COVID-19: GOVERNANCE: SUMMARY OF FINANCIAL REGULATORS' RESPONSE AND MEASURES (INDONESIA)

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Legal Briefings – By **David Dawborn, Vik Tang, Teguh Arwiko, Michelle Virgiany and Roni Marpaung**

In order to ensure that financial institutions and the market remain resilient in the changing circumstances, Indonesia's regulators have announced policy changes and issued guidance on a wide range of issues.

The policy response in Indonesia has focused on enhancing the powers of Indonesia's key regulators to ensure they have the tools to mitigate the potential impact of a severe economic downturn and to support the systemically important financial institutions.

This policy direction is not without risks. Recent constitutional challenges to the enhancement of executive powers reflect those concerns. While these defensive measures are needed to prepare the country for a worst-case scenario, some positive trends are also apparent, particularly in the accelerated digitalisation of financial services.

The COVID-19 pandemic has also accelerated the adoption of digital tools by Indonesian government agencies, which should have a lasting and positive impact even after the pandemic is over.

Our briefing provides a single list of these developments, with links to the original documents to help you navigate the following areas:

- Policies on State finances and financial system stability
- Issuance of COVID-19 bonds and lowering of banks' mandatory statutory reserves
- Relaxations on assessment of NPLs and restructured loans, and calculation of solvability ratios
- Loans from Bank Indonesia to banks and corporations
- OJK's power to order financial institutions to carry out M&A
- Increased digitalisation of regulatory processes

Further insights are also available on our global COVID-19 hub including similar financial regulatory summaries for Hong Kong and Singapore.

The latest COVID-19 related developments in the global financial services sector can be found in Herbert Smith Freehills' Financial Services Regulation Weekly Updates.

PERPPU 1/2020

One of the most important regulations issued in Indonesia to respond to the COVID-19 pandemic is Government Regulation in lieu of Law (Perppu) No. 1 of 2020 on Policies on State Finances and Financial System Stability for the Handling of the COVID-19 Pandemic and/or for Handling Threats Potentially Harmful to the National Economy and/or Financial System Stability **(Perppu 1/2020)**. This regulation was issued on 31 March 2020 and came into effect immediately. Perppu 1/2020 is likely to be formally approved by Indonesia's parliament at its next session, which is scheduled for 12 May 2020.

Perppu 1/2020 essentially gives various government bodies and regulators, including Bank Indonesia (the central bank) and the Financial Services Authority (*Otoritas Jasa Keuangan* or **OJK**), additional powers to take action and issue regulations to mitigate the impact of COVID-19 on Indonesia's economy and safeguard the stability of the country's financial system.

Article 27 of Perppu 1/2020 is worth noting. It provides, among other things, that expenditures of the Government and its agencies based on this regulation will not be considered as "state losses". It also grants employees of the Ministry of Finance, Bank Indonesia, and OJK immunity from civil and criminal liability as long as they act in good faith and in line with the regulation. This provision is now the subject of several constitutional challenges before Indonesia's Constitutional Court.

Under Indonesia's Anti-Corruption Law, one of the key elements for an action to be deemed as a corruption offence is the existence of "state losses". It seems that Article 27 of Perppu 1/2020 is intended to avoid criminalisation of government officials in performing their duties in implementing Perppu 1/2020, allowing the officials to be more agile in their policy-making and strategic decisions to limit the impact of COVID-19 without fear of being convicted under the Indonesian Anti-Corruption Law. However, some NGOs and political activists are concerned that this clause may be abused in practice, hence their constitutional challenges over its legality.

ISSUANCE OF COVID-19 BONDS AND LOWERING OF BANKS' MANDATORY STATUTORY RESERVES

In early April, Indonesia issued several tranches of bonds, including one tranche with a 50-year maturity, and raised a total of US$4.3 billion, primarily to fund its COVID-19 relief and recovery efforts. This is Indonesia's largest-ever bond issue, and the 50-year tranche is the longest-dated US dollar bond ever issued by an Asian country. Since then, the Government has raised additional funds by issuing several other "pandemic bonds".

With the Government's plan to issue nearly US$27 billion worth of "pandemic bonds", Perppu 1/2020 authorises Bank Indonesia to purchase Government bonds from the primary market to address financial system issues that threaten the national economy, including bonds issued as a result of the COVID-19 pandemic. This allows Bank Indonesia to act as the "last resort" when the market is unable to absorb all of the supply. Before Perppu 1/2020, Bank Indonesia could only purchase Government bonds from the secondary market.

Bank Indonesia has also issued a set of regulations to relax the minimum statutory reserve requirements for Indonesian banks. These are intended to give additional incentives for banks to provide funding during the COVID-19 pandemic for:

(i) export activities,

(ii) import activities,

(iii) micro, small, and medium enterprises (MSMEs), and/or

(iv) other priority sectors,

and to give the banks additional liquidity to support the Government by purchasing government bonds.

