

Acquisition of financial institutions in Indonesia

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In spite of the global crisis, Indonesia is still full of potential for foreign investors. The country seems to have been largely buffered from many of the worst impacts occurring in other economies. This is perhaps because, after the collapse of the banking system during the Asian crisis in the wake of 1997, the Indonesian financial sector was forced clean up its act, developing stronger fiscal resilience in the process. Banks were recapitalised and restructured by the Government and once the financial soundness of the banks was stabilised, many were sold to foreign institutions. The financial sector is now relatively healthy and provides a stable foundation for the Indonesian economy. There remains an attractive market for the acquisition of banks, insurance companies and securities companies.

Law No. 40 of 2007 Regarding Limited Liability Companies (August 16, 2007) (the Company Law) defines an acquisition as “a legal action undertaken by an individual or a legal entity to acquire the shares of a company that results in a change of control of the company”. While there is no definition of “control” in the Company Law, the market practice is to interpret this to mean the ability to control the management or operation of a company by way of controlling, among other things, voting in shareholder meetings, or Boards of Commissioners or Directors meetings. If the acquisition involves a majority shareholding in the company (presumably more than 50% of the shares) then an acquisition has most likely occurred, despite the determining factor being whether there has been a change in control of the company.

The Company Law also defines mergers, consolidations and demergers (spin-off) as types of business combinations. However, in this article we will only focus on recent acquisition trends in Indonesia.

LENGTHY VERSUS SHORT PROCEDURES

The Company Law and Government Regulation No. 27 of 1998 Regarding Mergers, Consolidations and Acquisitions (February 24, 1998) (GR 27/1998) impose a lengthy procedure upon the Board of Directors of both the acquirer and the company to be acquired with respect to an acquisition.

The Board of Directors of both the acquirer and the company to be acquired, must each prepare a proposal for the acquisition. This

proposal is subject to approval by the Board of Commissioners of the acquirer and the company to be acquired, respectively. Shareholders of the respective companies must also approve the proposal at a general meeting of shareholders with a minimum of 75% of all votes cast.

The proposal must include the name and domicile of the acquirer and the company to be acquired, a reason and explanation from the Boards of Directors of both the acquirer and the company to be acquired, the number of shares to be acquired, the availability of funds, the settlement procedure for the rights of shareholders who do not agree with the acquisition, the settlement procedure for the status, rights and obligations of the members of the Board of Directors, the Board of Commissioners and the employees of the company to be acquired, and a plan to amend the Articles of Association of the company as a result of the acquisition. SSEK has helped many clients through this complex process.

This acquisition proposal is not required if the acquirer directly purchases the company's shares from the existing shareholders, without the involvement of the Board of Directors of the target company. This is a much shorter method.

There are also various notification requirements for an acquisition. The Boards of Directors of both the acquirer and the company to be acquired, must announce the proposed acquisition to the public and the employees of the company to be acquired. This notice needs to be placed in an Indonesian daily newspaper at the latest 30 days before the notice of the general meeting of shareholders. Any objection from the creditors of the company to be acquired must be submitted within 14 days from the newspaper announcement of the proposed acquisition.

In addition to the Company Law and GR 27/1998 requirements, acquisitions involving banks, insurance companies and securities companies are subject to specific regulations and require prior approval from specific government authorities.

RELEVANT APPROVALS

Companies established under Indonesian law with foreign equity participation are generally subject to the rules of the Capital Investment Coordinating Board (BKPM). Law No. 25 of 2007 on Capital Investment

was enacted in 2007 with the objective of coordinating and monitoring all foreign investments under one roof. But to date, banks, insurance companies and securities companies are also subject to the various foreign ownership rules imposed by Bank Indonesia (BI), the Minister of Finance (MOF) or the Capital Markets and Financial Institutions Supervisory Board (Bapepam-LK), respectively.

Before conducting an acquisition, a foreign investor must also take into account the negative investment list for share ownership in certain business sectors. The negative investment list is a list of specific business sectors in which foreign direct investment is closed, or permitted only if the investment takes the form of a joint venture with domestic equity participation. Any business sectors not included in the negative investment list are considered open to foreign investment with no restrictions.

ACQUISITION AND TENDER OFFER FOR PUBLIC COMPANY

The Bapepam-LK has issued specific rules for the acquisition of public companies.

Taking over control of a public company whether by acquiring 50% of the shares or either directly or indirectly intending to control the management, will trigger a mandatory tender offer.

