

**THE ROLE OF CORPORATE GOVERNANCE CODES IN ENHANCING
ACCOUNTABILITY FOR EFFECTIVE DISCLOSURE IN INDONESIA**

By

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Abstract

Indonesia's performance in implementing corporate governance based on formal law has been poor because of weaknesses in its formal legal system. This thesis examines possible alternative approaches to the regulation of disclosure to achieve a better standard of corporate governance including the Indonesian Good Corporate Governance Code. The study considers the regulatory space corporate governance codes can occupy as an alternative regulatory strategy in the Indonesian context. Specifically, it evaluates the ways in which they can improve accountability for disclosure and corporate governance and also strengthen formal law and regulation. Different sources of data from the literature and media data bases and the interviews are used to be triangulated. It first explores the ideas and models in the literatures reviewed on disclosure, voluntary self-regulatory codes, alternative regulatory theories, the relationship between formal and informal law concepts, and comparative law on legal transplants. It examines how Indonesia's corporate governance codes accommodate these ideas, and in which areas their use may play a more significant role in strengthening formal law and regulation so that regulation becomes more effective, responsive, flexible, legitimate and transparent. It identifies relevant issues in political, social and business cultures which produced problems for formal law and regulation and the way in which the code as a form of alternative regulation may remedy such problems. And then these reviews are triangulated with business media data bases and empirical, semi-structured interviews.

The findings suggest that informal law represented by the code fails to serve its functions to be used as the alternative regulatory strategy and that it plays insignificant role in strengthening formal law and regulation and corporate governance especially in enhancing accountability for effective disclosure. Indonesia's context demonstrates inconsistency of the alternative regulatory theories. The thesis provides an understanding on why the capacity of alternative regulatory model such Code fails. It also displays the need of significant changes to address the failure. Changes in political and economic ideologies; structural and habitual executive, legislative and judiciary; legal and business culture; especially eradication of corruption are attributed toward the effective capacity of not only informal law but also formal law.

Student Declaration

“I, Jeannie Connie Rotinsulu, declare that the PhD thesis entitled ‘The Role of Corporate Governance Codes in Enhancing Accountability for Effective Disclosure in Indonesia’ is no more than 100,000 words in length including quotes and exclusive tables, figures, appendices, bibliography, references and footnotes. This thesis contains no material that has been submitted previously, in whole or in part, for the award of any other academic degree or diploma. Except where otherwise indicated, this thesis is my own work”.

Signature

Date 5/7/2016

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List of Abbreviations and Acronyms

The following abbreviations and acronyms appear in the main text or footnotes of this thesis.

AAI	: Asosiasi Akuntan Indonesia [Indonesian Accountant Association]
ACC	: Anti Corruption Court [Pengadilan Tindak Pidana Korupsi]
ACGA	: Asian Corporate Governance Association
ACMF	: ASEAN Capital Market Forum
ADB	: Asian Development Bank
ADB I	: Asian Development Bank Institute
AEI	: Asosiasi Emiten Indonesia [Indonesian Issuer Association]
APEI	: Asosiasi Perusahaan Efek Indonesia [Association of Indonesian Securities Company]
APRA	: Australian Prudential Regulation Authority
ASC	: Accounting Standards Council (Singapore)
ASEAN	: Association of Southeast Asian Nations
ASIC	: Australian Securities and Investments Commission
ASX	: Australian Securities Exchange
BAPEPAM-LK	: Badan Pengawas Pasar Modal dan Lembaga Keuangan [Indonesian Capital Market and Financial Institution Supervisory Agency]
Bareskrim Polri	: Badan Reserse Kriminal Kepolisian Negara [Criminal Investigation Agency of Indonesian National Police]
BCSC	: Business Competition Supervisory Commission [Komisi Pengawas Persaingan Usaha (KPPU)]
BIN	: Badan Intelijen Negara [Indonesian State Intelligence Agency]
BPPN	: Badan Penyehatan Perbankan Nasional [Indonesian Bank Restructuring Agency]
BPS	: Badan Pusat Statistik [Statistics Indonesia]
BSE	: Bulgarian Stock Exchange

BUMN	: Badan Usaha Milik Negara [State-owned Enterprises (SOEs)]
CALD	: Council of Australian Law Deans
CCDG	: Council on Corporate Disclosure and Governance (Singapore)
CG Watch	: Corporate Governance Watch
CGC	: Corporate Governance Committee (Singapore)
CGIP	: Corporate Governance Institute of the Philippines
CLDI	: Corporate Leadership Development Institute [Institut Pengembangan Kepemimpinan Korporasi] (Indonesia)
CLSA	: Credit Lyonnais Securities Asia
CPA	: Certified Public Accountant (Indonesia)
Dekopin	: Dewan Koperasi Indonesia [Indonesian Co-operative Board]
DEST	: Department of Education, Science and Training (Australia)
DPR	: Dewan Perwakilan Rakyat (Indonesian House of Representative)
EAFQ	: East Asia and Asia Forum Quarterly
ECGI	: European Corporate Governance Institute
ELIPS	: Economic Law and Improved Procurement Systems
ESOP	: Employee Stock Option Program
FCGI	: Forum for Corporate Governance in Indonesia
FKSPI BUMN/BUMD:	Forum Komunikasi Satuan Pengawasan Intern BUMN/BUMD [Forum for Communication of Internal Auditors of State-Owned Enterprises and Regional Government-Owned Enterprises]
FSMA	: Financial Services and Markets Authority (Belgium)
FSTB	: Financial Services and the Treasury Bureau (Hong Kong)
GCG Code	: Good Corporate Governance Code
GDP	: Gross Domestic Product
Gerindra	: Gerakan Indonesia Raya [Greater Indonesia Movement Party]
GMS	: General Meeting of Shareholder
Golkar	: Golongan Karya [Functional Group Party]
HAM	: Hak Asasi Manusia [Human Rights]
HIPPI	: Himpunan Pengusaha Pribumi Indonesia [Indonesian Indigenous

	Entrepreneurs' Association]
HKEx	: Hong Kong Exchanges and Clearing Limited
HREC	: Human Research Ethics Committee
IAI-KAM	: Ikatan Akuntansi Indonesia-Kompartemen Akuntan Manajemen [Indonesian Accountant Association-Management Accountant Compartment]
IAIM	: Irish Association of Investment Managers
ICAC	: Independent Commission Against Corruption (Hong Kong)
ICD	: Institute of Corporate Directors (Philippines)
ICPAS	: Institute of Certified Public Accountants of Singapore
ICW	: Indonesia Corruption Watch
IDEA.Net	: Institute of Directors East Asia Network
IDX	: Indonesia Stock Exchange [Bursa Efek Indonesia (BEI)]
IFC	: International Finance Corporation
IFEA	: Indonesian Financial Executives Association
IFRS	: International Financial Reporting Standards
IIA	: Indonesian Institute of Accountants
IICD	: Indonesian Institute for Corporate Directorship
IICG	: Indonesian Institute for Corporate Governance
ILO	: International Labor Organization
IMF	: International Monetary Fund
INA	: Indonesian Netherlands Association
INFID	: International NGO Forum for Indonesian Development
INSEAD	: Institut European d'Administration des Affaires [European Institute for Business Administration]
IOSCO	: International Organization of Securities Commission
IPO	: Initial Public Offering
IS	: Indische Staatregeling [de facto colonial constitution]
JITE	: Journal of Institutional and Theoretical Economics
JSX	: Jakarta Stock Exchange [Bursa Efek Jakarta (BEJ)]

KAGAMA	: Keluarga Alumni Universitas Gajah Mada [Alumni Family of Gajah Mada University]
KBBI	: Kamus Besar Bahasa Indonesia [General Dictionary of Indonesian Language]
Kemendikbud	: Kementerian Pendidikan dan Kebudayaan [Indonesian Ministry for Education and Culture]
KKN	: Korupsi, Kolusi dan Nepotisme [Corruption, Collusion and Nepotism]
KNKCG	: Komisi Nasional Kebijakan Corporate Governance [Indonesian National Commission on Corporate Governance Policy]
KNKG	: Komisi Nasional Kebijakan Governance [Indonesian National Commission on Governance Policy]
KPK	: Komisi Pemberantasan Korupsi [Indonesian Corruption Eradication Commission]
KPMG	: Klynveld Peat Marwick Goerdeler (accounting firm)
KPPU	: Komisi Pengawas Persaingan Usaha [Business Competition Commission Supervisory Commission]
KUHAP	: Kitab Undang-undang Hukum Acara Pidana [Indonesian Criminal Procedures Code]
KUHD	: Kitab Undang-undang Hukum Dagang [Indonesian Commercial Code]
KUHP	: Kitab Undang-undang Hukum Pidana [Indonesian Criminal Code]
KUMKM	: Koperasi, Usaha Mikro, Kecil dan Menengah [Co-operative, Micro, Small and Medium Enterprises]
KY	: Komisi Yudisial [Indonesian Judicial Commission]
LKDI	: Lembaga Komisaris dan Direktur Indonesia [Indonesian Institute of Commissioners and Directors]
LSI	: Lingkaran Survey Indonesia [Indonesian Survey Cycle (poolster)]
MAPPI	: Masyarakat Profesi Penilai [Indonesian Society of Appraisers]
MAS	: Monetary Authority of Singapore

MK	: Mahkamah Konstitusi [Indonesian Constitutional Court]
MPR	: Majelis Permusyawaratan Rakyat [Indonesian People's Consultative Assembly]
MPRA	: Munich Personal RePEc Archive
MSOP	: Management Stock Option Program
MTI	: Masyarakat Transparansi Indonesia [Indonesia Transparency Society]
Nasdem	: Partai Nasional Demokrasi [National Democratic Party]
NCGC	: National Corporate Governance Committee (Thailand)
NGOs	: Non Governmental Organizations
NHM	: Nederlandsche Handel-Maatschappij [Netherlands Trading Society]
NHMRC	: National Statement on Ethical Conduct in Human Research
NUS	: National University of Singapore
OECD	: Organization for Economic Co-operation & Development
OJK	: Otoritas Jasa Keuangan [Indonesian Financial Services Authority]
ORI	: Ombudsman Republik Indonesia
PDI-P	: Partai Demokrasi Indonesia – Perjuangan [Indonesian Democratic Party – Struggle]
PERADI	: Perhimpunan Advokat Indonesia [Indonesian Advocates Association]
PERC	: Political Economic Risk Consultancy
Permen	: Peraturan Menteri [ministerial regulation]
Perpu	: Peraturan Pemerintah Pengganti Undang-undang [Interim Law]
Pertamina	: Perusahaan Minyak Nasional [National Oil Company]
PHILTAR	: Philosophy, Theology and Religion
PKPI	: Partai Keadilan dan Persatuan Indonesia [Indonesian Justice and Unity Party]
POLRI	: Kepolisian Negara Republik Indonesia [Indonesian National Police]
PP	: Peraturan Pemerintah [Government Regulation]

PSAKs	: Pernyataan Standar Akuntansi Keuangan [Statement of Financial Accounting Standards]
PSE	: Philippines Stock Exchange
PUPUK	: Perkumpulan untuk Peningkatan Usaha Kecil [Association for Small Enterprises Development]
RBLCPP	: Resource-Based Learning Career Preparation Programme
RCB	: Registry of Companies and Business (Singapore)
RIS	: Republik Indonesia Serikat [Republic of the United States of Indonesia]
ROML	: Rakyat Merdeka Online [Independence people online political news]
ROSC	: Report on the Observance of Standards and Codes
RQF	: Research Quality Framework (Australia)
RSM AAJ	: Global Accounting firm
RUPS	: Rapat Umum Pemegang Saham [General Meeting of Shareholdres]
SAS	: Statement of Accounting Standards (Singapore)
SDI	: Sarekat Dagang Islam [Union of Islamic Traders]
SEC	: Securities and Exchange Commission
SET	: Stock Exchange of Thailand
SGX	: Singapore Stock Exchange
SI	: Sarekat Islam [Islamic Union]
SOEs	: State-owned Enterprises
SOX	: Sarbanes-Oxley Act
SRC	: Securities Regulation Code (Philippine)
SRO	: Self-Regulatory Organization
STAN	: Sekolah Tinggi Akuntansi Negara [Indonesian State College of Accountancy]
TAS	: Thai Accounting Standards
TGPTPK	: Tim Gabungan Pemberantasan Tindak Pidana Korupsi [Joint team

	for Eradication of Corruption Crimes]
TLCA	: Thai Listed Companies Association
TNI	: Tentara Nasional Indonesia [Indonesian Army]
UCL	: University College London
UNSF	: United Nations Security Force
UPS	: Uninterruptable Power Supply
USAID	: United States Agency for International Development
USU	: Universitas Sumatera Utara [North Sumatera University]
UU	: Undang-undang [Indonesian Act]
UUD 1945	: Undang Undang Dasar 1945 [Indonesian Constitution 1945]
UUDS	: Undang-undang Dasar Sementara [Provisional Constitution]
UUPT	: Undang-undang Perseroan Terbatas [Indonesian Limited Liability Company Act]
VOC	: Vereenigde Oostindische Compagnie [Royal East Indies Company]
Wantimpres	: Dewan Pertimbangan Presiden [Presidential Advisory Board]
WvK	: Wetboek van Koophandel voor Indonesie [Indonesian Commercial Code]
YPIA	: Yayasan Pendidikan Internal Audit [Indonesian Foundation for Internal Audit Education]

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Chapter 1 : Introduction

1.1. Background of the research

Significant efforts in law reform in Indonesia over the last 20 years designed to introduce good corporate governance principles appear to have been ineffective. The reform of regulatory processes of government agencies, the stock exchange and governance within corporations also appear to have been ineffective. Recent evidence provides many examples of this, including principles of disclosure and their application.

Weaknesses in formal law and regulation have come to be seen as major challenges to implementing better corporate governance. Experiences in some other jurisdictions show that corporate governance codes, as informal rules, may provide an alternative way to address the weaknesses of formal law.

This thesis is a study of possible approaches to the use of voluntary corporate governance codes in regulation of disclosure to achieve better standards in corporate governance in Indonesia. It considers the regulatory space that corporate governance codes can occupy as an alternative regulatory strategy in an Indonesian context. Specifically, it evaluates the ways in which they may improve accountability for disclosure, which underlies many other corporate governance principles, and also strengthens formal law and its application in regulation.

The study selectively explores the complementary relationships between formal and informal law in some other developing economies. This assists in understanding some aspects of the problem of corporate governance in such countries and also whether there are viable solutions to these problems which could be adopted by Indonesia.

The major question to be addressed in this study is: can a voluntary good corporate governance code be used as an alternative regulatory instrument to create effective corporate accountability for disclosure in the Indonesian context?

The following sub-questions are also explored:

1. What kind of functions can a code serve? Can these functions improve the effectiveness, efficiency and responsiveness of the regulation of corporate governance in Indonesia?

2. What aspects of Indonesian political, administrative and business cultures can be called on to support its use?

The study considers how these areas of culture and practice may assist in improving the implantation of codes and other regulatory strategies so that they are more effective.

The conceptual framework used in answering the research questions includes three other more general questions:

1. What factors influence the use of corporate governance codes as effective informal regulatory instruments?
2. What factors influence the effective use of formal and informal law as complementary regulatory instruments?
3. What are the factors which influence the effective transplantation of informal law between donor and host legal systems?

These questions are drawn from the ideas and models in the literature reviewed on voluntary self-regulatory codes and regulatory theory, including responsive regulation around co-operation between commercial enterprises and the state, and comparative law relating to legal transplants.

This thesis is divided into eight chapters with their own themes. This introductory chapter has six sections relating to the background to the dissertation, the aims and objectives of the study, the significance, the research methodology, the structure of the dissertation, and a conclusion. In order to give a contextual background to the research, a brief overview of Indonesia follows. The overview also summarises previous studies of corporate governance in Indonesia, in particular compliance with disclosure requirements, and considers the major factors which have been identified as contributing to poor disclosure and corporate governance. They indicate that there is an urgent need to increase accountability for disclosure in which the use of voluntary codes may still be significant.

1.1.1. A brief overview of Indonesia

Indonesia is the largest archipelago state in the world, comprising 17 508 islands. It is a developing economy with substantial natural resources scattered over 1.9 million square kilometres between the Indian and Pacific Oceans. It has massive human resources

comprising 240 million people¹, 2015 data shows almost 250 million people.² The country has diverse communities and cultures. This diversity has significant consequences. On the one hand it enriches the lives of Indonesians and provides the basis for relationships with global society through shared religions and other common cultural aspects but on the other hand it is often a source of internal conflicts. Both pose challenges to the national legal framework.³

The formal Indonesian legal system is classified as civil law. It is derived from a continental European legal system based on the original French codes as modified in the Netherlands from Indonesia's past as a Dutch colony. The legal system continues to reflect this Dutch tradition 70 years after independence. A number of colonial laws are still in force today including commercial laws. The Dutch influence is reflected in the dual board structure seen in listed companies which have a board of commissioners and a board of directors.

Adat [customary] law is also another source of national law although it has less influence. Customs vary across the archipelago. However, the *adat* principle *musyawarah untuk mufakat* [consensus through decision making] has been and is applied in framing contemporary Indonesian laws.⁴

In spite of its significant resources, the country is struggling to establish a stable and prosperous economy that distributes growing wealth across society. This is affected by the factors inhibiting greater stability and predictability in the legal system. These are rooted in historic, social, economic and political events. They are marked by different epochs: the traditional period (up to the early 16th century); the Dutch colonial period (from the early

¹ Portal Nasional Indonesia [Indonesia National Portal], *Profil Indonesia* [Profile of Indonesia] <http://www.indonesia.go.id/id/index.php?option=com_content&task=view&id=112&Itemid=1722>.

² Doing Business 2015, *Going Beyond Efficiency – Economic Profile 2015: Indonesia – Comparing Business Regulations for Domestic Firms in 189 Economies*, A World Bank Group Flagship Report 12th Edition, 6 <<http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Profiles/Country/IDN.pdf>>.

³ Tim Lindsey (ed), *Indonesia: Law and Society*, (Federation Press, 2nded, 2008) 2.

⁴ Benny S. Tabaluyan, *The Indonesian legal system: An overview* (2002) Law and Technology resources for legal professionals <<http://www.llrx.com/features/indonesia.htm>>.

16th century to 1945); and post independence period divided into the Old Order (from 1945 to March 1966); the Soeharto New Order (March 1966 to 21 May 1998); and, post Soeharto or *Era Reformasi* [reformation era].⁵ All have impacted on the present economic, political and social situation of the country which affects corporate governance and related disclosure practices.

1.1.2. The 1997 financial crisis and its impact

Under the Soeharto New Order, Indonesia was recognised as a *Macan Asia* [Asian Tiger] with economic growth of 7 per cent each year.⁶ Economic activities, however, were dominated by cronyism,⁷ particularly around President Soeharto's family and associates. This period of economic growth ended in the Asian financial crisis of 1997. Indonesia suffered the most of all Asian countries. The economy and the corporate sector were significantly affected. Thousand of firms collapsed. Seventy percent of the companies listed on the Jakarta Stock Exchange became insolvent or bankrupt.⁸ Fifty seven companies or nearly 25 per cent reported a decline in equity of over 100 per cent with another 50 shrinking by 99 per cent.⁹ The people were not spared. The poverty rate increased significantly to 50 per cent of the population. The International Labour Organisation (ILO) classified two thirds of the population as very poor in 1999.¹⁰ Twenty million people were jobless, or more than 20 per cent of the workforce.¹¹

The intervention of the International Monetary Fund (IMF) failed to revive the economy. Its bailout of US\$45 billion resulted in mandated economic and legal reform

⁵ Lindsey (ed), *Indonesia: Law and Society*, above n 3, 3.

⁶ Azis Tomia, *Dua sisi yang berbeda; Soekarno dan Soeharto* [Two different sides; Soekarno and Soeharto] (2008)

<http://burukab.go.id/web/index.php?option=com_content&task=view&id=192&Itemid=93>.

⁷ Adisulistiyono, *Reformasi Hukum Ekonomi Indonesia* [Indonesia's Economic Law Reform]

<<http://adisulistiyono.staff.uns.ac.id/files/2009/07/reformasi-hukum-di-idnonesia.doc>>.

⁸ SEAsite Indonesia: Center for Southeast Asian studies, *Laporan Akhir Tahun Bidang Ekonomi – Krisis Ekonomi 1998, Tragedi tak terlupakan* [End of Year Economic Report – 1998 Economic Crisis, Unforgettable tragedy] (21 December 1998) Northern Illinois University, [13]

<http://www.seasite.niu.edu/indonesian/reformasi/krisis_ekonomi.htm>.

⁹ Chris Manning and Peter van Diermen (eds), *Indonesia in transition: Social aspect of reformasi and crisis* (Institute of Southeast Asian studies, 2000).

¹⁰ SEAsite Indonesia: Center for Southeast Asian studies, above n 8, [16].

¹¹ *Ibid* [14].

policies.¹² The country was pushed by it into a ‘rush to law’, including new corporate law and governance principles. This resulted in ineffective laws which were merely formal transplants of legal rules and institutions from other legal systems without consideration of the local context.¹³ Sixty seven laws and one *Perpu* [Interim law] were passed in less than two years under BJ Habibie,¹⁴ – Soeharto’s successor – in 1998-1999. These legal and institutional reforms still do not work effectively.

The financial crisis of 1997 extended into a social crisis and ultimately a political crisis.¹⁵ These resulted in a severe loss of confidence and public trust in political and commercial institutions. Poor corporate governance and a lack of transparency was claimed to be at the root of the crisis and included a former governor of *Bank Indonesia*, the central bank, Sabirin.¹⁶

1.1.3. Changes and challenges

The economic crisis fed into other issues produced by democratisation and the transition from the autocracy of Soeharto,¹⁷ which were changing society and politics in Indonesia. The removal of Soeharto weakened military control and strengthened non-governmental organisations, interest and community groups and led to the emergence of greater levels of democracy.¹⁸ Civil society and its institutions became stronger than at any time in the previous 30 years.¹⁹ The general election in 1999 led to Indonesia’s first democratic parliament and president under the 1945 Constitution. The economic recovery

¹² Lindsey (ed), *Indonesia: Law and Society*, above n 3.

¹³ Manning and van Diermen (eds), above n 9.

¹⁴ Lindsey (ed), above n 3, 12.

¹⁵ SEAsite Indonesia: Center for Southeast Asian studies, above n 8.

¹⁶ Syahrir Sabirin [former Governor of Bank Indonesia], ‘Upaya pemulihan ekonomi melalui strategi kebijakan moneter: Perbankan dan independensi Bank Indonesia’ [The effort for economic recovery through a strategy on monetary policy: Banking and independency of Central Bank] (A paper presented on National Seminar on: A strategy for economic recovery in the era of the new government, KAGAMA East Java and Association for Small Enterprises Development (PUPUK), Surabaya, 5 February 2000) <<http://www.bi.go.id/NR/rdonlyres/4F64F9EB-CAF1-4D93-920068EC99C83584/7887/gubfeb022000.pdf>>.

¹⁷ J A C Mackie in Manning and van Diermen, above n 9, xxiv.

¹⁸ Manning and van Diermen, above n 9.

¹⁹ *Ibid.*

progressed. Financial markets rebounded strongly and by the first half of 1999 international fund managers returned to investing in the country.²⁰

Almost 20 years after the Asian currency crisis, Indonesia's economic performance has improved but it still struggles with significant challenges. The World Bank's *2014 Doing Business Report* ranked Indonesia as 120 out of 189 countries for ease of doing business,²¹ reflecting a slight but persistent improvement over the 2009 report which had placed it 129 out of 183.²² The OECD's economic surveys of Indonesia also show social and economic progress between 2010 and 2015.²³ However, it also revealed in 2015 persistent low investment growth, heightened regulatory uncertainty and infrastructure bottlenecks.²⁴ The 2015 World Bank overview of Indonesia also pointed to regulatory uncertainties as a persistent issue deterring investment.²⁵ The financial markets reflect a capital inflow dominated by foreign short term capital. There is a persistent risk that a short term capital reversal and a number of other factors could lead to another financial crisis in Indonesia.²⁶

²⁰ Colin Johnson, 'the Indonesian economy in 1999: some comments' in Chris Manning and Peter van Diermen (eds), *Indonesia in transition: Social aspect of reformasi and crisis* (Institute of Southeast Asian studies, 2000) 5.

²¹ Doing Business 2014, *Understanding Regulations for Small and Medium-Size Enterprises – Comparing Business Regulations for Domestic Firms in 189 Economies*, a World Bank Group Flagship Report 3 <<http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB14-Full-Report.pdf>>.

²² Doing Business 2013, *Smarter Regulation for Small and Medium-Size Enterprises – Comparing business regulations for domestic firms in 185 economies*, a World Bank Group Flagship Report, 3 <<http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB13-full-report.pdf>>.

²³ Organization for Economic Co-operation & Development (OECD), *Economic survey of Indonesia* (2010) <http://www.oecd.org/document/60/0,3343,en_2649_34595_46261052_1_1_1_1,00.html>.

²⁴ Organization for Economic Co-operation & Development (OECD), *OECD Economic Surveys Indonesia March 2015: Overview*, 2 <<http://www.oecd.org/eo/surveys/Overview-Indonesia-2015.pdf>>.

²⁵ World Bank, *Indonesia Overview* (17 April 2015), [8] <<http://www.worldbank.org/en/country/indonesia/overview>>.

²⁶ Sunarsip, 'Mencegah krisis datang lagi' [Preventing a potential forthcoming crisis], *Republika* (online), 22 Mei 2007 <<http://www.ici.or.id/publicationfiles/Mencegah%20Krisis%20Ekonomi%20Datang%20Lagi.pdf>>.

An unethical and corrupt business environment, complicated bureaucracy and poor law enforcement continues.²⁷ A business survey in 2010 rated Indonesia as the most corrupt of the 16 major Asia-Pacific investment destinations. It scored 9.07 out of 10.²⁸ A 2013 KPMG report showed the continuing poor business environment. It identified weak infrastructure, excessive bureaucracy and a lack of coordination at ministerial levels as persistent factors.²⁹ Vriens & Partners confirmed this with its 2014 Asia Pacific Investment Climate Index ranking Indonesia 15th out of 20 with an overall score of 46.7 out of 100. It had been 11th in the 2012 survey.³⁰

While general elections in 2004, 2009 and 2014 produced democratic parliaments and presidents they have been unable to eradicate the corruption that continues to undermine integrity and honesty. This has had an ongoing negative impact on economic activities.

Political intervention in business and its regulation is also still significant. A number of examples demonstrate this. One involves Sri Mulyani, the former Finance Minister who is now a managing director of the World Bank. She had successfully led Indonesia's economy through the global financial crisis of 2007 with prudent fiscal policies and key reforms. Subsequently she faced growing pressures because of her integrity which resulted in her resignation in May 2010.³¹ A recent governor of Jakarta, Basuki Tjahaja Purnama – popularly known as Ahok – has faced political pressure and impeachment over his

²⁷ '10 tahun setelah ledakan krisis ekonomi itu' [Ten years after the explosive economic crisis], *Majalah Swa* (online), 24 Januari 2008 <<http://swa.co.id/2008/01/10-tahun-setelah-ledakan-krisis-ekonomi-itu/>>.

²⁸ 'Indonesia most corrupt of key Asian nation', *Reuters* (online), 8 March 2010 <<http://in.reuters.com/article/idINIndia-46740620100308>>.

²⁹ Siddharta & Widjaja, *Investing in Indonesia* (2013) KPMG - a global network of professional firms providing audit, tax and advisory services in 155 countries, 5 <<http://www.kpmg.com/Ca/en/External%20Documents/investing-in-indonesia-2013.pdf>>.

³⁰ Vriens & Partners, *Asia Pacific Investment Index* (2014), 5–6 <<http://www.vrienspartners.com/wp-content/uploads/2014/04/VP-Asia-Pacific-Investment-Climate-Index-2014.pdf>>.

³¹ Aloysius Unditu and Sandrine Rastello, 'Indonesia's Sri Mulyani given top world bank role', *Business Week* (online), 5 May 2010 <<http://www.businessweek.com/news/2010-05-05/indonesia-s-sri-mulyani-given-top-world-bank-role-update2-.html>>.

revelation of graft and the manipulation in the city council budget to benefit UPS [Uninterruptable Power Supply].³²

Another example in 2015 was the appointment of political figures to key positions that have been widely questioned. These included the son of President Jokowi's former advisor as a commissioner in the giant state owned telecommunications company. One state owned enterprise expert pointed out that the appointed commissioners may engage in fund raising for political parties.³³ The independence of *Bank Indonesia* has been questioned over an unexpected shift in its monetary policy to lower interest rates which it was claimed demonstrated political pressure on it.³⁴

These problems remain significant challenges, despite a successful general and presidential election in 2014. President Joko Widodo, popularly known as Jokowi, faces significant challenges in passing his highly anticipated programs through the Parliament. It is dominated by the opposition *koalisi merah putih* [red and white coalition]. Prabowo, the defeated presidential candidate, from a new and rising political party, Gerindra, also supported by the biggest and well established party, Golkar, has masterminded the opposition to Jokowi's programs. Jokowi is also restrained by his own political party and his cabinet ministers.³⁵ He is increasingly perceived as a weak leader who is unable to direct and control his own government. He has struggled to meet the high expectations of

³² Lenny Tristia Tambun and Yustinus Paat, 'Budget watchdog backs Ahok's claim of budget manipulation', *The Jakarta Globe* (online), 6 March 2015 <<http://thejakartaglobe.beritasatu.com/news/jakarta/budget-watchdog-backs-ahoks-claims-budget-manipulation/>>; Dewanti A Wardhani, 'Jakarta city council moves one step closer to impeaching Ahok', *The Jakarta Post* (online), 7 April 2015 <<http://www.thejakartapost.com/news/2015/04/07/jakarta-city-council-moves-one-step-closer-impeaching-ahok.html>>; Farouk Arnaz, 'Police question city councillor in UPS graft', *The Jakarta Globe* (online), 20 April 2015 <<http://thejakartaglobe.beritasatu.com/news/jakarta/police-question-city-councilor-ups-graft-case/>>.

³³ Khoirul Amin, 'Experts lash out at appointment of controversial figures', *The Jakarta Post* (online), 8 January 2015 <<http://www.thejakartapost.com/news/2015/01/08/experts-lash-out-appointment-controversial-figures.html>>.

³⁴ Satria Sambijantoro, 'Jokowi denies intervention in monetary policy', *The Jakarta Post* (online), 26 February 2015 <<http://www.thejakartapost.com/news/2015/02/26/jokowi-denies-intervention-monetary-policy.html>>.

³⁵ 'Politisi PDI-P: Menteri perempuan bidang ekonomi yang menjelekkan Jokowi' [A PDI-P politician: A female minister for economic affairs who discredited Jokowi], *Kompas* (online), 29 Juni 2015 <<http://nasional.kompas.com/read/2015/06/29/11060301/Politisi.PDI-P.Menteri.Perempuan.Bidang.Ekonomi.yang.Menjelekkan.Jokowi>>.

his election promises. The foreign and local media have exposed his weaknesses. His lack of political experience further exposes him to political pressure. He is seen to be under the control of his political patron and party leader, Megawati.³⁶

It is claimed that Jokowi's poor policies and management have led to a chaotic political atmosphere.³⁷ He has been forced to revoke some presidential regulations because of public outrage.³⁸ His failure to manage the complex and nuanced politics in POLRI

³⁶ It is reflected in her keynote speech at the 2015 party congress in Bali that described all party members including Jokowi, cabinet ministers and members of parliament as "*petugas partai*" [party officials]. Editorial, 'Jokowi's dilemma', *The Jakarta Post* (online), 14 April 2015 <<http://www.thejakartapost.com/news/2015/04/14/editorial-jokowi-s-dilemma.html>>. See also, Aulia Bintang Pratama, 'Megawati: Jika tidak mau disebut petugas partai, keluar!' [If a party member is not willing to be called as a party official, they will be dismissed as the member], *CNN Indonesia* (online), 11 April 2015 <<http://www.cnnindonesia.com/politik/20150411145447-32-45908/megawati-jika-tak-mau-disebut-petugas-partai-keluar/>>.

³⁷ Samrut Lellolesima, 'Menurut bawahan SBY, kebijakan Jokowi-Jk bikin kacau situasi politik Indonesia' [According to SBY's subordinates, Jokowi-Jk's policy has created a chaos for Indonesia's political situation], *RMOL* (online), 12 Maret 2015 <[http://politik.rmol.co/read/2015/03/12/195243/Menurut-Bawahan-SBY,-Kebijakan-Jokowi-JK-Bikin-Kacau-Situasi-Politik-Indonesia-;";](http://politik.rmol.co/read/2015/03/12/195243/Menurut-Bawahan-SBY,-Kebijakan-Jokowi-JK-Bikin-Kacau-Situasi-Politik-Indonesia-;)>; Michael Vatikiotis, *Jokowi: The first hundred days* (20 January 2015) Australian National University <<http://asiapacific.anu.edu.au/newmandala/201aaaaaaq5/01/20/jokowi-the-first-hundred-days/>>; 'Manajemen pemerintahan dan politik Jokowi amburadul' [The governmental and political management under Jokowi is a ravage], *Tribun* (online), 11 April 2015 <<http://www.tribunnews.com/nasional/2015/04/11/manajemen-pemerintahan-dan-politik-jokowi-amburadul>>;

'Bekali-kali revisi aturan, manajemen pemerintahan Jokowi amburadul' [The repetitive revision of regulations shows Jokowi's governmental management in a ravaged condition], *Kompas* (online), 5 Juli 2015 <<http://nasional.kompas.com/read/2015/07/05/10175921/Berkali-kali.Revisi.Aturan.Manajemen.Pemerintahan.Jokowi.Dinilai.Amburadul?page=all>>; 'Jokowi harus berhenti "error" saat mengeluarkan peraturan' [Jokowi should stop making mistakes when issued regulations], *Kompas* (online), 4 Juli 2015 <<http://nasional.kompas.com/read/2015/07/04/17040931/Jokowi.Harus.Berhenti.Error.saak.Keluarkan.Peraturan>>; 'Presiden harus pelajari aturan yang ia teken, jangan bilang lagi saya tidak baca' [President should fully understand the regulation signed, he should not say that he did not read the draft before signing it], *Tribun* (online), 5 Juli 2015 <<http://m.tribunnews.com/nasional/2015/07/05/presiden-harus-pelajari-aturan-yang-ia-teken-jangan-bilang-lagi-saya-tidak-baca>>; 'Bambang Soesatyo: Banyak human error di pemerintahan Jokowi' [Many human errors in Jokowi's government], *Kompas* (online), 6 July 2015 <http://nasional.kompas.com/read/2015/07/06/09343011/Bambang.Soesatyo.Banyak.Human.Error.di.Pemerintahan.Jokowi?utm_campaign=related&utm_medium=bp&utm_source=news&>.

³⁸ Nadya Natahadibrata and Ina Parlina, 'Policy flip-flops plague Jokowi', *The Jakarta Post* (online), 7 April 2015 <<http://www.thejakartapost.com/news/2015/04/07/policy-flip-flops-plague-jokowi.html>>. See also, 'Berkali-kali revisi aturan, manajemen pemerintahan Jokowi amburadul', above n 37. Other revoked presidential regulations were Perpres No.190/2014 tentang unit staf

[Indonesian National Police] is also considered to demonstrate his personal and political weaknesses.³⁹ Many questioned his commitment to fight graft when he nominated Budi Gunawan, a controversial former aide of his party leader, Megawati, and a graft suspect, as chief.⁴⁰ Budi Gunawan became deputy chief and the investigation of the graft allegation against him has been dropped.⁴¹ After the Corruption Eradication Commission (KPK) named him as a graft suspect, its commissioners – Abraham Samad (former chief commissioner) and Bambang Widjojanto (former deputy chief commissioner) – were placed under political pressure as a result of criminal allegations being levelled against them. Their lawyers revealed that political power and interference led to failed legal proceedings by Samad and Widjojanto to clear their names. They also indicated that a political ‘deal’ would lead to them finding ‘justice’.⁴²

kepresidenan; and Perpres No, 6/2015 tentang Badan Ekonomi Kreatif. Jokowi defended his controversial regulation concerning a rise in car-purchase allowances for senior officials and members of parliaments on the ground that he did not read the draft before signing it.

³⁹ Jacqui Baker, ‘Jokowi’s police go unpliced’ on East Asia Forum (4 May 2015) <<http://www.eastasiaforum.org/2015/05/04/jokowis-police-go-unpliced/>>; See also, Peter Harcher, ‘Indonesian president widodo under corrupt thumb of Megawati’, *The Sydney Morning Herald* (online), 28 April 2015 <<http://www.smh.com.au/comment/indonesian-president-widodo-under-corrupt-thumb-of-megawati-20150428-1muhkk.html>>.

⁴⁰ ‘Kronologi kasus Budi Gunawan dan ketegangan KPK-Polri’ [The chronology of Budi Gunawan’s case and a tension between the KPK and the National Police], *BBC Indonesia* (online), 16 Februari 2015 <http://www.bbc.com/indonesia/berita_indonesia/2015/02/150216_kronologi_bg_kpk>. See also, ‘Political pressure spurring Indonesian leader’s execution drive’, *Daily Mail Australia* (online), 30 April 2015 <<http://www.dailymail.co.uk/wires/afp/article-3062205/Political-pressure-spurring-Indonesian-leaders-execution-drive.html>>. See also, ‘Berkaca dari perkara BG, Polri dinilai tidak serius lakukan bersih-bersih’ [Mirroring Budi Gunawan’s case, the National Police is seen lacking in serious efforts to clean the institution from grafters], *Kompas* (online), 26 Mei 2015 <<http://nasional.kompas.com/read/2015/05/26/19232751/Berkaca.dari.Perkara.BG.Polri.Dinilai.Tidak.Serius.Lakukan.Bersih-bersih>>; ‘Jokowi criticized for lack of commitment to corruption eradication’, *Jakarta Post* (online), 18 October 2015 <<http://www.thejakartapost.com/news/2015/10/18/jokowi-criticized-lack-commitment-corruption-eradication.html>>

⁴¹ Haeril Halim, ‘Police drop probe into Budi Gunawan’, *The Jakarta Post* (online), 20 May 2015 <<http://www.thejakartapost.com/news/2015/05/20/police-drop-probe-budi-gunawan.html>>.

⁴² Edward Febriyatri Kusuma, ‘Jalan panjang mencari keadilan dari belenggu kriminalisasi’ [A long journey seeking justice for criminalisation restraint], *Detik* (online), 5 Juli 2015 <<http://news.detik.com/berita/2960822/jalan-panjang-mencari-keadilan-dari-belenggu-kriminalisasi/>>.

It is against this background since the economic crisis of 2007, that the Indonesian government and business sector have been further tested in improving corporate governance. This is in spite of good corporate governance being considered critical for reviving and improving the national economy. Effective disclosure practices for listed companies are an important part of this.

The political crisis of 1999 which ended Soeharto's presidency also ended the secretive arrangement between the controllers of listed companies and the government, which had prevailed under Soeharto. The more democratic and decentralised political environment has led to greater expectation of transparency in these companies.⁴³ This has seen a number of laws requiring improved disclosure passed. These include: Company Law No. 40 of 2007, Capital Market Law No. 8 of 1999, Company Registry Law No. 3 of 1982, and Government Regulation No. 64 of 1999 on Annual Financial Statements. This also applies to the rules of the *Otoritas Jasa Keuangan* [OJK] [Financial Services Authority] and the Indonesia Stock Exchange regulations for publicly listed companies. OJK was previously *Badan Pengawas Pasar Modal dan Lembaga Keuangan* [BAPEPAM-LK] and the Indonesia Stock Exchange [IDX] was previously the Jakarta Stock Exchange [JSX]. Indonesia's Code of Good Corporate Governance of 2006 also sets out standards for disclosure and transparency.⁴⁴

1.1.4. Evidence of poor corporate governance disclosure

Empirical studies indicate that compliance with respect to these disclosure requirements is particularly poor. They show that transparency and disclosure compliance with the reforms following the 1997 financial crisis are still unsatisfactory.⁴⁵ For example,

⁴³ Christian Chua, 'The Conglomerates in crisis: Indonesia 1997-1998' (2008) 13 (1) *Journal of the Asia Pacific Economy* 107.

⁴⁴ A copy of the Code in English version is available at European Corporate Governance Institute (ECGI), *Indonesia's Code of Good Corporate Governance* (http://www.ecgi.org/codes/documents/indonesia_cg_2006_en.pdf). Indonesian version is available at http://www.ecgi.org/codes/documents/indonesia_cg_2006_id.pdf.

⁴⁵ Demetra Arsalidou and Margaret Wang, 'The Challenges with Imposing the OECD Disclosure Requirements in East Asia' (2005) 16 *European Business Law Review*, 1477-99; See generally, 'Penerapan GCG masih lemah' [Implementation of GCG remained weak], *Majalah Swa* (online) edisi no.1/Tahun I/Agustus 2007, 40 <http://74.220.207.194/~iaigloba/storage/ref_14.pdf>.

a 2003 study of 31 listed banks showed that only 15 published annual reports and only 58.3 per cent disclosed information required to be disclosed by the rules of the Central Bank [*Bank Indonesia*].⁴⁶ A 2008 study of the 342 companies listed on the Jakarta Stock Exchange (JSX) found only 62 companies (18 per cent) disclosed goodwill in their financial statements.⁴⁷ Another 2008 study of 104 listed corporations revealed that only 41.9 per cent of items disclosed were adequately explained in the annual report.⁴⁸ One of the key findings in a 2010 Report on the Observance of Standards and Codes (ROSC) was that significant poor disclosure of ultimate ownership and control hindered the effectiveness of rules on conflicts of interests. It also identified the limited rights of shareholders to access other information from companies and the limited mandatory content in corporate governance statements.⁴⁹ This has been seen as a weakness ‘that may contribute to a country’s economic and financial vulnerability...’.⁵⁰ It is also seen as requiring an improvement in the regulatory framework for the disclosure of beneficial ownership and control.⁵¹

A number of recent local studies on the level of disclosure compliance demonstrate that it remains unsatisfactory. Low compliance levels with mandatory disclosure requirements have been identified. This can be seen from the below table.

⁴⁶ S Utama, *Corporate Governance, Disclosure and its Evidence in Indonesia* (2003) Universitas Indonesia [University of Indonesia] <<http://www.digilib.ui.ac.id/file?file=digital/114267-MUIN-XXXII-05-Mei2003-11.pdf>>.

⁴⁷ E T Wahyuni and H Natasha, ‘The Evidence of Goodwill Disclosure at Indonesia Listed Company and Goodwill Relationship with Future Earnings’ (2008) 3(2) *Jurnal Reviu Akuntansi dan Keuangan* [Journal of Accountancy and Finance Review], Abstract <<http://ejournal.umm.ac.id/index.php/jrak/article/view/2109/2263>>.

⁴⁸ Utama, above n 46.

⁴⁹ World Bank, ‘Report on the Observance of Standards and Codes (ROSC) – Corporate governance country assessment Indonesia’, 2 (*ROSC – Indonesia*) <http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2012/05/30/000333037_20120530000907/Rendered/PDF/691570ESW0ROSC0overnance0April02010.pdf>.

⁵⁰ F Jurdant, ‘Disclosure of beneficial ownership and control in Indonesia: Legislative and regulatory policy options for sustainable capital markets’ (OECD Corporate Governance Working Papers, No. 9, OECD Publishing 2013) 4 <<http://www.oecd-ilibrary.org/docserver/download/5k43m4pdrj36.pdf?expires=1437375352&id=id&accname=guest&checksum=8DECB9D9C10E70727451CCB7A3D09EC2>>.

⁵¹ *Ibid.*

Table 1.1: Local studies on the level of compliance of disclosure in Indonesia

Researchers	Findings (the level of compliance in percentage figures)	Number of companies studied	Year of the study	Factors influencing compliance
Pitasari and Septiany ⁵²	50.61 per cent	40 service companies	2014	Number of audit committee and their frequency meetings
Meiflowerina et al ⁵³	70.6 per cent	Listed SOEs	2014	The number on board of commissioners and audit committees
Prawinandi et al ⁵⁴	69.90 per cent			The proportion of independent commissioners and audit committee members
Supriyono et al ⁵⁵	75.92 per cent	Banking's		The number on board of

⁵² Anggita Pitasari and Aditya Septiani, 'Analisis pengaruh struktur corporate governance terhadap tingkat kepatuhan pengungkapan konvergensi IFRS pada laporan laba rugi komprehensif' [An analysis of the influence of corporate governance structure on the level of compliance to disclosure, IFRS convergence on comprehensive reports of loss and profit] *Diponegoro Journal of Accounting* (2014) 03(02) 1, 1, 7 <<http://ejournal-s1.undip.ac.id/index.php/accounting/article/viewFile/6093/5880>>. The study was based on International Financial Reporting Standards (IFRS).

⁵³ Yeasy Darmayanti Meiflowerina and Posi Fauziati, 'Peran corporate governance terhadap tingkat kepatuhan mandatory disclosure konvergensi IFRS pada badan usaha milik Negara (BUMN) yang terdaftar di bursa' [The role of corporate governance on the level of compliance to mandatory disclosure, IFRS convergence on listed state-owned enterprises (SOEs) (2014) 4(1) *ejurnal Universitas Bung Hatta* 1 1 <<http://ejurnal.bunghatta.ac.id/index.php?journal=JFEK&page=article&op=view&path%5B%5D=2447>>.

⁵⁴ Wardani Prawinandi, Djoko Suhardjanto and Hanung Triatmoko, *Peran struktur corporate governance dalam tingkat kepatuhan mandatory disclosure konvergensi IFRS* [The role of corporate governance structure on the level of compliance to mandatory disclosure, IFRS convergence] (2014) Akuntansi Publik Universitas Trunojoyo Madura, 1 <<http://asp.trunojoyo.ac.id/wp-content/uploads/2014/03/067-CG-21.pdf>>. The compliance level was influenced by the proportion of independent commissioners and the number of audit committee.

⁵⁵ Eddy Supriyono, Achmad Abdual Mustaqim and Djoko Suhardjanto, *Pengaruh corporate governance terhadap tingkat kepatuhan mandatory disclosure konvergensi IFRS di Indonesia* [The influence of corporate governance structure on the level of compliance to mandatory disclosure, IFRS convergence in Indonesia] (September 2014) Universitas Brawijaya, 1 <<http://multiparadigma.lecture.ub.ac.id/files/2014/09/138.pdf>>. The study was based on IFRS. The number of board commissioners, audit committee size and the number of audit committee meetings affected the level of compliance.

		enterprises		commissioners; audit committees and the frequency of meetings
Sari Wulan ⁵⁶	73.65 per cent	106 listed banking companies	2009–2012	The frequency of audit committee meetings
Maysaroh ⁵⁷	N/A	144 listed manufacturing companies	2009–2012	Institutional ownership and frequency of audit committee meetings
Utami et al ⁵⁸	72.203 per cent			N/A
Trimuharni ⁵⁹	58.11 per cent (based on accounting standards) 60.28 per cent (based on Bapepam rules)	100 listed companies	2010	The number on board of commissioners and audit committees

These studies indicate that there is a need to increase disclosure compliance.

⁵⁶ Sari Wulan, *Pengaruh mekanisme corporate governance terhadap disclosure – Studi terhadap perusahaan perbankan yang terdaftar di bursa efek Indonesia tahun 2009–2012* [The influence of of corporate governance mechanisms on disclosure – A study of listed banks in the Indonesia Stock Exchange in 2009–2012] (Skripsi, Fakultas Ekonomika dan Bisnis Universitas Kristen SatyaWacana Salatiga, 2013) iv, v <http://repository.library.uksw.edu/jspui/bitstream/123456789/3710/2/T1_232009055_Full%20text.pdf>.

⁵⁷ Nurlaila Maysaroh C, *Pengaruh corporate governance terhadap tingkat kepatuhan mandatory disclosure konvergensi IFRS* [The influence of corporate governance on the level of compliance to mandatory disclosure, IFRS convergence] (Thesis, Universitas Gadjah Mada, 2014) iv, v <http://etd.ugm.ac.id/index.php?mod=penelitian_detail&sub=PenelitianDetail&act=view&typ=html&buku_id=71468&is_local=1>.

⁵⁸ Wulan Dwi Utami, Djoko Suhardjanto and Sri Hartoko, *Investigasi dalam konvergensi IFRS di Indonesia: Tingkat kepatuhan pengungkapan wajib dan kaitannya dengan mekanisme corporate governance* [An investigation of IFRS convergence in Indonesia: the level of compliance to mandatory disclosure and its relation with corporate governance mechanism] (2012) University of Indonesia Faculty of Economy, Central Data for Economy and Business), [3] <<http://pdeb.fe.ui.ac.id/?p=6374>>. The study based on IFRS

⁵⁹ Rini Trimuharni, *Pengaruh karakteristik perusahaan terhadap kepatuhan pengungkapan wajib dalam laporan keuangan perusahaan di bursa efek Indonesia (BEI)* [The influence of company's characteristic on compliance to mandatory disclosure in financial reports for Indonesia Stock Exchange] (Skripsi, Universitas Sebelas Maret Surakarta, 2010) 15, 84 <<http://core.kmi.open.ac.uk/download/pdf/12348657.pdf>>.

Compared with Malaysia and Thailand, Indonesia's performance on disclosure is poor in a region where the quality of disclosure is already low.⁶⁰ A number of other studies also show persistent poor disclosure especially in timeliness and reliability. A survey in 1999 by PricewaterhouseCoopers demonstrated poor performance around corporate disclosure including untrue and misleading information in financial statements, a lack of disclosure of material information in a timely manner and disclosure of price sensitive information during meetings with major investors.⁶¹ The 2012 report of Asian Corporate Governance Association (ACGA)⁶² and 2013-2014 report of the Asian Development Bank (ADB)⁶³ indicate that these issues continue and now include ownership and remuneration of members of the boards. It also shows investors' 'growing concerns about the reliability of financial statements and, at the extreme, outright fraud'.⁶⁴ Former BAPEPAM officials, Surya and Yustiavandana, admitted that financial reports were so easily manipulated that they could not be an integral indicator of a company's performance.⁶⁵

Some significant cases reflect this concern with fraud. In 2010 PT Antaboga Tbk; PT Prima Matahari Utama Tbk; Bakri Group; and PT Katarina Utama Tbk issued untrue,

⁶⁰ Stijn Claessens and Joseph P H Fan, 'Corporate Governance in Asia: A Survey' (2002) 3 *International Review of Finance* 71, 78.

⁶¹ Etty R Wulandari and Asheq R Rahman, 'Political patronage, cross-holding and corporate governance in Indonesia' in Ferdinand A Gul and Judy S L Tsui, *The Governance of East Asian Corporations: Post-Asian Financial crisis* (Palgrave Macmillan, 2004) 83.

⁶² CLSA Asia-Pacific Markets, CG Watch 2012 – Corporate Governance in Asia, *Tremors and cracks: Governance issues resurface* (10 September 2012) Asian Corporate Governance association (ACGA), 3, 103-11 <http://www.acga-asia.org/loadfile.cfm?SITE_FILE_ID=658>. Lack of access to full 2014 ACGA watch report; See also, CLSA Asia' Independent Voice, *Corporate governance watch 2012 – Cracks in Asian corporate governance reappear in recent years* (19 September 2012), [3] <<https://www.clsa.com/about-clsa/media-centre/2012-media-releases/corporate-governance-watch-2012cracks-in-asian-corporate-governance-reappear-in-recent-years.php>>.

⁶³ Asian Development Bank, *ASEAN Corporate Governance Scorecard – Country Reports and Assessments 2013-2014*, 5 <http://www.theacmf.org/ACMF/upload/adbcg2014_7th.pdf>.

⁶⁴ CLSA Asia-Pacific Markets, CG Watch 2012, above n 62.

⁶⁵ Indra Surya and Ivan Yustiavandana, *Penerapan good corporate governance – Mengesampingkan hak-hak istimewa demi kelangsungan usaha* [The implementation of good corporate governance – Overriding privileged rights to achieve the continuity of a business] (Prenada Media Group, 1st ed, 2nd printed, 2008). The authors were officials of Bapepam and PPTK. The quote is originally in Bahasa Indonesia saying as follows: 'Permasalahannya, laporan keuangan sangat mudah untuk direkayasa dan tidak mampu menggambarkan kinerja suatu perusahaan secara utuh.'

misleading and manipulated financial reports. PT Katarina Utama Tbk disclosed manipulated data in its financial report. The company also concealed the misuse of funds raised during its initial public offering [IPO].⁶⁶ Some capital market observers claim that BAPEPAM had not appropriately handled these cases as similar incidents appear to have increased. Among others, Yanuar Rizky regretted that BAPEPAM had not taken decisive action in the PT Katarina Utama case. However that company's directors were residing outside Indonesia.⁶⁷

Improved corporate governance practices in Indonesia have been identified as a more critical issue in its economic development than in other South East Asian countries due to its lack of effective corporate control mechanisms, other inefficiencies and corruption.⁶⁸ Numerous studies over an increasing period of time demonstrate the persistency of these issues. A study in 2005 on investor perception of corporate governance practices gave Indonesia the lowest score.⁶⁹ CG Watch, a joint report by ACGA and CLSA Asia-Pacific Markets on corporate governance in Asia, also demonstrates this poor performance. It awarded Indonesia the lowest score of 40 in 2004, and 37 in 2005 and again 2007.⁷⁰ Enforcement scored 22, and corporate governance culture scored 25, mainly contributing to the very poor overall scores in 2007.⁷¹ Another study in 2008 demonstrated

⁶⁶ 'BAPEPAM: Jangan menuduh macam-macam' [Don't accuse], *Antara News* (online), 7 October 2010 <<http://www.antaranews.com/berita/1286441974/bapepam-jangan-menuduh-macam-macam>>.

⁶⁷ Panin sekuritas, *Pengamat: BAPEPAM terlalu lamban tangani kasus Katarina* [Observer: BAPEPAM was too slow tackling Katarina's case] <<http://www.pans.co.id/?page=berita&id=SU5GLTIwMTAxMDA2MTc0NjQxLnhtbA==>>.

⁶⁸ Thomas S Kaihatu, *Good Corporate Governance dan Penerapannya di Indonesia* [Good corporate governance and its implementation in Indonesia], Faculty of Economy University of Kristen Petra Surabaya <<http://puslit2.petra.ac.id/gudangpaper/files/1957.pdf>>.

⁶⁹ Sang-Woo Nam and Il Chong Nam, Asian Development Bank Institute, *Corporate Governance in Asia: Recent Evidence from Indonesia, Republic of Korea, Malaysia, and Thailand* (2005) <<http://www.adbi.org/book/2005/02/02/884.corporate.governance.asia/>>.

⁷⁰ Jamie Allen, 'Indonesia's corporate governance standing' (Asian Corporate Governance Association (ACGA) paper at KNKG & RSM AAJ Conference, Bali, 13 May 2010) 8 <http://www.acga-asia.org/public/files/ACGA_Presentation_KNKG_Conference_May2010.pdf>. Jamie Allen is a Secretary General of Hong Kong.

⁷¹ CLSA Asia-Pacific Markets, CG Watch 2007 – Corporate Governance in Asia, *On a wing and a prayer: The greening of governance*, 88 <https://www.clsa.com/assets/files/reports/CLSA_ACGA_CGWatch2007_Extract-2.pdf>.

that Indonesia had the lowest good corporate governance index for East and South East Asian countries at 2.88, compared to Malaysia's 7.72, Singapore's 8.93 and Japan's 9.17.⁷² More recent scores are similar. An ACGA survey in 2012 awarded Indonesia the lowest scores in all categories with a total score of 37. Corporate governance rules and practices were scored 35, enforcement 22, political and regulatory conditions 33, and corporate governance culture 33.⁷³ In 2014, Indonesia was still in last place along with the Philippines with a total score of 39.⁷⁴ The ADB assessment of ASEAN corporate governance in 2013–2014 supports these ratings, stating that Indonesia's performance 'is still considered to be below an acceptable level.'⁷⁵ The ADB gave it the second lowest score for other ASEAN countries after Vietnam with 43.29 in 2012 and 54.55 in 2013. By comparison Thailand achieved a score of 67 in 2012 and 75.39 in 2013, followed by Malaysia with 62.29 and 71.69, Singapore with 55.67 and 71.68 and the Philippines with 48.90 and 57.99.⁷⁶

Poor disclosure was the main factor contributing to Indonesia's low scores. They included: the quality of the financial and non-financial reports, the timeliness of disclosure of substantial ownership stakes and of directors' and commissioner's share dealings, the disclosure of detail of issues on agendas for AGMs and methods of counting votes, disclosure of executive compensation and the effectiveness of controls over insider trading.⁷⁷

CG Watch 2007 category scores for Indonesia scored 39 for corporate governance rules & practices; 22 for enforcement; 35 for political/regulatory; 65 for adoption of international accounting/auditing standards; 25 for corporate governance culture. Total score was 37.

⁷² S A Djalil, *Good Corporate Governance* (2008) <<http://www.knkg>>.

⁷³ Asian Corporate Governance Association (ACGA), *CG Watch 2012: Market rankings* (September 2012), 4, 8 <http://www.acga-asia.org/public/files/CG_Watch_2012_ACGA_Market_Rankings.pdf>.

⁷⁴ Jamie Allen, *CG Watch 2014 – Market rankings* (2014) Asian Corporate Governance Association (ACGA), 2,3 <http://www.acga-asia.org/public/files/CG_Watch_2014_Key_Charts_Extract.pdf>.

⁷⁵ Asian Development Bank, above n 63, 24.

⁷⁶ Ibid 5.

⁷⁷ Ibid 13.

1.1.5. Factors hindering better corporate governance disclosure

The ACGA report in 2014 acknowledged the aspirations for better corporate governance reforms in Indonesia, but questioned their achievement.⁷⁸ The weak judicial system and weak enforcement, corruption and poor business and regulatory cultures were identified as the main factors hindering reform. These factors had also been identified in the 2012 report.⁷⁹ The 2012 report referred specifically to the lack of enforcement of corporate and securities law, the inadequacy of rules to prevent insider trading and market manipulation and the unrevised good corporate governance code.⁸⁰ Indonesia, it was noted, has declined for a number of years to sign the 2002 Multilateral Memorandum of Understanding concerning Consultation and Cooperation and the Exchange of Information of the International Organization of Securities Commission [IOSCO] reference. The unrevised Code of Good Corporate Governance of 2006 was also pointed as demonstrating the half-hearted efforts of government.⁸¹ The report concluded that ‘corporate governance reforms have stalled’.⁸²

The 2014 report indicated the increased politicization of domestic business issues and a weak legal system were hindering the reforms.⁸³ It identified the need for significance of political will, regulatory resources improvement, and having the right people in the right place.⁸⁴

With particular respect to the low level of disclosure, a number of persistent factors were identified, although there has been significant improvement with rules and standards so that they are closer to international norms. They included weak enforcement, limited private enforcement, feeble political and regulatory institutions, pervasive corruption, and a weak culture of governance in listed companies with the exception of some blue chips.⁸⁵

⁷⁸ Allen, CG Watch 2014, above n 74.

⁷⁹ CLSA Asia-Pacific Markets, CG Watch 2012, above n 62, 105.

⁸⁰ Ibid 103.

⁸¹ Ibid 105.

⁸² Ibid 103.

⁸³ Allen, CG Watch 2014, above n 74.

⁸⁴ Ibid.

⁸⁵ CLSA Asia-Pacific Market, CG Watch 2012, above n 62, 103–11.

Of these factors, the lack of enforcement, corruption, and the unethical business and regulatory culture are three fundamental elements that have long been regarded as impeding the Indonesian legal and regulatory systems. These are further discussed below.

1.1.5.1. Lack of enforcement

The lack of enforcement of the law has been identified as a significant problem. This is based on claims that the implementation of good corporate governance depends on effective law enforcement.⁸⁶ It is claimed to be a principal cause of the low level of implementation of good corporate governance. It is linked with a relationship-based business culture, and its lack of transparency.⁸⁷ Daniri has also made similar claims around lack of law enforcement and related them to the core problems of the absence of business ethics and morality.⁸⁸ It is generally recognised that there is a significant relationship between three contributing factors - *korupsi, kolusi dan nepotism* known as KKN [corruption, collusion and nepotism] and the lack of enforcement. Corruption is considered to be the most crucial factor.

1.1.5.2. Corruption

Corruption in Indonesia is both pervasive and deeply entrenched. There is significant and frequent evidence of this. Consequently it is a theme often referred to in this thesis and its impact significantly informs the conclusion.

(a) Pervasive corruption

⁸⁶ Indonesia Corruption Watch (ICW), *Penegakan hukum jadi prasyarat pemerintahan* [Law enforcement is a prerequisite for the government] (6 Mei 2010) [1] <<http://www.antikorupsi.org/id/content/penegakan-hukum-jadi-prasyarat-pemerintahan>>.

⁸⁷ Djohari Santosa, 'Kegagalan penerapan good corporate governance pada perusahaan public di Indonesia' [The failure of good corporate governance implementation in Indonesian public companies] *Jurnal Hukum* [Law Journal] (2008) 2(15) 182, 196 <<http://journal.uui.ac.id/index.php/jurnal-fakultas-hukum/article/viewFile/64/1844>>.

⁸⁸ Mas Achmad Daniri, 'Kiat berbisnis tanpa suap dan korupsi' [Tips for business without bribes and corruption] (Paper presented at the 4th Indonesia Anti-Corruption Forum, Jakarta, 10–12 Juni 2014) 4 <http://acch.kpk.go.id/documents/10157/1251583/Kiat+Berbisnis+Tanpa+Suap+dan+Korupsi_Mas+Achmad+Daniri.pdf>.

Corruption, collusion, and nepotism (KKN) occur in all parts of Indonesian life including the corporate economy and financial sectors⁸⁹ and in the political and legal systems.⁹⁰ A 2010 survey showed that corruption was extensive and that political issues have become the main obstacle to fighting it.⁹¹

Corruption had been previously claimed as the fundamental problem in government and governance as well as business.⁹² Worang in 2013 indicated how these areas are joined by pervasive KKN practices in Indonesian State Owned Enterprises [SOEs]. Boards of directors and boards of commissioners ‘were not properly implementing good corporate governance (GCG) practices’.⁹³ The interference by government including by politicians associated with the party in government was identified as a major factor. The SOEs have been described as “cash cows” or “automatic teller machines” for the governing party as the major shareholder.⁹⁴

Transparency International identified the legal system and courts as so corrupt that they generate significant uncertainty for business. The US Department of State in 2008 described Indonesia’s regulatory system as complex, resulting in foreign and domestic companies avoiding its justice system.⁹⁵ Green advised that the haphazardly

⁸⁹ Rajeswary Ampalavanar Brown, ‘Indonesian Corporations, Cronyism and Corruption’ (2006) 40 *Modern Asian Studies*, 953-992. See also, Nasution, ‘Kasus Bibit-Chandra adalah puncak es’, *Kompas* (online), 16 November 2009 <www.kompas.com>.

⁹⁰ Business Anti-Corruption Portal, *Indonesia show all – Business Corruption in Indonesia* <<http://www.business-anti-corruption.com/country-profiles/east-asia-the-pacific/indonesia/show-all.aspx>>.

⁹¹ ‘Indonesia most corrupt of key Asian nations’, above n 28; ‘PERC: Indonesia negara paling korup’ [PERC: Indonesia is the most corrupt nation], *Kompas* (online), 8 Maret 2010 <www.kompas.com>.

⁹² World Bank, *Corruption and Governance* <<http://lnweb90.worldbank.org/eca/eca.nsf/Sectors/ECSPE/E9AC26BAE82D37D685256A940073F4E9?OpenDocument>>.

⁹³ Frederik Gerard Worang, *A qualitative analysis of corporate governance in Indonesian state-owned enterprises: An internal stakeholders perspective* (PhD thesis, School of Management and Governance Murdoch University, 2013) iii <<http://researchrepository.murdoch.edu.au/22522/2/02Whole.pdf>>.

⁹⁴ *Ibid.*

⁹⁵ Business Anti-Corruption Portal, *Indonesia country profile* (2009) <<http://www.business-anti-corruption.com/country-profiles/east-asia-the-pacific/indonesia/snapshot/>>.

implementation of laws and actual corruption create an unfriendly business environment in Indonesia.⁹⁶

(b) Entrenched corruption

Corruption in Indonesia is deeply entrenched. Bribery, abuse of office and money laundering are common.⁹⁷ Law No. 17 of 2007, concerning the Indonesian Long-term National Plan 2005–2025 in Part G, clearly acknowledged this persistent misuse of power by authorities.⁹⁸ There is widespread non-compliance with the Anti-Corruption Law. There are many reported corruption cases across all Indonesian regions. Breaches of the law are generally settled by negotiation including bribery and any formal legal processes are avoided.⁹⁹

Daniri, KNKG chairman, highlighted corruption and bribery as a common practice by repeating a common statement *tanpa suap bisnis tidak akan berjalan* [business will not run without bribes] or [bribes are needed to keep business in existence].¹⁰⁰ Hehamahua, a former KPK advisor, states that many officials have made corruption a business. This creates a wider perception that corruption is a promising business opportunity.¹⁰¹ Cultural beliefs and practices, and economic and political interests are major contributing factors to its pervasiveness.

The efforts to eradicate corruption are still to see any significant achievements. Law No.30 of 2002 on the Corruption Eradication Commission created the Commission for the

⁹⁶ Keith Green, *Decentralization and good governance: The case of Indonesia* (28 February 2005) 9 <https://mpira.ub.unimuenchen.de/18097/1/Decentralization_and_Good_GovernanceThe_Case_of_Indonesia.pdf>. Indonesia was classified as one of the worst countries to grow a business. See, Business Insider Australia, *The 10 Worst Countries To Grow A Business* (25 October 2012) <<http://www.businessinsider.com.au/worst-business-environments-2012-10?r=US&IR=T>>.

⁹⁷ Business Anti-Corruption Portal, *Indonesia country profile: Business corruption in Indonesia* (April 2014) <<http://www.business-anti-corruption.com/country-profiles/east-asia-the-pacific/indonesia/information-network.aspx>>.

⁹⁸ 'Indonesia still one of the most corrupt', *Tempo.Co* (online), 7 December 2012 <<http://en.tempo.co/read/news/2012/12/07/055446641/Indonesia-still-one-of-the-Most-Corrupt>>.

⁹⁹ Ibid.

¹⁰⁰ Daniri, 'Kiat berbisnis tanpa suap dan korupsi', above n 88, 2.

¹⁰¹ 'Korupsi itu peluang bisnis yang menjanjikan' [Corruption is a promising business opportunity], *Kompas* (online), 7 Juli 2015 <<http://nasional.kompas.com/read/2015/07/07/16201861/.Korupsi.Itu.Peluang.Bisnis.yang.Menjanjikan.>>.

Eradication of Corruption (KPK). The Commission has been undermined and compromised. The law may be further undermined by bringing forward again the changes proposed to it in 2009.¹⁰² The parliament elected in 2014 still proposes the changes before it.¹⁰³ They include scrapping the KPK's powers to bring prosecutions and to authorise wiretapping.¹⁰⁴ In 2015, the recent efforts to scrap the KPK's power continued in proposing a revision of the scope of the KPK limiting its activities to prevention and as an assistant to other legal enforcement agencies in graft cases.¹⁰⁵ The agencies it would be assisting, as indicated earlier, are regarded as corrupt. These persistent attempts to limit the powers of KPK evidence the depth and strength of corruption in Indonesia. The progress made in fighting corruption has largely been through the efforts of the KPK. In early 2016 the effort to weaken the KPK's power continues.¹⁰⁶ This is supported by other evidence.

In late 2009 and early 2010 the media exposed attempts to dismiss senior members of the KPK. The former chief of the KPK, Antasari Azhar, was accused of being involved

¹⁰² 'Pengamat: Revisi UU buktikan kerja KPK usik oknum DPR' [Observer: Revision of the Law proves the performance of KPK disturbing corrupt parliament members], *Republika* (online), 28 September 2012 <<http://www.republika.co.id/berita/nasional/umum/12/09/28/mb2h68-pengamat-revisi-uu-buktikan-kerja-kpk-usik-oknum-dpr>>.

¹⁰³ 'Pimpinan KPK: Kenapa revisi UU KPK terlalu dipaksakan DPR?' [KPK Deputy: Why the Law of KPK has been forced to be revised by DPR (parliament)?], *Kompas* (online), 26 June 2015 <<http://nasional.kompas.com/read/2015/06/26/12224191/Pimpinan.KPK.Kenapa.Revisi.UU.KPK.Terlalu.Dipaksakan.DPR>>. See also, 'Jaksa KPK: Disadap saja tidak mengaku, apalagi tanpa penyadapan' [KPK Prosecutor: Even there are wiretappings, they have denied, altogether without wiretapping is all denials], *Kompas* (online), 29 June 2015 <<http://nasional.kompas.com/read/2015/06/29/22035821/Jaksa.KPK.Disadap.Saja.Tidak.Mengaku.apalagi.Tanpa.Penyadapan>>.

¹⁰⁴ Readers Forum, 'Text your say: KPK to be rendered toothless', *The Jakarta Post* (online), 23 June 2015 <<http://www.thejakartapost.com/news/2015/06/23/text-your-say-kpk-be-rendered-toothless.html>>.

¹⁰⁵ Aghnia Adzkie, 'Sebelas poin pelemahan KPK versi aktivis dalam revisi UU' [Eleven points of the revision of the Law to weaken the KPK's power, according to activists in response to a new Bill], *CNN Indonesia* (online), 9 October 2015 <<http://www.cnnindonesia.com/nasional/20151008155935-12-83765/sebelas-poin-pelemahan-kpk-versi-aktivis-dalam-revisi-uu/>>; Aghnia Adzkie, 'Revisi UU DPR buat KPK tergantung polisi dan jaksa' [Revision of the Law, DPR makes KPK depending on police and prosecutors], *CNN Indonesia* (online), 8 October 2015 <<http://www.cnnindonesia.com/politik/20151007140417-32-83429/revisi-uu-dpr-buat-kpk-tergantung-polisi-dan-jaksa/>>.

¹⁰⁶ 'Pengamat: Revisi UU KPK, Gerakan Besar Pelumpuhan' [Observer: Revision of the Law of the KPK is a significant movement to paralyse the KPK], *Kompas* (online), 8 February 2016 <<http://nasional.kompas.com/read/2016/02/08/12323171/Pengamat.Revisi.UU.KPK.Gerakan.Besar.Pelumpuhan>>.

in a murder and could face the death penalty.¹⁰⁷ The deputy chairs of the KPK, Bibit Samad Rianto and Chandra Hamzah, had also been charged with alleged bribery, extortion and misuse of authority.¹⁰⁸ After being charged, they were released as the police and prosecutors could not find evidence to support the charges.¹⁰⁹ There is widespread opinion that the cases are fabricated and intended to deter them and others from any efforts to eradicate corruption. The cases reflect the uncertainties in the legal system in Indonesia.¹¹⁰

These attempts to remove senior anti-corruption fighters are known locally as *kriminalisasi* [criminalisation]. It still continues under Jokowi's government although the media has now exposed that the earlier criminal allegations against the senior KPK leaders were engineered by police.¹¹¹ However, prosecution on the KPK continued. In mid 2015 Abraham Samad was dismissed as chair of the KPK because of an accusation of misuse of power and falsifying documents for a passport.¹¹² Bambang Widjojanto, a deputy chair of

¹⁰⁷ 'Indonesian graft fighter charged with murder', *International News* (online), 2 February 2010 <www.thenews.com.pk/updates.asp?id=884777>. He was convicted in 2010 and sentenced to 18 year imprisonment. His appeal has been dismissed. The allegation related to the murder of a businessman who was a director of a state-owned pharmaceutical firm. It was alleged that Azhar was being blackmailed by the businessman over an affair with a female golf caddy. Azhar drew public attention in 2000 as chief of the South district's Prosecutor Office. He was responsible for taking Tommy Soeharto to prison. Soeharto escaped leading to allegation that Antasari was involved in the escape.

¹⁰⁸ 'Kasus Bibit-Chandra adalah Puncak Gunung Es', [Bibit-Chandra's case is a peak of ice mountain], *Kompas* (online), 16 November 2009 <<http://nasional.kompas.com/read/2009/11/16/14514974/Kasus.BibitChandra.adalah.Puncak.Gunung.Es.>>.

¹⁰⁹ 'Police Admit They Have No Recordings in Bibit and Chandra Case', *The Jakarta Globe* (online), 29 October 2010 <<http://jakartaglobe.beritasatu.com/archive/police-admit-they-have-no-recordings-in-bibit-and-chandra-case/>>.

¹¹⁰ Indonesia Corruption Watch, *KPK Pegang Bukti Rekam Kasus Bibit-Chandra* [KPK hold evidence that Bibit-Chandra's case was engineered] (2009) <<http://www.antikorupsi.org/id/content/kpk-pegang-bukti-rekam-kasus-bibit-chandra>>; Hukumonline, *Rekam Kriminalisasi Bibit-Chandra Benar-Benar Terkuak* (4 November 2009) <<http://www.hukumonline.com/berita/baca/lt4af1190c0d87d/rekam-kriminalisasi-bibitchandra-benarbenar-terkuak>>.

¹¹¹ Fedina S Sundaryani and Hans Nicholas Jong, 'Jokowi offers no help to KPK', *The Jakarta Post* (online), 25 January 2015 <<http://www.thejakartapost.com/news/2015/01/25/jokowi-offers-no-help-kpk.html>>.

¹¹² 'Tiba di Bareskrim, Samad merasa kasusnya direkam' [Arrives in criminal investigation agency, Samad believes that his alleged criminal case has been engineered], *Metro TV News*, 24 June 2015 <<http://video.metrotvnews.com/play/2015/06/24/407250/tiba-di-bareskrim-samad-merasa-kasusnya-direkam>>; See also, Fabian Januarius Kuwado, 'Anggap kasusnya direkam,

the KPK, was accused of perjury in an election dispute in 2010 in which he acted as a lawyer. Other KPK deputy chairs were also under pressure with different accusations levelled at them. Adnan Pandu Praja has been accused of illegally obtaining shares and forging notarial certificates as a lawyer in 2006 and Zulkarnaen of corruption in 2008.¹¹³ These accusations were made after the then police chief candidate Budi Gunawan was named as a graft suspect by the KPK.¹¹⁴ Widjojanto was arrested but the arrest was challenged as POLRI had breached the Criminal Law Procedures Code (KUHAP).¹¹⁵

The entrenchment of corruption is also shown by surveys that persistently reveal Indonesia as one of the most corrupt countries in the region and very corrupt by international standards.¹¹⁶ The global corruption barometer in 2009 scored Indonesia at 3.7 which indicates that it is extremely corrupt and more corrupt than India 3.5, Malaysia 3.4,

Abraham Samad tetap penuhi panggilan polisi' [Abraham Samad fulfils police probe inquiry despite a belief that the case was an engineered criminal case], *Kompas* (online), 24 June 2015 <<http://nasional.kompas.com/read/2015/06/24/10572631/Anggap.Kasusnya.Direkayasa.Abraham.Samad.Tetap.Penuhi.Panggilan.Polisi>>.

¹¹³ 'Kronologi kasus Budi Gunawan dan ketegangan KPK-Polri', above n 40; Sundaryani and Jong, 'Jokowi offers no help to KPK', above n 111. See also, 'Adnan Pandu Praja juga dilaporkan ke Bareskrim Polri' [Adnan Pandu Praja is also reported to Bareskrim Polri for accused of a criminal offence], *Republika* (online), 24 January 2015 <<http://www.republika.co.id/berita/nasional/hukum/15/01/24/nio0n2-adnan-pandu-praja-juga-dilaporkan-ke-bareskrim-polri>>; Putu Merta Surya Putra, 'Wakil ketua KPK Adnan Pandu Praja dilaporkan ke Bareskrim Polri' [KPK deputy Adnan Pandu Praja is reported to Bareskrim Polri for accused of a criminal offence], *Liputan 6 news* (online), 24 January 2015 <<http://news.liputan6.com/read/2165815/wakil-ketua-kpk-adnan-pandu-praja-dilaporkan-ke-bareskrim-polri>>; Nanien Yuniar, 'Adnan Pandu Praja dituduh rugikan pemilik saham Daisy Timber' [Adnan Pandu Praja is accused of disadvantaging shareholders of Daisy Timber], *Antara News* (online) 24 Januari 2015 <<http://www.antaraneews.com/berita/476043/adnan-pandu-praja-dituduh-rugikan-pemilik-saham-daisy-timber>>.

¹¹⁴ Fedina S Sundaryani, 'Police grill Bambang Widjojanto again', *The Jakarta Post* (online), 23 April 2015 <<http://www.thejakartapost.com/news/2015/04/23/police-grill-bambang-widjojanto-again.html>>.

¹¹⁵ Fedina S Sundaryani and Hans Nicholas Jong, 'Crime Unit breached legal procedure in Bambang's arrest', *The Jakarta Post* (online), 25 January 2015 <<http://www.thejakartapost.com/news/2015/01/25/crime-unit-breached-legal-procedure-bambang-s-arrest.html>>. See also, Tahta Aidilla, 'Peradi: Bareskrim sewenang-wenang tangani kasus Bambang Widjojanto' [Peradi – Indonesian Advocates Association: Bareskrim uses an abusive force of power to address Bambang Widjojanto's case], *Republika* (online), 15 May 2015 <<http://www.republika.co.id/berita/nasional/hukum/15/05/15/nods5j-peradi-bareskrim-sewenang-wenang-tangani-kasus-bambang-widjojanto>>.

¹¹⁶ 'Indonesia still one of the most corrupt', above n 98.

Thailand 3.3, Hong Kong 3.2 and Singapore 2.2.¹¹⁷ A survey in 2010 by Political Economic Risk Consultancy (PERC) ranked Indonesia as the most corrupt of 16 major Asia-Pacific investment destinations with a score 9.07 out of 10 which was a higher score than the previous year of 7.69.¹¹⁸ Transparency International ranked Indonesia at 118 out of 176 countries with a score of 32 out of 100 in 2012, and 114 out of 177 countries in 2013 with a similar score of 32 out of 100,¹¹⁹ and 107 out of 175 with a score of 34 in 2014.¹²⁰ Corruption is claimed to be a major obstacle in strengthening Indonesia's economy.¹²¹

Corruption is seen as contributing to the further decline of moral integrity, more limited awareness of the law, greater uncertainty in the legal system and an increasing cause of injustice.¹²² Many people question whether Indonesia's institutions have any integrity or ethics pointing to recent corruption cases involving respected institutions including the Department of Religion's programs on the publication of the Holy Koran and the Hajj [pilgrimage] as well as the bribery charge brought against the Chief Justice of Constitutional Court in 2013.¹²³ A bribe paid by a senior prominent lawyer, O C Kaligis, in late 2015 to the Administrative Court justices in Medan, North Sumatra,¹²⁴ is another example of corrupt practices in the formal legal system.

¹¹⁷ Sunanda Creagh, 'Indonesia's battle against corruption', *Reuters*, 17 June 2009.

¹¹⁸ 'Indonesia most corrupt of key Asian nation', above n 28; PERC: Indonesia negara paling korup, above n 91.

¹¹⁹ Transparency International, *Corruption by country / territory – Indonesia* <<http://www.transparency.org/country#IDN>>. See also, 'RI ranks 100th in 2011 corruption perception index', *The Jakarta Post* (online), 1 December 2011 <<http://www.thejakartapost.com/news/2011/12/01/ri-ranks-100th-2011-corruption-perception-index.html>>. Indonesia was ranked 100th out of 183 countries in 2011, 110th out of 178 countries in 2010, and 111th out of 180 countries in 2009.

¹²⁰ Transparency International, *Corruption Perception Index 2014: Results* <<https://www.transparency.org/cpi2014/results>>.

¹²¹ Jimmy Koh, UOB chief economist, 'Speech in Asia awakening: an exclusive event jointly hosted by Globe Asia and United Overseas Bank (UOB)', *Globe Asia* (Jakarta), 'Who can run Indonesia Inc? vol. 3 No. 9, September 2009.

¹²² 'Indonesia still one of the most corrupt', above n 98.

¹²³ Daniri, 'Kiat berbisnis tanpa suap dan korupsi', above n 88, 2.

¹²⁴ Aghnia Adzka, 'Naik Alphard ke PTUN Medan, Kaligis Serahkan Suap ke Hakim' [Heading to Medan's Constitutional Court with Alphard's car, Kaligis delivered bribes to a judge], *CNN Indonesia* (online), 16 Oktober 2015 <<http://www.cnnindonesia.com/nasional/focus/oc-kaligis-terperangkap-suap-2633/>>; 'Rekaman Sogok Panitera PTUN dan OC Kaligis Dibeber di Sidang' [Taped recording of Kaligis bribed a clerk of the Constitutional Court has revealed in a court trial

Increasing moral awareness and responsibility has been seen as a solution to reducing corruption. Kurniawan and Indriantoro suggest that a sense of moral responsibility is more important for the effectiveness of good corporate governance than any regulatory infrastructure.¹²⁵ The ethical qualities of people in a company and their integrity may lead to them being transparent and implementing good corporate governance.¹²⁶ Daniri held a similar view that ethical behaviour flowing from the integrity of the board of directors is a prerequisite for achieving similar outcomes from all employees in all corporate activities.¹²⁷ It is not a view held by all. Others suggest good governance process as the solution. Pangaribuan did so partly as corruption is an outcome of bad governance process.¹²⁸ It is also considered by Mahfud as a solution as it upholds law enforcement.¹²⁹ However they do not indicate why unethical people would engage in good governance particularly as legal sanctions have been seen as an ineffective tool to deter those who are corrupt.¹³⁰ The outcomes are well described by Agus Rahardjo, now the KPK chairman, who observes that the grafter still has a happy, wealthy, and well respected life.¹³¹

proceeding], *Tempo.Co* (online), 1 Oktober 2015
 <<http://nasional.tempo.co/read/news/2015/10/01/063705555/rekaman-sogok-panitera-ptun-dan-oc-kaligis-dibeber-di-sidang>>.

¹²⁵ D M Kurniawan and N Indriantoro, *Corporate Governance: The Role of Disclosure in Strengthening Corporate Governance and Accountability: Corporate Governance in Indonesia, Hongkong China* (2000) The OECD Second Asian Roundtable, 30–1
 <<http://www.oecd.org/dataoecd/6/62/1931154.pdf>>.

¹²⁶ Dominikus Octavianto Kresno Widagdo and Anis Chariri, 'Pengaruh good corporate governance terhadap kinerja perusahaan' [The influence of good corporate governance on a company's performance] (2014) 3(3) *Diponegoro Journal of Accounting* 1, 1 <ejournal-s1.undip.ac.id/index.php/accounting/article/.../6069/5857>.

¹²⁷ Daniri, *Good Corporate Governance*, below n 157, 159.

¹²⁸ Daniel Pangaribuan, *Peran corporate governance dalam mencegah korupsi* [The role of corporate governance to prevent corruption], Sekolah Tinggi Akutansi Negara (STAN) [1] <<http://www.stan.ac.id/kategori/index/9/page/peran-corporate-governance-dalam-mencegah-korupsi>>.

¹²⁹ Moh. Mahfud MD, *Penegakan hukum dan tata kelola pemerintahan yang baik* [Law enforcement and good governance], 6
 <<http://www.mahfudmd.com/.../PENEGAKAN%20HUKUM...>>. Mahfud is a former chairman of the Indonesian Constitutional Court.

¹³⁰ Pangaribuan, above n 128.

¹³¹ 'Capim KPK Agus: Koruptor Masih Ketawa, Kaya, Dihormati' [KPK deputy candidate: a grafter is still able to laugh, be wealthy, and be respected], *Kompas* (online), 24 Agustus 2015 <<http://nasional.kompas.com/read/2015/08/24/10272911/Capim.KPK.Agus.Koruptor.Masih.Ketawa.Kaya.Dihormati>>; Erika Anindita, 'Agus Rahardjo elected new KPK chairman', *The Jakarta Post*

(c) Cultural factors

In addition to the lack of transparency encouraged by corruption Indonesian business culture has been identified as a common problem producing a lack of transparency in governance in Indonesian companies including in their financial dealings with government.¹³² They include the protection of the privacy of the controlling family shareholders, patrimonial values, collusive relationships, and a failure to appreciate the values of openness.

