

Foreign Ownership and Tax Laws of Indonesia

Land/Villa Ownership Options

For Indonesian buyers, property ownership is relatively straight forward. However, Indonesia is a complex foreign investment environment, so it's absolutely essential that a foreign buyer is familiar with the various purchase options and taxation consequences. Any buyer should engage competent and impartial legal counsel and an accounting specialist to advise on taxation matters.

Only Indonesian nationals may own freehold land in their own name (indeed even Indonesian companies may not own freehold land), but there are several trusted means for non-Indonesian nationals to acquire and control property in Bali.

There are essentially two types of property ownership:

1. Leasehold (Hak Sewa)
2. Freehold (Hak Milik).

The Hak Milik title can only be held in the name of an Indonesian citizen, however it is convertible to two forms of right of use title:

- a) Right of use (Hak Pakai)
- b) Corporate tenure (Hak Guna Bangunan or "HGB")

Indonesian buyers will generally only purchase Hak Milik title. For foreign buyers, it is usually clear which option is most appropriate once examining their reasons for purchasing.

1. Leasehold

Leasehold can be an attractive option for foreign buyers wishing to purchase an interest in a property that they can use for a specified period. You should be aware that a lease is only a temporary interest in the land. Once your lease term is up, the property – including any improvements you might have made to it – reverts to the owner of the underlying Hak Milik. The length of the lease is critical in terms of possessing a transferable asset that will appreciate with time and be attractive to anyone wishing to buy the lease if you decide to on-sell during the lease term.

A properly drafted lease will contain provisions for renewal of the lease, the stage of the lease that the renewal can be requested, and the price mechanism of the renewal. For example, the lease document should include whether you can opt to renew the lease at any time during the lease term, or whether this can only be done within a certain timeframe prior to the expiry of the initial term. Leases in Indonesia, whilst often formal documents prepared by a Notary, are not registered with the Indonesian Land Office as an encumbrance on the Hak Milik title and are thus considered a private agreement between two individuals. There are, however, strict laws protecting the interests of a lessee in land.

Leasehold interests in property are often more suited to those looking for a 'lifestyle' choice –as the asset itself is a limited right to the land for a limited period, and is not guaranteed to appreciate with time.

2. Freehold

Again, the Hak Milik title can only be held in the name of an Indonesian citizen and is the preferred title for Indonesian buyers. There are two forms of right of use titles attractive to foreign investors because of the direct link to the freehold title and which allow the benefit of an asset that can capitally appreciate.

a) Hak Pakai – “Right of Use”

A Hak Pakai, or Right of Use, is a mechanism specifically designed by the Indonesian government to allow foreign ownership of land. A Hak Pakai is a certificate that is granted by the Indonesian Land Office.

The Hak Pakai title is set for an initial period of 30 years, with rights of extension for 20 years and 30 years, totalling 80 years, with the condition that the owning party holds the relevant stay permit in Indonesia as a resident.

Taxes for the transaction granting the Hak Pakai will be assessed on the government assessed value of the freehold property ('NJOP').

This title is only suitable for properties with residential use.

HGB Title

This option for land ownership is only available for corporate ownership. Under this form of title, a foreign investment company is incorporated in Indonesia with approval of the Indonesian regulatory authorities. The freehold title to the land is relinquished to the state, and replaced for a set period (normally an initial term of 30 years, renewable) with the HGB title.

During the term of the HGB title, the company may deal with the land and build upon it. The company may also mortgage the land and this title is a form of ownership, registered with the Indonesian Land Office.

The difficult aspect of obtaining and maintaining HGB title is that the establishment of a foreign investment company is a detailed process, which may take up significant time and expense. The rationale behind allowing foreign companies ownership to land is to encourage commercial investment in Indonesia. Accordingly, to keep track of those investments, the Indonesian regulatory authorities impose stringent taxation and regulatory requirements and ongoing reporting obligations on foreign companies. There are also requirements for capital establishment and social responsibility of foreign investment companies. It is usually necessary for a foreign company with HGB title to retain the ongoing advice of legal and/or accounting specialists to assist with its corporate obligations.

The HGB title is suitable if a purchaser intends to operate a property as a business with rentals.

As in all countries, a purchaser should seek independent legal advice and consult with professional counsel to determine what is best for their personal or company circumstances.

Taxation

There are obviously taxation implications for the transfer of interests in property, building on land, and ongoing land tax obligations. The Indonesian government, like any other government, imposes taxation obligations on investors and it is therefore essential to obtain the advice of a qualified accountant. Here we do not intend to replace such advice but merely give a brief summary of some of the taxes that you may likely be liable for upon taking an interest in property in Indonesia such as Income Tax, Value Added Tax (Pajak Pertambahan Nilai or "PPN"), Stamp Duty and Levies, and Land and Building Tax.

