Indonesia M&A – Basic Framework to Navigate the Country's Regulatory Complexities

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By Erwin Thio (Senior Manager, IGPI Singapore)

Despite Indonesia being the 2nd most active markets in term of Merger and Acquisition (M&A) activities in Southeast Asia, based on the Global Business Complexity Index (GBCI) by the TMF Group, the country has been ranked as one of the most complex places to do business in Asia – ranked 11th in 2022 (was even ranked 1st and 6th in 2020 and 2021 respectively)[1].

This complexity partly owes to the country's economic dynamics and to the Indonesian government actively updating the country's rules and regulations in order to pursue ongoing economic reforms, aiming to make the country more attractive to foreign investment and at the same time to provide safety net and opportunities to its vast and relatively young labour market.

Key Major Regulation Updates in Indonesia

Below are some of the selection of Indonesia's key major regulation updates:
* Note: Abbrev: PR – presidential regulation; GR - Government Regulation

Period of announcement	Key regulations	Issuer	Summarised key content on the regulation
September 2022	Personal Data Protection Law Bill (to be soon enacted as Law)	House of representative – which will become Law once it is ratified by the President	The Personal Data Protection **("PDP")** Law will be the first comprehensive law in Indonesia to govern personal data protection in both electronic systems and non-electronic systems.
September 2022	Acceleration of Renewable Energy Development for Electric Supply ("**PR 112/2022**")	President of Indonesia	To accelerate the usage of renewable energy as an energy source as well as reducing greenhouse gas emission ("**GHG**"). restriction of operational period for steam power plants, limitation of new steam power plants construction, obligation to use local components in order to implement Electric Supply Business Plan by PT Perusahaan Listrik Negara ("**PLN**"), pricing of electricity based on a renewable source, electricity procurement, and many other provisions.
October 2021	Harmonisation of Tax Regulations ("**Law 7/2021**")	Government of Republic of Indonesia	Several tax provisions in Indonesia which had previously been regulated in separate regulations are now being amended simultaneously. Some of these regulations are Law on General Provisions and Tax Procedures (General Provisions of Taxation Law), Law on Income Tax (Income Tax Law), Law on Value Added Tax on Goods and Services and Sales Tax on Luxury Goods (VAT and Luxury Goods Sales Tax Law), Law on Excise (Excise Law), and other tax regulations issued during the Covid-19 Pandemic.

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[1]https://www.tmf-group.com/en/news-insights/publications/2022/global-business-complexity-index/

March 2021	Risk-Based Business Licensing Concept as part of the implementation law of Omnibus Law ("**GR 5/2021**")	Government of Republic of Indonesia	Business licensing is the legality which is granted to business actors to start and run their business and/or business activities,1 and risk is the potential loss caused by hazards.2 Thus, risk-based business licensing is a business licence based on the risk level of such business ("Risk-Based Business Licensing"). The implementation of Risk-Based Business Licensing is aimed to improve the investment ecosystem and business activities, through4: a. the implementation of the issuance of business licences is more effective and simpler; and b. transparency, structured, and accountable supervision of business activities in accordance with provisions of laws and regulations.
March 2021	Investment Line of Business – as part of the implementation law under the Omnibus Law ("**PR 10/2021**")	President of Indonesia	Offers ease of investment through amendment regarding the lists of lines of businesses that are open to investment, lines of business that are closed to investment, and lines of businesses that shall be carried out only by the central government

Source: Indonesia Government Officials (regulation database of Republic of Indonesia - JDIH BPK RI), SSEK, ARMA

The recent enactment of Omnibus Law (Law No.11 of 2020 – regarding Job Creation), which has refreshed previously approved laws, alongside its implementation regulations, has brought about a fresh restart to the country's business regime, including the easing off foreign investment restrictions in key industries such as retail, pharmaceutical and telecommunication and the introduction of risk-based business licensing, a major revamp from previously business-by-business licensing regime; all have resulted in reduction of red-tapes.

However, investors still need to remain cautious, as Indonesia remains a complex business place to navigate. In the context of doing M&A in Indonesia specifically, we would like to suggest a framework that investors could apply (as shown in the figure below). The framework analyses the Indonesia M&A legal aspect by looking at regulations at different tiers (on a vertical axis) and regulations at an operational level (on a horizontal axis).