The specific cultural background of a controlling family is important in this context. Many are ethnic Chinese and share similar beliefs to other families in the Chinese diaspora in South East Asia.¹³³ It makes transparency a significant issue¹³⁴ as family-owned companies and companies with political ties are reluctant to be transparent. An empirical study confirmed that the controllers of many of Indonesian's firms 'dislike the transparency and scrutiny that come with publicly traded securities'.¹³⁵ It is reinforced by the belief that information about the company is confidential to the controlling family and the fear that others may take advantage of any information disclosed. Strong influence and the power of controlling shareholders and their occupation of both management and governance positions has maintained their control.¹³⁶

The legacy of the Soeharto regime is marked by collusive relationships with government and political parties where executives gain senior positions in companies through lobbying, nepotism and collusion instead of through processes of merit under good

(online), 17 December 2015 <<http://www.thejakartapost.com/news/2015/12/17/agus-rahardjo-elected-new-kpk-chairman.html>>.

¹³² S Kristiansen *et al*, 'Public Sector Reforms and Financial Transparency: Experiences from Indonesian Districts' (2008) 31(1) *Contemporary Southeast Asia: A Journal of International and Strategic Affairs*.

¹³³ Michael Carney and Eric Gedajlovic, *The co-evolution of institutional environments and organizational strategies: The rise of family business groups in the Asean region* (2002) 14 <<http://www.sfu.ca/~erg/research/coevolution.pdf>>. See also, Brown, above n 89, 953–92. Companies originating in Indonesian state owned enterprises are more associated with *pribumi* [indigenous] culture.

¹³⁴ *Ibid* 79.

¹³⁵ Christian Leuz and Felix Oberholzer-Gee, 'Political relationship, global financing, and corporate transparency: Evidence from Indonesia' (2006) 81 *Journal of Financial Economics* 411, 436.

¹³⁶ *Ibid* 115.

norms of corporate management.¹³⁷ As a consequence, companies and their businesses are managed unprofessionally, disadvantaging minority shareholders. The fall of the Soeharto regime has forced controlling families, which depended on collusive relationships with government, to face the increasing willingness of the media and other business groups to expose issues that were once concealed.¹³⁸

The dominance of controlling family shareholders in Indonesian companies has impacted on the listing of medium to large enterprises. Indonesia has a relatively small number compared to Thailand, Singapore, Malaysia, Hong Kong and India. The limited listings in the capital market have resulted in greater dependency on foreign investors¹³⁹ for whom transparency and disclosure are crucial factors.

The small number of listed companies registered on the Indonesia Stock Exchange (IDX) compared with existing medium and large enterprises can be seen in the table below.¹⁴⁰

Table 1.2: A comparison between the existing medium/large enterprises and listed companies

Year	Medium/large enterprises ¹⁴¹	Listed companies ¹⁴²	Listed SOEs ¹⁴³
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¹³⁷ B R Amirudin, *Komisaris dan Good Corporate Governance: Peran Komisaris Independen dalam Mewujudkan Good Corporate Governance di Tubuh Perusahaan Publik* [Commissioner and Good Corporate Governance: The role of independent commissioners in creating good corporate governance in public companies] <<http://re-serachengines.com/badriyahamirudin.html>>.

¹³⁸ C Chua, above n 43, 1.

¹³⁹ Dewi Rachmat Kusuma, 'Perusahaan public Indonesia baru 479, di India sudah 5.267' [Indonesia has only 479 public compaies, India already has 5.267 public enterprises], *DetikNews* (online), 18 November 2013, [1], [4] <<http://finance.detik.com/read/2013/11/18/111548/2415591/6/perusahaan-publik-di-indonesia-baru-479-di-india-sudah-5267>>. This was addressed by OJK Chief Executive Capital Market, Nurhaida, in Annual Capital Market Outlook 2014. As of September 2013, IDX has recorded only 479 issuers compared to Thailand with 577, Singapore 782, Malaysia 909, Hong Kong 1.585 and India 5.267 issuers.

¹⁴⁰ Indonesia Stock Exchange [*Bursa Efek Indonesia*], *Fact Book 2014, 2013, 2012, 2011, 2010, 2009, 2008 Appendix Listed companies* <<http://www.idx.co.id/Home/Publication/FactBook/tabid/146/language/en-US/Default.aspx>>.

¹⁴¹ This excludes small-scale & micro establishment reached millions companies. See, Badan Pusat Statistik [Statistics Indonesia], *The number of establishment of large and medium manufacturing by subsector, 2008-2013 and 2000-2011* <http://www.bps.go.id/tab_sub/view.php?kat=2&tabel=1&daftar=1&id_subyek=09¬ab=2>; Badan Pusat Statistik, *Small-scale & micro establishment – Number of establishment without legal*

2007	27 998	354	14
2008	25 694	393	14
2009	24 468	399	15
2010	23 345	413	17
2011	23 370	428	18
2012	23 592	450	19 ¹⁴⁴
2013	23,941	472	20 ¹⁴⁵
2014	<i>Not available</i>	502	20 ¹⁴⁶

Companies which are listed are marked by concentrated ownership and controlling shareholders.¹⁴⁷ Families control 67.3 per cent of all listed companies.¹⁴⁸ The five largest

entity by industry 1996-2004<http://www.bps.go.id/eng/tab_sub/view.php?kat=2&tabel=1&daftar=1&id_subyek=35¬ab=1>. See also, Badan Pusat Statistik, *Berita resmi statistik: Hasil listing sensus ekonomi (SE06) jumlah perusahaan/usaha meningkat 3,32% per tahun* [Official statistics information: The result of economic census (SE06) shows the number of companies has increased 3,32 per cent per year] (2007-01-02) <<http://www.bps.go.id/?news=526>>.

¹⁴² Indonesia Stock Exchange [*Bursa Efek Indonesia*], above n 140.

¹⁴³ Gatot Trihargo, Deputy Assistant II for Strategic Industry & Manufacturing SOEs – Ministry of State-Owned Enterprises Republic Indonesia, *Good corporate governance implementation in Indonesia's state-owned enterprises* (18 May 2011), 3 <<http://www.oecd.org/corporate/ca/corporategovernanceofstate-ownedenterprises/48062544.pdf>>.

¹⁴⁴ See, BNI Securitas, *BEI: Hanya satu yang listing di 2012 dari target 5 BUMN* [BEI: Only one of the targeted five state owned enterprises listed in 2012] (19 Desember 2012) [1] <<http://bnisecurities.co.id/2012/12/bei-hanya-satu-yang-listing-di-2012-dari-target-5-bumn/>>. See also, 'Tahun ini, hanya satu BUMN tercatat di bursa' [Only one state owned enterprise listed this year], *Sindonews.com* (online), 8 November 2012 <<http://ekbis.sindonews.com/read/686654/32/tahun-ini-hanya-satu-bumn-tercatat-di-bursa>>.

¹⁴⁵ Pusat Informasi [Information Center], *Saham BUMN [SOE's shares]* <<http://pusatis.com/investasi-saham/daftar-saham/daftar-saham-bumn-di-bursa-efek-indonesia-be/>>.

¹⁴⁶ From total of 138 SOEs in 2014. See, Kementerian Badan Usaha Milik Negara (Ministry of State Owned Enterprises), *BUMN Listed – Saham BUMN* <<http://bumn.go.id/halaman/saham>>. See also, Kementerian Badan Usaha Milik Negara (Ministry of State Owned Enterprises), *Daftar BUMN [List of SOEs]* <<http://bumn.go.id/halaman/situs>>. See also, Dahlan Iskan, '8 BUMN ini disiapkan Dahlan untuk go public 2012' [Dahlan prepared 8 SOEs to go public – be listed in 2012], *Tempo.co* (online), 3 Januari 2012 <<http://www.tempo.co/read/news/2012/01/03/090375166/8-BUMN-Ini-Disiapkan-Dahlan-untuk-Go-Public-2012>>.

¹⁴⁷ World Bank, *Corruption and Governance*, above n 92.

¹⁴⁸ Stijn Claessens, Simeon Djankov and Larry H P Lang, *Who Controls East Asian Corporations – and the Implications for Legal Reform* (1999) Public Policy for the Private Sector Note No. 195, World Bank 7 <<http://siteresources.worldbank.org/EXTFINANCIALSECTOR/Resources/282884-1303327122200/195claes.pdf>>.

Indonesian shareholders control companies with between 57 and 65 per cent of all issued shares.¹⁴⁹

The power of the controlling family shareholders is reinforced by a patrimonial culture in which a father-figure exerts authority and in which corporations are seen to exist within a network of familial rather than legal relationships.¹⁵⁰

Such concentrated ownership is a common marker of poor corporate governance.¹⁵¹ Economic studies of governance have also correlated family-control with poor corporate governance and shareholder protection.¹⁵² The inadequate legal protections for minority shareholders, their inability to protect themselves and their vulnerability to political intervention is claimed to be common in developing civil law countries like Indonesia.¹⁵³

These problems are also related to values that are opposed to better governance and greater openness. Making controlling shareholders and management aware of the importance of good corporate governance and the application of its principles to practice has been identified as important. Many have not seen good corporate governance as an urgent issue as they may not benefit from it.¹⁵⁴ From a short-term economic perspective, it is not attractive as its implementation represents new costs and the promised outcomes may not be achieved in the long term.¹⁵⁵ It is 'costly since companies are required to have independent commissioners, an audit committee, transparent information system etc.'¹⁵⁶

¹⁴⁹ Kurniawan and Indriantoro, above n 125.

¹⁵⁰ B Tabaluyan, 'Why Indonesian Corporate Governance Failed-Conjectures concerning Legal Culture' (2002) 15 *Colombia Journal of Asian Law* 141–71.

¹⁵¹ J C Coffee and J J Coffee, *The Rise of Dispersed Ownership: The Role of Law in the Separation of Ownership and Control* (The Center for Law and Economic Studies, Columbia Law School, 2001).

¹⁵² J Farrar, *Corporate Governance: Theories, Principles, and Practice* (Oxford University Press, 2ed, 2005).

¹⁵³ Ramsay and Stapledon, 'Corporate Governance: An Overview of the Key Issues and Debates' (ASIC Corporate Governance Training Program, Sydney, March 20, 2000).

¹⁵⁴ Felia Salim, a former director of Jakarta Stock Exchange, cited in Daniri, *Good corporate governance*, below n 157, 67.

¹⁵⁵ Surya and Yustiavandana, above n 65, 61.

¹⁵⁶ Juniarti and The Lia Natalia, 'Corporate governance perception index (CGPI) and cost of debt' (2012) 3 (18) *International Journal of Business and Social Science* 223, 224 <http://ijbssnet.com/journals/Vol_3_No_18_Special_Issue_September_2012/26.pdf>.

The negative perception of good governance is reinforced by a former chair of BAPEPAM, Herwidayatmo. He saw this as the biggest challenge to better corporate governance. He described shifting the persistent poor mentality opposed to good governance as a third stage -supervising the seed's growth - in an extended analogy relating to the four stages of planting and harvesting.¹⁵⁷

Controlling shareholders and their advisers are also likely to be uncertain about how to implement corporate governance processes, particularly disclosure, as they are concepts unknown to them. Corporate governance principles derived from foreign sources do not fit with Indonesian business and social relations.¹⁵⁸ For instance, the presence of outsiders within a company's management has been previously absent. The creation and maintenance of independent commissioners, audits, nomination and remuneration committees are novel challenges within companies unaware of good corporate governance practices.¹⁵⁹

Addressing those cultural issues may be the crucial issue in improving corporate governance in Indonesia.

1.1.6. The consequences

As previously acknowledged, the poor state of corporate governance in general, and disclosure in particular, in Indonesia is generally related to corrupt practices, a business culture based on relationships, concentrated ownership structures with listed companies

¹⁵⁷ See, Daniri, *Good corporate governance – Konsep dan penerapannya dalam konteks Indonesia* [Concept and its implementation in Indonesian context] (Ray Indonesia, 1st ed, 2005) 79. Herwidayatmo outlined the need of a long timeframe to achieve an effective and qualified implementation of good corporate governance principle within Indonesian companies. He illustrated this by suggesting four planting processes, i.e. (1) selecting good seeds, (2) sowing and planting seeds, (3) supervising the seed's growth, and (4) harvesting or reaping process. The first process has been achieved referred to in the introduction of good corporate governance-oriented rules and related regulations reform and the good corporate governance code. The second process referred to socialization and dissemination of good corporate governance principles in raising awareness of their significances. The third was claimed as the most challenging process. See also, page 112–14. Those processes appear similar to Daniri's view that introduced three phases: namely the preparation phase (awareness building, assessment and manual development), the implementation phase (socialization, implementation and internalization) and the evaluation phase (independent audit and scoring or rating).

¹⁵⁸ Tabaluyan, 'Why Indonesia Corporate Governance Failed-Conjectures concerning Legal Culture', above n 150.

¹⁵⁹ Daniri, *Good corporate governance*, above n 157.

controlled by family shareholders, inadequacies in the formal legal and regulatory systems including a lack of enforcement capacity and adequate sanctions, which are also partly the result of corruption¹⁶⁰ and the problems in adapting legal transplants to Indonesia's situation.¹⁶¹

This study assumes that corruption in legal regulatory and corporate governance systems is inherently bad as it erodes perceptions of fairness and trust and, consequently, impairs economic growth. It assumes that legal and regulatory systems should operate in accordance with standards that are rational, reasonable and clear and that are congruent with actions taken by officials, following processes which minimise conflicts of interests and that maximise impartial decision making by people with relevant skills and knowledge.¹⁶² Such standards have long been regarded as necessary to create the level of trust which encourages lending and investment, which underlie the contemporary corporation.¹⁶³ Corruption and legal uncertainty have been seen as a deterrent to investment in Indonesia.¹⁶⁴

Corruption affects the credibility and legitimacy of the formal legal system. Formal law appears to have no power as laws are not enforced. In theory such laws and regulatory practices govern all aspects of business; in practice they are often ignored, and are inadequate, unenforceable, and irrelevant. In spite of some improvements in the last few years, the Indonesia legal system is still found to be corrupt and unpredictable.¹⁶⁵

The combined impact of these factors has resulted in Indonesia's reputation for having a very poor business and legal environment. It is claimed that this exposes business

¹⁶⁰ World Bank, *Report on the Observance of Standards & Codes Corporate Governance country assessment Republic of Indonesia* (2004) ('ROSC 2004') <<http://www.worldbank.org/html/prddr/trans/marapr02/pgs17-19.htm>>.

¹⁶¹ Tabaluyan, 'Why Indonesian Corporate Governance Failed'-Conjectures concerning Legal Culture', above n 150, 141–71.

¹⁶² L Fuller, *The Morality of Law* (Yale University Press, 2008).

¹⁶³ M Weber and H K Frank, *General Economic History* (1981).

¹⁶⁴ Sara Webb and Sunanda Creagh, 'Indonesia's corruption bill passed', *Reuters* (online), 20 September 2009 <<http://uk.reuters.com/article/uk-indonesia-corruption-snapanalysis-idUKTRE58S1XY20090929>>.

¹⁶⁵ E Davis, 'Indonesia Legal System under fire over e-mail case', *Reuters*, 23 June 2009; See also, B I Yakup, 'Poor legal culture in Indonesia', *The Jakarta Post* (online) July 16, 2007 [1] <<http://www.thejakartapost.com/news/2007/07/16/poor-legal-culture-indonesia.html>>.

to the highest legal risks in the world ¹⁶⁶ and a high degree of difficulty in doing business.¹⁶⁷ This was formally recognised by the Parliament in a legislative statement in 2007.¹⁶⁸

These issues have forced governments since 1999 to undertake significant legal and regulatory reforms to improve corporate law, regulation and governance. A new Company Law No. 25 was introduced in 2007. The 2001 code of good corporate governance was replaced in 2006 by new versions published by the National Committee on Governance Policy. There was an expectation that these changes would lead to better enforcement of corporate law and better corporate governance. However, the legal and regulatory systems have failed to ensure accountability under these revised laws and codes. The newly renamed Financial Services Authority (OJK) previously known as BAPEPAM-LK has confirmed the unsuccessful attempts to improve corporate governance by relying on regulations and codes.¹⁶⁹

Both the economic crisis in 1997 and the global financial crisis of 2007 have been attributed to the failure of corporate governance.¹⁷⁰ This indicates that improvements in standards of corporate governance are required. However the global financial crisis has added to the uncertainty of what regulatory policies to adopt. The policies underlying the reformed laws and code reflect responses to the 1997 crisis and emphasised policies based

¹⁶⁶ P Notowidigdo et al, *Asia Business Law Series: Employment Law Asia* (vol. II, 1st ed, 2005) 38,611.

¹⁶⁷ R H McLeod and A MacIntyre (eds), *Indonesia Democracy and the Promise of Good Governance* (2007).

¹⁶⁸ Badan Perencanaan Pembangunan Nasional (National Development Planning Agency), *Undang-undang Rencana Pembangunan Nasional Jangka Panjang 2005-2025* [The Law concerning Long Term National Development Plan for 2005-2025] (2007) <http://air.bappenas.go.id/index.php?sbf=35&prm_pdf=1&prm_page_id=1&prm_id=13&prm_type_id=2&prm_parent_id=10&prm_doc_cat_id=11&prm_doc_file_name=uu%2017%202007.pdf>.

¹⁶⁹ International Finance Corporation, *Roadmap tata kelola perusahaan Indonesia* [Indonesia corporate governance roadmap] – *Menuju tata kelola emiten dan perusahaan publik yang lebih baik* [Towards better corporate governance of issuers and public companies], 10 <<http://www.ifc.org/wps/wcm/connect/a476310042e2a54bbc09fc384c61d9f7/Indonesia+CG+Roadmap.pdf?MOD=AJPERES>>.

¹⁷⁰ H Jang, 'Failure of Corporate Governance has led to the global economic crisis' (Speech delivered at the lecture on Development of Corporate Governance in Asia, the Indian Institute of Management, 2008) <<http://www.indianexpress.com/news/failure-of-corporate-has-led-to-the-global-economic-crisis>>.

on free market and self-regulation. Those policies were re-evaluated internationally, including in Indonesia, after the global financial crises.¹⁷¹

1.2. Aims and objectives of the study

This study seeks to examine the role of informal or soft law in promoting effective corporate governance with respect to disclosure. It seeks to test whether informal or soft law in this respect is more or less effective in Indonesia. It also considers whether it is more effective in common law than in civil law countries. Indonesia is classified as a member of the civil law family, derived from the Dutch model, even though most recent Indonesian economic law has been influenced by principles from Anglo-American legal systems which have been influential at the international and transnational level.¹⁷²

There have been significant legal reform efforts to reshape economic law adjusted to economic and social changes and contemporary needs including adopting corporate governance concepts. Indonesia's performance in implementing corporate governance based on formal law has been poor compared with other Asian countries because of weaknesses in its underlying political and formal legal systems. There is an urgent need to seek more effective approaches. More recent regulatory theories suggest that alternative regulatory strategies, or informal or soft law, may be more effective in enhancing regulation, including the regulation of corporate governance, where formal legal systems are weak. Braithwaite, for example, promotes the use of informal regulation in the context of responsive regulation in Indonesia's context with limited regulatory capacity as indicated in the next chapter.

There is little analysis of the use of such alternative regulation in addressing weaknesses in Indonesian law although some aspects of informal law, such as voluntary codes of corporate governance, have been adopted in Indonesia as a result of pressure from international financial institutions. In particular there has been no study of how they may

¹⁷¹ Organization for Economic Co-operation and Development, *OECD Strategic Response to the Financial & Economic Crisis: Contribution to the Global Effort* (2009) <<http://www.oecd.org/economy/42061463.pdf>>; International Monetary Fund, *IMF Urges Rethink of How to Manage Global Systemic Risk* International Monetary Fund (2009) <<http://www.imf.org/external/pubs/ft/survey/so/2009/POLO0609A.htm>>.

¹⁷² R Tomasic (ed), *Insolvency Law in East Asia* (Ashgate Publishing Limited, 2006) 355.

affect accountability for corporate disclosure, although appropriate levels of disclosure are generally regarded as necessary for both transparency and accountability.

The key aims of this thesis are:

1. To map the interaction between formal law and regulations and corporate governance codes in Indonesian listed companies.
2. To identify and expand upon the strength and weaknesses in the use of such codes to achieve accountability.
3. To identify how corporate governance codes and self regulation impact on formal law in the regulation of these companies.
4. To assess and analyze the impact of formal law and corporate governance codes on disclosure and the effect, in turn, of that disclosure on formal law and corporate governance codes and accountability under them.

1.3. Significance

1.3.1. Academic contribution

This study seeks to extend current knowledge of the correlation between formal law and regulation and informal law and regulation establishing the potential for alternative methods to enhance contemporary corporate law, regulation and governance. It intends to provide an analysis to increase the influence, control and participation of the business community, government, and citizens in processes which may both simplify and improve the regulatory framework.

It also adds to the knowledge and theories about the capacity of alternative regulatory models to improve corporate governance application in the case of Indonesia. Such a study has not been undertaken in the Indonesian context.

As Indonesia has inherited civil law legal frameworks it needs to ensure that these are able to effectively accommodate forms and processes developed in common law jurisdictions that have been transplanted into it. This will also be relevant to understanding regulatory systems in other developing economies with weak or corrupt formal legal systems. So that, the outcome of this study may be adaptable to these countries with ineffective and corrupt formal legal and regulatory systems and low corporate governance

performances seeking to improve legal certainty, justice and efficiency in order to advance national economic interests.

1.3.2. Practical contribution

This study is also intended to make a practical contribution. It is hoped that its findings will be relevant to creating greater legal certainty and predictability in Indonesian commercial and corporate law and regulation as well as potentially increasing economic justice to better promote Indonesia's national economic interests. In particular it will:

- (1) better inform Indonesian policy and law making and regulatory practices regarding the usefulness and complementarities of alternative regulation and formal law in improving regulatory frameworks.
- (2) improve, on the basis of empirical evidence, corporate governance in listed companies as disclosure is recognized as essential for corporate accountability.
- (3) permit regulatory agencies and citizens to monitor developments and to use that information for other purposes in ensuring accountability for corporate actions.
- (4) contribute to knowledge around creating appropriate corporate governance applications suited to Indonesia's context.

These practical contributions extend to establishing whether formal law and informal law may be used in a collaborative way to embrace and improve a broader range of corporate governance issues and how this may be achieved. This may contribute to the development of more effective corporate governance practices and also help to further develop economic democracy.¹⁷³

1.4. Research Methodology

1.4.1. Introduction

Methodology is a tool.¹⁷⁴ Glass states that methodology is 'really a set of methods, practices, and procedures normatively followed by members from each discipline or field

¹⁷³ F Hutchinson, M Mellor and W Olsen, *The politics of money : towards sustainability and economic democracy* (Pluto, 2002).

¹⁷⁴ Sarah J Tracy, *Qualitative research methods: Collecting evidence, crafting analysis, communicating impact* (Wiley, 2012) 25.

of study'.¹⁷⁵ Greene explains similarly that 'methods are tools and that, in the hands of researchers with certain methodological persuasions, they can be used to promote social justice, maintain the status quo, or promote social transformation'.¹⁷⁶ Fassinger and Morrow support this claim that 'various research methods can be appropriate for social justice aims'.¹⁷⁷ The methodology used in this project is mixed.¹⁷⁸ It is drawn from methodologies, which include doctrinal legal research and qualitative research present in the social sciences. The study applies these research methods and techniques to collect data from three main sources.

Firstly, data has been collected from primary legal materials including legislation and regulations, judicial interpretation and formal guidance given by government and other bodies including soft law such as codes of practice. Secondly, data was gathered from academic monographs and journals, from media and other relevant data bases. It also included materials and reports published by international and transnational bodies and government agencies and other relevant bodies and organisations such as the OECD, the Asian Development Bank, the Asian Corporate Governance Association, rating agencies and investment advisors. The topics covered include corporate governance, new regulatory theories and the legal, political, social and business cultures of Indonesia in the past to better understand their influence in the present. The third source of data is interviews conducted in Indonesia. Informants were identified from their knowledge of, and experience with, information disclosure in corporate governance in Indonesia. The composition of the informants and their selection is described further below.

¹⁷⁵ Stephen D Lapan, Marylynn T Quartaroli and Frances Julia Riemer (eds), *Qualitative research: An introduction to methods and designs* (Jossey-Bass, 2012) 11. The authors made a distinction the term method as tools and methodology as a form of inquiry.

¹⁷⁶ Sharlene Nagy Hesse-Biber, *Mixed methods research – Merging theory with practice* (Guilford Press, 2010) 13.

¹⁷⁷ Ruth Fassinger and Susan L Morrow, 'Toward best practices in quantitative, qualitative, and mixed-method research: A social justice perspective' (2013) 5 (2) *Journal for Social Action in Counseling and Psychology* 69, 69.

¹⁷⁸ W Lawrence Neuman, *Research Design: Qualitative, Quantitative, and Mixed Methods Approaches* (Sage, 2nded, 2003) 30.

1.4.2. Doctrinal legal research

The methodology, in part, is based in doctrinal research but extended beyond the source of formal law to informal or soft law such as the Code of Good Corporate Governance.

Snel observes, writing partly in the context of the Dutch civil law tradition that Indonesia shares, that:

Within doctrinal legal research, scholars generally do not explicate the procedures and protocols they followed to assure the soundness of the usage of sources. ... In applications for research funding, doctrinal legal scholars have – until recently – invariably sufficed by stating that their research method(s) comprise ‘studying legislation, case law and literature’.

Hutchinson and Duncan point out, in the context of Australian PhD theses in law:

Unfortunately the doctrinal method is often so implicit and so tacit that many working within the legal paradigm consider that the process is unnecessary to verbalise. Any articulation that occurs is for the benefit of the outsiders.¹⁷⁹

Forced to justify what legal research is in the context of competing for government research funds the Council of Australian Law Deans stated:

To a large extent, it is the doctrinal aspect of law that makes legal research distinctive and provides an often under-recognised parallel to ‘discovery’ in the physical sciences. Doctrinal research, at its best, involves rigorous analysis and creative synthesis, the making of connections between seemingly disparate doctrinal strands, and the challenge of extracting general principles from an inchoate mass of primary materials. The very notion of ‘legal reasoning’ is a subtle and sophisticated jurisprudential concept, a unique blend of deduction and induction, that has engaged legal scholars for generations, and is a key to understanding the mystique of the legal system’s simultaneous achievement of constancy and change, especially in the growth and development of the common law.¹⁸⁰

This is a study in the context of Indonesian law rather than in the context of a common law jurisdiction but similar issues arise in interpretation. Because of the issues of corruption discussed above the issues of consistency and change in Indonesian law are different from the legal system that Australian law deans were describing. This, in some

¹⁷⁹ Terry Hutchinson & Nigel Duncan, ‘Defining and Describing What We do: Doctrinal Legal Research’, (2012) 17(1) *Deakin Law Review*, 83-119.

¹⁸⁰ Council of Australian Law Deans, *Statement on the Nature of Legal Research*, 3 <<http://www.cald.asn.au/docs/cald%20statement%20on%20the%20nature%20of%20legal%20research%20-%202005.pdf>>. The statement is taken from the CALD submissions to the Department of Education, Science and Training (DEST) in relation to the Research Quality Framework (RQF), May and October 2005.

ways, weakens the importance of how doctrinal law is stated as it is not always influential in determining the outcomes of judicial decisions. However, it is necessary for the formal legal system of Indonesia to move towards this if the impact of corruption is to be reduced and it is to play its appropriate role in facilitating the resolution of disputes in civil cases and also justice in criminal cases.

Writing of Dutch and civil law more generally Snel also makes two substantial points which the research has sought to address. One is the problem of collecting all of the sources of law including 'soft law'.¹⁸¹ This is not a major issue in Indonesian law. Most of the major sources of law including laws and regulations are published. In the area of corporate and securities law other important legal sources such as the listing rules of the stock exchange are also accessible. As Snel also observes the publication of case law, which in Indonesia's civil law system is generally not a source of law, is random. The other issue Snel raises is more significant and that is disagreement over methodologies to interpret and synthesise legal sources. He indicates that significant issues are objectivity of interpretation and how the researcher addresses that as well as the conscious and unconscious selective behaviour of the researcher.¹⁸² These issues are recognised by the researcher. They have

¹⁸¹ Collecting relevant sources: a challenging research activity. The challenge in the age of the internet in collecting all resources including whether 'soft law', 'notices', 'web pages', 'guidelines', official and non-official 'communication', are looked for; this proliferation makes it difficult to find the specifically relevant sources; impact of internationalisation on the number of sources; that what is found may not point to key sources which may be overlooked; the period of time over which literature needs to be covered; digitalisation has led to choice of data bases; digital data bases may not be comprehensive and the 'algorithms' may not be comprehensive; keywords create their problems.

¹⁸² Disagreement over theories of interpretation; legal sources are deeply ambiguous and raise the question of the objectivity of interpretation; how critical the researcher needs to be of prevailing views or check the adequacy of previous research and methodology; the first interpretation that a scholar makes remains the one that is preferred through the project; conscious or unconscious selective behaviour in the (selection and) interpretation of sources in doctrinal legal inquiry; establishing the mutual authority and cogency (weight or importance) of legal sources; it is often attempted to make inferences from a few exemplary or key cases, without providing any information on, first, what 'exemplary' or 'key' would mean within their research context; second, why the selected cases are 'exemplary' or 'key' cases, and whether, third, the selected cases adequately or fairly represent any cases other than those selected by the author; the inherently random nature of the publication of case law; when collecting sources the scholar is challenged to confine the broader context and contextual discussion of a particular research project so that it does not subsume the entire project. See, Marnix Vincent Roderick Snel, *Source-usage within doctrinal*

been partly mitigated by using other data including secondary sources and also by conducting interviews to gain an understanding of beliefs and practices, the policy and law makers, the business people, the regulators, the legal practitioners and the judges involved in making, interpretation and applying the formal law.

1.4.3. Qualitative and empirical research

As indicated this study uses data from two other major sources, secondary literature as well as media data bases and interviews. This is important as its focus extends beyond formal law to informal or soft law. It can be categorized as both qualitative and empirical research. Gubrium and Holsten pointed out that ‘qualitative researchers raise “what” and “how” questions’.¹⁸³ The questions ‘explore the specific dynamics and processes of everyday life’. They focus on ‘a specific social context, and these processes and dynamics are often difficult to quantify and often remain hidden’.¹⁸⁴ The research questions particularly those relating to informal law in this study justify the qualitative category.

There are a number of definitions of qualitative research. Bryman describes it as ‘a research strategy that usually emphasizes words rather than quantification in the collection and analysis of data’.¹⁸⁵ Sandelowski states that qualitative research is ‘an umbrella term for an array of attitudes towards and strategies for conducting inquiries that are aimed at discovering how human beings understand, experience, interpret, and produce the social world’.¹⁸⁶ Tracy pointed out that conducting qualitative research is considered:

research process by identifying a particular issue, problem, or dilemma in the world and then proceed to systematically interpret the data in order to provide an analysis that sheds light on the issue and/or opens a path for possible social transformation’.¹⁸⁷

Risjord *et al* similarly states that qualitative methods ‘are explanatory and textual, and include passive observation, participant observation and open-ended interviews ...’.¹⁸⁸

This study meets these descriptions and follows the path described by them.

legal inquiry: choice, problems, and challenges <
<http://www.lawandmethod.nl/tijdschrift/lawandmethod/2014/06/RENM-D-13-00003>>.

¹⁸³ Hesse-Biber, *Mixed methods research*, above n 176, 42.

¹⁸⁴ *Ibid* 43.

¹⁸⁵ Cited in Martyn Hammersley, *What is qualitative research?* (Bloomsbury Publishing, 2012) 1.

¹⁸⁶ *Ibid* 1.

¹⁸⁷ Tracy, above n 174, 4.

Qualitative approaches have the potential to contribute to:

enhance relationship and dialogue between researchers and participants in their communities; minimize the imposition of researcher assumptions on diverse others; empower participants by helping them to voice their stories and by honouring their strengths, needs, and values; stimulate collaborative social change efforts by researchers and participants; catalyse theory development; and frame communication and dissemination of research outcomes in ways that are immediately useful to communities.¹⁸⁹

Qualitative research ‘can enrich and inform the decisions of practitioners and policymakers’.¹⁹⁰ This research is conducted in pursuit of these objectives.

This study utilizes an approach based on triangulation. This employs the three separate sources of data, referred to above, in answering the research questions. It concentrates on primary legal sources, the secondary literature as well as media data bases and individual lived experiences. Marshall and Rosman classified individual lived experienced as one of the three focuses of qualitative research, besides a social and cultural focus, and a language and communication focus. The lived experience focus ‘typically relies on an in-depth interview strategy’. It ‘accepts the value of content and setting, and searches for a deeper understanding of the participants’ lived experiences of the phenomenon under study’.¹⁹¹ It tends to be exploratory or descriptive nature.¹⁹²

The use of the triangulation of sources fits with Indonesia’s present context as triangulation is seen not only as a useful tool for researchers but also a potential solution to the problem of providing valid and reliable data in a situation as complex in Indonesia as regulation and the enforcement of law.¹⁹³ The use of this strategy is considered to be effective by a number of scholars. Triangulation integrates the data during the interpretation

¹⁸⁸ Abir K Bekhet and Jaclene A Zauszniewski, ‘Methodological triangulation: an approach to understand data’ (2012) 20(2) *Nurse Researcher* 40, 40.

¹⁸⁹ Fassinger and Morrow, above n 177, 74–5.

¹⁹⁰ Margaret W Sallee and Julee T Flood, ‘Using qualitative research to bridge research, policy, and practice’ (2012) 51(2) *Theory Into Practice*, 137, 140.

¹⁹¹ Catherine Marshall and Gretchen B Rossman, *Designing qualitative research* (Sage, 5thed, 2011) 92–3.

¹⁹² *Ibid* 92.

¹⁹³ Somarie Holtzhausen, ‘Triangulation as a powerful tool to strengthen the qualitative research design: The Resource-based Learning Career Preparation Programme (RBLCPP) as a case study’ (Paper presented at the Higher Education Close Up Conference 2, Lancaster University, 16-18 July 2001) [34] <<http://www.leeds.ac.uk/educol/documents/00001759.htm>>.

phase. The main purpose of the strategy is ‘for confirmation, corroboration or cross-validation within a single study’.¹⁹⁴

Triangulation of the data is used to ‘increase confidence that we have correctly interpreted how things work’.¹⁹⁵ It provides ‘confirmation of findings, more comprehensive data, increased validity and enhanced understanding of studied phenomena’.¹⁹⁶ Utilizing triangulation strategy in qualitative research assists to ‘place the research findings in a wider context’. A researcher often refers back to the literature at different points in analysing the data.¹⁹⁷

With respect to the validity of the research referring to the findings that are true and certain – ‘true in the sense that research findings accurately reflect the situation, and certain in the sense that research findings are supported by the evidence’ – the triangulation method is used by the researcher to ‘check and establish validity in their studies by analysing a research question from multiple perspectives’.¹⁹⁸ Guion et al note that data triangulation ‘involves using different sources of information in order to increase the validity of the study’.¹⁹⁹ Denzin and Patton also write of the triangulation of sources which examines ‘the consistency of different data sources from within the same method’.²⁰⁰

¹⁹⁴ Steven R Terrell, ‘Mixed-methods research methodologies’ (2012) 17 (1) *The Qualitative Report* 254, 268.

¹⁹⁵ Robert E Stake, *Qualitative research: Studying how things work* (Guilford Publications, 2010) 37.

¹⁹⁶ Bekhet and Zauszniewski, above n 188, 40.

¹⁹⁷ Hesse-Biber, *Mixed methods research*, above n 176, 38–9.

¹⁹⁸ Lisa A Guion, David C Diehl and Debra McDonald, *Triangulation: Establishing the validity of qualitative research*, University of Florida, 1 <<http://edis.ifas.ufl.edu/fy394>>.

¹⁹⁹ *Ibid* 1–2. There are other different types of triangulation i.e. investigator triangulation, theory triangulation, methodological triangulation and environmental triangulation. Investigator triangulation uses several different investigators in the analysis process. Theory triangulation utilizes multiple perspectives to interpret a single set of data. Methodological triangulation uses multiple qualitative and/or quantitative methods to study the program. Environmental triangulation involves the use of different locations, settings, and other key factors related to the environment in which the study took place, such as the time, day, or reason.

²⁰⁰ Cited in Robert Wood Johnson Foundation – Qualitative research guideline project, *Triangulation* <<http://www.qualres.org/HomeTria-3692.html>>. The other three methods include methods triangulation – ‘checking out the consistency of findings generated by different data collection methods’ (qualitative and quantitative data commonly used); analyst triangulation – using multiple analyst to review findings or using multiple observers and analysts’; and

1.4.4. Research design

As indicated above, this study extends over diverse fields including law, new regulatory theories as well as legal, political, social and business cultures. These concentrate on law and regulation analysing the applicability of new regulatory theories to understanding Indonesia's use of informal regulation as represented by the corporate governance code. That in turn further focuses the study by concentrating on Indonesia's 2006 Code of Good Corporate Governance's impact on disclosure. This provides a detailed and contextualized study of the legal, politics and cultures that have challenged good regulation and corporate governance in Indonesia.

It employs a literature review to identify relevant issues in Indonesian political, social and business cultures which have produced problems for formal law and regulation and the way in which the code as a form of alternative regulation may remedy such problems by increasing regulatory effectiveness, legitimacy, flexibility and transparency.

The literature review includes the concept and role of corporate governance, particularly disclosure within the corporate governance framework, alternative regulatory theories, formal law and informal law and their relationship and a comparative study of models of corporate governance codes promoted by international governmental and non-governmental organisations and the adoption and application of disclosure principles in some select countries that are relevant to Indonesia including other developing economies in South East Asia such as Malaysia, Singapore, Philippines, and Thailand. It recognises that they exist in legal and regulatory systems that have evolved through different historic, social and economic experiences. An extensive area of secondary literature extending into the social economy and political history was used to construct the social and cultural values around business transparency in Indonesia in Chapter 4. All jurisdictions, however, are under pressure from globalisation – from international bodies and financial institutions - to apply similar regulatory strategies.²⁰¹

theory/perspective triangulation – using multiple theoretical perspectives to examine and interpret the data.

²⁰¹ L Martinez-Diaz, 'Pathways Through Financial Crisis: Indonesia,' (2006) 12 *Global Governance*, 395–412.

A separate search was undertaken of Indonesian business media data-bases including newspapers and internet sites to identify reports and other information relating to disclosure, the corporate governance code, regulatory and legal practices of exchanges, government regulatory bodies and the courts and the related activities of professional and non-government organisations.

Further data and information was collected in an empirical study, which was undertaken in both business and regulatory sectors involving direct interviews utilizing semi-structured questionnaires. It was conducted by face to face interviews that collect spontaneous and detailed answers.

The interview involved business people and their professional advisers, business organizations, law and policy makers, legal practitioners, accountants and auditors, legal institutions, law enforcement agencies, prosecutors and judges and non government organizations as well as some select corporate insiders.

Conducting interviews is ‘the most common form of data gathering in qualitative research studies,...’. It may directly be able to collect the perspectives of those people who experienced the issues under study.²⁰² This is to gain a better understanding of the practices relating to corporate governance and disclosure, especially their experience with the operation of existing laws and the corporate governance code and disclosure. It specifically seeks to identify the impact of the code on existing laws and formal regulation, and their effect on accountability for disclosure. It also seeks to identify the obstacles to implementing the practices expected by the code, including those relating to disclosure. Issues raised include their experience with the code, the importance given to the code in practice, the impact of the code on business and legal cultures, problems with enforcing the code and the role of informal sanctions, the role of regulatory bodies, business and professional organisations, corporate governance NGOs, the effectiveness of official law in ensuring disclosure, the importance attached to disclosure by individuals and in corporate practices, the impact of business and social culture on disclosure, the benefits of disclosure to the disclosing entity, the role of business associations, professional organisations and

²⁰² Johnny Saldana, *Fundamentals of qualitative research* (Oxford University Press, 2011) 75.

NGOs in ensuring that disclosure takes place, as well as their suggestions for improvements.

The data from the interviews was stored in three separate ways for analysis including on digital backup, on digital recorder storage and in hard copy.

1.4.4.1. Sampling for interviews

In the empirical study using interviews a purposive sampling method was applied in determining interviewees because of the large number of organisations and people involved in corporate regulation and governance. The 48 samplings were chosen from private and public categories as follows:

Table 1.3: The composition of the informants from private and public sectors

Private sector	Public Sector
Indonesia Stock Exchange [IDX]	National Committee on Governance
Professional independent directors	Judges involved in corporate and securities litigations and appeals
Non-governmental organisations including the Indonesian Institute of Accountants, Indonesian Association of Lawyers, Indonesian Institute for Corporate Directorship, Forum for Corporate Governance in Indonesia	Public prosecutor and investigatory authorities
Credit rating agency	Indonesian Capital Market and Financial Institutions Supervisory Agency [BAPEPAM-LK]
Corporate lawyers	Government policy and law makers
Auditors	Indonesian Finance and Development Supervisory Agency
Accountants	
Business journalists	
Academic researchers	

1.4.4.2. Conducting of interviews

Conducting research using interviews was a challenge in Indonesia, especially when it involves public officials and senior business people and professionals in discussing

sensitive issues such as governance and corruption. This is reflected by other researchers' experiences who have also faced difficulties in collecting data using this approach. Among others, Worang claimed that the Indonesia business world is not familiar with such research. He attributed the reluctance of potential respondents to respond to the lack of any obvious advantage in participating and suspicion about the topics to be discussed. Access to the managerial level and above in government and companies have been identified as being more difficult. Governance is seen as a taboo topic especially for bureaucrats and government officials, as it is associated with corruption, collusion and nepotism, which carry perceived risks to an informant's ongoing position. Another factor identified is in the influence of Javanese cultural practices, which also creates a large gap between subordinates, the researcher, and superiors, senior business people, managers and bureaucrats.²⁰³

The researcher initially faced difficulty in getting access to potential respondents. Contact by email and telephone to potential participants with full explanations of the study, the background to the research and a confidentiality guarantee in relation to the information gained were mostly unsuccessful. Besides the factors identified by Worang above, this may also be because the selected participants were too busy and had difficulty in allocating time to participate, already having had to prioritize very tight agendas. Marshall and Rossman confirm these difficulties with this approach. They consider that e-mail recipients 'get a sense of whether they are right for the study and whether the benefits outweigh any discomfort if they participate'. They see that an e-mail request is 'quite impersonal and easy to delete!'. Personalized requests, they identify, as likely to generate 'larger and committed responses from potential participants.'²⁰⁴ This approach effectively worked for the researcher in getting permission from targeted participants to agree to interviews.

The researcher's network, including alumni, friends and people from the same ethnicity working in the targeted informants' institutions, was used to provide introductions and references to credible informants. This was followed by personal delivery of the formal letters. Eventually, all participants voluntarily agreed to participate in the interview process.

²⁰³ Worang, above n 93, 117–18.

²⁰⁴ Marshall and Rossman, above n 191, 101.

Before the interview proceeded, the purpose and procedures of the study were explained as well as their right to withdraw and how confidentiality would be maintained. Each interviewee was given the *Information to Participants Involved in Research*²⁰⁵ form to read. The interviewee was also given sufficient time to read and to sign the *Consent Form for Participants Involved in Research*.²⁰⁶

1.4.4.3. Analysis of data

The information and data from the literature and data base research and the data interviews mentioned above have been analysed to assess regulatory, corporate governance and disclosure practices, identify their weaknesses and suggest approaches for improving effective accountability for disclosure.

They have also been analysed to identify related factors including relevant aspects of political and social cultures including the toleration of corruption and its impact on regulatory effectiveness. The purpose of using different data from informants involved in listed companies as well as in corporate law and regulation and other sources including media data bases and literature, is for further triangulation of this data. The usual purpose of data triangulation is for cross-checking data from multiple sources to search for irregularities and differences.²⁰⁷

Triangulation is appropriate to establish the trustworthiness of data analysis including credible, transferable, dependable and confirmable analysis.²⁰⁸ This is considered a suitable approach for this study to preserve the quality of the research.

Outcomes from the triangulation of the interviews were initially ascertained and then crossed checked and confirmed in relation to the media data bases. The results of this analysis have also been triangulated with conceptual models from the literature. Where there have been differences the empirical data has been carefully considered. The use of interviewees has been to ensure the credibility of the research findings. In this way the

²⁰⁵ See Appendix D for the Information to Participants Involved in Research.

²⁰⁶ See Appendix F for Consent Form for Participants Involved in Research.

²⁰⁷ N K Denzin, *Sociological Methods: A Sourcebook* (McGraw-Hill, c1978, 2nd ed, 2006).

²⁰⁸ University of the West of England, *Qualitative analysis; Issues of Analysis*
<<http://hsc.uwe.ac.uk/dataanalysis/qualIssues.asp>>.

analysis has sought to achieve some neutrality and objectivity based as much as possible on a rational and unprejudiced interpretation.²⁰⁹

1.5. Structure of Dissertation

This dissertation consists of eight main chapters. The outline of each chapter is as follows:

Chapter 1: Introduction – This chapter introduces the background to this dissertation on corporate governance and disclosure, in Indonesia and the potential impact of alternative regulatory approaches to improving its implementation, the research questions, the aims and objectives of the study and its significance, the research methodology used, and, a conclusion.

Chapter 2: Literature Review – The second chapter presents a review of the literature related to the research questions. This part is divided into seven major sections: the introduction; the concept and function of corporate governance; the role of disclosure in corporate governance frameworks; alternative regulatory theories including the use of corporate governance codes as informal regulation and informal law or soft law; the conceptual relationships between formal and informal law; comparative law and legal transplants, in particular the factors influencing successful transplantation of laws between legal systems, and, a conclusion.

Chapter 3: The internationalisation of corporate governance and the use of corporate governance codes in different jurisdictions – This chapter outlines the impact of globalization and internationalization on corporate governance requirements; the impact of economic crises on the appeal of corporate governance; developing a global corporate governance system; the use of corporate governance in different jurisdictions, in particular in South East Asian countries and between common law and civil law jurisdictions; the effective use of soft law and informal regulation in common law and civil law countries; and, a conclusion.

Chapter 4: Historical development of social and cultural values around business transparency in Indonesia – This chapter presents a historical background to practices of

²⁰⁹ A F Martin, *Methodology* (2008) University of Chester
<<http://chesterrep.openrepository.com/cdr/bitstream/10034/87076/4/chapter%204.pdf>>.

honesty and transparency from traditional commerce and enterprises practices through the colonial period to post independence and the present to identify contemporary ethical and moral attitudes which impact on corporate governance disclosure implementation. It also contains a conclusion.

Chapter 5: The challenges to disclosure in corporate governance in Indonesia context – This chapter considers local cultural and political factors, corporate governance concepts and international principles on disclosure as foreign ideas transplanted into the Indonesian legal, regulatory and business systems including in undermining their adoption and application, and, a conclusion.

Chapter 6: The use of the good corporate governance code for disclosure in Indonesia – This chapter discusses the basic framework for using corporate governance codes, the legal frameworks supporting codes, the impact of the good corporate governance codes on accountability for corporate disclosure, the role of government, the business community and NGOs in promoting the use of the code, and a conclusion.

Chapter 7: Results of field research and discussion – This chapter reports on the result of the field research. The analysis complements the findings in the other chapters.

Chapter 8: Conclusion – This chapter presents the conclusion drawn from the literature review, interviews and other sources including media data bases. These conclusions are used to answer the research questions. This chapter identifies the academic and practical contributions the research has made, their strengths and weaknesses as well as possible issues for further research. This is the final chapter that concludes this dissertation.

The last part of this dissertation contains the bibliography. The appendices follow.

1.6. Conclusion

This introductory chapter has highlighted the background, the importance and purpose of this study, the methodology used in the research and the structure of the thesis. The evidence of the effects of poor corporate governance, particularly disclosure, in Indonesia justifies the need to better understand it and to look for ways to better implement it and to improve standards and practices. Poor corporate governance has been identified as a significant contributing factor to the severe economic crisis of 1997 and remains a

potential source of future financial failures. The implementation of more effective corporate governance is crucial to secure Indonesia's economic development.

The formal legal system has failed as an effective way to implement more effective corporate governance disclosure. It has long been regarded as weak and corrupt and has lost its capacity, credibility and legitimacy. Significant law reforms around corporate governance and disclosure have not been effective due to persistent legal and cultural problems. The lack of law enforcement, pervasive corruption, and, poor business culture are deep rooted problems hindering the improvement of corporate governance disclosure based on formal law.

Seeking a solution to address weaknesses in formal law is crucial for Indonesia. Codes as informal rules have been seen as an alternative regulatory strategy to deal with the problems identified. This study seeks to ascertain whether informal rules may be used as a remedy for the problems in formal law in this context. Indonesia's Code of Good Corporate Governance is considered as a representation of these informal rules. That is why it has been chosen to be studied with respect to improving accountability for more effective disclosure.

In considering the complexity of the Indonesia context, a triangulation methodology has been chosen for the study. Three different sources of data have been used. This includes various primary sources of law including legislation and other regulations as well as the statements of soft law found in the Code of Good Corporate Governance. This is considered against the evidence of individual lived experiences, media data bases, and secondary literature identified in the literature review. This is an effective strategy to support the validity and reliability of the conclusions of the study.

The data of individual lived experiences was obtained through an empirical study undertaken in business and regulatory sectors using interviews. The other data was gathered from legal sources, secondary academic and related literature and from selected and credible media data bases. The next chapter covers the key sources used, the secondary literature reviewed in establishing the questions and the theoretical framework and research questions for this thesis.

Chapter 2 : Literature review

2.1. Introduction

The theoretical framework for this study and the research question and sub-questions are drawn from the literature review below. It covers selected relevant literature regarding the concept and role of corporate governance and disclosure, new and alternative regulatory theories, concepts relating to the relationship between formal and informal law as well as concepts from comparative law relating to legal transplants.

The concept of corporate governance seeks to contribute to corporate success through assisting business management in strategies to achieve a corporation's desired goals, in protecting shareholders' interests, and in supporting social and economic development. In particular, disclosure is perceived to be a fundamental element of a corporate governance system. The study considers how the concept and role of corporate governance is significant in assisting in understanding accountability for effective disclosure.

In alternative regulatory theories a corporate governance code may be used as a substitute for formal law by regulators. It may be seen by corporations as a way of avoiding a more expensive, difficult and corrupt legal regime. Governments may see it as an easy and politically popular way of quickly resolving difficult issues. It may also be used in the formal legal and regulatory systems as an adjunct to the formal legal regime. Alternative regulatory theories suggest that soft law may address core legal problems by filling gaps created by the failure of the formal legal and regulatory systems in Indonesia. Utilizing informal sanctions may be an effective deterrence to poor governance by damaging a company's reputation and eroding trust in it. These approaches suggest that such informal law may work effectively in Indonesia. In the context of corporate governance and disclosure there are a number of existing print and online media, NGOs, industry and professional associations that link into international networks which can also apply pressure to companies as well as to law and policy making and regulatory processes.

A number of the benefits of mixing formal and informal law claimed by some scholars may be applicable and contribute to more effective implementation of corporate

governance in Indonesia. When formal law is corrupt and the corporate governance framework is weak, informal law such as codes may supplement them to provide for better and more effective regulation. Such codes may offer some strategies and approaches to complement formal law so it is applicable and adaptable to real conditions. The involvement of both the public and private sectors is likely to be a better approach in Indonesia's context.

The experiences of some other South East Asian countries utilising legal and non-legal factors to achieve more effective implementation of corporate governance codes may also provide significant lessons for Indonesia. Concepts from comparative law including legal transplants may also be able to address the connection between law and various non-legal factors in successfully adopting and applying corporate governance codes as a foreign idea. The legal and cultural gaps between the donor legal systems which generated the 2004 OECD Principles of Corporate Governance and that of Indonesia will emerge as significant in this study. This requires consideration as to how to implement these concepts so that they may produce the same outcomes in Indonesia as they do in their donor jurisdictions.

2.2. The concept and functions of corporate governance

2.2.1. Introduction

Many writers argue that the corporation is the main pillar of the contemporary economy. It is an engine of economic growth, job creation, and innovation. Governance contributes and plays a central role in making corporations successful.²¹⁰ Keasey et al claimed that the successful operation of a company is a product of corporate governance.²¹¹

The concept of corporate governance has spread and been applied around the world including in Indonesia. It is seen as a significant instrument playing a pivotal function in economic development. The 2008 global financial crisis and the earlier Asian financial crisis of 1997 are claimed to reflect this role.²¹² The OECD justified reforms to corporate

²¹⁰ Holly Gregory, Gotshal Weil and LLP Manges, 'Preserving balance in corporate governance' on Corporate Governance and Financial Regulation, *The Harvard Law School Forum* (1 February 2013)

<<http://blogs.law.harvard.edu/corpgov/2013/02/01/preserving-balance-in-corporate-governance/#more-39681>>.

²¹¹ Cited in R Tomasic, *Corporate Governance: Challenges for China* (Law Press, China) 242.

²¹² Jang, above n 170.

governance because of the failure of corporate governance systems in these crises.²¹³ The failure included deficient governance structures²¹⁴ and non-transparency.²¹⁵

Reflecting these views, corporate governance is presented as a solution to preventing future crises. Some scholars claim that reinforcing corporate governance may improved recovery from any future crisis and assist in maintaining economic stability. It is argued that good corporate governance is required to restore confidence, improve regulation and promote trust.²¹⁶ In particular, two basic principles of corporate governance: transparency and accountability are claimed to be significant in building trust and confidence in investors.²¹⁷ These are crucial factors in attracting investment. Transparency, for example, is associated with creating stable and equitable economic systems.²¹⁸

The literature regarding corporate governance tends to adopt a broad or a narrow concept of what it is.

2.2.2. Broad and narrow concepts

Corporate governance, as a phrase, consists of two main concepts. *Governance* derives from the word *govern*, which means ‘to control a point in issue’.²¹⁹ Some scholars propose a wide view of what corporate governance is and others recommend a narrower one, but all share similar perspectives that its role is beneficial. The broader concept proposes significant economic and social advantages. The narrower concept emphasizes the benefits to the specific corporations and individuals associated with it. Both depict corporate governance as the application of effective managerial and control systems based on positive values.

²¹³ Organization for Economic Cooperation and Development, *Improving Corporate Governance Standards: the work of the OECD and the principles* <<http://www.oecd.org/dataoecd/45/24/33655111.pdf>>.

²¹⁴ H Kuroda, ‘Global Economic Governance, and Development’ (In High-Level Conference on Financial Crisis, New Delhi India, 2009) <<http://www.adb.org/Documents/Speeches/2009/ms2009005.asp>>.

²¹⁵ J E Stiglitz, *Towards a new global economic compact: Principles for addressing the current global financial crisis and beyond* <www.un.org/ga/president/63/interactive/gfc/joseph_p.pdf>.

²¹⁶ International Corporate Governance Network, *Statement on the Global Financial Crisis* (10 November 2008) <<http://www.iasplus.com/resource/0811icgn.pdf>>.

²¹⁷ Jang, above n 170.

²¹⁸ Stiglitz, above n 215.

²¹⁹ Bryan A Garner (ed), *Black’s Law Dictionary* (West Publishing) 715.

The World Bank, for example, has proposed a very broad definition of corporate governance as a mixture of law, regulation and voluntary private sector practices facilitating the attraction of financial and human capital, effective performance and long term economic values in a broad sense, not just for shareholders but also for society as a whole.²²⁰ Similarly the concept used by the Cadbury Committee proposed a balancing of economic and social objectives together with efficiency and accountability for resources should be the main concerns of corporate governance.²²¹ Wolfensohn, the former World Bank president, supported this wider notion of good social development, and wider ownership structures which reduced the centralisation of economic power to limited numbers of people. He also saw it as including support for capital markets development, the stimulation of innovation, enhancing long-term investment, eradicating conflicts and preventing runs on capital.²²² Tomasic proposes that corporate governance consists of an interrelated set of mechanisms.²²³

Narrower concepts, as indicated see corporate governance as the application of effective and good managerial and control systems. The OECD, for example, describes corporate governance as the system by which business corporations are directed and controlled:

The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance.²²⁴

²²⁰ Cited in D Iona and R Gherghina, *Remarks on Corporate Governance Standards and Their Importance* (2007)

<http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1347650>.

²²¹ University of Technology Sydney, Centre for Corporate Governance, *Corporate Governance: The Significance of Corporate Governance* (2007)

<http://www.ccg.uts.edu.au/corporate_governance.htm>.

²²² Cited in Ardiansyah A Fajarii, 'Good corporate governance, Sebuah keharusan [Good corporate governance is a must], *Kompas* (online), 15 April 2004 <<http://www.kompas.com/kompas-cetak/0404/15/ekonomi/970871.htm>>.

²²³ Tomasic (ed), *Corporate Governance*, above n 211, 12–13.

²²⁴ Organization for Economic Co-Operation and Development (OECD), *the OECD Principles of Corporate Governance 2004* <<http://www.oecd.org/dataoecd/32/18/31557724.pdf>>.

Corporate governance is seen as a monitoring system dealing with company decision-making particularly utilizing financial reports as the controlling mechanism.²²⁵ Perhaps influenced by the OECD's perspective the Indonesian Finance and Development Supervisory Agency describes corporate governance as a set of principles concerned with the governing of companies. It notes, however, that the application of corporate governance requires commitment, rules and business activities that are healthy and ethical.²²⁶

Economists have tended to see corporate governance as a solution to the agency costs in corporations.²²⁷ They have emphasised corporate governance as 'a set of mechanisms through which outside investors protect themselves against expropriation by the insiders' – i.e. steal the profits, sell the output or the assets of the firm they control, installing unqualified family members in managerial position, or overpaying executives.²²⁸ They also tend to see its objective as creating added value to the shareholders including easier to raise capital, lower capital costs, improved business and economic performance and with a positive impact on share prices.²²⁹

The narrower perspective of corporate governance found in the 2004 OECD Principles of Corporate Governance is now introducing a revised version in 2015 under the name of G20/OECD Principles of Corporate Governance.²³⁰ The model has assisted legislators and regulators in both OECD and non OECD countries, G20 countries, in establishing corporate governance. The new revision extends its suggestion for policymakers to raise awareness of good corporate governance for smaller and unlisted companies. This new model aims to assist 'policymakers evaluate and improve the legal,

²²⁵ J Dine and M Koutsias, *Company law* (6thed, 2007) 141.

²²⁶ Badan Pengawasan Keuangan dan Pembangunan [Indonesian Finance and Development Supervisory Agency], *Good corporate governance* [4] <<http://www.bpkp.go.id/dan/konten/299/Good-Corporate.bpkp>>.

²²⁷ Rafael La Porta et al, 'Investor Protection: Origins, Consequences, Reform' (Financial Sector Discussion Paper No.1, World Bank, September 1999) 1 <http://www1.worldbank.org/finance/assets/images/Fs01_web1.pdf>.

²²⁸ Ibid.

²²⁹ Forum Corporate Governance Indonesia [FCGI], *What is corporate governance* (2006) <<http://www.fcgi.or.id/>>.

²³⁰ Organization for Economic Co-operation and Development (OECD), *2014-2015 Review of the OECD Principles of Corporate Governance* <<http://www.oecd.org/corporate/2014-review-oecd-corporate-governance-principles.htm>>; Organization for Economic Co-operation and Development (OECD), *G20/OECD Principles of Corporate Governance*, below n 231, 4 & 9.

regulatory, and institutional framework for corporate governance, with a view to support economic efficiency, sustainable growth and financial stability'.²³¹ The 2004 model has six recommended principles, namely: ensuring the basis for an effective corporate governance framework, the rights of shareholders and key ownership functions, the equitable treatment of shareholders, the role of stakeholders in corporate governance, disclosure and transparency, and, the responsibilities of the board. The 2015 model has remained six principles but it has a new additional principle. The second and the third principles have been combined so that it becomes 'the rights and equitable treatment of shareholders and key ownership functions'. The new third principle as a new principle becomes 'institutional investors, stock markets, and other intermediaries'.²³² The OECD believes that the implementation of these principles has a major impact on growing financial markets, increasing investment and economic growth.²³³ The principles have become the universal standard for policy makers, investors, corporations and other stakeholders all over the world. Monks and Minow confirm the OECD Corporate Governance principles declaration of minimum acceptable standards for companies and investors around the world.²³⁴

2.2.3. The function of corporate governance

The effective implementation of corporate governance in Indonesia may potentially contribute to stabilizing and improving economic growth as the OECD has claimed.²³⁵ This not only applies to Indonesia. There are claims that the failure to implement good corporate governance contributed to the Asian currency crisis in 1997 and the 2008 global financial crisis. Jang, for example, claimed that the failure of corporate governance practices led to

²³¹ Organization for Economic Co-operation and Development (OECD), *G20/OECD Principles of Corporate Governance – OECD Report to G20 Finance Ministers and Central Bank Governors*, September 2015 <<https://www.oecd.org/daf/ca/Corporate-Governance-Principles-ENG.pdf>>.

²³² Ibid.

²³³ Organization for Economic Co-Operation and Development, *the OECD Principles of Corporate Governance 2004*, above n 224.

²³⁴ R A G Monks & N Minow, *Corporate Governance* (Blackwell Publishing, 3rd ed, 2004).

²³⁵ Helen Cabalu, 'Reforms in corporate governance in Asia after the financial crisis' (2005) 11 *Advances in Financial Economics* 51 <http://www.researchgate.net/publication/241418056_REFORMS_IN_CORPORATE_GOVERNANCE_IN_ASIA_AFTER_THE_FINANCIAL_CRISIS>.

the first crisis.²³⁶ Kuroda and others blamed deficient governance structures issues for the second crisis.²³⁷

Stiglitz believed that the problem was that specific corporate governance practices failed to ensure transparency.²³⁸ The OECD also found that existing standards failed to provide checks and balances that corporations need in order to cultivate sound business practices.²³⁹ In response to these perceived failures, in 2010, the OECD introduced a set of ambitious action plans for improvements in priority areas such as remuneration, risk management, board practices and the exercise of shareholders rights. These recommendations address how the implementation of the already-agreed standards can be improved.²⁴⁰

Reflecting on these opinions regarding the cause of the crises better corporate governance was suggested as a way to resolve the causes and maintain economic stability. Improved corporate governance was seen to have the power to restore confidence and prevent the erosion of trust.²⁴¹ In particular, two basic principles of corporate governance, transparency and accountability, were identified as essential in rebuilding and maintaining trust and confidence in investors.²⁴² They were seen as crucial factors in attracting investment. Transparency, for example, was identified as having the potential to create a more stable and equitable financial system.²⁴³ Accountability through appropriate corporate governance was seen to have the potential to restore confidence and prevent regulatory failure.²⁴⁴

²³⁶ Jang, above n 170.

²³⁷ Kuroda, above n 214; Organization for Economic Cooperation and Development, *Improving Corporate Governance Standards: the work of the OECD and the principles*, above n 213.

²³⁸ Stiglitz, above n 215.

²³⁹ Organization for Economic Co-operation and Development, *Corporate governance and the financial crisis*, [1] <<http://www.oecd.org/daf/ca/corporategovernanceprinciples/corporategovernanceandthefinancialcrisis.htm>>.

²⁴⁰ Ibid [2].

²⁴¹ International Corporate Governance Network, above n 216.

²⁴² Jang, above n 170.

²⁴³ Stiglitz, above n 215.

²⁴⁴ International Corporate Governance Network, above n 216.

Corporate governance is seen to have three broad functions: investor protection, improving economic performance, and, contributing to social development as described below.²⁴⁵

2.2.3.1. Protection of Investors' legal and other interests

Shleifer and Vishny claim, on the basis of empirical research, that good corporate governance rests on the legal protection of investors' interests and the return to them on their investment.²⁴⁶ In particular investors' interests must be protected from detrimental actions by insiders.²⁴⁷ Wilmot adds that good corporate governance 'limits the risk of serious fraud which is endemic within the business environment'.²⁴⁸

A number of studies indicate how such protection is required in the context of shares and other investments in firm and board performance.²⁴⁹ Such protection is particularly important where there is a restructuring or the need to resolve competing financial claims.²⁵⁰ In this way it is an instrument for shareholders to ensure that they get an appropriate return on their financial investment²⁵¹ as Keasey et al point out.²⁵² Through improving the liquidity of the market in the company's shares, good governance makes it easier for investors to sell their shares.²⁵³

Good governance also benefits other stakeholders' interests including the government.²⁵⁴ It has also been claimed as 'a safeguard against business failure',²⁵⁵ as the corporate governance framework evolves into a communication tool between companies

²⁴⁵ Organization for Economic Co-Operation and Development (OECD), *the OECD Principles of Corporate Governance 2004*, above n 224.

²⁴⁶ Andrei Shleifer and Robert W Vishny, 'A Survey of Corporate Governance' (1997) LII(2) *Journal of Finance* 737, 737.

²⁴⁷ La Porta et al, 'Investor Protection: Origins, Consequences, Reform', above n 227.

²⁴⁸ Cited in Ciaran Ryan, *Corporate governance is about collaboration, not annual reports* <www.btimes.co.za/top100/t29.htm>.

²⁴⁹ Organization for Economic Co-Operation and Development (OECD), *the OECD Principles of Corporate Governance 2004*, above n 224; Classens and Fan, above n 60.

²⁵⁰ La Porta et al, 'Investor Protection: Origins, Consequences, Reform', above n 227.

²⁵¹ Shleifer and Vishny, above n 246.

²⁵² Tomic, *Corporate Governance*, above n 211, 242.

²⁵³ Forum corporate governance Indonesia [FCGI], *What is corporate governance*, above n 229.

²⁵⁴ Tomic, *Corporate Governance*, above n 211, 242–43.

²⁵⁵ Ryan, above n 248.

and stakeholders with respect to strategic and operational goals.²⁵⁶ Sough claimed that the outcome of this framework creates better relations with shareholders, trading partners, staff, and better compliance with laws and regulations.²⁵⁷

2.2.3.2. Improved business and economic performances

Some wider benefits have been suggested for the benefit of corporations as the previous comment suggests. In addition to better relationships with stake holders corporate governance systems can assist business corporations attain their competitive goals,²⁵⁸ make it easier to raise capital, lower capital costs, improve business and economic performance, and have a positive impact on share prices,²⁵⁹ as well as improve firm performance through board structure.²⁶⁰ As indicated above good business management practices²⁶¹ may create an attractive business environment for investors.²⁶²

The OECD supports the view that good corporate governance improves corporate competitiveness and the value of investments.²⁶³ This is supported by a number of studies that also appear to show that good corporate governance promotes increased dispersed ownership of shares, greater efficiency in investment allocation and improved capacity for restructuring in a crisis.²⁶⁴

The International Finance Corporation (IFC) suggests that corporate governance ‘is a key factor in the ability of a country to have a conducive and attractive investment climate’.²⁶⁵ Investment is a powerful driver for economic growth.²⁶⁶ The quality of

²⁵⁶ Eva Parum, ‘Does Disclosure on Corporate Governance Lead to Openness and Transparency in How Companies are Managed?’ (2005) 13 *Corporate Governance* 702, 702.

²⁵⁷ Sough cited in Ryan, above n 248.

²⁵⁸ Organization for Economic Co-Operation and Development (OECD), *the OECD Principles of Corporate Governance 2004*, above n 224, 11.

²⁵⁹ Forum corporate governance Indonesia [FCGI], *What is corporate governance*, above n 229.

²⁶⁰ Eddy Wymeersch, ‘Enforcement of corporate governance codes’ (Law Working Paper No. 46/2005, June 2005) 6 <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=759364>.

²⁶¹ Sough, cited in Ryan, above n 257.

²⁶² Iona and Gherghina, above n 220, 1.

²⁶³ Organization for Economic Co-Operation and Development (OECD), *the OECD Principles of Corporate Governance 2004*, above n 224, 3

²⁶⁴ Rafael La Porta et al, ‘Investor Protection: Origins, Consequences, Reform’, above n 227, 11–15.

²⁶⁵ International Financial Corporation, *Factsheet: The Indonesia Corporate Governance Roadmap and Manual* (February 2014) 1

corporate governance standards and practices is related to the development and sustainability of capital markets.²⁶⁷

2.2.3.3. Contributing to social development

A number of extensive claims have been made of wider social and community benefits from improved corporate governance. The International Finance Corporation (IFC) suggests that corporate governance 'is a key factor in the ability of a country to have a conducive and attractive investment climate'.²⁶⁸ The quality of corporate governance standards and practices is seen to be directly related to the development and sustainability of capital markets.²⁶⁹ As already indicated wider benefits from good corporate governance have been suggested. As noted earlier, Wolfensohn observed that good corporate governance contributes to social development, a wider ownership structure in companies, and a greater dispersal of power throughout society. He also saw it as including support for capital markets development, the stimulation of innovation, the reduction in social conflict, enhancing long-term investment and the prevention of potential flights of capital.²⁷⁰

2.2.4. Disputed roles of corporate governance in economic and legal development

Notwithstanding these claims the role of good corporate governance in general and of law in particular in economic development remains contested. La Porta et al's prescription of United States or common law style protection for investors as a necessary element for economic growth, for example, has been challenged by a number of writers. It relates to older arguments over the relationship between the rule of law and economic development that is discussed below in the context of the comparative law literature. Milhaupt and Pistor, for example, in disputing La Porta et al's conclusions argue that it is difficult to generalize across economies and jurisdictions and their different cultures and histories. They claim that there is a 'rolling relationship between law and the economy

<<http://www.ifc.org/wps/wcm/connect/acd25a0042e8cf29af60ef384c61d9f7/CG+Roadmap+and+Manual+Factsheet.pdf?MOD=AJPERES>>.

²⁶⁶ Organization for Economic Co-operation and Development (OECD), *G20/OECD Principles of Corporate Governance*, above n 231, 3.

²⁶⁷ International Financial Corporation, *Factsheet: The Indonesia Corporate Governance Roadmap and Manual*, above n 265.

²⁶⁸ Ibid.

²⁶⁹ Ibid.

²⁷⁰ Cited in Fajarii, above n 222.

which varies between developed countries’.²⁷¹ This suggests that the implementation of good corporate governance also varies between countries and that Indonesia must choose its own path. The 2015 G20/OECD Principles of Corporate Governance suggests that ‘[e]ffective corporate governance requires a sound legal, regulatory and institutional framework that market participants can rely on’.²⁷² Ramsay identified that the successful application of corporate governance depends on a number of factors such as culture, ownership structures, business circumstances, competitive conditions and corporate life cycles.²⁷³

Chapter 4 discusses the historic experiences and cultural values of Indonesians and their potential to promote greater disclosure and transparency in corporate governance. Part 2.5 below discusses the differences between formal and informal law in which cultural issues are also significant.

It has been commonly observed that the effectiveness of corporate governance practices depends on several factors. ‘One size does not fit all’ is a term used to recognise the variety of good corporate governance principles potentially applicable.²⁷⁴ It is generally considered that the prescriptions for good corporate governance should take the form of recommendations with flexibility or discretion seen in “comply or explain” approaches. It permits principles to be adapted to the specific company’s circumstances.²⁷⁵

A number of scholars observe that cultural factors are particularly significant issues. Iu and Battern observe that national culture can be a challenge to the application of

²⁷¹ Curtis J Milhaupt and Katharina Pistor, *Law and Capitalism: What Corporate Crises Reveal About Legal Systems and Economic Development Around the World* (University of Chicago Press, 2008).

²⁷² Organization for Economic Co-operation & Development (OECD), *G20/OECD Principles of Corporate Governance*, above n 231, 13.

²⁷³ I Ramsay (ed), *Key Development in Corporate Law and Trusts Law* (LexisNexis Butterworths, 2002).

²⁷⁴ Gregory, Weil and Manges, above n 210, 68.

²⁷⁵ ASX Corporate Governance Council, *Corporate governance principles and recommendations with 2010 amendments 2nd edition*, Australian Securities Exchange, 5 <http://www.asx.com.au/documents/asx-compliance/cg_principles_recommendations_with_2010_amendments.pdf>.

governance principles.²⁷⁶ Hofstede describes national cultures as having six dimensions. These are: power distance (the less powerful members of organizations and institutions like family accept and expect that power is distributed unequally); individualism (the opposite to collectivism); masculinity (the opposite to femininity);²⁷⁷ uncertainty avoidance (a social tolerance for uncertainty and ambiguity); long term orientation (maintaining links with the past while dealing with the challenges of the present); and, indulgence (level of restrictions on enjoying life and having fun). In the context of disclosure, power distance, uncertainty avoidance, and individualism in particular affect its practices. Gray suggests that uncertainty avoidance affects perceptions in accounting practices around the significance of disclosure. It relates to four values, ie, professionalism versus statutory control, uniformity versus flexibility, conservatism versus optimism, and secrecy versus transparency.²⁷⁸ Gray also related uncertainty avoidance to the power distance dimension. He considered that societies with high power distances maintain secrecy or restrictions on information in order to preserve power inequalities.²⁷⁹

Other factors such as a commitment to the application of rules and business activities in healthy and ethical ways have been claimed to be responsible for improved corporate governance.²⁸⁰ In particular in emerging markets, Dallas demonstrated that the quality of public governance, including law enforcement and corruption; the incentives for and the quality of government officials and regulators; product market competition; financial market development; and ownership structures are significant factors in shaping

²⁷⁶ Justin Iu and Jonathan Batten, 'The implementation of OECD corporate governance principles in post-crisis Asia' (2001) 4 *Journal of Corporate Citizenship* 47, 51.

²⁷⁷ Geert Hofstede and Gert Jan Hofstede, *Dimensions of national cultures* <<http://geerthofstede.nl/dimensions-of-national-cultures>>.

²⁷⁸ S J Gray, *Towards a theory of cultural influence on the development of accounting systems internationally*, 8 <<http://www.acis.pamplin.vt.edu/faculty/tegarden/5034/handouts/Gray-Abacus-1988.pdf>>.

²⁷⁹ *Ibid.*

²⁸⁰ Indonesian Finance and Development Supervisory Board [Badan Pengawas Keuangan dan Pembangunan – BPKP] <<http://indonesia.go.id/en/lpnk/badan-pengawasan-keuangan-dan-pembangunan/2457-profile/372-badan-pengawasan-keuangan-dan-pembangunan>>.

corporate governance.²⁸¹ This is confirmed by other studies finding that legal institutions, politics, and history are also significant in corporate governance.²⁸² Local forces have been observed as significant in the success of corporate governance implementation. Olin observed that perceived moral hazards have also been identified as a decisive factor in corporate governance.²⁸³ For Indonesia, corruption in its political, legal and economic systems is a fundamental factor hindering corporate governance. It extends to how laws are written as observed by Immordino and Pagano.²⁸⁴

With respect to corporate disclosure, the efficiency of regulatory and judicial procedures and enforcement, as well as national cultures, affect the level of disclosure.²⁸⁵ Cultural dimensions are observed by a number of scholars as significant factors in this.

Hope's study, covering 42 countries, concluded that the differences between cultures were a valid determinant of the level of disclosure. The study demonstrated that the legal system type and other cultural variables were consistently associated with different levels of corporate disclosure.²⁸⁶ Individualism, for example, is positively associated with

²⁸¹ George Dallas, 'Corporate governance in emerging markets' on *Corporate Governance, the Harvard Law School Forum* (August 24, 2011) <<http://blogs.law.harvard.edu/corpgov/2011/08/24/corporate-governance-in-emerging-markets/>>.

²⁸² P Cornelius, 'Good corporate practices in poor corporate governance systems: Some evidence from the Global Competitiveness Report' (Working Paper No. 131, Columbia Law School, Center for Law and Economic Studies New York) <<http://www.eabis.org/responding-to-societal-expectations/responding-to-societal-expectations/good-corporate-practices-in-poor-corporate-governance-systems-some-evidence-from-the-global-competi/details.html>>.

²⁸³ Brian Olin, *Corporate Fraud and the Impact of Sarbanes-Oxley* (9 May 2005) 3, 6 & 7 <www.pugetsound.edu/files/.../1359_CorporateFraudandtheImpact.doc>.

²⁸⁴ Cited in Ira M Millstein et al, 'Enforcement and Corporate Governance: Three Views' on *Global Corporate Governance Forum* Focus 3, 53 <http://www.ifc.org/wps/wcm/connect/6ab71c8048a7e7b3accfef6060ad5911/Focus_ENFCorpGov3.pdf?MOD=AJPERES>.

²⁸⁵ Farina Vincenzo, 'Corporate disclosure determinants: a cross-country investigation' (Munich Personal RePEc Archive (MPRA) Paper No.5676, posted 9 November 2007) <<http://mpra.ub.uni-muenchen.de/5676/>>.

²⁸⁶ Cited in Richard D Morris, Isabelle Susilowati and Sidney J Gray, *The impact of IFRS adoption versus non-adoption on corporate disclosure levels in the Asian region* (July 2012) University of South Australia, 4-5 <<http://www.unisa.edu.au/Global/business/centres/cags/docs/seminars/GRAY%20PAPER%20MorrisSusilowatiGrayImpactofIFRSonDisclosureinAsianRegion%20July2012.pdf>>.

corporate disclosure, confirming that culture is an important explanatory factor for disclosure level.²⁸⁷

This literature suggests that these factors are significant issues that need to be addressed in the Indonesian context in considering the role of disclosure in its corporate governance system.

2.3. The role of disclosure in corporate governance frameworks

Generally, disclosure is defined as the ‘act or process of making known something that was previously unknown’.²⁸⁸ In the context of corporate governance and corporate disclosure it refers to the fact of disclosing any information concerning a company, whether on a voluntary or on a statutory basis.²⁸⁹

Disclosure is one essential pillar of a good corporate governance system. Many scholars acknowledge that disclosure is the key factor in corporate governance and at the heart of corporate accountability and as such, its most important element.²⁹⁰ It is one of the main concerns for investors regarding corporate governance and relates to their other concerns with transparency.²⁹¹

The level of disclosure in jurisdictions is measured by elements such as the ‘existence of the obligation to report all the events considered relevant for investors [information on family, indirect ownership, beneficial ownership and voting agreement between shareholders]; recourse to auditing companies from outside the enterprises; and the level of company-related information available on the market’.²⁹²

In general, disclosure is most likely required in listing rules of exchanges as one of central principles of corporate governance. For example, the Australian Securities Exchange (ASX) Listing rule 4.10.3 requires each entity to include in its annual report a

²⁸⁷ Vincenzo, above n 285.

²⁸⁸ Garner, above n 219.

²⁸⁹ World Bank, *ROSC – Indonesia*, above n 49.

²⁹⁰ Porter cited in D A Bavly, *Corporate Governance and Accountability: What Role for the Regulator, Director and Auditor?* (Quorum Books, 1999); J Salomon, *Corporate Governance and Accountability* (John Wiley & Sons, 2004).

²⁹¹ Directorate for Financial and Enterprise Affairs, *A framework for Investment Policy Transparency*, OECD, Abstract <<https://www.oecd.org/investment/investment-policy/16793978.pdf>>.

²⁹² World Bank, *ROSC – Indonesia*, above n 49.

disclosure of whether they follow the corporate governance recommendations set by the ASX Corporate Governance Council. Listed companies should disclose a number of matters relating to the board and senior management but in particular there should be timely and accurate disclosure of all material matters.²⁹³ In European countries the UK has the longest experiences with codes and related listing rules for the London Stock Exchange. The UK Cadbury Report suggested the ‘comply or explain’ used in its first corporate governance code. Other jurisdictions follow a similar pattern. In Italy, the *Preda* Report requires mandatory disclosure of compliance with the code as does Ireland through the IAIM guidelines adopted by the Irish Stock Exchange, Germany through the *Cromme* commission code and the Netherlands as a result of the Peters Report.²⁹⁴

Disclosure of information about listed corporations is significant in a number of theories relating to the corporation, its control and regulation as well as the efficiencies of securities markets.²⁹⁵ A number of efficacies have been attributed to disclosure. They include its role as a tool for corporate governance, transparency, efficiency, enhancing accountability, communication between management and investors, investor and shareholder protection, facilitating shareholder activism, attracting foreign capital, capital market stability and development, prevention of financial fraud, contributing to social benefits and as a tool for evaluating the enforcement of voluntary codes.

2.3.1. A tool for corporate governance

Disclosure is claimed to be an efficient corporate governance tool. Disclosure strengthens corporate governance. It assists directors to play their central roles.²⁹⁶ Frederik

²⁹³ ASX Listing Rules Guidance Note 9, *Disclosure of Corporate Governance Practices* (10 February 2013) 1–2

<http://www.asxgroup.com.au/media/PDFs/gn09_disclosure_corporate_governance_practices.pdf>.

²⁹⁴ Weil, Gotshal & Manges, *Comparative study of corporate governance codes relevant to the European Union and its member states* (Final report & Annexes I-III, 2002) 70

<http://ec.europa.eu/internal_market/company/docs/corpgov/corp-gov-codes-rpt-part1_en.pdf>

²⁹⁵ H G Manne, ‘Mergers and the Market for Corporate Control’ (1965) *Journal of Political Economy*, 73.

²⁹⁶ Porter cited in Bavly, above n 290.

argued that better disclosure may lead to better companies.²⁹⁷ Ramsey also claimed that disclosure may be used to monitor directors in applying corporate governance practices.²⁹⁸

2.3.2. A tool for transparency

Disclosure serves to establish market transparency and secure corporate accountability as demanded by corporate actors.²⁹⁹ Through disclosure of financial reporting, market transparency can be achieved.³⁰⁰ Financial reports are the instruments for controlling mechanisms in corporate governance systems.³⁰¹ They are also a mirror of management in that bad managers are likely to produce poor disclosure.³⁰²

In common law countries, corporate disclosure has been seen as an instrument contributing to market transparency, for the accountability of management to stakeholders and of the corporation itself to the public.³⁰³ Disclosure is a tool to determine whether the resources invested have been used to the best advantage or not.³⁰⁴ Transparency may also prevent fraudulent actions. The accountability brought about by it legitimates corporate power.³⁰⁵

2.3.3. A tool for efficiency

Disclosure is claimed to lead to efficiency. In economic theory disclosure is linked to the efficient use of corporate capital.³⁰⁶ It may increase capital markets' efficiency.³⁰⁷

²⁹⁷ R F Frederik, 'Disclosure: A Corporate Governance tool that really works?' (The third meeting of the Russian Corporate Governance Roundtable: The role of disclosure in strengthening corporate governance and Accountability, Moscow, 15–16 November 2000) 2 & 5.

²⁹⁸ Ian M Ramsey & Richard Hoad, 'Disclosure of Corporate Governance practices by Australian companies' (1997) 15(8) *Company and Securities Law Journal* <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=922779>.

²⁹⁹ Fiona Macmillan, 'Corporate disclosure on-line: An appropriate response to globalisation' (1998) 55 *University of New South Wales Law Journal*; (1998) 21 (2) *University of New South Wales Law Journal* 514, [49], [53] <<http://www.austlii.edu.au/au/journals/UNSWLJ/1998/55.html>>.

³⁰⁰ International Corporate Governance Network, above n 216.

³⁰¹ Dine and Koutsias, above n 225, 141.

³⁰² John F Olson, 'Looking beyond the efficient markets hypothesis: a comment on Professor Macey's post-Enron Analysis' (2004) 89 *Cornell Law Review* 527, 529.

³⁰³ Macmillan, Fiona, above n 299.

³⁰⁴ R W Gibson, *Disclosure by Australian companies* (Melbourne University Press, 1971) 5.

³⁰⁵ *Ibid.*

³⁰⁶ Manne, above n 295, 73.

³⁰⁷ Caruana cited in Vincenzo, above n 285.

