

Aircraft Lease in Indonesia: Key Legal Issues That You Need To Know

By: Haryo Baskoro*

The Indonesian aviation sector has grown rapidly in the last of a decade. To date there are more than 30 (thirty) private aviation companies in Indonesia. Most aircraft operated by Indonesian airlines are procured from foreign lessors or purchased with financing from foreign lenders in various structures.

There are many legal issues in relation to leasing or financing of aircraft to Indonesian airlines. This article intends to set out in brief some of those key issues that are, in practice, frequently asked by lessors/financiers.

Aircraft Registry in Indonesia

To be operated by Indonesian airlines, aircraft must be registered in Indonesia. The nature of civil aircraft register in Indonesia is an owner registration. The registry is maintained by the Directorate General of Civil Aviation (a sub-division of the Ministry of Transportation) ("**DGCA**").

To be registered in Indonesia certain requirements must be met, among others:

- a. the aircraft is not registered in other countries;
- b. if the aircraft is procured by way of operating lease, the minimum period of the lease is two (2) years; and
- c. the age of the aircraft shall not exceed the maximum age requirements. Under the relevant regulation, the maximum age of aircraft that can be registered and operated for the first time in Indonesia are as follows:
 - (i) fifteen (15) years - for passenger transport category aircraft¹;
 - (ii) twenty (20) years – for passenger non-transport category aircraft²;
 - (iii) thirty (30) years – for freighter (either transport category aircraft or non-transport category aircraft); and
 - (iv) twenty (20) years – for helicopters.

The aircraft register in Indonesia records: (i) registration mark, (ii) Manufacturer's Serial Number (MSN) of the airframe, (iii) the type of the aircraft, (iv) the year of manufacturing, (v) the date of the first registration, (vi) the age of the aircraft when it was registered for the first time, (vii) the expiry date of the certificate of registration, (viii) the name of the owner, (ix) the address of the owner, and (x) the name of the lessor (if it is different to the owner). The aircraft register do not record the serial numbers of the engines and there no aircraft engines registry in Indonesia. As

¹ Transport Category Aircraft is defined as aircraft with MTOW (maximum take-off weight) of equal or more than 5,700 kg.

² Non-Transport Category Aircraft includes aircraft with seats configuration of equal or less than 9 (nine) seats (excluding pilot) and with MTOW of equal or less than 5,700 kg either for non-aerobatic, limited aerobatic or full aerobatic operations.

the evidence of registration the DGCA will issue a certificate of registration. The information provided in the certificate of registration of the aircraft covers items (i), (ii), (iii), (vii), (viii) and (ix) above. Notwithstanding this, it is worth noting that the registration of the aircraft with the DGCA is for information purposes only. In the event of a dispute as to title to the aircraft, Indonesian courts will likely look at both the relevant registry and the documents supporting a claim to legal title

The Aircraft Register in Indonesia also record Irrevocable Deregistration and Export request Authorization (“**IDERA**”) that have been granted over the aircraft.

With regard to the mortgage over an Indonesian registered aircraft, after the enactment of Law No. 1 of 2009 regarding Aviation (the “**Aviation Law**”), to be recognized and enforceable in Indonesia it is sufficient to register the mortgage with the International Registry under the Cape Town Convention (as discussed below) (ie it is not necessary to register the mortgage with the DGCA).

Applicability of the Cape Town Convention

The Convention on International Interests in Mobile Equipment and the related Protocol on Matters Specific to Aircraft Equipment (known as the “**Cape Town Convention**”) is fully implemented and enforceable in Indonesia.

The Cape Town Convention ratified by Indonesia is lessors/financiers-friendly. Key features that worth to note are as follows:

- (i) Indonesia has adopted “Alternative A” for all insolvency proceedings. This is the most lessor favorable option as it requires the receiver to give possession of the aircraft to the lessor within a defined waiting period (60 calendar days in the case of Indonesia).
- (ii) Indonesia applies all provisions under Article X of the Protocol of the Cape Town Convention. Article X relates to Article 13 of the Cape Town Convention and deals with a number of key issues related to “Relief pending final determination”. The Cape Town Convention provides the creditor (including lessors) with a right to obtain “speedy relief” from a court in relation to certain orders pending final determination of a claim, relating for example to preservation, possession and immobilisation of the aircraft.

