

Real estate and construction disputes in Indonesia

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There are various types of dispute and dispute resolution mechanisms available to land and construction disputes in Indonesia, and parties involved in real estate investment, development and construction projects in Indonesia should be aware of these key issues and prepare accordingly.

This article examines the main types of real estate disputes; main methods to resolve real estate disputes; main types of construction disputes; and methods of construction dispute resolution.

This article is part of the multi-jurisdictional guide to corporate real estate law. For a full list of jurisdictional Q&As visit www.practicallaw.com/real-estate-mjg.

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Disputes between parties in private matters or business can occur for a variety of reasons, for example bad faith, breach of contract, negligence, unlawful acts, and coercion. In relation to Indonesian land and construction disputes, there are various types of dispute and dispute resolution mechanisms available, and parties involved in real estate investment, development and construction projects in Indonesia should be aware of these key issues and prepare accordingly. Against this background, this article examines:

- The main types of real estate disputes.
- Main methods to resolve real estate disputes.
- Main types of construction disputes.
- Methods of construction dispute resolution.

Real estate disputes

With regard to land, disputes can take various forms, particularly in Indonesia due to characteristics of the land registration system.

According to data from the National Land Agency of Indonesia (*Badan Pertanahan Nasional, BPN*) (www.bpn.go.id) (land agency) up to September 2013 there were 4,223 legal cases relating to land. 2,012 of these cases have been settled and the rest are ongoing. At provincial level, the number of cases is as follows:

- Central Java: 313.
- Maluku: 279.
- West Nusa Tenggara: 237.
- West Java: 201.
- West Sumatra: 164.
- Jakarta: 67.
- Bali: 69.

The different types of land dispute and their causes relate to the following:

- Land ownership.
- An heir controlling inherited land violates the rights of other heirs.
- Sale of land by an heir to a third party, where the other heirs were not involved. The sale may occur several times.
- Dispute between a holder of a land certificate and a holder of evidence of a controlling right over land that is not yet registered. Many claimants use *girik* (a land information letter) as evidence. A *girik* is evidence that the land is fiscally registered. In some real estate cases, a holder of *girik* can still prevail over a land certificate holder.
- Parties agree a loan and use a land certificate as security for repayment of the loan. A conditional sale agreement and power of attorney to sell the land are signed at the same time as the loan agreement. When the loan becomes due and the borrower defaults on the loan repayments, the lender will execute the power of attorney to sign the sale agreement, sell the land and use the sale proceeds to satisfy the loan. A dispute can arise if the loan value and the land value are very different.
- Dispute between parents and their children, where one of the children sells his parent's land by falsifying the identity of his parents.
- Parties often sign a deed to transfer land, where the purchase price is not fully paid initially but will be paid in instalments. A dispute can occur when the buyer is unable to make the payments and the land has been transferred to it.
- A landowner sells his unregistered land to third parties repeatedly.
- Land illegally occupied by a third party.

The validity of land documents

Most land in Indonesia is not registered, and unregistered land is occupied or controlled by cultivators. The cultivators usually co-operate with local officials to obtain an information letter that they are cultivating the land. After the letter is issued, they will register the land with the tax office, so that land and building tax over the land can be paid. In some cases, they will use this evidence to apply to the land agency for a land certificate.

When an investor is authorised by the government to acquire land for a project, the investor has to deal with cultivators that may not be the real cultivators over the land. In short, the investor has to pay compensation to all cultivators, so that they will leave the land and relinquish their controlling right over the land back to the state. The investor can then apply for a land certificate over the land from the land agency.

False land certificates

A land certificate is regarded as strong evidence of land ownership. However this may be falsified by an irresponsible party, including a land agency official. In addition, there may be two or three overlapping land certificates relating to the same land. This would probably be the fault of the land agency when it measured the land before issuing the land certificate.

Since the parties are authorised to own and use the land under the land certificate (even if they overlap), a party can only execute his right in these circumstances through a settlement or claim in court.

