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The Implementation of Good Corporate Governance in Indonesian  
Company

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# **The Implementation of Good Corporate Governance in Indonesian Company**

**By :  
Meria Utama**

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## **Abstract:**

*In the modern business world, it is very important to separate the ownership of a company with the management and control, in order to make the company getting more profit with the most efficient capital, But in the other hand this separation is also have weakness such as transparency in the use of funds in the company and in the proper balancing of the interests of, for instance, shareholders and managers and of controlling and minority shareholders<sup>1</sup>. So it is very important in such company to implement the Corporate governance code to eliminating these weakness , and the implementation of CGC also will improve the business and economic performance.*

*Keywords : GCG, Indonesian Company*

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## **A. Introduction**

Many countries in the world have realized that the implementation of corporate governance code is very important. Large corporate failures, financial scandal and economic crisis in several countries, have focused attention on the importance of corporate governance. The policy of large financial institution in financing companies through loans or equity, has come to include conditions on corporate governance in these companies.

One of example is CalPERS, big investor from USA, this investor has publish a set of minimum standard to which in its view the market throughout the world should strive to adhere. CalPERS just want to invest to the company that have implemented good corporate governance, not only CalPERS will adopt this policy but also another institutional investors world wide.<sup>2</sup>

The example of international institutions that also have an intention to the corporate governance code, this organization usually discuss to develop

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<sup>1</sup> Kraakman et al, 2004, "The Anatomy of Corporate Law : A Comparative and Functional Approach " Oxford University Press, p.3

<sup>2</sup> [www.Fcgi.or.id/Indonesia/002\\_04GCG\\_int'l.htm](http://www.Fcgi.or.id/Indonesia/002_04GCG_int'l.htm)

and regime economic and social policy, they seek the answer to the common problems, and one of their main policy is corporate governance code<sup>3</sup>.

Recognizing the increasing importance of corporate governance, government and business associations in many countries, both industrialized and developing, have started to develop or improve national systems of corporate governance. Since 1992, dozens of countries have started national initiatives to improve corporate governance in their economies. Countries such as the United States, Germany, Australia, Brazil, South Korea, Thailand, Malaysia and India have drawn up national reports and started to implement, on government and on company level, recommendations drawn up by expert groups.<sup>4</sup>

This entire means that those countries and companies has realized that by using good corporate governance will have better access to international capital than those without good corporate governance.

## **B. Result**

### **1. Situation in Indonesia**

Indonesia as a developing countries of course has many company that need more capital, and this capital not only come from the internal investment but also from another investment from another countries, In the other hand those investors do not want to invest their capital if they think that company is not well manage and be able to refund their capital.

In the report on "Corporate Governance and finance in East Asia, A study of Indonesia, Republic Korea, Malaysia, Philippines, and Thailand : Volume one (A Consolidate Report)" published in 1999, the Asian Development Bank ('ADB') reported that the economic crises in Indonesia, Malaysia, Philippines, Thailand and Republic of Korea were caused by the failure in implementing prudent corporate governance. The factor emphasized by the ADB are a high concentration of company ownership (57 % tp 65 %), Ineffective supervision by the board of directors (in Indonesia's case, it is the board of commissioner since Indonesia company law applies two tiers system); Inefficiency and lack of transparency on the procedures to acquire a company's control; Inadequate supervision by creditors.<sup>5</sup>

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<sup>3</sup> www.OECD.org.com

<sup>4</sup> ibid

<sup>5</sup> Asian Development Bank (ADB), 1999, "Corporate Governance and Finance in East Asia. (Edited by : Ma Virginita Capulong et al), vol 1 and 2.



In fact, during Soeharto era political support from Soeharto family was given to its crony. This had caused lack of financial responsibility. For example, state owned banks are forced to lend money to companies that linked to Soeharto family and they are forced to accept loss. Given the extensive links between government and business leaders, a lack of transparency and a politicized legal system, almost any member of Indonesia's corporate elite could be considered crony. Almost all of the wealthiest ethnic Chinese businessman owe their start in business to special favours handed out by friends in the government. The entrance requirement for this group is a continuing close, personal relationship with Soeharto family.<sup>6</sup>

Such crony relationship with government and Soeharto family had created in efficiency due to privilege given in licenses and project. This had causes bad governance practice in respective companies. Since many respective companies had been listed in the stock exchange, such bad governance practices had abused minority shareholders right.

Evidence shows that weak corporate governance practices in most of Indonesian companies have led to many deficiencies in their decision makings and corporate actions : inefficient investments, highly financial leverage, maturity mismatch of their borrowings, and un-hedged foreign exchange exposures. These have made the corporate sector in Indonesia Vulnerable to the currency shock during the crisis, leading to negative equity standing and inability to pay off their borrowing the lending banks. A spiral effect that ultimately cause banks collapse in Indonesia.<sup>7</sup>

Based on the situation above, after Soeharto era, Indonesia try to out from those bad situation. So it has Indonesia company laws of 1995 but this law haven't covered all corporate governance code, in March 2001, the National Committee of Corporate Governance (the 'NCGC') issued the National Code for Good Corporate Governance (the Code). The Code consist of 13 chapters.

The implementation of corporate governance code is rendered to make the investor belief with the company in Indonesia, and they want to put their investment in Indonesia again.

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<sup>6</sup> Adam Schwarz, 1999, "A Nation in Waiting : Indonesia's Search for Stability", second edition.

<sup>7</sup> Antonius Alijoyo et al, Review of Corporate Governance in Asia.

