

Could 2024 be the Year of Insurance Companies' Consolidation?



To strengthen the insurance sector and align it with the objectives outlined in Law No. 4 of 2023 (often referred to as the Omnibus Financial Law) and Government Regulation No. 14 of 2018 as amended by Government Regulation No. 3 of 2020 (which governs foreign ownership in insurance companies), the Financial Services Authority or OJK enacted OJK Regulation No. 23 of 2023 on Business and Institutional Licensing for Insurance Companies, Sharia Insurance Companies, Reinsurance Companies, and Sharia Reinsurance Companies (“**Regulation 23/2023**”) at the end of 2023.

Regulation 23/2023 comprises of 162 articles, distributed across 22 chapters. Effective since 22 December 2023, Regulation 23/2023 replaces OJK Regulation No. 67/POJK.05/2016 and its amendments, and amend certain articles in the following regulations:

- OJK Regulation No. 71/POJK.05/2016 on the Financial Soundness Levels of Insurance Companies and Reinsurance Companies.
- OJK Regulation No. 72/POJK.05/2016 on the Financial Soundness Levels of Insurance Companies and Reinsurance Companies operating under Sharia Principles.
- OJK Regulation No. 73/POJK.05/2016 on Good Corporate Governance of Insurance Companies.

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Notably, Regulation 23/2023 adopts the same approach for the insurance industry as those that have been adopted in the banking industry. Like OJK Regulation No. 12/POJK.03/2020, which governs the consolidation of commercial banks, Regulation 23/2023 permits insurance companies to engage in strategic measures, namely mergers, acquisitions, or the formation of business groups to meet the minimum capital requirements. In the banking sector, by the end of 2023, most banks had successfully met the minimum capital requirements under OJK Regulation No. 12/POJK.03/2020 through mergers, acquisitions, or forming a banking business group. Naturally, the expectation is that insurance companies will also engage in similar measures through the issuance of Regulation 23/2023.

For this client update, we will focus our discussion on the increased minimum capital requirements, consolidation and the creation of a corporate business group, and foreign ownership. We will also lightly touch base on other noteworthy provisions in Regulation 23/2023.

Increase of the Capital Requirement

Regulation 23/2023 increases the minimum paid-up capital for insurance and reinsurance companies regardless of their categories (conventional vs shariah and insurance vs reinsurance). The increases are substantial (representing an increase of between IDR400 billion to IDR1.7 trillion across the board). In light of it, the prospect of consolidation becomes particularly enticing. Indeed, the insurance sector is ripe with opportunities for consolidation, especially with only 39 out of 124 conventional insurance companies having an equity exceeding IDR1 trillion (as of 2022). Among these, 22 are life insurance companies and 17 are general insurance companies.¹

The increased capital requirements also apply to existing insurance and reinsurance companies, which must gradually increase their minimum capital before the prescribed deadlines. Seemingly mindful of the practical aspects of implementation, OJK has divided the capital increase into two phases. The dual deadlines provide both a structured timeframe and flexibility to insurance and reinsurance companies in meeting the capital requirements:

- By 31 December 2026, companies have to beef up their capital to the amounts specified in Regulation 23/2023.
- By 31 December 2028, companies must increase their capital based on their KPPE (*Kelompok Perusahaan Perasuransian berdasarkan Ekuitas* or a way to group insurance companies based on their equity). KPPE 1 companies, which can only offer simple insurance products, are subject to lower equity requirements compared to KPPE 2 companies (those who can offer various insurance products).

In the meantime, companies whose equity is still below the amount set by Regulation 23/2023 must submit an equity fulfilment plan to OJK within six months from 22 December 2023. Failure to do so may

¹ According to the Roadmap for the Development and Strengthening of the Indonesian Insurance Industry 2023–2027, as reported in <https://finansial.bisnis.com/read/20231120/215/1715946/ojk-baru-39-perusahaan-asuransi-punya-ekuitas-di-atas-rp1-triliun>.

