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INDONESIA CORPORATE GOVERNANCE MANUAL

Second Edition

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OJK OTORITAS JASA KEUANGAN

IFC International Finance Corporation WORLD BANK GROUP

Creating Markets, Creating Opportunities

INDONESIA CORPORATE GOVERNANCE MANUAL

Second Edition

Jakarta, June 2018

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The Indonesia Corporate Governance Manual second edition provides an overview of general corporate governance principles applicable to Indonesian limited liability companies. The Manual also addresses certain corporate governance principles for Indonesian companies that are active in the financial sector and are supervised by Indonesia's Financial Services Authority (*Otoritas Jasa Keuangan*). Companies in specific sectors, such as oil and gas, mining, and power, may be subject to different requirements which are either additional to or variations of those discussed in this publication. The laws of the Republic of Indonesia are frequently amended, such that legal rules referenced in this edition may be superseded by new legislation following the publication of this Manual.

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Foreword

Azam Khan

IFC Country Manager
Indonesia, Malaysia, and TimorLeste

It is my pleasure to present the 2nd edition of the Indonesia Corporate Governance Manual. Commissioned by IFC, this version updates the first edition of the Manual that was published in January 2014, incorporating recent corporate governance changes applicable to public and listed companies in Indonesia, as well as capturing major developments in the global landscape. Indonesia's Financial Services Authority issued the first "comply or explain" corporate governance guidelines for public companies in 2015 and since then has adopted additional regulations to raise governance standards among Indonesian companies, promote transparency and accountability in the corporate sector, and enhance public trust and confidence in Indonesian capital markets.

IFC, a member of the World Bank Group, is the largest global development institution focused on the private sector in emerging markets. As an investor, IFC continues to engage with our clients to influence change and help address various challenges companies face in emerging markets. A key aspect of our advisory support is to help IFC clients strengthen their governance practices. I believe that Indonesian companies will

find this publication useful in providing guidance on Indonesia's corporate governance regulatory framework and in aligning their governance with international best practices.

Regards,

Azam Khan
IFC Country Manager for Indonesia, Malaysia, and Timor-Leste

Wimboh Santoso

Chairman
Board of Commissioners
Otoritas Jasa Keuangan

I would like to congratulate IFC on the publication of the second version of its Indonesia Corporate Governance Manual. OJK and IFC have maintained a close collaboration in improving corporate governance practices of listed companies in Indonesia since the launch of the IFC Corporate Governance Program for Indonesia in 2012. A key objective of the Program is to raise awareness on good corporate governance practices through publications and case studies. This Manual contains pertinent legal references and practical guidance for local companies to implement good corporate governance practices.

OJK issued an Indonesia Corporate Governance Roadmap in 2014 to improve the country's regulatory framework and align governance practices of local companies with those of their peers in other ASEAN countries. As part of the implementation of the Corporate Governance Roadmap, OJK issued Regulation No. 21/POJK.04/2015 and Circular Letter No. 32/SEOJK.04/2015 on the Implementation of Corporate Governance Guidelines for Public Companies ("OJK CG Guidelines"), which is the country's first "comply or explain" guideline. Our objective was to raise governance standards among public companies while at the same time providing some flexibility for companies to tailor governance practices to their specific situations. To continue the momentum, OJK has issued numerous regulations to govern key elements that are essential to fostering good governance among public and listed companies. Together these regulatory changes are aimed at enhancing accountability and transparency in the corporate sector in Indonesia.

The second edition of the Indonesia Corporate Governance Manual takes into account major corporate governance regulations issued by OJK and other regulatory bodies, in addition to leading international practices and standards. The Manual provides Indonesian companies with an indispensable resource for guidance on corporate governance issues. The Manual also explains the rationale for adopting higher governance standards, which could be useful for reform-minded commissioners and directors to build the business case for implementing good governance practices across their organizations. The Manual will also be a valuable reference to academics, students, researchers, and other stakeholders in providing insights, sharing best practices, and documenting the corporate governance regime in Indonesia.

Corporate governance has an important role in promoting sustainable economic growth by building investor confidence, reducing the cost of capital, strengthening financial markets, and creating jobs. OJK hopes that this Manual will inspire Indonesian companies to adopt and implement good governance practices, not simply as an exercise in regulatory compliance, but as a means to create highly competitive, profitable, and well-governed companies.

Sincerely,

Wimboh Santoso
Chairman of the Board of Commissioners
Otoritas Jasa Keuangan

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Acknowledgement

The Indonesia Corporate Governance Manual Second Edition was produced as part of IFC's Corporate Governance Program in Indonesia. The Program has been in operation since 2012 with generous support from Switzerland's State Secretariat for Economic Affairs (SECO). The Indonesia Corporate Governance Manual was prepared based on other corporate governance manuals published by IFC's Corporate Governance Program and adapted to Indonesia's corporate governance legal framework and practices.

The preparation and publication of this Manual would not have been possible without the efforts of a number of highly dedicated people. The Manual's text was adapted under the direction of Mohsin Chaudhry, IFC Corporate Governance Officer, and Liana Lim Hinch, IFC Consultant. The content was revised with substantial contributions from Emir Nurmansyah, Partner at Ali Budiardjo, Nugroho, Reksodiputro, and his team members, Theodoor Bakker, Senior Foreign Council and Gustaaf Reerink, Foreign Council.

The team is also grateful for continuous support from the Financial Services Authority, including OJK's Chairman Wimboh Santoso, Nur Sigit Warsidi, Director of Accounting Standards and Corporate Governance, and their team in the development of this Manual.

How to Use This Manual

This Manual is divided into 15 chapters:

Chapter 1 : An Introduction to Corporate Governance
Chapter 2 : Company Governance Structure
Chapter 3 : Internal Corporate Documents
Chapter 4 : An Introduction to Shareholder Rights
Chapter 5 : General Meeting of Shareholders
Chapter 6 : Board of Commissioners
Chapter 7 : Board of Directors
Chapter 8 : Corporate Secretary
Chapter 9 : Risk Management and Internal Control
Chapter 10: Information Disclosure
Chapter 11 : Material Corporate Transactions
Chapter 12 : Dividends
Chapter 13 : Charter Capital
Chapter 14 : Corporate Securities
Chapter 15 : Corporate Governance Framework of Indonesian State-Owned Enterprises

The Indonesia Corporate Governance Manual discusses key corporate governance elements that have been contextualized to take into account current Indonesian laws and regulations as well as international best practices. While it is recommended to read the entire Manual to gain a full understanding of the corporate governance framework in Indonesia, it is not necessary to read all the chapters in chronological order. The Manual includes examples, illustrations, and checklists to aid clarity and understanding.

The following tools will reappear at various intervals in the text:

The Chairman's Checklist

The Chairman's Checklist is intended to help the Chairman of the Board of Commissioners focus board discussions on key issues and common challenges surrounding a particular governance topic.

Best Practice

Best Practices illustrate recommended governance practices based on the OECD Principles of Corporate Governance and leading international standards/ examples.

Comparative Practice

Comparative Practices illustrate how other countries approach specific corporate governance issues. They highlight red flags, such as common corporate governance abuses as well as exemplary governance models/practices.

ABBREVIATIONS

AGMS	Annual General Meeting of Shareholders
AoA	Articles of Association
ASEAN	Association of South East Asian Nations
ATMR	*Aset Terimbang Menurut Risiko* (Balanced Assets based on Risk)
BKPM	*Badan Koordinasi Penanaman Modal* (Indonesia Investment Coordinating Board)
BoC	Board of Commissioners
BoD	Board of Directors
CG	Corporate Governance
COSO	The Committee of Sponsoring Organizations
EGMS	Extraordinary General Meeting of Shareholders
FY	Fiscal Year
G20	The Group of Twenty, comprises 19 countries plus the European Union
GMS	General Meeting of Shareholders
ICL	Indonesian Company Law
IDX	Indonesia Stock Exchange
IFC	International Finance Corporation
IFRS	International Financial Reporting Standards
ISO	International Organization for Standardization
KPMM	*Kewajiban Penyediaan Modal Minimum* (Minimum Capital Provision Obligation)
KSEI	*Kustodian Sentral Efek Indonesia* (Indonesia Central Securities Depository)
LPS	*Lembaga Penjamin Simpanan* (Deposit Insurance Corporation)
MMT	Ministry of Manpower and Transmigration
MOF	Ministry of Finance
MOLHR	Ministry of Law and Human Rights
OECD	Organization for Economic Co-operation and Development
OJK	*Otoritas Jasa Keuangan* (Financial Services Authority)
POJK	*Peraturan OJK* (OJK Regulation)
PSAK	*Peraturan Standar Akuntansi Keuangan* (IFRS)
PT	*Perseroan Terbatas* (Limited Liability Company)
SEOJK	*Surat Edaran Otoritas Jasa Keuangan* (Circular Letter of OJK)
US GAAP	United States Generally Accepted Accounting Principles

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CHAPTER 1

An Introduction to Corporate Governance

THE CHAIRMAN'S CHECKLIST

- Do the general meeting of shareholders (GMS), the board of commissioners (BoC), and the board of directors (BoD) understand the concept of corporate governance and its significance to the company and its shareholders?
- Are key officers familiar with the G20/OECD Principles of Corporate Governance as well as the legal and regulatory framework that is applicable to companies in Indonesia?
- Do the BoC and BoD understand their roles and responsibilities?
- Does the company have a robust internal control and risk management framework?
- Has the BoC developed a clear governance policy?
- Have steps been taken to improve the company's corporate governance practices in accordance with this policy?
- Does the company follow mandatory corporate governance requirements and disclose information on compliance to shareholders and stakeholders in the annual report? Has the company adopted its own corporate governance code? Has the company included a report on its corporate governance structure and practice in the annual report?

Is the company familiar with the main institutions active in the field of corporate governance that can serve as external resources?

Corporate governance has become a familiar term in Indonesia. The private sector's role in promoting economic growth and creating jobs began to accelerate with the introduction of the Indonesian Company Law in 1995. The two decades that followed brought increasingly sophisticated domestic production, private enterprise growth, and increased global competition. The downside to these developments has been the occurrence of major corporate scandals. While various domestic and international efforts have made corporate governance a household phrase, few Indonesian companies appear to truly appreciate the depth and complexity of this topic. Indeed, companies in Indonesia often introduce corporate governance reforms only at a superficial level, such as to support a public relations strategy. In doing so, they miss valuable opportunities to introduce the internal structures and processes that enable a company to maintain shareholders' confidence, increase access to capital, and reduce vulnerability to financial crises.

This chapter defines corporate governance, makes a business case for its implementation, and provides an overview of the legal, regulatory, and institutional frameworks relevant to corporate governance in Indonesia today.

1.1 Definition of Corporate Governance

There is no single definition of corporate governance that applies to all situations and jurisdictions. Variations arise depending on the institution, national context, and legal tradition.

IFC defines corporate governance as "the structures and processes by which companies are directed and controlled." The Organization for Economic Co-operation and Development (OECD), which published its Principles of Corporate Governance in 1999 and reviewed the Principles in 2004 and 2015, offers a more detailed definition:[1]

"Corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined."

Most definitions that center on the company itself (an internal perspective) have certain elements in common. These can be summarized as follows:

- **Corporate governance is a system of relationships, defined by structures and processes**. For example, the relationship between shareholders (as the providers of capital), the company management, and stakeholders. Through their relationships, shareholders, management, and stakeholders share a mutual interest in maximizing the rate of return from shareholders' investment. Other specific relationships exist between a company's BoD, BoC or other supervisory body, and its shareholders. The BoD must provide shareholders with financial and operational reports on a regular basis and in a transparent manner. The BoC performs a supervisory function over the BoD. As such, the BoD is accountable to the BoC, which in turn must be accountable to all shareholders through the GMS. The structures and processes that define these relationships typically center on specific management performance and reporting mechanisms.

[1] *G20/OECD Principles of Corporate Governance* (Paris: OECD Publishing, 2015), 9.

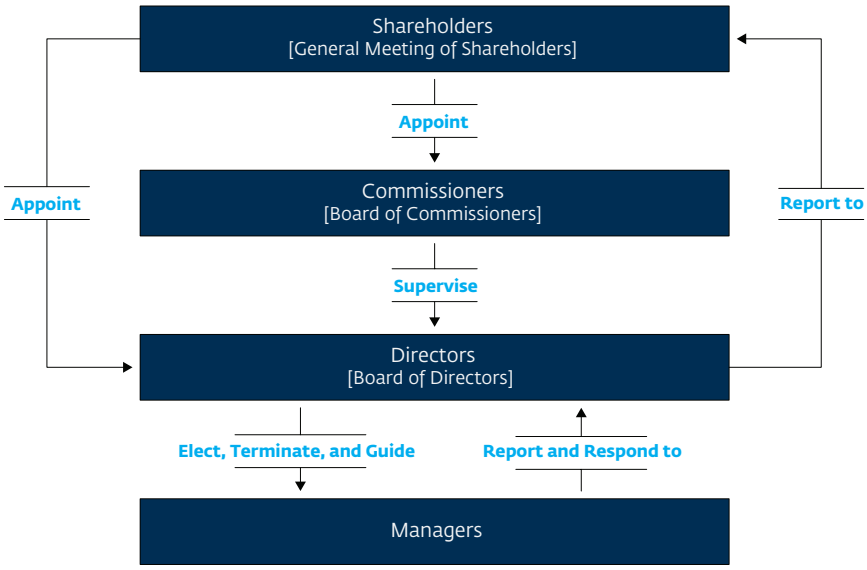
- **These relationships may involve parties with different and sometimes conflicting interests.** The various company organs—the GMS, the BoC, and the BoD—can hold different interests at any given time. Conflicting interests typically exist between shareholders (principals) and managers (agents), also known as the principal-agent problem. A principal-agent problem arises when the person who owns a firm is not the same as the person who manages or controls it. For example, although shareholders are interested in maximizing shareholder value, the BoD may have other objectives, such as maximizing their salaries, which sometimes leads to excessive risk-taking at the expense of the company's long-term interest. Conflicts may also exist within each governing organ, such as between shareholders (majority versus minority, controlling versus non-controlling, individual versus institutional) and company organs (executive versus non-executive, outsiders versus insiders, independent versus dependent). These tensions need to be carefully monitored and balanced.

- **All parties are involved in the direction and control of the company.** The GMS, representing shareholders, makes fundamental decisions such as those concerning the distribution of profits. The BoC is generally responsible for providing guidance and oversight, reviewing and monitoring the implementation of company strategy, and overseeing the BoD's performance. The BoD runs the day-to-day operations, such as implementing strategy, drafting business plans, managing human resources, developing marketing and sales strategies, and managing assets.

- **Corporate governance is designed to properly distribute rights and responsibilities in order to promote stable, long-term value to shareholders.** For instance, with appropriate balancing of the interests between shareholders, the BoC, and the BoD, minority shareholders will have the means to prevent a controlling shareholder from gaining undue benefits through related party transactions, tunneling, or other similar activity.

Figure 1 depicts the relationships between the governing bodies in a basic corporate governance system.

Figure **1** The Corporate Govenance System



The external perspective of corporate governance, on the other hand, concentrates on relationships between the company and its stakeholders. Stakeholders are those individuals or institutions that have an interest in the company. Such interests may arise through legislation or contract, or by way of social or geographic relationships. Stakeholders include investors, as well as employees, creditors, suppliers, consumers, regulatory bodies and state agencies, and the local community or environment in which a company operates.

Many international codes, including the OECD Principles, discuss the role of stakeholders in the governance process. The stakeholder's role in governance has been debated in the past, with some arguing that stakeholders have no claim on the company other than those specifically set forth in law or contract. This view is found in many countries with a common law tradition, such as the United Kingdom, the United States, and Australia. Others argue that companies fulfill an important social function, have a societal impact, and accordingly must act in the broader interests of society. This view, which is present in many countries with a civil law tradition, mostly in continental Europe, such as France, Germany, the Netherlands, and their former regions of influence, recognizes that companies should, at times, act at the expense of shareholders to fulfill stakeholder requests.

Best Practice

A key aspect of corporate governance involves ensuring the flow of external capital to firms. Corporate governance is also concerned with finding ways to encourage shareholders to undertake socially efficient levels of investment in firm-specific human and physical capital. The competitiveness and ultimate success of a corporation is the result of teamwork that embodies contributions from a range of resource providers including investors, employees, creditors, and suppliers. Corporations should recognize that stakeholders' contributions constitute a valuable resource for building competitive and profitable companies. It is therefore in the interest of the company to develop productive cooperation with its stakeholders, establish a governance framework to acknowledge the existence of these interests, and recognize their importance for the company's long-term success.

1.1.1 A Brief History of Corporate Governance

Systems of corporate governance have evolved over centuries, often in response to systemic crises or corporate failures. The first significant example was the collapse of the British South Sea Company in 1720. This created the well-documented South Sea Bubble which revolutionized business law and practice in England. Similarly, much of U.S. securities law was put in place following the stock market crash of 1929. There has been no shortage of other crises, such as the secondary banking crisis of the 1970s in the United Kingdom, the U.S. savings and loan debacle of the 1980s, the 1998 financial crisis in Russia, the 1997-1998 Asian financial crisis (the effects of which were particularly severe in Indonesia, South Korea, and Thailand), and the global financial crisis of 2008.

The history of corporate governance is also punctuated by a series of high-profile company failures. In the United Kingdom, the early 1990s saw the collapse of Barings Bank. The new century likewise opened with the dizzying fall of Enron in the United States, the near-bankruptcy of Vivendi Universal in France, the scandal at Parmalat in Italy, trading fraud at Société Générale, and

the multi-billion dollar Madoff Ponzi scheme. Governments responded to each of these corporate failures–often resulting from lack of oversight, incompetence, or outright fraud–by implementing new governance frameworks such as the United States' Sarbanes-Oxley Act for Public Company Accounting Reform and Investor Protection, other similar national corporate governance codes, and the current trend towards imposing stricter regulatory oversight on banking and financial institutions in many countries.

In Indonesia, the financial crisis of 1997-1998 sparked dramatic social, economic, and political effects. That event caused the Indonesian rupiah to depreciate by almost 80 percent, dramatically increasing poverty. As Furman and Stiglitz note, "The depth of the collapse in Indonesia is among the largest peacetime contractions since at least 1960 (excluding the experience of the transition economies of eastern Europe and the former Soviet Union)."[2] Many experts consider Indonesia's recession to have been fueled by an extremely poor supervision of the financial sector and lax enforcement of central bank regulations, which compounded irregular banking practices.

Although there is still great need for improvement, the Indonesian business community's awareness and understanding of the importance of corporate governance has improved dramatically since then. This change corresponds with ongoing advances made to the legal and regulatory corporate governance framework.

In recent years, Indonesia has implemented a number of initiatives to strengthen its corporate governance regime. These efforts include the establishment of corporate governance institutions and the adoption of new laws (or amendments to existing regulations) that support the implementation of good corporate governance processes. These measures include the establishment of the National Committee on Corporate Governance in 1999 under the supervision of the Coordinating Minister for Economic Affairs. The committee issued Indonesia's first Code of Good Corporate Governance ("CG Code") in 1999, which was later amended in 2001 and 2006. The Capital Markets and Financial Institutions Supervisory Agency, now merged into the Financial Services Authority (*Otoritas Jasa Keuangan* or OJK), also continues to advance and enforce its regulatory framework to improve investor protection. With respect to the banking sector, Indonesia's central bank, *Bank Indonesia*, introduced corporate governance rules in 2006 which it actively monitors and enforces.

Table 1 illustrates key corporate governance developments, including those in Indonesia.

[2] Jason E. Furman and Joseph E. Stiglitz, "Economic Crises: Evidence and Insights from East Asia," *Brookings Papers on Economic Activity*, no. 2 (1998), 3.

Table **1**	A Brief History of Corporate Governance
1600s	The East India Company introduces a Court of Directors, creating a basis for the separation of ownership and control (United Kingdom, the Netherlands).
1776	Adam Smith in *The Wealth of Nations* warns of weak controls over and incentives for management (United Kingdom).
1844	First Joint Stock Company Act (United Kingdom).
1931	Berle and Means publishes its seminal work *The Modern Corporation and Private Property* (United States).
1933-1934	The Securities Act of 1933 is the first act to regulate the securities markets, notably registration disclosure. The 1934 Act delegates responsibility for enforcement to the Securities and Exchange Commission (United States).
1967	Indonesia: The House of Representatives adopts Law No. 1 of 1967 on Foreign Investment.
1968	The European Union adopts its first company law directive (European Union).
1987	The Treadway Commission (COSO) reports on fraudulent financial reporting, confirms the role and status of audit committees, and develops a framework for internal control (United States).
Early 1990s	The Polly Peck (£1.3 billion in losses), BCCI, and Maxwell (£480 million) business empires collapse, leading to calls for improved corporate governance practices to protect investors (United Kingdom).
1992	The Cadbury Committee publishes the first code on corporate governance. In 1993, companies listed on the United Kingdom's stock exchanges are required to disclose governance on a "comply or explain" basis (United Kingdom).
	Indonesia: The House of Representatives adopts Law No. 2 of 1992 on Insurance Business.
1994	Publication of the King Report (South Africa).
1994-1995	Rutteman (on internal controls and financial reporting), Greenbury (on executive remuneration), and Hampel (on corporate governance) reports are published (United Kingdom).
1995	Publication of the Vienot Report (France).

	Indonesia: Adoption of Law No. 1 of 1995 on Limited Liability Companies.
	Indonesia: Adoption of Law No. 8 of 1995 on Capital Markets.
1996	Publication of the Peters Report (Netherlands).
1998	Publication of the Combined Code (United Kingdom).
1999	The OECD publishes the first international benchmark on corporate governance: OECD Principles of Corporate Governance (France).
	Publication of the Turnbull guidance on internal controls (United Kingdom).
	Indonesia: The House of Representatives adopts Law No. 5 of 1999 on Prohibition of Monopolistic Practices and Unfair Business Competition.
	Indonesia: Establishment of the National Committee on Corporate Governance, later changed to the National Committee on Governance.
	Indonesia: Establishment of the Corruption Eradication Commission by Law No. 31 of 1999, later amended by Law No. 3 of 2004.
	Indonesia: Establishment of the Commission for the Supervision of Business Competition by Law No. 5 of 1999.
	Indonesia: Adoption of Law No. 23 of 1999 on Bank Indonesia, later superseded by Law No. 3 of 2004.
2000	Indonesia: The National Committee on Corporate Governance publishes the first Code of Good Corporate Governance (CG Code of 2000).
2001	Enron Corporation, then the seventh largest listed company in the United States, declares bankruptcy (United States).
	Publication of the Lamfalussy Report on the Regulation of European Securities Markets (European Union).
	Indonesia: The National Committee on Corporate Governance publishes its second Indonesia's Code of Good Corporate Governance, an improvement of the previous version of the code (CG Code of 2001).
2002	Indonesia: State-owned enterprises are required to implement corporate governance by the decree of Minister of SOE KEP-117/

	M-MBU/2002 concerning the Implementation of Good Corporate Governance in State-Owned Enterprises.
	Publication of the German Corporate Governance Code (Germany).
	The Enron collapse and other corporate scandals lead to the Sarbanes-Oxley Act (United States); the Winter Report on company law reform in Europe is published (European Union).
2003	The Higgs Report on non-executive directors is published (United Kingdom).
	Indonesia: Establishment of the Center for Reporting and Financial Transaction Analysis (PPATK - *Pusat Pelaporan dan Analisis Transaksi Keuangan*), which is mandated by Law No. 15 of 2002 on Money Laundering. The Law is replaced by Law No. 25 of 2003.
	Indonesia: The House of Representatives adopts Law No. 19 of 2003 on State-Owned Enterprises.
2004	Indonesia: Adoption of Law No. 24 of 2004 on Deposit Insurance Corporation (*Lembaga Penjamin Simpanan* or LPS).
	The Parmalat scandal shakes Italy, with possible European Union-wide repercussions (European Union).
2006	Indonesia: The Central Bank issues a regulation that mandates the banking sector to implement corporate governance through PBI No. 8/4/PBI/2006 on Good Corporate Governance Implementation for Banks.
	Indonesia: The National Committee on Governance publishes its third Indonesia's Code of Good Corporate Governance (CG Code of 2006).
2007	Indonesia: The House of Representatives adopts Law No. 40 of 2007 on Limited Liability Company, which replaces Law No. 1 of 1995, and Law No. 25 of 2007 on Investment, replacing the 1967 Foreign Investment Law.
2012	The United Kingdom amends its Stewardship Code of 2010, marking a key development to enhance the role of institutional shareholders vis-à-vis investee companies (United Kingdom).
2015	Following the global financial crisis in 2008, the OECD conducts a comprehensive review of its CG Principles and issues an updated set of Principles of Corporate Governance (France).
	Indonesia: The Financial Services Authority issues Regulation No. 21/POJK.04/2015 and Circular Letter No. 32/SEOJK.04/2015 on the

	Implementation of Corporate Governance Guidelines for Public Companies.
2016 - 2017	Indonesia: The Financial Services Authority issues Regulation No. 55/POJK.03/2016 and Circular Letter No. 13/SEOJK.03/2017 on the Implementation of Corporate Governance for Banks.
2018	The United Kingdom will issue revisions to its Corporate Governance Code, scheduled to take effect in June 2018. Among the revisions, the new code will force some 900 publicly listed company to reveal the pay ratio between management and employees (United Kingdom).

1.1.2 International Standards of Corporate Governance

The past decade witnessed the development of numerous codes of corporate governance principles worldwide. More than 200 codes have now been written across 103 countries and regions, some of which are designed to have international application. Most of these codes focus on the role of the BoC and/or BoD in a company.

Among these, only the OECD Principles on Corporate Governance address both policymakers and businesses and focuses on the entire governance framework (shareholder rights, stakeholders, disclosure, and board practices). First published in 1999 and revised in 2004, the OECD issued its latest revision in 2015 to address the developments arising out of changing circumstances in the corporate and financial sectors, including the complexity of the investment chain, the changing role of stock exchanges, and the emergence of new investors and trading practices. This version was expected to support investment as a powerful driver of growth. The OECD Principles have since gained worldwide recognition as a reference point for good corporate governance. Although the OECD Principles primarily focus on publicly traded companies, both financial and non-financial, they provide a useful benchmark for improving corporate governance practices of privately-held companies. Many national corporate governance codes, including Indonesia, were developed based on the OECD Principles.

The OECD corporate governance framework is built on four core values:

- **Fairness:** The corporate governance framework should protect shareholder rights and ensure the equitable treatment of all shareholders,

including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violations of their rights.

• **Responsibility**: The corporate governance framework should recognize the rights of stakeholders as established by law, and encourage active cooperation between companies and stakeholders in creating wealth and jobs and ensuring sustainability.

• **Transparency**: The corporate governance framework should ensure that timely and accurate disclosure is made of all material matters regarding the company, including financial status, governance structure, performance, and ownership.

• **Accountability**: The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and shareholders.

In 2017, the OECD issued the OECD Corporate Governance Factbook, which tracks individual countries' implementation of the OECD Principles. The Factbook also offers a comprehensive set of recommendations to regulators for the development of sound corporate governance policies.

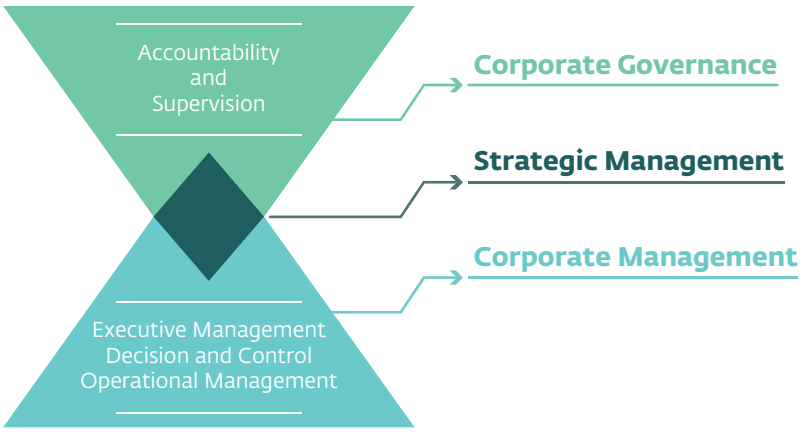
Although Indonesia's CG Code and related regulations represent a positive step towards improving corporate governance practices in Indonesia, they are less comprehensive and stringent than other national codes. The OECD Principles provide an excellent reference point to offset these limitations and are highly recommended for those interested in understanding some of the principles that underline national corporate governance standards.

1.1.3 Distinguishing Corporate Governance

Corporate governance focuses on a company's structure and processes to ensure fair, responsible, transparent, and accountable corporate behavior. It must be distinguished from public governance, which deals with governance structures and systems within the public sector. Corporate governance is also distinct from corporate management, which focuses on the tools required to operate a

business. One area of overlap between management and governance is corporate strategy, which is dealt with at the corporate management level and incorporates key corporate governance considerations. ***Figure 2*** illustrates the difference between corporate governance and corporate management.

Figure **2** Comparison between Corporate Governance and Corporate Management



Source: Robert I. Tricker, Corporate Governance, 1984

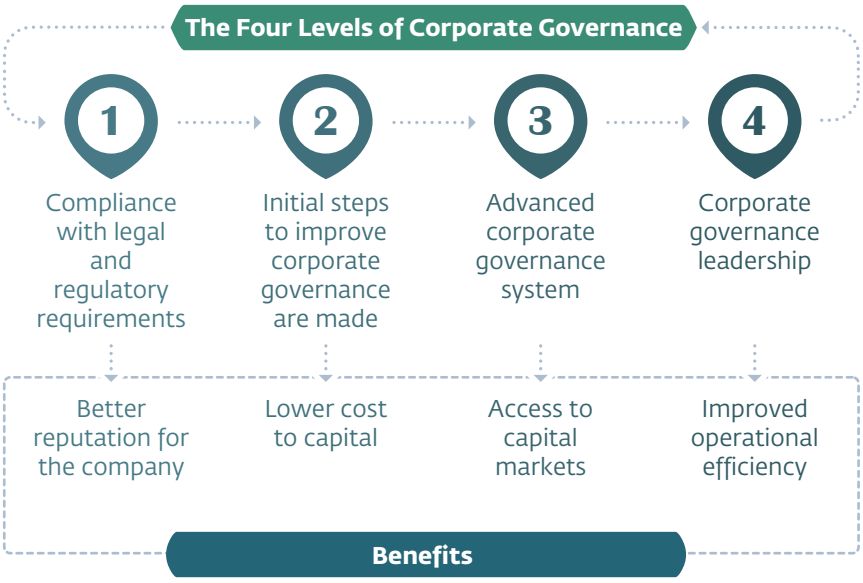
Corporate governance also differs from concepts such as good corporate citizenship and business ethics. Good corporate governance may certainly reinforce ethical and responsible business practices by promoting healthy management systems. However, corporate governance exists as a distinct set of principles whose primary purpose is to ensure that the company is managed in the best interests of the company.

1.2 The Business Case for Corporate Governance

Good corporate governance promotes sustainable business growth by facilitating companies' access to capital and protecting the rights of shareholders and other stakeholders. Companies that insist upon the highest standards of governance and integrity by management by their nature reduce many of the risks inherent in investment. In doing so, these companies are better able to secure reliable access to capital at a lower cost, and as a result tend to outperform their less well-governed peers over the long-term.

Generally, well-governed companies are better contributors to the national economy and society. They tend to deliver greater value to shareholders, workers, communities, and countries in contrast with poorly governed companies, which are more likely to undermine confidence in securities markets. Some of the building blocks, or levels, and specific benefits of good governance are depicted in ***Figure 3*** and discussed in further detail below.

Figure **3** Benefits of Good Corporate Governance



1.2.1 Increased Performance and Operational Efficiency

There are several ways in which good corporate governance can improve performance and operational efficiency, as ***Figure 4*** illustrates.

Figure **4** Advantages of Good Corporate Govenance

An improvement in the company's governance practices leads to a better oversight and accountability system, thereby minimizing the risk of fraud or self-dealing by the company's staff. Accountability for corporate actions, combined with effective risk management and internal controls, can bring potential problems to the forefront before the company faces a full-blown crisis.

Adherence to good corporate governance standards strengthens the decision-making process. For example, the BoC, BoD, and shareholders are more likely to make better informed and timely decisions when the company's governance structure clearly defines their respective roles and responsibilities, and where internal communication within the company operates effectively. High quality corporate governance streamlines the company's business processes, improving operational performance, and lowering capital expenditures, which may, in turn, contribute to the growth of sales and profits.

An effective system of governance also helps to ensure compliance with applicable laws and regulations, thus allowing companies to avoid costly litigation, including costs related to shareholder claims as well as other disputes resulting from fraud, conflicts of interest, corruption and bribery, and insider trading. Good corporate governance can help to facilitate the resolution of corporate conflicts between minority and controlling shareholders, between executives and shareholders, and between shareholders and stakeholders. In addition, company officers will be able to minimize the risk of personal liability.

1.2.2 Access to Capital Markets

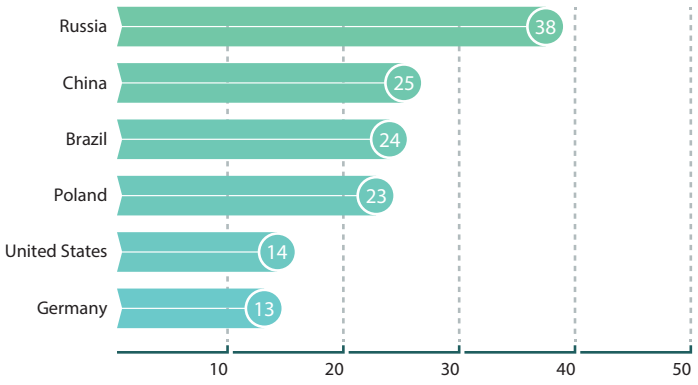
Corporate governance practices can improve access to capital, because well-governed firms provide investors with greater confidence in their ability to generate returns and protect shareholder rights. From an investor's point of view, the better a company's corporate governance structure and practices, the more likely that assets will be used in the interests of the company and not tunneled or otherwise misused by managers. Corporate governance practices can also take on a particular importance in emerging markets, where shareholders do not always benefit from the same protections available in more developed economies and where political or economic instability and institutional weakness contribute to elevated levels of perceived investment risk.

This holds particularly true in emerging market countries where regulations and enforcement are at times inconsistent, and courts do not always provide investors with effective recourse when their rights are violated. This means that even modest improvements in corporate governance relative to other companies can make a large difference for investors and decrease the cost of capital.

Good corporate governance also promotes transparency, which provides investors with an opportunity to gain insight into the company's business operations and financial data. Even if the information disclosed by the company is negative, shareholders will benefit from the decreased risk of uncertainty.

Figure 5 demonstrates that a significant percentage of investors are willing to pay a premium to invest in a well-governed company. For example, this premium amounts to 25 percent for Chinese companies.

Figure **5** Premium for Better Corporate Governance



Source: McKinsey & Company, Global Investor Opinion Survey, July 2002

1.2.3 Improved Reputation

In today's business environment, reputation has become a key element of a company's goodwill. A company's reputation and image effectively constitute an integral, if intangible, part of its assets. Good corporate governance practices contribute to and improve a company's reputation. Companies that respect the rights of shareholders and ensure financial transparency and accountability will be highly regarded as ardent advocates of investors' interests. As a result, such companies will enjoy more public confidence and goodwill. This public confidence and goodwill can lead to greater trust in the company and its products, which in turn may lead to higher sales and, ultimately, profits. A company's improved reputation can also positively affect its valuation.

Best Practice

The following principles set out useful guidelines with respect to the formation, operation, and enhancement of a company's corporate governance system:

- *Corporate governance practices should provide shareholders with a real opportunity to exercise their rights in relation to the company.*
- *Corporate governance practices should ensure the equitable treatment of all shareholders. Shareholders should have access to effective recourse in the event of a violation of their rights.*
- *Corporate governance practices should provide for the BoC's direction and supervision of the BoD and for the accountability of the BoC and the BoD to shareholders.*
- *Corporate governance practices should ensure that the BoD manages the day-to-day activities of the company without undue interference, in good faith and solely in the interests of the company, and that the BoD report in full and on a timely basis to the BoC and shareholders.*
- *Corporate governance practices should stipulate the full, timely, and accurate disclosure of all material information (including information about the company's*

financial position, financial indicators, and ownership and management structure) in order to enable shareholders and investors to make informed decisions.

- *Corporate governance practices should ensure compliance with applicable law related to the statutory or contractual rights of all stakeholders. Corporate governance practices should, more generally, encourage the consideration of stakeholders' interests, including employees, even when they are not expressly set forth in law, and support active cooperation between the company and stakeholders with a view to increasing the assets and value of the company.*
- *Corporate governance practices should provide for the effective control of financial and business operations of the company to protect the rights and lawful interests of shareholders.*
- *Corporate governance practices should provide robust internal controls and effective risk oversight by the BoC to ensure that all risks facing the company are identified and mitigated.*

Implementing good governance practices entails costs. Some of the costs include hiring dedicated staff, such as corporate secretaries, experienced and independent BoC and BoD members, internal auditors, or other governance specialists. It will likely require the payment of fees to external counsel, auditors, and consultants. The costs of additional disclosure can be significant as well. Furthermore, it requires a considerable time commitment from the BoC, especially in the early stages of a company's development. These costs tend to make implementation considerably easier for larger companies that may have more resources to spare than smaller companies whose resources may be stretched thin.

Higher corporate governance standards are applicable to larger companies that are publicly traded on an exchange. A large, dispersed shareholder base, where controlling shareholders and directors can wield extraordinary powers and potentially abuse shareholder rights, often defines such companies. In addition, large companies constitute an important element of a country's economy and thus require close public scrutiny and attention.

Notwithstanding the above, strong corporate governance practices benefit all companies, irrespective of size, legal form, number of shareholders, ownership structure, or other characteristics. Of course, a one-size-fits-all approach should be avoided and companies should apply corporate governance standards with care. For example, smaller companies may not require a full set of board committees or a full-time corporate secretary. On the other hand, even a small company may benefit from an advisory body.

A company will not always see instant improvements to its performance due to better corporate governance practices. However, returns, while sometimes difficult to quantify, generally exceed the costs over the long-term. This is especially true when one takes into account potential invested capital, job and pension loss risks, and the disruption that may be caused to communities when companies collapse. In some cases, systemic governance problems may undermine faith in financial markets and threaten market stability.

Finally, it must be noted that corporate governance is not a one-time exercise, but rather an ongoing process. Markets tend to value long-term commitment to good governance practices rather than a single action or "box-ticking" exercises. No matter how many corporate governance structures and processes a company has in place, these must be regularly updated and reviewed.

1.3 Corporate Governance Framework in Indonesia

1.3.1 Features of Corporate Governance in Indonesia

The following summarizes specific features that characterize Indonesia's corporate sector:

The role of state-owned enterprises: Over the last twenty years, Indonesia has converted a number of state-owned enterprises into partly privatized companies through public offerings and/or strategic alliances. Nevertheless, many important sectors in Indonesian economy remain either state monopolies or largely dominated by wholly state-owned enterprises, such as those in banking, electricity, mining, oil and gas, post and telecommunications, railway, and shipbuilding sectors. In numerous equitized state-owned enterprises, the state retains a majority interest of 51 percent, and exercises its control via the GMS and by retaining the right to appoint commissioners and/or directors.

Concentrated ownership: Many companies in Indonesia start out as small private companies owned either by a single controlling shareholder, a family patriarch, or a small group of shareholders. Although many have expanded significantly, the controlling shareholders often have not changed. This concentrated ownership structure poses distinct challenges, such as how best to manage family conflicts; decide on succession; define ownership policies; strengthen strategic planning and other management functions; and broaden the membership of the BoC to include non-family, independent commissioners. Not being able to tackle these challenges effectively restricts the capacity of these businesses to attract the additional capital required for achieving full growth potential. Such insider dominance and weak protection of external shareholders/investors have resulted in failed deals and the underdevelopment of the capital markets in Indonesia. A trend, albeit nascent, towards public offerings, and thus more dispersed ownership, has started. Whether these majority shareholders are truly willing to reduce or even exit their investments remains to be seen.

Little separation of ownership and control: Most controlling shareholders often occupy key positions at both the BoC and the BoD, although the ICL does not allow the same individual to serve concurrently as a commissioner and a director. Those companies that separate ownership and control often do so only

on paper. Failure to separate ownership and control typically results in weak accountability and control structures (the majority/controlling shareholders oversee themselves in their function as commissioners and directors), abusive related party transactions, and poor information disclosure (insiders have access to all information and are unmotivated to disclose to outsiders or minority shareholders).

Unwieldy holding structures: Some major business groups, especially large state-owned enterprises, are set up in the form of parent companies that maintain control over their subsidiaries. While holding structures can serve legitimate purposes, cross-shareholdings and lack of transparency often lead to opaque ownership structures that can disadvantage minority shareholders. Poor or incomplete accounting records present another corporate governance issue that has yet to be tackled.

Inexperienced corporate bodies: Indonesia first introduced parts of the current concepts of the BoC and BoD in the ICL of 1995 and the Law on State-Owned Enterprises in 2003. However, these concepts were not taken seriously until recently, when companies began to draft detailed articles of association (AoA) that adhere to existing laws and regulations. In reality, it is still common for the BoD to attempt to bypass the supervisory mechanisms (such as the BoC) put in place by the AoA, and to limit direct contact with the controlling shareholder (to the extent they are not one and the same). The role of the BoC as well as its committees, the BoD, and corporate secretary in day-to-day company operations often remains unclear. Members of these bodies are supposed to be experienced and capable, but in reality they often lack awareness of their responsibilities and authoritiy, due to a historical lack of good practices in these areas. Lack of experience as well lack of independence in the field of corporate governance is a big obstacle for further economic development. Unfortunately, strong, vigilant, and independent corporate bodies remain a rarity.

1.3.2 Legal and Regulatory Framework

The legal and regulatory framework in Indonesia has some unique characteristics resulting from the history and development of Indonesia's economy. The earliest regulation of limited liability companies derives from Chapter 3 of the Indonesia Commercial Code of 1848 (*Kitab Undang-Undang Hukum Dagang* or KUHD). Indonesia did not formally regulate foreign investment until 1967, with the first iteration of the Foreign Investment Law.

The introduction of the Foreign Investment Law brought the first concepts of corporatization to the Indonesian economy. Throughout the 1970s and up until now, foreign investment companies have been growing fast in both number and size. Most foreign investment companies have some corporate governance structures in place.

The first comprehensive piece of legislation for domestic companies was approved in 1968 (Law No. 6 of 1968 on Domestic Investment). In 1995, the House of Representatives enacted the first iteration of a comprehensive company law (Law No. 1 of 1995 on Limited Liability Companies, which is also known as the "Indonesian Company Law" or ICL). In 2007, the House of Representatives updated both the ICL and the Investment Law, which supersedes the previous Law No. 1 of 1967 on Foreign Investment.

In Indonesia, companies must comply with the ICL and other laws and regulations which govern the specific industry relevant to their business activities. For instance, a company in the insurance business is subject to the ICL and the Law on Insurance Business. Similarly, a bank is subject to the ICL and the Banking Law. In addition to these two laws, a listed bank will also be subject to the Capital Markets Law, and so on. This is one of many examples as to how companies occupying different sectors of the Indonesian economy may be subject to different legal requirements.

The ICL expressly provides that "in special cases where the establishment, organization, management, and operation of an enterprise are regulated by a specialized law, the provisions of such law shall prevail." However, in practice, there are numerous cases where these distinctions are not clear-cut, and where overlapping laws and regulations create confusion, ambiguity, and uncertainty for companies trying to follow the laws and implement good corporate governance practices. These also create the danger of inconsistency in the interpretation and enforcement of these laws by different ministries, the courts, and other law enforcement bodies.

For this reason, while companies may use this Manual as a reference, they should also review other laws and regulations which may be applicable to their lines of business (e.g., accounting, anti-corruption, auditing, bankruptcy, commerce, competition, construction, labor, tender process, and taxation laws). If a company encounters an inconsistency or ambiguity between different pieces of legislation, it should consult appropriate legal advice in order to achieve full compliance with the law and best corporate governance practices. Appropriate sources of such advice may be the company's in-house legal or compliance

department, the company's external legal counsel, or clarification from regulatory agencies.

Table **2** Principal Laws and Regulations on Corporate Governance in Indonesia

Law/Regulation	Applicability	Scope
Law No. 40 of 2007 on Limited Liability Companies ("Indonesian Company Law" or ICL)	Limited liability companies	Establishment of a limited liability company; AoA; capital and shares; company organs (GMS, BoC, BoD); merger, acquisition, and dissolution; work program and annual report; use of profit, liquidation, and expiry of company.
Law No. 8 of 1995 on Capital Markets ("Capital Markets Law")	Listed companies	Establishment of the capital market supervisory board (OJK); stock exchange; clearing and guarantee corporation; central securities depository; investment fund; securities company; securities company representatives and investment advisors; capital market supporting institutions and professionals; issuers and public companies; public documents and reporting to OJK.
Law No. 13 of 2003 on Manpower ("Manpower Law")	Manpower in companies	Manpower management; rights and obligations of employees; rights and obligations of the company; and all related manpower plans for business activities.
Law No. 25 of 2007 on Investment ("Investment Law")	All investment activities (domestic and foreign)	Formation of a business entity for investment; treatment of investors; manpower; investment business sectors; rights, obligations, and liabilities of investors; and investment facilities.

Law/Regulation	Applicability	Scope
Presidential Regulation No. 44 of 2016 on List of Business Sectors Closed to Foreign Investments and Sectors That Are Conditionally Open for Foreign Investments ("Negative List")	Business sectors for foreign investment activities	List of business sectors that are open, partially open, and closed for foreign investment.
Head of BKPM Regulation No. 14 of 2015 on Procedures and Guidelines of Investment Application as amended by Head of BKPM Regulation No. 6 of 2016 ("BKPM Reg. 6/2016")	Foreign investment activities	One stop service for permit applications; procedures and mechanisms to conduct foreign investment in Indonesia; transfer of foreign shares; fiscal and non-fiscal facilities; regional incentives; foreign workers manpower plan; tax facilities and customs.
Ministry of Manpower and Transmigration Decree No. 40 of 2012 on Certain Positions Prohibited for Foreign Workers ("MMT Reg. 40/2012") and Minister of Manpower Regulation No. 16 of 2015 as amended by Minister of Manpower Regulation No. 35 of 2015 on Guidelines for Employment of Foreign Workers ("MMT Reg. 35/2015")	Companies with foreign workers	Guidelines on positions which may and may not be filled by foreign employees.
Indonesia's Code of Good Corporate Governance of 2006 ("CG Code")	All companies	Code of conduct and business ethics that sets out recommendations for companies with respect to company organs; shareholders; stakeholders; and the implementation of good corporate governance.
OJK Regulation No. 32/POJK.04/2014 on GMS of Public Companies as amended by OJK Regulation No. 10/POJK.04/2017 dated March 14, 2017	Public companies	Guidelines and requirements concerning notification to shareholders and procedures during the GMS.
OJK Regulation No. 33/POJK.04/2014 on Directors and Board of Commissioners of Issuing Companies or Public Companies	Issuing companies, public companies	Provisions on the obligations of directors and commissioners in issuing and public companies.

Law/Regulation	Applicability	Scope
OJK Regulation No. 34/POJK.04/2014 on Nomination and Remuneration Committee of Issuing Companies or Public Companies	Issuing companies, public companies	Provisions on the establishment of a remuneration and nomination committee and guidelines for the committee's responsibilities.
OJK Regulation No. 35/POJK.04/2014 on Corporate Secretary of Issuing Companies or Public Companies	Issuing companies, public companies	Provisions on the obligations of the corporate secretary of an issuing or public company.
OJK Regulation No. 8/POJK.04/2015 on Website of Issuing Companies or Public Companies	Issuing companies, public companies	Provisions governing the website of an issuing or public company.
OJK Regulation No. 21/POJK.04/2015 and Circular Letter of OJK No. 32/SEOJK.04/2015 on Implementation of Corporate Governance Guidelines for Public Companies ("OJK CG Guidelines")	Public companies	The first "comply or explain" corporate governance guidelines issued by OJK that require compliance from all Indonesian public companies.
OJK Regulation No.31/POJK.04/2015 on Disclosure of Information or Material Facts by Issuing Companies or Public Companies	Issuing companies, public companies	Disclosure requirements on information or material facts.
OJK Regulation No. 32/POJK.04/2015 on Increase of Capital with Pre-Emptive Rights for Public Companies	Public companies	Provisions on increase of capital with pre-emptive rights.
OJK Regulation No. 55/POJK.04/2015 on Establishment and Guidelines for Implementation of the Audit Committee	Issuing companies, public companies	Provisions on the establishment of an audit committee and guidelines for the committee's responsibilities.
OJK Regulation No. 56/POJK.04/2015 on Establishment and Guidelines for Preparation of the Internal Audit Charter	Issuing companies, public companies	Guidelines and procedures for internal audit.

Law/Regulation	Applicability	Scope
OJK Regulation No. 29/POJK.04/2016 and Circular Letter of OJK No. 30/SEOJK.04/2016 on Annual Report of Issuing Companies or Public Companies	Issuing companies, public companies	Guidelines on annual reports.
Decision of the Chairman of the Capital Market and Financial Institutions Supervisory Agency No. KEP-346/BL/2011 on Periodical Submission of Financial Statement by Issuing Companies and Public Companies ("Regulation X.K.2")	Issuing companies, public companies	Requirement to submit a financial statement by issuing companies and public companies.
OJK Regulation No. 7/POJK.04/2017 on Registration Statement in the Context of Public Offering of Equity Securities, Debt Securities, and/or Sukuk	Issuing companies, public companies, securities underwriters, and public accountants	Public offering of equity securities, debt securities, and sukuk (Shariah stock).
OJK Regulation No. 8/POJK.04/2017 on Form and Content of Prospectus and Short Prospectus for General Offering of Equity Securities	Issuing companies, public companies, public accountants, legal consultants, and notaries	Form and content of prospectus and short prospectus for initial public offering.
OJK Regulation No. 11/POJK.04/2017 on Shareholding Report or Any Change of Shareholding in Public Companies	Public companies	Reporting requirements concerning share ownership in public companies.
OJK Regulation No. 51/POJK.03/2017 on Implementation of Sustainable Finance for Financial Institutions, Issuing Companies, and Public Companies	Financial institutions, issuing companies, and public companies	Provisions for financial institutions and public companies to apply sustainable finance principles by developing an annual sustainable finance business plan and a sustainability report.
OJK Regulation No. 11/POJK.03/2016 on Minimum Capital Provision of Commercial Banks as amended by POJK No. 34/POJK.03/2016	Commercial banks	Capital requirements for commercial banks.

Law/Regulation	Applicability	Scope
Circular Letter of OJK No. 39/SEOJK.03.2016 on Fit and Proper Test for Future Controlling Shareholders, Future Members of the Board of Directors, and Future Members of the Board of Commissioners of Commercial Banks	Commercial banks	Fit and proper test for principal parties (controlling shareholders, BoC and BoD members) in commercial banks.
OJK Regulation No.55/ POJK.03/2016 and Circular Letter of OJK No. 13/SEOJK.03/2017 on Implementation of Corporate Governance in Commercial Banks	Commercial banks	Corporate governance guidelines for commercial banks.
OJK Regulation No. 56/ POJK.03/2016 on Share Ownership in Commercial Banks	Commercial banks	Guidelines concerning share ownership in commercial banks.

Table 2 reflects major laws and regulations relevant to corporate governance in Indonesia, but the list is not exhaustive and it is important that companies seek legal advice. Moreover, Indonesian legislation continues to change as it develops and improves. For example, the ICL has been amended several times to eliminate inconsistencies in provisions that regulate the activities of governing bodies, securities issuance, the exercise of shareholder rights, and other matters. Most of the laws and regulations that impact corporate governance and are referred to in this Manual have been enacted in the last few years, although they may have evolved from past laws.

Finally, Indonesian regulators encourage all companies to adhere to the corporate governance related regulations issued by OJK, even though these provisions are only mandatory for public and listed companies.

1.3.3 Institutional Framework

There are numerous institutions that make-up the institutional framework for corporate governance in Indonesia today, too many to list exhaustively. The following institutions have at least one core activity focusing on corporate governance:

Table **3** Corporate Governance-Related Institutions

Arbitration Center	
BANI Arbitration Center	www.baniarbitration.org

Public Sector Institutions	
Ministry of National Development Planning (BAPPENAS)	www.bappenas.go.id
Bank Indonesia	www.bi.go.id
Chamber of Commerce and Industry (KADIN Indonesia)	www.kadin-indonesia.or.id
Corruption Eradication Commission (KPK)	www.kpk.go.id
Financial Services Authority (OJK)	www.ojk.go.id
Government of Indonesia	www.indonesia.go.id
Indonesia Stock Exchange (IDX)	www.idx.co
Ministry of Finance	www.depkeu.go.id
Ministry of Law and Human Rights	www.kemenkumham.go.id
National Committee on Governance (KNKG)	www.knkg-indonesia.org
National Police (POLRI)	www.polri.go.id
The House of Representatives (DPR)	www.dpr.go.id
Indonesia Central Securities Depository (KSEI)	www.ksei.co.id

Non-Governmental Institutions	
Center for Risk Management Studies (CRMS Indonesia)	www.crmsindonesia.org
Indonesian Corporate Secretary Association (ICSA)	www.icsa-indonesia.org
Indonesian Institute for Corporate Directorship (IICD)	www.iicd.org
National Center for Sustainability Reporting (NCSR)	www.ncsr-id.org

International Organizations	
International Finance Corporation (IFC)	www.ifc.org
Organization for Economic Co-operation and Development (OECD)	www.oecd.org
The World Bank	www.worldbank.org

CHAPTER 2
Company Governance Structure

THE CHAIRMAN'S CHECKLIST

- What is a limited liability company (*Perseroan Terbatas* or PT)?
- Why do we need PTs?
- What are the key advantages of PTs over other legal forms?
- What is the dividing line and significant governance difference between public and private companies?
- In addition to the GMS, BoC, and BoD, has the company established supporting bodies such as an audit committee, nomination and remuneration committee, governance committee, risk committee, and/or an internal audit function?
- Have these bodies been given the appropriate structures and proper resources to be effective?
- Does the company need to have a corporate secretary?

The ICL defines limited liability companies (*Perseroan Terbatas* or PT) and sets out the requirements for their governance structures. Indonesia's CG Code provides additional (non-binding) recommendations for companies to establish additional governing bodies and specific positions, such as committees to monitor the company's auditing and remuneration policies, and a corporate secretary. This chapter discusses general concepts and governance structures of the PT as defined by the ICL, with reference to the CG Code's recommendations. Subsequent chapters in this Manual describe the respective authoritiy, functions, and structures of each governing body in greater detail.

2.1 Limited Liability Company

2.1.1 Definition of Limited Liability Company

The ICL definition of a limited liability company or PT adheres in essence to equivalent legal terms in other jurisdictions. Under the ICL, a PT is a legal entity that forms a partnership of capital, established by an agreement, performs business activities with all of its authorized capital (being the total amount of shares that a company is allowed to issue to shareholders) divided into shares, and which fulfils all other relevant ICL and implementing regulatory requirements.

Limited liability companies meeting the ICL definition hold the following characteristics:

- Shareholders cannot be held personally liable for the company's debts/liabilities.
- The company holds legal identity, can enter into contracts in its own name, and may sue and be sued.
- The company adopts a two-tiered governance system comprising a BoC that supervises the BoD.
- The capital structure is divided into authorized capital, issued, and paid-up capital. Minimum authorized capital is Rp 50 million and the issued and paid-up capital must be at least 25 percent of its authorized capital (at least Rp 2.5 billion per business line for financial institutions).
- The company organs consist of the GMS, BoC, and BoD.
- The company may issue shares and bonds.

In Indonesia, PT is the only legal entity that can issue shares. Shares in a PT may include:

- Ordinary shares
- Shares with or without voting rights
- Shares with special right to nominate BoC and/or BoD members
- Shares which after a certain period of time will be withdrawn or

exchanged with other shares' classification

- Shares which provide priority rights to their owner to receive dividends over the other shareholders from different shares' classification for the distribution of dividends cumulatively or non-cumulatively
- Shares which confer priority rights to receive company assets (in proportion to their shareholding) on liquidation or winding up
- Other preferred shares as determined in the company's AoA

Shareholders of a PT are not personally liable for any agreement made on behalf of the PT, and will not be liable for or incur losses beyond those of their individual shareholding. The ICL, however, contains certain specific exceptions to the limited liability principle, resulting in the so-called piercing of the corporate veil, including:[3]

- Shareholders will be collectively liable for debts incurred where a company is not properly established following all ICL requirements. These include the requirement for at least 25 percent of the company's authorized capital to be subscribed and paid-up in full.[4]
- An ordinary shareholder will be personally liable if he/she/it commits any of the following acts in the company's name:
    1. Directly or indirectly exploits the company in bad faith in his/her/its personal interest
    2. Is involved in illegal acts committed by the company
    3. Directly or indirectly uses the company's assets with the result that the company's assets become insufficient to pay off the company's debt

2.1.2 Listed and Non-Listed Companies

Indonesian law distinguishes clearly between listed and non-listed companies. Listed companies require higher paid-up capital and are subject to stricter and more complex rules with respect to corporate governance and information disclosure. Listed companies are generally better suited for larger and growing companies that might wish to raise finance in the equity markets.

[3] Law No. 40 of 2007 on Limited Liability Companies ("Indonesian Company Law" or ICL), Article 3(2).

[4] ICL, Article 33(1).

Indonesia Stock Exchange (IDX) rules further require all listed companies to meet the Capital Markets Law's definition of "public company", being that they must have at least 300 shareholders and paid-up capital of at least Rp 3 billion.[5] A public company is not always a listed company, however a listed company must be a public company. Where a company intends to list on the IDX, it must first register with OJK. To transfer its status as a private to a public entity (or vice versa), a company must follow the procedures set out under the Capital Markets Law, which include amending the company's AoA and business registration certificate. Such conversions do not affect the company's legal identity.

Table **4** Comparison of Private, Public, and Listed Companies in Indonesia

	Private Companies	Non-Listed Public Companies	Listed Public Companies
Shareholding	Two shareholders or more	Public offering; 300 shareholders or more	Public offering and shares listed on the IDX; 300 shareholders or more
Capital Requirements	Authorized capital at least in the amount of Rp 50 million or more, at least 25 percent of which should be issued and paid-up	Paid-up capital at least in the amount of Rp 3 billion	Paid-up capital at least in the amount of Rp 3 billion
Issuance of Shares	Closed subscription (only among founders or other pre-determined groups of people); cannot issue shares through an open subscription	Open subscription; a closed subscription is subject to the approval of OJK	Open subscription; a closed subscription is subject to the approval of OJK
Transferability of Shares	Transferability of shares is unrestricted, except if the AoA requires a selling shareholder to offer his/her/its shares to shareholders with certain classes or other shareholders[6]	No restrictions allowed (except for voting preference shares and shares held by founding shareholders); neither the consent of other shareholders nor the company is required	No restrictions allowed (except for voting preference shares and shares held by founding shareholders); neither the consent of other shareholders nor the company is required
Corporate Secretary	Unregulated	Mandatory	Mandatory

[5] Law No. 8 of 1995 on Capital Markets ("Capital Markets Law"), Article 1(22).
[6] ICL, Article 58.