Taxes on Leasehold

Non VAT-able leases in Indonesia are subject to PPH (Income Tax), which is charged at a minimum of 10% of the total amount paid. On a 25 or even a 40 year lease, this can be quite a large sum. The tax is payable as an income tax, and is accordingly assessable on the income of the party receiving the money – the Lessor. Leases may also be subject to PPN if the Lessor is an entity obliged to charge PPN. It is very important when preparing your lease documentation to ensure that, if the lease is not expressed as including an amount for PPH and PPN, then the obligation to pay any applicable taxes is clearly stated as belonging to the Lessor. Nominal stamp duty may be payable if the lease is prepared as a Notarial Deed.

Taxes on Transfer of Freehold

Taxes on a transfer of Hak Milik are payable on the Tax Object Acquisition Value ("NJOP") which is the higher of the amount paid for the property, and the NJOP, or pre-assessed government value of the land and any improvements on it. The tax rate is 7.5% of the NJOP and is incurred as 2.5% to the seller and 5% to the buyer. It is common for the Notary handling the transaction to retain certain amounts of the settlement proceeds, pending final assessment and payment of the taxes assessed on the transaction, to avoid the buyer being left after settlement with a tax liability higher than that anticipated, and contributed to by the seller.

This tax amount is payable on transfers for Hak Milik and HGB purchases of title. It is also payable for the creation or transfer of a Hak Pakai, or conversions of any of these titles, again assessed on the NJOP.

Land and Building Tax

Yearly taxes are payable as a proportion of the NJOP for both the land and any buildings erected on land. There is also a one-time tax on the construction of a building, which is generally assessable at 10% of the total cost of building if contractors are used. When entering into an agreement with a contractor to build, the agreement should clearly state which party is responsible for payment of the tax on the amounts paid pursuant to the contract. This rate of tax may be reduced to 4% of the total cost of building, which will only be allowed in the case of "Self-Building". Self-Building is very strictly interpreted by the tax office, and is only available where the person claiming the lower rate of tax can establish that they actually did build the property themselves, with proof such as logs and spreadsheets covering the costs accrued over the course of construction. When purchasing a property with buildings already established on the land, you should ensure to obtain proof of payment of this tax on the construction of the buildings. If a government assessor determines that the tax has not been paid, the liability rests with the current owner of the property – you – despite the fact that the property may have been on-sold any number of times since the buildings were constructed.

Taxes on Rentals

Taxes on rental properties, both commercial and retail, are payable as PB1 and as withholding taxes, and the taxation object (in most cases the owner of the asset) must be accountable for withholding and reporting obligations, even if the object is not a resident of Indonesia for taxation purposes.

Luxury Tax

Luxury tax may be payable in relation to certain land and building transactions and the applicability is subject to quite a complex range of regulations. You should discuss this in detail with your accountant and tax consultant as to what transactions and goods will be subject to Luxury Sales Tax when purchasing land or constructing buildings.

Foreign Investment - PMA (Penanaman Modal Asing)

We can help you set up an up-to-100% foreign-owned limited liability company (PT PMA) in Indonesia in 6-8 weeks.

A PT PMA is a legal entity that can be fully owned by foreigners. However, the maximum foreign ownership is determined by the business sector and business activities. The restrictions are listed in a regulation called the Indonesian Negative Investment List.

- A limited liability company is required to have at least two shareholders. Both private and corporate shareholders are allowed.
- At least one director and one commissioner – A commissioner is a non-executive role of overseeing the company's directors. The directors are responsible for the management of the company.
- Some business activities, such as the operation of restaurants or hotels, require special licenses.

With a PT PMA, you can officially start doing business in Indonesia and have the same rights and responsibilities as other local companies:

- Your company can join and participate in all tenders in Indonesia.
- You can apply for import and other business licenses, apply for product registration
- under your company and thus have better conditions for importing goods.
- You and your foreign employees can apply for KITAS – an Indonesian government
- permit/visa that allows foreign nationals to work or stay in Indonesia legally – under the
- name of your company.
- Your foreign clients and visitors can directly obtain a business visa sponsored by your
- company.
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The entire registration and establishment process, including all procedures (as shown below), takes from 6 to 8 weeks:

- Registering your company name
- Approval of company name at the Ministry of Law and Human Rights
- Preparation of Article of Association by Notary
- Obtaining Deed of Establishment at the Ministry of Law and Human Rights
- Receiving Certificate of Domicile at the local government office
- Obtaining Taxpayer registration number
- Receiving NIB (Registration Number)
- Obtaining Business License and/or Commercial License at OSS
- Identification number to operate/business licence/NIB
- Permanent domicile letter

We are here to help you set up your foreign company and manage its compliance.

You can start using your capital as soon as your company is registered. Some business lines require a sub-licence or certificate of eligibility before they can operate, we will advise you accordingly on your needs.

Once we have collected all the needed information and documents from you we will process your application. You will be kept fully informed throughout the process with the chance to ask any legal questions along the way.

The above information is provided as a guide only. The above information does not constitute and is not to be relied on as legal and/or taxation advice. Before entering into any transaction, you should always discuss the relevant Indonesian legal, regulatory and taxation obligations with qualified advisors.