concerning the Basic Provisions concerning the Fundamentals of Agrarian Affairs (the ***Basic Agrarian Law***). Under the Basic Agrarian Law, the most extensive right to land in Indonesia is the *Hak milik* (right of ownership). Only Indonesian citizens (and other corporate bodies designated by the Government, such as State-established banks, associations of agricultural cooperation (*perkumpulan koperasi pertanian*), religious bodies that have been appointed by the Head of the National Land Agency (*Badan Pertanohan Nasional*) and social organisations that have been appointed by the Head of the National Land Agency (*Badan Pertanohan Nasional*), are permitted to 'own' land with the *Hak Milik* type, in the sense of holding indefeasible title. Under Government Regulation No. 41/1996, non-Indonesian citizens may occupy a building or land via agreement with the owner of *Hak Milik* type land right (for an initial period of 25 years and extendable to another 25 years), but this right does not equate to ownership by non-Indonesian citizens.

The Basic Agrarian Law recognizes several other types of rights over land. However, only the following land right permits may be issued to foreign investment companies:

> *Hak Guna Usaha* (leasehold);

> *Hak Guna Bangunan* (building rights); and

> *Hak Pakai* (right of use).

These permits are issued to PMA Companies on the condition that they do not require an extensive area and that they use State-owned land rights. With respect to 'State-owned land rights', this means that if the State does not already own the right, the land owner will need to enter an agreement with the PMA Company to relinquish the relevant right to the State before filing an application with the Land Office.

Each of the above land right permits authorises the use of land, but differs in the duration of the right, the type of use permitted, and whether the land user has the right to transfer or use their land use rights as security.

5.2 Leasehold

A *Hak Guna Usaha* may be granted by the State for a maximum period of 95 years (renewed in advance for 60 years with an option to be further renewed for 35 years). This permit may only be used for cultivation purposes. It may be transferred or mortgaged.

5.3 Building rights

A *Hak Guna Bangunan* may be granted by the State for 30 years and may be extended for another 20 years. For the purposes of foreign investment, the foreign investor may apply for *Hak Guna Bangunan* and its extension simultaneously, making the total term 50 years. After the expiry of the term of *Hak Guna Bangunan* and its extension, the holder may re-apply for *Hak Guna Bangunan* in the same plot of land, provided that the city planning still permits. This is a right to erect and possess construction on land. The right may also be transferred or mortgaged. A foreign investment company that requires land for a factory or storage would, in most cases, apply for this type of permit, as it is the closest thing to land ownership available in Indonesia. If the land is not *Hak Guna Bangunan* land, it is necessary for the land owner to first convert a *Hak milik* / *Hak Guna Usaha* / *Hak Pakai* land title to a *Hak Guna Bangunan* title. This is usually done through a binding agreement with the land owner to convert the existing land right to the *Hak Guna Bangunan* with approval of the Land Office before entry into a sale and purchase agreement for the land.

5.4 Right of use

Hak Pakai may be granted by the State for 70 years (renewed in advance for 45 years with an option to be further renewed for 25 years). It is a right to use and/or collect produce from land. Despite the right of its holder to use the land and/or collect produce from the land, the holder has the obligation to preserve the land, the buildings on it and its environment. This land right can be transferred if the land is directly controlled by the State with approval from the State, but otherwise it cannot be transferred unless explicitly stated in the relevant agreement.

6

Infrastructure / PPPs

6.1 Plan for economic development

The Indonesian Government supports infrastructure delivery through public private partnerships (***PPPs***). There has been significant progress over the last few years regarding the establishment of a framework for PPPs, including the creation of a government guarantee scheme and the Indonesia Infrastructure Guarantee Fund (***IIGF***), a financial body that provides guarantees for infrastructure projects. At the time of writing, only one PPP project has commenced under the government guarantee scheme (the Central Java Power Project). However, a number of PPP projects are in progress without a government guarantee.

PPPs are regulated by a specific set of regulations and must be conducted in accordance with the Government's foreign ownership policy as set out by BKPM (see section 2.4 for more information).

The MP3EI (the Indonesian Government's Economic Master Plan for Acceleration and Expansion of Economic Development 2011 – 2025) states that approximately one fifth of the nation's infrastructure needs (the total of which is estimated to be worth US$300 billion (around Rp 3.4 trillion)) are to be delivered through PPPs. The MP3EI identifies 389 proposed infrastructure projects.

In November 2013, Indonesia's Ministry of National Development Planning/National Development Planning Agency (***Bappenas***) issued the *Public-Private Partnerships: Infrastructure Projects Plan in Indonesia* (the ***PPP Book 2013***). The PPP Book 2013 outlines the 27 projects that Bappenas has determined meet the criteria to be labelled 'potential' and 'prospective'. It is the latest in a series of similar publications that Bappenas has issued annually since 2009.

The PPP Book 2013 is a valuable resource for investors, lenders and contractors contemplating an investment in Indonesia's PPP projects. It includes

> a high-level summary of Indonesia's PPP framework;
> the processes for both solicited and unsolicited proposals;
> a status report on the 21 projects previously tendered under the PPP framework; and
> an overview of 27 potential and prospective projects.

The 27 projects cover railways, urban revitalisation, toll roads and bridges, water supply, sanitation, sea port developments, airport developments and power generation.

Several sets of regulations affect Indonesia's PPP projects. The starting point for the PPP legal framework is Presidential Regulation 67/2005 on Cooperation between Government and Business Entities in Infrastructure Provision, which was subsequently amended in 2010, 2011 and 2013. This provides for Bappenas's coordinating role in relation to PPPs, and lists the sectors in which PPP projects may be implemented:

> transport infrastructure (ports, airports, rail);
> toll roads and bridges;
> water and sanitation;
> telecommunications networks;
> electricity generation, transmission and distribution; and
> petroleum and natural gas processing, storage, transportation, transmission and distribution.

It provides for implementation of PPP projects via 'Cooperation Agreements' to be entered into between the Government of Indonesia and private parties, and lists the minimum content of a cooperation agreement.

6.2 Relevant legislation

Key areas of regulation relevant to PPPs include the following.

Sectoral regulation Separate regulatory regimes apply to the operation of roads, ports, railway operations and each of the other sectors in which PPPs may be implemented.

Land acquisition Government support for PPPs will typically include undertaking necessary land acquisition and resettlement processes, though often with the private sector party bearing the cost. Law No.2 of 2012, and Presidential Regulation 71/2012, regulate land acquisition and compensation for infrastructure projects.

Environmental regulation Law No.32 of 2009 on Environmental Protection and Management and Government Regulation 27/2012 require an environmental impact analysis for projects of specified sizes before implementation, and provide for issue of environmental licences.

Foreign investment The Negative Investment List sets out maximum levels of foreign investment in certain industries (see the discussion in section 2.4).

