

# Indonesia

Miriam Andreta, Hans Adiputra Kurniawan and Femalia Indrainy Kusumowidagdo

Walangi & Partners (in association with Nishimura & Asahi)

## Regulatory framework

### 1 What are the principal governmental and regulatory policies that govern the banking sector?

Initially, the Central Bank of Indonesia (Bank Indonesia, BI) had the function and authority to regulate and supervise Indonesian banking industry, however, by virtue of Law No. 21 of 2011 on Financial Services Authority (OJK), such authorities were assigned to OJK, save for a monetary function in maintaining rupiah stability and implementing monetary policy, which are still attached to BI.

In specific, OJK has the following authorities that are (i) regulating and supervising banking institutions, (ii) regulating and supervising bank's solvency rating, (iii) regulating and supervising bank's prudent aspects and (iv) bank examination.

Further, in accordance to OJK's masterplan for 2015-2019, it is expected that regulatory policies to be issued will focus on achieving the following:

- fostering improvement in national economic growth;
- maintaining financial system stability; and
- realising society's financial interdependence.

### 2 Summarise the primary statutes and regulations that govern the banking industry.

The basic regulation for banking industry is set out under Law No. 7 of 1992 on Banking, as lastly amended by Law No. 10 of 1998 (the Banking Law). The amendment to Law No. 7 of 1992 was made to accommodate the emergence of sharia banking practice, in which Law No. 10 of 1998 allows commercial and rural banks to be operated based on sharia principles. The Sharia banking system is further regulated under Law No. 21 of 2008, which, among others, regulates the licensing mechanism and the scope of business activities. In addition, banks are also subject to detailed regulations as stipulated by BI and OJK from time to time.

### 3 Which regulatory authorities are primarily responsible for overseeing banks?

Since 2013, OJK by virtue of Law No. 21 of 2011, took over the regulatory and supervisory government functions in financial services sector, including banking, from BI, and becoming the primary regulatory authority responsible for overseeing banks. BI's authority since then is limited to macroprudential surveillance. However, banks are still subject to BI's supervision in certain matters, among others, reporting obligation in relation to foreign loan obtainment.

Given the complexity of business and the high risk involved in the banking industry, certain other governmental institutions are also involved in overseeing banks, among others, the Financial Transaction Reporting and Analysis Centre (PPATK), and the Indonesian Deposit Insurance Institution (LPS). For instance, in conducting its supervisory function, OJK also coordinates with PPATK, where OJK requires banks to submit report to PPATK on any suspicious financial transactions. In addition, OJK also coordinates with LPS with regard to the provision of underwriting of customers' deposits and handling the failing bank.

### 4 Describe the extent to which deposits are insured by the government. Describe the extent to which the government has taken an ownership interest in the banking sector and intends to maintain, increase or decrease that interest.

In light of the 1998's monetary crisis, Indonesians experienced a substantial decrease of trusts in banking system, resulting many people cashing out their deposit at Indonesian banks, and forcing Indonesian government to shut down a number of failing banks. To avoid the re-occurrence of this situation, the Indonesian government introduced a guarantee over deposits mechanism through Presidential Decree No. 26 of 1998 (as amended) where the government (through the Ministry of Finance and BI) agreed to insure deposits.

LPS has taken over this role by virtue of Law No. 24 of 2004 as lastly amended in 2008. LPS will guarantee customers' deposits (in the form of giro, deposit accounts, deposit certificates, savings or their equivalent) in the amount of maximum 2 billion rupiah per customer (subject to change due, among other things, to major inflation).

### 5 Which legal and regulatory limitations apply to transactions between a bank and its affiliates? What constitutes an 'affiliate' for this purpose? Briefly describe the range of permissible and prohibited activities for financial institutions and whether there have been any changes to how those activities are classified.

Regulatory limitations apply to transactions between a bank and its affiliates is generally regulated under BI Regulation No. 7/3/PBI/2005 on the Legal Lending Limit as amended by BI Regulation No. 8/13/PBI/2006, where the maximum limit for total loan portfolio granted to banks' related party is limited up to 10 per cent of the bank's capital and subject to prior approval from the bank's board of commissioners (BOC).

