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Indonesia: Trends & Developments

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Trends and Developments

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Introduction

The fintech sector has been very active in the past year despite the COVID-19 pandemic. In fact, it may even be said that the pandemic has given Indonesia's fintech sector an even bigger push as more people turn to digital solutions to carry out their daily activities. Businesses have accelerated their adoption of technology to adapt to, and survive in, the "new normal". E-commerce transaction volumes have also increased exponentially, contributing to the increased use of digital payments and online lending platforms.

To secure their place in Indonesia's growing digital economy, fintech players from financial institutions to digital platforms have been carrying out a range of activities. These include fundraising, bolt-on acquisitions to expand their offerings, entering commercial collaborations with other players, and even exploring consolidation options by merging with competitors.

The regulators have also become more alive to the relevant issues in the sector as well as the potential pitfalls. They have therefore updated the fintech regulatory framework by updating existing regulations and issuing new ones, and by preparing several draft regulations currently under consultation. These include regulations on peer-to-peer lending, payments, equity crowdfunding and digital banking.

As always, the key would be to strike a balance between protecting customers and preventing an adverse impact on the country's economy (in particular, the potential systemic risks that the fintech sector may pose to the broader economy) on the one hand, while still encouraging innovation and ensuring that the businesses continue to be agile on the other hand.

The Trending Collaboration: Fintech and E-commerce

According to a joint report produced by Google, Temasek, and Bain (SEA Report), Indonesia's internet-related economy has grown to USD44 billion and is poised to grow even more in the years to come. As more people turn to online platforms to make purchases and carry out their daily affairs, the adoption of digital payments (eg, e-money and e-wallet) has accelerated. Supporting fintech players such as merchant aggregators and payment gateways are also benefiting from this uptake. The e-commerce players either enter into collaboration agreements with fintech players to enable

the digital payment functions on their platforms or look to acquire fintech companies so that they can provide customers with integrated offerings on the platforms. As explained below, banks are also stepping up their digitalisation efforts in order to integrate their products into e-commerce and other digital platforms.

Banks are not the only financial institutions integrating their offerings into e-commerce platforms. Insurance and investment products are now also commonly sold through e-commerce platforms in Indonesia.

The Trending Payment Instrument: E-money

E-money is not only being used more often for online transactions, it has also become the payment instrument of choice among offline merchants as people move away from paper fiat money and adopt contactless payment during the COVID-19 pandemic. More people are also using e-money platforms for fund transfers as these platforms typically offer zero transaction fees. This is one illustration of how the fintech industry can promote financial inclusion; a sizeable portion of e-money users do not have banking accounts and therefore do not have access to mobile banking platforms or credit cards to make purchases or transfer funds.

The authors are seeing strong interest among offshore payment companies to enter the Indonesian market. These are mainly offshore e-money and e-wallet companies, but there are also cross-border remittance companies. These offshore players could enter the market by either applying for their own licences from Bank Indonesia (the Indonesian central bank) or entering into co-operation with local banks or local payment companies in order to make their products available in-country.

Another development worth noting is the increasing use of gamification techniques in digital payment and mobile banking applications to increase user "stickiness". These could be in the form of offering cashbacks or introducing virtual items and games.

The Trending New Regulation for Foreign Investors: Bank Indonesia's Regulation on Payment Systems

On 30 December 2020, Bank Indonesia issued a new regulation on Payment Systems (Bank Indonesia Regulation No 22/23/PBI/2020) that seeks to implement a major overhaul

of the payment licensing framework in Indonesia. This regulation will become effective on 1 July 2021. Industry players and foreign investors are particularly interested in the new minimum local shareholding requirements introduced by the regulation, which, by implication, set the ceiling for foreign shareholding.

The minimum local shareholding requirements are applicable to each of the two categories of payment system providers introduced under this new regulation:

- payment service providers (*penyelenggara jasa pembayaran*, or PJP); and
- payment system infrastructure providers (*penyelenggara infrastruktur sistem pembayaran*, or PIP).

Bank Indonesia will reclassify existing payment system providers (ie, e-money, e-wallet, payment gateway, fund transfer, acquirer, principal, clearing, switching and settlement) into these two new categories and will convert their licences accordingly.

The regulation sets out two tests that must be satisfied.