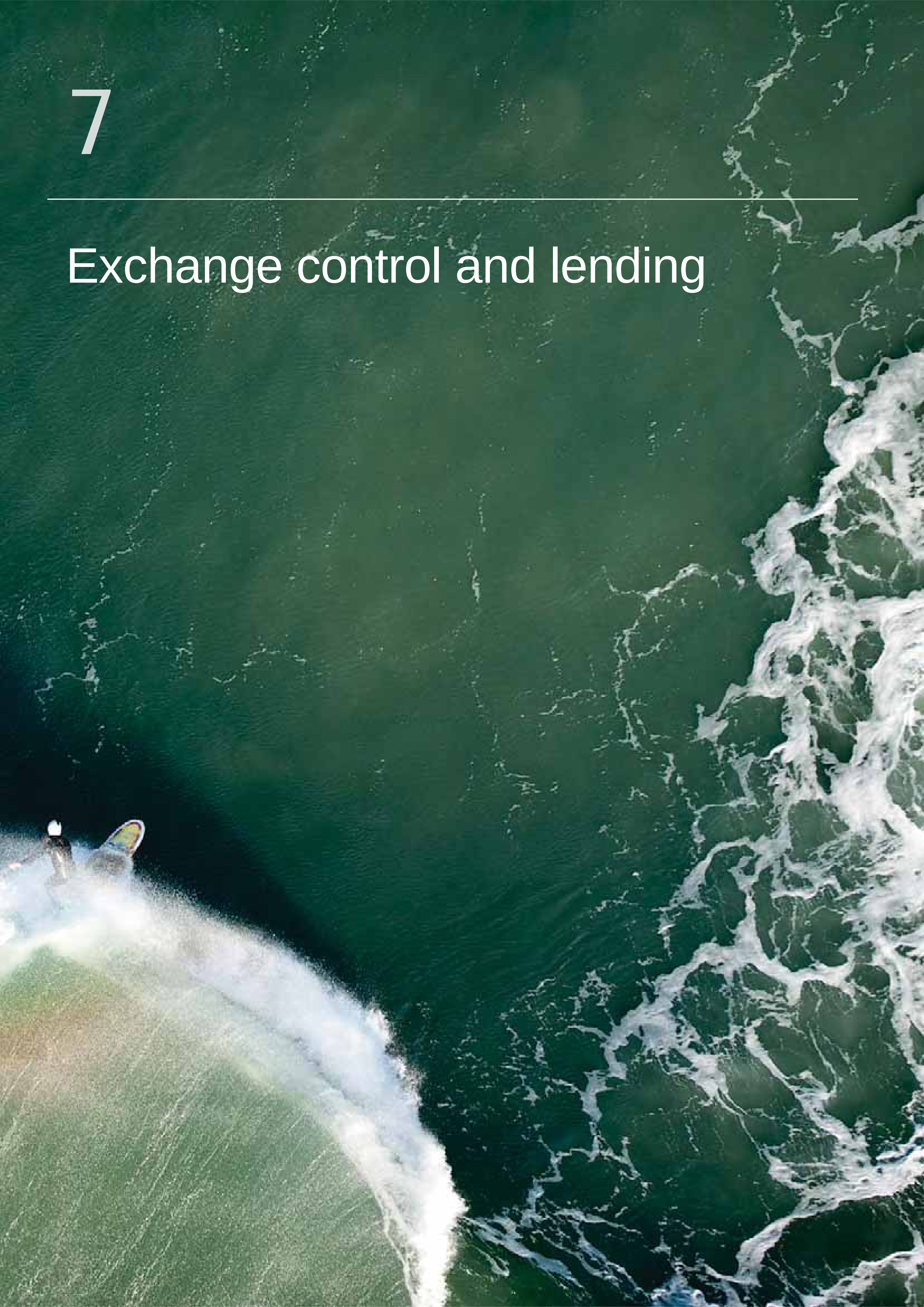
Government guarantees The Government may support PPP projects through the issue of guarantees, under Presidential Regulation 78/2010. Guarantees are issued by a single government entity, PT Penjaminan Infrastructure Indonesia or PT PII (in English, Indonesia Infrastructure Guarantee Fund or IIGF). Guarantees, where the Government agrees to issue them, may cover political risks, project performance risks (such as delays or cost overruns in the land acquisition process) or demand risk (eg by providing a minimum guaranteed revenue).

Bappenas's PPP procurement regime, implemented under regulations introduced in 2005 and refined on several occasions since, is now well established. As the PPP Book 2013 demonstrates, there is now a track record of projects that have successfully completed the project preparation phase and are undergoing tendering, and, in one case, commenced operation. Those are supported by a project pipeline across a range of sectors that are identified as 'potential' or 'prospective', at least some of which seem likely, on the basis of past experience, to progress to tendering in the coming year.

In reality, infrastructure projects continue to face challenges, including issues of capacity building and an uncertain regulatory framework. However, the signs are encouraging. Eg after commencing in 2003, then being abandoned in 2011, the Jakarta Monorail Project recommenced in 2013. In addition, a ceremony was recently held in Jakarta marking the commencement of the Jakarta Mass Rapid Transit system (108 kilometres with 13 stations). The project was launched after being delayed for almost 24 years.

7

Exchange control and lending



7.1 Exchange control

While Indonesia has no foreign currency control restrictions, the Indonesian Government monitors foreign exchange transactions via mandatory reporting. Under Law No.24 of 1999 concerning Foreign Exchange Flow and Exchange Rate System, Bank Indonesia has the authority to request information and data concerning activities of the Foreign Exchange Flow conducted by residents. In particular, all transfers of financial assets and liabilities between residents and non-residents must be reported by banks to Bank Indonesia on a monthly basis. There are also regulations requiring Indonesian exporters to deposit their entire export proceeds into foreign exchange banks in Indonesia and report their export activities to foreign exchange banks, which then pass on this information to Bank Indonesia.

7.2 Currency for transactions

On 28 June 2011, Law No. 7 of 2011 on Currency (the ***Currency Law***) came into force in Indonesia. The Currency Law requires parties to use IDR as the payment and settlement currency for all transactions in Indonesia. It is broadly drafted to capture all transactions in Indonesia. However, it does provide a list of exemptions as follows:

- transactions related to the state budget;
- grants given by or to a foreign state;
- international trade transactions;
- bank deposits denominated in foreign currencies; and
- international finance transactions.

The terms ‘international trade transactions’ and ‘international finance transactions’ are not defined in the Currency Law or its implementing regulations. However, a Guidance Note limits the operation of the Currency Law to cash transactions. In accordance with a 2011 statement made by the Secretary of Directorate General of Treasury, cash transactions are limited to transactions using bank notes and coins.[1] In principle, a cash transaction may only be conducted using Indonesian rupiah as the currency. However, Article 23 paragraph (1) of the Currency Law provides that a foreign currency may be used in the event that the parties have made a prior agreement in writing. We note that the application of this exception is often challenged by the Bank of Indonesia. [2]

7.3 Offshore borrowing

Indonesian companies are, in general, permitted to borrow money from offshore lenders whether denominated in foreign currency or Indonesian rupiah. Since 2000, offshore borrowings by Indonesian companies do not generally require prior approval from any Indonesian government institutions. However, Indonesian residents must report on their offshore loan obligations, whether denominated in foreign currency or rupiah, to Bank Indonesia. Bank Indonesia also requires that offshore loans denominated in a foreign currency and that satisfy certain criteria be funded into an account in a foreign exchange bank in Indonesia, and that the borrower report the drawing of the offshore loan to Bank Indonesia.