Disclosure	No legal requirements to publicly disclose information	Must disclose a wide range of information regarding its financial position, operations, and governance[7]	Must disclose a wide range of information regarding its financial position, operations, and governance

2.1.3 Advantages and Disadvantages of Listed Companies

Apart from the PT in private, public, or listed form, Indonesian law allows the establishment of the following legal entities:

- Civil Partnership (*Maatschap*)
- Firma (*Vennootschap onder Firma*)
- CV (*Commanditaire Vennootschap*)
- Cooperative[8]
- Foundation

PT is the most popular form of commercial entity in Indonesia. According to a 2006 economic survey (business/company listing result), there were 22.7 million PTs in operation in Indonesia. As of July 2017, there were 555 public companies, of which 554 were listed companies.

Listed companies enjoy many advantages, including:

- **Access to investors**: Listed companies have greater opportunities to attract investment from multiple investors and at lower cost. Listed companies also bear information disclosure obligations that improve their transparency compared to other forms of legal entities, which makes them attractive to investors. This is important for companies in capital-intensive sectors such as banking, which require significant investment that will typically be difficult to source from individual lenders.
- **Freedom of share transfers**: Shares can be transferred without the consent of other shareholders, the company, or its management, so long as those transfers comply with legal requirements. In addition, listed companies are not required to report share transfers of less than 5 percent of the total issued share capital.

[7] Capital Markets Law, Article 86.
[8] Law No. 25 of 1992 on Cooperatives.

- **Limitation on the risks to shareholders**: The risks carried by shareholders are limited to the value of their investment. Shareholders are not normally liable for the legal and financial obligations of the company.
- **Diversification of risk**: The public company structure disseminates the effects of risk across a large number of shareholders.

The principal economic advantage of the listed company is the ease with which it can access financial markets. However, this does not come without disadvantages. Companies must clear a number of legal and regulatory hurdles before they may offer shares:

- **Compliance with securities regulations**: A plethora of securities laws and regulations apply to listed companies and are not required for private entities.
- **Complex organizational structure**: As well as the GMS, BoC, and BoD, listed companies are required to form supporting committees, such as an audit committee, which operates under the BoC. This is designed to protect shareholders from abuse, and companies bear all costs associated with supporting its governing bodies.
- **Compliance with disclosure obligations and other regulations**: A public company must maintain transparency through timely, accurate, and complete disclosure of all events that are material to its legal and financial position. Information disclosure obligations encompass business, financial, and auditing reports, as well as any other relevant information, in accordance with the securities market regulations. A public company must therefore comply with more rigorous laws than other entity types. It must also ensure to properly register all issued shares.
- **Willingness of shareholders to invest**: The company must be able to attract shareholders willing to accept the risk of investing, and to maintain good investor relations once its shares have been floated. These activities attract significant costs, including those involved in marketing share offerings to investors and in maintaining continuous communication with shareholders after the initial public offering.
- **Professional management**: The separation of ownership and control allows the company's investors (the shareholders) to hire professional directors who devote their efforts and skills to corporate management. The separation of ownership and control also provides professional directors with access to capital needed

to manage the company. Finding and retaining trustworthy and capable directors, however, can be challenging.

- **Higher minimum charter capital requirements**: Listed companies must have a charter capital of at least Rp 3 billion, compared to Rp 50 million for private companies.

2.2 Governance Structure of Limited Liability Company

The ICL requires companies to maintain a core base of governing bodies, which differ depending on whether the company is a public or private entity, as listed below. These requirements do not change based on numbers of shareholders or the value of a company's charter capital.

Non-Listed Companies

A non-listed company must have the following bodies:

- General meeting of shareholders
- Board of commissioners
- Board of directors

Listed Companies

In addition to the bodies required for non-listed companies, listed companies must have:

- An audit committee
- A nomination and remuneration committee
- A corporate secretary
- An internal auditor

Listed companies may also establish one or more of the following board committees at their discretion:

- A risk policy committee
- A corporate governance committee
- Other board committees

2.2.1 General Meeting of Shareholders

The GMS of a limited liability company is a company organ that carries decision-making authority beyond that granted to the BoC and BoD, as determined by the ICL or company's AoA.

All ordinary shareholders have the right to participate in the GMS and hold the number of votes that correspond to their respective ordinary shares. The GMS approves the nomination for BoC and BoD membership. In addition, it approves annual reports, financial statements, distribution of profits and losses (including the payment of dividends), amendments of the authorized capital, amendments of the AoA, re-organization and dissolution, and extraordinary transactions.

2.2.2 Board of Commissioners

The BoC plays a central role in Indonesia's corporate governance framework. The BoC is responsible for overseeing and advising the BoD, in the context of pursuing the company's interests and objectives. The AoA may vest authority in the BoC to give consent or assistance to the BoD in the commission of specified legal acts.[9] The CG Code sets out general standards to the effect that a BoC must have the capacity to perform its responsibilities with integrity, and to ensure that company activities comply with applicable laws and regulations.

Comparative Practice

Different jurisdictions will typically adopt either a one-tier or two-tier board structure. Indonesia implements the two-tier system, comprised of the BoC and BoD. The two-tier system is common in other civil law jurisdictions such as the Netherlands, Germany, and many Eastern European countries. The United Kingdom, United States, Australia, and other common law countries typically use a one-tier or unitary board system. Unlike many European countries, which often allow companies the flexibility to choose between a unitary or dual system, the ICL requires all Indonesian companies to maintain a BoC and BoD under the two-tier board model.

[9] ICL, Article 117.

There are numerous differences between the one-tier and two-tier systems:

1. *The one-tier or unitary board system is characterized by a single board (the board of directors) that governs the company and includes both executive and non-executive members. This governance structure can facilitate a strong leadership structure and efficient decision-making. Non-executive and independent directors play a crucial role in monitoring managers and reducing agency costs.*
2. *The two-tier or dual board system is characterized by the existence of distinct supervisory and management bodies. The former is commonly referred to as the supervisory board or BoC in Indonesia, the latter as the executive board or BoD in Indonesia. Under this system, the executive board/BoD is responsible for day-to-day company management and will be overseen by the supervisory board/BoC. These two bodies have distinct authority and their composition cannot be mixed, i.e., members of the BoD cannot sit on the BoC and vice-versa. The advantage of the two-tier system is a clear oversight mechanism, but it has been criticized for inefficient decision-making.*
3. *Besides the one-tier and the two-tier systems, many countries recognize a third governance structure, the hybrid system, which is essentially an amalgam of the two models.*

Regardless of which system a country allows, the following must be kept in mind:

- *There is always a trade-off between efficiency and control. When conflicts of interest within a company are strong, shareholders might elect a two-tier system to ensure strong supervision over management. However, an excessively tight monitoring governance system also potentially restricts the BoD's capacity to make decisions effectively. On the other hand, when shareholders and managers trust each other and the*

company needs better efficiency to explore business opportunities, the company may choose a more pro-management oriented, one-tier board system.

- *While all systems have many elements in common, important differences do exist and these will affect the board's authority, structure, and operations, and consequently the duties and obligations of directors.*

2.2.3 Board of Directors

Every company must have a BoD that is responsible for day-to-day management. The BoD is the legal representative of the company, except when that would give rise to a conflict of interest or the BoD has not been appointed, in which case the BoC may temporarily fill this role.[10] The BoD is accountable to the GMS. The ICL and the company's AoA regulate the authority of the BoD, as well as procedures for the election and dismissal of individual directors.

2.2.4 Board Committees

A board committee has the duty to assist and make recommendations to the BoC. The CG Code recommends that companies establish committees to perform specific functions such as auditing, risk management, and monitoring the nomination and remuneration of directors. Responding to these recommendations, OJK now requires the BoC of public companies in Indonesia to establish an audit committee[11] and a nomination and remuneration committee,[12] which must report to the BoC.

[10] ICL, Article 98(2).
[11] OJK Regulation No. 55/POJK.04/2015 on Establishment and Guidelines for Implementation of the Audit Committee, Article 2.
[12] OJK Regulation No. 34/POJK.04/2014 on Nomination and Remuneration Committee of Issuing Companies or Public Companies, Article 2.

2.2.5 Corporate Secretary

Listed companies in Indonesia must also retain a corporate secretary,[13] whose task is to ensure the company makes relevant corporate information available to the public, advise the BoD with respect to compliance with the Capital Markets Law and its implementing regulations, and to act as a point of contact between issuers or listed companies and OJK as well as the public.

2.2.6 Internal Auditor

OJK requires the BoD of Indonesian listed companies to establish an internal audit function.[14] The internal auditor plays an increasingly important role in many Indonesian listed companies towards strengthening their governance standards.

2.2.7 External Auditor

The ICL provides that the BoD must prepare an annual report, which upon review by the BoC must be submitted to the GMS. The annual report includes a financial statement with a balance sheet and a profit and loss statement.[15]

External auditing of the financial statement by a certified independent external auditor (licensed and accredited audit company/organization) is obligatory for companies that are:[16]

- Considered to be a compliance-audited company (state-owned enterprises, companies funded with foreign investment, commercial banks, credit institutions, financial institutions, insurance

[13] OJK Regulation No. 35/POJK.04/2014 on Corporate Secretary of Issuing Companies or Public Companies, Article 2(1).

[14] OJK Regulation No. 56/POJK.04/2015 on Establishment and Guidelines for Preparation of the Internal Audit Charter, Article 3.

[15] ICL, Article 66.

[16] ICL, Article 68(1).

companies, and listed companies)

- A controlling company that makes consolidated financial statements
- Issuing securities or other financial instruments traded on the organized market

For listed companies, the external auditor is a separate body of the company, elected by the GMS from the list of auditors authorized by the Ministry of Finance to audit financial statements of listed companies, prepare auditor reports, and submit these reports to the BoD.

CHAPTER 3
Internal Corporate Documents

THE CHAIRMAN'S CHECKLIST

- Does the company have a valid AoA that fully complies with the ICL (particularly Article 15)?
- Is the AoA freely available to interested parties and accessible on the internet?
- Has the company adopted internal regulations? Is adopting internal regulations a legal obligation of the company? Is it possible for a company to be incorporated without having internal regulations? Does the company regularly consult and follow its internal regulations?
- Has the company adopted its own corporate governance code? If so, is the company's code based upon the principles of transparency, accountability, responsibility, independence, and fairness? Does the company's code provide recommendations on the relationship between the corporate bodies, notably the interaction between the BoC and the BoD?
- Has the company identified a core set of values? Does the company have a code of ethics based on these values?

The founding legal document for companies in Indonesia is the deed of establishment, which encompasses the AoA and supplementary documents.

All companies must have an AoA, which establishes corporate legal identity and determines the company's governance structure, objective and purpose, and distribution of capital. The AoA plays a fundamental role in the protection and equitable treatment of shareholders by disseminating authority across the company's governing bodies (GMS, BoC, and BoD) and providing disclosure and transparency of the company's activities.

Specific amendments to the AoA—including changes to the company name, headquarters location, authorized capital, or business activities—require approval from the Minister of Law and Human Rights (MOLHR).[17] For other, less significant changes, the company may amend the AoA so long as it notifies the MOLHR.

In addition to the AoA, companies may choose to adopt other internal regulations to serve a range of purposes.[18] Any internal regulations, however, must be consistent with the AoA. Another (voluntary) regulation some companies consider is the corporate governance code and/or code of conduct, which empowers companies to improve transparency in their management and accountability systems and demonstrates commitment to good corporate governance and good business practices.

This chapter explains when and how companies may (or, in some cases, must) make amendments to the AoA, and how these amendments must be registered. It also sets out the important role that strong company-level corporate governance plays, and the benefits of implementing a code of conduct.

[17] ICL, Article 21(2).
[18] Law No. 13 of 2003 on Manpower, Article 108(1).

3.1 Articles of Association

An AoA must include the following minimum provisions:

- The company's name and domicile/headquarters
- Business activities and objectives
- Terms of establishment
- Capital structure: the amount of the authorized capital, subscribed capital, and paid-up capital
- The number of shares and their classifications, including the number of shares allotted to each share class
- Names and titles of members of the BoC and BoD
- Determination of the place and procedure to conduct the GMS
- Procedures for the appointment, replacement, and dismissal of members of the BoC and BoD
- Procedures for the use of profits and allocation of dividends

In addition to these mandatory provisions, the company's AoA may set forth other matters as agreed by the shareholders, so long as these are consistent with Indonesian law. An Indonesian company must execute its deed of establishment and AoA through a notarial deed in Bahasa Indonesia.

Amendment of AoA

Companies must amend their AoA every time significant changes occur, in particular changes to:[19]

- Company name and/or domicile/headquarters
- Business objectives or activities
- Period of incorporation
- Authorized capital
- Amounts of subscribed and paid-up capital (share capital reductions)

[19] ICL, Article 21.

- Company status from public to private and vice versa
- Decisions to expand the company's scope of business
- Any other important events

Companies require approval from the MOLHR to perform any of these amendments. Pursuant to Article 19 of the ICL, only the GMS has the authority to make amendments to the AoA. The following table sets out the ICL's minimum requirements and thresholds for the GMS to legitimately authorize AoA amendments (see ***Table 5*** below for further details).

Table **5** ICL Requirements for AoA Amendment

Matters	Notice	Quorum	Voting
Amendment of AoA (1st meeting)	Fourteen days prior notice	At least 2/3 of the total number of shares with legal voting rights	At least 2/3 of the total number of votes legally cast at the meeting
Amendment of AoA (2nd meeting)	Seven days prior notice; the GMS may be convened within 10-21 days after the preceding GMS, or where a GMS is held following a court order, no later than 21 days as of the court order	At least 3/5 of the total number of shares with legal voting rights	At least 2/3 of the total number of votes legally cast at the meeting
Amendment of AoA (3rd meeting)	Seven days prior notice; the GMS may be convened within 10-21 days after the preceding GMS or, where a GMS is held following a court order, at the latest 21 days as of the court order	Based on the decision of the Chairman of the District Court	Not expressly prescribed under the ICL, however, the current interpretation governed by Article 87(2) of the ICL suggests more than half of the total number of votes legally cast at the meeting

Companies must notify shareholders of proposed amendments by clearly listing these changes as agenda items in the notice of GMS. For companies declared bankrupt, amendments will be subject to approval by the company's receiver.

Best Practice

It is accepted practice that the company, through its legal counsel/ department, prepares AoA amendments in cooperation with external legal consultants and with the participation of the corporate secretary.

The president commissioner and the president director should closely follow the process to ensure that provisions of the AoA are formulated in accordance with the company's internal guidelines. The final text of the draft proposal must be reviewed and accepted by the BoC and BoD. The accepted text will be submitted to the GMS as a proposal.

Since only the GMS can approve amendments to the AoA, the GMS is also the body responsible for resolving any objections from shareholders concerning amendments. Further, companies are prohibited from making amendments to the AoA if the amendment is contrary to the provisions governing the procedures for AoA amendment; the amendment violates existing laws and regulations or otherwise impairs public order and/or morality; or, with respect to decisions to decrease the companies' share capital, if there is any objection from creditors.

All amendments to a company's AoA require either acknowledgement from or approval of the MOLHR. The MOLHR must approve specific changes, namely those that affect:

- Company name and/or domicile
- Official business activities and/or purpose of the company
- The company's period of incorporation
- Amount of the authorized capital
- Decrease in paid-up and issued capital
- Transfer of status from a private company to a public company or vice versa

For any amendments other than those listed above, companies need to obtain

only an acknowledgment from the MOLHR.

Amendments to the AoA that require MOLHR approval will generally be effective from the date that approval is issued. All other amendments, which require only notification to the MOLHR, are effective from the date the MOLHR issues its letter of acknowledgement. However, specific provisions apply to amendments that involve a change from private to public company status (or vice versa), and in the context of mergers and acquisitions.

The ICL sets out the following timeframes:

1. Amendments to the AoA regarding a change in the company's status from a private company to a public company come into effect on:[20]
    - The date the Registration Statement the company submits to OJK becomes effective; or
    - The date a company makes a public offering by submitting a declaration of registration to OJK. This declaration confirms the company's intention to make a public offering in accordance with Indonesia's capital markets regulations.
2. Amendments to the AoA regarding a merger or acquisition come into effect on:[21]
    - The date the Minister issues approval or acknowledgement; or
    - A later date if specified in the Minister's approval as issued; or
    - A later date if specified in the deed of merger or deed of acquisition.

Disclosure of AoA

The AoA is an important source of information for shareholders and potential investors. Companies should keep the original AoA document, as well as all its amendments, at the company's registered office. A company's register should be open to the public.[22] Shareholders have the right to inspect and copy the AoA and any amendments.

[20] ICL, Article 25(1).
[21] ICL, Article 26.
[22] ICL, Article 29(5).

The MOLHR will announce the following corporate documents in the Supplement to the State Gazette of the Republic of Indonesia:

1. The deed of establishment together with the MOLHR's Decree;
2. The deeds of amendment to company's AoA together with the MOLHR's Decree; and
3. The deeds of notification of amendment to company's AoA.

The MOLHR is required to make these announcements no later than fourteen days from the date the MOLHR issues its decree, or from the receipt of the notification. Public companies must report any amendments to the AoA to the IDX.

3.2 Internal Regulations

Internal regulations are company documents that either set out greater detail relevant to provisions of the AoA, and/or govern internal management and company affairs. Some types of company may also be legally required to implement specific internal regulations. For instance, companies with at least ten employees need to adopt a company regulation setting out the rights and obligations of the company and employees.[23] Furthermore, the CG Code advises certain types of company—namely public listed companies, state-owned enterprises, province and region-owned companies, companies that raise and manage public funds, companies of which products or services are widely used by the public, and companies with extensive influence on the environment—to adopt a corporate governance code that requires the company and its management to protect shareholder interests.[24]

Such companies may choose to implement additional regulations at their discretion, as may other types of company, including non-listed entities. Companies do not need to register proposed internal regulations prior to being established; however, companies subject to mandatory requirements must implement the prescribed internal regulations once incorporated. All internal regulations must be consistent with the AoA and cannot conflict with Indonesian law. To the extent of any inconsistency, the AoA will always prevail over internal regulations.

Best Practice

Whether or not legally required to do so, companies may benefit from implementing internal regulations for several reasons:

- *Procedural requirements for amending internal regulations are less stringent compared to those concerning the AoA, making it easier for companies to adjust to changing circumstances.*

[23] Law No. 13 of 2003, Article 108(1).

[24] *Indonesia's Code of Good Corporate Governance* (Jakarta: National Committee on Governance, 2006), 2.

- *Internal regulations do not need to be registered with the authorities, saving the company resources by avoiding registration fees and bureaucratic procedures.*

Internal regulations contribute to the protection of shareholder rights. In particular, internal regulations set out a sound and proper framework for the administration and operation of the company. Internal regulations also assist shareholders to understand the implementation of the AoA provisions in practice.

For voluntary internal regulations—that is, other than those mandated by law—which must be implemented as directed by the relevant authority, companies may set their own requirements under the AoA. Should the AoA need to be amended to accommodate a new internal regulation, companies must follow the normal procedures for amendment through the GMS that are discussed earlier in this chapter. Generally, the company's BoD (under BoC supervision) may decide the content and procedures for implementation of voluntary internal regulations, but must follow any specifications in the AoA.

3.3 Indonesia's Code of Good Corporate Governance

Corporate governance codes serve as important resources in both advanced and transitional economies. Indonesia's framework for corporate governance has developed through several stages and is reasonably comprehensive, albeit non-binding.

A specialized body, the National Committee on Corporate Governance, developed Indonesia's first CG Code in 1999. Due to concern that the public sector should also comply with these governance principles, the Government of Indonesia later replaced the National Committee on Corporate Governance with the National Committee on Governance, consisting of a public sub-committee and a corporate sub-committee.[25]

Indonesia's CG Code has been revised several times, most recently in 2006. As already noted, it is not legally binding, but serves as an ethics-based model that provides a reference for the successful implementation of CG practices. The CG Code describes steps that can be taken by companies to create checks and balances over their governance and management, to enforce transparency and accountability, and to promote corporate social responsibility for their long-term sustainability. Updated regularly, the CG Code is a living instrument that sets standards and offers guidance as to how companies may implement corporate governance to:[26]

- Achieve sustainable growth through a management system based on transparency, accountability, responsibility, independence, and fairness
- Empower the functions and independence of each company organ, namely, the BoC, the BoD, and the GMS
- Encourage shareholders, members of the BoC, and members of the BoD to make responsible decisions that comply with laws and regulations
- Stimulate the company's awareness of social responsibilities, in particular the environmental and societal interests of local communities

[25] Decree of the Coordinating Minister for Economic Affairs No. KEP/49/M.EKON/11/2004, as amended by Decree of the Coordinating Minister for Economic Affairs No. 117 of 2016.
[26] *Indonesia's Code of Good Corporate Governance*, 2.

- Take shareholders' and other stakeholders' interests into account
- Enhance the national and/or international competitiveness of a company in order to enhance market confidence which may promote investment flow and a sustainable national economic growth

The CG Code applies to all companies in Indonesia, including Sharia-compliant companies. However, publicly listed companies, state-owned enterprises, provincial and regional-owned companies, companies that raise and manage public funds, companies that produce goods or services for public consumption, and companies that have a significant impact on the environment may be expected to implement the CG Code more thoroughly. Regulators and policy makers should use the CG Code as a reference for developing laws and applicable sanctions.

The CG Code provides a minimum standard for the implementation of good corporate governance, which companies may adapt in response to their particular characteristics. The National Committee on Governance also issues specific and more detailed governance codes that apply to specific industries/sectors.

Indonesian companies are encouraged to develop their own corporate governance codes using the CG Code as a reference, and which should cover at least the following:

- Procedures for convening and voting at shareholder meetings
- Procedures for nominating, electing, and dismissing commissioners and directors
- Procedures for board meetings
- Procedures governing the relationship and coordination between the BoC and the BoD
- Procedures to evaluate the performance of the BoC and the BoD

In 2014, OJK launched significant reforms under a corporate governance roadmap (*Tata Kelola Perusahaan Indonesia*)[27] designed to raise corporate governance standards of Indonesian companies, improve investor protection, and strengthen the business environment. This initiative is aligned with Indonesia's preparations as an ASEAN member state towards setting up the

[27] *Indonesia Corporate Governance Roadmap: Towards Better Governance of Issuers and Public Companies*, (Jakarta: Otoritas Jasa Keuangan, 2014), http://www.ifc.org/wps/wcm/connect/a476310042e2a54bbc09fc384c61d9f7/Indonesia+CG+Roadmap.pdf?MOD=AJPERES.

ASEAN Economic Community.

As part of the roadmap, OJK issued Regulation No. 21/POJK.04/2015 and Circular Letter No. 32/SEOJK.04/2015 on Implementation of Corporate Governance Guidelines for Public Companies ("OJK CG Guidelines"). Prior to 2015, Indonesia encouraged but did not mandate companies to implement corporate governance standards, and its 2006 CG Code was not legally binding. The OJK CG Guidelines implemented a "comply or explain" approach, and introduced key changes to strengthen issuers and public companies' obligations with respect to shareholder protections, the function and roles of the BoC and BoD, communication with stakeholders, and information disclosure.

The following are key elements of the OJK CG Guidelines that apply to issuers and public companies:[28]

1. *Protection of Shareholder Rights*

    a) Companies should establish technical voting procedures for either open (show of hands) or closed (electronic/voting card) voting that protects shareholders' autonomy.

    b) All members of the BoC and BoD should be present at the annual general meeting of shareholders (AGMS) and respond to all shareholder questions.

    c) Companies should publish summaries of the AGMS minutes in both Bahasa Indonesia and English on their website within two days of the meeting. These summaries should be available for at least one year.

2. *Function of the BoC and BoD*

    a) **Size and Composition of the BoC and BoD**
    Companies should disclose that they have considered the complexity of their business activities and corporate objectives when determining the size of their BoC and BoD, which should be sufficient to support their activities but not so large as to hinder decision making. This disclosure should also show that companies have taken into account

[28] Circular Letter of OJK No. 32/SEOJK.04/2015 on Implementation of Corporate Governance Guidelines for Public Companies

the scope of skills, knowledge, and experience that will be required for the BoC and BoD to function effectively. In particular, companies should ensure the director responsible for the company's accounting and finance has knowledge or expertise in these areas.

b) **Self-Assessment Policy**
Companies should implement a self-assessment policy that requires BoC and BoD members to evaluate their collective performance, promoting accountability and transparency through regular assessments. Companies should disclose this policy in the annual report.

c) **Financial Crimes**
The BoC and BoD should implement a policy that requires members to resign if found to have been involved in a financial crime.

d) **Succession**
The BoC, or its nomination and remuneration committee if it has one, should establish a clear policy for the succession of BoD members and other company managers to support long-term business sustainability.

3. Stakeholder Communication and Participation

a) **Communication**
Companies should develop a policy for ensuring strong, regular, two-way communication with shareholders/investors, and publish this policy on their website.

b) **Insider Trading**
Companies should establish a comprehensive policy to prevent insider trading (the misuse or disclosure of sensitive company information that is not available to the public). The policy should define insider trading clearly, set out the duties of BoC and BoD members, and establish protocols for reporting breaches.

c) **Anti-Corruption and Anti-Fraud**
Companies should implement an anti-corruption and anti-fraud policy, including strategies for prevention.

d) **Supply Chains**
Companies should implement procedures for the selection of suppliers, covering identification of critical suppliers, selection criteria and a transparent procurement mechanism, contingencies for loss of important suppliers, and protection of supplier rights.

e) **Whistleblowing**
Companies should develop a whistleblowing policy that sets out reporting mechanisms, defines violations, establishes whistleblower protections and confidentiality guarantees, and handling and follow up of complaints.

4. Information Disclosure

a) Companies should use a broad range of information technology, beyond the company's own website, to ensure transparency.

b) Companies should disclose the beneficiaries of all shareholdings greater than 5 percent, as well as beneficial ownership of shares by majority and controlling shareholders.

If a company complies with the OJK CG Guidelines in all aspects, then it should provide a statement in the annual report to that effect, specifically naming Regulation No. 21/POJK.04/2015 and Circular Letter No. 32/SEOJK.04/2015. Typically, companies make corporate governance disclosures in a separate statement through the annual report (and provided on the website), which may be in the form of a tabular chart addressing each principle and recommendation individually, stating how the company complied with the provisions in the OJK CG Guidelines over the past year.

Where a company's circumstances are such that it is unable to implement requirements under the OJK CG Guidelines, OJK requires companies to explain their reason for non-compliance and to set out an alternative strategy toward

implementing the guidelines.[29] Ideally, these explanations should:

- Address the manner in which the company has departed from OJK recommendations. The explanation should be convincing, understandable, company-specific, and provide some context as to why the company has decided to depart from the recommendations.
- Fully describe the departure and specify deviations from OJK provisions as well as from overarching best practice corporate governance principles.
- Describe mitigating actions taken to address risk arising from the company's decision not to comply with the recommendations.
- The deviation from recommendations should be time-bound (i.e., only expected for a limited period) and the company's explanation states when it intends to come into compliance.
- Elaborate how the company's alternative measures/solutions achieve the underlying objectives of the OJK CG Guidelines that the company cannot implement in full, and otherwise contributes to the objective of good governance.
- Companies should be specific when giving their reasons, avoiding responses that are vague, general, or formulaic and repeated year after year. The explanation should be carefully articulated, clear, accurate, and comprehensive—merely identifying an area of non-compliance is insufficient. Fundamental disagreement with the OJK CG Guidelines is not an adequate reason for non-compliance. Companies should indicate when they expect to be able to comply, and be prepared to engage in a dialogue with regulators and shareholders upon request.

[29] OJK Regulation No. 21/POJK.04/2015 on Implementation of Corporate Governance Guidelines for Public Companies, Article 2.

3.4 Company Code of Corporate Governance

A company's corporate governance code is a principle-based statement setting out expectations for the company's governance practices. It is intended to improve the transparency of the company's governance structure and to demonstrate the company's commitment to good corporate governance by developing and promoting:

- Responsible, accountable, and value-based management
- An effective BoC and BoD that act in the best interests of the company and its shareholders, including minority shareholders, and which seek to enhance the value of shareholders' investments in a sustainable manner
- Appropriate information disclosure and transparency, as well as an effective system of risk management and internal control

By adopting, implementing, and regularly updating a company-level corporate governance code, a company demonstrates a commitment towards good corporate governance. To foster the confidence of shareholders, employees, investors, and the public, a corporate governance code should reach beyond compliance with established local legal and regulatory frameworks to embrace both nationally and internationally recognized corporate governance best practices.

Best Practice

Many well-governed companies in countries with higher corporate governance standards have voluntary corporate governance codes or guidelines in addition to their AoAs. Most codes are brief and simple statements of principle that generally reflect the desire of the BoC and BoD to conduct company operations in an honest, fair, and socially responsible manner.

Company codes and guidelines may cover a vast number of topics including:

- ***General Issues of Corporate Governance***
  - *Company goals and objectives*
  - *Relationship between the shareholders, the BoC, and the BoD*
  - *Relationship between the BoC and the BoD*
  - *Relationship between controlling and minority shareholders*

- ***Good BoC Practices***
  - *Composition, including membership qualifications and independence*
  - *Responsibilities and working procedures of the BoC*
  - *Relationship between the BoC and the BoD, the GMS, and shareholders*
  - *Mechanism to ensure the independence of the BoC when conducting its oversight responsibilities*
  - *Remuneration of BoC members*

- ***Good BoD Practices***
  - *Director remuneration policy*
  - *Interaction and relationship with the BoC*

- ***Shareholder Rights***
  - *GMS procedures and mechanisms*
  - *Minority shareholder protection*
  - *Disclosure of related party transactions*
  - *The company's dividend policy*

- ***Internal Control and Risk Management***
  - *Internal control functions, including risk management framework*
  - *BoC role in risk oversight*
  - *Policy on the use of audit and consulting services and external auditor rotation*
  - *Accounting policies and standards*

- ***Disclosure and Transparency***
  - *Disclosure of financial reports and other material and important company information*

- *Disclosure of BoC and BoD composition and other corporate governance-related information*

- ***Accountability of the Company to Stakeholders***
  - *Communications and relations with investors and other parties that have an interest in the company*
  - *Policy on related party transactions*

Topics to be covered will depend upon the issues of greatest relevance to the company.

As a rule, company codes are approved by the BoC and the BoD, communicated to shareholders and investors, and published on the company's website. Company codes or guidelines must be consistent with the AoA and comply with any provisions under the country's relevant laws/regulations.

3.5 Company Code of Ethics

A code of ethics (also referred to as a code of conduct or responsibility statement) is a basic guide of conduct that imposes duties that a company's officers and employees owe towards its stakeholders, which may include customers, business partners, suppliers, government, and society.

A code of ethics:

- **Enhances the company's reputation/image**. A company's reputation and image constitute an integral, if intangible, part of its assets. Establishing a code of ethics is an effective way to communicate the value a company places on good business practices.
- **Improves risk and crisis management**. A code of ethics can bring potential problems to the attention of management and commissioners/directors before a full-blown crisis occurs, as it encourages employees to react to ethical dilemmas responsibly.
- **Develops a corporate culture and brings corporate values to the fore**. The distribution of a code of ethics to the company's officers and employees can assist in the development of a cohesive corporate culture, based on a shared set of values, which effectively guides employees in their daily work.
- **Advances stakeholder communications**. A code of ethics carries a strong signal to a company's stakeholders during times of crisis, communicating the company's commitment to ethical behavior and underlining that possible transgressions are exceptions rather than the rule.
- **Avoids litigation**. A code of ethics that is implemented effectively can help minimize litigation risks resulting from fraud, conflicts of interest, corruption and bribery, and insider trading.

All companies bear individual characteristics that reflect their size and industry objectives, as well as their respective business culture, values, shareholder composition, and many other factors. A code of ethics should reflect these differences.

Developing a code of ethics is a process as much as an outcome. To begin, a company should examine its internal ethics climate, such as the amount

and quality of ethical guidance its employees and officers receive in order to identify weaknesses and make recommendations for improvement. When moving to develop its specific code of ethics, a company should conduct a broad consultative process that includes input by all employees, from workers to senior executives. This will assist the development of a comprehensive instrument that guides the company's specific practices. By the time the code of ethics is submitted for approval by the BoC and BoD, every employee should ideally be familiar with it and have played a role in its drafting, a process that will likely improve internal compliance. The company must also recognize that the "tone at the top" matters, which means that commissioners, directors, and senior management must set an example of their commitment to the principles in the company's code of ethics.

A code of ethics should be user-friendly by providing practical (rather than aspirational) guidance on how to handle ethical dilemmas that may arise in the day-to-day course of business. In support of a code of ethics, the company may wish to establish an ethics training program, appoint an ethics officer or establish an ethics committee to advise and educate officers and employees, and provide guarantees for confidential counseling. The ethics committee should review and update the company's code of ethics on a regular basis.

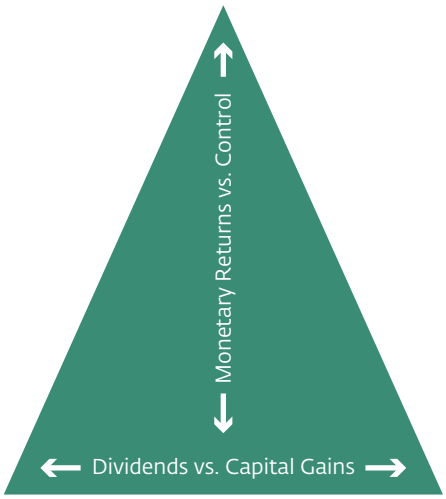
CHAPTER 4
An Introduction to Shareholder Rights

THE CHAIRMAN'S CHECKLIST

- Does the AoA protect shareholder rights in accordance with all relevant Indonesian laws and regulations? Do commissioners and directors take appropriate measures to ensure the protection of these rights?
- Does the company hold a GMS regularly?
- Do all commissioners and directors take measures to encourage shareholders to exercise their rights, particularly the right to vote? Do shareholders exercise their rights collectively?
- Does the company freely provide shareholders with company information? Are shareholder requests processed properly and on time?
- Do the BoC and BoD provide complete and accurate company information within appropriate timeframes, especially in relation to shareholder rights?
- Do the BoC and BoD facilitate the protection of shareholder rights?
- Do the BoC and BoD ensure the AoA, internal regulations, and other internal documents do not impose additional obligations on shareholders other than the ones clearly defined by law?

Investors purchase shares in a company for a variety of reasons, as illustrated in *Figure 6*.

Figure **6** Common Reasons for Becoming a Shareholder



Control: Shares provide investors with the opportunity to influence the company's decision-making. The greater the number of voting shares held by a shareholder, the greater the influence he/she normally wields.

Dividends: Dividends play an important role in investment decisions. Regular dividend payments, especially if an investor holds a portfolio of shares, can generate predictable cash flows.

Capital Gains: Investors purchase shares to benefit from capital growth. Unlike dividends, investors need to sell their shares to realize the gains represented by rising share prices.

Shareholders in Indonesia have various rights, including the right to attend and vote in the GMS (on the composition of BoC and BoD or amendments to the AoA); the right to dividends and company assets in the event of liquidation/winding up; and the right to information. To realize these rights, shareholders must be recorded in the company register, and different classes of shares may attract different sets of rights.

Laws and regulations that protect shareholder rights play an important role in maintaining healthy capital markets by building investor confidence and attracting shareholders to participate in trading. In contrast, where legal protections for shareholders are ineffective or poorly enforced, companies may struggle to attract investors, resulting in underdeveloped, thinly traded financial markets. This chapter provides an overview of Indonesia's legal framework with respect to the protection of shareholder rights.

4.1 Share Classifications

The ICL requires Indonesian companies to clearly define their share classifications. If a company has more than one share class, one of these will be common shares,[30] and other classes of shares may be referred to as preferred shares. Companies are permitted to choose whether to issue different share classes and to select the combination of rights and obligations attached to each class.[31] Once entered in the company register, shareholders will be provided with proof of ownership in the form of one or more share certificates.[32]

4.1.1 Common Shares

Common shares confer the right to participate in certain company decisions through voting rights at the GMS. They also confer the right to share in company profits, either through dividends or capital gains. In Indonesia, common shares have the following characteristics:[33]

- The right to vote on GMS resolutions concerning company management
- The right to dividends
- The right to company assets (in proportion to the shareholding) in liquidation/winding up

Each share holds a nominal value, also known as the accountable par, which is a portion of the company's capital. The company's AoA will define the number, the nominal value/accountable par, and the rights attached to common shares. All common shares carry the same rights, interests, and obligations in accordance with the ICL and the company's AoA.

[30] ICL, Article 53(1) and (3).
[31] ICL, Elucidation of Article 53(4).
[32] ICL, Article 51.
[33] ICL, Elucidation of Article 53(3).

4.1.2 Preferred Shares

Companies in Indonesia maintain the right to issue various classes of preferred shares. All shares in the same class must confer the same rights to the shareholders. In the case of listed companies that have various classes of preferred shares, the GMS must approve the rights and obligations attached to each class, which the company must also freely disclose to all shareholders.

It is good practice, although not a legal requirement in Indonesia, for the AoA to set out the company's procedures for determining the value of dividends and amounts to be paid upon winding up for each share class. The ICL distinguishes preferred shares according to the specific rights they confer. The following are common types of preferred shares:[34]

- Shares with or without voting rights
- Shares with special rights to nominate members of the BoC or BoD
- Shares that after a certain period can be transferred or exchanged for another share class
- Shares that confer priority rights to dividends, or priority rights to company assets in liquidation/winding up

Table 6 provides comparisons between common and preferred shares under the ICL.

Table **6** Main Differences between Common and Preferred Shares

	Common Shares	Preferred Shares
Is this share class mandatory?	Yes, must always be issued	No, preferred shares are optional
Can companies issue different classes of these shares?	No, only one class of common shares may be issued	Yes, different classes of preferred shares may be issued
Can this type of share be converted into other securities?	Yes, common shares may be converted into other securities	Yes, preferred shares may be converted into other securities
Do shareholders have the right to vote, to attend	Yes, with certain statutory exceptions	Yes, except for non-voting preferred shares

[34] ICL, Article 53(4).

the GMS, or to nominate candidates to the BoC and BoD		
Do shareholders have the right to freely transfer their shares?	Yes, subject to AoA requirements	Yes, subject to AoA requirements
Can the AoA grant additional rights to shareholders?	Yes	Yes

Best Practice

Companies should provide investors with adequate information on the rights attached to all series and classes of shares, which is material to their investment decisions. Further, companies must not make changes to the rights attached to classes of shares without the approval of those shareholders that will be negatively affected. Proposals to change the voting rights of different series and classes of shares should be submitted for approval at the GMS by a specified (normally higher) majority of voting shares in the affected categories.[35]

[35] *G20/OECD Principles of Corporate Governance*, 26.

4.2 General Shareholder Rights

The ICL distinguishes between the rights of individual shareholders and the rights that groups of shareholders hold collectively. Shareholder rights may also be distinguished according to whether they confer decision-making power (such as the right to vote on GMS resolutions) or simply the right to share in the company's profits through dividends and assets in liquidation. ***Figure 7*** illustrates these distinctions.

Figure **7** Types of Shareholder Rights

Indonesia's CG Code recommends that companies adhere to the following principles with regard to shareholder rights:[36]

1. Companies must protect shareholder rights in accordance with Indonesian law and OJK regulations, as well as relevant provisions of the AoA. Shareholder rights must at least include:
    - The right to attend, express an opinion, and vote in the GMS according to the principle of one share, one vote.
    - The right to obtain information in a reasonable time frame, except with respect to confidential matters.
    - The right to share in the company's profits (such as through dividends or other profit sharing arrangements) in proportion to the number of shares held.
    - The right to receive GMS notices and other details on GMS procedures in order to participate effectively in company decisions.

[36] *Indonesia's Code of Good Corporate Governance*, 21-22.

- Where a company has more than one share class, each shareholder should be entitled to cast a vote and receive fair treatment in accordance with his/her share classification and the number of shares owned.

2. Shareholders (including minority shareholders) should also abide by laws, regulations, and the AoA, as follows:
    - The controlling shareholder should (1) consider the interests of minority shareholders and other stakeholders in accordance with laws and regulations; and (2) disclose relevant information to law enforcement agencies if there is a suspected breach of laws and regulations or when otherwise requested by the relevant authorities.
    - Each shareholder should (1) segregate the company's assets from his/her personal assets; and (2) where a shareholder is also a member of the BoC or BoD, he/she must segregate his/her functions in each capacity.
    - Where a shareholder is the controlling shareholder in more than one company, accountability and inter-company relations should be carried out clearly.

In addition, each shareholder is entitled to file suit against the company in a district court if he/she/it has suffered harm as a result of GMS, BoC or BoD decisions.

In the banking industry, controlling shareholders must pass a fit and proper test issued by OJK in order to realize company rights. Shareholders who do not pass OJK's integrity standards under the fit and proper test will not be counted toward the GMS quorum, and therefore may not vote or receive dividends.[37] Shareholders who fail to meet OJK's financial standards under the fit and proper test will only be able to exercise those rights which they enjoyed through their shareholdings prior to becoming a controlling shareholder.[38]

[37] Circular Letter of OJK No. 39/SEOJK.03/2016 on Fit and Proper Test for Future Controlling Shareholders, Future Members of the Board of Directors, and Future Members of the Board of Commissioners of Commercial Banks, Article IX(10).
[38] Circular Letter of OJK No. 39/SEOJK.03/2016, Article IX(11).

4.3 Specific Shareholder Rights

4.3.1 The Right to Vote

Shareholders participate in the company's decision-making process by voting in the GMS. Important matters that fall within the GMS' authority include:

- Amending the AoA
- Developing corporate strategy
- Authorizing an increase/decrease of share capital
- Electing and dismissing BoC and BoD members
- Approving extraordinary transactions, such as investment or divestment of 50 percent or more of the company's assets
- Approving dividends and annual financial statements
- Approving reorganization of the company

Company shares generally carry one vote each, however, voting rights will not apply for:[39]

- Company shares that the company itself controls
- Shares in a parent company that are directly or indirectly controlled by its subsidiary
- Shares in the company controlled by another company whose shares are directly or indirectly owned by the company

The following are legal consequences when shares are classified to be non-voting:

- Precludes voting on all issues during the GMS
- Precludes voting on the approval of related party transactions in which the shareholder is an interested party

The ICL provides that if a shareholder owns a fraction of the nominal value of a share, he/she will generally not be granted an individual voting right.

[39] ICL, Article 84.

This is because the rights attached to shares are indivisible, and only one vote is attached to each share. However, a shareholder owning a fraction of the nominal value of a share will have the right to vote if his/her/its total shareholding is equal to the nominal value of one share in that share class.[40] Joint shareholders of a share with voting rights must appoint one representative to exercise the rights attached to that share (such as to vote) on their behalf.[41]

Shareholders may exercise their right to vote either individually in the GMS or by proxy through power of attorney.[42] Listed companies may not restrict their shareholders from participating in the GMS. Such companies must facilitate all shareholder requests for their authorized proxies to participate in voting. All companies should attach a standard proxy-authorization form/letter in the notice of GMS. Members of the BoC and BoD, or other company employees, may not act as proxies. Beyond that limitation, however, unless otherwise restricted by law/regulation, shareholders may appoint any individual to act as their proxy.[43]

In public companies, where the company intends to amend rights attached to one class of shares, only shareholders in that particular class may vote on the amendment. In the event the shares in that class do not carry voting rights, OJK grants shareholders in that class the right to vote and adopt a GMS resolution on the proposed amendment.[44]

Best Practice

Companies increasingly recognize the value of using information technology to facilitate efficient participation in voting by shareholders. These technologies include secure systems for electronic voting in absentia. A common voting system that helps shareholders to vote in absentia is the direct-recording electronic voting system, which uses electronic ballots and transmits voting data from the polling place to another location over a public network. Voting data may be transmitted either as individual

[40] ICL, Article 54(2).
[41] ICL, Article 52(5).
[42] ICL, Article 85(1).
[43] ICL, Article 85(4).
[44] OJK Regulation No. 10/POJK.04/2017 on Amendment to OJK Regulation No. 32/POJK.04/2014 on GMS of public companies, Article 1(29B).

ballots at the time they are being cast, periodically as batches of ballots throughout the election day, or as one batch at the close of voting period. Some countries that use this system include Estonia, Ireland, Switzerland, the United Kingdom, and the United States.

4.3.2 The Right to Information

Every shareholder has the right to examine the shareholder register, special register, minutes of the GMS, and annual reports.[45] During the GMS, shareholders are entitled to obtain company information related to agenda items from the BoC or BoD as long as such disclosure is not harmful to the company's interests.[46] Shareholders may also request copies of materials in the GMS.[47] The AoA and internal regulations should specify the procedures that the company and shareholders must follow for distribution of information and materials. ***Figure 8*** illustrates best practice guidelines concerning shareholder rights to information.

Figure **8** Shareholder Rights to Information

Shareholders have the right to receive information on:			
Company Documents	**Financial Information**	**GMS**	**Other Information**
The AoA (including amendments to the AoA or a restatement of the AoA)	Annual reports	Minutes of the GMS and minutes of BoC and BoD meetings	The company's prospectus
Certificate of company registration	Financial statements	Voting ballots and proxies for the GMS (or copies of the same)	Data on the company's governing bodies
Title documents that verify the ownership of the company's assets	Reports submitted by the BoC, BoD, and the external auditor	List of person entitled to participate in the GMS, or entitled to receive devidents, and any other list prepared by the company for exercising shareholder rights	Reports on the company's activities submitted to the authorities
Internal regulations and other company documents			Lists of affiliated parties of the company
Shareholder register			Other documents specified by legislation or the AoA

[45] ICL, Article 100(3).
[46] ICL, Article 75(2).
[47] ICL, Article 82(4).

Due to the volume of corporate documents and information likely to exist in any company, it is preferable for companies with many shareholders to set out the procedures for shareholders to access information under the AoA or other internal regulations. These procedures should ensure that shareholders may obtain information within a reasonable timeframe and without disturbing the company's day-to-day activities.

4.3.3 The Right to Review Shareholder Register

Every shareholder has the right to check, refer to, extract, and copy the shareholder register; to request the amendment of incorrect information; and to include additional information where necessary by submitting a written request to the BoD. This right allows shareholders to contact other shareholders and coordinate voting for collective action purposes. It is also important for verifying the information in the shareholder register, as well as exercising rights attached to the shares.

Apart from the shareholder register, the BoD must maintain a special register detailing the shareholdings of BoC and BoD members and their families, including all securities owned both within and outside of the company and the dates these securities were acquired.[48]

The company must make its shareholder register and special register available for inspection at its headquarters.[49] At a shareholder's written request, the BoD must give the shareholder permission to examine the shareholder register, special register, GMS minutes, and annual reports, and to obtain copies of GMS minutes and annual reports.[50]

4.3.4 The Right to Receive Dividends

The right to receive dividends plays an important role in investment decisions of a company's shareholders. The BoD will develop a proposal on the pay-out ratio for each of the company's classes of shares and submit this to the GMS for

[48] ICL, Article 50(2).
[49] ICL, Article 50(4).
[50] ICL, Article 100(3).

approval. For listed companies, the GMS must make final decisions concerning dividend payments, which must not be higher than the rate proposed by the BoD. Dividends can be made in cash or in the form of common shares.

All net profits after deducting for reserves shall be allocated to shareholders as dividends, unless determined otherwise in the GMS.[51] The BoD may decide on a mid-term payment of dividends when such payment is considered to conform with the profitability of the company.[52]

4.3.5 The Right to Freely Transfer Shares

Shareholders are free to transfer their shares to other shareholders and/or external individuals, following the procedures set out under the company's AoA.[53] Shareholders may sell their shares at any time and at any price, subject to the requirements under the company's AoA. Shareholders of public companies that own a minimum of 5 percent of the company's total shares must report any changes to their shareholding in the increment of 0.5 percent to OJK within ten days.[54] Banks also carry special obligations to report planned changes to shareholder composition at least one month prior to issuing the change,[55] and to report the change itself to OJK within ten working days of the event.[56] Where a change in shareholder composition causes a change of control, the new controlling shareholder must also pass OJK's fit and proper test.[57]

4.3.6 The Right of First Refusal and Pre-Emptive Rights

A company may provide specific guidelines concerning the right of first refusal under its AoA. In the event the AoA requires selling shareholders to first offer their shares to existing shareholders or shareholders in a particular class

[51] ICL, Article 71(2).
[52] ICL, Article 72.
[53] ICL, Article 60(1).
[54] OJK Regulation No. 11/POJK.04/2017 on Report on Shareholding or Any Changes in Shareholding in Listed Companies, Article 2(2)(3).
[55] OJK Regulation No. 27/POJK.03/2016 on Fit and Proper Test for Principal Parties of Financial Institutions, Article 30(1).
[56] Bank Indonesia Regulation No. 11/1/PBI/2009 on Commercial Banks as amended by Bank Indonesia Regulation No. 13/27/PBI/2011, Article 22(1).
[57] OJK Regulation No. 27/POJK.03/2016, Article 30(2).

before making a general offer, these shareholders will have thirty days to make a purchase. After that time the selling shareholder may offer and sell their shareholding to third parties. This right of first refusal to existing shareholders only applies once, which means that if existing shareholders decline to accept the offer within the 30-day period, the selling shareholder may withdraw the offer.[58]

Under Indonesian law, shareholders typically hold pre-emptive rights that allow them to purchase newly issued shares on a priority basis before they are offered to third parties. Existing shareholders may subscribe to newly issued shares in proportion to their shareholding for the equivalent class of shares. This also applies to listed companies.[59]

The Purpose of Pre-Emptive Rights

Pre-emptive rights allow existing shareholders to maintain a proportional level of ownership that they enjoyed prior to the issuance of new shares, helping to protect their shareholding from becoming diluted.

Procedures for Exercising Pre-Emptive Rights

For public companies that intend to increase capital by issuing new shares and offering existing shareholders pre-emptive rights to subscribe, the company must first (i) obtain shareholders' approval; (ii) submit a Registration Statement to OJK; and (iii) obtain an effective statement from OJK following submission of the Registration Statement.[60] No rights issue may be undertaken before the foregoing requirements have been fulfilled. The Registration Statement to OJK must include at least:[61]

- A cover letter
- A prospectus
- Other documents required as part of the Registration Statement as detailed in OJK regulations

[58] ICL, Article 58.
[59] Decision of the Head of the Financial Services Authority No. KEP-26/PM/2003 on Pre-Emptive Rights (Regulation IX.D.1), Article 2.
[60] OJK Regulation No. 32/POJK.04/2015 on Increase of Capital of Public Companies with Pre-Emptive Rights, Article 8(1).
[61] OJK Regulation No. 32/POJK.04/2015, Article 18-19.

A shareholder who holds pre-emptive rights may exercise these rights fully or in part by submitting a written statement to the company requesting to purchase additionally issued shares or other convertible securities. This statement must include:

- *The shareholder's name*
- *The shareholder's location of residence*
- *The number of shares to be purchased by the shareholder*
- *A document verifying payment*

4.3.7 The Right to Demand Share Redemption

A shareholder is entitled to request the company to buy his/her shares at a fair price in the event the company takes actions which harm his/her interests. Actions that may trigger the exercise of this right include:[62]

- Amending the AoA
- Assigning or securing company assets that comprise more than 50 percent of the company's net assets
- Merger, consolidation, acquisition, or spin-off

A company may redeem shares under the following conditions:[63]

- Share redemption must not reduce the company's net assets below the sum of total issued capital plus the statutory reserve that has been set aside.
- The nominal value of all shares the company buys back, including pledges on shares or fiduciary security on shares that are held either by the company itself or another company whose shares the company owns directly or indirectly, does not exceed 10 percent of the company's issued capital or any other maximum levels that may be set by applicable capital markets regulations.

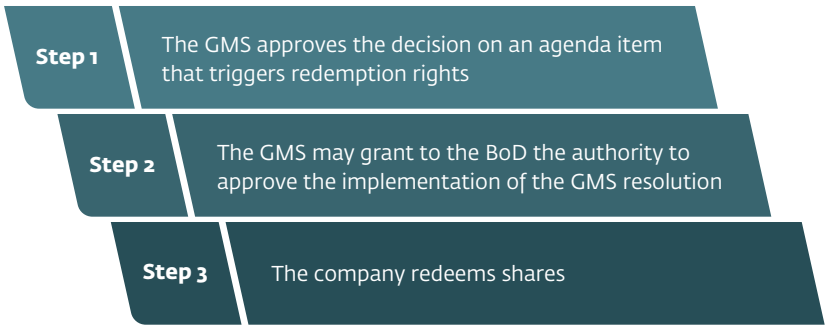
[62] ICL, Article 62(1).
[63] ICL, Article 37(1).

In the event the shares to be purchased exceed buy-back limits, which provide that a company may only redeem shares with a nominal value of up to 10 percent from the amount of issued capital in the company (unless otherwise regulated in the capital market legislation), the company must make efforts to ensure the remaining shares are bought by a third party.[64]

The ICL provides that the GMS must approve decisions to redeem shares, although other additional requirements may apply under the Law on Capital Markets. A GMS resolution on share buy-backs will be valid if adopted in accordance with requirements under the ICL and the company's AoA concerning notice, quorum, and voting. The GMS may confer upon the BoD authority to approve the implementation of the GMS resolution.

Figure 9 summarizes the steps required for a company to redeem shares:

Figure **9** Procedures for Share Redemption



4.3.8 The Right to Summon a GMS

The ICL stipulates that one or more shareholders representing at least one-tenth of the total number of voting shares in a company may request a GMS to be convened by submitting a request, together with reasons, to the BoD by way of registered letter.[65]

[64] ICL, Article 62(2).
[65] ICL, Article 79(2).

4.3.9 The Right to Nominate BoC and BoD Members

The GMS has the exclusive right to appoint members of the BoC and BoD.[66] In practice, majority shareholders often control the election and removal of board members.

4.3.10 The Right to Sue the Company

The ICL introduces the right for shareholders to request a court to overturn GMS decisions. Each shareholder is entitled to file suit against the company in a district court if the shareholder has been harmed by any action taken through a resolution of the GMS, BoC, or BoD which is considered unfair or unreasonable.[67] In addition, shareholders representing at least one-tenth of the total number of shares with voting rights may file suit through a district court against members of the BoC or BoD whose fault or negligence caused losses to the company.[68]

4.3.11 The Right to the Company's Assets During Liquidation

Shareholders are residual claimants when a company is being liquidated, which means that they will receive a portion of the remaining assets after creditor claims are satisfied. Owners of common shares have a right to receive a portion of the company's assets in proportion to their shareholding after the company has paid out its creditors and shareholders of other (higher) share classes (if any) in accordance with law.

During liquidation, a company must first satisfy its priority claimants (usually liquidation and administrative expenses, salaries, wages, employee benefits, and taxes) followed by obligations to its creditors. Finally, the liquidator divides the remaining assets among shareholders based on the share classes. The company's assets must be distributed to each group in order of priority. For example, the

[66] ICL, Article 94(1) and 111(1).
[67] ICL, Article 61(1).
[68] ICL, Article 97(6) and 114(6).

company cannot pay the liquidation value of common shares until it has paid the full liquidation value of higher priority shares. If the company does not have sufficient assets to pay all shareholders of the same priority class, then the assets must be distributed in proportion to the number of shares in that class. In the event that remaining assets have been divided among shareholders and there are outstanding creditors' bills, the district court will order the liquidator to retrieve the assets that have been divided among shareholders.[69]

[69] ICL, Article 150(4).

4.4 The State as Shareholder

The state can become a shareholder in a limited liability company, also known as a state-owned enterprise. State-owned enterprises may be either wholly or partially government owned. The percentage of shares that the government owns will normally determine its level of influence in the company. Indonesia's regulatory framework does not provide any provision regarding the government as the holder of privileged rights, unless for certain lines of business that are fully controlled by the state. However, under certain specified circumstances, the government may hold a so-called golden share, allowing the state to outvote all other shareholders in order to protect public interests. For banks, while a maximum ownership limitation is applicable to general shareholders, such limitations do not apply to the state.[70]

Best Practice

Foreign investors are usually cautious about investing in companies where shares are issued having privileged rights. Even though privileged rights arrangements can play a useful role in protecting the interests of the state and the public, it is recommended that state agencies carefully weigh all the pros and cons of implementing privileged rights arrangements on a case by case basis.

When the state owns all the shares of a state-owed enterprise, the GMS shall determine which minister shall be designated to act on behalf of the state as the shareholder. In cases in which the state does not own all the shares, the Minister of State-Owned Enterprises shall act as the shareholder.[71] The Minister of State-Owned Enterprises may authorize an individual or legal entity with the right of substitution to represent him/her in the GMS. Generally, the authorized party must first obtain approval of the Minister of State-Owned Enterprises with respect to:

- A change in the amount of capital

[70] OJK Regulation No. 56/POJK.03/2016 on Share Ownership in Commercial Banks, Article 3.
[71] Law No. 19 of 2003 on State-Owned Enterprises, Article 14(1).

- Amendments to the AoA
- Planned utilization of profits
- A merger, consolidation, acquisition, or dissolution of the state-owned enterprise
- Long-term investment and financing
- Requesting cooperation of the state-owned enterprise
- Formation of subsidiaries
- Transfer of assets

4.5 Shareholding Registration

4.5.1 Shareholder Register

The shareholder register is an important document that identifies the shareholders and the owners of other registered securities of the company. It can be used to verify the number, nominal value, type, and class of shares and other registered securities that are held. The shareholder register is also maintained to secure shareholder rights and to monitor the circulation of shares and other registered securities.

A company should create and maintain a shareholder register from the date of establishment. Such a register may be recorded on paper, electronically, or both. The shareholder register must contain at least:[72]

- Names and addresses of all shareholders
- Number, serial number, date of acquisition, and class of shares (if the company issues more than one share class)
- The amount of paid-up capital on every share
- Name and address of an individual or legal entity that has a pledge over shares, or who is the recipient of fiduciary security over shares, and the date of acquisition of this pledge or registration of the fiduciary security
- Information on the shares having been paid up in other forms

The shareholder register shall be kept in the head office of the company.[73] All shareholders have the right to check, refer to, extract, and copy the content of the shareholder register at any time during the working hours of the company.[74] As for public companies, the administration of the shareholder register can be assigned to a private company that is specifically established to engage in the business of shareholder registration.

