BUSINESS AND HUMAN RIGHTS LAW & POLICY
2025, VOL. 1, NO. 1

The Board Duty to Comply with Good Corporate Governance Principles under the Australian and Indonesian Company Law

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ABSTRACT
In the field of private economic activities, the formulation of a legal entity or a legal form chosen to run the business is a crucial part to be decided in the first place. In Indonesia, there are various forms of legal entity, such as sole trader, firm, commanditaire venootschap, limited liability corporation, and cooperation, in which the limited liability corporation is deemed as the most dominant form. Similarly, companies in Australia are dominated by limited liability corporations. In the light of setting up a company, the corporate governance aspect is an essential element that shall be highly upheld. This article compares the law on limited liability company in both Indonesia and Australia, as there is a significant difference in how both countries structuring the boards. The Indonesian company has two-tier boards: the board of directors and the board of commissioners, while the Australian company only has one, which comprises only the directors. Considering this difference, it is hypothetical that both systems have different approaches toward the compliance of corporate governance principles. This paper will discuss two issues: first, the overall comparison of board structure between Indonesian and Australian companies and the duty of the board. Second, discussion and criticism towards the compliance and implementation of corporate governance principles by each board system. It is notable that the company board system in both countries was formed by a long history of culture, politics, and law. Therefore, this paper aims not to make a simplistic conclusion of whether the one-board system in Indonesian companies is better than the two-board system in Australia or *vice versa*.

KEYWORDS: Good Corporate Governance, Company Law, Board of Company, Duty of Board

1. Introduction

Richard Posner, in the *Economic Analysis of Law*, stated that many lawyers thought the economics approach such as business cycles, monetary policy, foreign trade, and other macroeconomic phenomena, shall be forbiddingly remote from the day-to-day concerns of the legal system.[1] However, the proposition that law and economics are two significant factors that complement each other is logically acceptable. In 2016, Indonesia and Australia held an agreement called Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA).[2] Both governments have agreed to improve the trade and investment relationship between the two countries.[3] The geographical proximity between both countries is deemed as a strong advantage for economic activities across nations. However, the potential of economic activities cannot be secluded from the law, specifically the law of Australia and Indonesia.

In the field of private economic activities, the formulation of a legal entity or a legal form chosen to run the business is a crucial part to be decided in the first place. In Indonesia, there are various forms of legal entity, such as sole trader, firm, *commanditaire venootschap*, limited liability corporation, and cooperation, in which the limited liability corporation is deemed as the

1 Richard Posner, *Economic Analysis of Law* (Aspen Publishing, 9th ed, 2014) p. 1.
2 T Lindsey and D McRae, *Strangers Next Door?: Indonesia and Australia in the Asian Century* (Bloomsbury Publishing, 2018) p. 23.
3 *Ibid*.

most dominant form.[4] Similar to Indonesia, Australia and the world's economic driving force are dominated by limited liability corporations.[5] In the light of setting up a company, the corporate governance aspect is an essential element that shall be highly upheld.

Blackstone described a corporation as a "little republic",[6] by analogy, it indicates that a corporation must be managed as a republic. The basic idea of this principle is to separate functions and interests among the parties (stakeholders) in a company, namely the party providing the capital or the shareholders, supervisors, the day-to-day executives of the company, and the wider community. Later, corporate governance is used as a rule or standard in the field of economics that regulates the behaviour of company owners, directors, and managers by detailing the duties and authorities as well as their accountability to the shareholders. In short, good corporate governance principles shall be implemented in the very first beginning when setting up a company's structure, to be more specific the boards.

As a comparison between Indonesia and Australia, there is a significant difference in how both countries structuring the boards. The Indonesian company has two-tier boards: the board of directors and the board of commissioners, while the Australian company only has one, which comprises only the directors. In light of this difference, it is hypothetical that both systems have different approaches toward the compliance of corporate governance principles. This paper will discuss two issues: *first*, the overall comparison of board structure between Indonesian and Australian companies and the duty of the board. *Second*, discussion and criticism towards the compliance and implementation of corporate governance principles by each board system.

2. Company Board Structure in Indonesia and Australia

2.1. Indonesian Company Board's Structure

2.1.1. Background of Company Board's Structure

The present board structure in Indonesian companies cannot be secluded from the historical background of Indonesian reformation. Indonesia became independent from the Netherlands in 1945; therefore, the development of law specifically in commercial such as company law, greatly influenced by the colonialism. At that time, the regulation concerning corporations is envisaged in the Dutch Commercial Code 1848.[7] After the independence of Indonesia in 1945, the Dutch commercial code provisions about corporations remain enforced according to the transitional provision of the Indonesian constitution.[8] According to the transitional provision of the constitution, it is stated that, the law of corporations will be under the Dutch Commercial Code until Indonesian parliament establishes a new law governing companies. *Naamlooze Vennootschap* (NV) is one form of corporation introduced by the Netherlands during the *Netherlands-Hindi* (Indonesia before independence) period. The NV has become a *prima donna* because of the limited liability characteristic towards the capital

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4 Petra Mahy, 'The Evolution of Company Law in Indonesia: An Exploration of Legal Innovation and Stagnation' (2013) 61(2) *American Journal of Comparative Law* 377, p. 387.

5 Jonathan Charkham, *Keeping Better Company* (Oxford University Press, 2008) p. 299.

6 David Ciepley, 'Is the U.S. Government a Corporation? The Corporate Origins of Modern Constitutionalism' (2017) 111(2) *American Political Science Review* 418, p. 420.

7 *Ibid*, pp. 378, 418.

8 *Undang-Undang Dasar Negara Republik Indonesia Tahun 1945* [Constitution of the Republic of Indonesia 1945] (Indonesia).

owner. The form of NV later being adopted and known as Limited Liability Company ("LLC") when the Indonesian Parliament established the first Limited Liability Company Law ("LLC Law") in 1995.