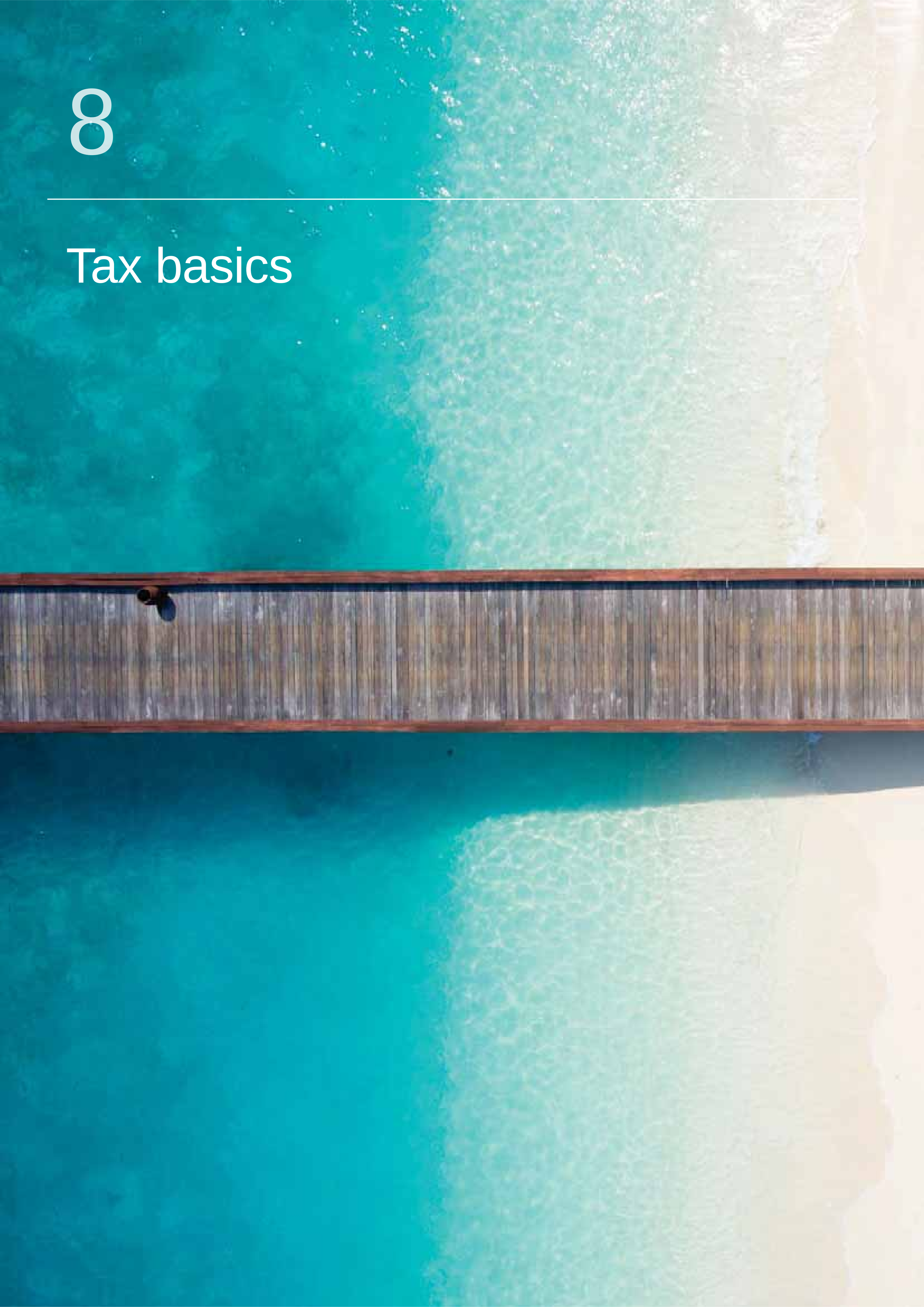
7.4 Onshore borrowing

Most major Indonesian banks (which includes the branch offices of foreign banks operating in Indonesia) may provide credit facilities in Indonesian rupiah or in foreign currency. Indonesian banks are, however, prohibited from granting credit facilities to non-residents, unless the lending is for personal use of the non-resident (eg personal credit cards and loans).

1 Sourced from *http://www.hukumonline.com/berita/baca/lt4edeb7bc6fc9b/bi-tawarkan-amandemen-uu-mata-uang.*
2 *ibid.*

8

Tax basics



Tax advice in Indonesia is generally obtained from accredited tax consultants at Indonesian accounting firms.

Most Indonesian taxes are similar to those that investors would expect to find in other jurisdictions. These include:

> income tax, which includes Corporate Income Tax, Capital Gains Tax, Individual Income Tax, Withholding Tax on employee's remuneration and Withholding Tax on various payments to third parties; and

> Value Added Tax (***VAT***) and Luxury Goods Sales Tax (***LGST***), levied on goods and services used for manufacturing, business and consumption in Indonesia (subject to certain criteria).

Taxation in Indonesia is determined on the basis of residency. A company is treated as being an Indonesian tax resident for taxation purposes if it has been incorporated or is domiciled in Indonesia. A foreign business engaging in business activities in Indonesia via a permanent establishment (***PE***) will typically assume the same tax obligations as a resident taxpayer.

The Indonesian tax regime incorporates both a self-assessment system and a withholding tax system.

The fundamental pieces of tax legislation in Indonesia include:

> the General Provisions and Taxation Procedures Law No. 28 of 2007;

> the Income Tax Law No 36 of 2008; and

> the Value Added VAT (termed 'Goods and Services and Sales Tax on Luxury Goods') Law No 42 of 2009.

Foreign companies intending to invest in Indonesia should obtain detailed tax advice from an accredited Indonesian tax consultant.

9

Employment

9.1 Introduction

Law No.13 of 2003 on Manpower (the ***Labour Law***), together with its regulations, creates a uniform legal framework for employment. The Labour Law applies both to local Indonesians and foreigners working in Indonesia, and it is not possible to contract out of the terms of the employment legislation, although, in practice, it is common to find contracts that do not comply with the Labour Law. If there is a dispute, the Labour Law will override the terms of the contract.

9.2 Employment contracts

Parties are generally free to negotiate and document their own employment contracts, provided that the terms contain those that must be included: eg name of employee, type of work and amount of wages, and provided that the terms are not less favourable than those prescribed by law: eg in relation to the minimum regional wages, and holiday and maternity leave entitlements.

9.3 Duration of employment

The Labour Law prescribes two types of employment contracts:

> indefinite term contracts; and

> definite term contracts.

Definite term contracts may be made based on a specific time or the completion of a certain job or work that is temporary in nature, but cannot be used for jobs that are permanent in nature. Definite term contracts can only be performed for a maximum period of two years and may be renewed once only, for a maximum period of one year, provided the employee is notified within seven days before the end of the contract. Once this renewal period expires, the employer and employee may continue the employment relationship by entering into another definite term contract, provided a 30-day grace period has lapsed. The second definite-term contract may only be made once, for a maximum period of two years.

An employee under a definite term contract cannot be employed on a trial or probationary basis; whereas an employee under an indefinite term contract may be employed on a trial or probation for a maximum period of up to three months.

See section 12.3 for information on the requirement to execute contracts in Bahasa Indonesia.

9.4 Form of contracts

A fixed-term employment agreement must be in Indonesian, although it may be written in both Indonesian and a foreign language. If the contract is in dual languages and there is an inconsistency, the Indonesian version prevails to the extent of any inconsistency. Employment contracts for an indefinite term can be made either orally or in writing; whereas definite term contracts must be in writing. All written work agreements must be signed.

9.5 Termination of employment

An employment contract comes to an end if:

> the employee dies;

> in the case of a fixed term employment contract, the contract expires;

> a court ruling, or a decision or resolution of the institute for the settlement of industrial relations disputes, ends the contract; or

> there is a certain situation or incident prescribed in the contract, the enterprise's rules and regulations, or the enterprise's collective work agreement that may effectively result in the termination of employment.

Termination of an indefinite term employment contract (outside of the probationary period) requires settlement via bipartite negotiations; conciliation, mediation or proceedings before the Industrial Relations Courts. If a fixed term employment contract terminates for reasons other than those listed above, the party that terminates the employment contract must pay compensation to the other party. The amount of compensation must be equal to the amount of wages the employee is entitled to receive from the point of termination to the expiration of the contract.

9.6 Working hours

The maximum number of hours per week that an employee can be employed to work is 40. These hours must be allocated in one of the following ways:

> seven hours per day over six days per week; or

> eight hours per day over five days per week.

The above restrictions do not apply to certain business sectors and types of work regulated by Ministerial Decision. However, in general, if an employer wishes to employ workers to work longer hours, they can do so provided that they obtain agreement from the worker to work the additional hours, they pay the employee overtime wages, and the overtime worked by the employee does not exceed three hours per day or 14 hours per week.

Employees are entitled to breaks of at least 30 minutes after four continuous hours of work. Employers must also provide employees with adequate opportunity to worship as required by their respective religions.

9.7 Wages and leave entitlements

There is no national minimum wage. However, each province has a set minimum wage and, within a given province, there may also be sector-based minimum wages, which cannot be lower than the minimum wage set by the province. The minimum wage must be based on an amount that will meet the costs of all basic needs for a decent livelihood.

All employees are entitled to 12 working days of paid vacation per year after one year of continuous work. Employees are not obliged to work on public holidays except if the nature of their work calls for continuous work (or it is required by the employment contract) and the employee is paid overtime.

Employees are entitled to paid sick leave, including extended paid sick leave. If a worker is ill and cannot perform their work, they are entitled to receive 100 per cent of their wages for the first four months. For the second four months, they are entitled to 75 per cent of their wages and for the third four months they are entitled to 50 per cent. Thereafter, employees are entitled to 25 per cent of their wages until termination of their employment.

Employees are also entitled to other paid leave, including leave for getting married (three days) and compassionate leave (two days).

9.8 Internal labour rules

Employers of more than 10 employees must create a set of internal rules that take effect after approval by the relevant Minister. The internal rules of the enterprise must cover the rights and obligations of the employer and its employees, working conditions and when the rules will expire, and must not be inconsistent with employment legislation. Enterprises that already have collective work agreements are not required to create internal rules.