Ogus supports Manne's view that proper disclosure of information creates efficiency.³⁰⁸ Frederik also argues that better disclosure contributes to a greater economic efficiency.³⁰⁹ Adequate disclosure should lower the costs of capital.³¹⁰ Voluntary disclosure has been found to have a positive correlation with increasing equity capital in listed Australian companies.³¹¹ Empirical research also shows that good disclosure has positive impacts elsewhere so that where there has been a greater level of disclosure there is greater efficiency in judicial recovery processes.³¹²

2.3.4. A tool for enhancing accountability

Corporate accountability means 'holding the management of an organization responsible for its performance, it entails making judgment on the proper use of executive power'.³¹³ One key reason for disclosure in corporate governance is enhancing companies' accountability by requiring them to establish their business aims and principles.³¹⁴ Disclosure also facilitates increased corporate accountability, and makes it easier for the company to become a global actor.³¹⁵

2.3.5. A communication tool between management and investors

Disclosure and financial reporting are widely seen as a potentially significant tool for 'management to communicate firm performance and governance to outside investors'.³¹⁶

³⁰⁸ A I Ogus, *Regulation: Legal Form and Economic Theory* (Hart Publishing, 2004)

³⁰⁹ Frederik, above n 297, 2,5.

³¹⁰ Jonathan R Macey, 'Efficient capital markets, corporate disclosure, and Enron' (2004) 89 *Cornell Law Review* 394, 411.

³¹¹ P Collet and S Hrazky 'Voluntary Disclosure of Corporate Governance Practices by Listed Australian Companies' (2005) 13(2) *Corporate Governance: An International Review*.

³¹² Vincenzo, above n 285.

³¹³ Bavly, above n 290.

³¹⁴ Parum, above n 256.

³¹⁵ Ibid.

³¹⁶ Paul M Healy and Krishna G Palepu, 'Information asymmetry, corporate disclosure, and the capital markets: a review of the empirical disclosure literature' (2001) 21 *Journal of Accounting and Economics* 405, 405 <<http://down.cenet.org.cn/upfile/36/2004121624112143.pdf>>.

2.3.6. Investor and shareholder protection

Disclosure is recognised as a key corporate governance protection for shareholders.³¹⁷ It is believed that disclosure is ‘an effective tool for improving investor protection’ and a powerful apparatus for monitoring the risks to which they are exposed.³¹⁸ Disclosure may increase investors’ confidence.³¹⁹ Financial reports have been seen as a significant protection for the interests of investors and creditors as disclosure should provide accurate and actual information concerning the economic and financial condition of businesses.³²⁰ The information assists investors in determining their decisions on investments.³²¹

It is a pivotal feature of market-based monitoring of corporate conduct and a powerful tool for influencing companies’ behaviour and for protecting investors.³²² Parkinson proposed that disclosure requirements may maximize shareholder wealth.³²³ Frederik also claims better disclosure generates wealth.³²⁴

At a wider level disclosure addresses information asymmetry in corporate relationships. Appropriate financial reporting and disclosure are essential to reduce information asymmetry.³²⁵ Improving disclosure reduces the unequal distribution of information between management and other stakeholders.³²⁶

³¹⁷ M Walsh, ‘Disclosure as an Aspect of Good Corporate Governance’ [2005] *International Company and Commercial Law Review* 16.

³¹⁸ Frederik, above n 297, 2.

³¹⁹ Caruana cited in Vincenzo, above n 285.

³²⁰ Vincenzo, above n 285.

³²¹ Porter cited in Bavly, above n 290.

³²² Hong Kong Society of Accountants, *Disclosure in annual reports: a guide to current requirements and recommendations for enhancement*, 5 <<http://www.hksa.org.hk>>.

³²³ J Parkinson, ‘Disclosure and Corporate Social and Environmental Performance: Competitiveness and Enterprise in a Broader Social Frame’ [2003] *Journal of Corporate Law Studies*, 3.

³²⁴ Frederik, above n 297.

³²⁵ Dariush Bahmani, ‘The relation between disclosure quality and information asymmetry: Empirical evidence from Iran’ (2014) 5(2) *International Journal of Financial Research* 110, 111 <<http://www.sciedu.ca/journal/index.php/ijfr/article/viewFile/4546/2627>>.

³²⁶ *Ibid* 110.

2.3.7. Facilitating shareholder activism

Disclosure has been claimed to have a key role in facilitating shareholder activism because it reduces information asymmetry and provides information which permits shareholders to take appropriate actions.³²⁷

2.3.8. Attracting foreign capital

Good disclosure is widely seen to attract capital.³²⁸ This follows from the previous claim regarding the confidence and trust the protection of investors generates.

2.3.9. Capital market stability and development

Disclosure is seen to play a crucial aspect in ensuring the stability and development of capital markets.³²⁹ Corporate disclosure plays an important role in their development and the credit activity of financial intermediaries.³³⁰ It also maintains confidence in capital markets.³³¹ Appropriate disclosure facilitates the regulation and supervision of financial services and assists in reducing the risks of future financial crises.³³²

2.3.10. Prevention of financial fraud

Simple, clear, and informative disclosure may prevent financial fraud. There are a number of examples where poor disclosure, including complicated and technical accounting creates a distorted view of the company and constitutes dishonesty. This includes the manipulation of information of off-balance sheets and other unintended use of accounting rules.³³³

³²⁷Arnold WA Boot, Jonathan R Macey and Anjolein Schmeits, *Towards a new theory of corporate governance: Objectivity versus Proximity* (2005) <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=686770>.

³²⁸Hong Kong Society of Accountants, above n 322; Macey, above n 310, 411; Mine H Aksu and Arman Kosedag 'Transparency and Disclosure Scores and their Determinants in the Istanbul Stock Exchange' (2006) 14 *Corporate Governance: An International Review* 277.

³²⁹Vincenzo, above n 285.

³³⁰Ibid.

³³¹Hong Kong Society of Accountants, above n 322.

³³²L A Turner, 'The financial crisis and the future of financial regulation' on *the Harvard Law School Forum* (2009) <<http://blogs.law.harvard.edu/corpgov/2009/02/04/-the-financial-crisis-and-the-future-of-regulation>>

³³³Macey, above n 310, 420.

2.3.11. Contributing to social benefits

Increased investment and more efficient use of capital lead to greater wealth and prosperity. Disclosure also encourages companies to address social concerns prior to any announcements.³³⁴ It helps to improve the public understanding of corporate structures and a company's activities, policies and performance.³³⁵ The disclosure of information to the market also permits social actors including communities and NGOs not focussed on the market to take political and legal actions to minimise harm.³³⁶

2.3.12. A tool for evaluating enforcement of voluntary codes

The disclosure system enables the market or interested parties to determine whether a company adheres to corporate governance code requirements or not.³³⁷ Disclosure is also a means to evaluate the effectiveness of voluntary codes based on the 'comply or explain' approach.

These claimed benefits of disclosure make it significant to improve a range of factors in Indonesia apart from corporate governance and regulation. In particular they could address issues of corruption and honesty. The OECD principles on disclosure require it to be:

timely and accurate; on all material matters of the corporation; in accordance with high quality standards of accounting and financial and non-financial disclosure; conducted by an independent, competent and qualified auditor.³³⁸

Navran and Pittman indicate that timely and accurate disclosure reflects values such as honesty.³³⁹ This is a crucial issue for Indonesia. These reasons for ensuring accurate disclosure are returned to in the context of Indonesia and other South East Asian

³³⁴ Parkinson, above n 323.

³³⁵ Hong Kong Society of Accountants, above n 322.

³³⁶ Parkinson, above n 323, 3–39.

³³⁷ Jeremy Cooper, Australian Securities & Investments Commission (ASIC), 'Corporate governance: an IOSCO perspective' (Paper presented at OECD-ADBI 8th round table Capital market reform in Asia, ADB Institute, Tokyo, 11 & 12 October 2006) 4 <[http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Corporate_Governance_IOSCO_Perspective.pdf/\\$file/Corporate_Governance_IOSCO_Perspective.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Corporate_Governance_IOSCO_Perspective.pdf/$file/Corporate_Governance_IOSCO_Perspective.pdf)>.

³³⁸ Organization for Economic Co-operation & Development, the OECD Principles of Corporate Governance 2004, above n 224.

³³⁹ Frank Navran and Edward L Pittman, *Corporate ethics and Sarbanes-Oxley* (31 December 2003) Ethics & Compliance Initiative <<http://www.ethics.org/resource/corporate-ethics-and-sarbanes-oxley>>.

jurisdictions in Chapter 3 which considers it in the context of the demands of corporate governance and the use of corporate governance codes.

The literature on alternative regulatory theories indicates that the use of alternative regulatory strategies including informal or soft law may improve accountability for effective disclosure.

2.4. Alternative regulatory theories

2.4.1. Introduction

Demand for governance without government has increased due to a rising interdependency among the members of international society and global civil society reflected in transnational organisations. In this context it has been observed that ‘the new regulatory mode is characterized as a soft law framework’.³⁴⁰ Many jurisdictions have increasingly migrated from hard to soft law due to costs, flexibility and risks. It is seen as associated with a greater emphasis on self-regulation. Voluntary instruments are promoted as enhancing flexibility, adaptability, and allowing experimentation and innovation in both internal and external compliance.³⁴¹

Soft law can be seen as a subcategory of informal law. The concept of soft law has been disputed in part on the positivist ground that law cannot be law without a sanction attached to its breach.³⁴² As it emerged in instruments in international law in the 1970s Weil observed that they “are neither ‘soft law’ nor ‘hard law’: they are simply not law at all.”³⁴³

Arend described soft law as:

“oxymoronic” and argued that “[i]f a rule meets the criteria for law, then it should be called ‘law.’ If, however, the rule is not binding—as soft law has been described to be—then it should not have law anywhere in its name.”³⁴⁴

³⁴⁰ Ulrika Morth (ed), *Soft Law in Governance and Regulation* (Edward Elgar Publishing, 2004) 1.

³⁴¹ Wymeersch above n 260, 20.

³⁴² L A Hart, *The Concept of Law* (2nd ed, 1994) 6.

³⁴³ Prosper Weil, ‘Towards Relative Normativity in International Law?’ (1983) 77 *American Journal of International Law* 413, 414–15.

³⁴⁴ Anthony Clark Arend, *Legal Rules and International Society* (Oxford University Press, 1999) 25.

More recently both in international law and also in regulatory studies it has been endorsed for its perceived usefulness.

The concept enables a different approach to influencing and controlling behaviour. It has been claimed to be more effective, flexible, relevant and responsive than formal law. Grabosky suggested other benefits in its use of the power of third parties to tackle enforcement actions on behalf of the state.³⁴⁵ It permits government as well as professional associations to advance systematic goals in a deliberate, measured, and context sensitive way.³⁴⁶ It can also become formal law at less cost by reducing the risk for error and opposition by trialing its principles and practices in a business context.³⁴⁷ It can spark discussions about what the formal law should be³⁴⁸ and also foreshadow what the formal law will be.³⁴⁹ The discussion in chapter six of the Indonesian Corporate Governance Code indicates that the soft law on disclosure has been taken up in the formal law of the Indonesia Stock Exchange.

Parker and Braithwaite, for example, support the use of soft law in an alternative approach to regulation by reference to the regulatory ‘trilemma’. The concept points to the choices which have to be made between the three pillars of regulation: effectiveness or the distinction between regulations in the book and in practice, responsiveness or the efficiency and practicability of compliance, and, coherence or the primacy of instrumentalist policy concerns in legislating for regulation.

This study examines this alternative regulatory concept employing new regulatory theories based on concepts selected from the relevant literature on [1] how regulatory discourse can be translated into business discourse in Indonesia, [2] the importance of

³⁴⁵ P N Grabosky, ‘Using Non-Government Resources to Foster Regulation Compliance’ (1995) 8 *Governance: An International Journal of Policy and Administration*.

³⁴⁶ John C Coffee Jr and Hillary A Sale, ‘Redesigning the SEC: Does the Treasury Have a Better Idea?’ (2009) 95 (4) *Virginia Law Review* 707, 750–52.

³⁴⁷ Kenneth W Abbott and Duncan Snidal, ‘Hard and Soft Law in International Governance’ (2000) 54 *International Organization* 421, 423, 434.

³⁴⁸ Seana Valentine Shiffrin, ‘Inducing Moral Deliberation: On the Occasional Virtues of Fog’ (2010) 123 *Harvard Law Review* 1214, 1231.

³⁴⁹ Jacob E Gersen and Eric A Posner, ‘Soft Law: Lessons from Congressional Practice’ (2008) 61(3) *Stanford Law Review* 573, 586 & 626.

informal sanctions and internalization of compliance which suggests that informal processes may be more significant than any deterrent in formal law, [3] the problems of creative compliance in regulatory communities, and [4], trust as a critical aspect of business regulation.

There is a relationship between formal and soft law. Soft law may even appear to be stated in a legislative way but contain no apparent sanction. It may duplicate obligations that already appear in formal law and therefore carry no additional sanctions. It may not constrain anyone at all. This last sense is found in voluntary corporate governance codes where the only constraint if they are not complied is that this is pointed out and an explanation offered. There is also a degree of cynicism associated with the use of soft law.³⁵⁰

The study considers and utilizes corporate governance codes as the alternative regulatory concept in the form of informal law in general and soft law in particular.

2.4.2. Corporate governance codes as informal regulatory concepts

2.4.2.1. Introduction

The effectiveness of corporate governance codes as informal and soft law that work effectively has been studied in several western jurisdictions but not Indonesia.³⁵¹ However, as Aguilera and Cuervo-Cazurra pointed out, there remains a divergence between the absence of the academic analysis of the effects of such codes and their increasing use.³⁵²

Some studies have demonstrated the effectiveness of informal law. One is an empirical review of the formal governance measures introduced by the US Sarbanes-Oxley Act of 2002 (SOX) that informal rules or norms have a positive effect on corporate governance.³⁵³ In Australia and New Zealand, codes and practical guidelines are claimed to support the best corporate governance practices and also provide solutions to the agency

³⁵⁰ Ibid. 'When law making authorities create laws that by their own terms or common understanding have no effect, one immediately suspects a cynical public-relations ploy'.

³⁵¹ A summary of the studies can be found in David Seidl, Paul Sanderson and John Roberts, 'Applying the 'comply-or-explain' principle: discursive legitimacy tactics with regard to codes of corporate governance' (2013) 17(3) *Journal of Management and Governance* 791, 800.

³⁵² Ruth V Aguilera and Alvaro Cuervo-Cazurra, 'Codes of Good Governance' (2009) 17(3) *Corporate Governance: An International Review* 376.

³⁵³ James A McConvill, 'Reflections on the Regulation of Contemporary Corporate Governance' (2006) 2 (1) *Corporate Governance Law Review* 1, 66.

cost problem.³⁵⁴ In the context of Israel, it is suggested that a code, used in a collaborative way between the state regulator and listed companies, may achieve a better outcome as the controllers of the company know what is best for them and it also promotes social good.³⁵⁵ Some research has looked at particular features of codes. A study by Sheridan *et al* on the corporate governance code in the United Kingdom demonstrated that the code increased the flow of news announcements by listed companies.³⁵⁶

In the context of Indonesia and the specific context of disclosure it has been found that the introduction of voluntary national governance codes had significant beneficial effects either directly or indirectly effect on company disclosure practices. The study was of eight East Asian countries – Hong Kong, Indonesia, Malaysia, the Philippines, Singapore, South Korea, Taiwan, and Thailand – during the period from 1993 to 2005. Specific sections that were designated to improve disclosure or information transparency were seen to be responsible for the improvement. The direct effect on company governance practices was seen and the indirect impact was an increase in board independence. It is also suggested that the availability of a code, in Indonesia's context, may be an effective way for the business community to respond to the state's failure to provide appropriate formal legal and regulatory systems.³⁵⁷

These justifications for alternative regulatory frameworks, as represented by codes, are supported by theoretical literature on such frameworks although, as Aguilera and Cuervo-Cazurra indicate more research is required.

2.4.2.2. *The role of corporate governance codes as informal regulation*

A number of efficacies have been attributed to corporate governance codes as informal regulation. They include: establishing good corporate governance practices, enhancing transparency, improving company reputation and performance, as an effective form of alternative regulation and as effective and efficient regulatory instruments.

³⁵⁴ R Grantham, 'Corporate Governance Codes in Australia and New Zealand: Propriety and Prosperity' (2004) 23 *Queensland Law Journal*.

³⁵⁵ U Procaccia, 'Crafting a Corporate Code From Scratch' (1996) 17 *Cardozo Law Review*.

³⁵⁶ L E Jones Sheridan and C Marston, 'Corporate Governance Codes and the Supply of Corporate Information in the UK' (2006) 14 *Corporate Governance: An International Review*.

³⁵⁷ A A Soetjipto, 'Legal Reform & Challenges in Indonesia' in Chris Manning and Peter van Diermen (eds), above n 9, 269–77.

a) *Establishing and addressing corporate governance practices*

It is claimed that corporate norms will enable the development of corporate governance practices. Norms are ‘observed behavioral regularities’.³⁵⁸ Rock and Wachter observe that ‘behavioral rules and standards for corporate actors are provided by corporate culture and are essentially norm-based’.³⁵⁹ They state:

Norms may help explain the manner in which the law, in the absence of bright line rules, influences corporate governance. Norms may also explain why standards rather than rules work well in a corporate setting.³⁶⁰

There is an issue with the relationship between informal law, including soft law, and norms. ‘Does soft law evolve into social norms or do social norms generate soft law?’³⁶¹ It appears to be accepted that norms and soft law are mutually reinforcing and develop in parallel.³⁶²

In this context of less formal standards it is argued that self-enforced regulation can establish good corporate governance practices.³⁶³ The self-regulatory nature of voluntary codes is considered to be an important characteristic for better regulating corporate governance.³⁶⁴ Such self-enforcing codes are also claimed to be able to address specific or targeted issues.

³⁵⁸ Edward B Rock and Michael L Wachter, ‘Symposium Norms and Corporate Law: Islands of Conscious Power: Law Norms and the Self-Governing Corporation’ (2001) 149(6) *University of Pennsylvania Law Review* 1619, 1641.

³⁵⁹ Edward B Rock and Michael L Wachter, ‘Norms & Corporate Law’ (2001) 149(6) *University of Pennsylvania Law Review* 1607, 1608.

³⁶⁰ *Ibid.*

³⁶¹ Morth, above n 340, 4.

³⁶² E Norman Veasey, ‘Should Corporation Law inform Aspirations for Good Corporate Governance Practices—or Vice Versa?’ (2001) 149 *University of Pennsylvania Law Review* 2179, 2189.

³⁶³ Soetjijto, above n 357, 18.

³⁶⁴ Ilir Haxhi and Ruth V Aguilera, ‘Are Codes Fostering Convergence in Corporate Governance? An Institutional Perspective’ in A Rasheed and T Yoshikawa (eds), *Convergence of Corporate Governance: Promise and Prospects* (Palgrave, 2012) 234, 239.

Bethoux et al found that compliance with codes of conduct, as voluntary initiatives within companies, became a means for companies to deal with specific issues and also assisted them in defining their corporate characteristics.³⁶⁵

Codes may better target specific problems compared with formal legal rules and principles.³⁶⁶ They may be necessary. Milstein *et al* claim that company and securities law and investor protection are forms of incomplete law in the sense that some contracts are incomplete as they fail to specify what happens in particular circumstances.³⁶⁷ They argued that law and regulation are unable to foresee all future contingencies. The law is only able to identify and cover some specific events beforehand. Xu and Pistor agree that law is incomplete when law fails to address the potentially harmful act.³⁶⁸ In contract law incomplete contracts are often described as dynamic contracts and missing rules need to be found from other sources. Monitoring and disclosure are significant in making them effective.³⁶⁹

Codes address essential governance issues, ie: fairness, accountability, transparency and responsibility. They may fill out incomplete formal rules in corporate and securities law³⁷⁰ for enhancing transparency and improving company reputation, reputation and efficiency.

(b) Enhancing transparency

Some scholars claim that corporate governance may increase transparency. Rapp et al, for example, argued that a corporate governance code may ‘increase transparency and

³⁶⁵ E C Didry Bethoux and A Mias, ‘What Codes of Conduct Tell Us: corporate social responsibility and the nature of the multinational corporation’ (2007) 15 *Corporate Governance: An International Review*, 77-88.

³⁶⁶ J M A E A Caral, ‘Lessons from ICANN: Is self-regulation of the Internet fundamentally flawed?’ (2004) 12 *International Journal of Law and Information Technology*.

³⁶⁷ Millstein et al, *Enforcement and Corporate Governance*, above n 284, 2

³⁶⁸ Chenggang Xu and Katharina Pistor, ‘Law Enforcement Under Incomplete Law: Theory and Evidence from Financial Market Regulation’ (Discussion Paper No. TE/02/442, London School of economics and Political Science, December 2002) 4 <http://eprints.lse.ac.uk/3748/1/Law_Enforcement_under_Incomplete_Law_Theory_and_Evidence_from_Financial_Market_Regulation.pdf>.

³⁶⁹ Gaetano Antinolfi and Francesco Carli, ‘Costly monitoring, dynamic incentives, and default’ (2015) 159 *Journal of Economic Theory* 105.

³⁷⁰ A Zattoni and F Cuomo, ‘Why Adopt Codes of Good Governance? A Comparison of Institutional and Efficiency Perspectives’ (2008) 16 *Corporate Governance: An International Review*.

put managers under external pressure to establish governance structures ...'. They argued that code compliance is always beneficial for shareholders and also mitigates the agency problem between manager and shareholder.³⁷¹ Similarly Carver also contends that codes may increase transparency and decrease conflicts of interest.³⁷²

(c) *Improving company reputation and performance*

Codes may also enhance a company's reputation and optimise its values for shareholders and other stakeholders and encourage them to work towards sustainable values and greater compliance with legal and regulatory requirements and, at the same time, increase investor confidence.³⁷³

Some scholars argue that voluntary codes lead to uniform structures that improve company performances by increasing shareholders' values.³⁷⁴

(d) *More effective and efficient regulatory instruments*

Some scholars consider informal law, represented by voluntary codes, as more effective and efficient than formal law. Among others, McConvill suggested that informal rules are more flexible, relevant and responsive compared with formal law which may adversely affect business practices because of its legalistic inflexibilities and costs.³⁷⁵ The distinctions between formal and informal law is discussed below in sub-section 2.5.2.

Curtis and Caral also suggested informal law benefits both business and its regulation through its 'flexibility, responsibility, relevancy and effective ... regulation',³⁷⁶ providing self-enforcement, expert skills, quick, efficient and less formal processes and low costs.³⁷⁷ It is less burdensome and costly compared with formal corporate governance

³⁷¹ Marc Steffen Rapp, Thomas Schmid and Michael Wolff, *Hard or Soft Regulation of Corporate Governance?*, 3, 17 <<http://ssrn.com/abstract=1930847>>.

³⁷² J Carver, 'The Promise of Governance Theory: beyond codes and best practices (2007) 15 *Corporate Governance: An International Review*.

³⁷³ Organization for Economic Co-operation and Development, *the OECD Principles of Corporate Governance 2004*, above n 224.

³⁷⁴ P Burton, 'Antecedents and Consequences of Corporate Governance Structures' (2000) 8 *Corporate Governance: An International Review*.

³⁷⁵ McConvill, above n 353, 18.

³⁷⁶ K Curtis, 'The Important of Self-Regulation in the Implementation of Data Protection Principles: The Australian Private Sector Experience' (Paper presented at the 27th International Conference of Data Protection and Privacy Commissioners, 2005).

³⁷⁷ Caral, above n 366.

rules.³⁷⁸ Other scholars noted that informal mechanisms are more efficient in relation to the costs of complying with them as opposed to complying with formal ones,³⁷⁹ with the US experience demonstrating the high level of burdens and costs in using a formal legal approach.³⁸⁰ The voluntary codes promote flexibility that allows companies to apply best practice and allow for company particularities.³⁸¹

Codes are also seen to promote a flexible and responsive approach to regulation. Responsive regulation is a concept developed by Gunningham and Grabosky in the context of smart regulation.³⁸² It draws on both informal law and soft regulation as part of its repertoire of approaches that are responsive to specific contexts in its search for effective and efficient practices in utilizing a wide range of policy approaches and regulatory actors.³⁸³ It is a concept widely used in contemporary regulation. The Canadian government, for example, claims that it use by its agencies is relevant, fair and transparent and leads to cooperation between the regulator and the regulated community at a number of levels.³⁸⁴

³⁷⁸ Ibid 18.

³⁷⁹ Claudia W Williamson and Carrie B Kerekes, *Securing private property: formal versus informal Institutions* <<http://www.jstor.org/discover/10.1086/658493?sid=21106168301513&uid=2&uid=4>>.

³⁸⁰ Wymeersch, above n 260, 21.

³⁸¹ Haxhi and Aguilera, above n 364, 239.

³⁸² Smart regulation focuses on closing the policy gap, investing more in policy evaluation and simplification. See, Marianne Klingbeil, *Smart Regulation*, Organisation for Economic Co-operation and Development, 2 <<http://www.oecd.org/regreform/policyconference/46528683.pdf>>. See also, External Advisory Committee on Smart Regulation, *Smart Regulation – Report to the Government of Canada* (2004) 12–13 <<http://publications.gc.ca/collections/Collection/CP22-78-2004E.pdf>>. There are three key characteristics of smart regulation i.e. both protecting and enabling (using the regulatory system to generate social and environmental benefits while enhancing the conditions for a competitive and innovative economy that will attract investment and skilled workers; more responsive regulation (self-renewing and keeping up with developments in science, technology and global markets); governing cooperatively for the public interests (sharing responsibility in which governments, citizens and industry all have an active role to play in making the system more effective).

³⁸³ N Gunningham and P Grabosky, *Smart Regulation: Designing Environmental Policy* (Clarendon Press, 1998).

³⁸⁴ Government of Canada, *Smart Regulation; A Regulatory Strategy for Canada* <www.regulation.gc.ca/docs/report1/faq-e.pdf>.

Formal law, by way of contrast, has been depicted, in the context of developed economies and legal systems, as marked by certainty and uniformity³⁸⁵ with compliance unproblematic because ‘formal law always implies the use of government power’.³⁸⁶ Formal law has been identified as having some significant problems include legalism and rigidity, which affects enforcement, over and under inclusiveness, vagueness, indeterminacy, and interpretative dilemmas.³⁸⁷ It has been pointed out that state regulation is reactive and often slow in responding to new sources of harm.³⁸⁸ Koutalakis also adds that the complexity of relevant laws and policies, uncertainty over regulatory goals and desirable outcomes and high levels of interdependence between multiple public and private actors produce uncertainty in legal and regulatory systems. It is argued, and not just in the context of incomplete contracts referred to above, that law always has gaps which need to be filled.³⁸⁹

Aldashev et al argued that there are other factors which contribute to a lack of recognition and enforcement of formal law. The law fails to fulfil the expectations that have been established in the past. The formal law may be ambiguous and this may lead to multiple interpretations. Another concern points to uncertain sanctions. When the formal law is seen to be unenforceable or unenforced it is claimed to be a ‘dead letter’. They argue that here other forms of law, including customary and informal law, may exist and produce different outcomes.³⁹⁰

Formal corporate law and securities regulation with their characteristics of formality and sophisticated complexity have been historically unable to prevent corporate misconduct or collapses.³⁹¹ These issues led to the search for alternative forms of regulation.³⁹² These

³⁸⁵ Julia Black, *Rules and Regulators* (Clarendon Press, 1997) 20.

³⁸⁶ M E Price and S G Verhulst, *Self-Regulation and the Internet* (Kluwer Law International, 2005).

³⁸⁷ Black, *Rules and Regulators*, above n 385, 7–12.

³⁸⁸ Parkinson, above n 323.

³⁸⁹ Koutalakis and Buzogany, below n 392.

³⁹⁰ Gani Aldashev et al, *An economic analysis of legal pluralism* <www.isnie.org/assets/files/.../platteau.pdf>.

³⁹¹ McConvill, above n 353.

³⁹² Charalampos Koutalakis and Aron Buzogany, *When soft law hits hard. On the effectiveness of new regulatory approaches in pollution prevention and control in the EU*, 2 <<http://regulation.upf.edu/dublin-10-papers/4C1.pdf>>.

were said to be found in self regulatory and voluntary codes. It was claimed by the discoverers that these forms effectively worked with support from management, administrative and political processes.³⁹³ Maassen, for example, claimed that self-regulation is the most important development in the European Union in response to corporate governance.³⁹⁴ This kind of self regulation has been described as ‘forms of interaction between community processes and private actors...’³⁹⁵

(e) An alternative regulatory strategy for developing countries

Alternative regulation is dependent on informal law of soft law. As indicated they came to be seen to be an alternative tool when formal rules appeared to fail in their functions. In developing countries with weak enforcement environments, Berglof and Claessens believe that voluntary codes are the key to establishing good corporate governance.³⁹⁶ Williamson has also argued that developing countries with ‘predatory government’ may benefit from employing informal institutions.’³⁹⁷

The effective implementation of voluntary codes in Indonesia may contribute to stabilizing and improving economic growth as good corporate governance is recognised as essential for economic growth.³⁹⁸ This is not only true of Indonesia. There are claims, as already indicated, that corporate governance failures were a major cause of the 2008 global financial crisis. Amongst others Kuroda, Stiglitz and the OECD have blamed deficient governance structures within corporate enterprises.³⁹⁹ Jang affirms this and also claims that the failure of corporate governance was the root cause of the Asian financial crisis in

³⁹³ Ibid.

³⁹⁴ G Maassen, Rotterdam School of Management Erasmus University Rotterdam the Netherlands ‘Corporate Governance developments in Europe: What are the opportunities for Indonesia?’ (Paper presented at National Conference on Corporate Governance, Bali Indonesia, 23 January 2003).

³⁹⁵ Linda Senden, ‘Soft law, self-regulation and co-regulation in European Law: Where do they meet?’ (2005) 9(1) *Electronic Journal of Comparative Law*, 11 <<http://www.ejcl.org>>.

³⁹⁶ Erik Berglof and Stijn Claessens, ‘Enforcement and Good corporate governance in developing countries and transition economies’ 21 (1) *Oxford journals Economic social sciences* 123–50.

³⁹⁷ Williamson and Kerekes, above n 379.

³⁹⁸ Cabalu, above n 235.

³⁹⁹ Kuroda, above n 214.

1997.⁴⁰⁰ Improved corporate governance is seen as a solution to the results of the financial crisis in terms of rebuilding trust and restoring confidence.⁴⁰¹

Good corporate governance, in essence, concerns the application of effective managerial and control systems for attaining desired corporate goals and maintaining competitiveness.⁴⁰² La Porta et al claim, on the basis of empirical research, that good corporate governance rests on the legal protection of investors' interests and the return to them on their investment.⁴⁰³ In particular investors' interests must be protected from detrimental actions by insiders.⁴⁰⁴ A number of studies have indicated how such protection is required in the context of share prices and other investments and to promote investment performance, economic growth as well as firm and board performance.⁴⁰⁵ As noted it is particularly important where there is restructuring and a resolution of competing financial claims in a crisis.⁴⁰⁶

Braithwaite considers informal regulation in the context of responsive regulation in developing countries like Indonesia. He argues that there is a potential for responsive regulation to be used by them as a strategy that mobilizes cheaper forms of social control than the state command and control of formal law as developing countries generally have less regulatory capacity and resources than developed ones. This suggests that developing countries could reduce the use of official law by the state in regulation and utilize responsive regulation by private groups as a response to their limited capacity.⁴⁰⁷ Black's concept of decentred regulation is similar. She suggested a diffusion of regulation throughout society away from the state, which has had a theoretical monopoly on the

⁴⁰⁰ Jang, above n 170.

⁴⁰¹ International Corporate Governance Network, above n 216.

⁴⁰² Organization for Economic Co-operation and Development, *the OCED Principles of Corporate Governance 2004*, above n 224.

⁴⁰³ Shleifer and Vishny, above n 246.

⁴⁰⁴ Rafael La Porta et al, 'Investor Protection: Origins, Consequences, Reform', above n 227.

⁴⁰⁵ Organization for Economic Co-operation and Development, *the OCED Principles of Corporate Governance 2004*, above n 224; Classens and Tan, above n 60.

⁴⁰⁶ Rafael La Porta et al, '*Investor Protection: Origins, Consequences, Reform*', above n 227.

⁴⁰⁷ John Braithwaite, 'Responsive Regulation and Developing Economies' (2006) 34 (5) *World Development* 884, 884-98
<http://regnet.anu.edu.au/sites/default/files/BraithwaiteJ_ResponsiveRegulation.pdf>.

exercise of power and control.⁴⁰⁸ Ogus also argued, using market principles, that the law and regulation could also be largely decentralized in this sense. The decentred law would leave it to individuals to enforce their rights, not the state because the law, in his opinion, has primarily a facilitative and market function.⁴⁰⁹

Pistor observed that an informal approach is significant and needed when the formal law lacks credibility and generates distrust.⁴¹⁰ Aldashev et al also suggests the need for informal rules as the formal law may not be trusted, recognized or followed. It is also suggested that customary rules – a form of informal rules – are resorted when the formal laws become ‘dead letters’ as they are not able to fulfil the required expectations.⁴¹¹

Aldashev concluded that the use of customary rules have been widely recognised to cope with legalistic approaches to business issues including ignorance or manipulation of the formal law or insufficient confidence in its enforcement.⁴¹² For these reasons after the fall of the Soviet Union Russia utilized more informal mechanisms based on trust and relationships than formal law.⁴¹³

Helmke and Levitsky suggest that there are three reasons to employ informal rules. The first is because of incompleteness of formal institutions. Formal rules are not able to deal with all contingencies. Bureaucracies and courts may undermine formal procedures in their anticipated addressing of issues. They suggest that informal institutions may be a second best approach when formal institutions fail to offer solutions. This is partly because the formal rules are likely not able to be changed. The second is where the existing formal rules are ineffective in practice due to their lack of credibility. The third is where the formal law may set objectives that are locally or internationally unacceptable.⁴¹⁴ This suggests that

⁴⁰⁸ J Black, *Decentring Regulation: Understanding the Role of Regulation and Self-Regulation in a Post Regulatory World, Current Legal Problems* (Oxford University Press, vol. 54, 2001) 103-46.

⁴⁰⁹ Ogus, above n 308.

⁴¹⁰ Katharina Pistor, ‘Can supply stimulate demand? Supply and demand for law in Russia,’ (1999) *Sage Journals online* 105.

⁴¹¹ Gani Aldashev et al, *Custom in the shadow of the formal law: an economic analysis* (December 2007) University of Namur, 2 & 7 <<http://e-cares.ulb.ac.be/e-caresdocuments/seminars0708/aldashev.pdf>>.

⁴¹² *Ibid* 29.

⁴¹³ Pistor, above n 410.

⁴¹⁴ Gretchen Helmke and Steven Levitsky, *Informal institutions and comparative politics: A research agenda*, 730–1 <www.wcfia.harvard.edu/sites/default/.../883__informal-institutions.pd...>

informal rules may be more effective, even if sanctions are informal, where formal regulations may be ignored particularly in developing countries with weak state institutions.⁴¹⁵

Rules from soft law instruments may also fill the gaps in formal law. Wymeersch notes that: ‘The absorption of soft law rules in the law by interpreting blank norms is a standard technique that has been used in many jurisdictions’. Corporate governance codes, for example, may become a source of standards for judges concerned with the specific conduct of directors.⁴¹⁶

2.4.2.3. *The legal bases of corporate governance code*

Wymeersch indicated that corporate governance codes could be based on three relationships with formal law: (1) without an express legal basis, (2) by incorporation of parts of the code in other statements of formal law, or (3) the corporate governance code itself being enacted as a formal law.⁴¹⁷ Pietrancosta suggested two categories for the endorsement of codes in formal law: (1) no recognition at all with the status of code being a series of recommendations for voluntary implementation and any enforcement based on market forces, or (2) official recognition without the rules being directly enshrined in the law but contained in a non-binding code.⁴¹⁸ Goldschmidt pointed to three potential legal bases for corporate governance codes: (1) voluntary recommendations, (2) as terms of a contract such as in the agreement between an exchange and a listed company and represented in the listing rules, or (3) their inclusion in formal law.⁴¹⁹

The legal status of corporate governance codes is generally that of recommendations to be implemented on a voluntary basis with any enforcement based on assessments made in the context of the exercise of market power.⁴²⁰

⁴¹⁵ Alice Sindzingre, *The relevance of the concepts of formality and informality: A theoretical appraisal*, 15 <<http://www.oecd.org/dac/governance-development/37791314.pdf>>.

⁴¹⁶ Wymeersch, above n 260, 6.

⁴¹⁷ *Ibid* 4–11.

⁴¹⁸ Alain Pietrancosta, *Enforcement of corporate governance codes. Legal perspective* (2009) <<http://www.unibz.it/en/economics/events/Documents/Pietrancosta.pdf>>

⁴¹⁹ Leo Goldschmidt, ‘Enforcement of corporate governance codes’ (OECD roundtable, Moscow, 2 June 2005) 2,4,6,10 <www.oecd.org/daf/corporateaffairs/35176266.ppt>.

⁴²⁰ Pietrancosta, above n 418; Wymeersch, above n 260, 2.

Where the legal basis of the code is based on contract and it is included in the listing rules there is often no explicit sanction for non-compliance. The Austrian Corporate Governance code is included as a part of the listing rules. The Vienna Stock Exchange requires a declaration of commitment to comply with the rules of the Austrian code of corporate governance.⁴²¹ There is no formal enforcement but false declarations could be administrative or criminal offences, and violation could result in a fine.⁴²² However, Austrian legislation favours self regulation in the area of corporate governance.⁴²³

Belgium enacted basic principles of corporate governance in the Belgian company legislation. The Belgian corporate governance codes are the ‘Code *Lippens*’ (2004 and 2010), for listed companies, and, the Code *Buysse* (2005) for non listed companies.⁴²⁴ There are no real sanctions for them and they rely on the moral authority of the company’s shareholders and the L’Autorité des services et marchés financiers [Financial Services and Markets Authority (FSMA)] is well respected by most companies. FSMA may invite companies to comply with the Code. It is believed the majority of the listed companies comply with the code. The moral authority of the FSMA is ‘quite effective in persuading companies to comply with corporate governance code’ and listed companies are aware that the market is expecting compliance.⁴²⁵ Bulgaria included its National Corporate Governance Code as part of the listing rules. There is a formal provision in national law which applies the comply or explain principle.⁴²⁶ The Bulgarian Stock Exchange [BSE] requires companies to declare that they comply with the code, but it does not monitor for compliance.⁴²⁷ Cyprus also inserted its code as part of the listing rules. Its contents form no part of the Companies Law.⁴²⁸ Other jurisdictions indicate the preference for the use of

⁴²¹ Weil, Gotshal & Manges, above n 294, 12.

⁴²² Ibid 16.

⁴²³ Ibid 7.

⁴²⁴ Ibid 24

⁴²⁵ Ibid 26.

⁴²⁶ Ibid 36.

⁴²⁷ Landwell & associates, *Study on monitoring and enforcement practices in corporate governance in the member states: Appendix 1 Detailed legal analysis Final report* (2009) <http://ec.europa.eu/internal_market/company/docs/ecgforum/studies/comply-or-explain-090923-appendix1_en.pdf>.

⁴²⁸ Weil, Gotshal & Manges, above n 294, 52.

codes in a non-binding way. In Italy, companies may choose to be bound by the Stock Exchange Code.⁴²⁹ In the Netherlands, the enforcement of the code is on a comply or explain basis leaving endorsement to the shareholders.⁴³⁰ In Australia, corporate governance is governed by mix mandatory and voluntary requirements. The Australian Stock Exchange's corporate governance code is voluntary guidelines with an 'if not, why not' comply or explain disclosure mechanism.⁴³¹

Many scholars consider the informal sanctions including market enforcement as a key factor for the effectiveness of corporate governance codes as informal law or self regulation.

2.4.3. The significance of informal sanctions

Enforcement is the main difference between self regulation and associated soft law and formal law and state regulation.⁴³² Haines identified compliance as a crucial problem for alternative or decentred regulation and the use of informal rules, soft law or decentred frameworks. She noted that voluntary codes are informal rules that may have functions equal to formal law. She noted that their enforcement relies on moral suasion.⁴³³ Zerilli also considered compliance with soft law or self-regulation to be centred on moral suasion.⁴³⁴ Voluntary compliance with corporate governance codes to create confidence in markets and third parties including potential investors and creditors rely on any statements be honest and complete.⁴³⁵

There is some conflict over the role of enforcement in informal law and self-regulation. Ottow suggested that self-regulation is only effective if sufficient enforcement mechanisms are in place. Others have extended this claim in arguing that the effectiveness of the enforcement of self-regulation also requires some general rules. They include that the compliance with the informal rules must be within the power of the addressees and that

⁴²⁹ Borsa Italia, *Corporate Governance Code, Article 1*, 4

<<http://www.borsaitaliana.it/borsaitaliana/regolamenti/corporategovernance/code2015.en.pdf>>.

⁴³⁰ Cooper, above n 337.

⁴³¹ Ibid.

⁴³² F Haines, *Corporate Regulation: Beyond Punishment and Persuade* (Clarendon Press, 1997) 5.

⁴³³ Ibid.

⁴³⁴ Filippo M Zerilli, *The rule of soft law: An introduction*, 3

<www.ingentaconnect.com/.../art00001>.

⁴³⁵ Wymeersch, above n 260, 8.

there is a sufficient enforcement mechanism [carrot and the stick principle] and that the enforcement must not be put in the hands of persons or entities that have conflicts of interest. They also argue that any informal rules used in self regulation should not conflict with mandatory rules or with the norms or standards generally accepted in the particular society.⁴³⁶ Waagstein claimed that there is a complex relationship between the legal character of a norm and an effectiveness of compliance. She argued that: ‘mandatory norm does not necessarily coincide with corporate compliance. What constitutes a voluntary or obligatory norm is a matter of compromise and acceptance, and is dependent on the subject and context.’⁴³⁷

Alternative regulatory concepts rely on the private or non-government sector constructing an effective regulatory process using incentives and deterrence with informal sanctions. The use of a pyramidal escalation of sanctions is argued by Braithwaite to be more effective for developing countries like Indonesia.⁴³⁸ Pyramidal escalation refers to a model of regulation in which regulators start with informal advice, move to formal warnings, then impose administrative sanctions that are followed by binding undertakings to behave in particular ways and that may be enforced by courts. At each stage fewer cases are intended to appear with any problem and solved at the lower levels. Towards the apex of the pyramid formal civil actions may be followed by formal criminal prosecutions if the offending conduct does not stop. At the apex is the corporate equivalent of capital punishment, winding up the offending company. Informal law and self regulation can be used in the levels of the pyramid below the apex. This is sometimes described as network branching. This involves bringing NGOs, industry associations, professional associations, corporations, and international organizations within the regulatory strategy.⁴³⁹

Parker and Braithwaite proposed general informal sanctions at a low level in the regulatory pyramid which include negative publicity, public criticism, gossip,

⁴³⁶ Annetje Ottow, *Enforcement of the Dutch corporate governance code* <http://www.uu.nl/SiteCollectionDocuments/REBO/REBO_RGL/REBO_RGL_EUROPA/Enforcement%20of%20the%20Dutch%20corporate%20governance%20code%2018%20april.pdf>.

⁴³⁷ Patricia Rinwigati Waagstein, ‘The Mandatory Corporate Social Responsibility in Indonesia: Problems and Implications’ (2011) 98 *Journal of Business Ethics* 455, 462.

⁴³⁸ Braithwaite, ‘Responsive Regulation and Developing Economies’, above n 407.

⁴³⁹ Ibid.

embarrassment, and shame that are believed to have a greater deterrent impact for some than formal legal sanctions.⁴⁴⁰

Other writers have also pointed to the effectiveness of informal sanctions outside the framework of the regulatory pyramid but in a similar context of the escalation of penalties. Millstein suggested that softer forms of enforcement including rating agencies, business institutions and the media play a significant role in improving corporate governance practices in developing countries.⁴⁴¹ Wymeersch also notes the importance of informal sanctions, ie reputation damage for the company and loss of trust in the management caused by dishonest, untrue, incomplete or misleading statements.⁴⁴² Goldschmidt also suggested the use of informal sanctions through corporate governance codes as legislative approaches were not a sufficient deterrent. He pointed to monitoring, investigating, sanctioning or admonishing, ordering change, and publicising (as a form of naming and shaming), as well as to fines, cancelling privileges and delisting. He also pointed to the network encompassing those who can be involved in enforcement: the courts, regulators, stock exchanges, special committees, professional bodies, auditors, shareholders, members of the public, and the media.⁴⁴³

With respect to disclosure specifically, it is claimed that the discipline of the marketplace is the best remedy for fraudulent disclosure rather than penalties and prescriptions.⁴⁴⁴ It is claimed that the market and the press are the best enforcers, although market supervisors play a crucial role in monitoring disclosure.⁴⁴⁵

However, confidence in self-regulation and reliance on informal rules has been shaken by periodic corporate scandals and market failure.⁴⁴⁶ Trust and its maintenance in this context is a fundamental issue.

⁴⁴⁰ C Parker and J Braithwaite, 'What is Regulation?' in Peter Cane and Mark Tushnet (eds), *The Oxford Handbook of Legal Studies* (Oxford University Press, 2005).

⁴⁴¹ Milstein et al, *Enforcement and Corporate Governance*, above n 284, 14.

⁴⁴² Wymeersch, above n 260, 8.

⁴⁴³ Goldschmidt, above n 419, 2,4,6,10.

⁴⁴⁴ Olson, above n 302, 532.

⁴⁴⁵ Wymeersch, above n 260, 5.

⁴⁴⁶ Pietrancosta, above n 418.

2.4.4. Trust as a critical issue

There is evidence demonstrating the significance of trust in the context of corporate investments and capital markets. Trust in the context of business has been defined as “a reasonable belief that trusted persons will tell the truth, and keep their promises”⁴⁴⁷. There is extensive literature outlining the link between trust and confidence which is important in maintaining investment and financial markets. As Tomasic and Akinbami observe, in their summary of relevant literature in the context of corporate governance and financial markets, trust is important:

in part, because it helps investors by providing a fairly easy and inexpensive way to help them decide whether or not to buy shares or other securities, and whether or not to enter into commercial relationships.⁴⁴⁸

The importance of the moral authority of the Belgian L’Autorité des services et marchés financiers [Financial Services and Markets Authority (FSMA)] has been pointed out in the context of the legal bases of corporate governance codes above. Another example is provided by the Grameen Bank, a Noble peace prize winning source of microfinance in Bangladesh. Its success is attributed to ‘trust, solidarity, and informal social pressure’ among the very poor, which is similar to informal banking institutions.⁴⁴⁹

Millstein et al argue that rebuilding trust in corporate governance without the need for further regulatory intervention may help an economy recovery in the wake of financial crises.⁴⁵⁰ Trust reduces the cost of monitoring and lower transaction costs.⁴⁵¹ Consequently,

⁴⁴⁷ Tamar Frankel, *Trust, Honesty and Ethics in Business*, Boston University, 87 <[http:// www.tamarfrankel.com/support-files/financeandcommongood.pdf](http://www.tamarfrankel.com/support-files/financeandcommongood.pdf)>.

⁴⁴⁸ Roman Tomasic and Folarin Akinbami. ‘The role of trust in maintaining the resilience of financial markets’ (2011) 11(2) *Journal of Corporate Law Studies* 369.

⁴⁴⁹ Indra de Soysa and Johannes Jutting, ‘Informal institutions and development: Think local, Act global?’ (International seminar on Informal institutions and development-what do we know and what can we do?, OECD Development centre and development Assistance Committee – Network on Governance) 2–3 <www.oecd.org/dac/governance-development/37790393.pdf>.

⁴⁵⁰ Ira Millstein et al, ‘Rebuilding trust: the corporate governance opportunity for 2012’ on Corporate Governance and Financial Regulation, *The Harvard Law School Forum* (24 January 2012) <<http://blogs.law.harvard.edu/corpgov/2012/01/24/rebuilding-trust-the-corporate-governance-opportunity-for-2012/#more-25061>>

⁴⁵¹ Williamson and Kerekes, above n 379, 13.

‘A higher trust society will experience higher levels of economic development and growth’.⁴⁵²

Trust and personal relationships are able to be preserved by informal mechanisms.⁴⁵³ These are important features in business transactions.⁴⁵⁴ De Soysa and Jutting claim that trust has a significant role in establishing norms in complex economies. In particular the level of social engagement in political and economic development contributes to the substitutability of the law in establishing more effective relationships.⁴⁵⁵ They are not traditional nor have they been observed for long periods of time, although they may contain several values including honesty and telling the truth. This reflects the importance of the relationship between informal and formal law suggested by a number of scholars.

2.5. Relationship between formal and informal law

2.5.1. Introduction

A number of concepts found in the literature have been identified including formal law and informal law. The latter extends to norms and soft law. The concepts of formal and informal law have been considered by a number of scholars. The term informal is often opposed in this context to the official legal system and its associated state institutions.⁴⁵⁶ This is seen in the refusal by some to acknowledge that ‘soft law’ could be law in the discussion above in 2.4.2.3. In terms of formal and informal law, they have been described in terms of official and unofficial rules, or official and unofficial institutions. In this context official and unofficial relates to their association with the state or the government and their promulgation within the legal system associated with the state. A number of writers have noted the distinction and have described it in different ways but share this distinction. Significant in their descriptions is how law is defined in relation to sanctions imposed by the state, which is a feature of legal positivism.⁴⁵⁷

⁴⁵² Ibid.

⁴⁵³ Sindzingre, above n 415, 15.

⁴⁵⁴ Pistor, above n 410, 105.

⁴⁵⁵ de Soysa and Jutting, above n 449, 5.

⁴⁵⁶ Ramses A Wessel, ‘Informal International Law-making as a New Form of World Legislation?’ (2011) 8 *International Organization Law Review*, 256.

⁴⁵⁷ Hart, above n 342.

2.5.2. The distinction between formal and informal law

The major distinction between formal and informal law relates to whether the principles or the rules being promulgated are within the legal system associated with the state and its sanctions in relation to their breach. This can be seen running through regulatory literature.

It is seen in Pejovich's classification. He considers that informal rules, like *adat*, have a long standing, socially ingrained and traditional aspect to them. They are 'traditions, customs, moral values, religious beliefs, and all other norms of behaviour that have passed the test of time'. Their enforcement includes sanctions such as 'expulsion from the community, ostracism, or loss of reputation'. Formal rules, on the other hand, comprise 'constitutions, statutes, common law, and other governmental regulations. Their sanction's apparatus are fines, imprisonment, and execution.'⁴⁵⁸

North similarly describes informal laws or norms as unwritten conventions that have evolved over time with self-enforcing propositions. They include sanctions, taboos, customs, traditions, codes of conduct, conventions and other behavioural norms. Informal rules have been claimed as formal rules' extensions, elaborations and modifications. Formal law, by contrast, is a written and intentional creation, which originates in the state.⁴⁵⁹ Formal rules are codified laws and regulations, and are created through formal legislative or other state based processes.'⁴⁶⁰

Helmke and Levitsky also assign formal rules to the domain of the state and its agencies that are enforced by the state. Informal rules, for them, are found in organizations in civil society and self-enforcing within them.⁴⁶¹ Huppel-Cluysenaer pointed to social scientists' concepts of formal and informal rules. Formal norms have been defined in written form or verbal forms and may not reflect pre-existing patterns of behaviour. Informal rules are social norms that reflect established regularities in behaviour, which may

⁴⁵⁸ Svetozar Pejovich, 'The effects of the interaction of formal and informal institutions on social stability and economic development' (1999) 2 *Journal of Market & Morality* 164, 166-7.

⁴⁵⁹ Cited in Sindzingre, above n 415, 10.

⁴⁶⁰ FAO Corporate Document Repository, *Chapter 5: The characteristics of the rules and resource management incentives*, 2 <<http://www.fao.org/docrep/w7483e/w7483e07.htm>>.

⁴⁶¹ Helmke and Levitsky, above n 414, 726-7.

carry social sanctions for their breaches.⁴⁶² They may be internal to particular social institutions.⁴⁶³ A pragmatic definition of them for Huppés-Cluysenaer is the habitual conduct or the behaviour or the feeling of obligation which is expected in particular situations.⁴⁶⁴

De Soysa and Jutting specify informal rules without reference to tradition or the time evolution they have been extended as ‘rules governing behaviour outside official channels’. They are widely recognized as legitimate rules in use rather than the ‘rules in force’ by the state.⁴⁶⁵

In the context of formal and informal law voluntary codes of conduct represent informal law but also contain features of formal law. They are written and they are endorsed, but not by the state. They may not carry the same expectations about conforming to them or the same social sanctions for their breaches.

The differences between informal and formal law indicated earlier suggest that both may need each other. Some theories suggest that they are most effective when they are combined.

2.5.3. The efficacies of the mixing of formal and informal law

A number of scholars have suggested combining formal and informal law as well as processes so each supplements the other to achieve better regulation. Parkinson, Black and Braithwaite amongst others have considered that they are most effective and efficient, particularly in enforcement, when deployed in this way.

2.5.3.1. An effective and efficient regulatory strategy

Parkinson contends that a mix of private regulatory mechanisms with some elements of state processes may be the most effective and efficient regulatory mechanism.⁴⁶⁶ Black claims that such a combination can create the right balance of discretion between the two ‘competing models of rationalities’ these two forms of

⁴⁶² E A Huppés-Cluysenaer, *Informal rules do not exist*, 3
<http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1407017>.

⁴⁶³ Ibid.

⁴⁶⁴ Ibid 5.

⁴⁶⁵ de Soysa and Jutting, above n 449, 2–3.

⁴⁶⁶ Parkinson, above n 323.

regulation represent, between certainty and flexibility and uniformity and individual action.⁴⁶⁷

Parker and Braithwaite also claim that:

a mixture of rules and principles can be even better as binding rules interpreted by non-binding principles and non-binding rules backed by binding rules; principles are considered more consistent than rules in a more complex phenomena.⁴⁶⁸

Their conclusions suggest that the use of codes as informal rules in Indonesia may be beneficial in improving corporate governance. The codes may be both cheaper and more effectual in the regulatory system of a developing country with low level capacities in its formal legal system.⁴⁶⁹ Pilarczyk also suggests that informal law may complement, circumvent and supplant the formal law. For instance, informal law may replace the law that is not being implemented.⁴⁷⁰

This combination of formal law and informal law represented by such voluntary codes covers all important issues relating to corporate governance. Some believe that the comply-or-explain system has been recognised as having a positive impact but that it has also continued the low quality of disclosure in company statements. A comply-or-explain system may effectively work in a three pronged approach. The first prong is a genuine obligation to comply-or-explain. The second is a high level of transparency. The third holds boards accountable for their use of these in its disclosure.⁴⁷¹

2.5.3.2. An effective instrument for enforcement

Bergloff and Claessens claimed that formal laws and voluntary codes are ‘key to effective corporate governance in developing countries’. They suggest that the effectiveness of enforcement needs both public forms and private tools. Even though the private tool is believed to be more effective than the public one, private enforcement may

⁴⁶⁷ Black, *Rules and Regulators*, above n 385.

⁴⁶⁸ Parker and Braithwaite, above n 440.

⁴⁶⁹ Braithwaite, above n 407; Parker and Braithwaite, above n 440.

⁴⁷⁰ Ian C Pilarczyk, *Informal law and customs*

<<http://iancpilarczyk.com/2011/02/theroleofinformallaw>>.

⁴⁷¹ Wymeersch, above n 260, 167, 177–9.

work more effectively with the public support of formal law enforcement. They complement each other.⁴⁷²

Pietrancosta has also argued that the effectiveness of corporate governance requires being both used to legitimate or justify the approach taken. This requires a:

contribution of public authorities to the elaboration of corporate governance codes, incorporation of corporate governance requirements into the law and regulations – a codification, and requirement to publicly declare adherence to a code.⁴⁷³

This is seen in German and Dutch practices where a formal legal backing has been applied to the code. The formal law provides appropriate sanctions so that the code is taken seriously. The German situation over director's remuneration showed the need for formal law to intervene when business leaders continued to refuse to disclose the remuneration of individual managers.⁴⁷⁴ Particularly relevant to Indonesia given its adoption of Dutch corporate law, is the demonstrated efficacy in the Netherlands of combining informal and formal mechanisms. The Dutch corporate governance code [Code Tabaksblat] is claimed to be a form of self regulation. It is also claimed that it reflects the regulator's perspective that 'self regulation might be an effective instrument to ensure compliance with legislation instead of public enforcement'.⁴⁷⁵ Compliance is first left to the market, but there was still a perceived need for public enforcement in case significant principles were not followed. A mixed approach was adopted to ensure compliance. Articles 8 and 9 of the Dutch Civil Code [Book 2] provide several open standards that can be interpreted according to the circumstances of individual cases. While they are legal principles they also reflect values accepted in Dutch society. In this way the voluntary corporate governance code has been accepted as part of their formal legal framework.⁴⁷⁶

⁴⁷² Erik Berglof and Stijn Claessens, 'Corporate Governance and enforcement' in Ira M Millstein, Shri GN Bajpai, Erik Berglof and Stijn Claessens, 'Enforcement and corporate governance: Three Views' on Global Corporate Governance Forum – Focus 3, *World Bank*, 27, 62

www1.ifc.org/wps/wcm/connect/.../Focus_ENFCorpGov3.pdf?MOD...

⁴⁷³ Pietrancosta, above n 418.

⁴⁷⁴ Wymeersch above n 260, 21

⁴⁷⁵ Ottow, above n 436.

⁴⁷⁶ Ibid.

Even in the UK with its long tradition of informal law and social sanctions the contemporary corporate governance framework shows a successful approach to utilizing a balance of hard law and soft law. Companies are required to adhere to the corporate governance codes by selected statutory provisions.⁴⁷⁷

This amalgam of formal and informal law in enforcement is also relevant to Indonesia. As discussed in Chapter 6 part of the Indonesia's Code of Good Corporate Governance has been reflected in the new Company Law. The merging of soft law with formal law may come about for the reasons given above: that corporate governance codes have some of the forms of formal law in being written and enforced but not initially by the state. The extent to which the hybrid can retain the advantages of soft law including in enforcement is considered at a number of places in the thesis.

Corporate governance codes around the world have grown from the model of the British Cadbury report, particularly as reformed by the OECD in its Principles of Corporate Governance. The significance of the role soft or informal law plays in them also contributes to a global trend of borrowing ideas and concepts across formal and informal legal systems long studied in comparative law.

2.6. Comparative law and legal transplants

2.6.1. Introduction

The history of a system of law, Roscoe Pound claimed, 'is largely a history of borrowings of legal materials from other legal systems and of assimilation of materials from outside of the law'.⁴⁷⁸ In the late 19th century, there was a massive legal transplant from western legal systems and culture⁴⁷⁹ to developing economy countries as part of both

⁴⁷⁷ BusinessEurope ecoDa, *Final report: Study on monitoring and enforcement practices in corporate governance in the member states, appendix 2 Detailed company and director perception survey results* (23 September 2009) <ec.europa.eu/internal.../studies/comply-or-explain-090923_en.pdf>.

⁴⁷⁸ Vlad F Perju, 'Constitutional transplants, Borrowing, and Migrations' (Boston College Law School Faculty papers) 2
<<http://lawdigitalcommons.bc.edu/cgi/viewcontent.cgi?article=1365&context=lsfp>>.

⁴⁷⁹ Manuel Gutan, *Legal transplant as socio-cultural engineering in modern Romania*
<papers.ssrn.com/sol3/papers.cfm?abstract_id=2207718>.

colonisation and also legal modernisation. Since then, the volume of legal transplants has increased.⁴⁸⁰

Globalization is believed to have contributed to the increasing use of transplants,⁴⁸¹ and 'leads to an indeterminate space of diffusion of law'.⁴⁸² It is seen as the main reason why legal transplants take place in the contemporary world economy.⁴⁸³

The importation of the Dutch legal system to Indonesia is discussed in Chapter 4 at 4.2.2.2. The current transplant of concepts from western legal systems to Indonesia as an emerging economy is an inevitable result of globalisation and internationalisation. This follows the pattern in other developing economies of importing legal models from mature market economies.⁴⁸⁴ The transplanting of international standards for corporate governance has potentially significant benefits for Indonesia. However, the identity, tradition and culture, historical and social condition of Indonesia are challenging factors in implementing foreign concepts.

The framework of comparative law and the concept of legal transplants enable a better understanding of whether disclosure as a concept in corporate governance as a foreign concept is able to be effectively applied in the Indonesian context. It may also be able to identify significant practical problems in its implementation and suggest ways to resolve them.

It should also be noted that since the 1990s there has been a debate around the nature of comparative law as a discipline which coincides with the interest in informal or soft law in other areas of law and regulation. There was a recognition that informal law

⁴⁸⁰ Frederick Schauer, 'The politics and incentives of legal transplantation' (Working Paper No.44, Law and Development Paper No. 2, Center for International Development Harvard University, April 2000) I <www.hks.harvard.edu/var/ezp_site/storage/fckeditor/file/.../044.pdf>.

⁴⁸¹ Edward Burnett Tylor cited in Marlorzata Krol, 'Legal culture and legal transplants Polish national report' in Jorge A Sanchez Cordero (ed), *Legal Culture and Legal Transplants* ((2010) Reports to the XVIIIth International Congress of Comparative Law <www.isaidat.di.unito.it/index.php/isaidat/article/view/55/65>.

⁴⁸² Ana Batricevic, *Legal transplants and the code of Serbian Tsar Stephan Dushan: A comparative study*, 50 <http://www.alanwatson.org/dushans_code.pdf>.

⁴⁸³ Irma Johanna Mosquera Valderrama, *Legal transplants and comparative law*, 264 <www.javeriana.edu.co/juridicas/pub_rev/international_law/...2/7.pdf>.

⁴⁸⁴ Catherine Walsh, 'The law in law and development' in *Law in transition: Advancing legal reform* (European Bank for Reconstuction and Development, 2000) 1 <<http://siteresources.worldbank.org/INTLAWJUSTINST/Resources/lawintransition.pdf>>.

could not be ignored in comparative legal studies.⁴⁸⁵ Some scholars consciously sought to enlarge the field of comparative law to 'comparative legal cultures',⁴⁸⁶ labelling the older and narrower discipline that compared formal law as 'foreign law'.⁴⁸⁷ Legrand argues that the two cannot be separated in that the legal cannot be disconnected from the non-legal, or in the language of this thesis, formal law cannot be disconnected from informal or soft law.⁴⁸⁸

2.6.2. Comparative law and legal transplants

Watson defined comparative law in a practical way as the 'study of the legal borrowings or transplants that can and should be made'.⁴⁸⁹ Mistelis similarly pointed out that comparative law 'was employed to decide either the compatibility of foreign legal concepts or the merits of foreign legal systems and to provide an anthology of foreign legal

⁴⁸⁵ 'We thus have reason to conjecture that the scope of traditional comparative law has been too narrow, and that it has paid insufficient heed to context. But we also have reason to conjecture that it has studied the wrong kind of phenomenon. The issues here are somewhat elusive, and the situation is made complicated by the diversity of different practices within traditional comparative law, and by the absence of explicit theories. But as a first approximation we can say that traditional comparative law tends to view a foreign legal system from the outside; that is, it takes its object of study to be black-letter rules, or an authoritative text, or the social function of a rule, or some other range of empirical phenomena that is capable of being described in sociological or behavioristic terms, from an external point of view. No doubt such an externalist approach can draw upon deep philosophical sources for its justification: after all, for Kant the distinction between law and morality consists precisely in the fact that law is concerned with the regulation of external behavior, whereas morality is concerned with internal motives to action.' William Ewald, 'Comparative jurisprudence (I): What was it like to try a rat?' (1995) 143 *University of Pennsylvania Law Review* 1889, 2108-9.

⁴⁸⁶ Huxley suggests that "the term 'comparative law' now is so tainted that we should refer to context-rich comparative studies as a quite different discipline - as 'legal cosmology' perhaps, or as 'comparative legal cultures'. See, Andrew Huxley, 'Golden yoke, silken text' (1997) 106 *Yale Law Journal* 1885, 1924-25; Csaba Varga (ed), *Introduction to Comparative Legal Cultures* (1992) xv, xix; Lawrence M Friedman, 'Some thoughts on comparative legal culture' in David S Clark (ed), *Comparative and Private International Law* (1990) 52-55. But see, 'Symposium: new directions in comparative law' (1998) 46 *American Journal of Comparative Law* 597; and, 'Symposium: new approaches to comparative law' [1997] *Utah Law Review* 255.

⁴⁸⁷ Merryman stated that most comparative law teaching and scholarship could more accurately be called 'foreign law,' as its principal aim is to describe foreign legal systems). See, John Henry Merryman, David S Clark and John O Haley, *The Civil Law Tradition: Europe, Latin America, and East Asia* (Charlottesville: Michie, 1994) 1.

⁴⁸⁸ Pierre Legrand, 'The impossibility of legal transplants' (1997) 4 *Maastricht J.Eur. & Comp. L.* <<http://heinonline.org>>

⁴⁸⁹ Cited in Valderrama, above n 483, 270.

ideas'. Foreign concepts might be used to improve aspects of a national legal system or to replace ineffective aspects of it.⁴⁹⁰

According to the Oxford English Dictionary, transplant means 'remove or reposition', 'convey or remove elsewhere'. Legrand remarked that transplant 'implies displacement', and 'for the lawyer's purposes, the transfer is one that is across jurisdictions'.⁴⁹¹ It is an older concept than the medical term which means 'the moving of an organ from one place to another' which has been suggested by some writers as its source.⁴⁹² Legal transplants have been defined as 'the movement of legal norms or specific laws from one state to another during the process of law-making or legal reform'.⁴⁹³ Krol describes it as 'a transfer of the normative content in its legal form ... or a transfer of a new method of legal regulation, ... from one system of law (foreign) to another one (host)'.⁴⁹⁴

2.6.3. Functions of comparative law and legal transplants

Batricevic claimed that 'since the ancient times legal transplants have been the vital, indispensable and one of the most common sources of a legal system's foundation and sustainable development'.⁴⁹⁵ It has been claimed, as Pound did above, that legal transplants are the 'most important element in legal development'.⁴⁹⁶

These descriptions of transplants developed in the context of formal law as did the justification that adopting legal ideas, concepts, processes and practices from developed economies may assist developing economies. The recognition of the importance of informal or soft law in regulatory systems has led to the suggestions that soft law may be preferred in creating regulatory systems which harmonise national regulatory systems under

⁴⁹⁰ Loukas A Mistelis, 'Regulatory aspects: Globalization, Harmonization, Legal Transplants, and Law Reform – Some Fundamental Observations' (2000) 34 *International Lawyer*, 1055 <<http://www.cisg.law.pace.edu/cisg/biblio/mistel.html>>.

⁴⁹¹ Legrand, above n 488.

⁴⁹² Malgorzata Krol, 'Legal culture and legal transplants Polish national report' in Jorge A. Sanchez Cordero (ed), *Legal Culture and Legal Transplants* (2010) Reports to the XVIIIth International Congress of Comparative Law, 5 <www.isaidat.di.unito.it/index.php/isaidat/article/view/55/65>.

⁴⁹³ Mistelis, above n 490.

⁴⁹⁴ Krol, above n 492, 6.

⁴⁹⁵ Batricevic, above n 482, 4,

⁴⁹⁶ Alan Watson cited in Jean-Louis Halperin, *Western legal transplants and India*, 1 <http://halshs.archives-ouvertes.fr/docs/00/55/91/18/PDF/Western_Legal_Transplants_and_India_2.pdf>.

globalisation.⁴⁹⁷ Private, rather than state, initiatives at national levels have been claimed to have greater capacity to embody global standards because they represent transnational organizational capabilities and by their nature stand outside state interest groups.⁴⁹⁸

Watson was a strong advocate of legal transplants as ‘the essence of comparative law in its practical conception, offering the prospect of making improvements to one’s own legal system’.⁴⁹⁹ Kahn-Freund also recommended comparative law as a potential law reform tool although he was more cautious about successful outcomes. More recently Teubner has supported transplants as a major source of legal change, and pointed out the degree of connection between law and its social context as determinant factors in successful transfers of legal concepts.⁵⁰⁰ Mistelis noted that legal transplants may be needed to implement dramatic political and economic changes in response to external and internal developments.⁵⁰¹

Mistelis also argued that a commercial law framework will be able to assist economic development by adopting voluntary convergences through inspiration from foreign legal concepts and carefully selected legal transplants.⁵⁰² Legal transplants are recognised by others as ‘important for building effective legal institutions and for economic progress’. The success of transplants depends on reflective, adaptive and other cultural factors.⁵⁰³ Legal transplants into some national legal systems reflect the needs produced by rapid change where the ‘law as a strong instrument for producing social change’.⁵⁰⁴ The literature indicates that there are a number of factors that have been attributed to the success of legal transplants.

⁴⁹⁷Mistelis, above n 490.

⁴⁹⁸ O Dilling, M Herberg and D Winter, *Responsible Business: Self-Governance and Law in Transnational Economic Transactions* (Hart Publishing, 2008).

⁴⁹⁹ Alan Watson in Jean-Louis Halperin, above n 496.

⁵⁰⁰ Anthony Forsyth, ‘The transplant ability debate in comparative law and comparative labour law: Implications for Australian borrowing from European Labour Law’ (Working Paper No. 38, Center for Employment and Labour Relations Law The University of Melbourne, June 2008) 2–8 <www.law.unimelb.edu.au/download.cfm?downloadfile...AF9B..>.

⁵⁰¹ Mistelis, above n 490.

⁵⁰² Ibid.

⁵⁰³ Fernando Gomez Pomar, *Legal harmonization seminar: Legal transplants and harmonization* <http://www.upf.edu/dretcivil/_pdf/mat_fernando/LH7.pdf>.

⁵⁰⁴ Gutan, above n 479 , 2.

2.6.4. Influencing factors for successful transplantation of informal law to donor legal system

2.6.4.1. Introduction

There is conflict in the literature over the case of which laws can be successfully transplanted. It is generally accepted that legal ideas can be transplanted. The conflict has been over what happens when a foreign legal transplant is placed in the new legal culture of the host and whether the wider legal culture of the donor can also be transplanted? Laws may look the same but may be applied very differently by officials and legal professionals from other national legal systems with different mentalities and epistemologies. Watson argued that because law is so autonomous, transplants can be made easily and this ease is facilitated by a group of elite lawyers who guide both the choice of transplant and its use in its new setting.⁵⁰⁵ Kahn Freund, coincidentally, published an article on the topic at the same time. He was in conflict with Watson's claims that there is no relationship between the law and the society in which it existed. He followed Montesquieu: 'laws should be so appropriate to the people for whom they are made that it is very unlikely that the laws of one nation can suit another.'⁵⁰⁶ As indicated the use of informal or soft law in voluntary codes makes them less autonomous than the claims made by Watson regarding formal legal system's being more sensitive in fitting in with other norms, values and practices in the legal and regulatory systems into which they are transplanted.

These debates provide a framework for exploring the transposition of international and transnational principles on corporate disclosure into Indonesian law. This is a crucial issue in the Indonesian context.

⁵⁰⁵ A Watson, 'Comparative law and legal change' (1978) (37(2) *Cambridge Law Journal* 313, 324.

⁵⁰⁶ Otto Kahn-Freund, 'On uses and misuses of comparative law' (1974) 37 *Modern Law Review* 1; Alan Watson, *Legal Transplants: An Approach to Comparative Law*, below n 1288.

2.6.4.2. Determining factors for successful informal legal transplants

Cranston claimed that theories about legal transplants assist in explaining the successful adoption of principles including their incorporation into national legislation.⁵⁰⁷ According to him a successful legal transplant involves non-legal factors and may need significant adjustment to the local situation. It is never an easy task to successfully transfer concepts and practices from one legal system or model to another.⁵⁰⁸

Walsh claimed that a successful transplant is determined by the capability of the foreign principle or idea to adapt to the legal traditions and institutions, and the social and economic realities of the recipient system.⁵⁰⁹ Legrand, as noted above, also argued that formal law could not be disconnected from informal or soft law.⁵¹⁰ Kahn Freund shared Legrand's view but accepted that there are degrees of transferability depending on how similar the political, social and economic institutions of the donor and recipient are. Already in the 1970s he observed that globalisation had flattened out cultural and economic diversity between national legal systems and that legal principles had become increasingly decoupled from local society and as such easier to transplant.⁵¹¹ The move to alternative regulatory theories and informal or soft law have, however, made local norms significant as indicated in the discussion of the literature above.

Both Watson and Kahn Freund saw organised non-state groups as potent forces in the selection of laws for transplanting. As pressure groups, they shape the ideas of national officials and are also influential in shaping how such laws are adapted and implemented. Kahn Freund went much further than Watson in recognising that there were elites within the political and social structures of host countries which may explain the acceptance and resistance between the donor and host's political, economic and social systems.⁵¹²

⁵⁰⁷ Ross Cranston, 'Theorizing transnational commercial law' (2007) 42 *Texas International Law Journal* 3 <www.tilj.org/content/journal/42/num3/Cranston597.pdf>.

⁵⁰⁸ Ibid.

⁵⁰⁹ Walsh, Catherine, above n 484, 1.

⁵¹⁰ Legrand, above n 488.

⁵¹¹ Kahn-Freund, above n 506, 1–27, 12–14; Mistelis, above n 490.

⁵¹² Watson, 'Comparative law and legal change', above n 505; Kahn-Freund, above n 506; Y Dezalay and B G Garth, *The Internationalization of palace wars: lawyers, economists, and the contest to transform Latin American states* (University of Chicago Press, 2001).

The transposing of unofficial or soft law or alternative regulatory strategies has been explored little in spite of the recognition that comparative law involves, in large part, a comparison of legal cultures. But culture is a nebulous concept, descriptive in its use, registering differences and inconsistencies across cultures but with few measures for any interactions.⁵¹³

Cotterell has argued that culture has to be situated and defined in the context of the particular study and requires some more precise analysis using ‘knowledge, art, belief, or technology, or tradition, or even ideology.’⁵¹⁴ It is the field contested by Legrand in comparative law theory, how possible is it to change the mentalities and epistemologies of participants in other legal and regulatory cultures? Legrand would suggest that it is not. But the observations of Kahn Freund and Watson may apply there as well, that these cultures are also levelling out through economic globalisation and that the elites who have persuaded national officials to adopt these regulatory processes have also adapted their behaviour to fit with them. Business people also form a different cultural and interpretive community which has a different perspective or may constitute ‘socially segregated sub-universes of meaning’.⁵¹⁵

Friedman remarked that the legal culture is the climate of social thought and social force that determines how law is used, avoided, or abused. Without legal culture, the legal system is inert. Basically, the law has multi-values because it depends on the individuals who implement the law.⁵¹⁶ Legal culture also relates to legal awareness: awareness of the law, familiarity with the law, its goals and its processes, legal attitudes and legal behaviour.⁵¹⁷ Blankenburg explained legal culture as ‘a complex interrelationship on four levels ie: the level of values, beliefs and attitudes towards law; patterns of behaviour;

⁵¹³ L M Friedman, ‘The Concept of legal culture: a reply’ in D Nelken (ed), *Comparing Legal Cultures* (Dartmouth, 1997) 33–40; C Pennisi, ‘Sociological Uses of the Concept of Legal Cultures’ in D Nelken (ed), *Comparing Legal Cultures* (Dartmouth, 1996) 2001.

⁵¹⁴ R Cotterell, ‘Law in Culture’ (2003) 7 (1) *Associations: Journal for Social and Legal Theory*, 213–25.

⁵¹⁵ P L Berger and T Luckman, *The Social Construction of Reality: A Treatise in the Sociology of Knowledge* (Garden City, 1966)

⁵¹⁶ Lawrence M Friedman, ‘Legal Culture and Social Development’ (1969) 4(1) *Law & Society Review* 29, 34–44.

⁵¹⁷ *Ibid.*

institutional features; and the body of substantive as well as procedural law'.⁵¹⁸ Watson also argued that understanding legal tradition and legal culture is the only approach to discovering the nature of law and its place in society.⁵¹⁹ There is an added dimension to the required awareness in the context of the subject of this thesis, disclosure, where alternative regulatory theories and informal or soft law has been borrowed.

A number of writers have pointed to non-legal factors as being significant in the study of comparative law. Peter and Schwenke pointed out that they are significant at all stages in comparative legal research. The understanding of the historical, social, economic, political, cultural and psychological contexts of the rule or the proposition and the examination of legal cultures, traditions, ideals, ideologies, identities, and entire legal discourses contribute to the understanding acquired by the use of comparative law methodologies.⁵²⁰ Valderrama stated that the influencing factors determining the outcome of any transplantation include legal culture, accounting, technological, political and economical circumstances in the transplantation process. The transplant may come to have a different effect from that in the jurisdiction of origin.⁵²¹

A study by Berkowitz et al demonstrates that the development of any borrowed law through the internal law making procedures of the borrowing country and the familiarity with the basic principles of the transplanted law resulted in its more effective implementation than where those factors were absent. These factors also had a strong indirect effect on economic development through the acceptance of the legitimacy of the borrowed law.⁵²²

Bedner noted the debates focusing on cultural dimensions around transplantation and that this was appropriate for well-developed legal systems. He suggested that transplants in developing countries like Indonesia require a greater focus on social and cultural issues. This includes the integrity of formal law and associated institutions such as the courts and the legal profession. These are debates on the impact of the uniformity of

⁵¹⁸ Valderrama, above n 483, 271.

⁵¹⁹ Ibid.

⁵²⁰ Ibid.

⁵²¹ Ibid 273.

⁵²² Daniel Berkowitz, Katharina Pistor and Jean-Francois Richard, 'The transplant effect' (2003) 51 *American Journal of Comparative Law* 163.

interpretation in achieving legal certainty.⁵²³ They are significant in the context of Indonesia's formal legal system.

2.7. Conclusion

This chapter has identified the reasons given in the literature for the importance of corporate governance and the use, in particular and as a result of the influence of the OECD Principles of Corporate Governance, of a narrower concept of corporate governance. As well as protecting investors and encouraging investment in corporations good corporate governance can also influence national economic development and contribute to wider social development in a country. The literature indicates that there is a failure to agree on ways to achieve this and that recent writing by scholars such as Milhaupt and Pistor indicate that there is a rolling relationship between law, including its use in corporate governance, and successful economic development which varies across countries. In this mix are aspects of the formal legal system and cultural values including commitment to ethical principles is important. This can vary depending on the toleration of uncertainty and power distance or significant inequalities in society. Disclosure and the extent to which it creates openness or preserves secrecy and impacts on ethics and power distance is important.

It has identified the claims in the literature of the importance of disclosure in corporate governance which will be returned to in the next chapter.

It has noted the turn to alternative regulatory theories which, unlike the older model of control and command through formal or official or state law, have used informal or soft law. The popularization of national corporate governance codes including Indonesia's GCG Code is an example of this. They have been seen by a number of writers as an alternative and smart way to create good practice, or norms. They do so through being more responsive. Good practice promotes a company's reputation and hence its performance. This form of regulation is seen as more flexible and less expensive than the use of formal law, which appears to have failed in respect to specific companies and to some national jurisdictions. Scholars, including Braithwaite, have suggested that where the formal legal

⁵²³ Adriaan Bedner, 'Indonesian legal scholarship and jurisprudence as an obstacle for transplanting legal institutions' (2013) 5(2) *Hague Journal on the Rule of Law* 253, 253–5.

system is ineffective for reasons such as corruption alternative regulatory strategies and the use of informal or soft law may be successfully used.

Voluntary corporate governance codes, which include provisions relating to disclosure, do have the features of informal or soft law in that they are a series of recommendations oriented towards good practice. Non compliance with them generally requires an acknowledgement of this and an explanation of why they have not been complied with. However, a number of jurisdictions including Belgium and the Netherlands and, as will be seen, Indonesia, have enacted parts of the codes as standards in corporate and securities laws. As informal law the codes permit the use of market based and self-regulatory sanctions. In this way they can form the lower level of intervention in regulatory strategies including the well known pyramidal escalation of penalties developed by Braithwaite and Ayres. These can include negative publicity, public criticism and embarrassment. They may assist in ensuring the accurate disclosure which is required to maintain the required trust for shareholders and other stakeholders.

Alternative regulatory strategies require the use of informal or soft law. How these are distinguished from formal law is generally in terms of the latter being promulgated within the legal system associated with the state and sanctions for their breach imposed by the state. Informal law, on the other hand, are standards or norms recognized as being legitimate in their use even though they are not the rules enforced by the state. They are marked by obligations to behave in particular ways in specific contexts or expectations to conform to particular standards. A number of writers, including Parkinson, argue that for regulation to be effective there needs to be a mixture of formal and informal law. This provides a range of private and public tools to be used. It may be seen in the adoption of provisions in voluntary' self-regulatory corporate governance codes into formal legislative statements of the law.

The chapter concluded with a discussion of key principles from comparative law, including the concept of transplants. Transplants have been common across legal systems. It is noted that in comparative legal theory there has been some recognition that it included formal and official law, or the law in the books, as well as cultural aspects of law in a particular society including legal cultures. This is particularly relevant where the law being

compared is an informal law or soft law and it is used in regulatory processes as is the case with corporate governance codes. Comparative law is commonly recommended as a source to be used in law reform. There is disagreement over how easily legal transplants may be made and the extent to which their success depends on non-legal factors. Writers such as Kahn Freund observed as long ago as the 1970s that globalisation was flattening out cultural diversity between nationals' laws making formal legal principles increasingly decoupled from local society and potentially making legal transplants easier. However, informal and soft law represented by corporate governance codes is more closely related to norms based in social practices and expectations and affected by legal culture, accounting, technological, political and economical circumstances.

A number of critical issues have been identified to be addressed in the Indonesian context of corporate disclosure. The analysis of the concept of comparative law and legal transplants demonstrates that the connection between formal law and various aspects of culture is crucial in successful legal transplants including the adoption of foreign ideas to corporate disclosure in Indonesia. These issues are addressed in the next two chapters.

Chapter 3 considers the impact of globalization on Indonesia and how it has driven the reform of Indonesian law and regulatory practices relating to disclosure. It also considers the experiences of some South East Asian countries in the implementation of corporate governance codes and some of the significant informal or soft law that has impacted on those jurisdictions including the local ethos around anti corruption, business and political cultures and trust.

Chapter 4 considers the local features of Indonesian culture which impact on disclosure in Indonesia because of their influence on alternative regulatory strategies through informal or soft law in a world where cultural differences may be more resistant to being flattened.

Chapter 3 : The internationalisation of corporate governance and the use of corporate governance codes in different jurisdictions

3.1. Introduction

This chapter explores the forces that have led to Indonesia accommodating new principles of corporate governance and informal and soft law associated with corporate governance and disclosure within its domestic legal and regulatory systems. It considers the impacts of globalization and internationalization in the promotion of corporate governance and the OECD Principles of Corporate Governance. The principles of corporate governance represent transplants: a concept from comparative law described in the previous chapter.

This chapter also investigates the impact of economic crises that led to the highlighting of the significance of corporate governance in global patterns of development and economic stability. These crises led to an international body requiring Indonesia to adopt transplanted principles of corporate governance. It considers the experience of other developing economies that have adopted similar corporate governance codes and whether Indonesia could adopt some successful reform strategies found in them to improve its own implementation of them. It concludes with a discussion of whether the origins of national legal systems in common law or civil law may affect the effectiveness of implementing soft law, which is represented by corporate governance voluntary codes embodying disclosure principles.