[72] ICL, Article 50(1).
[73] ICL, Article 100(2).
[74] ICL, Article 100(3).

4.5.2 Company Register

The Company Register is a list of official records containing matters to be registered by each company.[75] This list must include data on the company's shareholding structure (authorized capital, number and nominal value of each share, and amount of subscribed and paid-up capital).[76] The aim of the Company Register is to record material information concerning Indonesian companies, which serves as the official source of information for all interested parties regarding the identity, data, and other important corporate information.[77] The Ministry of Trade is the authority responsible for maintaining the Company Register.[78] Companies that have been registered in the Company Register will be given a Company Registration Certificate for a period of five years, which must be renewed at least three months before the expiration date.[79]

[75] Law No. 8 of 1982 concerning Mandatory Company Register.
[76] Law No. 8 of 1982, Article 11(1).
[77] Law No. 8 of 1982, Article 2.
[78] Law No. 8 of 1982, Article 18.
[78] Law No. 8 of 1982, Article 22.

4.6 Protection of Shareholder Rights

The protection of shareholder rights is central to corporate governance, and is particularly important for companies operating in emerging markets or transitional economies. In Indonesia, protections for shareholders exist under the ICL, OJK regulations (which apply to listed companies), and additional internal regulations that companies may choose to adopt.

4.6.1 Guarantees in the Indonesian Company Law

The ICL provides many guarantees for the realization of shareholder rights. Some of these guarantees are procedural in nature and relate to the organization of the GMS. Others derive from the respective obligations of the company's governing bodies (the BoC and BoD) to protect shareholders.

The ICL adopts a one share, one vote principle, unless the AoA stipulates otherwise.[80] Judicial protection for minority shareholders under the ICL applies as follows:

ICL	Minority Shareholder Rights
Article 61(1)	Each shareholder is entitled to file suit against the company in a district court if the shareholder has been harmed by any company action considered unfair and unreasonable due to a resolution of the GMS, BoC, or BoD.
Article 62(1)	Each shareholder is entitled to request that his/her shares be bought at a fair price if the shareholder does not approve of actions taken by the company that harm the shareholder or the company. Actions that trigger this right include: • Amendments of the AoA • Assignment or securing of assets of the company that have a value of more than 50 percent of the company's net assets • Mergers, consolidations, acquisitions, or spin-offs

[80] ICL, Article 84(1).

Article 97(6) and 114(6)	On behalf of the company, shareholders representing at least one-tenth of the total number of shares with voting rights may file suit against members of the BoC/BoD who by their fault or negligence cause losses to the company.
Article 138(3)	One or more shareholders representing at least one-tenth of the total number of shares with voting rights may submit a petition requesting the company to be inspected.
Article 144(1)	The BoC, BoD, or one or more shareholders representing at least one-tenth of the total number of shares with voting rights may submit a proposal to the GMS for the company to be wound up.

The protection of minority shareholder rights remains a key concern for many international investors considering investing in Indonesian companies. Powerful company owners and majority shareholders often pay little or no heed to minority shareholders. On the other hand, minority shareholders are often passive and rarely participate in shareholder meetings, reflecting the lack of a strong participatory culture among Indonesian investors. This makes the role of regulatory and supervisory bodies even more important to ensure that proper attention is paid to the protection of shareholder rights.

Comparative Practice

In some countries, non-governmental organizations play an important role in exerting pressure on companies. Organizations do this in various ways. For example, some organizations may become shareholders themselves and participate in the GMS. Others may conduct media campaigns to exert pressure on companies and draw public attention to the issue of shareholder protection. Non-governmental organizations may also assist shareholders by providing legal help for filing a claim in court or establishing a special fund for the protection of shareholder interests.

4.6.2 Articles of Association

It is important for the AoA to ensure that shareholder rights, and the mechanisms designed to ensure and protect these rights, are clearly defined. These systems are necessary to ensure companies treat their shareholders fairly and support shareholders to fully exercise their legal rights.

Listed companies must follow OJK's model for developing an AoA. The AoA of a listed company should include:[81]

- The name and domicile of the company
- The company's period of incorporation
- The company's purposes, objectives, and business activities
- Capital structure
- Issuance of equity securities
- Increase in the company's authorized capital
- Shares
- Proof of share ownership
- Share certificates and collective share certificates for damaged or lost shares
- Collective custody
- Transfer of rights to shares
- Members of the BoC and BoD
- Work plans, annual reports, annual financial reports, and use of profits
- Information on the GMS

4.6.3 Shareholder Activism

The protection of shareholder rights begins with good corporate behavior, an appropriate legal and regulatory framework, and strong enforcement

[81] Decision of the Chairman of the Capital Market and Financial Institutions Supervisory Agency No. Kep-179/BL/2008 on Articles of Association for Public and Listed Companies (Regulation IX.J.1).

procedures. Shareholders themselves must also play a role in this process, because they are often the only parties aware of violations of their rights and therefore are in the best position to file a complaint with the company or, ultimately, with the regulatory and judicial bodies.

Institutional investors vary in the extent to which they actively participate in company management. When such investors hold a significant equity stake, they are more likely to monitor their portfolio companies closely, vote their shares, and sometimes demand a board seat. Other institutional investors limit their participation to voting at the GMS, typically following the advice of a proxy. Additional factors that affect the extent to which institutional investors participate in company management may include the investors' business model, their investment strategies, and socio-political objectives.

The OECD Principles recommend that institutional investors acting in a fiduciary capacity disclose their overall corporate governance and voting policies with respect to their investments, including the procedures that they have in place for deciding on the use of their voting rights. They should also disclose how they manage material conflicts of interest that may affect the exercise of key ownership rights regarding their investments.[82]

Since institutional investors can provide an important source of capital to support the development of capital markets, policy makers in different jurisdictions have developed stewardship codes to encourage such investors to engage actively in a purposeful and constructive dialogue with investee companies. Institutional investors can provide an outside view, assist in detecting blind-spots in corporate strategy, raise awareness of external risks, and help connect other stakeholders to add value.

The United Kingdom's Financial Reporting Council produced the first country-based stewardship code in 2010, which was amended in 2012. The Stewardship Code focuses on the role of institutional investors. The Stewardship Code requires companies to "comply or explain" and includes the following principles: "So as to protect and enhance the value that accrues to the ultimate beneficiary, institutional investors should: (i) publicly disclose their policy on how they will discharge their stewardship responsibilities; (ii) have a robust policy on managing conflicts of interest in relation to stewardship which should be publicly disclosed; (iii) monitor their investee companies; (iv) establish clear guidelines on when and how they will escalate their stewardship activities; (v)

[82] *G20/OECD Principles of Corporate Governance*, 22-23.

be willing to act collectively with other investors where appropriate; (vi) have a clear policy on voting and disclosure of voting activity; (vii) report periodically on their stewardship and voting activities."[83]

Several jurisdictions including Malaysia, Singapore, and Thailand have begun to develop similar codes. In Southeast Asia, Malaysia was the first mover with the implementation of the Malaysian Code for Institutional Investors in 2016. While Indonesia has not yet introduced such a code, OJK established similar guidelines for institutional investors in 2015 with OJK Regulation No. 43/POJK.04/2015 on the Code of Conduct for Investment Managers.

4.6.4 Shareholder Agreement

Shareholder agreements can be an important tool to allow shareholders to exercise collective action. Such agreements support minority shareholders to make use of minority rights, for instance, a shareholder agreement may allow shareholders with at least 10 percent ownership to appoint a fiduciary to examine the company's financial statements.

In principle, shareholder agreements are based on the principle of freedom of contract. Nevertheless, because they carry important corporate governance implications, it is necessary to ensure the following:

- First, shareholder agreements cannot substitute (or contradict) the company's founding documents (the AoA).
- Second, to prevent the company from attempting to control shareholders' voting power, it is important to prohibit the inclusion of certain terms in such agreements.
- Finally, it is necessary (particularly for publicly traded companies) to ensure greater transparency of voting control by requiring the disclosure of such arrangements.
- Accordingly, it is good practice for shareholders to inform the GMS when a shareholder agreement is concluded or amended prior to the next shareholder meeting.

[83] *The UK Stewardship Code* (Financial Reporting Council, 2012), 5, https://www.frc.org.uk/getattachment/d67933f9-ca38-4233-b603-3d24b2f62c5f/UK-Stewardship-Code-(September-2012).pdf.

Under prevailing laws, there is no specific regulation on the terms of shareholder agreements or on the disclosure of shareholder agreements.

4.7 Shareholder Responsibilities

4.7.1 Obligation to Make Full Payment for Subscribed Shares

The main legal responsibility of shareholders is to make full payment for their subscribed shares. At least 25 percent of the authorized capital must be issued and paid up in full.[84]

4.7.2 Obligation to be Liable for Debt and Other Liabilities of the Company

Shareholders are generally not personally liable for legal relationships that the company enters with other parties, and are not liable for losses the company incurs beyond their individual shareholding. However, the provisions above do not apply under the following circumstances:[85]

- The requirements for the company to be a legal entity have not been fulfilled
- The shareholder directly or indirectly exploits the company in bad faith for his/her personal interest
- The shareholder is involved in illegal acts committed by the company
- The shareholder illegally uses the company's assets resulting in the company's assets becoming insufficient to pay off the company's debts

4.7.3 Other Obligation

Shareholders are responsible to comply with the AoA and prevailing laws and regulations; to observe resolutions of the GMS, the BoC, and the BoD; and to provide the correct address when he/she registers for shares. Other obligations

[84] ICL, Article 33(1).
[85] ICL, Article 3.

may include disclosure obligations that apply when shareholders pass certain ownership thresholds, or disclosure of the intent to acquire further shares or gain control of a company. These additional responsibilities generally apply to larger shareholders.

CHAPTER 5
General Meeting of Shareholders

THE CHAIRMAN'S CHECKLIST

- Authority of the General Meeting of Shareholders
  - Does the AoA clearly set out the GMS' authority?
  - Does the AoA explicitly delegate any specific authority to the BoC and BoD?
- Preparation for the General Meeting of Shareholders
  - Does the BoD provide workable and timely mechanisms to include all legitimate shareholder proposals on the agenda?
  - Does the BoD have a clear duty to ensure that the agenda is not changed after it has been sent to all shareholders?
  - Does the company properly inform all shareholders of the GMS?
  - Is sufficient information available for all shareholders to make well-informed decisions on agenda items?
  - Does the AoA require the company to provide additional information to shareholders (or others having recognized interests) on specific agenda items?
- Conducting the General Meeting of Shareholders
  - Is the venue of the GMS convenient, easily accessible for all shareholders, and in line with the requirement under the ICL and the AoA?

- Does the company ensure that the GMS' quorum is properly verified and recorded?
- Are members of the BoC and BoD and the external auditor present during the GMS? Do shareholders have the right and opportunity to ask questions during the GMS?
- Does the BoD (or other corporate body authorized with this responsibility) ensure that effective and independent mechanisms to count votes are in place during the GMS and that the voting results are properly recorded? Does the BoD ensure that all decisions are valid and that all applicable legal requirements are met?
- Are the voting results properly communicated to shareholders?

Extraordinary General Meeting of Shareholders

- Does the BoD convene an EGMS when circumstances require, in conformity with the law?
- Does the BoD convene an EGMS upon a request by shareholders (or a group of shareholders) owning at least 10 percent or less of voting shares, as stipulated in the company's AoA?

Shareholders are the main contributors of a company's equity capital. At the same time, shareholders may lack the necessary skills to run a company and do not always wish to participate in day-to-day management. For this reason, shareholders entrust professionals in the BoD to run the company's operations, and elect a BoC to supervise and guide the BoD. This does not mean that shareholders completely give up their rights with respect to the governance of the company. Rather, shareholders most commonly exercise these rights through the GMS.

A company's AoA will determine the GMS as a specific company organ with separate rights and responsibilities from the BoC and BoD. The ICL and the AoA set the boundaries of the GMS authority and responsibilities. It is through the GMS that shareholders express their opinions concerning important corporate decisions, such as amendment of the AoA, approval of annual reports

and financial statements, election and dismissal of BoC and BoD members, payment of dividends and distribution of company profits, major corporate transactions, and other matters as determined under the ICL and the company's AoA. The GMS also provides shareholders with an opportunity to discuss issues, meet in person with the company's commissioners and directors, ask questions, and make decisions concerning the company's future direction. As such, shareholders exercise their right to participate in the decision-making of the company through the GMS.

There are two types of GMS:

1. **Annual General Meeting of Shareholders (AGMS)**
   The ICL requires companies to hold a GMS at least once a year, in which the BoD must present the company's annual report.[86] The AGMS must be held within six months from the end of the fiscal year. The BoD shall convene the AGMS in the company's domicile or in the place where the company conducts its main business activity, pursuant to its AoA. For public companies, the AGMS must be held at the stock exchange where the company is listed. However, if all shareholders are present or represented in the AGMS and are in agreement, the company may hold the AGMS at any location within Indonesian territory. Under these circumstances, the ICL requires unanimous shareholder agreement for AGMS resolutions to be approved.[87]

2. **Extraordinary General Meeting of Shareholders (EGMS)**
   All other GMS (aside from the AGMS) are called EGMS. An EGMS is a meeting held in response to specific company needs and interests, such as to give approval for consolidation, merger, acquisition, or spinoff; to elect and dismiss the BoC/BoD; or to approve capital increase or reduction. There are no limitations on the number of EGMS that a company can conduct during the year.

The preparation and conduct of a company's GMS is subject to detailed procedural requirements under the ICL, as well as internal corporate policies and procedures. This chapter describes the authority of the GMS, its organization, and legal requirements for adopting valid decisions.

[86] ICL, Article 78(3).
[87] ICL, Article 76.

5.1 Authority of the General Meeting of Shareholders

Chapter VI of the ICL sets out the authority of the GMS. The AoA may, however, provide additional authority to the GMS, unless otherwise determined by the law.

Figure **10** GMS Authority

The GMS Has Authority Over:

- Amendment of the AoA
- Annual reports, financial statements, and reports of the BoC and BoD
- Annual work program
- Appointment and dismissal of BoC and BoD members
- Remuneration of BoC and BoD members
- Dividend payments and utilization of company profits
- Buybacks and share transfers
- Capital increase or reduction
- Company assets
- Legal actions of the company
- Mergers, acquisitions, spinoffs, consolidation, and bankruptcy
- Dissolution and liquidation

The GMS holds primary authority over the following matters:

1. Decisions on governing bodies

The ICL stipulates that the GMS has the authority to appoint BoC and BoD members, while the AoA should dictate the procedures for nomination,

appointment, replacement, and dismissal of BoC and BoD members.[88] The ICL also provides that the GMS may set the remuneration of BoC and BoD members.[89]

For banks, members of the BoC and BoD appointed by the GMS can only exercise their duties once they obtain approval from OJK.[90]

2. Control over the company's operations

- Approve annual reports and annual financial statements
- Review and approve the BoC's supervisory report
- Review and approve the BoD's report
- Approve company strategies/plans
- Approve amendments to the AoA

For public companies, OJK stipulates the minimum content that the BoC and BoD must include in the annual report to the GMS. Under the OJK requirements, the BoD must report at least the following:[91]

- Brief description of the performance of the company that includes: (i) the company's strategies and strategic policies; (ii) comparison between targets and achievements; (iii) obstacles encountered by the company
- Description of business prospects
- Application of good governance by the company
- Changes in the membership composition of the BoD and reasons for such changes

The BoC must report at least the following:[92]

- Assessment of the BoD's performance
- Assessment of the implementation of company strategy
- Assessment on the BoD's projections for the company's business prospects
- Assessment of the application of good corporate governance
- Any changes to composition of the BoC and reasons for such changes
- Frequency and methods of the provision of advice to the BoD

[88] ICL, Article 94 and 111.
[89] ICL, Article 96 and 113.
[90] OJK Regulation No. 27/POJK.03/2016, Article 2(4).
[91] Circular Letter of OJK No. 30/SEOJK.04/2016 on Format and Contents of Annual Reports of Issuers or Public Companies, Article III(2c).
[92] Circular Letter of OJK No. 30/SEOJK.04/2016, Article III(2d).

There is no regulation on the authority to appoint and dismiss the external auditor. In practice, the company usually appoints its external auditor through the AGMS. However, the ICL requires the BoD to submit the company's financial statements to a public accountant under the following cases:[93]

- The company's activities involve collecting and managing public funds
- The company issues a letter of acknowledgement of debt to the public
- The company is a public company
- The company is a state-owned enterprise
- The company owns more than Rp 50 billion of assets and/or total turnover
- It is required under Indonesian laws and regulations

3. Decisions on dividends

The GMS has the right to make decisions concerning the use of the company's net profits, including determining the amount to be set aside as reserves (if the amount is bigger than the amount required by the ICL, which is 20 percent of the issued and paid up capital of the company). All net profits (aside from reserve funds) shall be allocated to the shareholders as dividends unless the GMS determines otherwise. However, the company can only allocate dividends to shareholders if it has a positive balance of profits.[94] The BoD, subject to prior approval by the BoC, may decide on the timing of dividend payments and how dividends shall be paid to shareholders.

4. Decisions on major corporate transactions

The ICL specifies that the BoD must obtain GMS approval for significant company transactions that include either the transfer or encumbrance of more than 50 percent of the company's net assets.[95]

For lower value transactions, common practice is for the GMS to authorize the BoC to approve these transactions. The BoD should submit the transaction proposal to the BoC for its approval, or at a minimum, must consult with the BoC before undertaking such transactions. Some companies include a provision in their AoA specifying the threshold amount for transactions to require approval from the BoC.

[93] ICL, Article 68.
[94] ICL, Article 70.
[95] ICL, Article 102.

5. Decisions on capitalization

The ICL stipulates that the GMS has the authority to approve a capital increase or reduction. However, to be valid, all GMS resolutions concerning capitalization must meet the minimum quorum and voting requirements set out under the ICL as well as any additional provisions stipulated under the company's AoA.[96]

6. Decisions on the company's reorganization and liquidation

- Approve all changes to the composition of the company including mergers, acquisitions, spinoffs, and consolidations
- Approve the liquidation of the company

Chapter X of the ICL regulates the dissolution, liquidation, and expiration of companies as legal entities and stipulates that the GMS has the authority to authorize such measures by means of GMS resolutions.

[96] ICL, Article 41 and 44.

5.2 Preparing for the General Meeting of Shareholders

The ICL sets out the principal requirements for private and public companies on how to conduct a GMS. In addition, listed companies must also comply with the following regulations:

- Decision of the Chairman of the Capital Market and Financial Institutions Supervisory Agency No. Kep-179/BL/2008 on Articles of Association for Public and Listed Companies (Regulation IX.J.1)
- OJK Regulation No. 32/POJK.04/2014 on GMS of Public Companies as amended by OJK regulation No. 10/POJK.04/2017

Preparing for the GMS requires careful planning and adherence to procedural requirements under the ICL and the company's AoA. ***Figure 11*** summarizes the steps that a company should follow to prepare for the GMS.

Figure **11** Preparation for the GMS

STEP

1. Set the date for the GMS.
2. Draft the agenda.
3. Prepare materials and documents for the meeting.
4. Prepare a draft resolution for each issue to be discussed in the meeting.
5. Determine the location and time of the meeting.
6. Determine the record date, which is the date on which shareholders must be recorded in the company register in order to receive dividends.
7. Provide a copy of GMS materials in the head office.

NOTE

For public companies:

Announce GMS invitation at least twenty-one days before the invitation is sent to the shareholders, not counting the date of the announcement and GMS invitation. The mechanism of the announcement shall comply with OJK regulation on GMS for public companies

For non-public companies:

Send an invitation to all shareholders with voting rights at least fourteen days before the GMS is held without calculating the date of the announcement and GMS invitation.

5.2.1 Drafting the Agenda

The initial step in preparing for a GMS is to draft the agenda. The agenda structures the GMS and lists all the issues to be addressed. The GMS must discuss all items included in the agenda, and generally may make decisions concerning only those items that are properly included in the agenda and meet the ICL requirements. Other issues that are not included in the agenda may only be discussed if all shareholders representing 100 percent of the voting shares attend the GMS (whether in person or via an authorized representative/proxy) and agree to the addition of the new agenda items. In such cases, the GMS may pass resolutions on items that are not included in the agenda if all shareholders present unanimously approve the relevant resolution.[97]

Best Practice

In the period preceding the decision to conduct a GMS, the BoC should review all the proposals (formal and informal) made by shareholders to include specific items on the agenda. Mutual understanding and cooperation between the BoC and shareholders is critical and therefore it is a good practice to notify shareholders about rejected agenda items. This by no means precludes the shareholders from including items on the agenda after the decision to conduct the GMS.

5.2.2 Making Preliminary Decisions

The BoD must make key decisions concerning the agenda, date, place, time, notification procedures, list of materials, and proxy voting before logistical preparations for the GMS can be made.

Date of the GMS

The ICL requires companies to conduct their AGMS not more than six

[97] ICL, Article 75(4).

months from the end of the financial year. The BoD may determine the exact date for each AGMS within that six-month period, following any additional requirements set out under the company's AoA. Companies have the discretion to hold an EGMS at any time as needed.[98]

Location of the GMS

An Indonesian company must hold its GMS (1) within its place of domicile or where the company conducts its main business; or (2) or at any location within Indonesian territory, as long as all shareholders attend (or are represented at) the meeting and approve the agenda. Public companies must hold their GMS within the domicile of the stock exchange where they are listed or the domicile of the company.

Generally, a company should hold its GMS at its place of domicile or at a location specified in the AoA. If the company's domicile is difficult to reach, the company may consider other means to conduct the GMS permitted by the ICL, for example through video conference or by passing a circular resolution of shareholders. The ICL requires unanimous approval by all shareholders to pass a circular resolution.

5.2.3 Preparing the Shareholder List

Shares bestow on their owners the right to attend and cast votes in the GMS.[99] However, these rights will apply only after the shares are recorded in the shareholder register under the shareholder's name.[100]

The next step is to compile a list of shareholders who are entitled to participate in the GMS. Pursuant to the ICL, the BoD shall keep and maintain the list of all shareholders.[101] For listed companies, the Securities Administration Agency will conduct all administrative matters relating to shareholders. Only persons included in the shareholder list are entitled to participate in the GMS, except for holders of shares with non-voting rights.[102] Only shareholders with voting rights may vote in the GMS.

[98] ICL, Article 78(4).
[99] ICL, Article 52(1)(a).
[100] ICL, Article 52(2).
[101] ICL, Article 50(1).
[102] ICL, Article 52(3).

Shareholders lose voting rights when they sell their shares, as voting rights are transferred automatically to the new owner. The ICL stipulates that a company's AoA may determine the procedures for share transfers as long as they do not contravene other relevant laws and regulations.[103] Shares must be transferred by way of a deed (either notarial or private deed for minority transactions) or by a notarial acquisition deed (if the transaction is considered an acquisition transferring the rights to shares). The shareholder making the transfer must submit a copy of this deed to the company. After receiving a copy of the deed of transfer, the BoD must update the shareholder register.

In practice, if the shareholder register is not updated after the record date (the date on which shareholders must be recorded in the company register in order to receive dividends), the selling shareholder still has the right to attend the meeting and vote. However, the selling shareholder must ensure that the new shareholder can vote at the GMS. There are two ways for the selling shareholder to fulfill this obligation:

- Grant power of attorney to the new owner, or
- Participate in the GMS and vote in accordance with the instructions of the new owner

5.2.4 Providing Proper Notice

Once the procedures set out above are completed, all shareholders eligible to participate must be notified of the GMS no later than fourteen working days prior to the opening date of the GMS, not counting the date of announcement and the date of the GMS.[104] For public companies, OJK regulations set out the requirements for announcement, invitation, and timing of the GMS notice.[105]

It is good practice to ensure that the GMS notification:

- Allows sufficient time for all shareholders to prepare for the GMS
- Be given to all shareholders
- Allows sufficient time for shareholders to contact other shareholders

[103] ICL, Article 55.
[104] ICL, Article 82(1).
[105] OJK Regulation No. 32/POJK.04/2014 as amended by OJK regulation No. 10/POJK.04/2017.

- Allows sufficient time for shareholders to read and understand the agenda

How to Notify

The ICL provides that companies may issue invitations to the GMS by registered letter and/or by an advertisement in newspapers.[106] Public companies must also make an announcement that invitations to the GMS will be sent shortly prior to issuing these invitations to shareholders.[107]

OJK sets out additional requirements concerning GMS invitation that public companies must meet:

- Announce the GMS invitation at least fourteen days before sending the invitation.[108]
- Issue the invitation at least twenty-one days before the GMS.[109]
- Where a second GMS is necessary (due to failure to meet quorum at the first meeting), companies must issue an invitation to the second GMS at least seven days before the second GMS, with a notification that the first GMS did not meet quorum.[110]
- The invitation to the second GMS must include the date, time, location, and meeting agenda. It must inform shareholders that materials to be discussed in the GMS are available at the company's office, unless additional regulations provide otherwise.
- Companies must hold the second GMS between ten and twenty-one days after the first GMS (not including the dates of either GMS).[111]

Information in the GMS Invitation

A GMS invitation should contain sufficient information to enable shareholders to participate.[112] The list of information that should be included in the GMS invitation is summarized in ***Table 7***.

[106] ICL, Article 82.
[107] ICL, Article 84(1).
[108] OJK Regulation No. 32/POJK.04/2014 as amended by OJK regulation No. 10/POJK.04/2017, Article 10(1).
[109] OJK Regulation No. 32/POJK.04/2014 as amended by OJK regulation No. 10/POJK.04/2017, Article 13(1).
[110] OJK Regulation No. 32/POJK.04/2014 as amended by OJK regulation No. 10/POJK.04/2017, Article 17.
[111] OJK Regulation No. 32/POJK.04/2014 as amended by OJK regulation No. 10/POJK.04/2017, Article 17.
[112] ICL, Article 82(3).

Table **7** Information in GMS Invitation

Information	Mandatory	Recommended
1. Full name and company location	●	●
2. Date, location, and time of the GMS	●	●
3. Names and addresses of shareholders or authorized proxies	●	●
4. Agenda	●	●
5. Proxy forms	●	●
6. Details of the place and time at which shareholders can obtain the materials to be discussed during the GMS	●	●
7. Procedure for obtaining background information on the GMS	–	●
8. Commencement time of shareholders' registration	–	●
9. Registration place	–	●
10. Details on where and how to report violations of GMS procedural requirements	–	●

Information and Materials for the GMS

The ICL requires that the GMS invitation should include information that the materials to be discussed during the meeting will be available at the company's offices between the date from which the invitation is issued until the date of the GMS. Companies must also provide shareholders with copies of the materials to be discussed free of charge.[113]

Table 8 summarizes the recommended GMS materials that should be made available to shareholders.

[113] ICL, Article 82(3)(4).

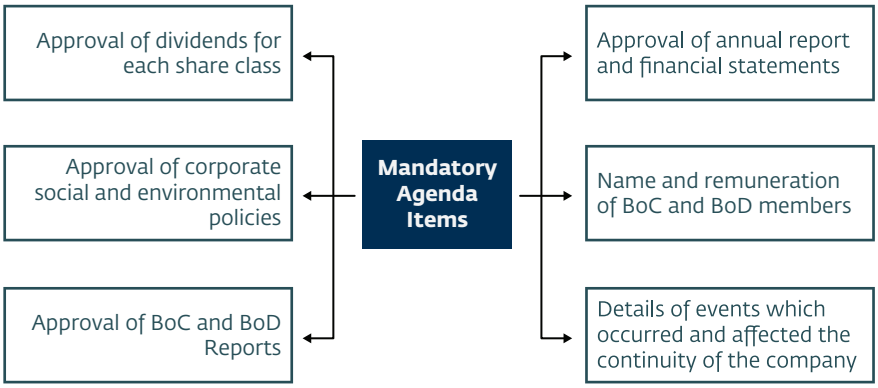
Table **8**	GMS Materials
1.	Annual report and annual financial statements
2.	External auditor report
3.	BoC supervisory report
4.	BoD report on the company's activities
5.	Draft amendment of the AoA (if any)
6.	Draft of GMS resolutions
7.	Information on candidates nominated as members of the BoC and BoD (if any)

It is good practice to specify the deadline for ensuring all GMS materials are available to shareholders in the company's AoA. The ICL requires these materials to be available at the company's domicile at least fourteen days prior to the GMS. Ideally, these materials should also be made available online and posted to the company's website to ensure public access. The materials may also be made available at other places, preferably in an area where a significant number of shareholders reside, as long as the address is specified in the GMS notification. Each shareholder has the right to receive copies of GMS materials. The AoA or internal regulations should specify when copies of the materials must be provided to the shareholder upon request.

5.2.5 Approving the Agenda

The ICL does not impose specific guidelines on the rights of shareholders to approve or amend the GMS agenda, beyond the requirement to include a copy of the agenda in the GMS invitation to allow shareholders the opportunity to review it. There are mandatory items that all companies must include in the GMS agenda, as illustrated in ***Figure 12***, beyond which either the BoD or shareholders may propose additional items. The GMS may only address matters listed in the agenda, unless all shareholders attending the meeting agree to add additional items. Resolutions on such items require unanimous shareholder approval.

Figure **12** Mandatory GMS Agenda Items



A shareholder (or a group of shareholders) holding at least 10 percent of shares in the company may submit agenda items, unless the AoA allows shareholders with a smaller holding to do so. Members of the BoC and BoD may also submit agenda items. In addition, the BoD should prepare draft resolutions for each agenda item.

5.3 Conducting the General Meeting of Shareholders

Indonesian law does not provide detailed guidelines on the process for conducting a GMS. It is common practice for the company to set its own procedures in the AoA or other internal regulations, ideally using corporate governance best practices as a reference.

Companies should use the GMS as a forum through which to inform shareholders about company activities, achievements, and upcoming plans, as well as to involve shareholders in important decisions. For minority shareholders, the GMS is often the only opportunity to obtain detailed information about the company's operations and to meet the commissioners and directors.

Companies should steer away from holding an excessively lengthy GMS that is likely to exhaust participants, even though this may be difficult when the issues to be decided are complex, contentious, or numerous. The overriding principle is for companies to conduct the GMS in a manner that facilitates effective shareholder participation and decision-making.

Figure 13 provides an overview of the procedures for conducting the GMS.

Figure **13** Procedures to Conduct the GMS

5.3.1 Registering Shareholders

The company should register shareholders or their representatives before the GMS begins. The ICL does not provide any guidelines on how a company should conduct shareholder registration. Companies may determine their own procedures for registering shareholders, including delegating a responsible officer to perform these duties. Participants must be registered to be counted toward the quorum and to vote during the GMS.

It is a normal practice for a company to set the documentation requirement for shareholders to register and state these requirements in the GMS notification. Required documents may include an ID card, a passport, or a copy of business registration certificate, the GMS invitation letter and (where relevant) a proxy authorization letter. Proxy authorization letters do not need to be notarized, however they must be in writing, signed, and formatted according to the company's requirements. Any person authorized to attend a GMS must submit his/her written authorization prior to entering the meeting room. The company may require shareholders and their authorized representatives to be checked or subject to other security measures that it considers appropriate. It may also engage a security company to maintain order and to expel those who do not comply with the chairman's instructions or who intentionally disrupt order.

Registration of GMS participants officially starts at the time stated in the GMS notice and ends when the chairman of the meeting counts the number of attendees to calculate the quorum. Registration should take place at the location where the GMS is held.

Best Practice

Participant registration should be carried out on the same day as the GMS and completed before the GMS is scheduled to begin. Poorly organized registration may result in shareholders having to wait in line while the GMS starts. Accordingly, companies should make every effort to ensure that the registration process is quick and efficient, and that shareholders are not prevented from participating in the GMS due to administrative delays. This means that the registration desk needs to be adequately staffed and opened well in advance of the GMS' scheduled start time.

5.3.2 Verifying and Announcing Quorum

The ICL does not specifically regulate the procedures through which companies should verify the GMS quorum. It is best practice for the AoA, internal regulations, or other corporate documents to specify the body or the person who is responsible to verify and announce the quorum. The quorum should be announced once the shareholder registration process is complete and before the shareholders may vote.

The ICL requires the following minimum quorum and voting thresholds:

Table **9** Minimum Quorum and Voting Threshold

No.	Corporate Action	ICL	Quorum	Votes
1.	To convene a GMS	Article 86(1)	More than 1/2 of the total shares having voting rights	More than 1/2 of the total amount of votes cast
2.	To convene a second GMS	Article 86(3)	At least 1/3 of the total shares having voting rights	More than 1/2 of the total amount of votes cast
3.	To buy-back the company's shares	Article 38(2) with reference to Article 88(1)	At least 2/3 of the total shares having voting rights	At least 2/3 of the total amount of votes cast
4.	To increase the company's authorized capital	Article 42(1) with reference to Article 88(1)	At least 2/3 of the total shares having voting rights	At least 2/3 of the total amount of votes cast
5.	To increase the company's issued and paid-up capital	Article 42(2)	More than 1/2 of the total shares having voting rights	More than 1/2 of the total amount of votes cast
6.	To decrease the company's capital	Article 44(1) with reference to Article 88(1)	At least 2/3 of the total shares having voting rights	At least 2/3 of the total amount of votes cast
7.	To amend the company's AoA	Article 88(1)	At least 2/3 of the total shares having voting rights	At least 2/3 of the total amount of votes cast
8.	To convene a second	Article 88(3)	At least 3/5 of	At least 2/3 of the

	GMS to amend the company's AoA		the total shares having voting rights	total amount of votes cast
9.	To conduct a merger, consolidation, acquisition, and division; file petition for bankruptcy, extension of the company's duration, and dissolution	Article 89(1)	At least 3/4 of the total shares having voting rights	At least 3/4 of the total amount of votes cast
10.	To convene a second GMS to approve a merger, consolidation, acquisition, and division; file petition for bankruptcy, extension of the company's duration, and dissolution	Article 89(3)	At least 2/3 of the total shares having voting rights	At least 3/4 of the total amount of votes cast
11.	Action by the BoD to transfer or encumber assets of the company having value that exceeds 50 percent of the company's assets	Article 102(5), with reference to Article 89	At least 3/4 of the total shares having voting rights	At least 3/4 of the total amount of votes cast

When the number of attendees required is insufficient, the meeting shall be reconvened within a period between ten days after the first GMS and twenty-one days (at the latest) from the date the first GMS was scheduled to be held. The company must send notice of the second GMS no later than seven days before the GMS is held. The second GMS shall be conducted when the number of attending shareholders and authorized representatives account for at least one-third of the voting shares. If the second GMS fails to meet this one-third requirement, the notice of the third GMS must explain that the second GMS has been convened but that it failed to meet the quorum required to proceed. The company must then convene a third meeting, for which the head of a district court will determine the quorum requirement. The company will provide notice of this third meeting to shareholders, stating the quorum as set by the district court.

5.3.3 Opening the General Meeting of Shareholders

A GMS will be deemed valid if attended by shareholders representing at least half of the voting shares, unless the ICL or the company's AoA sets a higher

quorum. If the BoD convenes the GMS, the president director usually chairs the meeting. If the president director is absent or temporarily unavailable, the remaining BoD members shall select one member to fulfill this role. In case none of the BoD members can act as the GMS chair, the person who signed the decision to convene the meeting should guide the GMS to vote for a GMS chairman.

For listed companies, the BoC will appoint a commissioner to chair the GMS. If no commissioners are available, the BoD will appoint a director to act as the GMS chairman. If neither a BoC nor a BoD member is available, the shareholders attending the GMS will appoint a shareholder to chair the GMS.[114]

As a practical matter, companies may invite a notary or legal consultant to the GMS to take minutes and assist management in conducting the GMS.

5.3.4 Presenting the Agenda and the Rules of Order

The meeting agenda must include details and timing for each of the issues to be discussed. The agenda may be amended if all shareholders attend the meeting and provide their approval for the amendment.

5.3.5 Discussing Agenda Items

It is good practice to ensure that:

- All BoC and BoD members, including committee members, the head of internal audit, and the external auditor are present at the GMS. If they are not, the GMS chairman should explain their absence.
- Shareholders have the opportunity to question commissioners, directors, and the external auditor. Shareholders should receive clear answers to their questions.
- Questions from shareholders are answered immediately. If a question cannot be answered immediately, a written response should be given as soon as possible after the GMS.

[114] OJK Regulation No. 32/POJK.04/2014 as amended by OJK regulation No. 10/POJK.04/2017, Article 22.

- The GMS chairman only interrupts speakers to maintain order or comply with procedural requirements.

5.3.6 Voting

After one or several agenda items have been thoroughly discussed, the GMS chairman should invite shareholders to vote based on the principle of one share, one vote. Each shareholder with voting rights or his/her proxy may vote on each issue on the agenda. The ICL does not set any requirements on voting mechanisms or the specific format that voting ballots must follow. Companies therefore may determine these details at their discretion according to their needs. Nevertheless, the AoA of a company usually stipulates that when voting relates to a person, a closed voting can be made and with unsigned ballots.

It is recommended that companies should only consider a ballot as valid if a shareholder marks only one of the possible options for a particular item. A failure to do so makes it difficult to properly count votes. If a ballot is received in which multiple options have been selected for one item, the GMS should invalidate the ballot with respect to that particular item.

Table 10 provides a summary of the information recommended to be included on the voting ballot.

Table **10** Information on Voting Ballot

1.	The full name and location of the company
2.	The type of GMS (AGMS or EGMS)
3.	The date, place, and time of the GMS
4.	Issues to be voted on, in the order given in the agenda
5.	Voting options "for", "against", or "abstained" on each issue
6.	The name of each candidate, in the case of the appointment of BoC or BoD members

7.	An instruction that the ballot must be signed by the shareholder, unless the voting is being conducted anonymously
8.	The ballot must show the number of votes each shareholder may cast on each item based on information from the shareholder list
9.	An instruction on how to complete the ballot
10.	An instruction that an individual who completes the ballot on behalf of a shareholder who is a legal entity must indicate his/her name and position and the full name of the legal entity which he/she represents
11.	An instruction that a copy of the power of attorney must be attached to the ballot, and that the representative of the shareholder must sign the voting ballot (if the voting is by proxy)

5.3.7 Announcing Voting Results and Decisions

Although the ICL is silent on this matter, it is recommended that the GMS chairman announce the voting results before the meeting closes. For public companies, the overall number of votes which agree, do not agree, or abstain shall be announced immediately after an issue is voted on.

5.3.8 Closing the General Meeting of Shareholders

The GMS chairman closes the meeting when all agenda items have been discussed and voted upon, and when the voting results have been announced.

5.4 Preparing Minutes of General Meeting of Shareholders

The company must keep minutes of each GMS. The minutes must be signed by the GMS chairman and at least one shareholder appointed by GMS participants.[115] This requirement is intended to ensure the accuracy of the contents of GMS minutes, although the signatures are not required if the minutes are notarized.[116]

GMS minutes should be inserted in the minutes book. The company should provide a copy of the GMS minutes to shareholders upon request. GMS minutes can be written in Indonesian and in a foreign language (specifically if the company has a foreign shareholder). The following documents should be attached to the GMS minutes:

- List of registered attendees
- Approved agenda and decisions adopted by the GMS
- All materials attached with the GMS invitation

Table 11 presents a summary of information that should be included in the GMS minutes.

Table **11** Information for Inclusion in GMS Minutes

1.	Full name and location of the company
2.	GMS date and location
3.	Type of GMS (AGMS or EGMS
4.	Agenda
5.	Time when participant registration started and ended
6.	Time when the GMS was opened and closed
7.	Summary of speeches and discussions
8.	Voting methods

[115] ICL, Article 90(1).
[116] ICL, Article 90(2).

9.	Number of votes on each agenda item and the required quorum
10.	Number of votes cast on each agenda item
11.	Voting results (number of votes "for", "against", and "abstained" on each agenda item with a quorum)
12.	Number of votes on each agenda item that were not counted because they were invalid
13.	Time when the votes were calculated (and whether the decision was approved by the GMS) and time when the voting results were announced during the meeting
14.	Text of approved decisions
15.	Names of the GMS chairman and secretary
16.	Names of the verifying shareholders
17.	Date when the GMS minutes were prepared

5.5 Extraordinary General Meeting of Shareholders

The ICL provides that companies may hold an EGMS at any time, as necessary.[117] An EGMS allows the company's governing bodies to address important matters outside of the regular schedule, and also provides shareholders an opportunity to request a meeting. Any of the following parties may request an EGMS:

- The BoC
- The BoD
- A shareholder or shareholders owning at least one-tenth or more of the total shares with voting rights in the company, unless the AoA provides that shareholders with a smaller holding may request a meeting

Other than the timing of the meeting (with the AGMS to be held annually), there are no major differences between preparing an EGMS and an AGMS. The BoD initiates the preparations for an EGMS when requested by the BoC or by shareholders meeting the minimum ownership requirement. The BoD has the right to reject the request if the shareholders making the request do not own or represent the required percentage of votes (at least 10 percent of shares giving them the right to vote on issues put before the EGMS). If the EGMS is proposed by the BoC or shareholders, it is recommended that the proposal is made in writing and forwarded to the company without delay so that the BoD can prepare for the EGMS by sending out notice to the other shareholders within the required timeframe as regulated under the ICL or the company's AoA.

[117] ICL, Article 78(4).

5.6 Circular Resolution

The ICL allows shareholders to pass binding decisions outside of the GMS by passing a circular resolution.[118] Shareholders must unanimously approve and sign the resolution in order for it to be valid and binding.

The company must send the draft resolution and supporting documents by registered mail to the permanent address of each shareholder. The draft resolution normally contains the following basic information:

- Company's name and the address of the head office
- Purpose of the resolution
- Full name, permanent address, and nationality of each shareholder, accompanied with the class and number of shares owned and the number of votes based on his/her shareholding
- Discussion of issues which require approval

A circular resolution that meets these requirements will be valid and have the same legal effect as a resolution passed by the GMS.

[118] ICL, Article 91.

5.7 Decisions of the General Meeting of Shareholders

It is important to follow the prescribed procedures for preparing and conducting the GMS to ensure the validity and lawfulness of decisions reached by the governing body.

5.7.1 Decisions Requiring Simple Majority Vote

The ICL requires GMS resolutions to be passed either unanimously or to be approved by more than half of the number of votes cast (unless the AoA requires a higher proportion of affirmative votes) if shareholders are unable to reach a consensus.[119]

5.7.2 Decisions Requiring Supermajority Vote

All resolutions of the GMS require approval by more than half of the total votes of participating shareholders, except for vital resolutions which require at least 65 percent or 75 percent of the total votes. For examples of issues that require a supermajority vote, please refer to ***Table 9*** in Section 5.3.2.

5.7.3 Decisions Requiring Unanimous Vote

If decisions are adopted by means of a circular resolution of shareholders, then the resolution needs to be unanimously approved by all shareholders to be valid. In addition, the company's AoA may also list matters which must be approved unanimously by shareholders, which are usually referred to as reserved matters.

[119] ICL, Article 87.

5.7.4 Filing a Lawsuit against GMS Decisions

Under certain circumstances, shareholders have the right to contest a GMS resolution in court. This primarily occurs when shareholders can show that a resolution has caused losses to themselves or the company, is unfair, and was made without reasonable consideration of shareholder rights. Shareholders must file in the first instance at a district court with jurisdiction over the domicile of the company.[120]

[120] ICL, Article 61.

CHAPTER 6
Board of Commissioners

THE CHAIRMAN'S CHECKLIST

Authority of the Board of Commissioners:

- Does the BoC focus on protecting the interests of the company and its shareholders? Do all commissioners understand the role and priorities of the BoC? Does the BoC have sufficient authority according to the AoA and other internal company regulations to fulfill its oversight duties? Has this authority been properly communicated? Does the BoC utilize its authority in practice?

- What is the BoC's role with respect to the company's governance, organization of the GMS, protection of company assets, resolution of conflicts, and supervision of internal controls and risk management? How effective is the BoC in guiding and setting strategy? Does the BoC have the tools to properly oversee the operational and financial performance of the company? Is a succession plan in place, particularly for the president commissioner?

- Is the BoC's authority distinct from that of the BoD, both on paper and in practice?

Election of the Board of Commissioners:

- Who nominates candidates to the BoC? Is sufficient information provided to shareholders about the nominees? How does the BoC influence the nomination process?

- Does the BoC ensure that all shareholders understand how cumulative voting works?

Composition of the Board of Commissioners:

- Has the BoC designed, articulated, and implemented policies relating to its size, composition and mix-of-skills, breadth of experience, and other pertinent qualities?
- Is the BoC's composition, considering its competencies and skill mix, suited to its oversight and strategic duties?
- How effectively does the BoC work as a team? Is the BoC constituted of a majority of independent commissioners?
- How effective is the BoC's leadership, both at the board and committee level?
- Is the number of commissioners consistent with the needs of the company? Does the company have enough commissioners to establish BoC committees?

Structure and Committees of the Board of Commissioners:

- Does the BoC have audit, risk, nomination and remuneration, or other board committees in accordance with legal requirements and sound corporate governance practices? What are the costs and benefits of these or other committees? Are there sufficient independent commissioners to chair and sit on these committees?
- Do the BoC committees have sufficient resources, both human and financial, to properly fulfill their functions?
- How well informed are non-committee members about the committee's deliberations? Is the information prepared by the

committee for the BoC adequate for effective decision-making?

- Do BoC committee members have sufficient expertise on issues relevant to their committees? Do they have access to information from the external auditor, internal auditor, and management involved in the financial, economic, and other activities of the company?

Working Procedures of the Board of Commissioners:

- Has the BoC identified, prioritized, and scheduled key issues that should be reviewed on a regular basis? Has the BoC identified the information it requires to properly analyze these issues?

- Does the president commissioner take an active role in organizing the work of the BoC? Does the BoC meet regularly in accordance with its annual work plan?

- Does the president commissioner encourage a free and open exchange of views?

- Are procedures in place to ensure proper preparation and conduct of BoC meetings (e.g., advance notification on agenda issues, distribution of materials and documents, proper determination of the quorum, voting through absentee ballots, and preparation of the minutes)? How efficient are BoC meetings in practice? Is the information provided to commissioners thorough, succinct, and to the point, thus allowing for effective decision-making? Are key issues and risks highlighted? Do the materials contain annexes with further relevant details?

- How does the BoC ensure that it properly oversees the BoD? Does it receive periodic reports and updates from the BoD? Does the BoC have joint meetings with the BoD to receive updates on key issues affecting the company? How well does the BoC interact with the BoD, including the president director? Does the BoC provide wise counsel and clear direction to BoD members? Does it challenge the

BoD sufficiently? How does it balance oversight against micro-management

Duties and Liabilities of the Board of Commissioners:

- Do all BoC members understand their duties to act reasonably and in good faith in the best interests of the company and its shareholders? Do BoC members properly prepare themselves for BoC meetings? Does the BoC give proper consideration to the interests of other stakeholders?

- Do the company's contracts with commissioners adequately explain their duties and liabilities?

The ICL and the CG Code require limited liability companies in Indonesia to adopt a two-tier board system, comprising the BoC and BoD. Each of these bodies possess distinct responsibilities, as set under the ICL and other regulations. Companies may set out details and/or additional responsibilities in their AoA beyond these legal requirements. Nevertheless, both the BoC and BoD are responsible for maintaining the company's long-term sustainability. Accordingly, the BoC and BoD must share a mutual perspective of the company's vision, mission, and values.

An effective, professional, and independent BoC is essential for good corporate governance. In Indonesia, the BoC is the corporate organ that is responsible for overseeing and advising the BoD as well as ensuring that the company implements good corporate governance practices. The CG Code prohibits the BoC from participating in making any operational decisions.[121]

While the BoC cannot change the economic environment in which a company operates, its role in providing strategic oversight and control over management can have a positive influence on the company's performance. The BoC's activities may go entirely unnoticed when an economy is strong, share prices are rising, and everything appears to be going well. On the other hand, when things go badly, the importance of the BoC becomes clear.

[121] *Indonesia's Code of Good Corporate Governance*, 13.

Companies should observe the following principles when establishing a BoC:[122]

- The composition of the BoC should enable it to act independently and to make decisions efficiently.
- BoC members must be professionals who possess the integrity and capability to enable them to properly carry out their functions.
- The BoC's oversight and advisory functions include acts related to prevention of breaches of national law and internal company regulations concerning corporate governance, improving compliance with these requirements, and temporary suspension of BoD members when deemed necessary in the interests of the company.

Figure 14 illustrates how to build an effective and competent BoC.

Figure **14** Five Steps in Developing an Effective Board of Commissioners

Step 1 Establish the BoC's purpose, duties, authorities, and responsibilities.

Step 2 Decide on the BoC's structure (number of independent members, committees) and size (total number of commissioners).

Step 3 Identify compentencies and mix-of-skills required for Boc members, and develop corresponding profile for commissioners (e.g., industry experience, integrity, financial literacy).

Step 4 Develop a plan to hire commissioners, using human resource firms and/or institute of directors if needed.

Step 5 Develop an induction program for new commissioners. Identify key performance indicator, conduct regular performace evaluation, and provide on going training.

[122] *Indonesia's Code of Good Corporate Governance*, 13.

Case Study

The catastrophic collapse of Enron in the United States drew attention to corporate governance and management of the board of directors.[123] *On May 7, 2002, the United States Senate concluded the following with respect to the role of the Board in Enron's collapse and bankruptcy:*[124]

- ***Fiduciary failure:*** *Enron's Board failed to safeguard shareholders and contributed to the collapse of the seventh largest public company in the United States.*
- ***Lack of independence:*** *Financial ties between the company and certain board members compromised the independence of the Board.*
- ***Conflicts of interest:*** *Despite clear conflicts of interest, the Board approved an unprecedented arrangement allowing Enron's Chief Financial Officer to establish and operate private equity funds that transacted business with Enron and profited at Enron's expense.*
- ***Excessive compensation:*** *The Board approved excessive compensation for company executives, failed to monitor the cumulative cash drain caused by Enron's annual bonus and performance unit plans given in FY 2000, and failed to monitor or halt a company-financed, multi-million dollar personal credit line.*
- ***High-risk accounting:*** *The Board knowingly allowed Enron to engage in high-risk accounting practices.*
- ***Extensive undisclosed off-the-books activity:*** *The Board knowingly allowed the company to conduct billions of dollars in off-the-books activity to make its financial condition appear healthier than it was, and failed to ensure adequate public disclosure of material liabilities that contributed to the company's collapse.*

[123] The United States uses a unitary board structure in which the board of directors performs roughly the same function as the BoC in the Indonesian context.

[124] Report by the Permanent Subcommittee on Investigations of the Committee on Governmental Affairs United States Senate, *The Role of the Board of Directors in Enron's Collapse* (Washington, DC: United States Government Printing Office, 2002), https://www.gpo.gov/fdsys/pkg/CPRT-107SPRT80393/pdf/CPRT-107SPRT80393.pdf.

6.1 Authority

Every limited liability company in Indonesia must establish a BoC.[125] The ICL defines the scope of the BoC's authority.[126] The law stipulates that the BoC is responsible for supervising management policies, overseeing management of both the company and the company's business operations, and advising the BoD on its management duties. However, the BoC's primary role is to supervise rather than manage. The AoA may also assign additional powers to the BoC to meet the company's needs.

The AoA of a limited liability company will typically stipulate the general duties of the BoC, as follows:

- Supervise the company's management (the BoD).
- Perform any duty specifically provided for by the AoA, prevailing laws and regulations, or GMS resolutions.
- Perform its duties, authority, and responsibilities in accordance with the company's AoA and GMS resolutions.
- Act in the interests of the company and be accountable to the GMS.
- Supervise, review, and approve the implementation of the company's work plan and annual budget prepared and submitted by the BoD.
- Assess the BoD's periodic report and, at any time, provide a response on the performance of the company and report the implementation of its duties to shareholders in a timely manner.
- Follow the development of the company's activities. In the event of corporate distress, the BoC must report to the GMS as soon as possible and provide advice on steps that may be taken for recovery.
- Propose candidates for appointment as the external auditor to the GMS.

[125] ICL, Article 1(2).
[126] ICL, Article 108(1).

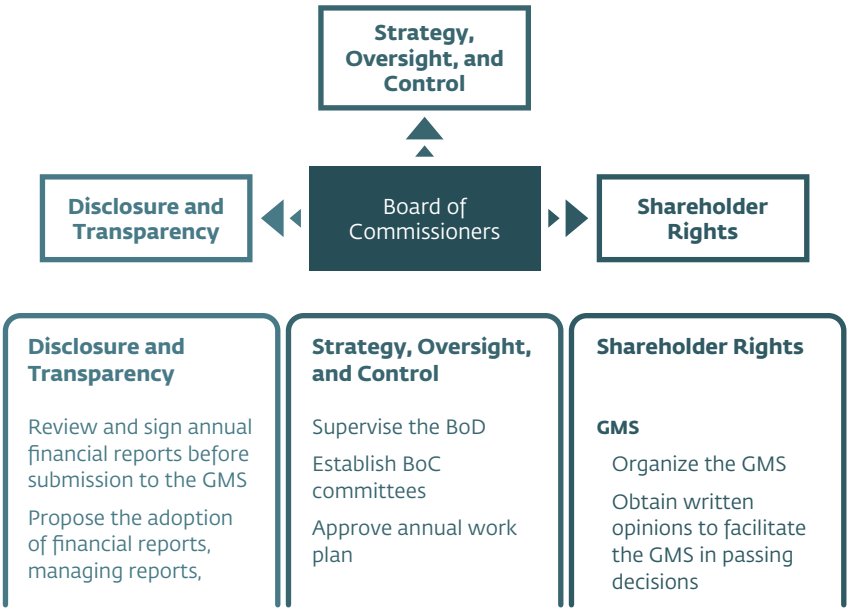
- Examine, review, and sign the annual report prepared by the BoD.

The ICL (Article 116-118) also requires the BoC to:

- Take minutes of BoC meetings and keep copies of these minutes.
- Report shareholdings held by BoC members or their families in the company or other companies.
- Report to the GMS on the performance of its supervisory duties during each financial year.
- Approve or assist the BoD in performing certain legal actions as conferred to the BoC by the AoA (the BoC may only act within the scope of authority provided under the AoA).
- Perform management activities in specific situations as provided in the ICL for a specified time, when the AoA or a GMS resolution confers authority to do so.

As a rule, the BoC has the authority to decide on all issues that do not fall under the authority of the GMS and/or other corporate bodies. To avoid ambiguity over the division of powers between the GMS, BoC, and BoD, any additional responsibilities the AoA grants to the BoC should correspond with the typical function of the BoC.

Figure **15** Authority of the Board of Commissioners



auditor reports (and corporate governance reports for listed companies) to the GMS	Approve investment plans/projects within its authority Formulate company policies (and corporate governance code for listed companies) Approve and review risk management and internal control framework	**Dividends** Recommend to the GMS the dividend to be paid, as well as the time-limit and procedures for payment of dividend **Conflict Resolution** Approve related party transactions valued at 50 percent or as referred to in the AoA Resolve corporate conflicts

Best Practice

Good corporate governance principles also suggest:

- *The president director and BoD members should seek the approval of the BoC for transactions that fall outside the scope of the company's regular financial and business plan (non-standard operations).*
- *The BoC should be given the right to veto decisions of the BoD to implement non-standard operations, provided that the BoC can provide adequate justification.*
- *The company's internal regulations should determine the rights and duties of its executive bodies.*

The BoD normally reports to the BoC. In many companies, the shareholders, particularly minority shareholders, will not be in a position to effectively supervise management. It is for this reason that the BoC assumes responsibility to oversee the BoD on behalf of all shareholders.

Companies must maintain an appropriate balance between providing oversight over the BoD and allowing the BoD sufficient autonomy to conduct corporate affairs. The dangers of weak board oversight, including fraud and mismanagement, are well

known. There are, on the other hand, dangers associated with excessive oversight. These include micro-management and the politicization of managerial decision-making. Both weak and excessive oversight can lead to economic inefficiencies and legal problems. Consequently, the company's AoA, internal regulations, and other corporate policy documents should be developed with a view towards dividing responsibilities among its governing bodies. Managerial tasks should, clearly, be left to professional managers. Oversight tasks should be carried out by oversight bodies, such as the the BoC.

Key issues every BoC should closely monitor include the following:

- The company's overall performance, especially in comparison to its competitors and industry peers
- The BoD's compliance with law and internal procedures, including on corporate governance, risk management and internal control, and ethics
- The BoD's performance, both at the team and individual levels
- Implementation of the company's strategy
- Relations with key stakeholders, including the company's shareholders, as well as employees, suppliers, and customers

The BoC typically also has the authority to approve internal documents related to the following:

- Dividend policy
- Information policy
- Ethical standards
- Control and supervision of the BoD and company management
- Risk management
- Audits of the financial and business activity of the company
- Policy on corporate secretary

Listed companies in Indonesia must make public disclosure of the company's corporate governance practices at the annual GMS. The BoC should prepare the corporate governance report and submit this to the annual GMS. The corporate governance report should detail all essential elements of the company's

corporate governance policies and practices. The BoC must disclose the extent to which the company complies with the CG Code and explain any discrepancy from these requirements. Finally, the BoC should also use the corporate governance report to make suggestions for improving the company's corporate governance practices.

Best Practice

Risk management is one of the BoC's most important functions. The BoC should ensure the company maintains systems which enable it to assess and mitigate risks. Among other things, the BoC should:

- *Approve risk management procedures and monitor the company's compliance with these procedures (the procedures should require the company and its employees to notify the BoC promptly of any substantial deficiency in risk management mechanisms)*
- *Set the company's risk appetite in the pursuit of its strategic objectives*
- *Review and evaluate the effectiveness of risk management and internal controls on a regular basis*
- *Develop adequate incentives for the executive bodies, departments, and employees to apply internal control systems*
- *Establish a risk management committee if necessary*
- *Ensure the company complies with laws and regulations as well as its AoA*

The AoA of a limited liability company sets out the scope of the BoC's authority, which typically includes the following:

- BoC members, whether collectively or individually, have the right to enter any building, office, or premise used by the Company during business hours and to examine accounts, letters, and other evidence to review the company's finances and other matters. The

BoC is also authorized to obtain information relevant to the BoD's activities.

- The BoC has the right to request explanation from the BoD on any matters relating to the company, and each member of the BoD is obliged to provide information as requested.
- If necessary, the BoC has the right to request professional assistance in order to perform its duties for a limited period, and to form an audit committee, at the company's expense.

6.2 Duties and Liabilities

The ICL provides that each BoC member must perform his or her duties to supervise and advise the BoD in good faith and with regard to the best interests of the company in accordance with its objectives and purposes.[127]

It is important to note, however, that although the ICL imposes a duty of good faith for commissioners, it does not define this term. Turning to other jurisdictions (the United States and the United Kingdom) for guidance, good faith serves as a fundamental principle behind the duties of care and loyalty that a company's board members owe to its shareholders.