9.9 Bipartite cooperation institute

Employers of more than 50 employees must establish a ‘bipartite cooperation institute’, which functions as a forum for communication, consultation and resolution on employment issues at an enterprise. The institute must include representatives of the employer and employees.

9.10 Trade unions

Employees have the right to form and become members of a trade union. Once a trade union has been established, a collective work agreement must be made between trade union(s) and employers. This is a written agreement covering the rights and obligations of the employer, trade union and employees. Employment contracts must not be contrary to what is contained in a collective work agreement, and to the extent the employment contract is silent on any matters, the rules in the collective work agreement will apply. A copy of the collective work agreement must be given to each employee.

9.11 Employing foreigners

Generally expatriate employees can work in Indonesia, provided that:

> the work to be performed cannot be performed by local Indonesians;

> the law does not prohibit foreign nationals from performing that type of work; and

> the employer has obtained written permission from the relevant Minister to employ the foreign national.

However, the Labour Law forbids foreign employees from holding positions of authority in a human resources capacity. The Minister of Labour and Transmigration issued Decree No. 40 of 2012 on Restricted Positions for Foreign Employees, which lists 19 positions that cannot be held by foreign employees. While 18 of the positions listed relate to human resources, the list also includes the position of chief executive officer.

Employers of foreign workers are required to submit a plan to the relevant Minister on the use of the foreign employee, which must among other things explain why the foreign worker is needed (the ***Expatriate Manpower Utilisation Plan***). The employer is also required to appoint Indonesian citizens as assisting partners to the foreign workers, so that they can be trained in the foreign worker's expertise and replace foreign employees (except in the case of positions of management or directorship). Employers are also required to pay an amount for each expatriate employee into a skills and development fund managed by the Department of Manpower.

The same laws apply to both local companies and foreign investment companies employing expatriates.

To be able to work in Indonesia, foreign workers must obtain a Limited Stay Visa (*Visa Tinggal Terbatas*). This visa has a minimum validity period of six months and a maximum validity period of two years. An employer must first apply to the relevant Minister for approval of the Expatriate Manpower Utilisation Plan before submitting a working visa application.

9.12 Outsourcing

In Indonesia, companies are restricted in the type of work they can contract to subcontractors and labour suppliers. Both types of third-party contracting arrangements are described in Indonesia as 'outsourcing'.

Until recently, there was uncertainty around the practice of outsourcing. Regulations, which companies were given until 19 November 2013 to comply with, divide outsourcing activities into two types: labour outsourcing (*penyediaan tenaga kerja*) and business process outsourcing (*pemborongan pekerjaan*), and restrict labour outsourcing to the following services: cleaning, catering, security, oil and mining support, and transport. One key objective of the new regulations was to protect labourers employed under an outsourcing contract and, in this regard, labour suppliers are now required to have written employment contracts with their employees that include labourers' rights in accordance with prevailing laws.

In relation to business process (or subcontractor) outsourcing, the regulations do not list specific activities that may be outsourced; rather, the regulations allow business process outsourcing only if certain conditions are satisfied. Such conditions include that the proposed delegated work is separate from the company's core business activities, is categorised as a business supporting activity and will not directly affect the production process if the delegated activity were to stop. Industry associations are expected to publish flowcharts categorising typical core and non-core activities in the given sector, which are to form the basis of a decision on whether an activity may be outsourced.

It is also mandatory to register with the local Ministry of Manpower and Transmigration (***MOMT***) all outsourcing agreements, certain other accompanying documents and, in the case of business process outsourcing, a description of the type of work that will be subcontracted. Failure to comply with the regulations may lead to the company being deemed to be the employer of employees of the labour supplier or subcontractor company.

9.13 Occupational health and safety

Occupational health and safety (***OHS***) issues have seldom been presented as issues of national level significance in Indonesia. However, working conditions are becoming increasingly regulated as the nation becomes more industrialised. Through the MOMT, the Government of Indonesia has accorded increasing priority to OHS and the improvement of working conditions. MOMT is now actively promoting OHS, and stressing the importance of adherence to OHS principles and regulations, in order to reduce the number of industrial accidents. Enforcement of OHS obligations remains an issue.

The basic legal provisions for occupational safety and health are set out in the Safety Act No.1 of 1970 (the ***Safety Act***), Indonesia's founding OHS legislation. The Safety Act is enforced by MOMT. In principle, the Act regulates safety in all workplaces in Indonesia. However, the application of the law is limited to hazardous workplaces listed in Article 2 of the Act. The application of the law to 'other workplaces' depends on the availability of detailed ordinances and regulations, as the safety conditions to be fulfilled by employers must be prescribed by legislation, as stipulated in Article 3.

In addition to the Safety Act, OHS rights and obligations are contained in several other Acts and regulations, including the Labour Law and Regulation PER-01/MEN/1980 on Safety and Health in Building Construction. Together with the Safety Act, these instruments impose obligations on employers including: duties on managers, the requirement to establish safety and health committees in certain circumstances, duties to provide personal protective equipment (**PPE**), obligations with respect to the application of an OHS Safety Management System, an obligation to provide occupation accident security, first aid obligations, pre-employment safety obligations including health checks, obligations in relation to workplace conditions and accident reporting requirements.

The Safety Act is also supplemented by a number of Presidential and Ministerial decrees. The coverage of these decrees includes provisions concerning safety and health in relation to specific work place hazards such as pesticides, radiation, fire, pressure vessels, construction, electrical installation and logging.

The Directorate-General of Industrial Relations and Labour Standards of MOMT is responsible for enforcement of occupational safety and health, and labour standards legislation. MOMT has regional offices and district offices, which have an enforcement function for OHS legislation.

A Worker's Social Security Program known as Jamsostek was established in 1978 as the principal social security scheme. The health fund of the scheme is now managed by Health Social Security Executive Agency or *Badan Penyelenggara Jaminan Sosial Kesehatan* (***BPJSK***); while all other funds are managed by the Manpower Social Security Executive Agency or *Badan Penyelenggara Jaminan Sosial Kesehatan* (***BPJSTK***).

10

Intellectual property

10.1 Overview

Indonesia is a signatory to the Trade Related Aspects of Intellectual Property Rights Agreement (***TRIPS***), a schedule to the General Agreement on Tariffs and Trade Agreement (***GATT***) of the WTO. Indonesia has also ratified the Paris Convention for Protection of Intellectual Property and the Convention Establishing the World Intellectual Property Organisation (the ***WIPO Convention***). Following ratification of these conventions, Indonesia passed several legislative instruments to improve its compliance with TRIPS, the Paris Convention and the WIPO Convention.

IP rights registrable in Indonesia include patents, trademarks, designs and copyright. Registration is the basis upon which intellectual property rights in Indonesia are typically claimed. Foreign businesses that do not have a place of business in Indonesia must lodge IP applications through an Indonesian IP attorney or agent.

The government body responsible for the administration, registration and enforcement of IP rights is the Directorate General of Intellectual Property Rights (*Direktorat Jenderal Hak Atas Kekayaan Intelektual)* *(*the ***DGIP***). The DGIP website (www.dgip.go.id) provides a searchable database for patents, trademarks, designs and copyright registrations.

The cost of filing applications for IP rights is relatively low. However, the process leading to registration can be slow, and may take up to two years from the initial filing of an application until the issuance of a certificate of registration. Dispute settlement procedures, including litigation, tend to be heard comparatively quickly, due to IP pre-hearing procedures, which significantly reduce time and costs. However, filing of evidence in litigation can be expensive, as courts require original evidence or the legalisation of copies by a notary public.

While the laws regulating IP rights in Indonesia are fairly comprehensive, the IP regime suffers from a lack of robust enforcement. The impediments to effective enforcement of intellectual property in Indonesia are significant. One contributing factor is that Indonesia's IP laws are not widely publicised. As a consequence, infringing parties are frequently unaware of the legal implications of their actions.

In practice, however, infringement cases can often be resolved without resorting to legal proceedings. For example, infringements can sometimes be remedied by a 'cease and desist' letter and/or by following up with a notice published in newspapers concerning the intellectual property owner's intention to take further enforcement action. Formal enforcement of intellectual property rights is provided through the Commercial Court.

