

# Indonesia - Digital Banking Business By Rural Bank And Potential Development Of Rural Bank.

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## Introduction

In Indonesia, there is another type of bank which is the Rural Bank (*Bank Perkreditan Rakyat* or "BPR"). BPR has different scope of services and purposes compared to Commercial Bank. BPR is known by the public as the bank to serve the community needs specifically in rural area in Indonesia. Most of the time, BPR serves their customers through traditional interpretation of banking services. This is understandable considering the customers targeted are the society with low or no educational background living in rural area which is predominantly medium-low income. For so long, these types of traditional banking services are welcomed by these consumers even though the digital world keeps changing significantly. However, we must take note that this current situation with Covid-19 pandemic may be the pivotal role that change BPR's traditional banking services and the rural society as the main customers.

## The definition of BPR

The first question which might interest the investor is how BPR is defined and scope of services and how it is different than the *Bank Umum*.

The basic concept of BPR in Indonesia is based on conventional principles in carrying their business activities with no ability to provide money transfer services. Their main purpose of BPR is to serve their local community's needs, including developing micro, small and medium enterprises (MSMEs).

Under Law No. 7 of 1992 on Banking, as amended by Law No. 10 of 1998 ("**Banking Law**"), in general BPR shall cover the following business activities:

- a. mobilizing funds from society in the form of deposits like time deposits, savings, and/or others of similar types;
- b. providing loan;
- c. providing financing and placement of funds based on the Shariah principle, in accordance with the provisions stipulated by Bank Indonesia;
- d. placing their funds in the form of Bank Indonesia Certificates (*Sertifikat Bank Indonesia* or SBI), time deposits, deposit certificates, and/or savings at other banks.

Unlike Commercial Bank, BPR is prohibited, i.e. (i) to receive deposits in the form of giro and participate in payments; (ii) to have capital participation; (iii) to be engaged in the insurance business; and (iv) to undertake business activities other than the above <sup>[1]</sup>.

### **The digital banking era of BPR**

When Indonesia faces the pandemic of Covid-19, the style and function of the banking services also changes significantly. This pandemic condition also gives a push to BPR to evolve in the world of digital banking era. Luckily some of the OJK regulations, namely Regulation No. 12/POJK.03/2016 on Business Activities and Office Network Area based on Rural Bank Core Capital have covered the basic electronic banking services which can be conducted by BPR, even though it is strict to only allow the BPRKU 3 (as further explained in the next section).

BPRKU 3 are allowed to provide Electronic Banking covering: (i) phone banking that allows the customer to execute transactions by calling the BPR, (ii) SMS banking that allows the customer to obtain information or to execute banking transaction, (iii) mobile banking that allows the customer to execute transactions through mobile phone, and (iv) internet banking that allows the customer to execute transactions through the internet network, only for BPR that provides *Laku Pandai* services. Those Electronic Banking services basically can be utilized to support BPR banking service at most, subject to the related Regulation No. 12/POJK.03/2016

However, based on our interview with some of BPRs, a lot of BPR cannot utilize most of the digital banking facilities in their daily business operation as they still conduct business conventionally and therefore require physical document verifications and wet signature when opening bank accounts, creating security interest, etc. For instance, since BPR is divided their reach of services based on zones, for BPR is difficult to conduct verification online on whether such person is domiciled or working in the area where such BPR is conducting their business. They believe that to conduct such verification, they need to verify such person face to face with the original documents on hand.

The next question that might pop to welcome the new future of the digital banking era of BPR is on whether the rural society is ready or not, considering that BPR is to reach the rural area and society where technology and digital banking seem unrecognizable.

### **Scope of Services of BPR**

Based on the core capital, a BPR is classified into 3 classes, namely BPRKU 1, BPRKU 2, and BPRKU 3. Such classes shall determine business activities allowed to be carried out and the area of the office network. BPRKU 1 is BPR with core capital of less than IDR15 billion; BPRKU 2 is BPR with core capital between IDR15 billion and less than IDR 50 billion; and BPRKU 3 is BPR with core capital at least IDR 50 billion.

BPRKU 1 shall be able to carry out the following business activities:

1. fund collection in the form of savings (including deposit, loan received),
2. fund disbursement
3. fund placement (demand deposit, time deposit, certificate of Bank Indonesia)
4. other activities to support business activity:
  - activities as agents of financial services using virtual offices in the framework of inclusive finance (*Laku Pandai*);
  - payroll services for customers of BPR;
  - partnership activities in the framework of fund transfer that is limited to the receipt of remittance from overseas;
  - marketing activities of Electronic Money from other issuers;
  - fund transfer for its own and customer's interests through the account of BPR in commercial banks;
  - partnership activities with insurance companies for referral of insurance products to customers related to products of BPR;
  - to receive deposits of fund for the purpose of bill payment services such as payment of electricity, telephone, water bills, and taxes; and
  - activity as the issuer of ATM Card, for BPRKU 1 that has a minimum core capital of IDR6 billion.

