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Client Update: Indonesia

29 April 2020

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New OJK Regulation on Material Transaction and Change of Business Activity

After two years in the making, the OJK, Indonesia's financial services authority finally issued the new regulation on material transaction and change of business activity, Regulation No. 17/POJK.04/2020, which will revoke and replace Bapepam-LK Regulation No. IX.E.2.

The OJK Regulation 17/2020 was issued as part of a series of regulations issued by OJK to support the government's attempt to safeguard the stability of the nation's financial system. Some of the regulations were issued to respond to the Covid-19 pandemic. Others, including this one, have a wider reach.

As we will see below, while it offers some clarity over the previous regulation, the requirements in the new regulation are much stricter.

Material Transaction

Definition

OJK Regulation 17/2020 significantly broadens the definition of a material transaction, capturing any transaction conducted by a public company or its controlled company that meets or exceeds the thresholds stipulated in the regulation. The elucidation in the new regulation retains the examples of a material transaction from the previous regulation and adds new categories of material transaction.

These new categories include:

1. the acquisition, disposal, or utilisation of services by a public company;

2. the sale or purchase of an offshore public company's shares;

3. the capital expenditure transactions to support the production or the business activity; and

4. the dilution of the shares ownership of a public company in a controlled company that results in the exit of the controlled company from the public company's consolidated financial statements. Here, it means that the ownership of the public company in its controlled company becomes less than 50% based on the Indonesian Financial Accounting Standards Guidelines (*Pedoman Standar Akuntansi Keuangan*).

Thresholds

In addition to the threshold in the previous regulation of at least 20% or more of a public company's equity, OJK Regulation 17/2020 sets the following additional thresholds:

1. For the acquisition and disposal of a controlled company or business segment:

   a. the transaction value is equal to or exceeds 20% of the public company's equity;

   b. the total assets (*jumlah aset)* of the transaction object divided by the public company's total assets is equal to or exceeds 20%;

   c. the net income for the year (*laba bersih tahun berjalan)* of the transaction object divided by the public company's net income for the year is equal to or exceeds 20%; or

   d. the operating revenue (*pendapatan usaha)* of the transaction object divided by the public company's operating revenue is equal to or exceeds 20%. Operating revenue comes from the total revenue from the business products or services carried out by the company in a certain period.

2. If the public company has negative equity, the OJK will apply a threshold of 10% or more of its total assets.

3. For dilution of a public company's ownership in a controlled company that results in the latter existing the public company's consolidated financial statements, the total assets/net income for the year/operating revenue of the controlled company divided by the total assets/net income for the year/operating revenue of the public company is equal to 20% or more.

   Here, the calculation must be based on the audited financial statements within 12 months before (i) the date of dilution, if the calculation less than 50% or more, or (ii) the general meeting of shareholders ("**GMS**") date, if the calculation is more than 50%.

If a transaction satisfies any of the above thresholds, it will be deemed as a material transaction.

For financial statements used as the base to calculate the other threshold, OJK Regulation 17/2020 allows a public company to use the audited annual financial statements, the limited review or audited quarterly financial statements, or any other audited interim financial statements. However, if the material transaction involved the purchase or disposal of a company or a business segment, OJK Regulation 17/2020 is silent on which financial statements must be used for the calculation of the transaction object. Similar to the previous regulation, the period between the date of the financial statements and the date of the transaction or GMS must not be longer than six months.

Disclosure in the annual report

The old regulation's requirements to appoint an independent appraiser to assess the material transaction, announce the material transaction in the IDX's website and the public company's website and obtain approval for the material transaction from GMS still apply. The new regulation now also requires the company to disclose the result of the material transaction in its upcoming annual report, even if the company has not fully implemented such transaction. If so, the company must provide a specific reason in its nearest GMS.

Shareholders' approval

The new regulation retains the old regulation's requirement of GMS' approval for a material transaction that exceeds 50% of the company's equity, save for 25% or more of the company's total assets if the company's equity is negative. However, now, a material transaction must also obtain a GMS' approval if the fairness opinion finds the material transaction to be unfair. The OJK Regulation 17/2020 is unclear whether an unfair opinion from the appraiser is immediately deemed as having a conflict of interest, as this relates to the quorum of the GMS.

In addition, a material transaction must now be approved by the independent shareholders if the material transaction:

1. is subject to GMS' approval and is an affiliated transaction;

2. contains a conflict of interest, which is still governed under the old Bapepam-LK Regulation No. IX.E.1 on affiliated transaction and conflict of interest of certain transaction; or

3. potentially disrupts the going concern of the public company. An example of this situation is where the transaction reduces the company's proforma operating revenue (*pendapatan usaha)* by 80% or more or results in a proforma net loss (*rugi bersih)* for the company. However, the OJK Regulation 17/2020 does not provide any specific requirement (audited or reviewed by an external or internal auditor) on the proforma used as a comparison.

Exemptions

OJK Regulation 17/2020 provides a list of transactions exempted from obtaining a fairness opinion and GMS' approval.

The exemptions include a transaction between the public company and its controlled company that is owned at least 99% by the public company; a loan and collateral transaction with onshore or offshore banks, venture capitals or financial institutions; a transaction resulting from a court ruling or an auction; and restructuring transaction by a public company controlled, directly or indirectly, by the government. But these transactions must still be disclosed to the public and submitted to the OJK along with its supporting documents.