Title restriction

A party who has evidence or valid reasons can apply to the land agency to impose a title restriction over certain land. The restriction is valid for 30 days and automatically terminates after then. A dispute can arise when parties want to transfer the land but cannot because the title to the land is restricted. To revoke the restriction, the owner must show evidence to the land agency to answer the reasons for the restriction, even if the 30-day validity period for the restriction has lapsed.

This creates problems with the implementation of the land transfer. The Land Conveyancing Officer is obligated by law to check the land before the deed of transfer is signed by the parties. In some circumstances, the land can be suddenly restricted by a third party on the signing date. The restriction can be registered by a land agency official, and can create problems when the land certificate is to be registered in the new owner's name.

Other real estate disputes

There are many other types of real estate disputes. Boedi Harsono, in *Penyelesaian Sengketa Pertanahan Sesuai Ketentuan-Ketentuan Dalam UUPA* (Land Dispute Resolutions according to Provisions in UUPA), summarises the type of real estate dispute from a legal perspective:

- Land object.
- Land boundaries.
- Land area.
- Land status (state land or land with right).
- Owner of land.
- Pledged right over land.
- Transfer of land.
- Location designation and determination of land area for a government/private project.
- Land relinquishment.
- Land clearance.
- Compensation as a result of land relinquishment.
- Nullification of land right.
- Revocation of land right.
- Granting of land right.
- Issuing of land certificate.

Methods of real estate dispute resolution

Real estate disputes can be resolved in or out of court.

Court settlement

General court. Private disputes between parties are referred to a general court. This type of court generally resolves cases on breach of contract, unlawful act, nullification of agreement, breach of certain legal provisions (for example, limited liability company law), and many others.

Most land disputes are referred to and resolved by a general court. The claimant will usually file a private claim to the district court with jurisdiction over where the land is located. If included in the agreement, the claimant will file the claim with the district court agreed by the parties.

The district court's decision can be appealed to the high court and requested for cassation to the supreme court. The supreme court's decision is final, binding, and enforceable. Judicial review as a final resort to re-examine the final and binding court decision can also be requested, if one of the conditions to apply for judicial review is fulfilled.

State administrative court. The state administrative court administers a dispute concerning a state administrative decision, filed by an individual or private legal entity. There are two means to resolve the dispute: administration procedure or claim.

Administration procedure consists of:

- **Administrative appeal.** This is an administrative resolution by a higher-rank body or other body.
- **Objection.** This is an administrative resolution by the body or state official that issued the state administrative decision.

An individual or private legal entity that is damaged by a state administrative decision can file a claim against the decision, on the basis that it is against the prevailing laws and regulations and/or violates general principles of good governance. The claimant can include a demand to nullify or declare the decision as unlawful, supplemented with a claim for damages and/or rehabilitation.

The following are examples of land disputes in the state administrative court:

- Between the land agency and an applicant to register land and obtain a land certificate. In this case, the land agency rejects the application, since it considers the applicant's land as state land.
- Between the land agency and an applicant, where the land agency rejects the application for registration because there are no documents proving that the applicant is the owner, or there are other parties claiming to be the rightful owner.
- The unlawful certification of land by the land agency.

Out-of-court settlement

Alternative dispute resolution (ADR). ADR is defined as a mechanism to resolve disputes or differences of opinion through procedures agreed by the parties. In particular, resolution outside the courts by consultation, negotiation, mediation, conciliation, or expert assessment.

Parties that have agreed to settle their dispute through ADR must generally meet within 14 days of when notice of the dispute is duly served on the parties. The outcome must be set out in a written agreement. If the dispute cannot be resolved by written agreement, the dispute or difference of opinion can be settled through the assistance of one or more expert advisers or a mediator.

If the parties fail to reach an agreement within 14 days of the meeting with the assistance of one or more expert advisers or a mediator, or the mediator cannot reconcile the disputed parties, they can request an arbitration or ADR institution to appoint a mediator:

- Efforts to resolve disputes or differences of opinion through mediation must be performed confidentially.
- A settlement is set out in a written agreement, signed by all the parties.
- The settlement agreement is final and binding on the parties, implemented in good faith, and must be registered in the district court no more than 30 days after it has been signed.