6.2.1 Duty of Care

Under their duty of care, commissioners are responsible for exercising their rights and discharging their duties in good faith, with due diligence and care, and in a professional manner. A commissioner should:

- Act honestly, on a fully informed basis, and in good faith
- Use care and prudence to the maximum extent that may be expected of a good commissioner in a similar situation under similar circumstances
- Not cause the company to act unlawfully
- Regularly attend and actively participate in BoC meetings
- Place matters on the agenda of BoC meetings and demand such meetings when necessary
- Ensure that an effective and efficient system of internal control is in place
- Ensure that the president director and the BoD provide adequate information to the BoC, so that its members are properly informed on corporate matters
- Exercise a reasonable amount of supervision over the BoD

[127] ICL, Article 108(1).

6.2.2 Duty of Loyalty

The duty of loyalty plays a central role in corporate governance. Loyalty underpins the effective implementation of key corporate governance principles, for example the need to monitor related party transactions and to establish appropriate remuneration policies for BoC and BoD members.

Duty of loyalty requires commissioners to exercise their powers in the interests of the company as a whole. Simply put, commissioners should not allow personal interests to prevail over those of the company. The duty of loyalty usually prohibits commissioners from:

- Participating in a competing company
- Entering into any transaction with the company without first disclosing the transaction and obtaining approval from the GMS and the BoC
- Using corporate property and facilities for personal needs
- Disclosing non-public, confidential information
- Using company information or business opportunities for private advantage, i.e., personal profit or gain

The duty of loyalty requires commissioners to act in the best interest of the company regardless of:

- Who nominated and elected the member
- Pressure from other commissioners, shareholders, or other individuals to take actions or make decisions that are not in the best interest of the company

The BoC should not act as an assembly of individuals who represent various constituencies. Rather, as a company organ, the BoC must operate as a cohesive unit.[128] While specific commissioners may be nominated or elected by certain shareholders (and sometimes contested by others), it is an important feature of the BoC's work that commissioners carry out their duties in an even-handed manner with respect to all shareholders. It is particularly important to establish this principle in a company whose ownership structure includes controlling shareholders that are able to select the majority of or in some cases all commissioners.

Further, commissioners and affiliated persons (for example, family, friends, and

[128] *G20/OECD Principles of Corporate Governance*, 52.

business partners) should not accept gifts from persons with a vested interest in decisions of the BoC, or accept any other direct or indirect benefits. An exception can be made for symbolic gifts that are given as a common courtesy or souvenirs that are given during official events. These exceptions should be described in internal regulations or other internal documents of the company.

6.2.3 Conflicts of Interest

A commissioner should not be discharged from his/her duties if there is a conflict of interest between him/her and the company and its shareholders in a single instance or transaction. However, if a commissioner has a general conflict of interest with the company and its shareholders, he/she ought to be discharged from his/her position as commissioner.

Examples of how a conflict of interest may arise include when a commissioner or his/her related person:

- Enters into a contractual relationship with a company
- Holds commercial/financial interests in a way that can be reasonably expected to influence the commissioner's behavior contrary to the interests of the company

Commissioners should refrain from actions that may potentially result in a conflict between their own interests and the interests of the company. They are also advised to refrain from voting in situations in which they have a personal interest in the matter in question. Commissioners should immediately inform and disclose to the BoC about any potential conflicts of interest. Such information must be disclosed at the first BoC meeting after the commissioner is aware of the conflict. For example, BoC members of banks are obliged to disclose their (i) ownership of shares which amount to 5 percent or more in any company, in or out of Indonesia; and (ii) financial and family relations with other BoC and/or BoD members and/or controlling shareholders of the bank.[129]

[129] OJK Regulation No. 55/POJK.03/2016 on Implementation of Corporate Governance in Commercial Banks, Article 39.

6.2.4 Confidential Information

Commissioners should not disclose confidential information or use their access to corporate information for their personal interests or the interests of third parties. The personal use of confidential information ultimately damages shareholders. It is recommended that:

- Commissioners should take steps to protect confidential information.
- Commissioners should not disclose information or use it for their own interests.
- Companies should set standards with respect to treatment of confidential information and set these out in internal regulations.
- Contracts between the company and commissioners stipulate the obligation of commissioners to not disclose confidential information for a period of ten years after they leave the company.

To create an effective mechanism to prevent the unauthorized use of confidential information, the company should require commissioners to:

- Notify the BoC in writing of their intention to enter into transactions that involve securities of the company or its subsidiaries.
- Disclose information about previous transactions involving securities of the company in accordance with the procedures for disclosing material facts as specified by securities legislation.
- Upon their appointment, sign an agreement to comply with all legal requirements regarding the treatment of confidential information and non-disclosure of confidential information.

6.2.5 Access to Information

Every commissioner has a right to request the president director and BoD members to provide information regarding the company's business performance, budgets, forecasts, monthly internal financial statements (including explanation

of any material variance between the projections and actual results), and any other documents that may be relevant in order for the BoC to properly discharge its duties, including full and accurate responses to his/her inquiries from the BoD and other company officers.

The company should create a mechanism to ensure commissioners receive all information relevant to the company's financial and business activities, as well as other developments that may impact shareholder interests. The company's internal regulations or other internal documents should stipulate that the president director, BoD members, and heads of major divisions have the duty to promptly submit full and reliable information to the BoC.

6.2.6 Liabilities

Each commissioner will share personal liability for the company's losses if the commissioner concerned is at fault or negligent in performing the tasks to supervise and advise the BoD in good faith and with regard to the best interests of the company in accordance with its objectives and purposes. Where the BoC consists of two or more members, they will be jointly and severally liable for such losses.[130]

BoC members may not be held liable for the losses if they can prove that:[131]

- They have performed their duties in good faith and with prudence and in accordance with the company's interests, objectives, and purposes.
- They do not have any direct or indirect personal interest in the actions of the BoD which caused such losses.
- They have given the BoD advice to prevent the occurrence or continuity of such losses.

Commissioners are not relieved from liability for actions and decisions made during their tenure after they have resigned from or are dismissed by the BoC. On behalf of the company, shareholders representing at least one-tenth of the total number of shares with voting rights may sue members of the BoC who cause losses to the company as a result of their fault or negligence in the district court.[132]

[130] ICL, Article 114(3)(4).
[131] ICL, Article 114(5).
[132] ICL, Article 114(6).

To effectively enforce provisions that regulate the liability of commissioners, it is recommended that the company keep detailed minutes (and possibly verbatim reports) of BoC meetings to determine who voted for a certain decision and who can be held liable (to the extent the court considers such factors). In addition, the company should:

- Encourage commissioners to perform their duties in a proper way
- Take measures to terminate the authority of commissioners who are responsible for inflicting losses
- Hold commissioners responsible when they do not fulfill their obligations to the company

Managing the affairs of a company is a complex process. There is a risk that even when acting reasonably and in good faith, the BoC may make decisions that prove to be adverse to the company's interests. Companies should allow their commissioners to protect themselves from, or at least limit the liability for, losses incurred while they fulfill their duties. Such mechanisms may include:

- Liability insurance
- Provisions in the AoA and/or internal regulations that indemnify commissioners against claims, litigation expenses, and liabilities in certain circumstances

Companies may wish to obtain liability insurance for commissioners to cover the risk that their actions might result in losses to the company or third parties. Liability insurance for commissioners allows companies to use civil law remedies more productively, and the protections that such insurance offer may help companies to attract competent commissioners. In addition, companies may reimburse a commissioner for expenses incurred in defending a claim related to his/her role as a BoC member, if he or she acted:

- Honestly
- In good faith
- In the best interest of the company
- In compliance with law and regulations, the AoA, and internal regulations

6.3 Independence

International best practice classifies different categories of commissioners according to their degree of involvement in a company's corporate affairs. In Indonesia, the ICL provides that commissioners fall within two main categories: independent commissioners (*komisaris independen*) and delegated or representative commissioners (*komisaris utusan*).[133] Independent commissioners must have no affiliation to the company. Delegated commissioners, on the other hand, may include shareholders and/or individuals who are affiliated with members of the BoC or BoD. An independent commissioner shall be appointed by a GMS resolution from among the parties not affiliated with the ultimate shareholders and other BoC and/or BoD members. The BoC nominates delegated commissioners by way of a BoC resolution.[134]

Many Indonesian public companies are controlled by a single majority shareholder, or a group of shareholders, that is well informed of the company's affairs. The remaining ownership is often widely dispersed. Many of these minority shareholders lack the resources and information to effectively monitor management or defend themselves against potential abuse by the majority. In these types of companies, independent commissioners play an especially vital role. Independent commissioners should make up at least 30 percent of the BoC of a listed company in Indonesia.[135] Indonesia's CG Code provides that the number of independent commissioners should ensure that the control mechanism runs effectively and in accordance with laws and regulations.

Best Practice

Most international and national codes of corporate governance recommend that the supervisory board be primarily composed of members who are independent of the company, and who contribute:

- *An impartial perspective in their judgments*

[133] ICL, Article 120.
[134] ICL, Article 120.
[135] IDX Listing Rules, Attachment I, Article III.1.4.2; OJK Regulation No. 33/POJK.04/2014 on Directors and Board of Commissioners of Issuing Companies or Public Companies, Article 20.

- *Knowledge and experience outside of the company*
- *Useful contacts*

In most European Union countries, commissioners normally exercise oversight of the company's financial and strategic decision-making bodies. They play an important role in ensuring the unbiased monitoring of:

- *Nomination of directors to the BoD*
- *Directors' remuneration, including the president director*
- *Internal and external audits*

In the U.K., the Higgs report categorized the role of commissioners around four issues:

1. ***Strategy:*** *Commissioners should constructively challenge and contribute to the development of the company's strategy.*
2. ***Performance:*** *Commissioners should scrutinize the performance of management in meeting agreed upon goals and objectives and monitor the reporting of the company's performance.*
3. ***Risk:*** *Commissioners should satisfy themselves that financial information is accurate and that financial controls and risk management systems are robust and defensible.*
4. ***People:*** *Commissioners are responsible for determining appropriate levels of remuneration for directors, have a primary role in appointing, and where necessary removing, the president director, and in succession planning.*

International best practice suggests an independent commissioner ought to be an individual who has no direct connection to the company, and should not receive any substantial financial or other benefits. He or she should:

- Have never been an employee of the company, or a shareholder owning more than 10 percent of the company's shares
- Have not paid or received from the company a substantial amount,

or been a major shareholder of a company that has paid or received from the company a substantial amount (the threshold of such amount should be determined by the GMS and set out in the AoA of the company)

OJK places further restrictions on the eligibility of independent commissioners for publicly listed companies and issuers. An independent commissioner must:[136]

- Have not worked or held responsibilities for planning, directing, controlling, or supervising the activities of the company for six months prior to being engaged as an independent commissioner, unless that individual is being re-appointed to the position of independent commissioner for a new term
- Not hold any shares either directly or indirectly in the company
- Not have any affiliation with the company, BoC or BoD members, or majority shareholders
- Not have any business relationship, either directly or indirectly related to the business activities of the company

Independent commissioners can make a substantial contribution to important company decisions, especially in evaluating executive performance, setting appropriate remuneration for executives and commissioners, reviewing financial statements, and resolving corporate conflicts. Independent commissioners provide investors with additional assurance that the BoC's deliberations will be free of obvious bias. Companies are advised to disclose information about independent commissioners in their annual report.

According to the IFC's definition of independence, an independent commissioner is a commissioner who has no direct or indirect material relationship to the company other than his/her membership on the board, and who:

1. *Is not, and has not been in the past five years, employed by the company or its affiliates*

[136] OJK Regulation No. 33/POJK.04/2014, Article 21(2).

2. *Does not have, and has not had in the past five years, a business relationship with the company or its affiliates (either directly or as a partner or shareholder, and is not a director, officer or senior employee of a person that has or had such a relationship)*
3. *Is not affiliated with any non-profit organization that receives significant funding from the company or its affiliates*
4. *Does not receive and has not received in the past five years, any additional remuneration from the company or its affiliates other than his or her commissioner's fee and such fee does not constitute a significant portion of his or her annual income*
5. *Does not participate in any share option or pension scheme/plan of the company or any of its affiliates*
6. *Is not employed as an executive officer of another company where any of the company's executives serve on that company's board*
7. *Is not, nor has been at any time during the past five years, affiliated with or employed by a present or former auditor of the company or any of its affiliates*
8. *Does not hold a material interest*[137] *in the company or its affiliates (either directly or as a partner, shareholder, director, officer, or senior employee of a person that holds such an interest)*
9. *Is not a member of the immediate family (and is not the executor, administrator, or personal representative of any such person who is deceased or legally incompetent) of any individual who would not meet any of the tests set out in (1) to (8) (were he or she a commissioner/director of the company)*
10. *Is identified in the annual report of the company distributed to the shareholders of the company as an independent commissioner*

[137] For the purpose of this definition, "material interest" shall mean a direct or indirect ownership of voting shares representing at least 5 percent of the outstanding voting power or equity of the company or any of its affiliates.

11. Has not served on the board for more than ten years.

The considerable number of these definitions with their detailed qualifications may give rise to confusion. However, understanding and defining independence is not complex. The Council of Institutional Investors, a grouping of some of the world's largest institutional investors, defines independence as follows: "Stated most simply, an independent director[138] is a person whose directorship constitutes his or her only connection to the corporation."[139] For those interested in learning how to apply this simple definition in practice, the Council of Institutional Investors also lists specific circumstances that compromise independence.

[138] In this context, "director" is a reference to a member of the board of directors in a unitary system, which is the equivalent of a commissioner in Indonesia's two-tier board structure.
[139] Council of Institutional Investors, Policies on Corporate Governance, https://www.cii.org/corp_gov_policies#indep_director.

6.4 BoC Committees

The demands and responsibilities of the BoC and its members will continue to grow as a company's business operations become more complex. To overcome these challenges, the BoC may choose to establish committees and delegate the authority to make decisions to any board committee without abdicating its ultimate responsibility.

More specifically, a committee system:

- Assists the BoC to handle a greater number of complex issues more efficiently, by allowing specialists to focus on specific issues and provide detailed analysis and recommendations back to the board.
- Allows the BoC to develop subject-specific expertise on the company's operations, most notably on financial reporting, risk management, and internal control.
- Enhances the objectivity and independence of the BoC's judgement, insulating it from potential undue influence of managers and controlling shareholders.

The BoC establishes committees, sets their terms of reference through committee internal regulations, appoints their members, and turns their recommendations into action.[140] It is important that committees are understood to be sub-groups of the BoC instead of external committees. The committees will submit all proposals for planned action to the BoC for approval.[141]

In Indonesia, the ICL and the CG Code provide that a company may choose to establish several types of committees. An important additional consideration is that, although committees are useful for creating structures to address specific and complex issues, over-reliance on a committee system may cause the BoC to fragment. To strike an appropriate balance, it is advisable that the company form committees to address specific needs, which may require the committees to be either permanent or ad-hoc, or a combination of both. The CG Code suggests that larger companies should consider establishing at least an audit committee, nomination and remuneration committee, risk policy committee, and corporate governance committee. The CG Code permits companies to set up other

[140] *Indonesia's Code of Good Corporate Governance*, 15.
[141] ICL, Article 121.

committees according to their needs.

OJK mandates issuers and public companies to establish an audit committee as well as a nomination and remuneration committee. ***Table 12*** sets out the most common types of BoC committees with proposed function and composition, and specifying whether these bodies are mandatory or recommended.

Table **12** Board of Commissioners Committees

Audit Committee[142]

- Mandatory for issuers and public companies (OJK)
- Recommended for other companies (OJK CG Guidelines)

Function	Composition
The audit committee should assist the BoC to ensure that: • Financial reports are presented appropriately in accordance with generally accepted accounting principles • The internal control structure is adequate and effective • Internal and external audits are conducted in accordance with applicable audit standards • Management follows up on audit findings In addition, the audit committee will assist the BoC with the appointment, re-appointment, and removal of the external auditors, including approving the remuneration and terms of engagement of the external auditors , as well as assessing the quality of their work.	The audit committee should consist of at least three members, comprising an independent commissioner as well as parties from outside the company. One member should have knowledge and/or expertise in finance and accounting. The audit committee should be chaired by an independent commissioner.

[142] OJK Regulation No. 55/POJK.04/2015, Article 2.

Nomination and Remuneration Committee[143]

- Mandatory for issuers and public companies (OJK)
- Recommended for other companies (OJK CG Guidelines)

Function	Composition
The nomination and remuneration committee is responsible for the following: • Make recommendations to the BoC on the composition of the BoC and BoD, including required policies and criteria for board nomination and performance evaluation • Make recommendations to the BoC on training programs to develop the capacities of the BoC and BoD • Propose to the BoC any candidate who might qualify as a member of the BoC or BoD, to be submitted to the GMS • Make recommendations to the BoC on remuneration structure, remuneration policy, and amount of remuneration	OJK requires the nomination and remuneration committee to have at least three members, who must fulfill these requirements: • The chairman of the committee must be an independent commissioner • Other members of the committee may be: 1. Members of the BoC 2. Persons from outside the company who: • Have no affiliated relationship with that company, any members of its BoC or BoD, or with any principal shareholders • Have experience related to nomination and remuneration • Not hold any position in any other committees of the company 3. Persons who hold a managerial position in human resources under the authority of the BoD (should not be the majority members of the committee)

[143] OJK Regulation No. 34/POJK.04/2014, Article 2.

Risk Policy Committee

Recommended for all companies (OJK CG Guidelines)

Function	Composition
The risk policy committee should assist the BoC in: • Setting the risk governance structure, determining levels of risk tolerance, and monitoring key risk indicators and results regularly • Reviewing the adequacy and effectiveness of risk management and internal control systems	Members of the risk policy committee need experience in the industry in which the company is active. However, the committee will likely benefit from having members with other areas of expertise such as risk management, finance, and operations. The committee should consist primarily of BoC members but the company may appoint professionals from outside of the company if needed.

Corporate Governance Committee

Recommended for all companies (OJK CG Guidelines)

Function	Composition
The corporate governance committee typically has the following responsibilities: • Assist the BoC in developing the company's corporate governance policies • Monitoring and reviewing the effectiveness of the company's corporate governance practices, including those related to environmental and social aspects.	Members of the committee should meet high integrity standards, enjoy the trust of all shareholders, and be knowledgeable on legal and ethical standards. The committee should consist primarily of BoC members, but the company may appoint professionals from outside of the company if needed. The corporate governance committee may be combined with the nomination and remuneration committee.

The BoC is a collective body in which:

- All members have equal rights and responsibilities
- All members bear joint and several liabilities
- Members act together as a body according to specific decision-making procedures

Although BoC members act collectively, the committee system allows the BoC to delegate specific functions or issues to facilitate more efficient decision-making. A BoC committee may make decisions by passing a resolution on matters that fall within the scope of its responsibility. However, for a committee resolution to be valid and enforceable, the majority of committee members who are present and vote on that resolution must also be BoC members.

The BoC will determine the appropriate number of commissioners to serve on a committee. At least one committee member must be a member of the BoC and meet the criteria required of an independent commissioner. Where a committee has more than one member, the BoC must appoint a committee chairman. Other parties, most notably managers, who are not members of the committee, may be invited to participate and provide input; however, they will only have observer status and are precluded from conferring or deciding on particular issues.

Best Practice

BoC members should be experienced and knowledgeable. The BoC needs to have a sufficient number of members to accomplish the work at hand. However, the BoC should not be so large as to be unwieldy. Since the duties of BoC committees may involve time-consuming reviews, individual commissioners should be restricted from participating in multiple committees unless they have sufficient time and capacity to meet these demands.

Many stock exchanges further recommend that board committees—whether formed by the board of directors (in a unitary board system) or the BoC (in a two-tier board system such as Indonesia)—be primarily composed of and/or chaired by independent members. The listing requirements of some stock exchanges, for example the New York Stock Exchange, go further

by requiring the majority of board members to be independent and for the audit and human resources committees to be composed solely of independent members.

The committee chairman is responsible to ensure the committee's effectiveness, regardless of his/her other duties. The chairman plays a key role in organizing committee operations. Best practice recommends that the chairman should be an independent commissioner, particularly for the audit and nomination/remuneration committees. The chairman should keep the president commissioner informed about the committee's work. In addition, the chairman should be present at the GMS to respond to shareholders' questions.

A committee chairman should:

- Inform the BoC on all relevant issues at least on a quarterly basis
- Respond to all requests for information from the BoC without delay
- Take necessary measures to ensure the committee performs its tasks

6.5 President Commissioner

The ICL provides that a BoC should consist of at least one member.[144] In addition, a company's AoA usually states that if a BoC comprises more than one member, one of these members should be appointed president commissioner. Indonesia's CG Code states that all BoC members, including the president commissioner, share equal status (similar to the relationship between the president director and the BoD). The duty of the president commissioner as *primus inter pares* is to coordinate the activities of the BoC.

The president commissioner's capacity to properly discharge his/her duties depends on his/her personal and professional qualifications, and requires him/her to be vested with an appropriate level of authority. The president commissioner should hold an outstanding professional reputation and a high-level of integrity, be committed to the interests of the company, and enjoy the trust of shareholders and other commissioners.

Companies should define the authority of the president commissioner, as well as that of the president director, in as much detail as possible in their internal regulations. In addition, the company may wish to draft a description of the position and/or terms of reference. For example, the president commissioner:

- Establishes, implements, and reviews the procedures that govern the BoC's work
- Schedules board meetings and coordinates the BoC's calendar
- Organizes and presents meeting agendas and ensures that all commissioners receive appropriate information on a timely basis
- Periodically interacts with the president director and acts as a liaison between the BoC and executives
- Ensures accurate, timely, and clear information passes to and from the other commissioners
- Ensures effective communication with the BoD and shareholders
- Arranges regular evaluations of the BoC's performance, as well as evaluations of its committees and individual commissioners
- Facilitates the effective contribution of independent commissioners

[144] ICL, Article 108.

and encourages open discussion in a friendly and constructive atmosphere

- Facilitates efficient decision-making
- Carries out other duties as requested by the GMS and the BoC, depending on needs and circumstances

6.6 Size and Composition

A BoC must have at least one member.[145] Beyond this, a company's AoA may set out other requirements concerning maximum numbers of commissioners who may sit on the board. Where a BoC has more than one member, these members form a council that must act collectively by passing BoC resolutions and in which no member may act alone.[146]

The ICL states that companies whose business activities are related to the collection and/or management of public funds, companies that issue acknowledgements of indebtedness to the public, and public companies, must have at least two members on their BoC.[147] One of these must be an independent commissioner (who has no affiliation with a majority shareholder or with any member of the BoD or BoC). In case the BoC consists of two members or more, independent commissioners should make up at least 30 percent of its composition.[148] The BoC of banks in Indonesia must have at least three members.[149]

When determining the size of its BoC, beyond following legal requirements a company should be guided by its specific needs and the interests of its shareholders. The number of commissioners chosen should enable the board to:

- Hold productive and constructive discussions
- Make prompt and rational decisions
- Efficiently organize the work of any committees

Having either too few or too many commissioners can be problematic for effective decision-making. A small BoC may not allow the company to benefit from an appropriate mix of skills and breadth of experience. On the other hand, a larger BoC is typically more difficult to manage and building consensus can be time-consuming. The challenge in selecting the correct size for a BoC lies in striking an effective balance between these problems.

[145] ICL, Article 108(3).
[146] ICL, Article 108(4).
[147] ICL, Article 108(5).
[148] IDX Listing Rules, Attachment I, Article III.1.4.2; OJK Regulation No. 33/POJK.04/2014, Article 20(2)(3).
[149] OJK Regulation No. 55/POJK.03/2016, Article 23(1).

In Indonesia, the CG Code states that the composition of the BoC should be sufficient to respond to the relative complexity of the company's business, while also taking into account the need for efficient decision-making.

6.7 Qualifications

Under the ICL: Any individual capable of performing legal actions may be a commissioner, except for those who in the five years before their appointment have been:[150]

1. Declared bankrupt
2. Member of a BoC or BoD that was declared to be at fault in causing a company to become bankrupt
3. Convicted of a crime that caused financial loss to the state and/or which was related to the financial sector

Under the company's AoA: The company's AoA may also set out additional criteria and conditions which a commissioner must satisfy, provided that such requirements do not violate basic shareholder rights.

Other requirements: Commissioners of companies in which industry-specific regulations apply, such as banks, insurance, or securities companies, may be subject to stricter requirements. It would be prudent for such companies to investigate their industry's requirements carefully while selecting commissioners. For banks, any proposals to the GMS for the replacement and/or appointment of BoC members must take into account recommendations of the remuneration and nomination committee.[151]

Additional requirements apply to BoC candidates in issuers and public companies. These include requirements that such candidates:[152]

1. Be of good character and moral standing
2. Be legally competent
3. Have never been:
    - Declared bankrupt
    - Member of a BoC or BoD that was held responsible for causing a company to go bankrupt
    - Convicted of a crime that caused financial loss to the state and/or a crime related to the financial sector

[150] ICL, Article 110(1).
[151] OJK Regulation No. 55/POJK.03/2016, Article 27.
[152] OJK Regulation No. 33/POJK.04/2014, Article 4.

- Member of a BoC or BoD which during their service:
    1. Failed to hold an annual GMS
    2. Failed to provide an accountability report to the GMS, or provided a report that the GMS rejected, or
    3. Was responsible for a company's failure to meet its obligation to submit annual reports and/or financial reports to OJK within five previous years before appointment

4. Comply with laws and regulations
5. Possess knowledge and/or expertise needed in the field of business of the company

The GMS should be responsible for determining the conditions necessary for commissioners to be elected to the BoC, taking into consideration the nature of the company's activities and its purposes.

Every BoC member must fulfill all the conditions required by law, corporate governance regulations, and any applicable internal company documents from the beginning of his/her term on the BoC.

To avoid conflicts of interest, individuals should not be elected to the company's BoC when they are a commissioner, director, manager, or employee of a competing company.

Nominees for the BoC should also not be related to suppliers, affiliated persons, or employees of the independent external auditor.

The CG Code states that BoC members:[153]

- Must possess the capability and integrity necessary to ensure that the BoC properly carries out its oversight and advisory functions

[153] *Indonesia's Code of Good Corporate Governance*, 14

- Must not use the company to pursue his/her personal, family, business group, or other parties' interests
- BoC members must understand and comply with the AoA as well as laws and regulations that govern their duties and responsibilities
- Must understand and implement the CG Code

Figure **16** Recommended Characteristics and Competencies for Board Members

Indonesian law does not impose specific legal requirements on the personal qualifications that commissioners must hold. As a result, such criteria must be specified elsewhere. For example, companies may find it useful to include required qualifications for commissioners in their internal company documents, such as their AoA, internal regulations, or other company policies.

Notwithstanding the above, BoC candidates for companies subject to industry-specific regulations, such as banks, insurance companies, or securities companies, must meet additional requirements with respect to their qualifications. For instance, in addition to the requirements set out above, such companies must consider the rules regarding dominant positions stipulated under Indonesia's antitrust and competition laws and policies, in particular Law No. 5 of 1999 on the Prohibition of Monopoly Practice and Unfair Competition (Article 26). Companies are advised to examine their industry's particular requirements carefully when selecting commissioners.

Best Practice

The AoA should set forth the qualification criteria of BoC members. Commissioners should typically possess:

- *The trust of shareholders (reflected in their supporting votes for the commissioner), other BoC members, directors, managers, and other company employees*
- *Ability to relate to the interests of all stakeholders and make well-reasoned decisions*
- *Professional expertise and education needed to be effective*
- *International business experience, knowledge of national issues and trends, knowledge of the market, products, and competitors*
- *Ability to translate knowledge and experience into solutions*

It may, however, be difficult for the company to determine whether a potential commissioner possesses these qualifications. Moreover, a brief description of such qualifications in the company's AoA may lead to ambiguity and thus be of little use. To improve clarity, companies may wish to set out their criteria in greater detail under internal regulations or other internal documents.

Shareholders should be informed of the commissioners' qualifications, and the list of candidates for the BoC should indicate whether, at the time of election, the candidate is or will be:

- *An officer or employee of the company*
- *Able to meet the qualifications of an independent commissioner*

Companies should also screen potential BoC candidates for a criminal record or significant offenses to determine whether such candidates meet the requirements set out in the ICL, relevant regulations, and the company's AoA.

The BoC should be comprised of members who collectively

have the knowledge, capability, and professional experience necessary to promote the company's success. At least one member needs to have knowledge and experience in finance or accounting.

6.8 Election and Dismissal

The ICL stipulates that:[154]

1. The GMS will appoint BoC members.
2. For newly established companies, the company's founders will appoint commissioners to the BoC in the deed of establishment.
3. BoC members will be appointed for a limited period, and may be reappointed.
4. The AoA will determine procedures for the nomination, appointment, replacement, and dismissal of BoC members.

Supplementing these requirements, the CG Code recommends that BoC members should be appointed and terminated by the GMS through a transparent process. In addition, certain types of company, including publicly listed companies, state-owned enterprises, province and regional government-owned companies, companies that raise and manage public funds, companies whose products or services are widely used by the public, and companies with an extensive influence on the environment, must appoint a nomination and remuneration committee to evaluate and propose candidates for the BoC.[155]

The appointment of an independent commissioner should also consider the opinions of minority shareholders, which shall be obtained through the nomination and remuneration committee. In addition, publicly listed companies must publish the curriculum vitae of any persons nominated to serve on the BoC on its corporate website prior to the GMS.

Best Practice

Companies should ensure BoC independence by setting a limit on its members' length of service. Commissioners are no longer perceived as independent if they remain on the board for too long. A company may wish to impose term limits, either for the

[154] ICL, Article 111.
[155] *Indonesia's Code of Good Corporate Governance*, 16.

entire BoC or a certain percentage, to ensure its independence. Either way, reappointment should not be automatic, but rather a conscious decision made by the shareholders and the commissioner concerned.

For example, Singapore's Corporate Governance Code requires companies to 'rigorously' review the independence of directors who have served for longer than nine years from the date of their first appointment. If the board chooses to retain long-serving (nine years or more) directors, the Code requires companies to explain and defend why that director should be considered independent.

Shareholders should receive sufficient information to assess the capacity of BoC nominees to fulfill their duties and, if applicable, to ascertain their independence. Some useful items of information include:

- The candidate's identity
- The identity of the shareholder (or group of shareholders) that is nominating the candidate
- The candidate's age and educational background
- The candidate's relevant professional qualifications and experience
- Positions the candidate has held during the last five years
- Other positions the candidate holds (if any) at the time he/she is nominated
- For candidates nominated for reappointment to the BoC: the date of the candidate's most recent performance evaluation
- The nature of the candidate's relationship with the company
- Other BoC memberships or official positions held by the candidate
- Nominations of the candidate to other boards or official positions
- The candidate's relationship with persons affiliated to the company
- The candidate's relationship with the company's major business partners
- Information related to the financial status of the candidate and other circumstances that may affect the candidate's ability to properly exercise his/her duties and independence
- Any refusal by the candidate to respond to a request for information

Information about BoC nominees should be made available to shareholders before the GMS (typically twenty days prior to the GMS). This information should be available at the company's head office and any other places specified under the notice of the GMS that is distributed to shareholders. Posting this information online, preferably on the company's website, is a simple and cost-effective method to ensure public access.

Procedures concerning dismissal of BoD members will apply equally to the dismissal of BoC members, as follows:[156]

1. BoC members may be dismissed at any time by a GMS resolution which gives reasons for dismissal.
2. A resolution to dismiss a BoC member will be adopted after the commissioner concerned has been given the opportunity to defend him/herself before the GMS.
3. In the event a resolution to dismiss a BoC member is adopted outside the GMS—in accordance with the provisions contemplated in Article 91[157]—the commissioner concerned must first be notified of his/her planned dismissal and be given the opportunity to defend him/herself.
4. If a commissioner does not object to his/her dismissal, it will not be necessary to provide the individual with the opportunity to defend him/herself.
5. The dismissal of a BoC member comes into effect from:
    - The closing of the GMS contemplated in number (1)
    - The date of the resolution contemplated in number (3)
    - Another date determined in the GMS resolution contemplated in number (1); or another date determined by the GMS resolution contemplated in number (3)

Both international standards and the ICL allow companies to set additional grounds for dismissing BoC members in their AoA. Such grounds may include providing false information to the company during the candidate nomination process, willful neglect of BoC responsibilities, or being convicted of a crime.

[156] ICL, Article 105.

[157] The ICL (Article 91) stipulates that shareholders may also adopt binding resolution without convening the GMS, provided shareholders which are voting in the affirmative give their approval in writing by signing the relevant proposal.

6.9 Meeting and Working Procedures

The BoC should operate according to procedures defined by the ICL, the AoA, or internal company regulations. The BoC must follow legal requirements in order to pass valid decisions, or risk having those overruled in court.

A quorum is the minimum number of commissioners that must participate in a meeting for its decisions to be valid. Since the ICL does not specify the quorum for BoC meetings, a company's AoA may require a quorum to consist of more than one-half of total BoC members.

Neither the ICL nor the CG Code provide specific guidance concerning the first meeting of the BoC. As such, companies in Indonesia should address the procedures for these meetings in their AoA or other internal guidelines. A newly elected BoC should hold its first meeting no later than one month after the election. As a matter of convenience, the first BoC meeting can be scheduled to follow the GMS. In addition, it is recommended that the first BoC meeting:

- Define and confirm the priorities of the BoC
- Establish committees as appropriate

Best Practice

A company may also wish to develop an orientation program for new BoC members that covers, among other topics, an overview of the company's:

- *Industry and sector of operation*
- *Business operations*
- *Current financial situation*
- *Strategy*
- *Business risks*
- *The background and skills of key employees*

The AoA or other internal guidelines can specify the procedures for convening and conducting BoC meetings. For publicly listed companies, BoC meetings should be held at least once every two months,[158] and banks are required to hold BoC meetings no less than four times per year.[159] It is also obligatory for all BoC members to physically attend the meeting at least twice a year.[160]

The president commissioner normally convenes regular BoC meetings. However, a company's AoA may state that a BoC meeting may also be convened by any members of the BoC, upon a written request of the BoD, or upon a written request by one or more shareholders that jointly make up at least one-tenth of the total number of shares with valid voting rights issued by the company.

Relevant information and materials should be sent to commissioners together with the notice of BoC meeting, and sufficiently in advance to enable commissioners to review the material thoroughly. The company's AoA or an internal company manual will usually state the regulations concerning notice of BoC meetings. For example, a public company's AoA may provide that:

- Notice for a BoC meeting shall be made by a member of the BoC who is authorized to represent the BoC.
- Notice for a BoC meeting must be made in writing and delivered directly to each BoC member with his/her acknowledgement of receipt through registered mail/courier services, telex, facsimile, or e-mail no later than three days prior to the meeting, not including the date of the notice and the date of the meeting, or within a shorter time period for an urgent matter.
- The notice for a BoC meeting must contain the agenda, date, time, and venue of the meeting. The BoC meeting shall be held within the domicile of the company or the place where the company conducts its activities.

Internal regulations or other internal documents should determine the form of the notice and method of delivering the materials that is most convenient and acceptable to all commissioners (for example by mail, fax, or e-mail). The delivery method must be sufficiently secure to ensure the notice reaches the commissioner at his/her registered address.

Commissioners can participate and vote in meetings in a number of ways, however specific restrictions apply to banks. For companies other than banks,

[158] OJK Regulation No. 33/POJK.04/2014, Article 31.
[159] OJK Regulation No. 55/POJK.03/2016, Article 37(1); OJK Circular Letter No. 13/SEOJK.03/2017 on Implementation of Corporate Governance of Commercial Banks.
[160] OJK Regulation No. 55/POJK.03/2016, Article 37(2).

BoC members may participate if they are either:

- Physically present at the meeting, or
- Represented by a power of attorney

For banks, the BoC may make provision for its members to participate in meetings through teleconference technology by passing a resolution to that effect. The resolution must be passed at a meeting and signed by all BoC members.[161]

Best Practice

In addition to a meeting schedule, the BoC should have a working plan that includes the topics to be addressed. A standard AoA of a limited liability company may include provisions on BoC meetings. Ideally, the BoC should meet at least four times a year, although it may wish to hold meetings as often as it deems necessary.

Guidance on conducting productive and efficient BoC meetings:

- ***Develop an annual calendar of meetings**. This will allow commissioners to schedule the meetings in their agendas. Note that this calendar should serve as a guide, i.e., the BoC should hold additional meetings when warranted and, vice versa, cancel meetings when there are no issues to be resolved.*
- ***Set an agenda for each meeting well in advance**. This will allow commissioners to properly prepare for and focus on the task at hand. The president commissioner may wish to send a draft agenda in advance, allowing for comments and suggestions.*
- ***Reserve important agenda items for the beginning of the meeting**. Commissioners often have other commitments and may not be able to attend the*

[161] OJK Regulation No. 55/POJK.03/2016, Article 37(2); Circular Letter of OJK No. 13/SEOJK.03/2017, Article 8(a)(c).

entire length of the meeting. It will be useful to address the most pressing agenda items early.

In addition to regular meetings, the BoC needs to organize a meeting to review and approve the annual report. This board meeting needs to take place two months prior to the AGM.

When participating in BoC meetings, each commissioner should:

- *Actively listen and ask questions. This is particularly important for presentations or reports given by management, especially when these materials are presented in a complex or ambiguous manner.*
- *Request supporting materials. When presented with an issue that does not correspond to the commissioner's area of expertise, additional information in the form of studies, independent appraisals or opinions, and other documentation on the subject should be requested prior to the meeting.*

Although Indonesian law does not impose specific requirements on whether commissioners must attend all meetings, certain agenda items at BoC meetings will be so important that the company should consider making it compulsory for commissioners to be physically present in order to pass resolutions concerning these specific items, rather than allowing voting by way of teleconference or for resolutions to be passed in writing.

Particularly important matters include:

- Approval of the company's strategic plan, including financial and business plans
- Calling the AGM and making decisions on related items
- Preliminary approval of the company's annual report
- Convening or refusing a request by third parties to convene an EGMS
- Election of the president commissioner
- Creation and early termination of the authority of executive bodies
- Suspension of the president director and appointment of an interim president director

- Recommendation on the reorganization or liquidation of the company

The company's AoA will typically determine the procedure to pass a valid BoC resolution. The company may provide that if the BoC is unable to reach consensus, a resolution may be adopted when more than one-half of the total votes cast during that meeting are affirmative. In case of a tie, the president commissioner (or other meeting chairperson) will pass the deciding vote. For banks, if any members of the BoC pass a dissenting opinion, these differences and their reasons must be included in the minutes of the meeting.[162]

Good corporate governance suggests the AoA or internal regulations should allow absentee ballots to count towards the quorum, and therefore contribute to voting (other than for important agenda items requiring physical votes). If the AoA requires BoC members to be present to pass some but not all types of company resolutions, absentee votes may be counted for those resolutions. Companies should develop procedures for absentee voting, including deadlines for the delivery of voting ballots and the return of completed ballots. The procedures should give commissioners enough time to receive the ballots and make decisions on agenda items.

The ICL requires the BoC to keep copies of minutes from all meetings, which provide details of all proceedings and resolutions, and store copies of the details in company records.[163] However, the AoA may allow the BoC to pass resolutions without physically convening a meeting. A standard AoA for a limited liability company may provide that:

- Any matters that are discussed and decided in a BoC meeting should be recorded in the minutes. The president commissioner should assign a BoC member—who will be present at the meeting—to take minutes. These should be signed by the president and countersigned by another member of the BoC.
- The BoC may pass a resolution without convening a BoC meeting, provided that all members are notified in writing of the proposed resolution, grant their approval, and sign the resolution. A resolution made in such manner will have the same legal effect as a valid resolution made at a BoC meeting.

Ideally, the president commissioner or meeting chairperson (if other than the president) should designate a BoC secretary to take notes and help prepare the minutes. Typically, the corporate secretary also serves as the BoC secretary.

[162] OJK Regulation No. 55/POJK.03/2016, Article 38(5).
[163] ICL, Article 116.

These minutes must be signed by the president/meeting chair and countersigned by another BoC member who is present at the meeting, unless made before a notary in which case the minutes do not have to be signed. BoC minutes serve as valid evidence with respect to any resolutions made at the meeting.

As the legal and regulatory demands on commissioners become more onerous, minutes are important records to show that the BoC has discharged its duty of care. It is highly recommended for companies to include a record of the votes that individual commissioners pass in the minutes of each meeting.

It is important to note that minutes typically provide only a summary of the meeting. Companies should supplement this with a transcript of meeting proceedings. This transcript will form an integral component of the meeting record that should be incorporated into and stored with the minutes.

The following documents should be preserved together with BoC meeting minutes and/or transcripts:

- The voting ballots
- Dissenting opinions
- Written opinions of commissioners who were not able to attend

Each commissioner should also be provided with a summary of the meeting's discussions, along with:

- Copies of the minutes and/or meeting transcripts
- Reports detailing the voting outcome of all resolutions

OJK Regulation No. 35/POJK.04/2014 provides that the corporate secretary is responsible for preparing, organizing, and documenting both BoC and BoD meetings. While the president commissioner will decide when to convene a BoC meeting, the corporate secretary should be responsible for handling such matters as:

- Notifying all BoC members of BoC meetings
- Sending voting ballots
- Collecting completed ballots and absentee ballots
- Ensuring compliance with procedures for BoC meetings
- Keeping minutes and meeting transcripts

6.10 Remuneration

The remuneration of commissioners is one of the more contentious issues in the field of corporate governance, and companies are advised to choose a cautious and circumspect approach to the question. Excessive remuneration is perceived to be an unjustified privilege of power. Therefore, it is of the utmost importance that commissioner compensation be competitive, yet stay within reasonable limits.

BoC members in Indonesia typically receive an honorarium/fee for service (*uang jasa*) or monthly salary, which is set by the GMS. The company's annual financial statements should disclose the details of its remuneration policy for the BoC as well as for individual commissioners. Ideally, details such as the annual salary and other benefits for each commissioner should be published in the annual financial statements. It should also be included as an explicit item on the AGM agenda, to give shareholders the opportunity to debate these matters.

The BoC should regularly review the remuneration of its commissioners. Pursuant to Article 66 of the ICL, the BoC should review the company's annual report submitted by the BoD, part of which deals with remuneration provided to the BoC.

Banks must meet additional corporate governance standards with respect to reviewing their remuneration levels. These relate to, at a minimum:

- The duties and responsibilities of the BoC and BoD
- The duties and responsibilities of the remuneration committee
- Implementation of the caution principle in remuneration payments
- Disclosure of remuneration

OJK has the authority to monitor the remuneration policies of banks, and under certain conditions OJK is authorized to review variable remuneration amounts.[164]

[164] OJK Regulation No. 45/POJK.03/2015 on Corporate Governance of Remuneration of Commercial Banks, Article 31.

Best Practice

Ideally, all members of the BoC should receive the same base remuneration. Additional compensation should be commensurate with their committee responsibilities (if any). Moreover, the fees that a company pays should be sufficiently competitive to attract competent individuals. Fees should be neither significantly below nor significantly higher than the remuneration paid to commissioners by peer companies. Setting a reasonable level of remuneration for commissioners is particularly important to prevent jeopardizing the special status of independent commissioners. Independent or not, a commissioner's judgment may be clouded if he/she receives a significant percentage of his/her total income in the form of a commissioner's fee. A commissioner who relies on board compensation for his/her livelihood will soon become beholden to the company and may not be relied upon to fulfill his/her responsibilities in an unbiased manner.

The company should disclose its remuneration plan and the remuneration of each commissioner, either on an individual basis or in the aggregate, in its annual report. The former is easiest to implement when all BoC members receive the same fees. In such cases the annual report may include a simple statement such as: "All commissioners receive fees of____ per year."

6.11 Performance Evaluation

To be effective, BoC members should have the necessary resources to develop and maintain their knowledge, skills, and expertise. Training programs based on periodic evaluations of the BoC and its members play a fundamental role in meeting this need.

It is important that the BoC conduct performance evaluations on a regular basis through self-evaluation, confidential peer evaluation, or evaluation by an external party. The collective results of the BoC performance evaluations should be disclosed in the company's annual reports. OJK requires public companies to develop a mechanism to evaluate the effectiveness of the BoC as a whole, the effectiveness of each of its committees' activities, and the performance of individual BoC members. Self-evaluation serves as a useful tool for the BoC to assess the quality of its work. Through critical reflection and self-evaluation, commissioners can be more responsive to shareholders, investors, and other stakeholders.

Self-evaluation methods may include:

- Organizing a retreat and inviting an outside facilitator.
- Organizing a special BoC meeting to evaluate the work of the BoC or, alternatively, setting aside time during a regular meeting to address performance issues.
- Designing checklists that BoC members can use to assess their work.
- Participating in specialized training programs, thereby providing commissioners the opportunity to critically reflect on their performance and develop and share ideas.

Evaluations can generate important insights into the strengths and weaknesses of the BoC and its members. This information is useful to assist the BoC to identify areas of weakness and where further training may be needed. Corporate governance training can be particularly valuable for companies that operate in transitional economies, where commissioners need to stay abreast of frequent changes to the legal and regulatory framework as well as best practice standards. All this makes a company's education and training policy a key factor for success in developing and supporting a competent, knowledgeable, and vigilant BoC.

Best Practice

A variety of organizations contribute to the professional development and training of commissioners. These include stock exchanges, financial institutions, government and industry regulators, business associations, chambers of commerce, higher education, and institutes of directors/commissioners.

Commissioner training is delivered primarily by two types of organization. The first category includes corporate governance associations, which work towards improving corporate governance and provide training to advance that effort. The other includes organizations that focus on the commissioners/directors themselves, which support, represent, and set standards. Both types of organization can be membership associations, such as the National Association of Corporate Directors in the United States, the Institute of Directors in the United Kingdom, and the Brazilian Institute of Corporate Governance. Alternatively, they may serve commissioners/directors without having a membership base, such as the Indonesian Institute for Corporate Directorship, the Corporate Governance Center in Kenya, and the Corporate Governance Forum of Turkey.

Training can provide commissioners with:

- *New skills*
- *Increased professionalism*
- *Greater awareness of relevant issues*
- *Access to current thinking on governance and other issues*
- *Opportunities to discuss issues with peers and mentors*

Appendix 1

Checklist to Determine the Effectiveness of the Board of commissioners

Questions	Yes	No
Has the BoC considered the company's long-term objectives and examined what strategic options will be available to achieve these objectives? If so, has the BoC reached a decision on its future objectives and strategies? Have these been put in writing?		
Has the BoC consciously considered its underlying corporate philosophy, including its value system, its ethical and social responsibilities, its desired 'image', and so forth? Has the company developed internal policies that set out these values? Does the company have formal procedures for recording and promulgating major BoC decisions such as policy guidelines for line managers?		
Does the BoC periodically review the organizational structure of the company and consider how this may have to change in the future? Does it review and approve the appointment of all senior executives? Are adequate human resource development programs in place?		
Does the BoC routinely receive all the information it needs to ensure that it is in effective control of the company and its management? Have there been any unpleasant surprises, for example, unfavorable results or unforeseen crises that could be attributed to a lack of timely or accurate information?		
Does the BoC routinely require the president director to present his/her annual plans and budgets for its review and approval? Does the BoC regularly monitor the performance of the president director and senior management in terms of actual results achieved against agreed plans and budgets?		
When the BoC is required to make major decisions on future objectives, strategies, policies, major investments, senior appointments, etc., does it have adequate time and knowledge to make these decisions soundly, rather than finding itself overtaken by events and, in effect, obliged to rubber-stamp decisions already taken or commitments already made?		

If the answers to these questions are yes, it is safe to say that the company's BoC can be considered effective. If the answers are largely negative, however, or perhaps not clear, the company needs to reevaluate the composition and role of its BoC and undertake activities to improve its performance.

CHAPTER 7
Board of Directors

THE CHAIRMAN'S CHECKLIST

- Has the company properly established a BoD? Does the company clearly define the boundaries of the shareholders, commissioners, and directors' respective authority? Does the AoA or other company regulations clearly distinguish the powers of the president director from those of other BoD members?
- Do the president director and all BoD members possess the knowledge and skills necessary to manage the company? Do they perform their functions on a full-time basis? Is there a transparent division of tasks among BoD members, such as between duties related to finance, legal, marketing, and operations?
- Who elects the BoD members? Is the president director sufficiently involved in the nomination process?
- Does the BoD meet regularly to discuss the company's affairs? Are these meetings well prepared, with an agenda and reference materials distributed in advance (in writing or electronically)?
- Does the BoD regularly and adequately inform the BoC about all operations of the company? Does the BoD provide all relevant information to the BoC, the BoC's committees, and the external auditor in a timely manner?

- Do all BoD members clearly understand their duties to act reasonably and in good faith in the best interests of the company? Does the BoC take measures to hold directors who fail to act in line with these duties liable under civil, administrative, and/or criminal law?

- Does the company conduct thorough performance reviews of the BoD based on periodic analysis of key performance indicators? Does the BoC rigorously evaluate directors at least annually? Does the BoC clearly link performance and remuneration when deciding on directors' remuneration?

The executive body of a limited liability company in Indonesia is called the BoD. It is one of the three primary organs of a company (together with the GMS and the BoC). A number of laws (including the ICL, OJK regulations, and the company's AoA) regulate matters relevant to the BoD, which plays a central role in the governance structure of all companies. Also relevant, but not binding, are the recommendations under Indonesia's CG Code. These laws, regulations, and recommendations cover matters such as the BoD structure and composition; its authority, roles, and responsibilities; meeting and working procedures; nomination, appointment, and dismissal of BoD members; and remuneration. This chapter addresses how these requirements apply to companies in Indonesia.

7.1 Authority

The ICL defines the BoD as a company organ with full authority to manage the company in the best interest of the company in accordance with the company's purposes and objectives as defined in the AoA.[165] The ICL also provides that the BoD is authorized to represent the company both in and out of court.[166]

All companies must have at least one member to serve in the BoD. Where a company's BoD consists of two or more members, a GMS resolution will determine the allocation of duties and authority among the directors. Alternatively, if the GMS does not or cannot pass such a resolution, the division of tasks will be determined by way of a resolution of the BoD.[167]

Although each BoD member may carry out his/her duties and make decisions within the parameters of his/her respective authority as assigned, the BoD remains collectively responsible for the execution of tasks by each of its members.[168] All BoD members, including the president director, hold equal positions. The president director's duty, as senior or representative member of the group (*primus inter pares*), is to coordinate the activities of the BoD.[169]

[165] ICL, Article 1(5).
[166] ICL, Article 98(1).
[167] ICL, Article 92(5)(6).
[168] ICL, Article 97(4).
[169] *Indonesia's Code of Good Corporate Governance*, 17.

7.2 Duties and Liabilities

Since the BoD is responsible for the company's overall management, it has the authority to implement management policies which it considers appropriate to advance the company's interests, insofar as such policies comply with requirements under the ICL and the AoA.[170]

The ICL specifies key duties and obligations of the BoD, which include:

- To undertake the management of the company in the interest of the company and in accordance with the company's purpose and objectives[171]
- To represent the company both in and out of court[172]
- To declare and distribute interim dividends upon obtaining BoC approval
- To hold an annual GMS
- To create a register and special register of shareholders, GMS minutes, and minutes of BoD meetings; to create annual reports and the company's financial documents as specified in Law No. 8 of 1997 on Company Documents; to record any transfer of shares; and to maintain all registers, minutes, and financial documents and other company documents[173]

The CG Code provides general guidelines on the five main elements that the BoD's duties should include: management, risk management, internal control, public relations, and social responsibility,[174] as summarized below.

1. **Management**
    - The BoD should develop the company's vision, mission, and values. It is responsible for the company's strategic direction, and formulates short and long-term plans to be approved by the BoC or GMS, in accordance with the AoA.
    - The BoD should manage the use of the company's resources efficiently and effectively.
    - The BoD should ensure that stakeholders' interests are properly considered.
    - The BoD may delegate specific authority to a committee that is established to support the execution of its duties, or to a

[170] ICL, Article 92(1)(2).
[171] ICL, Article 92(1).
[172] ICL, Article 98(1).
[173] ICL, Article 100.
[174] *Indonesia's Code of Good Corporate Governance*, 18-19.

company employee, but the ultimate responsibility remains with the BoD.

- The BoD should set out its working procedures, regulations, and guidelines in a charter to facilitate the objective and effective execution of its duties. The charter may also serve as a tool for the appraisal of the performance of the BoD and individual directors.

2. Risk Management

- The BoD should establish and implement sound risk management policies that cover all aspects of the company's activities.
- When making strategic decisions concerning the company's business objectives and direction, including the creation of new products or services, the BoD should take care to assess risk exposure and maintain an appropriate balance between benefit and risk.
- The company should retain a department or person to ensure proper implementation of risk management policies.

3. Internal Control

- The BoD should establish and maintain a sound internal control system to safeguard the company's assets and monitor the organization's performance and compliance with laws and regulations.
- Indonesian law requires certain types of companies to maintain an internal control function or unit. These include: publicly listed companies, state-owned enterprises, province and region-owned companies, companies that raise and manage public funds (including finance companies), companies that provide products or services that are widely used by the public, and companies that have an extensive impact on the environment.
- The internal control unit should assist the BoD to ensure the company attains its business objectives by: (i) evaluating the implementation of the company's internal control program; (ii) providing recommendations to improve the effectiveness of the risk management process; (iii) evaluating the company's compliance with internal company regulations, national laws and regulations, and implementation of good corporate governance; and (iv) coordinating with the

external auditor.

- The internal control unit or responsible officer is accountable to the president director or the director in charge of the internal control unit. The internal control unit has a functional relationship with the BoC through the audit committee.

4. Public Relations

- The BoD should support the company's public relations strategy by retaining a corporate secretary specifically dedicated to conduct public relations.
- The corporate secretary is responsible for: (i) sound communication from the company to the public and its stakeholders; and (ii) making relevant information easily accessible to stakeholders.
- The following types of company must retain a corporate secretary: publicly listed companies, state-owned enterprises, province and region-owned companies, companies that raise and manage public funds, companies that provide products or services that are widely used by the public, and companies that have an extensive influence on the environment. The corporate secretary's function in these companies may also include investor relations.
- If a company does not have a dedicated department to monitor its compliance with laws and regulations, the corporate secretary shall perform this role.
- The corporate secretary will be responsible to the BoD. The corporate secretary's duties and activities will also be reported to the BoC.

5. Social Responsibility

- The BoD should be responsible to fulfill the company's social responsibility.
- The BoD should develop a clear and focused plan for its corporate social responsibility strategies.

BoD members carry the same duties of care and loyalty as BoC members, and are subject to the same liability standards as the BoC unless either the AoA, internal regulations, other general internal documents, or employment contracts provide for stricter standards.

7.3 President Director

If a BoD has two or more members, one director will be appointed to serve as a president director. The president director has the authority to:

- Convene, organize, and preside over meetings of the BoD.
- Sign all documents, decisions, and minutes of the BoD.
- Perform any other duties as specified in the AoA, internal regulations, or a resolution of the BoC.

In addition, the president director should:

- Create a constructive atmosphere to facilitate discussion and the decision making process.
- Take steps to ensure that all members are sufficiently prepared to contribute to the work of the BoD.

An important additional requirement applicable to Indonesian banks is that the president director must be independent from the controlling shareholders.[175]

[175] OJK Regulation No.55/POJK.03/2016, Article 5.

7.4 Size and Composition

The ICL stipulates that a company's BoD must consist of at least one or more members.[176] Public companies, companies whose business relates to the collection of or management of public funds, and companies that issue acknowledgements of indebtedness to the public, must maintain a BoD with at least two members.[177] Indonesian banks must have at least three members to serve in the BoD.[178] Beyond this requirement, either the BoC will determine the company's policies for the size of the BoD by passing a special resolution, or, alternatively, in the AoA or through internal regulations.

OJK recommends all issuers and public companies to show that they have considered the complexity of their business activities and corporate objectives when determining the size of their BoD. The BoD should have a sufficient number of members to support the company's activities, but not be so large as to compromise effective decision making.[179]

Best Practice

The number of BoD members must be appropriate to the company's size and line of business. The most appropriate number of directors to serve on the BoD therefore largely depends on the company's activities, size (number of employees), level of development, etc. Positions that companies may find useful to include on the BoD include:

- *President Director*
- *Chief Operating Officer/Operation Director*
- *Chief Financial Officer/Finance Director*
- *Chief Risk Officer*
- *Head of Strategy*

[176] ICL, Article 92.
[177] ICL, Article 92(3)(4).
[178] OJK Regulation No.55/POJK.03/2016, Article 5(1).
[179] Circular Letter of OJK No. 32/SEOJK.04/2015, Article 5.1.

- *Marketing and Sales Director*
- *General Affairs Director*
- *Human Resources Director*

7.5 Qualifications

The ICL sets out the minimum requirements for eligibility to sit on a company's BoD. For entities other than public companies or commercial banks, individuals who are capable of performing legal actions are typically eligible to sit on the BoD, except those who within five years prior to their appointment have:[180]

- Been declared bankrupt
- Been member of a BoC or a BoD found to be responsible for a company's bankruptcy
- Been convicted of a crime or crimes which caused losses to the state and/or were related to the finance sector

In addition to the ICL threshold requirements listed above, such individuals must:[181]

1. Be of good character and moral standing
2. Be legally competent
3. Have never been a member of a BoD or BoC which, during the term of his/her service:
    - Failed to hold an annual GMS
    - Failed to implement appropriate mechanisms for accountability to the GMS, or where a proposed mechanism was rejected by the GMS
    - Was responsible for the company's failure to submit annual reports or financial reports to OJK within the past five years before his/her appointment to the new company
4. Comply with all laws and regulations, and possess the relevant knowledge and/or experience necessary within the company's field of business.

With regard to commercial banks, in addition to the ICL threshold requirements and regulations concerning public companies listed above, OJK also requires that:[182]

1. Each proposal to make changes to the BoD composition or

[180] ICL, Article 93(1).
[181] OJK Regulation No. 33/POJK.04/2014, Article 4(1).
[182] OJK Regulation No. 55/POJK.03/2016, Article 6.

appointment submitted by the BoC to the GMS takes into account the recommendation of the nomination and remuneration committee

2. The majority of BoD members of commercial banks have relevant operational experience (at least as a bank's executive officer for five years)
3. Each BoD member passes OJK's fit and proper test

Directors in commercial banks also have additional limitations imposed by OJK to the effect that these directors:[183]

- Are prohibited from holding a position as director, commissioner or executive officer in any other entity
- May not severally or jointly own shares consisting of 25 percent of paid-up capital in other companies
- May not be related by two or more degrees of separation to any other BoC or BoD member

In addition, IDX listing rules require public companies to nominate an independent director to the BoD. The rationale behind this requirement is to provide an impartial and objective reference point from which to monitor board decisions. An independent director provides important checks and balances over the BoD and ensure the BoD manages the company's assets in a way that serves its best interests. To meet the IDX's definition of an independent director, an individual must:[184]

- Have not been affiliated with the controller of the company[185] within at least six months prior to his/her appointment
- Have no affiliation to any of the company's commissioners or directors
- Not hold any position as a BoD member in another company
- Have not been connected to or employed by an institution that provides services in the capital markets industry and which the company has utilized within a six-month period prior to his/her appointment as an independent director

[183] OJK Regulation No. 55/POJK.03/2016, Article 7(1)(3) and Article 8.
[184] IDX Listing Rules, Attachment I, Article III.1.5.2.
[185] The controller of the company is a shareholder that owns more than 50 percent of the total issued and paid-up capital in the company, or a shareholder that has capacity to determine the management and/or policy of the company, either directly or indirectly.