- Total shareholding test – at least 15% (direct and indirect up to the ultimate shareholder) of the total shares in a non-bank PJP must be owned by Indonesian shareholders, and at least 80% of the total shares in a non-bank PIP must be owned by Indonesian shareholders.
- Domestic control test – at least 51% of the shares with voting rights in a non-bank PJP must be owned by Indonesian shareholders, and at least 80% of the shares with voting rights in a non-bank PIP must be owned by Indonesian shareholders. If there is any special right (i) to nominate a majority of the board of directors and/or board of commissioners, or (ii) to exercise a veto over any decision or approval in the general meeting of shareholders that has a significant impact on the company (eg, amendment of articles of association, change of capital structure, appointment of directors or commissioners, merger, consolidation, acquisition, spin-off or dissolution), then such right must be held by the Indonesian shareholders.

These shareholding and control tests apply to direct and indirect share ownership up to the ultimate shareholders. The consequences of these new tests are as follows.

- Non-bank companies currently applying to Bank Indonesia for a PIP or PJP licence will have to ensure they comply with the above requirements. However, in the case of existing licensed non-bank companies, Bank Indonesia will only require them to comply with the new

minimum local shareholding and control requirements upon a change in the foreign shareholding composition or a change of control by a foreign shareholder, unless such change of shareholding composition or control is carried out in accordance with the discretionary policy or supervisory action of Bank Indonesia.

- Prior to the issuance of this new regulation, there were several categories of payment system providers not subject to any maximum foreign ownership, namely e-wallet, payment gateway, fund transfer and acquirers. With the issuance of this new regulation, those existing licensed companies (which are likely to be reclassified as PJPs) need to be mindful of any corporate actions that would, in effect, require them to comply with these new requirements.
- On the other hand, any existing e-money issuer (which is also likely to be categorised as a PJP and previously restricted to a maximum of 49% foreign shareholding ownership) can increase its foreign shareholding ownership to 85%. This ownership can be a combination of voting and non-voting shares in order to still comply with the control test (whereby at least 51% of the voting shares must be owned by Indonesian shareholders).

The Trending Topic: Digital Banking

One common question the authors receive is whether there are virtual-only banks in Indonesia. In recent months, there have been reports and market developments suggesting that the Indonesian Financial Services Authority (OJK) is considering issuing a new regulation on digital banking. The authors understand that this new regulation could lead to the issuance of virtual-only banking licences like those found in jurisdictions such as Singapore, Malaysia and Hong Kong. This shows that OJK has been monitoring the relevant regional developments, and is aware of the need to ensure Indonesia's regulatory landscape remains competitive.

In anticipation of the new regulation, digital platform companies have already begun acquiring stakes in Indonesian banks with a view to integrating their offerings (eg, by allowing their users to open bank accounts and apply for bank loans via their platform, and even linking them to e-money accounts available on the platform). However, Indonesia may face more challenges in practice than other more mature jurisdictions in introducing virtual-only banks without any physical branches, and the authors expect most players to retain a physical presence to serve their customers.

Until the new digital banking regulation is issued, market players should note that there are existing banking regulations governing the offering of digital banking products, which allow conventional banks to offer such products either

alone or in collaboration with other companies. OJK has also published a draft regulatory amendment on banking business activities that seeks to cover digital banking services and acknowledges the need for banks to adopt information technology more intensively to compete in the fintech sector.

Indonesian banks have also been improving their digital banking offerings. Some now allow customers to open bank accounts without meeting in person, relying on video technology. Some have introduced video banking in their branches and even shopping malls. They have also improved their mobile banking applications, in terms of both user interface and functionality. The introduction of QRIS (QR Code, Indonesian Standard) by Bank Indonesia to standardise QR code payments has also helped banks to offer their customers the convenience of digital payment solutions. The authors are also seeing large banks in Indonesia buying smaller banks with the express aim of turning them into a digital arm of the acquiring bank.

The Trending Commodity: Cryptocurrency

Back in September 2018, cryptocurrency was declared by Indonesia's Supervisory Agency for Commodity Futures Trading (*Badan Pengawas Perdagangan Berjangka Komoditi*, or BAPPEBTI) to be—for regulatory purposes—a commodity that can be the underlying object of futures trading on the Indonesian futures exchange. In 2020, there was increased interest in cryptocurrency trading in Indonesia, and several local news media sources described cryptocurrency assets as one of the best investment assets in 2020.

In response to this trend, BAPPEBTI has issued a set of regulations on cryptocurrency asset trading, most recently amended on 31 March 2020. These regulations set out the key principles applicable to cryptocurrency trading players, including licensing and capital requirements. On 17 December 2020, BAPPEBTI issued a list of cryptocurrency assets that can be traded in Indonesia, through Regulation No 7 of 2020, which contains 229 types of cryptocurrency assets, including Bitcoin, Ethereum, Xrp/ripple, Litecoin, NEM, NEO, EOS, Binance coin and Tron.

