

**AUTHORITY, OBLIGATION, AND RESPONSIBILITY
OF THE COMPANY BOARD OF DIRECTORS
BASED ON THE 1995 COMPANY LAW**

by

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I. Introduction –Background

For almost one and a half centuries the Indonesian business community has used the Commercial Code ("Wetboek van Koophandel", valid since 1848) which consists of laws and regulations governing limited companies.

These laws and regulations were very suitable back then, but today's business activities have been changing along with the development of the globalization era and the ratification of WTO Convention into the Law number 7/1994, and the involvement of Indonesia in APEC forum.

The provisions regarding limited companies were embodied in 21 article (Article 36-Article 56) of the Commercial Code, and for indangerous people known as *pribumi* the laws are based on the Indonesian Limited Liability Company Ordinance ("Ordonantie op de Indonesische Maatschappij op Aandelen", Stb 1939:569 jo 717) consisting of 42 articles.

The risk faced by the Board of Directors in conducting any activity which is detrimental or causes damages to third parties is covered by only 2 articles (articles 45 and 47 of the Commercial Code) These state that the Board of Directors is responsible personally for any loss caused by their mistakes. Further, the shareholders may fire them.

Both articles allow a suit to be filed against the Board of Directors due to their wrongdoing, and this is also implicit in other, more general provision of the Civil Code, for example:

- Article 1365 of Indonesian Civil Code regards all acts against the law; this article is known as of "Sapu Jagad".
- Article 1601-1603 of Indonesian Civil Code regarding labor union,
- Article 1792-1819 Indonesian Civil Code regarding line of authorization, in case the shareholders' would like to sue The Board of Directors raised from works relationship among themselves.

Under the new Company Law (law No. 1 of 1995, dated 7 March, 1995), there are detailed many obligations and responsibilities which way be used against Board of Directors if they are fail to perform their jobs. This is aligned with one of the purposes the Company Law, being established to protect the shareholders', creditors, other related parties, and the company itself (General Elucidation of Company Law).

II. The law regarding the Board of Directors in the Company Law

The provisions governing the Board of Directors in Company Law are found in Chapter VI, Part one, Articles 79 through 93. The laws regarding the BOD responsibilities could be found in Article 23, Article 30 (3), and Article 60 (3).

III. Basic Principle of Company Management under the Board of Directors

In the Company Law, there are at least 3 (three) company's management principles that must be obeyed and followed by the Board of Directors:

- Piercing The Company's Veil
- Fiduciary Duty
- Duty of Skill and Care

A. Piercing The Company's Veil

Previously, the Board of Directors could hide behind the limited liability status of the company. If they made mistakes, they could always put the blame and responsibility on the company.

In litigation practice, the Board of Directors in their capacity as individuals were often sued with the Company. But Indonesian Commercial Code does not list specially the wrongdoing of the Board of Directors (except any wrongdoing against the company's Article of Association pursuant Article 45 (2) of Indonesian Commercial Code) and a judge could have different interpretations as to this provision's impact on the case.

Under the new Company Law, the Board of Directors cannot transfer all of their wrongdoing or mistakes to the company. This is known as the law of "Piercing the Company's Veil". The Board of Directors can now be responsible individually.

B. Fiduciary Duty

The Board of Directors are given the trust and the authority by the shareholders to manage the company.

Based on the "Fiduciary Duty" principle, the Board of Directors and also (including the Board of Commissioners) must avoid conflict of interest between themselves as individual and as the director or commissioners of the company.

Article 82 of Company Law Strictly States that the Board of Directors is fully responsible to manage the company for the benefit and objectives of the company, not for the benefit of themselves as individual.

C. Duty of Skill and Care

An other principle that must be obeyed by the Board of Directors is to manage the company professionally, based on their skills, and do manage the company seriously with good intentions and full responsibility, as stated by Article 85 of the Commercial Law. Unlike the current situation, somebody could become a director of many companies, but no matter good that person is, he/she would not be able to manage the company with maximum effort and optimally. And as the impact of such condition, the company's objectives would be less focused and the company would not be able to achieve their optimal goals and objectives.

All the above three principles are stated in the Company Law.