7.6 Election and Dismissal

The ICL sets out the requirements regarding the appointment, replacement, and dismissal of BoD members, as follows:[186]

1. The GMS will appoint BoD members.
2. BoD members will be appointed for a certain period and may be re-appointed.
3. The AoA will determine specific procedures for the appointment, replacement, and dismissal of BoD members and may also set nomination procedures.
4. The GMS will determine when directors are to be appointed, replaced, or dismissed, and set out its policies with respect to these actions in a GMS resolution. If the resolution does not set a specific date or time-frame, the ICL provides that any necessary appointment, replacement, or dismissal will take effect at the time the GMS closes.
5. The BoD should notify the MOLHR of all changes in its membership, so that these may be recorded in the company registry, no later than thirty days from the date of the GMS resolution.

The CG Code reinforces these provisions and states that the appointment and termination of BoD members by the GMS must occur in a manner that is transparent. For publicly listed companies, state-owned enterprises, province and region-owned companies, companies that raise and manage public funds, companies whose products or services are widely used by the public, and companies with extensive influence on the environment, the process of evaluating candidates for the BoD will be carried out prior to the GMS by a nomination and remuneration committee.

Shareholders should have the opportunity to receive sufficient information (in writing or electronic format) on BoD candidates prior to the GMS. Up-to-date information should also be made available to all shareholders during the GMS. The information should include:

- The identity of the candidate, including age and gender

[186] ICL, Article 94

- The candidate's educational background
- Positions held by the candidate during the last five years
- Positions held by the candidate at the time of his/her nomination
- Any existing relationships the candidate has with the company
- The candidate's board membership (either BoC and BoD) in other legal entities
- The candidate's relationships with affiliated persons, including the company's major business partners
- Information related to the financial status of the candidate and other circumstances that may affect the candidate's ability to exercise his/her duties
- Any refusals by the candidate to provide requested information

It is recommended that candidates present a written statement to the BoD confirming their willingness to sit on the board, as well as their capacity to satisfy all relevant ICL and OJK requirements should they be elected. In the absence of a written statement, candidates should verbally confirm that they are willing to accept the position.

7.7 BoD Contract

A company will determine its appointment of BoD members through a GMS resolution. The ICL is silent on requirements concerning employment contracts for the BoD, and a director is not considered as an employee under the Indonesian Manpower Law. As such, Indonesian law considers a director's contract to be commercial in nature, rather than an employment contract.

For this reason, a GMS resolution should set out the employment terms and conditions of company directors. The GMS should also decide on relevant policies and amounts of remuneration to be provided to BoD members.

In addition to general information concerning contracting parties, contracts for company directors should include:

- Start and end dates
- Rights and duties of the director
- Rights and duties of the company
- Detailed remuneration, including benefits and other privileges (e.g., discounts on purchases of company shares, health insurance, reimbursement for housing/transportation costs)
- Terms and conditions, including penalties for failure to carry out specific duties and responsibilities
- Confidentiality clauses during the term of the contract and after the executive leaves the company regardless of the reason for leaving
- Non-compete clauses that apply during and after an executive's employment with the company
- A commitment to protect the interests of the company and its shareholders
- Grounds for early termination
- Indemnification

The ICL does not set a term limit for BoD members. The company's AoA will generally address this issue. Common practice in Indonesia is for BoD members to serve a maximum term of five years, with the opportunity to be re-elected for a maximum of two terms. For issuers and public companies, OJK provides that the elected term held by both BoD and BoC members must not exceed

five years.[187] If the annual GMS in the fifth year of a BoD or BoC member's term falls before the date that the member's term is due to expire, the term will end at the close of that GMS. OJK also requires the BoC of issuers and public companies to develop a succession policy for BoD members.[188] In addition, BoD members may be dismissed at any time by way of a GMS resolution that gives reasons, provided he/she has been given a chance to submit a defense.[189]

Decisions over the company's human resources should not be politicized in any way. Rather than insisting on close control over hiring decisions, it may be most effective for shareholders and commissioners to develop policies that specify desired outcomes to guide the BoD candidate selection process. For instance, commissioners may choose to be involved in drafting the terms of reference for key executive positions and ensure that these terms are sufficiently detailed and precise. The president director can use these terms of reference as guidelines when nominating BoD candidates to the GMS.

A public company may consider delegating duties related to the appointment of BoD members to a nomination and remuneration committee. The committee may, for instance, perform the following tasks:

- *Submit proposals of potential BoD candidates to the president director and the BoC.*
- *Provide an opinion on proposals for the appointment of BoD members originating from shareholders or the BoC.*
- *Draft or evaluate the nomination and appointment procedures for BoD members.*
- *Periodically assess the size and composition of the BoD and criteria for appointment, and make recommendations for change where appropriate. The committee may present these recommendations to the shareholders at the GMS*

[187] OJK Regulation No. 33/POJK.04/2014, Article 3 and Article 23.
[188] Circular Letter of OJK No. 32/SEOJK.04/2015, Article 4.4.
[189] ICL, Article 5(1)(2).

7.8 Meeting and Working Procedures

The AoA should determine the required:

- Frequency of BoD meetings
- Procedures for organizing and conducting BoD meetings
- Decision making procedures

OJK requires the BoD of public companies to hold meetings at least monthly and joint BoC and BoD meetings once every four months.[190]

The AoA or a specific resolution by the BoD should establish who has the power to convene a BoD meeting and specify the procedures for convening and conducting such meetings. It is generally common practice in Indonesia for the AoA to confer this power to the president director. However, all BoD members should have a voice in calling BoD meetings and setting agenda items.

The quorum of BoD meetings refers to the number of directors that must participate before decisions made within a meeting are considered valid. The AoA or a specific resolution by the BoD should specify the quorum required for BoD meetings. Typically, the quorum should not be less than one-half of the total number of BoD members. A BoD meeting that lacks a quorum cannot make valid decisions. However, the AoA will typically provide that in the event a BoD meeting does not achieve a quorum, the BoD may hold a second meeting the next day. The AoA typically confers upon the president director decision-making authority should the second meeting also fail to achieve a quorum.

Internal regulations should determine the form in which meeting notices and materials are to be delivered to BoD members in the most convenient and appropriate way. Directors should receive in advance a meeting notice with a detailed agenda to give them time to prepare and participate effectively.

A simple majority of BoD members who participate in the meeting should be sufficient to approve decisions of the BoD, unless the AoA or a specific resolution of the BoD requires a supermajority vote. Each BoD member should have one vote. The AoA may specify that the president director can cast a deciding vote in the event of a tie.

[190] OJK Regulation No. 33/POJK.04/2014, Article 16.

The minutes of BoD meetings should include the following information:

- Location and time of the meeting
- Names of meeting attendees
- Meeting agenda
- Issues on the agenda as well as the voting record of individual directors
- Decisions made by the BoD
- The rationale for these decisions

All attendees of the BoD meeting must sign the minutes.[191] For banks, any dissenting opinions in the BoD meeting must be included in the minutes together with the reasons for dissent.[192] Although not legally compulsory, in order to practice good corporate governance and improve transparency, the minutes of BoD meetings should be made available upon the request of:

- The BoC or audit committee members
- The external auditor
- A shareholder (or group of shareholders) possessing voting shares

[191] ICL, Article 91.
[192] OJK Regulation No. 55/POJK.03/2016, Article 20(5).

7.9 Remuneration

Executive remuneration is an important aspect in attracting managerial talent. Excessive executive remuneration packages, on the other hand, are often perceived to be an unjustified abuse of power and privilege. It is critical that executive compensation be set at a rate that is competitive, yet within reason compared to salaries in peer companies.

The remuneration of the BoD should not be left to its sole discretion. This should fall under the authority of the BoC or the GMS, as stated in the company's AoA. As a matter of good corporate governance, companies should set a remuneration policy that will apply to all directors and disclose all details in the company's annual financial statements. This information ought to feature clearly in the agenda of the annual GMS in order to give shareholders the opportunity to debate these matters.

Companies in the banking sector should take greater care when determining their remuneration policies. At a minimum, such policies should cover:

- The duties and responsibilities of directors and commissioners
- The duties and responsibilities of the nomination and remuneration committee
- Implementation of prudence and caution
- Appropriate disclosure

Where the BoC has established a nomination and remuneration committee, this committee may be responsible for drafting the company's remuneration policy for the BoC's review and approval. Alternatively, where the BoC drafts the policy in the first instance, the committee's role will be to provide an opinion on its proposal.

When setting remuneration policies for the BoD, it is important that the GMS or the BoC considers factors specified in the company's key performance indicators. Some issues relevant to determining appropriate remuneration levels include:

- The scope of responsibilities
- The required type and level of qualifications
- Required experience and skills

- Comparable levels of remuneration in peer companies and the industry
- The company's financial performance

Best Practice

International corporate governance practices typically divide a director's remuneration into two parts: base/fixed salary and variable or performance-related compensation. A director's base salary is usually based on his/her relevant background and experience and ideally should be comparable to the executive compensation in a peer group of similar companies. On the other hand, variable compensation is generally contingent on the executive's performance and his/her contribution toward the company's financial performance.

Variable compensation has come to represent a large part of an executive's remuneration package in many countries in order to better motivate performance. Variable compensation should align the interests of executive directors with the long-term interests of the company and its shareholders. There are many ways to link executive pay to individual and company performance, including both financial and non-financial indicators. Some common financial indicators utilized in variable compensation plans typically include:

- *Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA)*
- *Operating profit*
- *Return on Assets (ROA)*
- *Return on Investment (ROI) or Equity (ROE)*
- *Return on Capital Employed (ROCE)*
- *Economic Value Added (EVA)*
- *Achievement of specific individual objectives*

Non-financial indicators are equally important and valuable in managing executive performance, and can be organized around:

- *Customers (e.g., customer satisfaction, retention rates)*

- *Operational processes and efficiency (e.g., quality, cycle time and cost measures, after sales service)*
- *Internal growth/knowledge management (e.g., training programs, employee satisfaction rates, absenteeism, turnover)*
- *Robust control environment*

A typical form of variable compensation is stock options or performance-related bonuses. It is recommended for companies to seek shareholder approval prior to providing stock and option-based compensation, since such forms of compensation incurs considerable hidden costs for shareholders. These costs are usually hidden because accounting practices do not sufficiently reveal the true price tag of option-based compensation plans. As such, many companies are increasingly moving to amend their accounting and disclosure procedures. In addition, some financial market exchanges, such as the New York Stock Exchange, now require shareholder approval of all equity-based compensation plans.[193]

While remuneration plans may serve to attract top executive talent and motivate superior performance, the field of executive remuneration is complex and a lightning rod for shareholder and public criticism. Companies that introduce plans such as stock-options should do so only after a good deal of consideration and maintain full transparency.

Comparative Practice

In other jurisdictions, executives may be dismissed without cause under certain circumstances, and will receive severance payments as compensation. This may occur when a company has been acquired and the acquirer wishes to install new management. These severance plans are sometimes referred to as golden parachutes. A golden parachute is effectively a clause in an

[193] *The New York Stock Exchange Listed Company Manual* (New York: New York Stock Exchange, 2009), Article 703.09 Stock Option, Stock Purchase and Other Remuneration, http://wallstreet.cch.com/LCMTools/PlatformViewer.asp?searched=1&selectednode=chp_1_8_3_12&CiRestriction=remuneration&manual=%2FLCM%2FSections%2Flcm-sections%2F.

executive's employment contract, providing that he/she will receive large benefits in the event of a merger or takeover where the executive's employment is terminated. These benefits can take the form of severance pay, a bonus, stock options, or a combination thereof. Like other forms of compensation, the use of golden parachute clauses often attracts criticism. However, directors are not considered as employees under Indonesian labor law. In practice, the GMS or the company's internal rules will determine whether companies will provide directors with an "appreciation bonus/fee" in the case of a merger or takeover.

7.10 Performance Evaluation

Periodic performance evaluations serve as an important tool to conducting oversight of a company's BoD. It can help create a consistent and impartial system for the management of BoD performance. The results of periodic evaluations can also provide insight to identify required measures to improve the capabilities and functioning of the BoD.

A company's AoA or internal regulations may stipulate that the BoC can evaluate BoD performance at least annually, and more frequently if deemed necessary. The BoC may also find it useful to receive evaluations on the performance of the BoD that are carried out by the president director, or individual BoD members through self-evaluation, within the framework of the company's human resources performance evaluation and planning procedures.

CHAPTER 8
Corporate Secretary

THE CHAIRMAN'S CHECKLIST

- Does the company have a corporate secretary? Does the company need a corporate secretary? What contributions can a corporate secretary make to the company's governing bodies?
- Is the position of corporate secretary filled on a full-time basis, or does the corporate secretary combine his/her functions with other duties?
- Does the corporate secretary have an adequate mix of professional and personal skills?
- How does the company regulate the corporate secretary's activities? Does the company address the position of corporate secretary in its AoA or adopt specific internal regulations for the corporate secretary?
- Are commissioners and directors obliged to provide the corporate secretary with access to all information he/she needs to properly fulfill his/her duties? Does the corporate secretary serve as an effective link between the BoC and the BoD?
- What is the corporate secretary's role in ensuring timely and material disclosure to investors and the public? Does the corporate secretary collaborate with the company's legal and investor relations departments?

- What role does the corporate secretary play in planning and organizing the GMS?
- How does the corporate secretary assist the BoC and BoD in preparing for and conducting board meetings? Does the corporate secretary play a meaningful role in facilitating orientation and assisting with the professional development of board members?

The corporate secretary plays an essential role in a company's governance and administration by providing critical support to enable the BoC and BoD to perform their duties and responsibilities. This chapter focuses on the functions, qualifications, and authority of corporate secretaries in implementing good corporate governance practices.

8.1 Authority, Duties, and Responsibilities

Requirements for Indonesian companies to retain a corporate secretary vary according to corporate structure. It is obligatory for Indonesian public companies to appoint a corporate secretary.[194] The CG Code also recommends the following types of companies to retain a corporate secretary: state-owned companies, provincial or regional government-owned companies, companies that raise and manage public funds, companies whose products or services are widely used by the public, and companies that have significant impacts on the environment.[195] In addition, the National Committee on Governance introduced guidelines on corporate secretaries that apply to all companies,[196] as well as a specific corporate governance code for banks that provides recommendations for the role of corporate secretaries in the banking sector. International best practice recommends that larger companies, both public and private, appoint a corporate secretary.

According to the CG Code, the corporate secretary's primary function is to ensure sound communication between the company and its stakeholders, as well as to make information available to stakeholders in accordance with their needs. OJK requires corporate secretaries of issuers and public companies in Indonesia to perform additional duties as follows:[197]

- Inform and advise the BoC and BoD on any legal/regulatory changes to ensure compliance with Indonesia's Capital Markets Law and its implementing regulations.
- Ensure the company's public disclosure of material information, including making such information available on the company's website.
- Ensure timely submission of company reports to OJK.
- Prepare, organize, and document GMS and all BoC and BoD meetings.
- Facilitate induction program for newly elected BoC and BoD members.
- Maintain confidentiality of the company's documents, data, and information, except where prevailing laws and regulations require these to be disclosed.
- Prepare a periodic report on the implementation of the corporate

[194] OJK Regulation No. 35/POJK.04/2014, Article 2(1).
[195] *Indonesia's Code of Good Corporate Governance*, 19.
[196] *Indonesia's Code of Good Corporate Governance*, 19.
[197] OJK Regulation No. 35/POJK.04/2014, Article 5.

secretary's function to the BoD, and provide a copy to the BoC at least annually. This must include details of any education and training programs in which the corporate secretary has participated, to be included in the company's annual report.[198]

- Act as a liaison between the company and its shareholders and stakeholders.

International best practice suggests that a company's AoA or other internal documents should define the corporate secretary's authority in detail and specify requirements for of all governing bodies to assist the corporate secretary in discharging his/her duties. The following is an overview of the authority of the corporate secretary:

1. **Develop corporate governance policies**

   The corporate secretary can play an important role in developing the company's corporate governance policies and practices, and in monitoring compliance with such policies. In performing this function, the corporate secretary should review the company's policies on a regular basis and measure these against international best practices, making sure to stay abreast of the latest developments in corporate governance, including any changes to relevant national and international laws and regulations. He/she should communicate any breaches to the BoC and/or BoD. By reviewing the company's policies on a regular basis, the corporate secretary ensures the company maintains strong and up-to-date corporate governance standards.

2. **Provide assistance on governance issues**

   Best practice recommends that the corporate secretary should assist commissioners and directors to interpret corporate governance related laws and regulations, including listing rules, corporate governance codes, and international regulations and developments. The secretary must also assist the company to ensure it meets all information disclosure obligations and follows proper procedures for conducting the GMS, BoC, and BoD meetings. In doing so, the corporate secretary's role is to monitor the company's compliance with all relevant laws and external regulations as well as the AoA and internal regulations. The corporate secretary should not, however, render legal advice that falls outside the scope of his/her duties. The company should therefore clearly delineate

[198] OJK Regulation No. 35/POJK.04/2014, Article 11.

the duties of the corporate secretary from those of its legal counsel.

The corporate secretary should directly notify the president commissioner and/or the president director of any potential violations of corporate procedures if and when he/she becomes aware of possible issues. Violations may include:

- Alleged illegal acts or omissions of corporate officers or other corporate employees in fulfilling their legal duties and obligations
- Violation of procedures regulating the organization of the GMS, BoC, and BoD meetings, disclosure of information, and protection of shareholder rights.

3. Ensure information disclosure and transparency

The corporate secretary plays an important role in supporting the BoD and the president director to fulfill their respective information disclosure obligations, in accordance with Indonesia's capital markets regulations, such as by disclosing material information to all shareholders and potential investors. The corporate secretary also helps to maintain transparency in corporate procedures and acts as a liaison between the BoC and the BoD.

Figure **17** Corporate Secretary Function Related to Information Disclosure

The Corporate Secretary			
Ensure that the company operates in compliance with procedures for the maintenance and disclosure of information about the company.	Certify copies of documents before they are given to shareholders.	Guarantee the safekeeping of corporate documents.	Ensure unrestricted access for all shareholders to information in accordance with prevailing laws and regulations.

4. Assist in the protection of shareholder rights

Organizing the GMS

The corporate secretary plays an important role in organizing the GMS.

Figure **18** Corporate Secretary Function Related to the GMS

The Corporate Secretary

- Ensure compliance with GMS registration procedures.
- Notify shareholders of the GMS.
- Distribute materials for and during the GMS.
- Answer procedural questions during the GMS and resolve disputes related to preparing and conducting the GMS.
- Collect voting ballots and transfer them to the counting commission.
- Ensure that minutes on the voting results and the GMS are kept.
- Communicate the results of the GMS to shareholders.

Assisting in the enforcement of shareholder rights

The corporate secretary should:

- Ensure the company takes proper notice of all shareholder petitions that are submitted.
- Channel all shareholder inquiries to the appropriate governing bodies and departments.
- Resolve any conflicts, especially those concerning the maintenance of the shareholder register, promptly and fairly.

Liaising between shareholders during control transactions

Indonesian regulations do not cover the role of the corporate secretary during a control transaction, which is a transaction that results in a change of control of the company. Best practice recommends that the corporate secretary should act as a liaison between the controlling shareholder(s) and the company's remaining shareholders. The corporate secretary does this by ensuring that the mandatory offer made by the bidder is distributed to all shareholders. The corporate secretary should follow procedures for the distribution of the mandatory offer

to non-controlling shareholders. The same procedures can be applied to squeeze-out and sell-out procedures. The role of the corporate secretary also includes active co-operation with external parties (such as brokers, dealers, and banks) that are authorized for the realization of these activities. The corporate secretary should also communicate with minority shareholders to inform them about their rights in the context of takeovers.

Assisting in resolving corporate conflicts

Corporate conflicts can arise between the company's BoC, BoD, and shareholders. If so, the corporate secretary should take responsibility for liaising between the conflicting parties. The corporate secretary must also notify the president commissioner and/or president director of any existing or potential conflicts so that these may be dealt with appropriately.

A company's effectiveness in preventing and resolving conflict depends on its capacity to respond to legitimate complaints. The corporate secretary should register inquiries, letters, and demands filed by shareholders, and review, record, and duly transmit them to the governing bodies that have the authority to resolve the conflict. The corporate secretary also needs to periodically follow up on the status of complaints in order to make sure they are fully addressed, and either resolved or rejected as appropriate.

5. Facilitate the Flow of Information

According to the CG Code, the corporate secretary plays a key role in providing the BoC and BoD with timely, regular, and comprehensive information to properly execute their duties and responsibilities. Such information typically includes:

- Minutes of BoC and BoD meetings
- Decisions and documents approved by the BoC and BoD
- Minutes of meetings and reports prepared by the audit committee and any other committees, internal audit, and the external auditor
- Financial documents

6. Organize Board Meetings

Although the president commissioner and president director are primarily responsible for conducting BoC and BoD meetings, the

corporate secretary handles all administrative and organizational matters. Companies may choose to set out the corporate secretary's role in organizing board meetings under internal corporate regulations. The secretary's primary duties in this respect typically include:

- Assisting the president commissioner/president director in preparing the agenda
- Developing presentations on substantive and procedural issues that are under discussion
- Preparing briefs for boardroom discussions
- Providing all commissioners and directors with notice of board meetings
- Distributing and collecting voting ballots and written opinions of commissioners/directors who are not physically present at the meeting
- Forwarding the ballots and written opinions to the president director/president commissioner
- Ensuring all meetings follow the procedures required under the ICL, AoA, and other relevant regulations, including drafting, distributing, and storing minutes in the company's archives

7. Facilitate Induction Program for New Board Members

The corporate secretary should brief newly elected commissioners and directors on:

- Corporate procedures regulating the company's governing bodies
- Corporate structure and company officers
- The company's internal regulations and other documents
- Decisions of the GMS, BoC, and BoD that are in effect
- Any other relevant information required by the commissioners/directors for the proper discharge of their duties

8.2 Qualifications

When selecting a corporate secretary, the BoD should use a range of sources to determine the general requirements and specific criteria to be used in evaluating candidates for the position, such as the CG Code, relevant regulations, the AoA, and internal regulations. Importantly, the corporate secretary also needs to be a person with an impeccable reputation. Companies must avoid appointing individuals with a criminal record or who have been connected to significant administrative offenses.

Best practice recommends that this position be filled by a dedicated employee in a full-time capacity. Large companies may find it necessary to establish an office of the corporate secretary, to be staffed by several officers. Additional staffing may be useful for companies with large numbers of directors, commissioners, and shareholders. Should a company decide to establish an office of the corporate secretary, it may wish to specify the office's responsibilities in the internal company regulations or other documents. In smaller companies, legal counsel or a person holding a similar position may carry out the duties of the corporate secretary. However, the corporate secretary must devote sufficient time to his/her duties. Positions should be shared only if this does not hinder the corporate secretary from fulfilling his/her duties effectively. OJK also allows any BoD members of a public company to concurrently hold the position of corporate secretary.[199]

In Indonesia, OJK sets out minimum requirements for corporate secretaries, which apply to public companies. OJK requires a corporate secretary to:[200]

- Be capable of performing legal actions.
- Have knowledge and understanding in the fields of law, finance, and corporate governance.
- Understand the company's business activities.
- Have the ability to communicate effectively.
- Be domiciled in Indonesia.

[199] OJK Regulation No. 35/POJK.04/2014, Article 3(2).
[200] OJK Regulation No. 35/POJK.04/2014, Article 9.

In addition, a corporate secretary may not hold any position in other public companies.[201]

To be able to act in the company's best interest at all times, the corporate secretary must be shielded from undue influence from management and other parties. The corporate secretary should be accountable to and controlled by the BoD.

Figure 19 illustrates core qualifications that are necessary to effectively perform the corporate secretary's role.

Figure **19** Qualifications and Skills of Corporate Secretaries

The Corporate Secretary

- Understands corporate and securities law
- Has "presence" and good communication skills
- Is detail-oriented, flexible, and creative
- Knows how to overcome bureaucratic thinking in the company
- Understands the company's business
- Mediates and achieves consensus
- Read signals on the horizon and provides early warning to management
- Is intuitive and sensitive to what the president director and directors are thinking and feeling

[201] OJK Regulation No. 35/POJK.04/2014, Article 3(3).

8.3 Appointment and Dismissal

A company's internal regulations should set out the procedures for nominating and appointing the corporate secretary. The BoD is responsible for the appointment and dismissal of the corporate secretary.[202] Ideally, the BoD should consult and appraise the BoC throughout the entire process. The BoD should produce detailed terms of reference, which may include the corporate secretary's authority, duties, and responsibilities beyond those required by law, the corporate secretary's term of office, and other relevant provisions. In addition, the corporate secretary's contract of employment should precisely define the remuneration and other rights and duties that apply to the position.

Before deciding on the appropriate candidate to fill the corporate secretary role, the BoD must possess all relevant information necessary to assess all candidates' qualifications, experience, and personal qualities. A nominee for the position of corporate secretary should provide the BoD with sufficient information to evaluate his/her candidacy. Candidates should, at a minimum, be required to provide evidence of their:

- Educational background
- Employment in other companies
- Any relationship they may have with affiliated persons or major business partners of the company
- The number and type of company shares they own, if any
- Declaration of non-conviction for criminal or significant administrative offences
- Any other aspects and circumstances that may influence their performance as corporate secretary, in accordance with general company documents and any specific requests from the BoD

This information may be supplemented by personal references and interviews with BoD or BoC members, since a good rapport between directors, commissioners, and the corporate secretary will be important in maintaining effective working relationships. The corporate secretary should notify the BoD immediately of any changes in circumstances that may influence his/her ability to fulfill the role.

[202] OJK Regulation No. 35/POJK.04/2014, Article 3(1).

CHAPTER 9
Risk Management and Internal Control

THE CHAIRMAN'S CHECKLIST

Risk Management and Internal Control

- Does the company have a risk management system in place? Does this system cover risks at the subsidiary level as well? How does the company identify business, operational, financial, reputational, environmental and social risks?
- Does the company have an internal control system in place? Does the company have a formal document that regulates the internal control system and procedures? Is this document periodically reviewed?

Audit Committee

- Should the company's BoC have an audit committee? What are the costs and benefits?
- If the company has an audit committee, is it staffed with individuals who are independent, able, and willing to do the job properly and effectively?
- Does the head of the audit committee have the requisite professional and human relations skills? Are members of the audit committee have accounting and financial expertise?
- Does the audit committee meet often enough to perform its duties effectively? Does it place the necessary and relevant issues on the agenda?

- Does the audit committee add value to the BoC's discussions covering audit, risk, internal control, compliance, and financial reporting?
- Does the audit committee receive the necessary information to perform its duties effectively? Does it have resources to hire outside accounting or legal advice? Does the audit committee have access to and meet periodically with external auditors and the head of internal audit?
- Does the audit committee perform self-evaluations, as well as assess the performance of internal audit and the external auditor on a regular basis?

External Auditor

- Does the company have a reputable and independent external auditor? Does the external auditor provide other, non-audit services to the company that could compromise its independence? Are audit partners rotated?
- How does the company select its external auditor and assess its independence? Does an open tender process take place? If so, who organizes the tender process? Does the company have a rotation policy for the external auditor?
- To whom does the external auditor report?
- Does the external auditor participate in the AGMS and answer all questions posed by shareholders?

9.1 Risk Management

Successful management of risk is central to the success of all organizations. The practice of risk management has evolved significantly from its original emphasis on operational risks. Key differentiators of the recent international standards on risk management (such as ISO 31000:2009, COSO Enterprise Risk Management—Integrated Framework) from traditional risk management are the linking of key risks into an organization's strategic objectives, the expansion of responsibility for managing risks across the organization, and a broader definition of risk as "the effect of uncertainty on objectives", which therefore includes strategic, reputational, financial, or IT risks, among others, as opposed to focusing solely on operational risks.

The BoC and BoD are ultimately responsible for determining the nature and extent of risks that an organization is willing to take to achieve its strategic objectives and for ensuring that these risks are identified and managed properly. The BoD is responsible for implementing the risk management system while the BoC is in charge of monitoring and reviewing its implementation.[203] The CG Code recommends the following:[204]

- The BoD should establish and implement a sound risk management system within the company, covering all aspects of the company's activities.
- Each strategic decision taken, including the creation of new products or services, should be carefully considered against its risk exposure to ensure an appropriate balance between benefit and risk.
- To ensure proper implementation of risk management, the company should have a work unit or person in charge of this function.

Best Practice

To ensure effective risk management, ISO 31000:2009 recommends that organizations comply with the following principles:[205]

[203] *Indonesia's Code of Good Corporate Governance*, 16.
[204] *Indonesia's Code of Good Corporate Governance*, 18.
[205] *ISO 3100:2009 Risk Management—Principles and Guidelines* (Geneva: International Organization for Standardization, 2009), 7-8.

1. ***Risk management creates and protects value.***

   Risk management contributes to the demonstrable achievement of objectives and improvement of performance in, for example, human health and safety, security, legal and regulatory compliance, public acceptance, environmental protection, product quality, project management, efficiency in operations, governance, and reputation.

2. ***Risk management is an integral part of all organizational processes.***

   Risk management is not a stand-alone activity that is separate from the main activities and processes of the organization. Risk management is part of the responsibilities of management and an integral part of all organizational processes, including strategic planning and all project and change management processes.

3. ***Risk management is part of decision making.***

   Risk management helps decision makers make informed choices, prioritize actions, and distinguish among alternative courses of action.

4. ***Risk management explicitly addresses uncertainty.***

   Risk management explicitly takes account of uncertainty, the nature of that uncertainty, and how it can be addressed.

5. ***Risk management is systematic, structured, and timely.***

   A systematic, structured, and timely approach to risk management contributes to efficiency and to consistent, comparable, and reliable results.

6. ***Risk management is based on the best available information.***

   The inputs to the process of managing risk are based on information sources such as historical data, experience, stakeholder feedback, observation, forecasts, and expert judgment. However, decision-makers should inform themselves of, and should take into account, any limitations of the data or modelling used or the possibility of

divergence among experts.

7. ***Risk management is tailored.***

   Risk management is aligned with the organization's external and internal context and risk profile.

8. ***Risk management takes human and cultural factors into account.***

   Risk management recognizes the capabilities, perceptions, and intentions of external and internal people that can facilitate or hinder achievement of the organization's objectives.

9. ***Risk management is transparent and inclusive.***

   Appropriate and timely involvement of stakeholders and, in particular, decision makers at all levels of the organization, ensures that risk management remains relevant and up-to-date. Involvement also allows stakeholders to be properly represented and to have their views taken into account in determining risk criteria.

10. ***Risk management is dynamic, iterative, and responsive to change.***

    Risk management continually senses and responds to change. As external and internal events occur, context and knowledge change, monitoring and review of risks take place, new risks emerge, some change, and others disappear.

11. ***Risk management facilitates continual improvement of the organization.***

    Organizations should develop and implement strategies to improve their risk management maturity alongside all other aspects of their organization.

9.2 Internal Control

The management of risk requires the establishment and maintenance of an effective internal control system. Internal control is "a process, effected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting, and compliance."[206] Internal control is not merely about standards, policies, procedures, systems, and forms but also refers to people, behavior, and actions taken at every level of an organization to affect internal control. Internal controls therefore can provide reasonable, not absolute, assurance that an organization can achieve its objectives under these categories: operations (the effectiveness and efficiency of the entity's operations, including operational and financial goals and safeguarding assets against loss), reporting (the reliability, timeliness, and transparency of internal and external financial and non-financial reporting), and compliance (adherence to relevant laws and regulations).

The CG Code sets out the following provisions on internal control:[207]

- The BoD should establish and maintain a sound internal control system to safeguard the company's assets, its performance, and its compliance with laws and regulations.
- Issuers and public companies are required to have an internal control function or unit.
- The internal control unit should assist the BoD in achieving the company's objectives and business sustainability by evaluating the implementation of the company's program, providing recommendations to improve the effectiveness of the risk management process, evaluating the company's compliance with laws and regulations, and facilitating coordination with the external auditor.
- The internal control unit is responsible to the president director or the director in charge of this function. The internal control unit has a functional relationship with the BoC through the audit committee.

In addition, the BoC, through the Audit Committee, is required to ensure that the internal control structure is adequate and effective.[208]

[206] *Internal Control—Integrated Framework* (Committee of Sponsoring Organizations of the Treadway Commission, 2013), 1.
[207] *Indonesia's Code of Good Corporate Governance*, 18-19.
[208] *Indonesia's Code of Good Corporate Governance*, 15.

A company's internal control system should be based on the following principles:

- An internal control system should operate continuously and without interruption. A system that functions on a permanent basis allows the company to identify deviations on a timely basis and helps to predict future deviations.
- Each person involved in the internal control process should be held accountable. Therefore, the internal control system should include a monitoring system, in which the performance of each person carrying out a control function is managed by yet another person in the system.
- Key controls in business processes should be clearly defined, documented, and segregated. Companies should prohibit duplication of control functions and should distribute functions among the employees. The following are some examples of key controls that should be segregated:
    1. Sales from accounting and billing
    2. Purchasing from receipt and payment
    3. Cash access from cash accounting and reconciling
    4. Cash access from processing or approval of sales reversals, adjustments, and credit memos
    5. Depositing cash from reconciling bank accounts
    6. Financial statement review/approval from recording and approving entries
    7. Payroll records maintenance from authorizing payroll disbursements
    8. Payroll disbursements authorization from payroll reconciliations
    9. Systems development from systems operations and database administration
    10. Systems operation from data control
    11. All authorization activities from related record keeping activities
    12. All custody activities from related record keeping and reconciling activities
- The unit responsible for internal control should be directly accountable to the BoD and separated from other corporate bodies, including the BoC, the BoD, and other internal departments. The BoC should review and monitor the effectiveness of internal control on a regular basis.

- A culture of continuous development and improvement needs to be put in place. A company's internal control system should be structured to allow it to address new issues and be easily expanded and upgraded.
- A system for timely reporting of any deviations should be put in place. Ensuring the timeliness of reporting on deviations with the shortest possible deadline allows authorized persons to act swiftly to correct problems.

Best Practice

An internal control system includes the following inter-related elements:[209]

1. ***Control environment***
   Control environment is a set of standards, processes, and structures that provides the foundation for carrying out internal control across the organization. Components of a control environment include the integrity and ethical values of the organization; the parameters that enable the board to carry out its oversight responsibilities; the organizational structure and assignment of authority and responsibility; the process for attracting and retaining human resources; and the performance measures, incentives, and rewards to ensure accountability and performance.

2. ***Risk assessment***
   Risk assessment is the process of identifying and assessing risks to achieve a company's objectives, which forms a basis for determining how these risks should be managed. Central to risk assessment is the establishment of specific objectives related to operations, reporting, and compliance, which enables the identification and management of risks related to these objectives.

3. ***Control activities***
   Control activities are the actions that emanate from policies

[209] *Internal Control—Integrated Framework*, 12-14.

and procedures to mitigate risks to acceptable levels. Control activities occur throughout the organization, at all levels and functions. They include a range of activities as diverse as approvals, authorizations, verifications, reconciliations, reviews of operating performance, security of assets, and segregation of duties.

Control activities should be as strict at the top as at the bottom of the company's operations, lending credibility to the control environment and setting the tone from senior management to ensure all employees comply.

4. ***Information and communication***
Companies must identify, obtain or generate, and disseminate pertinent information in a form and within a timeframe that enables employees to effectively carry out their responsibilities. Effective communication should occur in a broad sense—flowing up, down, and across the organization. All personnel should receive a clear message from senior management that control responsibilities must be taken seriously. Furthermore, they must understand their own role in the internal control system, as well as how individual activities relate to the work of others. It is particularly important that management does not limit itself to communicating on a control measure in and of itself, but properly emphasize the meaning and purpose of various internal control elements. Employees should also have a means of communicating significant information upstream. The company should communicate with external parties, such as customers, suppliers, regulators, and shareholders, regarding matters affecting the functioning of internal control.

5. ***Monitoring activities***
An internal control system needs to be monitored over time to assess the quality of the system's performance. This is accomplished through ongoing evaluations, separate evaluations, or some combination of the two. Ongoing monitoring occurs during the course of operations and is built into business processes at different levels of

the organization. It includes regular management and supervisory activities and other actions personnel take in performing their duties. The scope and frequency of separate evaluations depend primarily on the assessment of the risks and effectiveness of ongoing monitoring procedures. Internal control deficiencies should be reported upstream, with the most serious matters reported directly to the BoC. The BoD and the BoC need to clearly formulate sanctions to be imposed as a result of control violations on an ex ante basis.

Internal control is, to some degree, the responsibility of everyone in an organization and should form an explicit or implicit part of every employee's job description. Virtually all employees produce information used in the internal control system or take other actions needed to affect control. In addition, all personnel should be responsible for communicating upward problems in operations, non-compliance with an internal code of conduct or company-level corporate governance code, other policy violations, and illegal actions.

Best Practice

The department responsible for corporate training programs should ensure that all employees and executives receive training on the company's control culture and system. Furthermore, although each company has its own specific internal control system and responsible bodies, there are some general rules that a company should follow.

Internal control should always start at the top of the company, from the board and management. The executive bodies are responsible for establishing a proper internal control environment and maintaining high ethical standards at all levels of the company's operations. Furthermore, the approval of internal control procedures falls within the authority of the BoC, typically

exercised through the audit committee. The audit committee should review and evaluate the efficiency of the internal control system as a whole and prepare recommendations on how to improve it. Finally, the implementation of internal control procedures is the responsibility of the executive bodies.

The president director is ultimately responsible for and should assume ownership of the internal control system. More than any other individual, he/she sets the tone at the top that affects the integrity and ethics of a positive control environment.

In a large company, the president director fulfils this duty by providing leadership and direction to senior managers and reviewing the way they control the business. Senior managers, in turn, assign responsibility to establish more specific internal control policies and procedures to personnel responsible for each function. For example, controls for the company's IT system should fall under the responsibility of the chief information officer or manager responsible for IT. Financial officers and their staff, whose control activities cut across as well as up and down the operations and other units of a company, play a critical role in the internal control system.

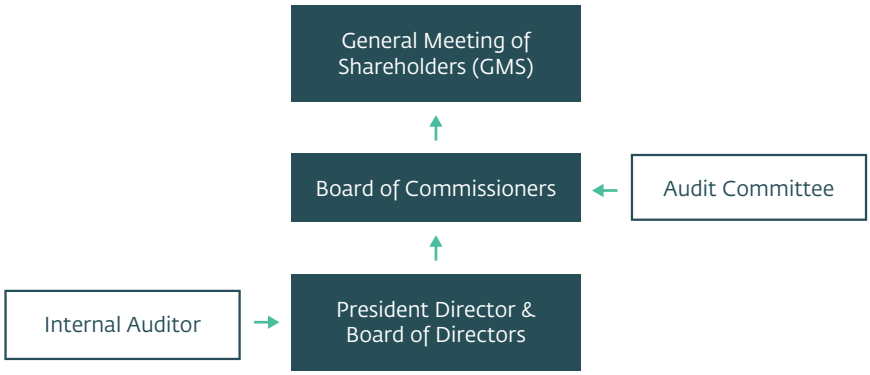
9.3 Board of Commissioners

Effective oversight by the BoC is key to ensuring the company continuously reviews its internal controls and mitigates risks to enable the company to achieve its objectives.

For banks and financial institutions engaged in Islamic finance, another important oversight organ is the Sharia supervisory board. The ICL requires all Sharia-compliant companies to establish a Sharia supervisory board in addition to the BoC. The Sharia supervisory board supervises and provides recommendations to ensure that the company's activities conform with Sharia principles.[210]

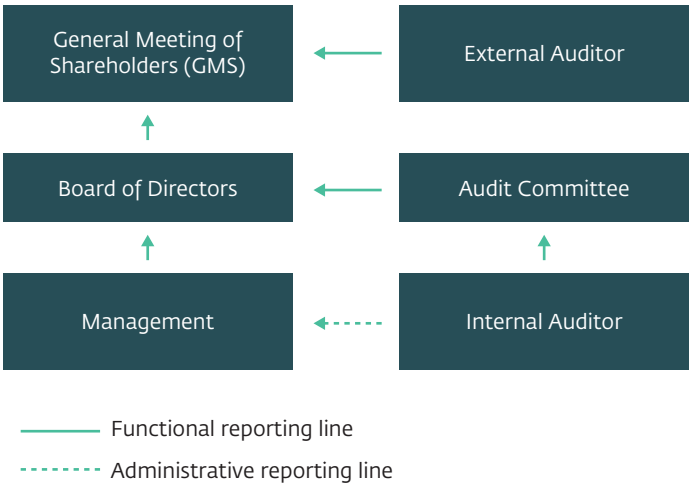
For an overview of these governance organs/functions and their reporting lines, see ***Figure 20*** for Indonesia's system and ***Figure 21*** for countries with a unitary board system.

Figure **20** Reporting Line of Indonesian Governing Bodies



[210] ICL, General Elucidation, Article 1(7).

Figure **21** Reporting Line of Governing Bodies in Unitary Board System



9.4 Audit Committee

Audit committees play a critical role in assisting the BoC to discharge its oversight responsibility for adequate and effective risk management, financial reporting, control, and governance. Issuers, public companies, and listed companies in Indonesia must establish an audit committee[211] and develop and disclose an audit committee charter that includes the following:[212]

- Authority, duties, and responsibilities of the audit committee
- Composition, structure, and membership requirements
- Working procedures
- Meeting policy
- Reporting system to disclose the committee's activities
- Policy on handling complaints/reports regarding financial reporting irregularities
- Tenure for audit committee members

Figure **22** Main Focus Areas of Audit Committees

[211] OJK Regulation No. 55/POJK.04/2015, Article 2.
[212] OJK Regulation No. 55/POJK.04/2015, Article 12.

9.4.1 Function

OJK regulates the audit committee's duties and responsibilities, as follows:[213]

- Review financial-related information published by the company for public or official use, including financial statements, projections, and other related statements.
- Monitor the company's compliance with relevant laws and regulations that govern the activities of the company.
- Provide an independent opinion when there are disagreements between management and the external auditor.
- Provide recommendations to the BoC on the appointment, re-appointment, and removal of the external auditor, including the remuneration, terms/scope of engagement, and independence of the external auditor.
- Review the implementation of the audit by internal auditors and monitor the BoD's response to internal audit findings.
- Evaluate the implementation of a risk management system by the BoD if there is no separate risk function under the BoC.
- Evaluate complaints concerning the company's accounting and financial reporting processes.
- Evaluate and providing recommendations to the BoC on handling potential conflicts of interest.
- Guard the confidentiality of the company's documents, data, and information.

Best Practice

The National Association of Corporate Directors, an international independent training institute for directors, has identified the following risk indicators that the audit committee should monitor and examine closely:

- *Complex business arrangements which appear to serve little practical purpose.*

[213] OJK Regulation No. 55/POJK.04/2015, Article 10.

- *Large last-minute transactions that result in significant revenues in quarterly or annual reports.*
- *Dismissal or changes to the appointed auditor following accounting or auditing disagreements.*
- *Overly optimistic news releases in which the chief executive officer seeks to cajole investors into believing in future growth.*
- *Widely dispersed business locations with a decentralized management and poor internal reporting system.*
- *Inconsistencies between management's discussion and analysis and the underlying financial statements.*
- *Insistence by the chief financial officer that he/she be present at all meetings of the audit committee and internal and external auditors.*
- *A consistently close or exact match between planned results and reported results, and managers who always achieve 100 percent of their bonus opportunities.*
- *Hesitancy, evasiveness, or lack of specifics from management or auditors regarding questions about the financial statements.*
- *Frequent differences of view between management and the external auditors.*
- *A pattern of shipping most of the month's or quarter's sales in the last week or last day.*
- *The internal audit operating under scope restrictions, such as the internal auditor not having a direct line of communication to the audit committee.*
- *Unusual balance sheet changes, or changes in trends/important financial statement relationships. For example, receivables growing faster than revenues, or accounts payable that are continually delayed.*
- *Unusual accounting policies, particularly for revenue recognition and cost deferrals, such as recognizing revenues before products have been shipped ("bill and hold"), or deferring cost items that are normally expensed when they are incurred.*

- *Accounting methods that appear to favor form over substance.*
- *Accounting principles/practices at variance with industry norms.*
- *Numerous or recurring unrecorded or "waived" adjustments detected in connection with the annual audit.*

9.4.2 Composition

OJK requires the audit committee of public companies and issuers to consist of at least three members, including independent commissioners and those appointed from external sources, and to be chaired by an independent commissioner. The BoC appoints and dismisses all members of the audit committee.

In addition, members of the audit committee of issuers or public companies must meet the following criteria:[214]

- Have high integrity, possess relevant skills, knowledge, and experience, and be able to communicate well
- Be financially literate, understand the company's business, audit process, risk management, and regulatory provisions that govern the capital market
- Be compliant with the company's code of ethics
- Be willing to continuously improve their competence through education and training
- At least one member must have educational background or experience in accounting and finance
- Shall not be an insider in a public accounting firm, legal firm, public appraiser office, or other parties that have provided insurance and non-insurance, appraisal, or other consulting services to the company within the last six months
- Have no authority or responsibility to plan, lead, control, or

[214] OJK Regulation No. 55/POJK.04/2015, Article 7.

supervise the activities of the company, except in their capacity as independent commissioners, within the last six months

- Have no share ownership, directly or indirectly, in the company
- If any member of the audit committee obtains company shares, whether directly or indirectly due to a legal event, such shares shall be transferred to another party no later than six months following such event
- Have no affiliated relationship with BoC and BoD members and majority shareholders
- Have no direct or indirect business relationship that is related to the company's business activities

For banks, OJK also requires the chairman of the audit committee to be an independent commissioner. A bank's audit committee must consist of at least one independent commissioner, one external party with expertise in finance or accounting, and one external party with expertise in law or banking. At least 51 percent of the audit committee's members must be independent commissioners or other external parties. No member of the BoD may serve as a member of the audit committee.

9.4.3 Meeting

The audit committee shall conduct meetings on at least a quarterly basis. A quorum requires at least more than half of the committee members to be present.[215]

A meeting of a bank's audit committee can only be held if 51 percent of total committee members, including an independent commissioner and an external party, are present.[216] A resolution of the audit committee meeting is based on consensus, which if not achieved can be replaced by majority voting.[217] All meetings must be recorded and the minutes should include any dissenting opinion raised during the meeting.[218]

[215] OJK Regulation No. 55/POJK.04/2015, Article 14.
[216] OJK Regulation No. 55/POJK.03/2016, Article 50(2).
[217] OJK Regulation No. 55/POJK.03/2016, Article 51(1)(2).
[218] OJK Regulation No. 55/POJK.03/2016, Article 51(3)(4).

9.4.4 Access to Information and Resources

To perform its function effectively, the audit committee should have the authority to investigate any matter that falls under its purview. Its members should have unfettered access to all documents and corporate information, including full cooperation by management. The corporate secretary often plays a crucial role in this respect by facilitating a flow of information to fulfill the audit committee's requests. The audit committee should also be provided with reasonable resources that are needed to fulfill its function, and be authorized to hire external advisors if needed at the company's expense.

9.5 Internal Audit

Separate from the audit committee, internal audit is responsible for ensuring that internal controls are adequate and effective, and thus capable of protecting the organization against loss. Internal audit evaluates the control environment, assesses risks and components of risk management, communicates these findings to the BoC (through the Audit Committee) and the BoD, and makes suggestions for improvement. An internal audit does not only cover the company's finances, but also its operations, systems, and procedures. Thus, internal audit helps companies accomplish their objectives by introducing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and corporate governance processes.

Internal audits provide assurance to the BoC and BoD regarding:

- The efficiency and effectiveness of operations for the overall entity, divisions, subsidiaries, operating units, and business functions
- The risk management framework (including risk identification, risk assessment, response, and monitoring)
- The internal control environment, including safeguarding of assets and soundness and integrity of reporting processes
- Compliance with regulations, policies, and procedures

The BoD, with consent from the BoC, has the authority to appoint and dismiss the head of internal audit, provided (for all public companies) that the BoD notify OJK of any appointment, replacement, or dismissal of the head of internal audit. The head of internal audit has the authority to appoint and dismiss the deputy head and other positions within the team.

Best Practice

To effectively perform its duties, internal audit must be independent. Independence is defined as "the freedom from conditions that threaten the ability of the internal audit activity to carry out internal audit responsibilities in an unbiased manner. To

achieve the degree of independence necessary to effectively carry out the responsibilities of the internal audit activity, the chief audit executive has direct and unrestricted access to senior management and the board. This can be achieved through a dual-reporting relationship."[219] The BoC should approve decisions regarding the appointment and dismissal of the head of internal audit. The Institute of Internal Auditors recommends that the head of internal audit should functionally report to the BoC through the audit committee and administratively to the president director.

OJK sets out the internal audit unit's duties and responsibilities as follows:[220]

1. Prepare and implement the annual audit plan.
2. Review and evaluate the implementation of internal control and risk management in accordance with the company's policies.
3. Perform audits and assess efficiency and effectiveness in the areas of finance, accounting, operation, human resources, marketing, information technology, and other activities.
4. Provide objective information and advice to all levels of management based on audit findings to improve company activities.
5. Report and deliver audit results to the president director and the BoC.
6. Monitor, analyze, and report on the progress of recommended actions.
7. Cooperate with the audit committee.
8. Develop programs to evaluate the adequacy and effectiveness of the internal audit function.
9. Perform a special audit, if necessary.

It is mandatory for banks to establish an independent internal audit unit. The unit is responsible to draft and update working guidelines as well as systems and procedures based on the regulatory provisions that govern the implementation of the internal audit function of commercial banks.[221] To effectively discharge its duties, an internal audit unit needs to be adequately resourced and competently staffed, thoroughly independent, and have appropriate standing within the

[219] *International Standards for the Professional Practice of Internal Auditing* (International Internal Audit Standards Board, 2017), https://na.theiia.org/standards-guidance/mandatory-guidance/Pages/Standards.aspx.
[220] OJK Regulation No. 56/POJK.04/2015, Article 7.
[221] OJK Regulation No. 55/POJK.03/2016, Article 54.

organization. Companies can achieve this by making the unit accountable to the BoC (through the audit committee).

Best Practice

Typical internal audit tasks across jurisdictions include:

- *Appraise compliance of business activities with internal policies and procedures*
- *Provide advice in setting up internal policies and procedures*
- *Appraise internal controls over the safeguarding of assets*
- *Appraise compliance with laws and regulations*
- *Appraise internal controls over financial information*
- *Appraise internal controls over business processes*
- *Appraise internal controls over strategy implementation*
- *Appraise the process for identifying, evaluating, and managing business risks*
- *Appraise operational efficiency*
- *Appraise compliance with contractual obligations*
- *Conduct audits of information technologies and information security*

9.6 External Audit

An independent audit conducted by an external auditor is an important element of a company's control framework. The external auditor's role is to express an opinion on whether the company's financial statements are prepared in accordance with an identified financial reporting framework and whether they are reliable. The external auditor provides shareholders, managers, employees, and market participants an independent opinion on the company's financial position and, if performed properly, should attest to the accuracy of the statements. An independent audit conducted by a publicly recognized and accredited accounting firm enhances the company's credibility, and accordingly, its prospects for attracting investment.

The ICL requires the BoD to submit its financial statement to a public accountant if:[222]

- The company's line of business involves raising and/or managing public funds
- The company issues Debt Acknowledgement Letters to the public
- The company is a public company
- The company is a state-owned company
- The company owns assets or has turnover of at least Rp 50,000,000,000
- If required by laws and regulations

The following are key principles to ensure an independent external audit:

1. Management is responsible for preparing and presenting the company's financial statements.
2. The external auditor is responsible for forming and expressing an opinion on the financial statements prepared by management.
3. Audit of the financial statements does not relieve management of any of its responsibilities.

All public and listed companies must have their annual financial statements audited by an independent and accredited public accountant that is registered with OJK.

[222] ICL, Article 68.

In conducting a company's external audit, the external auditor (or auditing firm) has the right to:

- Receive fees for services rendered
- Request the company to supply accounting documents and other documents/information relevant to the audit and receive the required documents promptly and in full
- Request, inspect, and confirm economic and financial information on the company under audit from relevant sources of information, both from within and outside of those entities

Meanwhile, the external auditor (of the auditing firm) should abide by the following principles:

- Allocate adequate and professional human resources to ensure the quality of the audit service delivery.
- During the audit process, if the auditor detects signs of regulatory violations (including financial and accounting regulations, capital market regulations, and other relevant laws) or any other issues that may endanger the company's financial condition and client interests, the external auditor must notify the company of these issues and write appropriate comments in the audit reports.
- Provide the company under audit with details of the auditor's operating licenses and other audited clients to prevent conflicts of interest.
- To refuse providing services if the client is not able/willing to ensure the external auditor's independence or if the client violates professional auditing conditions or any other related regulations.

The external auditor or a representative from the auditing firm should be permitted to attend all GMS, and is entitled to receive the same notice and information relating to the GMS that would be provided to shareholders. The external auditor may also be entitled to express his/her opinions about issues relating to the audit at the GMS.

Best Practice

The external auditor will often submit, and companies seeking to implement good corporate governance should demand, what is referred to as a management letter in addition to the audit report. The management letter typically covers all material weaknesses in the company's internal control, accounting, and operating procedures. The purpose of the letter is to provide constructive suggestions to management concerning improvements for such procedures.

The findings contained in the management letter are considered to be "non- reportable" to third parties, yet require corrective action by management. Companies wishing to attract external finance should be aware that investors will typically request a copy of the management letter.

9.6.1 Rights and Duties of the Company

The audited company has the right to:

- Select an external auditor that satisfies the conditions for lawful professional practice in Indonesia to sign contracts on the provision of auditing services, except otherwise provided for by law.
- Request the external auditor to provide relevant details on its registered business license, any auditing opinion provided, or its practicing auditors (if the auditor is a company).
- Refuse to provide information that is not relevant for the purpose of the audit and request that the auditor be replaced if he/she violates the principle of auditing independence.
- Discuss or demand written explanations relating to unclear issues stated in the draft audit report.
- Complain about practicing auditors if they commit illegal acts during the audit.

- Request the external auditor to compensate for any damages caused by the audit.

The audited company is obligated to:

- Provide accurate, sufficient, and timely information/documents according to the external auditor's requests, and take full responsibility for the accuracy, integrity, and objectivity of the information provided.
- Coordinate with and facilitate the external auditor during the audit.
- Make no effort to block or hinder the scope of the audit.
- Implement all recommendations made by the external auditor in a complete and timely manner.
- Inform the authorized agency and professional auditing body of any violations conducted by the auditor and provide this information in a full and timely manner.
- Pay audit fees in accordance with terms of the audit contract.
- Where a company appoints an auditing firm to perform services for more than three consecutive years, the company must request that the external auditor change the practicing auditors who sign the audit report. It is recommended that a firm only engage any single auditing firm for a maximum of six consecutive years to ensure independence.
- Refuse the external auditor/auditing firm's services if the auditor is deemed unqualified to perform the audit services.
- Other obligations in accordance with legal provisions.

9.6.2 Appointment

The ICL does not specify which company organ should be responsible to appoint and dismiss the external auditor. However, the CG Code recommends that for a company with an audit committee, the audit committee should recommend the appointment of an external auditor to the BoC and the final decision be passed by the GMS while taking into account the committee's recommendations.

Best Practice

It is increasingly common for external auditors to be recommended by an independent audit committee of the board or an equivalent body, and to be appointed either by that committee or by shareholders directly.

Moreover, international guidelines such as those set by the International Organization of Securities Commissions recommend that companies guard against the following threats to auditor independence:[223]

- *Self-interest, where an auditor could benefit from a financial or other form of interest in or relationship with the company being audited, e.g., an investment in the company or undue dependence on fees from assurance or non-assurance services*
- *Self-review, e.g., performance of services for an audit client that result in the audit firm auditing its own work*
- *Advocacy, e.g., acting as an advocate for an audit client's position in dealings with third parties*
- *Familiarity, e.g., long association of an audit engagement partner or other key engagement personnel with a particular client, or a recent former partner or senior staff member of an audit firm serving as chief financial officer or in some other key management role at an audit client*
- *Intimidation, e.g., threat of replacement of an auditor over a disagreement on the application of accounting principle*

Any legal entity with a license to perform auditing services can be appointed as an external auditor. However, as mentioned above, the external auditor of a public company must be independent and registered with OJK.

An external audit is served by a public accountant office. A public accountant office is a business entity which obtains its permit from the Ministry of Finance

[223] *Principles of Auditor Independence and the Role of Corporate Governance in Monitoring an Auditor's Independence* (International Organization of Securities Commissions, 2002), 4-5, https://www.iosco.org/library/pubdocs/pdf/IOSCOPD133.pdf.

to deliver its services.[224] The Ministry of Finance sets out several conditions that public accountants must meet in order to be awarded a permit, primarily requirements to comply with the following standards/laws when delivering public accounting services:

- Public Accountant Professional Standards, as enacted by the Indonesian Institute of Certified Public Accountants
- The Code of Ethics of the Public Accountant Profession, as enacted by the Indonesian Institute of Certified Public Accountants
- All laws and regulations relevant to public accountant services[225]

The company must enter into a contract with the external auditor once the GMS has approved the appointment of the auditor. The ICL does not specify who must sign the contract on behalf of the company. However, given that one of the authorities the ICL confers on the BoD is to represent the company, the president director will generally be authorized to sign the contract on behalf of the company. The audit contract will set out the rights, obligations, and duties to be performed by the external auditor and the auditing company, and may also include any additional terms that the parties agree upon.

Best Practice

In the US, the 2002 Sarbanes-Oxley Act prohibits public accounting firms from providing non-audit services to their audit clients. Prohibited services include:

- *Bookkeeping or other services related to the accounting records or financial statements of the audit client*
- *Design and implementation of financial information systems*
- *Appraisal or valuation services, fairness opinions, or contribution-in-kind reports*
- *Actuarial services*
- *Internal audit outsourcing services*
- *Management functions or human resources*

[224] Minister of Finance Regulation No. 154/PMK.01/2017 on Development and Supervision of Public Accountant, Article 2(b).
[225] Minister of Finance Regulation No. 154/PMK.01/2017, Article 3.

