



Indonesia:
Essential tips for successful investment

C L I F F O R D
C H A N C E

LWP



Indonesia: Essential tips for successful investment

Indonesia offers great opportunities for foreign investors. It has the fourth largest population in the world (over 250 million people) and a rising middle class which is driving huge domestic demand. It has a wealth of natural resources and is currently the 16th largest economy globally and, according to McKinsey, is on track to become the world's 7th largest economy by 2030.

Here are our top legal tips for successfully investing in Indonesia.

Relationships are key

Establishing and maintaining relationships is at the heart of doing business in Indonesia. Decisions made by Indonesian partners can be influenced by the strength of business relationships. It is therefore important to invest the time and effort to build trust and a rapport with your proposed Indonesian partner.

The importance of due diligence

You should conduct a comprehensive due diligence exercise to understand and evaluate the risks associated with the target and/or your proposed Indonesian partner. Some of the risks include legal and regulatory challenges, corruption and bribery risks, the availability of skilled labour and the enforceability of contractual rights. You should also be mindful of the history of your proposed Indonesian partner's other joint venture relationships, which could provide a useful insight into the way in which it does business.

Foreign investment restrictions

Differing levels of foreign investment are permitted in Indonesia depending on the relevant industry. A list of the industries with foreign ownership restrictions is set out in the "negative list" issued by the Indonesian government. This list is updated periodically with the latest negative list being issued in 2014. All acquisitions by a foreign investor of shares in a private Indonesian company (other than a bank and financial institution) must be approved by the Indonesian Investment Coordinating Board (**BKPM**). It is therefore important to consider the maximum foreign ownership in the industry of interest at an early stage when structuring your investment in Indonesia.

Regulation of specific industries

As in other countries, Indonesia has specific regulatory regimes for certain industries, including banking and finance, insurance, telecommunications, mining and oil and gas. The specific industry regulatory regimes may impose additional obligations on foreign investors, including capital requirements and divestiture obligations. For example, the mining industry has undergone, and is still in the process of undergoing, significant regulatory change, including the introduction of more onerous divestiture obligations for foreign investors.

If you are considering investing in one of the Indonesian industries mentioned above, you should seek up to date advice given the ever changing and volatile regulatory environment in these industries.

Merger control

The Indonesian Anti-Monopoly Law and implementing regulations contain merger control provisions. If a merger, consolidation or acquisition results in the asset or turnover value of the involved parties (target and acquirer/controller, including the ultimate shareholder and all subsidiaries) in Indonesia exceeding certain thresholds, then the relevant parties must notify the Business Competition Supervisory Commission (the **KPPU**) of the merger, consolidation or acquisition within 30 business days of completion of the transaction. It is now possible to hold a voluntary consultation with the KKPU pre-completion, but this does not negate the requirement to make a post-completion filing. In assessing a transaction, the KPPU's main objective is to ensure that the transaction does not cause monopolistic or unfair competition practices. You should conduct an early analysis of the value of the involved parties assets and turnover in Indonesia to determine if a notification filing will need to be made or a pre-completion voluntary consultation sought.

Employment

The Indonesian Manpower Law allows an employee to terminate his or her employment upon the change of ownership of a company, and claim a termination payment which consists of severance payment, long service payment and compensation. The amount of severance payment depends on the number of years of employment and is based on the last monthly salary. This could give rise to significant cost implications, particularly if the target has a large and/or long-serving workforce. You will need to manage this risk through an effective communication campaign and, possibly, the payment of retention bonuses. You could also negotiate indemnities for such termination costs or walk-away rights in the event of a mass resignation, but these remedies are less common in practice.

Mandatory announcements – change of control

If the proposed transaction results in a change of control of an Indonesian company (the transfer of more than 50% of the shares in that company), Indonesian company law requires the transaction to be announced in one daily newspaper (for the benefit of the target's creditors) and to the target's employees at least 30 days before the shareholders meeting to approve the transaction. Any issues raised will need to be "settled" before the transaction can complete. You should be aware of the impact on the timing and cost of the transaction that such mandatory notifications pose.

