

Worry no more, foreign investors! Indonesia established a sovereign wealth fund

19 January 2021

In line with the spirit of bolstering investment from foreign investors into Indonesia with the aim to create new job opportunities as mandated by Law No. 11 of 2020 on job creation (Omnibus Law), the Government of Republic of Indonesia issued the implementing regulations of Omnibus Law for the creation of Indonesia's first sovereign wealth fund Lembaga Pengelola Investasi (LPI). LPI is officially created by virtue of Government Regulation No. 73 of 2020 on Initial Capital of LPI and Government Regulation No. 74 of 2020 on LPI. Both government regulations were issued on 14 December 2020 and came into force on 15 December 2020.

With the government regulations now in place, the LPI aspires to be a trusted investment partner for Indonesia's long term and sustainable economic development. President Joko Widodo in his recent interview described the LPI as a breakthrough for the funding needed by the government to build and develop infrastructure domestically pointing out that public debt was mounting, while state-owned entities (SOE) had a limit in their capacity to borrow funds. From media reports, we understand that LPI is targeted to commence its operation by second quarter of 2021 while at the moment the selection of supervisory board members are currently ongoing.

In anticipation of its launch this year, the United States (U.S.) and Japan have pledged US\$2 billion and US\$4 billion respectively to the LPI¹.

¹ <https://jakartaglobe.id/business/japan-pledges-4b-to-indonesias-sovereign-wealth-fund>

What is LPI?

The LPI is an Indonesian legal entity established as a sui generis (granted special authority) for the purpose of managing central government investment (i.e. asset management in the form of money or property or for the benefit of the central government which aims to make a profit and economic benefits).

The LPI is owned entirely by the government and directly responsible to the president of the Republic of Indonesia. LPI is established to attract capital (sovereign, private, and others) to invest in economically viable strategic sectors of the Indonesian economy, supporting sustainable development and boosting economic growth.

What is the main function and authority of the LPI?

The main function of the LPI is to manage central government investments as well as planning, organizing, supervising and controlling, and evaluating such investments. To implement that function, the LPI is authorized to conduct the following activities:

1. Placing funds in financial instruments.
2. Carrying out asset management activities.
3. Cooperating with other parties including trust fund entities.
4. Determining potential investment partners.
5. Giving and receiving loans.
6. Administering assets.

In doing the abovementioned activities, the LPI may cooperate with investment partners, investment managers, SOEs, government agencies or institutions, and/or domestic and foreign entities.

How much capital has been contributed into LPI?

As provided in GR 74/2020, the total amount of LPI's capital has been set at IDR75 trillion, of which IDR15 trillion has been injected in cash pursuant to the other government regulation which specifies that this amount as a separate state asset which is sourced from the Indonesian state budget for 2020 while the remaining capital (e.g. IDR60 trillion) must be added gradually until 2021. We understand from media reports that the source of funds will be coming from 2021 state budget

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Who will manage the LPI?

The LPI will be managed by the board of directors with the full supervision by the board of supervisors.

² <https://jakartaglobe.id/business/japan-pledges-4b-to-indonesias-sovereign-wealth-fund>

Set out below are the key features of the boards:

Boards	Duty	Members	Subordinates
Board of supervisors	<p>Supervising operational activities carried out by the Board of Directors</p> <p>Authorities The authorities possessed by the board of supervisors are, among others, to appoint and dismiss the members of board of directors, to propose any increase and/or reduction in LPI capital to the president and to approve annual financial statements of LPI.</p>	<ol style="list-style-type: none"> 1. Minister of Finance as chairperson. 2. Minister of SOE as a member. 3. Three people from professional elements as members (the professionally-related members are to be appointed for a five-year term of office and may only be re-appointed for one subsequent term of office) 	<ol style="list-style-type: none"> 1. Secretariat 2. Audit committee 3. Ethics committee 4. Remuneration and human resources committee <p>To be appointed and dismissed by the board of supervisors</p>
Board of directors	<p>Organizing the day-to-day operational management of the LPI.</p> <p>Authorities The authorities possessed by the board of directors are, among others, to formulate and determine LPI policies, implement LPI policies and operational management, and represent the LPI inside and outside the court</p>	<p>Five people, all of whom come from professional elements who are appointed by the board of supervisors for a five-year term of office with a possible one subsequent term of office.</p>	<ol style="list-style-type: none"> 1. Investment committee. 2. Risk management committee. <p>To be appointed by the board of directors decision.</p>

Recently, President Joko Widodo already submitted the names for the candidates of the board of supervisor of LPI to the House of Representatives on Tuesday, 12 January 2021³.

How LPI is going to position itself to the international guidelines on the sovereign wealth fund that have been provided in the Santiago Principles?

While not clearly specified under either the Omnibus Law or GR 74/2020, we understand from the media reports and the various clarifications provided by the Ministry of Finance and Ministry of State Owned Enterprise that the sovereign wealth fund model will be the combination of development fund and stabilization fund.

What are the assets of LPI and how is it going to be managed?

The assets of LPI can originate from several sources, namely:

1. LPI capital (as mentioned above).

2. Proceeds from businesses and asset development.
3. Transfers of state or SOE's assets.
4. Grants.
5. Other lawful sources (e.g., bonds).

In terms of increasing the value of its assets, GR 74/2020 allows LPI to cooperate with third parties. In selecting its partners, LPI will appoint its partners based on good reputation, financial capability to support its commitment to the investment, and expertise in the field of investment to be undertaken. Such cooperation should be conducted by way of:

1. Granting or receiving of the authority to manage (kuasa kelola).

This cooperation should be conducted through the handing over of agreed assets to third parties or through receiving of the management of the agreed assets from third parties through the granting of authorization.

2. Establishing a joint venture company.

The establishment of joint venture companies in a) sole drinking-water distribution within cities or regencies; or b) domestic oil-and-gas extraction sectors should be conducted on the condition that the LPI holds majority shares ownership and should have at least a veto in business decision-making situations. For investments in other sectors, there are no clear guidelines on the similar requirements.

3. Any other cooperation forms.

Is LPI allowed to provide or obtain loans?

Yes, LPI is allowed to provide or obtain loans in the form of credit facilities, debt securities, or other loan instruments. In providing or obtaining loans GR 74/2020 provides that those activities should be based on a risk analysis that should address the following elements at the least:

1. The purpose of providing or obtaining the loans.
2. Assessment on the relevant project and/or investment feasibility.
3. Loan repayment ability.

Is LPI allowed to grant security in obtaining loans?

In order to obtain loans, LPI is allowed to pledge its own assets. The LPI can also act as a security provider for the loan received by joint-venture companies established by LPI and its partners.

Is LPI protected against bankruptcy?

The LPI cannot be declared bankrupt unless it can be proven that the LPI is in an insolvent condition based on the results of insolvency testing conducted by an independent agency appointed by the Minister of Finance.

Closing remarks

The establishment of the LPI should be seen as a historic move from Indonesian government to create more job opportunities and attract more investment into Indonesia with the main intention to support economic growth in general. The grand idea behind the establishment is to function as a strategic partner for foreign and domestic investors and also LPI is expected to take an active role in the enhancement value of assets under management. In managing the assets, LPI can also establish investment-managed funds (in the form of joint venture companies,

mutual funds, or investment collective contract) as well as participating in funds established by third parties. We understand from media reports that the initial investment would focus in infrastructure sector such as toll roads, airports, and seaports. While the healthcare, tourism, and technology sector will be the next priority sector.

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