The form of LLC dominates business transactions in Indonesia, not only because of its characteristic, yet it is also the only form of the company allowed to be listed in the stock market. The Indonesian Stock Exchange imposed a company shall be in a form of LLC when it intends to conduct an initial public offering.[9] Furthermore, in the context of foreign capital investment, the Indonesian Law suggest that foreign capital investment to be executed in the form of an LLC.[10]

The process of the LLC Law lawmaking started in 1970 and took up to 25 years in the Parliament before it was publicly announce in 1995.[11] The 1995 LLC Law was later replaced with the latest version in 2007.[12] During the long process, some political influence on behalf of International monetary or funding institutions as a condition of *Post-Asian Financial Crisis* bail-out policy from the International Monetary Fund for Indonesia's economy and pursued some policies to be adopted in the domestic law. Consequently, the law relates to LLC in Indonesia influenced by Organisation for Economic Co-operation and Development's good corporate governance principle, United States Agency for International Development and Economic Law and Improved Procurement Systems project[13], and incorporated some of the common law aspects such as piercing corporate veil principle, director duties and the business judgement rule, as well as derivative actions.[14]

However, the long history of colonialism left Indonesia in the shadow of civil law as the former colonialist and adopted the civil law corporation model. The main character for most civil law companies is the two-tier board structure. Indonesia purely adopts the formal structure of the company board of LLC from the Dutch, which is identified by keeping the supervisory board named the board of commissioner as a default structure in LLC. In the LLC Law, it is explicitly stated that LLCs adopt the two-tier board system, with the structure of a Board of Director and a Board of Commissioner.[15]

2.1.2. Background of Company Board's Structure

According to the LLC Law the LLC board of directors shall have at least one director.[16] However, when there is a condition that a company has more than one director, the LLC Law ruled that the company shall differentiate each director's duties.[17] However, the authority to

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9 *Keputusan Direktur Bursa Efek Indonesia* No. Kep-00101/BEI/12-2021 *perihal Perubahan Peraturan Nomor I-A tentang Pencatatan Saham Dan Efek Bersifat Ekuitas Selain Saham Yang Diterbitkan Oleh Perusahaan Tercatat* [Decree of The Board of Directors of The Indonesian Stock Exchange No. Kep-00101/BEI/12-2021 regarding the Amendment of the Regulation no. I-A on Listing of Shares and Equity Securities other than Shares Issued by the Listed Company] (Indonesia) December 2021, pt III, s 1, ss 1.

10 *Undang-Undang Nomor 25 Tahun 2007 tentang Penanaman Modal* [Law No 25 of 2007 on Capital Investment] (Indonesia) art 5(2).

11 Mahy (n 4) p. 408.

12 *Undang-Undang Nomor 40 Tahun 2007 tentang Perseroan Terbatas* [Law No 40 of 2007 on Limited Liability Company] (Indonesia) ('*LLC Act 2007*').

13 Mahy (n 4) 411.

14 *Ibid*, p. 412.

15 LLC Act 2007 (n 14) art 1(2).

16 *Ibid,* art 92(3).

17 *Ibid,* art 92(5).

determine the duties, including each director's task and responsibility, is given to the general meeting of shareholders. Regardless, such authority can also be exercised in the board meeting if the general meeting of shareholders does not exercise such authority. Based on the divisions that have been made, each director is allowed to perform their duties severally.

In the context of the board size, the mandatory provision in LLC Law ruled that board of commissioners minimum member is one individual. However, there is different treatment in the event that the board consists of more than one person. For the board of directors, each member is allowed to act severally, while for the board of commissioners, the member shall act in a committee (collective collegial).[18]

2.1.3. Selection and Appointment

There are limitations on the selection and appointment of a member of the board, that is to meet the following criteria:

1. An individual who has the capability to perform legal action; and
2. Within 5 (five) years prior to his appointment, the member shall never:
   a. Been declared bankrupt;
   b. being the member of the Board of Directors or the member of the Board of Commissioners who has been adjudicated to have caused the bankruptcy of a Company; or
   c. had been sentenced for a criminal offence that caused financial loss to the state and/or relating to the financial sector.

Concerning the selection and appointment mechanism, both board of directors and both commissioners are selected and appointed by the general meeting of shareholders. Prevailing regulations do not stipulate the length of position for both boards, thus leaving it for each Company to regulate within its articles of association. Some companies prefer to give the board opportunity for 5 years and a limitation of re-election, and some prefer to shorten it to 1 year in conjunction with the annual general meeting of shareholders schedule without any limitation of re-election. However, the general meeting of shareholders is entitled to dismiss the board at any time by passing the extraordinary general meeting of shareholders resolution.

2.1.4. Duty of the Boards

In accordance with the background of forming a limited liability company, in which the capital owner will be in position as the shareholder and appoint agents as their boards with the imposition of duties to be performed, it is necessary to examine the duty of the boards. The characteristic of a two-tier board structure creates a formalized separation of duty between the boards, as elaborated below:

First the Board of Director. The Board of directors is a formal organ imposed with the duty to lead and manage the company in accordance with the interest and objectives of the company as specified in the policy and provision regulated under the law or company's regulation.[19] With the existence of a duty, the board of directors is given the authority to act for and on behalf of the company. Hence, the decisions made by the board of directors will represent the company as whole towards other parties. The existence of such responsibility is an inseparable component with the duty and authority that is given. Every member of the Board of directors can be held personally liable for the losses they caused to the company due to personal fault/negligence while carrying out their duties. In addition, if the board of

[18] *Ibid*, art 98(2), art 108(4).
[19] *Ibid,* art 1(5), art 92(1).

directors of a company consists of two or more individuals, they automatically have a joint and individual liability applicable to each member of the board of directors**.** However, there are some limitations to the director's responsibility regarding the company's loss. Those limitations will only become applicable under the circumstance where the director can prove that:

a. The director's fault/negligence did not cause such loss;
b. The director(s) have performed the management of the company with good faith and prudence for the company's interest in the pursuit of its purposes and objectives;
c. There is no conflict of interest, either directly or indirectly, over the management that led to the loss suffered; and
d. The director(s) have taken all the precautionary measures they might foresee to eliminate the liability.