Remedies available in IP infringement actions brought through civil action in the Commercial Court include compensation for damages, and interlocutory injunctions to stop the infringing actions. The Commercial Court can order both of these remedies together.

Indonesia is currently in the process of updating many of its IP laws, so do contact us for advice on any recent changes.

10.2 Trade marks

The regime regulating the application, registration and enforcement of trademarks is set out in Trademark Law No.15 of 2001 (the ***Trademark Law***). Indonesia utilises a 'first-to-file' rule for obtaining trade mark rights. In a practical sense, this means that the first person to file a trademark application in Indonesia will generally have priority over the prior use of an identical or substantially similar mark. Trade marks filed for registration must be both filed in good faith and not be similar to, or identical with, prior trade mark registrations in the name of other parties for the same kinds of goods or services. By incorporating the 'good faith' criterion, the Trademark Law prevents the registration in Indonesia of trademarks that are registered and 'well-known' in foreign jurisdictions, in cases where the applicant is acting in 'bad faith'.

It is necessary to register trade marks in Indonesia: the Trademark Law does not provide any protection for unregistered trademarks. The period of protection for a registered trade mark is 10 years from the filing date. Trade mark registrations are renewable. Trade mark assignments must be in writing, confirming that the trade mark to be assigned will be used for the trade of goods and services. Trade mark registrations may be removed from the trade mark register for non-use if they are not used during a period of three or more consecutive years after registration. Additionally, the Trademark Law requires trade mark licences to be registered. The DGIP registers all trademarks and licences.

A summary of the application process for trademarks is set out in the following paragraphs.

Within 30 days of the filing date, the DGIP starts a substantive examination of the application, to decide whether the application should be put forward for registration or rejection. In principle, the examination should be completed within nine months but, in practice, it usually takes longer.

If the application is put forward for registration, it enters a three-month publication period. During the publication period, other parties can file oppositions to registration of the trademark.

If there is any opposition or rebuttal during the publication period, the Trademark Office re-examines the application. If, on re-examination, the Trademark Office decides that the trade mark is rejected, the Trademark Office writes to the applicant, outlining the grounds for rejection.

Appeal proceedings must be brought to the Mark Appeal Commission. If the Mark Appeal Commission accepts the appeal, the application is published. If the appeal is rejected, the applicant can challenge the Mark Appeal Commission's decision at the Commercial Court within three months of the date of receipt of the decision.

It is worth noting that the DGIP accepts applications for trademarks with 'priority rights' where the trademark has been registered in another country under the Paris Convention and the GATT. A priority application must be submitted within six months of the filing date of the application for registration of the trademark in the other country.

As is the case in many jurisdictions, the DGIP can reject the registration of a trade mark on a number of grounds, including that the trademark is not filed in good faith, is too simplistic, is in the public domain, describes the goods or services filed for registration, constitutes the name of a famous person, resembles an official seal of a state or international institution or that the trademark is not sufficiently distinguishable from prior registered trademarks. A trademark can also be rejected by the DGIP for 'contravening laws in force, religious morality, decency or public order'. Third parties can oppose a trade mark application on the same grounds that the Trademark Office can refuse to register a trade mark.

The Commercial Court deals with civil trade mark infringement matters. The District Court handles any potential criminal actions involving trade mark infringement issues. In recent years, harsher penalties have been imposed for trade mark infringement. In addition to formal litigation, the Trademark Law provides for alternative dispute resolution, including arbitration.

Interestingly, there is a designated team on the police force mandated with investigating trademark infringement complaints. Foreign enterprises operating in Indonesia should familiarise themselves with how police operate in Indonesia when seeking to enforce IP rights in the archipelago. Since April 2011, IP owners in Indonesia have another enforcement avenue available to them in addition to conventional police raids: enforcement through the Directorate of Investigation at the Directorate General of Intellectual Property (***PPNS***). The results of the PPNS investigation activities are reportedly promising, particularly in terms of relative efficiency. It remains to be seen whether the promising work of the PPNS will continue in the long term.

Indonesia's Customs authorities provide cross-border measures for the protection of trade marks.

10.3 Copyright

The Indonesian copyright system is set out in the Copyright Law No.19 of 2002, which came into effect in July 2003 (the ***Copyright Law***). Indonesia has also ratified the Bern Convention for Protection of Literary and Artistic Works (under Presidential Degree no.18/1997) and the WIPO Copyrights Treaty (under Presidential Degree no. 19/1997).

To receive copyright protection a work must be fixed (ie have a material form) and must be in the field of science, arts or literature. While the registration of copyright is available in Indonesia under the Copyright Law, it is not mandatory. In light of the enforcement issues encountered in Indonesia with respect to IP generally (typically exacerbated in the case of copyright), copyright registration is recommended.

When copyright protection starts and how long it lasts depends on the type of work.

- Books and other written works, speeches, visual aids for educational and scientific purposes (ie any two- or three-dimensional works that are related to biology or other sciences), songs and music, performances such as drama and dance, fine arts, architectural work, maps, batik and translations: the period of protection lasts as long as the creator lives plus 50 years (or, for a legal entity, 50 years from first publication).
- Databases, photography, typographical arrangements, computer programs, cinematography and works resulting from adaptations: the period of protection is 50 years from first publication for natural persons and legal entities.
- Shows and performances: the period of protection is 50 years from the first performance.
- Sound recording works: the period of protection is 50 years from completion of the first sound recording.
- Broadcasting works: the period of protection is 20 years from the first broadcast.

A civil action based on copyright infringement (eg unauthorised use or modification of a copyright work) is addressed to the Commercial Court. As in most jurisdictions, defences to copyright infringement in Indonesia include demonstrating that the work published or reproduced is not copyrightable or is in the public domain.

10.4 Patents

Under the Patent Law No 14 of 2001 (the ***Patent Law***) there are two forms of patent protection available to be registered in Indonesia:

> patents that have a 20-year term; and

> simple patents that have a 10-year term and have a lower inventiveness threshold.

Both patents and simple patents are non-renewable. Holders of a patent have the right to license patents for use by other parties. Any such licence must be registered with the DGIP and announced in the Official Gazette on Patents.