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result in administrative sanction (i.e., written warning and/or decrease in the company's soundness level) and a fine of up to IDR100 million. Likewise, if a company fails to fulfil the minimum equity requirements, it may be subject to administrative sanctions in the form of written warnings and/or a decrease in the company's overall soundness level.

Consolidation and Creation of KUPA

One of the ways that an insurance company can fulfil the minimum capital requirement is by consolidating with other insurance companies. Under Regulation 23/2023, consolidation can occur through conventional methods, e.g., mergers and acquisitions. Alternatively, a corporate business group or *Kelompok Usaha Perusahaan* ("**KUPA**") can be established. A KUPA must also be established if a merger does not significantly increase the business scale of the insurance company.

In the KUPA structure, the parties must establish a holding company. Here, the insurance company can take the lead as the holding company, controlling other insurance companies as its subsidiaries. Alternatively, it can play the role of the "administrator of the holding company" or *pelaksana perusahaan induk* under a non-insurance holding company, where the insurance company is a subsidiary of the non-insurance holding company alongside other insurance companies in the KUPA.

This concept of administrator is newly introduced by Regulation 23/2023 and there is no similar concept in the Indonesian Companies Law (Law No. 40 of 2007, as amended). Under Regulation 23/2023, the administrator's responsibilities are to ensure that companies within the KUPA meet the minimum equity thresholds and to submit documentation to establish the KUPA to OJK. While the current framework suggests a specific scope, analogy should be drawn to OJK Regulation No. 45/POJK.03/2020 on financial conglomerates. In its practical application, the administrator's duties may extend beyond those outlined in Regulation 23/2023. Furthermore, the individual management members of the administrator must also tread carefully and consider their fiduciary duties under the Indonesian Companies Law. In any event, we anticipate certain amendments to the provisions in OJK Regulation No. 45/POJK.03/2020 to bring it in line with the concept of KUPA and administrator in this Regulation.

New Foreign Ownership Requirements

OJK maintains the 80% limit of foreign ownership in insurance and reinsurance company under Government Regulation No. 14 of 2018 on Foreign Ownership in Insurance Companies. Concurrently, Regulation 23/2023 introduces several new requirements for a foreign company that directly or indirectly owns 25% or more of the shares of an Indonesian insurance company, namely that:

- The foreign company shareholder must be engaged in a similar business or act as a parent company with one of its subsidiaries operating in a similar insurance business;
- The foreign company shareholder must maintain equity of at least five times the amount of direct participation in the insurance company at the time of establishment and during any changes in the insurance company's ownership; and

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- The foreign company shareholder must hold a minimum rating of A or its equivalent from an internationally recognised rating agency.

Other Noteworthy Provisions

Besides the provisions that have been discussed in this client update, we thought it worthwhile to also highlight several other provisions from Regulation 23/2023:

- ***For directors, prohibition on concurrent positions and requirement for certification***

Under Regulation 23/2023, directors in an insurance company are prohibited from holding directorship in other companies (except for non-CEO directors, who can serve as a commissioner in a subsidiary controlled by the insurance company).

Additionally, Regulation 23/2023 requires directors, commissioners, and officers holding positions one level below the board of directors-level to hold a risk management certificate.

- ***Insurance agents must be registered***

Going forward, all insurance agents in Indonesia must be registered with OJK. Regulation 23/2023 requires insurance agents to consistently adhere to certain conditions. These include holding a valid insurance field agency certificate, having agreements with insurance companies, avoiding concurrent agreements with the insurance company in the same business field, maintaining a sanction-free record within the last year, and not having a financial or economic services-related criminal conviction in the past five years.

- ***Cooperation of companies under one ownership***

Provided that OJK has given its approval, insurance companies under one ownership structure (e.g., parent-subsidiary relationship, under the same controlling entity, or part of the same KUPA) can collaborate to enhance efficiency, optimise resources through support, and provide added value for business activities, services, and operations.