The above limitations apply to banks' 'related party', which has a broader meaning other than the term of 'affiliated party'. Based on Regulation No. 32/POJK.03/2018 on the Legal Lending Limit and Provision of Large Funds for Commercial Banks, a related party is defined as, among other things:

- any individual, company or legal entity exercising control over the bank;
- any legal entity controlled by the bank;
- any company controlled by individual or company exercising control in a company or legal entity exercising control over the bank;
- members of the BOC, board of directors (BOD), executive officers of the bank; and
- any company or legal entity possessing financial interdependence with the bank.

The regulations provide limited exemptions for certain facility granted to related party not to be included in the 10 per cent threshold, among others, fund placement with prime banks and provision of loan to banks' officials for welfare purposes.

Additional limitations also apply to banks whose shares are publicly listed or traded on the Indonesian Stock Exchange, where certain requirements of public disclosure and approval from minority shareholders may be required to comply with Indonesian capital markets laws and regulations.

## 6 What are the principal regulatory challenges facing the banking industry?

As highlighted in OJK's 2018 banking booklet volume 5 (ISSN: 1858-4233), as a member of G20, Financial Stability Board, and the Basel Committee on Banking Supervision, Indonesia is committed to fully adopt and integrate recommendations issued by these organisations to its banking regulatory framework, including the Basel III standards that apply for certain commercial banks.

As of late 2018, OJK announced that the Indonesian banking industry is currently well capitalised with capital adequacy ratio reached 23 per cent and therefore ready to continue the adoption and integration of Basel III standards, including liquidity and a leverage framework.

In addition to the above, OJK, recently issued technical guidelines on sustainable financing for commercial banks (Sustainable Financing Guidelines). OJK requires all banks to gradually adopt and integrate certain principles into banks' strategic planning and business plans, including, (i) responsible investment, (ii) sustainable strategy and business practice, (iii) social and living environment risk management, (iv) governance, (v) informative communication, (vi) inclusion, (vii) development of priority sector and (viii) coordination and collaboration.

Further, in implementing the sustainable financing requirement, banks are expected to implement the following priorities:

- to develop sustainable financing products or services, by way of, among others, increasing the financing, investment or capital participation portfolio;
- to develop the internal capacity of banks; and
- to make certain adjustment within banks' organisation, risk management, corporate governance, to comply with the Sustainable Financing Guidelines.

## 7 Are banks subject to consumer protection rules?

Yes, for financial service consumers (including bank's customers), the protection is provided under OJK Regulation No. 1/POJK07/2013 on Consumer Protection in Financial Services Sector (OJKR No. 1/2013).

OJKR 1/2013 requires banks to have an internal policy on the settlement of consumer complaints, which should be carried out by a specific business unit and/or function, established by the banks. Banks must resolve complaints received from customers within 20 business days of receipt of the complaint (extendable for another 20 business days under certain circumstances, among others, if the complaint requires special investigation).

In 2018, OJK has issued Regulation No. 18/POJK.07/2018 on a Consumer Complaint Service Within the Financial Services Sector, providing guidance in the consumer complaints for financial services business, and requiring banks to prepare their own written procedures to be attached to their financial transaction agreements and/or documents.

## 8 In what ways do you anticipate the legal and regulatory policy changing over the next few years?

It is expected that OJK will continuously issue further regulations aiming at:

- supporting infrastructure financing;
- enhancing financial education and literacy;
- optimising supervision of the financial services industry;
- promoting innovations in financial technology products or services that are beneficial to the public;
- stepping up efficiency and competitiveness of the financial industry; and
- encouraging the improvement and equity of community welfare (eg, developing People's Business Credit Programme).

## Supervision

### 9 How are banks supervised by their regulatory authorities? How often do these examinations occur and how extensive are they?

OJK's supervisory duties of the banks are implemented through on-site and off-site methods.

On-site supervision comprises general and specific examination, by conducting an annual examination or at any time OJK may deem necessary to determine banks' financial condition, monitoring

the compliance and identifying whether they have been involved in any unsound practices that may endanger the banks' business sustainability.