3.2. The stimulus of the forces of globalisation and internationalisation on trends in corporate governance

3.2.1. Introduction

Globalisation has been seen as ‘one of three great forces shaping the world through the rapid advance of hugely complex worldwide networks of money, resources, production and consumer needs’.⁵²⁴ Nelson refers to it as ‘an irresistible force driving all countries

⁵²⁴ Robert Shapiro cited in Adrian Davies, *The globalization of corporate governance: The challenge of clashing cultures* (Govwer Pub, 2011) 77.

toward common economic, political, and even cultural forms and practices'.⁵²⁵ It creates 'a new way of ordering a wide variety of different economies and cultures to achieve a new and richer synthesis'.⁵²⁶

Globalisation in this sense has led to free trade and free capital mobility that has further entrenched the global integration of national economies.⁵²⁷ It frees up the international movement of goods and capital. This free trade in goods is seen as beneficial and the free trade in capital is seen as even more beneficial.⁵²⁸ This has led to an increase in international trade that has further intensified internationalization.⁵²⁹ Internationalisation has increased the significance of international product markets and capital and also the governance of companies involved in these.⁵³⁰ It has been claimed that corporate governance is a 'compelling force in the transformation of the world economy'. Its role impacts on both private and public sector participation in global markets including capital markets.⁵³¹ This increases the interdependence between countries and their peoples.⁵³²

Globalisation has also had a significant impact on corporate governance. The convergence it has produced the OECD Principles of Corporate Governance and in international trade treaties, which has changed Indonesian law and regulation and attracted

⁵²⁵ Douglas Nelson, *Globalization and corporate governance* (26 June 2009) Worldbank.org, 13 <http://siteresources.worldbank.org/INTRANETTRADE/Resources/239054-1239120299171/5998577-1244842549684/Nelson_Globalization&Corporate_Governance.pdf>.

⁵²⁶ Davies, above n 524, 78.

⁵²⁷ Herman E Daly, 'Commentary: Globalization versus internationalization – some implications' (1999) 31 *Ecological Economics* 31, 31–32. See also, Herman E Daly, 'Globalization versus Internationalization' on Global Policy Forum (1999), [1] <<https://www.globalpolicy.org/component/content/article/162/27995.html>>.

⁵²⁸ Ibid.

⁵²⁹ Alan Dignam and Michael J Galanis, *The globalization of corporate governance* (Ashgate, 2009) 91. Internationalization is described as 'a world of nations which increasingly act and interact with each other as separate and autonomous units, either directly or through their citizens'. See also, Daly, Commentary: Globalization versus internationalization, above n 527. It also increases the importance of international relations, treaties, alliances, etc.

⁵³⁰ Sven-Olof Collin et al, *Mechanism of corporate governance going international: Outlining a theory and initial test of the performance effects*, Department of Business Studies Kristianstad University College, 1 <<http://www.diva-portal.org/smash/get/diva2:640587/FULLTEXT01.pdf>>.

⁵³¹ Thomas Clarke and Marie dela Rama, *Introduction: The governance of globalization*, xvi <<http://www.ccg.uts.edu.au/pdfs/governance-and-globalization-intro.pdf>>. This is based on OECD study on the assumption of corporations on corporate governance's role.

⁵³² James A Caporaso and Mary Anne Madeira, *Globalization, Institutions & Governance* (Sage Publications, 2012) 73.

increasing foreign investment to Indonesia. The ASEAN Free Trade Agreement, for example, led Indonesian companies to comply with international practices required by it.⁵³³ Claims that ‘good corporate governance can improve national economic performance’⁵³⁴ increased the pressure on Indonesia to accommodate these external standards. Internally it was also promoted as a way to boost national economic development. Applying good corporate governance, it was claimed, would have a significant benefit for Indonesia because it would attract foreign investment and international trade to support the country’s economic development. In particular, after the economic crises of 1997 and 2008, new sources of capital have been needed.

The other impacts of globalization will be discussed below.

3.2.2. Towards corporate governance convergence

As indicated earlier, globalization has been associated with creating a convergence of corporate governance. Convergence has two different aspects, ie: convergence in form and convergence in function. Convergence in form ‘relates to increasing similarity in terms of legal framework and institutions’.⁵³⁵ In the discussion in the previous chapter this is what is described in comparative law as the “law in the books”. Convergence in function refers to the fact that ‘different countries may have different rules and institutions but may still be able to perform the same function such as ensuring fair disclosure or accountability by managers’.⁵³⁶ This can also acknowledge the role of informal or soft law. Generally in practice it is convergence in function that is aimed for. This recognises that ‘there is no single model of corporate governance and each country has through time developed a wide

⁵³³ William E Daniel, ‘Corporate governance in Indonesian listed companies: a problem of legal transplant’ (2003) 15(1) *Bond Law Review* 345, 358.

⁵³⁴ Jennifer Hill, ‘The persistent debate about convergence in comparative corporate governance’ in Jeffrey N Gordon & Mark J Roe (eds), *Convergence and persistence in corporate governance* (2004), 743.

⁵³⁵ Toru Yoshikawa and Abdul A Rasheed, ‘Convergence of corporate governance: Critical review and future direction’ (2009) 17(3) *Corporate Governance: An International Review* 388, 389.

⁵³⁶ *Ibid.*

variety of mechanisms'.⁵³⁷ The OECD Principles of Corporate Governance permit them to be adapted to the fit with the formal and informal law of each jurisdiction.

The impact of globalization on convergences in corporate governance is reflected in a number of studies. Saheed demonstrated that globalization has influenced corporate governance practices providing 'an international benchmark for policy makers on issues of corporate governance'.⁵³⁸ Convergence, it is claimed, is forming international best practices.⁵³⁹ Nelson also considered that the convergence seen in national corporate governance regimes and practices is a product of globalization. It is 'the primary source of pressure for change in corporate governance practices and regimes'.⁵⁴⁰ It places governments and companies under pressure to adopt the most efficient corporate governance practices.⁵⁴¹ Khanna, Kogan, and Palepu also see that globalization is an accelerator of the convergence of corporate governance towards international standards.⁵⁴² However, some other studies have shown that 'national systems of corporate governance had been quite robust to globalization'.⁵⁴³

Indonesia has needed to respond to this convergence in corporate governance reflecting contemporary business activities and also international economic policies and accompanying transnational regulatory policies. It needs to ensure that changes within its own legal and regulatory systems, as part of this convergence, are effective both in practice

⁵³⁷ Maria Maher and Thomas Andersson, *Corporate governance: Effects on firm performance and economic growth* (1999) Organisation for Economic Co-operation and Development, 3 <<http://www.oecd.org/sti/ind/2090569.pdf>>.

⁵³⁸ Zakaree Saheed, 'Impact of globalization on corporate governance in developing economies: A theoretical approach' (2013) 2(1) *Journal of Business and Management* 1

⁵³⁹ Kaneko Yuka, 'Theories and realities of Asian corporate governance: From 'Transplantation' to the Asian Best Practices' (2010) 2(5) *Procedia Social and Behavioral Sciences* 6883, 6883 <http://ac.els-cdn.com/S1877042810011730/1-s2.0-S1877042810011730-main.pdf?_tid=8cd5c1f8-d4f1-11e3-8f5e-00000aab0f01&acdnat=1399362146_9afc57f33427f4c85f805a01c8da6298>.

⁵⁴⁰ Nelson, Douglas, above n 525, 13, 17, 21.

⁵⁴¹ Xun Wu, 'Corporate governance and corruption: A cross-country analysis' (2005) 18(2) *An International Journal of Policy, Administration, and Institutions* 151, 152 <http://actoolkit.unprme.org/wp-content/resourcepdf/cg_corr_xw1.pdf>.

⁵⁴² Tarun Khanna, Joe Kogan and Krishna Palepu 'Globalization and similarities in corporate governance: A cross-country analysis' (CEI Working paper series, No. 2002-6, Center for Economic Institutions Hitotsubashi University, 9 August 2002) 1 <<http://hermes-ir.lib.hit-u.ac.jp/rs/bitstream/10086/13927/1/wp2002-6a.pdf>>. Others 'maintain that such convergence will not occur because of a variety of forms of path-dependence'.

⁵⁴³ Nelson, Douglas, above n 525, 18–19.

and cost. The literature relating to the benefits that may be achieved by implementing good corporate governance principles are summarised in Chapter 2, at [2.2] the concept and function of corporate governance and the role of disclosure in particular at [2.3] the role of disclosure in corporate governance frameworks. Three factors that are significant in driving convergence, at least in principle, are the competition in attracting investment, in promoting stability in national and international economic systems and stimulating national and international economic and social development.

3.2.3. Attracting global investors

As indicated above, one of the impacts of globalisation through the internationalization of corporate governance has been a need for nations to attract global investors.

As a part of globalization the internationalization of corporations has become a central feature of commerce and financial markets in which the movement of capital and direct foreign investment growth has surpassed that of commodities.⁵⁴⁴ Convergence in corporate governance and associated disclosure to investors should encourage both direct and portfolio foreign investment.⁵⁴⁵ This is one way in which corporate governance is seen as ‘an effort to improve corporate efficiency and to attract external capital funds’.⁵⁴⁶ It is believed to ‘lead to the more efficient allocation of capital by improving saver’s access to investment opportunities and companies’ access to financing’.⁵⁴⁷

Growing evidence shows that ‘firms are adopting corporate governance arrangements that international investors appear to value’⁵⁴⁸ in a significant effort to attract global investors. The need for external funding is considered by Davies as the key underlying driver of corporate governance.⁵⁴⁹ This suggests that a firm that has applied recognised corporate governance principles will be attractive to investors. It demonstrates

⁵⁴⁴ Clarke and dela Rama, above n 531.

⁵⁴⁵ Saheed, above n 538.

⁵⁴⁶ Maher and Andersson, above n 537, 30.

⁵⁴⁷ Mary O’Sullivan, *Corporate governance and globalization*, INSEAD – The Business School for the world, 4 <https://flora.insead.edu/fichiersti_wp/inseadwp1999/99-71.pdf>.

⁵⁴⁸ Maher and Andersson, above n 537, 30.

⁵⁴⁹ Davies, above n 524, 51.

an intention to effectively use investor's funds to produce consistent returns for them.⁵⁵⁰ Studies of governance and disclosure have demonstrated that 'the quality of governance practices is positively related to growth opportunities, the need for external financing'.⁵⁵¹

Corporate governance is considered crucial for Indonesia as 'foreign investment is a "must"⁵⁵² for economic development. As Lindsey indicated in the context of Indonesia 'economic development cannot occur without capital' and that the 'ability to attract foreign capital and retain domestic capital' is a principal factor for any developing economy's success.⁵⁵³ The Indonesian government acknowledges that foreign capital investment has a major role to play in the development of the country's economy.⁵⁵⁴

The implementation of corporate governance and enhanced disclosure in Indonesia is seen 'as an effort to attract investors to purchase equity or debt instruments in the domestic stock market'⁵⁵⁵ particularly after the economic crises of 1997 and 2008. The impact of these crises will be discussed in the following sub-chapter.

3.3. The impact of economic crises on the demand for good corporate governance practices

3.3.1. Introduction

As indicated, the convergence in corporate governance principles and their efficacy in attracting global investors have contributed to the further development of corporate governance. As indicated in Chapter [2.2], the concept and function of corporate governance, the importance of avoiding economic crises and creating stability in economic systems has led to the acknowledgement of corporate governance in achieving these goals.

⁵⁵⁰ Ibid 51.

⁵⁵¹ Craig Doidge, G Andrew Karolyi and Rene M Stulz, 'Why do countries matter so much for corporate governance?' (2007) 86(1) *Journal of Financial Economics* 1, 2.

⁵⁵² Sudargo Gautama, 'Recent developments concerning investment in Indonesia (with special reference to the new Company Law 1995)' (1997) 1 *Singapore Journal of International & Comparative Law* 117, 117 <<http://law.nus.edu.sg/sybil/downloads/articles/SJICL-1997-1/SJICL-1997-117.pdf>>.

⁵⁵³ Tim Lindsey, 'Legal infrastructure and governance reform in post-crisis Asia: The case of Indonesia' (May 2004) 18(1) *Asian-Pacific Economic Literature* 12, 14.

⁵⁵⁴ National University of Singapore, 'Recent developments concerning investment in Indonesia (with special reference to the new Company Law 1995)' (1997) 1 *Singapore Journal of International & Comparative Law* 117.

⁵⁵⁵ Daniel, above n 533.

This has both promoted the further development of corporate governance and disclosure principles at a global level and increased interest in them at the national and corporate levels.

The turn to good corporate governance principles and related law reforms for this reason is being seen in Indonesia.⁵⁵⁶ Young supports this by claiming that corporate governance has been mainly enacted in response to individual corporate collapses, particularly where they have revealed systemic risks in national economic systems.⁵⁵⁷ A number of incidents confirm this claim.

In the UK the Committee on the Financial Aspects of Corporate Governance, chaired by Sir Adrian Cadbury, led to the Cadbury Report. It was established as a reaction to the collapse of BCCI, Polly Peck and Maxwell Communications.⁵⁵⁸ The report introduced recommendations in the form of a Code of Best Practice. The method of enforcement arrangement was through the London Stock Exchange, which included the Code as an appendix to its listing rules. It required listed companies to comply with the Code provision or explain why they failed to do so.⁵⁵⁹

Australia's Bosch report of 1995 was the delayed response to the collapse of a number of prominent companies: Rothwells (1986), Elders (1986), Bond Corporation (1987), Tricontinental (1989), Pyramid Building Society (1990) and Quintex (1990).⁵⁶⁰

The OECD Principles of Corporate Governance of 1999 were also issued in the context of the severe Asian economic crisis of 1997.⁵⁶¹

The Sarbanes-Oxley Act 2002, which contains extensive principles relating to corporate governance and disclosure, was enacted in response to a number of corporate

⁵⁵⁶ T Mulya Lubis and Mas Achmad Santosa, 'Economic regulation, good governance and the environment: an agenda for law reform in Indonesia' in Arief Budiman, Barbara Hatley and Damien Kingsbury (eds), *Reformasi – Crisis and change in Indonesia* (Monash Asia Institute, 1999) 345, 346.

⁵⁵⁷ Raymond Young, *A brief history of corporate governance* (July 27, 2009) i, 1 <<http://ise.canberra.edu.au/raymond/>>.

⁵⁵⁸ *Ibid.*

⁵⁵⁹ Brian R Cheffins, 'The history of corporate governance' (Working Paper No. 184/2012, University of Cambridge and ECGI Law, January 2012) 19

<http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1975404>.

⁵⁶⁰ Young, above n 557.

⁵⁶¹ Cheffins, above n 559, 21.

disasters in 2001 including the collapse of Enron, WorldCom, Tyco, Adelphia and Qwest.⁵⁶² Its changes to corporate governance extended to the board of director's responsibilities. The Act was seen as a milestone on the way to better corporate governance.⁵⁶³ Although the global financial crisis of 2008, and the further scandals revealed by it, affected the credibility of the US model of corporate governance.⁵⁶⁴

3.3.2. The recognition of the significance of corporate governance

After the economic crises of 1997 and 2008, the concepts of good corporate governance and disclosure and their application have become even better known and enjoyed more popular support. As well as avoiding crises or reducing their impact, this interest also relates to the claims that they have a pivotal role, as indicated in Chapter 2, in developing economies and societies. The literature cited also indicated that at the level of a specific company, better corporate governance further facilitated achieving the company's goals, preventing business failures, limiting the risk of serious fraud and better protection for investors including ensuring investment returns.

Those responses have contributed to a notable development of corporate governance that widely occurred around the world as discussed below.

3.4. Developing a global corporate governance system

3.4.1. The evolution of corporate governance

Relevant literature introducing corporate governance is covered in Chapter 2 at [2.2]: the concept and function of corporate governance. It noted the distinction between broader and narrower uses of the term. Many of the issues corporate governance deals with occurred before the term was developed. They are seen, for example, in the English speaking world in the history of the British East India Company, the Hudson's Bay Company, the Levant Company and the other chartered companies in the 16th and 17th centuries. The term itself first became popular in the United States in the 1970s.⁵⁶⁵ There

⁵⁶² Young, above n 557.

⁵⁶³ S Shalahuddin, *Bab II: Konsep good corporate governance* [Chapter II: A concept of good corporate governance], Faculty of Law University of Indonesia, 29–30 <lontar.ui.ac.id/file?file=digital/...Good%20corporate...>.

⁵⁶⁴ Cheffins, above n 559, 22.

⁵⁶⁵ Ibid.

are competing claims that it was in use in the US after the Wall Street crash in 1929 and the banking crisis in the UK in 1970.⁵⁶⁶

The corporate and securities law of the United Kingdom and the United States, as well as their corporate structures and practices, have made a significant contribution to the development of corporate governance internationally. The Cadbury report and the US corporate governance models, particularly around disclosure in securities regulation, have been important sources. The Cadbury report became a model for the development of corporate governance codes around the world.⁵⁶⁷ It is seen as the source of many contemporary ideas of corporate governance. The US corporate governance model has provided an international archetype based partly on the prosperity of the US economy, which uses it, as well as the economic ascendancy and dominance of its companies globally during the second part of the 20th century and into the 21st.⁵⁶⁸ The term corporate governance was consistently used in the US Federal Register, the journal of the federal government, and the federal Securities and Exchange Commission (SEC) in 1976. By the 1990s it saw widespread use.⁵⁶⁹

Cheffins supports the claim that the contemporary corporate governance movement began in the US. It then ‘had become established in the UK and put down roots in continental Europe and Japan’.⁵⁷⁰

A notable development has been the establishment of a number of public and private institutions to promote better corporate governance. One significant example of this

⁵⁶⁶ Muhamad Said Didu, ‘GCG cegah intervensi [GCG prevents intervention], *Majalah Akuntan Indonesia* – edisi no,1/Tahun I/Agustus 2007 [Indonesian Accountant Magazine – 1st edition/Year I/ August 2007] (online), 14 <http://74.220.207.194/~iaigloba/storage/ref_14.pdf>.

⁵⁶⁷ Cheffins, above n 559, 19.

⁵⁶⁸ Ibid 17.

⁵⁶⁹ Ibid 2. See also, page 5, 17, 19 & 20. The earliest theory of the term corporate governance can be found in the 1976 book on ‘Taming the Giant Corporation’ written by Ralph Nader, Mark Green and Joel Seligman. The term governance was used multiple times by Jensen and Jerold Warner in a *Journal of Financial Economics* in 1980s. The 1990s was claimed as the decade of corporate governance. By the early 1990s the corporate governance topic became extensively used. Prior to the 1990s, the use of corporate governance as a term was just mentioned once in the Times newspaper, but then in 1991, it began being widely used when it established the Committee on the Financial Aspects of Corporate by the accountancy profession, the London Stock Exchange and the Financial reporting Council in which regulating accounting standards in the U.K.

⁵⁷⁰ Cheffins, above n 559, 20.

is the Asian Corporate Governance Association founded in 1999 in Hong Kong with sponsorship from US and European investment funds seeking to improve corporate governance practices in Asian listed companies so that they would be better able to invest in companies in rapidly growing economies.⁵⁷¹ Codes relating corporate governance were also sponsored globally to address the insufficiency of existing national regulations regarding shareholder's rights and as a measure to achieve international legitimacy by meeting the expectations of foreign investors.⁵⁷²

Global development and international organization pressures have largely contributed to the transposition of corporate governance globally. In Indonesia, the most intense pressures came from the IMF in the conditions it forced on the government to reform corporate law, including corporate governance in the process of assisting Indonesia recover from the Asian currency crisis of 1997.⁵⁷³ This led to significant changes in Indonesian corporate and securities law and regulation, including the adoption of codes and informal and soft law as part of a more comprehensive approach to improve corporate governance and related disclosure.

3.4.2. The wider use of corporate governance concepts and systems

The drive to improve corporate governance globally has led to a need to address two different models of corporate structures, which have become archetypes. They are the outsider and insider systems. The outsider system, sometimes called shareholder system, is a market based system or Anglo-American system commonly found in common law and in Anglo- American countries. The US and the UK are the archetypical countries. "Outsider" refers to the wider distribution of shareholders. The insider system is referred to as a relationship based or stakeholder system. The archetypes for this system have been Germany and Japan. This system is seen in other continental European and Asian relationship based systems.⁵⁷⁴ The distinctive differences in terms of the structure of

⁵⁷¹ See, Asian Corporate Governance Association, *About ACGA* <http://www.acga-asia.org/content.cfm?SITE_CONTENT_TYPE_ID=21>; Asian Corporate Governance Association, *Members* <http://www.acga-asia.org/content.cfm?SITE_CONTENT_TYPE_ID=36>.

⁵⁷² Miko Kamal, *Corporate governance for state-owned enterprises: a Study of codes of corporate governance* [1] <www.fmb.unimore.it/on-line/Home/Eventi/.../documento8366.htmlIn>.

⁵⁷³ See, Manning and van Dierman (eds), above n 9.

⁵⁷⁴ Thomas Clarke and Marie dela Rama, 'The Fundamentals Dimensions and Dillemas of

control are described in Tables 3.1 and 3.2 below. They are generalisations and may not accurately represent all forms of insider or outsider systems. For example, Australia has common law and may be associated with the Anglo-American model but like some other common law countries, has a significant number of companies that are not controlled by outsiders.⁵⁷⁵ The two models' financial systems are described in Tables 3.1 and 3.2.

Table 3.1: The two widely used models of corporate governance systems

	Outsider [shareholder] system / Market based system	Insider [stakeholder] system / Relation based system
Jurisdictions	Initially developed in the UK and the USA ⁵⁷⁶ Specifically found in common law – Anglo-American countries ⁵⁷⁷	Specifically found in Japan and Germany ⁵⁷⁸ The rest of the world ⁵⁷⁹
General features ⁵⁸⁰	Rule-based governance, arm's length contracting; based on impersonal and explicit agreements Disclosure of material information to market	Relation-based governance Most relevant information only available for insiders
Specific feature ⁵⁸¹	Public good (trust)	Private good (social capital)

Corporate Governance' in Thomas Clarke and Marie dela Rama (eds), *Fundamentals of Corporate Governance* (SAGE, 2008) 2 <<http://www.ccg.uts.edu.au/pdfs/fundamentals-of-cg.pdf>>.

⁵⁷⁵ Alan J Diagnam and Michael Galanis. 'Australia Inside/Out: The Corporate Governance System of the Australian Listed Market' (2004) 28(3) *Melbourne University Law Review*.

⁵⁷⁶ Lay-Hong Tan and Jiangyu Wang, *Modelling an effective corporate governance system for China's listed state-owned enterprises – Issues and challenges in a transitional economy*, 1 <<http://eastlaw.net/jyworks/tan-wang-corp.gov.pdf>>.

⁵⁷⁷ Bishop's University Canada, *Comparative corporate governance: A global perspective*, 1 <<http://www.ubishops.ca/faculty/cvalsan/CorporateGovernance/TextMoreComparativeCG.pdf>>.

⁵⁷⁸ Tan and Wang, above n 576.

⁵⁷⁹ Bishop's University Canada, above n 577.

⁵⁸⁰ Ibid 16.

⁵⁸¹ Andrew D Clarke, 'The models of the corporation and the development of corporate governance' (2005) *Corporate Governance eJournal* 1, 4 & 6 <<http://epublications.bond.edu.au/cgi/viewcontent.cgi?article=1001&context=cgej>>. The non-recognition of employees is the Berle model and the recognition of employees is the Dodd model. The first model (contrarianism) focuses on shareholders. The latter model (communitarian

	Non-recognition of employees; may not be formally recognized in statute or in other formal sources; blocks employees from a participatory role in the corporation. More responsive to change	The recognition of employees (communitarian paradigm); formally recognized and accepted as integral participants in corporate governance. Changes to policies and implementation involve relations with stakeholders ⁵⁸²
Pattern of share ownership ⁵⁸³	Widely dispersed	Concentrated
Management focus and control ⁵⁸⁴	Investor and shareholder-centric; ⁵⁸⁵ focus on investor return maximization ⁵⁸⁶	Stakeholders with a focus on stakeholder value maximization ⁵⁸⁷
Conflicts of interest or agency ⁵⁸⁸	Between strong managers and widely-dispersed shareholders	Between controlling shareholders (or block holders) and weak minority shareholders
General characteristics ⁵⁸⁹	Priority to market and its regulation;	Priority to stakeholders' control;

paradigm) in Germany with provision of formal mechanism for employees and Japan with soft, informal provisions. See also, Christel Lane, below n 584.

The form of corporate governance in Germany focuses on labour as a stakeholder and on the opportunity of labour participation in strategic decision-making and the adoption of a high-skill/high-security model of human resources development.

⁵⁸² Colin Mayer, 'Financial systems and corporate governance: A review of the international evidence' (Mar.1998) 154 (1) *Journal of Institutional and Theoretical Economics (JITE)* 144, 144 <http://www.jstor.org/stable/40752051?seq=1#page_scan_tab_contents>.

⁵⁸³ Maher and Anderson, above n 537; See also, Qiang, below n 592, 775; Denis and McConnell, below n 591.

⁵⁸⁴ Christel Lane, *Changes in corporate governance of European corporations: convergence to the Anglo-American model?* 1 <http://src-h.slav.hokudai.ac.jp/pdf_seminar/021106christel.pdf>. See also, Davletguldeev, below n 589.

⁵⁸⁵ Malla Praveen Bhasa, 'Relationship-based model of corporate governance: A competing governance model' [2005] *IUP Journal of Corporate Governance*, description page <http://www.iupindia.in/405/IJCG_Relationship_based_model_of_Corporate_Governance_47.html>.

⁵⁸⁶ Marc Goergen, Miguel C Manjon and Luc Runneboog, *Is the German system of corporate governance converging towards the Anglo-American model?* (23 February 2008), 38 <http://link.springer.com/static/pdf/316/art%253A10.1007%252Fs10997-007-9040-7.pdf?auth66=1380436002_6c7352570234de7abe77b513fae089a2&ext=.pdf>.

⁵⁸⁷ Ibid.

⁵⁸⁸ Maher and Andersson, above n 537.

	<p>Owners have transitory interests in the company;</p> <p>Absence of close relationship between shareholders and management;</p> <p>Active market for corporate control;</p> <p>Shareholders rights have primacy over other stakeholders.</p>	<p>Owners have an enduring interest in the company; and often hold positions on the board of directors or other senior manager positions;</p> <p>Close and stable relationship between management and shareholders;</p> <p>Limited market for corporate control;</p> <p>Formal rights for employees to influence key managerial decisions.</p>
Key governance mechanisms ⁵⁹⁰	Market for corporate control; legal protections; independent boards; contractual incentives	Contractual incentives; and direct control from block-holders (banks and families)
Legal protection ⁵⁹¹	Strong	Weak
Source of discipline/sanctions	Market (shareholders selling shares, or hostile takeover) ⁵⁹²	Stakeholders influencing management ⁵⁹³

The insider system which is seen in both Europe and Asia differs between the two regions as described in Table 3.2.

Table 3.2: The different characteristic of the insider system or relationship based systems

European relationship based system	Asia Pacific relationship based system	Outsider or market based Anglo-American
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⁵⁸⁹ Roustem Davletguldeev, 'Two models of corporate governance – The role of employees as stakeholders in corporate governance' (Trade Union Advisory to the OECD Third Eurasian Roundtable on Corporate Governance, Bishkek, 29–30 October 2003) 6–7 <www.oecd.org/daf/ca/corporategovernanceprinciples/19802369.ppt>.

⁵⁹⁰ Dale Griffin, *National culture, Corporate Governance systems and Firm Corporate Governance practices*, 2 <<http://northernfinance.org/2012/program/papers/365.pdf>>.

⁵⁹¹ Diane K Denis and John J McConnell, 'International Corporate Governance' (2003) 38 (1) *Journal of Financial and Quantitative Analysis* 1, 27.

⁵⁹² Qu Qiang, 'Corporate governance and state-owned shares in China listed companies' (October 2003) 14 (5) *Journal of Asian Economic* 771, 775. Sanctions to unsatisfactory corporation's performance.

⁵⁹³ Bhasa, above n 585.

		system
Dualistic with two separate boards – Germany (separating the power and control between two groups, those who are managing the firm and those who are exercising supervisory control). ⁵⁹⁴	Pluralistic – Japan (numerous interest groups exercise power and control). ⁵⁹⁵	Monistic in that there is only one board (the board of directors is the centre of power & control). ⁵⁹⁶

The division between these two models of corporate governance are related to differences in the financial systems associated with them and described in Table 3.3

Table 3.3: Financial systems

	Market-based system	Bank-based system
Archetypes	Generally found in the USA-the UK model	Specifically found in German-Japanese model
Central roles in financing and governance activities ⁵⁹⁷	Capital market	Banks
Control mechanism	Market	Core investors: commercial banks monitor and control the managers ⁵⁹⁸

⁵⁹⁴ See, Hauwa Lamino Abubakar, *The Impact of Sound Corporate Governance on the Productivity of firm*, 78 <http://www.academia.edu/2767584/The_Impact_of_Sound_Corporate_Governance_on_Organizational_Performance>. The dualism is widely used in Germany. Corporate governance differentiates between the groups who are leading the firm, and the group who exercises the control. Power and control are separate between those two groups to serve better stakeholders interests. This is the principle of cooperative decision making within the board of directors. See also, Goergen, Manjon and Runneboog, above n 586, 50. Wealthy individuals and families dominate control in German corporation.

⁵⁹⁵ These companies are marked by dual boards in the German model. In 2002 the Japanese Commercial Code was revised to permit companies to retain the dual structure of directors and statutory auditors or to have a board with committees on the model of the Anglo-American company. See, Hiroyuki Itami, 'Revision of the Commercial Code and Reform of the Japanese Corporate Governance' (2005) 2(1) *Japan Labor Review* 4–25.

⁵⁹⁶ See, Abubakar, above n 594. It refers to highly shareholder oriented. The corporation is seen as the private property of its owners. The principle of directorship dominates based on the authority of the CEO. The CEO has the responsibility and therefore his performance is crucial.

⁵⁹⁷ Goergen, Manjon and Runneboog, above n 586, 39.

⁵⁹⁸ Qiang, above n 592.

Benefits	Markets as the key financial services stimulate innovation and long run growth ⁵⁹⁹	Allocation of capital by banks mobilises savings, allocates capital, and exerts corporate control
Financial assets and liabilities ⁶⁰⁰	Tradeable securities in financial markets.	Through bank deposits and direct loans ⁶⁰¹

As indicated above these distinctions are generalisations and differences will be found between these systems in different jurisdictions. They are ‘based on historical cultural and institutional differences that involved different approaches to the values and objectives of business activity’.⁶⁰² Germany and Japan, for example, have typically relationship-based systems and bank-centred economies with financial institutions exercising significant control over firms. However, Germany has a different structure of equity ownership to Japan. Financial institutions ‘are the most important block-holders in Japan’ meanwhile other companies ‘are the most prevalent block-holders in Germany’.⁶⁰³

In East Asia, China demonstrates a distinct difference in its corporate governance system although its corporate law is based on a German Japanese model of dual boards allowing stakeholder interests to be represented. Many of its most significant listed companies are divisions of state owned enterprises (SOEs). They have a very high concentrated ownership, which is an indicator of relation-based systems and lack many necessary market-based mechanisms. China has some Anglo-American characteristics with their board of directors including independent directors who are nominally influential in the

⁵⁹⁹ Ross Levine, ‘Bank-based or Market-based financial systems: Which is better?’ (Working Paper No. 442, William Davidson Institute, February 2002) 23 <<http://deepblue.lib.umich.edu/bitstream/handle/2027.42/39826/wp442.pdf?sequence=3>>.

⁶⁰⁰ Sigurt Vitols, ‘The origins of bank-based and market-based financial systems: Germany, Japan and the United States’ (Discussion Paper No. FS 101 – 302, Wissenschaftszentrum Berlin für Sozialforschung, Provided in Cooperation with Social Science Research Center Berlin, 2001) 1 <<http://skylla.wz-berlin.de/pdf/2001/i01-302.pdf>>.

⁶⁰¹ Levine, above n 599, 25. Empirical assessment on the bank-based view – particularly at early stages economic development and in weak institutional settings.

⁶⁰² Clarke and dela Rama, The Fundamentals Dimensions and Dilemmas of Corporate Governance, above n 574, 2.

⁶⁰³ Denis and McConnell, above n 591, 11.

committee system.⁶⁰⁴ Tan and Wang claim that neither the outsider nor insider system provides suitable classifications for China, given the absence of a number of characteristics associated with both.⁶⁰⁵

Indonesia, as described further in Chapter [4.2.2.2], has a dual board structure inherited from Dutch law which is constituted by the board directors and the board of commissioners. It has been claimed it follows a Japanese relationship-based model in corporate structures and governance.⁶⁰⁶ In fact, some of the characteristics of its companies are similar to Chinese companies. Amongst others, the main banks have been an assured source of easy credit for enterprises. There have been weak management incentives in state owned enterprises, which have hived off listed companies. The dominance of the state as owner ensures its power over the companies, including the appointment of management and their remuneration.⁶⁰⁷ Most board members and managers are civil servants with their remuneration and promotions relying on the assessment of superiors in the political and administrative hierarchy instead of on performance.⁶⁰⁸

Despite Indonesia's corporate governance system is generally classified as a relationship based-system with a financial system based on banks. The country has adopted corporate governance codes and other aspects of corporate law and regulation, which derive from the market-based system. As indicated earlier, this is due to reforms that were intended to enhance its corporate governance system after the financial crises. This pressure to reform is one of the reasons the Indonesian Code of GCG was developed.

⁶⁰⁴ Tan and Wang, above n 576, 4.

⁶⁰⁵ Ibid 9 & 20. Outsider system natures such as active market for corporate control, competitive managerial manpower and products markets, a high degree of transparency and disclosure, arm-length transactions, independent board of directors and independent monitoring role of a strong court system, the mass media and professional bodies. The absent of German and Japanese bank-based mechanism amongst others Chinese banks are unable to carry out *ex post* monitoring of distressed client firm as Japanese banks do; and the main bank became the friendly bank and an assured source of easy credit for enterprises.

⁶⁰⁶ John Shuhe Li, *The benefits and costs of relation-based governance: An explanation of the East Asian miracle and crisis* (1998, new version 2000) 19, 21 <http://www.stanford.edu/~avner/Greif_228_2007/2000%20Li%20The%20Benefits%20and%20Costs%20of%20Relation-based%20governance.pdf>.

⁶⁰⁷ Qiang, above n 592, 777.

⁶⁰⁸ Ibid.

3.4.3. The prevalence of corporate governance codes

The use of corporate governance codes commenced with the Cadbury Code in the UK in 1992.⁶⁰⁹ This was in response to specific corporate collapses as indicated earlier.

The World Bank subsequently observed the increasing use of voluntary codes across the globe to drive corporate governance reform⁶¹⁰ including in Indonesia. Cunningham also observed that many jurisdictions adopted structures and mechanisms from other countries which were partly mandated by the IMF and the OECD and other transnational institutions to enhance their corporate governance regimes.⁶¹¹

The codes emerged 'as the main regulatory instrument with respect to shaping the direction of some crucial corporate governance-related issues'.⁶¹² The codes provide normative guidelines regarding shareholders and senior management relationships, remuneration, auditing and information disclosure, among others issues.⁶¹³ The codes are in the form of a set of best practices and are designed to address insufficiencies in existing institutions including formal law.⁶¹⁴

The codes promote general goals for improving a company's governance quality particularly focussing on a company's accountability to shareholders to maximize shareholder's or stakeholders' value.⁶¹⁵ This represents the common set of good corporate governance practices issued by the OECD. It represents a narrower concept of corporate governance, discussed in Chapter 2 at [2.2] the concept and function of corporate governance. It can be seen as part of the convergence toward a general global model.⁶¹⁶ Notwithstanding, the provisions in codes vary across the countries due to 'differences in

⁶⁰⁹ Haxhi and Aguilera, above n 364, 234, 239.

⁶¹⁰ Simon C Y Wong, *Developing and Implementing Corporate Governance Codes*, Private Sector Opinion (2008) A Global Corporate Governance Forum Publication, International Finance Corporation 3 <<https://openknowledge.worldbank.org/bitstream/handle/10986/11132/472770BRI0Box31SO1issue11001PUBLIC1.pdf?sequence=5&isAllowed=y>>.

⁶¹¹ Francesco de Zwart, *Global and National Comparative Corporate Governance Codes* (2007) 8 <<http://law.unimelb.edu.au/files/dmfile/DEZWARTFrancesco-GLOBALANDNATIONALCOMPARATIVECORPORATEGOVERNANCECODES2.pdf>>.

⁶¹² Haxhi and Aguilera, above n 364, 234.

⁶¹³ Ibid 239.

⁶¹⁴ Ibid 235.

⁶¹⁵ Ibid 239.

⁶¹⁶ Ibid 241.

ownership structure, legal and regulatory frameworks, and the nature of agency issues confronted'.⁶¹⁷

The study surveys some selected Asian countries below that share significant similarities with Indonesia. It represents the use of comparative law methodology and the practice of using it to assist in national law reform considered in Chapter 2 at [2.6] comparative law and legal transplants. It contributes to this study by possibly suggesting effective strategies for the use of voluntary corporate governance codes.

3.5. The use of corporate governance codes in South East and East Asian jurisdictions

3.5.1. Introduction

Lessons from the use of corporate governance codes in other comparable jurisdictions may contribute to the more effective application of such codes in Indonesia. They demonstrate that the successful implementation of such codes as a form of informal or soft law require support from other sources.

The similarities to Indonesia include the high concentration of ownership, family dominance, state control or ownership, linking political institutions and corporate governance, regulatory environments and corruption.⁶¹⁸

3.5.2. Singapore

Singapore, a common law jurisdiction, is regarded as being successful in implementing good corporate governance due to its anti corruption ethos and the political determination or commitment behind it.⁶¹⁹ Singaporean listed companies have similar characteristics to Indonesian companies including concentrated ownership, which 'potentially violates corporate governance principles'.⁶²⁰ Some are different in being

⁶¹⁷ Wong, above n 610, 5.

⁶¹⁸ Xun Wu, *Political institutions and corporate governance reforms in Southeast Asia* <http://www.spp.nus.edu.sg/docs/fac/wu_xun/Published%20Papers/Reforming%20Corporate%20Governance%20in%20SE%20A.pdf>.

⁶¹⁹ See, Koh Tech Hin, *Corruption Control in Singapore*, 122–31 <http://www.unafei.or.jp/english/pdf/RS_No83/No83_17VE_Koh1.pdf>.

⁶²⁰ Fama and Jensen cited in Yuen Teen Mak, 'Corporate Governance in Singapore: Past, Present and Future' in Ferdinand A Gul and Judy S L Tsui (eds), *The Governance of East Asian Corporations: Post-Asian Financial crisis* (Palgrave Macmillan, 2004).

controlled by government through state-ownership.⁶²¹ Singapore has been recognized as having better implemented good corporate governance practices compared with other South East Asian countries. This is believed to be one factor that led to it being affected less by the 1997 Asian currency crisis.⁶²² The government has further encouraged it on the basis that ‘good corporate governance is a key pillar underpinning Singapore’s reputation as a trusted financial and business hub’.⁶²³

This apparent successful implementation of corporate governance practices involves effective legal and corporate governance frameworks, institutional structures as well as business cultures. The *Companies Act*, the establishment of a number of supporting institutions that are indicated below, and also disciplined and ethical business practices are significant contributing factors. The regulatory system integrates different levels of the public and private sectors. The *Companies Act* is the primary source of company law including disclosure regulation governing the Registry of Companies and Business (RCB).⁶²⁴ The Act also provides for standards on accounting practices, and the rules of the Stock Exchange Listing Manual in the Statement of Accounting Standards (SAS). Other relevant legislation is the 1986 *Securities Industry Act* which provides for the regulatory functions of the Monetary Authority of Singapore (MAS) that, together with RCB, oversees compliance with disclosure requirements. The regulation of disclosure standards is governed by several different institutions, including the Singapore Exchange (SGX), the MAS, Securities Industry Council, the RCB and the Commercial Affairs Department of the Ministry of Finance. Private institutions are also involved such as the professional accounting association: the Institute of Certified Public Accountants of Singapore (ICPAS).

⁶²¹ Laura Oetterli, *A Comparative Analysis of the Corporate Governance of Public Enterprises in Singapore and Switzerland* (Thesis, University of Bern, 2014) 24–30 <http://www.rechtswissenschaft.unibe.ch/unibe/portal/fak_rechtwis/content/e6024/e6025/e118744/e144658/e271902/files271910/OetterliLaura_Masterarbeit_final_ger.pdf>.

⁶²² Mak, above n 620, 164.

⁶²³ Heng Swee Keat, Managing Director of the Monetary Authority of Singapore, ‘Corporate governance development in Singapore’ (Paper presented at the 2009 Asian investors’ Corporate Governance Conference, Bank for International Settlements, Singapore, 19 November 2009) 1 <<http://www.bis.org/review/r091123e.pdf>>.

⁶²⁴ Phillip H Phan and Toru Yoshikawa, *Corporate Governance in Singapore: Developments and Prognoses*, Singapore Management University <http://www.research.smu.edu.sg/faculty/edge/corp_gov/papers/Singapore%20CG.pdf>.

Singapore's Corporate Governance Code has also had a significant role in improving Singapore's corporate governance.⁶²⁵ The Barings Bank case is claimed to be a classic example of the failure of corporate governance and related to the absence of provisions now found in the Code. It related to deficiencies in internal controls and its compliance culture, the absence of risk management, and unethical behaviour by a key person.⁶²⁶

The Singaporean Code of Corporate Governance was issued in 2001. It was produced by the Corporate Governance Committee (CGC) that is led by the private sector.⁶²⁷ The Code of Corporate Governance was promulgated by the Ministry of Finance and the MAS and incorporated into the listing rules of the Singapore Stock Exchange (SGX).⁶²⁸ A review in 2004 by the Council on Corporate Disclosure and Governance (CCDG) produced a revised code in 2005. In 2012, the MAS revised the Code to reflect recent developments⁶²⁹ accepting all of the CCG's recommendations.⁶³⁰ The code addressed, among other issues, a claim that a comprehensive code was required, as

⁶²⁵ Ibid 21.

⁶²⁶ See, Lay Hong Tan, *Recent case studies on Corporate Governance in Singapore: The good, the bad and the ugly*, 5 <<http://www.clta.edu.au/professional/papers/conference2009/TanCLTA09.pdf>>. Barings Bank was Britain's oldest merchant bank and established a small office in Singapore in 1987 named Baring Securities (Singapore) Limited (BSS). The main business was on equities and futures trading on the floor of the Singapore International Monetary Exchange (SIMEX), now the Singapore Exchange. General Manager, Nick Leeson, manipulated the day trading books and created fictitious contracts that never existed in order to record profits in the reports that were sent to the head office in London. He was able to cover up his huge trading losses by putting it through the unused error account (8888), which was set up to cover losses of inexperienced traders and was hidden from the report to the head office. His action led the Bank collapsing.

⁶²⁷ Lenice Lim, 'Corporate governance – A survey of Australian and South East Asian systems' (2010) *Faculty of Law Bond University Corporate Governance eJournal*, 9 <<http://epublications.bond.edu.au/cgi/viewcontent.cgi?article=1018&context=cgej>>.

⁶²⁸ Jainty Gopalakrishnan, *Examination of the Singapore code of corporate governance and its impact on corporate reporting and investor perception/decision* (Dissertation, University of Nottingham, 2006).

⁶²⁹ Keat, above n 623.

⁶³⁰ Asian Corporate Governance Association, '*Library – Codes and Rules – Singapore*' [14] <http://www.acga-asia.org/content.cfm?SITE_CONTENT_TYPE_ID=12&COUNTRY_ID=276>. The key changes include the areas of director independence, board composition, director training, multiple directorships, alternate directors, remuneration practices and disclosures, risk management and shareholder rights and roles.

disclosure in annual reports were unsatisfactory and offered only minimum information.⁶³¹ The Accounting Standards Council initiated a proposal to revise the code in 2011, specifically requiring ‘company boards to take a more active role in checking financial statements and forcing more disclosure of management pay’.⁶³²

Compliance with the Code is on a non-mandatory basis.⁶³³ Some believe that compliance should be compulsory.⁶³⁴ Under the SGX Listing Rules, listed companies are required to disclose corporate governance practices including non-compliance with the principles in the Code in their annual reports.⁶³⁵ Some of the principles relate to key processes in corporate governance. They include: the type of material transactions that require board approval under internal guidelines (Guideline 1.5), whether a company considers a director to be independent in spite of a relationship that would deem the director not independent (Guideline 2.2), the relationship between the chair and the CEO where they are related to each other (Guideline 3.1), the composition of the audit committee and details of the committee’s activities (Guideline 11.8), and adequacy of internal controls – including financial; operational and compliance controls and risk management systems (Guideline 12.2).⁶³⁶

⁶³¹ Mak Yuen Teen, *Improving the Implementation of Corporate Governance Practices in Singapore* (26 June 2007) Monetary Authority of Singapore and Singapore Exchange, 6–7 <http://www.mas.gov.sg/~media/resource/news_room/press_releases/2007/CG_Study_Complete_Report_260607.pdf>. See generally, Monetary Authority of Singapore, *Code of Corporate Governance* (2 May 2012), below n 633. <http://www.mas.gov.sg/~media/resource/fin_development/corporate_governance/CGCRevisedCodeofCorporateGovernance3May2012.pdf>.

⁶³² ‘Singapore proposes shake-up of corporate governance code’, *Reuters* (online), 14 June 2011 <<http://www.uk.reuters.com/article/2011/06/14/singapore-governance-idUKL3E7HE0FZ20110614>>.

⁶³³ Monetary Authority of Singapore, *Code of Corporate Governance* (2 May 2012) <http://www.mas.gov.sg/~media/resource/fin_development/corporate_governance/CGCRevisedCodeofCorporateGovernance3May2012.pdf>.

⁶³⁴ Tan, above n 626, 8.

⁶³⁵ Monetary Authority of Singapore, *Code of Corporate Governance 2005: Board Matters*, 9 <http://www.mas.gov.sg/resource/fin_development/corporate_governance/CG%20Code%202005%20Code.pdf>.

⁶³⁶ *Ibid* 20–2.

The Accounting Standards Council (ASC) supports accounting regimes that enhance disclosure standards.⁶³⁷ The ASC has public and private sector participation, including representatives from the professional accounting body, the Institute of Certified Public Accountants of Singapore (ICPAS) and the SGX.⁶³⁸ In addition to the code and the listing rules the 1990 *Companies Act* also provides for detailed disclosure in financial statements.⁶³⁹

Even though poor enforcement of disclosure in Singapore has been identified, compared with developed economies, it is better than in other South East Asian countries.⁶⁴⁰ The Asian Corporate Governance Association in its Corporate Governance Watch 2012 report, placed Singapore as the best in corporate governance performance in Asia. It was rated as having the best corporate boards in Asia by the World Economic Forum in its Global Competitiveness Report 2011-2012.⁶⁴¹

3.5.3. Malaysia

Corporate governance implementation in Malaysia, a common law country, provides another example for Indonesia of better practice. Malaysia has a similar culture to Indonesia in having ‘a high power distance basis’.⁶⁴² It has family-dominated listed companies, cronyism, corruption and powerful political influences.⁶⁴³ It also experienced a financial crisis in 1997 due to, among other factors, weak corporate governance. The country has subsequently recorded a high score on corporate governance implementation. The Asian Development Bank (ADB) in 2013 ranked Malaysia as having higher quality

⁶³⁷ Tan, above n 626, 2.

⁶³⁸ Accounting Standards Council (Singapore), *Composition of Council* <<http://www.asc.gov.sg/council.htm>>.

⁶³⁹ Mak, above n 620, 157.

⁶⁴⁰ Ibid 163.

⁶⁴¹ Asian Developing Bank, ASEAN Corporate Governance Scorecard, above n 63.

⁶⁴² Theo Christopher and Salleh Hassan, ‘Culture and Corporate Governance Disclosure’ (Working paper series, School of Accounting, Finance and Economics, Edith Cowan University, Church lands West Australia, 2005) 3 <http://www.ecu.edu.au/_data/assets/pdf_file/0020/.../wp0513tc.pdf>.

⁶⁴³ Gomez and Jomo cited in Ong Wei Jiin, *Corporate Governance Disclosure in Malaysia, a Risk Management* (Dissertation, University of Nottingham, 2006) 24–5 <<http://www.edissertation.nottingham.ac.uk/357/1/0GMAlixwjo.pdf>>.

corporate governance compared with Indonesia, South Korea, Thailand and the Philippines.⁶⁴⁴ The ADB scored Malaysia at 71.69 compared with Indonesia at 54.55.⁶⁴⁵

The corporate governance framework in Malaysia includes the *Companies Act* 1965, the listing rules of the Bursa Malaysia (formerly the *Kuala Lumpur Stock Exchange*), the *Securities Commission Malaysia* and the Code on Corporate Governance. To strengthen the corporate governance framework the Finance Committee on Corporate Governance was established in 1998 with the aim to ‘provide a comprehensive report in measures to improve corporate governance’.⁶⁴⁶ It reported in 2002 and the code was introduced the same year. It was revised in 2007 and in 2012. The Code ‘was principally an initiative of the private sector, which ‘was based on the belief that self-regulation was preferable and standards developed by those involved would be more acceptable and more enduring’.⁶⁴⁷

Malaysia employs a more stringent approach in relation to compliance with the Code.⁶⁴⁸ This has been identified as a hybrid approach between prescriptive and non-prescriptive.⁶⁴⁹ A prescriptive approach is ‘where the standards of desirable practices for disclosure of compliance’ and a non-prescriptive one which only insists on disclosure of actual corporate governance practices’.⁶⁵⁰ A mandatory report is required to notify compliance with the Code.⁶⁵¹ Failure to comply will result in sanctions, including action against the company or its directors by the Bursa Malaysia as set out in the listing rules of

⁶⁴⁴ Lim, above n 627.

⁶⁴⁵ Ibid 5.

⁶⁴⁶ Philip Koh, *Corporate Governance in Malaysia: Current reforms in light of post 1998 crisis*, 43 <http://www.aicg.org/paper_2nd/Recent_Corporate_governance.pdf>.

⁶⁴⁷ Securities Commission (Malaysia), *2007 Malaysian Code on Corporate Governance* (Revised 2007) <<http://www.sc.com.my/eng/html/cg/cg2007.pdf>>. See also, Suruhanjaya Sekuriti Securities Commission Malaysia, *Malaysian Code on Corporate Governance 2012* <<http://www.sc.com.my/malaysian-code-on-corporate-governance-2012/>>. The Code was revised in 2012 considering market dynamics changes, international development, and the need to continuously recalibrate and enhance the effectiveness of the corporate governance framework.

⁶⁴⁸ Lim, above n 627.

⁶⁴⁹ Ong Wei Jiin, *Corporate Governance Disclosure in Malaysia* (a Risk Management Dissertation, University of Nottingham, 2006) 34 <<http://www.edissertation.nottingham.ac.uk/357/1/OGMALixwjo.pdf>>

⁶⁵⁰ Ibid 33–4.

⁶⁵¹ Securities Commission (Malaysia), above n 647, 1.

the Bursa.⁶⁵² A study has shown that the Code has contributed to a significant improvement in corporate governance practices.⁶⁵³

As in Indonesia, there are some factors undermining the effectiveness of corporate governance. Government intervention in companies is one factor.⁶⁵⁴ This is linked with the close relationship between the business and political elite including the Prime Minister. There are also significant economic policies which advantage *bumiputras* [son of the soil or natives], powerful and rich business people and their business associations.⁶⁵⁵ Political discrimination is also a factor with two types of discrimination. One is ‘the approved position conferred to firms that are operating by *bumiputera* and unofficial ties that are present between leading policy-makers and organisations.’⁶⁵⁶ Directors of indigenous Malay descent have been protected under *bumiputra* policies regardless of their performance.⁶⁵⁷

3.5.4. Thailand

Thai law is mainly derived from civil law legal systems but parts have been subject to strong common law influences including its commercial and corporate law. It represents a mixed legal system.⁶⁵⁸ The market value resembles that of Indonesia in that family controlled companies constitute 70 per cent of Thailand’s economy. Also, as in Indonesia, there is a significant ethnic Chinese influence with the overwhelming majority of companies being controlled by Thai-Chinese families.⁶⁵⁹ Thai corporate and regulatory

⁶⁵² Ibid 5.

⁶⁵³ Jiin, above n 649.

⁶⁵⁴ Lim, above n 627.

⁶⁵⁵ Gomez and Jomo cited in Jiin, above n 643.

⁶⁵⁶ See, Ibid 24. In Malaysia, special treatments apply to Bumiputeras , e.g. education and business opportunities, etc.

⁶⁵⁷ Lim, above n 627.

⁶⁵⁸ Daniel M Klerman, et al, ‘Legal Origin or Colonial History?’ (2011) 3(2) *Journal of Legal Analysis* 379–409.

⁶⁵⁹ Akachai Apisakkul, ‘A comparison of Family and Non-Family Business Growth in the Stock Exchange of Thailand’ *International Journal of Business and Economics (IJBE)* 65, 65–6 <http://utcc2.utcc.ac.th/utccijbe/_uploads/Vol07No1_04.pdf>; Akira Suehiro and Natenapha Wailerdsak, ‘Family Business in Thailand – Its Management, Governance, and Future Challenges’ (2004) *ASEAN Economic Bulletin* 21(1) 81, 81–3 <<http://www.bus.tu.ac.th/departement/thai/download/news/346/SuehiroWailerdsak2004.pdf>>.

activities are also marked by corruption, although it may be less pervasive than in Indonesia.⁶⁶⁰

Thailand, like Indonesia, is struggling to establish better corporate governance practices. Traditional Thai culture and customs have weakened formal legal frameworks and the power of regulators and judicial enforcement which are seen by many as crucial in implementing good corporate governance.⁶⁶¹ Thai culture and the dominance of Confucianism amongst both ethnic Thais and Chinese are believed to contribute to the dominance of family-owned corporations.⁶⁶² The political system has also contributed by requiring approval from different levels of government with associated patronage and nepotism contributing to a failure to implement laws and regulations.⁶⁶³ A study by the World Bank confirmed that formal law affords insufficient protection to investors in Thailand.⁶⁶⁴

Culture and the individual's personal values have been blamed as the major problems in implementing better governance and disclosure. Cultural and social obligations or responsibilities justify decisions that are inconsistent with the moral or ethical principles underlying the imported principles.⁶⁶⁵ These have hampered the implementation of Thai Accounting Standards (TAS).⁶⁶⁶ They are seen as necessary evils in their focus on shareholders rather than other stakeholders. It is believed that investors must run their own business to protect their own interests. Auditing practices are seen as generic services to be

⁶⁶⁰ Nureni Wijayati, Niels Hermes and Ronald Holzhaacker, 'Corporate Governance and Corruption: A Comparative Study of Southeast Asia' in Ronald L Holzhaacker, Rafael Wittek and Johan Woltjer (eds), *Decentralization and Governance in Indonesia* (Springer International, 2016) 259–92.

⁶⁶¹ F A Gul and Judy S L Tsui, 'Problems of corporate governance reforms in Thailand' in F A Gul and Judy S L Tsui (eds), *The Governance of East Asian Corporations: Post-Asian Financial crisis* (Palgrave Macmillan, 2004) 216.

⁶⁶² Lhuengusakul Sukontacha, *The changing face of corporate governance in Thailand* (2005) <http://www.allbusiness.com/business_planning/business_structures_corporation/578608_1.html>.

⁶⁶³ Ibid.

⁶⁶⁴ Gul and Tsui, above n 661.

⁶⁶⁵ Kiattisak Jelatianranat, Chairman of the Institute of Internal Auditors of Thailand and Director of PricewaterhouseCoopers Thailand, 'The role of Disclosure in strengthening corporate governance and accountability: Thailand's corporate governance issues and development' (The second Asian round on Corporate Governance, Hong Kong 31 May – 2 June 2000) 14.

⁶⁶⁶ Ibid 13.

bought rather than professional services.⁶⁶⁷ Companies with financial problems tend to concentrate on improving their relationship to get more access to their creditor banks instead of through corporate law norms.⁶⁶⁸ Some specific cultural factors have also been cited including that Thai people are also ‘generally familiar with verbal discussion rather than formal disclosure in writing’.⁶⁶⁹

The Asian currency crisis led to significant reforms. The major efforts were revising and updating laws, rules and regulatory oversight.⁶⁷⁰ The lead was taken by the Thai government when they established the National Corporate Governance Committee (NCGC) in 2002 that was chaired by the Prime Minister. The Stock Exchange of Thailand (SET) quickly took up the issues of corporate governance. The SET issued 15 principles of corporate governance in 2002, the Compass for Good Corporate Governance, that were recognized as addressing most of the key points in the US *Sarbanes-Oxley Act*. The SET in 2002 ‘issued codes of best practice and a set of corporate governance principles’ requiring listed companies disclose their compliance or non-compliance in annual reports⁶⁷¹ based on a comply-or-explain basis.⁶⁷² It is claimed that this increased firm values by approximately 10 per cent compared to before the introduction of the Code.⁶⁷³ The 15 principles issued in 2002 were expanded in 2006 in the Principles of Good Corporate Governance for Listed Companies⁶⁷⁴ This included adopting the five key OECD corporate governance principles and the World Bank’s recommendations.⁶⁷⁵

⁶⁶⁷ Ibid.

⁶⁶⁸ Nam and Nam, above n 69, 3.

⁶⁶⁹ Jelatianranat, above n 665.

⁶⁷⁰ Chatrudee Jongsureyapart, *Factors that determine corporate governance in Thailand* (Doctor of Philosophy Dissertation, Victoria University Melbourne, 2007) 238 <http://www.wallaby.vu.edu.au/adt-VVUT/uploads/approved/adt_VVUT20070907.160331/public/01front/pdf>.

⁶⁷¹ Ibid 238–9.

⁶⁷² Accounting and Finance Association of Australia and New Zealand, *The determination of Corporate Governance Quality in Thailand* <http://www.afaanz.org/openconf/2008/modules/request.php?module=oc_proceedings&action=view.php&a=Accept+as+Paper&id=612>.

⁶⁷³ Roy Kouwenberg, ‘Does voluntary corporate governance code adoption increase firm value in emerging market? Evidence from Thailand’ (The 2007 Asian roundtable on Corporate Governance, Singapore, 27–28 June 2007) <<http://www.oecd.org/dataoecd/62/41/39490591.pdf>>.

⁶⁷⁴ Principles of Good Corporate Governance for Listed Companies (Thailand) at

The SET has also developed corporate governance ratings to disseminate and to assist investors with decision making.⁶⁷⁶ This includes, with the Thai Institute of Directors Association, the Corporate Governance Report of Thai Listed Companies.⁶⁷⁷ The reforms have contributed to significant progress in corporate governance performance. Many key corporate governance principles were ranked as above world average in 2005.⁶⁷⁸ A 2008 corporate governance study of Asia ranked Thailand higher than Indonesia.⁶⁷⁹ In the 2013 World Bank Report on the Observance of Standards and Codes (ROSC), Thailand achieved a score of 82.83 out of 100 with disclosure and transparency contributing the highest portion.⁶⁸⁰ It has led Thailand to be acknowledged as a leader in corporate governance among Asian economies and emerging economies.⁶⁸¹

The relatively comprehensive framework of corporate governance has enhanced ‘investor trust and protected investors’ rights, especially non-majority shareholders, increased board professionalism and promoted high levels of corporate transparency.’⁶⁸² Enduring reforms include ‘legal reforms, amendments to pertinent rules and regulations and strict compliance with the respective principles and guidelines’. The involvement of both

<http://www.ecgi.org/codes/documents/cg_principles_thailand_2006_en.pdf>.

⁶⁷⁵ Asian Corporate Governance Association, *Code and Rules – Thailand* (2011) <http://www.acga-asia.org/content.cfm?SITE_CONTENT_TYPEID=12&COUNTRY>.

⁶⁷⁶ Lim, above n 627.

⁶⁷⁷ Thai Institute of Directors Association, *Corporate Governance Report of Thai Listed Companies* (2014) <<http://www.thai-iod.com/imgUpload/CGR%202014%20Report%283%29.pdf>>.

⁶⁷⁸ Chrissa La Porte, ‘Thailand ranks high on corporate governance’ (2005) 14(10) *Thailand Investment Review* 11, 11.

⁶⁷⁹ See, Robert W McGee, ‘Corporate governance in Asia: A comparative study of Indonesia, Malaysia, Thailand and Vietnam’ (Working paper, Florida Graduate School of Business, 2008). Corporate governance scores in four Asian countries in 22 categories: Malaysia had the highest score at 85, Thailand was in second place at 80, Indonesia ranked third at 66 and Vietnam had the lowest score at 56.

⁶⁸⁰ World Bank, ‘Thailand makes significant improvements in corporate governance practices’ (Press Release, 25 April 2013) [3], [5], [6] <<http://www.worldbank.org/en/news/press-release/2013/04/25/thailand-makes-significant-improvements-in-corporate-governance-practices>>. Ibid [3], [5], [6]; See also, World Bank, *Report on the Observance of Standards and Codes (ROSC) Corporate Governance country assessment Thailand* (January 2013) (‘ROSC 2013 Thailand’) <http://siteresources.worldbank.org/FINANCIALSECTOR/Resources/ROSC_Thailand_web.pdf>.

⁶⁸¹ World Bank, ‘Thailand makes significant improvements in corporate governance practices’, above n 680.

⁶⁸² Ibid [2], [4].

the public and private sectors has been seen as a key factor in these successes.⁶⁸³ However, it has been claimed that adoption of Anglo-American corporate governance based models in the Thai context has not been appropriate and that it has resulted in variations in the quality of corporate governance practices in Thai companies.⁶⁸⁴

3.5.5. The Philippines

Similar to Indonesia and other South East Asian states, the Philippines has a significant proportion of companies with concentrated family ownership⁶⁸⁵ and political cronyism.⁶⁸⁶ There are also poor accounting and auditing systems,⁶⁸⁷ a weak legal system, poor corporate governance practices and weak enforcement mechanisms.⁶⁸⁸ There is also pervasive corruption and some indication that this may make investment even more difficult than in Indonesia as it is even more unpredictable.⁶⁸⁹

The formal legal and regulatory framework of the Philippines have been identified as largely adequate⁶⁹⁰ and are supplemented with a mandatory Code of Corporate

⁶⁸³ Ibid [3], [5], [6]; See also, World Bank, *ROSC 2013 Thailand*, above n 680. The Thai Listed Companies Association (TLCA) has played a significant role and contributed to significant progress through a constant encouragement of corporate governance development among listed companiesIbid [7].

⁶⁸⁴ Accounting and Finance Association of Australia and New Zealand, above n 672.

⁶⁸⁵ The World Bank study in 2003 showed the Philippines had 52.5 per cent family business and 57.7 per cent in Indonesian businesses compared with Thailand at 46.2 per cent, and Malaysia just had 28.3 per cent. See, Haider A Khan, 'Corporate Governance: The limits of the principal – Agent approach in light the family-based corporate governance system in Asia' (Discussion Paper, University of Denver, 2003).

⁶⁸⁶ Marie dela Rama, 'Corporate governance and corruption: Ethical dilemmas of Asian business groups' (2012) 109(4) *Journal of Business Ethics* 501, 505

⁶⁸⁷ Stephen G Lynn, 'Corporate Governance in the Philippines: Legal institutional aspects and impact on the 1997 financial crisis and its aftermath' in F A Gul and Judy S L Tsui (eds), *The Governance of East Asian Corporations: Post-Asian Financial crisis* (Palgrave Macmillan, 2004) 138.

⁶⁸⁸ Lim, above n 627, 14.

⁶⁸⁹ One informant told dela Rama, 'In Indonesia and Vietnam, when you have to be in a position to bribe someone, what's delivered is delivered. Here, what's supposed to be delivered is not delivered. You can't trust the person you've bri-bed.' dela Rama, above n 686, 513.

⁶⁹⁰ World Bank, *2006 Report on the Observance of Standards and Codes (ROSC) Corporate Governance, country assessment the Philippines* (2006) <http://www.worldbank.org/ifa/rosc_cg_phl_07.pdf> ('*ROSC 2006 Philippines*'); Roberto F De Ocampo, President of Asian Institute of Management, 'Corporate ownership and corporate governance: Issues and concerns in the Philippines' (Paper presented at ADB-OECD-World Bank 2nd Asian Roundtable on Corporate Governance, 31 May–2 June 2000, Hong Kong)

Governance establishing good corporate governance practices.⁶⁹¹ It was introduced by the Philippines Securities and Exchange Commission (SEC) in 2002.⁶⁹² The *Securities Regulation Code* (SRC) (RA) No. 8799 in 2000 superseded the *Securities Act* of 1982 as part of the initial reform after the Asian currency crisis. It sought to strengthen the Securities and Exchange Commission and delegate certain regulatory power to self-regulatory organisations (SROs) including the Philippine Stock Exchange (PSE).⁶⁹³ The *Corporation Code* of the Philippines, enacted in 1980, and the SRC establish the legal principles for governing the capital market.⁶⁹⁴

The SEC issued the Code of Corporate Governance in 2002,⁶⁹⁵ focussed on disclosure issues.⁶⁹⁶ The SEC requires listed companies to observe the Code on a mandatory basis as per the Memorandum Circular No 2 of 2002. The Code was revised in 2009⁶⁹⁷ with the intention, amongst other things, of introducing new mechanisms for greater compliance⁶⁹⁸ and increasing penalties for non-compliance from P100 000 to P200 000.⁶⁹⁹ A full disclosure policy has been applied to all listed companies and enforced by the

<<http://www.oecd.org/corporate/ca/corporategovernanceprinciples/1931183.pdf>>. He identified inadequacy of the regulatory framework for corporate governance i.e. large shareholder-dominated companies, corporate groups and ownership of banks by group of companies.

⁶⁹¹ World Bank, *ROSC 2006 Philippines*, above n 690.

⁶⁹² Securities and Exchange Commission of the Philippines, below n 697.

⁶⁹³ World Bank, *2006 ROSC the Philippines*, above n 690.

⁶⁹⁴ Ibid.

⁶⁹⁵ Ibid.

⁶⁹⁶ A Beltazar Wilfredo, *Corporate Governance in the Philippines* (2002) De La Salle University College of Business and Economics, Accountancy Department <<http://www.dlsu.edu.ph/research>>.

⁶⁹⁷ Securities and Exchange Commission, Republic of the Philippines, *SEC Memorandum Circular No. 2 Series of 2002: Code of corporate governance*, 8 <<http://www.sec.gov.ph/laws/memorandumcircular/CY%202002/sec-memo-2,s2002.html>>; Jonathan Juan D C Moreno, Head of Corporate Governance Office & Chief Risk Officer Philippine Stock Exchange, *Corporate Governance in the Philippines* (3 July 2009) <http://www.competitive.org.ph/files/downloads/Corporate_Governance_by_JJMoreno_APEC_Hanoi070309.pdf>.

⁶⁹⁸ Financial Standards Foundation, 'Philippines: Principles of Corporate Governance' on EStandards Forum (2010) <<http://www.estandardsforum.org/philippines/standards/principles-of-corporate-governance>>.

⁶⁹⁹ The 2002 Code of Corporate Governance on Chapter IX, Administrative Sanction imposes P100 000 for the failure to adopt a manual of corporate governance after due notice and hearing. See, [Philippines] Memorandum Circular No. 2, Series of 2002 at <<http://www.chanrobles.com/secmemorandumcircularno022002.html>>; See also, [Philippines] 2009 Revised Code of Corporate Governance Article 11: Administrative Sanctions at

SEC and the PSE.⁷⁰⁰ The online disclosure system (Odisy) of the PSE from 2003 has made available all reports to the public.⁷⁰¹

A number of institutions were also established to enhance good corporate governance practices among them the Institute of Corporate Directors (ICD), the Corporate Governance Institute of the Philippines (CGIP) and the AIM-Hills Governance Center.⁷⁰²

Their implementation of these initiatives has been poor.⁷⁰³ Specific studies have revealed a lack of understanding illustrated by directors regarding their duties, responsibilities, accountabilities and liabilities, and insufficient knowledge of finance as well as of statutory requirements and business practices.⁷⁰⁴

3.5.6. Hong Kong

The final jurisdiction is the Hong Kong Special Administrative Region of the People's Republic of China. It, from the period of British colonisation, remains a common law jurisdiction. In the past 50 years it has been transformed from a goods-trade-based entrepôt of the British Empire to an international financial centre of the People's Republic of China. It is a global financial centre largely because of the use of the capital market and financial services by Chinese companies including state owned enterprises.⁷⁰⁵ It is regarded, like Singapore, as also having been successful in implementing good governance practices including disclosure, as well as having curbed the extensive corruption, which

<<http://www.sec.gov.ph/circulars/cy,2009/sec-memo-06,s2009.pdf>>. It imposes a fine of not more than P200 000 after notice and hearing to be imposed every year that a covered corporate violates the provisions of the Code. <<http://www.sec.gov.ph/circulars/cy,2009/sec-memo-06,s2009.pdf>>.

⁷⁰⁰ World Bank, *2006 ROSC the Phillipines*, above n 690, 4.

⁷⁰¹ Ibid.

⁷⁰² Ibid.

⁷⁰³ The 2005 Asian Development Bank (ADB) assessment and the 2006 Report on the Observance of Standards and Codes (ROSC) showed slowly improvement due to the implementation and the enforcement of corporate governance requirements remains weak. See, Financial Standards Foundation, 'Hong Kong SAR: Principles of Corporate Governance' on eStandards Forum (2010) <<http://www.estandardsforum.org/hong-kong-sar/standards/principles-of-corporate-governance>>.

⁷⁰⁴ Mariano M Lerin, 'Compliance with Corporate Governance Mechanisms among rural banks' (2008) *Lieco Journal of Higher Education Research Business and Public Policy section* <http://www.eisrjc.com/journals/journal_1/Compliance%20with%20Corporate%20Governance%20Mechanisms%20among%20of%20Rural%20Banks.pdf>.

⁷⁰⁵ Flora Xiao Huang and Horace Yeung, *Chinese Companies and the Hong Kong Stock Market* (Routledge, 2013) vol 1.

once dominated the British colony.⁷⁰⁶ The resistance to corruption reflects the commitment of both the colonial and special administrative region government but it is also widely supported by the people.

The reduction of corruption and the continuing efforts to reduce it further are largely associated with the Independent Commission Against Corruption (ICAC). Its establishment, success and impact on other aspects of Hong Kong society is an example of the individual rolling relationship between law and economic development described by Milhaupt and Pistor.⁷⁰⁷ It commenced with a single incident when a chief superintendent of the Hong Kong Police, Peter Godber, fled to the United Kingdom via Singapore after the Acting Attorney General informed him that he was being investigated for corruption.⁷⁰⁸ The incident undermined the legitimacy of the British government of Hong Kong. The public reaction to the lack of effective control of corruption even in the police force led to the creation of ICAC. The Blair-Kerr Commission investigated his escape and suggested the establishment of ICAC to replace the Anti-Corruption Office established in 1971. It had, in turn, replaced the Anti-Corruption Branch of the HK police created in 1948. ICAC was established in February 1974. Between 1974 and 2010 its staffs expanded from 369 to 1321 and its budget from HK\$12.9 million to HK\$824.1 million as at 2011. As an institutional response, Hong Kong's ICAC has been widely emulated, including in Indonesia in the *Komisi Pemberantasan Korupsi* [Corruption Eradication Commission]. There are questions of how generalize ICAC and its policies may be as a response to corruption.⁷⁰⁹ It has been argued that it represented deep-seated British cultural values

⁷⁰⁶ Suwina Cheng, Gladie Lui and Connie Shum, 'Did corporate governance safeguard investor interest in the global financial crisis? Evidence from Hong Kong SAR' (2015) *Asia Pacific Business Review* (ahead-of-print) 1–17.

⁷⁰⁷ Leslie Holmes, 'Different Paths to Curbing Corruption: Lessons from Denmark, Finland, Hong Kong, New Zealand and Singapore' (2015) 23(1) *Asian Journal of Political Science* 102–105.

⁷⁰⁸ Mark Hampton, 'British Legal Culture and Colonial Governance: The Attack on Corruption in Hong Kong, 1968–1974' (2012) 5 *Britain and the World* 223–39.

⁷⁰⁹ Yina Moa, Chi-Sum Wong and Kelly Z Peng, 'Breaking institutionalized corruption: Is the experience of the Hong Kong Independent Commission Against Corruption generalizable?' (2013) 30 *Asia Pacific Journal of Management* 1115–24.

opposed to corruption.⁷¹⁰ This, however, does not explain the widespread support for ICAC and its anti-corruption strategies amongst Hong Kong residents.⁷¹¹

Local listed Hong Kong companies have similar characteristics to Chinese companies seen in Indonesia and also in Thailand, as described above.⁷¹² The family control and attitudes towards confidentiality and secrecy limit disclosure.⁷¹³ An unusual characteristic is that many of the companies are incorporated in British Overseas Territories in the Caribbean because of political uncertainties regarding the return of the territory to the People's Republic of China.⁷¹⁴ A significant number of listed companies include those controlled by Chinese State-Owned Enterprises. They also have potentially reduced transparency. This is because of Chinese state involvement in them and Chinese secrecy laws as well as the inability of Hong Kong regulators to access information in the rest of China where corporate activities take place.⁷¹⁵ These factors limit confidence in disclosure. Overall, in spite of successes there are many examples of poor governance produced by family relationships, shareholder concentration and self-dealing by insiders.⁷¹⁶

⁷¹⁰ Hampton, above n 708.

⁷¹¹ Ian Scott, 'Engaging the public: Hong Kong's Independent Commission Against Corruption's community relations strategy' (2013) *Different paths to curbing corruption* 79–108; See also, Ian Scott and Ting Gong, 'Evidence-based policy-making for corruption prevention in Hong Kong: a bottom-up approach' (2015) 37(2) *Asia Pacific Journal of Public Administration* 87–101.

⁷¹² Morten Bennesen, Joseph P H Fan, Ming Jian and Yin-Hua Yeh, 'The family business map: framework, selective survey, and evidence from Chinese family firm succession' (2015) *Journal of Corporate Finance*; See also, Sidney Leung, Grant Richardson and Bikki Jaggi, 'Corporate board and board committee independence, firm performance, and family ownership concentration: An analysis based on Hong Kong firms' (2014) 10(1) *Journal of Contemporary Accounting & Economics* 16–31.

⁷¹³ Bryane Michael and S H Goo, 'Corporate governance and its reform in Hong Kong: a study in comparative corporate governance' (2015) 15(4) *Corporate Governance* 444–75.

⁷¹⁴ Dongmei Qui, 'Collecting Unpaid Tax Offshore: Caribbean Tax Havens and Foreign Direct Investment in China' (2014) 12 *Bulletin of International Taxation*.

⁷¹⁵ Raymond Siu Yeung Chan and Kong Shan John Ho, 'Could Complying China's Secrecy Laws Be an Excuse for Auditors Not to Provide Their Working Papers of Auditing Chinese Companies? Recent Cases in Hong Kong and the United States' (10 December 2014) *King's Law Journal* (Subject to some revisions, Forthcoming).

⁷¹⁶ Michael and Goo, above n 713. Research in the early 2000s indicated that family control limited disclosure. See also, Li Li Eng and Yuen Teen Mak, 'Corporate governance and voluntary disclosure' (2003) 22(4) *Journal of accounting and public policy* 325–345; Charles J P Chen and Bikki Jaggi, 'Association between independent non-executive directors, family control and financial disclosures in Hong Kong' (2001) 19 (4) *Journal of Accounting and Public Policy* 285–310.

Hong Kong, since 2014, has had a reformed *Companies Ordinance* replacing an Ordinance that dated back to 1932. The new Ordinance is intended to enhance corporate governance and complement Hong Kong's role as a global financial centre.⁷¹⁷ It strengthened the accountability of directors under provisions relating to directors' duties, improved transparency and disclosure of company information while also strengthening auditors' rights, enhancing shareholders' engagement in the decision-making process, and fostering shareholder protection.⁷¹⁸ As indicated above, many listed companies are not incorporated in Hong Kong so that the *Companies Ordinance* and its governance provisions may not apply to them. The regulation of corporate governance is largely in the context of listed shares and trading in them. The Securities and Futures Ordinance of 2002, which provides for the issuing of, and trading in, shares is overseen by the *Securities and Futures Commission*. It also has provisions for exchanges, their listing rules and the listing of companies. The Hong Kong Exchanges and Clearing Limited (HKEx) provide the listing rule and also the Code of Corporate Governance Practices of 2005, which is incorporated into the Main Board Listing Rules. Listed companies must report on their compliance with them on a "comply or explain" basis.⁷¹⁹ The 2005 code replaced the 1993 Code of Best Practices. The "comply or explain" principle in Hong Kong is seen to contribute to selective disclosure or 'impression management.'⁷²⁰ The 1993 code was one of the first corporate governance codes in Asia. There is also support for corporate governance from the Hong Kong Institute of Certified Public Accountants through the Hong Kong Audit Committee Institute. It has published a guide on effective internal control and risk management practices to meet requirements of the Code.⁷²¹

⁷¹⁷ FSTB, Rewrite of the Companies Ordinance – Draft Companies Bill First Phase Consultation: Consultation Paper (2009) at [1.5].

⁷¹⁸ Ibid.

⁷¹⁹ Tom Ng, 'Judicial Enforcement of the Listing Rules in Hong Kong' 2015 (45) *Hong Kong Law Journal* 389–404.

⁷²⁰ Sydney Leung, Lee Parker and John Curtis, 'Impression management through minimal narrative disclosure in annual reports' (2015) *The British Accounting Review*.

⁷²¹ Hong Kong Institute of Certified Public Accountants, *Improving corporate governance disclosure and practices* (2014) <<http://www.hkicpa.org.hk/en/membership-and-benefits/professional-representation/corporate-governance/publications/gov-publications/cg-practices/>>.

There is some evidence that the attempts to improve corporate governance have afforded some stability to Hong Kong's listed companies in the financial crises of 1997 and 2008.⁷²² There is also evidence that effective audit committees and internal audits effectiveness and the improved ethical ethos in companies created by adherence to the listing rules is positively associated with a lack of fraud.⁷²³

3.5.7. Explaining the pattern in the use and effectiveness of corporate governance codes

The experiences in these jurisdictions generally appear to demonstrate that corporate governance codes as a form of soft law or informal law appear to be working more effectively in common law jurisdictions. This would suggest that it is the formal legal system that is contributing to the effectiveness of corporate governance codes. It may be that common law countries are more easily able to accommodate good corporate governance codes as a form of soft law or self regulation. It may relate to the literature on legal transplants in Chapter 2, at 2.6.4: influencing factors for successful transplantation of informal law to donor legal system, which suggest that transplants should come from related legal systems to increase the chance of success. That success may relate to other aspects of soft law such as legal culture discussed in that part of Chapter 2.

The origin of the legal system may not be the explanation. Also in Chapter 2, in the context of the protection of investors, the work of La Porta et al is referred to.⁷²⁴ That work suggests that legal origins do matter with regard to protecting investors and encouraging the trust required for economies to grow. There is other work that suggests it may not be the origin of the legal system that is important but the colonising power, which introduced the legal system. The British, Dutch and United States who colonized these jurisdictions, with the exception of Thailand, differed in their policies relating to trade and commerce, education, public health, infrastructure, European immigration, and local governance.

⁷²² Aditya Shankar Mishra and Soumitra Bhattacharya, 'The Linkage Between Financial Crisis and Corporate Governance: A Literature Review' (2011) 10(3) *IUP Journal of Corporate Governance* 71.

⁷²³ Philip Law, 'Corporate governance and no fraud occurrence in organizations: Hong Kong evidence' (2011) 26(6) *Managerial Auditing Journal* 501–18.

⁷²⁴ See, Shleifer and Vishny, above n 246; See also, La Porta et al, 'Investor Protection: Origins, Consequences, Reform', above n 227.

These also have a potential impact on how soft law interacts with formal law. One recent study indicates that it was the colonial power's willingness to invest in education that leads to economic growth in the now independent state rather than the legal system. It is not possible to explore this and what possible variables may be important within the limits of this thesis.⁷²⁵

In the context of these jurisdictions there are other significant factors that may contribute to the successful use of soft law and which persist from the colonial period or that may be strengthened in the period after their independence. These include the scale and importance of the private sector in the economy and effective enforcement mechanisms including mechanisms and attitudes towards reducing corruption seen that were seen in Singapore and Hong Kong. The Philippines provides an indication that the understanding and knowledge of corporate leaders is significant in developing good corporate governance. The Philippine's experience demonstrates that a lack in understanding of directors regarding their duties, responsibilities, accountabilities and liabilities, business statutory requirements and business practices may hinder the use of corporate governance codes in common law countries.

The following sub-chapter attempts to further clarify whether the origin of legal systems in common law or civil law system contributes to the more effective use of voluntary corporate governance codes as soft law.

3.6. The effective use of soft law in common law and civil law countries

3.6.1. Introduction

Is soft law more or less effective in common law or civil law countries? The answer to this question may assist in determining whether the origin of the legal system may affect the effectiveness of the application of soft law, in this context, corporate governance codes.⁷²⁶

⁷²⁵ Klerman et al, above n 658.

⁷²⁶ Codes of practice, guidance, guidance notes, codes of conducts, codes of ethics are among other prototype of soft law. See, Greg Weeks, 'The use of soft law by Australian Public Authorities: Issues and Remedies' (Paper presented to the practice and theory of soft law academic symposium, Peking University soft law centre, 9 July 2011) 2 <www.gtcentre.unsw.edu.au/sites/.../Weeks_SoftLaw_%20Australia.pdf>.

The concept of soft law is discussed in Chapter 2, at [2.5.2] the distinction between formal and informal law. It essentially connotes non-binding norms or instruments. The term, in its origin in international law ‘refers broadly to quasi-legal rules that are not legally binding on states’.⁷²⁷ Snyder defines soft law as ‘rules of conduct which in principle have no legally binding force but nevertheless may have practical effects.’⁷²⁸

One of the reasons for its expansion beyond international law into national legal and regulatory systems is the belief that hard law lacks capacity. Among others, Koutalakis found that soft, or legally non-binding regulation, has sufficient power to be effective.⁷²⁹ It is argued that the coinciding of interest between industry and consumers are significant factors to make soft law work.⁷³⁰ In the context of corporate governance, this is illustrated by the mutual interest that both investors have in investing and corporate managers have in attracting investment. A study of soft law in the context of international financial regulation demonstrated that ‘soft laws and institutions can exert considerable power’.⁷³¹ International soft law, the setting of international standards, is believed to be highly influential in establishing best practices as market norms. Soft law also offers considerable opportunity for adaption to fit local circumstances.⁷³²

The examples provided above from a number of Asian jurisdictions indicate that government, regulators and other national and international institutions as well as legal scholars accept soft law as an appropriate way to boost corporate governance at a national and international level.⁷³³ It is of interest to legislators, regulators and business because of

⁷²⁷ Andrew T Guzman and Timothy L Meyer, ‘International Common Law: The soft law of international tribunals’ (2008-2009) *Chicago Journal of International Law* 515, 518 <<http://heinonline.org>>.

⁷²⁸ Cited in David M Trubek, Patrick Cottrell, and Mark Nance, *Soft law, hard law and European integration: Toward a theory of hybridity*, 1–2 <<http://ssrn.com/abstract=855447>>.

⁷²⁹ Koutalakis and Buzogany, above n 392.

⁷³⁰ European Consumer Law Group, *Soft law and the consumer interest*, 7 <http://ec.europa.eu/consumers/policy/eclg/rep03_en.pdf>

⁷³¹ Eilis Ferran and Kern Alexander, ‘Can soft law bodies be effective? Soft systemic risk oversight bodies and the special case of the European systemic risk board’ (Paper no.36/2011, June 2011) 32 <<http://ssrn.com/abstract=1676140>>.

⁷³² Ibid 6.