Hence, when the director can prove that they have fulfilled the abovementioned cumulative requirements, the director in question cannot be held liable for the loss suffered by the Company.

Second is the Board of Commissioners. The board of commissioners is a formal organ of the company, authorized by law or the company's articles of association to conduct general or specific supervision over the board of directors.[20] The supervisory duty mentioned can be performed by supervising the management policy, the implementation of the management in general, or regarding the company's business.[21] The phrase 'supervising' is often misled as 'monitoring'. However, supervising has broader definition than duty to monitor alone. It is expected that the board of commissioners play the role as an advisor to the board of directors. In addition, board of commissioner shall conduct the supervision continually for the company's interest and in accordance with the purpose and objective of the company.

Following the duty of supervision imposed on the board of commissioners, the LLC Law gives some authorities to support the board. For instance, the board of commissioners is entitled to temporarily suspend the board of directors.[22] During the period of suspension, the general meeting of shareholders shall be convened before the expiration of 30 (thirty) days of the date of suspension.[23] Furthermore, if the 30 (thirty) days have lapsed and the general meeting of shareholders fails to be convened, or the general meeting of shareholders fails to adopt any resolution, the suspension shall be declared void by the law.[24] However, the board of commissioners is expected to perform this authority based on a reasonable basis and pass the resolution with specific reasons. The essence of this authority is based on the consideration of time constraints towards the dismissal of members of the board of directors by the general meeting of shareholders.

As a case study, case of *Stefanus v Anton*[25] can be referred as the precedent of suspension of the board of directors performed by the board of commissioners in Indonesia. The plaintiffs in this case were the former directors who suspended by the defendant. The supreme court judges entered the judgments in favour of the defendant and clearly stated that it was reasonable to legitimize the dismissal of the board of directors in this case because the defendant succeeded in proving that there was an urgency of the company's interest towards the suspension of the plaintiff.

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[20] *Ibid*, art 1(6).
[21] *Ibid*, art 108(1).
[22] *Ibid*, art 106(1).
[23] *Ibid*, art 106(4).
[24] *Ibid*, art 106(8).
[25] Supreme Court of Indonesia [2022], No 770 K/Pdt/2022, 4 April 2022, 8 (Indonesia) (‘Case 1’).

Unlike the duty to manage day to day operations held by the board of directors, which is more measurable by certain key performance indicator, the implementation of supervision duty seems to be more abstract. In the absence of law governed by legislation, the technical implementation of supervision duty must be governed rigidly by internal company's regulation. One reasonable proposal, implemented by *PT Pertamina Gas*, a subsidiary company of *PT Pertamina (Persero)* Largest Public-Private Partnership Oil and Gas Company in Indonesia, which proposed to measure the commissioner's duty based on 2 (two) indicators: performance and conformance.[26] The performance-based indicator emphasizes the board of commissioner's performance towards the duty to provide direction and guidance to the board of directors and provide an advise to the General Meeting of Shareholders.[27] However, the conformance indicator emphasized monitoring the board of director activity and ensure the advice which had been given are implemented.[28]

In matters of liability regarding company's loss that might be carried by the board of commissioners when failed to perform the duty, the LLC Law constituted that the member of the boards shall jointly and severally be liable for the company's loss.[29] However, practically the implementation of personal liability might be imposed severally towards each member, is contradicted with the provision[30] which clearly mention that the member of the board of commissioners should act in committee (collective collegial). The Supreme Court of Indonesia position on the case: *Asian Development Bank Ltd v Djaya Tunggal Ltd*[31], could be referred to clear up the perplexity towards the liability of the board's members. This case decided that the Board of Commissioners was jointly liable (not severally) with the Board of Directors for the company's losses caused by the failure to perform their duties.

2.2. Australian Company Board's Structure

2.2.1. Board's Structure

Prior to the establishment of the Corporations Act 2001 (Cth) ("Corporations Act"), companies in Australia were governed under States legislation.[32] The government made several attempts to unify the corporation law across the states regarding the urgency from the economic point of view and for the companies operating across the states.[33] However, this attempt met failure regarding constitutional validity concerning on the capability to bind each state. Further back, Australia's first state corporations' legislation was the Uniform Companies Act 1961 (Vic), and the limited liability characteristic was first mentioned on the Acts of 1855-

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[26] *Surat Keputusan Direksi dan Dewan Komisaris PT Pertamina Gas No. Kpts-003/PG0000/2021-S0, No. Kpts-015/DK-PG/II/2021-S0 tentang Dokumen Good Corporate Governance* [The Decree of Board of Director and Board of Commissioner PT Pertamina Gas regarding the Good Corporate Governance Document], 28 Februrari 2021 (Indonesia) p. 6.

[27] *Ibid*.

[28] *Ibid*.

[29] LLC Act 2007 (n 14) art 114(3).

[30] *Ibid*, art 98(2), art 108(4).

[31] Supreme Court of Indonesia [1991], No. 1916K/Pdt/1991, 14 August 1996, 9-10 (Indonesia) ('Case 2').

[32] Tony Ciro, *Corporations Law: In* Principle / *Tony Ciro, Christopher Symes* (Thomson Reuters (Professional) Australia Limited, 9th ed, 2009) p. 3.