Off-site supervision is conducted by way of requiring banks to submit periodical reports (daily, monthly, annually) and other relevant information relating to their banking business activities to be further assessed by OJK.

Based on the result of the above supervisions, OJK will determine the status of bank supervision, which is classified into three categories, namely (i) normal supervision; (ii) intensive supervision and (c) special supervision. OJK is authorised to instruct banks under the category of intensive supervision or special supervision to take necessary measures to improve their status under normal supervision, among others:

- requiring banks to submit report on specific matters to OJK (ie, latest financial statement, details on productive assets, latest soundness level, etc);
- suspending certain business activities of the banks;
- prohibiting banks to sell and/or decrease their assets, and adjust their shareholding structure; and
- requiring banks, as relevant, to submit recovery plan, action, plan or capital restoration plan.

In carrying out its supervision duties, there are two combined approaches used by OJK: compliance-based supervision and risk-based supervision. Compliance-based supervision focuses on the monitoring of banks' compliance with the applicable regulations related to banks' business operation and management to ensure the proper implementation of prudential principles by the banks. Risk-based supervision is conducted by using risk-based strategies and methodologies (by taking into account credit risks, market risks, liquidity risks and operational risks) to enable the supervisors to detect any significant risks at early stage and to take the appropriate and timely supervisory measures.

## 10 How do the regulatory authorities enforce banking laws and regulations?

OJK and BI, as relevant, may impose sanctions to non-compliant banks, including administrative sanctions ranging from fines, mandatory order to take or to cease certain actions, temporary business suspension, and up to revocation of license.

## 11 What are the most common enforcement issues and how have they been addressed by the regulators and the banks?

The biggest challenge in terms of enforcement is the limited resources of the regulators in dealing with complex and widespread nature of the financial and banking industry in Indonesia - taking into account various potential financial crimes exposures with various forms of sophisticated methods that are constantly being evolved. To deal with that issue, the regulators have been continuously enhancing their supervisory efforts, including by way of, among others, integrating the licensing and supervision mechanism for the entire financial services sector, and implementing a single-presence policy (to narrow the focus of supervision) and data onshoring requirement. We have seen that banks have been continuously expanding their internal audit and human resources compliance as well as enhancing their financial risk anticipation system.

## Resolution

### 12 In what circumstances may banks be taken over by the government or regulatory authorities? How frequent is this in practice? How are the interests of the various stakeholders treated?

LPS may take over a bank that has been assessed by OJK as a failing bank with a solvability problem after coordination with OJK. The take-over methods will be determined by LPS by taking into account various aspects, among others, the complexity and the anticipated impact of the issues (eg, whether the bank concerned is considered as systemic bank), the economic condition and the availability of the investor. Pursuant to LPS Regulations No. 1 and 2 of 2017 on the Resolution of Systemic Banks and Non-Systemic Banks Dealing with Solvability Issues, the available resolution mechanisms are: (i) transferring part of or all assets and/or liabilities to a receiving bank; (ii) transferring part of and/or all assets or liabilities, to an intermediary bank; (iii)

temporary capital contribution; and/or, only applicable for the non-systemic banks (iv) liquidation.

In 2008, a takeover was conducted by LPS by way of capital contribution to Bank Century, which was determined as a failing bank with systemic impact according to Law No. 24/2004. For non-systemic banks, according to LPS' official website, there have been 60 banks that have been liquidated and 35 banks in the liquidation process from 2006 up to February 2019.

In carrying out the resolution methods, LPS has the authority to take over all authorities of shareholders and management of the bank, to review, cancel, terminate and/or amend any contract with a third party adversely affecting the bank, and sell and/or assign the bank's assets without debtors' consent and/or the bank's obligation without creditors' consent. Customers' deposits with the bank will be guaranteed by LPS up to 2 billion rupiah per customer.

### 13 What is the role of the bank's management and directors in the case of a bank failure? Must banks have a resolution plan or similar document?

After being taken over by LPS, the bank's management and directors' duties and authority will be carried out by LPS. The recovery plan may be required by LPS in the preparation stage of the takeover of a systemic bank.

