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CLIENTALERT

BKPM Issues Important New Regulations on Investment

The Investment Coordinating Board ("BKPM") recently issued a set of important new rules on investment licensing and other procedures, covering both Indonesian domestic direct investment companies (PMDN) and foreign direct investment companies (PMA).

The new rules are set out in BKPM Regulation No. 5 of 2013 (the "New Regulation"), which was promulgated on 12 April and entered into effect 30 working days thereafter.

KEY FEATURES

The key features of the New Regulation from the foreign investor's perspective are as follows:

PMA Status and Consequences for Portfolio Investors

1. A public company (including a PMDN) will now be treated by the BKPM as a PMA if the controlling shareholder of such company is a foreign investor. The term "controlling shareholder" is defined as a shareholder that holds more than 50% of the issued share capital or has de facto control of the company, that is, "the ability to directly or indirectly, by any means, determine management and/or policy decisions in the

company." This accords with the approach adopted by the Financial Services Authority ("OJK").

2. Should an investor hold less than 50 percent of the shares of a company, it will not be treated as the controlling shareholder, unless it has de facto control of the company, in which case the New Regulation appears to expect the company to file a declaration with the OJK to that effect.
3. Upon the submission of the declaration of de facto control to the OJK, the company is expected to apply for investment license to the BKPM, following which the investment in the company in question will be reclassified by the BKPM as a direct investment and the company as a PMA.
4. Classification as a PMA gives rise to various procedural consequences, including the need to obtain a foreign direct investment license. From the substantive perspective, it has major implications as regards compliance with the "Negative List" (a long list of business sectors that are fully or partially off-limits to foreign investment). This is discussed in greater detail in the Commentary below.
5. Where an existing company is converted into a PMA, its subsidiaries must also convert to PMA status within a maximum period of one year. While this has always been the view of the BKPM based on the Investment Act (Law No. 25 of 2007), actual implementation has been lax. It is unclear as to whether enforcement will now be stepped up, or even whether the BKPM has the means and resources to actively verify conversion. There is also a lack of clarity as to the consequences of non-compliance.

Other Key Features

6. The minimum investment required of a new foreign direct investment company is more than Rp 10 billion, or the equivalent thereof in United States dollars. In addition, the company must also have a minimum issued share capital of over Rp 2.5 billion. This was also the subject of much uncertainty in the past, with the thresholds apparently being set by the BPKM on a case-by-case basis. While the New Regulation aims to resolve this unsatisfactory state of affairs, the time frame within which the minimum investment amount must be satisfied remains uncertain.
7. An investment project must be completed within three years, extendable by a maximum of a further three years. Should the project not be completed within a total of six years but the company still wishes to proceed, subject to BKPM inspection a new license may have to be obtained based on the regulations prevailing at that time.
8. Venture capital companies are prohibited from holding shares in both PMAs and PMDNs. In the case of existing venture capital shareholdings, these must be divested within not more than 10 years (strictly non-extendable). This appears to be designed to put an end to venture capital arrangements being used to circumvent the restrictions on foreign investment contained in the Negative List.

COMMENTARY

Aside from potential questions as to whether a BKPM regulation is the appropriate vehicle for restricting the scope of the term "portfolio investment," as used in the Investment Act (Law No. 25

of 2007), perhaps the most significant consequence of the new regulation is that it appears to clear up, for good or for bad, the previous confusion over whether portfolio investments by non-Indonesian entities in Indonesian public companies constitute direct or indirect investments. Prior to this, the consensus among both legal and market practitioners, as well as academics, had been that portfolio investments by non-Indonesians should be treated as indirect investments, thereby exempting them from the Negative List. In other words, the prevailing view was that the stock market provided a means by which foreign investors could bypass the Negative List. However, the matter was far from clear-cut as there had been incidences in the past when this approach was departed from, such as the case where an investment by a Middle Eastern telecommunications provider in an Indonesian telco was disallowed by the Ministry of Telecommunications on the ground that it fell foul of the Negative List, despite the investment being made through the stock market. At the very least, investors will now know where they stand in this regard, although there is no doubt that most people in the investment community would have preferred to see portfolio investments continuing to be treated as indirect, and thereby outside the ambit of the Negative List

Unfortunately, the New Regulation fails to clarify whether a public company that was controlled by a foreign shareholder and engaged in a restricted business sector under the Negative List prior to the coming into effect of the New Regulation will be “grandfathered” under the previous rules and so not be subject to the new rules. This issue will obviously be of major concern to existing foreign investors and should be clarified as expeditiously as possible.

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