BPRKU 2 shall be able to carry out the following business activities:

- all business activities that can be carried out by BPRKU 1
- money changer business activities; and
- acting as issuer of Debit Card and Electronic Money.

BPRKU 3 shall be able to carry out the following business activities:

- all business activities that can be carried out by BPRKU 2;
- provide electronic banking services; and
- Organizer of financial services using virtual office in the framework of inclusive finance (*Laku Pandai*).

### **The new potential development of Rural Bank**

In the spirit of full motivation and support from the Financial Services Authority (*Otoritas Jasa Keuangan* or “**OJK**”) of Indonesia on BPR’s development and function towards the rural area, OJK has an intention to amend the current regulation which is Regulation No. 20/POJK.03/2014. The draft of such amendment has been prepared and then published on OJK website on 9 September 2020 (***Draft***).

The newly published amendment Draft basically still catches the previous and same intention of the function of the Rural Bank in Indonesia. Even though the spirit is the same, under the new Draft of the amendment, the Authors can find the major differences which might put more attention on the authority and function of OJK to supervise and rule the BPR. The enhancement of such additional power and authority of OJK is believed to overrule and give detailed attention to BPR which mostly deals with citizens within rural area that sometimes have no access to the Commercial Bank (or locally known as *Bank Umum*).

### **The legal entity of BPR**

Based on the Draft, the establishment of the BPR could be based on (i) application from the founder / prospect investors; or (ii) the change of license from Commercial Bank to BPR.

As the Authors note, the point (ii) is a new process being address in the Draft. Such change of license can be from (I) the initiative of the Commercial Bank or through decision from the OJK.

With regards to the type of legal entity of the BPR, it could be in form of Limited Liability Company; Limited Liability Regional Owned Company (*Perusahaan Perseroan Daerah*); General Regional Owned Company (*Perusahaan Umum Daerah*); or Cooperative (*Koperasi*).

Further, the Draft requires several provisions to be incorporated in the Articles of Association of BPR, among others: (i) clearly states the objectives and purposes as a BPR, (ii) requires every change in capital and Board of Director (“**BOD**”) and Board of Commissioners (“**BOC**”) first shall obtain approval from OJK.



### **Minimum capital of BPR**

One of the highlights that the Authors would like to spot in the Draft is a significant increase in the minimum paid up capital of BPR. Under the Draft, in article 6, the minimum paid up capital for BPR in (i) zone 1 is IDR 100,000,000,000 (one hundred billion Indonesian Rupiah); (ii) zone 2 is IDR 50,000,000,000 (fifty billion Indonesian Rupiah); and (iii) zone 3 is IDR 25,000,000,000 (twenty billion Rupiah). Comparing to the current applicable POJK, where the minimum paid up capital of BPR in (i) zone 1 is IDR 14,000,000,000 (fourteen billion Indonesian Rupiah); zone 2 is IDR 8,000,000,000 (eight billion Indonesian Rupiah); and zone 3 is IDR 6,000,000,000 (six billion Indonesian Rupiah). Zone 1 is related to higher economic potential and tighter financial competition between financial institutions, while Zone 4 is related to lower economic potential and looser financial competition between financial institutions.

Another highlight also relates to the authority of OJK to stipulate a higher standard of minimum paid up capital under certain reasons, such as the rural development situation, certain government policy, or the activities of the BPR itself that might require a higher operational expenses.

Such minimum paid up capital, comparing to the current POJK, must be injected in full payment in form of deposits in other banks. The source of the fund also cannot be from any loan structure.

### **The foreign investment ownership of BPR**

In comparison with the previous POJK and the Draft, the foreign investment ownership of BPR is still prohibited. However, OJK adds new clauses in the draft where it is possible for legal entity registered in the Indonesian Stock Exchange to own the ownership of BPR, in which the shareholders could be foreigner or foreign entity as long as it is not registered in the articles of association, as temporary, and does not qualify as the controller in BPR. The Authors believe that this has opened a slight opportunity for foreign investors to invest through such structure, even though the opportunity is still in question favor the foreign investor.

### The license of the Rural Bank

BPR might only conduct their business and provide their approved banking services with a license granted by OJK and Bank Indonesia (to the extent applicable).

Based on the Draft, the application of the license shall take place in two major stages:

- principle approval, meaning approval to conduct preparations for establishing a rural bank; and
- operational license, meaning a license to conduct operations as a commercial bank or rural bank after the preparations referred to in letter (a) above have been completed.