### 14 Are managers or directors personally liable in the case of a bank failure?

If a bank's failure is caused by fault or negligence by the board of directors, each of the directors may be held jointly and severally liable, unless proven otherwise. There is no specific law or regulations that would make bank managers liable for a bank's failure.

### 15 Describe any resolution planning or similar exercises that banks are required to conduct.

Recovery plan is required to be prepared by the systemic bank under OJK Regulation No. 14/POJK.03/2017 on a Recovery Plan for Systemic Banks. The recovery plan must contain, at least, an executive summary, general overview of the systemic bank, recovery options and the disclosure of a recovery plan to both internal and external parties. The recovery plan must be submitted not later than six months of a bank being determined as a systemic bank by OJK.

## Capital requirements

### 16 Describe the legal and regulatory capital adequacy requirements for banks. Must banks make contingent capital arrangements?

OJK Regulation No. 11/POJK.03/2016 on Minimum Capital Adequacy Requirement of Commercial Banks (as amended by OJK Regulation No. 34/POJK.03/2016, collectively OJKR 11) obliges banks to fulfil and maintain certain capital requirements, among others:

- maintaining minimum capital requirement in accordance with the relevant risk profile of the bank, as follows:
  - risk profile ranking 1: 8 per cent of the risk-weighted assets (RWA);
  - risk profile ranking 2: 9 per cent < 10 per cent of the RWA;
  - risk profile ranking 3: 10 per cent < 11 per cent of the RWA; or
  - risk profile ranking 4 or ranking 5: 11 per cent to 14 per cent of the RWA;
- maintaining core capital of at least 6 per cent of the RWA and main core capital at least 4.5 per cent of the RWA, on both an individual and consolidated basis; and
- providing additional buffer capital according to the relevant risk profile:
  - a capital conservation buffer (to anticipate losses during crisis period): 2.5 per cent of the RWA (applicable to banks classified as BUKU 3 and BUKU 4);
  - a countercyclical buffer (to anticipate losses owing to extraordinary banking credit growth that potentially disrupt the financial system's stability): zero per cent up to 2.5 per cent of the RWA (as determined by OJK); and
  - a capital surcharge for systemic banks (to minimise negative impact to the financial system stability and economy in the

occurrence of the systemic bank's failure): 1 per cent to 2.5 per cent of the RW (as determined by OJK).

### 17 How are the capital adequacy guidelines enforced?

In the event that banks do not comply with the requirements mentioned in the previous section, OJK may impose administrative sanctions in the form of, among others:

- written warning;
- prohibition on profit transfer to overseas headquarters;
- prohibition on business activities expansion;
- suspension of the bank's certain business activities;
- prohibition on opening office networks;
- downgrading of bank's soundness level; and/or
- inclusion of bank's managers and/or shareholders, in a list of persons prohibited as bank's shareholders and managers.

### 18 What happens in the event that a bank becomes undercapitalised?

In accordance with Law No. 21 of 2011 on Financial Services Authority (OJK), if OJK indicates that a bank is experiencing liquidity difficulty, OJK will immediately inform BI to take the necessary steps in accordance with the authority of BI. In such a case, the Banking Law authorises BI to carry out certain actions, among others:

- requiring the bank's shareholders to inject additional capital;
- replacing the bank's board of directors and/or board of commissioners;
- merging or consolidating the bank with other banks;
- selling the bank to a buyer who intends to acquire all liabilities;
- handing over the management of part of or all of the bank's activities to other parties; and
- selling part of or all of the bank's assets and/or liabilities to other banks or parties.

### 19 What are the legal and regulatory processes in the event that a bank becomes insolvent?

In accordance with Law No. 37 Year 2004 on Bankruptcy and Suspension of Obligations for Payment of Debts (Law No. 37/2004), if a bank becomes insolvent, OJK has the authority to file a bankruptcy petition for such a bank with the relevant commercial court.

See also question 12 for the resolution steps that may be taken by LPS.

### 20 Have capital adequacy guidelines changed, or are they expected to change in the near future?

The requirements for capital adequacy still rely upon OJKR 11 and has not been significantly changed.