[33] *Ibid*, 4.

62, English legislation.[34] There are several types of corporations in Australia such as corporations formed by Royal Charter, sole corporations, corporations formed by special statutes, and corporations formed by registration. Company, is one of the form of corporations. A Company has a 'limited liability' character which is introduced by the Corporations Act; this feature makes companies become *prima donna* among other forms of association.[35]

Before the regime of state legislation, companies in Australia were tailored based on English Companies Act; therefore, Australia adopted the characteristics of United Kingdom (UK) companies.[36] The fundamental idea of company legal structure in the UK is the owner of capital shall be seated behind the table as a shareholder, and appoints agents, known as directors, to run the business and report it periodically to them.[37] The agents appointed be seated on a board to perform and act as the face of the company which called as directors. The legal framework of Australian companies which adopt the UK company model is based on a unitary board system.[38]

In addition, for Australian companies, primarily in the stock market, are highly influenced by the Australian Securities Exchange (ASX) and the Australian Securities Investment Council (ASIC). The ASX is a listed exchange group that has a role as the market operator of the stock market in Australia, formed by the legislation passed by the Australian Parliament to merge the state-based stock exchanges into a single organization.[39] However, the ASIC is an Independent Australian Government body that was set up under the *Australian Securities and Investment Commission Act 2001* (Cth) as an integrated regulator[40] of financial service, market, consumer credit, and corporate, acting as the primary body that performs the administration of company law.[41] ASX and ASIC provide several guidelines and publications related to corporate governance, such as *Corporate Governance Principles and Recommendations* (ASX Recommendation);[42] handling corporate information;[43] directors and corporate culture[44] to answer some practical problems of the board even at some of the details at technical level.

2.2.2. Composition of the Board

The Corporations Act stipulates that a proprietary company shall have at least one director and ordinarily stay in Australia.[45] In the condition where a company has one or more

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34 Elizabeth J Boros, *Corporate Law / Elizabeth Boros, John Duns* (Oxford University Press, 2nd ed, 2010) p. 13.

35 Boros (n 39) p. 31.

36 *Ibid*, 13.

37 Charkham (n 5) p. 15.

38 Boros (n 39) p. 84.

39 ASX, 'ASX Story*',* see *History*, https://www2.asx.com.au/about/asx-story .

40 Australian Securities & Investments Commission, 'Our Role', https://asic.gov.au/about-asic/what-we-do/our-role/ .

41 Boros (n 39) p. 20.

42 ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations*, (4th edition, 2019) ('ASX Recommendation').

43 Australian Securities & Investments Commission, 'Handling Corporate Information', https://asic.gov.au/regulatory-resources/corporate-governance/handling-corporate-information/

44 Australian Securities & Investments Commission, 'Executive Remuneration', https://asic.gov.au/regulatory-resources/corporate-governance/executive-remuneration/.

45 Corporations Act 2001 (Cth) ('*CA 2001*') pt 2D.3, s 201A, ss 1.

crowdsource funding (CSF) shareholders, the company shall have at least two directors.[46] However, a public company requires three directors for the minimum.[47] Regarding the composition and structure of the board, some suggestions are proposed by the ASX recommendations, especially by the ASX recommendation 2. For instance, recommendation 2.1 points out that the board shall have a nomination committee consists of at least three members, with the majority being independent directors.

Furthermore, recommendation 2.4 suggests an independent Director shall dominate the board. Although the recommendations are non-binding and have no *expressive-verbis* sanction, the ASX Listing Rule set out that the entities subject to the ASX Listing Rule on their annual report should declare conformity with the ASX Recommendations, known as 'comply or explain' rule of the game. On the other hand, for small companies, compliance towards the ASX recommendations, such as the board size, including the independent, executive and non-executive director composition at the board, might be unduly costly.[48]

2.2.3. Selection and Appointment

The Corporations Act states the director's qualifications and some conditions that might cause the director to become disqualified. The details of disqualification provisions for the director selection are written in Part 2D.6 of the Corporations Act. In addition, some general qualifications of a director are:

1. An individual at least 18 years old;[49]
2. Prior to the lasts five years, never being convicted on indictment or an offence as written in Part 2D.6, section 206B, subsection 1;[50]
3. The person is not involved in bankruptcy or personal insolvency agreement to some extent as written in Part 2D.6, section 206B, subsection 3-5;[51]
4. The person is not declared unqualified by the foreign court orders as written in Part 2D.6, section 206B, subsection 6.

On the other hand, it is explained that an individual disqualified under Part 2D.6 of The CA probably has the chance to be appointed as director of a company if ASIC grants permission or leave granted by the court.[52]

In general, decisions to elect and remove the director are made by shareholders in a shareholders meeting.[53] In addition, the Corporations Act provides a unique provision that allows the existing directors to appoint a 'board-appointed director' and appoint an 'alternate director' for a set period.[54]

2.2.4. Duty of the Board

The statutory provision relates to the duties and power of the director are set out under the Corporations Act, which generally states that the director has the responsibility to manage

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46 *Ibid,* pt 2D.3, s 201A, ss 1A.

47 *Ibid,* pt 2D.3, s 201A, ss 2.

48 Ray Da Silva Rosa et al, 'Board Characteristics of Australian IPOs: An Analysis in Light of the ASX Best Practice Recommendations' (2004) 14(32) *Australian Accounting Review* 25, p. 32.

49 CA 2001 (n 51) pt 2D.3, s 201B, ss 1.

50 *Ibid,* pt 2D.6, s 206B, ss 2.

51 *Ibid,* pt 2D.6, s 206B, ss 3.

52 *Ibid,* pt 2D.3, s 201B, ss 2.