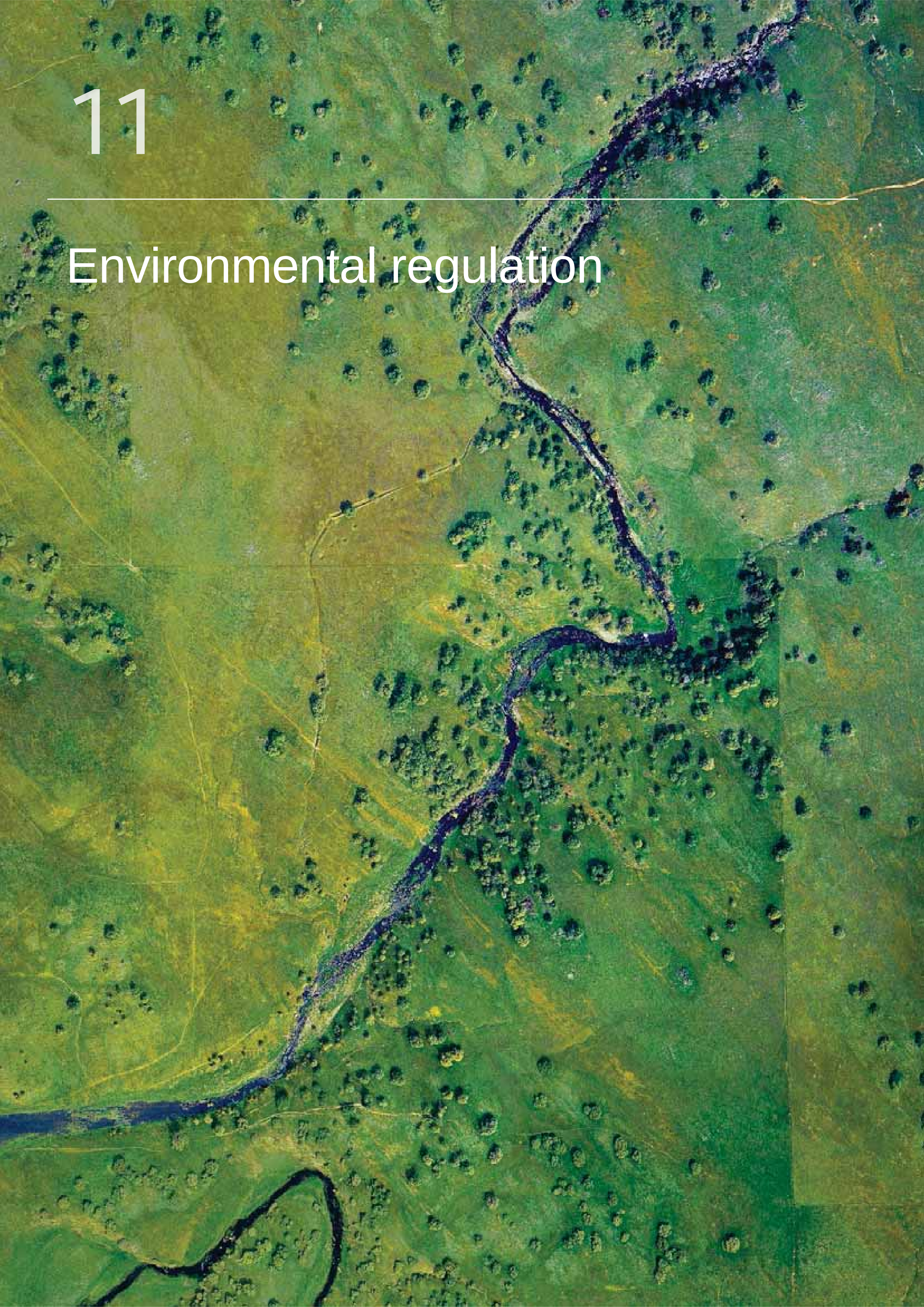
Certain types of subject matter cannot be patented in Indonesia, including inventions regarding living things (defined as consisting of ‘human beings, animals, or plants’) on the basis that to grant a patent would be in violation of religious morality, ethics and decency.

10.5 Other IP protection

Other forms of intellectual property regulated under Indonesian law include designs, plant varieties, domain names, trade secrets and industrial designs.

11

Environmental regulation



11.1 General

The relevant law in relation to environmental regulation is contained in Law No.32 of 2009 on Environmental Protection and Management and its supplementary regulations.

In Indonesia, every business and/or activity that may give rise to significant environmental impacts must prepare an environmental impact analysis (***AMDAL***). The AMDAL document is reviewed by an AMDAL appraisal commission and, based on the commission's recommendation, the Minister, Governors or Regents/Mayors decides on the environmental feasibility or infeasibility of the business and/or activity. Every business and/or activity that is not required to prepare an AMDAL must have an environmental management and monitoring program (***UKL-UPL***). Governors or Regents/Mayors are required to stipulate the kinds of businesses and/or activities that must have a UKL-UPL. Businesses and/activities not required to have either an AMDAL or a UKL-UPL are obliged to prepare a statement of readiness to manage and monitor the environment.

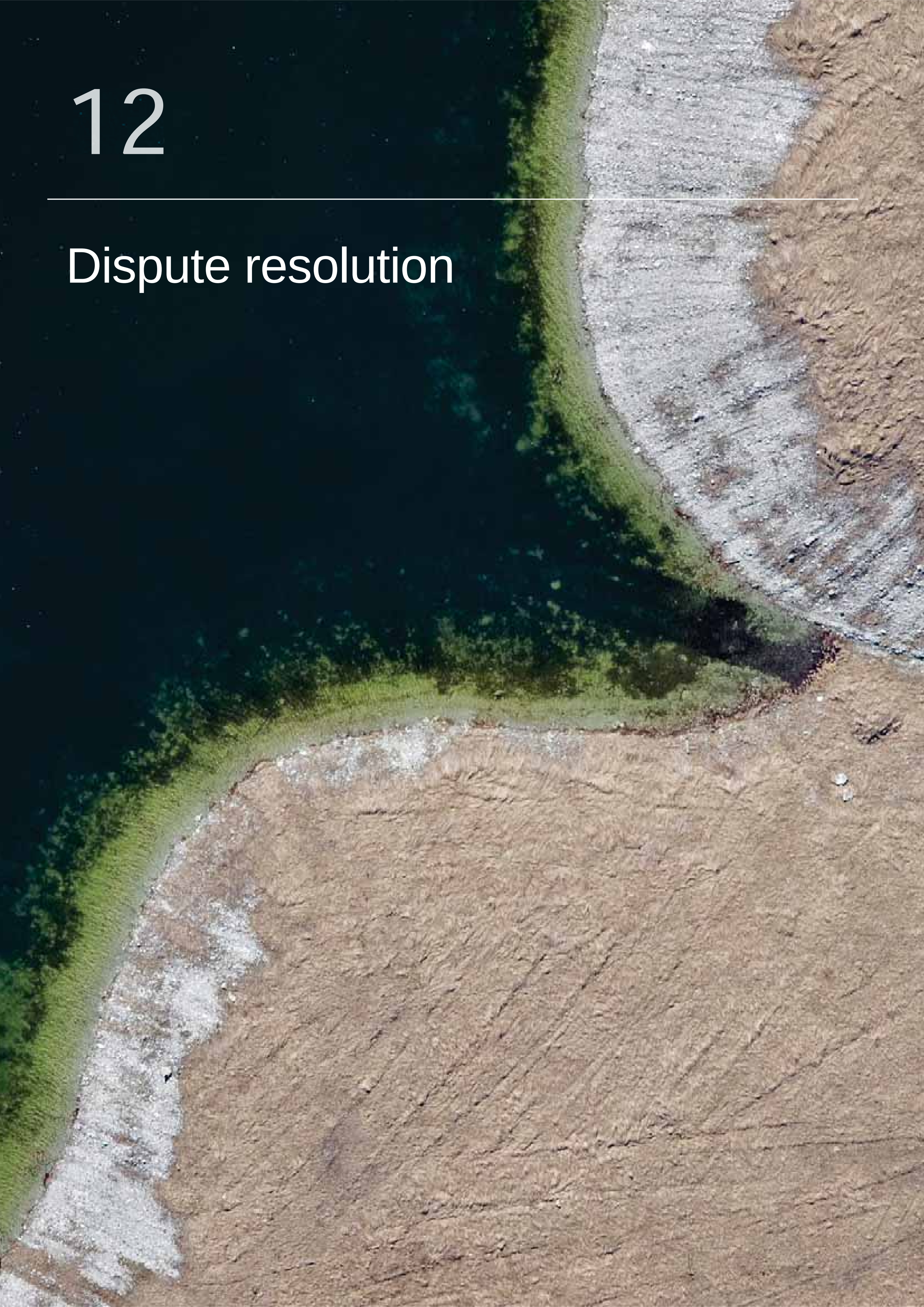
Every business or activity that is required to obtain an AMDAL or UKL-UPL is required to hold an environmental licence. An environmental licence will only be issued by the Minister of Environment/ Governor/Regent/Mayor after receiving or reviewing an AMDAL or UKL-UPL recommendation. In this respect, a decision on the environmental feasibility of a business and/or activity is the basis of the issuance of an environmental licence. Environmental licences are a pre-condition to the acquisition of activity or business licences from different Ministries. The elucidation of this provision states that a business and/or activity licence includes a licence with another name, such as an operating permit and construction permit. If an environmental licence is revoked, all licences subsequently obtained as a result of the environmental licence, such as any activity or business licences, will also be revoked.

11.2 Mining

IUP and IUPK holders must carry out reclamation and post-mining activities, and are required to allocate funds in stages for the recovery of the location that fulfils the standard of environmental worthiness. The minimal obligations regarding reclamation are contained in the Mining Law for IUP and IUPK holders (see Articles 79, 96, 99 and 100 of the Mining Law). Similar obligations would generally also be contained in the IUP/IUPK permits. The preparation of reclamation and post-mining plans must be approved by the Minister, Governor or Regent/Mayor at the time of applying for IUP or IUPK for operational production. IUP and IUPK holders must also provide security deposits for reclamation and post-mining activities, which the Government may use to appoint third parties to conduct reclamation if the holder of IUP/IUPK does not conduct reclamation and post-mining activities in accordance with its plan. Small mining permit holders have an obligation to manage the environment, including also reclamation and post-mining plans.