Under the Protocol to the Cape Town Convention, a contracting state can declare a number of working days by which the court must provide the relief – i.e. defining “speedy”. The Indonesian declaration defines this to be:

- a. ten calendar days in respect of the remedies specified in Article 13 (1) (a) (b) and (c) of the Convention; and
 - b. thirty calendar days in respect of the remedies specified in Article 13 (1) (d) and (e) of the Cape Town Convention for the court orders mentioned above.
- (iii) Indonesia applies the entire provisions of Articles VIII, XII and XIII of the Protocol to the Cape Town Convention. These Articles are related to Choice of Law; Insolvency

Assistance and De-registration and Export. Article XIII is the most critical in terms of the requirement that the contracting state must recognise and give effect to IDERA. The authorisation cannot be revoked without the consent in writing of the authorised person.

- (iv) Indonesia has declared that, pursuant to Article 54(2) of the Cape Town Convention, any remedy available to a creditor (including lessor) under any provision of the Cape Town Convention which is not expressed to require application to a court, may be exercised without leave of the court. This is very positive to expedite the process (including a repossession process).
- (v) Indonesia did not make any declaration under Article 55 of the Cape Town Convention. Declaration to Article 55 of the Cape Town Conventions is required if a contracting state will not apply the provisions of Article 13 or 43 of the Cape Town Convention. This is a lessor friendly outcome.
- (vi) Indonesia has made a declaration under Article 39 paragraph (1) letter (a) of the Cape Town Convention pursuant to which Indonesia declares that the following categories of non-consensual right or interest have priority under its laws over an interest in an aircraft object equivalent to that of the holder of a registered international interest and shall have priority over a registered international interest, whether inside or outside insolvency proceedings:
 - i. liens in favor of airline employees for unpaid wages arising since the time of a declared default under a contract to finance or lease an aircraft object;
 - ii. liens or other rights of an authority of Indonesia relating to taxes or other unpaid charges arising from or related to the use of that aircraft object, and arising since the time of a declared default under a contract to finance or lease that aircraft object; and
 - iii. liens or other rights in favour of repairers of an aircraft object in their possession to the extent of service or services performed on and value added to that aircraft object

IDERA

By the enactment of Law No. 1 of 2009 regarding Aviation, IDERA is recognized and enforceable in Indonesia. To be enforced in Indonesia, the IDERA must be granted in accordance with a form prescribed and countersigned by the DGCA. Only one IDERA can be granted and registered with the DGCA for each aircraft.

Repossession and Deregistration

Bearing in mind the applicability of the Cape Town Convention and IDERA in Indonesia, following the lessee's default under the lease agreement the lessor/owner, who holds the IDERA (registered with and acknowledged by the DGCA), may resort to the remedies provided under Chapter III, Article 10 of the Cape Town Convention, ie termination of the lease and repossession

of the aircraft without any involvement of the Indonesian courts. Under the Aviation Law, the DGCA must deregister the aircraft within 5 business days of the application being submitted by the holder of the IDERA.

To export the aircraft outside Indonesia, there are certain documents that need to be obtained, among others:

1. Export recommendation issued by the DGCA
2. If required by the importing country, Lessor/Owner must also obtain an Export Certificate of Airworthiness (Export C of A) which will be issued by the DGCA.
3. Flight Approval (or international flight permit) from the DGCA.
4. Export permit and notice of export from the Directorate General of Customs and Excise (DGCE).
5. Endorsement for the pilot of the aircraft by the DGCA if the pilot is not an Indonesian pilot and the aircraft still bear Indonesian registration mark during the export flight.
6. If the aircraft has been deregistered before export flight (ie no longer bear Indonesian registration mark), the following documents need to be obtained:
 - (i) Diplomatic Clearance from the Ministry of Foreign Affairs.
 - (ii) Security Clearance from the Head Quarters of the National Army of the Republic of Indonesia.

It is not possible to obtain the above export documents in advance.

Bankruptcy and Insolvency

The Indonesian bankruptcy and insolvency rules are governed by Law No. 37 of 2004 regarding Bankruptcy and Suspension of Payment. In the context of Indonesian airline, the law is supplemented by the provisions provided under the Aviation Law and the Cape Town Convention (together, the “**Bankruptcy Rules**”).

If an Indonesian airline is declared bankrupt, a receiver will be appointed by the commercial court to manage the airline. The key provisions under the Bankruptcy Rules that worth to note in the context of aircraft lease are as follows:

- (i) the receiver must transfer possession of the Aircraft to the owner/lessor so long as the lease has been registered with the International Registry within 60 calendar days.