RELAXATIONS ON ASSESSMENT OF NPLS AND RESTRUCTURED LOANS, AND CALCULATION OF SOLVABILITY RATIOS

On 13 March 2020, OJK issued Regulation No. 11/POJK.03/2020 on National Economic Stimulus as Countercyclical Policy in relation to the Impact of COVID-19 (**POJK 11/2020**), which is valid until 31 March 2021. This regulation allows banks to introduce internal guidelines for providing special assistance to debtors affected by the COVID-19 pandemic, especially MSMEs.

POJK 11/2020 also introduces more relaxed requirements when assessing debtors' credit quality and rating restructured loans. For example, banks are now allowed to only consider the punctuality of repayment by their debtors when assigning a rating to debtors' loans with a credit ceiling of up to IDR10 billion if the debtor has been affected by the COVID-19 pandemic. In other cases, banks are required to consider other factors in addition to punctuality of repayment, including business prospects.

For more details on POJK 11/2020, please see our e-bulletin on the credit stimulus package.

OJK also issued OJK Regulation No. 14/POJK.05/2020 on Countercyclical Policy in relation to the Impact of COVID-19 for Non-Bank Financial Institutions (**POJK 14/2020**). While POJK 11/2020 covers banks, POJK 14/2020 applies to non-bank financial institutions, including insurance and reinsurance companies, multi-finance companies, and pension funds. Like POJK 11/2020, POJK 14/2020 eases the requirements when assessing debtors' credit quality and rating restructured loans. It also softens calculation of the solvability ratio for insurance companies.

While the relaxation in the assessment of credit quality and restructured loans should be welcomed by financial institutions, potential investors in financial institution assets will need to take more care in conducting financial due diligence so as to ensure they fully understand the quality of the target's loan book.

LOANS FROM BANK INDONESIA TO BANKS AND CORPORATIONS, AND OJK'S POWER TO ORDER FINANCIAL INSTITUTIONS TO CARRY OUT M&A

Perppu 1/2020 allows Bank Indonesia to provide short-term liquidity loans to both systemic and non-systemic banks. Making these loans requires cooperation with OJK, which would need to assess the particular bank's soundness and solvability level, among other things. Under Perppu 1/2020, Bank Indonesia is also given the authority to provide special liquidity loans to systemic banks that face liquidity issues but do not satisfy the requirements for obtaining short-term liquidity loans.

Interestingly, Perppu 1/2020 also allows Bank Indonesia to extend funds to private corporations by repurchasing Government bonds that they hold through banks. This enables Bank Indonesia to support business outside the financial services sector.

Among the powers given to OJK by Perppu 1/2020 is the ability to order Indonesian financial institutions to carry out a merger, consolidation, acquisition, integration and/or conversion (together, M&A). OJK Regulation No. 18/POJK.03/2020 (**POJK 18/2020**) implements that authority in the banking sector, and we would expect OJK to issue a similar regulation for non-bank financial institutions.

Under POJK 18/2020, OJK can instruct Indonesian banks facing financial difficulties that threaten business continuity, and banks whose controlling shareholders are not able to strengthen the banks' liquidity position, to carry out M&A. OJK may also essentially order banks that are sufficiently strong to accept these "troubled" banks. This significant enhancement of OJK's powers could have a substantial impact on Indonesia's M&A landscape, provided of course that these powers are actually used.

POJK 18/2020 allows OJK to grant these banks certain exemptions, including exemptions from the single presence policy and bank ownership rules. It is also worth noting that in March 2020, OJK issued Regulation No. 12/POJK.03/2020 on Consolidation of Banks, which relaxed the single presence policy in the banking sector by allowing a qualifying party to control more than one bank in certain circumstances.

For more details on POJK 18/2020, please see our e-bulletin on OJK's new powers to order banking M&A.

INCREASED DIGITALISATION OF REGULATORY PROCESSES

One trend emerging across key business sectors, including financial services, is the increased adoption of digital tools. With officers from Bank Indonesia and OJK now working from home, they are carrying out fit-and-proper tests and consultations remotely, by teleconference or videoconference.

In April, OJK issued Regulation No. 15/POJK.04/2020 on the Planning and Organisation of General Meetings of Shareholders of Public Companies **(POJK 15/2020)** and OJK Regulation No. 16/POJK.04/2020 on Implementation of Electronic General Meetings of Shareholders of Public Companies **(POJK 16/2020)**, which together provide a framework for public companies to hold electronic general meetings of shareholders.

While there are still practical challenges and a lack of clarity on certain aspects of the implementation of POJK 15/2020 and POJK 16/2020, this is undoubtedly a positive move towards more widespread adoption of technology by the regulators. Please see our e-bulletin on electronic general meetings of shareholders for more details on POJK 15/2020 and POJK 16/2020.

It is not surprising that banks and other financial institutions in Indonesia have come to rely on their digital offerings even more during the COVID-19 pandemic. As we noted in our February 2020 e-bulletin on digitalisation in the financial services sector, Indonesia's financial institutions are improving their digital products. The COVID-19 pandemic is likely to accelerate this digitalisation trend going forward.

More on COVID-19

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

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