In 2018, BI issued Regulation No. 20/4/PBI/2018 where it introduced the Macroprudential Intermediation Ratio (MIR) concept where BI requires every bank to maintain its MIR between 80 per cent to 92 per cent (or more depending the bank's capital adequacy ratio) to ensure a bank's asset liquidity to maintain monetary stability.

## Ownership restrictions and implications

### 21 Describe the legal and regulatory limitations regarding the types of entities and individuals that may own a controlling interest in a bank. What constitutes 'control' for this purpose?

A controlling shareholder is defined as a shareholder (it can be a legal entity, individual or a business group) that owns:

- 25 per cent or more of bank's paid-up shares capital with voting rights; or
- less than 25 per cent of bank's paid-up shares capital, but it can be proven that such shareholder possesses factual control (eg, to determine bank's management and/or policies), either directly or indirectly.

Under OJK Regulation No. 27/POJK.03/2016 on Fit and Proper Test for a Primary Party of Financial Institution, a candidate of controlling shareholder of a bank is required to obtain approval from OJK after passing a certain fit and proper test held by OJK.

See also question 22 for the maximum limit of a party's shareholding in a bank based on the type of shareholder.

### Update and trends

The massive development of fintech business in Indonesia since 2016 has led the government to regulate fintech and to introduce a number of fintech regulations, including on peer-to-peer lending (OJK Regulation No. 77/POJK.01/2016 on information technology-based loan arrangements (peer-to-peer lending services on a technology information basis), implementation of financial technology relating to the payment system services (BI Regulation No. 19/12/PBI/2017 on the Implementation of Financial Technology), and the regulatory framework for digital financial innovation (OJK Regulation No. 13/POJK.02/2018).

In addition, BI has recently issued a regulation on Integrated Services of Banking Licensing. To improve banking licensing services and coordination between BI and OJK, BI (through the issuance of BI

Regulation No. 19/13/PBI/2017 on One-Stop Integrated Services for the Operational Affairs of Commercial Banks with Bank Indonesia – enacted on 15 December 2017), introduced an integrated-service facility for the granting of licences related to operational affairs between the commercial banks and BI. The licences cover, among other things:

- participation in monetary operations;
- issuance of money-market instruments;
- BI – real time gross settlements (BI-RTGS);
- BI Script-less Securities Settlement System (BI-SSSS);
- BI clearing system (SKNBI);
- intra-day liquidity facility; and
- a bank's offshore loan.

### 22 Are there any restrictions on foreign ownership of banks?

A commercial bank can be established by Indonesians or jointly between Indonesians and foreigners (either individuals or legal entities), with a maximum foreign participation of 99 per cent of the bank's total issued and paid-up capital.

Nonetheless, individually, a party's maximum ownership in a commercial bank under OJK Regulation No. 56/POJK.03/2016 (OJKR 56) is limited to the following (subject to certain limited exemptions):

- 40 per cent of bank's capital: for banks or other non-banking financial institutions;
- 30 per cent of bank's capital: for a non-financial legal entity; and
- 20 per cent of bank's capital (or 25 per cent of shariah bank's capital): for individual shareholders.

The above does not apply to banks with existing shareholders exceeding the threshold prior to the issuance of OJKR 56 as long as the relevant bank has a soundness level of 1 or 2. However, the exception will be voided, and the relevant bank must adjust its shareholding composition to the prescribed threshold if any of the following events occur:

- the bank's soundness level has deteriorated to level 3, 4 or 5 for three consecutive assessment periods; or
- the relevant shareholder exceeding the threshold voluntarily sells its shares to any other party.

### 23 What are the legal and regulatory implications for entities that control banks?

Controlling shareholder is subject to certain specific obligations, including to maintain and implement its commitment for the healthy development of the bank.

Further, OJK (through its Regulation No. 39/POJK.03/2017 concerning Single Ownership in Indonesian Banking) introduced the single presence policy by way of restricting a party from becoming a controlling shareholder in more than one bank. In the event a party purchases shares in a commercial bank resulting it becoming the controlling shareholder in more than one commercial bank, it is required to:

- at the latest one year after the closing of the share purchase (i) merge or consolidate the controlled commercial banks or (ii) establish a holding company in the form of a limited liability company; or
- at the latest six months after the closing of the share purchase, establish a holding function (a function established within the controlling shareholder to consolidate its controlled commercial banks).