⁷³³ Zerilli, above n 434, 11.

globalisation, market forces, the cost of regulation and its quick and flexible qualities.⁷³⁴ This is confirmed by Abbott and Snidal who claim softer forms of corporate governance have been elected by international actors as it offers superior solutions.⁷³⁵ They argued that where many issues are new and complex hard law may not resolve the problems, as states cannot anticipate all the possible consequences of any formal law they enact to deal with them. Soft law offers a number of potential alternatives and is also a tool for compromise.⁷³⁶

The increase of migration from hard to soft law in many jurisdictions occurred due to cost, flexibility and risks. As self-regulatory voluntary instruments corporate governance codes reflect flexibility, adaptability, allowing for experimentation and innovation without the need for ongoing legislative oversight and intervention.⁷³⁷

Soft law, such as codes have long been used in many countries with different legal systems. It is claimed that the formal legal system impacts on the soft or informal law. Codes as self-regulatory standards may be absorbed into formal legal system.⁷³⁸ Some believe soft law is particularly effective in some countries with common law systems as common law is more open to and supportive of soft or informal law.

Common law was based on case or judge made law although legislation is now the major source of law in all common law jurisdictions. There is still generally no practice of extensive codification in corporate law leading to a comprehensive compilation of legal principles and rules that exclude other sources of law. Civil law, by contrast, is codified and comprehensive and excludes other sources. This becomes a problem if the law is not updated. In common law systems, however, where gaps emerge in legislation the common law may provide a statement of the law.⁷³⁹ Millstein notes this difference describing ‘civil law as an effort to provide black letter rules and common law as intentionally leaving many

⁷³⁴ European Consumer Law Group, above n 730, 4.

⁷³⁵ Abbott and Snidal, above n 347, 441.

⁷³⁶ Ibid 441, 444.

⁷³⁷ Ferran and Alexander, above n 731, 20; Weeks, above n 726, 27

⁷³⁸ Wymeersch, above n 260, 4.

⁷³⁹ Robbins collection, School of Law University of California Berkeley, *The Common law and Civil law traditions* <<http://www.law.berkeley.edu/library/robbins/CommonLawCivilLawTraditions.html>>.

open ended questions'.⁷⁴⁰ The only primary source of law in civil law systems are the codes or special legislation regarding case law ranked as a secondary source. Case law remains a primary source of law in common law jurisdictions and judges are open to using precedents from other jurisdictions or other statements of relevant standards or principles, such as self-regulatory codes, as persuasive in framing new rules for particular contexts.⁷⁴¹

Martin Shapiro confirms these different methodologies permitting the use of different sources of law as distinguishing civil law and common law. Common law, he claims, emphasises supra-statutory or natural legal rights; the principle of *stare decisis* recognized, case-by-case inclusion and exclusion and analogy. On the other hand, civil law is based on statutes; and reflects a strong form of positivism. Statutes are sources of rights and lawyers and jurists work from statutory texts.⁷⁴² This indicates that civil law systems may be less open in their foundations to other influences including self-regulatory codes as a source of legal principles and rules unless they are enacted as legislation.

Indonesia utilises a civil law system, which inherited continental legal views on legal frameworks, as indicated in Chapter 1, indicating that it too may be less open to using soft law in of the form of corporate governance codes. However, parts of the Indonesian Code of GCG including those relating to disclosure have been reflected in legislation. This is considered further in Chapter [6.3] – the legal framework supporting codes.

Soft law represented by Codes is widely used among European states with different legal systems. The next part considers the use of the codes in these jurisdictions to assist in clarifying whether the origin and type of legal system contributes to the effective use of these as soft law.

⁷⁴⁰ Millstein, et al, above n 284, 2.

⁷⁴¹ Vincy Fon and Francesco Parisi, 'Judicial precedents in civil law systems: A dynamic analysis' *International Review of Law and Economics* 26 (2006) 522 <<http://ssrn.com/abstract=534504>>.

⁷⁴² Cited in World Bank, *Comparing legal system* <<http://siteresources.worldbank.org/INTLAWJUSTINST/Resources/ComparingLegalSystems.pdf>>.

3.6.2. The use of soft law in different legal systems in European jurisdictions

The European Union has employed informal and soft law in a number of contexts including recommendations to official instruments and in directives permitting member states to rely on self regulatory systems for implementing the directives in national law.⁷⁴³

The relationship between corporate governance codes and legislation shows a balanced use of formal law and soft law across member states. Some believe that soft law is the best way to improve corporate governance by providing an adequate framework but also greater flexibility.⁷⁴⁴ Some also claim that one of the benefits of implementing a corporate governance code is the creation of greater trust, which is valuable in markets.⁷⁴⁵

Some evidence below demonstrates the outcomes of the use of soft law in different European legal systems, which are the origin of those legal systems in other parts of the world.

3.6.2.1. The use of soft law in common law countries

There are a number of European Union member states with common law systems. They demonstrate similar outcomes.

The use of the UK Combined Code on Corporate Governance with its “comply or explain” principle is very positive with a balance of hard law where improved governance standards have been achieved. The UK approach is to link the Combined Code with the listing rules of the London Stock Exchange.⁷⁴⁶ But the code has had limited impact on raising awareness of the interests of shareholders and stakeholders.⁷⁴⁷ Three smaller markets have also been subject to some study. Ireland showed some positive effects from utilizing a code. In Cyprus, respondents noted the code has had a positive effect in increasing the trust and confidence of shareholders and potential investors.⁷⁴⁸ In Malta the code was seen as being inadequate in promoting good corporate governance.⁷⁴⁹

⁷⁴³ European Consumer Law Group, above n 730, 11.

⁷⁴⁴ Ibid 139–40.

⁷⁴⁵ Ibid 143.

⁷⁴⁶ Dallas, above n 281, 16.

⁷⁴⁷ European Consumer Law Group, above n 730, 4. In 1973 the United Kingdom, through the Office of Fair Trading encouraged trade associations to develop codes of conducts.

⁷⁴⁸ Ibid 145.

⁷⁴⁹ Ibid 147.

3.6.2.2. The use of soft law in civil law system countries

The use of soft law in civil law European countries has shown more mixed outcomes. The codes have been successful in reaching their initial objectives as a reference tool for corporate governance practices and creating awareness of corporate governance.⁷⁵⁰ Overall, codes appear to have had positive effects on governance activities. In a few countries they have not achieved these targets.

The most positive and significant effects related to governance activities has been found in one of the largest economies: France (for one-tier companies) and in one of the smallest: Slovenia (for two-tier companies). The codes' effects on management in these jurisdictions have been found to be positive irrespective of board structure and both countries show greater confidence on the part of stakeholders.⁷⁵¹ Slovenia outranked France overall in positive indicators. It was, however, more negative around controlling shareholders in the use of "comply or explain".⁷⁵²

In Germany, the largest economy, the effectiveness of the code was found to be good. It was also seen as an important interpretative reference or standard for the courts. The Dutch corporate governance codes were also considered to have demonstrated a positive effect.⁷⁵³ In Spain and Sweden the code was also shown to have had a positive effect. The respective codes functioned properly and companies committed to their application. The codes were considered to be adequate and clearly formulated. In Portugal, the code was also perceived to be positive in its impact on management, shareholders and stakeholders. The "comply or explain" principle was seen to offer more flexibility for companies. It is similar in Denmark where the perceived effectiveness of the code in meeting its objectives was also positive. The "comply or explain" principles were seen to offer sufficient flexibility for companies to implement the right corporate governance structures. Finland also showed positive effects regarding the code and that initial objectives had been mostly reached.⁷⁵⁴

⁷⁵⁰ Ibid 131.

⁷⁵¹ Ibid 133–6.

⁷⁵² Ibid 148–51

⁷⁵³ Ibid .

⁷⁵⁴ Ibid 146.

In smaller and more transitional economies the results are more mixed. In Estonia, the effectiveness of the code has been found to be significant and positive for shareholders and stakeholders.⁷⁵⁵ Latvia has also showed positive results. However, the flexibility of the “comply or explain” principles is thought to be insufficient to achieve better regulation. In Bulgaria the corporate governance code was regarded as neutral or slightly positive. It was thought by those surveyed that “comply or explain” principles worked effectively.⁷⁵⁶

For some other countries the codes are perceived as not being as successful. The Czech corporate governance code is, like the others, based on the OECD principles and showed an effectiveness below the European median score. Respondents believed the code needs amendment to meet general European standards. The code is not based on the “comply or explain” principle.⁷⁵⁷ Greece’s Corporate Governance Law 3016/2002 implements a code as legislation and this is seen as having a positive effect. However, since it is law, business considers that companies are given insufficient flexibility. Its effectiveness in corporate governance is understood to be negative. One large economy, Italy, also showed similar outcomes. Legislation has adopted the corporate governance code and made it mandatory to comply. Respondents highlighted that the excessive amount of legislation does not leave sufficient space for self regulation. The Hungarian code has a “comply or explain” principle but it is seen to lack real impact. The code is criticised, perhaps unfairly, for providing no guidance on what an adequate explanation should contain.⁷⁵⁸ In Lithuania and Poland the relevant code is also seen to be performing below the standards of other European states. The code in Lithuania does not contain the “comply or explain” principle.⁷⁵⁹

⁷⁵⁵ Ibid.

⁷⁵⁶ Ibid 145.

⁷⁵⁷ Ibid 146.

⁷⁵⁸ Ibid 147.

⁷⁵⁹ Ibid 147.

3.6.2.3. Preliminary findings of the use of soft law in different legal systems in European jurisdictions

The findings of these studies, summarised above, generally show that the perception of national corporate governance codes are positive. The effectiveness of their use in common and civil law systems demonstrates similar outcomes. The codes appear to be more effective in older developed economies and formal legal systems. The less developed European states appear to be less successful in their use. This suggests that there are other factors impacting on success rather than the origin of the legal system and its openness to the use of soft law for the standards discussed by Millstein and Martin Shapiro above. The outcome is different from that with respect to the use of codes in Asian jurisdictions in 3.5 above, – the use of corporate governance codes in South East and East Asian jurisdictions. This may indicate that there are other factors in the history of colonisation and independence that have affected the relationship other than the origin of the legal system.

The findings also show support the comply-or-explain principle. It is claimed to be best suited to take into account the variety of situations of individual companies. This is a more efficient approach for companies and regulators to implement than detailed regulation. Some respondents to the surveys pointed out that self regulation and soft law represents a more effective corporate governance tool than formal law, as it is able to take the diversity of listed companies into account. The “comply or explain” principle offers flexibility to these companies to implement the right corporate governance structures for their specific situation. From a shareholder’s or investor’s perspective the comply-or-explain regime is suggested as an acceptable balance between legislation and mandatory codes.⁷⁶⁰

Based on the above outcomes, there is no strong evidence showing that the origin and type of legal system affects the effectiveness of soft law. This is in spite of claims, seen in Millstein and Martin Shapiro, that soft law in common law system countries is likely to be more effective compared with civil law countries as they may be more open to soft law as a source of formal law. It may be that formal law in civil law systems is also open to

⁷⁶⁰ Ibid 148–51.

using principles from soft law when formal law fails to achieve desired goals, as seen in the comments about German law above. This is an issue that requires further research.⁷⁶¹

3.7. Conclusion

Globalization and internationalization have driven the convergence of corporate governance partly as a result of attempts to stabilise and insulate the global financial system from the impact of crises. They have led to the promotion of corporate governance concepts and the convergence of corporate governance including in Indonesia. Improved corporate governance has appealed to individual states and governments as a way to attract global investors in order to increase the rate of their economic development. For Indonesia, this was crucial especially after the financial crisis of 1997 and to a lesser extent after the global financial crisis of 2008. Improvements in corporate governance regulation was also a condition for assistance from international bodies who required principles taken from international standards, such as the OECD Principles of Corporate Governance to be used. This has partly raised the significance of corporate governance and driven the convergence in the principles used globally.

The origin of these principles is in the US and the UK and they reflect the shareholder orientation of Anglo-American law and corporate governance practice. The common law model or outsider (shareholder) or market based system that informs the management of companies and their governance is not used universally. The other model in wide use is also associated with civil law systems and is the insider [stakeholder] or relation based system. There are different structures to be found within them including the use of single and dual boards. There are also significantly different social, cultural and political values associated with legal cultures, business cultures and the role of stock exchanges and other bodies in the regulation and oversight of corporate governance. The use of principles at a global level allows for these differences to be accommodated in formal legal systems but also in the soft or informal law represented by corporate governance codes, which represent part of the convergence of corporate governance practices.

Some of these differences and the use of principles in corporate governance codes can be seen across South East Asian and East Asian countries that have common law or

⁷⁶¹ Rapp, Schmid and Wolff, above n 371, 4.

civil law as their formal law. Their experiences of the use of corporate governance codes in some aspects reflect several potential strategies and areas for significant reform that Indonesia may adopt to improve its implementation of corporate governance. The countries selected have faced similar issues to Indonesia in grappling with corruption and poorly developed legal and regulatory infrastructure and capacity, as they seek to improve corporate governance and related disclosure practices.

The lessons from Singapore, Malaysia, Thailand, and Hong Kong demonstrate that non-legal factors such as corruption, political stability and commitment and culture are substantial factors that need to be addressed by making efforts to seek to improve corporate governance performance. Such improvements require strong political commitment and social engagement to establish effective legal, cultural, and corporate governance changes. Indonesia needs to consider these factors in bringing both the public and private sectors together in a collaborative way. This could be achieved partly through a revision of the 2006 GCG Code to accommodate international developments and update changes in market practices and expectations. This is addressed further in Chapter 6.

The final issue considered was whether either type of legal system makes a difference to the effectiveness of soft or informal law seen in corporate governance codes. The review of South East and East Asia may suggest a tendency for common law systems to be more successful in integrating the two forms of law. The literature reviewed also appeared to suggest that common law was more open to using such codes as a source for standards as opposed to civil law systems with their focus on the code or other legislation. A review of the European Union, the origin of both common and civil legal systems does not suggest that soft law, represented by corporate governance code, is more effective in one system or another. However, common law systems with their characteristic openness to sources of law appear to have greater potential to accommodate soft law than civil law systems. Both the review of South East and East Asian countries as well as the European Union is consistent with Milhaupt's and Pistor's claim that there is no single way to successfully use law in the context of economic activities and that it is a rolling relationship that is individual to each state. This also relates to the effectiveness of legal transplants discussed in Chapter 2 at [2.6] comparative law and legal transplants.

The success of transplants, including soft law represented by corporate governance codes, depends in part on favourable conditions in the jurisdiction into which they are transplanted. As well as consistency with the formal legal system, they need to fit with local legal culture, and in this context, with business and social values. As a number of comparative law writers have pointed out support from the local elite is important in their success. Comparative law is seen partly as a study of comparative cultures. The position of corporate governance and its development around specific cultural values and practices in trade and commercial activities in Indonesia is considered in the next chapter.

Chapter 4 : Historical development of social and cultural values around business transparency in Indonesia

4.1. Introduction

This chapter seeks to position the present requirements for and practices around disclosure in corporate governance within the cultural and social values of Indonesian people. It traces the historical development of beliefs and practices in trade and commercial enterprises in Indonesia from the Hindu and Buddhist periods to the present. It considers the key values underlying disclosure of honesty, openness and transparency in both traditional commercial practices and in the western forms of enterprise that came with colonisation. It also outlines the increasing globalisation behind the transplanting of values and concepts between cultures.

The key social and cultural values of the Indonesian people are considered to be linked to Blankenburg's concept of legal culture as indicated in Chapter 2. It relates to the complex relationship on four levels including values, beliefs and attitudes towards the law, patterns of behaviours, institutional features and the body of substantive and procedural law that has created the legal culture of the Indonesian people.

The historical development of social and cultural values around business practices are significant in exploring the issues raised in the research. It relates to understanding the familiarity Indonesian business people have with principles and rules including legal, religious and moral values. It aims to identify relevant social and cultural issues that create patterns of behaviour and attitudes towards these as local or foreign concepts. It relates to understanding how and why foreign values and concepts have been accepted or rejected by Indonesians. These decisions have shaped Indonesian beliefs and culture. It seeks to locate any local or indigenous values or concepts that might make transplanted informal or soft law more acceptable.

This assists this study in exploring basic values and cultural attitudes that may promote the use of a good corporate governance code as an informal rule. It also provides an understanding of why persistent problems in legal and political systems have undermined honesty and openness since independence. This is significant in identifying

factors that might present resistance against greater transparency, including the use of informal law.

Culture is widely recognised in the literature referred to in Chapter 2 as a fundamental non-legal factor determining a successful legal transplant. It is also one of the determining factors for the successful application of corporate governance suggested by a number of scholars whose writings were reviewed in chapter two. This makes culture a significant element to be explored in this study. Spiritual beliefs and their relation to business practices and ethics first became significant in Max Weber's work.⁷⁶²

The cultural aspect is seen by many scholars, as indicated in Chapter 2, as a kind of informal concept. The informal concept is observed as social norms by Huppel-Cluysenaer, as rules governing behaviour outside official channels by De Soysa and Jutting and as North suggests unwritten features with self-enforcing characteristics such as sanctions; taboos; customs; traditions; codes of conduct and norms of behaviour. Parker and Baitwaite consider that the moral suasion as an informal approach has a greater deterrence impacts than formal legal sanctions. However, the claim of Milhaupt and Pistor may need to be considered in respect to the differences across economy, jurisdictions, and history. They emphasize the importance of the economy and social and political history and its rolling relationship to law.

With respect to legal transplants, for example, Cotterell argues that particular study and precise analysis are required to situate and define the cultural context of any specific transplants. Watson claims, more generally, that understanding legal traditions and legal culture is the only approach to discovering the nature of laws and their place in society. It seeks to engage with Blankenburg's suggestion that law involves a complex interrelationship on four levels: see Chapter [2.6.4.2] – determining factors for successful informal legal transplants. This is significant for this study as it may help to reveal whether

⁷⁶² Max Weber, *The Protestant Ethic and the Spirit of Capitalism* (Talcott Parsons trans, Routledge, 1992) [trans of: *Die protestantische Ethik und der Geist des Kapitalismus* (first published 1904–5)]; Roger Friedland, 'Divine institution: Max Weber's value spheres and institutional theory' in Michael Lounsbury and Paul Tacey, *Research in the Sociology of Organizations, Volume 41: Religion and Organization Theory* (Emerald Group Publishing, April 2014) 217–58.

Indonesians are inclined to accept informal rules or a soft law approach to corporate disclosure and good corporate governance codes or perceive them as the imposition of foreign concepts and possible threats to their interests.

This chapter provides a historical background that explores how different eras of globalisation have brought new values, ideas and concepts including corporate governance to Indonesia. The use of good corporate governance codes marks a point of convergence in corporate governance and is an outcome of globalisation.

As indicated in Chapter [2.4.2] informal law has been created because of the incompleteness of formal institutions. It may not only complement or supplement the formal law but may also circumvent and supplant that formal law.

The level of political and economic corruption in contemporary periods, explored in Chapter 3, indicates that there is resistance to globalisation, which produces common economic political cultural forms and practices. The historical background of some South Asian jurisdictions, indicated in Chapter 3, show their similarity as common law jurisdictions and British colonized countries that appears to contribute to their familiarity with corporate governance practices and codes which have been driven at the global level by Anglo-American models. They also appear to have been more responsive to changes driven by globalisation.

The understanding of those issues is important in answering the research questions to which this study seeks answers. The relevant questions are related to the aspects of Indonesian political, administrative and business culture that can be called on to support the use of the good corporate governance code as an informal law. It is also relevant to answer the question concerning the factors which influence the effective transplantation of informal law into Indonesia as a host country. This later question assists in providing the conceptual framework to answering the previous question.

4.2. Historical background to honesty and transparency

This part outlines the way in which increasing globalisation has led to foreign concepts being introduced and then evolving in the economic practices of people in the Indonesian archipelago. It can be divided into four broad periods of economic globalisation that have impacted on people involved in commerce in Indonesia.

It starts with considering the level of honesty and openness in traditional commerce. These values have been impacted upon, and changed by the later forces of globalisation. Some are archaic such as Hinduism and Buddhism, which reached their peak in the 1300s. By the 1000s Islamic traders and missionaries had arrived and by the 1500s Islam had more followers than the earlier religions in Java and Sumatra.

Wider forces came with the spread of European influence under pre-modern globalisation over the small coastal trading and inland agrarian states in Java and Sumatra and other parts of the archipelago. The Portuguese were followed by Dutch and British traders and the Dutch and British East India Companies. The early contact in Java and Sumatra by the Dutch East India Company was largely driven by trade. It avoided territorial conquests. However, its advanced technology in weaponry and shipping permitted it to assert superiority over local rulers. Its bankruptcy in 1800 was followed by modern globalisation, which was marked by territorial acquisitions and the direct rule of the Dutch government which, by the early 1900s, was able to exert its power over most of the archipelago.

In 1942 the Dutch East Indies were occupied by Japan and included in its Greater East Asia Co-Prosperity Sphere until its defeat in 1945. Japan developed its own institutions to control its new territories, which survived its defeat. The Dutch government, weakened by the occupation of The Netherlands by Germany, was unable to recover its former authority. A declaration of independence by Soekarno and Hatta on 17 August 1945 was followed by a war of independence. Dutch power ended in 1949 with the surrender of Dutch forces.

Independence and the political developments in the new republic have had their own impact on commerce and the values of business people. It can be divided into three periods that have particularly marked the corporate sector and the financial services industry: the Soekarno period of the old order, the Soeharto period of the new order, and the present reformation period. Post independence Indonesia has also seen increasing globalisation underwritten by the internet and digital technology of the contemporary era.

In early traditional commerce, honesty was an underlying value for trading. It created trust and confidence among traders. The arrival of foreign traders, which brought

their religious beliefs, especially Hinduism, Buddhism and Islam, re-enforced the value of honesty in trade transactions. The later European colonisation changed and transformed this traditional value through paternalism and capitalism. They shaped the understanding, attitudes, leadership styles, and commercial activities in the post independence period.

4.2.1. Traditional commerce and enterprises practices up to the early 16th century

In the past, as well as in the present, life in Indonesia has been dominated by working to provide the necessities of life.⁷⁶³ Sea-based trade has long brought foreign influences, beliefs and values into daily life and work on the Indonesian archipelago. The openness of Indonesian people facilitated the changes outsiders brought. Traditional values and religions, social and economic structures have adapted to these external influences.

4.2.1.1. Early trade practices and traditional values

The traditional basis of Indonesian society on Sumatra and Java and other islands was rural village communities.⁷⁶⁴ Their economies were agricultural and predominantly rice-growing. Mutual assistance between villagers was important to fulfil their needs. Reputation and the history of people and families mattered. Exchange and trade relations relied on trust. Farmers were clustered into ‘small inland principalities’.⁷⁶⁵ On the coast there were small sea ports. They acted as ‘trading links between inland agricultural societies and the multicultural sea traders of Southeast Asia’.⁷⁶⁶

Some communities in the Straits of Malacca became significant trading posts. The Straits are the junction of sea traffic between east and west Asia, as well as between Asia and Africa and the Middle East and Europe.⁷⁶⁷ Indonesian traders were engaged in trade

⁷⁶³ Christopher Richardson, Lalita Sinha and Md Salleh Yaapar. ‘Work ethics from the Islamic and Hindu traditions: in quest of common ground’ (2014) 11(1) *Journal of Management, Spirituality & Religion* 65–90.

⁷⁶⁴ Tim Lindsey (contributing eds), ‘Indonesia’ in Asia Business Law series, *Doing Business in Asia* (Kluwer Law International, 1st ed, 2005) vol II, 31,001 & 31,251.

⁷⁶⁵ Ibid.

⁷⁶⁶ Ibid.

⁷⁶⁷ Suwardi, *The Silk Road, A Road of Dialog between East and West Hemisphere – A case of Malay culture in Malacca Strait in Budaya Melayu dalam perjalanannya menuju masa depan* [Malay culture in the way towards the future] (Yayasan Penerbit MSI, 1991) 180. See also, Unit Khusus Museum Bank Indonesia [Special Unit of Central Bank Museum], *Sejarah Pra Bank Indonesia, Nusantara s.d. awal abad ke-19* [History of Pre-Central Bank, Great Indonesia until early 19th century], below n 790, [1]. The trade was from China through the China Sea and the Straits of

with India's Malabar Coast as it was a centre for the spice trade. They traded cloves with Arab merchants from the Red Sea and Persian Gulf.⁷⁶⁸

Traditional trade was characterised by sole proprietorships (sole traders) and included *beri-memberi* [mutual gifts], *pakai-memakai* or *tukar-guling* [swap] (bartering), *jual-beli* or *panjer* [sale and purchase], *titip-menitip* or *titip-curah* [consignment] and *hutang-piutang* [loans and repayments]. It mainly consisted of *adat* [indigenous customs, values and traditions].⁷⁶⁹ Within Java and Sumatra, barter was the traditional economic system. Transactions were based on consensus [*mufakat*].⁷⁷⁰

Pribumi [indigenous] people were known as wise and honest traders. Buginese traders from Makassar, South Sulawesi, for example, were well-respected. They had a reputation for selflessness and strong morality. *Siri* and *pesse* were their basic values. *Siri* was a philosophy of self-identity and shame referring to self-esteem, or self-regard. It was a powerful value confirmed by the phrase: *lebih baik mati demi mempertahankan siri dibandingkan dengan sebuah kehidupan yang tidak memiliki siri* [better to die defending *siri* than live without *siri*]. *Pesse* is a belief in spiritual unity. It derived from a spirit of brotherhood. This spirit was seen as a significant element in defending and confirming the

Malacca to Calicut in South India. It continued on to the Persian Gulf through Syria to the Mediterranean Sea, or the Red Sea to Egypt and the Mediterranean Sea.

⁷⁶⁸ Shane Winser, 'Vasco da Gama', *BBC History* (online) [18]

<http://www.bbc.co.uk/history/british/tudors/vasco_da_gama_01.shtml>.

⁷⁶⁹ Peter Burns, 'The myth of adat' (1989) 2 *Journal of Legal Pularism*

<<http://jlp.bham.ac.uk/volumes/28/burns-art.pdf>>.

⁷⁷⁰ Bernadetta Budi Lestari, *Hubungan internasional kuno Indonesia* [Ancient international relation of Indonesia] (*Konsep perdagangan system barter di selat Malaka dan pemberian nama nusantara – Indonesia*) [Trading concept of barter system in Malaca strait and given name of Great Indonesia], 50 <<http://digilib.unipasby.ac.id/files/disk1/5/gdlhub--bernadetta-248-1-bernadet-2.pdf>>; See also, 'Sejarah singkat penggunaan uang di Indonesia [Brief history of the usage of money in Indonesia], *Warta Kota Tribun News* (online), 7 November 2012, [2]-[3] <<http://wartakota.tribunnews.com/detil/berita/105900/Sejarah-Singkat-Penggunaan-Uang-di-Indonesia>>. From the 5th century and later gold, silver, copper and bronze currencies were used. Under Dutch colonialism, the Gulden was used. The Indonesian currency, *Oeang Republik Indonesia* was used in 1946; See also, Jan Luiten van Zanden and Daan Marks, *An economic history of Indonesia 1800-2012* (Routledge, 2012) 39. Paper money was introduced in 1782 used firstly as bonds.

unity of their communities. It is similar to the concept of “*gotong royong*” in Malay culture.⁷⁷¹

Gotong royong, or *tolong-menolong* [communal work or mutual aid] was a fundamental characteristic of traditional communities. It is literally defined as ‘carrying work together’ [*gotong*] and ‘distributing the earnings or income’ [*royong*]. Practically, it means ‘working together for the benefit of the community’.⁷⁷² Reciprocity and equality are the two basic forms of the *gotong royong*. This reflects strong solidarity. It provides self-respect, a sense of belonging in the need to help each other and a sense of awareness of facing and tackling problems together.⁷⁷³ This reflects a familial principle [*asas kekeluargaan*],⁷⁷⁴ which is a foundation of Indonesia’s economic system and a constitutional value. This principle relates inter-personal relationships with attitudes in society.⁷⁷⁵ It also reflects a collectivism. The underlying values of the principle are familiarity, aid, care, responsibility, democracy, equality, fairness, honesty and transparency.

⁷⁷¹ Nordin Hussin, ‘Pedagang Bugis dan Kuasa Eropah di Selat Melaka’ [Bugis traders and the power of Europe in Malacca Strait] (2008) 26 *SARI: Jurnal Alam dan Tamadun Melayu* 199, 201–2 <<http://www.ukm.my/penerbit/sari/SARI26-07/sari26-2007%5B13%5Dnew.pdf>>. Buginese, along with Bajau, Butung and Malays were sea peoples specialized in providing links to the outside world for communities in forested highlands such as Dayaks, Bataks, Minangkabau, Torajans, Timorese, and Balinese. See also, Taylor, below n 802, 145.

⁷⁷² Institute for Social Sustainability, *Chapter 4: Indonesian community values of relevance to the new development paradigm*, Murdoch University, 39 <<http://www.istp.murdoch.edu.au/ISTP/publications/suriptono/wastewater/04Suript.pdf>>.

⁷⁷³ Ibid.

⁷⁷⁴ The term *asas kekeluargaan* consists of two words i.e ‘*asas*’ means principle and ‘*kekeluargaan*’ means familial values. The concept of *asas kekeluargaan* is based on mutualism and brotherhood. See, Sri-Edi Swasono, *Neo-sontoloyo menggusur Ukhuwah* [Neo-silly displacing brotherhood], 2 <http://www.bappenas.go.id/files/1313/5022/6058/07sri-ediswasono__20091014130308__2253__0.pdf>. Familial principle was often misinterpreted as the family of Soeharto. Familial principle was described as ‘the state as family, with Soeharto as the head of the state-cum-family’. He was often referred to as *bapak* [father]. See, Julia Suryakusuma, *Death of a consort, end of a dynasty?*, Inside Indonesia, [5] <<http://www.insideindonesia.org/weekly-articles/death-of-a-consort-end-of-a-dynasty>>.

⁷⁷⁵ Sarbini Sumawinata, *Politik Ekonomi Kerakyatan* (Gramedia Pustaka Utama, 2004) 124.

4.2.1.2. *Impact of foreign traders on traditional values*

The arrival of overseas traders impacted these societies, cultures and values. The local people were tolerant, accommodating and flexible in accepting new values.⁷⁷⁶ In particular, the Javanese ‘strongly prefer[ed] to work in cooperation’. This was suggested by Bowen as a cultural habit, which was exploited much later by corporations in the new order era.⁷⁷⁷

The significant foreign values that came to influence these traditional communities were Hindu-Buddhism and Islam.

(a) *Hindu-Buddhist influences*

Trade at the beginning of this period was, as indicated, between South India and Indonesia. This developed into diplomatic relationships. These activities contributed to the spread of new beliefs and values.⁷⁷⁸ Between the 1st and 2nd centuries the first Buddhists arrived.⁷⁷⁹ Migrants from India also brought Hinduism.⁷⁸⁰ It spread increasingly from the 8th century, particularly the Mahayana and Hinayana sects.⁷⁸¹

The diffusion of Hindu-Buddhist beliefs affected the traditional beliefs of pre-animism or dynamism and animism⁷⁸² and most regions. The social structure also changed. A monarchy system was introduced and kings [*raja*] replaced tribal chiefs [*kepala suku*]. Hinduism also introduced the division of society into castes or *varnas*.⁷⁸³

⁷⁷⁶ Abdul Ghoffur Muhaimin, *The Islamic traditions of Cirebon – Ibadat and adat among Javanese muslims* (ANU Press, 2006) 1.

⁷⁷⁷ Java and Javanese have been seen as to be the core of the nation. See, Taylor, below n 802, xviii.

⁷⁷⁸ Asianinfo.org, *Indonesia’s history and background*, [4] <<http://www.asianinfo.org/asianinfo/indonesia/pro-history.htm>>.

⁷⁷⁹ Ibid [8].

⁷⁸⁰ Ibid [4]–[5].

⁷⁸¹ Ibid [8].

⁷⁸² See, PHILTAR – Philosophy, Theology and Religion University of Cumbria, *Animism*, [1] <<http://www.philtar.ac.uk/encyclopedia/seasia/animism.html>>. Animism and dynamism believed that inanimate objects, such as rocks, trees, mountains and rivers, had spirits which could affect the well-being of those around them. See also, Ridwan Hasan and Muhammad Azizan bin Sabjan, *Aceh Islamic society: Beliefs in animism and dynamism*, 1 <<http://images.gmanews.tv/pdf/aseanconf/HASAN%20Ridwan%20and%20Muhammad%20Azizan%20bin%20Sabjan.pdf>>. The banyan tree and the *ketapang* tree, for example in Aceh, had the strength of *ghaib* animism and dynamism.

⁷⁸³ Asianinfo.org, above n 778, [7].

The Buddhist Sriwijaya kingdom in Sumatra became the largest maritime power in South East Asia⁷⁸⁴ and a trade centre for southern Sumatra.⁷⁸⁵ Sumatra was known as *swarna dwipa* [island of gold].⁷⁸⁶ The Buddhist Sailendra kingdom in Central Java was also culturally and economically significant.⁷⁸⁷ Java was known as *java dwipa* [island of rice].⁷⁸⁸

From the 7th to the 15th century kings came to have a significant role in trade. They collected taxes, provided security and were participants in commerce. The kings of Sriwijaya and Majapahit played significant roles. The Sriwijaya kingdom, most powerful between the 9th and 11th century,⁷⁸⁹ depended on international trade. Its location linked it to the main international sea-based trade routes from China to Europe through the Straits of Malacca. Every merchant ship was obliged to transit Sriwijaya's seaport.⁷⁹⁰ Malacca, on the northern side of the Straits, became one of the 'emporiums',⁷⁹¹ in the 10th and 11th century.⁷⁹² From 1293 to 1500 Sriwijaya's role was replaced by the Hindu kingdom, Majapahit, in East Java. It was an agrarian and trading empire that controlled territories from the Moluccas to North Sumatra.⁷⁹³

⁷⁸⁴ Suara Edukasi Kemdikbud [The Voice of Ministry for Education and Culture for Education], *Kerajaan Sriwijaya sebagai pusat agama Budha* [Sriwijaya kingdom as a central of Buddhism] (2012) [1] <<http://suaraedukasi.kemdikbud.go.id/listings/kerajaan-sriwijaya-sebagai-pusat-agama-budha/>>.

⁷⁸⁵ Robert Cribb, 'Nation: Making Indonesia' in Donald K Emmerson (ed), *Indonesia beyond Suharto – Polity economy society transition* (East Gate Book in cooperation with the Asia Society, 1999) 3, 5.

⁷⁸⁶ Asianinfo.org, above n 778, [8].

⁷⁸⁷ Ibid [13]. It was the location of the large Buddhist temple, Borobudur, built between 750–850.

⁷⁸⁸ Ibid [4].

⁷⁸⁹ Suwardi, above n 767, 181.

⁷⁹⁰ Unit Khusus Museum Bank Indonesia, *Sejarah Pra Bank Indonesia, Nusantara s.d. awal abad ke-19*, 1 <<http://www.bi.go.id/id/tentang-bi/museum/sejarah-bi/prabi/Documents/18745b6d03f7413ba8ab53c2a29ec8e5NusantarasdAwalAbadke19.pdf>>.

⁷⁹¹ See, Ibid 5. The emporium was a port city which had complete facilities for repairing merchant ships and conducting business transactions. There were marked by significant large entrepreneurs, warehouses, and also ships for rent and purchase.

⁷⁹² Ibid. Other emporiums were Aden and Mocha in the Red Sea; Muskat, Bandar Abaz and Hormuz in the Persian Gulf; Kambai and Kalikut in the Arabian Sea; Satgaon in the Benggala Gulf and Zaiton and Nanking in China.

⁷⁹³ Ibid 6.

Religious beliefs influenced trading behaviour. Shared values and ethical standpoints strengthened trust and reduced transaction costs.⁷⁹⁴ Hindu values favoured economic exchange with trading ‘traditionally reserved to a specific caste’ indicating the high level of trust between trading partners.⁷⁹⁵ Adherence to Hinduism is marked by renouncing selfish desires and exercising selfless service, renouncing dishonesty, exercising integrity and seeking happiness that is beneficial to all.⁷⁹⁶ Hinduism like Buddhism is focussed on escaping materialism.⁷⁹⁷ In Buddhism the fifth element in the right path of living is the right livelihood, which is based on doing no harm to others or engaging in ethical behaviour, including not lying and not stealing.⁷⁹⁸ In Buddhism, the trust between merchants from different countries may have been less. It may have been limited by the considerable differences between country-specific versions of Buddhism. Buddhism is known as ‘a highly flexible and diversified belief’.⁷⁹⁹ Yet, one of the

⁷⁹⁴ Matthias Helble, *On the influence of world religions on international trade*, 211–12 <<http://www.princeton.edu/jpia/past-issues-1/2006/11.pdf>>.

⁷⁹⁵ Ibid 212–13. There are four legitimate aims of life in Hinduism: dharma, artha, karma, and moksha [righteousness, economic well-being, pleasure, and salvation]. The sacred scriptures, Veddas, introduces economic concepts: production, exchange, wages, interest, rent, profit, and the market. A Hindu is born into a certain caste which is often defined by the profession of their members. The castes of Agrawal and Aroras in India, for example, are responsible for good’s trade. The trading system under Hindu values implies high transaction costs.

⁷⁹⁶ Balakrishnan Muniapan, ‘The Bhagavad-Gita and Business Ethics: A Leadership Perspective’ in Dasho Karma Ura and Patricia Ordonez de Pablos, *Asian Business and Management Practices: Trends and Global Consideration* (2014) 232, 245; Balakrishnan Muniapan, ‘The Roots of Indian Corporate Social Responsibility (CSR) Practice from a Vedantic Perspective’ in Kim Cheng Patrick Low, Samuel O Idowu and Sik Liong Ang (eds), *Corporate Social Responsibility in Asia* (Springer International Publishing, 2014) 19–33.

⁷⁹⁷ Bruno Dyck, ‘God on management: The world’s largest religions, the “theological turn,” and organization and management theory and practice’ in Paul Tracey, Nelson Phillips and Michael Lounsbury (eds), *Research in the Sociology of Organizations, Volume 41: Religion and Organization Theory* (Emerald Group Publishing Limited, 2014) 23, 43.

⁷⁹⁸ Kate Stirling, ‘Buddhist wisdom as a path to a new economic enlightenment’ (2014) 33 (8/9) *Journal of Management Development* 812–823; Wanna Prayukvong and M John Foster, ‘Buddhist economics meets corporate social responsibility’ (2014) 8(2) *International Journal of Economics and Business Research* 175–192.

⁷⁹⁹ Prayukvong and Foster, above n 798, 214. Buddhism is a tolerant belief to other religions. The principle of interdependency is its important principle. The principles of sustainability and provision of all species are seen as the basis principles to use the resources. It respects differences in ability and wealth as long as all participants’ interests are maintained.

significant elements in Buddhism is shame.⁸⁰⁰ The coming of Moslem traders and their beliefs and values ended the direct influences of Hindu and Buddhist religions in the archipelago, except for Bali.

(b) Muslim influences

In the 13th century, Moslem merchants from Gujarat and Persia arrived. Their politeness and honesty appealed to locals. These influences led Hindus, including kings, to convert to Islam.⁸⁰¹ The former rajas were now known as ‘sultans’, literally meaning ‘power’ or ‘authority’.⁸⁰² These sultans have been described as ‘the heads of a highly organized municipal government, whose main purpose was to facilitate trade’.⁸⁰³ A greater profit from trade was a significant goal for the sultans.⁸⁰⁴ In northern Sumatra, for example, Aceh’s rulers ‘financed the laying out of pepper plantations from their taxes on trade’.⁸⁰⁵ The sultans ‘used their wealth to create political power’ as well as to support religious teachers and institutions⁸⁰⁶ leading to the expansion of Islam. In Malacca it became the official religion. In 1414, Malacca emerged as the largest emporium in the Asian region.⁸⁰⁷ In 1520, the powerful Hindu kingdom, Majapahit, in East Java collapsed. Islam spread further to the east. It spread further west to Sumatra. In 1527, *Sunda Kelapa*, the capital of the West Java kingdom of *Pajajaran*, was conquered. It was renamed *Jaya Karta* [great city]. It is now known as Jakarta.⁸⁰⁸

⁸⁰⁰ S Manik, *Abstrak* [Abstract] (2013) 69
<<http://repository.usu.ac.id/bitstream/123456789/38111/6/Abstract.pdf>>.

⁸⁰¹ Asiainfo.org, above n 778, [22].

⁸⁰² Jean Gelman Taylor, *Indonesia: Peoples and histories* (Yale University Press, 2003) 69.

⁸⁰³ Travel and Cultural Guide Geographia, *Islam and the golden age of Malacca 1400 AD–1511 AD*, [2] <<http://www.geographia.com/malaysia/history03.htm>>.

⁸⁰⁴ Taylor, above n 802, 73.

⁸⁰⁵ *Ibid* 125.

⁸⁰⁶ *Ibid* 126. See also, page 123. Banten in Java became a centre of Islamic learning. Its rulers had ‘a reputation for generosity and hospitality to scholars travelling the Islamic world’. They extended their influence by defeating Sumatran rulers, and marrying from families of sultans who controlled important markets. See, eg, Asiainfo.org, above n 778, [23]. The Sultan of Demak in Central Java, for example, spread Islam through West Java from Cirebon to Banten, and along the northern coast of Java to the kingdom of Gresik in East Java.

⁸⁰⁷ Open University Malaysia, *Traditional Malay kingdoms*, 3
<http://www.oum.edu.my/oum/v3/download/MPW1133_2133.pdf#page=5&zoom=auto,0,153>.

⁸⁰⁸ Asiainfo.org, above n 778, [22]–[26].

The conversion of the kingdoms to Islam attracted more Moslem traders from the Middle East and India.⁸⁰⁹ Their commercial activities were governed by *sharia*. Its values are trustworthiness [*bersikap benar*] and honesty [*amanah dan jujur*].⁸¹⁰ The Koran ‘gives very explicit guidelines for economic behaviour’. Commerce is ‘considered as important as producing’. Honesty is the most important value. Rules have to be obeyed. Deceivers or cheaters are condemned. The quality of the traded goods is the trader’s responsibility.⁸¹¹ It also upholds justice [*menjunjung tinggi keadilan*]. It forbids interest and monopolies [*mengharamkan bunga dan monopoli*].⁸¹² It emphasizes the qualitative rather than quantitative aspects of commercial transactions.⁸¹³

4.2.2. European influences and their impacts

The Portuguese arrived in the archipelago in 15th century and were followed by other European traders.⁸¹⁴ The Portuguese were noted for the violent disruption of what had been relatively peaceful trade until their surrender in 1949. They had a revolutionary impact on traditional cultures and values. European ideas and individualism and liberty, particularly after the English and French revolutions, came to contrast with Javanese and other Asian cultures who emphasised collectivism and command. In the 15th century, European society was still largely feudal. Importantly, after the French revolution, colonial powers encouraged individualism or liberty for indigenous people in their colonies. The Dutch law discriminated against natives.

The introduction of Catholicism challenged the spread of Islam. As Portuguese power faded outside of East Timor it had little influence, as many Catholics were converted to the Protestantism of the new coloniser: the Dutch.⁸¹⁵ The Dutch colonial social order was

⁸⁰⁹ Unit Khusus Bank Indonesia, above n 790, 5.

⁸¹⁰ Elfina Yenti, *Pengaruh pemahaman nilai-nilai syariah terhadap perilaku bisnis pedagang Minang pada pasar Aur Kuning Bukittinggi*, [The influence of sharia values on business attitudes of Minang traders at Aur Kuning Bukittinggi market] 3 <<http://pasca.unand.ac.id/id/wp-content/uploads/2011/09/PENGARUH-PEMAHAMAN-NILAI-NILAI-SYARIAH.pdf>>.

⁸¹¹ Helble, above n 794, 216

⁸¹² Yenti, above n 810.

⁸¹³ Helble, above n 794, 217.

⁸¹⁴ Rotem Kowner, *An obscure history* (2011) Inside Indonesia, [2]

<<http://www.insideindonesia.org/an-obscure-history>>.

⁸¹⁵ Karel Adriaan Steenbrink and Jan Sihar Aritonang (eds), *A history of Christianity in Indonesia* (Brill, 2008) vol 35, 14.

based on rigid racial and social structures with a Dutch elite living separate from, but linked to, their native subjects.⁸¹⁶

Dutch control over parts of the archipelago lasted over 350 years and had a pivotal influence. Dutch law came to be the official legal system in the Dutch East Indies. The introduction of capitalism came through the introduction of the monopoly system of the Dutch East Indies Company that dominated commercial practices and business associations. The *Koperasi* [cooperative] represented some basic traditional cultures of *gotong-royong* [communal work or mutual aid] and *asas kekeluargaan* [familial principle], as indicated, as earlier values were influenced by western values. The concept of the company itself was introduced. The practices associated with western capitalism, such as accounting, were also introduced.⁸¹⁷ Under colonisation paternalism became the norm. Dutch power enforced some western values on people.

4.2.2.1. Portuguese influence (1509–1659)

The Portuguese occupation had less lasting influence on traditional values and trade practices, apart from the regions of significant conversion to Catholicism, mostly in Flores and Timor and the eastern parts of the archipelago.⁸¹⁸

Bartolomeu Dias sailed east past the Cape of Good Hope in South Africa in 1488 and Vasco da Gamma followed, reaching the Indian coast at Calicut in 1498.⁸¹⁹ In India, the Portuguese learnt of Malacca and its spices. In 1509, the Portuguese landed there to

⁸¹⁶ Robert B Cribb and Audrey Kahin, *Historical dictionary of Indonesia* (Scarecrow Press, 2004) vol 51, 118.

⁸¹⁷ Eko G Sukoharsono and Michael J R Gaffikin, 'The genesis of accounting in Indonesia: the Dutch colonialism in the early 17th century' (2014) 1(1) *The International Journal of Accounting and Business Society* 4, 9–10; Eko Ganis Sukoharsono, 'Accounting, Colonial Capitalists, and Liberal Order: The Case of Accounting History in Indonesia during the Dutch Colonial Period of the Mid-to-End of the 19th Century' (2014) 3(1) *The International Journal of Accounting and Business Society* 1–28 <<http://ijabs.uib.ac.id/index.php/ijabs/article/view/225/153>>.

⁸¹⁸ The Portuguese contributed to the introduction of some skills and equipments and became a good supplier. See, Taylor, above n 802, 138. The Portuguese introduced new knowledge of mechanical clocks and printed books. The introduction of firearms, ammunition, and cannon contributed to the ability of rulers in equipping fleets and extending taxpaying territories under their command. They also supplied European manufactured goods to the archipelago.

⁸¹⁹ Winsor, above n 768, [17]–[18].

trade. Their offers were rejected and in 1511 Alfonso d’Burquerque conquered it.⁸²⁰ The Portuguese controlled some parts of the archipelago until 1659 and East Timor until 1975.⁸²¹ From Malacca they expanded to Maluku and to Minahasa⁸²² in North Sulawesi.

During the Portuguese occupation, the influence of its Christian culture on commerce spread.⁸²³ The religious values of that culture, as with the later Dutch colonisers, contrasted with the violence used to seize control of territory and the unequal treatment of indigenous peoples.⁸²⁴ Christianity, for the Portuguese, was considered part of the natural order and ‘more as a necessity than a contribution to the economic well-being’. However, the avoidance of fraud and greed were common. As in Islam, honesty is an important prerequisite for trust in commerce, reflecting Christian morality. The role of the market and the use of money were justified by St Thomas Aquinas. Exchange must be voluntary and at a fair price. Subjective human estimations determined that just price. Transactions should take place in a free market and be equitable.⁸²⁵ They need to accord with commutative and distributive justice. The first is where the form of transactions is ‘an exchange of goods

⁸²⁰ Asianinfo.org, above n 778, [27]. In 1570, the Portuguese killed the Sultan of Ternate, Khairun. The Sultan’s successor, Sultan Baabullah, allied with the Dutch against the Portuguese and Spaniards.

⁸²¹ Unit Khusus Museum Bank Indonesia, above n 790, 6. More than 200 years, the formal and precise territories between the two colonial powers, Dutch and Portugal, were unclear. A treaty on 20 April 1859 finally concluded the division of controlled territories: the Dutch won the western part and Portugal the eastern part of the Timor islands. Portugal secured control over the East Timor until 1975. See, Asia.info.org, above n 778, [27] & [29].

⁸²² Asianinfo.org, above n 778, [27]. Later, Dutch Protestant’ influence dominated over Portuguese Catholics in Moluccas, Manado and Minahasa. See, Seta Basri, *Pengaruh budaya barat Belanda Portugis serta Jepang atas kebudayaan Indonesia* [The influence of western culture of Dutch, Portuguese and Japan on Indonesian culture] <<http://setabasri01.blogspot.com.au/2012/04/pengaruh-barat-di-indonesia.html>>. See, Unit Khusus Museum Bank Indonesia, above n 790, 6. In 1521, Spaniards landed in the Moluccas from the Philippines. There were welcomed by local people, but the Portuguese attacked them as potential competitors.

⁸²³ See generally, Taylor, above n 802, 119–20. They circulated printed Catholic books as gifts. They also discussed Christianity and debated Islamic beliefs with the non-Moslem rulers. Moslems believed that ‘their religion as a perfect knowledge, information originating in Christian Europe was sometimes considered irrelevant or useless’. The Portuguese were categorised as *kafir*, Indonesian language from Arabic, means ‘a person who has no belief (rather than a person who believes in another religion) and has a pejorative connotation’

⁸²⁴ Perry Anderson, ‘Portugal and the End of Ultra-colonialism’ (1961) 1 *New Left Review* 83, 91–3.

⁸²⁵ Helble, above n 794, 215. St. Thomas Aquinas economic thinking was widely adopted by the Catholic Church.

between two persons, or as the distribution of the good in a community to its member'. There should be equivalence between the value of the goods given and the goods received. The second is the reception of a share of the community's goods in a standing proportion.⁸²⁶ Usury or the charging of interest was not just⁸²⁷ and similar to the Islamic value of *mengharamkan bunga* or *riba* [forbidding interest]. Demanding any payment beyond the principal of a loan was a sin against charity.⁸²⁸ St Thomas Aquinas stated it was inconsistent with commutative justice⁸²⁹ as the amount borrowed and repaid was not equal.⁸³⁰

4.2.2.2. Dutch influence (1602–1942)

The Dutch's occupation brought several forms of influences on Indonesia including among others the introduction of capitalist enterprises and the concept of the corporation as well as Western values and the evolution of traditional association and colonial paternalism.

(a) The introduction of capitalist enterprise

The Dutch landed in Banten on the east coast of Java. They initially came as traders under the umbrella of the Royal East Indies Company [*Vereenigde Oostindische Compagnie* (VOC)].⁸³¹

⁸²⁶ Joseph Burke, 'Money for nothing: the sin of usury' (Working Paper No. 0801, Department of Economics, Ave Maria University, 25 November 2008) 1 <<http://mysite.avemaria.edu/jburke/working-papers/WP0801-Burke-Usury.pdf>>.

⁸²⁷ Ibid. Cf, Constant J Mews and Ibrahim Abraham, 'Usury and just compensation: Religious and Financial ethics in historical perspective' (2007) 72(1) *Journal of Business Ethics* 1, 1 <[http://www.jstor.org/discover/pgs/index?id=10.2307/25075354&img=dtc.7.tif.gif&uid=2129&uid=2&uid=70&uid=4&sid=21102880340623](http://www.jstor.org/discover/pgs/index?id=10.2307/25075354&img=dtc.7.tif.gif&uid=2129&uid=2&uid=70&uid=4&sid=21102880340623&orig=/discover/10.2307/25075354?uid=2129&uid=2&uid=70&uid=4&sid=21102880340623)>. From the contemporary mainstream of finance, charging interest practices are 'considered so normal'. It has been seen as market forces compulsion rather than ethical proportion. It was also challenged by difficulties in constituting an ethical correct of charging excessive interest on a loan.

⁸²⁸ John Munro, *Usury and Calvinism in Protestant England from the sixteenth century to the industrial revolution* (May 2011) University of Toronto, 1-2 <www.economics.utoronto.ca/munro5/UsuryCalvinProtEngland.ppt>.

⁸²⁹ Burke, above n 826, 1.

⁸³⁰ Ibid 2.

⁸³¹ 'Indonesian history – Indonesia, a nation in transition', *The Jakarta Post* (online,) [4] <http://www.thejakartapost.com/resources/indonesian_history>. The Dutch were believed to have arrived in Indonesia in 1605, partially displacing the Javanese dynasts, and held onto their territories

The VOC was established in Amsterdam on 20 March 1602.⁸³² It was ‘a combination of commercial organisations in various cities of Holland and Zeeland’,⁸³³ with sole trading rights in Asia.⁸³⁴ It has been described as the first multinational corporation⁸³⁵ and the world’s first joint-stock company⁸³⁶ with distributed stock or negotiable shares.⁸³⁷ It was controlled by a board.⁸³⁸ The seventeen directors ‘appointed the governor-general, senior officials, merchants, clerks, artisans, scholars, and clergy and authorized the outfitting of ships and the hiring of crews and soldiers’. They ran the company by written instructions from Amsterdam.⁸³⁹

The VOC was the Dutch instrument for conducting a monopoly business in the East Indies, particularly in Java.⁸⁴⁰ Batavia, previously *Sunda Kelapa*, now Jakarta, was its capital or headquarters of the company’s administration.⁸⁴¹

The company’s monopoly on trade was further secured after the seizure of Ambon in Maluku in 1605 and Banda in 1623. Under its monopoly system, agricultural produce

until 1942. See also, James H Cassing, ‘Economic policy and political culture in Indonesia’ (2000) 16 *European Journal of Political Economy* 159, 161. Taylor introduced that the Dutch sailed to the archipelago for the first time in 1595. See also, Taylor, above n 802, 138. See also, page 122, 140. Banten had a deep harbour protected by many small islands from the open sea. It was a royal city, a site of pilgrimage, a center of Islamic learning, had an attractive market, and a place for repairing and provisioning ships. The Dutch arrived when Moslem governments were maturing. Aceh, for example, had developed Islamic institutions, values, and outlook for almost one hundred years. Banten as the second was Moslem for fifty years.

⁸³² I Bima, *Sejarah VOC di jaman Hindia Belanda* [History of VOC in Dutch East Indies period] (2012), 1 <[eprints.uny.ac.id/.../BAB%201%20\(04407141013\).rtf](http://eprints.uny.ac.id/.../BAB%201%20(04407141013).rtf)>.

⁸³³ Rijksmuseum – Het museum van Nederland, *Multinational* <<https://www.rijksmuseum.nl/en/explore-the-collection/timeline-dutch-history/1602-trade-with-the-east-voc>>.

⁸³⁴ Peter Burns, *The Leiden legacy – Concepts of law in Indonesia* (KITLV, Royal Netherlands Institute of Southeast Asian and Caribbean studies, 2004) 47.

⁸³⁵ Abdul Irsan, *Indonesia dan VOC (Verenigde Oostindische Compagnie)* [Indonesia and VOC], [4] <<http://www.blimbing.nl/irsan.htm>>.

⁸³⁶ AmerIndo, *Indonesia under the VOC* (2010) Dutch Studies Department, UC Berkeley, [1] <<http://amerindo.berkeley.edu/history/indonesia-under-the-voc/>>.

⁸³⁷ ‘Hari ini 20 Maret: VOC didirikan’ [Today in history March 20th: VOC was established], *Republika* (online), 9 September 2013, [2] <<http://www.republika.co.id/berita/nasional/umum/13/03/20/mjxp74-hari-ini-20-maret-voc-didirikan>>.

⁸³⁸ AmerIndo, above n 836, [2]. The members were called the Heren XVII [17 lords].

⁸³⁹ Taylor, above n 802, 149.

⁸⁴⁰ Bima, above n 832.

⁸⁴¹ Taylor, above n 802, 147.

had to be surrendered by farmers to Dutch merchants. This gradually destroyed local inter-island trade.⁸⁴² In 1651, Kupang in west Timor was also invaded by the Dutch.⁸⁴³

During the period of the VOC's power, *Tionghoa* [Chinese] merchants played a key role as intermediaries involved in collecting and distributing products.⁸⁴⁴ Unlike indigenous entrepreneurs, Chinese traders were encouraged 'to modify and codify their traditional form of commercial associations or partnerships called "kongsi".' These had some aspects of contemporary limited liability partnerships but customary family connections and personal networks for accessing resources and information persisted.⁸⁴⁵ Predominant in both large and small scale domestic trading,⁸⁴⁶ they therefore dominated regional and local trade.⁸⁴⁷ The mutual trust through sharing capital with family members who worked together was one factor for their success.⁸⁴⁸ There was also a willingness among them to work hard in difficult conditions. They also had experience and knowledge of market conditions across regions.⁸⁴⁹

The VOC dominated for two centuries.⁸⁵⁰ Through mismanagement it collapsed in bankruptcy in 1799.⁸⁵¹ The significant causes were inefficient and ineffective management, lack of transparency to shareholders, improper recruitment and corruption.⁸⁵² Of these,

⁸⁴² Asiainfo.org, above n 778, [31], [34].

⁸⁴³ Ibid [27] & [29].

⁸⁴⁴ Bima, above n 832, 2–3.

⁸⁴⁵ Ahmad D Habir, 'Conglomerates: All in the family?' in Donald K Emmerson (ed), *Indonesia beyond Suharto – Polity Economy Society Transition* (East Gate Book in cooperation with the Asia Society, 1999) 168–9. Their business type was relied on trusted shareholders including family members rather than impersonal capital markets. Directors were often their relatives.

⁸⁴⁶ I Ketut Marjana, 'Policy changes in Indonesian public enterprises during the old order and new order governments' (1992) 9 (2) *ASEAN Economic Bulletin* 187, 191.

⁸⁴⁷ van Zanden and Marks, above n 770, 30.

⁸⁴⁸ Bima, above n 832, 2–3. See also, Taylor, above n 802, 129. Their businesses were closed to a source of employment and expansion of skill among locals.

⁸⁴⁹ Taylor, above n 802, 128. They also included 'skilled artisans who were products of China's long traditions of manufacturing and processing', as well as skilled farmers specializing in export crops.

⁸⁵⁰ Repository Universitas Sumatra Utara, *Tinjauan umum terhadap perbankan* [A general review of banking], 1–2 <<http://repository.usu.ac.id/bitstream/123456789/30113/3/Chapter%20II.pdf>>.

⁸⁵¹ Ibid.

⁸⁵² A Kardiyat Wiharyanto, *Pergantian kekuasaan di Indonesia tahun 1800* [A transition of the power in 1800 in Indonesia], 5–8

corruption was believed to be the main factor.⁸⁵³ The occupation by France of the Netherlands in 1795 had also contributed. The Napoleonic wars had consequences in Southeast Asia. The Dutch East Indies came under the rule of the British East India Company, often seen as one of the origins of global corporate governance.⁸⁵⁴ A treaty signed in London in 1814 at the end of the wars returned the East Indies to the Dutch.⁸⁵⁵ In the absence of the VOC the Dutch government took over their administration.

In 1824, the Dutch established a new trading company called the Netherlands Trading Society [*Nederlandsche Handel-Maatschappij (NHM)*].⁸⁵⁶ It embraced ‘all merchants in the Indies trade and was supported by the Netherland’s government with the king as its chief shareholder’.⁸⁵⁷ This became the tool of the Dutch government in Indonesia to continue its ‘monopoly on trade in products produced under the cultivation system’⁸⁵⁸ or culture system [*cultuurstelsel*] after 1830. The system required a fifth of cultivable land be planted with export crops.⁸⁵⁹ It was a successful system that brought a very large income to the Dutch⁸⁶⁰ representing 18 million gulden, or about a third of the Dutch budget in the period between 1840 and 1880.⁸⁶¹ A number of factors contributed to its success. These included cooperation by local and regional elites from village heads and

<<http://www.usd.ac.id/lembaga/lppm/f113/Jurnal%20Historia%20Vitae/vol21no1april2007/PERGANTIAN%20KEKUASAAN%20DI%20INDONESIA%20kardiyat.pdf>>.

⁸⁵³ Fiki Priyatna, *Perlindungan hukum terhadap pemegang saham minoritas perseroan terbatas terbuka* [Legal protection to minority shareholders of public limited companies], [10] <<http://fikiwarobay.blogspot.com.au/2012/05/perlindungan-hukum-terhadap-pemegang.html>>.

⁸⁵⁴ Cheffins, above n 559, 20. The launching of the formation of the East Indies’ company, the Hudson’s Bay company, the Levant company and the other major chartered companies in the 16th and 17th centuries was believed as the initial historical background of corporate governance. See also, Asiainfo.org, above n 778, [40], [42]. Under British control, Sir Thomas Stamford Raffles, as Lieutenant Governor General of Java and its dependencies, introduced partial self-government, abolished the slave trade, and land-tenure system. It replaced the Dutch forced-agricultural system under which the crops ‘were grown and surrendered to the government’.

⁸⁵⁵ Asiainfo.org, above n 778, [44].

⁸⁵⁶ van Zanden and Marks, above n 770, 47.

⁸⁵⁷ Network Indonesia, *Dutch rule from 1815 to 1920s – The cultivation system*, [1] <<http://users.skynet.be/network.indonesia/ni4001c9c.htm>>.

⁸⁵⁸ van Zanden and Marks, above n 770.

⁸⁵⁹ Network Indonesia, above n 857. The culture system was the idea of Johannes van den Bosch, a governor-general.

⁸⁶⁰ van Zanden and Marks, above n 770.

⁸⁶¹ Network Indonesia, above n 857.

higher members of the *priyayi*⁸⁶² class. They received a share of the proceeds [*kultuurprocenten*], which was a strong incentive for them to cooperate. Chinese merchants were also incorporated into it. They played a significant role in supplying the new entrepreneurship and expertise, especially in sugar processing.⁸⁶³ For the Javanese, the system was an extension of village production. The exports increased the economic openness of Java to foreign trade, rising from about 15 per cent to almost 40 per cent of its production.⁸⁶⁴ Such openness usually accelerates economic development⁸⁶⁵ but the monopoly system benefited the NHM and the Dutch government rather than the Javanese people.⁸⁶⁶

The colonial and bureaucratic capitalism of the Dutch left a legacy after independence of state and crony capitalism, and military bureaucracy.

(b) *The introduction of the concept of the corporation*

From the time of the Dutch occupation, the concept of corporate governance existed in Indonesia long before it had a name. The VOC demonstrated ideas of corporate governance. Corporate law subsequently appeared in the colonial jurisprudence. The Dutch law, *Wetboek van Koophandel voor Indonesie* (WvK), promulgated on 1 May 1848⁸⁶⁷

⁸⁶² See, the meaning of term ‘priyayi’ at Encyclopaedia Britannica, *Priyayi*, [1] <<http://www.britannica.com/EBchecked/topic/477417/priyayi>>. Priyayi or Prijaji was the elite in traditional Javanese society. They were the rulers of the Javanese states under the royal families until the 18th century. They gradually became professional civil servants. They were the first Indonesians to get Western (Dutch) education. See also at Kamus Besar Bahasa Indonesia [General Dictionary of Indonesian Language], *Priayi* <<http://kbbi.web.id/priyayi>>. Indonesian word ‘priayi’ means orang yang termasuk lapisan masyarakat yang kedudukannya dianggap terhormat, misalnya golongan pegawai negeri [class of people who are considered having respectable position in society such as a civil servant].

⁸⁶³ van Zanden and Marks, above n 770, 47–8. See also, page 21. Chinese merchants engaged in small trading, tax farming and money-lending.

⁸⁶⁴ Ibid 21. See generally, Living in Indonesia, *The Javanese*, [1] <<http://livinginindonesia.info/item/the-javanese>>. Javanese are the majority population, comprising 47 per cent of the total population of Indonesia. Java island politically, culturally and geographically sits on the center of the nation.

⁸⁶⁵ van Zanden and Marks, above n 770, 20.

⁸⁶⁶ Network Indonesia, above n 857, [3].

⁸⁶⁷ Priyatna, above n 853, [4]–[6]. See also, Susan Fitriyanti, *Pokok-pokok Hukum Perdata* [Principles of Civil Law], 4, 5 <file.upi.edu/...S.../HUKUM_PERDATA.pptx>. The WvK was derived from Dutch law i.e. *Wetboek van Koophandel* which was promulgated on 1 October 1838 – the same promulgation date of the *Burgerlijk Wetboek* (Civil Code or *Kitab Undang-undang Hukum*

introduced the concept of the company. The law is now known as *Kitab Undang-undang Hukum Dagang* (KUHD) [Indonesian Commercial Code] and it has been partially replaced by other laws.⁸⁶⁸ Article 54 of the WvK, for example, represented the super majority principle [*prinsip majoritas super*] and the quota principle to protect minority shareholders.⁸⁶⁹ These were subsequently amended to introduce the one share one vote system.⁸⁷⁰ The governance structure followed the Dutch civil law tradition, adopting a two-tier board system. It comprises a board of directors [*dewan direksi*] and a board of commissioners [*dewan komisaris*].⁸⁷¹

The WvK initially applied to Dutch and other European settlers in the East Indies. Colonial jurisprudence reflected the apartheid structure of Dutch colonial society based on

Perdata). The WvK applied to Indische Nederlanders – Dutch people who lived in the Dutch East Indies, now Indonesia. Based on the concordance principle [*asas konkordansi*], the law for Dutch people living in the Dutch Indies should be adjusted and adopted to Dutch laws. The Dutch WvK was derived from the French ‘Code du Commerce’ in 1808.

⁸⁶⁸ In 1906, the chapter two of the WvK was replaced by Bankruptcy Law [*Faillissement Verordening*]. Under the Article I & II of Transitional Provision of the 1945 Constitution, all existing institutions and regulations (Dutch legal legacies) shall continue to be valid pending the enactment of new legislation. Indonesian government introduced a national Bankruptcy Law in 1998 and was replaced by the Law No.37 of 2004. See generally, Rosalia Suci et al, ‘Aspek hukum kepailitan dan insovensi bank di negara-negara ASEAN’ [Legal aspects of bankruptcy and insolvent bank in ASEAN countries] (2011) 9 (3) *Buletin Hukum Perbankan dan Kebanksentralan* [Bulletin of Banking Law and Central Bank] 1, 3 <<http://www.bi.go.id/NR/rdonlyres/9B7BB0CB-AF5F-432E-BCF5-79AFEAC0A30B/26825/BuletinHukum09091211.pdf>>. See also, USU Institutional Repository, *Bab II – Hukum Kepailitan* [Bankruptcy Law], 20 <<http://repository.usu.ac.id/bitstream/123456789/26118/3/Chapter%20II.pdf>>.

⁸⁶⁹ Priyatna, above n 853. See also, Aripin, *Perlindungan hukum terhadap pemegang saham minoritas perseroan terbatas terbuka dalam rangka menciptakan kepastian hukum sebagai sarana peningkatan iklim investasi Indonesia* [Legal protection for minority shareholders of public limited companies in order to create legal certainty as an instrument for improving the investment atmosphere in Indonesia] (Skripsi, Universitas Sebelas Maret, 2009) 4 <<http://eprints.uns.ac.id/4818/1/143281208201003021.pdf>>. Prinsip majoritas super is a decision made in general meeting of shareholders should achieve more than certain numbers of legitimate votes – i.e. two-thirds or three-quarters votes. Prinsip Quota is a system of limited voting rights – shareholders should not have more than six votes if they own 100 or more shares of the capital of the company; and no more than three votes for less than 100 shares.

⁸⁷⁰ Law No. 4 of 1971 concerning Amendments and Augmentations to Article 54 of the Commercial Code [Undang-undang No. 4 Tahun 1971 tentang Perubahan and Penambahan atas ketentuan pasal 54 Kitab Undang-undang Hukum Dagang] This was accommodated into the Company Law No. 1 of 1995 which was replaced by the Law No. 40 of 2007. See, Priyatna, above n 853, [4]–[6].

⁸⁷¹ Benny S Tabaluyan, ‘The New Indonesian Company Law’ (1996) 17(3) *University of Pennsylvania Journal of International Economic Law* 883, 890 <<http://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=1480&context=jil>>.

Article 75 of the *Regerings Reglement* of 1854, the de facto colonial constitution. In 1929, the amendment of articles 163 and 131 of the *Indische Staatsregeling*, replacing the *Regerings Reglement*, confirmed the division of the population in Article 75 into three different racial groups ie: Europeans (including the Japanese as honorary Europeans), foreign Orientals (Chinese, Indians and Arabs) and natives. Different laws applied to each group created, with the expectation that while Dutch law would prevail, the non-European population would live under their own law and customs including *adat* for those classified as natives.⁸⁷²

In this period, the capital market was established in 1912 in Batavia [Jakarta]. It mainly served the interests of the Dutch. It never functioned effectively due to the First and the Second World Wars and the transfer of power from the Dutch government to the Indonesian government.⁸⁷³ It was closed from 1914 to 1918, re-opened from 1925–1942 and closed again from 1942 to 1952.⁸⁷⁴ By the end of Dutch rule, the concept of the company and the stock market were known to the business elite.

(c) Western values and the evolution of traditional business association

Historically, mutuality and cooperation was the form of enterprise in agricultural societies, like Indonesia. Working together, as indicated earlier by *gotong royong*, was a common example of the value of mutual assistance. Farmers ‘relied on one another to defend land, harvest crops, build barns and storage buildings and share equipment’.⁸⁷⁵ The later period of Dutch colonisation impacted to reinforce these values with the introduction of co-operatives. The earliest contemporary form of cooperatives had appeared during the Industrial Revolution in Europe in the late 18th and early 19th centuries.⁸⁷⁶

⁸⁷² Lindsey, ‘Indonesia’, above n 764, 31,253–4. The population of the Netherlands East Indies was divided into non-native Christians and inlanders or natives. See generally, Asean Law Association, *Chapter II: Legal system*, 22 <<http://www.aseanlawassociation.org/papers/LegalSystem.pdf>>. Article 163 of *Indische Staatregelings* was an amendment to Article 109 of *Regerings Reglement* of 1920.

⁸⁷³ Bursa Efek Indonesia [Indonesia Stock Exchange], *Sejarah* [History], [1]–[2] <<http://www.idx.co.id/id-id/beranda/tentangbei/sejarah.aspx>>.

⁸⁷⁴ *Ibid.*

⁸⁷⁵ Cooperative Development Foundation, *History of Cooperative*, [2] <<http://www.cdf.coop/history-of-cooperatives/>>

⁸⁷⁶ *Ibid* [3].

Cooperatives, known as '*koperasi*' in Indonesian, broaden knowledge about the corporate form. They represented basic traditional values of *gotong royong* and *asas kekeluargaan* [familial principle]. A Dutch government official, Booke, agreed that *koperasi* was an appropriate form for *pribumi* [indigenous] rather than other forms of capitalist enterprises.⁸⁷⁷ *Koperasi* is still seen as a middle way between capitalism and socialism.⁸⁷⁸

The first *koperasi* was established by the vice regent of Purwokerto, East Java, Aria Wiraatmadja, on 16 December 1886.⁸⁷⁹ It was aimed at helping those who were indebted to moneylenders.⁸⁸⁰ The *koperasi* movement was enlarged by *Sarekat Dagang Islam* (SDI) [Union of Islamic Traders]. The SDI established *koperasi* among indigenous traders in *batik* [traditional Javanese cloth made] entrepreneurs in 1913. It was established by Hajj Samanhudi in Surakarta in 1905.⁸⁸¹ In 1912 it became *Sarekat Islam* (SI) and expanded from commercial to political activities.

By the 1920s, *koperasi* were not only business organisations but also institutions for improving education and promoting nationalism.⁸⁸² The Dutch authorities then restricted the movement, as they thought they may become centres of resistance. The movement continued under the Japanese occupation and into independence.⁸⁸³

The 1945 Constitution adopted the *koperasi* as a fundamental economic system. In Chapter XIV, concerning the National Economy and Social Welfare, Article 33:1 states that

⁸⁷⁷ Media Info KUMKM, *Mengubah paradigm tentang koperasi* [Changing a paradigm of cooperatives], [2]–[3] <<http://www.diskopjatim.go.id/lensa/halaman-utama/opini/275-mengubah-paradigma-tentang-koperasi.html>>.

⁸⁷⁸ Ibid [2]. A British sociologist, Anthony Giddens, introduced and made known *koperasi* as the third way.

⁸⁷⁹ International Co-operative Alliance – Asia and Pacific, *Dewan Koperasi Indonesia (DEKOPIN)* (2008) [1] <<http://ica-ap.coop/AboutUs/dewan-koperasi-indonesia-dekopin>>.

⁸⁸⁰ Media Info KUMKM, above n 877, [2]

⁸⁸¹ Ari Sentani, *Sarekat Islam yang terlupakan – Dari sejarah kebangkitan bangsa* [Forgotten Islamic Union – From history of nation awakening], Sultan Agung Islamic University, [11] <http://unissula.ac.id/index.php?option=com_content&view=article&id=289:sarekat-islam-yang-terlupakan&catid=49:artikel&Itemid=163>.

⁸⁸² International Co-operative Alliance – Asia and Pacific, above n 879.

⁸⁸³ Media Info KUMKM, above n 877, [2]–[3].

‘the economy shall be organized as a common endeavour based upon the principles of the family system’.⁸⁸⁴

(d) Colonial paternalism

Dutch colonisation was to have a lasting impact on the local commercial elite. Stripriaan claimed that Dutch ‘colonialism equals paternalism’. He argued that colonization led to paternalism in economic dominance, exploitation and control.⁸⁸⁵ The period of colonisation by the VOC was described by Jan van Baal as that of a modern enterprise with the promotion of the interests of the company rather than the shareholders as the highest priority. ‘Profit is first and foremost used to ensure the company’s preservation and expansion’.⁸⁸⁶

Paternalism was seen as a ‘de facto rationale of white/European superiority and other race/culture inferiority’.⁸⁸⁷ Paternalism is generally defined as ‘the interference of a state or an individual with another person, against their will, and defended or motivated by a claim that the person interfered with will be better off or protected from harm’.⁸⁸⁸

Paternalism has been seen in different ways. In most Western countries it is regarded as ‘manipulative acts with higher levels of authoritarianism’. It has, in Turkey, India and China been considered ‘a positive process in which leaders are caring and considerate’.⁸⁸⁹ From a commercial perspective it reflects a Western perspective as ‘that

⁸⁸⁴ See, the Constitution of the Republic of Indonesia 1945 – As amended by the First Amendment of 1999, the Second Amendment of 2000, the Third Amendment of 2001 and the Fourth Amendment of 2002 at Embassy of Indonesia <<http://www.embassyofindonesia.org/about/pdf/IndonesianConstitution.pdf>>.

⁸⁸⁵ Anouk Eigenraam, Jeffrey Hochstetler and Karima Yebari, *The Dutch know best? Paternalism in the Netherlands past and present*, Humanity in Action.org, [7] <<http://www.humanityinaction.org/knowledgebase/218-the-dutch-know-best-paternalism-in-the-netherlands-past-and-present>>.

⁸⁸⁶ Kees van Dijk, *The Netherlands Indies and the Great War 1914-1918* (KITLV Press, 2007) xii-iii

⁸⁸⁷ Eigenraam, Hochstetler and Yebari, above n 885.

⁸⁸⁸ Stanford Encyclopedia of Philosophy, *Paternalism* (1st published 2002, revision 2010), [1] <<http://plato.stanford.edu/entries/paternalism/>>.

⁸⁸⁹ Dodi Wirawan Irawanto, *Exploring Paternalistic Leadership and its Application to the Indonesian Context* (PhD Dissertation, Massey University New Zealand, 2011) 5 <http://mro.massey.ac.nz/bitstream/handle/10179/2482/02_whole.pdf?sequence=1>. See also, page 4. In theory, paternalistic leadership is an applicable approach in a non-western-setting. It refers to authoritarianism. Leaders render absolute guidance, care and protection to its followers.

kind of management that does for people what ideally they should do for themselves'.⁸⁹⁰ From the perspective of governance, it introduces a hierarchal order. The leader is the sole decision maker and is often a skilful and charismatic figure.⁸⁹¹ Paternalism may be seen in family businesses. Negative connotations of paternalism in this context are challenged by Aronoff and Ward. They claim that an appearance of paternalism is found in firms, which are genuinely committed to investing in their people and that 'not all family-like firms are paternalistic'.⁸⁹² In typical family businesses, loyalty and a family-like atmosphere are valued.⁸⁹³ Compliance is highly valued compared with independence.⁸⁹⁴ This creates dependency. It may also undermine employees' initiative, creativity and responsibility.⁸⁹⁵

The Dutch continued paternalistic practices in the management of sugar plantations. This was an acceptance of local cultural traditions. Workers received the same treatment from wealthy Moslem employers based on Islamic concepts of charity.⁸⁹⁶ Similarly kings and sultans used hierarchal and authoritarian power to establish individual loyalty to them.⁸⁹⁷ However, workers under Dutch colonisation had 'a strong feeling that work was something the Dutch imposed upon them'.⁸⁹⁸ Since the workers were forced labourers rather than volunteers, their treatment was much harder rather than soft paternalism.⁸⁹⁹

⁸⁹⁰ Craig E Aronoff and John L Ward, 'The high cost of paternalism' (May 93) 81(5) *Nation's Business*, [6]–[7].

⁸⁹¹ Himawan Wijanarko, *Bisnis Indonesia – Budaya perusahaan keluarga* [Indonesian Business – Culture of family business] Jakarta Consulting Group, [5] <<http://www.jakartaconsulting.com/art-05-13.htm>>.

⁸⁹² *Ibid* [7].

⁸⁹³ *Ibid* [1]–[2], [4].

⁸⁹⁴ *Ibid* [6]–[7].

⁸⁹⁵ *Ibid* [1]–[2], [4].

⁸⁹⁶ International Encyclopedia of the Social Sciences, *Paternalism* (1968), [10] <<http://www.encyclopedia.com/topic/Paternalism.aspx>>.

⁸⁹⁷ Ahmad Adaby Darban, *Pengaruh akar budaya politik pada dinamika politik ekonomi di Indonesia* [The influence of the root of political culture in a dynamic of economic politics in Indonesia], 3 <http://www.geocities.ws/konferensinasionalsejarah/adabydarban_pengaruh_akar_budaya_politik.pdf>.

⁸⁹⁸ International Encyclopedia of the Social Sciences, above n 896.

⁸⁹⁹ Stanford Encyclopedia of Philosophy, above n 888, [20].

Paternalism had long been a model of Indonesian leadership and governance. It was found in traditional and communal societies and in extended family systems.⁹⁰⁰ It is called *bapakisme* [loyalty to a hierarchical structure of authority]. It reflects a relationship like *bapak* [father] and *anak* [child].⁹⁰¹

Other relationships came to be built on patronage and leaders became role models. Their attitudes become a justification for similar actions. It legitimises leaders, or superiors, exercising influence over subordinates. This is reflected in the three pre-eminent attitudes [*tri pakarti utama*] in the character of Indonesian corporations introduced by an educational pioneer, Ki Hajar Dewantara.⁹⁰² They are: *ing ngarso sung tuludo* [leaders of a company should be exemplary models for their subordinates], *ing madyo mangun karso* [leaders should be able to empower their subordinates] and *tut wuri handayani* [leaders should have a sense of responsibility to their subordinates].⁹⁰³

Harmony, trust, and deference are encouraged to motivate the subordinate to work diligently in obtaining the superior's approved goals. It leads to 'a blind submission to a higher authority with a lack of concern about work performance, standards, or initiative'.⁹⁰⁴

The paternalism introduced by the Dutch came to be based on individualism but the individualism of the patron. It is called the personal principle [*asas perorangan*]. It was based on a liberal paradigm.⁹⁰⁵ It established institutional, legal and cultural goals

⁹⁰⁰ Universitas Terbuka, *Tipe kepemimpinan* [Leadership types], [4] <http://www.ut.ac.id/html/suplemen/adpu4334/w2_4_2_1.htm>.

⁹⁰¹ Fatkhan Ashari, *Paternalisme: Sebuah pengaruh system politik kerajaan* [Paternalism: An influence of kingdom political system] (30 June 2012) Universitas Airlangga, [9] <http://fatkhan-ashari-fisip11.web.unair.ac.id/artikel_detail-49552-d.%20Politik-PATERNALISME:%20Sebuah%20Pengaruh%20Sistem%20Politik%20Kerajaan.html>.

⁹⁰² Rob Goodfellow, *An insider guide – Indonesian business culture* (Reed Academic Publishing Asia, 1997) 104.

⁹⁰³ Anis Chariri, *The dynamics of financial reporting practice in an Indonesian insurance company: a reflection of Javanese views of an ethical social relationship* (PhD thesis, University of Wollongong, 2006) x <<http://ro.uow.edu.au/cgi/viewcontent.cgi?article=1612&context=theses>>.

⁹⁰⁴ George B Whitfield, *Doing business in Indonesia, Cross cultural understanding – The Indonesian big five Part I: Bapakisme*, [4] <<http://www.expat.or.id/business/bigfive-bapakisme.html>>.

⁹⁰⁵ Sri-Edi Swarsono, 'Catatan tentang UU usaha kecil: Paternalism, kelembagaan hukum dan demokrasi ekonomi' [Notes for the Law of small business: Paternalism, legal entity and economic democracy] (Paper presented at the Seminar of Indonesian Advocates Association [PERADI], Jakarta, 18 Januari 1996), 54–5 <perpustakaan.bappenas.go.id/lontar/file?file...pdf>.

emphasising achieving individual or personal interests rather than community ones. It is opposed to traditional communalism as an Indonesian social value. In spite of the Dutch legacy of an egocentric patron confirming older cultural individualism of the elite, for most of the people, the national economic system should be based on collective and familial principles.⁹⁰⁶ As indicated earlier, this is reflected in Article 33 (1) of the 1945 Constitution.⁹⁰⁷

4.2.3. Japanese influence (1942–1945)

The effect of the brief Japanese occupation was marked by the establishment of a number of social and governmental institutions. They were aimed at maintaining Japanese control over the archipelago. The priority was to fulfil Japanese superiority and Japan's need for war materials rather than commerce. It led to changes in some existing Indonesian traditional cultures and beliefs.⁹⁰⁸

The Japanese sought to utilise their moral superiority over European colonial authority in their conquest of Indonesia. They successfully convinced many Indonesians of the Western lack of capacity to understand Asian morals, values, and needs.⁹⁰⁹

Ultimately the pressure of the Japanese occupation affected the integrity of people. Many suffered from brutal military punishment sanctioned by local rulers,⁹¹⁰ insufficient food because of the Japanese control over all natural resources and the application of

⁹⁰⁶ Ibid 55.

⁹⁰⁷ The Constitution of the Republic of Indonesia 1945, above n 884. Article 33 (1) says; '[t]he economy shall be organized as a common endeavour based upon the principles of the family system'.

⁹⁰⁸ See, Peter Post (General Ed), *The Encyclopedia of Indonesia in the Pacific War - In cooperation with the Netherlands Institute for war documentation* (Nederlands Instituut, 2012) 62. Japan initially occupied several regions in Sumatra in 1942. Sumatra was seen as an attractive potential island to be a permanent possession in the Greater East Asia Co-prosperity Sphere. It was rich in raw materials such as rubber, tin, bauxite and especially oil which was essential for Japan's war machine. See also, Asiainfo.org, above n 778, [77]–[78]. Japanese propaganda campaign called 'Great East Asia Co-prosperity' was believed as a camouflage for their imperialism replacing Dutch colonialism.

⁹⁰⁹ Peter Steele, 'Memorializing colonialism: Images of the Japanese occupation of Indonesia in Japanese popular theatre' (2012) 29(2) *Asian Theatre Journal* 528, 534. See also, page 535. The colonial occupation of non-Asian countries was explicitly opposed by the Japanese government. Among the critiques was that of the Western inability to understand Asian societies, as Western culture lacked moral values.

⁹¹⁰ Post, above n 908, 68. Japan distributed more than 25,000 ha of land to traditional communities and required them to grow some crops. But the Japanese tortured some people as punishment.

autarky [forced labour or *romusha*]. These compelled people to cooperate with the Japanese to survive.⁹¹¹

The early Japanese regional governments established particular organisations and changed the role of traditional rulers. The village heads and the rajas were changed from ruling elite to prominent local people. In order to control sultans' activities and to maintain their loyalty to the Japanese, *Musyrawarah Para Sultan or Sultans* [Sultan's Consultative Council] were established.⁹¹² They introduced decentralised local government with a semi-autonomy approach. It permitted different policies to be applied in each region depending on its economic potential, culture and socio-political conditions.⁹¹³ The Japanese also introduced the more open recruitment of court officials⁹¹⁴ and *uleebalang* or *hulubalang* [war leader] who varied from nobles with political powers in Aceh or kings with authority in a specific region⁹¹⁵ and who replaced Dutch customary rulers.