## **2. Corporate Governance Code In Indonesia**

Corporate Governance Code in Indonesia is composed by the National Committee on Corporate Governance ("NCCG"). The objective of the Code is to provide a guide to excellence in corporate governance for the business world which has drawn on international best practice in corporate governance appropriately adjusted to suit the Indonesian legal and regulatory environment. The good corporate governance principles as set out in the Code are intended to be implemented as soon as possible.

A first draft of the code was made in march 2000 and finally published in its final form in March 2001. The aim's of this committee is to develop a model which, while consistent with best international practice, would suit Indonesia's legal frame work.<sup>8</sup>

### **1. Definition of Corporate Governance Code**

There are many definition of Corporate Governance because the issues of corporate governance is relative new<sup>9</sup>. There is still divergence in today's academic literature regarding the definition of corporate governance.

#### **a. Definition according to Cochran and Watric (1988)**

Corporate Governance is an umbrella that covers many aspects related to concepts, theories, and practices of board of director and their executive and non executive directors. It is a field that concentrates on the relationship between board, stockholders, top management, regulators, auditors and other stakeholders.

#### **b. Monks (1995)**

Give a similar definition to the previous one it is the relationship among various participants in determining the direction and performance of corporations.

### **3. Forum for Corporate Governance Indonesia**

Definition of Corporate Governance Code is a set of rules that define the relationship between shareholders, managers, creditors, the government, employees and other internal and external stakeholders in respect to their rights and responsibilities, or the system by which companies are directed and controlled<sup>10</sup>.

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<sup>8</sup> Kartini Mulyadi, 1998, Corporate Governance in Indonesia.

<sup>9</sup> <http://www.fcgi.org>

<sup>10</sup> A.W.P.Henny, 1997, corporate governance and shareholder value.



### **The purpose of corporate governance code are :**

1. To maximize corporate and shareholder value by enhancing transparency, accountability, reliability, responsibility, and fairness in order to strengthen the company's competitive position both domestically and internationally, and also to support investment.
2. To encourage the management of the company to behave in a professional and efficient manner, as well as optimizing the use of the independence of the board of commisaris, and the director.
3. To encourage shareholders, members of the board of comisaris, and director to make decisions and to act with a strict sense of morality, in compliance with the prevailing regulations having the force of law, and in accordance with their social responsibility towards the various stakeholders and the environmental protection.<sup>11</sup>

### **4. What is Indonesian Code for Good Corporate Governance**

This code is a guidelines / recommendations of GCG practices for Public Listed company, State owned companies (BUMNs) and Indonesian limited liability company in general.

The content of Indonesia code for GCG are General meeting of shareholder, Board of Commisioner, Board of Director, Audit System, Corporate secretary, Stakeholder, Discloser, Confidentiality, Insider information, Business ethnics & corruption, Donations, Compliance with health , safety, & environmental protection regulation having the force of law, Equal employment opportunity.<sup>12</sup>

Mostly, some principles of Good Corporate Governance in Indonesia which is set by National Committee of Corporate Governance among the guidelines contained in the code are :

#### **a. Shareholder, Commissioners and Directors**

Indonesia's company law (Law no.1 of 1995 regarding limited liability companies) contains a number of provisions directed to wards sound corporate management and the protection of the shareholders' rights. The company law has preserved the two-tier management structure that has long been a feature of Indonesian companies (a board of directors with executive management responsibility and a supervisory board of commissioners). Among other things, it states that the directors

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<sup>11</sup> Antonius Alijoyo et al, 2004, Corporate Governance in Indonesia, June.

<sup>12</sup> Indonesian Code for Corporate Governance, April 2001.

must perform their duties in good faith and in the best interests of the company and that each director is personally liable for failure to do so.

The code amplifies and, in certain respects, goes significantly beyond the provisions of the company law. For example, the code provides that each member of the board of directors and the board of commissioners should be of good character and have relevant experience, and should each be composed in such a way as to allow effective, appropriate and swift decision making and so that its members have no interests which might impair their ability to perform their duties independently and critically, depending on the specific character of the company, at least 20 % of the board of directors should be outside directors independent of the board of commissioners and controlling shareholders, the view of minority shareholders should be considered in the process of their nomination and appointment. And the last is that members of the board of directors and the board of commissioners should derive no personal gain from the company's activities other than their remuneration in that capacity.

The code also states that all shareholders should be treated equally and be provided with full and accurate information to enable their participation in decision-making at shareholders meetings. Controlling shareholders should also be mindful of their responsibilities as shareholders in exercising influence over corporate management.

#### **b. Stakeholders**

One notable feature of the code is its recognition of the rights of stakeholders other than a company's shareholders. The code says that the rights of stakeholders, including the company's customers, supplier and creditors, and the surrounding community, are to be respected. Stakeholders are to be afforded a means of redress for infringement of their rights. The company must provided them with the information necessary to protect their rights and they must be given the opportunity to monitor the company's directors and provide input.

#### **c. Audit**

The board of commissioners should establish an independent audit committee. External auditors should be appointed by the shareholders from candidates nominated by the audit committee.



#### **d. Business Ethics**

The code specially provides that directors, commissioners and employees of a company should never attempt to influence decisions by offering financial inducements to government officials. It also state that it is inappropriate for company funds or assets to be used to make political donations.<sup>13</sup><sup>13</sup> Corporate Governance Guide 2002, [www.corporatefinancemag.com](http://www.corporatefinancemag.com).

#### **C. Conclusion**

All of these codes hope will be implemented in all of companies in Indonesia, not only state owned enterprise but also limited liability companies, public listed company and banking companies, which has listed in Jakarta Stock Exchange mostly have implemented this code, but since these code doesn't have force in law yet, this is just become the reference point as a model of good corporate governance for the Indonesian business community. It is expected that these code will be adopted as a law in Indonesia.

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