IV. Authority of the Board of Directors and the limitations thereof

As in the Indonesian Commercial Code, the Company Law stipulates that the Board of Directors, appointed by the General Shareholders' Meeting, is responsible for the company's management. (Article 79 (1) and Article 80 of Commercial Law). The law provides that the delegation of assignments and authority for each member of Board of Directors, and the amount of income of the Board of Directors, be stipulated by the General Shareholders' Meeting (Article 81 of Company Law). The board of Directors is the representative of the company both internally and externally (Article 82 of Company Law) except Article 84 stipulates that members of Board of Directors are not authorised to represent the company if:

- a. There is case in court between the company and the members of the Boar of Directors, or
- b. Members of Board of Directors have their own interests that are in conflict with the interests of the company.

Generally, a company could be managed by single director, but companies with the following activities are obliged to have at least 2 directors, based on Article 79 (2) of the Company Law:

- a. a company having core business managing the public or people's funds
- b. a company issuing letters of obligation
- c. a company is a public-by owned company

Article 79 (2) of the Company Law gives needed protection, considering the responsibility for companies which manage public funds or other creditors. Other limitations on the authority of the Board of Directors are governed by the Company Law and the Article of Association of the Company. The Articles may require permissions from the commissioners in order for the Directors to take certain enumerated actions (Article 100 of Company Law).

V. Requirements of Members of the Board of Directors

Due to their obligation and responsibility, and the interest of the company, each member of the Board of Directors is obligated, with good intention and full responsibility, to perform their jobs (Article 85 of Company Law).

Article 79 (3) of the Company Law sets out the requirements to become a member of Board of the Directors:

- a. Able to act within the law
- b. Never been declared bankrupt
- c. Never been convicted of wrongdoing nor caused a company to become bankrupt
- d. Never been convicted and sentenced to jail which causes financial loss to the company for the past five years prior to the appointment as member of Board of Directors.

VI. Obligations of the Board of Directors

Besides the obligation to have good intention in running the company (Article 85 of the Company Law), the Board of Directors also has the following obligations:

- a. The Board of Directors is obligated to make and maintain a list of shareholders, keep minutes of General Shareholders' Meeting; and minutes of Board of Directors meetings, and to manage the company ledger (Article 86 of the Company Law).
- b. Each member of the Board of Directors is obligated to report to the company all his/her ownership of shares or that of other family members, at the company or other companies (Article 87 of Company Law)
- c. Board of Directors is obligated to ask permission of General Shareholders' Meeting prior to transferring or putting up the company's assets as collateral.
- d. Obligation to register, to announce, and to inform
Beside the Board of Directors obligations as provided in Chapter VI Part One of the Company Law, Board of Directors' obligations also can be found in Article 21 and 22 of the Company Law, where the Board of Directors is obligated to register in the company list:
 1. The Deed of establishment and letter of approval of the Minister of Justice
 2. Any amendments to the articles of association, including report to, or letters of approval of the Minister of Justice regarding such amendments the Board of Directors also is obligated to push all the above information in the Addendum to the State Gazette (Berita Negara).

In the case of merger and acquisition or takeover of a company, the Board of the Directors is obligated to announce in 2 daily newspapers regarding such plan at least 14 days prior to the notification of General Shareholders' Meeting. Furthermore, the resulting Board of Directors of the company is obligated to announce the result of such merger, acquisition or take over in 2 daily newspaper at least 30 days after such process has taken place.

The Board of Directors is also obligated to inform creditors, and then interested companies regarding the result of General Shareholders' Meeting to reduce the capital of the company and to announce the same in the State Gazette (Article 37 of Company Law).

e. Obligation to Release Information

Other Board of Directors obligations are ruled by Article 111 (5) and Article 110 of the Company Law. The Board of Directors, the Board of Commissioners, and all employees are obligated to release any information needed to the Court of 1st Instance in auditing process if there is an indication that:

1. The Company is engaged in any practice which is against the law or causes losses to the shareholders or third parties;
2. Any member of the Board of Directors or Board of Commissioners is conducting any acts against the law or which causes losses to the company, shareholders, or third parties.

Such auditing by the Court of 1st Instance could be requested by:

- a. Shareholders on their own behalf of the company if they represent a minimum of 10% of the shares, or
- b. Other parties so designated in the Articles of Association of the company or in an agreement with the company which is given the authority to request such audit, or
- c. The District Attorney, in representing public interest

f. Obligation to Appoint Public Accountant

Based on Article 59 of the Company Law, the Board of Directors has the obligation to appoint a Public Accountant to do the annual calculation of the company to be audited if:

1. The core business of the company is related to management of people or public funds.
2. The company issues letters of obligation
3. The company is a public company

VII. Responsibility of Board of Directors

The Company Law stipulates that all losses of the company or third parties caused by the mistakes done by Board of Directors must be covered with their own personal assets long with the company's assets.