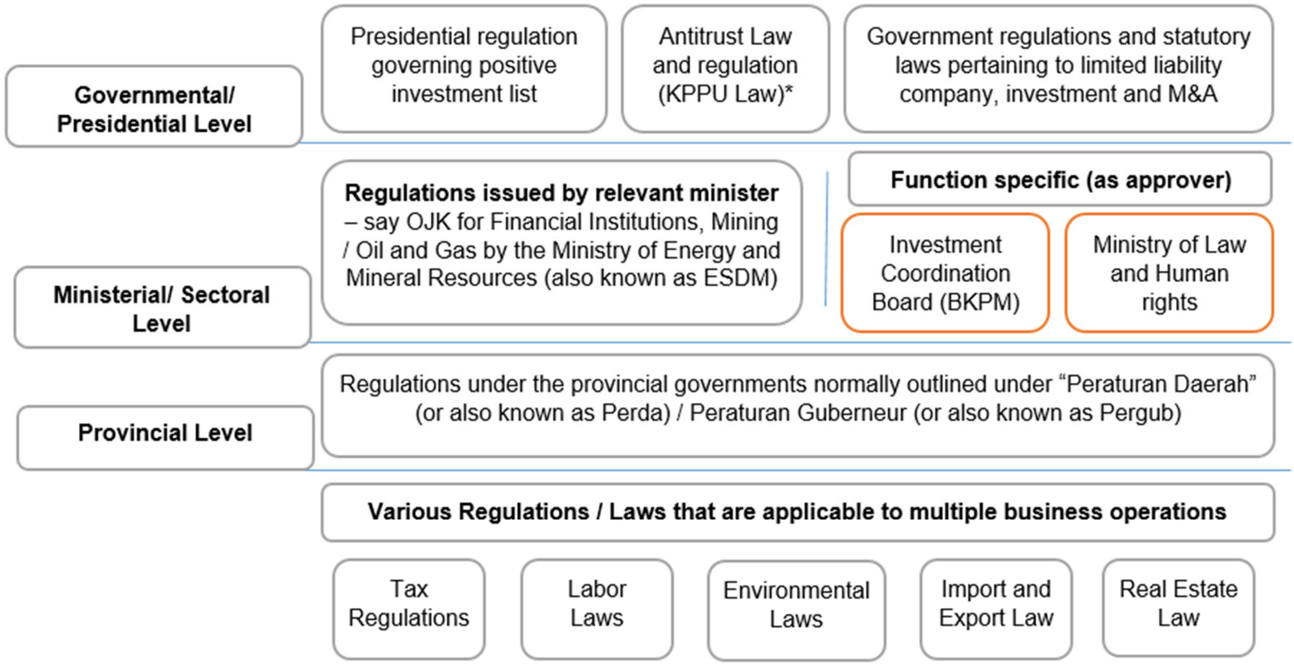
In the context of Indonesia, the different tiers of regulations generally can include, in descending order, the governmental level, the ministerial/sectoral level (e.g. Financial Service Authority (also known as the *Otoritas Jasa Keuangan* or OJK) governs the financial institution and the Ministry of Energy and Minerals (also known as *Kementerian Energi dan Sumber Daya Mineral* or ESDM) governs the energy and mineral resources), and at the provincial level (i.e. within the province that the business is based).

It is worth noting that at the ministerial level, we have divided this into two forms – sector-specific and function specific. The former is self-explanatory, whilst the latter plays a special role; the Ministry of Investment and its Investment Coordinating Board (also known as *Badan Koordinasi Penanaman Modal* or BKPM) will need to approve any shares acquisition of an Indonesian company by a foreign party. BKPM is the key ministry on risk-based business licensing by operating the online single submission system, which you will need to use when you apply for a licence. Also, any transfer of shares will need to be registered to the Ministry of Law and Human Rights, which oversees all registers pertaining to the limited liabilities companies.

At each of these regulatory tiers, any regulation hurdles may provide significant risk to completing your M&A transaction, or even if completed, certain legal implications may ensue – hence, many times, these form the “conditions” to any M&A transactions you contemplate. Going through in descending order in terms of regulatory tiers and becoming familiar with the applicable rules and regulations on each is highly advisable.

The horizontal axis represents the various regulations that will generally be applicable to various M&A transactions. These regulations, among others, include tax laws, labour laws, import/export laws, environmental laws and property laws. An oversight on any of these aspects of the law may not bar you from completing the M&A transaction, but may require some changes to your business operations or to a certain extent, may require you to pay fines for any oversights.

Indonesia M&A General Legal Analysis Framework



* Notification to the KPPU of an M&A transaction is only mandatory when the transaction is not conducted between affiliated companies and the value of assets or the value of sales of the companies involved in the transaction exceeds a certain amount, such as if the combined worldwide assets of the parties to the transaction exceeds IDR2.5 trillion (approximately $172m) or IDR20 trillion (approximately $1.3bn) for banking institutions, or, if the combined national turnover (revenue) of the parties exceeds IDR5 trillion (approximately $343m).

