Asia Pacific Insurance - Indonesia

Insurance Regulatory Landscape and Key Considerations for M&A Transactions

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# Who is the main regulator with oversight of insurance companies?

Financial Services Authority or *Otoritas Jasa Keuangan* (**OJK**)

# Are there foreign ownership limitations for insurance companies? Are there shareholding caps on individuals and/or corporate bodies for insurance companies? If in the affirmative, is this encapsulated within statute or a matter of policy?

There is a maximum foreign ownership of 80%, calculated directly and indirectly. The maximum foreign ownership does not apply to listed insurance companies.

Law No. 40 of 2014 on Insurance (Insurance Law), which was enacted on 17 October 2014, provides that foreign individuals can only have shares in listed insurance companies.

# Can an insurance company carry on a composite business (i.e., life and non-life)? Is this encapsulated in statute or a matter of policy?

No (a matter of law). Further, the operation of *takaful* insurance activities must be undertaken by a separate entity/business unit (i.e.,separate from the conventional insurance business).

The Insurance Law provides a 10-year transitional period for conventional insurance companies to divest or spin off their existing *syariah* units (or otherwise once *syariah* funds exceed more than 50% of all insurance funds held). All insurance companies that have *syariah* business must submit in 2020 their respective action plans to comply with the 10-year transitional period - the spin off must be completed by October 2024.

# Are there other conditions imposed by the regulator in doing an M&A transaction?

**Foreign investor’s criteria**

Foreign insurers must meet certain conditions, including:

Be either an insurance/reinsurance company that engages in the same line of insurance/reinsurance business as the target company, or a holding company with at least one subsidiary engaging in the same line of insurance/reinsurance business as the target company

Have a minimum of A rating or equivalent from an internationally recognized rating institution

Have equity of a minimum of five times its capital participation in the local insurance company

Must have had audited financial statements for the last two full years reflecting financial soundess

Submit, among other items, a cooperation agreement between the Indonesian party and the foreign party in Indonesia

A foreign shareholder (a), which holds shares in a listed insurance company, or (b), which holds shares in an Indonesian listed company that holds shares in a non-listed insurance company is not subject to the above requirements, provided that in scenario (a), the foreign shareholder is not the listed insurance company's controlling shareholder.

**Controlling shareholder's fit and proper test**

Shareholders that own 25% or more, or own less than 25% but control, (e.g., control being asserted through a strong shareholders' agreement) the insurance company ("Controlling Shareholder") must pass a controlling shareholder's fit and proper test by the OJK.

**Controller**

The Insurance Law defines a controller as a party that directly or indirectly has the ability to determine the management of an insurance company and/or to influence the action of the management of an insurance company.

An insurance/reinsurance company is required to identify at least one controller. The OJK can designate another controller based on its own assessment.

**Time period to complete a transaction**

Once approval is given by the OJK, the transaction must be completed generally within 60 days (as approvals require).

# Is dispensation given for fulfillment of these conditions and in what circumstances?

Generally no, except for the A rating requirement where the OJK is willing to give a dispensation on a case-by-case basis.

However, it is usually only in the case of a holding company that does not of itself have a rating, but other members of the foreign insurer group have an A rating or an equivalent from an internationally recognized rating institution (this is policy).

The OJK is firm about each of the other requirements for the foreign shareholder, even if this will be disruptive to a regional organization, as two full years of accounts may not be available for the holding company.

# Is there a single presence policy and is it imposed under statute or policy? Is dispensation given and what criteria will the regulator consider?

Yes.

The Insurance Law prohibits a party from being a controlling shareholder in more than one life insurance company; more than one general insurance company; more than one reinsurance company; more than one *syariah* life insurance company; more than one *syariah* general insurance company; and more than one *syariah* reinsurance company.

The OJK may give a dispensation on a case-by-case basis in an acquisition scenario that there is a strong justification why a dispensation could be given (e.g., there is a robust compliance action plan to move to a single presence) and whether the transaction assists consolidation in the insurance sector.