The Japanese also created and enforced a tributary system that impacted commercial integrity.

⁹¹¹ Ibid 69. The Japanese recruited forced-labour [*romusha*] for plantation and construction projects.

⁹¹² Ibid 64–5. See also page 66 & 69. The first regional representative assembly in Sumatra was the *Majelis Kesejahteraan Minangkabau* in July 1942. Aceh had an advisory body in November 1942. Adat leaders and Islamic teachers had the *Balai Penyelidikan Masyarakat Minangkabau* [Institute for Research in Minangkabau Society] and the *Majelis Islam Tinggi* [Supreme Islamic Conference of Minangkabau]. *Barisan Keamanan Umum* [Public Security Organisation] was established in Palembang and aimed to keep law and order and prevent natives from illegally copying estates and oil-fields. An intelligence service, the Tokkokan, was also established with the main task of infiltrating anti-Japanese resistance movements and spy on the native population.

⁹¹³ Ibid 66.

⁹¹⁴ Ibid 67. The president and members of the *musapat* – public court institution was recruited from independent jurists, lawyers and teachers. It was separate to the civil administration. In Dutch customs, the highest official where the court was situated automatically served as the head of the court. It was under strict governmental control and was intervened by the Dutch colonial administration. Religious courts were established reflecting the respect the Japanese had for Islam.

⁹¹⁵ Ibid 67. *Uleebalang* was an official appointed by the Sultan. It was changed to open up to people from all social stratas: from Islamic teacher group and common people. The title was previously limited to traditional noble families, or the native ruling elite families. The original meaning was war leader. See generally, Atjehcyber team, *Kiprah Uleebalang dalam pemerintahan Aceh* [The role of Uleebalang in Aceh's governmental system] (1 July 2011), [7] <<http://www.atjehcyber.net/2011/07/kiprah-uleebalang-di-aceh.html>>.

4.2.3.1. *The impact of forced tributary system on business integrity*

The legacy of the tribute system of the Japanese is seen in its name *upeti* [tribute] becoming synonymous with bribe.⁹¹⁶ From the original meaning of tribute as showing loyalty and respect it was transformed to mean the common practice of bribery.⁹¹⁷ It has come to weaken the integrity of business practices. It also created a model of military involvement in commercial activities that the armed forces of the newly independent country could use.

The Japanese introduced financial and accounting standards that compelled entrepreneurs to donate large parts of their profits to the Japanese military. In March 1943 the Ministry of the Army standardized finance and accounting systems for each military administration district. Companies were obliged to dedicate part of their profits to the military account. A company's net profit was assumed to be nine per cent of its annual investment and income over that amount was divided into 70 per cent for the military and 30 per cent for the company.⁹¹⁸

⁹¹⁶ The term 'upeti' is defined as a bribe. See, Kamus Besar Bahasa Indonesia [General Dictionary of Indonesian Language], *Upeti* [Tribute] <<http://bahasa.cs.ui.ac.id/kbbi/kbbi.php?keyword=upeti&varbidang=all&vardialek=all&varragam=all&varkelas=all&submit=tabel>>. The word 'upeti' has two meanings : [1] '*uang (emas dsb) yang wajib dibayarkan (dipersembahkan) oleh Negara(-negara) kecil kepada raja atau Negara yang berkuasa atau yang menaklukkan* [money or gold, etc that is obliged to be paid or offered by small state(s) to ruling or conquering state, [2] *uang dsb yang diberikan (diantarkan) kepada seorang pejabat dsb dengan maksud menyuap*' [money, etc given or delivered to an official with the intent to bribe].

⁹¹⁷ See, Wahyudi Kumorotomo, *Budaya upeti, suap, dan birokrasi publik* [Tributes and bribes culture and public bureaucracy] (3 March 2008) 2 <<http://kumoro.staff.ugm.ac.id/wp-content/uploads/2008/03/budaya-upeti-suap-dan-birokrasi-publik.pdf>>. Upeti derives from Sanskrit word 'utpatii'. It defines a proof of loyalty or respect. Historically, it was a kind of offering from small kings to king (conqueror). See also, Heru Wicaksono, *Apakah upeti termasuk perbuatan korupsi?* [Does tribute classify as corruption?] (2001) Buletin Pengawasan [Supervision Bulletin], 31–32 <<http://www.pu.go.id/satminkal/itjen/buletin/3031upeti.htm>>. The *upeti* system was already applied by ancient kingdoms. It was recognised as an administrative apparatus in financing domestic costs as voluntary tribute [*upeti sukarela*] from people to the ruling king as recognition and loyalty. Dutch imperialism continued the *upeti* system with forced tribute [*upeti paksaan*] for commercial purposes.

⁹¹⁸ Yoko Hayashi and Yasuki Hikita, cited in Post, above n 908, 236.

The policy favoured large and well established companies in agriculture and mining. Newcomers were restricted to business sectors vital to Japan's war effort.⁹¹⁹ It contributed to large Japanese companies exploiting natural resources in the archipelago, including Mitsubishi, Sumitomo, Kawasaki Heavy Industries and Toyota Motors in 1944. Over 280 Japanese companies were identified as active in Java. Chinese and local merchants became the intermediary traders. The Japanese intended to take over existing Dutch, Chinese and any other nation's enterprises. In fact, Dutch and Chinese merchants and managers remained in business and employed with Dutch technicians and executives being preferred in Java and Sumatra.⁹²⁰

In 1945 Japan surrendered but military conflict with the Dutch delayed an independent Indonesia from controlling of its own civil administration.⁹²¹

4.3. Commercial activities and honesty and transparency post independence (1945–present)

4.3.1. Introduction

From the proclamation of independence on 17 August 1945, Indonesia has seen three major political and economic periods. The Old Order era (1945–1966) was marked by systems of economic nationalism, liberal economy, and state capitalism; the New Order era (1966–1998) by crony capitalism and the Reformation period (1998–present) by democracy and economy. In each period different values have been valued and influenced commercial activities.

The role of honesty and transparency in commercial activities in each period will be discussed below. Corruption was a common issue in all three periods. This is a significant issue in this study as the quality of public governance including law enforcement and corruption, the incentive and the quality of government officials and regulators, which were observed by Dallas, see Chapter [2.2.4] and the efficiency of judicial procedures and enforcement claimed by Vincenzo indicated in Chapter 2, are the determining factors in shaping corporate governance: particularly disclosure. It also becomes a crucial issue for

⁹¹⁹ Ibid.

⁹²⁰ Ibid 234–5.

⁹²¹ Asiainfo.org, above n 778.

the use of a good corporate governance code as Haines and Zerilli indicated in Chapter 2 that a voluntary code relies upon moral suasion, see Chapter [2.4.3].

4.3.2. The old order (1945–1966)

The period from independence in 1945 until 1966 is old order under the first president, Soekarno.⁹²²

Soekarno, as president demonstrated a strong character. He was known for his bravery, confidence and independence. Forging the development of Indonesia was his priority. *Tri Sakti*, or *tiga keutamaan* [three priorities] were asserted. They were a self-sufficient economy [*berkemandirian dalam ekonomi*], political sovereignty [*berkedaulatan dalam politik*] and national culture [*berkepribadian dalam kebudayaan*].⁹²³

The new nation was poor and underdeveloped. Poverty, the lack of capacity and ineffectiveness of the government and its bureaucracy were the main factors inhibiting economic development.⁹²⁴

The old order itself was divided into three main periods: the Revolution Period (1945–1949), the Parliamentary Period (1950–1959) and the Guided Democracy Period (1959–1966)⁹²⁵ within its economic policy of nationalism, liberalism and state capitalism.

4.3.2.1. The revolution period (1945–1949) – transitioning economy and economic nationalism

The revolutionary period falls between the declaration of independence in 1945 and the Dutch recognition of Indonesia's independence in 1949. The declaration of

⁹²² Badan Pengawas Pasar Modal (BAPEPAM) [Capital Market Supervisory Agency], *Orde Lama* [Old Order] <http://www.bapepam.go.id/old/old/profil/sejarah/orde_lama.htm>.

⁹²³ Agam Bayu Suryanto, *Upaya membentuk pribadi yang berkarakter dan berintegritas melalui implementasi nilai-nilai pendidikan* [Efforts to create a personal character and integrity through educational values] (12 September 2012) Inspektorat Jenderal Kementerian Pendidikan Nasional [Inspectorate-General of the Ministry of National Education], [5] <<http://itjen.kemdiknas.go.id/berita-101-upaya-membentuk-pribadi-yang-berkarakter-dan-berintegritas-melalui-implementasi-nilainilai--pendidik.html>>. See also, Max Lane, below n 961, 8.

⁹²⁴ Howard Dick, 'Brief reflection on Indonesian economic history' in Grayson Lloyd and Shannon Smith (eds), *Indonesia today – Challenges of history* (Institute of Southeast Asian Studies, 2001) 161.

⁹²⁵ Adriaan Bedner, *Administrative Courts in Indonesia – A socio-legal study* (Kluwer Law International, 2001) The London-Leiden series on law, administration and development vol. 6, 16.

independence was followed by armed conflict⁹²⁶ until the Dutch formally recognized Indonesian sovereignty in 1949.⁹²⁷

In this period, the old colonial economic structures still dominated. Therefore, economic policies focused on a transformation to a more autonomous Indonesian national economy.⁹²⁸ Political instability made this impossible. The country was still struggling to defend its independence and the military could not depend on government funding. The military developed business activities to meet its needs⁹²⁹

The revolution changed many of the colonial institutions of the Dutch but not all. For example, factories and equipment belonging to Dutch businesses were destroyed by local residents.⁹³⁰ The continued existence of Dutch laws under the Transitional Provision of the 1945 Constitution was clearly inconsistent with Indonesia's independence. They were used to avoid a legal vacuum in the absence of new national legislation. Until they were revoked, many Dutch institutions of government and administration continued to exist.⁹³¹ The substantive law remained the same, only the political context had changed.⁹³²

⁹²⁶ Lindsey (ed), *Indonesia: Law and Society*, above n 3, 5.

⁹²⁷ The status of West New Guinea (*Irian Jaya* and *Papua*) possessed by the Dutch since 1828 remained unclear until 1969 when it was annexed by Indonesia. See, United Nations, *West New Guinea – UNSF: Background*, [1] <<http://www.un.org/en/peacekeeping/missions/past/unsfbackgr.html>>. It was transferred to Indonesia in 1963.

⁹²⁸ Mardjana, above n 846, 188.

⁹²⁹ Yusa Djuyandi, 'Pengalihan aktivitas bisnis militer di Indonesia', *DetikNews* (online), 5 Oktober 2009 <<http://news.detik.com/read/2009/10/05/084514/1215116/471/pengalihan-aktivitas-bisnis-militer-di-indonesia?nd771104bcj>>. The military was Tentara Nasional Indonesia [the Indonesian Army] or TNI which was established by uniting the Koninklijk Nederlands Indisch Leger, or KNIL, and Pembela Tanah Air, or PETA as well as other movement groups, or units from different regions around Indonesia. It established a military unit in each region delegating a self-financing system.

⁹³⁰ Florence Lamoureux, *Indonesia: A global studies handbook* (ABC CLIO, 2003) 60. For example, a prosperous Dutch sugarcane plantation and refined sugar in a factory located on the plantation ground in East Java. The harvested sugar cane was burnt and the heavy equipment in the sugar refining process was smashed. It was a celebration of the departure of the Dutch. There came a high cost for replacing the equipments and preparing fields for planting to the new Indonesian owners who took over the land and factories.

⁹³¹ Asean Law Association, above n 872, 23; See also, page 24. Government Regulation No. 2 of 1945 stipulated that the amendment or replacement of Dutch laws shall comply with the Constitution, It was seen as complicated and unsatisfactory process. There was 'difficulty in determining which laws remain valid and which laws have been revoked'.

⁹³² Daniel S Lev, *Legal evolution and political authority in Indonesia – Selected essays* (Kluwer Law International, 2000) 29. See also, Lindsey (ed), *Indonesia: Law and Society*, above n 3, 7.

An effort to abandon Dutch laws was made. It sought to use intrinsic Indonesian legal principles to change the principles of the Dutch legislative codes.⁹³³ It attempted to use the Codes as guidelines. However, judicial practice did not reflect this new legal discourse as judges still continued to use the Civil Code in particular.⁹³⁴ The Codes were seen by lawyers as ‘attractively modern but symbolically European which might still work to the advantage for European and ethnic Chinese commerce’.⁹³⁵ *Adat* was regarded as too primitive for the legal system of a modern state.⁹³⁶ It was also seen as ‘essentially Islamic’ and this was considered an ‘impediment in creating laws for an autonomous nation-state’.⁹³⁷

The fundamental legal task during this period was to prepare a Constitution for the independent Indonesian state. An integralist or communitarian vision of the state, advocated by the chairman of the drafting team, Soepomo, dominated its drafting. This was claimed to be the basis of Indonesian culture. It denied any conflict between state and society. It recognized the spirit of work together [*gotong royong*] as the foundation of society and the duties of individuals to better society. This supported a stronger executive rather than parliamentary style of government.⁹³⁸ The 1945 Constitution was initially adopted as the foundation of the new Republic. Subsequently in 1946 the Dutch government proposed a federation of seven states in the Dutch East Indies. Under the Linggadjati Agreement, made between the Dutch government and the provisional government of Indonesia, the federation would, on independence being granted, form part

The inherited Dutch Criminal Code, for example, was almost pristine except a few changes i.e. Queen and Governor-General were amended to President and Vice President. The Civil and Commercial Codes still applied mainly to Europeans, ethnic Chinese, and partial others. Notwithstanding, these Codes were officially considered as ‘guidelines’ rather than enforceable laws. The Codes were officially considered as guidelines through the Circulation Letter [*surat edaran*] of the Supreme Court in the 1960s.

⁹³³ Lev, above n 932, 26–7.

⁹³⁴ Bedner, *Administrative Courts in Indonesia*, above n 925, 23.

⁹³⁵ *Ibid* 27.

⁹³⁶ *Ibid* 28.

⁹³⁷ Burns, above n 834, 49

⁹³⁸ Bedner, *Administrative Courts in Indonesia*, above n 925, 15,18.

of the Netherlands – Indonesia Union modelled on the emerging British Commonwealth.⁹³⁹ The agreement was followed by further military conflict. When the Dutch finally recognised the transfer of the sovereignty of Dutch East Indies in 1949, Indonesia adopted a federal structure, called *Republik Indonesia Serikat* (RIS) [Republic of the United States of Indonesia] based on the Linggadjati Agreement. The Federal Constitution of 1949 was provisional and provided for a parliamentary system.⁹⁴⁰

4.3.2.2. *The parliamentary years (1950–1959) and the liberal economy*

The period after 1949 was initially marked by the negotiation to resolve a series of conflicts around the federal United States of Indonesia, which led to a staggered transition to a unitary republic. In retrospect, the years between 1950 and 1957 were seen as a time of constitutional democracy.⁹⁴¹

Immediately after independence it appeared that there was popular support in Indonesia for a single state rather than a continuation of the federation. The Indonesian Parliament supported this in the Provisional Constitution [*Undang-undang Dasar Sementara - UUDS*] of 1950. It modified the 1949 Constitution but retained its western or liberal values based on the 1948 Universal Declaration of Human Rights, in the face of a push for it to represent more distinctive Islamic principles. It also retained a symbolic provision that “the right to property is a social function. In 1955 a Constituent Assembly [*Konstituante*] was convened. It was a representative body established to prepare a permanent constitution as stipulated in Article 134 of the Provisional Constitution. The assembly reached an impasse on ‘whether Indonesia ought to be an Islamic or a secular

⁹³⁹ Australian Government Publishing Service, *Documents on Australian Foreign Policy, 1937-49, Vol XI Indonesia 1947* (AGPS: Canberra, 1975), xxi, 3 and 458.

⁹⁴⁰ Ibid 16, 18, 22. Soepomo and Yamin were among those associated to the federal constitution. See generally, Komunitas & Perpustakaan Online Indonesia, *16 negara bagian bentukan RIS Republik Indonesia Serikat – Berdasarkan Keputusan Konferensi Meja Bundar – Sejarah Nasional* [The Republic of the United States of Indonesia established 16 states – Based on the decision of the Round Table Conference – National History] [1], <http://organisasi.org/16_negara_bagian_bentukan_ris_republik_indonesia_serikat_kmb_berdasarkan_keputusan_konferensi_meja_bundar_sejarah_nasional>. The Round Table was attended by Indonesian Moh. Hatta and Moh. Roem and Van Maarseven came into the decision to establish The Republic of the United States of Indonesia [*Republik Indonesia Serikat*].

⁹⁴¹ Jennifer Lindsay and Maya H T Liem (eds), *Heirs to world culture – Being Indonesian 1950-1965* (KITLV Press, 2012) 7.

state.’ In 1958 Nasution, the chief of the army general staff recommended a return to the 1945 Constitution. The army organised demonstrations in support of this and it was supported by a number of political parties. The assembly refused to agree by a two thirds majority. Soekarno, by presidential decree, dissolved it and restored the 1945 Constitution.⁹⁴²

The utilization of liberal principles in the economic and political systems, with the provision about the social purposes of property, led to the used market principles in economic activities. This affected *pribumi* entrepreneurs and communities who were unable to compete with Chinese and other foreign entrepreneurs. Lack of experience in international commerce, shortages of business people and trained professionals including economists, affected the profitability of many companies. This was made worse by dishonesty in government. It compounded the graft and bribery practices in the businesses.⁹⁴³ Efforts to stabilise, transition and grow the economy stagnated.

Commercial activities were focused on domestic interests. The inward-looking approach reduced both productivity and trade to low figures. As export and import duties were important in financing the new state, they led to the state controlling foreign trade. State enterprises were the sole authority for granting export approval and import licences.⁹⁴⁴ The involvement of the military in business was also extended. It was now not only for meeting the needs of the military, as indicated earlier, but also became profit oriented. *TNI Angkatan Darat* [the Indonesian Army] took over control of Dutch firms. In 1957 military business activities were institutionalized. This was partly to resource it in the confrontation with the Dutch over the status of West Papua (*Irian Barat*).⁹⁴⁵

In the 1950s any continuation of an association with the Netherlands was rejected in the conflict over West Papua and the nationalisation of Dutch assets in Indonesia.⁹⁴⁶ The non-functioning Netherlands – Indonesia Union created in the Linggadjati Agreement was unilaterally abolished by Indonesia in 1956. Dutch banks were nationalized. *De Javasche*

⁹⁴² Bedner, *Administrative Courts in Indonesia*, above n 925, 16, 18, 22.

⁹⁴³ Lamoureux, above n 930, 61.

⁹⁴⁴ van Zanden and Marks, above n 770, 21–3.

⁹⁴⁵ Djuyandi, above n 929.

⁹⁴⁶ Bedner, *Administrative Courts in Indonesia*, above n 925, 23.

Bank NV became the Central Bank, Bank Indonesia in Law No. 24/1951.⁹⁴⁷ Other Dutch banks were later nationalized under Law No 86/1958. Other foreign banks such as the Overseas Chinese Banking Corporation, the Bank of China and the Hong Kong and Shanghai Banking Corporation were closed.⁹⁴⁸ In 1957, more than 245 Dutch businesses were taken over by the Indonesian government. Only the prosperous oil industry remained partially controlled by foreign owners.⁹⁴⁹

Many new business enterprises were set up. Sutter claimed that each year in the early 1950s some 500 new firms were established. Forty per cent of these were established by *pribumi* [indigenous] businesspeople. A comprehensive business directory in 1953 showed about 4200 registered business enterprises.⁹⁵⁰

This partly reflected programs introduced to strengthen the *pribumi* presence in business. 'Benteng' [fortress] was one such programme. The government provided special facilities including licences and credit to *pribumi* entrepreneurs.⁹⁵¹ More than 700 enterprises were registered under this programme. However, they were still unable to compete effectively with foreign enterprises within the free market system.⁹⁵² Another programme forged cooperation or partnership between *pribumi* and Chinese entrepreneurs. The Chinese or non-*pribumi* entrepreneurs were obliged to train the *pribumi* partners and in return the government provided loans and licenses. They were used by Chinese

⁹⁴⁷ Fakultas Hukum Universitas Sam Ratulangi, UU 24/1951, *Nasionalisasi De Javasche Bank N.V* [Law No. 24 of 1951, Nationalization of De Javasche Bank NV] <http://hukum.unsrat.ac.id/uu/uu_24_1951.htm>.

⁹⁴⁸ Unit Khusus Museum Bank Indonesia, *Sejarah Bank Indonesia: Perbankan Periode 1953–1959* [History of Central Bank: Banking in periods of 1953–1959], 1-2 <<http://www.bi.go.id/NR/rdonlyres/A6011CBA-1B4E-49B1-9DDC-CB01AB6C60D0/19383/SejarahPerbankanPeriode19531959.pdf>>.

⁹⁴⁹ Lamoureux, above n 930, 61.

⁹⁵⁰ Ibid.

⁹⁵¹ Richard W Baker et al (eds), *Indonesia – The challenge of change* (KITLV Press, 1999) 28.

⁹⁵² Syafaat Muhari, *Sejarah perekonomian Indonesia sejak orde lama hingga reformasi* [History of Indonesia's economy from the old order to reformation] (13 Agustus 2011), [4] <<http://syafaatmuhari.wordpress.com/2011/08/13/sejarah-perekonomian-indonesia-sejak-orde-lama-hingga-reformasi/>>.

entrepreneurs to access these government services and failed to enhance *pribumi* business skills and experiences.⁹⁵³

4.3.2.3. The guided democracy era (1959–1966) – state capitalism and the beginning of the involvement of bureaucrats in business

The period of presidential rule known as Guided Democracy between 1959 and 1965 became a period of radical legal culture change. Law was to be ‘Indonesianised’.⁹⁵⁴ It was to become secondary to policy under the revolutionary political style embraced by the charismatic president, Soekarno.⁹⁵⁵ In 1960 this was symbolised in the changing of the icon of justice from ‘the blindfolded lady holding the scales of justices’ to the ‘paternalistic Banyan tree’.⁹⁵⁶ The political style became more dictatorial. It was also paternalistic with Soekarno styling himself as the father of the nation.⁹⁵⁷

In this era, public enterprises were used to implement government policies.⁹⁵⁸ They become ‘an extra arm of the government ... fitted into the government’s policy

⁹⁵³ Adypato, ‘Kebijakan ekonomi pada masa orde lama, orde baru dan reformasi’ on *Ekonomi Mikro* (September 22, 2010) [5] <<http://ekonomikro.blogspot.com.au/2010/09/kebijakan-ekonomi-pada-masa-orde-lama.html>>; See also, Muhammad Ruslailang, *Program Ali Baba: Ekonomi kerakyatan a la orde lama* [Ali Baba program: Democratic Economy in the old order version] [4] <<http://www.komunitashistoria.org/2009/06/program-ali-baba-ekonomi-kerakyatan-la.html>>. This program was called ‘Ali Baba’ program. Ali represented idiom of *pribumi* entrepreneurs and Baba were Chinese entrepreneurs.

⁹⁵⁴ Indonesianised laws mean that Indonesian owned-laws (the laws were drafted or made by Indonesians). This considered the Dutch laws had been used since the absence of products of Indonesian laws.

⁹⁵⁵ Lindsey (ed), *Indonesia: Law and Society*, above n 3, 7.

⁹⁵⁶ Bedner, *Administrative Courts in Indonesia*, above n 925, 23. Banyan tree in Indonesian language is known as ‘pohon beringin’. See also, I Kadek Merta Wijaya, *Konsep ruang di sekitar pohon beringin yang tumbuh pada area public di wilayah Denpasar-Bali* [The concept of the space around the Banyan tree, which grew in the public area in the region of Denpasar-Bali], abstract <http://etd.ugm.ac.id/index.php?mod=penelitian_detail&sub=PenelitianDetail&act=view&typ=html&buku_id=43555&obyek_id=4>. The Banyan tree is thought as an identical tree with Kalpavrsa, one of the five holy trees growing in the abode of the Indra God in the Indian myth. It is believed having lots of sacred and ritual values within the culture of Indonesian society, especially in the majority Hinduism followers in Bali. They believe that it has supernatural power called Tenget. It is also used for social and economic activities as their large canopy creates space for the surrounding activities.

⁹⁵⁷ Maribeth Erb, Carol Faucher and Priyambudi Sulistiyanto (eds), *Regionalism in Post-Suharto Indonesia* (RoutledgeCurzon, 2005) 4.

⁹⁵⁸ Mardjana, above n 846, 188, 190.

framework'.⁹⁵⁹ They were seen as the best apparatus for implementing the guided democracy economic policy of a centralized economic system.⁹⁶⁰ The policy aimed to transform the economy from a colonial to a national system. Direct state intervention and regulation of the business sector were the main instruments.⁹⁶¹ However, excessive government control led to the inefficiency of enterprises.⁹⁶²

This state intervention was legitimated by the 1945 Constitution. Article 33 (2) of the Constitution stipulates that '[p]roduction sectors that are vital to the state and that affect the livelihood of a considerable part of the population are to be controlled by the state'.⁹⁶³ [*Cabang-cabang produksi yang penting bagi negara dan yang menguasai hajat hidup orang banyak dikuasai oleh negara*].⁹⁶⁴ The state's involvement was also a continuation of the model established under the Dutch as indicated earlier.⁹⁶⁵

The state came to control most large enterprises. More than 600 Dutch enterprises were nationalized by 1961. Almost half were plantations, more than a hundred were industrial and mining businesses, and the rest were trading, banking and insurance, communication, gas, electricity and construction enterprises. The government also nationalised British and American companies in 1964.⁹⁶⁶ Companies became a 'cash cow' [*sapi perah*] for the government including officials and politicians and their associates.⁹⁶⁷

⁹⁵⁹ Ibid.

⁹⁶⁰ Ibid.

⁹⁶¹ Max Lane, *Unfinished nation – Indonesia before and after Suharto* (Verso, 2008) 37. See generally, Dapice, below n 965, 51. The state involvement and control in economy was the model which established under the Dutch.

⁹⁶² Mardjana, above n 846.

⁹⁶³ The Constitution of the Republic of Indonesia 1945, above n 884. See also, Mardjana, above n 846, 188. The Article 33(2) of the Constitution has been translated that 'economic activities essential to the nation and to the life of the people shall be controlled by the state'. There is a debate concerning the term 'controlled by the state' [*dikuasai oleh negara*]. On one hand, *dikuasai* means to be controlled. It suggests that economic sectors should be directed, supervised, controlled and evaluated by the government and that the state does not necessarily need to own them. On the other hand, *dikuasai* may also means to be owned by the state. The government may directly run the economic sectors through public ownership.

⁹⁶⁴ Mardjana, above n 846.

⁹⁶⁵ David O Dapice, 'An overview of the Indonesian economy' in Gustav F Papanek (ed), *The Indonesian economy* (Praeger, 1980) 51.

⁹⁶⁶ Mardjana, above n 846, 191–2.

⁹⁶⁷ See, eg, Virna Puspa Setyorini, 'Upeti, korupsi dan kebebalaan anak bangsa' [Tribute,

A consequence of the nationalization of the Dutch and other foreign companies was foreign managers and workers were replaced by Indonesians. They tended to be military officers, civil servants or previous lower level employees in the enterprise.⁹⁶⁸ The introduction of military and civil officers created integrity issues that tied them more closely to other members of the national elites.⁹⁶⁹ It affected the integrity of *pribumi* and *Tionghoa* [Chinese] ethnic entrepreneurs in their commercial activities with them.⁹⁷⁰ Bureaucrats were seen as hampered by their political ties.⁹⁷¹ They lacked management and entrepreneurial backgrounds and experiences. It was claimed that the period was ‘the beginning of the creation of a new generation of bureaucrats and military officers to manage public enterprises’.⁹⁷²

There are examples of these consequences. Prolonged dishonest practices in the state-owned National Oil Company (Pertamina) led the company into heavy debt. This case was seen as a demonstration of the impact of the nationalization of Dutch enterprises, which had led public officials, especially the military, to run the businesses.⁹⁷³

Eventually, the guided democracy economic policy failed to achieve national economic independence. The extensive patronage, low productivity and mismanagement of public enterprises contributed to national economic losses. These contributed to the chaotic domestic political situation that culminated in a communist and military coup attempt in

corruption and the foolishness of youth], *Antara News* (online), 21 December 2012, [7] <<http://www.antaranews.com/berita/349560/upeti-korupsi-dan-kebebalan-anak-bangsa>>. Some Parliament members demanded ‘upeti; (from five per cent to 10 per cent of hundreds of billion projects) from BUMN’s [state-owned enterprises] directors.

⁹⁶⁸ Mardjana, above n 846, 191–2.

⁹⁶⁹ Lamoureux, above n 930, 61; See also, Riant Nugroho Dwidjowijoto, ‘Analisa privatisasi BUMN di Indonesia’ (2003) 6(3) *Jurnal Ilmu Sosial dan Ilmu Politik* 285, 292.

⁹⁷⁰ Muhammad Findi Alexandi, *Negara dan pengusaha – Tinjauan literature – Bab II: Negara dan kapitalisme dalam kebijakan industrialisasi di Indonesia* [State and entrepreneur – Literature review – Chapter II: State and capitalism in industrialized policy in Indonesia], 1 <<http://aontar.ui.ac.id/file?file=digital/116775...pdf>>.

⁹⁷¹ Lamoureux, above n 930, 61; Dwidjowijoto, above n 969.

⁹⁷² Mardjana, above n 846, 191–2. All public enterprises became *Perusahaan Negara* (state enterprises).

⁹⁷³ Lamoureux, above n 930, 61. Ibnu Sutowo was appointed in 1957 as the head of Pertamina regarded as corrupt in his dealings with the government. The government granted \$10 billion bail out to cover the company deficit in 1975. See also, Hosen, below n 980, 292.

September and October 1965. This led to the downfall of Soekarno in 1966.⁹⁷⁴ He was replaced by Soeharto.

4.3.3. The new order (1966–1998)

4.3.3.1. Introduction

The new order began when Soeharto, who was then a major general and commander of the Army Strategic Reserves Command, deposed Soekarno.⁹⁷⁵ A hallmark of the period is the concentration of power in the Soeharto's hands.⁹⁷⁶ His authoritarian leadership was backed by the military and technocrats. It was also supported by the middle class and elements of the Islamic community.⁹⁷⁷ Paternalism and patronage continued as Soeharto distributed power, position and wealth among his family and loyal friends.

Under the Soeharto government, the efforts to 'Indonesianize' law ended dramatically. Initially Soeharto emphasised the rule of law [*negara hukum*] and the Dutch-derived legal and political model of guided democracy continued. The executive, however, dominated the political system and both the legislature and the courts were under its control.⁹⁷⁸ Law enforcement and the courts became increasingly less effective.⁹⁷⁹ The rule of law 'was subordinated to the goals of economic development'.⁹⁸⁰

Two ideological factors affecting economic policy since 1949 also continued. Firstly, there was the legitimate economic role given to the state by Article 33 of the

⁹⁷⁴ Mardjana, above n 846, 192.

⁹⁷⁵ See generally, Donald K Emmerson (ed), *Indonesia beyond Suharto – Polity economy society transition* (East Gate Book in cooperation with the Asia Society, 1999) xix. Some authors used the name of Suharto rather than Soeharto. The letter 'u' replaced 'oe' under the 1972 reform. Names of people are still 'spelled herein the way their owners sign or signed them or as printed in historical accounts or contemporary local media'. The title of Indonesian president from 1966 to 1998 still signs his name "Soeharto". In fact, Western journalistic practice used Suharto instead.

⁹⁷⁶ Richard Borsuk, 'Markets: The limits of reform' in Donald K Emmerson (ed), *Indonesia beyond Suharto – Polity economy society transition* (East Gate Book in cooperation with the Asia Society, 1999) 136, 165. The power concentration to Soeharto 'permitted quick remedial action on economy'. Legislators, lobbyists, and judges could not stop Soeharto 'from stripping corrupt and dilatory customs officials of their authority to inspect shipments.'

⁹⁷⁷ Erb, Faucher and Sulistiyanto (eds), above n 957, 4.

⁹⁷⁸ Lindsey (ed), *Indonesia: Law and Society*, above n 3, 8.

⁹⁷⁹ Ross H McLeod, 'Soehartos Indonesia: A Better Class of Corruption' (2000) 7(2) *Agenda* 99, 102 <<http://press.anu.edu.au/wp-content/uploads/2011/06/7-2-A-1.pdf>>.

⁹⁸⁰ Nadirsyah Hosen, *Reform of Indonesian law in the post-Soeharto era (1998-1999)* (PhD Thesis, University of Wollongong, 2004) 445 <<http://ro.uow.edu.au/cgi/viewcontent.cgi?filename=0&article=1245....>>.

Constitution that market forces must be tempered by social objectives. Secondly, foreign ownership and control of the Indonesian economy was to be restrained. Domestic investment became a priority and the development of the national autonomy remained the basic objective.⁹⁸¹

Later, Soeharto replaced elements of Soekarno's guided economy.⁹⁸² The government encouraged private domestic and foreign investment as well as the development of co-operatives. The Foreign Capital Investment Act No 1 of 1967 and the Domestic Capital Investment Act No 6 of 1968 sought to facilitate private sector activities. Act No 12 of 1967 sought to regulate the management of co-operatives. The ministerial department dealing with co-operatives and their development was also established. Presidential Instruction No 17 of 1967 and Act No 9 of 1969 categorised public enterprises into three groups, ie: the *Persero* (an enterprise similar to a private company); the *Perum* (enterprise concerned with public service and profit); and, the *Perjan* (enterprise attached to a ministerial department concerned with public service).⁹⁸³

Under Soeharto, Indonesia experienced economic growth. However, it was fragile. The absence of transparency, accountability, democratic institutions and a free press as well as the suppression of demonstrations and protests by citizens, were part of Soeharto's authoritarian style.⁹⁸⁴ It reinforced the values of corruption, collusion, and nepotism – popularly known as KKN - which promoted crony capitalism. KKN is discussed further below at [4.3.3.4].

4.3.3.2. *The phenomenal success in fragile economy*

Prior to the Asian currency crisis of 1997, under Soeharto Indonesia had become a 'macan Asia' [Asian tiger]. Indonesia was described, in economic terms, as a 'phenomenal

⁹⁸¹ Richard Robinson, *Power and economy in Suharto's Indonesia* (Journal of Contemporary Asia Publishers, 1990) 102.

⁹⁸² Mardjana, above n 846, 189.

⁹⁸³ Ibid 190.

⁹⁸⁴ UCL Constitution Unit, *Indonesia – International focus*, University College London (1 May 2012) <<http://www.ucl.ac.uk/constitution-unit/research/foi/countries/indonesia>>; Nadirsyah Hosen, above n 980, 445. Hosen's study demonstrated the absence of accountability and transparency during the Soeharto regime.

success without the use of rule of law' having utilised political centralisation instead.⁹⁸⁵ Like a number of other Asian countries, Indonesia seemed to be a successful state. However, that success had been 'measured by many social indicators, without relying on rule of law and rule-based behaviour as principal means of social ordering, direction, and control'.⁹⁸⁶

The success commenced after 1967, when foreign investment was again permitted.⁹⁸⁷ The expansion of private economic enterprises and the emergence of a private sector was also a major factor in Indonesia's economic growth.⁹⁸⁸ Private enterprises enjoyed a conducive business environment with easy access to finance as well as the improvement of physical infrastructure.⁹⁸⁹

The stock market also contributed to economic growth. It was supervised by the Capital Market Supervisory Agency (BAPEPAM). Initially, there were just 24 listed companies with banks as the most preferred investment.⁹⁹⁰ The Jakarta Stock Exchange (JSX) activities grew when banking and capital market deregulation was introduced in 1988–1990 including provisions for foreigners to invest.⁹⁹¹ The JSX itself was demutualised in July 1992. BAPEPAM become the Capital Market and Financial Institution Supervisory Agency [*Badan Pengawas Pasar Modal dan Lembaga Keuangan* (BAPEPAM-LK)]. The JSX later changed its name to *Bursa Efek Indonesia* (BEI) [Indonesia Stock Exchange (IDX)] by merging with the Surabaya Stock Exchange.⁹⁹² However, financial markets were still limited by excessive state interference.⁹⁹³ The

⁹⁸⁵ Gary Goodpaster, 'The rule of law, Economic development & Indonesia' in Timothy Lindsey (ed), *Indonesia – Law and society* (Federation Press, 1999) 21, 22.

⁹⁸⁶ Ibid.

⁹⁸⁷ Baker et al (eds), above n 951, 14.

⁹⁸⁸ Ibid 13.

⁹⁸⁹ Pierre van der Eng, 'Business in Indonesia: Old problems and new challenges' in M Chatib Basri and Pierre van der Eng (eds), *Business in Indonesia – New challenges, Old problems* (Institute of Southeast Asian Studies, 2004). See generally, page 4. In the colonial era, the business atmosphere was not conducive due to underdeveloped physical and financial infrastructure. However, 'the business regulations were transparent'.

⁹⁹⁰ Bursa Efek Indonesia [Indonesia Stock Exchange], *Sejarah*, above n 873, [3].

⁹⁹¹ Ibid.

⁹⁹² Ibid. The JSX has changed to become the BEI in the reformation era in 2007.

⁹⁹³ Lubis and Santosa, above n 556, 343, 354.

economic growth had mainly benefited a small minority including Soeharto's family and their cronies.⁹⁹⁴

The economic success ended with the Asian currency crisis of 1997. Indonesia's fragile economic foundation meant that it suffered most compared to other South East countries.

The crisis has been attributed to a number of factors. Corruption, collusion, nepotism and poor governance in institutions were claimed to be the major causes.⁹⁹⁵ In particular, public corruption had led to distortions in the economy.⁹⁹⁶ The lack of transparency in the banking and financial systems and boom-fuelled private corporate debt were also significant.⁹⁹⁷

4.3.3.3. Crony capitalism and its impacts

Capitalism and industrialisation had developed significantly from the early Soeharto period. It was crony capitalism associated with a state driven industrialisation.⁹⁹⁸ The government's economic and political policies had benefitted particular capitalists. They were dominated by domestic investors including ethnic *Tionghoa* [Chinese] and foreign investors mainly from the United States and Western Europe.⁹⁹⁹ Manufacturing became more developed than the agrarian sector, which was the dominant sector for many Indonesians. It was believed that manufacturing business activities were more important for national growth as they had more "value add". Economic growth was dependent on government guidance of larger local capitalists, government officials and foreign investors;

⁹⁹⁴ Lane, Max, above n 961, 133.

⁹⁹⁵ Muhammad Chatib Basri, 'Indonesia: the political economy of policy reform' in Arief Budiman, Barbara Hatley and Damien Kingsbury (eds), *Reformasi – Crisis and change in Indonesia* (Monash Asia Institute, 1999) 27, 28.

⁹⁹⁶ Joanna MacMillan, 'Reformasi and public corruption: Why Indonesia's Anti-Corruption Agency strategy should be reformed to effectively combat public corruption' (2011) 25(1) *Emory International Law Review* 587, 587.

⁹⁹⁷ Baker et al (eds), above n 951,4.

⁹⁹⁸ George A Barnett (ed), *Encyclopedia of Social Network* (Sage Publication, 2011) vol 1, 408. See also, Adrian Vickers, 'The new order: Keeping up appearances' in Grayson Lloyd and Shannon Smith (eds), *Indonesia today – Challenges of history* (Institute of Southeast Asian Studies, 2001) 72, 78. Indonesia was officially a capitalist state and then was counted as being part of the free world.

⁹⁹⁹ Alexandi, above n 970, 1–2.

supported by a limited system of market mechanisms. Small and median businesses were less well supported by the government and more dependent on markets for investment.¹⁰⁰⁰

The values underlying these commercial activities were marked by strong characteristics of crony capitalism. These led to highly concentrated ownership and conglomerate structure. They also further corrupted integrity. Soeharto's family and their associates controlled most large businesses. Claessens et al found that 'Indonesia exhibited the highest level of corporate concentration in East Asia in 1996, with 10 families owning 57.7 per cent of listed corporate assets'.¹⁰⁰¹ Fitzpatrick also identified the highly concentrated ownership and conglomerate patterns in large corporations. Most conglomerates owned banks – after the financial sector deregulation – that they utilized for loans for their own interests. Prudential lending requirements and rules governing related party lending were largely ignored as the banks became subordinate to related borrowers.¹⁰⁰²

Through Soeharto's patronage of these family-owned business groups,¹⁰⁰³ he maintained control over wealthier business people. One of Soeharto's concerns was that *pribumi* who grew powerful through business may become his political enemies and threaten his power. He ensured that 'the bulk of corporate enterprises were controlled by ethnic-Chinese tycoons, whose ethnicity prevented them from pursuing political office'.¹⁰⁰⁴ The resulting antagonism against non-Muslim ethnic Chinese is believed to have led to Soeharto promoting his children as a group of *pribumi* whom he fully trusted.¹⁰⁰⁵

¹⁰⁰⁰ Ibid 3. See generally, Thee Kian Wie, 'Reflection on the new order miracle' in Grayson Lloyd and Shannon Smith (eds), *Indonesia today – Challenges of history* (Institute of Southeast Asian Studies, 2001) 163, 165. The New Order changed economic structure from agriculture production to manufacturing and modern services.

¹⁰⁰¹ Hal Hill and Dionisisu Narjoko, *Managing industrialisation in a globalising economy – Lessons from the Soeharto era*, [5], [13] <<http://epress.anu.edu.au/apps/bookworm/view/Soeharto%E2%80%99s+New+Order+and+its+Legacy%3A+Essays+in+honour+of+Harold+Crouch/5331/ch04.xhtml>>.

¹⁰⁰² Daniel Fitzpatrick, 'Tinkering around the edges: Inadequacy of corporate governance reform in post-crisis Indonesia' in M Chatib Basri and Pierre van der Eng (eds), *Business in Indonesia – New challenges, Old problems* (Institute of Southeast Asian Studies, 2004) 178, 179.

¹⁰⁰³ van der Eng, above n 989, 1, 5.

¹⁰⁰⁴ Kevin O'Rourke, *Reformasi – The struggle for power in post-Soeharto Indonesia* (Allen & Unwin, 2002) 55.

¹⁰⁰⁵ Ibid.

4.3.3.4. *Practices around corruption, collusion and nepotism*

Corruption, collusion and nepotism [KKN] became even more extensive in this period. Its endemic nature justified the country's reputation as a 'high-cost economy'.¹⁰⁰⁶ Three generations of the Soeharto family and their cronies were mainly involved in it.¹⁰⁰⁷ Family and friends controlled major companies and resources. KKN was an undeniable fact.¹⁰⁰⁸

It became a fundamental problem in the business and legal sectors. In the legal system the courts were corrupt and politically submissive. The prosecution and the police abused rights, legislation was out of date, and enforcement was often marginal and ineffective. The most crucial issue was the failure of the rule of law or law-state [*negara hukum* or *rechstaat*].¹⁰⁰⁹ Some writers describe the Soeharto era as based on the ruler's law

¹⁰⁰⁶ Borsuk, above n 976, 136, 143.

¹⁰⁰⁷ Sudarmo Sumarto, Asep Suryahadi and Alex Arifianto, *Tata kelola pemerintahan dan penanggulangan kemiskinan: Bukti-bukti awal desentralisasi di Indonesia* [Public governance and poverty reduction: Initial evidence of decentralisation in Indonesia], 1 <<http://www.smeru.or.id/report/workpaper/goverpovreduct/governancepovreductina.pdf>>. See also, Lamoureux, above n 930, 47. Soeharto's three daughters established a business partnership in 1983 and controlled a profitable Jakarta toll road concession. Ibnu Sutowo, Soeharto's supporter, became the head of Pertamina, the Indonesian oil monopoly. Probosutejo, a half brother of Soeharto, and Lim Siew Liong, a close friend, were allowed to the corner clove import market. Later, Tommy Soeharto totally controlled the clove import market. This created hardship for many local farmers. Soeharto built close friendships with prominent Chinese businessmen and provided opportunities for them. See also, Borsuk, above n 976, 136, 148–9. PT Timor Putra Nasional, a company owned by Soeharto's youngest son, Hutomo (Tommy) Mandala Putra worked on the project with Kia Motors of South Korea and assembled Kia's components in Indonesia to produce an automobile known as 'mobil Timor' and was free of the stiff tariffs and luxury tax. Soeharto's grandson, Ari Sigit Haryo Wibowo, was given a lucrative licence to stick labels on all imported Chinese medicines. See also, Habir, above n 757, 168, 187. Each of Soeharto's children had their own business group: Bimantara (oldest son, Bambang Trihatmojo), Citra Lamtoro Agung (oldest daughter, Siti Hardiyanti - Tutut), Humpus (youngest son, Hutomo – Tommy – Mandala Putra), Arseto (son, Sigit Harjojudanto) and Datam/Maharani (youngest daughter, Siti Hediati Harijadi – Titiek).

¹⁰⁰⁸ Mark McGillvray and Oliver Morrissey, 'Economic and financial meltdown in Indonesia: prospects for sustained and equitable economic and social recovery' in Arief Budiman, Barbara Hatley and Damien Kingsbury (eds), *Reformasi – Crisis and change in Indonesia* (Monash Asia Institute, 1999) 3, 16. See also, Habir, above n 845, 136, 168. Salim Group owned by Liem Sioe Liong (Sudono Salim) built his business empire utilized official monopolies and concessions due to his ties to Soeharto.

¹⁰⁰⁹ Lev, above n 932, 3; See, eg, Timothy Lindsey, 'Indonesia's negara hukum: walking the tightrope to the rule of law' in Arief Budiman, Barbara Hatley and Damien Kingsbury (eds), *Reformasi – Crisis and change in Indonesia* (Monash Asia Institute, 1999) 363, 378. Indonesian

because of the supremacy of the ruler rather than the supremacy of the law.¹⁰¹⁰ Budiman highlighted that ‘law was manipulated to serve politics and the expression of law, of rules, was more often heard than the rule of law’.¹⁰¹¹

In the economy, large business groups were developed. They were also based on political networks.¹⁰¹² Capitalists in the network were privileged and grew large profits thanks to protection from tariffs and by the granting of monopoly rights and the granting of other privileges, including government subsidies, reductions on taxes and duties reduction as well as cheap energy, electricity and water.¹⁰¹³ Monopoly licences and preferential credit were used as economic favours.¹⁰¹⁴ Monopolies raised costs, which reduced the country’s international competitiveness.¹⁰¹⁵ Special licences and facilities, for example, in oil and gas, automotive, cement, cloves, transportation and infrastructure were given to some entrepreneurs.¹⁰¹⁶ Local business people not linked to the networks of patronage and special privileges were increasingly dissatisfied.¹⁰¹⁷

A large part of the economy came to be based on patrimonial patronage and discretion rather than a rule based approach.¹⁰¹⁸ The president’s associates and family ‘controlled power and wealth through patronage links across the archipelago and created

courts were described as ‘corrupt, politically subordinate and incompetent...’ and a judicial mafia. See also, O’Rourke, above n 1004, 150. It was claimed that the absence of law enforcement was the fundamental problem obstructing economic recovery. The legal system actors were recruited and promoted based on loyalty rather than professionalism, principles or ideals of public service.

¹⁰¹⁰ O’Rourke, above n 1004, 150.

¹⁰¹¹ Arief Budiman, ‘Foreword’ in Timothy Lindsey (ed), *Indonesia – Law and society* (Federation Press, 1999) v.

¹⁰¹² Alexandi, above n 970, 3.

¹⁰¹³ Ibid 12.

¹⁰¹⁴ R William Liddle, ‘Regime: The new order’ in Donald K Emmerson (ed), *Indonesia beyond Suharto – Polity economy society transition* (East Gate Book in cooperation with the Asia Society, 1999) 39, 52.

¹⁰¹⁵ Baker et al (eds), above n 951, 5. See also, Lubis and Santosa, above n 556, 343, 354. Corruption, collusion and nepotism weakened the economic system. The imperium of conglomerates and cronyism was established.

¹⁰¹⁶ Lubis and Santosa, above n 556, 343, 354.

¹⁰¹⁷ Taylor, above n 802, 284.

¹⁰¹⁸ Peter McCawley, ‘The Indonesian economy in transition: the international context’ (United Nations support facility for Indonesian recovery conference: Lessons from the Indonesian transition – Setting a future reform agenda, Jakarta, 24–25 February 2004) 5 <<http://www.adbi.org/files/2004.02.25.spc002.mccawley.jakarta.pdf>>.

policies that worked in their favour'.¹⁰¹⁹ Business was dominated by these patrimonial or clientele-centric relations between individual business people and senior government figures. Chinese Indonesians and the president's family members became proxy political patrons for other investors.¹⁰²⁰ Foreign investors, and the World Bank, discovered that the price of buying into and sustaining a patronage relationship was too high.¹⁰²¹ The integrity of large business groups was compromised by this regime of patronage.¹⁰²² These patrimonial relationships also reflected the Dutch legacy, as indicated earlier in this chapter. The involvement of most large corporations in patrimonial relationships with corrupt political and bureaucratic elites further entrenched crony capitalism.¹⁰²³

The basic value in Art 33 of the Constitution of *asas kekeluargaan* [familial principle] became *asas prioritas keluarga and kroni* [family and cronies oriented principle]. It made significant efforts to reform or strengthen political, social and governance institutions very difficult.¹⁰²⁴

Soeharto ruled for 32 years. The regime was ended by people power that had long been suppressed. This was part of the reaction to the severe economic crisis of 1997, as indicated earlier.¹⁰²⁵ The obstruction to the implementation of the International Monetary Fund's measures to repair the economic and financial systems and the appointment of his

¹⁰¹⁹ Erb, Faucher and Sulistiyanto (eds), above n 957, 2.

¹⁰²⁰ Taylor, above n 802, 279, 284. See also, Wanandi, below n 1038, 132. Under the Soeharto regime, Indonesian Chinese concentrated in business sectors since it was difficult for them to become civil servants and to enter many other professions. This was based on Soeharto's view that their best performance was in economic field, and therefore they should focus in business field. See, eg, Lindsey, 'Indonesia's negara hukum: walking the tightrope to the rule of law', above n 1009, 369 & 371. The fundamentally patrimonial nature established elites, which resisted the reform. The elites enjoyed the political and business monopolies.

¹⁰²¹ Taylor, above n 802, 284.

¹⁰²² Alexandi, above n 970, 3.

¹⁰²³ Fitzpatrick, above n 1002, 178, 179. This was the third characteristic of corporate governance identified in the New Order era. The first and the second characteristics were identified as a highly concentrated ownership pattern and the establishment of conglomerates structure.

¹⁰²⁴ McCawley, above n 1018.

¹⁰²⁵ Crayonpedia.org, *Berakhirnya masa orde baru dan lahirnya reformasi – Runtuhnya orde baru* [The end of the new order and the start of the reform – The fall of the new order] [7] <http://www.crayonpedia.org/mw/BSE:Berakhirnya_Masa_Orde_Baru_dan_Lahirnya_Reformasi_9.2_%28BAB_13%29>.

family members and friends to cabinet contributed to Soeharto's downfall.¹⁰²⁶ This led into the new, and present era, known as the *era reformasi* [reformation era].

4.3.4. The reformation era and its commercial activities and values (1998–present)

4.3.4.1. Introduction

The fall of Soeharto was driven by the protests of people and their demand for *reformasi* (reform). *Reformasi* in political terms demanded, 'firstly, greater democracy, secondly, honesty and accountability in public life and, lastly policies that secure people's welfare'.¹⁰²⁷ As a movement it was significantly opposed to the prevailing KKN [corruption, collusion and nepotism],¹⁰²⁸ which is identified as one of vulnerable factors in Indonesia.¹⁰²⁹

After 1998 Indonesia became a more democratic country. Internal and external factors contributed to this.¹⁰³⁰ The internal factors included 'public awareness of democracy, the more professional organisation of socio-political groups and the worsening image of the dual function of the military'. The external factor was 'the growing global capitalism that rejected authoritarian political systems'.¹⁰³¹ *Keterbukaan* [openness] further developed as a significant part of the revolution.¹⁰³²

In this era five presidents governed and each has reflected different approaches to commercial activities and their underlying values: B J Habibie, Abdurahman Wahid,

¹⁰²⁶ Marcus Mietzner, 'From Soeharto to Habibie: the Indonesian Armed Forces and political Islam during the transition' in Geoff Forrester (ed), *Post-Soeharto Indonesia – Renewal or Chaos?* (Crawford House Publishing Bathurst, 1999) 65, 84. See generally, Wie, above n 1000, 163, 164. The IMF's financial aid to counteract the currency crisis failed to restore market confidence due to political uncertainty and Soeharto's reluctance for implementing economic reform.

¹⁰²⁷ Ken Young, 'Post-Suharto: a change of regime?' in Arief Budiman, Barbara Hatley and Damien Kingsbury (eds), *Reformasi – Crisis and change in Indonesia* (Monash Asia Institute, 1999) 73.

¹⁰²⁸ Ibid 74.

¹⁰²⁹ Gary Goodpaster, 'Combating Corruption in Indonesia: Enhancing Accountability for Development' (Report No. 27246-IND, World Bank, 12 November 2003) ii.

¹⁰³⁰ Arief Budiman, 'The 1998 crisis: change and continuity in Indonesia' in Arief Budiman, Barbara Hatley and Damien Kingsbury (eds), *Reformasi – Crisis and change in Indonesia* (Monash Asia Institute, 1999) 41, 56–7.

¹⁰³¹ Ibid.

¹⁰³² Gerry van Klinken, 'How a democratic deal might be struck' in Arief Budiman, Barbara Hatley and Damien Kingsbury (eds), *Reformasi – Crisis and change in Indonesia* (Monash Asia Institute, 1999) 59, 61.

Megawati Soekarno Putri, Susilo Bambang Yudoyono and Joko Widodo. Corruption, which impacts on transparency and accountability, has been the recurring and significant issue for each government.

4.3.4.2. Habibie era (21 May 1998–20 October 1999)

B J Habibie, the vice president, replaced Soeharto in May 1998. Many people claim that his presidency was a transitional period in government rather than a part of the *reformasi* era. From the business community's perspective it was seen as a continuation of the Soeharto regime.¹⁰³³ KKN persisted. There was a change in the government's political agenda, leadership style and greater media freedom.¹⁰³⁴ There was a focus on stabilizing political and economic systems, promoting economic small enterprises and cooperatives and for the purpose of this thesis, the acknowledgement of the importance of corporate governance.

(a) The focus on economic stability and its effects

Most policies were focused on establishing economic stability. The government was required to implement economic reform as an IMF requirement. A number of new laws and institutions were introduced, as also indicated in chapter one.¹⁰³⁵ The Anti-Monopoly and Unfair Competition Law and Consumer Protection Law were amongst these. The Laws No. 22/1999 and No 25/1999, decentralizing government were also introduced. They required 'the transfer of governance from Jakarta to the regions'.¹⁰³⁶ This is known as *otonomi*

¹⁰³³ Geoff Forrester (ed), *Post-Soeharto – Renewal or Chaos?* (Crawford House Publishing, 1999) 44. See also, Nyman, below n 1074, 166. Habibie's leadership was seen as reinstating and reusing the New Order institutions; See also, Hadi Soesastro, 'Introduction – Indonesia under Megawati' in Hadi Soesastro, Anthony L Smith and Han Mui Ling (eds), *Governance in Indonesia – Challenges facing the Megawati presidency* (Institute of Southeast Asian Studies, 1st ed, 2003) 211.

¹⁰³⁴ Forrester (ed), above n 1033, 44. Habibie's Westernised thought derived from his educational and work experience background. He obtained a doctorate degree and worked in the aircraft industry in Germany for over 20 years. He displayed an informal style such as allowing the existence of open debates during official meeting and disagreement with the dichotomy between Western and Asian values. This was contrary with Soeharto who did not believe and recognise Western ideas and values such as democracy and human rights. They were seen as alien concepts, which had to be resisted as they did not conform to the pure Indonesian way of life. Soeharto's cabinet meeting was characterised by the absence of open debate and disagreement with the opinions of Soeharto.

¹⁰³⁵ Sixty seven laws and one interim law were introduced. See, Lindsey (ed), above n 3, 12.

¹⁰³⁶ Erb, Faucher and Sulistiyanto, (eds), above n 957, 7.

daerah [local autonomy]. *Badan Penyehatan Perbankan Nasional (BPPN)* [Indonesian Bank Restructuring Agency (IBRA)] was also established.

The reforms were claimed to re-enforce Soeharto's legacies. For example, the new laws on decentralization through local autonomy have been claimed to have contributed to the extension of corruption in the regions. Fitzpatrick claimed that the IBRA itself represented crony capitalism. The long process conducted by IBRA of divesting corporate and banking assets raised concerns about transparency and collusion. Conglomerate owners reclaimed ownership of assets 'through the back door'.¹⁰³⁷

The strengthening of small enterprises and cooperatives [*koperasi*] was better promoted than before. They previously played a weak and marginal role. The partnership [*kemitraan*] schemes also encouraged larger private enterprises to enhance small enterprises and cooperatives.¹⁰³⁸

However, the promotion of small enterprises and cooperatives led to deep concern in larger businesses. They were in serious trouble but were not being assisted by government. The conglomerates controlled by Indonesian Chinese were in 'danger of hostile takeovers by groups sponsored by the government.' Some business owners believed that the government intended to replace them with government sponsored cooperatives and enterprises.¹⁰³⁹ Anti-Chinese feelings also contributed to their concerns.¹⁰⁴⁰

(b) The acknowledgement of the significance of corporate governance and transparency

The year 1998 was a milestone for corporate governance in Indonesia. The Indonesia Stock Exchange (IDX) proposed comprehensive listing rules requiring listed companies to appoint independent commissioners and to establish audit committees.¹⁰⁴¹

In 1999 there was another milestone for accountability and transparency for the country as a whole in the first democratic election.¹⁰⁴² Civil society took on a new

¹⁰³⁷ Fitzpatrick, above n 1002, 178, 180.

¹⁰³⁸ Sofyan Wanandi, 'The post-Soeharto business environment' in Geoff Forrester (ed), *Post-Soeharto Indonesia – Renewal or Chaos?* (Crawford House Publishing Bathurst, 1999) 128.

¹⁰³⁹ Ibid.

¹⁰⁴⁰ Ibid.

¹⁰⁴¹ G Amri, *Sejarah lahir GCG dan perkembangannya di Indonesia* (4 Oktober 2004)

< gustiphd.blogspot.com/.../sejarah-lahir-gcg-dan-perke... >.

importance by becoming a vital apparatus to control governance processes.¹⁰⁴³ The president and parliament were directly elected. This demanded transparency and created the conditions for a popularity culture¹⁰⁴⁴ [*budaya popularitas*] or political image [*pencitraan politik*]. Political parties generally presented their images to the public through the mass media. It transformed the role of the mass media.

Habibie failed to demonstrate his capability to improve the economic condition of Indonesia. It was a claim that he had poor political instincts¹⁰⁴⁵ that worsened the political situation and finally led him withdrawing his candidacy in the presidential election. The reformation movement criticised his performance and demanded his resignation.¹⁰⁴⁶ In October 1999, Abdurrahman Wahid became president.

4.3.4.3. Abdurrahman Wahid (20 October 1999–23 July 2001)

Abdurrahman Wahid, better known as Gus Dur, was elected president by the People's Consultative Assembly [*Majelis Permusyawaratan Rakyat – MPR*] as a reformist leader thought to be able to lead the country through a difficult transition.¹⁰⁴⁷ He was seen to have the capacity to bridge the two largest political groups, the nationalists and Islamic-oriented groups.¹⁰⁴⁸ He also had the potential to restore the confidence of the international

¹⁰⁴² Goodpaster, 'Combating Corruption in Indonesia: Enhancing Accountability for Development', above n 1029, v.

¹⁰⁴³ *Ibid* xv.

¹⁰⁴⁴ See generally, Sven Cederroth and Hans Antlov (eds), *Elections in Indonesia: the new order and beyond* (RoutledgeCurzon, 2004) 1; Anwar Arifin, *Politik Pencitraan* [Imaging Politics Political Imaging] (Graha Ilmu, 2nd ed, 2014) vii; Kamaruddin Hasan Kuya, *Komunikasi Politik dan Pencitraan (Analisis Teoritis Pencitraan Politik di Indonesia)* [Political Communication and Imaging (Theoretical analysis of political imaging in Indonesia)] <<http://www.kamaruddinhasan.com/2010/10/komunikasi-politik-dan-pecitraan.html>>

¹⁰⁴⁵ Greg Barton, *Abdurrahman Wahid, Muslim Democrat, Indonesian president: A view from the inside* (UNSW Press, 2002) 254. Given example, Habibie gave Indonesia's highest honours awards to close associates and family members and his own wife.

¹⁰⁴⁶ *Ibid* 255.

¹⁰⁴⁷ *Ibid* 296–7. Gus Dur's visit in East Timor was claimed as a confirmation of his credentials and capacity as a reformist leader. Apart from a handful of demonstrators, the people of Dili, Xanana Gusmao and Jose Ramos-Horta warmly welcomed his one-day visit

¹⁰⁴⁸ Aditi Chakrabarty, 'Challenges before Megawati Sukarnoputri' (2001) 36 (36) *Economic and Political Weekly* 3439, 3440.

business community in Indonesia and to rebuild domestic confidence by establishing the rule of law.¹⁰⁴⁹

(a) *The significant changes and the challenge of the persistence of corrupt practices*

Under Abdurrahman Wahid there were some dramatic changes. Transparency through the mass media grew.¹⁰⁵⁰ The country came to have ‘one of the freest presses in south-east Asia’.¹⁰⁵¹ The Ministry for Information, which had controlled the media, was closed. It was argued that its control of information was Stalinist and that its ‘practices of extorting money from media outlets’ was also harmful.¹⁰⁵² The Department of Welfare was also closed. It was believed that its activities had to be carried out by other departments because of the scale of corruption and extortion within and without it.¹⁰⁵³

A significant anti-corruption institution was established as a part of the on-going reformation of state institutions: the *Tim Gabungan Pemberantasan Tindak Pidana Korupsi (TGPTPK)* [Joint team for Eradication of Corruption Crimes].¹⁰⁵⁴

Unfortunately, persistent corruption remained a major problem that the government appeared unable to address. It led to a chaotic political situation, which added to uncertainty concerning economic stability. The president was seen to be reluctant in prosecuting corruption. The legal system was inadequate for the task and the Attorney General, Marzuki Darusman, was overloaded. Government was also lobbied by corrupt business people and business associates of the former regime, who were believed to be key to economic recovery, to abandon the Attorney General prosecution of anti-corruption

¹⁰⁴⁹ Marcus Mietzner, ‘Abdurrahman’s Indonesia: Political conflict and institutional crisis’ in Grayson Lloyd and Shannon Smith (eds), *Indonesia today – Challenges of history* (Institute of Southeast Asian Studies, 2001) 29, 37.

¹⁰⁵⁰ Solehuddin Dori, ‘Perbandingan reformasi era Gus Dur, Mega, dan SBY’ [A comparison of reformation era of Gus Dur, Mega and SBY], *Kompas* (online), 3 Juni 2013) [3] <<http://politik.kompasiana.com/2013/06/03/perbandingan-reformasi-era-gus-dur-mega-dan-sby-565349.html>>.

¹⁰⁵¹ Chakrabarty, above n 1048.

¹⁰⁵² Barton, above n 1045, 290.

¹⁰⁵³ Ibid.

¹⁰⁵⁴ Didin S Damanhuri, *Korupsi, Reformasi Birokrasi dan Masa Depan Ekonomi Indonesia* [Corruption, Bureaucratic reform and the future of Indonesia’s economy] (Lembaga Penerbit Fakultas Ekonomi Universitas Indonesia [Faculty of Economy University of Indonesia Press, 2006])

cases.¹⁰⁵⁵ The government's failure also represented other problems. The lack of a majority in the parliament hampered the introduction of important reform legislation.¹⁰⁵⁶ The lack of effective law and enforcement also worsened the country's economic performance. It was claimed that Indonesia was 'a truly risky place to do business'.¹⁰⁵⁷

Abdurrahman Wahid was seen to have failed to establish regime change. He had not met expectations to resolve the economic crisis or to reform the legal system. He was also seen to have failed in reforming the military and the civil service.¹⁰⁵⁸ A practice of 'money-filled envelopes' – or, 'envelope culture' [*budaya amplop*]¹⁰⁵⁹ to encourage and reward journalists was used to undermine his legitimacy and to call for his impeachment.¹⁰⁶⁰ In July 2001, in the face of ongoing communal tensions, he was removed from office by the People's Consultative Assembly for alleged corruption and incompetence and replaced by the vice president, Megawati Soekarnoputri.

4.3.4.4. Megawati Soekarnoputri (23 July 2001–20 October 2004)

Megawati became president after the dismissal of Abdurrahman Wahid.¹⁰⁶¹ A daughter of the first president, Soekarno, her political capabilities were considered dubious as she had described herself as '*ibu rumah tangga*' [a housewife] and intended to manage the country's economy in the way a housewife managed her family's finances.¹⁰⁶² She

¹⁰⁵⁵ Barton, above n 1045, 307.

¹⁰⁵⁶ van der Eng, above n 989, 1, 5.

¹⁰⁵⁷ Kevin O'Rourke, 1004, 381.

¹⁰⁵⁸ Barton, above n 1045, 300.

¹⁰⁵⁹ *Budaya amplop* is widely known as a practice of bribing officials, journalists or associated persons. It is a gift in the form of a sum of money put inside an envelope to bribe someone in order to illicit favour. It appears to be a common practice in Indonesia. See, 'KPK minta pejabat stop budaya amplop buat wartawan' [KPK calls for officials to stop giving envelope/bribe to journalists], *Tempo.Co* (online) 5 December 2013 <<http://nasional.tempo.co/read/news/2013/12/05/063534951/kpk-minta-pejabat-stop-budaya-amplop-buat-wartawan>>.

¹⁰⁶⁰ Barton, above n 1045, 301. The low salaries of journalists led to a real need of supplementation: for example the paying of travel expenses, or per diems.

¹⁰⁶¹ 'Profile: Megawati Sukarnoputri,' *BBC News* (online), 3 July 2004

<<http://news.bbc.co.uk/2/hi/asia-pacific/1452246.stm>>.

¹⁰⁶² 'Megawati's achievements', *The Jakarta Post* (online), July 23 2003

<<http://www.thejakartapost.com/news/2003/07/23/megawati039s-achievements.html>>.

became president with the country facing economic hardship related to its persistent corruption problems and ongoing sectarian violence.¹⁰⁶³

(a) *The struggle to combat corruption*

Under Megawati's leadership economic hardships and corruption persisted. Foreign and domestic investments plunged dramatically and unemployment increased steadily.¹⁰⁶⁴ In 2002 an anti corruption body with significant legal powers, the *Komisi Pemberantasan Korupsi (KPK)* [Commission on Eradication Corruption] was established.¹⁰⁶⁵ Corruption, however, remained a significant factor in most Indonesian lives including those involved in politics and in law enforcement.¹⁰⁶⁶ Megawati came to be seen as making little effort to combat corruption.¹⁰⁶⁷ Poor policy development under her was attributed to both incompetence and corruption. It produced inconsistencies in implementing programs across her administration.¹⁰⁶⁸ It led to poor governance and a lack of legal and administrative certainty.¹⁰⁶⁹ It was also claimed to have contributed to a continued deterioration in public finance and in private sector activities.¹⁰⁷⁰ This ineffective administration was also claimed to reflect her weak leadership of the economy overall.¹⁰⁷¹ Despite these weaknesses Megawati's presidency was marked by some progress.

(b) *The improvement of political stability, macro-economy recovery and good corporate governance efforts*

Economic growth was one area of improvement between 2001 and 2004 as Indonesia emerged from the Asian currency crisis. Macro-economic policy was stabilized, both inflation and fiscal deficits were reduced and dependency on the International

¹⁰⁶³ 'Profile: Megawati Sukarnoputri', above n 1061.

¹⁰⁶⁴ Ibid. See also, 'Megawati's achievements', above n 1062.

¹⁰⁶⁵ Damanhuri, above n 1054.

¹⁰⁶⁶ Erb, Faucher and Sulistiyanto, (eds), above n 957, 7.

¹⁰⁶⁷ 'Profile: Megawati Sukarnoputri', above n 1061.

¹⁰⁶⁸ Soedradjad Djiwandono, 'Role of the IMF in Indonesia's financial crisis' in Hadi Soesastro, Anthony L Smith and Han Mui Ling (eds), *Governance in Indonesia – Challenges facing the Megawati presidency* (Institute of Southeast Asian Studies, 1st ed, 2003) 215.

¹⁰⁶⁹ Hadi Soesastro, Anthony L Smith and Han Mui Ling (eds), *Governance in Indonesia – Challenges facing the Megawati presidency* (Institute of Southeast Asian Studies, 1st ed, 2003) 7.

¹⁰⁷⁰ Ibid 12.

¹⁰⁷¹ Berkley Center, *Resources on Faith, Ethics, and Public Life – Megawati Sukarnoputri* (6 January 2014) [1] <<http://berkleycenter.georgetown.edu/resources/people/megawati-sukarnoputri>>.

Monetary Fund (IMF) ended.¹⁰⁷² The currency was stabilised. There was significant consumer growth.¹⁰⁷³ The GDP grew between 3.3 and 4.1 per cent.¹⁰⁷⁴ Economic focus was concentrated on medium to small business.¹⁰⁷⁵ These achievements were claimed to be at the expense of the reform of the state apparatus, including the judiciary, the police and the military as well as the improvement of civil society and political parties.¹⁰⁷⁶

The period also saw the privatisation of state owned enterprises (SOEs). This was advised by the World Bank and International Monetary Fund (IMF). Dwidjowijoto supported the privatisation, considering SOEs as a burden on government and society. They ran monopolistic businesses imposing costs on the community. The monopolies were likely to be related to corruption, collusion, and nepotism. Their practices demonstrated the absence of two crucial principles of good corporate governance: transparency and accountability.¹⁰⁷⁷

¹⁰⁷² R William Liddle and Saiful Mujani, 'Indonesia in 2004: The rise of Susilo Bambang Yudhoyono' (January/February 2005) 45 (1) *Asian Survey* 119, 125.

¹⁰⁷³ 'Megawati's achievements', above n 1062; See also, 'Profile: Megawati Sukarnoputri,' above n 1061.

¹⁰⁷⁴ Mikaela Nyman, *Democratising Indonesia : The challenges of civil society in the era of reformasi* (NIAS, 2006) 174. This was still much lower than before the economic crisis where growth was six to seven per cent.

¹⁰⁷⁵ Soesastro, Smith and Ling (eds), above n 1069. Given example, Expansion of retail space, sales of cars and motorcycles, renovation of office space, and a mini-boom in small-and medium-sized housing estates were amongst its indicators. Previous concentration was in big corporations and state enterprises.

¹⁰⁷⁶ Nyman, above n 1074.

¹⁰⁷⁷ Dwidjowijoto, above n 969, 286–8. It was argued that privatisation in all economy activities was the answer for improving social welfare since they have to compete as opposed to a monopoly. In fact, privatisation was a perfect transformation towards the capitalist economy. It is libertarianist and capitalist. See generally, World Bank Policy Research Report, *Bureaucrats in business – The economics and politics of government ownership* (Report No. 16341 Sept.1995), 1-3 <http://www-wds.worldbank.org/external/default/WDSContentServer/IW3P/IB/1995/09/01/000009265_3970716145144/Rendered/PDF/multi0page.pdf>. The 1995 World Bank findings demonstrated four disadvantages for SOEs in developing countries. Firstly, the SOEs absorbed large amounts of funds that could be better spent on basic social services social services. Secondly, SOEs often capture a disproportionate share of credit, squeezing private sector borrowing [due to political ties]. Thirdly, SOE's factories were often pollute[d] more than privately owned factories. Fourthly, a modest improvement in SOEs efficiency would substantially reduce and in some cases eliminate the fiscal. 'Bureaucrats typically perform poorly in business, not because they are incompetent (they aren't) but because they face contradictory goals and perverse incentives that can distract and discourage even very able and dedicated public servants.

More progress was seen in expanding the scope of corporate governance across other enterprises. The *Komisi Nasional Kebijakan* Corporate Governance [National Committee on Corporate Governance Policy] changed to the *Komite Nasional Kebijakan Governance* (KNKG) [National Committee on Governance Policy] in 2004. This represented an expansion of its role from governance in the corporate sector to the public sector.¹⁰⁷⁸ The Committee introduced several codes including the 2004 Banking Corporate Governance Code, the Independent Commissioner Code and the Code for the Establishment of an Effective Audit Committee.¹⁰⁷⁹

In 2004 Megawati was defeated by Susilo Bambang Yudhoyono.

4.3.4.5. Susilo Bambang Yudhoyono (20 October 2004–October 2014)

Susilo Bambang Yudhoyono, known as SBY, became Indonesia's first directly elected president.¹⁰⁸⁰ He was in power for two terms. Economic development was the main focus of his government, focusing on developing middle and large enterprises.¹⁰⁸¹ It is claimed that these priorities can be seen from his choice of vice presidents, Jusuf Kalla and Boediono.¹⁰⁸² He pursued a neo-liberal agenda concentrating on greater economic freedom

¹⁰⁷⁸ Amri, above n 1041. The change was under a ministerial decree of *the Surat Keputusan Menteri Koordinator Perekonomian RI* No. KEP-49/M.EKON/II/TAHUN 2004. Very low rates of growths or incurred losses were recorded from most SOEs (63 per cent, or 103 of 162) until 2001. However, the privatisation raised a controversy as the program utilized strategic sales rather than IPOs. It was dominated by foreign vendors.

¹⁰⁷⁹ Ibid.

¹⁰⁸⁰ Liddle and Mujani, above n 1072, 119. This was the last term for SBY – he is not eligible for the third term – since the third direct presidential election was conducted on 9 July 2014.

¹⁰⁸¹ Aldi Gultom, 'Bantahan SBY soal arah ekonomi dibantah lagi oleh konstitusi' [SBY's rebuttal of his economic direction was contradicted with the Constitution], *RMOL.CO* (online), 2 April 2011 <<http://www.rmol.co/read/2011/04/02/22970/Bantahan-SBY-Soal-Arah-Ekonomi-Dibantah-Lagi-oleh-Konstitusi->>. This economic direction was criticized, as opposed to democratic economy [*ekonomi kerakyatan*] – such as cooperative – as mandated by the Constitution. See also, 'SBY_Boediono tidak jalankan ekonomi kerakyatan' [SBY_Budiono do not apply democratic economy], *Suara Merdeka* [Independent Voice] (online), 31 Januari 2010 <<http://m.suaramerdeka.com/index.php/read/news/2010/01/31/45729>>.

¹⁰⁸² Heri Susanto, 'Pilih Boediono, SBY fokus bangun ekonomi – Boediono memiliki kemampuan yang tidak perlu diragukan di bidang ekonomi' [SBY chose Boediono reflecting a focus of economic development – Boediono has un-doubtful capability in the economy], *Vivanews* (online), 12 Mei 2009 <http://us.bisnis.news.viva.co.id/news/read/56944-pilih_boediono__sby_fokus_bangun_ekonomi>; See also, Sunny Tanuwidjaja, 'Boediono, a safe and prudent choice as Indonesia's VP' on *East Asia Forum Quarterly (EAFQ) – Economics*,

in trading, industry and investment. It is reflected in Investment Law No 25 of 2007 that removed the differentiation between foreign and domestic investors.¹⁰⁸³ SBY's period as president was also marked by significant failures in addressing persistent problems of corruption.

(a) *The improvement of macro-economy and foreign investor confidence*

Economic growth was one of the SBY's main policies in his election campaign. They also included measures relating to anti-corruption, strengthening democracy and human rights. Significant reforms were made which led to macro-economic improvements. Government debt as a share of GDP significantly decreased from over 60 percent in 2004 to only 25 per cent by 2012. Indonesia became one of the world's fastest growing economies. Foreign investor confidence increased. The excellent economic performance¹⁰⁸⁴ was reflected in Indonesia's GDP becoming the biggest in Southeast Asia and by becoming an associate of the G20 economies.¹⁰⁸⁵

Policies, which further liberalised the economy, were introduced as 'a third avenue for the country's economic development to make people more prosperous'. It was claimed that they were not free-market or anti free market policy. Market and anti-market ideologies, it was claimed, had grown together.¹⁰⁸⁶ The policies had four points: pro-growth, pro-employment, pro-poverty alleviation and pro-environment.¹⁰⁸⁷

Politics and Public Policy in East Asia and the Pacific (17 May 2009) <<http://www.eastasiaforum.org/2009/05/17/boediono-a-safe-and-prudent-choice-as-indonesias-vp/>>. Jusuf Kalla was the first vice president of the SBY. He is a business man. Boediono is an experienced and highly skilled economist. He has economic credentials. He was previously State Minister of National Planning and Development, Minister of Finance, Coordinating Minister for the Economy, and deputy governor of Bank Central. He graduated from University of Western Australia in Perth, Monash University in Melbourne and the Wharton School of the University of Pennsylvania. He was one of the Wharton School's 125 influential people and ideas list in 2007.

¹⁰⁸³ It was introduced replacing Foreign Investment Law No 1 of 1967 and Domestic Investment Law No. 6 of 1968.

¹⁰⁸⁴ Sacha Passi, 'Eye of the tiger: Portrait of Susilo Bambang Yudhoyono' *Southeast Asia Globe* (online), 16 July 2012 <<http://sea-globe.com/eye-of-the-tiger/>>.

¹⁰⁸⁵ Consulate General of the Republic of Indonesia in Vancouver B.C., Canada, *President Yudhoyono explains about Indonesia's economy policy* <<http://www.indonesiavancouver.org/news-a-articles/904-president-yudhoyono-explains-about-indonesias-economic-policy/>>.

¹⁰⁸⁶ Ibid.

¹⁰⁸⁷ Ibid.

The policy targets were not met. The 6.3 per cent economic growth for 2013 was not achieved. The rupiah plunged and at its worst cost IDR 11 000 to buy 1 US dollar. The weaker currency impacted on capital goods and basic commodities imports including the imports of soybeans, wheat, beef, electronics and cars. Price rises became unavoidable. It also impacted on other imported goods. The current account deficit soared to 4.4 percent of GDP in the second quarter of 2013: equivalent to \$9.8 billion. Bank Indonesia stated this was ‘the largest deficit ever and a sharp jump from the 2.4 per cent deficit in the first quarter’.¹⁰⁸⁸

The economic failures were attributed to several factors. They included widespread corruption, political interference in the economy and a weak judicial system. They contributed to the creation of further uncertainty and risk.¹⁰⁸⁹

(b) Pervasive corruption and chaotic legal system

Under SBY’s presidency, pervasive corruption remained a crucial problem. It added to chaos in the legal system and the lack of law enforcement undermined economic and business activities. Indonesia was ranked as the most corrupt investment destination amongst 16 major Asia-Pacific countries.¹⁰⁹⁰ This deterred foreign investors.¹⁰⁹¹

The problem continued to worsen in the absence of commitments to combating corruption. Buehler claimed that ‘[t]he law bends in the direction of the rich and powerful, which undermines transparency and accountability’.¹⁰⁹² The government was seen to protect the interests of the entrenched elite. Buehler also observed that ‘Many of the reform laws have only been partially implemented, or not at all, leaving legal loopholes rife for graft and underhand business dealings at the expense of the Indonesian government’s integrity’.¹⁰⁹³

¹⁰⁸⁸ Novy Lumanauw and Ezra Sihite, ‘SBY flags economic policy plans’, *The Jakarta Globe* (online), 22 August 2013 <<http://www.thejakartaglobe.com/business/sby-flags-economic-policy-plans/>>.

¹⁰⁸⁹ Passi, above n 1084.

¹⁰⁹⁰ See generally, ‘Indonesia most corrupt of key Asian nations’, above n 28.

¹⁰⁹¹ ‘Less caviar, more gado-gado: Indonesia’s star begins to wane’, *The Sydney Morning Herald* (online), 28 August 2013 <<http://www.smh.com.au/business/world-business/less-caviar-more-gadogado-indonesias-star-begins-to-wane-20130828-2sq4j.html>>.

¹⁰⁹² Passi, above n 1084.

¹⁰⁹³ *Ibid.*

The SBY's government commitment to anti-graft efforts was doubted. Some believed that the bills for amendment of the Criminal Code [*KUHP*] and the Criminal Procedures Code [*KUHAP*] weakened the KPK's power.¹⁰⁹⁴ The chairman of the Supreme Court Criminal Chamber [*Kamar Pidana Mahkamah Agung*] supported this claim pointing to the provisions in the Bill preventing the Supreme Court from imposing heavier penalties or punishment than the lower courts.¹⁰⁹⁵

Legal certainty around business transactions and contracts were also poor and significantly influenced the investment environment. Inconsistency in court decisions were among the main factors. Many contracts had been cancelled by corrupt courts: *praktik mafia pengadilan* [mafia practices in court cases]. The lack of understanding of the contents of a contract by the judge is also claimed to be another factor. Foreign investors often faced difficulties in the legal system.¹⁰⁹⁶

Despite these poor conditions, there were some improvements in corporate law, governance and securities regulations.

(c) The improvement of good corporate governance awareness

Some significant efforts had been made in improving corporate governance practices. In 2001, the GCG Code was introduced by the National Committee on Corporate Governance Policy (KNKCG), which was later changed becoming the National Committee on Governance Policy (KNKG), see Chapter [4.3.4.4]. In 2006, the 2001 GCG Code had been revised. The revision introduced several significant provisions. They are: a clear description of the role of the state, corporate community and society; guidelines for business ethics and conduct; required corporate structures such as an audit committee, a

¹⁰⁹⁴ Ina Parlina, 'Govt, House ignore KUHP, KUHAP demands', *The Jakarta Post* (online), 22 Februari 2014 <<http://www.thejakartapost.com/news/2014/02/22/govt-house-ignore-kuhp-kuhap-demands.html>>.

¹⁰⁹⁵ 'RUU KUHP dan KUHAP – Aneh, MA tidak boleh putuskan hukuman lebih berat' [The KUHP and KUHAP Bills – It is strange, the Supreme Court would unable to give heavier penalties], *Tribunnews* (online), 4 Maret 2014 <<http://m.tribunnews.com/nasional/2014/03/04/aneh-ma-tidak-boleh-putuskan-hukuman-lebih-berat>>.

¹⁰⁹⁶ Mahmud Siregar, *Kepastian hukum dalam transaksi bisnis internasional dan implikasinya terhadap kegiatan investasi di Indonesia* [Legal certainty in international business transactions and its implication on investment activities in Indonesia] 6 <www.ocw.usu.ac.id/...hukum-transaksi-bisnis-internasional/...>.

risk policy committee, a remuneration and nomination committee, a committee for corporate governance policy, a director's function in company management, corporate responsibilities of stakeholders, corporate governance implementation and practical guidelines for the implementation of corporate governance code.¹⁰⁹⁷ Bank Indonesia [Central Bank] also issued a regulation concerning good corporate governance implementation for commercial banks in 2006.¹⁰⁹⁸

In 2011, *Otoritas Jasa Keuangan* (OJK) [Financial Services Authority] was established under the Law No 21 of 2011. The OJK replaced the Capital Market and Financial Institutions Supervisory Agency (BAPEPAM-LK) and the central bank's functions in banking supervision.¹⁰⁹⁹ The OJK is an independent agency created to regulate, supervise and protect financial industries including banking, capital markets and non-bank financial industry. Transparent and accountable financial services are among its main objectives.¹¹⁰⁰ The OJK introduced a roadmap to corporate governance in 2014. It is a

¹⁰⁹⁷ Amri, above n 1041.

