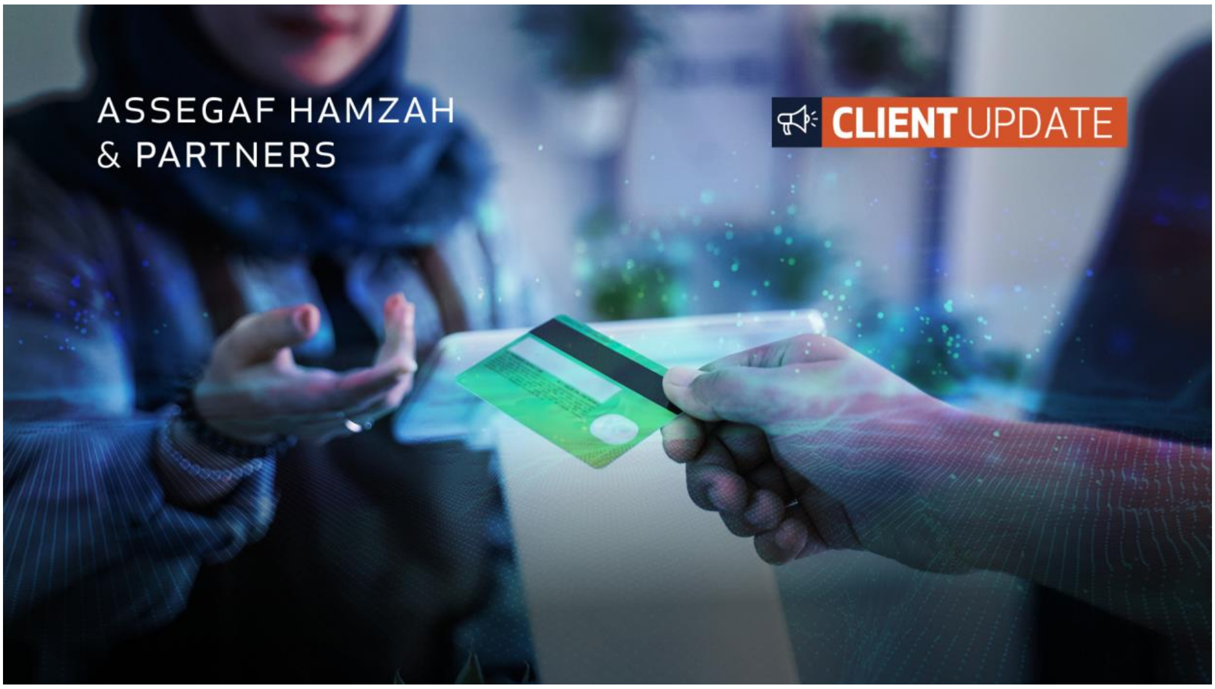
Client Update: Indonesia
27 March 2024

OJK Regulation Mandates Spin-Off of Sharia Insurance Units



In July 2023, the Financial Services Authority ("**OJK**") issued OJK Regulation No. 11 of 2023 ("**New Regulation**") to regulate the spin-off of sharia units of insurance and reinsurance companies. Along with the recently issued OJK Regulation No. 23 of 2023 on the licensing of conventional and sharia insurance and reinsurance companies, the New Regulation is part of the legislative framework that replaces OJK Regulation No. 67/POJK.05/2016.

Moreover, the New Regulation showcases OJK's effort to align the insurance sector with the objectives under Law No. 4 of 2023 (the so-called Omnibus Financial Law), which mandates that insurance and reinsurance companies with sharia units must conduct a spin-off of these units upon satisfaction of certain criteria.

Generally, the New Regulation requires an insurance or reinsurance company to spin-off its sharia unit if the unit has fulfilled the criteria set by OJK, there is a spin-off request from the company, or the spin-off is carried out as part of a consolidation of insurance and reinsurance companies. Besides this requirement, the New Regulation also has other key elements that are worth highlighting.

Deadline for Spin-Off is Extended

Previously, under Law No. 40 of 2014 on insurance, insurance and reinsurance companies must spin-off their sharia units by 17 October 2024. This deadline has now been extended under the New Regulation to 31 December 2026. As part of this obligation, companies must submit their sharia spin-off proposal for OJK's approval by 31 December 2023.

This extension should give ample time for insurance and reinsurance companies to strategise and develop an appropriate plan. In 2023, there were 42 insurance companies with sharia business units, and 10 of them had discontinued these business units and transferred their sharia portfolios to other sharia insurance companies due to, among others, their equity being below the required standards.[1]

Despite the extension, the New Regulation shortens the duration for insurance companies to finalise their portfolio transfer after obtaining OJK's approval from 12 months to 6 months. While we believe that this timeframe should allow for the completion of the transfer, companies are advised to have a comprehensive spin-off plan when seeking approval from the OJK.

Mandatory Spin-off is Possible

The New Regulation states that the spin-off of sharia units is intended to enhance the resilience and competitiveness of the insurance industry, as well as to safeguard the interests of policyholders and participants. Consequently, as part of this mandate, OJK is authorised to order a specific company to spin-off its sharia unit in anticipation of a consolidation of insurance or reinsurance companies.

In the same vein, the OJK may revoke the licence of an insurance or reinsurance company that has not spun-off its sharia unit by the deadline.