- *Broker or dealer, investment adviser, or investment banking services*
- *Legal services and expert services unrelated to the audit*
- *Any other service that the board determines, by regulation, is impermissible.*

An exception to this rule applies should non-audit services that are not listed above be pre-approved by the audit committee. The audit committee should, however, disclose these services to investors in periodic reports. Another exception is made when the non-audit services constitute less than 5 percent of the total amount of revenues paid to the auditor, these services were not recognized to be non-audit services at the time of engagement, and the audit committee promptly approves these services prior to the completion of the audit.

9.6.3 Remuneration

The company pays for the auditor/auditing firm's services. The audit committee (if there is any) must review the external auditor fees and submit its recommendations to the BoC. Importantly, compensation procedures and the amount of compensation must be determined independently of the audit results.

Auditors and audited companies may agree to apply one of the following methods of calculating the auditing service charge:

- Calculating according to working hours of practicing auditors and a charge rate per hour
- Calculating according to the services provided within an agreed charge package
- Calculating according to each auditing service at charge rates in the percentage of the contract or project values
- Calculating under multi-period audit contracts with a fixed charge rate for each period

9.6.4 Reporting

For listed companies, the external auditor will prepare an audit report and submit it to the BoD no later than three months from the end of the financial year. The external auditor presents his/her conclusions on the reliability of the company's financial statements and compliance with accounting procedures. The opinion paragraph of the auditor's report should state the auditor's opinion as to whether the financial statements give a true and fair view (in all material respects) in accordance with the financial reporting framework used by the company and, where appropriate, whether the financial statements comply with statutory requirements. The external auditor must prepare a report on the annual audit that includes:

- Opinions on the accuracy of the company's reports and financial documents
- Information on any found violations of accounting or financial reporting procedures, rules on disclosure, or any other relevant laws and regulations

Best Practice

The external auditor should divulge (potential) errors, misconduct, and violations of regulations or the company's internal rules during audits, and report them immediately to the audit committee or BoC. The external auditor should make the company aware, as soon as practical and at an appropriate level of responsibility, of material weaknesses in the design or operation of the accounting and internal control systems, which have come to the auditor's attention. The audit committee or the supervisory board should take appropriate steps to remedy these problems.

If a company plans to seek access to international capital markets, the external auditor should prepare its report in accordance with the International Standards on Auditing issued by the International Federation of Accountants. The audit report must give an opinion on the financial statements prepared in accordance with the International Financial Reporting Standards (IFRS) adopted by the International Accounting Standards Board.

9.6.5 Liabilities

Indonesian law does not clearly determine the source of liabilities (civil, administrative, or criminal) that will apply to a licensed auditor, and auditors may instead be liable under all three. Because the auditor or auditing firm may potentially be liable for civil, administrative, and criminal infractions, it/he/she should be adequately insured by a reputable (domestic or international) insurance provider with appropriate coverage. As a general rule, insurance should cover risks associated with inaccuracies in the audit opinion, as well as failure to properly apply the International Standards on Auditing and code of ethics for professional accountants.

- **Civil Liability**

  The grounds and terms of civil liabilities are usually specified in the contract between the auditor or auditing firm and the audited company. The licensed auditor or auditing firm must maintain confidentiality regarding the company's operations. If they divulge confidential information, the company may seek compensation for the resulting losses.

- **Administrative Liability**

  Auditing and accounting regulations state that the licensed auditor bears administrative liability if it/he/she conducts certain actions which fall into administrative sanction pursuant to the prevailing laws and regulations in Indonesia regarding public accountants, including manipulating or assisting to manipulate or falsifying data related to the services provided. The administrative sanctions vary from recommendation, written warnings, and penalty, to revocation of licenses.

- **Criminal Liability**

  A licensed auditor may be prosecuted for conducting certain actions which are considered as criminal actions pursuant to the prevailing laws and regulations in Indonesia. One such action is falsifying or manipulating data related to the given services. This may lead to a maximum penalty of five years of imprisonment and fine of up to Rp 300,000,000.

CHAPTER 10
Information Disclosure

THE CHAIRMAN'S CHECKLIST

- Does the company have a written disclosure policy? Does the policy clearly express the company's commitment to transparency? Is the disclosure policy easily available to market participants and other interested parties?
- Does the company fully comply with its legal disclosure obligations? What systems are in place to ensure that the company makes full and timely disclosure of material information?
- Are commissioners and directors entirely aware of the personal and corporate repercussions of false or incomplete disclosure? Do commissioners and directors act accordingly to ensure responsible disclosure?
- Is the company's ownership structure transparent? For companies with a complex ownership structure or acting as a subsidiary in a large conglomerate/business group, are names of individuals who ultimately own or control the company disclosed to the public as beneficial owners?
- What steps are being taken to ensure that the company's financial position is communicated clearly to the markets?

- Is the disclosure fair? For example, does the company ensure that all investors receive information at the same time, not giving special access to a few privileged individuals or institutional investors?
- Does the company have a policy on insider trading and does it enforce this policy? What systems are in place to manage the flow of inside and other sensitive information?
- Does the company understand that it is in its own interest to make voluntary disclosures to the market? If so, how does the company monitor the veracity of this information and ensure that its disclosures are not merely for marketing or public relations purposes?
- Does the company understand the definition of commercially sensitive information? Or does the company hide behind protections provided for sensitive information to withhold material facts from the markets?
- In the case of joint stock companies with capital participation by foreign shareholders, how does the company's disclosure compare to international disclosure requirements, for example, the G20/OECD Principles of Corporate Governance?

There are two basic forms of market regulations: substantive rule-based regulations and disclosure-based regulations. Both regulatory approaches seek to protect shareholders and ensure fair and stable financial markets. Rule-based regulations set down what companies can and cannot do, and seek to establish a wide-reaching set of regulations that cover many potential circumstances. Disclosure-based regulations rely more heavily upon market mechanisms to punish and reward certain types of corporate behavior. Such regulations shift part of the responsibility for protecting investors to market participants, applying the motto *caveat emptor* or buyer beware. Disclosure-based regulations are partly predicated upon the assumption that markets are better at policing corporate misconduct than regulatory agencies and disclosure is an effective and inexpensive substitute for substantive regulations. In practice, the two approaches are almost always used in combination with one another, although some countries rely more heavily on disclosure than others.

For disclosure-based regulations to work effectively, a number of elements and incentives need to work together. These include a proper legal and regulatory environment, combined with effective enforcement mechanisms such as regulators that screen financial information for misstatements and courts that provide effective redress. Independent external auditors also play an important role in providing assurance to the markets, as does an active and interested appraiser that questions company strategies and communications. Finally, a competent and vigilant BoC is crucial. It is broadly accepted that even the best disclosure system cannot thwart individuals who are intent upon defrauding a company and its shareholders. Without a BoC that is uniformly intolerant of obfuscation, a disclosure regime cannot be fully effective.

While disclosure-based regulations may function imperfectly in emerging financial markets, disclosure is critical and only likely to grow in importance in Indonesia as its financial markets mature. Among the broad palette of disclosures, particular importance must be attached to financial and operating results, related party transactions, and ownership structures.

Companies have an obligation to inform the markets in which they operate of all matters relevant to their financial status and business outlook. In the corporate governance context, information disclosure refers to the processes through which a company ensures all interested parties may access relevant corporate information through efficient and transparent procedures.

Access to material information helps to protect shareholder rights by allowing shareholders to assess the company's position and respond to changes that are relevant to their concerns. Disclosure also benefits companies by allowing them to demonstrate corporate responsibility toward shareholders, act transparently towards the markets, and maintain public confidence and trust. Finally, transparency and disclosure fill information gaps for investors, creditors, suppliers, customers, and employees and, as a result, can have a positive impact on a company's revenues or its access to human and financial capital.

10.1 Regulatory Framework

In Indonesia, the primary legal instrument that regulates disclosure and reporting obligations of issuers, public companies, and all other supporting institutions and professions that support the country's capital markets is Law No. 8 of 1995 on Capital Markets.

The Capital Markets Law states that the primary obligation of public companies and all other capital market-related institutions is to disclose *material information* within prescribed timeframes. Material information is a specific legal term that means any important and relevant fact concerning events or data that may affect the price of a company's securities, and may therefore impact investment decisions and share prices. Bankruptcy filings, a change in BoC, BoD, or other corporate officers, plans for merger, acquisition, consolidation or spinoff are all examples of material information.

Supplementing these obligations, OJK also sets out a number of additional requirements under the following regulations:

1. OJK Regulation No. 11/POJK.04/2017 on Shareholding Report or Any Change of Shareholding in Public Companies
2. OJK Regulation No. 31/POJK.04/2015 on Disclosure of Information or Material Facts by Issuing Companies or Public Companies
3. OJK Regulation No. 29/POJK.04/2016 and Circular Letter of OJK No. 30/SEOJK.04/2016 on Annual Report of Issuing Companies or Public Companies
4. Decision of the Chairman of the Capital Market and Financial Institutions Supervisory Agency No. KEP-346/BL/2011 dated July 5, 2011 on Periodical Submission of Financial Statement by Issuing Companies and Public Companies (OJK Regulation Number X.K.2)

Best Practice

The following principles provide a foundation for strong information disclosure practices:

- *Information should be provided on a regular and timely basis.*
- *Information should be easily and broadly available.*
- *Information should be accurate, complete, and reliable.*
- *Information should be consistent, relevant, and properly documented.*

10.2 Information Classification

10.2.1 Confidential Information

As a signatory to the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS),[226] Indonesian regulators recognize that some forms of business-information may be commercially sensitive. Indonesia addresses these issues and its obligations under the TRIPS Agreement through Law No. 30 of 2000 on Trade Secrets. The law defines trade secrets consistently with the relevant definition under the TRIPS Agreement, as information in the field of technology and/or business that has economic value, which is not known by the public, and where the owner of the information takes steps to maintain its confidentiality.[227] Examples include technical and scientific information such as formulae, manufacturing methods and specifications, designs and computer coding, as well as commercial and financial information such as customer lists, customer buying preferences and requirements, pricing information, marketing and business plans, supplier arrangements, internal cost structures, and other similar non-public information.[228]

To meet the full criteria for 'trade secrets' that the law protects, information must:

- Be confidential in the sense that it is known only by certain people, or such information is not known by the public in general
- Have economic value with the capacity to generate economic benefit to the owner's business interests
- The owner of the information, or parties which control it, must have made necessary and appropriate effort to protect its secrecy.

[226] Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1C, 1869 U.N.T.S.299 (TRIPS Agreement).
[227] Law No. 30 of 2000 on Trade Secrets, Article 2.
[228] *TRIPS Agreement*, Article 39(2).

Companies should be clear on what truly constitutes confidential information and should not interpret the broad definitions provided by law so widely as to withhold relevant information from investors. Companies are well advised to develop written policies and procedures, and define what should be considered confidential in their internal regulations. For example, they can consider personal data as confidential information, and forbid the collection, storage, usage, and dissemination of private information without the person's consent, unless otherwise provided by a court decision.

10.2.2 Insider Information

Insider trading occurs when someone closely connected to a company (such as a commissioner, director, or employee) utilizes inside material or non-public information to benefit him/herself when buying/selling securities in the company. It is important to distinguish insider trading from the common practice for company directors, managers, and employees to buy or sell shares in their own companies, which is permissible in Indonesia so long as the seller discloses these transactions to OJK in accordance with its procedural requirements.

Insider trading, on the other hand, potentially allows company insiders to make profits or avoid loss at the expense of other market participants, and undermines the transparency and credibility of the capital market system.

Indonesia responds to these problems under the Capital Markets Law, which sets out the definitions and sanctions that apply for trading using inside information.

The Capital Markets Law defines inside information as material information of a precise nature relating to a public company that is not made public, and which can, directly or indirectly, significantly influence the trade of the securities or the

share prices of the company on the market. The law defines an insider broadly as:[229]

- Commissioners, directors, or company employees
- Substantial shareholders
- Individuals who have access to insider information due to their professional or business relationship with the company (such as accountants or lawyers)
- Any individual who falls in these categories within the last six months

The law prohibits any insider meeting the above criteria from buying or selling securities in a company to which they are connected, as well as from trading in securities of any subsidiaries or otherwise connected/related companies. The law also prohibits insiders from influencing any person to buy or sell the securities in the relevant company/companies, and from providing insider information to third parties.[230] Criminal sanctions including imprisonment for up to ten years and a fine apply to any person guilty of these acts.

Best Practice

Disclosure of inside information may substantially affect the market value of shares and other securities of a company. Therefore, persons may not use inside information to which they have access to execute transactions, nor may they transfer inside information to a third party. Illegal use of inside information can damage shareholder interests and adversely affect not only the financial status and reputation of the company involved, but also the securities markets more broadly. The company should have a written policy on insider dealing in place and vigorously enforce it. The internal auditor of the company should monitor whether directors, managers, and other officers comply with the law, regulations, and internal rules on insider dealing.

[229] Capital Markets Law, Article 95 and Elucidation of Article 95.
[230] Capital Markets Law, Article 96.

10.2.3 Disclosure Versus Transparency

Disclosure is sometimes confused with transparency. Companies may disclose an enormous amount of information that is of no value to the users of such information while withholding important data. Disclosure can be irrelevant or, worse, manipulated in such a way as to conceal the true state of the enterprise. For example, while many companies disclose their ownership as required by law, the true owners and the extent of their control may remain hidden behind complex legal structures such as special purpose entities and off-shore holding companies. A strong disclosure regime that promotes real transparency is a pivotal feature of market-based monitoring of companies and is central to shareholders' ability to exercise their ownership rights on an informed basis.

10.2.4 Liabilities for Non-Disclosure

As a rule, companies that provide information that is false, incomplete, or distorted will be liable for damage caused to shareholders and investors. Besides the company, all persons involved in the preparation or disclosure of such information will also be liable if they either knew, or, by the nature of their work, ought to have known the information to be false. For example, the president director, the chief accountant or the person fulfilling this function, and the external auditor will be deemed responsible. They are jointly and severally liable with the issuer for any damage caused to investors because of untruthful, incomplete, or misleading information. If investors believe that they have suffered damages, they can file claims with a court.

Organizations and individuals who violate legal provisions on information disclosure shall, depending on the nature and severity of their violation, be disciplined, administratively sanctioned, or examined for penal liability. If damage is caused, they must pay compensation in accordance with the law. Sanctions that apply to violations of information disclosure regulations may be warnings, fines, or imprisonment (depending on the impact and severity of the breach). The maximum penalty for violations that cause significant harm will be a ten-year prison sentence and/or fine of up to Rp 15,000,000,000.

10.3 Disclosure Items

The OECD Principles of Corporate Governance recommend that companies make timely and accurate disclosure of all material matters, including financial situation, performance, ownership, and governance of the company.[231] The key concept that underlies the OECD recommendation is that of materiality, meaning the extent to which information or an event will impact a company's share price and therefore affect investors' decisions. The principle of materiality sets boundaries around the scope of information that companies must disclose. The concept recognizes that disclosure obligations which are too onerous (for example, by forcing companies to disclose information beyond that which is relevant to shareholders, investors, and the market) may impose excessive administrative costs that adversely impact business.

Whether information is material to a company's operations depends on a range of factors, including its business activities, company size, and ownership structure. For example, damage of Rp 130 million (~$9,100) worth of paper in a multi-million dollar publicly traded company will be of little importance to the investor. It may, on the other hand, be material to a small family-owned print shop. Consequently, materiality is a relative concept that is often difficult to define with great precision. Companies and auditors sometimes apply certain numerical thresholds (for example, corporate events that cost the company 5 percent or more of its earnings) to simplify its application. However, these thresholds can only serve as a starting point for a more rigorous application of the concept of materiality.

In Indonesia, disclosure requirements for listed companies differ from those of public (non-listed) and private companies, where more stringent rules apply to listed and non-listed public companies. This is due to the typically widely-dispersed ownership base that public companies hold and therefore the number of shareholders that these companies are accountable to. Private companies that do not rely on the public for investment usually need only comply with minimal disclosure requirements and are not subject to OJK reporting obligations.

Indonesian regulations apply the concept of materiality by requiring listed companies to provide to the public, in addition to mandatory minimum informational requirements, information on all other matters relevant to

[231] *G20/OECD Principles of Corporate Governance*, 41.

understanding the company's legal, financial, and profit status. As such, companies themselves must assess matters and litigation that may significantly affect the price of securities and provide those assessments to the public.

OJK requires public companies to disclose all material information regarding events that may affect investors' decisions or the company's share prices as soon as possible, and no later than the second working day after the event occurs. Companies must announce this information publicly as well as report it directly to OJK. Examples of events, information, or material facts that companies must disclose are:[232]

- A merger, spinoff, consolidation, or joint venture
- An offer to purchase another company's listed shares
- Distribution of interim dividends
- Listing or de-listing of shares on the stock exchange
- A share split or combination of shares
- Entering into or disposition of an important contract/agreement
- New findings, products, or other inventions that affect the company's value
- Change in the composition of the BoC or BoD
- Sale/purchase of material assets
- Any dispute against the company, its BoC, or BoD, as well as any labor disputes that may disrupt business activities
- Replacement of a company's auditor
- Replacement of a trustee (*wali amanat*)
- Replacement of a Securities Administration Bureau (*Biro Administrasi Efek*)
- Significant changes reported in the company's annual financial statement for any particular year
- Debt restructuring
- The company comes under the supervision of a regulatory agency
- A regulatory agency imposes restrictions on the company's business activities
- Any other material event which may give rise to additional financial obligations or otherwise disrupt the company's revenue stream

[232] OJK Regulation No. 31/ POJK.04/2015 on Disclosure of Information or Material Facts by Issuing Companies or Public Companies.

The OECD Principles call for disclosure of all material information in the following areas:[233]

- *Financial and operating results*
- *Company objectives and non-financial information*
- *Major share ownership, including beneficial ownership and voting rights*
- *Information about board members, including their qualifications, the selection process, positions on the boards of other companies, and whether or not they are regarded as independent*
- *Remuneration of board members and key executives*
- *Foreseeable risk factors*
- *Governance structure and policies, including the content and implementation of any corporate governance codes/ policies*
- *Issues regarding employees and other stakeholders*
- *Related party transactions*

The following section provides details on recommended disclosure items based on the OECD Principles.

10.3.1 Financial and Operating Results

Information about financial results, performance, and operations of the company is of utmost importance to shareholders, potential investors, creditors, and other stakeholders. The following list sets out the most typical forms of financial reporting:

[233] *G20/OECD Principles of Corporate Governance*, 41-46.

- **The balance sheet** provides a snapshot of the company's assets, capital, and liabilities on a particular date. To skilled analysts, it presents important information on the degree of risk an investment in the company carries, such as by indicating the company's ability to pay creditors.
- **The income statement** provides information on the company's performance during a specified period. Income statements may be organized in different ways. Standard practice in most jurisdictions requires income statements to show: 1) revenues or sales, 2) results of operating activities, 3) financing costs, 4) income from associates and joint ventures, 5) taxes, 6) profit or loss from ordinary activities, and 7) net profit or loss. The income statement demonstrates business sustainability.
- **The cash flow statement** illustrates a company's sources and uses of cash. It lists all changes affecting cash in operations, investments, and financing. For example, a manufacturing company's net operating income will show as a positive credit in cash, the purchase of a production plant will be an investment that decreases cash, and the issuance of shares or bonds is a financing activity that will show as an increase in cash.
- **Explanatory notes to the financial statements** help explain the company's financial statements by providing important details and insights into how the company prepared its accounts. It also briefly describes features of the company's activities, its main performance indicators, and factors that affect the company's financial results as well as decisions on financial statements and distribution of net profit reviews. The notes to the financial statements also provide information that enable users to receive a complete and objective picture of the company's financial condition, financial results for the reporting period, and any changes in its financial position. These notes must specifically state the contents of related party transactions in accordance with Indonesian Financial Accounting Standards (*Peraturan Standar Akuntansi Keuangan* or PSAK). This section also contains, when required, the statement of changes in owners' equity that shows all changes to the AoA, additional paid-in and reserve capital, as well as retained earnings. In addition, it provides information on changes in statutory and additional funds and briefs on net assets.
- Finally, **the external auditor's report** allows an independent external auditor to express an opinion on whether or not the company's financial statements are prepared, in all material respects, in accordance with an identified financial reporting framework and whether they are reliable. This provides shareholders, managers, employees, and market

participants with an independent opinion about the company's financial position and, if performed properly, should attest to the accuracy of the statements. The annual financial statements of all public and listed companies must be audited by an independent and eligible audit firm. Annual audited financial statements must be submitted to the GMS for approval.

Best Practice

International best practice also calls for management's discussion and analysis (MD&A), which provides management's view on the company's performance and future prospects. The MD&A, which is typically disclosed in the company's annual report, should:

- *Complement as well as supplement financial statements*
- *Have a forward-looking orientation*
- *Focus on long-term value creation*
- *Integrate long and short term perspectives*
- *Present information that is significant to the decision-making needs of users*
- *Embody the qualities of reliability, comparability, consistency, relevance, and understandability.*

The MD&A presents a more analytical and qualitative view than the rest of the financial statements.

Preparing Financial Information

Regulations, accounting standards, and other standards will determine the specific content and format of financial statements. Taken together and compared over time, financial statements should provide a well-rounded picture of the company's operations and financial position. Companies should implement the following principles when preparing their financial information:

- ***Accrual based accounting***

  This accounting method enters revenue and expenses into company records at the time they accrue, not only at the time of payment or receipt

of funds.

- *Going concern*

  Financial statements are prepared on the assumption that the company is a going concern, meaning that it is operating and will continue to operate for the foreseeable future. The going concern principle assumes that the company has neither the intention nor obligation to liquidate or materially curtail the scale of its operations. It is the responsibility of the company's managing bodies, primarily the BoD, to assess the entity's ability to continue as a going concern. This may not always require detailed analysis, particularly when the company has a history of profitable operations and ready access to financial resources.

- *Consistency*

  Companies should maintain a consistent format in how they present and classify information from one period to the next, unless change is required either due to the company's circumstances or under new accounting regulations/standards.

- *Separation of assets and liabilities*

  Assets (fixed and current) and liabilities (debt payables and equity of owners) should be recorded separately from those of the company's owners and other organizations.

- *Completeness of information disclosure*

  Financial statements should disclose all material business facts that may have an impact on the economic decisions of those who use and refer to these documents. An omission of such information may cause the records to be false or misleading, and therefore unreliable.

- *Timeliness*

  Companies need to publish reports in reasonable time, for information that is up-to-date will have far greater value to users than older information that may be irrelevant due to superseding events. For public companies where a public accountant must audit the financial reports, companies should publicize these reports no later than seven days after the GMS ratifies them.

- *Conservatism*

  Companies should make their accounting choices deliberately and with

prudence, estimating when future events may negatively impact their financial conditions.

- *Substance over form*

  Companies should record transactions and events in a manner that accurately reflects their substance and economic realities (which should prevail), not merely their legal form.

- *Balance between costs and benefits*

  Given the complexity and breadth of certain reporting requirements, this principle allows smaller companies to tailor their financial information to be cost-effective. This concept, however, should not be used to deny information to those with a right to receive it (such as company shareholders, investors, and other interested parties). The presumption must be that information required by law and accounting standards should be provided to users unless there is a clear indication that the cost of doing so outweighs the value or benefit of the information for interested parties.

- *Matching*

  Expenses should be matched to the appropriately related revenues when determining earnings for the period.

Best Practice

To access international capital markets or improve the quality of their financial reporting, companies should prepare their financial statements according to an internationally accepted body of accounting standards. The most widely recognized standards are the International Financial Reporting Standards (IFRS)[234] and US Generally Accepted Accounting Principles (US GAAP).

In addition to standard financial reporting according to the PSAK, a company may consider reporting in accordance with IFRS for the following reasons:

- *IFRS has clear economic logic and provides better information to management than the current Indonesian*

[234] Details on IFRS Conceptual Framework are available at *IFRS Standards and IFRIC Interpretations*, http://www.ifrs.org/issued-standards/.

accounting standards.

- *There is global convergence of national standards towards IFRS.*
- *Unification of standards will allow users of financial statements to "read" all financial statements under common rules.*
- *Implementing IFRS could help Indonesian companies decrease the expenses of attracting investment.*

Applying IFRS typically has the following impact on the balance sheet of a standard Indonesian company:

- *The need to prepare consolidated financial statements*
- *Inventories can no longer be generally carried at cost, but at the lower cost or net realizable value*
- *A significant change in the value of fixed assets*
- *Use of a fair market valuation rather than the historical cost approach for many assets and liabilities*
- *The appearance of new financial instruments, particularly derivatives*
- *Recognition of assets and liabilities, the control over which does not stem directly from participation in equity*
- *Additional items are included in the income statement, such as fair value adjustment for financial instruments and recognition or recovery of asset impairment, among others. Disclosures also become more informative and user-oriented.*

Disclosing Financial Information

Indonesian companies will typically need to present their financial information in different forms and at different times throughout the financial year. Financial and operating results will appear in the prospectus, annual report, and annual, semi-annual, and quarterly financial statements.

The ICL requires all companies to disclose their annual audited financial statements no later than seven days after the GMS ratifies these documents.[235]

[235] ICL, Article 68(5).

Companies should complete their annual financial statements and include them in the annual reports no later than six months from the last day of the annual accounting period.[236] To ensure investors' access to the annual financial statements, companies must produce these documents in Bahasa Indonesia (accompanied by an English translation if applicable), publish them in print as well as on the company's website, and archive the print version at the company's head office. Finally, public companies must disclose all content and information relevant to the annual financial statements at OJK and IDX's electronic disclosure centers, and publish the full text of the auditors' report (as a part of the audited financial statements) in at least one edition of a Bahasa Indonesia newspaper with national circulation.

Public companies must disclose additional financial information as follows:[237]

- Semi-annual financial statements should be presented in comparison with the same period during the previous year, except that the semi-annual balance sheet should be compared to the balance at the end of the previous year.
- Semi-annual financial statements should be submitted to OJK and the public within the following period: (i) not more than one month after the date of the semi-annual financial statements, if audited; (ii) not more than two months after the date of the semi-annual financial statements, if the statements are undergoing an audit; and (iii) not more than three months after the date of the semi-annual financial statements, if the statements are accompanied by an accountant's audit.
- Public companies must disclose semi-annual financial statements at OJK and IDX's electronic disclosure centers, publish them in print as well as on the company's website, and archive the print version at the company's head office.

Banks have additional obligations to submit financial reports at regular and pre-determined intervals (monthly, quarterly, annually, and at other times when directed). The BoC and BoD of banks are primarily responsible for ensuring these reports are complete and correct.[238] The monthly and quarterly publication reports should include financial statements that provide:[239]

- Balance sheet
- Statement of loss and profit and other comprehensive income

[236] ICL, Article 66(1).
[237] Decision of the Chairman of the Capital Market and Financial Institutions Supervisory Agency No. KEP-346/BL/2011 on Periodical Submission of Financial Statement by Issuing Companies and Public Companies, Article 3.
[238] OJK Regulation No. 6/POJK.03/2015 on Transparency and Publication of Bank Reports, Article 3.
[239] OJK Regulation No. 6/POJK.03/2015, Article 8.

- Commitment and contingency report

In addition to the above, the quarterly publication report must contain information on (i) financial performance; (ii) shareholding structure; (iii) for Sharia commercial banks, the structure of the BoC and BoD, as well as of the Sharia supervisory board; and (iv) any other information as required by OJK.[240] Further, it should also contain information on the bank's capitalization, following international standards under Basell III, the international regulatory framework for banks.

Banks must publish both their monthly and quarterly publication reports on their websites. The quarterly report must also be published in at least one Indonesian language newspaper and submitted to OJK.[241]

Annual publication reports must contain not only financial statements and information on financial performance, but also general information; disclosure on capitalization, risk management, and risk mitigation practices; other disclosure pursuant to financial accounting standards; and any other relevant information determined by OJK.[242] Banks must present their annual financial statements as part of the annual publication report and provide both (i) individual financial statements and (ii) consolidated financial statements.[243]

The annual publication report must also cover information pertaining to their business groups and subsidiaries.[244] This additional information should at least include:

1. Business group structure
2. Any transactions between the bank and its affiliated parties
3. Transactions in the field of finance between any entity within the bank's group structure and affiliated parties
4. Fund provisions, commitments, and other facilities provided by any entity within the banking group to debtors or other parties who have obtained finance from the bank
5. Consolidated disclosure on capitalization, risk management practice, loss potential, and risk mitigation
6. Any restrictions, limitation, or other significant obstacles to the transfer of funds required to meet OJK's capitalization requirements

[240] OJK Regulation No. 6/POJK.03/2015, Article 13.
[241] OJK Regulation No. 6/POJK.03/2015, Article 18(1) and 20(1).
[242] OJK Regulation No. 6/POJK.03/2015, Article 24(1).
[243] OJK Regulation No. 6/POJK.03/2015, Article 27.
[244] OJK Regulation No. 6/POJK.03/2015, Article 26.

Financial Information in a Corporate Group

Finally, a crucial component to ensure transparency in the context of a corporate group is for all subsidiary companies to make full disclosure of all intra-group relations, transactions and their financial terms, and consolidated accounts. Indonesian regulations also require companies to prepare consolidated financial statements in addition to individual financial reports on all subsidiary companies within the group. This data will form an integral component of the prospectus documents.

Best Practice

When preparing consolidated accounts, companies should follow uniform accounting policies for the parent and its subsidiaries or, if this is not practical, the company must disclose the proportion of items in the consolidated financial statements in which different accounting policies have been applied. In the parent's separate financial statements, subsidiaries may be shown at cost, at re-valued amounts, or using the equity method. IFRS stipulates that a company's consolidated accounts should include at least:

- *The name, ownership, and voting percentages for each significant subsidiary*
- *The reason for not consolidating a subsidiary*
- *The nature of the relationship if the parent does not own more than 50 percent of the voting power of a consolidated subsidiary*
- *The nature of the relationship if the parent owns more than 50 percent of the voting power of a subsidiary excluded from consolidation*
- *The effect of acquisitions and disposals of subsidiaries during the period*
- *In the parent company's separate financial statements, a description of its methods for monitoring the accounts of subsidiaries*

10.3.2 Company Objectives

It is important for markets, shareholders, and other stakeholders to be aware of the company's objectives. Company objectives (such as the issuance of securities, acquisition plans, replacement and sales of assets, or research and development) should be disclosed in the prospectus. In addition, quarterly (or semi-annual) reports should contain forward-looking information including sources of revenue, plans for new production, expansion or reduction of production, new product development, substitution of old products, modernization or repair of fixed assets, and modification of company activities. In addition, the annual report should outline the company's position in the industry, priority areas of activity, and development trends.

10.3.3 Major Share Ownership and Voting Rights

Shareholders should be informed about the company's ownership structure to enable them to understand their rights, role, and authority in governing the company and influencing its policy. Depending on the size of ownership, shareholders have various degrees of influence over decision-making in a company. Indonesian legislation (as in many other jurisdictions) provides greater rights to shareholders with larger shareholdings and a company's AoA may also confer additional rights on major shareholders.

For investors and others with interests in a company, it is vital to know who is in a position to make (or influence) decisions, such as major shareholders with significant voting power. Under Indonesian regulations, a public company must submit a monthly report of its shareholders no later than the 12th day of the following month. The report must contain the following information:[245]

- Names and addresses of the controlling shareholders and their total number of shares
- Names and addresses of all shareholders who own 5 percent or more of the company's shares and their total number of shares
- The total number of shares owned by the company's BoC and BoD
- Total number of shareholders

[245] Decision of the Board of Directors of Jakarta Stock Exchange No. KEP-306/BEJ/07-2004 Rule I-E on Obligations Concerning Information Disclosure, Article III.3.4.2.

Best Practice

Companies seeking to disclose their ownership structure may wish to follow examples under US and EU regulations. US regulations define a beneficial owner as any person who, directly or indirectly, through any contract arrangement, understanding, relationship, or otherwise has or shares:

- *Voting power, which includes the power to vote or to direct the voting of such a security; and/or*
- *Investment power that includes the power to dispose, or direct the disposition of such security*

US securities law states that any person who is directly or indirectly the beneficial owner of more than 5 percent of any equity security of a class, shall notify the issuer and each exchange where the security is traded of such acquisition within ten days, as well as of any increase or decrease by 1 percent of more. If the beneficial owner acts in concert with other institutions or persons, their names and the relationship with the beneficial owner must be disclosed.

The EU Transparency Directive of 2004 provides a framework for disclosure. In summary:

- *Article 9 stipulates that investors must disclose the acquisition or disposal of major shareholdings in public companies based on thresholds starting at 5 percent and continuing at intervals of 5 percent up to 30 percent of voting rights, charter capital, or both.*
- *Article 11(2) shortens the reporting obligation of the acquirer to the company and the competent regulatory authority from seven calendar days to five business days on the one hand and, on the other, of the company to the public from nine calendar days to three business days.*
- *Article 2 extends the definition of "security holder" to include custodians and those holding securities for clearing and settlement purposes.*

- *Article 11(5) extends notification requirements to various classes of shares, such as warrants and convertible bonds if the holdings reach or fall below the thresholds defined in Article 9.*

All member states have introduced this directive by law or regulation. In addition, the EU Takeover Bids Directive regulates transparency issues, including the disclosure of beneficial ownership structures. Public companies in the EU must disclose relevant information in their annual reports on, among other things:

- *The structure of their capital*
- *Any restrictions on the free transferability of securities*
- *Significant direct and indirect shareholdings (including pyramid schemes and cross-shareholdings)*
- *The holders of any securities with special control rights*
- *The system of control of any employee share scheme where the control rights are not exercised directly by employees*
- *Restrictions on voting rights*
- *Shareholder agreements that are known to the company*
- *The rules governing the appointment and replacement of board members*
- *Significant agreements made by the company that take effect upon a change of control*

Indonesian companies that wish to demonstrate their responsibility and adherence to good corporate governance practices should disclose their ownership structure, including information on beneficial owners, in a transparent manner.

Indirect Control and Beneficial Ownership

Shareholders that own less than a majority of shares can exercise indirect control over the company through pyramid structures or cross shareholdings. Any existing related parties may also influence a company's control structure.

Beneficial ownership is a legal term that refers to any person or entity that enjoys the benefit of property (including ownership of securities in a company), where another person is the legal or registered owner. The consequences of beneficial ownership came to the fore of public dialogue in 2016 with the so-called "Panama Papers". The leak of over 11.5 million confidential documents from a law firm in Panama revealed the extent to which powerful individuals had used elaborate corporate ownership structures to conceal personal wealth.[246] In Indonesia, there are several different definitions of beneficial ownership. For instance, in the capital markets sector, OJK defines a beneficial owner as any person who (whether directly or indirectly through legal agreement or any other means):[247]

- Is entitled to and/or receives certain benefits associated with:
    1. A securities account in a financial services provider (such as a trading company, investment manager, or custodian) in the capital markets sector, or
    2. A business relationship with a financial services provider in the capital markets sector
- Is the ultimate owner of funds and/or securities listed in the financial services provider's account
- Controls a client's (or natural person's) transactions
- Gives authority to conduct transactions, and/or
- Controls the transactions of a client that is a legal entity

Indonesia's anti-money laundering laws and OJK and Bank Indonesia regulations currently implement strong know-your-customer provisions that require financial institutions and listed companies to scrutinize and verify supporting documents to identify customers.[248] However, these regulations do not apply to all companies. Further, Indonesian law does not recognize the concept of nominee shareholders and directors generally, such that the registered legal owner is automatically understood to be the legal owner. In Indonesia, the MOLHR maintains a company register that records information of all registered companies (including non-listed companies). The company register includes each company's name, address, business activities, details on shareholders and ownership structure, details on members of the BoC and BoD,

[246] For further detail, see: *Focus 14: Disclosure of Beneficial Ownership after the Panama Papers* published by IFC Corporate Governance Knowledge Publication.

[247] OJK Regulation No. 22/POJK.04/2014 on Know Your Customer Principles for Financial Services Providers in the Capital Markets, Article 1(10).

[248] Law No. 8 of 2010 on Countermeasures and Eradication of Money Laundering; Law No. 9 of 2013 on Prevention and Suppression of Terrorist Financing; Bank Indonesia Regulation No. 14/27/PBI/2012 on Implementation of Anti-Money Laundering and Combating the Financing of Terrorism Program for Commercial banks; OJK Regulation No. 22/POJK.04/2014 on Know Your Customer Principles for Financial Services Providers in the Capital Markets.

and audited balance sheet. This information is available online for a nominal fee. However, the MOLHR does not have enforcement powers to ensure the data in the company register is correct or to scrutinize information provided to identify potential nominee shareholders and other forms of beneficial ownership structures.

Best Practice

The G20 High-Level Principles on Beneficial Ownership Transparency[249] *recommend that countries develop a strong and clear definition of beneficial owner that captures the natural person(s) who ultimately own or control the legal person or arrangement. The G20 Principles cover the following elements:*

- *The definition of a beneficial owner*
- *Risk assessments relating to legal entities and arrangements*
- *Beneficial ownership information of legal entities*
- *Access to beneficial ownership of legal entities*
- *Beneficial ownership information of trusts*
- *Access to beneficial ownership of trusts*
- *Roles and responsibilities of financial institutions and businesses and supporting professionals*
- *Domestic and international cooperation*
- *Beneficial ownership information and tax evasion*
- *Bearer shares and nominees*

The G20 Principles recommend that a beneficial owner should be defined as "a natural person who directly or indirectly exercises ultimate control over a legal entity of arrangement," and that ownership ought to be interpreted widely to cover control through other means in addition to legal ownership.

Importantly, the G20 Principles emphasize the need for companies to collect and maintain information on their ultimate beneficial

[249] *G20 High-Level Principles on Beneficial Ownership Transparency* (The World Bank and UNODC, 2015), https://star.worldbank.org/star/resource/g20-high-level-principles-beneficial-ownership-transparency.

owners. For example, in 2016 the United Kingdom amended the Companies Act 2006 to include new provisions requiring companies to obtain information on beneficial ownership by shareholders, and for all nominee shareholders in turn to inform the company if he/she owns shares on behalf of a third person.[250] *The United Kingdom also requires companies to register these details with Companies House, the government's registrar of companies, enabling the government to maintain records of beneficial ownership information.*

Shareholder Agreements and Voting Caps

Shareholders agreements and voting caps can also have an impact on a company's control structure. Shareholder (voting) agreements typically oblige parties to vote as a block and may give first-refusal rights for the purchase of shares. Shareholder agreements can cover many issues, such as which candidates to nominate for the BoC/BoD, and are clearly of material interest to shareholders. While difficult to detect, companies should make reasonable efforts to obtain information about the existence of shareholder agreements and disclose such information to all shareholders. In principle, parties to shareholder agreements should voluntarily disclose this information themselves.

Voting caps limit the number of votes that a shareholder may cast regardless of the number of shares he/she owns. As such, caps go against the principle of one share, one vote and control that is proportional to ownership. Companies typically use voting caps to entrench the positions of either existing controlling shareholders or management, and these will rarely be supported by good faith investors. The ICL implicitly prohibits voting caps by adopting the mandatory one share, one vote principle.

10.3.4 Information on Commissioners and Directors

For investors and shareholders to be able to appropriately evaluate the capabilities and qualifications of BoC and BoD members, it is important they have access to all relevant information on these members. Companies should

[250] UK Companies Act 2006, Part 21A.

disclose details on their BoC and BoD members' educational background, current occupation, and professional experience, and make these details readily accessible to interested parties. It is also important that shareholders and investors have access to information relevant to any (existing or potential) conflicts of interest that may affect the independence and decision-making capacity of the BoC and BoD.

Companies should disclose additional board memberships or professional commitments currently held by each board member so that shareholders can assess whether the BoC and BoD dedicate sufficient time to their duties and properly carry out their responsibilities. Accordingly, companies should disclose all BoC and BoD meeting attendance records. Another important related disclosure is the selection criteria and processes to nominate and appoint BoC and BoD members, including the role of the nomination and remuneration committee in vetting the candidates and making recommendations to the GMS.

Best Practice

Disclosure requirements mandated by law generally fall short of best practices. In the interests of genuine transparency, companies should also disclose the following information in their annual reports:

- *Any key officials in the company beyond BoC and BoD members, including their curriculum vitae*
- *Information about all transactions between these key officials and the company*
- *Age, profession, employment, and citizenship of each member of the BoC and BoD, as well as all other positions, date of initial appointment, and their current appointment term*
- *Information on all claims filed in courts (or arbitration tribunals) against BoC and BoD members*

Indonesian law requires companies to disclose the remuneration paid to each individual member of the BoC and the BoD over the relevant financial year as a separate item in the company's annual financial statements, and report this at

the annual GMS. Remuneration packages for commissioners of listed companies in Indonesia tend to be among the highest in Southeast Asia. One likely explanation is because commissioners tend to be influential individuals, such as founders or major shareholders in the company or affiliated parties, or ex-high ranking government officials.

In light of this reality, to prevent conflicts of interest between commissioners and shareholders and other stakeholders, listed companies in Indonesia should disclose not only the remuneration paid to each commissioner in their annual financial statements, but also the company's processes for approval of BoC remuneration. Companies may improve transparency even further by also providing an explanation of how the company aligns its remuneration policies with peer companies in the relevant industry or sector.

Best Practice

Companies should provide shareholders with a clear and comprehensive overview of their remuneration policy. Disclosure of remuneration policy allows shareholders and investors to assess the main parameters and rationale for different components of the remuneration package and the linkage between remuneration and performance. Such disclosure aims to strengthen the company's accountability to shareholders. The remuneration policy should be part of an independent remuneration report or be included in the annual financial statements or the notes to the financial statements, as well as in the company's annual report. The remuneration policy should also be posted on the company's website.

Companies should also be transparent about the methods for determining remuneration. The criteria for determining the amount of remuneration for members of the BoC/BoD, as well as the total amount of remuneration paid or to be paid depending on the results of the reporting year, should be disclosed in the annual report. The methods for determining remuneration are usually an integral part of the remuneration policy.

For example, a large majority of EU member states have

introduced high disclosure standards with regard to the remuneration of individual board members and key executives, putting shareholders in a better position to assess the extent to which an individual's remuneration is justified in view of his/her responsibility and performance. It also allows shareholders to hold board members and executives fully accountable for the performance of their duties.

- *With respect to executive remuneration plans, shareholders and investors should have sufficient information to properly assess the costs and benefits to the company and the relations between the performance of the company, on the one hand, and the level of executive remuneration on the other.*
- *At some point, the independence of non-executive directors may be compromised if they earn a significant amount of their total income from board activities. Some countries have monetary thresholds that serve as convenient "rules of thumb" or warning signals. While numerical thresholds may be a reasonable starting point, judgments on independence require a much more sophisticated analysis. The disclosure of a non-executive director's remuneration (or an independent commissioner) remains critical to assess the extent to which his/her independence may be compromised.*

10.3.5 Material Foreseeable Risk Factors

Consideration of risk (along with return) is an important concern for any investor. Foreseeable risk factors may include risks specific to certain industries, for example, employee strikes will have greater impacts on manufacturing and other industries heavily dependent on manpower. Other sources of risk may be driven by factors related to regulatory changes, political circumstances, commodities pricing, environmental factors, market conditions, or interest and currency fluctuation risks.

Risk is, by its very nature, forward looking and extremely difficult to quantify. Nevertheless, specific industry, financial, and legal risks as well as other material risks need to be disclosed in prospectus documents. As part of their obligation to prepare publication reports, banks are also required to disclose capitalization and management risks.[251] Banks must also submit a second report that covers (i) credit base interest rates, (ii) material information and facts, and (iii) any other information as necessary.[252]

10.3.6 Corporate Governance Structures and Policies

When assessing a company's governance structure, market participants may want to obtain information on the company's governing bodies, including the division of authority between shareholders, commissioners, and directors, as well as the company's corporate governance policy, its commitment to corporate governance principles, and compliance mechanisms.

Commitment to Corporate Governance

Markets have a keen interest in companies' level of commitment to good governance practices. They are concerned with whether a company sees governance as a public relations, box-ticking, window-dressing exercise, or whether it is in fact willing "to do right" by shareholders and implement real change whenever necessary and appropriate. While good disclosure, in and of itself, is not sufficient to consistently and uniformly ensure good corporate governance, it is clearly one way of demonstrating the commitment a company is willing and able to make to its shareholders and stakeholders.

Corporate Governance Structures

Companies must describe their governance structures, including the authority of each governing body and internal control mechanisms, in their prospectus and annual reports. Also, companies should regulate and make publicly available through their internal documents the procedures for convening and conducting the GMS and make GMS decisions publicly available through material events reports.

[251] OJK Regulation No. 6/POJK.03/2015, Article 24(1d) and 26(e).
[252] OJK Regulation No. 6/POJK.03/2015, Article 33(1).

Corporate Governance Policies

The AoA is a document that sets the rules and procedures of a company's governance system and should be made publicly available. Company-level corporate governance codes also serve to highlight general corporate governance concepts and structures. Internal regulations provide more detailed guidance on processes. Companies should make this information readily accessible to interested parties at minimal cost.

Best Practice

Corporate governance best practice recommends that companies develop disclosure policies that will be binding on the company once approved by the board. Some suggested policies include:

- *List of information the company intends to disclose*
- *Rules for communicating with the media, as well as the source and frequency of communications*
- *Media contacts, including press conferences, publications, brochures, and booklets*
- *Requirements for executive bodies to conduct meetings for shareholders and analysts*
- *Procedures for answering questions from all shareholders*
- *List of information, documents, and materials to be provided to all shareholders for the GMS*
- *List of confidential information*
- *Procedures for the identification and treatment of insider information*
- *Other internal policies or regulations, including a code of ethics, environmental and social policies, and internal regulations that apply to the BoC and BoD.*

Companies should disclose information about corporate conflicts resulting from improper implementation of corporate governance principles/practices that the company declared binding upon itself. Also, companies must adhere to the "comply or explain" principle in the application of accepted corporate governance rules and recommendations, and in that respect explain the reasons for

deviations from their implementation in practice.

Companies should also disclose information about changes in the identity of (or contractual arrangements with) the company's external auditor and other externally engaged persons that provide the company with material impact services on the company's business operations (e.g., law firms engaged for representation in major litigation).

For public companies, OJK has issued specific regulations on corporate governance-related disclosures, as described in details in Section 3.3.[253] The following are the primary elements that OJK provides under the regulations:

- Recommendations to increase the value of the GMS
- Recommendations that public companies implement communication policies to increase the quality of communications between public companies and their shareholders or investors
- Recommendations to strengthen the membership and composition of the BoC
- Recommendations to improve the quality of the implementation of the BoC's duties and responsibilities
- Recommendations to strengthen the membership and composition of the BoD
- Recommendations to improve the quality of the implementation of the BoD's duties and responsibilities
- Recommendations to have certain policies to encourage stakeholder participation, including (i) a policy to prevent insider trading, (ii) an anti-corruption and anti-fraud policy, (iii) a whistleblowing policy and (vi) a policy to provide long term incentives to members of the BoD and employees
- Recommendations concerning information disclosure

For banks, corporate governance disclosures must include at a minimum:[254]

- Implementation of duties and responsibilities of the BoC and BoD
- Completeness and fulfillment of all duties held by the committees and work units that manage the bank's internal control functions

[253] OJK Regulation No. 21/POJK.04/2015 and Circular Letter of OJK No. 32/SEOJK.04/2015.
[254] OJK Regulation No. 55/POJK.03/2016 and Circular Letter of OJK No. 13/SEOJK.03/2017.

- Implementation of compliance and internal and external audit functions
- Implementation of risk management
- Procurement policies, including procurement in large amounts
- Strategic plans
- Transparency of financial and non-financial conditions

10.3.7 Employees and Other Stakeholders

Strictly speaking, most of the information on employees and other stakeholders may not be "material" according to the accounting or financial definitions of the term. On the other hand, information about the company's employees, creditors, and suppliers, as well as the company's relationship with local communities can be "material" to other constituencies. Employees are also users of information, and disclosure helps them to make better employment decisions, protect themselves in the workplace, and participate in other aspects of company life. Stakeholder disclosure is becoming increasingly common worldwide and such disclosure might include health protection for employees, safety conditions in the workplace, collective bargaining agreements, and environmental or community impact statements.

10.3.8 Prospectus

Companies may only perform a public offer of securities with prior registration of their prospectuses with OJK. A prospectus provides material information on the company that is essential to allow investors to make informed decisions on the merits of potential investments. Prospectuses set forth the nature and object of shares, debentures, or other securities, and the investment and risk characteristics of the issue. Investors must be furnished with a prospectus before purchasing securities.

10.4 Voluntary Disclosure

It is good practice for companies to voluntarily disclose material information beyond formal legal requirements. This holds particularly true for companies operating in emerging markets that may be marred by weak legal and regulatory environments and poor enforcement mechanisms. To the extent possible, companies are encouraged to use various forms of disclosure and adhere to the same quality standards that are demanded for all forms of reporting. They are also encouraged to use other channels of communication, such as the internet and print media.

10.4.1 Corporate Websites

Corporate websites can be an exceptionally powerful means of communication, because they are accessible to the public at low cost. To this end, more and more Indonesian companies are using the internet for voluntary disclosure. At a minimum, companies should place the following information on their corporate websites:

- The company's AoA and all amendments
- Information on the company's development strategy
- Business and financial reports
- Prospectus documents
- External auditor's reports
- Information on material events
- Information regarding the GMS
- Important decisions of the BoC and BoD

Public companies typically place their annual and financial reports and governance information (such as information on members of the BoC, BoD, and key executives) on their websites. Some websites have special sections devoted to corporate governance and include contact addresses and telephone numbers for inquiries. Some Indonesian companies follow best practice and disclose additional information on their websites, including:

- Financial statements from the last three years
- Financial ratios from the last three years
- Internal corporate documents
- Structure, authority, and composition of the governing bodies
- List of affiliated persons
- Annual and quarterly reports from the last three years
- Materials and GMS decisions from the last three years
- Information on corporate securities
- A corporate news ticker

10.4.2 Mass Media

The print media is an additional channel for disclosure. Although print publication will likely incur additional costs, it is also an important and legally recognized channel for disclosure. Indonesian law specifically requires companies to publish some types of information in national newspapers, such as the auditors' reports. Publication of information in the mass media also ensures active dissemination of information among the public, unlike passive communication via the company website that requires public parties to search for details independently.

Most companies also disclose information about new products, major contracts, acquisitions, financial results, production plans, and securities issues in the print media in addition to their websites.

CHAPTER 11
Material Corporate Transactions

THE CHAIRMAN'S CHECKLIST

Extraordinary Transactions

- Do all commissioners and directors understand the concept of extraordinary transactions? When necessary, does the company's AoA specify criteria for transactions that are to be treated as extraordinary beyond the minimum criteria mandated by law? Does the BoD distinguish between extraordinary transactions and those entered into in the ordinary course of business?
- How does the BoD ensure the BoC and shareholders have sufficient opportunity to evaluate extraordinary transactions before providing their approval?
- Has the BoD engaged an independent appraiser to ascertain the market value of assets involved in extraordinary transactions?
- What steps are taken to protect the rights of shareholders who do not approve of extraordinary transactions?
- Does the company properly disclose information on completed extraordinary transactions?

Affiliated Transactions

- Does the BoD ensure that related parties properly disclose their interests in transactions? Do related parties abstain from participating in the discussion and voting on such transactions?
- Does the BoD ensure the company adheres to all legal requirements to obtain approval for affiliated transactions?
- Does the BoD take adequate measures to disclose information on

affiliated transactions and related parties?

- Do all directors understand their respective liability for violating procedures while approving affiliated transactions?

When a company undergoes a transaction that significantly changes its capital structure, such transaction may have major implications on the company's value, share price, and the property rights of shareholders. Indonesian law refers to these types of corporate events, including mergers, consolidations, share exchanges, spinoffs, sales of assets, or dissolution as extraordinary or material transactions. These transactions typically require special safeguards to be put in place to protect shareholder rights. Listed companies bear stronger obligations under Indonesian regulations when engaging in extraordinary transactions than private or public non-listed entities.

Although laws and regulations implement many specific protections with respect to extraordinary transactions, corporate governance abuses in these types of dealings continue to take place in Indonesia. For example, beneficial ownership structures typically remain non-transparent, making it nearly impossible to identify related parties in a transaction. In the meantime, insiders continue to develop complex structures and sophisticated techniques that allow them to tunnel assets, profits, and corporate opportunities away from the company and its shareholders.

This chapter discusses the legal and regulatory methods of addressing extraordinary transactions in Indonesia and considers international best practice to illustrate how Indonesian companies can maintain strong governance standards and shareholder protections when undergoing major corporate events.

11.1 Extraordinary Transactions

Extraordinary transactions refer to corporate events that significantly alter a company's capital structure, including mergers, dissolution, consolidation, share exchanges, and asset sales. In Indonesia, OJK regulations typically refer to such events as material transactions, which are defined as any transaction or series of transactions in the form of:

- Investment in business entities, projects, or business activities
- The purchase, sale, transfer, or exchange of assets or business segments
- Lease of assets
- Borrowing funds
- Pledge of assets
- Provision of guarantees

which are valued at 20 percent or more of the company's net assets.[255]

The ICL also requires companies to obtain GMS approval for material transactions that involve assignment or encumbrance of more than 50 percent of the company's net assets, whether in only one or a series of inter-related transactions.[256] Combined, Indonesia's overarching legal framework requires companies to obtain GMS approval for all material transactions involving more than 50 percent of the company's net assets and to comply with any additional demands made under the AoA.

OJK does not require listed companies to obtain GMS approval for transactions valued between 20-50 percent of the company's net assets, but they must announce such transactions to the public in at least one Indonesian-language newspaper with national circulation and submit the transaction documents to OJK within at least two days of being signed.

[255] Bapepam Regulation No. IX.E.2, as amended by Decision of the Chairman of the Capital Markets and Financial Institutions Supervisory Agency No. KEP-614/BL/2011 on Material Transactions and Change of Main Business Activity, Article 1.
[256] ICL, Article 102.

11.1.1 Valuing Extraordinary Transactions

An important aspect in determining whether a transaction is extraordinary or material is establishing the value of the transaction in relation to the company's net assets. The value of such transactions should be calculated according to the company's latest audited annual financial report, mid-term or other audited interim financial report if available, whichever is most recent. An independent appraiser should assist the BoD to determine the value of assets.

Table **13** Determining Transaction Value

Type of Transaction	Basis of Valuation
Sale of Assets	The value of assets involved in the transaction, determined by reference to the company's financial statements from the most recent reporting date
Acquisition of Assets	The acquisition price of assets involved in the transaction

11.1.2 Procedure for Approving Extraordinary Transactions

The procedures and disclosure requirements for approval of extraordinary transactions include the following:

- Transactions involving 20-50 percent of the company's net assets require unanimous approval from the BoD. If the BoD is not able to reach a unanimous decision, it can request that the GMS approve the transaction. The GMS can then approve the transaction with a simple majority vote of participating shareholders.
- Transactions involving more than 50 percent of the company's net assets require approval by a three-quarter majority vote of participating shareholders.[257]

[257] ICL, Article 102.

When passing a decision to approve or reject an extraordinary transaction, the BoD and GMS should include information on:

- The parties involved in the transaction
- Any other beneficiaries of the transaction
- The price of the transaction
- The object of the transaction
- Any other significant terms and conditions related to the extraordinary transaction

The main remedy in Indonesia for shareholders who object to the company undergoing an extraordinary transaction is to request that their securities be bought at a fair price. The ICL sets the necessary conditions for this remedy to be available. The transaction must be one that could harm the company or the shareholder's interests, such as amendment of the AoA, assignment or encumbrance of more than 50 percent of the company's net assets, or merger, acquisition, dissolution, or spinoff.[258]

If a shareholder does not agree with an extraordinary transaction that the company has conducted in full compliance with the law and procedural requirements, he/she may:

- Sell his/her shares. Practically, this is only possible if the company's shares are liquid, meaning that there are interested buyers such that the shareholder can sell his/her shares at a fair price.
- Demand that the company buy-back his/her shares in part or in full.
- File a claim to the district court.

11.1.3 Disclosure Requirements

OJK requires listed companies entering a material transaction valued at 20-50 percent of the company's net assets to make a public announcement in at least one national Indonesian-language newspaper within two days of signing the transaction documents and include the following information:[259]

- Description of the material transaction, including value and parties involved in the transaction (names, addresses, and contact numbers)

[258] ICL, Article 62(1).
[259] Bapepam Regulation No. IX.E.2, as amended by Chairman of Bapepam-LK Decree No. KEP-614/BL/2011, Article 2.

- Reasons for undertaking the transaction and its implications for the company's financial conditions
- Summary of the appraiser's report
- Statement from the BoC and BoD that all material information provided is correct and not misleading
- Place and address where shareholders may obtain information
- Declaration from the BoD stating that there are no conflicts of interest and that the transaction is not an affiliated (related party) transaction

Best Practice

Companies should include the following information on extraordinary transactions in their annual reports:

- *A list of all extraordinary transactions concluded by the company during the reporting year*
- *A list of transactions that are considered extraordinary based on the definition in the AoA*
- *Key terms of each extraordinary transaction*

11.2 Affiliated (Related Party) Transactions

Affiliated transactions involve parties that are either insiders or related to the company, such as directors, managers, or large shareholders. Some affiliated transactions have legitimate purposes and can be conducted fairly while others cannot. Regardless, they are easily abused and warrant attention since they can potentially reduce the company's value and may expropriate shareholder rights.

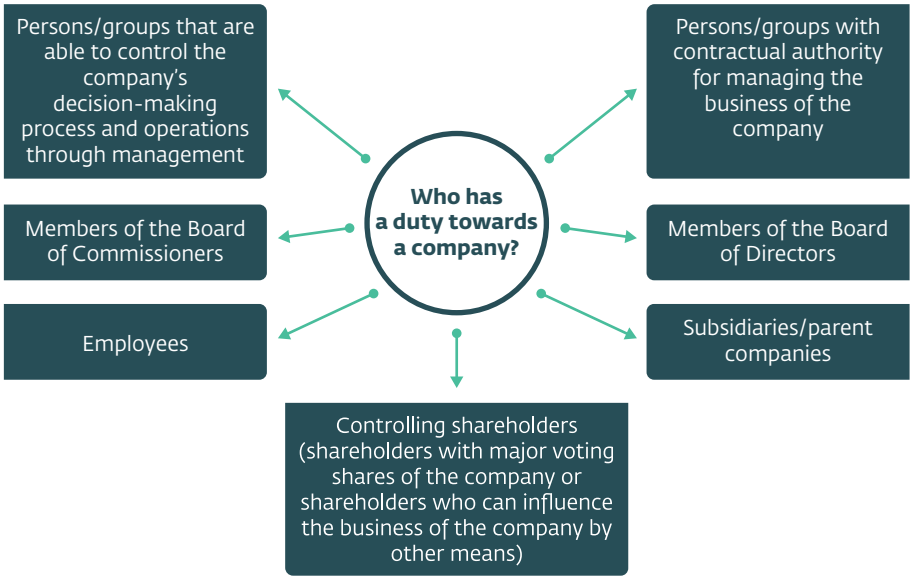
For listed companies, OJK sets detailed requirements concerning procedures for entering into affiliated transactions to discourage insiders from entering into such transactions and to help ensure fairness when a related party transaction does take place. Affiliated transactions may occur not only between the company and its directors, managers, and large shareholders, but more importantly, within groups of companies (holding structures) where transactions between the parent and subsidiary companies frequently occur. In other words, related party transactions are typically conducted among related parties of the company.

