

## Client Alert



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### How Insurers are Affected by The New Fit and Proper Test Regulation for Financial Services

#### Recent Development

On 27 July 2016, the Financial Services Authority (*Otoritas Jasa Keuangan* or "**OJK**") issued Regulation No. 27/POJK.03/2016 on Fit and Proper Test ("**FPT**") for Primary Parties of Financial Services Institutions ("**Regulation 27**") which took effect on 1 August 2016.

Regulation 27 intends to harmonize all FPT requirements for Financial Services Institutions ("**FSI**") and therefore is applicable to: (i) banks, (ii) securities companies, (iii) investment advisors, (iv) insurance companies, (v) pension funds, (vi) financing companies, (vii) credit guarantee companies, (viii) venture capital companies and (ix) pawn shops.

Regulation 27 partially revokes Regulation No. 4/POJK.05/2013 on Fit and Proper Test for Primary Parties of Insurance Companies, Pension Funds, Financing Companies and Credit Guarantee Companies ("**Regulation 4**"). Regulation 27 revokes most of the provisions under Regulation 4, including Chapter III - Scoring Components of FPT and Chapter IV - FPT Procedure, except those that are related to continuous education for primary parties and incidental FPT requested by the OJK.

In light of the above, until the implementing circular letter of Regulation 27 is issued, there is an absence of FPT rules for assessing insurance companies' Primary Parties. The OJK has confirmed that the implementing circular letter is targeted to be issued one month after the issuance of Regulation 27. However, in practice this may take longer.

#### OJK's Interim Policy

Due to the absence of the FPT assessment rules for insurance companies, it is unclear how the OJK will treat an insurance company's FPT application during this transition period.

The OJK has suggested that, to avoid uncertainty and a prolonged process, insurance companies should wait until the circular letter is issued before filing any FPT application.

#### Noteworthy Changes

##### a. Primary Parties of an Insurance Company

Regulation 27 introduces a definition of Primary Parties as any parties that own, manage, supervise or have significant control over a financial services institution. All Primary Parties are obliged to obtain and pass an

FPT. Although the concept of an insurance company's Primary Parties was introduced in Regulation 4, it was not specifically defined.

Regulation 27 amends the list of an insurance company's Primary Parties and these parties are now: (i) the Controller (ii) the Board of Directors, (iii) the Board of Commissioners, (iv) the Syariah Supervisory Board, (v) the Internal Auditor and (vi) the Company Actuary (as defined). Insurance Experts and Foreign Employees are now excluded under Regulation 27, and so are no longer required to take the FPT.

#### **b. Controller and Controlling Shareholder of an Insurance Company are Subject to FPT**

Particularly for insurance companies, Regulation 27 uses the term "Controller" as one of an insurance company's Primary Parties which is subject to the FPT, but it uses the term "Controlling Shareholder" as one of other FSIs' Primary Parties.

According to the OJK, this is to be consistent with the term that is used under Law No. 40 of 2014 on Insurance ("**Insurance Law**"), which in fact requires a "Controller"<sup>1</sup> to be subject to the FPT - not a "Controlling Shareholder" as had been stipulated under Regulation 4.

The OJK has also confirmed that the definition of an insurance company "Controller" will be perfected upon the issuance of a draft OJK regulation on Insurance Companies Licensing and Institution ("**Draft Licensing Regulation**"). The Draft Licensing Regulation will clearly provide that a Controller that holds shares in an insurance company is deemed to be a Controlling Shareholder.

In light of the above, the Controller and the Controlling Shareholder of an insurance company as Primary Parties should be subject to FPT. However, before the Draft Licensing Regulation is issued, there is no clear basis for the OJK to require a Controlling Shareholder of an insurance company to sit an FPT, given that no provision in the Insurance Law and Regulation 27 requires it.

#### **c. Appointment of Primary Parties Before Passing the FPT**

Before Regulation 27 took effect, the Primary Parties could not acquire an insurance company's shares or assume any rights, duties and obligations before passing the FPT. Regulation 27 now provides that Primary Parties can acquire an insurance company's shares<sup>2</sup> and can assume rights, duties and obligations before passing the FPT.

However, Regulation 27 provides that if a Controlling Shareholder which acquires an insurance company's shares fails to pass the FPT: (i) it is required to transfer the shares to an eligible party, (ii) it is prohibited from controlling the insurance company and (iii) it has limited shareholder's

<sup>1</sup> The Insurance Law and Regulation 27 both define "Controller" as any party that has direct or indirect capability to determine members of the BOD and the BOC and/or to influence actions of the members of the BOD and BOC.

<sup>2</sup> Only applicable to publicly listed insurance companies, where shares transfer can be made without the OJK's prior approval.

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rights (no clarification on what the limitation is). If the other appointed Primary Parties fail to pass the FPT, then his/her appointment must be immediately cancelled.

However, given the uncertainty during this transitional period, before the implementing circular letter of Regulation 27 and the issuance of the Draft Licensing Regulation, the OJK has suggested that a prospective Controller or Controlling Shareholder not take any control over or otherwise acquire any shares of an insurance company, and no application for an FPT for Controller should be made until the issuance of the implementing circular letter.

**d. Insurance company to initially self-assess any Primary Party candidates (except for the Controller and the Controlling Shareholder candidates)**

Regulation 27 requires an insurance company to make an initial self-assessment on the prospective members of the Board of Directors, the Board of Commissioners, the Syariah Supervisory Board, the Internal Auditor and the Company Actuary. Procedures and requirements on the self-assessment are to be further stipulated in the implementing circular letter.

According to the OJK, in the absence of the implementing circular letter, the OJK will not enforce this requirement.

**e. Validity Period of an FPT Approval**

Regulation 27 provides that an FPT approval is valid as long as the Primary Parties remain in the same positions at the same insurance company (this is a key change and no longer is there a fixed term for the same position). The Primary Parties are obliged to retake the FPT if they take new or other positions in accordance with Regulation 4. However, the OJK still has the discretion to request that any Primary Parties retake an FPT, at any time, if deemed necessary.

**f. Transitional Period**

Primary Parties of capital venture companies and pawn shops and members of syariah supervisory boards of pension funds and internal auditors of insurance companies that have not passed an FPT can continue to hold their positions and conduct their functions.

However, each of them must pass an FPT if (i) his term of office is renewed or (ii) his title is changed in the same company.