- ***OJK can determine controlling shareholders and controllers***

Similar to the banking sector, OJK has the authority to designate controllers in instances where an insurance company has not appointed any. Additionally, OJK has the power to identify other controllers beyond those appointed by the company.

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Conclusion

In conclusion, Regulation 23/2023 marked the first step of the transformation of the nation's insurance landscape. By imposing the minimum capital requirements and facilitating strategic measures such as the formation of KUPA, the Regulation opens avenues for collaboration, innovation, and risk-sharing between insurance companies, essentially extending a lifeline to the insurance industry to foster a more resilient and healthier insurance ecosystem in Indonesia.

This proactive approach mirrors the measures adopted in the banking sector, and it is hoped that the insurance industry will experience the same success as the banking industry. All in all, Regulation 23/2023 is a game-changer.

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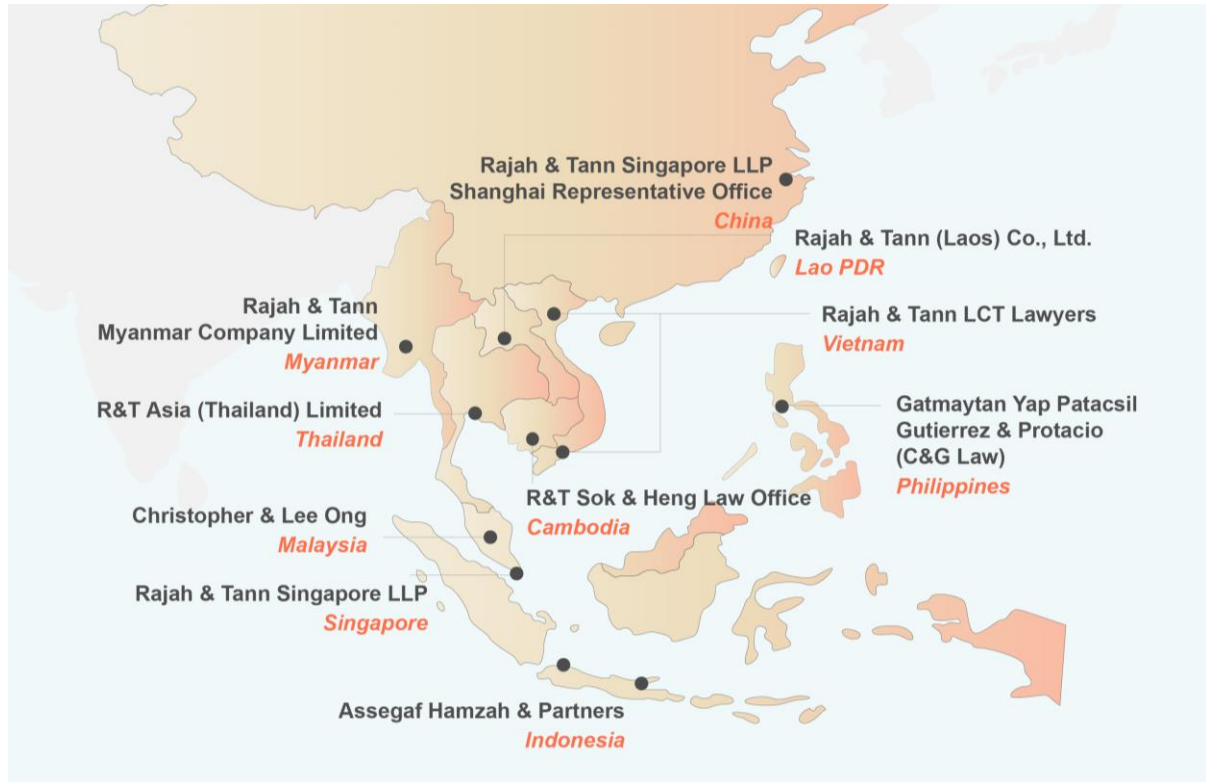
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