Under Indonesian regulations, an affiliated transaction is a transaction undertaken by a company or controlling company that is affiliated or related to either the company, members of the BoC, members of the BoD, or majority shareholders.[260] In addition, companies must meet the following two conditions in order for a transaction to fulfil the definition of an affiliated transaction:

- To be deemed affiliated or related to the company for the purposes of an affiliated transaction, the party must owe a duty to the company. ***Figure 23*** illustrates the types of party that may owe such a duty.

[260] Bapepam Regulation No. IX.E.1, as amended by Decision of the of the Chairman of the Capital Markets and Financial Institutions Supervisory Agency No. KEP-412/BL/2009 on Affiliated Transactions and Conflict of Interest on Certain Transactions, Article 1(d).

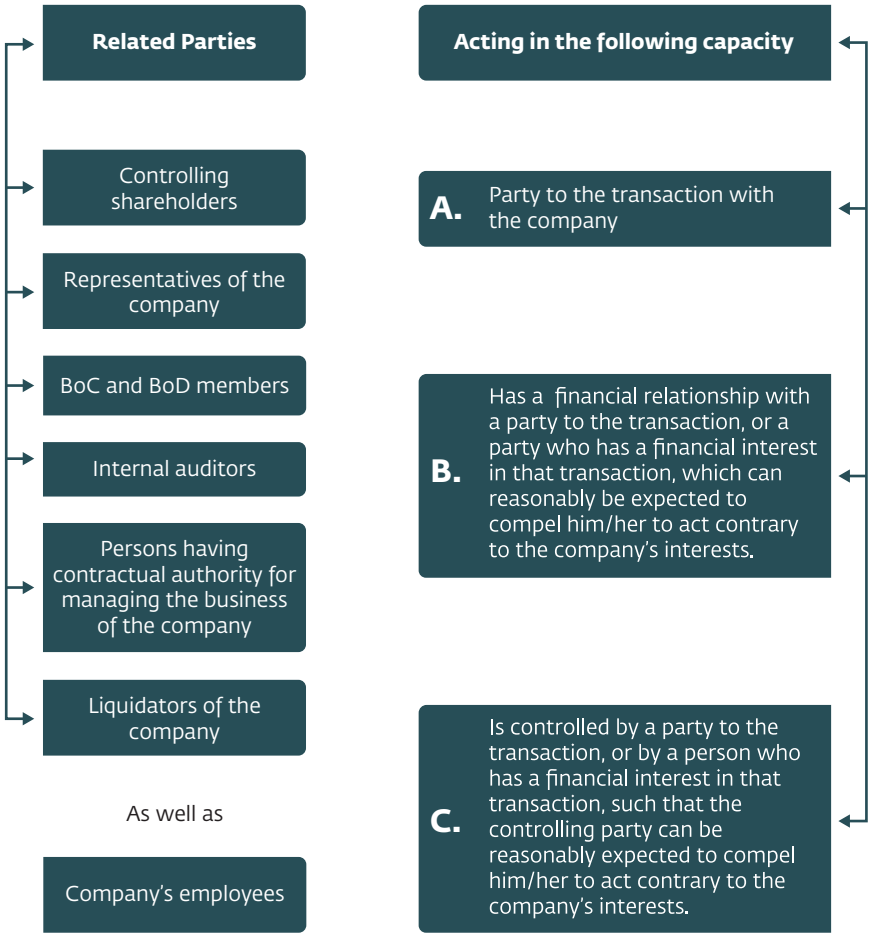
Figure **23** Parties that Owe a Duty to the Company



- The parties must be involved in the transaction in one of the following capacities:
  1. Act directly as a party to the transaction
  2. Have a financial relationship with a party to the transaction, or with a person who has a financial interest in that transaction, which can reasonably be expected to make him/her act contrary to the company's interests
  3. Is controlled by a party to the transaction, or by a person who has a financial interest in that transaction, such that the controlling party can be reasonably expected to compel him/her to act contrary to the company's interests.

Figure 24 depicts the components of an affiliated transaction.

Figure **24** Identifying Affiliated (Related Party) Transaction



A transaction is a related-party transaction if an interested party from the left-hand column is involved in a transaction in any capacity as indicated in the right-hand column. In practice, this means that a company must create a list of related parties and always check whether any of these parties or their affiliates are involved in a company's transaction in any of the capacities mentioned in the right-hand column.

Case Study

Company (X) concludes a contract with Company (Y), stating that that Company (Y) will sell Company (X) products online.

Mr. (A) is a member of the board of directors of Company (X) and is also the general director of Company (Z). Company (Z) will receive a special discount on products that Company (Y) sells to Company (Z) if the transaction between Company (X) and Company (Y) is concluded.

In such a transaction between Company (X) and Company (Y), Mr. (A) is considered a related party who is a beneficiary of the transaction. The transaction is an affiliated transaction for Company (X) and requires approval. At the same time, it is not an affiliated transaction for Company (Y).

As illustrated above, it is important to note that the same transaction can be an affiliated transaction for one company but not for another. In such cases, only one company needs to approve the transaction as an affiliated transaction.

Best Practice

The OECD Principles provide a general definition of related parties, including entities that control or are under common control with the company, share significant shareholders including members of the family, and share key management personnel.[261] *International Accounting Standard (IAS) Number 24 provides a more detailed definition: parties are considered to be related if one party has the ability to control the other party or to exercise significant influence or joint control over the other party in making financial and operating decisions. A party is related to an entity if:*

[261] *G20/OECD Principles of Corporate Governance*, 45.

1. *Directly, or indirectly through one or more intermediaries, the party:*
    - *Controls, is controlled by, or is under common control with the entity (this includes parents, subsidiaries, and fellow subsidiaries)*
    - *Has an interest in the entity that gives it significant influence over the entity, or*
    - *Has joint control over the entity*
2. *The party is an associate of the entity (as defined in IAS 28 Investments in Associates and Joint Ventures)*
3. *The party is in a joint venture with the entity (see IAS 31 Interests in Joint Ventures)*
4. *The party is a member of the key management personnel of the entity or its parent*
5. *The party is a close member of the family of any individual referred to in (1) or (4)*
6. *The party is an entity that is controlled, jointly controlled, or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (4) or (5)*
7. *The party has a post-employment benefit plan for the benefit of employees of the entity, or of any entity that is a related party of the entity*

At the same time, IAS 24 specifies which parties are not deemed to be related:

- *Two enterprises simply because they have a director or key manager in common*
- *Two parties who share joint control over a joint venture*
- *Providers of finance, trade unions, public utilities, and government departments and agencies in the course of their normal dealings with an enterprise*
- *A single customer, supplier, franchisor, distributor, or general agent with whom an enterprise transacts a significant volume of business merely by virtue of the resulting economic dependence*

11.2.1 Approving Affiliated Transactions

While the ICL does not provide great detail on requirements for approval of affiliated transactions, OJK requires listed and public companies to submit the following information within two business days following the transaction:[262]

- Description of the transaction (objects, value, parties involved and their relationship with the company, and the nature of their relationship)
- Summary of the appraiser's report (identity, purpose, objects, assumptions, approach and method of appraisal, conclusion on the value, and appraiser fairness opinion)
- Explanation, consideration, and reasons for conducting the transaction with an affiliated party, as opposed to with a non-affiliated party
- In the event the transaction involves an acquisition: the company's business plan, data on the acquired company, and any other relevant information
- Statements from the BoC and BoD that all material information has been disclosed and is not misleading
- Summary of a report from experts or independent consultants, if necessary

11.2.2 Identifying Affiliated Transactions

Under Indonesian law, any related party transaction that involves conflicts of interest or is valued at greater than 50 percent of the company's net assets requires GMS approval. However, in practice not all companies meet this requirement. There are different reasons for this, such as the reality that the BoC, BoD, and shareholders may not always be aware that a transaction involves related parties, particularly when insiders conceal their affiliation and personal interest.

One step towards identifying affiliations involves creating a list of parties to the transaction and setting out their relationships to the company and each other. However, this is often a challenging task, made difficult by the fact that many ownership structures in Indonesian companies remain opaque. In

[262] Bapepam Regulation No. IX.E.1, as amended by Chairman of Bapepam-LK Decree No. KEP-412/BL/2009, Article 2.

addition, individuals involved in a related-party transaction may design an elaborate transaction structure to disguise the significance of the dealing, such as by incorporating complicated off-shore schemes. In the banking sector, OJK regulations require institutions to implement an internal reporting system and to disclose all potential conflicts of interest that may arise under a transaction.[263]

The BoC's composition and experience will largely determine the success of identifying related party transactions. Independent commissioners who enjoy an arms-length relationship with directors will certainly play a key role in this respect. The external auditor's role is also important. The BoC and the audit committee will want to ensure that the company's external auditor uses the full range of audit procedures to evaluate self-dealing by management, such as interest free borrowing, asset sales that diverge from appraisal value, in-kind transactions, and loans made without scheduled terms.

11.2.3 Disclosure Requirements

For public companies, Indonesian law requires all BoC and BoD members and shareholders that own at least 5 percent of the total number of issued shares to declare their shareholding. This is applicable to both direct and indirect shareholdings. Individuals should disclose the following information:[264]

- Name, domicile, and nationality
- Company/companies in which shares are held
- Number of shares held and percentage of share ownership in the company both prior to and following the transaction
- Purchase or sale price per share
- Date of transaction
- Purpose of transaction

[263] OJK Regulation No. 55/POJK.03/2016, Article 62-63.
[264] OJK Regulation No. 11/POJK.04/2017, Article 7.

- Share ownership status (direct or indirect)
- In the event of indirect share ownership, information regarding the shareholder should be recorded in the shareholder registry of the publicly listed company for the interest of beneficial owners.

Comparative Practice

Company laws of many countries require persons who are related parties to disclose information to the board of directors, the audit committee, and the external auditor regarding:

- *Legal entities in which they, either independently or together with affiliated persons, own a certain percentage of voting shares*
- *Legal entities in which they hold managerial positions*
- *Pending or planned transactions in which they may be considered a related party*

Moreover, disclosure of beneficial ownership is an important aspect in detecting related party transactions. If the identity of the company's true owners is hidden, then it is difficult, if not impossible, to establish whether the parties in the transaction are related.

In addition, public companies must follow disclosure requirements on affiliated transactions as stated in Bapepam Regulation No. IX.E.1, as amended by Decision of the of the Chairman of the Capital Markets and Financial Institutions Supervisory Agency No. KEP-412/BL/2009 on Affiliated Transactions and Conflict of Interest on Certain Transactions.

Best Practice

Companies should be required to include the following information regarding related party transactions in their annual report:

- *A list of related party transactions concluded by the company during the reporting year*
- *Significant terms and conditions of each related party transaction*
- *The governing body that approved any related party transactions*

In addition, securities regulations should require that companies disclose the following information on related party transactions:

- *Minutes of the meeting of the approving body, including information on the quorum and voting results*
- *The list of persons with whom transactions may be qualified as related party transactions and the list of those persons with whom transactions have already been approved by the company*
- *Information on related parties before the placement starts, in case of an open subscription*
- *The prospectus and quarterly reports must provide information on related party transactions.*

Accounting legislation typically requires companies to disclose information on operations with related parties in their accounting documents.

11.2.4 Invalidation of Affiliated Transactions

A related party transaction can be challenged by a third party (e.g., a shareholder or creditor) if it does not obtain the necessary approvals in accordance with all legal requirements, or is not proven to be in the company's best interests at the time it is concluded or executed. Any party that feels disadvantaged may file an objection to the company or the court. The transaction will only be declared null and void based on the decision of the court.

11.2.5 Liability for Violation of Procedural Requirements

Without prejudice to the criminal sanctions that apply to some offenses in the capital markets sector, OJK has the authority to impose the following sanctions for violation of OJK regulations:

- Written warning
- Fines
- Limitation of business activities
- Suspension of business activities
- Revocation of business license
- Cancellation of an approval
- Cancellation of registration

CHAPTER 12
Dividends

THE CHAIRMAN'S CHECKLIST

- Does the AoA set out a procedure for the use of profits and distribution of dividends?
- Does the GMS make responsible decisions concerning the use of net profits to pay annual dividends versus reinvesting these profits?
- Does the BoD propose intermediary dividends and submit these to the BoC for approval? How does the BoC ensure this is done in the best interests of the company?
- Does the GMS ensure that preferred and common shareholders are treated equitably when distributing dividends?
- Does the GMS/BoC/BoD ensure the protection of creditor rights when declaring and paying dividends or interim dividends to shareholders?

Successful companies generate profits and either reinvest these in the business or distribute them to shareholders as dividends. In Indonesia, there is an expectation (particularly among minority shareholders with small shareholdings) for companies to make dividend payments in reasonable amounts rather than to retain profits. However, companies often need to source additional capital, and in cases where there is no immediate alternative other than to use company profits, decisions of whether or not to make dividend payments become difficult. This chapter discusses dividends from the perspective of both shareholders and creditors, as well as procedures for declaring and paying dividends.

12.1 General Provisions

Shareholders have a right to share in the profits of the company in proportion to the number of shares they own.[265] They may do so by enjoying capital gains (an increase in the market value of shares they hold in the company) and through dividend payments. As such, dividends represent an important component of shareholder rights.

At the company level, management ought to respect the obligation to pay dividends. To this end, the ICL stipulates that unless the GMS determines otherwise, companies must allocate net profits (minus approved deductions to be set aside as reserves) to be disbursed to shareholders as dividends.[266] However, companies must also fulfil their obligations to creditors. Paying dividends means paying out cash to shareholders, which may decrease the company's level of cash and equity (profit balance or reserved profit) available to service debt on a timely basis. Indonesian legislation accordingly imposes limitations on the types and manner in which companies may make dividend payments to ensure companies fulfill their responsibilities to creditors.

In Indonesia, the ICL sets out minimum obligations with respect to the distribution of company profits and protection of creditor interests. A key requirement is for companies to maintain a mandatory reserve to be collected each financial year from a proportion of the company's net profits.[267] The mandatory reserve need not always be in the form of cash, but may take the form of other assets that are easily liquidated and cannot be allocated as dividends. Further, companies may only allocate dividends when they have a positive balance of profits (when a company's net profits in the current financial year are sufficient to cover any accumulated losses from previous financial years).

A company's AoA will set out procedures for the use of company profits and allocation of dividends to shareholders.[268] The BoC/BoD may make recommendations to the GMS on the amount of dividend payments; however, the GMS maintains the ultimate authority to determine the value of all dividend payments, apart from interim dividends. For interim dividends, the BoD may

[265] ICL, Article 52(1).
[266] ICL, Article 71(2).
[267] ICL, Article 70.
[268] ICL, Article 15(1).

decide to allocate interim dividends and set the value of these payments by passing a BoD resolution, which the BoC must also approve.[269]

12.1.1 Dividend Rights

Owners of common and preferred shares have different rights with respect to dividends, which the company will set out under the AoA. The ICL also stipulates that under some conditions (such as when shareholders obtain their shares due to re-purchase, transfer by operation of law, grant, or by bequest), these shares do not entitle their owners to dividends.[270]

12.1.2 Types of Dividends

The ICL defines two types of dividends: annual and interim. It sets specific requirements with respect to interim dividends as follows:[271]

- A company may allocate interim dividends before the end of the company's financial year, as long as it is regulated by the company's AoA.
- Companies may allocate interim dividends so long as their total net assets do not fall below the total subscribed and paid up capital plus the mandatory reserve.
- Allocation of interim dividends must not disrupt the company's business activities or result in the company becoming unable to fulfill its obligations to creditors.
- The BoD will make decisions concerning the allocation of interim dividends by passing a resolution, which must also obtain BoC approval.
- If it transpires at the end of a financial year that the company has suffered losses, shareholders must return any interim dividends received during that year to the company.
- The BoC and BoD will be jointly and severally liable for the company's losses in the event shareholders do not return interim dividends.

[269] ICL, Article 72(4).
[270] ICL, Article 40(2).
[271] ICL, Article 72.

12.1.3 Forms of Dividend Payments

There are no specific requirements under the ICL or the Capital Markets Law as to the form in which companies must make dividend payments, although a typical method is to pay in cash. OJK recognizes both stock and cash-based dividend payments.[272] Non-cash transactions are typically unsuitable for dividend payments. Companies should generally pay dividends in cash.

The ICL requires shareholders to claim dividends paid to them within five years. Beyond that period companies must place dividend amounts in a special reserve.[273] The GMS will determine the procedures for management and administration of the special reserve. Any dividends in the reserve that remain unclaimed after ten years will become company property.[274]

12.1.4 Dividend Amounts

The BoD's priority when determining how and in what amounts to distribute dividends should be to maximize value for shareholders. The company should set its target payout ratio—defined as the percentage of net income to be paid out as cash dividends—with regard to shareholder preferences as well as the ICL requirement to maintain a reserve fund (the reserve may be up to 20 percent of the company's total subscribed and paid-up capital). More specifically, shareholder preferences may be to receive either capital gains (for example, the opportunity to use excess cash to buy back shares or re-invest in the company), dividends, or a combination of the two. The BoD will then need to define its optimal dividend policy, which should strike a balance between distributing dividends and supporting sustainable growth.

For any given company, four primary factors will determine the optimal payout ratio:

1. Investor preference for capital gains versus dividends
2. The company's investment opportunities (for example, companies with excess cash but limited investment opportunities would typically distribute a large percentage of their income to shareholders via

[272] Decision of the Head of the Financial Services Authority No. KEP-35/PM/2003 on Bonus Shares (Regulation No. IX.D.5), Article 1.
[273] ICL, Article 73(1).
[274] ICL, Article 73(2)(3).

dividends, while companies in high-growth sectors typically reinvest their earnings in the business)

3. The company's existing capital structure
4. The availability and cost of external capital

Stability in dividend payments is important to shareholders, and many shareholders rely on dividends to meet their own expenses. For this reason, it is essential that companies achieve a careful balance with respect to the stability and dependability of its dividend policy.

12.2 Procedures for Declaring and Paying Dividends

To declare and pay dividends, companies should follow specific steps as summarized in ***Figure 25***.

Figure **25** Procedures for Declaring and Paying Dividends

Step 1

After calculating the company's net profits and the reserve fund, the BoD (provided the BoC grants approval) may recommend that the GMS declare dividends after setting out the amounts to be paid and procedures for payment.

Step 2

The BoD prepares a list of shareholders entitled to receive dividends.

Step 3

The GMS votes to declare a dividend payment.

Step 4

The company pays the declared dividends.

12.2.1 Declaring Dividends

A company may declare dividends annually or more frequently, according to its AoA. However, interim dividends may only be paid if the company's total net assets do not fall below the sum of the total subscribed and paid-up capital plus the mandatory reserve.[275] When deciding to declare dividends, companies must address two basic issues:

- The percentage of profits to be distributed

[275] ICL, Article 72(2).

- The frequency of payments, i.e., should the dividends vary from year to year, or remain stable over time

Dividend payments must also take into account the priority rights of shareholders that hold preferred shares, or other classes of shares with special dividend rights, as regulated in the company's AoA. Until a company has declared and paid in full shareholders with priority rights to dividends (including accumulated dividends), as specified by the AoA, it cannot declare and pay dividends for other preferred or common shares. Further, the company cannot declare dividends for common shares (or any share class with lesser priority) until the claims of priority shareholders have been paid. Unless regulated otherwise in the AoA, the ICL requires a simple majority vote of shareholders participating in the GMS to declare all dividend payments.

Best Practice

To help shareholders properly assess a company's capacity to make dividend payments, companies are advised to:

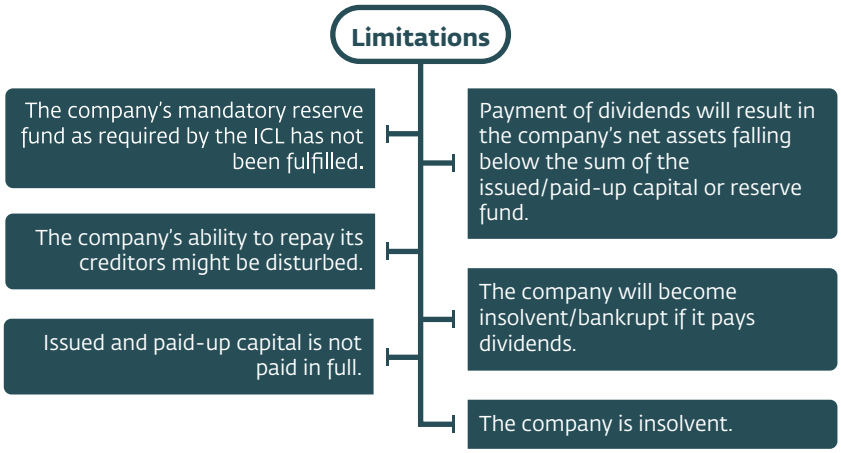
- *Establish a transparent and shareholder-friendly mechanism for evaluating the payment of dividends.*
- *Provide sufficient information to shareholders to enable them to understand the conditions that must be met before the company will pay dividends.*
- *Provide sufficient information to shareholders to enable them to understand procedures for the payment of dividends.*
- *Ensure that there is no misleading information that might artificially influence shareholders' assessment of policies governing dividend payments.*
- *Provide simple dividend payment procedures.*
- *Impose (financial) sanctions on the president director and members of the BoD for incomplete or delayed payments of declared dividends.*

A useful tool for assessing a listed company's dividend policy and

prior history of making dividend payments is a dividend report, which commercial accounting firms and other organizations typically produce to track the dividend performance of listed companies. These reports are usually available for a fee.

Figure 26 lists circumstances under which the company must not declare dividends (however, this list is not exhaustive). Both the AoA and the company's debt instruments can specify other circumstances in which the company will be prohibited from declaring dividends.

Figure **26** When a Company Cannot Declare Dividends



12.2.2 Shareholder List

When a company declares dividends, it sets the date by which its shareholders must be registered on the company's books in order to receive dividend payments at that time. For listed companies, the stock exchange will fix the date upon which companies must finalize their list of shareholders entitled to dividends, which is called the "ex-dividend date". Shareholders registered in the company's books as entitled to receive dividends before the ex-dividend date

will receive dividends. Consequently, shareholders who own shares on the ex-dividend date, and who sell them after that date, may retain the right to receive dividends; whereas shareholders that purchased shares after the ex-dividend date may not be entitled to receive dividends until the next ex-dividend date. The buying and selling shareholders may, however, choose to transfer dividend rights from seller to buyer under their contract of sale.

In the banking sector, a controlling shareholder that does not pass the fit and proper test for integrity reasons will neither be entitled to hold shares nor receive dividends.[276]

12.2.3 Paying Dividends

Once dividends have been declared, the company must pay within a period as set either under the AoA or by the GMS. Shareholders have the right to file a claim in court against the company to demand payment when declared dividends remain unpaid.

Indonesian law does not require companies to penalize the BoD or other senior company employees (such as the chief operating officer or chief executive officer) when dividend payments are incomplete or in arrears. However, considering failure to pay declared dividends can give shareholders the right to file a court claim, companies are advised to establish a penalty system. One method may be to authorize the BoC to reduce the remuneration of the president director, BoD, or senior management when the company fails to pay declared dividends in full or on time.

12.2.4 Information Disclosure on Dividends

A company must make the BoC and BoD's recommendations for distribution of profits easily available to all shareholders, including the amounts of dividends to be distributed to each share class and procedures for payment. Securities legislation regulates the disclosure requirements concerning dividend payments.

[276] Circular Letter of OJK No. 39/SEOJK.03/2016, Article 10(b).

For listed companies intending to distribute dividends in the form of cash, stock, or bonus stock, the company must submit a report to the IDX that includes relevant GMS resolutions, specifying details of the distribution no later than two working days after the GMS.[277] Companies are also required to include a report on dividend payments in their annual reports.

Best Practice

Companies should consider adopting a by-law to standardize their dividend disclosures, although this is not a requirement under Indonesian law. This by-law may include a list of information, documents, and other materials that the company must provide to shareholders to enable them to make appropriate decisions when voting to declare dividends. The information should refer to agenda items for the GMS, such as:

- *Recommendations of the BoC/BoD regarding the distribution of profits*
- *Recommendations of the BoC/BoD on the payment of dividends*
- *Reasons for each recommendation*

Companies should disclose information on dividend payments to all shareholders, and give reasons when dividends are not paid.

[277] Decision of the Board of directors of the Jakarta Stock Exchange No. KEP-306/BEJ/07-2004 Rule I-E on Obligations concerning Information Disclosure.

CHAPTER 13
Charter Capital

THE CHAIRMAN'S CHECKLIST

- Has the founding GMS established whether shares are subscribed and paid-up properly, and whether capital contributions in other forms conform with the law? Have the company's founders paid their initial contributions, and have all in-kind contributions been properly valued?
- Does the BoD understand the company's financial needs and different techniques of corporate finance? Which governing bodies have the authority to increase the charter capital? Is the company careful not to dilute the ownership of shareholders when deciding to restrict or preclude pre-emptive rights of shareholders?
- Are capital increases justified?
- Does the company ensure that the charter capital, and consequently creditors, are adequately protected in cases of charter capital decreases? Who make decisions regarding the buyback of company shares? Has the company ensured that all shareholders who submit their shares are treated equitably?
- How does the BoD ensure that the reserve fund is utilized in the best interests of the company? What other funds has the company established?

Charter capital is defined as the total assets brought together to form a company, comprising the amount of capital that shareholders contribute or commit within a specific period, as recorded in the company's AoA. The ICL does not use the term charter capital specifically, but refers to issued and paid-up capital. Given that charter capital is a term commonly used in the international context to refer to issued and paid-up capital, reference will be made in this chapter to charter capital.

The ICL and related regulations attach certain protective functions to charter capital. These are designed to safeguard shareholders from their shares becoming diluted and provide a minimum guarantee that companies will meet their obligations towards creditors. Although charter capital alone cannot provide full protection, it creates one element of guarantee over creditor interests. For shareholders, charter capital plays an important role because many shareholder rights are linked directly to the size of their investment in the charter capital.

Indonesian companies must observe legal requirements to maintain charter capital, therefore strong corporate governance in this area continues to be important. Indonesian regulations govern both increases and decreases in the charter capital and other procedural guarantees over shareholder and creditor rights, including provisions concerning share buybacks, the redemption of shares, reciprocal shareholdings, and the maintenance of statutory reserves. This chapter will discuss all of the above.

13.1 General Provisions

Charter capital is an important element in the legal definition of a limited liability company, which is defined as a commercial entity whose charter capital is determined and divided into a specified number of shares, certifying shareholder rights in relation to the company. The charter capital has important legal implications for:

- Determining the minimum amount of a shareholder's liability
- Determining shareholder rights in relation to their proportionate share in the charter capital
- Offering support to protect creditor rights by setting the minimum amount of assets a company must have; this is one of the legal instruments upon which creditors can rely when seeking to ensure that the company fulfills its contractual obligations

13.1.1 Definition of Charter Capital

Charter capital is defined as the total assets, usually in the form of cash that is brought together to form a company, comprising the amount of capital that shareholders contribute or commit within a specific period, as recorded in the company's AoA. For a limited liability company, charter capital is divided into shares. Bonds and other credit instruments do not form part of charter capital.

13.1.2 Legal Capital or Minimum Charter Capital

Legal capital means the minimum level of capital that companies must have by law to be incorporated. This requirement is implemented to protect the interests of consumers and creditors. In Indonesia, the ICL regulates the legal capital threshold, which is set at minimum Rp 50,000,000.[278] For a foreign investment

[278] ICL, Article 32.

company, the minimum investment is above Rp 10,000,000,000 (excluding land and buildings). Other regulations may require a greater minimum charter capital amount for companies active in certain business fields.

For banks, minimum capital requirements are proportional to their risk profile, which is calculated based on the ratio of minimum capital provision obligation (*Kewajiban Penyediaan Modal Minimum* or KPMM).[279] Minimum capital must constitute at least:[280]

- 8 percent of balanced assets based on risk (*Aset Terimbang Menurut Risiko* or ATMR) for banks with 1st rank risk profile
- 9 to just less than 10 percent of ATMR for banks with 2nd rank risk profile
- 10 to just less than 11 percent of ATMR for banks with 3rd rank risk profile
- 11 percent to 14 of ATMR for banks with 4th and 5th rank risk profile

OJK may set a higher minimum capital requirement if it considers a bank likely to incur additional losses.[281] In addition to the prescribed minimum capital requirements, banks must also have additional capital constituting a buffer which can be in the form of (i) a capital conservation buffer, (ii) a countercyclical buffer, or (iii) a capital surcharge for systemic banks. The amount of additional capital required is:[282]

a. 2.5 percent of ATMR for capital conservation buffer
b. Between 0 and 2.5 percent of ATMR for countercyclical buffer
c. Between 1 and 2.5 percent of ATMR for capital surcharge of systemic banks

13.1.3 Charter Capital and Share Capital

A company's charter capital will generally be equal to the total nominal value of its shares. In the field of capital markets, public companies are allowed to issue shares without nominal value. The company is not required to issue all of its authorized shares. Often companies will authorize a far greater number of shares than required, to give the company flexibility to issue more shares later as needed. If the company chooses not to issue authorized shares, these shares are

[279] OJK Regulation No. 11/POJK.03/2016 on Minimum Capital Provision of Commercial Banks, as amended by OJK Regulation No. 34/POJK.03/2016, Article 2(1)(2).
[280] OJK Regulation No. 11/POJK.03/2016, Article 2(3).
[281] OJK Regulation No. 11/POJK.03/2016, Article 2(4).
[282] OJK Regulation No. 11/POJK.03/2016, Article 3(3).

referred to as authorized but not issued.

Only those shares that are issued and fully paid constitute charter capital. The total charter capital that a company sets forth in its AoA is based upon the amount of money that the company requires at its establishment. This amount is conditioned by the percentage of dilution its founders are willing to accept in the future. During its business operation, the company may decide to issue additional shares to increase the charter capital.

13.1.4 Full Payment of Shares

Founding shareholders must collectively subscribe and pay in full at least 25 percent of the total common shares the company issues at the time it is established.[283] The ICL requires shareholders to provide proof of valid payment.[284] Proof of valid payment may include evidence that the shareholders have deposited payment into a bank account held in the company's name, data from financial reports audited by an accountant, or the company's balance sheet signed by the BoC and BoD.[285] Any further issuance of shares at any time to increase the subscribed capital must be paid in full. This means that the ICL does not provide the possibility to pay up shares by means of installments.[286] If any founding shareholder does not pay his/her subscribed shares in full, the outstanding payment must be made in one of the following ways. Either:

- All other founding shareholders will buy the unpaid subscribed shares, in proportion to the shares they own in the company
- One or more founding shareholders agree to contribute fully the unpaid shares, in which case these founding shareholders become the owners of the shares, or
- The company calls for other persons who are not shareholders to contribute the unpaid shares, in which case these persons will become additional founding shareholders

Companies must provide evidence of payment for issued shares to the MOLHR within sixty days after signing the deed of establishment.[287] In practice, notaries who assist in the establishment of the company often try to avoid this situation

[283] ICL, Article 33(1).
[284] ICL, Article 33(2).
[285] ICL, Elucidation of Article 33(2).
[286] ICL, Article 33(3).
[287] Government Regulation No. 29 of 2016 on Changes to Authorized Capital of Limited Liability Companies, Article 2(2).

by having shareholders sign a document, on the basis of which they undertake to pay up the shares as soon as the company has opened a bank account.

13.1.5 Contributions to the Charter Capital

Unless the AoA stipulates otherwise, under Indonesian law investors can generally pay for shares in cash or in other forms. However, the value of contribution in other forms must be determined objectively, either in accordance with market price or appraised by an expert with no affiliation to the company.[288] Shares paid for in the form of immoveable property must be announced in one or more newspapers within a period of fourteen days following GMS approval. Alternatively, if this payment is made at the time the company is established, then the announcement must be made within the fourteen-day period after the deed of establishment is signed.[289]

It is good practice that if the decision to place shares allows shareholders to pay for additional shares with other securities, or with other assets having monetary value, such a decision should include:

- Detailed description of the other forms of contribution
- Identity of the person providing the contribution
- Number and nominal value (or accountable par in case of shares without nominal value) of shares to be acquired by that contribution

For listed companies, the following requirements apply to contributions for shares made in forms other than cash, whether through tangible or intangible assets:[290]

1. The company must list the types of assets to be used as contribution for shares in the invitation to the GMS.
2. The professional who conducts the appraisal must be registered with OJK. The appraised assets must not be encumbered.
3. The GMS must approve payment in this form. For this approval to be valid, the GMS must meet minimum quorum requirements: at least half of voting shares must be represented in the first meeting. If a second

[288] ICL, Article 34(1)(2).
[289] ICL, Article 34.
[290] Decision of the Chairman of the Capital Market and Financial Institutions Supervisory Agency No. KEP-179/BL/2008, Article 5(c).

meeting is required due to failure to meet quorum, at least one-third of voting shares must be represented.[291]

4. If the assets used as contribution take the form of shares held in another listed company, the price of those shares will be determined according to their fair market value.
5. If the payments come from either the company's retained earnings, paid-up capital in excess of par value, net profit, or other components of the company's equity capital, then the company must state the source of these payments in its next annual financial report. In addition, an accountant registered with OJK must audit these reports.

A shareholder, employee, contractor, or any person otherwise affiliated with a company should be prohibited from conducting appraisals for that organization.

A company should use a properly accredited, licensed independent appraiser to determine the market value of property, value debts, and assess liabilities. An independent appraiser can also play an important role in assisting management and shareholders during the company reorganization. It is also good corporate practice to insure an independent appraiser against civil liability.

[291] ICL, Article 86(1)(4).

13.2 Increasing Charter Capital

A number of factors, such as market conditions, business expansion, and other forms of corporate reorganization, may require companies to increase their charter capital. A company can make this increase using:

- External sources, such as when the company attracts financial resources from existing shareholders or third parties
- Internal sources, where the company uses its own funds to capitalize its internal reserves

This section discusses the most important issues that companies must address when increasing their charter capital.

13.2.1 Methods to Increase Charter Capital

A company requires consent from the GMS (achieved by passing a valid resolution) to increase its charter capital. Once the GMS approves the increase, it may confer upon the BoC authority to take necessary steps to implement this decision. The GMS may give the BoC up to one year to take the necessary action. The GMS may withdraw its consent at any time.[292]

A GMS resolution to increase subscribed and paid-up capital without affecting authorized capital will be valid if adopted by a quorum of more than one-half of all the shares with voting rights, with more than one-half of votes cast in favor, unless the company's AoA requires a larger proportion of approving votes. The company must inform the MOLHR when it increases charter capital, and the Ministry will record these changes in its company register.[293]

OJK regulations allow listed entities to issue an increase in charter capital that dilutes total subscribed shares to less than 25 percent of the original charter capital, on the condition that the company:

1. Obtains GMS and MOLHR approval for the increase

[292] ICL, Article 41(1)(2).
[293] ICL, Article 42(2)(3).

2. Performs the increase to paid-up and issued capital no later than six months from the date of MOLHR approval
3. If the company cannot perform the increase within six months, the company must amend its AoA, authorized capital, and issued and paid-up capital in order to comply with the 25 percent requirement. This amendment has to be made within two months following the six months period.

For increases to charter capital involving conversion of convertible bonds into shares, the company must meet all conditions under Indonesian laws and regulations, including announcing the proposed conversion in two daily newspapers and the plan of issuance, in order for the increase to be effective.

In general, the increase in charter capital can be conducted through one of the following methods:

- Capital increase against contributions
- Conditional capital increase
- Capital increase taken from capital surplus, retained earnings, and other funds available from internal sources

Technically, every method of increasing charter capital can be done by issuing additional shares. In many countries, companies can increase their charter capital by issuing shares with a higher nominal value. However, companies must offer new shares issued in the context of a charter capital increase to existing shareholders, in proportion to their shareholdings in the same share class. This provision applies unless the increase:[294]

- Is directed to the company's employees
- Is directed to bondholders or other securities that are convertible into shares and are issued with GMS consent
- Is made in the context of a restructuring or reorganization that the GMS has approved

Typically, the number of additional shares issued will be rounded down to a unit of share. The GMS shall decide how to treat the residual surplus of shares due to rounding. Some companies may transfer the face value of those shares to fund investment and development; others may repurchase those shares to be kept in the company's reserves.

[294] ICL, Article 43(3).

When a public company intends to issue shares for the purpose of paying dividends to its existing shareholders and to increase the company's charter capital, it may do so on condition that:

- The GMS approves the action
- The company has sufficient funds to service the issuance from after-tax profits, based on the company's latest audited financial statements.

Table 14 provides a summary of methods to increase charter capital.

Table **14** Increasing Charter Capital

	Capital Increase against Contributions	Conditional Capital Increase	Capital Increase out of Capital Surplus, Retained Earnings, and Other Funds
Source	External	External	Internal
Contributor	Shareholders and third parties	The owner of convertible bonds	The company (using funds available from internal sources as defined by legislation)
Purpose	To attract additional funding; however, this method will dilute the holdings of existing shareholders if they are unwilling/unable to make use of their pre-emptive rights.	To allow owners of convertible bonds to use their rights of conversion into shares	To increase the company's equity and to decrease the company's funds and reserves available for distribution
Recipient	Existing shareholders and third parties	The owners of convertible bonds	Only existing shareholders
Changing the Company's Ownership Structure	Possibly	Yes	No

Method of Capital Increase	Issue of additional shares	Issue of additional shares	Issue of additional shares
Method of Placement	Subscription (open or closed)	Conversion	Distribution
Required Approval	The GMS, unless delegated to the BoC	The GMS	The GMS
Pre-Emptive Rights	Yes	No	No

13.2.2 Methods of Placement

There are three methods to place issued shares:

- Distribution among existing shareholders
- Conversion of convertible bonds
- Subscription by new shareholder/third parties

13.2.3 Procedural Guarantees for Increasing Charter Capital

The ICL and securities regulations provide detailed procedures that public companies must follow to increase their charter capital. These procedures aim to guarantee the protection of shareholder rights. OJK provides approval for share issuance and administers registration procedures to ensure the legality of all share increases.

At the company level, the GMS typically plays a primary role in increasing charter capital, as follows:

1. **The GMS makes the decision to increase capital**
   As previously mentioned, the ICL stipulates that a company's capital may be increased with GMS consent. The GMS may assign its consent to

the BoC for no longer than one year and the delivery of such authority may be withdrawn by the GMS at any time.[295] However, GMS approval will be required for companies to issue shares for the purpose of paying dividends or to issue bonus shares. There is no specific regulatory requirement on the issuance of additional shares for capital increases against contributions. For listed companies, GMS approval is also needed for the issuance of additional shares.

2. **The BoC and BoD implement the GMS decision**
   When the GMS authorizes a capital increase, the BoC governs the timing, methods, and the total value of the capital increase, ensuring that it stays within the company's maximum limits. Meanwhile, the BoD plays a more specific role in receiving payment for newly issued shares and recording details in the shareholders' register.

Public offerings must be registered with OJK, which will then grant the company a 'public offering of shares' certificate. To register, the issuing company must submit the following information to OJK, among others:[296]

- Written registration of public offering of shares
- Prospectus
- Audited financial statement
- Legal report and legal opinion
- GMS decision adopting the issuance plan and the capital usage plan generated from the public offering of shares
- An issuance underwriting commitment (if any)

[295] ICL, Article 41.
[296] Decision of the Chairman of the Capital Market and Financial Institutions Supervisory Agency No. KEP-122/BL/2009 on Registration Procedures during Public Offerings (Regulation IX.A.2).

13.3 Protecting Charter Capital

One of the purposes of the charter capital is to provide a minimum guarantee that the company will fulfil its obligations toward its creditors. This function can only be effective if it is not linked to preserving a minimum level of company assets. The company must send a notice of the decision to reduce the company's charter capital to the authorized business registration body. The company must also commit to meeting all debts and other obligations that remain outstanding after the reduction of the charter capital takes effect. Where the company operates in an industry that requires it to maintain a minimum level of legal capital, the company cannot register to reduce charter capital to an amount that is lower than the capital threshold required by law.

There are other events that may, in one way or another, affect the charter capital and net assets. ***Figure 27*** lists the primary examples of such mechanisms, which are designed to prevent the distribution of the company's assets to shareholders or other parties to the detriment of creditors.

Figure **27** Protecting Charter Capital

- Share buybacks
- Decrease of the charter capital
- Distribution of dividends
- Share redemption
- Reciprocal shareholdings
- Maintaining statutory reserves

13.3.1 Decreasing Charter Capital

The practice of decreasing charter capital creates an opportunity for companies to provide returns to shareholders without paying dividends. A decrease in the charter capital can favor some shareholders at the expense of others, and consequently presents potential for abuse. It is essential that companies endeavor to ensure equitable treatment of all shareholders. This holds particularly true if the company has several classes of shareholders with different rights, or holders of other securities. A decrease in the charter capital reduces the level of shareholder liability, as well as the minimum amount of assets intended to serve as a guarantee that the company will fulfill its obligations toward creditors. Any decrease in the charter capital can be:

- Real when it involves a share buyback from shareholders, or
- Nominal when the charter capital is decreased by writing off losses, intended to reorganize the company's financial position, or when the charter capital is transformed into reserves that can be used for future distribution

Methods to Decrease Charter Capital

The GMS may pass a resolution to reduce subscribed and paid-up capital by either withdrawing shares from the charter capital or reducing their nominal value. A company may make a withdrawal (for the purpose of decreasing charter capital) against those shares that it has re-purchased, or against shares from a share class that specifies that they may be withdrawn. Where the decrease is made by reducing the nominal value of shares, the company must make these reductions in proportional amounts to all shares from each share class.[297]

Indonesia's regulatory framework does not provide detailed guidelines on how to perform a capital reduction. In practice, companies may decrease charter capital using the following methods:

- The company may purchase and cancel a number of treasury stocks with par value equal to the amount of capital planned to be reduced, or the company cancels the treasury shares which must be cancelled. This option would not require companies to return money to their shareholders.
- The company may withdraw and cancel a quantity of shares from shareholders with a total par value equal to the amount of capital reduced. By this mode, the company will buy back a number of shares

[297] ICL, Article 47(1)(3).

from each shareholder in proportion to the amount of shares in accordance with his/her equity proportion in the company. The company will have to pay the shareholders an amount of money equal to the number of shares withdrawn times the par value of shares.

- Reducing the nominal value of shares without changing the number of shares. By this mode, the company withdraws shares from shareholders and issues new shares with reduced par value. The company must pay its shareholders an amount of money calculated according to the number of shares that they hold multiplied by the difference between the old and new par values.
- A combination of the above methods. Joint-stock companies may potentially apply a combination of the above methods to reduce share capital, depending on their particular capital structure.

Banks may decrease their charter capital through the following methods, among others:[298]

- Buyback of a capital instrument which has been recognized as a capital component
- Placement of funds in another banks' debt instrument which has been recognized as a modal component by the other banks (issuing banks)
- Cross-ownership which is obtained from transfer due to law, grant, or bequest (*hibah wasiat*) as referred to in the ICL to the extent that it has not been transferred to a third party

Procedures to Decrease Charter Capital

Indonesian law does not regulate issues related to mandatory decrease of charter capital. However, the ICL sets out the following guidelines for decreasing charter capital that apply to limited liability companies:[299]

1. Capital reduction can only be conducted with GMS approval.
2. A GMS resolution approving capital reduction will be valid only if adopted with due attention to the requirements for quorum and the number of votes that must be passed to approve the reduction in accordance with the ICL provisions or the AoA.
3. The BoD must notify all creditors of a GMS resolution to reduce the company's capital by announcing it in one or more newspapers within a period of not more than seven days from the date of the GMS resolution.
4. The company must obtain MOLHR approval before taking action to

[298] OJK Regulation No. 11/POJK.03/2016, as amended by OJK Regulation No. 34/POJK.03/2016, Article 22(1).
[299] ICL, Article 44-47.

reduce charter capital.

The ICL provides clear guidelines regulating protections for creditors in case of liquidation or winding up. Within a period of not more than thirty days from the date the company is wound up, the liquidator must notify:[300]

- All creditors of the winding up of the company through an announcement in a newspaper and the State Gazette of the Republic of Indonesia, and
- The MOLHR of the winding up of the company to be recorded in the company register that the company is in liquidation

Notification to creditors published in newspapers and the Indonesian State Gazette should contain details covering:

- The legal basis for the winding up
- The liquidator's name and address
- Procedures for submission of claims, including the time period to submit claims

13.3.2 Share Buybacks

Under certain circumstances and conditions, companies have the right to repurchase their own shares. Share buybacks have a number of corporate governance implications. First, there may be a financial planning concern; since cash is used to purchase shares, fewer funds may be available for further business development. Second, shareholder rights can be abused if the company does not provide equal opportunities to all shareholders to sell their shares back to the company. To strengthen shareholder protections, the ICL provides that shareholders may in some circumstances request the company to buy back their shares at a fair price. Such requests will be valid if the company performs one of the following acts which causes harm to the company or shareholders' interests:[301]

- Amend the AoA
- Assign or secure company assets valued at more than 50 percent of the company's net assets
- Conduct a merger, consolidation, acquisition, or spinoff

[300] ICL, Article 147(1)(2).
[301] ICL, Article 62(1).

If the shares requested in the buy-back exceed the company's limits on re-purchase, the company must endeavor to allow the remaining shares to be purchased by a third party.[302] Companies may repurchase issued shares provided that:[303]

- The re-purchase of shares does not cause the company's net assets to fall below the subscribed capital plus the company's mandatory reserves
- The total nominal value of all repurchased shares and any pledge of shares or fiduciary security over shares held by the company itself (or another company whose shares the company owns, whether directly or indirectly) does not exceed 10 percent of the total amount of capital subscribed in the company or any other maximum levels that may be set by applicable capital market regulations

The following requirements of buyback are applicable to banks:

- The shares have been issued for five years
- The buyback is for a certain purpose, for example a share reserve in the event of employee stock option or management stock option programs or avoidance of take-over action[304]
- The buyback is in accordance with applicable laws, such as the ICL and other capital market regulations
- The buyback is approved by OJK
- The buyback does not decrease capital below the minimum capital requirement

In practice, a company is also not allowed to repurchase its own shares under any of the following conditions:

- The company is conducting business operations at a loss, or owes overdue debts
- The company is offering shares to mobilize more capital
- The company is splitting-up or splitting-down shares
- The company's shares are subject to public bids

A company is not allowed to purchase shares from the following entities for use as treasury shares:

- Its managers and their spouses, parents, adopted parents, children,

[302] ICL, Article 62(2).
[303] ICL, Article 37(1).
[304] OJK Regulation No. 11/POJK.03/2016, as amended by OJK Regulation No. 34/POJK.03/2016, Elucidation of Article 13(b).

adopted children, or blood siblings

- Share owners subject to transfer restrictions according to law or the AoA
- Shareholders holding controlling shares, except for cases in which the shareholders sell shares to reduce their ownership percentage.

Table 15 summarizes the rules that apply to share buybacks. The rules differ depending on the purpose of the buyback, whether it is to decrease the charter capital (specific buyback) or for any other reasons (general buyback).

Table **15** Types of Buyback

Specific	General
The shares issued by the company are repurchased and retired to decrease the charter capital.	The shares issued by the company are repurchased for other reasons.
The decision to decrease charter capital by retiring treasury shares is made by the GMS, unless otherwise provided by the charter or by-laws.	The decision to purchase is carried out by the GMS. Under specific legal circumstances this decision can be made by the BoD.
Shares must be retired upon the buyback.	Purchased shares must be replaced or retired within a certain period.

To repurchase its own shares, a company should follow the steps summarized in *Table 16*.

Table **16** General Buyback Procedures

Initiation	The buyback is initiated at the discretion of the BoD or a shareholder proposal.
Decision-making	The GMS must provide its approval.
Limitations	A joint stock company is entitled to buy back no more than 30 percent of its issued common shares and may buy back a portion or all of its sold preferred shares.
Retiring shares	Shares must be retired within a certain period (three years) or re-placed if the capital contributed by shareholders is smaller than the charter capital.

The company must have a plan for share capital redemption which clearly states details on the timing and pricing of this redemption. For the redemption of treasury shares, the company must also have sufficient capital from either a capital surplus, retained earnings, or other sources stipulated by law.

There is no specific regulation governing requirements for information that must be included in the notice of a decision to buy back shares. In practice, companies should at least provide the following details to all shareholders:

- The name and address of the company's head office
- Total number and type of shares to be repurchased
- Price the company is offering to pay for the repurchase
- Procedures and time limits for payment
- Procedures and time limits for a shareholder to offer his/her shares to the company

Indonesian law does not specifically regulate pro-rata share buybacks. Indonesian law also does not regulate disclosure obligations for share buybacks other than to report the change in shareholding composition to the MOLHR. In case the company cancels shares resulting in a reduction of capital, the decision of the GMS to reduce capital must first be announced to the public in at least one daily newspaper.

However, public companies must disclose the following information in their report of all planned share buybacks:

- Estimated schedule, estimated costs of the buyback, and estimate of the nominal value of all shares to be purchased
- Explanation, consideration, and reason for the buyback
- Estimation of the decrease of the company's income as a result of the buyback and the effect of the buyback on the financing costs of the company
- A pro forma yield per share after the completion of the buyback, after considering the decrease of the company's income
- Limitation on the price of shares for the buyback
- Limitation on the buyback period
- Method that is used for the buyback
- The management's analysis and discussion regarding the effect of the buyback to the company's future business and growth

Public companies listed on the IDX must make an additional buyback report to the IDX, including the information listed above. They must also disclose these details via the IDX's specific mechanisms for information disclosure.

13.3.3 Reciprocal Shareholdings

Reciprocal or cross-shareholdings are quite common between different companies and may be set up to establish mutual influence or to diversify portfolios. However, reciprocal shareholdings are explicitly prohibited by the ICL. The prohibition does not apply in case the shares are acquired from a transfer by operation of law, grant, or bequest.[305]

[305] ICL, Article 36.

13.4 Statutory and Voluntary Reserves

Beyond protecting its charter capital, a company must maintain a level of reserve funds that can be used as a safeguard to protect creditor interests. Indonesian law requires companies to maintain a minimum reserve (statutory reserves), which they may choose to augment voluntarily (voluntary reserves). As with the charter capital, statutory and voluntary reserves exist only in accounting terms as recorded in the company's balance sheet.

13.4.1 Statutory Reserve

The ICL requires companies to have a mandatory reserve fund (statutory reserve) every time the company maintains a positive balance of profits. The company must set aside net profits until the reserve reaches at least 20 percent of the total subscribed and paid-up capital.[306] The statutory reserve's main purpose is to protect creditors by ensuring that the company maintains a portion of its assets, in addition to the charter capital, which it cannot distribute to shareholders.

13.4.2 Other Funds

Beside statutory reserves, a company may also establish other funds (voluntary, non-obligatory reserves):

1. **Employee Funds**

   The GMS may choose to establish a special fund from its net profits for company employees at its discretion. Since this is not a requirement under the ICL, the company must specify all details concerning the management of this fund in its AoA or other internal regulations. For example, the fund can be created for the purpose of acquiring shares, provided that

[306] ICL, Article 70.

such shares are to be transferred to the company's employees.

2. Other Company Funds

The AoA, internal regulations, or a GMS decision may establish other internal funds, such as financial reserves or investment and development funds. Such internal funds are financed through a deduction from the company's net profits.

3. Additional Paid-In Capital

Additional paid-in capital forms part of the company's equity and is typically composed of the following sources:

- Any increase resulting from the revaluation of non-current assets
- The positive difference between the nominal value and the placement value of the company's shares

Additional paid-in capital has only an accounting meaning, since there is no actual accumulation of funds. Additional paid-in capital can be used, for example, to:

- Offset losses that arise following revaluation of non-current assets
- Increase the charter capital from internal company resources

CHAPTER 14
Corporate Securities

THE CHAIRMAN'S CHECKLIST

- When was the last time the company rigorously examined its financial position?
- If the company needs external financing, what are alternative sources? What are the advantages and disadvantages of debt versus equity financing? What are the costs? What is the company's optimal debt-to-equity ratio? What are the corporate governance implications of each of these alternatives?
- What financing method will be most appropriate for the company and why?
- Has the company explored international financing options?
- What are the advantages and disadvantages of accessing capital in foreign markets? What are the corporate governance implications of listing on foreign exchanges?
- What are the disadvantages and advantages of stock options?

Companies have a number of options when they need to obtain finance. They may fund their investment needs from internally generated capital, if available, or seek external financing. Among external sources of funding, they may borrow from banks or issue securities.

Financing decisions are usually quite complex. The methods that a company chooses to finance its operations will depend on many internal and external factors. Some factors that are specific to the company include the intended use of the funds (whether for short-term working capital needs or long-term capital investment), the capacity to service interest payments and to repay principal, and the nature of the company's business, including the degree of risk involved. Important external factors include the home country's level of economic development, political stability, and regulation of its banking system and financial markets.

Each financing option, whether bank lending or the sale of shares or bonds, has its own financial and legal characteristics with different corporate governance implications. Equity finance has some important advantages for companies. Although it is not the cheapest source of funding, equity finance has the advantage of permitting companies to access large amounts of capital that do not need to be paid back in the same manner as debt financing.

However, access to the enormous potential of securities markets, with its millions of potential investors, comes at a price. Securities markets are traditionally tightly regulated to protect investors from potential abuse by fraudulent company practices. Regulators, therefore, make significant demands on companies. They require that investors receive complete information on investment risk and go to great lengths to protect investor rights. While market regulators are often criticized for the burdens they impose on companies, the reasons for these regulations and corporate governance standards stem from the real and significant potential for abuse that is inherent in the securities market system. This chapter discusses the different types of securities that companies may issue and their corporate governance implications.

14.1 Overview of Corporate Securities

There are two basic types of securities that companies use to raise capital: shares (also referred to as stock or equities) and corporate bonds. Shares confer a level of ownership in the company in proportion to the value of the shareholding, and therefore encompass certain ownership rights. Bonds, on the other hand, represent a creditor relationship with the company. Unlike shareholders, bondholders have no corporate ownership rights, although they may be accorded a significant degree of control over certain corporate activities during the life of the creditor/debtor relationship.

Corporate bonds come in many different forms and structures. Bonds issued with a "coupon" set a specific interest rate (the coupon) which companies must repay periodically until the bond matures. Companies determine the maturity date at the time of issuing the bond and must repay creditors with the principal amount borrowed on this date. "Zero coupon" bonds, on the other hand, do not require interest payments. Instead of interest, zero coupon bondholders receive compensation through a discounted purchase price (zero coupon bonds are typically cheaper than bonds issued with a coupon) and gradual appreciation in the principal price to be repaid when the bond matures. Despite many differences, all types of bonds have one element in common, being that they come with predictable and contractually fixed repayment obligations.

Shares function differently. Companies can use share capital for an unlimited period and are under no immediate obligation to repay investors. Investors are compensated for their investment through rights which may include capital gains (an increase in the value of their shares), dividends, and rights to vote on company governance. From an investor's point of view, shares typically carry more risk than bonds, because unlike the fixed bond-repayment, capital gains from securities are never guaranteed (share prices go up and down) and if the company does not have a positive net income, dividends may not be distributed. An important implication of the difference in risk is that share capital is often more expensive than bonds or bank lending. One of the most fundamental rules of finance is the higher the level of risk, the greater the level of return that investors will expect for taking such risk. Given that the risk of receiving a return on one's investment is higher for shares than for bonds or other types of loan transactions, shareholders will demand a greater stake in the company in return for their capital investment.

One method to manage shareholders' demands is to grant governance rights, such as the right to vote on company decisions and board composition. To maintain investor confidence among shareholders and continue to attract capital investment, it is important that companies protect the rights of shareholders through accountable management and strong corporate governance structures.

Shares and bonds offer different advantages and disadvantages for investors and companies, as outlined in ***Table 17***.

Table **17** Comparison of Shares and Bonds

	Shares	Bonds
Duration of investment	Unlimited. The company does not repay the investment. The company is not restricted in how it may invest funds.	Bonds have a maturity date. While bonds differ, the principal is generally repaid with interest. Repayment is predictable and regular, which reduces risk to bondholders. Funds from the issuance of bonds must be invested in accordance with the proposed fund utilization as stated in the prospectus, unless the bondholder agrees to changes in how these funds are used.
Obligations in return for the investment	Investors may expect dividend payments when the company has positive net income. However, dividend payments are made at the discretion of the company.	The company must repay the principal and usually makes coupon payments.
Governance rights	If common shares are issued, the investor is granted governance rights. If preferred shares are issued, the investor holds governance rights only in specific circumstances (in case of voting preferred shares). Governance rights and their enforcement	No governance rights are granted to bondholders.

	Shares	Bonds
	reduce the equity investment risk.	
Ease of securing the investment	The ease of securing equity investment depends on numerous external and internal factors. Ultimately, the attractiveness of a share offering depends on the company's future prospects and its ability to assure shareholders and investors that their rights to capital gains/dividends will be respected. In addition, the company's financial stability and capacity to demonstrate transparent and accountable corporate governance will influence the extent to which investors will be willing to subscribe to its shares.	Bonds are attractive to investors interested in predictable and secure returns. The company's health, including compliance with good corporate governance practices, is important for the credit rating of the company and will influence the price at which it may borrow.
Cost	From the company's perspective, shares can be more expensive than bonds. Investors charge a premium for the higher risk associated with equities.	Bonds are less risky to investors than shares, therefore investors charge a lower risk premium for bonds as compared to securities. Bonds consequently carry less cost to the company, however the company also incurs an absolute obligation to repay the bondholder the full principal amount (plus interest/compensation) at a future date.
Advantages to investors	Most investors are compensated through capital gains (the increase in share price on the equity markets). If the company generates sufficient free cash flow, the shareholder may receive a dividend. The	The bondholder receives his/her principal back with some compensation for the investment, usually in the form of interest. Generally, interest payments are fixed in advance and predictable. If the company defaults,

	Shares	Bonds
	potential long-term returns on equities as an investment class are higher than bonds.	the bond may, under certain circumstances, still be sold on the market at a discount, meaning that the bondholder may not lose the full amount of his/her investment.
Risks	Shares potentially offer higher rates of return than bonds, depending on market conditions, but this is predicated on higher levels of risk. Share prices go up and down, at times quite dramatically. Capital gains on shares are uncertain and dividend payments are not guaranteed. If the company becomes insolvent, shareholders are typically last in line to receive compensation. In practice, shareholders may lose the full value of their investment in case of bankruptcy or liquidation.	Once the company has the cash, it may use the money for riskier activities than those foreseen by the bondholder. In such cases, the bondholder may have little recourse. In case of default, the bondholder is granted a set of legal mechanisms to enforce his/her contractual rights, including seeking the insolvency of the company. However, seeking insolvency is not generally in the interest of the bondholder. If the bond is secured, the risk to the bondholder may be minimized.

