

Peer-to-Peer Lending Regulation Released by OJK

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Authors: [Kristo Molina](#), [Putra Nugraha](#), [Fatah Adzkia](#)

In light of the rapid development of peer-to-peer (P2P) lending using information technology (IT) (“**P2P Lending**”) in Indonesia, on 28 December 2016¹ the Indonesian Financial Services Authority (“**OJK**”) enacted OJK Regulation No. 77/POJK.01/2016 regarding IT Based Lending Services (“**Regulation**”). The Regulation introduces various guidelines, obligations and restrictions relevant to P2P Lending services and the organisation of P2P Lending service providers. Some key matters are highlighted in this alert.

To begin, we clarify some basic terms used in the Regulation:

- A P2P Lending Service refers to financial services provided via an online platform that matches lenders and borrowers to facilitate entry into loan arrangements.
- A P2P Lending Service Provider (“**Provider**”) is an Indonesian party that provides, maintains and operates the P2P Lending Services. Under the Regulation, Providers are specified as a financial institution.

What does the Regulation cover?

Providers: Organisation and licensing

- *Form of entity:* Only Indonesian limited liability companies (“**PT**”) or certain type of cooperatives (*Koperasi*) (namely, “services cooperatives (*koperasi jasa*)”) can be Providers.
- *Foreign ownership cap:* For PT Providers, the Regulation provides that foreign investors can own up to 85 percent of total issued and paid up shares of a PT Provider, either directly or indirectly. The Regulation is silent on who may own a *Koperasi* Provider.
- *Registration and licensing:* The Regulation stipulates a two-stage process for Providers, namely the (i) registration stage and (ii) business license stage. Registration certificates and business licenses are issued by OJK.

Existing Providers (i.e. those operating before the Regulations were issued) must register with OJK by 29 June 2017 (being within 6 months of the Regulation taking effect). Once registered, Providers must obtain their business license within one year from the date of the registration certificate; otherwise OJK will declare their registration certificates to be void. As re-registration is not permitted, a void certificate means that a PT or a *Koperasi* can no longer operate as a Provider and it must ensure that any outstanding rights or obligations of each lender and borrower are settled properly.

¹ The Regulation came into force on 29 December 2016.

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- *Capital thresholds:* A PT Provider's issued and paid-up capital must be at least IDR1 billion (approximately USD75,100²) when the PT Provider applies for a registration certificate, and must increase to at least IDR2.5 billion (around USD188,000) by the time the PT Provider applies for a business license. A *Koperasi* Provider is subject to the same capital requirements for its equity at the registration and business license stage.

Borrowers, lenders and loans

While borrowers must be originated from and domiciled in Indonesia, lenders can be local or foreign parties (in this case, offshore loan requirements should be taken into consideration). The loan must be denominated in IDR and the loan amount cannot exceed IDR2 billion for each borrower. Any P2P Lending existing prior to the Regulation taking effect and which amount exceeds IDR2 billion remains in effect until expiry of the loan arrangements.

The Regulation does not specify any maximum interest rates, and the Provider can propose interest rates for a lender and a borrower taking into account fairness (e.g. inflation rate) and the state of the national economy. The agreed interest rate must be stated on the loan agreement made in the online platform.

Virtual account and escrow account

P2P Lending funds must be placed by lenders in virtual accounts, while repayment by borrowers must be conducted through escrow accounts, with both accounts provided by the Provider.

Main obligations and restrictions

Providers are subject to a set of financial and technological obligations and restrictions which are tailored to promote business sustainability in general, and user³ protection in particular.

- *Qualifications of employees and management:* Providers must have, among others: (i) employees who have IT expertise or background⁴; (ii) a data center and disaster recovery center located in Indonesia; and (iii) at least one director and commissioner with at least one year's experience in the financial services industry.
- *Protections for Users:* The Regulation requires P2P Lending agreements⁵ to include specific provisions for each type of agreement, including, among others: (i) interest rate; (ii) tenure; (iii) details of related costs; (iii) fines (if any); and (iv) dispute resolution mechanism. Provider-Lender Agreements must also include the amount of commission and the settlement mechanism if the Provider becomes unable to continue to operate its business, while Loan Agreements must also include the amount of instalments and the collateral (if any).