12

Dispute resolution



In any international investment, the choice of dispute resolution forum and governing law is important to ensure the certainty, stability and enforceability of contractual rights and obligations. Foreign investors in Indonesia often find themselves negotiating with their Indonesian partners and counter-parties over:

> the choice of either Indonesian courts, Indonesian arbitration or international arbitration as the forum for resolution of any disputes arising in relation to their investment; and

> the choice of either Indonesian law or foreign law as the governing law of their contract.

Under Indonesian law, parties can always choose Indonesian law and Indonesian law in their contracts. This is, in fact, the default position. In addition, where the relationship is a commercial one, parties can opt to arbitrate under foreign law or submit to international arbitration. However, the choice of foreign law or international arbitration can be problematic.

Making the 'right' choice will depend on the particular circumstances of each individual contract, and it is important to understand the advantages and risks posed by each possible choice, as well as any mandatory Indonesian rules that may impact on the available choices.

12.1 Foreign judgments

Indonesia is not currently a party to any international convention for the enforcement of foreign court judgments. As a result, foreign judgments are not enforceable in Indonesia. A judgment of a foreign court made against an Indonesian company would only be enforceable against that company to the extent that the company has assets in the jurisdiction in which the judgment was handed down.

12.2 Choice of law

If the parties to an agreement elect non-Indonesian law, then that choice of law should be honoured by the Indonesian courts under the principle of freedom of contract, embodied in Article 1338(1) of the Indonesian Civil Code. Notwithstanding this, the courts may nevertheless apply the laws of Indonesia. In light of this, the most practical choice of law and jurisdiction in agreements with Indonesian parties and Indonesian subject matter may well be the laws and courts of Indonesia. If a contract does not stipulate a choice of law, Indonesian law will apply in proceedings in Indonesian courts.

12.3 Language requirements

In 2013 an Indonesian party pleaded to the West Jakarta District Court, an Indonesian court of first instance, that a loan agreement entered into with a foreign company should be nullified on the basis that it violated Article 31 of Indonesia's Law No 24 of 2009 concerning Flag, Language and Symbol of State and National Anthem. The loan agreement was governed by Indonesian law, but was written in the English language. The court ruled that the loan agreement was void by operation of law because it was in the English language only, as opposed to Bahasa Indonesia, and it therefore violated Law No 24.

The Ruling, which was dated 20 June 2013 but was only made available to the public several months later, took the Indonesian legal market by surprise and raised concerns among foreign investors and lenders.

Article 31 of Law 24 provides that, with effect from 9 July 2009:

a) Bahasa Indonesia must be used in a memorandum of understanding or an agreement involving a state institution, a government institution of Indonesia, an Indonesian private institution or an Indonesian citizen.

b) A memorandum of understanding or agreement as referred to in paragraph (1) which involves a foreign party, is also to be drawn up in the national language of the foreign party and/or in English.

Law 24 does not identify the consequences of a failure to comply with Article 31. Furthermore, Law 24 required the Government to issue an implementing regulation within 24 months setting out further details, and it was hoped that this would clarify the extent and impact of the law's requirements. To date, this implementing regulation has not been issued.

Although the case in question is arguably of limited jurisprudential value, as it is currently being appealed to the Jakarta High Court, it is possible that other courts may nevertheless decide to follow the same analysis as the West Jakarta District Court. Additionally, it may indicate how the Indonesian judicial system is likely to react to the issue.

There are two ways sign to an agreement in more than one language:

a) Dual Language Execution: An agreement may be drafted and executed in both English and Bahasa Indonesia. However, in practice, it is often very difficult to negotiate and finalise both versions simultaneously (especially for lengthy, complex or highly technical documents), particularly when facing tight timelines. This would also require both versions to be negotiated and translated/updated on an ongoing basis, which would almost certainly cause parties to incur significantly higher costs.

b) Translation Following Signing: Alternatively, the agreement may be drafted and executed in English, but include a provision requiring the parties to commission and execute an Indonesian language translation, either within a specified time period (eg within 30 to 90 days after the English version is executed) or simply as and when such translation is requested by a party or is required for any purpose (eg for admission as evidence in court proceedings) .

Typically, parties agree that the foreign language version (usually English) will prevail to the extent of any inconsistency between the two versions. This appears to be permissible, as there is no specific prohibition in Law 24.

The ruling has not helped to clarify the significant degree of uncertainty that already existed on this topic; it has, unfortunately, fuelled more uncertainty, affected investor confidence and created much chatter within the legal community as regards to whether the Ruling had been properly made as a matter of Indonesian law and how the ambiguity inherent in Law 24 (and lack of implementing regulations) may be used to the disadvantage of foreign parties. Until the appeals process is completed on this case, or much needed clarifications are made to Law 24, there can be no clear-cut 'yes' or 'no' responses to the many questions surrounding this language issue.

It is essential to conduct a risk assessment on a case-by-case basis when considering the choice of language in agreements with Indonesian parties. Generally, where an agreement is perceived to have a higher degree of risk, parties would aim for Dual Language Execution, and the opposite would apply where it is perceived to have a lower degree of risk. Factors to consider in the risk assessment include the nature of the agreement, governing law, dispute resolution mechanism, identity of Indonesian counterparty, and whether the contract would likely require any performance or enforcement in Indonesia.

While the most conservative approach would be to employ Dual Language Execution for each agreement, as noted above, this has significant cost implications; is often difficult to achieve in practice, given tight timelines and complexity of documents; and parties often take comfort that commissioning a translation shortly after signing a non-Bahasa Indonesia version is sufficient to satisfy compliance with Law 24. There may also be delays in securing translation services, since the market has been reacting to the Ruling and commissioning more translations.

12.4 Arbitration

As an alternative to Indonesian law and jurisdiction, it is possible to draft commercial agreements to state that the laws of Indonesia govern the agreement, but that any disputes that arise are to be referred exclusively to foreign arbitration and may not be referred to Indonesian courts for resolution.

Arbitration is an increasingly popular method of dispute resolution in Indonesia. The principal source of the law of arbitration in Indonesia is Law No.30 of 1999 concerning Arbitration and Alternative Dispute Resolution (the ***Arbitration Law***). The Arbitration Law was created to reduce the intervention of courts, to reduce the judicial burden and to ensure the finality and enforceability of arbitral awards. The Arbitration Law does not follow the United Nations Commission on International Trade Law (UNCITRAL) Model Law.

Indonesia is a signatory to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the ***New York Convention***) and has exercised the reciprocity and commerciality reservations.

The key arbitral institutions in Indonesia are:

> the Indonesian National Board of Arbitration (*Badan Arbitrase Nasional Indonesia*) (***BANI***);

> the Indonesian Capital Market Arbitration Board (*Badan Arbitrase Pasar Modal Indonesia*) (***BAPMI***); and

> the Shariah National Arbitration Body (*Badan Arbitrase Shariah Nasionah*) (***BASYARNAS***).

Under the Arbitration Law, any legal entity may become a party to arbitration proceedings. The parties in dispute initiate arbitration proceedings based on an arbitration agreement made in writing.

12.5 Tribunal selection

The Arbitration Law provides for circumstances where the parties agree to appoint a single arbitrator or two arbitrators, with the authority to appoint the third. However, nothing in the Arbitration Law expressly prohibits the parties from arranging a tribunal with an alternative composition.

12.6 Domestic arbitral awards

In the context of domestic arbitrations, the Arbitration Law stipulates that any arbitral award is final and binding on the parties to the dispute, and therefore no appeal against the award may be filed. The arbitrator, or their representative, must subsequently submit and register the award with the relevant District Court. If the unsuccessful party refuses to comply with the award, the winning party may request the Chief Judge of the District Court to issue an enforcement order. In order to issue the instruction, the Chief Judge must:

- review the arbitration agreement;
- determine whether or not the nature of the dispute is a commercial law issue (which includes trading, banking, finance, capital investment, industry and intellectual property rights); and
- determine that the award is not contrary to ethics and Indonesian public policy.