As of December 2020, 13 cryptocurrency trading platforms had registered with BAPPEBTI, all of which have to be licensed by BAPPEBTI in 2021. New cryptocurrency trading platform companies will need to apply directly for a licence from BAPPEBTI. The authors are also seeing international cryptocurrency trading platforms seeking to enter into joint ventures with Indonesian conglomerates in order to strengthen their offering to Indonesian users.

The Trending Credit Option: BNPL (Buy Now, Pay Later)

The ongoing need among Indonesians (particularly the “unbanked”) for credit and the strict regulatory framework associated with traditional lending services have meant that peer-to-peer lending (“P2P Lending”) platforms are still very popular in Indonesia. These lending platforms are also increasingly being integrated into e-commerce platforms. According to an OJK statement, in 2020, loan disbursements via P2P Lending platforms stood at IDR155.9 trillion – an increase of 91.3% on 2019, when the figure was IDR81.49 trillion. Many of these loans were distributed to micro, small and medium enterprises in urgent need of liquidity due to the COVID-19 pandemic.

Under the current OJK regulation on P2P Lending (OJK Regulation No 77/POJK.01/2016), OJK adopts a two-stage licensing process for P2P Lending players: registration followed by licensing. As at 22 December 2020, there were 149 P2P Lending companies, of which 112 were registered with OJK and 37 licensed by OJK.

In addition, OJK has increased its efforts to stamp down on P2P Lending platforms operating illegally (without registration or a licence), which have tarnished the reputation of P2P Lending platforms generally by adopting aggressive debt collection strategies and improperly collecting data from their users. Based on an OJK press release dated 25 September 2020, a total of 2,840 illegal P2P Lending platforms were blocked in Indonesia between January 2018 and September 2020.

One other development worth noting in the P2P Lending vertical is the rise of edfintech platforms, coinciding with the increased popularity of edutech in Indonesia. Edfintech platforms serve to connect lenders with borrowers (ie, students or their parents), and enter into collaboration with academic institutions to offer loans to students.

Given the large number of P2P Lending companies and the potential impact of non-performing loans, OJK has reviewed the licensing process for P2P Lending companies, and is expected to issue a new P2P Lending regulation to simplify licensing into a single-stage process but with more stringent requirements. Under the contemplated regime, there will no longer be a registration stage, and companies will need to directly apply for a P2P Lending licence.

The draft OJK regulation on P2P Lending also seeks to introduce several other key changes to the licensing requirements for P2P Lending companies, by increasing the minimum paid-up capital for licensed P2P Lending companies from IDR2.5 billion to IDR15 billion, by changing the scope of

activities that can be facilitated on a P2P Lending platform (from general loan arrangements to productive financing and multi-financing activities), and by requiring controlling shareholders, directors and commissioners to pass OJK's fit and proper test. There is also a new requirement for P2P Lending company shareholders that are foreign legal entities to be engaged in the financial services sector. Once this

regulation comes into effect, these new requirements are likely to attract more specialised investors with the relevant financial services experience who are able to meet the relevant qualification requirements, and also (if the new rules are properly applied) improve the level of governance of P2P Lending companies.

INDONESIA TRENDS AND DEVELOPMENTS

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Hiswara Bunjamin & Tandjung is a full-service Indonesian law firm, associated with global law firm Herbert Smith Freehills. All of the partners are experienced Indonesian lawyers with many years' experience in advising clients across all major industry sectors. The firm's client base includes some of the largest multinational corporations and financial institutions. The Jakarta office has several long-term international counsel seconded from Herbert Smith Freehills, while Herbert Smith Freehills' Singapore office includes Indonesian lawyers and recognised Indo-

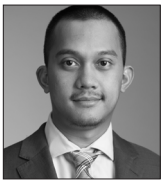
nesia specialists, including in the TMT and fintech space. The fintech practice group includes ten members of the broader corporate M&A and TMT practices, ranging from partner level to associates and trainees. The firm's key areas of practice in relation to the fintech sector include corporate M&A, regulatory advice, company establishment and general corporate advice in the areas of digital payments, peer-to-peer lending, traditional finance models (including digital developments in Indonesia's banking, insurance and multi-finance sectors) and data protection.

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Michelle frequently advises and represents established financial institutions as well as new market entrants on investment structuring, licensing requirements, commercial contracts and joint ventures. She is a member of Herbert Smith Freehills' Digital Law Group, a global team of lawyers working on the firm's and its clients' digital transformation efforts.

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