- The performance by each party set out in the settlement agreement must be completely implemented no more than 30 days after it is registered.

Arbitration. Arbitration is one of the best known mechanisms to resolve disputes out of court. The basis of arbitration is the arbitration agreement. Without it arbitration cannot be used by the parties, unless it is agreed after the dispute has arisen.

The parties can resolve disputes through an arbitration institution or ad-hoc. It is quite common at the moment to refer disputes to an arbitration institution, for example the Indonesian National Arbitration Board (*Badan Arbitrase Nasional Indonesia, BANI*) (www.bani-arb.org/bani_main_eng.html). BANI has its own arbitration procedure.

For ad-hoc arbitration, the parties have to adopt an arbitration procedure issued by the arbitration institution, or draft their own procedures.

International arbitration has become increasingly popular, due to the liberalisation of trade and services and the Association of Southeast Asian Nations Economic Community (ASEAN) (see www.asean.org/communities/asean-economic-community) that will commence in 2015.

The District Court of Central Jakarta has authority to handle the recognition and enforcement of international arbitration awards. They are only recognised and enforceable in Indonesia if they fulfil the following requirements:

- The award must have been rendered by an arbitrator or arbitration tribunal in a country which, together with Indonesia, is a party to a bilateral or multilateral treaty on the recognition and enforcement of international arbitration awards.
- The award falls within the scope of commercial law, according to Indonesian law.
- The award does not violate public policy.
- An exequatur order has been obtained from the chief judge of the District Court of Central Jakarta.

Since land law has private and public elements, most land disputes are referred to courts. This is the natural tendency among parties in Indonesia. This tendency is strengthened by the fact that foreign ownership of land in Indonesia is limited and strictly regulated.

However, it is possible to settle land dispute through arbitration, as long as it is agreed by the parties, such as disputes between a foreign investment company and a local limited company in Indonesia. For example, in the purchase agreement, the parties may agree to settle and refer disputes to an international arbitration institution. Its award may be considered an international arbitration award under Indonesian law.

Construction disputes

Real estate and construction are different but closely related subjects. Every real estate development will involve construction services, and therefore will refer to a construction contract. High-scale and high-risk construction work may cause a more sophisticated construction contract. In addition, the smooth operation and implementation of construction will result in the smooth completion of the real estate project, as well as delivery to the buyers of property units. If the operation and completion of construction are not on schedule, it may result in a claim of damages against the real estate developers, and in return may result in a claim of damages against the contractor.

Accordingly, it is imperative to understand the legal risks that may occur along the way and stipulate their mitigation through clauses in the contract.

Construction claims or disputes can be in different forms. They can originate from an owner or contractor, or between a sub-contractor and contractor. The causes of disputes can therefore depend on the parties' roles.

Professor H Priyatna Abdurasyid, in *Arbitration & Alternative Dispute Resolution - An Introduction*, states that the causes of construction claims are:

- Delayed design information.
- Inadequate design information.

- Inadequate site investigation.
- Slow client response.
- Poor communication.
- Unrealistic time frame.
- Inadequate contract administration.
- Uncontrollable external events.
- Incomplete tender information.
- Unclear risk allocation.
- Lateness or non-payment.

Further, Robert D Gilbreath, in *Managing Construction Contracts*, writes that in general, owners file claims against their contractors (and, for that matter, engineering firms or other consultants) for one or more of the following reasons:

- **Defective work.** Owners not satisfied with the contractor's product can claim damages that include the cost of repair, replacement, or removal of the defective work. In most cases the work does not meet the contractual specifications or is otherwise not fit for its intended purposes. Occasionally, the goods or services do not meet express or implied warranties provided by the contractor or its suppliers.
- **Delay caused by the contractor.** If the contractor has obligated itself to perform the contract work, in whole or part by a specified time, the owner can claim damages when a delay was not beyond the control of the contractor. Typical damages claimed by owners in this regard are loss of use of the facility, the ripple effect on other contractors, and the increased cost of other delayed work.
- **A defence and counterclaim.** Owners faced with claims from contractors can make a counterclaim. This usually counters, or attempts to discredit, the contractor claim, by uncovering overlapping or duplicate cost claims. For example, citing changes or provisions in the contract that prohibit or modify the contractor's right to claim in the event of a dispute.