Another key aspect in user protection emphasized under the Regulation is data privacy and protection of the user's data which Providers collect, retain, process, utilize, and publish. Certain obligations imposed under Law No. 11 of 2008 on Electronic Information and Transaction are adopted under the Regulation, such as the obligation to (i) obtain consents from each user to disclose or use its data; (ii) ensure the stability and safety of the electronic system; and (iii) notify users if their data privacy has been breached.

In addition, Providers are responsible for damage or loss incurred by the users arising from errors and omissions of the management or the employees of the Providers.

- *Reports:* Registered Providers must submit quarterly reports to OJK covering at least: (i) number of lenders and borrowers; (ii) loan rating/quality; and (iii) activities which have been conducted post-registration.

² Using the exchange rate of USD1 = IDR13,300.

³ i.e. borrowers and lenders.

⁴ Evidenced by relevant certification(s) or having at least one year experience in the IT field.

⁵ Namely, agreements between (i) the Provider and the lender ("**Provider-Lender Agreements**") and (ii) the lender and the borrower ("**Loan Agreements**").

Licensed Providers must submit monthly and annual reports to OJK. Monthly reports must include, at least the following: (i) financial and operating performance of Providers; (ii) electronic documents regarding the P2P Lending activity; and (iii) users complaints together with the relevant mitigation measures taken by the Providers. Annual reports must include financial statements and a P2P Lending activity report in accordance with the form prescribed in the Regulation.

- *Prohibited activities:* Providers are prohibited from conducting specified activities, including: (i) conducting any business activities other than as regulated under the Regulation; (ii) acting as lender or borrower; (iii) providing guarantees for third party's liability; (iv) providing recommendations to users; (v) issuing bonds/debt securities (e.g. promissory notes, or medium term notes); and (vi) conducting direct marketing to users or the public through personal communication media without user consent.
- *Sanctions:* Failure to comply with the Regulation may subject the offending Provider to administrative sanctions ranging from a written warning to a revocation of its business license.

What remains unclear?

The Regulation mandates that various aspects of its provisions will be further regulated under an OJK Circular Letter. However, we note that the Regulation remains uncertain in many areas, as detailed below.

Foreign ownership limit for existing PT Providers

It is unclear whether existing PT Providers will be exempted or grandfathered in relation to the new foreign ownership limit. There are no transition provisions or clarifications about adjustments to existing shareholding structures, or investment licenses to be made by existing PT Providers. In practice, it is common for start-up IT companies to receive funding from a foreign source.

Dispute resolution

Significant uncertainties exist in respect of dispute resolution. Can Providers be exposed to lawsuits in circumstances where lenders who feel aggrieved intend to file a lawsuit for loss or damage arising from a default by the borrower? Can the aggrieved lenders sue the Provider as a co-defendant of the borrower? Can the Provider opt to support the lawsuit by providing assistance, or are they obliged to present facts and data relating to the lawsuit? It is not clear if these ambiguities will be addressed by way of an OJK circular or otherwise.

Concluding thoughts

The Regulation is a new and important milestone in the P2P Lending industry, and provides some basic guidelines to support the industry. In our view, the Regulation suggests flexibility in terms of financial transaction matters, which may relate to the fact that the P2P Lending industry in Indonesia is still in its developmental stage. For example, the Regulation has eliminated the maximum interest rate provision which was present under the earlier draft of the Regulation. The effort and attention by OJK certainly shows that P2P Lending has a significant role to play in the financial services industry, especially for lenders and borrowers seeking alternatives for investing or financing.

White & Case in exclusive association with Wicara Cakra Advocates (WCA)
Sampoerna Strategic Square
North Tower, Level 17, Jl. Jend. Sudirman Kav. 45-46
Jakarta 12930
Indonesia

T +62 21 2992 7000

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