¹⁰⁹⁸ Asian Corporate Governance Association, *Library – Codes and Rules – Indonesia*, [8]–[9] <http://www.acga-asia.org/content.cfm?SITE_CONTENT_TYPE_ID=12&COUNTRY_ID=265>. The regulation requires banks to implement good corporate governance based on five main principles i.e. transparency, accountability, responsibility to maintain the prevailing laws and regulations and prudential bank management, independency from undue influence/pressure from any parties, and fairness in fulfilling the rights of stakeholders arising from agreements and prevailing laws and regulations. A regular self-assessment on the adequacy of good corporate governance implementation and the preparation of a report from each bank is required. Fail to comply will be imposed sanctions. The amendments were mainly the roles and duties of the Board of Commissioners and the Board of Directors.

¹⁰⁹⁹ Rio Fafen Ciptaswara, *Implikasi pembentukan OJK terhadap pengaturan dan pengawasan perbankan* [The implication of the establishment of OJK in regulating and supervising banking sector] (22 April 2013) Pusat Studi Perdagangan Dunia Universitas Gadjah Mada (Center for World Trade Studies Gadjah Mada University), [1] <<http://cwts.ugm.ac.id/2013/04/implikasi-pembentukan-otoritas-jasa-keuangan-terhadap-pengaturan-dan-pengawasan-perbankan-indonesia/>>. The OJK – Otoritas Jasa Keuangan [Indonesia Financial Services Authority] has operated in January 2013 for capital market and non-bank financial industries as well as banking sectors in 2014. It was officially operated in 31 December 2013. See at <<http://www.ojk.go.id/en/>>. As of December 31st, 2013 OJK officially regulates and supervises Indonesia's banking sector'.

¹¹⁰⁰ Otoritas Jasa Keuangan, *Tugas dan fungsi* [Task and function], [1] <<http://www.ojk.go.id/tugas-dan-fungsi/>>. See also, Rio Fafen Ciptaswara, above n 1099, [2]- [3]. The OJK is considered an independent institution and is expected to be a professional agency. See also, Rudy Hendra Pakpahan, *Akibat hukum dibentuknya lembaga otoritas jasa keuangan terhadap pengawasan lembaga keuangan di Indonesia* [Legal consequences of the establishment of OJK for the supervision of financial institutions in Indonesia], 2–4

series of recommendations to improve existing regulations. The objective is to strengthen corporate governance regulations for Indonesian listed enterprises and new issuers. Specifically, it seeks to enhance the supervising roles of company boards, the quality of disclosure and transparency.¹¹⁰¹

SBY finished his second term as president in 2014 and was prohibited by the Constitution from seeking a third term and Joko Widodo was elected president.

4.3.4.6. Joko Widodo (October 2014– present)

Joko Widodo, or Jokowi, is the second directly elected president. He was previously the mayor of the city of Solo, Central Java, and was elected in 2012 as governor of Jakarta. His populist style as a governor made him famous. He had a reputation for streamlining bureaucracy and improving public services.¹¹⁰² He introduced a different leadership approach. He visited poor communities in *blusukan* [walkabout or spontaneous visit], made unannounced visits to government offices, opened his office to anyone to report complaints, refused any kind of gifts, encouraged greater citizen participation through social media and dressed informally.¹¹⁰³

Jokowi became the first ordinary person to become president in the sense that he was not the chair of a political party and has no ties to the military.¹¹⁰⁴ He has been

<http://www.academia.edu/4845281/Akibat_Hukum_Pembentukan_Lembaga_OJK>. It is believed that the establishment of the OJK was the best solution for the effectiveness and efficiency for supervising financial institutions. It was claimed that it replaced ineffective supervisory function of the Bank Indonesia and Bapepam. This is a separation of supervisory function to banking sectors from central bank. For example: Monetary Authority of Singapore (MAS) in Singapore, the Federal Reserve (The Fed) in the USA, and the Australian Prudential Regulation Authority (APRA) in Australia.

¹¹⁰¹ International Financial Corporation, above n 265, 1.

¹¹⁰² Karon Snowdon, 'Indonesia's next president Jokowi: a 'man of the people' from outside the traditional elite', *ABC News* (online), 22 July 2014 <<http://www.abc.net.au/news/2014-07-22/jokowi-profile-by-karon-snowdon/5585268>>.

¹¹⁰³ The popularity as governor led him to being promoted by the Indonesian Democratic Party of Stuggle [PDI-P] chaired by Megawati to run in to the second presidential election in July 2014. Jokowi won with 71 millions votes, or 53 percent of total votes, defeating former special-forces general Prabowo Subianto. See, 'Joko Widodo wins Indonesia presidential election', *BBC News* (online), 22 July 2014 <<http://www.bbc.com/news/world-asia-28415536>>.

¹¹⁰⁴ Mong Palatino, 'Jokowi's first week as Indonesia's president-elect', *The Diplomat* (online), 31 July 2014 <<http://thediplomat.com/2014/07/jokowis-first-week-as-indonesias-president-elect/>>.

acknowledged as the ‘man of the people from outside the traditional elite’ and this brought a new hope for change.¹¹⁰⁵

Early in his presidency many indicated that ‘optimism has turned into scepticism’.¹¹⁰⁶ What is perceived as weak leadership, a lack of political experience, and commitment to his political allies have led to a changed assessment. These have hindered his government from addressing a number of challenges including a faltering economy, destabilising current-account deficit, a persistently corrupt bureaucracy and judiciary¹¹⁰⁷ and regulatory as well as legal uncertainty that handicaps the economy.¹¹⁰⁸

Many associate Jokowi’s weaknesses with his lack of political capability and his distance from the elite. Baker described Jokowi as outclassed, outmanoeuvred and under the control of his political patrons, particularly Megawati the chair of the PDI-P and Surya Paloh of Nasdem [National Democratic Party] who are experienced chairs of party machines.¹¹⁰⁹ McRae described him as ‘a complete new comer to national politics who rose to power without the complete support of his own political party’.¹¹¹⁰ Jokowi is considered the weakest president in terms of political support.¹¹¹¹ He is portrayed by Djayadi as being in a triple minority position: supported by a smaller coalition, not in control of his political

¹¹⁰⁵ Snowden, above n 1102.

¹¹⁰⁶ Yenni Kwok, ‘Indonesia’s Jokowi marks 100 days of presidency with scandal, falling support’, *Time* (online), 28 January 2015 <<http://time.com/3685421/indonesia-joko-widodo-jokowi-100-days-of-presidency/>>.

¹¹⁰⁷ ‘Indonesia’s presidential election: Jokowi’s day though his opponent attempts to spoil it’, *The Economist* (online), 26 July 2014 <<http://www.economist.com/news/asia/21608800-though-his-opponent-attempts-spoil-it-jokowis-day>>.

¹¹⁰⁸ Snowden, above n 1102.

¹¹⁰⁹ Kwok, ‘Indonesia’s Jokowi marks 100 days of presidency with scandal, falling support’, above n 1106.

¹¹¹⁰ Jewel Topsfield, ‘After just six months on the job, Indonesian president Joko Widodo’s halo is slipping’, *The Sydney Morning Herald* (online), 20 April 2015 <<http://www.smh.com.au/world/after-just-six-months-on-the-job-indonesian-president-joko-widodos-halo-is-slipping-20150420-1mn1sn.html>>.

¹¹¹¹ ‘Pengamat: Posisi politik Jokowi-Kalla terlemah dari presiden sebelumnya’ [Observer: the political position of Jokowi-Kalla is the weakest compared to former presidents], *Kompas* (online), 21 Desember 2014 <<http://nasional.kompas.com/read/2014/12/21/16293111/Pengamat.Posisi.Politik.Jokowi-Kalla.Terlemah.dari.Presiden.Sebelumnya>>; ‘Jokowi jadi presiden terlemah dalam sejarah Indonesia’ [Jokowi becomes the weakest president in Indonesian history], *Republika* (online), 9 October 2014 <<http://www.republika.co.id/berita/nasional/politik/14/10/09/nd5e6h-jokowi-jadi-presiden-terlemah-dalam-sejarah-indonesia>>.

party and a new kid on the block.¹¹¹² As a consequence, Baker claimed, that this has created a complex political conflict.¹¹¹³ It has the potential to continue to derail his highly anticipated programs.¹¹¹⁴

The appointments of high ranking positions, including cabinet ministers, have been seen as a showing the fulfilment of his commitments to others. Nearly half of Jokowi's cabinet are associates of his political allies including Megawati's daughter.¹¹¹⁵ Prasetyo, a politician from *Nasdem* was appointed as the Attorney General¹¹¹⁶ who promoted his own son to the coordinator of the Attorney-General's Jakarta office.¹¹¹⁷ The head of the State Intelligence Agency [*Badan Intelijen Negara – BIN*] is Sutiyoso, chair of *PKPI* [Indonesian Justice and Unity Party]. This reflects a common practice of political bargaining. It is

¹¹¹² Fendina S Sundaryani, 'Jokowi must act firmly or lose trust: Expert', *The Jakarta Post* (online), 15 February 2015 <<http://www.thejakartapost.com/news/2015/02/15/jokowi-must-act-firmly-or-lose-trust-expert.html>>; See also, 'Banyak aktivis di kekuasaan, kriminalisasi KPK dianggap sulit dihentikan' [Many activists in power, criminalisation is seen difficult to be discontinued], *Kompas* (online), 11 July 2015 <<http://nasional.kompas.com/read/2015/07/11/04010041/Banyak.Aktivis.di.Kekuasaan.Kriminalisasi.KPK.Dianggap.Sulit.Dihentikan>>.

¹¹¹³ Kwok, 'Indonesia's Jokowi marks 100 days of presidency with scandal, falling support', above n 1106.

¹¹¹⁴ Sundaryani, 'Jokowi must act firmly or lose trust: Expert', above n 1112; See also, 'Banyak aktivis di kekuasaan, kriminalisasi KPK dianggap sulit dihentikan', above n 1112.

¹¹¹⁵ Kwok, 'Indonesia's Jokowi marks 100 days of presidency with scandal, falling support', above n 1106.

¹¹¹⁶ 'Observers slam appointment of politician H.M. Prasetyo as Attorney General: Impossible to clean dirty floor with a dirty sweeper', *The Jakarta Globe* (online), 20 November 2014 <<http://thejakartaglobe.beritasatu.com/news/observers-slam-appointment-politician-h-m-prasetyo-attorney-general/>>; Rendi A Witular, 'Mediocrity, controversy shroud Attorney General Prasetyo', *The Jakarta Post* (online), 21 November 2014 <<http://www.thejakartapost.com/news/2014/11/21/mediocrity-controversy-shroud-attorney-general-prasetyo.html>>: '3 dosa Jokowi saat pilih jaksa agung Prasetyo' [3 sins of Jokowi when he elected Prasetyo as Attorney General], *Tempo* (online), 21 November 2014 <<http://nasional.tempo.co/read/news/2014/11/21/078623438/3-dosa-jokowi-saat-pilih-jaksa-agung-prasetyo>>; 'PDI-P tidak puas Jokowi tunjuk HM Prasetyo sebagai jaksa agung' [PDI-P is unhappy that Jokowi appointed HM Prasetyo as Attorney General], *Kompas* (online), 20 November 2014 <<http://nasional.kompas.com/read/2014/11/20/18475481/PDI-P.Tidak.Puas.Jokowi.Tunjuk.HM.Prasetyo.sebagai.Jaksa.Agung.>>.

¹¹¹⁷ Haeril Halim, 'Attorney General promotes son to coordinator at Jakarta office', *The Jakarta Post* (online), 18 May 2015 <<http://www.thejakartapost.com/news/2015/05/18/attorney-general-promotes-son-coordinator-jakarta-office.html>>.

locally known as *'bagi-bagi jatah kursi menteri'* [share ministerial seats for political alliances].

These appointments have tested Jokowi's promises of major reform, particularly those related to tackling corruption and strengthening bureaucracy.¹¹¹⁸ The hope for change is in question.

(a) The weakening of the KPK continues

One of Jokowi's significant campaign promises was to strengthen the role of the KPK in order to create a fear of engaging in corrupt conduct. The promise included a social revolution, which would free the political system of corruption and intimidation. This is also now being questioned.¹¹¹⁹ Since Jokowi took office, media coverage has exposed a number of weaknesses in his leadership and his broken promises on anti corruption activities.

The lack of Jokowi's leadership is said to be demonstrated by his failure to defend the KPK. He was perceived as unable to stop a police conspiracy to damage it. It is claimed that 'the KPK is now crippled'.¹¹²⁰ The result is that the KPK is now seen as a political body rather than an independent law enforcement agency.¹¹²¹

Powerful political interests are considered to have threatened the KPK's power. The nomination of graft suspect, Budi Gunawan, a former aide of Megawati, to the role of police chief¹¹²² is one example. Gunawan challenged the KPK's naming him of him as a graft suspect in a court. The verdict of the South Jakarta Court annulled his suspect

¹¹¹⁸ Snowden, above n 1102.

¹¹¹⁹ Topsfield, above n 1110; See also, Wahyu Aji, 'Aktivis lintas generasi: Nawacita Jokowi kini jadi duka cita' [Activists of across generation: Jokowi's nine agendas turns sorrow], *Tribun* (online), 11 July 2015 <<http://www.tribunnews.com/nasional/2015/07/11/aktivis-lintas-generasi-nawacita-jokowi-kini-jadi-duka-cita>>.

¹¹²⁰ Simon Butt and Tim Lindsey, 'Joko Widodo's support wanes as Indonesia's anti-corruption agency KPK rendered toothless: The Indonesian president looks impotent as the anti-corruption agency is crippled', *The Age* (online), 11 April 2015 <<http://www.theage.com.au/comment/joko-widodos-support-wanes-as-indonesias-anticorruption-agency-kpk-rendered-toothless-20150401-1mdawv.html>>. The tensions between police and the KPK have been seen as a lack of Jokowi's leadership on corruption.

¹¹²¹ Jusuf Wanandi, 'Insight: The first challenge of president Joko Widodo', *The Jakarta Post* (online), 13 February 2015 <<http://www.thejakartapost.com/news/2015/02/13/insight-the-first-challenge-president-joko-widodo.html>>.

¹¹²² Topsfield, above n 1110.

status.¹¹²³ This is the first annulment of a graft suspect status named by the KPK. It led to growing number of graft suspects challenging their graft suspect status in court and creates a legal uncertainty issue. The KPK is a state agency with legislatively entrusted power. The agency has a prosecutorial power that was previously used to successfully prosecute graft suspects.¹¹²⁴ Budi Gunawan was subsequently nominated as deputy chief of police, which has created further political tension between the police and the KPK.¹¹²⁵

After the Budi Gunawan case, conflict over criminal charges brought against the anti-graft body's commissioners and fighters intensified. There are four commissioners of the KPK facing different accusations. Criminal charges have been brought against the former chairman, Abraham Samad over a falsified passport document; and against former deputy commissioners, Bambang Widjojanto over perjury charges, Adnan Pandu Praja over alleged mishandling of company shares in 2006 and against Zulkarnain over bribery in 2008.¹¹²⁶ There are also two commissioners of the *Komisi Yudisial* (KY) [Judicial Commission – a commission with a constitutional mandate to supervise the corps of judges] implicated for alleged defamation against Justice Sarpin Rizaldi for his verdict over

¹¹²³ Editorial, 'Jokowi against us', *The Jakarta Post* (online), 17 February 2015 <<http://www.thejakartapost.com/news/2015/02/17/jokowi-against-us.html>>. Comr. Gen. Budi Gunawan was named by the KPK as a graft suspect over receiving bribes when serving in a number of posts at the National Police. He challenged the KPK's move by filing a pre-trial petition to the South Jakarta District Court. The Court ruling annuled the graft suspect status of Gunawan and he avoided the KPK criminal investigation.

¹¹²⁴ 'KPK dinilai berhasil buat koruptor tidak tenang' [KPK is seen succeeding in making grafters worry], *Islam Pos* (online), 25 April 2014 <<https://www.islampos.com/kpk-dinilai-berhasil-buat-koruptor-tidak-tenang-107361/>>; See also, Emil P Bolongaita, *Why Indonesia's Anti-Corruption Commission succeeds where others don't – a comparison with the Philippines' Ombudsman* (August 2010) Anti-Corruption Resource Centre, 4 <<http://www.u4.no/publications/an-exception-to-the-rule-why-indonesia-s-anti-corruption-commission-succeeds-where-others-don-t-a-comparison-with-the-philippines-ombudsman/downloadasset/190>>.

¹¹²⁵ Ina Parlina and Fedina S Sundaryani, 'Jokowi blindsided by Budi', *The Jakarta Post* (online), 23 April 2015 <<http://www.thejakartapost.com/news/2015/04/23/jokowi-blindsided-budi.html>>. Bambang Widodo Umar, a police expert, suggested that Gunawan's appointment would be a ticket to the top job as Badrodin, a newly appointed chief of police, is expected to retire in 15 months.

¹¹²⁶ Hamish McDonald, 'Indonesian state power masks political weakness', *ABC News* (online), 17 February 2015 <<http://www.abc.net.au/news/2015-02-17/mcdonald-corruption-in-indonesia/6129508>>.

the Budi Gunawan case.¹¹²⁷ The Judicial Commission of Indonesia is a self-reliant state institution, which was established under the Law No. 22 of 2004 concerning Judicial Commission, carrying the authority to uphold the honour and dignity of judges and control their behaviour [Article 13].¹¹²⁸ The police named two of KY's commissioners, Suparman Marzuki and Taufiqurrohman Syahuri, as suspects for the defamation case after Justice Sarpin was criticized by them over his controversial ruling that favoured high-ranking police officer Budi Gunawan.¹¹²⁹ These are considered as threats 'to decapitate the anti-corruption commission'.¹¹³⁰ Many believed that those cases represented strong interference by political power.¹¹³¹ This is considered as an abuse of police power,¹¹³² which is claimed

¹¹²⁷ Fedina S Sundaryani, 'KY pair named suspects for defamation', *The Jakarta Post* (online), 12 July 2015 <<http://www.thejakartapost.com/news/2015/07/12/ky-pair-named-suspects-defamation.html>>; Editorial, 'Criminalizing criticism', *The Jakarta Post* (online), 14 July 2015 <<http://www.thejakartapost.com/news/2015/07/14/editorial-criminalizing-criticism.html>>; See also, Utama, below n 1135; Taufik Ismail, 'Komisi Yudisial pertanyakan penetapan tersangka dua komisionernya ke Bareskrim' [The Judicial Commission questioned the Criminal Investigation Agency (Bareskrim) regarding their two commissioners became criminal suspects], *Tribun* (online), 12 July 2015 <<http://www.tribunnews.com/nasional/2015/07/12/komisi-yudisial-pertanyakan-penetapan-tersangka-dua-komisionernya-ke-bareskrim>>. Criminal cases against the chairman and deputy chairman of judicial commissioners, Suparman Marzuki and Taufiqurrohman Syahuri, over alleged defamation for criticizing a verdict of Justice Sarpin over a pre-trial case of police General Budi Gunawan. A grounding of the verdict was that Budi Gunawan, as a administrative officer at the National Police, was not considered as a legal enforcer. Therefore, Budi Gunawan's status as a corruption suspect was invalid/annuled . As a result, Budi Gunawan has cleared for graft charges.

¹¹²⁸ Komisi Yudisial Republik Indonesia, *Sejarah Pembentukan* [History of the Establishment], [5] <<http://www.komisiyudisial.go.id/statis-14-sejarah-pembentukan.html>>. The Body conducts a selection of judges and propose an appointment of the Supreme Court's judges, a promotion or a dismissal of judges [Article 14–25]. However, the Judicial Commission's power has been stripped by a ruling of the Constitutional Court for its role in the selection of judges. 'The ruling allows the Supreme Court to select judges without having to be accountable to other state bodies'; See, Ina Parlina, 'Court ruling weakens Judicial Commission' *The Jakarta Post* (online), 8 October 2015 <<http://www.thejakartapost.com/news/2015/10/08/court-ruling-weakens-judicial-commission.html>>.

¹¹²⁹ Fedina S Sundaryani, 'Police deliver quick progress in Sarpin case', *The Jakarta Post* (online), 8 August 2015 <<http://www.thejakartapost.com/news/2015/08/08/police-deliver-quick-progress-sarpin-case.html>>.

¹¹³⁰ McDonald, above n 1126. Criminal cases include those against the chairman, Abraham Samad over falsified passport documents, deputy commissioners, Bambang Widjojanto over perjury charges, Adnan Pandu Praja over alleged mishandling of company shares in 2006 and Zulkarnain over accused bribery in 2008

¹¹³¹ 'Relawan Jokowi: Mengenakan wajah penegekakan hukum, ada aroma balas dendam' [Jokowi's volunteers: A pitiful display of law enforcement, there was a revenge], *Kompas* (online), 15 July 2015

<<http://nasional.kompas.com/read/2015/07/15/1648070/Relawan.Jokowi.Mengenakan.Wajah.Pene>

by Mahfud MD, a former chief of the Constitutional Court, as a common phenomenon occurring in all state institutions.¹¹³³ They indicate poor and unfair law enforcement.

(b) A persistent negative portrait of law enforcement

Under Jokowi the high expectation for respect of the use of law and the reform for law enforcement he created, has been tested. This includes the controversial appointment to key law enforcement positions, the charges against KPK and the Judicial Commission officials. The appointments of politicians as Attorney General and as chief of the State Intelligence Agency,¹¹³⁴ as indicated earlier, are considered to have had a negative impact on law enforcement.¹¹³⁵ It is seen as a lack of commitment to law enforcement reform.¹¹³⁶

gakan.Hukum.Ada.Aroma.Balas.Dendam>; ‘Kontras: Budi Waseso lebih terlihat mewakili kepentingan balas dendam’ [Kontras: Budi Waseso appears to represent an interest for revenge], *Kompas* (online), 16 July 2016 <http://nasional.kompas.com/read/2015/07/16/10220111/Kontras.Budi.Waseso.Lebih.Terlihat.Mewakili.Kepentingan.Balas.Dendam?utm_campaign=related_left&utm_medium=bp&utm_source=news>.

¹¹³² ‘Hukum dipakai sebagai alat kekuasaan, Presiden harus menghentikan...’ [Law is used as an instrument of power, President should discontinue it], *Kompas* (online), 14 July 2015 <http://nasional.kompas.com/read/2015/07/14/11403451/.Hukum.Dipakai.sebagai.Alat.Kekuasaan.President.Harus.Menghentikan.?utm_campaign=related_left&utm_medium=bp&utm_source=news>.

¹¹³³ ‘Mahfud MD: Mulai lemah, KPK bisa saja dibubarkan’ [Appear to be weak, KPK may be dismissed], *Kompas* (online), 7 July 2015 <<http://web.law.columbia.edu/millstein-center/corporate-governance-forum/supplemental-materials>>.

¹¹³⁴ ‘Prasetyo jadi jaksa agung, komitmen penegakan hukum Jokowi dipertanyakan’ [Prasetyo becomes a General Attorney, Jokowi’s commitment for law enforcement is questioned], *Kompas* (online), 20 November 2014 <<http://nasional.kompas.com/read/2014/11/20/15465581/Prasetyo.Jadi.Jaksa.Agung.Komitmen.Penegakan.Hukum.Jokowi.Dipertanyakan>>.

¹¹³⁵ Abraham Utama, ‘Jimly: Penetapan komisioner KY jadi tersangka merusak hukum’ [Jimly: Determination of KY’s commissioners as criminal suspects damages legal reputation], *CNN Indonesia* (online), 14 July 2015 <<http://www.cnnindonesia.com/nasional/20150713170859-12-66138/jimly-penetapan-komisioner-ky-jadi-tersangka-merusak-hukum/>>; See also, ‘Penetapan tersangka pimpinan KY dianggap rangkaian kriminalisasi sistematis’ [Determination of KY’s deputy commissioners as criminal suspects is observed as a series of systematic criminalisation], *Kompas* (online), 11 July 2015 <<http://nasional.kompas.com/read/2015/07/11/16465821/Penetapan.Tersangka.Pimpinan.KY.Dianggap.Rangkaian.Kriminalisasi.Sistematis>>; ‘PBNU: Penetapan tersangka pimpinan KY oleh polisi beri kesan negatif’ [PBNU: Determination of KY’s deputy commissioners by police reflects a negative impression], *Kompas* (online), 14 July 2015 <<http://nasional.kompas.com/read/2015/07/14/09545041/PBNU.Penetapan.Tersangka.Pimpinan.KY.oleh.Polisi.Beri.Kesan.Negatif>>.

¹¹³⁶ ‘Prasetyo jadi jaksa agung, komitmen penegakan hukum Jokowi dipertanyakan’, above n 1134.

Other cases are also claimed to reflect the poor state of law enforcement. Criminal charges were brought against two poor and elderly persons over allegedly harvesting teak wood in forests owned by a state forestry company. This has been seen as reflecting discrimination by law enforcement.¹¹³⁷ It is claimed that the cases indicate that enforcement is subject to the principle that ‘those who have access to money and power can defy, or even bend, the rules’. It is said that ‘[t]he law is strictly enforced against the weak, but leniently enforced against the powerful’.¹¹³⁸

These events indicate that Jokowi will struggle to fulfil his promises and the high expectations of him regarding the role of law, law enforcement and anti corruption activities.

4.4. Conclusion

This chapter has provided a background to the values of honesty and transparency in Indonesian society that underlay attitudes towards openness and disclosure in business relations. It also, indirectly, shows how new values, ideas and concepts from abroad, including recently corporate governance and disclosure, have impacted on the values of Indonesian people. These values themselves, as represented in attitudes and customs, are a form of soft law.

The traditional societies mutual assistance between villagers was important and the reputation of people and families mattered. Exchange relations relied on trust. *Pribumi* [indigenous] traders were respected as honest. Reciprocity and equality provided a basis for the familial principle now found in Indonesia’s *Constitution*. The early overseas traders found *pribumi* to be tolerant and flexible in adopting new values. Hindus, Buddhists, Muslims and Christians brought different religions but with underlying moralities and ethical principles about honesty consistent with each other and as a fundamental value in exchange and trade. Ultimately Moslem beliefs and values were to become the most significant source of such influences. Those values, however, existed within societies marked by paternalism of the rulers and the clientelism of the people.

¹¹³⁷ Editorial, ‘Inequality before the law’, *The Jakarta Post* (online), 20 March 2015 <<http://www.thejakartapost.com/news/2015/03/20/inequality-law.html>>.

¹¹³⁸ Ibid. Minor criminal charges of two poor elderly persons for allegedly harvesting teakwood belonging to state forestry company are seen as an indiscriminate law enforcement.

The arrival of the Portuguese and Dutch as traders and then colonisers influenced the establishment of Western-style enterprises, including the company, as Indonesia was drawn into a globalizing economy. Their own formal moral Christian values gave significance to honesty. The colonisers also used *tionghoa* [Chinese] merchants as intermediaries in commerce. They were also familiar with the mutual trust required in their commercial associations or partnerships which came to dominate trade within the country. The Dutch East India Company and subsequently the Dutch colonial government were at the apex of an unequal culture system [*cultuurstelsel*] under which arable land was planted with export crops. This system connected *pribumi*, particularly local elites who benefited from it, with *tionghoa* merchants and the East India Company and the agencies which replaced it. The system was supported by the colonial bureaucracy and government that left a legacy after independence of state, military and crony capitalism which had also further entrenched indigenous patronage [*bapakisme*]. Deference and unquestioning obedience was encouraged. However, the concepts of collective interests and familial principles continued and survived to form the basis of the national economy in the *Constitution*.

The end of Dutch rule in the Japanese occupation changed the role of the traditional rulers. The Japanese widened access to power but patronage was retained. The tribute system for business that they introduced ultimately became synonymous with the word for bribe [*upeti*]. It weakened the integrity of business practices and created a model of military involvement in commercial enterprises to support the armed forces.

The early period of independence was marked by the inability of the new government to control the country as the Dutch resisted. This has had a lasting impact on honesty and transparency in business and on corruption and law enforcement. The Indonesian armed forces followed the Japanese military in developing business activities to support themselves partly independently of money from government. As independence became a greater reality Dutch businesses were destroyed or seized. The instability also had an effect on the legal system. Dutch law continued as there was no time or resources to create a new legal system. In 1958 over a decade of uncertainty about the basic law was resolved when the Constitution of 1945 was finally confirmed. It recognized the social purposes of property and the familial principle but also used liberal principles in both the

economic and political systems. This led to the use of market principles in economic activities. Other programs sought to involve more *pribumi* in business to match ethnic Chinese involvement in the economy. After 1960 the period of guided democracy made law secondary consideration to national policies including the guided democracy economic policy that was intended to create a centralized economic system. In some ways this continued the role the colonial Dutch government had played in the economy as the government came to control significant economic activities which were managed by army officers and bureaucrats. This led to extensive patronage, low productivity, mismanagement of public enterprises and corruption. It contributed to the national economic losses which ended Soekarno's presidency and which led to the rise of Soeharto and the New Order.

The Soeharto era ostensibly reinstated the significance of law in society and in the state but the executive government's domination of the courts further weakened law enforcement and the rule of law. Soeharto's authoritarian style also further emphasized policies and practices that limited transparency and accountability as the Indonesian state and people evolved. This included the absence of democratic institutions and a free press as well as the suppression of demonstrations and protests by citizens. Corruption, collusion, and nepotism which promoted a paternalistic crony capitalism increasingly prevailed. It led to highly concentrated ownership and conglomerate structures that further eroded integrity and values of honesty and openness. The courts were corrupted and remained even more politically submissive. The prosecutors and the police abused rights and enforcement of the law was often marginal and ineffective. The state came to be marked by 'the ruler's law' and law was manipulated to support Soeharto.

The Soeharto era ended in the Asian currency crisis and the assertion of people power to reclaim government in the reform movement which was focused both on improving the welfare of the people and honesty and accountability in public life. The entrenched values of paternalism, cronyism, government and military involvement in business that have benefited the elite have been resistant to change and have continued to provide ways to obtain power and wealth. The growing commitment to democratic values and resistance to authoritarian rule has seen conflicting approaches to honesty, transparency and corruption which continue to benefit social and economic elites. Transparency in the

media appeared under Habibie. This period also saw the beginning of extensive reforms of corporate and securities law to reflect the guidance from the IMF and other international financial bodies. Under the next president, Abdurrahman Wahid, media transparency increased and the steps were taken to create and strengthen anti-corruption agencies. These were to be returned to under Susilo Bambang Yudhoyono but in ways that were seen to protect the entrenched elite making the pervasiveness of corruption and the lack of transparency even clearer.

The most recent, and current president, Joko Widodo, found popular support for his promise of a social revolution that would eradicate corruption and create greater openness. His appointments to key official positions have tended to reveal that the network of interests is too entwined for him to be able change behaviour. He also appears unable to protect anti-corruption bodies from the elites threatened by their power to reveal their corruption. His promises to promote the impartial enforcement of the law are similarly frustrated. In some ways he represents the dilemma of the Indonesian people. Their long history has made them value integrity, openness and honesty. In conflict with those values their long history has also created a society based on patronage in which privacy and collusive relationships conceal corruption and accept the wealth it produces in the hands of individuals.

The concepts of corporate governance and disclosure and related legislation and the GCG Code transplanted into Indonesia in the reform era are also based on honesty and openness. They are discussed in the next chapter.

Chapter 5 : The challenges to disclosure in corporate governance in Indonesia context

5.1. Introduction

This chapter provides a more structured account to the challenges of corporate disclosure within the Indonesian corporate governance framework. It aims to identify potential factors that may be used to support the effectiveness of disclosure as a transplanted concept. It also describes the need for some adjustments of transplanted concepts to be suitable for local conditions.

The description and analysis is informed generally by the literature and themes investigated in the previous chapters, including specific literature about uncertainty avoidance and power distance. In particular it demonstrates how the values of Indonesia's social, economic and political culture are fundamental threats to good disclosure practices. It also considers the challenge to those practices within the framework of transplants of both hard and soft law.

The major challenges are the entrenched corrupt practices in economic and political systems that erode trust and honesty and that resist reforms to improve corporate governance and disclosure. These significantly impact on disclosure practices and not only on mandatory requirements but also on informal or soft forms of disclosure. The challenge is increased by disclosure being a foreign concept and perceived to be as such: derived from Western values and cultures, which clash with Indonesia's cultural values. The Western values reflected in disclosure concepts have different characteristics or dimensions in Indonesian economic, political and social cultures because of uncertainty avoidance and power distance. The incompatibilities between the cultural and legal ideological backgrounds of the donor jurisdictions compared with Indonesia, as the host country, are considered to contribute to the unfavourable reception of transplanted concepts and disclosure principles.

The challenges posed by corruption have significant consequences for disclosure as adopted in Indonesia as legal transplants. It is a complicated context for such legal transplants. Indonesian legal and regulatory cultures and structures, practices, the weak

observance of the rule of law and the consequences of lack of law enforcement are also contributing to this complexity. The complex context makes transplanted concepts, including disclosure, potentially less effective and also more likely to be rejected.

This chapter also provides an insight into how the transposition of the disclosure concept proceeded in Indonesia's legal and regulatory system. It attempts to describe the challenges and consequences to these transplanted disclosure concepts translated into Indonesian business discourse as indicated in Chapter 2. The pressures of economic crises and globalisation, as indicated in Chapter 1 and 3, led to the adoption of more complex concepts into Indonesian corporate regulation than previously. It could be considered an involuntary legal transplant. And that brings significant consequences for it in effectively implementing disclosure principles and other related transplanted concepts. The chapter, in doing so, also provides examples of other aspects of transplanted legal concepts that have both been challenged and accepted from a previous era of globalisation in Indonesia's reception of the Dutch civil law system.

Discussion of these issues is significant to this study with regard to mapping and analysing important challenges from disclosure to corporate governance in the contemporary Indonesian regulatory framework. This assists in the identification of issues that need to be addressed in supporting the use of the GCG Code to enhance accountability for effective disclosure. It relates to the second research sub-question regarding the aspects of Indonesian political, administrative and business cultures that can be called on to support the use of the GCG Code as an alternative regulatory instrument.

5.2. The significance of cultural and political factors

5.2.1. Introduction

Experiences from other South East Asian jurisdictions summarised in Chapter 3 provide examples of the significance of cultural and political factors in disclosure practices within corporate governance.¹¹³⁹ These jurisdictions, like Indonesia, have significant issues around concentrated ownership structures. Yet, Singapore, for example, illustrates that in

¹¹³⁹ In this context, successful corporate governance in Singapore indicated in chapter three is regarded as successful disclosure considering disclosure as a one of the crucial elements of corporate governance indicated in chapter two.

spite of such concentrated ownership structures, the anti-corruption ethos and political determination to improve corporate governance have also improved disclosure practices. This indicates that corruption affects corporate governance performance, particularly disclosure practices and the associated values of trust and honesty.

As the historical background indicated in Chapter 4, trust and honesty have been generally respected in Indonesia's main religious traditions. The openness of Indonesian people led to the welcoming of foreign arrivals and their values and beliefs, which also supported these values. Hinduism, however, left a hierarchal and stratified society as a result of its caste system. This was not eliminated by the tradition of equality within Islam, as kings and sultans used this, and authoritarian power, to establish loyalty to themselves.¹¹⁴⁰ The hierarchy extended through the social and economic elite into the agrarian highlands of these kingdoms. The pattern of paternalism and the forces of colonisation significantly changed traditional values. They transformed business practices and values with a capitalist mentality and reduced their integrity. The Japanese added practices of military influence and bribery in business to the mix, see Chapter [4.2.3]. After independence, these legacy values were preserved. Corruption, secrecy and non-transparency became entrenched. Damanhuri confirms that corruption became the 'way of life'¹¹⁴¹ including in the corporate sector.

The consequences of corruption have a fundamental impact on the integrity of the business community, political institutions and on the legal system and practices within them. As noted in Chapter 1, corruption is widely observed to erode moral integrity, to contribute to the lack of awareness and significance of the law and to lead to legal uncertainty and increasing injustice. Corruption destroys the fundamental values of honesty and trust.

With respect to disclosure, corruption is a fundamental challenge, as the values of honesty and trust are crucial elements underpinning it. The absence of trust and honesty in disclosure practices, as indicated in Chapter 2, may lead to the distribution of untruthful, deceitful and inaccurate information. Disclosure becomes a vehicle for the dissemination of

¹¹⁴⁰ See, Chapter [4.2.1].

¹¹⁴¹ Damanhuri, above n 1054.

misleading corporate information and the related accounting principles are manipulated in order to gain desired outcomes as observed by Navran and Pittman in Chapter [2.3.], included in the previous paragraph. They also note that honesty is reflected in disclosure principles. Good disclosure principles require the provision of timely, fair, and accurate information. They suggested that honesty is essential in disclosing the truth, see Chapter [2.3].

The other fundamental value is trust, which is also observed to be a critical aspect of business regulation as indicated in Chapter 2. The level of trust in the enforcement of the relevant law and in the regulation of the corporate sector determines the level of orderly compliance. Indonesia's experience reflects this. The loss of trust in the legal system due to corruption and its resulting ineffectiveness, indicated in Chapter 1 and 4, has greatly affected the level of respect for the mandatory system of disclosure. This impacts on how the business community translates required disclosure principles into practice. Trust is also significant, as it reduces transaction costs¹¹⁴² and through this creates higher levels of economic development and growth.¹¹⁴³

Trust is significant in this study in identifying factors that compromise disclosure. It is relevant to the use of GCG Code as informal law, which utilizes moral suasion for compliance with it as indicated in Chapter [2.4.3].

Boucher regarded corruption as the biggest challenge to government and companies in implementing corporate governance including disclosure.¹¹⁴⁴ Daniel observed in the Indonesia context that corruption is a crucial problem undermining corporate governance and disclosure. This is because corruption has become deeply entrenched in companies.¹¹⁴⁵

The fundamental challenges raised by corruption to disclosure in Indonesia are discussed below. They are then placed in the wider context of the pervasiveness of

¹¹⁴² Williamson and Kerekes, above n 379

¹¹⁴³ Ibid 13.

¹¹⁴⁴ Esther Samboh, Interview with Richard Boucher – OECD deputy secretary general, Good corporate governance crucial to weathering crisis, *The Jakarta Post* (online), 4 October 2011) <<http://www.thejakartapost.com/news/2011/10/04/good-corporate-governance-crucial-weathering-crisis.html>>

¹¹⁴⁵ Daniel, above n 533, 371.

corruption in Indonesia. Corruption emerges as the most significant reason for the failure of corporate disclosure regimes.

5.2.2. The effect of corruption on corporate disclosure

It is widely observed that corruption has a negative effect on disclosure within corporate governance frameworks. A number of studies demonstrate its impact. As indicated earlier, it erodes the fundamental value of trust. The impact obstructs corporate governance practices in general and disclosure in particular. Corruption impairs the efficiency and reliability of disclosure, transparency, laws and regulations, levels of compliance and investor confidence.

Corruption damages disclosure practices and confidence in them. It discourages honesty and transparency.¹¹⁴⁶ Caron suggests that high corruption levels contribute to the lack of efficient corporate governance practices in firms. Weak corporate governance practices and associated low compliance levels feed corruption and lead to transparency issues. These are critical for good disclosure practices. The information disclosed, for example, may be falsified.¹¹⁴⁷ This relates to Braithwaite's claim that management has a lack of good will to comply and a rational calculation to cheat because they do not have the competence to comply.¹¹⁴⁸ This potentially destroys trust in the reliability of any information disclosed.¹¹⁴⁹ Empirical studies indicate that corruption impacts on investors' confidence. Xun showed that corruption both reduces transparency and damages investors' interests and impaired their confidence.¹¹⁵⁰ A study by Dela Rama demonstrates how corruption discourages both internal and foreign investment. It is 'a major obstacle and disincentive to economic growth'.¹¹⁵¹

¹¹⁴⁶ dela Rama, above n 686.

¹¹⁴⁷ Michelle I Caron, Aysun Ficici and Christopher L Richter 'The influence of corruption on corporate governance standards: Shared characteristics of rapidly developing economies' (2012) 2 *Emerging Market Journal* 21, 22, 23 & 32.

¹¹⁴⁸ Braithwaite, 'Responsive Regulation and Developing Economies', above n 407, 887.

¹¹⁴⁹ Alan Waring, *Corporate risk and governance: An end to mismanagement, tunnel vision and quackery* (Gower Publishing Limited, 2013) 115.

¹¹⁵⁰ Cited in Caron, Ficici and Richter, above n 1147; See also, dela Rama, above n 686, 518.

¹¹⁵¹ dela Rama, above n 686.

Corruption renders laws and regulations on disclosure ineffective. It erodes trust and confidence in the laws and rules that govern behaviour around disclosure.¹¹⁵² It reveals their failure to demonstrate the required accountability. This also impacts on the level of respect for both formal and informal laws and related practices.

The effectiveness of the law making process is also brought into question. Immordino and Pagano suggested, as indicated in Chapter [2.2.4] that corruption affects how laws are written.¹¹⁵³ This is confirmed by Berkowitz *et al* in their findings, demonstrating that the process of law making determines the effectiveness of legal institutions.¹¹⁵⁴

Kingsley points to a significant problem in the general drafting of Indonesian law, which results in its legal-over-determination. As each law is seen to fail, further laws are added. They become more detailed. Legislation becomes more complex. This increases bureaucratic power and, in turn, creates further possibilities for corruption.¹¹⁵⁵ Brietzke points out that over-determination also results from ‘the Dutch-Indonesian passion for regulating everything in detail’ but also notes that it is ‘the source of much bureaucratic power and many bribe-opportunities.’¹¹⁵⁶

The following sub-chapter describes the extensiveness of corruption in Indonesia. Its purpose is to situate corruption as the biggest obstacle to corporate disclosure.

5.2.3. The pervasiveness of corruption in Indonesia

As indicated in Chapter 4, corruption has been a persistent phenomenon in Indonesia. Historical experiences clearly demonstrate the existence of corruption under Dutch colonisation and the Japanese occupation, in Soekarno’s Old Order regime and then, increasing and even more deeply entrenched in government and commercial institutions

¹¹⁵² *Ibid* 518.

¹¹⁵³ Millstein et al, above n 284.

¹¹⁵⁴ Berkowitz, Pistor and Richard, above n 522, 189.

¹¹⁵⁵ Jeremy J Kingsley, ‘Legal transplantation: Is this what the doctor ordered and are the blood types compatible? The application of interdisciplinary research to law reform in the developing world – A case study of corporate governance in Indonesia’ (2004) 21(2) *Arizona Journal of International & Comparative Law* 493, 508.

¹¹⁵⁶ Paul H Brietzke, ‘Governance and companies law in Indonesia’ (2000) 2(2) *Australian Journal of Asian Law* 194, 195.

during Soeharto's New Order era.¹¹⁵⁷ Soeharto seems to have further corrupted the legal system and increased the failings of the rule of law. Even after Soeharto fell, corruption has remained a persistent problem for all presidents in the reformation era.

Corruption has been observed to have increased after Soeharto's presidency. Under Soeharto's regime corruption was limited to the president's family, cronies and close associates as indicated in Chapter 4. It is now been transferred to all administrative levels. The regional autonomy (decentralisation) policy is claimed to be responsible for the widespread corruption at local levels.¹¹⁵⁸ Busyro Muqoddas, a former deputy chairman of KPK, supports this claim that corruption has expanded in Indonesian life, likening it to the recent devastating eruption of Mount Kelud.¹¹⁵⁹

Corruption has become pervasive at all levels. A number of writers confirm this. Damanhuri claims that corruption rules most of Indonesian life.¹¹⁶⁰ Others believe it rules all of Indonesian life. It is found to be systematic and structural in all state administration sectors.¹¹⁶¹ It dominates all levels of national, provincial, city, municipality and village government. Muqoddas stated that pervasive corruption persists at all levels of the executive from local to central government, as well as to legislative institutions.¹¹⁶² The chief judge of the Constitutional Court and police generals,¹¹⁶³ corruption court judges¹¹⁶⁴ as well as other well respected officials; such as chairs of audit agencies, prominent parliament members, minister of religious affairs, governors and district majors have been charged with corruption and sentenced to jail.¹¹⁶⁵

¹¹⁵⁷ Simon Butt, *Corruption and law in Indonesia* (Routledge, 2012) 12.

¹¹⁵⁸ Ibid.

¹¹⁵⁹ 'KPK: Presiden, Letusan korupsi sedahsyat letusan Kelud' [KPK: President, an explosion of corruption is similar to the devastating eruption of Kelud mountain], *Kompas* (online), 22 Februari 2014

<<http://nasional.kompas.com/read/2014/02/22/1247366/KPK.Presiden.Letusan.Korupsi.Sedahsyat.Letusan.Kelud..>>. Mount Kelud is an active volcano located in East Java, which erupted on 13 February 2014.

¹¹⁶⁰ Damanhuri, above n 1054.

¹¹⁶¹ Ibid.

¹¹⁶² 'KPK: Presiden, Letusan korupsi sedahsyat letusan Kelud', above n 1159.

¹¹⁶³ Butt, above n 1157, 9–10.

¹¹⁶⁴ Global Legal Monitor, *Indonesia: Corruption Court Judges Arrested* (23 August 2012)

<<http://www.loc.gov/law/foreign-news/article/indonesia-corruption-court-judges-arrested/>>.

¹¹⁶⁵ Butt, above n 1157.

This pervasiveness is particularly found in law and law making institutions and law enforcement and regulatory agencies. The House of Representatives [DPR], the courts and law enforcement bodies are named as the most corrupt institutions.¹¹⁶⁶ Butt specifically observed that law making and judicial institutions are amongst the most corrupt.¹¹⁶⁷ As a consequence, Indonesian courts are generally considered as ‘incapable of dealing with commercial disputes fairly and competently’.¹¹⁶⁸ Litigants, for example, can purchase favourable decisions.

A corruption case in 2013 involved the chief justice of the Constitutional Court.¹¹⁶⁹ This has been seen as reflecting the dire condition of corruption in legal enforcement and the judiciary. His long standing practice of accepting bribes for favourable decisions has been described as representing the failure of Indonesia as a state.¹¹⁷⁰ Hasibuan, for example, claims that this case demonstrates that judicial authorities have reached their lowest point.¹¹⁷¹ The *Lingkaran Survei Indonesia* (LSI) survey previously reflected that the courts had lost almost all credibility.¹¹⁷²

¹¹⁶⁶ ‘KPK: Lembaga terkorup, 1. Kepolisian, 2. DPR dan 3. Pengadilan’ [KPK: The most corrupt institutions are: 1. Police, 2. House of Representative/Parliament, and 3. Courts], *Sriwijaya Post* (online), 17 September 2013 <<http://palembang.tribunnews.com/2013/09/17/kpk-lembaga-terkorup-1-kepolisian-2-dpr-dan-3-pengadilan>>.

¹¹⁶⁷ Butt, above n 1157.

¹¹⁶⁸ Stacey Steele, ‘The new law on bankruptcy in Indonesia: Towards a modern corporate bankruptcy regime?’ (1999) 23(1) *Melbourne University Law Review* 144, 154.

¹¹⁶⁹ Yenni Kwok, ‘Top Indonesian Anti-corruption Judge Is Arrested for Graft’, *Time* (online), 4 October 2013 <<http://world.time.com/2013/10/04/arrest-of-antigraft-judge-shows-depth-of-indonesias-corruption-crisis/>>. See also, Michael Bachelard and Karuni Rompies, ‘Anti-corruption agency arrests court’s chief judge over bribe’, *The Sydney Morning Herald* (online), 4 October 2013 <<http://www.smh.com.au/world/anticorruption-agency-arrests-courts-chief-judge-over-bribe-20131003-2uxcp.html>>.

¹¹⁷⁰ ‘Ketua KPK: Dunia serasa akan runtuh’ [KPK chairman: the World seemed to collapse], *Kompas* (online), 5 Oktober 2013 <<http://nasional.kompas.com/read/2013/10/05/1248346/Ketua.KPK.Dunia.Serasa.Akan.Runtuh>>.

¹¹⁷¹ ‘Wantimpres: Ketua MK ditangkap, wibawa hukum di titik nadir’ [Wantimpres: Chief justice of MK was arrested, the law’s image is at its lowest point], *Kompas* (online), 3 Oktober 2013 <<http://nasional.kompas.com/read/2013/10/03/1627554/Wantimpres.Ketua.MK.Ditangkap.Wibawa.Hukum.di.Titik.Nadir>>. Albert Hasibuan is a member of Dewan Pertimbangan Presiden (Wantimpres) [Presidential Advisory Board] in legal and human rights affairs.

¹¹⁷² ‘Wibawa hukum terpuruk, Ini komentar presiden’ [The law’s image severely collapses, here a comment from the president], *Kompas* (online), 8 April 2013 <<http://nasional.kompas.com/read/2013/04/08/22422345/Wibawa.Hukum.Terpuruk..Ini.Komentar.Presiden>>.

In spite of a number of anti corruption reforms, including legislation and anti corruption institutions and other working groups across many sectors, corruption has not been reduced.¹¹⁷³

The persistence of corruption has been attributed to a number of factors. They are ineffectiveness of anti-corruption bodies, weakness of state control, loopholes in anti-corruption laws, the power of corrupt law making institutions over the anti-corruption bodies, and resistance to the power of anti corruption bodies.

Indonesia has enacted the Anti-Corruption Law No. 20 of 2001 but it appears ineffective. The country also ratified the United Nations Convention against Corruption in 2003. The Anti-Corruption Court (ACC) has massive support from reformist groups and the public,¹¹⁷⁴ but corruption is still growing.¹¹⁷⁵ This may relate to the fact that the KPK seems to target only big cases. Butt observes ‘the KPK and ACC [Anti Corruption Court] handle only a very small proportion of corruption cases; most are still handled by ordinary law enforcement institutions’.¹¹⁷⁶ These other law enforcement institutions handling corruption cases are ‘widely considered to be highly corrupt’.¹¹⁷⁷ As a consequence, law enforcement is observed to be generally poor. Law enforcement is undermined by those who are in power and also by rivalry between law enforcement agencies.¹¹⁷⁸ The lack of law enforcement is claimed to be the main weakness in eradicating corruption.¹¹⁷⁹

¹¹⁷³ Butt, above n 1157, 1. The study on corruption cases ‘from its early successes in relatively minor corruption cases, to its consolidation up to 2007, and its emboldening from 2008’.

¹¹⁷⁴ Ibid 9.

¹¹⁷⁵ Ibid 10.

¹¹⁷⁶ The ACC is Anti Corruption Court [*Pengadilan Tindak Pidana Korupsi*], which was established under the Law No. 46 of 2009 concerning Anti Corruption Court [Undang-undang No. 46 Tahun 2009 tentang Pengadilan Tindak Pidana Korupsi]. It is Indonesia’s special court for corruption crimes in Jakarta. See, Butt, above n 1157; Sofie Arjon Schutte and Simon Butt, *The Indonesian Court for Corruption Crimes: Circumventing judicial impropriety* (September 2013) Anti-Corruption Resource Centre <<http://www.u4.no/publications/the-indonesian-court-for-corruption-crimes-circumventing-judicial-impropriety/>>.

¹¹⁷⁷ Butt, above n 1157, 15.

¹¹⁷⁸ Laksono Hari Wiwoho, *Hukum Indonesia masih akan karut-marut? [Will Indonesian laws still chaos?]* Report of Perhimpunan Advokat Indonesia- Peradi [Indonesian Advocaat Association] Discussion on ‘Quo Vadis penegakan hukum di Indonesia?’ [Quo Vadis law enforcement in Indonesia?], *Kompas* (online) 20 October 2009 [3]-[4] <http://ads.kompas.com/www/delivery/ck.php?n=a8942f6b&cb=INSERT_RANDOM_NUMBER_HERE></img

The weakness of state control of bureaucrats is also pointed to as a cause for the persistence of corruption that has weakened the rule of law and has attributed to the spread of corruption.¹¹⁸⁰ Butt considered this to be Soeharto's enduring legacy and one that reforming presidents have been unable to dislodge.¹¹⁸¹

Butt also points to some other potential factors impeding the eradication of corruption. Anti-corruption law contains provisions and loopholes that are used by defendants to hinder KPK investigations and prosecutions and Anti Corruption Court (ACC) [*Pengadilan Tindak Pidana Korupsi*] trials. It is argued that the power of the KPK to eradicate corruption in the future is uncertain.¹¹⁸²

Parliament – considered one of the most corrupt institutions – holds significant trump cards. It 'has, and always will have, the legislative power to alter, and even close down, both the KPK and the ACC. It also controls the KPK's budget.'¹¹⁸³ Butt sees the absence of provincial offices of the KPK as another factor.¹¹⁸⁴

Government officials including members of the executive, legislative and judicial institutions have demonstrated strong resistance to the KPK's power.¹¹⁸⁵ The requirement for approval from the Communications and Information Ministry for wiretaps, other amendments to the KPK and ACC laws and other parliamentary interference are considered to reflect clear efforts to weaken the KPK's power.¹¹⁸⁶ Chapter 4 referred to this in describing the measure in the reform era by prosecutors to reduce corruption, see Chapter [4.3.4.]. The weakening of the KPK's power still continues under president Jokowi.

To address corruption, Indonesia may need to seriously consider a number of suggestions made by scholars and experts. Krishnamurthy et al suggest that good corporate

src='http://ads.kompas.com/www/delivery/avw.php?zoneid=407&cb=INSERT_RANDOM_NUMBER_HERE&n=a8942f6b' border='0' alt=" />

¹¹⁷⁹ But, above n 1157, 14.

¹¹⁸⁰ Caron, Ficici and Richter, above n 1147.

¹¹⁸¹ Butt, above n 1157, 1.

¹¹⁸² Ibid 117.

¹¹⁸³ Ibid 126.

¹¹⁸⁴ Ibid 121.

¹¹⁸⁵ Ibid 1.

¹¹⁸⁶ Ibid 121–4.

governance itself assists in preventing corruption, or at very last, limits its negative effects.¹¹⁸⁷ It is considered that it promotes ‘honest and responsible behaviour, and adheres its practices to the letter and the spirit of the law. Collectively, these are the antithesis of corruption’.¹¹⁸⁸ Caron et al observed that reducing corruption is the best way to safeguard foreign direct investment as well as effective and efficient corporate governance.¹¹⁸⁹

In fact, Indonesian social and cultural values have further contributed to the creation of corrupt practices. Those relevant values and their impact on disclosure and the use of soft law are discussed below.

5.2.4. The cultural values that perpetuate corrupt practices impact on the use of soft law

There are a number of values and practices persisting in the Indonesian community that continue to further entrench corrupt practices. Trust is a basic value in business and commercial activities as it is elsewhere. Patience becomes a highly important element in this context to develop the relationship for establishing trust.¹¹⁹⁰ Relationships are the pivotal factor for access to opportunities and success. Family connections and ethnic ties are significant factors in establishing possible business relationships. This is based on a general feeling of moral obligation to the extended family and to members of the same ethnic group. Who you know, is often more important than what you know. A foreign company, for example, may need reliable local partners to act as intermediaries in gaining access to other business people. Their connections with government officials and politicians may contribute significantly to extending future contracts and favours.¹¹⁹¹ These types of corrupt patron-client relationships have contributed to the failure of the implementation of

¹¹⁸⁷ Prabhakar Krishnamurthy, D Rangaswamy and C Prabhakaran, *Impact of corruption on corporate governance-An overview under the context of policy framework against corporate corruption* (3 September 2011) 5 <<http://ssrn.com/abstract=1937733>>.

¹¹⁸⁸ Ibid.

¹¹⁸⁹ Caron, Ficici and Richter, above n 1147, 34.

¹¹⁹⁰ Sihar Sitorus and Pawan S Budhwar, ‘Doing business in Indonesia’ (2003) 45(5) *Thunderbird International Business Review* 587.

¹¹⁹¹ Ibid 606.

sound corporate governance standards including disclosure.¹¹⁹² They have created a corrupt system of corporate governance.

Corrupt practices have significantly eroded other values in respect to reputation and social standing. These values are observed to be significant factors for the effective use of informal or soft law associated with informal sanctions as indicated in Chapter [2.4.3]. This is significant for this investigation into the use of good corporate governance codes as informal law. Those values rest on the concept of saving face.¹¹⁹³ In business culture, it is called *malu*, literally, *embarrassment* or *shame*. *Budaya rasa malu* [shame culture, or the culture of feeling guilty] refers to the loss of face [*kehilangan muka*]. Loss of face is ‘more than simple embarrassment’. It is also known as social shame.¹¹⁹⁴ Loss of face is an external concept. It is the fear or anxiety of losing one’s good reputation and the respect of others. Social shame is an internal idea. It is the inner feeling of being ashamed because of one’s actions.¹¹⁹⁵ The erosion of this culture of shame and lack of face is related to the ineffectiveness of informal sanction.

5.2.5. The fragility of political institutions and consequences

Fragile political institutions are also observed to have negative consequences in relation to good corporate governance in general and good disclosure in particular. They are considered to be significant obstacles to the use of principles such as transparency, honesty and accountability, which have not been widely applied in Indonesia.¹¹⁹⁶ High profile company scandals are often settled by a political compromise rather than legal action and sanctions.¹¹⁹⁷ Political interferences in firms discourage them from being transparent.

¹¹⁹² See, eg, Piers Gillespie, ‘The challenges of corporate governance in Indonesian oil palm: Opportunities to move beyond legalism?’ (2012) 36 *Asian Studies Review* 247, 262–3. A study of the Indonesian palm oil industry demonstrated critical issues including the failure of the implementation of sound corporate governance standards and ‘the development of corrupt patron-client relations between officials and plantations’ as one of a number identified issue.

¹¹⁹³ Sitorus and Budhwar, above n 1190.

¹¹⁹⁴ George B Whitfield, *Business across cultures: From face to shame*, [8] <<http://www.expatriate.or.id/business/facetoshame.html>>.

¹¹⁹⁵ Ibid [9]–[10].

¹¹⁹⁶ Akuntan Indonesia, ‘GCG BUMN Implementasi belum optimal [Implementation of GCG in SOEs has not optimized yet]’ *Akuntan Indonesia*, Edition no,1/Tahun I/Agustus 2007, 12 <http://74.220.207.194/~iaigloba/storage/ref_14.pdf>.

¹¹⁹⁷ Ibid 12.

The involvement of political institutions is seen to produce partisan policies to benefit interest groups. It may confirm Cerny's view that the architecture of these politics means that domestic governance has been shaped by institutional arrangements.¹¹⁹⁸

In all jurisdictions, elements of politics including interests, institutions, and political conflict are in play¹¹⁹⁹ shaping corporate governance and disclosure. Political variables have shaped corporate governance disclosure rules as political processes set the rules. Interest group preferences (alliances of owners, managers and workers) and formal institutions for preference aggregation (decision by majority and consensus) are basic ways to accommodate political variables.¹²⁰⁰ Tanter showed that a degree of dependence on external political and economic pre-conditions was, and is, fundamental in Indonesia policy and law making.¹²⁰¹

Political institutions are 'the machinery that refracts the preferences and that aggregates them into policy outcomes.'¹²⁰² The importance of politics can be seen in policies and laws that make for legal protections and for market structures. The policy derives from 'decisions made in the political process: laws passed, law enforced, regulations applied, court sheltered from corruption – all deeply political variables'.¹²⁰³ Gourevitch and Shinn observed that:

corporate governance structures are fundamentally the result of political decisions. Corporate governance systems [including disclosure] reflect policy choices. They are shaped by a mixture of laws, rules, regulations, and the degree of their enforcement.¹²⁰⁴

Laws express the outcomes of a political process – a broad political bargain among the relevant elites contesting a variety of policies that influence incentives.¹²⁰⁵ The shape of the present political institutions within Indonesia, have been mainly influenced by two former presidents: Soekarno and Soeharto. Soekarno, with his guided democracy policy in

¹¹⁹⁸ Cited in J Pierre, *Globalisation and governance* (Edward Elgar Publishing, 2013) 1.

¹¹⁹⁹ Peter A Gourevitch and James Shinn, *Political power & corporate control – The new global politics of corporate governance* (Princeton University Press, 2005) 2.

¹²⁰⁰ *Ibid* 57–8.

¹²⁰¹ Richard Tanter, 'Indonesian politics after Suharto' (1998) 11 *Arena Journal* 7, 8.

¹²⁰² Gourevitch and Shinn, above n 1199, 8.

¹²⁰³ *Ibid* 55.

¹²⁰⁴ *Ibid* 3.

¹²⁰⁵ *Ibid* 8.

the old order diminished the authority of political parties as they ‘were seen as a serious threat to presidential power’.¹²⁰⁶ On the other hand, political parties in the new order era were fully controlled by Soeharto who ‘manipulated the party system to enhance his personal power’.¹²⁰⁷ Political parties became ineffective and were ‘perceived as incompetent and dysfunctional’.¹²⁰⁸ The relationship between government and citizens became very limited. Participation in formal politics only involved a handful of people.¹²⁰⁹

After Soeharto’s fall, the freedom to operate openly and compete amongst political parties has emerged. Unfortunately, the level of trust in Indonesian political parties is low as they are perceived to have failed to play meaningful roles in the democratic process. In particular, the legacy parties have failed to demonstrate a capacity to lead significant changes.¹²¹⁰

The decades under Soekarno and Soeharto have further established corruption, as indicated earlier. It has been money politics that has shaped the fragile political parties in the reform era. It was outlined that political parties, especially the elites of the party in government, benefit from corruption as the enforcement of accountability does not exist.¹²¹¹ Others have also observed that leaders’ personalities and charisma are important influences, which ignore political organisations and their processes.¹²¹² Patronage and money politics have become obstructions to the establishment of more credible and transparent parties.¹²¹³

Undemocratic practices have been seen to remain strong in the reform era¹²¹⁴ reflecting an absence of strong democratic values. Choi points to the danger of the undemocratic consolidation of parties and political power. Their guiding rules appear to be democratic, ‘but the substance of the system – those practices that have become habitual –

¹²⁰⁶ Ulla Fiona, *The institutionalization of political parties in post-authoritarian Indonesia: From the grass-roots up* (Amsterdam University Press, 2013) 13.

¹²⁰⁷ *Ibid.*

¹²⁰⁸ *Ibid* 13–14.

¹²⁰⁹ *Ibid.*

¹²¹⁰ *Ibid.*

¹²¹¹ *Ibid* 201.

¹²¹² *Ibid.*

¹²¹³ *Ibid.*

¹²¹⁴ *Ibid.*

is far from democratic'.¹²¹⁵ Hadiz has observed the establishment of illiberal forms of democracy in Indonesia. The continuing condition of corrupt lower level officials and the political henchmen and thugs from the period before the reform era, demonstrates the contradictions in the democracy of the new period. The continuation of the unfair accumulation of wealth from the new order era also still persists.¹²¹⁶

Significant evidence demonstrates the strong connection with political interference and business institutions. Banking is attributed with having contributed significantly to the financial crisis of 1997–98 in Indonesia. The accumulation of huge unsecured loans, which established the entire financial system, was based largely on political recommendations and favours.¹²¹⁷

State Owned Enterprises (SOEs) are seen to have been often subject to intervention in the interests of political parties. They have become a well-established place for corruption, collusion and nepotism. The commitment to the improvement of good corporate governance in all state-owned enterprises (SOEs) was clearly articulated,¹²¹⁸ with a hope that it may lead to better performances not only for SOEs but also other institutions of the government and the judiciary. However, political interference and lack of transparency remained significant issues for SOEs.¹²¹⁹

Kamal observes that the business activities of Indonesian SOEs are potentially still disrupted by political interference from members of the Indonesian parliament (DPR). This creates 'opportunities for inappropriate political deals between parliament members and the SOE's management'.¹²²⁰ As indicated earlier, parliament has been well known as one of the most corrupt institutions.

¹²¹⁵ Cited in Fiona, *ibid* 202.

¹²¹⁶ Cited in Fiona, *ibid*.

¹²¹⁷ Petra Mahy, 'The evolution of company law in Indonesia: An exploration of legal innovation and stagnation' (2013) 16(1) *American Journal of Comparative Law* 377, 413.

¹²¹⁸ Akuntan Indonesia, 'GCG BUMN Implementasi belum optimal', above n 1196, 11. The commitment was declared by the Minister for state-owned company affairs, Sofyan Djalil, in 2007.

¹²¹⁹ *Ibid* 12.

¹²²⁰ Miko Kamal, 'Dealing with the principles dilemma: a proposal for the governance of Indonesia's state-owned enterprises' (2010) *Law Asia Journal* 155, 175.

Bedner states that ‘political interference led to a sharp rise in judicial corruption and a general decline in its standards and morals’ during the new order regime’.¹²²¹ It persists, as Lindsey notes, in the political power and factors that have paralysed the *kejaksaan* [public prosecution]. It is seen in the confusion of the roles and authority of the attorney general, which has essentially been a political role, and the public prosecutor, who must be seen to be independent to be effective, demonstrating impartial technical legal skills rather than political skills.¹²²²

Good corporate governance practices have been seen as the most powerful way of avoiding any kind of self interested political intervention in state-owned companies.¹²²³ In particular, disclosure may be an effective tool to prevent these unwarranted outside interferences. Corporate governance, including appropriate disclosure, however, remains a foreign concept that raises significant issues as discussed below.

5.3. Disclosure in a corporate governance framework as a foreign concept

5.3.1. Introduction

As indicated earlier in Chapter 3, globalisation has shaped a convergence in standards of corporate governance leading to the global adoption of particular principles. Good corporate governance, adopted globally, is seen to lead to the flow of finance capital between countries particularly within multinational companies. It has led to the establishment of governance standards, which apply norms developed in Western economies and jurisdictions.¹²²⁴

Hansmann and Kraakman argued that the most effective corporate law and governance is seen in the US model, which emphasizes shareholder value maximization.¹²²⁵ They argued that this was a driving principle in the convergence of corporate law. The US framework sets shareholder value maximization as the company’s

¹²²¹ Bedner, ‘Indonesian legal scholarship and jurisprudence as an obstacle for transplanting legal institutions’, above n 523, 259.

¹²²² Lindsey, ‘Legal infrastructure and governance reform post-crisis Asia: The case of Indonesia’, above n 553, 26. Pressure on prosecution to prosecute prominent members of the New Order elite for crimes of a public nature has become very hard for the Kejaksaan.

¹²²³ Akuntan Indonesia, above n 1196, 12.

¹²²⁴ Davies, above n 524, 79. In fact, this pattern has changed in recent years where finance capital is increasingly coming from the Middle East and Asia.

¹²²⁵ Hansmann and Kraakman in Yuka, above n 539.

ultimate goal.¹²²⁶ Farrar supports this claim in his reference to corporate governance ‘as perceived by the Anglo-American model’.¹²²⁷

The US style of corporate governance is not seen so favourably by others. Hill observed that many view the convergence thesis as code for the global Westernisation or Americanisation of corporate law and governance.¹²²⁸ This can be seen from Mooney’s and Evans’s definition of Americanisation, that it:

has a particular meaning with regard to globalization in that it encompasses anything from an alleged cultural imperialism by the United States, to stimulating changes in local patterns of behaviour and consumption of the dominance of free-market economics.¹²²⁹

Leading international development agencies have played a significant role in shaping the convergence in corporate governance. They have actively promoted laws, which are based on US models.¹²³⁰ The OECD, for example, has developed global standards of corporate governance derived from them. Its model of corporate governance codes has been adopted, or transplanted internationally¹²³¹ including in Indonesia as discussed in Chapter [3.2]. The Indonesian 2006 Code of Good Corporate Governance was updated to reflect these OECD endorsed good corporate governance principles.¹²³²

The adoption of the US style corporate governance, as indicated earlier, raises an issue of its applicability in Indonesia. Corporate governance is considered to be a foreign idea based on Western models, which do not conform to Indonesia’s legal system or its social and cultural characteristics. Indonesia, like all developing economies, is also not an OECD member and has not been involved in establishing those principles to accommodate its conditions or interests. As Ramsay indicates there needs to be an appropriate adjustment

¹²²⁶ Hansmaan and Kraakman in Yuka, above n 539, 6884.

¹²²⁷ John H Farrar, ‘Developing corporate governance in greater China’ (2002) 29; (2002) 25(2) *University of New South Wales Law Journal*, [4] <<http://www.austlii.edu.au/au/journals/UNSWLJ/2002/29.html>>. It consists of a system of legal rules supplemented by systems of self regulation (such as listing rules, statement of accounting practices, institutional codes of self regulation and codes of individual companies).

¹²²⁸ Hill, above n 534.

¹²²⁹ Annabelle Mooney and Betsy Evans (eds), *Globalization: The key concepts* (Routledge, 2007)

4.

¹²³⁰ Yuka, above n 539.

¹²³¹ Ibid.

¹²³² Mahy, above n 1217, 414.

of foreign concepts into a local context. Numerous factors need to be addressed in these adjustments including local business, regulatory, legal cultures and the function of ownership structures, as well as business circumstances, competitive conditions, and corporate life cycles.¹²³³ Among those factors, local cultures, particularly in the context of legal transplants, are important. They are a focus of discussions in this chapter, given the significant cultural factors that have been given in the literature reviewed.

Most Indonesians share a common view that Western culture has had a negative influence on the nation. There are a number of reasons for this perception. It is also recognised that there are different foundations underlying western culture compared to Indonesian beliefs, such as individualism opposed to collectivistic values, indicated below at sub-section [5.3.3]. There are contradictory aspects when comparing Indonesian and Western cultural fundamentals that affect corporate governance and its implementation, as discussed below.

5.3.2. The clash of cultural foundations

The dimensions of Indonesian culture, as discussed in Chapter 4, are marked by collectivism, strong uncertainty avoidance, and high power distance. These values have apparently placed the country in a position of low performance in corporate disclosure practices. These dimensions are directly contradictory to the cultural values of the countries of origin of the corporate governance disclosure principles seen in the GCG Code. This may explain why the implementation of the transplanted international principles of corporate governance in the GCG Code in Indonesia has not been effective.

Research indicates that national cultures usually represent the values and practices of the dominant groups in society, and not of the marginalized, whether the marginalized groups represent a majority or a minority in that society.¹²³⁴ Hofstede introduced four dimensions in comparing national cultures, ie, power distance (the less powerful members of organizations and institutions including the family accept and expect that power is distributed unequally), uncertainty avoidance (a societal tolerance for uncertainty and

¹²³³ Ramsay, above n 273.

¹²³⁴ Bryan W Husted, 'Globalization and cultural change in international business research' (2003) 9(4) *Journal of International Management* 427, 428.

ambiguity), individualism (the opposite to collectivism) and masculinity (the opposite to femininity).¹²³⁵

It is claimed that aspects of culture have constitutive and regulatory effects. They shape economic behaviour in the way of ‘guiding relative valuations, categorizations and understandings of economic processes and outcomes, which are passed through the generations’ as well as the manifestation of values and beliefs through social norms and attitudes.¹²³⁶

Cultural factors, as indicated earlier, are widely acknowledged in the literature indicated in Chapter [2.2.4] as one of the determining factors for the significant effectiveness of corporate governance. Iu and Batten, for example, argued that manifestations of culture will challenge the implementation of governance principles. They claimed, in particular, that cultural factors will affect the implementation of universal governance principles at the national level. They contend that the nature of universal applicability of the principles does not assure their successful application. The difficulty in reform lies in the principles’ implementation rather than in their development as adequate standards.¹²³⁷

Particularly in corporate disclosure, culture is a significant factor in determining disclosure levels as indicated by a number of scholars. Vincenzo, Gray and Hofstede among others suggest the influence of culture on corporate disclosure. Hope also concluded that culture affects corporate disclosure and considers it as a valid determinant of adequate disclosure, see Chapter 2.2.4.

5.3.2.1. Relevant cultural differences

The influences of national cultural dimensions, as described by Hofstede, are suggested by a number of other studies. They, however, are contested by Jaggi and Low. In considering legal systems and related legal culture, Jaggi and Low indicated, as noted in

¹²³⁵ Hofstede and Hofstede, above n 277.

¹²³⁶ de Soysa and Jutting, above n 449, 2.

¹²³⁷ Iu and Batten, above n 276.

Chapter 3 the insignificant influence of cultural factors in some common law countries.¹²³⁸ One reason for this may be that the standards are based on standards already found in common law systems and their legal cultures.

Hofstede's study, as indicated in Chapter [2.2.4] and above in sub-section [5.3.2.], concluded that cultural differences determined the levels of corporate disclosure. Zarzeski, in 1996, also suggested that higher levels of information disclosure were found in more individualistic cultures with low uncertainty avoidance. That study associated the secretive nature of a culture directly with the level of local disclosure and accounting practices.¹²³⁹

Some other studies particularly emphasized that the individualistic dimension of a culture contributed to the level of disclosure. The research indicated earlier in Chapter [2.2.4] demonstrated that a higher level of disclosure is more likely to be established in individualistic cultures than in collectivistic ones. As such, the higher the scores for individualism the greater pressure for disclosure. It has been claimed that these individualistic societies 'demand accountability and require extensive disclosure relative to collectivist societies'.¹²⁴⁰ It can be seen from the characteristics of a collectivistic culture in which people:

behave according to social norms that are designed to maintain social harmony among members of an in-group[,], consider implications of their actions for the wider collective[,], share resources and are prepared to sacrifice personal interest for collective interests[,], favour certain in-groups ...[,], belong to a small number of in-groups that influence their lives and have a greater tendency toward conformity than individualists[,], are very concerned about in-group members and are indifferent or hostile toward out-group members[,], and, emphasize hierarchy and harmony within group[and] regulate behaviour through group norms.¹²⁴¹

¹²³⁸ Bikki Jaggi and Pek Yee Low, 'Impact of Culture, Market Forces, and Legal System on Financial Disclosure' (2000) 35(4) *International Journal of Accounting* 495, 496 <<http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.466.9833&rep=rep1&type=pdf>>.

¹²³⁹ Nigel Finch, *Towards an understanding of cultural influence on the international practice of accounting*, Academic and Business Research Institute, 4 <<http://www.aabri.com/manuscripts/09175.pdf>>.

¹²⁴⁰ Nazh Hosal Akman, 'The effect of IFRS adoption on financial disclosure: Does culture still play a role?' (2011) 1(1) *American International Journal of Contemporary Research* 6, 8 <http://www.aijcrnet.com/journals/Vol._1_No.1_July_2011/2.pdf>.

¹²⁴¹ University of San Diego, *Hofstede's 5 dimensions*, 2 <<http://home.sandiego.edu/~dimon/CulturalFrameworks.pdf>>.

Collectivism is a basic value and characteristic of Indonesian culture.¹²⁴² The group prevails over individuals in its business culture. The group subsumes individual identity. In public, praise or criticism of individuals must be avoided.¹²⁴³ Collectivist values, which place priority of the group over the individual, are in the interests of individuals who exercise power over these groups.¹²⁴⁴ It can be seen in the economic ideology reflected in the 1945 Constitution which ‘concentrated power in the hands of the executive and its drafters explicitly rejected the inclusion of individual rights’.¹²⁴⁵ It portrayed collectivist ideals, reflecting modes of social organization of Indonesian village life.¹²⁴⁶ Based on this grounding in collectivist values, Indonesia fits into a pattern where there is a low pressure to disclose and a low quality of information disclosed. Gray reinforces this point in his claim that secrecy, which is characterized by restrictions on information disclosure, is a collectivist preference and that secrecy is linked to the high level of two other cultural dimensions of uncertainty avoidance and power distance.¹²⁴⁷

(a) *Uncertainty avoidance*

Uncertainty avoidance reflects cultural values in business and other activities.¹²⁴⁸ Hofstede and Bond relate uncertainty avoidance with ‘man’s search for the Truth’.¹²⁴⁹ They define it as ‘the extent to which people feel threatened by ambiguous situations, and have created beliefs and institutions that try to avoid these’.¹²⁵⁰ It is related to ‘the degree to which members of a society are able to cope with the uncertainty of the future without

¹²⁴² Sitorus and Budhwar, above n 1190.

¹²⁴³ Ibid 606.

¹²⁴⁴ Husted, above n 1234.

¹²⁴⁵ Mahy, above n 1217, 398.

¹²⁴⁶ Ibid 400. The provision of the 1945 Constitution stipulates that ‘economic affairs are to be organized as a joint effort based on the family principle (*asas kekeluargaan*)’ attributed to the first Vice-President Muhammad Hatta who championed cooperatives and collectivist ideals for an economic primary base.

¹²⁴⁷ Gray, above n 278, 11.

¹²⁴⁸ University of San Diego, above n 1241, 1.

¹²⁴⁹ Geert Hofstede and Michael Harris Bond, ‘The Confucius connection: From cultural roots to economic growth’ (1988) 16(4) *Organizational Dynamics* 5, 11.

¹²⁵⁰ Geert Hofstede and Michael H Bond, ‘Hofstede’s culture dimensions: An independent validation using Rokeach’s value survey’ (1984) 15 *Journal of Cross-Cultural Psychology* 417, 419.

experiencing undue stress'.¹²⁵¹ Western values are characterised by weak uncertainty avoidance including 'risk taking[,] tolerance of differing behaviours and opinions[,] flexibility[,] organizations with a relatively low degree of structure and few rules [,] and promotions based on merits'.¹²⁵²

These contrast with the strong uncertainty avoidance found in Indonesia, which is characterized by:

avoidance of risk[,] organizations that have clearly delineated structures, many written rules, standardized procedures, promotions based on seniority or age[,] lack of tolerance for deviants[,] strong need for consensus[,] need for predictability hence, planning is important[,] respect for authority.¹²⁵³

The high uncertainty avoidance characteristics of Indonesia can be seen in several basic local values. For example, uncertainty avoidance underlies the basic value of conflict avoidance, locally known as *harmony kelompok* [group harmony]. The appearance of harmony is maintained by most Indonesians at all costs. There is a preference for using 'the conflict resolution strategy of "denial" to maintain the appearance of harmony rather than risk even the possibility of confrontation'.¹²⁵⁴ It is prudent and polite to say 'yes' when in fact meaning 'no' to avoid conflict. It is believed that a negative response will invite conflict.¹²⁵⁵ A positive response may bring a calm and controlling influence to bear. However, this approach may also represent passive attitudes, the avoidance of issues and duplicity.¹²⁵⁶

Its characteristics also relate to typical Indonesian beliefs about the essential unity of society. Tranquillity, harmony, stability, acceptance, the subordination of the individual to wider society and of society to the universe are the basis of nature and society. Religious

¹²⁵¹ University of San Diego, above n 1241.

¹²⁵² Ibid; See also, Hofstede and Bond, 'The Confucius connection: From cultural roots to economic growth', above n 1249, 11.

¹²⁵³ Ibid.

¹²⁵⁴ Living in Indonesia, *Doing business in Indonesia – Cross cultural understanding – The Indonesian big five: Part II Conflicts of nature*, a site for expatriates, [3], [5] <<http://www.expatriates.or.id/business/bigfive-conflicts-of-nature.html>>.

¹²⁵⁵ Goodfellow, above n 902, 99.

¹²⁵⁶ Living in Indonesia, *Doing business in Indonesia – Cross cultural understanding*, above n 1254, [10].

experiences are reflected in living in harmony with a universal order. Polite, non confrontational, customs and etiquette regulate interpersonal relations.¹²⁵⁷

The level of uncertainty avoidance is observed to influence disclosure practices. Societies with strong uncertainty avoidance tend to be more conservative and secret in disclosing information, including corporate annual reports. They tend to focus on the precise requirements of the laws and rules. The strict limits of disclosure requirements are observed leaving little ground for innovation and experimentation in disclosure.¹²⁵⁸ Weak uncertainty avoidance societies, on the other hand, appear to be more innovative in terms of the information requirements of their stock exchanges and the information disclosed.¹²⁵⁹

The influences of the dimension of the uncertainty avoidance dimension on disclosure practices are clearly described by Gray. It is linked to a country's accounting subculture¹²⁶⁰ and to the four dimensions of accounting values. They are professionalism versus statutory control (a preference of individual professional judgment and the maintenance of professional self-regulation as opposed to compliance with prescriptive legal requirements and statutory control), uniformity versus flexibility (a preference for the enforcement of uniform accounting practices between companies and for the consistent use of such practices over time as opposed to flexibility in accordance with the perceived circumstances of individual companies), conservatism versus optimism (a preference for a cautious approach to measurement to cope with the uncertainty of future events opposed to a more optimistic, laissez-faire, risk-taking approach); and, secrecy versus transparency (a preference for confidentiality and the restriction of disclosure of information about business only to those who are closely involved with its management and financing as opposed to a more transparent, open and publicly accountable approach).¹²⁶¹ A preference for secrecy is associated with strong uncertainty avoidance, which restricts information disclosure in

¹²⁵⁷ Sitorus and Budhwar, above n 1190, 604.

¹²⁵⁸ Ahmed Riahi-Belkaoui, *The cultural shaping of accounting* (Greenwood Publication Group, 1995) 122.

¹²⁵⁹ Ibid.

¹²⁶⁰ Gray used the word 'subculture' referred for the use for the level of an organization, profession or family. Culture is used for societies as a whole, or nation. See, Gray, above n 278, 4 < <http://www.acis.pamplin.vt.edu/faculty/tegarden/5034/handouts/Gray-Abacus-1988.pdf>>.

¹²⁶¹ Gray, above n 278.

order to avoid conflict and competition and to preserve security.¹²⁶² Conservatism versus optimism and secrecy versus transparency were two values associated with ‘the measurement and disclosure of accounting information at a country level’. The other two values include professionalism versus statutory control and uniformity versus conformity, which were related to authority and the enforcement of accounting practices.¹²⁶³

(b) Hierarchy and power differences

Power distance has also been observed to be associated with disclosure practices. Gray related power distance to a preference for secrecy together with other societal values such as uncertainty avoidance as indicated above. It was argued that societies with high power distances place more restriction on information to preserve those power inequalities.¹²⁶⁴ An empirical study by Christopher and Hassan also suggested that a jurisdiction with a large power distance provides less disclosure of information in corporate governance statements than in jurisdictions with a small power distance.¹²⁶⁵ Sudarwan’s and Fogarty’s study of Indonesia in 1996 demonstrated ‘a significant positive relationship between power distance and both conservatism and uniformity’.¹²⁶⁶ Their study indicated that ‘change of accounting values related to the change in power distance in Indonesia’s context.’¹²⁶⁷

Indonesia is typical of large power distance societies as described by Hofstede and Bond. They defined power distance as ‘the extent to which the less powerful members of organizations and institutions (like the family) accept and expect that power is distributed unequally’.¹²⁶⁸ Centralized authority, autocratic leadership, paternalistic management styles, hierarchical layers, large numbers of supervisory staff, acceptance that power brings privileges, expectation of inequalities and differences in power are the characteristics of

¹²⁶² Ibid 11.

¹²⁶³ Finch, above n, 1239, 2.

¹²⁶⁴ Gray, above n 278, 11.

¹²⁶⁵ Their study on Malaysia Airlines represented a large power distance country and Australia Qantas Airlines represented a small power distance country. See, Christopher and Hassan, above n 642, Abstract.

¹²⁶⁶ Finch, above n 1239, 3.

¹²⁶⁷ Ibid.

¹²⁶⁸ Hofstede and Bond, ‘The Confucius connection, From cultural roots to economic growth’, above n 1249, 10; Hofstede and Bond, ‘Hofstede’s culture dimensions’, above n 1250, 430.

high power distance.¹²⁶⁹ The cultural values of high power distance tend to support the interests of the ruling class in a society.¹²⁷⁰ These characteristics meet Indonesia's condition as it is a typically large power distance society. They appear to be a significant part of the local paternalism and hierarchy.

Indonesian business culture is hierarchical. Leadership is assumed by the oldest or most competent person. Status is accorded by age, seniority, or military rank. Superiors are expected to be paternalistic¹²⁷¹ with a patronage system as a basic value. The vertical axis in human relationships in the firm becomes the main focus, as opposed to the horizontal axis in cultures marked by individualism and egalitarianism.¹²⁷² As indicated in Chapter [4.2.2.2], paternalism is a legacy of both traditional culture and Dutch colonisation that is based on the individualism of the patron who, it is accepted, will manage a firm's affair in an egocentric manner. However, this is in conflict with other Indonesian values present in its economic system, which is based on collectivism, as indicated earlier.