53 *Ibid,* pt 2D.3, div 1 s 201G, s 201H, ss 3., s 203D.

54 *Ibid,* pt 2D.3, div 1 s 201H, ss 1-2, 201K.

the business of a company and might exercise all of the power of the company except the power that requires the company to exercise in a general meeting of shareholders.[55] On the other hand, no particular provisions in the act mentioned the duty of supervision, and the internal board structure makes the board create an 'organic' separation of duty. Therefore, the board usually consists of an executive director, who in charge of the management, and a non-executive director, who will supervise the management.[56] In addition, the ASX Recommendation suggests the board formulate committees with a special duty to conduct such as nomination, audit, and remuneration risk committees.[57]

3. Corporate Governance Principle in the Board Structure

It has been common knowledge that the corporate governance principle has to be implemented across all of the company's aspects to maximize the effectiveness and efficiency of corporate performance and sustainability. Some perspectives regarding the board structure in Indonesia and Australia are compared to test whether the board's structure might significantly affect the implementation of corporate governance principles.

3.1. Implementation of the Independency Principle

3.1.1. Role of Chairman and Executive Board

Independence in the board has a strong relationship with role of chairman and chief executive or managing director.[58] The further discussion emphasizes the atmosphere of independency within the board created by the relationship between the chairmanship and chief of the board rather than focusing on the composition of independent board members. Research on the board structure in France companies stated that the concept of a unitary board system is a setting where the chairman and chief executive are placed in one room.[59] It is found that, there is no stipulative definition found in both Australian and Indonesian statutes, regarding the chairman and chief executive. However, the customary in the world of a corporation is that the primary role entitled to the chief executive is managing the company while the chairman is running the board.[60] The discussion below are going to examine further the role and relationship between chairman with chief of the board in both Australian and Indonesian company.

The absence of mandatory statutory provisions about the chairman and chief executive roles provides space for the company's article of association to regulate. As mentioned before, the primary role of a chief executive as the top of executive authority, which running the

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55 *Ibid,* pt 2D.1, div 4, s 198A.

56 Perth Casino Royal Commission, *Final Report*, vol IV 4 March 2022, Appendix E:Corporate Governance Theory, 886.

57 ASX Recommendation (n 48) see 2.1, 4.1, 7.1, 8.1., Australian Council of Superannuation Investors, ACSI Governance Guidelines (2021) ('ACSI Guidelines') 15.

58 Grit Tüngler, 'The Anglo-American Board of Directors and the German Supervisory Board - Marionettes in a Puppet Theatre of Corporate Governance or Efficient Controlling Devices?' (2000) 12(2) *Bond Law Review* 21.

59 Benedicte Millet-Reyes and Ronald Zhao, 'A Comparison Between One-Tier and Two-Tier Board Structures in France' (2010) 21(3) *Journal of International Financial Management & Accounting* 279, 286.

60 Andrew Kakabadse et al, 'Chairman and Chief Executive Officer (CEO): That Sacred and Secret Relationship' (2006) 25(2) *Journal of Management Development* 134, 143.

company's management, is easier to be measured.[61] On the other hand, the overall role of the chairman might seems to be as mentioned below: [62]

1. To set the time and agenda for board meetings;
2. To ensure the documents and all of the information related to board meeting agendas' is provided;

Apparently, the chairman is expected to go beyond just chairing the board meetings. Harmonization in the board is one essential responsibility carried by a chairperson. Based on the case *Woolworths Ltd v Kelly*[63], the judge opined that a person who is chairman of a board of directors has "additional rights and duties and additional opportunities", as he mentioned that:

> "Ordinarily it is the function of a chairman to settle the agenda of the meetings of the board: at least he exercises a significant influence upon it. He is in a position, in the sense here relevant, to ensure that proposals are brought forward for consideration by the directors at their meetings. And this, in a particular case, this may affect the content of fiduciary duties he owes to his company."

In the single-tier board structure; there is a possibility that the role of chairman and chief executive will be held by one individual. On the other hand, in Australia, non-executive directors are mostly selected by the chairman.[64] These two scenarios cause concern about the independency among the board of directors since the non-executive director will be influenced by the CEO, who also acts as chairman. Such a problem has become a concern not just in Australia but also in the United States, proven by the establishment of the provision of section 972 in the *Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010* in the United States, which prohibits an individual concurrent role as Chairman and CEO.

In response to this issue, the ASX recommendation 2.5. advises that the chair of the board should be independent and must not be the same individual as the chief executive officer (CEO).[65] Furthermore, in the selection of a chairman, it is necessary to consider whether the chairman shall not be an executive either.[66] When an executive acts as a chairman, who has the duty as the bridge between executive and non-executive, it is unlikely to be seen that they could perform duty purely neutral from any tendency upon the interest of management. However, with the compliance of certain matters related to chairman and chief executive selection and appointment mentioned above, it is believed that the board members' independence will be improved.

Similar to Australia, the LLC Law in Indonesia is absence regarding the key roles of chief executive and chairman. Based on the common understanding that the chief executive is the top authority at the management level, therefore, the chief executive function shall be carried out by the director, who acts as the leader of the board of directors. The LLC Law stipulates that in the event the board of directors consists of 2 (two) members or more, the distribution of duty and authority among the member of board of director shall be determined based on the resolution of the general meeting of shareholders or based on the company's

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61 Charkham (n 5) p. 321.

62 Perth Royal Casino Commission (n 66) p. 889.

63 (1991) 4 ACSR 431, Mahoney JA 445.

64 P Staple Don, 'Board Composition, Structure and Independence in Australia's Largest Listed Companies' (1997) 21(1) *Melbourne University Law Review* 37, p. 158.