Mandatory tender offer

The acquisition of "control" of a publicly listed company in Indonesia will trigger a mandatory tender offer (**MTO**) where the acquirer must make an offer to acquire all remaining shares of the listed company owned by the public at a price which is the higher of the price paid for the controlling stake and the average of the highest traded price in the 90 days before the MTO announcement. "Control" is defined as more than 50% of the voting shares of a public company or the ability to determine the management or policies of the public company. If you are considering acquiring "control" of a publicly listed company, you will need to consider the potentially significant financial obligations that may be incurred with the MTO.

Good faith obligations

The Indonesian Civil Code implies a general duty on contract parties to act reasonably and in good faith. This requirement may impact whether or not and to what extent a party may be able to exercise its contractual rights and what the parties can expect from each other. For instance, a seller may be required to make a disclosure of a matter which it knows

to be of importance to a buyer even if the buyer does not make inquiries. Failure to do so may lead to a claim or suspension or termination. Importantly, good faith obligations apply even prior to signing of contracts. Once the essential components of a contract have been agreed, even if only verbally, the parties may have a binding agreement in place. If this is not intended, the parties must make clear to each other – in writing and in their actions – that no binding agreement may be inferred unless and until a definitive contract has been signed by both parties. This is of particular importance in the term sheet phase as a term sheet may constitute a binding agreement. Clear drafting reduces the risk that parties have a different understanding of the nature or scope of their expectations and intentions.

Bribery and corruption

While Indonesia is typically awarded a low score by Transparency International, its ranking in the corruption perception index is improving year-on-year. The local corruption bureau has been active in combating graft, however the decentralisation of government decision making processes has increased the risk of bribery and corruption. With more governments around the world enforcing anti-bribery laws, you should take the time to understand the local practices of the target and/or your Indonesian partner, and review their anti-corruption and sanctions compliance programs, or establish such programs if none exist.

Enforcement

Foreign court judgments cannot be directly enforced in Indonesia, so the relevant dispute would have to be adjudicated by the Indonesian courts. In relation to arbitration, Indonesia is party to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, so a foreign arbitral award from a jurisdiction which is also party to the New York Convention should be recognised in Indonesia, provided that the arbitral award meets the requirements set out in the Indonesian Arbitration Law, including that it does not offend public order and morality. If you require dispute resolution outside Indonesia, you should choose arbitration over court proceedings. Given that foreign investors have had difficulties enforcing against assets in Indonesia in the past, when dealing with an Indonesian counterparty, you may also want to consider seeking suitable security outside Indonesia or, possibly, agreeing with your Indonesian partner a retention of funds to cover, for example, any breaches of representation, warranty or indemnity contained within your investment documents.

Contacts



Linda Widyati

Partner

T: +62 21 2988 8301

E: linda.widyati@cliffordchance.com



Jeroen Koster

Foreign Legal Consultant

T: +62 21 2988 8303

E: jeroen.koster@cliffordchance.com



Melissa Ng

Partner

T: +65 6410 2254

E: melissa.ng@cliffordchance.com



Simon Clinton

Partner

T: +65 6410 2269

E: simon.clinton@cliffordchance.com



Lee Taylor

Partner

T: +65 6410 2290

E: lee.taylor@cliffordchance.com



Dezi Kirana

Counsel

T: +65 6661 2081

E: dezi.kirana@cliffordchance.com

The ASEAN Economic Community

The ASEAN Economic Blueprint was adopted in November 2007 as the master plan guiding the establishment of the ASEAN Economic Community (AEC) by December 2015. The intention is to transform the region into an EU-style economic area that will increase cross-border trade and investment as well as the flow of capital and the movement of skilled labour. In 2013, ASEAN attracted USD122 billion, accounting for 8% of the global Foreign Direct Investment (FDI). This includes increasing investments from ASEAN Members States, which at 17% of the total FDI inflows, is now the third largest source of FDI in the region. As we move closer to the December 2015 milestone, we expect business interest in the AEC to continue to rise, as more businesses benefit from such ASEAN integration efforts.

Read our other publications

If you would like to receive copies of any of our other South East Asia investment guides, please email one of the contacts listed on this page:

Malaysia
The Philippines
Singapore

Thailand
Vietnam