During this stay-period, it will be up to the receiver(s) whether the aircraft operator can continue its operation or not during the stay-period. If the receiver(s) decide that the aircraft operator will continue its operation, any payment under the lease for the operation of the aircraft (such as the rent and/or supplemental rent) during the stay-period can only be collected from the bankruptcy estate. The rent payment will rank *pari passu* with other

unsecured creditors. Accordingly, lessor needs to consider to agree in the lease that lessee shall stop to operate the aircraft upon the occurrence of an event of default (particularly an event of default occurs from an insolvency event);

- (ii) receivers, pursuant to the Indonesian Bankruptcy Law, have general rights in the ordinary course of conducting the business of the debtor to use and/or sell current assets and inventory under its control during the stay period under the Indonesian Bankruptcy Law, except the assets and inventory that are not owned by the debtor (such as lease objects); and
- (iii) the Indonesian Bankruptcy Law provides that with approval from the relevant receivers, a bankrupt company may terminate the relevant Lease Agreement by providing notice of termination within the time period provided in the relevant lease agreement or the time period prevailing according to local custom (which is currently ninety days). If the rent has been paid in advance, the lease may not be terminated earlier than the day on which the time period for which the advance rent was paid expires. From the date of the declaration of bankruptcy or a temporary delay of payment, the rent becomes a debt of the bankruptcy estate.

The Use of Indonesian Language

Another key issue in relation to lease of aircraft to Indonesian airline is regarding the use of Indonesian language in documents where they are party. Law No. 24 of 2009 on the National Flag, Language, Emblem, and Anthem (the “**Language Law**”) requires agreements where Indonesian parties are party to be executed in Indonesian language. If an agreement involves foreign parties, it can be executed in a bilingual version (ie using the Indonesian language and the language of the relevant foreign parties and/or the English language). It is not clear under the Language Law as to what is the consequence for failure to comply with the requirements provided under the Language Law. However, there is a court case which declared that an agreement executed in English language only (where there is an Indonesian party as a party) is null and void, but in Indonesia this case is not binding to other judges as Indonesian judicial system do not recognize the concept of precedents. In other words, a decision by judges in a case will not bind other judges in the future cases.

In light of the above, the prevailing practice, so far as this can be determined, appears to be as follows:

- (i) some parties still take a commercial attitude (regardless of the recent court case) and will execute agreements only in English, unless and until more certainty is forthcoming. In such cases, they will likely insert the following provisions into the agreement:
 - (a) the Indonesian parties confirm that they have read and understood the content and consequences of the agreement and have no objection to executing it in an English language only version;

- (b) the Indonesian parties will execute a version of the agreement in the Indonesian language and this version will be deemed to be effective as of the date of the English language version of the agreement;
 - (c) to the extent permitted by applicable laws, the Indonesian parties waive the requirement to execute the agreement in the Indonesian language and agree that the execution of the agreement in an English version only will not affect the validity, binding effect or enforceability of the agreement; and
 - (d) the Indonesian parties will not claim or file any legal proceedings with regard to the validity, binding nature or enforceability of the agreement;
- (ii) other parties make case-by-case decisions on the execution of agreements in a bilingual version (ie English-Indonesian version) taking into account risk management principles, weighing the cost of a translation and possible delays against the risk of an unfavorable judgment or a legal challenge.

In the context of aircraft transaction:

- a. some parties opt to sign the English version first with the Indonesian version to follows within certain periods of time (as far as it can be determined, the market practice for this middle ground option is 60-120 days as of closing depending on the volume of the documents);
- b. it is not uncommon that the manufacturers will refuse to sign the Indonesian version of an agreement where they are parties. If this is the case then the wordings in item (i) can be incorporated in the document to minimize risks; and
- c. for practicality and cost efficiency, for documents that will unlikely to be enforced in Indonesia, it may worth to consider to waive signing the Indonesian versions. However, it is still advisable to incorporate wordings referred to in item (i) above to minimize risks.

Taxation

To take advantage from tax treaty, the lease of aircraft to Indonesian airline is commonly structured via an entity incorporated in countries that have tax treaties with Indonesia (such as France and the United States of America). So long as the lessor entities meet certain requirements to enjoy the benefits of the tax treaties, no withholding tax for the rent is payable by an Indonesian lessee to the lessors.

With respect to the import of aircraft, the import duties of aircraft into Indonesia is currently zero. However, the import of the aircraft is subject to VAT at the rate of 10% of the value of the aircraft. The VAT can be exempted if the Indonesian aircraft operator can obtain a VAT exemption certificate from the Directorate General of Tax prior to importing the Aircraft.



This article is not substitute to legal advice and should not be relied upon under any circumstances. It is advisable to seek for a specific legal advice for the actual transaction.

**Haryo Baskoro is Partner of Dwipo Lubis Baskoro & Partners.*

Contact:

Dwipo Lubis Baskoro & Partners

*Anakida Building, 6th Floor
Jl. Prof. Dr. Soepomo, S.H. No. 27 Jakarta 12810
Phone: +62-21-83705820
Fax: +62-21-83705821
Mobile: +62-815-8640-8730
Email: hbaskoro@dlplawoffices.com*