Technological innovation has transformed the way in which stock exchanges around the globe issue and trade securities. Many jurisdictions have replaced the traditional paper-based form of issuing securities (typically guaranteed by a stock-exchange certificate) with electronic/paperless or "dematerialized" methods of issuing securities.

In Indonesia, companies may issue shares and other securities (warrants, bonds) in either paper or paperless form, as determined in their AoA. Whichever form securities take, companies must comply with all relevant legal requirements. For securities issued in paper form, investors must ensure they record their information and ownership correctly in the company's shareholder register in order to fully realize the rights attached to their shareholdings. For paperless securities, rights of ownership are also derived from entry into a bond or shareholder register, similar to an entry in a bank account reflecting the

depositor's rights to funds.

IDX follows the common practice among most leading exchanges, including the United States, United Kingdom, Europe, and Australia, by facilitating electronic trading. As such, paperless securities in Indonesia are transferrable electronic documents. The ICL provides that a company's AoA must specify the method of transferring rights over shares in compliance with OJK and all other applicable regulations and that such exchanges are conducted through a deed of transfer.[307] All public companies must also register their securities—whether in paper or paperless form—with the Indonesian Central Securities Depository (*Kustodian Sentral Efek Indonesia* or KSEI).

Indonesian companies may raise finance on either domestic or international markets (e.g., the New York Stock Exchange) by issuing shares or bonds. Another way for companies to raise international capital is to issue shares indirectly through depositary receipts. Depositary receipts require the original security to be registered in the name of a foreign trust company or, more commonly, a bank. The bank holds the shares in safekeeping and issues receipts against the shares. These receipts are referred to as "depositary receipts". This system was developed because investors in the world's largest capital markets discovered it could take several months to have their foreign share purchases registered in their name. The system is also attractive for companies, since it allows them to establish a presence in foreign markets without having to go through the process of a complete issue. The corporate governance implications of this system mean that Indonesian issuers of depositary receipts must comply, to varying degrees, with foreign standards of corporate governance.

[307] ICL, Article 55 and 56(1).

14.2 Types of Securities

14.2.1 Shares

Shares (stocks or equities) entitle their holder to a set of property and governance rights. A share is a type of security that certifies its holders' legitimate rights and benefits to a portion of equity of an issuing organization/company. Shares have several fundamental characteristics:

Name of shareholder: The ICL requires companies to issue shares under the name of their respective owner (the shareholder). The BoD must maintain records of these shareholdings, including details of each shareholder, in the shareholder register.[308] The ICL further stipulates that rights attached to shares will take legal effect once these details are correctly entered in the register under the relevant shareholder's name.[309] Registering securities in this way improves the transparency of the company's ownership structure, and in doing so enhances the protection of shareholder rights.

Shareholder rights: The rights attached to each type of share a company issues (such as common or preferred shares) derive from the ICL and the company's AoA.

Nominal value: Each share has a nominal value, also referred to as par value, face value, or accountable par. In Indonesia, companies must state this value in rupiah and may not issue shares without setting the nominal value.[310] The company's AoA will state the nominal value or the accountable par of shares, which forms the basis for calculating the charter capital. The nominal value of all shares the company issues must generally be the same, unless the AoA provides otherwise or if market conditions so require (for listed companies). In the event the market price of a company's shares is lower than the nominal value, companies may issue new shares with a different nominal value to that originally set under the AoA. If a listed company chooses to issue shares with a different nominal value in this way, the issuance must meet the following requirements:[311]

[308] ICL, Article 50(1).
[309] ICL, Article 52(2).
[310] ICL, Article 49(2).
[311] OJK Regulation No. 31/POJK.04/2017 on Requirements for Issuing Shares with Different Nominal Values, Article 4.

1. Shares issued with a different nominal value will carry the same rights as all other shares in their respective share class.
2. Shares issued under the original nominal value cannot be converted into shares issued under the new nominal value.

The nominal value of shares rarely reflects the company's market value. Because market prices constantly fluctuate in response to a number of factors, including supply and demand, the difference between the nominal value and the price at which shares trade on the market can be significant.

The value of shares may be determined by investors and other professionals using different analytical methods. These methods take many factors into account, such as the company's current performance and future prospects, its dividend policies, reputation, macroeconomic conditions, and government support for, or interference in, business development. In this context, the quality of a company's governance structure embodies an important component in investment decisions. Strong corporate governance structures signal to shareholders that their ownership rights will be protected, thus making the company a more secure and attractive investment.

14.2.2 Bonds

Bonds (corporate bonds) are instruments through which companies raise finance by incurring a debt by borrowing funds from, rather than selling company stock to investors. When issuing bonds, the company promises to repay the lender/investor the amount borrowed (principal) plus interest (the coupon rate) over a specified period of time. The company will usually pay interest at specified intervals, such as semi-annually or quarterly. When the specified period ends, the bond matures and the issuer must repay the total debt owed to investors.

Nominal value: Companies will set the nominal value, otherwise known as face value or par, of their bonds. This is the amount of principal that the issuer borrows and must return to the bondholder when the bond has matured.

Rights of bondholders: The bondholder has the rights of a creditor and is entitled to:

1. Redeem the bond at maturity for its face value. A company can issue

bonds with schedules or a series of bonds with different payment schedules. The company may also choose to facilitate requests for early payment from the bondholder if appropriate.

2. Receive interest payable on the bond. Interest payments on bonds are generally referred to as coupons. Historically, bonds were issued with detachable coupons that were submitted in exchange for payment.
3. Convert into shares (for holders of convertible bonds). There are two types of bonds: convertible bonds and non-convertible bonds. Convertible bonds can be converted into shares in accordance with their terms of issue and with the requirements of the company's AoA, whereas non-convertible bonds cannot.

Since bonds are freely transferable, the bondholder can sell his/her bonds to another investor. As with equities, bonds are subject to a market pricing mechanism. This means that bond prices constantly fluctuate and that bondholders may make or lose money from buying and selling bonds.

Types of bond: Bonds encompass a broad array of different instruments whose terms and conditions vary significantly. The three principal types of bonds are registered and bearer bonds, unsecured bonds, and convertible bonds. Each type of bond has its own particular characteristics:

1. **Registered and Bearer Bonds**

   Registered bonds refer to bonds where the issuing company registers the bond's owner in its own accounting records, keeping the bondholder's name and contact information on file. This allows the company to ensure it makes all payments to the appropriate person/entity. If the bond is in a physical form, the owner's name will be printed on a certificate. In contrast, bearer bonds are unregistered, and the issuing company keeps no records of the owner or the transaction involving ownership. Bearer bonds reduce the administrative costs to companies since they do not need to maintain a bond register, and bearer bonds' anonymity can be attractive to investors by making transfer of ownership straightforward. However, this ease of transfer also allows unscrupulous bondholders greater opportunity to avoid laws and regulations in attempts to conceal assets from creditors and tax authorities when selling their bondholding. Bearer bonds therefore carry significant risk violations of securities and tax laws, and many jurisdictions, including the United States, Australia, and the United Kingdom, have prohibited the issuance of bearer bonds.

2. Secured and Unsecured Bonds

Companies may issue both secured and unsecured bonds. Secured bonds provide additional protections to bondholders in case the company defaults on its obligations. Types of guarantee that may be provided with secured bonds include:

- Pledge of company property: Securities can be the subject of a pledge. All secured bondholders of the same issue have equal rights with regard to the pledged property.
- Third-party guarantee: A third-party guarantee can be submitted to the company for the purposes of the bond issue. The third party may be a bank, a corporation (for example, a parent company guaranteeing bonds issued by a subsidiary), or a person. The guarantor is jointly and severally liable for the redemption of the bond.

For bonds secured by a pledge of property or a third-party guarantee, it is in the interests of bondholders and shareholders that the face value of such bonds does not exceed the value of the guarantee.

3. Convertible Bonds

Companies may also issue bonds that can be converted into shares. Convertible bonds may be secured or unsecured. Convertible bonds may be exchanged for a set number of common shares at a pre-determined price. Issuers may choose to issue bonds with a convertible feature to make the bond more attractive to potential creditors and enhance the marketability of the bond.

Under Indonesian law, foreign investment by way of purchasing convertible bonds will not trigger foreign investment restrictions, unless those bonds are converted into equity shares. This is because the Ministry of Finance defines the purchase of convertible bonds as "quasi-equity" rather than "equity" participation in a company, and "quasi-equity" participation is permitted under Indonesian foreign investment law.[312] Also, Indonesian investment law[313] considers investment in Indonesian listed companies through the debt capital markets to be portfolio investments, which are also not subject to foreign investment restrictions. The rationale for allowing Indonesian companies to raise foreign capital through foreign portfolio investments and convertible bonds is that investors and companies engage in such transactions for capital gains only and not to facilitate the foreign investor's long-term participation in company.

[312] Presidential Regulation No. 44 of 2016 on List of Business Sectors that are Closed to Foreign Investments and Sectors that are Conditionally Open for Foreign Investments ("Negative List").
[313] Law No. 25 of 2007 on Capital Investment.

Commercially, while the benefits of holding convertible bonds include those of regular bonds (such as interest payments, capital gains, and the first right to reclaim principal), the primary benefit to investors lies in the option to convert these bonds into company shares. However, commercial bonds also pose risk, such as potential for company default and the resulting loss of capital. More significantly, another feature of convertible bonds is that they allow the issuing company to "call" the bond prior to its maturity date, which forces bondholders to convert their investment into company shares at a pre-determined price. The selling company controls this price at the time of bond issuance by setting a bond-conversion ratio. The final price at conversion will be calculated by dividing the nominal value of the bond by its conversion rate. Moreover, if at the time of conversion the company's average share price exceeds the share price at the time of bond issuance, the company maintains the right to make appropriate adjustments to the bond-conversion ratio.

Differences between shareholder and bondholder interests: Both shareholders and bondholders have interest in the company's profitability and financial health. For shareholders, a well-functioning company generates cash flow, raises market value, and will be more likely to pay dividends than businesses that are underperforming. For bondholders, a strong financial position reduces the risk that a company will default on its obligation to repay the principal and interest owed at maturity. As such, a successful and profitable company will increase in market value over time and generate significant returns for investors in both shares and bonds. There are, however, some important differences between the interests of these two types of investors.

- Interests between shareholders and bondholders diverge most distinctly during insolvency. During insolvency proceedings, different priorities are assigned to different types of claimants. In general, creditor claims (including those of bondholders) will always be satisfied before those of shareholders.
- Shareholders and bondholders have different risk appetites. Shareholders will generally accept a higher level of corporate risk-taking than bondholders in exchange for potentially higher returns. Both shareholders and bondholders stand to lose if a company's risky business policies fail (for example, shareholders will see significant reductions to the value of their investment and bondholders face the risk that the company will not have funds to repay its debt). However, when a company's business policies are successful, the returns to shareholders can be significant. Bondholders will, on the other hand, always receive the same contractually stipulated return regardless of the level of risk involved

in the projects the company undertakes. Because bondholders stand to gain little, but have much to lose from risky corporate business practices, such investors typically hope to see a predictable, stable cash flow and, if possible, a reduction in the company's risk profile.

- However, shareholders and bondholders (particularly holders of convertible bonds) have a similar interest in limiting the dilution of their holdings. Shareholders are always interested in preventing their shareholdings from being diluted. It is, in part, for this reason that they enjoy governance rights, and why company decisions that may dilute share ownership will always require approval from the company's governing bodies. Similarly, holders of convertible bonds are interested in preventing reduction of capital or redemption of shares when this conflicts with the exercise of their conversion rights.

Best Practice

In some countries, company laws incorporate special measures to balance the interests of shareholders and bondholders by:

- *Granting bondholders consultation rights. In France, for example, companies must consult with bondholders before pursuing many financing policies, such as reorganizing or issuing bonds that are secured by significant company assets.*
- *Allowing bondholders to inspect documents during the GMS, as is the case in Germany.*
- *Prohibiting the redemption of shares and reductions in share capital in some circumstances. France, for instance, prohibits companies from redeeming shares or reducing share capital while bonds are open to conversion or being offered. France also protects bondholders' rights with respect to the availability of information and may require companies to provide bondholders with information that may be of special concern to them.*

Companies may wish to develop specific policies with respect to bondholders and are encouraged to integrate them into their

overall corporate governance practices. Holders of convertible bonds and share warrants have the same rights as shareholders with regard to information and inspection of the company books and documents, unless otherwise provided by the decision on the issuance of such securities or agreed otherwise.

14.3 Issuing Securities

Issuing securities is a complex process that involves a transfer of funds in exchange for specific rights (such as rights to share in the company's profits through capital gains and dividends, governance/voting rights, etc.) that are subject to different assurances and guarantees. Efficient capital markets help companies raise finance for productive use. They also allow investors to reap returns on capital that might otherwise lie dormant and to select investments that correspond to their desired level of risk and return.

Capital markets cannot bring users and providers of capital together unless they are managed with accountability and transparency. Unfortunately, the history of international financial markets is rife with examples of abuse resulting in market failure. Regulators should design securities legislation in such a way as to protect the interests of both companies and investors, while also supporting efficient capital markets.

In Indonesia, securities regulations determine the procedures and conditions for the issuance of securities, whether through company stock or bonds. OJK is responsible for protecting the legality and transparency of these transactions. Securities legislation primarily applies to public companies, which bear different and typically more onerous obligations than private entities. Every limited liability company can issue shares through public offer or private placement; however, the legal requirements for these types of public or private issuance are different.

All public offerings must be registered with OJK. However, certain types of companies (such as banks, financial institutions, or insurance companies) require additional approval from relevant authorities to register a public offering of shares with OJK. ***Table 18*** summarizes the legal requirements for private and public offerings that apply to different types of companies.

Table **18** Legal Requirements for Issuance of Securities

	Private Offering	Public Offering
Limited Liability Company (Private)	May issue both shares and bonds. In case of bond issuance, if the issuer is a state-owned entity, the	May issue both shares and bonds. For shares, an initial public offering will be subject to specific

	Private Offering	Public Offering
	issuance plan must be approved by the Ministry of Finance. The decision to issue shares and the report on the results thereof are subject to registration with a business registration agency. The company will store the shareholder register at its corporate headquarters.	legal requirements. After the public offering, the company will become a public company and must fulfill the obligations of a public company as required by Indonesian Capital Markets Law. Dossiers for registration of public offering of securities shall be regarded as public company dossiers.
Public (Non-Listed) Company	May issue both shares and bonds. The decision to issue shares and the report on the results thereof are subject to registration with OJK. Must register private issuances of securities with OJK. Changes to the AoA concerning issued shares must be registered with the business registration agency.	May issue both shares and bonds. The registration dossiers of the public offering of securities must be prepared and submitted to OJK. The securities must be registered with the Indonesia Central Securities Depository or KSEI. The change in the charter capital for shares issued must be registered with the business registration agency.
Public Listed Company	May issue both shares and bonds. The decision to issue shares and the report on the results thereof are subject to registration with OJK. Must register private issuances of shares with OJK and KSEI. The change in the charter capital for shares issued must be registered with the business registration agency.	May issue both shares and bonds. The registration dossiers of the public offering of securities must be prepared and submitted to OJK. The securities must be registered with KSEI. The change in the charter capital for shares issued must be registered with the business registration agency. The shares issued must be admitted to a stock exchange.

The process of issuing securities involves several steps, which have different requirements depending on the issuing company (whether public or private), the type of securities involved, and methods used for the issuance. To issue bonds, companies must comply with specific capital market regulations and procedures set under the AoA. The following sections discusses the steps required to issue shares and bonds in greater detail and highlights key differences.

14.3.1 Decision Making Authority

Different company organs are responsible for making the decision to issue securities in Indonesia, with different requirements depending on the type of security and any other specific procedures set under the AoA.

Table **19** Decision Making Authority for Issuance of Securities

Shares	The GMS generally makes the decision to issue shares.
Convertible and Non-Convertible Bonds	In practice, the GMS typically makes the decision to issue convertible bonds, which will be converted into shares at maturity. The BoD typically makes the decision to issue non-convertible bonds. Specific requirements also apply if the issuing company is a state-owned entity, in which case the Ministry of Finance must approve all private bond offerings.

The GMS must authorize all company decisions to issue securities by passing a resolution, which will serve as the main document to certify the rights and obligations of the holders of securities and of the company. The specific contents of the resolution will vary depending on the circumstances of the issue. However, the document should generally include the following information at a minimum:

- Details on the issuing company: full name, place of business, and postal address
- Decision to issue securities: date and the decision-making body

- Securities to be issued: type and class, their nominal value, the rights of the holders of securities, and the number of securities to be issued
- Conditions of placement

For bonds, the resolution must include additional information on:

- Form of bond redemption (monetary or in-kind)
- Maturity date (and details regarding early redemption, where applicable)
- Other terms of redemption, i.e., the value of the payment, if early redemption is possible
- For convertible bonds: procedures for conversion into shares
- For secured bonds: information on the security or the person submitting the guarantee and the conditions of the guarantee (in the latter case, the decision must also be signed by the guarantor)

In Indonesia, the capital markets regulator (OJK) closely monitors the mandatory content of the company decision to issue securities and ex-ante OJK approval will typically be required for issuances to be legitimate.

14.3.2 Registering a Decision to Issue Securities

In general, an issuing company making a public offering of securities must register its decision to issue securities with OJK, unless in the case of:

- Offering debt securities with a maturity of less than one year
- Issuance of a certificate of deposit
- Issuance of insurance policies
- Issuance of securities by the Government of Indonesia or securities guaranteed by the Indonesian government
- Offering other types of securities as determined by OJK

For issuances made to increase share capital, best practice guidelines recommend companies should register the decision to issue shares within six months.

In Indonesia, all public offerings are subject to OJK approval. Companies must submit a Registration Statement to OJK and obtain OJK's authorization of the statement's validity. A Registration Statement for public offerings of shares must

include at least:[314]

1. Cover letter
2. Prospectus
3. Brief prospectus
4. Initial prospectus (if any)
5. Other documents, consisting of:
    - The proposed issue schedule
    - A draft of the securities certificate
    - A copy of the latest AoA that the MOLHR has approved or been notified of
    - An audited financial statement
    - A letter of comfort from the accountant with respect to changes after the date of the audited financial statement
    - A written statement from the issuer addressing accounting matters
    - Further information on forecast or projection, if included in the prospectus
    - A legal audit report and opinion
    - The curriculum vitae of members of the BoC and BoD
    - The underwriting agreements (if any)
    - A structure that describes the company position vertically from individual shareholders up to subsidiaries and the position of the company horizontally
    - A statement by the company in the form as attached to the regulation
    - A statement of the capital market supporting professional
    - A statement from the underwriter (if any)
    - Other information requested by OJK as deemed necessary

The prospectus is the primary document that companies must provide when registering an offering. A prospectus covers detailed corporate information that is important for investors and sets out the rights and duties attached to the shares on offer, including risks, returns, and any other relevant materials associated with the investment. There are costs attached to the preparation of a prospectus that some companies may wish to avoid. However, the long-term benefits of preparing the prospectus are likely to outweigh any short-term costs.

[314] OJK Regulation No. 7/POJK.04/2017 on Document of Registration Statement in the Context of Public Offering of Equity Securities, Debt Securities, and/or Sukuk, Article 3 and 7.

By clarifying the projected risks and returns, the company will be more likely to attract investors and reduce capital costs. For investors, the details presented under the prospectus helps them to make informed investment decisions. The Capital Markets Law protects investor interests in this regard by making it a mandatory legal requirement for companies to produce a prospectus when making any public offerings.

Contents of the Prospectus

Indonesia's Capital Markets Law defines the company prospectus as a written document produced in relation to a public offering that is made to attract another party to purchase securities.[315] OJK Regulation No. 8/POJK.04/2017 contains detailed provisions setting out the information that companies must disclose, as follows:

1. **The *introductory section* of the prospectus should consist of:**

   Part One:

   - Date the public offering becomes effective
   - Offer period
   - Allotment date
   - Refund date
   - Distribution date
   - Listing date
   - The company's full name, business address, logo (if any), telephone, telex, facsimile, and post office box number (head office, factories, and any representative offices) and its main business activity/activities
   - Name of the securities exchange(s) (if any) where the securities will be listed
   - Nature of the offering, including a description of the essential elements, amount, nominal value, and price of the securities
   - Full name of the managing underwriter and other underwriters, if any
   - Place and date of issuance of the prospectus
   - The following statement in large type, which directly attracts the attention of readers: "OJK HAS NOT APPROVED OR DISAPPROVED THESE SECURITIES, NOR DOES IT PASS

[315] Capital Markets Law, Article 16.

JUDGMENT UPON THE ACCURANCY OR ADEQUACY OF THIS PROSPECTUS. ANY CONTRADICTING REPRESENTATION THERETO IS ILLEGAL. THIS PROSPECTUS IS AN IMPORTANT DOCUMENT WHICH REQUIRES IMMEDIATE ATTENTION. IF IN ANY DOUBT WITH RESPECT TO ITS CONTENTS, CONSULT THE COMPETENT PARTIES."

- A statement that the issuer and underwriter, if any, are fully responsible for the truthfulness of all information and fairness of opinions disclosed in the prospectus as follows: "THE ISSUER AND UNDERWRITER(S), (if any), ARE FULLY RESPONSIBLE FOR THE ACCURACY OF INFORMATION OR MATERIAL FACTS, AND OBJECTIVITY OF OPINIONS INCLUDED IN THIS PROSPECTUS."
- A statement in capital letters which draws readers' attention to risk factors and any issues concerning liquidity of the securities offered

Part Two

- If there is an intention to stabilize a certain securities price on an exchange in order to facilitate the public offering, there must be a statement with the following content in large type to attract the attention of readers: "IN ORDER TO MAINTAIN A STABLE MARKET PRICE FOR SECURITIES OFFERED IN THE SAME OR SIMILAR TYPE OR CLASS AS SECURITIES OFFERED IN THIS PUBLIC OFFERING, THE UNDERWRITER MAY SET THE OFFERING PRICE AT A HIGHER FIGURE THAN WOULD OTHERWISE EXIST ON THE SECURITIES EXCHANGE IF THE PRICE WERE NOT SET AT THIS FIGURE. WHERE THE UNDERWRITER CONDUCTS PRICE-STABILIZATION IN THIS WAY, BOTH THE SET-PRICE AND THIS PUBLIC OFFERING MAY BE TERMINATED AT ANY TIME."
- Information that the Registration Statement has been submitted to OJK in accordance with capital market regulations
- A statement that all the capital market supporting institutions and professionals mentioned in the prospectus are fully responsible for the data presented in accordance with the existing regulations as well as their respective codes of ethics and professional standards
- A statement that no affiliated person is permitted to provide

information or statements regarding data that are not disclosed in the prospectus without written authorization from the issuer or managing underwriter, if any

- Whether a securities exchange has given preliminary approval for the securities to be listed and the action that will be taken if the securities exchange rejects the issuer's listing application
- In the event the prospectus names a party that assisted the company in the preparation of the prospectus, such party shall make a statement that it has granted written approval on the inclusion of the party's name and not revoke such approval

2. **The *main section* of the prospectus should consist of at least:**
    - Principle details of the public offering
    - Planned uses of funds obtained from the public offering
    - Statement of Liabilities Management Analysis
    - Arrangements to manage business risk
    - Important events following the date the Auditor's Report is issued
    - Description of the issuing company
    - Details on the issuing company's business activities
    - Summary of material financial information
    - Stockholders' equity
    - Taxation
    - Underwriting (if any)
    - Capital market supporting institutions and professionals
    - Legal opinion
    - Financial statements
    - Appraiser's report (if any)
    - Terms for orders to purchase securities
    - Distribution of prospectus and order forms

OJK requires companies to publish a Summary Prospectus in at least one daily Indonesian newspaper with nationwide circulation no later than two business days from receiving notice of OJK's authorization of the public offering.[316]

[316] Decision of the Chairman of the Capital Market and Financial Institutions Supervisory Agency No. KEP-122/BL/2009 (Regulation IX.A.2), Article 2(b).

Best Practice

It is good practice to disclose all information that is material to the company's value and prospects for shareholders and prospective investors in the prospectus. In addition, for prospectus documents specific to public offering of bonds, the issuing company ought also to provide information on the company's investment ratings by international standard ratings agencies, such as Standard and Poor's (S&P), Moody's, and Fitch.

S&P, Moody's, and Fitch each apply different ratings systems, but share the same objective. These ratings agencies exist to provide investors with an independent evaluation of whether issuing companies will be able to meet their debt obligations with respect to the securities that they offer and therefore the relative level of risk involved in such investments. An important note is that while the ratings can offer a general assessment of the issuing company's credit worthiness, they are not intended to act as stand-alone recommendations. Investors may take note of a company's ratings, but should not rely on these benchmarks as their sole source of information from which to base investment decisions.

Prospectus Approval by the Company

The issuing company is responsible for ensuring the information it provides in the prospectus is true and complete. All persons involved in preparing the prospectus, including any consulting companies, underwriters, external auditors, anyone who signed the auditor's report, and any organizations or individuals who signed the registration documents, may be liable for damage caused by inaccuracies or omissions in the prospectus documents. This liability will arise if such persons had knowledge, or by the nature of their position ought to have known, that the information was inaccurate; for instance, the president director, chief accountant, and external auditor will always be liable. All parties with the requisite knowledge will be jointly and severally liable, together with the issuing company, for any damage caused to investors due to untruthful, incomplete, or misleading information. In some countries, if investors believe that they have suffered damage as a result of information contained in (or omitted from) the prospectus, they may file a claim in court.

14.3.3 Approval of Securities Registration Dossier

For all public offerings in Indonesia, issuing companies must obtain approval from OJK and complete the registration process for the issuance. This requirement creates important protections for investors by ensuring OJK supervision over the public offering and affords OJK a level of control over the securities issuance process.

When examining a company's supporting documents (the dossier) to support a public offering, OJK may request issuing companies to modify or supplement the information provided to ensure it is both accurate and complete. Within forty-five days of receiving the dossier, OJK will decide whether to grant a securities certificate to validate the offering. If OJK refuses the company's application, the regulator will provide reasons for refusal in writing. If the issuing company is unable to provide OJK with valid information and documents as required, it may take significantly longer than forty-five days to obtain OJK approval. As such, companies should prepare their files for submission to OJK carefully, and make sure that all third parties, including consulting companies, underwriter, auditing company, and auditors that are involved in the process are competent and appropriately accredited.

Upon receiving OJK approval in the form of a Prospectus Letter of Effectiveness and securities certificate, the issuing company must make a public announcement of the issuance within two business days from the date of the securities certificate, after which it may begin placing securities.[317] The placement of securities is the actual transaction between the company and investors. This transaction is subject to several legal requirements and will only take effect upon compliance with the following procedures:

1. **Number of Securities Placed**
   The number of securities placed should be no more than indicated in the GMS resolution authorizing the decision to issue securities. The number of securities placed may, however, be less than the number indicated in the prospectus. This is because, in practice, the company's capacity to sell securities depends on investor demand, which may or may not meet the number of securities set in the GMS decision. The company must disclose the actual number of securities placed in its report on the results of the issue.

[317] Decision of the Chairman of the Capital Market and Financial Institutions Supervisory Agency No. KEP-122/BL/2009 (Regulation IX.A.2), Annex 2(b) in conjunction with Attachment 9.

2. **Publication of the Announcement**
After the date of receiving the OJK Registration Statement, but prior to making its public offering, issuing companies must fulfill the following requirements:
    - Publish any corrections or additions to the summary prospectus, if any, in at least one Indonesian language daily newspaper with national circulation no later than two working days from the date OJK issues the Prospectus Letter of Effectiveness.
    - Distribute the formal prospectus as required under the Registration Statement to the public or the prospective purchasers.
    - Submit a soft-copy and two hard-copies of the prospectus to OJK.
    - Submit the proof of the announcement no later than two working days from the date of that announcement being made.

3. **Commencement of the Offering**
The securities offering commences at the time the company makes its public offering. This must be no later than two working days from the date the Registration Statement becomes effective, and the period of offer may last a maximum of five working days. Investors must pay for securities purchased at the time they are transferred under the investor's name.

4. **End of the Offering**
Either the underwriter or issuing company (if not using an underwriter) must report on the results of the public offering to OJK no later than five working days from the allotment date. In addition, the underwriter or issuer must appoint an auditor registered with OJK to conduct examination of the receipt of funds from the public offering by the issuer. The auditor must submit this report for examination to OJK no later than thirty working days after the public offering period expires. For the securities issuance to be legally valid, the issuing company must comply with multiple deadlines as set-out in ***Figure 28*** and ***29*** below.[318]

[318] Decision of the Chairman of the Capital Market and Financial Institutions Supervisory Agency No. KEP-122/BL/2009 (Regulation IX.A.2), Exhibit 12.

Figure **28** Public Offering Process (before registration is effective)

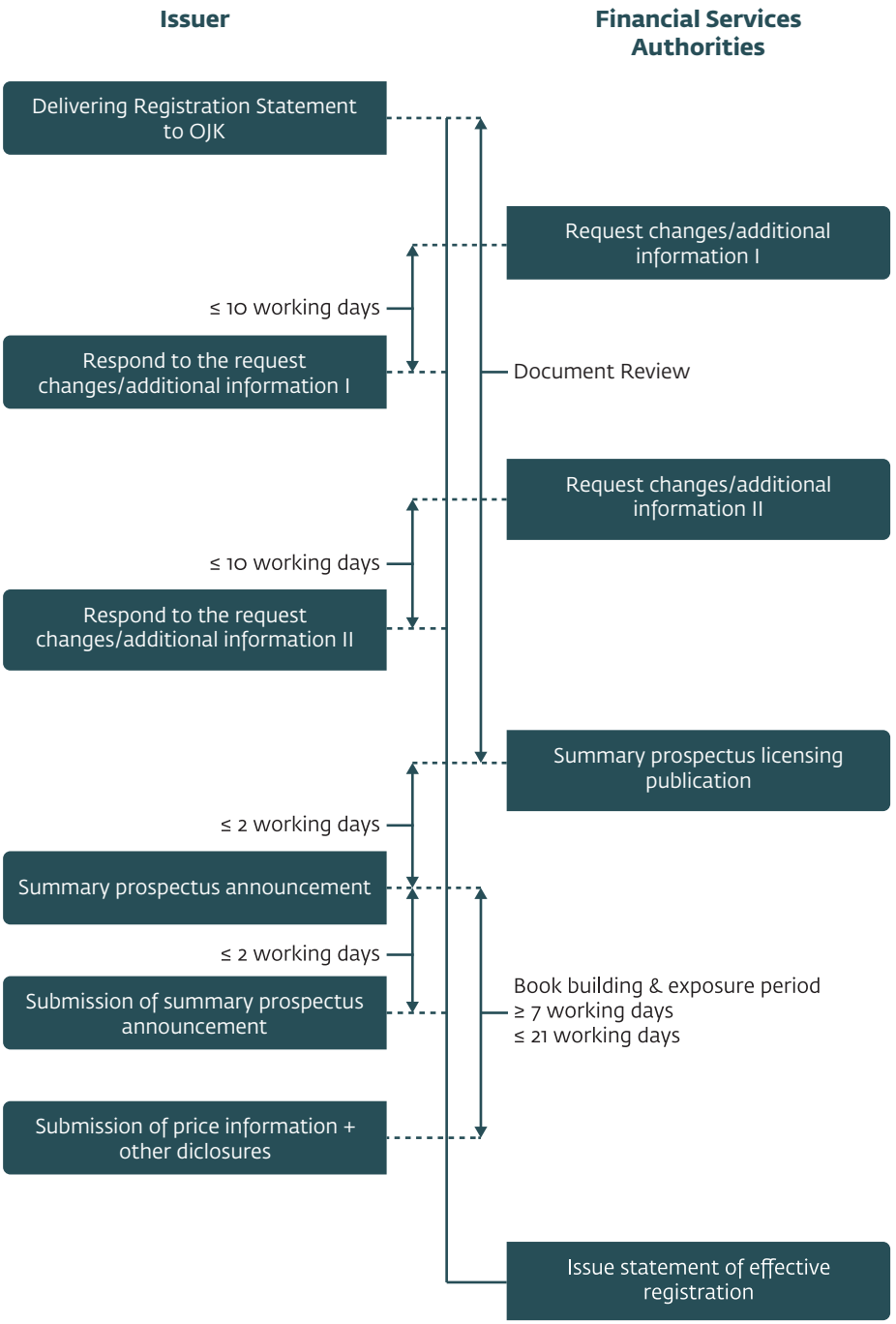
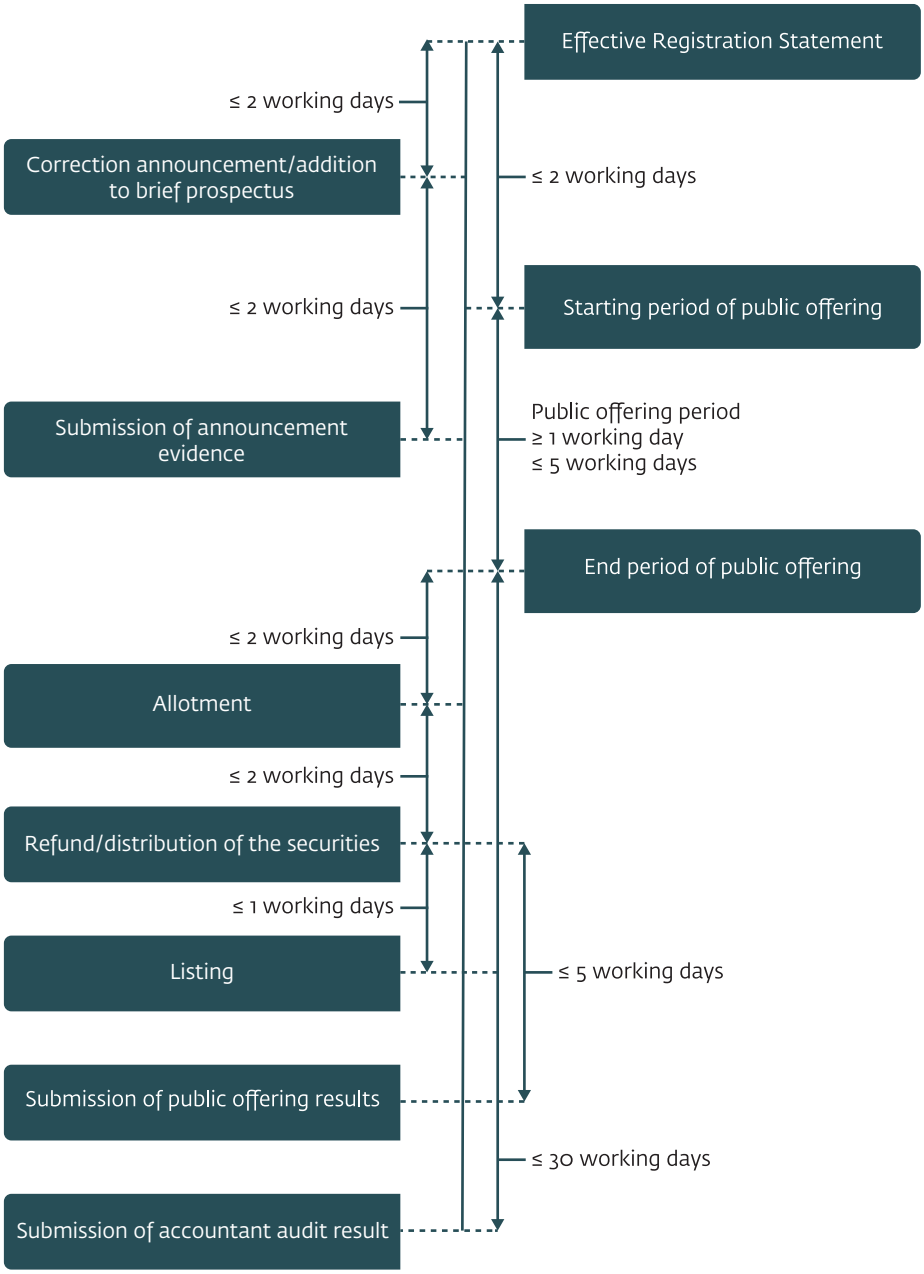


Figure **29** Public Offering Process (after registration becomes effective)



The GMS has the right to determine the issue price for securities offered. However, restrictions apply in order to prevent directors or large shareholders from acquiring securities at below market price (see ***Table 20***).

Table **20** Issue Price

Security	Price
Shares	The minimum nominal value for each share is Rp 100. The issue price must correspond to market value.
Convertible Bonds and Warrants	• Shares must be offered to all shareholders in proportion to their current respective percentage of shares in the company. • When exercising pre-emptive rights, shareholders can acquire convertible bonds or warrants at a price no more than 10 percent lower than the price determined for other investors.
Non-Convertible Bonds	The bond's value will be reflected in the bond yield. Depending on the nominal yield on the bond (which is the interest that will be paid to investors based on the coupon/interest rate and divided by the face value of the bond) compared with the market bond rates, the issue price of bonds may vary significantly.

When public issuances result in any changes to the charter capital, companies must amend their AoA accordingly. When raising finance by issuing securities to increase charter capital, the issuing company must register this increase with an authorized business registration agency within the timeframe prescribed by that agency.[319]

[319] Law No. 3 of 1982 on Company Registration Obligations, Article 25(1).

14.4 Conversion of Securities

Companies not only issue securities when seeking to raise capital, but also when an issuance is necessary to restructure/convert existing securities or the rights attached to them. Companies may convert existing securities under the following circumstances:

- The company intends to decrease charter capital by decreasing the nominal value of shares without changing the number of shares. By this mode, the company withdraws shares from shareholders and issues new shares with a reduced par value. The company will need to pay its shareholders an amount of money equal to the number of shares held by each shareholder multiplied by the difference between old and new par values. Currently, there is no specific regulation or guidance on increasing the charter capital by increasing the nominal value or accountable par of shares.
- To split shares
- When necessary to convert one type and class of shares into another
- When necessary to convert bonds into shares
- When necessary to reorganize the company

Procedures for converting existing shares are simpler and quicker than for issuing additional shares, because it does not change the charter capital. The conversion of convertible bonds into shares does increase the issuing company's charter capital, however, the effect of this conversion is anticipated from the time the company issues the bonds.

14.5 Derivatives

Shares and bonds are primary securities that confer a specific set of rights on their owners. Companies may also issue derivative instruments that embody rights, depending on the performance of underlying or primary securities, assets, or other property. Such instruments can, in international practice, relate to both equities and debt securities. The Capital Markets Law stipulates that derivatives also include rights, warrants, options, or futures contracts.

Types of derivatives that companies may issue to raise finance include:

- **Rights**: A type of security instrument available only to joint stock companies, meaning that shareholders may buy or sell their own shares. Such companies may offer rights (such as rights to dividends) to existing shareholders when issuing additional new shares to ensure these shareholders can buy the new shares under specified conditions. Shareholders can transfer their rights to others within a specified period.
- **Warrants**: A type of security instrument that companies may offer when issuing bonds or preferred shares that entitles warrant-holders to buy a specified number of common shares at a designated price within a given period.
- **Stock Options**: A call option on the common stock of a company, issued as a form of non-cash compensation. In practice, stock options can play a key role in the context of executive remuneration programs and may have significant corporate governance implications.

In the corporate governance context, a relatively mundane form of option, such as the incentive stock option, is used to provide performance-enhancing incentives to management and employees. In some countries, options represent a primary component in remuneration packages for top executives. These are popular because the returns to executives can be large. The incentive stock option ostensibly aligns the interests of management and shareholders, by rewarding management for actions that benefit and increase the value of the company and because the true cost of options (the dilution of other shareholders) is not readily apparent under current accounting standards. Stock option compensation is a complex and contentious remuneration technique that requires close monitoring by the company's governing bodies, GMS approval, and detailed disclosure in the company's annual financial statements.

Shareholders need to be aware of the company's use of this tool, since it could potentially expose the company to unexpected and significant risks.

Other types of derivatives, such as call options, put options, futures, securities classes, or indexes, are used primarily by financial institutions (i.e., banks, securities firms) for trading purposes or as risk-reduction instruments. Use of derivatives in trading can be seen more commonly on the secondary market, where the main players are securities companies, institutional and individual investors, and other financial institutions such as banks and insurance companies. These derivatives are highly standardized and may be used only in officially designated (international) markets. Further, derivatives trading occurs primarily in mature financial systems rather than in emerging capital markets such as Indonesia.

14.6 Raising Capital in International Markets

Indonesian companies may raise capital in international markets by issuing bonds or shares, provided they satisfy the following conditions:

- The company's business activities cannot be listed as 100 percent owned by foreign investors under the Negative Investment List, and companies which are partially closed must abide by the foreign participation ratios specified under the list.
- The company must obtain BoD or GMS approval (subject to any requirements under the company's AoA) for all securities issuances and plans for use of mobilized capital.
- The company must satisfy the offering conditions specified by the competent authority of the country in which the offering is registered.
- The company must comply with Indonesian regulations on foreign exchange management (see below).

Indonesian regulations require issuers or public companies that intend to issue shares in Foreign Depositary Receipts (such as American Depositary Receipts, Singapore Depositary Receipts, and Global Depositary Receipts) to submit their plan to OJK.[318] The report must contain complete information concerning the plan, such as the involvement of issuers or public companies in the foreign depositary receipts and any additional requirements they might have to fulfill to issue the securities in the international market. Issuers and public companies must report their foreign securities activities to OJK. In addition, they must also submit financial reports and annual reports to OJK on the same day these reports are submitted in the country where the foreign depositary receipt is placed.

Listing on foreign stock exchanges brings advantages to listed companies, such as lower capital costs, higher liquidity, and greater prestige. Nevertheless, the world's largest foreign markets tend to have much higher standards of corporate governance than the Indonesian market. The most popular markets are located in the United States, Hong Kong, and Singapore, which arguably have some of the most rigorous governance standards in the world. As such, Indonesian

[320] Decision of the of the Chairman of the Capital Markets and Financial Institutions Supervisory Agency No. KEP-62/PM/1996 on Issuance of Foreign Depository Receipts (Regulation IX.1.3), Article 1.

companies that aspire to enter these markets, or aim to maintain a strong existing position, must maintain rigorous corporate governance standards.

CHAPTER 15

Corporate Governance Framework of Indonesian State-Owned Enterprises

15.1 Origin of Indonesian State-Owned Enterprises

The history of state-owned enterprises in Indonesia dates back to the Dutch colonial era. The Dutch government formed many enterprises for public use, such as railways, post offices, seaports, etc. Two primary laws originally governed these enterprises, namely the *Indonesische Comptabiliteitswet Stb 1925 No. 448* (ICW Enterprises) and *Indonesische Bedrijvenwet Stb 1927 No. 419* as amended by *Stb 1936 No. 445* (IBW Enterprises). Under these laws, both ICW Enterprises and IBW Enterprises obtained their capital entirely from the Dutch government. IBW Enterprises were permitted to raise additional capital from government loans subject to interest. In all cases the Dutch government applied stringent auditing procedures to ensure these enterprises could settle their debts.

After independence, the Indonesian government took over most of the state-owned enterprises established by the Dutch. Following takeover, the government converted all existing state-owned enterprises into state enterprises, also known as *Perusahaan Negara*. The law governing this transformation was Law No. 19 of 1960 on State Enterprises. Many considered this initiative to be unsuccessful and responsible for negative repercussions.

Starting in 1966, the government reformed Indonesia's state-owned enterprises arrangement by issuing Law No. 9 of 1969 on Forms of State Business, which created three categories of state enterprises, including Departmental Enterprise (*Perusahaan Jawatan* or *Perjan*), Public Enterprise (*Perusahaan Umum* or *Perum*), and Limited Liability Enterprise (*Perusahaan Perseroan* or *Persero*). Under Soeharto, the Directorate General of State-Owned Enterprises under the Ministry of Finance was primarily responsible for maintaining "state control" over all state-owned enterprises. State control in this context means that the state had both ownership and control over these entities. Nevertheless, many state-owned enterprises still tended to perform poorly due to problems in management and organizational structure. Many of them collapsed during the Asian financial crisis in the late 1990s.

15.2 Legal and Regulatory Framework

The Asian financial crisis forced the government to reform the nation's systems of corporate governance. As such, the crisis and the government's response represented a fundamental milestone in the history of good corporate governance practice by Indonesian state-owned enterprises. In the aftermath of the crisis, the government, along with a number of stakeholders such as the Capital Markets Supervisory Agency (*Badan Pengawas Pasar Modal* or *Bapepam*) (which later was replaced by the Financial Services Authority (*Otoritas Jasa Keuangan* or OJK)), the Jakarta Stock Exchange (now the Indonesia Stock Exchange or IDX), and members of the financial profession launched several initiatives, including the establishment of the National Committee on Corporate Governance (which was later replaced by the National Committee on Governance).

In 2003, the government enacted Law No. 19 of 2003 on State-Owned Enterprises, which provides a comprehensive framework for the governance and management of state-owned enterprises. The law divides Indonesian state-owned enterprises into two categories, namely Limited Liability Enterprises (*Perusahaan Perseroan* or *Persero*) and Public Enterprises (*Perusahaan Umum* or *Perum*). To encourage the adoption of higher standards of governance, the Ministry for State-Owned Enterprises also issued Ministry Regulation No. 1 of 2011 on the Implementation of Good Corporate Governance by State-Owned Enterprises. This regulation is partly an attempt to mainstream the principles enshrined in the OECD Guidelines on Corporate Governance for State-Owned Enterprises, which was revised in 2015 and recommends the following:[321]

- The state exercises the ownership of state-owned enterprises in the interest of the general public. It should carefully evaluate and disclose the objectives that justify state ownership and subject these to a recurrent review.
- The state should act as an informed and active owner, ensuring that the governance of state-owned enterprises is carried out in a transparent and accountable manner and with a high degree of professionalism and effectiveness.
- Consistent with the rationale for state ownership, the legal and regulatory framework for state-owned enterprises should ensure a level playing field

[321] *OECD Guidelines on Corporate Governance of State-Owned Enterprises* (Paris: OECD Publishing, 2015).

and fair competition in the marketplace when state-owned enterprises undertake economic activities.

- Where state-owned enterprises are listed or otherwise include non-state investors among their owners, the state and the enterprises should recognize the rights of all shareholders and ensure shareholders' equitable treatment and equal access to corporate information.
- The state ownership policy should fully recognize state-owned enterprises' responsibilities towards stakeholders and request that they report on their relations with stakeholders. It should make clear any expectations the state has in respect of responsible business conduct by state-owned enterprises.
- State-owned enterprises should observe high standards of transparency and be subject to the same high-quality accounting, disclosure, compliance, and auditing standards as listed companies.
- The boards of state-owned enterprises should have the necessary authority, competencies, and objectivity to carry out their functions of strategic guidance and monitoring of management. They should act with integrity and be held accountable for their actions.

The Ministry for State Owned Enterprises has taken further measures to improve corporate governance standards among Indonesian state-owned enterprises, including:

- Coordinating state-auditing procedures for state-owned enterprises
- Appointing a corporate governance advisor to the Minister of State-Owned Enterprises
- Reforming remuneration policies for senior management of state-owned enterprises
- Revising the fit and proper test for directors
- Prioritizing and mainstreaming risk management in all state-owned enterprises

15.3 Governance Challenges

15.3.1 The State as Owner

Since the main objective of state-owned enterprises is to serve the public, the manner in which the state exercises its control over these entities is critical. The law provides that the state is the owner of state-owned enterprises, and a minister shall represent the state in state-owned enterprises. The minister represents the state as the sole shareholder in cases where the state owns all the shares, and as a shareholder where the state has a partial shareholding. In doing so, the law guarantees that the state has some level of control through the minister, although the degree of control the state may exercise will be in proportion to the level of its shareholding.

While the state may maintain control over these entities, the primary concern lies in the capacity of the minister as the state representative to exercise his/her control in a balanced manner by providing effective oversight while granting full autonomy. It is particularly challenging for Indonesian state-owned enterprises to maintain operational autonomy without state interference in their day-to-day management.

Best Practice

Ideally, the state should respect the independence and autonomy of the boards of state-owned enterprises by implementing a clear and consistent ownership policy in which the state provides broad mandates and strategic objectives while refraining from making operational decision-making to avoid undue political influence and conflicts of interest. The state should only be primarily responsible for the following:[322]

1. *Being represented at the GMS and effectively exercising voting rights.*

[322] *OECD Guidelines on Corporate Governance of State-Owned Enterprises*, 20-21.

2. *Establishing well-structured, merit-based and transparent board nomination processes in fully- or majority-owned enterprises, actively participating in the nomination of all board members and contributing to board diversity.*
3. *Setting and monitoring the implementation of broad mandates and objectives for state-owned enterprises, including financial targets, capital structure objectives, and risk tolerance levels.*
4. *Setting up reporting systems to regularly monitor, audit and assess performance, and oversee and monitor compliance of state-owned enterprises with applicable corporate governance standards.*
5. *Developing a disclosure policy for state-owned enterprises that identifies what information should be publicly disclosed, the appropriate channels for disclosure, and mechanisms for ensuring quality of information.*
6. *When appropriate and permitted by the legal system and the state's level of ownership, maintaining continuous dialogue with external auditors and specific state control organs.*
7. *Establishing a clear remuneration policy for boards of state-owned enterprises that fosters the long- and medium-term interest of the enterprise and can attract and motivate qualified professionals.*

15.3.2 Responsibilities of the Board

Limited liability state-owned enterprises consist of a BoC and a BoD. The BoD is an executive organ that is responsible for day-to-day management while the BoC is responsible to supervise and advise the BoD. The law also stipulates that the GMS has the authority to appoint BoC and BoD members. A prospective BoD member needs to pass a fit and proper test and sign a management contract before he/she can be appointed as a director.[323]

[323] Law No. 19 of 2003, Article 16(2)(3).

Some of the challenges facing Indonesian state-owned enterprises stem from their diverse stakeholders, many of whom have different agendas that may conflict with the interests of the company and inhibit commercial decision making. Due to insufficient separation of ownership and control, the boards of state-owned enterprises often act as a "rubber stamp" for the government and exercise little oversight over managers, particularly in cases where board members are government employees with little to no experience in managing companies and who are appointed for political reasons rather than for professional or technical competence.

To combat these dangers, it is essential for these companies to strengthen and disclose the process for selecting and appointing board members. This means that policymakers should clearly set-out the mechanisms for board appointment, including developing transparent selection criteria and search and recruitment processes. Once appropriate candidates have been appointed, it is also essential to ensure that board members are able to perform their responsibilities independently of political or any other influence.

Best Practice

The OECD Guidelines offer the following recommendations:[324]

- *The boards of state-owned enterprises should be assigned a clear mandate and ultimate responsibility for the enterprise's performance. The role of the board should be clearly defined in legislation, preferably according to company law. The board should be fully accountable to the owners, act in the best interest of the enterprise, and treat all shareholders equitably.*
- *The board should effectively carry out its functions of setting strategy and supervising management, based on broad mandates and objectives set by the government. The board should have the power to appoint and remove the chief executive officer and should set executive remuneration levels that are in the long-term interest of the enterprise.*
- *The board composition should allow the exercise of*

[324] *OECD Guidelines on Corporate Governance of State-Owned Enterprises*, 28-29.

objective and independent judgment. All board members, including any public officials, should be nominated based on qualifications and have equivalent legal responsibilities.

- *Independent board members, where applicable, should be free of any material interests or relationships with the enterprise, its management, other major shareholders, and the ownership entity that could jeopardize their exercise of objective judgment.*
- *Mechanisms should be implemented to avoid conflicts of interest preventing board members from objectively carrying out their board duties and to limit political interference in board processes.*
- *The boards of state-owned enterprises should consider setting up specialized committees, composed of independent and qualified members, to support the full board in performing its functions, particularly in respect to audit, risk management, and remuneration. The establishment of specialized committees should improve boardroom efficiency and should not detract from the responsibility of the full board.*
- *The board should, under the chair's oversight, carry out an annual, well-structured evaluation to appraise its performance and efficiency.*
- *State-owned enterprises should develop efficient internal audit procedures and establish an internal audit function that is monitored by and reports directly to the board and to the audit committee or the equivalent corporate organ.*

15.3.3 Equitable Treatment of Shareholders

The OECD Guidelines recommend that the state and the enterprise should recognize the rights of all shareholders and ensure shareholders' equitable treatment and equal access to corporate information. In Indonesia, the Ministry of State-Owned Enterprises requires that shareholders who possess the same share classification must be treated equitably. Further, this regulation also

reserves the right of all shareholders to attend and vote in the GMS, access material information, receive dividends, and exercise other rights as set out under the law, the company's AoA, and other relevant legislation. These laws imply that the minority shareholders in a state-owned enterprise have equal rights as majority or controlling shareholders of the same share class. However, lack of protections for minority shareholders in Indonesian state-owned enterprises remains an ongoing problem.

Best Practice

To ensure the protection of minority, non-state shareholders, the OECD Guidelines recommend that:[325]

- *The state and state-owned enterprises should ensure that all shareholders are treated equitably. For example, the government should disclose the existence of any shareholder agreements and capital structures that allow a shareholder to exercise a disproportionate control compared with his/her shareholding.*
- *State-owned enterprises should observe a high degree of transparency, including as a general rule equal and simultaneous disclosure of information, towards all shareholders.*
- *State-owned enterprises should develop an active policy of communication and consultation with all shareholders.*
- *The participation of minority shareholders in shareholder meetings should be facilitated so they can take part in fundamental corporate decisions such as board elections.*
- *Transactions between the state and state-owned enterprises, and between separate state-owned enterprises, should take place on market consistent terms.*

[325] *OECD Guidelines on Corporate Governance of State-Owned Enterprises*, 53-54.

15.3.4 Stakeholder Relations

Stakeholders in a state-owned enterprise may include employees, customers, creditors, suppliers, local communities, and other parties that are affected by its activities, or can influence the fulfillment of its objectives, activities, and reputation. The Ministry requires companies to consider and respect the rights of stakeholders—including those rights that are covered under existing legislation and agreements between the company and employees, customers, creditors, surrounding communities, and other stakeholders.[326] In doing so, the regulation recognizes that there may be a variety of stakeholder groups with diverse interests in state-owned enterprises whose rights must be respected.

Implementation of this requirement by SOEs, however, remains inconsistent. One major problem area relates to the protection of stakeholders and employees during privatization. Indonesian laws do not provide clear guidance on how to manage stakeholder relationships during privatization of state-owned enterprises, and such processes typically create significant anxiety for employees and other affected groups.

Best Practice

The OECD Guidelines set out the following recommendations on stakeholder relations:[327]

- *The state , its representatives, and the enterprise itself should recognize and respect stakeholders' rights established by law or through mutual agreements. For example, by ensuring that all stakeholders have access to relevant information on a timely and regular basis, providing a redress mechanism for stakeholders to report alleged violations of their rights, or creating a whistleblower mechanism.*
- *Listed or large state-owned enterprises should report on stakeholder relations, including (where relevant and feasible) with regard to labor, creditors, and affected communities, such as by issuing sustainability reporting and*

[326] Ministry Regulation No. 1 of 2011 on Implementation of Good Corporate Governance by State-Owned Enterprises, Article 38.
[327] *OECD Guidelines on Corporate Governance of State-Owned Enterprises*, 25.

publishing stakeholders policies.

- *The boards of state-owned enterprises should develop, implement, monitor, and communicate internal controls, ethics, and compliance programs or measures, including those which contribute to preventing fraud and corruption, which are applicable to the entity and its subsidiaries. Ideally, the board should develop a code of ethics that provides clear and detailed guidelines for all employees.*
- *State-owned enterprises should observe high standards of responsible business conduct, including with regard to the environment, employees, public health and safety, and human rights. Expectations established by the government in this regard should be publicly disclosed and mechanisms for their implementation clearly established.*
- *State-owned enterprises should not be used as vehicles for financing political activities. These entities should not make political campaign contributions.*

15.3.5 Transparency and Disclosure

The Ministry of State-Owned Enterprises requires these entities to disclose important information in their annual reports and financial statements in accordance with laws and regulations, not only in a timely manner but also in an accurate, clear, and objective way. Finding the balance between maintaining transparency vis-à-vis protecting confidential information remains a challenge for state-owned enterprises in Indonesia. Indonesian laws do not set out detailed guidance on how these entities can meet their obligation to remain transparent, while also protecting the integrity of confidential information. Without clear guidance or strong enforcement of these requirements, most state-owned enterprises are reluctant to disclose sensitive information, such as financial statements or procurement procedures. Some argue that the lack of transparency is intentional, reflecting self-interest among political interest groups and bureaucrats, and results in lack of accountability and transparency. Going public may pressure state-owned enterprises to implement a stronger disclosure regime. However, listing procedures and requirements are demanding, and may not be appropriate for all state-owned enterprises.

Best Practice

The OECD Guidelines recommend that all state-owned enterprises be subject to the same high-quality accounting, disclosure, compliance, and auditing standards as listed companies. In addition:[328]

- *State-owned enterprises should report material financial and non-financial information in line with high quality internationally recognized standards of corporate disclosure, and including areas of significant concern for the state as an owner and the general public.*
- *The annual financial statements should be subject to an independent external audit based on high quality standards. Specific state control procedures do not substitute for an independent external audit.*
- *The state or its representative should develop consistent reporting on state-owned enterprises and publish annually an aggregate report on all of state-owned entities to facilitate easy access by the public.*

[328] *OECD Guidelines on Corporate Governance of State-Owned Enterprises*, 26-27.

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Indonesian Laws and Regulations

Law No. 3 of 1982 on Company Registration Obligations.

Law No. 8 of 1982 on Mandatory Company Register.

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Law No. 30 of 2000 on Trade Secrets.

Law No. 13 of 2003 on Manpower.

Law No. 19 of 2003 on State-Owned Enterprises.

Law No. 25 of 2007 on Capital Investment.

Law No. 40 of 2007 on Limited Liability Companies ("Indonesian Company Law" or ICL).

Law No. 8 of 2010 on Countermeasures and Eradication of Money Laundering.

Law No. 9 of 2013 on Prevention and Suppression of Terrorist Financing.

Government Regulation No. 29 of 2016 on Changes to Authorized Capital of Limited Liability Companies.

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