# What approvals are required for a foreign entity to take a stake in an insurer? Is there a distinction between a share deal or an asset deal?

**Share deal**

The approval of the OJK is required for a share deal, even if there is only one share transferred, and controlling shareholders must pass a fit and proper test as the insurance company's new controlling shareholder. This includes any acquisition involving a controlling stake in a listed insurance company.

Approval for the share acquisition itself is not required if a non-controlling stake is taken in a listed public company.

The process under the Company Law for a change in control of a company, including public announcements, waiting periods and settlement of creditor claims, and announcement to employees, would also apply. In addition, note that under the Labor Law, employees can demand to be terminated and paid out if there is "change in ownership."

**Asset deal**

The transfer of an insurance portfolio requires prior approval from OJK and announcements to the company's policyholders need to be made.

The transferee/purchaser of an insurance business must, prior to completion of the acquisition, be duly licensed as an insurer and must have the same line of business as the transferor (life to life, or general to general).

As it currently stands, the OJK is only issuing new licenses on a selective basis. In any event, the OJK will not issue an insurance license to an entity that is not incorporated in Indonesia.

# How long will regulatory approvals typically take for a share deal versus an asset deal?

Much will depend on circumstances and how the OJK is approached. In many transactions, the OJK is briefed prior to an application being submitted and the transaction is outlined. OJK's approval (whether for a share transfer or a transfer of an insurance portfolio) can take up around eight to 12 weeks (including the fit and proper test, which can be processed in parallel), depending on circumstances (longer if the target company is under OJK monitoring or if the foreign acquirer is not known to the OJK).

No distinction is made between share and assets deals, but generally an asset deal takes longer as the OJK is concerned about how policy holders are dealt with and the OJK conducts an audit before it declares that an asset deal is complete to ensure that there are no outstanding liabilities/claims (particularly long-tail liabilities) left with the transferor.

# How open is the regulator to private equity participation in an insurer?

There is no statutory prohibition but generally, private equity players will not meet the foreign shareholder criteria set out above (unless they have made other insurance investments and use one of those entities).

# Is there a financial holding company concept (FHC) or other equivalent status? What are the implications?

There is no FHC concept for insurance companies.

The OJK has issued a draft regulation on FHC where it would formalize the concept of FHCs. Most of the draft provisions appear to follow an OJK regulation on Financial Conglomeration Good Corporate Governance Regulation, which regulates a financial services group and introduces the definition of Main Entity (being the parent financial services institution of a financial conglomerate or a financial services institution assigned as a main entity by the controlling shareholder of the financial conglomerate), which will be subject to OJK monitoring and a fit and proper test).

It remains to be seen how the final regulation would regulate FHCs and its impact on any FHC's insurance subsidiary.

# What are the typical modes of distribution for insurance companies?

Agency force, bancassurance, brokers, non-bank distribution channels and telemarketing

# Is bancassurance a popular mode of distribution? What approvals are required? What are the main parameters in negotiating a bancassurance agreement?

Yes, bancassurance is a popular mode of distribution.

OJK insurance and OJK banking prior approvals are required before entering into a bancassurance arrangement.

The salient terms are:

The scope of partnership (exclusive, strategic partnership, etc.)

Remuneration (upfront fees, commissions, marketing allowances, etc.)

Term and renewal

Products (including overlap products)

The bank's distribution channels' growth

Claw-back or penalty

Termination of partnership

Business plan and sales targets

Mining of the bank's customer data and use of common customer data

# What are the top challenges in closing an insurance M&A transaction (share deal versus asset deal)?

**Share and asset deals**

Availability of quality target companies and valuation gap on pricing of deals

Quality of offered distribution channels (if the deal involves a strategic distribution partnership with the selling shareholder's group)

Approval from OJK

If the seller is a bank, regulatory approval

The 80% cap on foreign shareholding and identifying a local joint venture partner

**Asset deal**

Approval from OJK

Transfer of insurance portfolios

Transfer of employees

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