The District Court Head must issue its decision on the enforcement request within 30 days after the request is submitted.

12.7 Foreign arbitral awards

As with domestic arbitral awards, the enforcement procedure for foreign arbitral awards begins with award registration at the office of the relevant District Court. Under the Arbitration Law, a foreign arbitral award may only be enforced after the Indonesian court has recognised the award through the issue of 'exequatur'. The District Court of Central Jakarta has jurisdiction to issue exequatur to enforce foreign arbitral awards in Indonesia (except where the Republic of Indonesia is a party to the arbitrated dispute).

The court must grant an exequatur to enforce the award unless:

- the award is rendered in a state that is not bound by a bilateral or multilateral convention or treaty on the recognition and enforcement of foreign arbitral awards, under which Indonesia is bound;
- the legal relationship on which the award was based cannot be considered as commercial under Indonesian law; or
- enforcement of the award would be contrary to public policy.

A foreign arbitral award that has received an exequatur becomes enforceable. If the losing party does not voluntarily fulfil its obligations under the exequatur, the partying seeking to enforce the order may request the Chief Judge of the District Court to issue an enforcement order (a writ of execution).

While a sufficient regulatory framework exists with respect to arbitral awards, in practice, parties seeking to enforce arbitral awards face a number of challenges. Judgments of Indonesian courts on the validity of arbitration agreements and the enforcement of the foreign arbitral awards tend to vary from one case to the next.

12.8 Arbitral rules

BANI has published its Rules of Arbitral Procedure. Parties to a dispute may, however, choose ad hoc or institutional arbitration, subject to such rules as may be agreed between the parties. It is also open to the parties to agree modifications in writing to the BANI rules, provided that any such modifications do not contravene mandatory provisions of Arbitration Law or BANI policies.

12.9 Enforcement issues

Historically, Indonesian law did not address a range of issues that often arose during arbitration proceedings. This led to scrutiny by foreign investors. In this respect, the Arbitration Law is a significant step towards Indonesia adopting a 'pro-arbitration' legal mindset. As noted, while, in theory, foreign arbitral awards are now enforceable in Indonesia, in practice, those seeking to enforce foreign arbitral awards continue to face significant legal and practical challenges.

13

Bankruptcy

13.1 Bankruptcy

The law on bankruptcy is set out in Law Number 37 of 2004 on Bankruptcy and Postponement of Debt Payment (the ***Bankruptcy Law***). The Bankruptcy Law applies to individuals and corporations.

An individual or corporation is considered insolvent when it has two or more creditors and fails to pay at least one debt when it falls due. Once an enterprise or individual fails to pay at least one of its due debts, any one or more of its creditors, the public prosecutor, or the individual or enterprise itself, may file a bankruptcy petition with the court. In the case of a debtor that is a bank, a bankruptcy petition may only be filed by Bank Indonesia.

Pending a decision on the bankruptcy petition, any creditor may file a petition to the court to appoint a liquidator to manage and liquidate the assets of the debtor under supervision of a judge. The consequences of a declaration of bankruptcy include the recovery of the total wealth of the bankrupt debtor, together with any further wealth they acquire during bankruptcy; the bankrupt debtor forfeiting their right to control and manage their assets from the date an individual or enterprise is declared bankrupt; and the liquidation of the enterprise or individual's assets. On the liquidation of an enterprise, secured creditors broadly receive priority in payment from the proceeds of the sale of assets over which they have security. A creditor who has the right to retain goods owned by the debtor does not lose this right following a bankruptcy declaration.

Legal acts undertaken by the debtor before the declaration of bankruptcy may be annulled if it is proven that at the time of the legal act, the debtor and the other party with whom the debtor engaged in the legal act realised, or should have realised, that such an act would adversely affect creditors of the debtor. The Bankruptcy Law also deems the debtor and the other person to hold this realisation for certain acts committed within one year before the bankruptcy. Any person who has received payment or property from a legal act that has been annulled must return it.

13.2 Directors

In Indonesia, there is no specific law on the liability of directors in the event of insolvency of a company. However, each member of the board of directors of a company is individually responsible, if he or she has committed a wrongful act, or is negligent in conducting the director's duties with good faith and with full responsibility for the interests and business of the company, which may be broad enough to cover the conduct of insolvent trading.

In addition, where the bankruptcy of the company occurs due to the fault or negligence of the board of directors and the company's assets are insufficient to cover losses incurred as a result of such bankruptcy, every member of the board of directors is collectively responsible for the company's liabilities that are not settled by the bankruptcy assets. The liability applies to all members of the board of directors of the company within a period of five years before the date of bankruptcy of the company.

14

Trading

14.1 Overview

Foreign investors generally have the right to import any goods, provided that the imported good does not violate the law governing ‘merchandise trade’ and provided the goods have no negative impact on the safety, security, health, environment and morals of the nation. Certain products, however, are restricted for trading whether by locally owned companies or foreign-owned companies. As Indonesia is a member of the Association of South East Asian Nations (***ASEAN***), preferential rates are applied to imports to Indonesia from other ASEAN members.

To encourage export from Indonesia, the Indonesian Government offers incentives to investors operating in bonded zones throughout Indonesia (the largest being the bonded zone of the Batam Island Industrial Area). The Value Added Tax and Sales Tax on Luxury Goods are not imposed on the import of goods to investors in bonded zones who are producing taxable goods for export, provided that those goods themselves are not used to produce taxable goods for export.

14.2 Import restrictions

A General Import Licence (***API-U***) or the Producer Import Licence (***API-P***) is required before importation. The API-U permits trade of the imported product to third parties; whereas the API-P allows importation of products, such as raw materials, for the holder’s use only (ie in production) and does not allow trade to third parties, including to related parties of the licence holder. A company may only hold one of these licences.

Certain goods are also subject to strict import quotas. The importer must declare all goods imported into Indonesia to the Indonesian Directorate General of Customs and Excise, and be registered with a Customs Identification Number.

Goods restricted for trading include:

- narcotics;
- explosives, including fireworks;
- arms and ammunitions;
- defined books and printed materials, audio and visual recording media; and
- certain species of flora and fauna.

Foreign companies that are based outside Indonesia but wish to sell their products in Indonesia must, under Ministry of Trade Regulation No. 36/1977, appoint an Indonesian import agent or distributor.

Apart from the importation of motor vehicles, which attract high import duty, most imported products attract import duties in the range of 5 to 20 per cent. Preferential tariff rates are applied to imports from other members of the Association of South East Asian Nations (currently Brunei, Burma (Myanmar), Cambodia, Indonesia, Laos, Malaysia, Philippines, Singapore, Thailand and Vietnam). Under the ASEAN Free Trade Area, ASEAN aims to become a free trade area by 2015, with no tariff and non-tariff barriers on cross-border transactions between ASEAN countries.

Some goods are exempt from import duty, including goods for representatives of foreign countries, and international bodies and their officials who work in Indonesia. New foreign investors (or expanding businesses) are also granted relief from import duty on capital goods and raw materials and components for production.

The use of labels in Bahasa Indonesia is also mandatory for all types of imported goods.

14.3 Export restrictions

Indonesia restricts the exportation of certain animal and plant products. Some categories of rubber are prohibited from being exported; while some commodities (eg flour, palm oil and certain metals) may only be exported if domestic demand is met. Some commodities are subject to export tax also. The most recent export to be regulated is the exportation of unprocessed ore. New export taxes have also been imposed on copper, iron, ilmenite, titanium, manganese, lead and zinc concentrates (see section 4.5 for more information).

Australia and Indonesia are parties to the ASEAN, Australia, New Zealand Free Trade Agreement (the ***AANZFTA***), which came into force on 1 January 2010. Under the AANZFTA, a number of tariffs have been eliminated for exports to Indonesia of certain products, including pasta, a range of seafood, and most copper and lead products.

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Assisting your Investment in Indonesia

Investing in any foreign country is a complex and challenging process. We regularly advise clients not only on their strict legal requirements, but also on the practical steps they need to take to avoid the pitfalls and risks that arise when investing in Indonesia. Please speak to one of our experts to discuss your investment needs. We are committed to helping our clients succeed in Indonesia.

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