65 ASX Recommendation (n 48) 2.5

66 Don (n 76) p. 160.

articles of association.[67] A company's articles of association typically regulates that the general meeting of shareholders shall appoint one of the directors as the president director. Best practices also showed that the company's articles of association typically give the president director the authority to initiate and set up the board meeting agenda. In this scenario, an individual which likely carries the chief executive and chairman role: the president director.

Related to the board of commissioners, the common provision in the company constitution governs that if there are 2 (two) or more members of the board, the general meeting shall appoint one of them as the president commissioner. Furthermore, the company's articles of association typically states that the president commissioner has the authority to chair the board of commissioner's meetings and to act as the head/leader to act for and on behalf of the board of commissioners.

The idea that in a two-tier structure company, the chief executive and chairman sit in different rooms[68], whereabout the chief executive role held by president director and the chairman role carried by the president commissioner does not fit in the Indonesian board structure. The formalized separation of duty limits the power of each board to interferes each other. Therefore, the board of commissioners has no power to chair the board meeting of the board of directors and *vice versa*.

Based on the separation of the board structure as illustrated above, it is seen that the monitoring activity as the supervisory board duty can be performed independently without any influence from the management. However, this structure leaves a flaw in the matter of independency in each board internally. Several research have been done regarding the issue of chairperson and chief roles carried by one individual and show that it is highly potential to create domination and reliance towards dual roles held by the president director and the president commissioner, which led the dependency of its board's member.[69]

3.1.2. Remuneration

The remuneration plan significantly influences the independency while the board performs its duty. In general, the remuneration is divided into two schemes, fixed remuneration with fixed sum amounts payable and variable remuneration with short-term incentives and long-term incentive.[70] Variable remuneration often calculates based on performance indicators towards the company's business. However, in this event, it is suggested that the non-executive should not be paid by the variable remuneration because it is likely to be seen they will have a conflict between their interest in the remuneration and their independent assessment after the management decisions.[71] The discussion below is going to describe the remuneration plan in both Australian and Indonesian company.

The ASX Recommendation 8.2[72] strongly suggested that the non-executive director is not entitled to any performance-based remuneration and is only entitled to receive fixed remuneration and equity-based. Furthermore, the ASX recommendation 8.1[73]suggested the board shall establish the remuneration committee with the majority and be chaired by

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67 LLC Act 2007 (n 14) art 92(5).
68 Millet-Reyes and Zhao (n 70).
69 Grit Tüngler (n 70) p. 21.
70 ACSI Guidelines (n 48) p. 17.
71 *Ibid,* p. 21.
72 ASX Recommendation (n 48) 8.2.
73 *Ibid*, 8.1.

independent directors. Based on the recommendation mentioned, it is shown that Australia has paid serious attention to remuneration and the board's independence.

Whereas, under the Article 96 of the Indonesian Corporations Act, the power to determine the remuneration of the Board of Directors has been given to the General Meeting of Shareholders. However, the authority may be conferred to the Board of Commissioners and determined based on the resolution of the Meeting of the Board of Commissioners. Furthermore, based on the explanation section of the Corporations Act Article 71 paragraph 1, the board of commissioners is entitled to receive bonuses and profit sharing from the company. Based on this provision, the Indonesian company has to be more aware, especially in terms of governing their remuneration policy. They should specify the type of remuneration entitled to the member of BOC, in the light of maintaining BOC independency towards the BOD.

3.1.3. The Duty to Monitor

A company monitoring process is important in determining a company's accountability. There are various of type of reports to be monitored, such as the report of the company's regular activity, report of risk, and financial report, which then could be audited by internal or external auditor. In this context, 'auditing' is an element that cannot be secluded from the monitoring process. However, independence during the audit process is an essential point in order to maintain the integrity of the audit result.

To reach the level of independency in auditing process, it is necessary to discharge the involvement of the management during the process.[74] For instance, if the Chief Executive Officer, as the head of management, directly engaged with the auditor, the CEO would likely influence the auditor to audit on behalf of the management's interest. For instance, they could possibly threaten the auditor, that they will engage with another auditor, if it does not go in line with their interest. In connection with this problem, the discussion below aims to examine how the board system in Australian and Indonesian company cope with this issue.

The idea of a one-board system might cause substantial management interference towards the auditing process. Concerning this emerging problem, ASX released recommendation 4.1, which encourages the company to establish an audit committee composed of non-executive directors, and the majority shall be independent directors.[75] This committee would act independently from the board with general duty related to all of the matters concerning the audit process, such as providing the company's documents and engaging with the auditor, establishing and being responsible for the internal audit system, et cetera.[76] The end game ought to be achieved by establishing the audit committee is adding credibility to the audit process.[77]

On the other hand, in the formalized separation of the two-boards structure applied in an Indonesian company, it seems easier to maintaining independency during the audit process. Unfortunately, the LLC Law does not stipulate any provision related to the company's audit. In general, based on the provision that the company management held by BOD, therefore they are the one who performed the engagement with the auditors. In response to

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74 ASIC Guidelines (n 48) p. 37.

75 ASX Recommendation (n 48) 4.1.

76 *Ibid* 4.1, 7.3.

77 Elizabeth Shi, 'Board Structure and Board Composition in Australia and Germany: A Comparison in the Context of Corporate Governance' (2007) 10(4) Macquarie Journal of Business Law 197 pp. 11, 16.

this issue, the Indonesian Financial Services Authority has released the regulation related to the establishment and guidelines of implementation of the audit committee.[78] Moreover, the Indonesian National Committee on Governance Policy, which was established according to *The Decree of The Coordinating Minister of Economic Affairs of the Republic of Indonesia Number 44 of 2021 concerning the National Committee of Governance Policy,* has issued the guidelines to establish an effective audit committee in May of 2022.[79] Both guidelines strongly encourage a company to establish its audit committee. It is explained that the audit committee is a committee formed by the member board of commissioners with the duties of establishing and monitoring the internal audit system and interacting with external audits. However, the representation has become a practical problem when the committee interacts with the party outside the company's body.

