

## Client Alert



May 2016

### OJK's New Rule on Licensing of Underwriters and Broker-Dealers

#### Recent Developments

To increase investor protection and keep up with the developments in market practice, on 18 April 2016, the Indonesian Financial Services Authority (*Otoritas Jasa Keuangan* - "**OJK**") enacted OJK Rule No. 20/POJK.04/2016 on the Licensing of Securities Companies that Undertake Business Activities as Underwriters and Broker-Dealers ("**OJK Rule No. 20/2016**"). This rule was published on OJK's website in late April 2016.

This rule replaces Rule of the Capital Market and Financial Institution Supervisory Agency ("**Bapepam-LK**") No. V.A.1 on the Licensing of Securities Companies, as attached to Decision of the Chairman of Bapepam-LK No. Kep-334/BL/2007 ("**Rule No. V.A.1**"). The provisions of OJK Rule No. 20/2016 are far more extensive and detailed than those of the previous rule and they set out more requirements and prohibitions than the previous rule.

#### What's New?

We set out below a summary of the key changes in the new regulation.

- **Permitted Activities.** The permitted business activities of underwriters and broker-dealers under OJK Rule No. 20/2016 are slightly different from those of the previous rule. The permitted business activities of underwriters and broker-dealers are:

Underwriters	Broker-Dealers
1. securities underwriting	1. transacting securities for its own and other parties' interests
2. other activities related to corporate actions of <b>a company that will or has carried out a public offering</b> , such as providing advice on securities issuances, mergers, consolidations, acquisitions and/or restructurings	2. <b><u>marketing of securities for the interest of other securities companies</u></b>
3. other activities as determined and/or approved by OJK.	3. other activities as determined and/or approved by OJK.

OJK Rule No. 20/2016 expressly prohibits underwriters and broker-dealers from carrying out business activities other than those listed above.

- **Licensing Regime and Requirements.** As with Rule No. V.A.1, under OJK Rule No. 20/2016 a securities company which obtains a license as an underwriter, can also act as a broker-dealer (but not vice versa). However, OJK Rule No. 20/2016 provides a more detailed licensing regime, e.g.:

1. In applying for a license as an underwriter, prospective securities companies may exclude brokerage activities from the scope of the license;
2. The scope of a license as a broker-dealer can be limited to marketing mutual funds participation units only.

OJK Rule No. 20/2016 also provides more requirements for obtaining a license as an underwriter or broker-dealer.

- **Corporate Governance.** Underwriters and broker-dealers must, among other things:
  1. have an organizational structure that conforms with the requirements of applicable rules related to underwriters and broker-dealers, e.g. on the functions of underwriters and broker-dealers;
  2. have operational procedures and standards, the minimum coverage of which is detailed in OJK Rule No. 20/2016;
  3. employ at least one employee that holds:
    - a an individual license as an underwriter representative (for underwriters); and
    - b an individual license as an underwriter representative or broker-dealer representative (for broker-dealers);
  4. prepare and implement policies and procedures on research reports, the minimum coverage of which is detailed in OJK Rule No. 20/2016, so that research carried out by their analysts are independent, and these policies and procedures must be prepared, implemented and submitted to OJK at the latest 6 months after the enactment of OJK Rule No. 20/2016 (i.e. by 18 October 2016).

- **Controlling Shareholders Definition, Shareholders Requirements and Source of Funds Restrictions.** Unlike Rule No. V.A.1, OJK Rule No. 20/2016 defines the term "controlling shareholder" of an underwriter or a broker-dealer. A controlling shareholder of an underwriter or a broker-dealer is defined as a party who directly or indirectly (i) owns at least 20% of the issued shares with voting rights; or (ii) owns less than 20% of the issued shares with voting rights but can be proven to have direct or indirect control of the underwriter and/or broker-dealer.

Further, OJK Rule No. 20/2016 sets out additional requirements to become a controlling shareholder and shareholder of an underwriter and broker-dealer, including (i) never having been punished for committing

(A) a special criminal act (*tindak pidana khusus*) in the last 20 years and (B) a felony (*tindak pidana kejahatan*) in the last 10 years and (ii) not having a non-performing loan (*kredit atau pembiayaan macet*). If the prospective controlling shareholder or shareholder is a legal entity, the requirements to become a controlling shareholder and shareholder of an underwriter and broker-dealer provided under OJK Rule No. 20/2016 would also apply to its direct and indirect controlling shareholders and shareholders. Under OJK Rule No. 20/2016, if a prospective shareholder fails to pass OJK's fit and proper test, it cannot reapply to take another fit and proper test until 6 months after failing the fit and proper test.

OJK Rule No. 20/2016 also expressly prohibits shareholders from using any form of financing to fund their purchase or subscription of shares in an underwriter or broker-dealer, subject to certain exceptions (e.g. this prohibition does not apply to non-controlling shareholders of an underwriter or broker-dealer which are public companies). This prohibition will start to apply one year after the enactment of the rule (i.e. on 18 April 2017).

- **Directors and Commissioners Requirements.** OJK Rule No. 20/2016 sets out additional requirements to become a director or commissioner of an underwriter and broker-dealer, including (i) never having been punished for committing (A) a special criminal act (*tindak pidana khusus*) in the last 20 years and (B) a felony (*tindak pidana kejahatan*) in the last 10 years and (ii) not having a non-performing loan (*kredit atau pembiayaan macet*). Further, directors and commissioners must participate in a continuous education program at least once every 2 years and submit certificates with other supporting documents at the latest 30 days after the certification date.

Under OJK Rule No. 20/2016, if a prospective director or commissioner fails to pass OJK's fit and proper test, he or she cannot reapply to take another fit and proper test until 6 months after failing the fit and proper test.

- **Ownership Restrictions.** The ownership restrictions (e.g. foreign shareholding restrictions, Indonesia Stock Exchange ("IDX") members ownership restrictions and cross holding restrictions) generally remain the same. However, OJK Rule No. 20/2016 makes further elaborations on the application of some of these restrictions, including exemptions from their applicability. For example, OJK Rule No. 20/2016 provides that IDX members who, as a result of (i) underwriting a securities offering or (ii) acting as a standby purchaser in a rights issue, of another IDX member, breaches the IDX members ownership restrictions, are given a 1-year remedy period to transfer the shares of the other IDX member to a third party.
- **Requirement to Become a Member of an Association.** Underwriters and broker-dealers must now be a member of an association of underwriters or broker-dealers, respectively, that has been approved by OJK, the details of which will be further regulated in a circular letter to be issued by OJK.
- **Sanctions.** Unlike Rule No. V.A.1, OJK Rule No. 20/2016 lists specific administrative sanctions for parties that violate that rule (including parties that cause the violation). These sanctions include fines, suspension of business activities and revocation of business licenses. In addition, OJK

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Rule No. 20/2016 provides that OJK may also carry out "certain actions" against violators of the rule, without further detailing what these "certain actions" are.

## Conclusion

There are significant changes between OJK Rule No. 20/2016 and Rule No. V.A.1. OJK Rule No. 20/2016 sets new standards for underwriters, broker-dealers and their management, requiring them to improve, among other things, their corporate governance practice. But on the other hand, OJK Rule No. 20/2016 also provides more clarity on certain issues that were not clear under Rule No. V.A.1.