Other types of claim, though rare, arise from termination or breach of contract. This generally occurs when a contractor fails to complete the work or for some reason leaves the job site. Owners in this situation usually demand to be compensated for the increased cost, over and above that paid to the contractor, for completing the work through other means.

In contrast, from the contractor's perspective, Robert D Gilbreath summarises the following causes of claims:

- Late or defective owner-provided information, generally in the form of a drawing or specification.
- Late or defective owner-provided material or equipment.
- Changes in regulatory requirements, drawings, or specifications.
- Changed or unknown site conditions.
- The ripple effect or collateral work.
- Restrictions in work method, including delay or acceleration of contractor's performance.
- Ambiguous contracts or contract interpretation.

In each situation above, the contractor will claim that something has occurred (or failed to occur) that caused it to incur additional cost or spend additional time, beyond that called for in the contract or that could have been reasonably expected at the time of bidding or contract award.

Contractors can also claim damages when they feel they have been unjustly removed from a project or otherwise prevented from completing their work. These situations can arise when the contract, in effect, has been terminated by one party.

Methods of construction dispute resolution

Construction dispute resolution is similar to any other dispute resolution. Construction disputes can be resolved in or out of court. Construction law clearly provides that if the parties have chosen to resolve the dispute out of court, a court claim can only be filed if the out-of-court settlement process is unsuccessful. The law also stipulates that an out-of-court settlement can also be used in cases of defects in a building arising after it is completed.

A construction dispute in court is filed with a general court. It will not be filed with a state administrative court, unless it relates to a state administrative decision. Most claims are based on breach of contract. A claim of an unlawful act is still possible, depending on the legal issues, but this is rare.

In Indonesia, especially in the construction industry, ADR is becoming increasingly recognised and used by the parties. This is because a court dispute takes much longer than an out of court settlement. Adjudication and arbitration are two of the most popular ADR mechanisms.

Adjudication. Adjudication is already familiar with construction players. In the *Construction Contracts Dictionary* by Chow Kok Fong, adjudication is defined as the act of formally deciding or determining a dispute or matter in the courts or other tribunals. *Black's Law Dictionary* defines adjudication as the legal process of resolving a dispute; the process of judicially deciding a case. Adjudication may have different forms, depending on the parties' agreement. However, adjudication is essentially a dispute settlement that involves the adjudication board. The decision by the adjudication board can be final and binding, without waiving the right of the unsatisfied party to challenge the decision by adjudication board to arbitration.

Mediation and conciliation. It is essential to note that Indonesian law regulates in more detail ADR in the construction industry. A dispute can be settled out of court through a third party by mediation (appointed by the parties or arbitration institution), conciliation, or arbitration. An expert appraiser may be involved in either mediation or conciliation to provide professional consideration as required by the parties.

The following are the conditions for mediation:

- One mediator appointed by the parties in dispute.
- The mediator has a professional certificate.
- The mediator can request assistance by an expert appraiser, if necessary.
- The mediator acts as a facilitator to guide the disputed parties to arrange a meeting and reach a settlement.
- The settlement is made in writing.

The following are the conditions for conciliation:

- One conciliator is appointed by the disputed parties.
- The conciliator has a professional certificate.
- The conciliator prepares a proposal for settlement.
- If the proposal is agreed by the parties, the solution made by the conciliator becomes the proposal for resolution.
- The proposal for resolution is made in writing.

An agreement in writing by the parties reached through mediation or conciliation is final and binding, to be implemented in good faith.

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