The new regulation exempts a transaction relating to a public company's business activity that is intended to generate revenue and has been implemented continuously. This type of transaction must be disclosed in the company's annual report or financial statements. The exemption also applies to financial institutions in a specific condition, which will be determined by the OJK. Here, such institutions will only be required to report the transaction to the OJK.

But there is a major shift in the exemption. Previously, Bapepam-LK Regulation No. IX.E.2 exempts a transaction over assets that are directly used by the public company for its production or main business activity that directly support such production or main business activity. Now, OJK Regulation 17/2020 deems such transaction as a material transaction. This change is in line with the OJK's explanation that only operational expenditures, e.g. the purchase of raw materials, will be considered as a company's business activity. In contrast, capital expenditure transactions such as land acquisitions for plants or assets purchased for production, will not be exempted.

Change of Business Activity

The new regulation clarifies that the change of business activity that requires GMS, public disclosure and feasibility study will be triggered if the company intends to:

1. include a new business activity in its articles of association;

2. conduct a business activity that is already included in the company's articles of association but has never been conducted by the company;

3. permanently reduce part or the entirety of its business activities that have been performed by the company, except if the reduced business activities have experienced loss for three consecutive years and the reducing of such business activities will not materially affect the company's current business activities; or

4. change its current business activities with new business activities.

Conclusion

While the OJK Regulation 17/2020 broadens the definition of a material transaction and clarifies the thresholds to calculate a material transaction, it also imposes stricter requirements, especially concerning the independent shareholders' approval requirement. It is unclear why the OJK still requires the independent shareholders to give their approval if a transaction has already been deemed as a fair transaction by an appraiser.

Further, compared to the previous regulation, OJK Regulation 17/2020 does not explicitly exempt debt securities offerings through a public offering. Thus, it is unclear whether a public offering of debt securities will be subject to the material transaction requirements. It is also unclear whether a material transaction that is already disclosed in a prospectus will be subject to OJK Regulation 17/2020.

Keeping in mind that there will be a six-month gap before the new regulation becomes effective, the OJK may issue further clarifications during this period.

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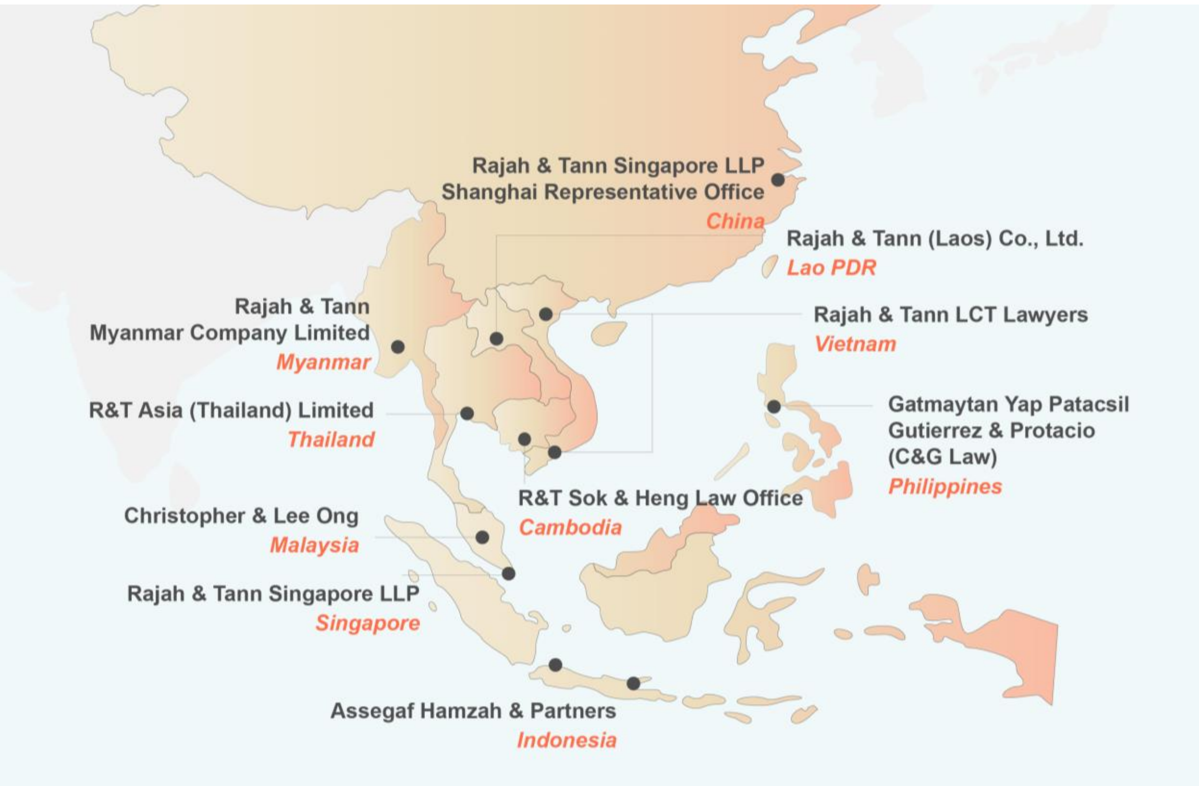

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