Exemptions apply where a party is a controlling shareholder of (i) two banks with different banking business principles (one conventional bank and one sharia bank) and (ii) two banks, where one of them is joint venture bank.

### 24 What are the legal and regulatory duties and responsibilities of an entity or individual that controls a bank?

See question 23.

### 25 What are the implications for a controlling entity or individual in the event that a bank becomes insolvent?

See questions 12 and 19.

### Changes in control

### 26 Describe the regulatory approvals needed to acquire control of a bank. How is 'control' defined for this purpose?

For the definition of control, see question 21.

Pursuant to Decree of Board of Directors of BI No. 32/51/KEP/DIR 1999 on Requirements and Procedures for Merger, Consolidation and Acquisition of Commercial Banks, the following approvals are required for the acquisition of bank:

- approval from the board of commissioners of the acquiring party and the bank that will be acquired (target bank) on the proposed acquisition plan;
- approval from general meeting of shareholders of the target bank;
- approval from the OJK for fit and proper test of the acquiring party;
- if the target bank is a listed company, compliance with the applicable mandatory tender with rules and disclosure of information; and
- approval from OJK for the acquisition.

Another relevant regulatory aspect that needs to be carefully observed and assessed when conducting acquisition of a bank is the requirement set out under Law No. 5 of 1999 on the Prohibition of Monopoly and Unfair Business Competition Practices and its implementing regulations (Competition Law). The Competition Law generally prohibits mergers, consolidation and acquisitions of shares that may result in a monopoly or unfair business practices. The Competition Law sets out a certain threshold for any merger, consolidation or acquisition transaction that will trigger mandatory notification to KPPU after completion of the transaction.

### 27 Are the regulatory authorities receptive to foreign acquirers? How is the regulatory process different for a foreign acquirer?

Generally, there is no difference in criteria for domestic and foreign shareholders (see also question 22). However, OJK sets certain additional requirements for foreign controlling shareholders, as follows:

- it must commit to support the economic development in Indonesia through the bank it owns;
- if it is a financial institution, it must obtain the recommendation from the supervising authority of its country of origin; and
- it must fulfil a certain minimum investment rating depending on the type of investment vehicle entity (ie, bank, non-bank financial institution or non-financial institution legal entity).

### 28 What factors are considered by the relevant regulatory authorities in an acquisition of control of a bank?

See questions 21, 22, 23 and 27.

**29 Describe the required filings for an acquisition of control of a bank.**

In addition to the regulatory approvals referred to in question 26, certain additional filing requirements relating to an acquisition of a bank are as follows:

- announcement of the summary of the acquisition plan (i) in two daily newspapers with a wide circulation at least 30 days before the general meeting of shareholders of the target bank and (ii) in writing to the target bank's employees at least 14 days before the general meeting of shareholders of the target bank; and

- submission of report to OJK by the target bank's board of directors at the latest 10 days after the signing of the deed of acquisition, by attaching copy of the deed of acquisition.

**30 What is the typical time frame for regulatory approval for both a domestic and a foreign acquirer?**

Pursuant to Decree of Board of Directors of BI No. 32/51/ KEP/DIR 1999 on Requirements and Procedures for Merger, Consolidation and Acquisition of Commercial Banks, OJK should issue its approval or rejection within 30 days after the application documentation has been received by OJK.



**Miriam Andreta**  
**Hans Adiputra Kurniawan**  
**Femalia Indrainy Kusumowidagdo**

**mandreta@wplaws.com**  
**hadiputra@wplaws.com**  
**fkusumowidagdo@wplaws.com**

Pacific Century Place 19th Floor, SCBD Lot. 10  
 Jalan Jenderal Sudirman Kav. 52-53  
 Jakarta 12190  
 Indonesia

Tel: +62 21 50808600  
 Fax: +62 21 50808601  
 www.wplaws.com