For example, say you, an overseas investor operating in the mining services business, are looking to acquire a coal mining Operating Company that also owns a coal mining licence in East Sumatera. This exercise itself can be quite broad and complex, but as a start, you have to look into the latest regulation aspects governing your acquisition – including whether the transaction is allowed under positive investment list and to also understand the various steps needed to complete your transaction, including having it approved by the Ministry of Law and Human Rights, the BKPM and if necessary the anti-trust regulatory commissioner (or also known as *Komisi Pengawas Persaingan Usaha* or KPPU).

You will also need to understand the latest regulations governing coal mining operations and ownership as this is governed by the ESDM – specifically, there is a foreign ownership restriction on the company that owns the coal mining licence, and the need to follow rules on how to transfer such mining business licences in the event there is a change of ownership. At times, the government through ESDM may also issue temporary restrictions on certain business activities for example, on the export of coals, which happened in early 2022[2].

The target's mining company operation may also be subject to the local provincial government – for example in the case of Tanjung Enim (an area known for Coal mining) there have been provincial rules (also known as Peraturan Daerah or "perda") issued to govern the coal mining operations within that precinct[3]. In addition to all these, aspects pertaining to tax, environmental, labour, trade (including any ban of exports/ imports on coal-related commodities) and real estate law (esp. on land ownership) have to also be considered in your transactions.

The framework that we outlined above is to help you to have an overview of the regulatory framework that is applicable in Indonesia. This helps to at least provide a basic concept and an early guideline in performing M&A transactions. Besides the framework above, below are also additional tips we believe would be important to consider when you are looking to perform M&A in Indonesia:

1. **Understand the basic nature and mechanics of Indonesian limited liability company regulations**
   Gaining an understanding of the mechanics behind the Indonesian Limited Liability Company is your key first step to navigate this complexity. You may start by gaining an understanding of the Indonesia Standard Industrial Classification (or formally known as Klasifikasi Buku Lapangan Indonesia (KBLI)) and the various licences needed to operate certain businesses (or also known as Surat Izin Usaha Perdagangan (SIUP)).
   Beyond that, it is also important to understand the basic structure of Indonesia Limited Liability Company as coded by Law No.40 of 2007 (Company Law) as amended by Law No.11 of 2020 of Omnibus Law and Law No.25 of 2007 on Capital Investment (Investment Law), which governs the basic legal framework of investing into the country.

2. **Go to the source and have your local Indonesian team vet through the regulations**
   When in doubt, you should always go back to the source and not just rely on the interpretation of the law itself (or as reviewed/ commented by many legal advisors). Where necessary, it is definitely very important to have your Indonesian team members or representatives look into the original regulations as issued by the official source.

3. **Seek advice from government investment services**
   It is always important to get advice from not only your legal key person but also from government investment services and relevant trade associations. This is probably the only time that getting multiple pieces of advice from various sources is an efficient way to do business in the context of performing M&A in Indonesia, as a simple wrong step may cause a significant setback. Hence, other than getting reliable advice from your trusted legal advisor, it may also be necessary to contact the investment service department of the Investment Coordination Board (BKPM) OR your contacts in the relevant trade associations.

4. **Always keep yourself updated and aware that many regulations are not always permanent**
   In the example above, there was a ban imposed on the exports of coal – but this was only ephemeral – at the end of January 2022, which is just a few days from when the ban was

[2] https://www.esdm.go.id/en/media-center/news-archives/preventing-power-outages-govt-temporarily-bans-coal-export

[3] The various provincial rules issued pertaining to PT Tambang Batu Bara Bukit Asam (Persero) Tbnk at Tanjung ENIM

announced, these regulations have been updated and there is no longer a ban imposed on such exports. This is to show that rules do change frequently.

At IGPI, we believe that it is very important to understand the local regulatory customs governing your business needs. We hope that the legal framework and advice above would be of great assistance when you explore M&A in Indonesia.

Feel free to reach out to our M&A advisory team for any further discussion.

About the author

Mr. Erwin Thio is the Senior Manager of IGPI Singapore. Before joining IGPI, Erwin was part of KPMG Corporate Finance team in Indonesia, where he led various cross-border transactions, working with both local/ regional and global players. He also acted as engagement lead for a handful of Corporate Finance strategy/ advisory engagements for Indonesian state-owned enterprises, including an engagement for a major strategic national project, a government-to-government cooperation between a consortium of Indonesia state-owned enterprises and a consortium of leading Chinese corporations. Erwin's areas of expertise are in M&A deal management (both buy-side and sell-side), deal structuring, valuation and commercial due diligence, market analysis, and project management. He has also spent a number of years working within the investment and fund management (particularly for Real Estate Private Equity Funds) division of major developers such as Mapletree, Lendlease, Savills IM, and CFLD, where he helped with deal execution and origination, capital raising, fund creation/ development, and management. Erwin graduated with a Bachelor of Business Management from Singapore Management University with a Major in Finance and he is also a CFA Charterholder.

About IGPI

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