Spin-off Procedure

After an insurance or reinsurance company obtained OJK's approval, the spin-off procedure of the sharia unit can generally be summarised as follows:

1. A company can carry out the spin-off by:

   (i) establishing a new sharia insurance or reinsurance company – in this process, the new company must obtain the necessary licences and afterward, the original company can transfer the relevant portfolios to the new company; or

[1] Mediatama, G. (2024, January 11). *Ojk catat 10 perusahaan Asuransi Tak memilih spin off, Begini Alasannya*. kontan.co.id. https://keuangan.kontan.co.id/news/ojk-catat-10-perusahaan-asuransi-tak-memilih-spin-off-begini-alasannya

(ii) transferring the portfolio to an existing insurance or reinsurance company.

2. The transfer of the portfolios must include all the assets, liabilities, and equities owned and managed by the sharia unit. If the spin-off involves the transfer of the entire portfolio, the transfer must include the tabarru' funds, participant investment funds, minimum company funds, and necessary qardh.

3. The transfer of the portfolios must be completed within six months from the date of the OJK's approval of the spin-off.

4. The entire spin-off process must comply with the applicable laws and regulations.

If an insurance or reinsurance company chooses to establish a new sharia insurance company but does not meet the minimum equity requirement (IDR100 billion for insurance companies and IDR200 billion for reinsurance companies), such company must:

1. Increases the equity of the sharia unit by asking for capital injection from the shareholders;

2. Invites new investors to increase the equity of the sharia unit; and/or

3. Transfer the entire membership portfolio of the sharia unit to a sharia insurance company or sharia reinsurance company that has obtained a business licence.

Incentives for Spin-off

In application, companies often shy away from a spin-off because of the significant costs involved. Companies that choose to spin-off are often companies whose businesses that have achieved sustainable profitability, enabling them to pursue expansion opportunities.

To counter this, the New Regulation offers incentives for spin-off, so that companies are more inclined to opt for spin-offs because they provide special advantages, especially in terms of capital.

Among others, an insurance or reinsurance company that spun-off its sharia unit will be exempted from the minimum capital requirement (IDR500 billion for sharia insurance companies and IDR1 trillion for sharia reinsurance companies).

With this incentive, companies originating from sharia spin-offs will no longer need to meet the minimum capital requirements that apply. This may encourage more companies to undertake spin-offs, as they do not have to worry about the high minimum capital requirement as a condition to start their operations.

Conclusion

In summary, POJK 11/2023 introduces key changes to the spin-off process for sharia units within insurance and reinsurance companies in Indonesia. With extended deadlines, mandatory spin-off provisions, and incentives, the regulation aims to enhance industry resilience while promoting compliance and competitiveness. Companies must carefully plan spin-offs to navigate regulatory requirements and capitalise on the provided incentives for sustainable growth.

If you have any queries on the above, please feel free to contact our team members below who will be happy to assist.

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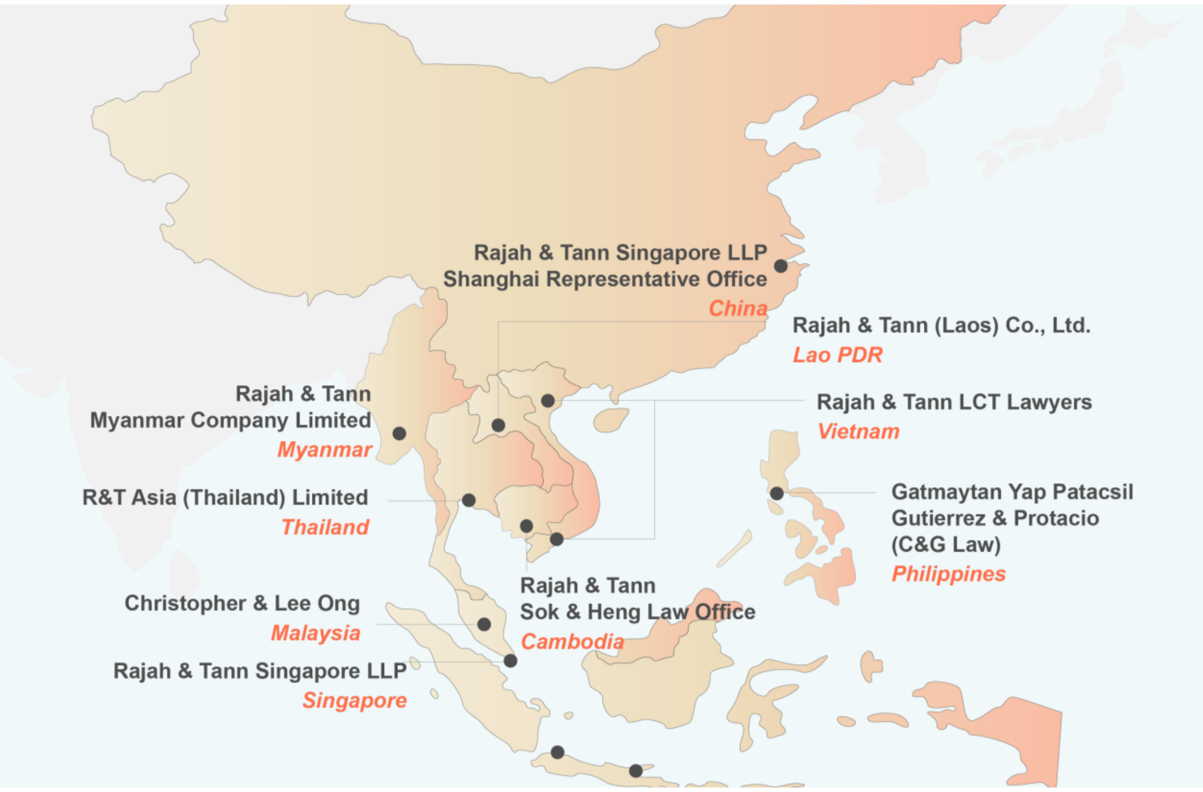

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