

Indonesia: Key Employment Considerations in M&A Transactions

Beyond the potential return on investment, investors should carefully consider employee rights and potential employment liabilities in M&A transactions.

IN BRIEF

Indonesian laws provide a safeguard for employees of the target/merging companies in the form of compensation rights due to merger and acquisition (“M&A”) transactions. For sure, M&A transactions are largely driven by commercial aspects. But investors should consider that there should be cash allocated to be disbursed to the relevant employees due to M&A. Investors should really be aware of this requirement, especially for acquiring or merging human capital-intensive companies.

KEY EMPLOYMENT CONSIDERATIONS IN M&A

Aspect	Key Considerations
Compulsory Notification to Employees	Quite often than not, the policy (including the employment policy) of the merging and acquired companies may drastically change post M&A transaction. With the spirit of protecting the employees, the Indonesian Company Law requires the Board of Directors to, among others, notify the proposed transaction in writing to the employees by no later than 30 days before the notice of the General Meeting of Shareholders approving the proposed M&A transaction.
Termination Payments	A merger or acquisition does not automatically terminate existing employment relationship. However, GR 35/2021 provides specific termination rights and statutory entitlements depending on the nature of the transaction and the circumstance of the termination. Merger In a merger, GR 35/2021 does not distinguish between employees of the merging company and those of the surviving company for purpose of the relevant termination provisions. Unlike in an acquisition, the exercise of the termination rights in a merger either the employee or the employer may choose not to continue the employment relationship. If the employment relationship is terminated in this circumstance, the employee is entitled to receive 1x statutory severance pay, 1x long-service pay, and compensation of rights. The above requirements apply for both definite-term employees (“PKWT”) and indefinite-term employees (“PKWTT”) in a merger. Acquisition <u>PKWTT Employees</u> Different considerations apply in an acquisition. Where the employer terminates the employment relationship due to an acquisition, the PKWTT employee is entitled to receive 1x statutory severance pay, 1x long-service pay, and compensation of rights.

Aspect	Key Considerations
	However, if the acquisition results in change to the PKWTT employee's employment terms and the PKWTT employee does not wish to continue the employment relationship, the PKWTT employee is entitled to receive 0.5x statutory severance pay, 1x long-service pay, and compensation of rights. <u>PKWT Employees</u> If the PKWT employees are terminated by the target company before the end of the employment term, the employer remains required to pay statutory compensation calculated based on the current employment term in accordance with GR 35/2021.
Employment legal due diligence	Legal due diligence in the employment aspects is inevitable to avoid any employment legal risks, especially for human capital-intensive companies. For example: - Whether there is an ongoing industrial relations dispute in the relevant company - Whether the mandatory employment organizational structure and qualified employees are already available e.g., requirements in insurance companies The relevant transaction documents should also be drafted and structured protecting the relevant investors towards any employment legal risks.

TRANSACTION PLANNING CONSIDERATIONS

Aspect	Key Considerations
Employment Due Diligence	Review the employment agreements, PKWT compliance, collective labour agreements, outstanding disputes, accrued severance, employee benefits, BPJS compliance, outsourcing arrangements and other material historical employment liabilities.
Transaction Structuring	Quantify material employment exposure and consider appropriate protections through representations and warranties, indemnities, purchase price adjustments, conditions precedent or pre-closing remediation obligations.
Post-Closing Integration	Assess proposed changes to remuneration, benefits, reporting lines or other employment conditions before implementation.
Transaction Documents	Clearly allocate responsibility for employee notification, severance liabilities, KPPU notification, regulatory costs and post-closing cooperation.

RECENT REGULATORY DEVELOPMENTS

Constitutional Court Decision No.168/PUU-XXI/2023

The Constitutional Court, through Decision No 168/PUU-XXI/2023 dated 31 October 2024, held that the severance pay formula under Article 156(2) of the Manpower Law must be interpreted as a minimum statutory entitlement, rather than a fixed amount. Accordingly, the statutory severance calculation represents the minimum amount payable, while higher entitlements may apply under the relevant employment agreement, company regulation or collective labour agreement.

For M&A transactions, investors should therefore not rely solely on the statutory formula when assessing potential termination costs. The target company's employment arrangement should also be reviewed during legal due diligence, as they may provide higher entitlements and consequently increase the overall employment-related exposure of the transaction.



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