The responsibility of the company and Board of Directors is called "*Tanggung Renteng*" (Back to back responsibility).

A. Responsibility Prior to Registration and Announcement

Prior to the registration and the announcement. Articles 21 and 22 of the Company Law states that the Board of Directors is fully responsible for every action by law done within the company.

The question is whom they are supposed to be responsible to.

There are three possibilities:

- a) If there are 2 directors, both directors are responsible to each other
- b) The Board of Directors is responsible to the founders of the company. Details of such responsibility could be found in Article 32 (b), (c), and (d) of the Company Law
- c) Once the company has become a legal entity, the Board of Directors is responsible together with the company.

Penalties for negligence and/or intentionally not performing the responsibilities are ruled in Article 23 of the Company Law, This law has not lessened the penalties against Board of Directors based on law No.3/1982 regarding the obligation to Register the Company (Article 23 of Company Law).

B. Cancellation of Re-possession or Buy Back Shares By the Company

Article 30 of the Company Law stipulates that the company may buy back shares that have been issued, upon the following conditions:

1. The re-purchase price must be paid from the net profit, as long as not such will not lessen the net value of the equity, now the invested capital and reserve obligation, based on the Company Law; and
2. The amount of nominal value of the shares owned by the company and subsidiaries and security shares, may not exceed 0% of the total capital of the Company

All shares purchase by the company in violation of the above laws are void by law and the payments made or received by the shareholders must be returned to the company.

Any losses to shareholders, who have good intentions, caused by the company's cancellation due to breaching Article 30:1 of the Company

Law are considered as a loss. These include all payments for shares which have been paid to the shareholders, which must be returned to the company, borne by the Board of Directors and the company.

C. Misleading Financial Report

Within 5 months (?) after the closing of the company ledger the Board of Directors is obligated to make an annual which must align with the Standard Financial Accounting to be presented to the General Shareholder' Meeting (Article 58 of Company Law).

In the case that the annual report provide is not true and or is misleading, the members of the Board of Directors and Board of Commissioners will be responsible to all parties who suffered from the loss. Except if proven that the loss is not the fault of the Board of Directors and the Board of Commissioners.

(Article 60 (3) and Article 60 (4) of Law Company) back to back responsibility of the Board of Directors and Board of Commissioners arises because they sign the annual report as form of their responsibility in performing their jobs (Article 57 (1) of Company Law).

However, the Board of Directors and Board of Commissioners may be released from their responsibilities under 2 (two) conditions:

1. they do not sign the annual report, giving a written explanation
2. incorrect annual report is not their fault, but it is the fault of the public accountant or finance department of the company, without knowledge of Board of Directors and Board of Commissioners.

D. Good Intention

A member of Board of Directors is responsible personally if he/she is guilty or neglected his/her jobs, not keeping with good intention and full responsibility for the benefit of the company.

On behalf of the company, shareholders representing a minimum 1/10 of the shares with legitimate voting rights could, may first claim against the Board of Directors members who caused such loss to the company due to his/her fault or negligence.

Due to the important of good intention, this general law principle (Article 533 jo. Article 1965 of the Indonesian Civil Code), need to be stated again, along with the risks of being sued at court (Article 85 of Company Law).

E. Bankrupt Due to Board of Directors False

In Article 90 (2) of Company Law is stipulated that in case of bankruptcy occurring due to the fault and negligence of the Board of Directors, where the assets or equity of the company could not cover the loss, each member of Board of Directors is responsible for such loss.

Of each member of Board of Directors has the opportunity to prove that the bankruptcy is not because of the Board of Directors fault and they are not responsible for the company loss.

VIII. Closing

It is not the intention of lawmakers to scare Directors of Companies with the law and regulations regarding their duties and responsibilities, but it is to improve the development of limited corporation and business environment generally.

By having clear definition of law and regulations regarding Director's responsibilities, they would have a better grip and clear understanding to execute their responsibilities in running the company.

The laws and regulations also limit Director's authorizations. Prior to these law and regulations, Director's authorization was only limited by the Articles of Association of the company made by the founders on behalf of the shareholders.

Now, beside the Article of Association of the Company, the Laws and regulations limit Directors' authority in order to protect the shareholders, creditors, all related parties, and the directors.

Beside duties, responsibilities, and authorization limit, the laws and regulations also provide the rights of Directors such as giving protection to Directors from being abused and fired unfairly by having the right to defend themselves (Chapter 91, 92) against such issues.

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