The final issue is LLC Law regulates that the company's representative is the board of directors.[80] On the other hand, if the audit committee is a board of commissioners, by the law they do not have the authority to make any deal on behalf of the company, including the appointment of the auditor. Concerning to this problem, it is necessary to constitute a provision in the company constitution, specifically regarding to the board of commissioners authority as audit committee to conduct, engage, and appoint the auditor without any interference of the board of directors.

3.2. Transparency and Disclosure of Information

Disclosure of information plays a significant role in almost all of the company's aspects. It is a crucial instrument to achieve the fulfillment of good corporate governance principle: transparency.[81] However, before going further to the end game, the transparency ought to achieved towards the external party (such as customer etc.), company must pay attention to transparency in its internal structure: especially in between the board member. The disclosure of information emphasizes on the flow of information. Basically, there are two major types of information: (i) information about the company's activities and decisions, and (ii) information that may affect the company's actions and decisions.

The approach to information disclosure may be significantly different in connection with the board's structure, whether a single-tier or two-tier board. However, the matter of information was crucial to performing the board's duty. Furthermore, monitoring and assessing a company's decisions or activities cannot be secluded from the information availability and it is essential to the decision making process. In relation with this issue, the discussion below aims to examine how the board in Australian and Indonesian company disclose the company's information.

In light of the importance of information disclosure regarding management activity, the single-tier board structure adopted in Australian companies tends to have more advantages than the two-tier board structure. It is essential that the board shall have an effective flow of information, which enables the non-executive director to perform their duty to monitor the

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78 Keputusan Ketua Badan Pengawas Pasar Modal Dan Lembaga Keuangan No. KEP-643/BL/2012 [The Decree of Chief of Financial Service Authority No. KEP-643/BL/2012] 7 December 2012 (Indonesia).

79 National Committee of Governance Policy, *Guidelines of establishment of effective audit committee guidelines*, 30 May 2002, https://knkg.or.id/publikasi/ (Indonesia).

80 LLC Act 2007 (n 14) art 98(1).

81 UN Guidelines (n 68) p. 2.

management activities. With enough resource and relevant information make the non-executive directors more accountable for their monitoring result.

Some factors as a fundamental measurement to examine the effectiveness of information flow in the board are orderliness and accessibility of information. Orderliness in the storage or record of information is a significant key factor in the flow of information. Irregularity in the record of company's minutes meetings, dispositions, and resolutions will deteriorate the flow. On the other hand, accessibility to collect the information is no less important than orderliness. No matter how many the information has been recorded and stored, it is useless unless the board member has to have the key to access it. The nature of board's structure in a one-tier board system, is the non-executive directors and executives are seated in the same room. Therefore, it is reasonable to presume that the non-executives certainly have easier access to obtain the information from the executives.[82]

In the absence of statutory provisions, the board shall regulate how frequent the board meetings shall be conducted in order to supervise and evaluate the management's performance. However, the organic relationship built with the constant interaction between the executive and non-executive directors promotes individual chemistry as the information across the board's member. Once the flow information went smoothly and chemistry has been established, it will certainly results a transparency during the decision-making process.

Furthermore, in the context of decision-making, compared to the two-tier board structure where both boards demanded to hold a formal meeting to discuss and approve particular issues, in an organic relationship found at single-tier board, allows the board to hold meetings frequently (formally or informally) and enabled them to make decision more quickly.[83] Ultimately, in the Australian company, the exchange of information brought by the diverse background of the directors might enrich the board's knowledge.[84] When the board is running the company, there is more dimension than just the business itself, therefore, the more diverse knowledge be brought to the board would eventually benefit the company.[85] A one-tier board structure allows the diverse individuals mentioned before to be seated as non-executive directors. The positioning of non-executive directors in the same room with the management enables them to contribute a wider range of knowledges, expertise, and network to the management while simultaneously performing their supervisory duty.

Whereas in Indonesia, the board of commissioners has the duty to supervise the executive board. As explained in the previous section, the board of commissioners has no power related to management and operation of a company. It is a necessity that the board of commissioners shall have enough knowledge of the business run by the board of directors to perform this duty. The formalized separation structure in two-tier board companies tends to create a circumstance where the supervisory board has minimum insider business knowledge because they were placed in a completely different 'room', therefore, they tend to be uninvolved in the business operation.

In terms of the exchange of information, the golden standard is, the chairman of the management board should provide the chairman of the supervisory board a monthly report which at least consists of financial statement, asset position, and license (the content of the

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[82] David Block and Anne-Marie Gerstner, 'One-Tier vs. Two-Tier Board Structure: A Comparison Between the United States and Germany' (2016) *Comparative Corporate Governance and Financial Regulation*, 19.

[83] *Ibid*.

[84] *Ibid*, p. 21.

[85] Elizabeth Shi (n 90) p. 16.

report might be in various form, depends on the particular business of the company).[86] The best practice in Indonesia suggests that the board of commissioners is given the authority to check the corporate documents and the right to question the board of directors. Usually, the company's articles of association stipulate that the board of commissioners has the right to inspect all corporate documents at any working time.