Principle approval application shall be submitted by the Controlling Shareholder (*Pemegang Saham Pengendali* or PSP) (owned at least 25% of the shares) of the BPR by attaching the following documents, among others:

- the draft of Deed of Establishment;
- the ownership list (*The Author notes that this is a new requirement that appears in the Draft*);
- prospective members of BOD and BOC, as well as documents required for fit and proper test by OJK;
- organizational structure, manpower structure, job description, as well as the standard operational procedures;
- potential and worthiness analysis;
- system plan and working procedures;
- the capital payment receipt in the form of deposit slip;
- statement letters signed by the prospective shareholders that the fund does not come from: (i) loan or any kind of financing facility from Bank/other parties, unless sourced from State Budget (*Anggaran Pendapatan Belanja Negara* or "APBN"); and (ii) does not come from and for money laundering;
- list and financial statement of the financial service institutions owned by prospective PSP (*The Author notes that this is a new requirement that appears in the Draft where OJK requires a detail on the financial statement of the entity owned by PSP*);
- evidence of full payment of licensing application in connection to the establishment of BPR to OJK.

Upon receiving the application, OJK shall review the completeness of the application and issue the approval/rejection within 30 working days as the application is deemed complete. Such a 30-days-period is excluding time given to the applicant to complete, fix, revise, and/or update the requested documents in relation to the principal approval application. The Author notes that this 30-days-period is shorter than the current POJK (40 working days), meaning that it aims for a faster application process. However, at the same time, the Author also notes that OJK is given additional authority to request additional supporting documents (which has not been requested previously under the regulations) and more timeline for the completeness process of the additional supporting documents during the application. This somehow at the same time will also give more burden on the Investors during the application and strict timeline to satisfy the additional supporting documents.

While reviewing the application, OJK may also request for presentations (offline or online presentations) on: (i) fit and proper test of the members of BOD, BOC, and the Controlling Shareholder; and (ii) and the financial performance and the compliance in relation to BPR application or other financial institutions owned by the Controlling Shareholder. With the consideration of the pandemic situation, the Author views that online presentation may be a solution to amid the COVID-19 pandemic as well as to accelerate the utilization of technology in BPR itself.

After successfully obtaining the principle approval, the applicant may file for an operational license to OJK by attaching several documents, among others: operational readiness evidence (electronic system, list of fix assets and inventories) and list and financial statement of BPR and/or other financial institutions owned by the prospective Controlling Shareholder. The Author notes that these are newly requested documents in the process of establishment.

After obtaining the operational license, BPR might start their banking services to the assigned rural area.

**The duty to report to OJK and/or to obtain approval from OJK**

BPR's daily activities fall under the supervision of OJK, therefore, there are several actions that need prior approval from OJK or triggers reporting obligation to OJK, among others:

No.	Actions	Obtain Approval	Reporting Obligation	Draft Reference
1	Carry out business activities after obtaining OJK's approval		√	Art. 18
3	Change of shareholders, Controlling Shareholders, latest controlling shareholders of legal entity owning the BPR		√	Art. 43
4	Change in shareholder composition (During the change of shareholder composition, in case there is new PSP, such PSP must provide the financial capability analysis and the 3 years projection prepared by independent consultant)	√ (prior the change)	√ (after the change)	Art. 48
7	Change in paid-up capital	√	√	Art. 44 and 47
8	Change in the composition of BOD and/or BOC	√	√	Art. 43, Art 62 and 65
9	Death of members of BOD and/or BOC		√	Art. 63
10	Change in authorized capital		√	Art. 52
11	Re-appointment of BOD and/or BOC members		√	Art. 66
12	Appointment, change in, and/or removal of the Executive Officer		√	Art. 67
13	Change in the address of headquarter and/or branch office	√	√	Art. 88 and 92
14	Closure of branch office	√	√	Art. 102
15	Change of BPR's name	√	√	Art. 108
16	Exhibition event		√	Art. 84
17	Electronic Banking		√	Art 87



### **Last Note**

The Author understands that the impact of this Covid-19 pandemic is also faced by the rural area in which they might require additional investment or loan to survive during this pandemic. The Author believes that with the existence of BPR, the rural society might be given an opportunity to have additional loan to continue their business. However, on the other hand, we also need to take note on whether the BPR itself can continue growing during this Covid-19 pandemic with a higher risk of collapse once their customers cannot give any guarantee anything. Specifically for the BPR, unfortunately, the new Draft of POJK has not completely addressed this situation to which extent the BPR can be protected during this pandemic.

### **For further information, please contact:**

**Freddy Karyadi, Partner, ABNR**  
+62818103949  
fkaryadi@abnrlaw.com

**Christine Hakim, Associate, ABNR**  
chakim@abnrlaw.com

**Ivan F. Irawan, Associate, ABNR**  
iirawan@abnrlaw.com

[1] Article 13 of Banking Law