The tender offer process must begin within two business days after the acquisition of a public company. At the same time, the acquirer needs to disclose to the target company, the Bapepam-LK and the stock exchange, information about the shares or equity securities to be acquired, the profile of the acquirer and the purpose of the acquisition. The tender offer should be made no later than 180 days after the commencement of negotiations.

In addition, the Bapepam-LK also requires any party holding at least 5% of the shares of a public company to report to the Bapepam-LK and the stock exchange any changes in ownership, within 10 days of the acquisition or sale taking place.

ACQUISITION OF BANKS

Bank Indonesia, regulations require that any acquisition of a bank must follow a lengthy procedure without any option to expedite the process.

Specific rules for the acquisition of banks are contained in Government Regulation No. 28 of 1999 Regarding Mergers, Consolidations and Acquisitions of Banks (May 7, 1999) (GR 28/1999). This was implemented by Decision the Board of Directors of BI, on the Requirements and Procedures for the Merger, Consolidation or

Acquisition of Commercial Banks (May 14, 1999). Foreign parties may purchase up to 99% of the shares of an Indonesian bank, but if the intention is to acquire control of the target bank or more than 25% of its issued shares, the acquirer must obtain BI's approval and pass BI's "fit and proper" test.

As part of this fit and proper test, BI requires information on the financial standing of the (intending) new controlling shareholders of a bank. They must also provide a letter of undertaking which resolves any financial and liquidity problems of the target bank after they become the controlling shareholder.

Individuals, legal entities and business groups, both local and foreign, may all hold shares in a bank. However, they must satisfy certain criteria. For example, shareholders are required to have integrity and a "clean" funding source, and they must never have been convicted of a financial crime or been found to have caused a company to be declared bankrupt within the previous five years. Bank shareholders must also pass BI's fit and proper test. A legal entity's ownership in a bank may not exceed its net equity. If the legal entity is a bank, it can only invest 25% of its capital in the bank.

Under BI's Single Presence Policy, a foreign party may only control one bank, with some exemptions. There is no requirement for a bank's shareholders to be entities engaging in the financial or banking sector.

ACQUISITION OF INSURANCE COMPANIES

Under MOF Decree No. 426/KMK.06/2003 Regarding Business Licensing and Institutional Aspects of Insurance Companies and Reinsurance Companies (September 30, 2003, MOF Decree 246/2003), an acquisition may be conducted by an insurance company or reinsurance company taking over all or a majority of the shares of another insurance company or reinsurance company, thereby causing the transfer of control of such company. MOF Decree 246/2003 requires that an acquisition must be conducted by a similar type of insurance or reinsurance company. To conduct an acquisition, the new acquirer must obtain prior approval from the MOF.

Government Regulation No. 73 of 1992 Regarding Conducting an Insurance Business (October 30, 1992), as amended (GR 73/1992) stipulates that the direct investment of a foreign party in the joint venture insurance company "at the stage of incorporation" shall not exceed 80%. GR 73/1992 only addresses the percentage of foreign ownership at the time the insurance company was established and does not regulate the percentage of foreign or local ownership thereafter.

GR 73/1992 does provides that a foreign party can increase its ownership percentage after the company has been incorporated but that the Indonesian party's capital must be maintained - meaning it cannot sell its shares to the foreign party. Its percentage of capital can be reduced only by dilution. Consequently, in an acquisition of an insurance company, a foreign acquirer can only acquire shares from another foreign shareholder in the insurance company. The foreign acquirer cannot acquire any shares of the Indonesian shareholders.

ACQUISITION OF SECURITIES COMPANIES

An acquisition of a securities company requires the prior approval of the Bapepam-LK. Foreign entities may only acquire up to 85% of a securities company's shares. However, if the securities company is a public company, the foreign acquirer may own 99% of the shares. Currently, the Bapepam-LK does not favour any acquisition of shares in a securities company engaging in investment management. The Bapepam-LK only allows acquisitions by existing shareholders of a securities company that would not result in any new players entering

the funds market in Indonesia. This also applies to acquisitions at the parent level of the securities company concerned.

CONCLUSION

The acquisition trend for financial institutions – except banks – in Indonesia is mostly accomplished by acquisition with the direct shareholders of the banks, in order to avoid the lengthy procedures under the Company Law and the relevant regulations. For public companies, the procedures for the takeover are more sophisticated and complex since the new acquirer must conduct a tender offer to the public shareholders if the acquisition is considered to be changing the control of the public company. At SSEK we have extensive experience with both scenarios and have successfully guided many international clients through these processes.

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