In Indonesia, the law of Company document is governed under two Acts. First one is LLC Law and second is Law Number 9 Year 1997 on Company Document. Generally, the law imposed the duty towards the Board of Directors to keep the record of the following documents, including:[87]

1. Shareholders register, Special register, Minutes of the General Meeting of Shareholders, and the Board of Directors meeting minutes.
2. Annual report of a Company, which is at least contains of:
    a. the financial statement, which at least consists of the current balance sheet of the latest accounting year in comparison with the previous accounting year, a profit and loss statement from the relevant accounting year, cash flows, report on the equity changes, and the record on such financial statement;
    b. report on the company's activities;
    c. compliance to the corporate social and environmental responsibility;
    d. report on supervisory duty that Board of Commissioners has performed during the previous accounting year;
    e. name of the members of the Board of Directors and Board of Commissioners; and
    f. Remuneration execution for the previous year.
3. Other financial documents of the Company include any supporting documents of the transaction.
4. Other Company's documents (any writing that contains valuable information valuable for the company)

The documents as referred in (2)-(4) are classified as essential information which shall be monitored by the Board Commissioners. The authority to inspect company's documents and enquiring the director might be seen as an answer in order satisfy the board of commissioner's access towards source of information from the management: board of director. However, while exercising this authority the board of commissioner shall consider one important aspect which is harmonization across the boards and avoid the raise of 'temperatures' between the boards.

In practice, it is recommended to create more of organic relationship across the boards instead of exercising formal authority regards the access to company's business information. In addition, it is also suggested that BOD and BOC shall conduct a join meeting periodically with a fixed schedule. The best practice proposed by board manual of Indonesian largest public-private partnership company in oil and gas, *PT Pertamina (Persero)*, encourages the board of directors and board of commissioners to hold a scheduled meeting at least once in a month. In this meeting it is presumed that the board of commissioners can fully exercise their right to access all the company documents and enquiries the board of directors.

In connection with the board's meeting, minutes of meeting is a crucial document, therefore, the minutes shall be detailed and include the dissenting opinion of each member of

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[86] Grit Tüngler (n 70) p. 12.

[87] *Undang-Undang No. 8 Tahun 1997 tentang Dokumen Perusahaan* [Law No. 8 of 1997 regarding Company Document] Act art 66, art 100 (Indonesia).

the meeting.[88] Later, the minute shall be signed by the member of the meeting and whoever declines to sign it must explain their reason in the letter. Furthermore, with the technology and information revolution, it is necessary to establish the disclosure of information system, which allows all of the minutes of meetings and any other company documents to be uploaded in the database and authorize the members of the board of commissioner access to it. However, to set up and run the system mentioned before, it is necessary to appoint a company secretary who will be in charge to perform this duty.[89]

In the light of exchange of information among the boards, a company shall also emphasise in the diversity of the commissioners.[90] Research on listed companies in Indonesia from 2014 to 2018 showed that diversity such as expertise and industry experience in board of directors is not as significant as the diversity in the board of commissioners towards corporate performance. It is proven that the management shall be focused on the particular matter of the core company's business, left the other additional knowledge to be brought by the supervisory board. Ultimately, to ensure the overall knowledge of the business, the former member of the board of directors shall be highly considered as candidates in the event of board of commissioner's nomination.[91]

4. Conclusion

It is notable that the company board system in both countries was formed by a long history of culture, politics, and law. Therefore, this paper aims not to make a simplistic conclusion of whether the one-board system in Indonesian companies is better than the two-board system in Australia or vice versa. The discussion started with comparison of the formal board structure between both countries, concerned on the board's duty, where Indonesian company adopted a formalized separation of duty between the management by the board of directors and supervision by the board of commissioners. On the other hand, for Australian company apply the organic separation between management duty by executive director and supervision by non-executive director. The duty imposed always comes with liability when such is failed to be performed.

The aim of this paper is far from suggesting Indonesia or Australia to swap its board system. Although the board system of both countries derives from opposite system of law, civil law and common law, evidently those two have common grounds relate to spirit of fulfillment towards the corporate governance principles. The implementation of the independence principle over the chairman and chief executive roles is more applicable the Australian board. While in Indonesian boards the "actual" chairmanship role is in absence, the role which carried by an individual who can chair the meeting between the board of management and board of supervisor. Therefore, the Indonesian company should address this issue and governed it under its company constitution. Regarding the remuneration, it is necessary for the Indonesian company to learn from Australia system, specifically relates to performance-based remuneration. Furthermore, relates to monitoring duty it is notable that the formalized

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88 *Surat Keputusan Direksi PT Pertamina (Persero) No. Kpts-50/C00000/2017-S0 tentang Board Manual* [The Decree of Board of Directors of PT Pertamina (Persero) No. Kpts-50/C00000/2017-S0 regarding Board Manual] 14 September 2017 (Indonesia) pp. 41, 61, 62.

89 Charkham (n 5) 321.

90 Widyahayu Warmmeswara Kusumastati et al, 'Board Diversity and Corporate Performance in a Two-Tier Governance Context' (2022) 28(3/4) *Team Performance Management: An International Journal* 260, 275.

91 David Block (n 95) 34.

separation adopted by Indonesian company allows the board of commissioner to act more independent.

Lastly, in connection with the implementation of transparency principle, ultimately will be measured by how smooth the flow of information and the quality of information disclosure process among the board. The nature of the one-board system in Australia allows the non-executive and executive director to interact continually and built personal relationship. On the other hand, although the formalized separation in Indonesia seems to be a barrier towards a 'smooth' flow of information, the board of commissioner has the authority to inspect all of the company's documents and questioned the board of directors. Nevertheless, for both Indonesian and Australian company, the intensive and periodic board meetings certainly increase the effectiveness of the board performance. Furthermore, the revolution of technology shall be implemented to improve the record and database of company's document, allowing the board to perform their duty based on enough knowledge and understanding towards the company’s business. In addition, the diverse background brought by the non-executive director or member of board of commissioner, evidently enhance the exchange of information among the board and positively impacted the company's performance. To conclude, this paper aims to enrich the understanding of each system's approach towards the principles discussed above and identify whether each system calls for refinement.

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