The incompatibility of these cultural dimensions, based on uncertainty avoidance and power distance with the requirements of good corporate governance, appear to be significant factors resulting in the failure to observe good corporate disclosure practices. The concept of disclosure in corporate governance is a legal transplant. The transposition of foreign disclosure concepts into the framework of Indonesian law and regulation will be discussed below.

5.4. The transposition of international disclosure principles to an Indonesia context

5.4.1. Economic crisis as a driving force to corporate governance transposition

The transplantation of concepts of Western disclosure in corporate governance in south East Asia intensified after the severe economic crisis in 1997. The transposition of the concept is consistent with the observations on legal transplants by some scholars indicated in Chapter [2.6.3]. Among others, Watson suggested the use of legal transplants

¹²⁶⁹ University of San Diego, above n 1241, 11. See also, Hofstede and Bond, *The Confucius connection*, above n 1249, 11; Hofstede and Bond, *Hofstede's culture dimensions*, above n 1250, 419.

¹²⁷⁰ Husted, above n 1234, 428.

¹²⁷¹ Sitorus and Budhwar, above n 1190, 604–5.

¹²⁷² *Ibid.*

to improve the legal system. Kahn-Freund also proposed them as a law reform tool and Teubner saw them as a major source of legal change.¹²⁷³

The crash of Asian stock markets in 1997 was seen to be the result of poor corporate governance, including weaknesses in disclosure. It led to immediate calls for legal reforms designed to protect minority shareholders¹²⁷⁴ and attract global investors as indicated in Chapter [3.2.3]. Demands for reforms for the protection of foreign and domestic investors led to a focus on corporate governance, including disclosure, in Asian markets.¹²⁷⁵ The pressures were strong on Asia tycoons and controlling shareholders, including those in Indonesia, to adopt more shareholder-friendly Western style approaches because of ‘their reliance of Anglo-American equity capital growth’.¹²⁷⁶ Corporate governance, including disclosure principles, became a major law reform objective for international institutions in the Asia-Pacific region’¹²⁷⁷ including Indonesia.

The shock of the Asian economic crisis, business globalization, and of increasing international capital flow forced Indonesia to make significant changes to Indonesian corporation law and corporate regulation including the development of the GCG Code. It led to a number of transplants of Western legal concepts and frameworks.¹²⁷⁸

Legal transplants, as a major source of legal change for disclosure, were driven by the pressures on Indonesia from the IMF in particular. The agreement between Indonesia and the IMF to refinance the country after the economic crisis demanded that law reforms be undertaken in Indonesia.¹²⁷⁹ The IMF dictated almost every piece of national legislation passed from 1998 to 2000 as part of the conditions for the bailout of the Indonesian economy.¹²⁸⁰ With respect to the many IMF imposed conditions, Steele argued that

¹²⁷³ See, Forsyth, above n 500, 253.

¹²⁷⁴ Cheffins, above n 559, 21.

¹²⁷⁵ Kingsley, above n 1155, 502.

¹²⁷⁶ Cheffins, above n 559, 21.

¹²⁷⁷ Kingsley, above n 1155, 493, 494 .

¹²⁷⁸ Ibid 498.

¹²⁷⁹ Ibid 511.

¹²⁸⁰ Mahy, above n 1217, 413–14. See also, Daniel, above n 533, 358

Indonesia was forced to assimilate Western standards into its corporate law and governance.¹²⁸¹

The reforms were intended to transform Indonesia from chaotic economic and legal regimes to ones with stronger corporate and legal bases. A number of reform programs were established. They included the introduction of new laws, amendments to relevant laws, and privatization of state owned assets. The setting up of the National Committee for Corporate Governance (NCCG) in 1999 was also part of the reform. The Committee drafted a corporate governance code assisted by the World Bank.¹²⁸² The Code adopted the OECD models of global corporate governance standards. The introduction of the OECD principles of disclosure principles was considered as urgent reform to correct poor corporate governance.¹²⁸³ Indonesian company law was also later changed to adopt common law, or Anglo American, governance standards.¹²⁸⁴

The transplant of the model of disclosure, particularly based on the US style of disclosure, was a challenge for Indonesia as a civil law jurisdiction with lesser levels of shareholder protection than common law countries, characterized by higher levels of shareholder protection. This protection is believed to encourage investment, and in turn, results in greater market capitalization'.¹²⁸⁵

5.4.2. The adaptability of transplanted foreign legal concepts

As indicated in Chapter 3 and 4, globalisation has played a significant role in the continuing occurrence of Western legal transplants into Indonesia's legal and regulatory systems.

Lindsey has pointed out that 'Indonesia's history has been characterized not only by successive influence from overseas but also by its people's ability to absorb those influences and make them part of their own system'.¹²⁸⁶ This proposition is true in the

¹²⁸¹ Steele, Stacey, above n 1168, 146.

¹²⁸² Mahy, above n 1217, 414. See also, Daniel, above n 533, 359.

¹²⁸³ Iu and Batten, above n 276, 52.

¹²⁸⁴ Mahy, above 1217, 413. The long-term consequences of deregulation in the mid-1980s and critical problems with the banking sector were amongst other factors besides poor corporate governance.

¹²⁸⁵ Ibid 378–9.

¹²⁸⁶ Lindsey (ed), *Indonesia: Law and Society*, above n 3.

context of the earlier traditional communities as indicated in Chapter 4.¹²⁸⁷ It is associated with what Watson termed voluntary transplants. People took their law with them when they moved to different territories. People in those territories voluntarily accepted other people and those peoples' legal systems.¹²⁸⁸

The historical background in Chapter 4 shows that Indonesia has had a very extensive transplantation of the Dutch legal system since its colonization. Dutch law was extended to the Netherlands and its colonies including Indonesia based on the *Asas Konkordansi (Concordantie Beginselen)* [Concordance Principle],¹²⁸⁹ found in Article 131 (1a) of the IS (*Indische Staatregeling*), see Chapter [4.2.2.2].¹²⁹⁰ Dutch colonial laws had been applied for over 150 years and still persist in the Indonesian legal system. Amongst others, the limited liability companies (*Perseroan Terbatas* or *PT*) provisions in the Commercial Code have been applied for almost all that time until the 1995 Company Law (Limited Liability Company) locally known as UUPT [*Undang-undang Perseroan Terbatas*] replaced them.¹²⁹¹

A well known example of a legal transplant, which was widely accepted was a native cooperative law [*Regeling Inlandsche Cooperatieve Verenigingen*] introduced by the Dutch in 1927. The introduction of the law was based on the consideration that the imposition of a Western concept on the natives required that it be tailored to local requirements, see Chapter [4.2.2.2] particularly at sub-section (c). The law made it possible

¹²⁸⁷ See, Chapter 4 – The implementation and development of corporate governance disclosure in Indonesia. The increasing scale of globalisation has led to foreign concepts being introduced and evolving in Indonesian economic life, beliefs and practices. Foreign concepts come from the spread of Hinduism and Buddhism, Islam and influences from colonial forces including the Portuguese, Dutch and Japanese.

¹²⁸⁸ Alan Watson, *Legal transplant: An approach to Comparative Law* (University of Georgia Press, 2nd ed, 1993) 29–30.

¹²⁸⁹ Mahy, above n 1217, 384. *Asas Konkordansi* means the principle to follow; the European or the Netherlands's laws applied to the native Indonesians.

¹²⁹⁰ *Indische Staatregeling (IS)* was de facto colonial Constitution. Article 131 (1a) IS stipulated that Europeans living in the East Indies applied their origin Civil Code which was Dutch Civil Code based on concordance principles; See, Fitika Andraini, *Perbedaan Golongan Penduduk Dalam Proses Pendaftaran Hak Atas Tanah Karena Pewarisan* [A group division of citizens in the process of the registration of land title from inheritance] (Thesis, Postgraduate for Notary, Diponegoro University, Semarang) 6 <<https://core.ac.uk/download/files/379/11717138.pdf>>.

¹²⁹¹ Gautama, above n 552, 130.

for indigenous Indonesians to establish partnerships and business forms that had not existed before.¹²⁹² It was considered to be appropriate to adopt the legislation into the local concepts of business and law.¹²⁹³ It was also considered as ‘the appropriate legal tool for change’ to bring indigenous Indonesians into the modern economy by way of cooperatives.¹²⁹⁴ The law had an immediate impact and increased the number of cooperatives established during the 1930s.¹²⁹⁵ Prior to the introduction of this law, the application of the Cooperative Law of 1915, which was a direct copy of the Netherlands Cooperative Law of 1876, ‘was judged to be unsuitable for the native population’.¹²⁹⁶ This example indicates that the adaptation of the law was a significant factor for its success as a legal transplant as suggested by Mahy, Kingsley and Bedner and discussed below at sub-section [5.4.4]. The complexity created by transplanted laws in the Indonesian context, discussed below at sub-section [5.4.5], provides examples of the need to consider and address the adaptation of transplanted foreign legal concepts to local conditions. The transplanting of foreign legal concepts continues to be part of the country’s legal development. The following discussion provides a survey of the continuation of legal transplants after independence using company law as the main example.

5.4.3. The persistence of Western corporate legal transplant after independence

After independence, there were many debates on ‘how to change the old legal order to fit the new ideology’.¹²⁹⁷ The calls for Indonesian civil and commercial law codes raised issues as to whether the country should follow European legal principles or *adat*, as a

¹²⁹² Mahy, above n 1217, 395. The 1927 native cooperative law was the outcome of a Commission which was formed under Julius Herman Boeke to look into a more suitable approach for the native population.

¹²⁹³ Ibid 395; See also, Kementerian Koperasi dan Usaha Kecil dan Menengah [Ministry of Cooperatives, Small and Medium Enterprises of the Republic of Indonesia], *Sejarah Kementerian* [History of the Ministry] <<http://www.depkop.go.id/sejarah-kementerian/>>; Rusdiyono, *Perkembangan Pengaturan Pendirian Koperasi Di Indonesia* [The development of regulating the establishment of cooperatives in Indonesia], (Thesis, Postgraduate of Diponegoro University, Semarang, 2009) 42 <<https://core.ac.uk/download/files/379/11718104.pdf>>.

¹²⁹⁴ Mahy, above n 1217, 395.

¹²⁹⁵ M Iskandar Soesilo in Mahy, above n 1217, 395.

¹²⁹⁶ Mahy, above n 1217, 395. The 1915 law required a notarial deed, the articles of association written in Dutch and to obtain consent for its establishment from the Governor General. It made the cooperative establishment were difficult and expensive.

¹²⁹⁷ Ibid 399.

symbol of a unique Indonesian identity. To choose one system of *adat* above others in a country with so many different ethnic groups would have caused ethnic divisions at a time when the unity of the new country was still fragile.¹²⁹⁸

Unable to establish any other legislative resolution, the colonial Commercial Code continued to be used as the law.¹²⁹⁹ It took almost 50 years after independence for an Indonesian company law to be finally introduced as landmark legislation in 1995. However, the 1995 Company Law [*Undang-undang Perseroan Terbatas – UUPT*] still reflected an inheritance from the colonial law. The law embodied a large part, or twenty-one articles, from the *Wetboek van Koophandel* [Indonesian Commercial Code or *Kitab Undang-Undang Hukum Dagang* or “KUHD”], which had been first promulgated in 1847.¹³⁰⁰

The 1995 Company Law, however, adopted not only the earlier Dutch civil law concepts, but also common law ideas. It was seen as being a unique legislation in that it adopted a mixed legal system approach. The Law ‘retains civil law concepts such as the two-tier management structure and the company investigation.’¹³⁰¹ It used Dutch concepts in requiring a minimum of two promoters, minimum capital, the approval of the Minister and the establishment of a Board of Commissioners and potential judicial investigation of the company.¹³⁰² It also contained provisions on negligence relating to the duties of directors and commissioners. This concept was adopted from the Anglo-American law related to the duties of directors.¹³⁰³

¹²⁹⁸ Ibid.

¹²⁹⁹ Ibid.

¹³⁰⁰ Tabaluyan, ‘The New Indonesian Company Law’, above n 871, 883.

¹³⁰¹ Ibid 908.

¹³⁰² Mahy, above 1217, 412. See generally, Undang-undang Republik Indonesia Nomor 1 Tahun 1995 tentang Perseroan Terbatas [Law No. 1 of 1995 of the Republic of Indonesia concerning Limited Liability Company], available at <[www.bpn.go.id/.../DocumentDownload.ashx?...>. Directors and Commissioners \[Chapter VI Articles 79–101\]; A new Company Law – Undang-undang Republik Indonesia No. 40 Tahun 2007 \[Law No. 40 of 2007 concerning Limited Liability Company\] is available at <\[http://www.setneg.go.id/index.php?option=com_perundangan&id=1776&task=detail&catid=1&Itemid=42&tahun=2007\]\(http://www.setneg.go.id/index.php?option=com_perundangan&id=1776&task=detail&catid=1&Itemid=42&tahun=2007\)>. Directors and Board of Commissioners \[Chapter VII Articles 92–121\] and Investigation on Company \[Chapter IX Articles 138–141\]. Company investigation shall be conducted by submitting an application in writing together with the reasons to the District Court, which jurisdiction covers the domicile of the company.](http://www.bpn.go.id/.../DocumentDownload.ashx?...)

¹³⁰³ Tabaluyan, ‘The New Indonesian Company Law’, above n 871, 908.

Mahy observed that the 1995 Company Law ‘was clear common law influence with provisions on piercing the corporate veil, directors’ duties and the business judgment rule, and permission for a derivative action’. This reflected the involvement of the World Bank and USAID in the legal drafting process. The 1995 Company Law was developed with the major assistance of these two international organisations.¹³⁰⁴ It was a product of the project on Economic Law and Improved Procurement Systems (ELIPS), funded by USAID, to modernize Indonesian economic laws. International legal experts, supported the drafting and dissemination of not only the Company Law but also a new banking law and a new capital markets law. These were the major outcomes of the ELIPS projects.¹³⁰⁵ Similarly, in the early years of the Soeharto regime, other pivotal laws, the Foreign Investment Law no. 1/1967, the Forestry Law no.5/1967 and the Mining Law no.11/1967 had reflected similar involvements. They were ‘designed by a team of mostly US-trained technocrats appointed by Suharto’.¹³⁰⁶ The Investment Law waited for almost 37 years after its amendment in 1970 to be reformed with the introduction of a new Investment Law no. 25 of 2007.

The influence of common law concepts, particularly adopted from US law, continues in legal reforms. After twelve years, the 1995 Company Law was amended in 2007 with the application of a template of the World Bank, which was influenced by US law under the Reports of the Observance of Standards and Codes (ROSC) program.¹³⁰⁷ These amendments have been seen as a significant step in the further transposition of laws relating to corporate governance disclosure. The OECD principles related to corporate governance disclosure in the model of US law, as indicated earlier, were transplanted in the new law. The importation of OECD principles derived from the US model has led to the increasing refinement of the existing law, leaving little reference to earlier Dutch models.¹³⁰⁸

The elucidation of the changes represented by the 2007 Company Law (*Undang-undang Perseroan Terbatas – UUPT*) indicates that the globalisation trend has led to

¹³⁰⁴ Mahy, above n 1217, 412.

¹³⁰⁵ Ibid 411.

¹³⁰⁶ Ibid 405.

¹³⁰⁷ Ibid.

¹³⁰⁸ Ibid 418.

significant changes in the corporate governance regime. The previous law was amended to address globalized demands.¹³⁰⁹ The changes to company law were acknowledged as a necessary part of convergence in corporate governance frameworks.¹³¹⁰ This is a further indication of how the phenomenon of globalisation has shaped the convergence of corporate governance, as indicated in Chapter [3.2].

5.4.4. Legal transplant frameworks for the transposition of disclosure in the Indonesia context

Transplanting international principles of corporate disclosure derived from foreign sources into Indonesia's context risked some adverse consequences. Integrating or internalising transplanted laws or models into a significantly different national legal system may lead to different outcomes than those expected. They may be interpreted and applied very differently from when in the donor country and produce different results. They may even be ignored and not be used at all. Kingsley highlighted these issues in describing some potential unfavourable outcomes to transplantation.¹³¹¹ This indicates the need for significant consideration before embedding new concepts or principles, such as corporate disclosure into domestic legal and regulatory systems.

As indicated in Chapter [2.6.4], the differences between Legrand, Kahn Freund and Watson over legal transplants provide a framework for exploring how laws on disclosure can be successfully transplanted. Watson stated that 'a successful legal transplant – like that of a human organ – will grow in its new body, and become part of that body as the rule or institution would have continued to develop in its parent system.'¹³¹²

It is widely observed that the success of a legal transplant requires a number of supporting factors as indicated in Chapter [2.6.4]. Legal, political, social, culture and economic impact have to be taken into account. Legrand, for example, has emphasized the culture of local society as impacting on the transplanted law's growth. It suggests the local

¹³⁰⁹ Pusat Informasi Hukum Mahkamah Konstitusi RI, *Penjelasan Atas Undang-Undang Republik Indonesia Nomor 40 Tahun 2007 Tentang Perseroan Terbatas* [Elucidation of Law of Republic Indonesia No. 40 of 2007 concerning Limited Liability Company], 60 <portal.mahkamahkonstitusi.go.id/.../download_pdf.ph...>.

¹³¹⁰ Gautama, above n 552, 130.

¹³¹¹ Kingsley, above n 1155, 514.

¹³¹² Watson, *Legal transplant: An approach to comparative law*, above n 1288, 27.

culture as a determining factor in successful transplantations. Political factors were also emphasized by Kahn-Freund.¹³¹³

Some studies observed that recipient initiatives have played a fundamental role in transplant successes. Yuka suggests that transplantation requires local initiatives to apply them as a living law within commercial practices.¹³¹⁴ Kingsley also observed that the borrowed ideas need to be translated into practical and real activities. He suggests that both the intellectual and practical frameworks need to be considered in law reform.¹³¹⁵ Yuka further indicates that successful outcomes of transplantation rely on appropriating good models. In this context, either the recipients or their initiatives lead to transplants succeeding. On the other hand, the outcomes of transplantation with less developed models vary, particularly where they represent significant deregulation. Initiatives in some states, such as China and Vietnam, are seen to depend on other factors.¹³¹⁶

Other studies demonstrate that adaption of transplanted concepts to the local context is a significant factor. Mahy, for example, emphasized people's capability to adapt to new laws. They learn to deal with them and then further develop the transplanted models to suit the local environment.¹³¹⁷ Berkowitz *et al* suggests that familiarity with the basic principles in the transplanted laws is a determining factor in the effectiveness of legal transplants, see Chapter [2.6.4.2].¹³¹⁸ They contended that there are two determinants of receptivity other than the concept coming from the same legal family. They are, its application in a meaningful social context in the law and the support of judges, lawyers, politicians, and other legal intermediaries in shaping the law so that it is responsive to the legality demanded of it.¹³¹⁹

¹³¹³ G Edwards, *Legal Transplants and Economics: The World Bank & Third World Economics in the 1980s – A Case Study of Jamaica, the Republic of Kenya and the Philipines*, 2009 <http://sas-space.sas.ac.uk/dspace/bitstream/10065/349/2/Gail_Edwards_Thesis_Contents.pdf>.

¹³¹⁴ Yuka, above n 539, 6893.

¹³¹⁵ Kingsley, above n 1155, 496.

¹³¹⁶ Yuka, above n 539.

¹³¹⁷ Mahy, above n 1217, 381.

¹³¹⁸ Berkowitz, Pistor and Richard, above n 522, 189.

¹³¹⁹ *Ibid* 167. See page 179. Receptivity is defined 'as the country's ability to give meaning to the imported law'.

Kingsley, in the context of Indonesia, suggested the similar significance of adaptation to local conditions. He observed that not adapting the borrowed law to the Indonesian system would create considerable complexities.¹³²⁰ The study further indicated that legal transplants in Indonesia would continue to fail:

if they remain premised on merely protecting outside interests, utilizing Western frameworks without adaption, and continuing to fail to accept a more pluralistic approach that recognizes the cultural diversity of Indonesian society.¹³²¹

A failure to meet the indigenous commercial and social needs as well as expectations and aspirations is significant. This has often been the case when the focus has been mainly on the need of the coloniser or international community rather than those of facilitating domestic communities in their development of commerce and markets.¹³²²

Bedner appears to accommodate Legrand's, Kahn-Freund's and Watson's concepts. He argued that legal transplants in developing countries, like Indonesia, are directly impacted by their reception in local society. He emphasizes this social effectiveness in how the transplanted rules effectively work on local social processes, see Chapter [2.6.4.2]. This, he states, is a distinct marker of their reception in domestic law and the focus in well-developed legal systems on 'how the deeper lying legal epistemological structures shape the way in which transplanted rules and institutions acquire new meaning'.¹³²³ The Indonesian legal system may not be sufficiently developed for this later observation to apply.

Bedner also considered the significance of the reception in the context of Indonesia, where laws often contain foreign legal influences and involve legal transplantation. He points to legal co-operation with the United States, Australia, the Netherlands and Canada that 'has influenced important parts of Indonesian legislation'.¹³²⁴ The adoption of the universal model of the OECD corporate governance principles as the basis of Indonesia

¹³²⁰ Kingsley, above n 1155, 510.

¹³²¹ Ibid 495.

¹³²² Ibid 498.

¹³²³ Bedner, 'Indonesian legal scholarship and jurisprudence as an obstacle for transplanting legal institutions', above n 523, 253–5.

¹³²⁴ Ibid 255.

corporate governance policies and law¹³²⁵ is one of a number of contemporary legal transplants in Indonesia. This trend reflects a claim that adopting legal ideas, concepts, processes and practices from developed economies can assist developing economies like Indonesia.¹³²⁶

The complexity of legal transplants in the Indonesian context and their consequences are discussed below.

5.4.5. The complexity of transplanted laws in the Indonesian context

A number of scholars have highlighted the complexity of legal transplants within the Indonesia legal system. The complexity is related to issues around the country's formal legal system, legal culture, legal scholarship and its jurisprudence.

Steele underlined Indonesia's experience as an example of the difficulties in introducing Western modelled laws into other jurisdictions. He contends that legislation is 'an inappropriate tool for change because it performs an 'infrastructural' rather than a 'catalytic' role'.¹³²⁷

Since the financial crisis of 1997, Indonesia has experienced extensive and extended trouble in radical political and legal infrastructure reform.¹³²⁸ There are competing visions of democratization. There is resulting fragmentation, resistance by the elite and complexity in the constitutional processes that affect legal institutions and new regulations.¹³²⁹

Mahy is sceptical about the outcomes of the transplantation of Western concepts through company law reforms after the financial crisis. Problems with weak law enforcement still persist. There is no evidence of radical changes to ownership structures or family control of listed and private companies.¹³³⁰ He underlines the claim by Pistor *et al* of a gap between formal company law and corporate practice as a result of the 'lack of responsiveness of formal law reform to political and economic reality in transplant

¹³²⁵ Monks and Minow, above n 234.

¹³²⁶ Mistelis, above n 490, 200.

¹³²⁷ Steele, Stacey, above n 1168, 159.

¹³²⁸ Lindsey, 'Legal infrastructure and governance reform in post-crisis Asia: The case of Indonesia', above n 553, 13.

¹³²⁹ *Ibid* 20.

¹³³⁰ Mahy, above n 1217, 427.

countries'.¹³³¹ The weakness of the rule of law was also observed as adding to the complexities of Indonesia as a recipient of legal transplants.¹³³²

Daniel related Indonesia's complex legal situation to the country's legal culture problems. Current Indonesian attitudes, values and opinions show little faith in the legal system. A corrupt legal system has led to scepticism about formal law and its enforcement.¹³³³ This is a crucial issue as Miller points out, social attitudes towards law impact on the successful reception of legal transplants. If the process of law making and law enforcement has strong legitimacy, these 'will give greater effect to any new law'.¹³³⁴

Bedner, in his study of Indonesia, demonstrated that structural problems within the legal system contributed to the resistance to legal transplants. This applies not only to Indonesia but also to countries with similar problems in adopting legal transplants. The problems obstruct the proper functioning of legal institutions and legal principles. Bedner showed that the culture around jurisprudence and legal scholarship could impede the acceptance of foreign legal institutions into Indonesia. Amongst other sources of resistance to the improvement of the legal system by adopting legal concepts from elsewhere: corruption, a malfunctioning political system as well as governmental fragmentation and a conflicted legal plural colonial heritage.¹³³⁵ He observed that since the Indonesia's independence, the decline in legal scholarship and jurisprudence has undermined the development of its legal system. This adds to the complexity of Indonesia's contemporary legal system.¹³³⁶

There are four significant factors Bedner attributes to the decline of Indonesian legal scholarship and jurisprudence. They are the lack of primary legal sources, the mentality of jurists, inconsistencies in the legal system and the absence of a tradition of resolving legal

¹³³¹ Ibid.

¹³³² Steele, Stacey, above n 1168, 432.

¹³³³ Daniel, above n 533, 370.

¹³³⁴ Jonathan M Miller, 'A typology of legal transplants: Using sociology, legal history and Argentine examples to explain the transplant process' (2003) 51 *American Journal of Comparative Law* 839, 844.

¹³³⁵ Bedner, 'Indonesian legal scholarship and jurisprudence as an obstacle for transplants legal institutions', above n 523, 253.

¹³³⁶ Ibid 256–7.

problems in the education of law students. These all have serious consequences for the judiciary, the profession and law faculties and their students.¹³³⁷

Firstly, the persisting condition of the lack of primary legal sources has been seen as a portrait of the decline in legal scholarship. Bedner points to ‘the blockage of relevant legal information and its corresponding drop in quality’.¹³³⁸ Legal information is not well organized despite the fundamental political reforms and legal changes always available in the digital revolution.¹³³⁹ Parliamentary and other resources are not easily available on the internet.¹³⁴⁰ Churchill also observed similar issues in identifying difficulties in access to court judgments, lower level legislation, administrative procedures and dictums, and doctrinal exegesis and analysis. The lack of access to legal information for lawyers has affected their work.¹³⁴¹

There have been attempts to address the lack of access to legal sources but they have failed. The initiative of an older generation of Supreme Court justices in the 1980s to publish systematic reports of cases as a part of legal cooperation with The Netherlands faced resistance from internal counterparts. The publication of a new administrative court journal carrying case law and relevant articles also failed to attract judges to read them.¹³⁴²

Secondly, in respect to the judiciary, Bedner observed the poor mentality of Indonesian jurists drawing earlier observations by Lev. Lev claimed that the revolutionary aspects of government policy in the old order regime under Soekarno contributed to the demoralization of jurists with substantial consequences.¹³⁴³ They were also intimidated by an authoritarian political system. Jurists had been summoned by revolutionary politicians and informed that they ‘should no longer use legal sources dating from the colonial period, which meant the large majority of legal rules.’¹³⁴⁴ It became worse after Soekarno’s Guided Democracy was replaced by Soeharto’s New Order regime. The promotion of a rule of law

¹³³⁷ Ibid.

¹³³⁸ Ibid 263.

¹³³⁹ Ibid.

¹³⁴⁰ Ibid 268.

¹³⁴¹ Ibid 256.

¹³⁴² Ibid 268.

¹³⁴³ Ibid 258.

¹³⁴⁴ Ibid.

agenda in the early years of Soeharto's power turned to the exertion of full control over the judiciary in the 1970s and 1980s. Structural problems between the executive and judicial branches of government were resolved, but 'the political interference led to a sharp rise in judicial corruption and a general decline in its standards and morals.'¹³⁴⁵ The rise of corruption is considered the most significant outcome from this period. It directly contributed to the growth of legal uncertainty and the poor quality of judgments.¹³⁴⁶ Law lost its predictability and its usefulness as a source of guidance in dispute resolution. Bedner claimed that these problems still persist as the legacy of the new order's policies, particularly in the judiciary.¹³⁴⁷ Lindsey also observed poor institutional support for judges including limited research facilities as among other factors creating the low skill and competence levels of Indonesian courts.¹³⁴⁸

While the 1998 financial crisis provided opportunities for change, the structural components of the legal system undermined any improvement in legal scholarship.¹³⁴⁹ Bedner claimed that many Indonesian jurists maintain 'the idea that precedent is not binding, because Indonesia is a civil law country.'¹³⁵⁰

The Indonesian experience reveals that in any legal infrastructure reform, the differences between civil law and common law systems are critical and need to be considered. From judicial independence in the Supreme Court, to the Ombudsman Republik Indonesia (ORI) and to the Business Competition Supervisory Commission (BCSC) [*Komisi Pengawas Persaingan Usaha – KPPU*] people and institutions struggle to

¹³⁴⁵ Ibid 259.

¹³⁴⁶ Ibid 261.

¹³⁴⁷ Ibid 262.

¹³⁴⁸ Lindsey, 'Legal infrastructure and governance reform in post-crisis Asia: The case of Indonesia', above n 553, 21.

¹³⁴⁹ Bedner, 'Indonesian legal scholarship and jurisprudence as an obstacle for transplants legal institutions', above n 523, 263.

¹³⁵⁰ Ibid. With respect to the ombudsman & competition commission, See generally, Ombudsman Republik Indonesia, *Sekilas Ombudsman Republik Indonesia* [A brief overview of Ombudsman of the Republic of Indonesia] <<http://www.ombudsman.go.id/index.php/tentang-ombudsman/sekilas-ombudsman.html>>. Ombudsman is a state institution that has authority to supervise over the implementation of public services; Komisi Pengawas Persaingan Usaha (KPPU) [Commission for Supervision of Business Competition], *Overview* <<http://www.kppu.go.id/eng/about-2/overview/>>. KPPU is a state commission, a law enforcement agency for issues of business competition practices.

perform roles that are derived from, or that have been modified by common law models.¹³⁵¹ This is a significant point for this study, that the legal family affects the usability of informal or soft law, such as good corporate governance codes, which derive from common law countries. It also confirms the claim that soft law is more likely to be effective in common law than in civil law jurisdictions considered its characteristics indicated in Chapter [3.6]. The effectiveness of good corporate codes as soft law may relate to some observations that countries with common law systems ‘have the most investor-friendly laws, French and German civil law countries have the least investor-friendly laws’.¹³⁵²

Thirdly, uncertain judicial practices create further complexity for legal transplants. Bedner argued that Indonesian judges are not accustomed to reading and understanding precedents and that in the application of the law to similar cases inconsistency is the inevitable result. The judges applying law are ‘looking at the facts of the case and applying usually broad, general statutory rules to them’.¹³⁵³ Legislation is the only legal source for them.¹³⁵⁴ Massier added other issues contributing to misinterpretation, misunderstanding and misapplication of the law related to the absence of official translations into Indonesian of the major codes written in Dutch language of Netherlands East Indies law.¹³⁵⁵

There are also the problems of lawyers. Lawyers prepare advice and arguments using textbooks, most of which tend to be superficial and do not reflect a good or deep understanding of the relevant legislative text.¹³⁵⁶

Fourthly, the model of Indonesian legal education has also been claimed to contribute to the problems. Legal studies are highly theoretical and abstract. The absences of exercises in which students apply legal principles to resolving problems mean that they never learn how to ‘do law’.¹³⁵⁷ An effort to address this issue by former foreign minister,

¹³⁵¹ Lindsey, ‘Legal infrastructure and governance reform in post-crisis Asia: The case of Indonesia’, above n 553, 32–3. See also, Berkowitz, Pistor and Richard, above n 522, 165–6.

¹³⁵² Berkowitz, Pistor and Richard, above n 522, 165–6.

¹³⁵³ Bedner, ‘Indonesian legal scholarship and jurisprudence as an obstacle for transplants legal institutions’, above n 523, 256.

¹³⁵⁴ *Ibid* 271.

¹³⁵⁵ *Ibid* 259.

¹³⁵⁶ *Ibid*.

¹³⁵⁷ *Ibid* 257.

Mochtar Kusumaarmadja, by a review of law schools' curricula to include more legal skills failed.¹³⁵⁸

These complex conditions, discussed above, are considered to have contributed to the unsuccessful transplanting of corporate governance as another failed legal transplant in Indonesia. Lessons from the past with respect to successful legal transplants indicate that adapting it to local conditions, as Mahy, Berkowitz et al, and Kingsley claim, is important.

5.5. Conclusion

This chapter provides a more structured account of the challenges to corporate disclosure with regard to Indonesian corporate governance framework. It builds on the cultural aspects of Indonesian society impacting on soft law and its use in corporate disclosure considered in the previous chapter.

As indicated in the previous chapter, honesty and transparency are fundamental values found in local culture and trust is considered important in business transactions. Those values have been compromised by the development of paternalistic values, which was further emphasized during the period of Dutch colonization. Corruption grew under the Japanese occupation. Corruption has impacted on the practice of disclosure. It discourages honesty and transparency. Disclosure can become misleading and ineffective. A number of studies are referenced that confirm this.

The literature, which considers the pervasiveness of corruption, shows that corruption is found in law making and law enforcement institutions. The courts are considered incapable of deciding commercial disputes, with litigants being able to buy favourable decisions. The anticorruption body, the KPK, has been undermined by those in power in the legislative, executive and judicial branches of government. Its legislation contains loopholes. The cultural values that perpetuate corruption are identifiable. They include corrupt patron-client relationships and the erosion of older values of shame around reputation and social standing. The corruption of the judicial system and resulting lack of law enforcement is significant in the perpetuation of corruption.

In law making, political institutions are regarded as fragile and the influence of the old order of Soekarno and the new order of Soeharto are implicated in this. The Soeharto

¹³⁵⁸ Ibid 261.

period spread corruption to all levels of government including the judiciary and has left a legacy of moneyed politics that undermine democracy, corrupt political parties and that continue to promote an unequal society. SOEs and their governance are significant sources of wealth to corrupt and for those who are corrupt.

The promotion of better corporate governance and related disclosure on an Anglo-American model was promoted by a number of international bodies in Indonesia as a price for assistance in financial crises. Both are seen as foreign ideas, which are even foreign to the legal system, which has largely been shaped by the period of Dutch colonisation that introduced it. Western ideas are generally viewed with suspicion by most Indonesians. In the context of the problems with successfully implementing disclosure, Hofstede's concept of the four dimensions of national culture has some explanatory power: power distance, uncertainty avoidance and individualism. There is clear recognition in the literature that culture is a major determining factor in the success of disclosure regimes. It has both a constitutive and regulatory impact. It is constitutive in that it shapes economic behaviour and impacts upon regulation.

In this context, effective disclosure is indicated as occurring in cultures with low uncertainty avoidance and low power distances. This is related to other studies, which indicate that disclosure is more effective in individualist societies than communitarian or collectivist ones as collective rights tend to be less well protected than individual rights. Indonesian society is also marked by collectivism in which the individualism of the patrons are a significant exception. Indonesian society is also marked by high uncertainty avoidance and high power differences. With respect to uncertainty avoidance, this is shown in approaches to accounting, particularly in a preference for secrecy over transparency and also in conflict avoidance with considerable value given to the apparent maintenance of harmony. Accounting studies have also confirmed that Indonesia is marked by high power distances. This is part of the paternalism in which clients are very deferential to the patron.

Introduced concepts of corporate governance and disclosure do not fit well with these values, which limit the extent to which they are followed. They were transplanted as a result of the influence of international bodies as a result of the impact on Indonesia of financial crises. As informal, soft or reflexive law they have little force with respect to

established values. Values, such as a sense of shame and loss of face are required for them to be effective but are not to be found among the commercial, political and social elite. As values, which are perceived to be linked with western cultures and which were non-voluntary transplants forced on Indonesia, they do not have the traction that is required for soft law to be effective.

In respect of the formal legal system some legal transplants including a civil law legal system based on Dutch law have been more successful. While concepts based on corporate law continued, they were added to by concepts derived from common law jurisdictions as a result of intervention by these bodies. The ability of Indonesian people to absorb influences and make them part of their own values has broken down at this point. There are earlier examples, such as the 1927 Cooperative Law, being adapted for local conditions and then taken up and adapted further at the local level. Other laws from the Dutch period were also accepted and continued to be used after independence.

It is unlikely that Indonesian society will cease to be marked by uncertainty avoidances and power distances. Knowledge from comparative law studies on the importance of adapting law to local circumstances need to be considered. There is conflict in the literature over how easily law can be transplanted. The modification of common law concepts reflecting Anglo-American business is required before they are transplanted into the intellectual and practical framework of Indonesian institutions. As Yuka indicates they require local initiatives to make them living law in commercial practices that meet indigenous commercial and social needs. Unless this is done, transplants may just add to the complexity and over determination of the Indonesian legal system. They will not play a catalytic role.

There is reason for scepticism whether this can be done. As Pistor and others have noted there is a lack of a gap between formal corporate law and practice as a result of transplants. In the context of Milhaupt's and Pistor's rolling relationship between law and the economy, there are major problems in Indonesia, as the legal system is so ineffective it is difficult for this relationship to develop. There are underlying problems including corruption, which have weakened the rule of law and the role of the courts and regulatory bodies. It is difficult to turn back or to even stem the corruption that pervades Indonesian

life. It may be possible to make some changes in the culture of law and regulation to make the transplants of both formal and informal law more successful. The literature points to problems such as the decline in legal scholarship and jurisprudence. This would require the better publication of legal and related sources to assist lawyers and others to find and understand law, administrative procedures and related informal law. It requires a new professionalism and energized legal profession that is better educated, is more rigorous in its legal reasoning and arguments and is open to and familiar with reading and understanding other sources of informal law and regulation including codes of good practice. It also needs to be an ethical profession, which resists corruption. This needs to commence in legal education and include practical exercises in problem solving.

Chapter 6 : The use of the good corporate governance code for disclosure in Indonesia

6.1. Introduction

This chapter discusses the use of corporate governance codes in corporate disclosure. It considers the national Code of Good Corporate Governance (GCG Code) that is based on a voluntary or ethical approach. It explores the function of the Code within the Indonesian legal and corporate governance frameworks. It also observes the role of legal framework in facilitating the use of the Code for disclosure and its enforcement. It then considers the impact of the code on accountability for corporate disclosure. The roles of government, the business community and corporate governance NGOs are also discussed to see how they may further promote the effective use of the GCG Code in disclosure.

The GCG Code was expected to serve as a basis for operational requirements in meeting good corporate governance practices including disclosure. It promotes transparency in addressing fundamental governance issues including fairness, accountability and responsibility. But in practice, it serves as merely a reference and has not been widely used by Indonesian firms, particularly listed companies.

The GCG Code is not seen locally as a potential source of informal or soft law. This may be a significant missed opportunity to employ the GCG Code in an effective alternative regulatory strategy to address the state's failure to provide appropriate formal legal and regulatory systems, as suggested by some scholars indicated in Chapter [2.4.2.2]. The GCG Code is also evaluated in the context of the limited capacity of the mandatory disclosure regimes for Indonesian firms, especially listed companies. However, the GCG Code has not been used to support disclosure regulations in being more effective, efficient and responsive regulations as the literature reviewed suggested they could be.

Kingsley's, Mahy's, Daniel's and Bedner's views, as indicated in Chapter [5.4.4]–[5.4.5], may be relevant in explaining the failure of the GCG Code in the Indonesian context. They regarded the adaptation and the reception by a society as a significant factor in successful legal transplants. The GCG Code was transplanted from foreign sources. It

may be too flexible and too responsive to local conditions to be effective as a source of any kind of restraint on local practices, which are inconsistent with it.

The legal culture of Indonesia, within a civil law system, does not see the GCG Code as a potentially significant part of its regulatory framework. The country's lawyers struggle to accommodate the GCG Code within a legal system based on legislation, although some provisions of the GCG Code on good corporate governance and disclosure have been reflected in a number of laws and regulations. This is particularly true of the disclosure provisions. Since the disclosure provisions have been incorporated into the legislations, the impact of the GCG Code as voluntary and as an alternative source of informal accountability for corporate disclosure has been reduced.

Lessons from some comparable South East Asian jurisdictions, summarised in Chapter [3.5], demonstrated some relative success in using codes to improve corporate governance in general and disclosure in particular. The more successful use of such codes in Singapore and Thailand, for example, involve the role of public and private sectors. They have contributed significantly to establishing integrated effective legal and corporate governance frameworks. That is why the roles of the public and private sectors are considered a significant avenue to be explored in the use of the code in Indonesia. These sectors are the government, business and professional communities and relevant NGOs. They play important roles in establishing sufficient trust in the legal system and in the diffusion of power and regulation in the private sector through business culture and capacity building respectively.

The discussion of the use of the GCG Code in this chapter is significant in addressing the research sub-questions regarding the functions that the GCG Code can serve and also whether the GCG Code can improve the effectiveness, efficiency and responsiveness of corporate disclosure regulations.

It concludes that the function of the GCG Code is limited to being a reference document and that it is unlikely, in the present context, to be able to improve the effectiveness, efficiency, and responsiveness of the disclosure rules as observed.

6.2. The basic framework for using corporate governance codes

6.2.1. Introduction

As indicated in the literature review there is an increasing use of corporate governance codes, which may be employed on either a voluntary (in the form of recommendations or without a legal basis) or a mandatory (official recognition by or incorporation in formal law) basis.¹³⁵⁹ The implementation mechanisms for each are generally an ethics-based or regulatory approach. The ethics-based approach depends on the awareness by companies of the need to maintain sustainable long-term relationships with stakeholders. The regulatory based approach is a command and obey style, which relies on government initiated regulations that are inconsistent with some codes.¹³⁶⁰ The codes are often depicted as significant in promoting disclosure, which is in many ways a communication tool and of major significance to investors as indicated in Chapter [2.3].

Indonesia's GCG Code was initially introduced in 2000 by the *Komisi Nasional Kebijakan Governance – KNKG* (National Commission on Governance Policy) on an ethics based or voluntary basis. This approach differs from the common practice in many other jurisdictions, as indicated in Chapter 3 at 3.5. that use voluntary codes but with a comply or explain mechanism. This mechanism does not exist in the GCG Code.

A claim made in the GCG Code that it is an ethics based driver is not realistic. The Code sets out potentially significant guidelines for both listed and non-listed firms but has largely been an advisory or rhetorical tool. It is largely used as a reference document and, occasionally, for inspiration.¹³⁶¹

The code has not been widely used and respected as an informal source of norms in the practices of corporate governance or disclosure. This is inconsistent with some observations by Braithwaite, Pistor, Aldasev, Helmke and Levitsky, as indicated in the

¹³⁵⁹ See, Chapter 2 – Literature Review on alternative regulatory theories, section [2.4]. Three stages of legal standpoints of the corporate governance code introduced by Wymeersch and two categories introduced by Pientrancosta, section [2.4.2.3].

¹³⁶⁰ Alex Yap, 'Good corporate governance pays off for Indonesia', *The Jakarta Post* (online), 13 February 2012 <<http://www.thejakartapost.com/news/2012/02/13/good-corporate-governance-pays-indonesia.html>>. See generally, Indonesia's Code of Good Corporate Governance 2006, above n 44.

¹³⁶¹ See, foreword of Coordinating Minister for Economic Affairs and chairman of National Committee on Governance at Indonesia's Code of Good Corporate Governance 2006.

literature review.¹³⁶² They regard codes as potential sources of informal regulation or soft law or responsive regulation. They see codes as an effective alternative regulatory tool for countries like Indonesia with weak legal systems in responding to limited capacity, the failure of the formal legal system and in filling gaps in the law. Braithwaite considered informal rules as significant for responsive regulation, as they offered a less expensive strategy for social control than formal law. Pistor suggested the need for informal rules to address the poor credibility and distrust of formal law in jurisdictions such as Indonesia. Aldasev et al also promoted the use of informal rules to cope with the ineffectiveness of formal ones. They observed that they effectively deal with business issues as opposed to formal rules with their legalistic approaches. Helmke and Levitsky suggested the use of informal rules to deal with the incompleteness of formal law's lack of capacity to cover all contingencies, its lack of changeability its ineffectiveness because of its poor credibility and sometimes unacceptable objectives.

Indonesia's GCG Code, in this context, is described and critically evaluated immediately below.

6.2.2. A code with Indonesian characteristics

The Indonesian Code of Good Corporate Governance has similarities with, but also differs from, similar codes used in other jurisdictions. It is similar among other South East Asian jurisdictions in being introduced as a response to an economic crisis as indicated in Chapter 3. It is different from similar codes in the absence of a discretionary approach. This approach has been considered as the best method to address the implementation of the Code as guidelines or recommendations to be implemented effectively. Corporate governance regimes, as promoted by such codes, are widely observed, as indicated in Chapter 2, to require a flexible approach recognising that it may be inappropriate to apply them in the particular circumstances of a business. This characteristic does not exist in the Indonesian Code.

The Indonesian GCG Code appears to have become symbolic in merely meeting external expectations and requirements. The promulgation of the GCG code was driven by

¹³⁶² See Chapter 2 at [2.4.2.2]: The role of corporate governance codes as informal regulation at section (e): An alternative regulatory strategy for developing countries.

external pressures, particularly the Asian financial crisis and by the International Monetary Fund (IMF), as indicated in Chapter 3. In this sense it was an involuntary transplant as described in the previous chapter. The commitments to the IMF as the country's major lender, as outlined in a Letter of Intent signed in January 2000,¹³⁶³ forced the Indonesian government to make relevant legal and institutional reforms including establishing a national committee on corporate governance, namely National Commission on Corporate Governance Policy (KNKCG). It has been subsequently renamed National Commission on Governance Policy (KNKG).¹³⁶⁴ Kingsley observed, as noted in Chapter [5.4.4], that changes it attempted to bring about failed, since it employed foreign concepts without adaptation to Indonesia's context.

The KNKG was mandated, amongst other things, to create a code for good corporate governance.¹³⁶⁵ This is similar, as indicated in Chapter 3, to other South East Asian countries where governments drove initiatives for the establishment of such codes as part of the response to the financial crisis. The experience of Singapore and Malaysia, with common law systems, has been different from some other South East Asian jurisdictions. Making and enforcing the codes in these jurisdictions was left to the private sector. Thailand, with a more mixed legal system, is similar to Indonesia in respect to the creation of a national corporate governance committee that was established as a public sector initiative. However the Thai Stock Exchange, in the private sector also promulgated similar concepts. Indonesia, however, did not take a similar approach to Thailand. This indicates the absence of a diffusion of regulation as suggested in Black's concept of decentred regulation as noted in Chapter [2.4.2.2].

¹³⁶³ Kurniawan and Indriantoro, above n 125, 9. The commitment included the establishment of the KNKG, educational events on corporate governance for the public, pilot projects in industries for implementing corporate governance principles, regulatory reform in the capital market, the Forum of Corporate Governance (FCGI), a fit and proper test for directors and commissioners, and technical assistance from the international community.

¹³⁶⁴ Ibid.

¹³⁶⁵ KNKG has set up an ambitious vision to be one of the best governance practices in the world with the function as a facilitator and catalyst of corporate governance in Indonesia. See, Komite Nasional Kebijakan Governance [National Commission on Governance Policy], *Visi & Misi* [Vision & Mission] <<http://knkg-indonesia.com/home/tentang-kami/visi-a-misi.html>>.

Indonesia's GCG Code was formally introduced in March 2000 and was revised in 2006 under the title of Indonesia's Code of Good Corporate Governance¹³⁶⁶ [*Pedoman Umum Tata Kelola Perusahaan yang baik – Pedoman Umum Good Corporate Governance*].¹³⁶⁷

'Code' is translated into Bahasa Indonesia as 'general guidance', [*pedoman umum*] which suggests that it is recommendatory. It represents a guideline for good practices based on moral values within a business culture.¹³⁶⁸ It outlines a set of underlying principles, values and norms followed by provisions containing several operational steps.¹³⁶⁹

¹³⁶⁶ Kamal, *Corporate governance for state-owned enterprises: a Study of codes of corporate governance*, above n 572, [2]; Cf Tim Studi Kementerian Keuangan Republik Indonesia Badan Pengawas Pasar Modal dan Lembaga Keuangan, below n 1368, 10, 11–26. Codes have been issued by the Stock Exchange in Malaysia, Singapore, Thailand and the Philippines, and have embodied the Code into Listing Rules with a comply and explain approach. Malaysia with one board system, the Malaysian Code on Corporate Governance was issued by Malaysia's Stock Exchange and stipulated in listing rules. The comply and explain mechanism is mandatory to disclose in financial reporting. Singapore is similar, as comply and explain approaches and are mandatory to disclose corporate governance implementation in financial report. Thailand is also similar with a mandatory requirement to disclose the implementation to media, which recommended to the company website. The Philippine has employed a mandatory approach and the enforcement has been conducted by Securities and Exchange Commission.

¹³⁶⁷ Maulia Eka Riani, 'Penerapan good corporate governance pada perusahaan – Studi kasus: PT. Astra International Tbk.' [The implementation of good corporate governance in companies – A case study of PT. Astra International, Tbk] (Makalah mata kuliah Organisasi Sumber Daya Manusia, Program Pascasarjana Manajemen dan Bisnis [A paper for a lecturing subject of human resources organisation, Postgraduate Program of Business and Management] Institut Pertanian Bogor, February 2014) 9 <<http://maulia49e.blogstudent.mb.ipb.ac.id/files/2014/02/Maulia-Eka-Riani-P056132852.49E-Penerapan-Good-Corporate-Governance-Pada-Perusahaan.pdf>>.

¹³⁶⁸ Tim Studi Kementerian Keuangan Republik Indonesia Badan Pengawas Pasar Modal dan Lembaga Keuangan [Study Team of Capital Market and Financial Institution Supervisory Agency Ministry for Finance Republic of Indonesia], *Kajian tentang Pedoman Good Corporate Governance di Negara-negara anggota ACMF* [Analysis of Good Corporate Governance Codes in ACMF countries members] (2010), 36–7 <http://www.bapepam.go.id/pasar_modal/publikasi_pm/kajian_pm/studi-2010/PEDOMAN_GCG_DI_NEGARA_ANGGOTA_ACMF.pdf>.

¹³⁶⁹ The Code sets out eight main chapters including ensuring the basis for an effective corporate governance framework in Indonesia, good corporate governance general principles, business ethics and code of conduct, organs of the company, rights and role of shareholders, the rights and role of other stakeholders, implementation statement of the code and general guidance of GCG implementation. It introduces five general principles including transparency, accountability, responsibility, independency, and fairness. Each principle is accompanied by code provisions. These principles are similar with the OECD principles, with the specific principle of fairness [*kewajaran dan kesetaraan* – literally meaning fairness and equality]. The Code also stipulates the

As the Code contains those operational requirements for good corporate governance practices, it has at times been presented as the national code to implement a corporate governance regime.¹³⁷⁰ It has been promoted as representing ‘the basic principles for the execution of corporate governance for all companies in Indonesia’,¹³⁷¹ public and private enterprises.¹³⁷² In practice, the regime it lays out does not work effectively and the representations it makes do not represent reality.

As indicated in Chapter [3.5], codes in some South East Asian jurisdictions are similar to Indonesia with a non-mandatory approach. But the codes are embodied in the listing rules and enforced by the operators and regulators of their capital market. The voluntary basis of the Code differs to that found in other countries such as Singapore, Malaysia, and Thailand with their comply or explain mechanism. These countries utilize a flexible regulatory approach in the self-regulatory context of the stock exchange listing rules.¹³⁷³

With respect to Indonesia, there is no obligation required by any regulations or listing rules for Indonesian listed companies to provide a statement of their compliance or an explanation for their non-compliance with the GCG Code.¹³⁷⁴ The Indonesia Stock

role of the state regarding regulatory, supervisory and enforcement authorities, market participants and the public role in the need for ensuring the basis for an effective corporate governance framework. It also elaborates on a set of guidelines for business ethics and a code of conduct as significant in establishing high integrity in the company’s organs and its employees, which in turn may become a company’s culture. See, Indonesia’s Code of Good Corporate Governance Code [Pedoman Umum Good Corporate Governance Indonesia 2006] at European Corporate Governance Institute, above n 44.

¹³⁷⁰ The KNKG also has issued a Good Corporate Governance Code for Banking in 2004, which was revised in 2013 and for Insurance and Reinsurance in 2009, for Insurance and Reinsurance Brokers in 2011, and for Actuarial Consultants in 2011.

¹³⁷¹ Kamal, *Corporate governance for state-owned enterprises a Study of codes of corporate governance*, above n 572, [2].

¹³⁷² See, *Ibid.* Listed companies, state-owned enterprises, province and region-owned companies, and companies that raised and managed public funds, and of which products or services widely used by public and with extensive influence on environment as pioneers are the companies subject to the Code

¹³⁷³ See Literature Review Chapter 2. For examples, Bulgaria and Australia.

¹³⁷⁴ A roadmap of good corporate governance for issuers and public companies introduced by *Otoritas Jasa Keuangan-OJK* (Financial Service Authority) in 2014 provides a recommendation for utilizing comply or explain approach for the code, but it has not been used. The roadmap was supported by the International Financial Corporation, a World Bank subsidiary.

Exchange and the Financial Services Authority (OJK previously BAPEPAM-LK), do not engage with or impose the Code on issuers and public enterprises. But the disclosure provisions promoted by the Code have become mandatory in formal law and regulation.¹³⁷⁵ The OJK has also recently introduced a Good Corporate Governance Roadmap in 2014.¹³⁷⁶ This has eroded the GCG Code's functions in enhancing accountability for effective disclosure.

As noted, a discretion for using Indonesia's GCG Code does not exist. This indicates a consistency with Coffee's claim, as referred to in Chapter 2 that civil law systems like Indonesia, leave less room for flexibility or innovation. He argues that codified civil law minimizes opportunities for discretion by eliminating all gaps in the law. This differs from common law systems such as those of Singapore and Malaysia. Their legal

¹³⁷⁵ It is a mandatory requirement to disclose corporate governance in annual financial report including meeting frequency of the boards and their attendance, meetings with audit committee, the boards' duties & responsibilities and their remuneration and also to establish an audit committee and independent commissioner. The Bapepam has ruled a minimum of one independent commissioner and the Indonesia's Stock Exchange has required 30 per cent minimum of an independent commissioner from board of commissioner. See, Tim Studi Kementerian Keuangan Republik Indonesia Badan Pengawas Pasar Modal dan Lembaga Keuangan, above n 1368, 4, 5.

¹³⁷⁶ Indonesia Corporate Governance Roadmap of 2014 is available at <http://www.ojk.go.id/id/data-dan-statistik/ojk/Documents/ROADMAPTATAKELOLAPERUSAHAANINDONESIA_1391520776.PDF>; Otoritas Jasa Keuangan (OJK) [Indonesia Financial Services Authority], 'OJK launches the Indonesian Corporate Governance Roadmap' (Press Release, 4 February 2014) <<http://www.ojk.go.id/en/berita-dan-kegiatan/siaran-pers/Pages/press-release-ojk-launches-the-indonesian-corporate-governance-roadmap.aspx>>; Tassia Sipahutar, 'OJK launches roadmap for good corporate practices', *The Jakarta Post* (online), 5 February 2014 <<http://www.thejakartapost.com/news/2014/02/05/ojk-launches-roadmap-good-corporate-practice.html>>. See also, 'OJK launches GCG roadmap', *Tempo.co* (online), 4 February 2014 <<http://en.tempo.co/read/news/2014/02/04/056550956/OJK-Launches-GCG-Roadmap>>. The roadmap is expected to improve corporate governance. It is a part of the preparation for the ASEAN Economic Community in 2015. It was formulated by the OJK and directly supported by the International Financial Corporation, a subsidiary of the World Bank. It is considered as one of the outcomes of the government effort by changing the capital market and financial institution supervisory agency [Bapepam-LK] to a broader scope and integral agency namely Financial Services Authority [*Otoritas Jasa Keuangan – OJK*] in 2011. It outlines strategic plans on corporate governance, shareholder protection, the role of stakeholders, transparency of information, and the role and responsibility of commissioners and directors. The road map re-emphasizes among others on transparency as the main reference in the capital market improvement and disclosure in accurate and timely manner as the main prerequisite in corporate governance. One of the strategies in place is the made available of a website for public companies to disclose material information in respect to investor able to make decisions in investing into a potential company.

cultures are likely to be more open to the possibility of employing soft law, such as codes, as lawyers do not merely refer to statutes as the only source of law unlike in civil law systems. This may partly explain why, in the Indonesian, that the code has not been a successful transplant of legal culture, as described in the previous chapter. However, good corporate governance principles, including disclosure promoted by the Code, have been reflected in the formal legal framework, as discussed below.

6.3. The legal framework supporting codes

Bedner's observations on the complexity of the Indonesian legal framework, as indicated in Chapter [5.4.5], provide explanations for the lack of support for using the Code as soft law or an informal rule. The main factor identified by Bedner includes the rooted mentality of lawyers and regulators in a civil law system struggling with concepts or models derived from common law systems. Their mentality are based on beliefs consisting of legislation as the only source of law, an uncritical use of poorly researched and written text books, a highly theoretical legal education void of skills in interpreting and applying the law and a lack of concern with consistency in decision making or *jurisprudence constante*. These are critical challenges to accommodating informal or soft law. Others, such as a Lev, see Chapter [5.4.5], accept that the ideas of what law pose challenges the use of involuntary codes.

These factors appear to have led Indonesia to approach corporate governance, particularly disclosure, in a formal way rather than relying on informal or soft law. This may also be seen to be characteristic of civil law jurisdictions as indicated in Chapter [3.6.].

To summarise, the GCG Code is not recognized by any law or any regulation, but provisions similar to the principles in the GCG Code can be seen in a number of laws and regulations. In particular, disclosure provisions have become mandatory in the stock exchange listing rules. The laws and regulations containing provisions on disclosure from the GCG Code are discussed below.

6.3.1. Legislative framework

Legislation and regulations relating to aspects of corporate governance found in the GCG Code do not directly refer to that part of the Code as binding law. Some relevant laws have incorporated and expressed the same general principles, including disclosure in

particular. The relevant laws are: 1995 Capital Market Law, 2007 Company Law, 1982 Company Registry Law, 2003 State-Owned Enterprises Law and regulations related to state-owned enterprises, Rules of the Capital Market Regulator and Stock Exchange, as well as Contractual framework of the Listing Rules, which are discussed immediately below.

6.3.1.1. Capital Market Law

Law No. 8 of 1995, the Capital Market Law, has been in use for about 19 years.¹³⁷⁷

It was promulgated prior to the introduction of the GCG Code. A number of Articles in the Law regulate aspects of disclosure. This can be seen in Article 1 (25), which stipulates that:

‘[t]he Disclosure Principle is the general guideline that requires an Issuer, a Public Company, and other Persons subject to this Law, to disclose to the public within a certain time, Material information with respect to their business or Securities, when such information may influence decisions of investors in such Securities and/or the price of the Securities’

The below table sets out the relevant disclosure principles, found in the GCG Code which are also embodied in the 1995 Capital Market Law.

Table 6.1: Relevant disclosure principles in the 1995 Capital Market Law

Article(s)	Theme(s)	Provision(s)	Description
75 (1)	Registration statements of issuers and public companies	Disclosure procedures for submitting registration statements	Ensuring the fulfilment of disclosure principles by BAPEPAM (OJK) based on considerations of completeness, adequacy, objectivity, comprehensiveness and clarity of a registration statement; BAPEPAM (OJK) evaluation of a security is not based on its

¹³⁷⁷ A copy of the Capital Market Law No. 8 of 1995 is available at <<http://www.ojk.go.id/id/kanal/pasar-modal/regulasi/undang-undang/Pages/undang-undang-nomor-8-tahun-1995-tentang-pasar-modal.aspx>>; An unofficial translation of the Law is available at <<http://www.slideshare.net/AdnanSiregar/indonesian-capital-market-actuu-no8-tahun-1995-tentang-pasar-modal>>. The Financial Services Authority [OJK) is now planning to revise the Capital Market Law. See, ‘2014, UU Pasar Modal bakal direvisi’ [Capital Market Law would be revised], *Tribun News* (online), 15 Agustus 2014 <<http://www.tribunnews.com/bisnis/2013/08/15/2014-uu-pasar-modal-bakal-direvisi>>.

			merits and weaknesses
78, 79	True and honest content of prospectuses and publications	Disclosure in prospectuses and publications	Prohibition of false statements and misleading material information in a prospectus, and in the mass media related to public offerings announcements.
80-81, 90 (1), 91, 92, 93	Liabilities of involved parties for disclosing false and misleading material information	Liability for false or misleading information	Consequences of disclosing false or misleading material information for persons signing the registration statements, the issuer's directors and commissioners, the managing underwriters, capital market supporting professionals, and other persons involved in the registration statement.
82-84		Disclosure in pre-emptive rights, conflicts of interest, tender offers, mergers, consolidations and acquisitions	Requirements for pre-emptive subscription rights to shareholders; requirements for obtaining approval from independent shareholders for transactions with conflict of interests; mandatory compliance with rules on disclosure, fairness and BAPEPAM (OJK) reporting rules for a tender offer, merger or consolidation.
85-89	Reporting and disclosing information	Requirements for reporting and disclosing information	Mandatory reports submission to BAPEPAM (OJK); requirements for periodic reports and publication; directors' and commissioners' mandatory reports on their share ownership; mandatory availability of all information to the public .

90 (1), 91, 92, 93	Fraud and market manipulation	Prohibition on fraudulent disclosure	Prohibition on disclosing false material information or misleading statements of conditions at the time; misleading appearance of trading activities, market conditions or the securities price.
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These disclosure provisions, as indicated in Chapter 2, reflect the Code’s principle of transparency, which requires timely, appropriate, clear, accurate and comparable information. It covers all information on the vision, mission, business targets, business strategy, financial condition, composition and compensation of the management; controlling shareholders, shares owned by members of the Board of Directors, the Board of Commissioners, their family members in the company and related companies; its risk management system, its oversight and internal control systems, its good corporate governance structure, mechanisms and the level of compliance with them and important events that may affect the condition of a company.

This Law, with related regulations on disclosure obligations, has been claimed to be largely irrelevant. It applies in practical terms to listed companies while, in practice, most enterprises in Indonesia are private companies.¹³⁷⁸

In the context of the 1995 Capital Market Law, the GCG Code may play a role in resolving ambiguities and other unregulated corporate governance issues. Some scholars, as indicated in the literature review, have considered this as a complementary function of informal law such as the code. Unfortunately, as indicated earlier, the Code does not serve this role.

6.3.1.2. Company Law and Company Registry Law

After twelve years in 2007, the Company Law (Limited Liability Company Law – UUPM) No. 1 of 1995 was replaced by the new Company Law no. 40 of 2007. The previous Law ‘was based largely upon twenty-one articles of the Indonesian Commercial

¹³⁷⁸ David Hayes, *Indonesian audit demand muted*, Accountancy Asia
 < <http://www.accountancyasia.com/news/indonesian-audit-demand-muted> > [7].

Code (the *Wetboek van Koophandel, Kitab Undang-undang Hukum Dagang* or “KUHD”), which were promulgated in 1847.¹³⁷⁹

The revision was part of a series of legal reforms leading to corporate law and governance convergence. This can be seen from the general Elucidation of the Law, which acknowledged that standardisation of Indonesian company law alongside other national law and international standards were driving forces for the revision.¹³⁸⁰ Ratnawati W Prasojo, the chair of the drafting team for the Law in the Department of Justice and Human Rights indicated that the aim of the revision on directors and commissioners’ duties was to adopt a stricter approach to accountability.¹³⁸¹

The 2007 Company Law introduced several revised and new provisions relating to corporate governance.¹³⁸² It more firmly states the law regarding directors’ and

¹³⁷⁹ Tabaluyan, ‘The new Indonesian Company Law’, above n 871, 883.

¹³⁸⁰ A copy of Law No. 40 of 2007 concerning Limited Liability Company is available at <<http://aria.bapepam.go.id/reksadana/files/regulasi/UU%2040%202007%20Perseroan%20Terbatas.pdf>>; An unofficial translation of the Law is available at <http://api.iuli.ac.id/storage/downloads/UU-040-2007-Perseroan_Terbatas-English.pdf>.

¹³⁸¹ Hukum online, *UUPT 2007 pertegas tanggung jawab direksi dan komisaris* [UUPT 2007 reaffirms the responsibilities of directors and commissioners] (16 Oktober 2007) [2] <<http://www.hukumonline.com/berita/baca/hol17807/uupt-2007-pertegas-tanggung-jawab-direksi-dan-komisaris>>. Sixteen articles [92–107] regulate the responsibilities and duties of board of directors and 14 articles [108–121] of board of commissioners.

¹³⁸² Some additional provisions with respect to the board of directors, including among others the obligation of directors to act in good faith and with full responsibilities in the best interests of the company require a minimum of one director for a private company, a minimum of two directors for public companies and companies that engage in the activities of pooling or managing public funds or issuing acknowledgements of indebtedness; personal liability for each member of the board of directors for all company losses and for the failure of their duty’s unless the evidence shows that the losses were not due to their role, or beyond their control. They are also required to prepare an annual business plan, including an annual budget, before the start of a financial year that must be presented to the board of commissioners or meet the GMS approval. With respect to the board of commissioners, the new law introduces some additional provisions including among others the obligation to supervise the policy and management of the company by the board of director, a minimum of one commissioner for a company unless it is a public company or companies engaged in the pooling and management of public funds, or issuing acknowledgements of indebtedness, which are required to have a minimum of two commissioners; personal liability for any losses for the failure of their duty’s unless they can prove otherwise and the introduction of independent and delegated commissioners; See, Hadiputranto, Hadinoto & Partners, *Indonesia’s new Company Law*, 5, 8–10 <http://www.hhp.co.id/files/Uploads/Documents/Type%202/HHP/br_hhp_indonesiasnewcompanylaw.pdf>. The new law has reinforced board of commissioners to a more involvement in a significant process. It can be seen from Article 64 (2) that the work or business plan (prepared by board of director as required in Article 63 requires an approval from the board of commissioners or

commissioners' duties.¹³⁸³ It mainly clarifies and reinforces their fiduciary duties and responsibilities.

Relevant provisions relate to disclosure can be seen in a table below.

Table 6.2: Relevant disclosure principles in the 2007 Company Law

Article(s)	Provision(s)	Description
8 (1) (2), 9 (1) (2), 12, 15	The establishment, articles of association and amendments of articles of association, registering of company and announcements	Requirements for information disclosed in the deed of establishment, in the application to obtain the ministerial decree for the company's legal entity, and in articles of association;

GMS, unless determined otherwise. The board of commissioners are also required to review an annual report prior to the submission to the GMS [Article 66]. Previous Law no. 1 of 1995 Article 57 has only imposed the signatures of the board of directors and board of commissioner on an annual report. The supervisory duties of commissioners are not only limited to supervise the management policy over the company, but also to its business [Article 108]. They are also required to analyse and sign an annual report [Article 66 (1) & 67 (1)]. The Law also requires the inclusion of a 'report on supervisory duty that has been performed by the Board of Commissioners during the previous accounting year' in an annual report [Article 66 (2e)].

¹³⁸³ Hukum online, *UUPT 2007 pertegas tanggung jawab direksi dan komisaris*, above n 1381, [2]; See also, Miko Kamal, *The new Indonesian Company Law: Does it support good corporate governance?* (August 2008) Macquarie University, 16 <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1215867>. List of roles of board of commissioners under Law No.40 of 2007: To receive annual plan [Article 64 (1)] – should be stated in the company's article of association, To approve work plan [Article 64 (2)] – should be stated in the company's articles of association, as long as it does not violate other rules, To analyse annual report (article 66 (1), To sign company's annual report [Article 67(1)], To approve interim dividend [Article 72 (4)], To call shareholders for holding general meeting – based on court's decision [Article 81 (2)], To decide board of management's remuneration – should be authorized by GMS [Article 96 (2),(3)], To represent company in a court – if there is conflict of interest from all of members of board management [Article 99 (2b)], Top suspend member of board of management [Article 106 (1)], To give a writing approval or to assist board of directors to do particular legal action – should be stated in the company's articles of association [Article 117 (1)], To organize company in particular condition and time – should be stated in teh company's articles of association [Article 118 (1)], To approve draft of merger of company (article 123 (3); and to approve the take over of the company [Article 125 (6)]; Cf, Previous Law no. 1 of 1995 Article 57 was only imposed the signatures of board of directors and board of commissioner on an annual report. It was only stipulated supervision duty over the management policy regarding the Company [Article 97]. In Indonesian context, the company organs are the General Meeting of Shareholders [Rapat Umum Pemegang Saham – RUPS], the board of directors and the board of commissioners [Article 1 (2)].

		requirement for disclosing legal actions relating to share ownership
29	Company registry and announcement	Requirements for disclosing data concerning the company
63, 66	Work plans, annual reports, and the use of profit	Requirement for board of directors to prepare an annual work plan prior to the commencement of the coming financial year; Requirement for an annual report submission to the General Meeting of Shareholder (GMS)
68	Annual report	Requirement for an audit by a public accountant of the annual report

Article 68 is a new provision that requires directors provide financial reports audited by a public accountant and published in a newspaper. This applies to public companies, companies that engage with pooled public funds or collection investment, companies that issue acknowledgement of indebtedness to the public and companies with a turnover of at least IDR 50 billion.¹³⁸⁴

This requirement, for a mandatory audit, was expected to lead to a boom in demand for auditors but compliance with the provision has turned out to be a significant issue. It is claimed that ‘accounting firms that expected a sudden increase in audit work have been disappointed’.¹³⁸⁵ The lack of compliance is attributed to the absence of enforcement action. Ahmadi Hadibroto, the president of the Indonesian Institute of Accountants (IIA), admitted that ‘the law is not effective. Accountancy laws and regulation become a

¹³⁸⁴ Law No. 40 of 2007 concerning Limited Liability Company.

¹³⁸⁵ Hayes, above n 1378, [2]–[5].

disincentive.’ Directors and commissioners do not regard themselves as obliged to prepare a proper financial report. Audits are a negotiation between the auditor and the corporate client.¹³⁸⁶ The low number of qualified auditors is part of the problem. About 3 000 qualified CPAs (Certified Public Accountants) serve a country of 240 million people. The factors contributing to the shortage of numbers includes concerns around personal liability risk. Less than 50 newly qualified CPAs join the profession each year with most accounting students preferring to work in the more protected space of internal audit.¹³⁸⁷

Another new development in the legislation was the introduction of independent commissioners [*komisaris independen*] and representatives or delegated commissioners [*komisaris utusan*] in Article 120.¹³⁸⁸ This has been claimed to be an adoption of the Australian one tier board model, which was proposed by Forum for Corporate Governance in Indonesia (FCGI) through the National Commission on Governance Policy (KNKG) and incorporated into the Law.¹³⁸⁹

The board of commissioners may establish committees to support their supervisory duties [Article 121], for example, an audit committee.¹³⁹⁰ This reflects that the significance of an audit committee has been acknowledged and accommodated by the law. It is optional and not mandatory. However, an audit committee is mandatory under the IDX listing rules and OJK regulations.¹³⁹¹ This adopts the OECD recommendation that audit committees should be mandatory in listed companies.¹³⁹²

¹³⁸⁶ Ibid. See also, [12]

¹³⁸⁷ Ibid [7]–[9], [10]

¹³⁸⁸ There is no definition of Representative or Delegated commissioner. See, eg, Hukum online, *UUPT 2007 pertegas tanggung jawab direksi dan komisaris*, above n 1381, [12]–[13]. Ratnawati Prasajo portrayed a delegated commissioner as almost similar as a compliance director. Partomuan Pohan, a senior notary, further described its function as ‘from day to day commissioners’. A delegated commissioner is expected to be in the office by day, which enable them to perform effective control over the company.

¹³⁸⁹ Kamal, *The new Indonesian Company Law*, above n 1383, 19. ‘

¹³⁹⁰ Law No. 40 of 2007 concerning Limited Liability Company.

¹³⁹¹ See, KEP-339/BEJ/07-2001 and Keputusan Ketua Badan Pengawas Pasar Modal dan Lembaga Keuangan [Decree of Capital Market and Financial Institution Supervisory Agency] No. KEP-643/BL/2012 tentang Pembentukan dan Pedoman Pelaksanaan Kerja Komite Audit [Establishment and Practical Guidelines for Audit Committee]; See also, Muh Arief Effendi, *Pedoman pembentukan komite audit yang efektif* disusun untuk Komite Nasional Good Corporate Governance [A code for the establishment of an effective audit committee was arranged to a

The mandatory requirement for audit committees appears to not be effective in practice. The Chair of the OJK board of audit, Ilya Avianti, revealed that the establishment of an audit committee has been seen as merely fulfilling a formality. In practice, the chair of an audit committee is generally one of the members of the board of commissioners and their friends are appointed as members. A member of an audit committee is also often appointed by a number of companies, making it difficult for them to fulfil their duties.¹³⁹³ Daniri, the chair of KNKG, has also indicated that the appointment of independent commissioners and audit committees is a mere formality rather than making the supervisory functions of the board of commissioner more effective.¹³⁹⁴ This is another example of ineffective legal transplants in the context of Indonesia.

Kamal shares the pessimism about the effective implementation of good corporate governance in boards of commissioners in the 2007 Company Law. He argued that fundamental principles governing professionalism of member of the board of commissioners does not exist in the Law.¹³⁹⁵ He claims that the board of commissioners are in a weak position in the absence of ‘rights to appoint and dismiss the board of management’.¹³⁹⁶ The Law also provides a loophole by which ministerial departments and their individual officials may collect levies that put additional business costs on companies.¹³⁹⁷

national committee] (2002) 3 <<https://muharieffendi.files.wordpress.com/2009/12/pedoman-pembentukan-komite-audit-yang-efektif-knkcg.pdf>>.

¹³⁹² Organization for Economic Co-Operation and Development (OECD), ‘Implementing the white paper on corporate governance in Asia – Stock-take of progress on priorities and recommendation for reform’ (Asian Roundtable on Corporate Governance, October 2006) 53 <<http://www.oecd.org/corporate/ca/corporategovernanceprinciples/38120678.pdf>>.

¹³⁹³ Akuntan Online, *OJK akan batasi rangkap jabatan komite audit* [OJK would limit double position of audit committee] (18 Juli 2013), [4] <<http://akuntanonline.com/showdetail.php?mod=art&id=616&t=OJK%20Akan%20Batasi%20Rangkap%20Jabatan%20Komite%20Audit&kat=Organisasi>>. As indicated in the previous chapter, Indonesian companies were previously not required to establish an audit committee; See generally, Kurniawan and Indriantoro, above n 125, 5.

¹³⁹⁴ Daniri, *Good corporate governance*, above n 157, 186.

¹³⁹⁵ Kamal, *The new Indonesian Company Law*, above n 1383, 3.

¹³⁹⁶ *Ibid* 22.

¹³⁹⁷ Akuntan Online, *Harus ada sanksi pelanggar pasal 68 UU No. 40/2007* [Should have sanctions for violators of article 68 of UU No.40/2007] <

Another relevant law but not significant is the Law No. 3 of 1982 concerning Mandatory Company Registration, which also imposes disclosure requirements. The Law requires all companies to register and disclose information about their company's identity and its business.¹³⁹⁸ This Law also reflects similar issues in practice. The requirements for the mandatory audit of financial reports stipulated in it have been ignored by all companies due to the absence of any effective sanctions.¹³⁹⁹

6.3.1.3. State-Owned Enterprises Law and regulations relating to state-owned enterprises

A relevant legislation and some regulations relating to aspects of disclosure for state-owned enterprises (SOEs) found in the 2003 State-Owned Enterprises Law and several ministerial regulations and Bank Indonesia's regulations as discussed below.

(a) The State-Owned Enterprises Law

Good corporate governance principles promoted by the GCG Code are also embodied in Law No. 19 of 2003 concerning State-Owned Enterprises (SOEs), locally known as *UU BUMN*. Article 5 (3) and Article 6 (3) require the SOEs to implement good corporate governance principles. The Elucidation for the Law restates that the SOEs management and supervision should be conducted on the basis of good corporate governance principles.¹⁴⁰⁰

Several relevant disclosure provisions can be seen in the below table.

<http://akuntanonline.com/showdetail.php?mod=art&id=291&t=Harus%20Ada%20Sanksi%20Pelan%20Pasar%2068%20UU%20No%2040/%202007&kat=Auditing>>.

¹³⁹⁸ Law No. 3 of 1982 concerning Mandatory Company Registration is available at <<http://www.hukumonline.com/pusatdata/detail/54/node/75/uu-no-3-tahun-1982-wajib-daftar-perusahaan>>. An unofficial English version of the Law is available at <<http://www.flevin.com/id/lgs0/translations/JICA%20Mirror/english/2.03.1982.eng.qc.html>>.

¹³⁹⁹ Ahmadi Hadibroto – Chairman of Indonesia Accountant Association (AAI), ‘Dua kenangan yang tak terlupakan sampai akhir hayat’ [Two unforgettable memories till the end of my life], *Majalah Akuntan Indonesia* [Indonesian Accountant Magazine], edition no,1/Tahun I/Agustus 2007, 24 <http://74.220.207.194/~iaigloba/storage/ref_14.pdf>. See, Keputusan Menteri Perindustrian dan Perdagangan No. 121/MPP/Kep/2/2002 tentang Ketentuan Penyampaian Laporan Keuangan Tahunan Perusahaan [Decree of Minister for Industry and Trade No. 121/MPP/Kep/2/2002 concerning Provisions for Submitting Annual Reports of Companies] requires a mandatory annual audited financial report [Article 2 (3)]. Article 13 stipulates sanctions referring to Law No. 3 of 1982 concerning Mandatory Company Registry [Articles 34 (1) and 35].

¹⁴⁰⁰ Shalahuddin, above n 563, 24; See generally, The Law No. 19 of 2003 concerning State Owned Enterprise (SOE) is available at <www.komisiinformasi.go.id/regulasi/download/id/100>.

Table 6.3: Relevant disclosure principles in the 2003 State-Owned Enterprise Law

Article(s)	Provision(s)	Description
5 (3)	General provisions	Mandatory implementation of principles of professionalism, efficiency, transparency, independence, accountability, responsibility and fairness for directors
6 (3)	General provisions	Mandatory implementation of principles of professionalism, efficiency, transparency, independency, accountability, responsibility and fairness for the board of commissioners and <i>Dewan Pengawas</i> (the board of supervisors for Perum). ¹⁴⁰¹
70	Audit committee and other committee	Mandatory establishment of audit committee.

(b) Other relevant regulations

Besides the Law, a number of government regulations (PP), presidential decrees (*Keppres*) and ministerial regulations (*Permen*) also contain disclosure provisions, as can be seen in the below tables.

Table 6.4: Government regulations [PP] relating to disclosure

Regulation Number	Theme(s)	Description
PP No.64 of 1999 ¹⁴⁰² Article 4	Company annual financial information	Requirement for annual financial report from all limited liability companies including public companies; companies that engage with pooled public funds and collection investment; companies that issue acknowledgement of indebtedness to the public; and companies with a turnover of at least IDR 25 billion (previously IDR 50 billion) must be audited by public accountant.
PP No. 8 of 2006 ¹⁴⁰³	Financial and	Mandatory financial and performance

¹⁴⁰¹ Dewan Pengawas supervises and provides advices to the board of directors in carrying out the business activities of the Perum [public corporation]. See, Article 1 (8) Law No. 19 of 2003 concerning State Owned Enterprises], available at <<http://www.hukumonline.com/pusatdata/detail/13588/node/535/uu-no-19-tahun-2003-badan-usaha-milik-negara>>.

¹⁴⁰² This regulation is available at <http://dapp.bappenas.go.id/website/peraturan/file/pdf/PP_1999_064.pdf>. The introduction of this regulation was among the efforts to improve transparency (disclosure).

	Performace Reporting of State Institutions	reports for state institutions.
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Ministerial regulations relating to disclosure can be seen in the *Peraturan Menteri Negara Badan Usaha Milik Negara* [State-Owned Enterprises Minister Regulation] No.PER-01/MBU/2011 concerning the implementation of Good Corporate Governance.¹⁴⁰³ Article 1 and 12 of this regulation has been revised under the SOE's Minister Regulation No.PER-09/MBU/2012.¹⁴⁰⁵ The particular disclosure is described in a table below.

Table 6.5: Relevant disclosure principles in the Ministerial Regulation for State Owned Enterprises No.PER-01/MBU/2011

Article(s)	Disclosure provision(s)	Description
2,3	Mandatory implementation of good corporate governance referring to principles of transparency, accountability, responsibility, independency, and fairness.	SOEs are required to implement good corporate governance consistently and continuously; directors are required to provide for this in the company's manual.
19 (3) (4)	Duties and responsibilities of directors	Mandatory disclosure in a annual report relating to directors duties and responsibilities, share ownership including their family members.
31	External auditor	Board of commissioner or supervisory board propose potential external auditors who are to be appointed by General Meeting of Shareholders or the Minister.
34	The openness of information	Mandatory disclosure of significant information in an annual report and a financial

¹⁴⁰³ This regulation is available at <<http://www.djpk.depkeu.go.id/attach/post-pp-no-8-tahun-2006-tentang-pelaporan-keuangan-dan-kinerja-instansi-pemerintah/PP82006LAKIP.pdf>>.

¹⁴⁰⁴ This regulation is available at <https://askrindo.co.id/new/files/data/uu/PER-01_MBU_2011_PENERAPAN_TATA_KELOLA_PERUSAHAAN_YANG_BAIK_-_GCG.pdf>.

¹⁴⁰⁵ This regulation is available at <<http://bumn.go.id/data/uploads/files/1/PER-09~1.PDF>>.

		report based on the law and regulations in timely, accurate, clear and objective manner.
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Other relevant ministerial regulations include SOE's Minister Decrees No. Kep-103/MBU/2002, No.Kep-117/M-Mbu/2002 and Finance Minister Regulation No.88/PMK.06/2015¹⁴⁰⁶ as can be seen in the below table.

Table 6.6: Relevant disclosure principles in other ministerial regulations and decrees

Type(s) of regulation	Theme(s)	Provision(s)
SOE's Minister Decree No. Kep-103/Mbu/2002 Article 3 (a) (c)	The Establishment of Audit Committee for SOE	The establishment of Audit committee for assisting commissioners/supervisory board in performing their duties [Article 1]; the function of Audit committee to review internal and external auditing in order to prevent inappropriate reports, satisfactory procedures for disclosed information [Article 3 (a)(c)]
SOE's Minister Decree No. Kep-117/M-Mbu/2002	Good corporate governance implementation in SOEs	Mandatory implementation of good corporate governance for SOEs including transparency, independency, accountability, and fairness principles
Finance Minister Regulation No.88/PMK.06/2015	Good corporate governance implementation in state owned limited liability companies [<i>Persero</i>] under supervision of Minister for Finance	Requirement to implement good corporate governance consistently and continuously; requirement for directors to arrange codes of good corporate governance including guidelines for directors, risk management, internal controlling system, reporting mechanism for suspect deviations,

¹⁴⁰⁶ These SOE's Minister Decrees are available at <http://auditorinternal.com/wp-content/uploads/2010/01/sk_117_2002_gcg_bumn.pdf>; This Finance Minister Regulation is available at <<https://www.djkn.kemenkeu.go.id/2013/peraturan/detail/pmk-nomor-88pmk062015>>.

		information technology governance and code of ethics
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These government and ministerial regulations and decrees reflect the Code's principles of good corporate governance including transparency, independency, accountability and fairness, which its implementation of is mandatory for SOEs. But, as indicated earlier, the performance of good corporate governance including disclosure is poor.

(c) Bank Indonesia regulations

In the banking sector, Bank Indonesia [Central Bank] has imposed the implementation of good corporate governance including transparency in several regulations such as regulations number 8/4/Pbi/2006, 8/14/PBI/2006, No. 7/50/PBI/2005 and No.14/14/PBI/2012¹⁴⁰⁷ as can be seen in the below table.

Table 6.7: Relevant disclosure principles in the Bank Indonesia regulations

<i>Bank Indonesia [central bank] regulation(s)</i>	Theme(s)	Description
No. 8/4/Pbi/2006 and 8/14/PBI/2006	Good corporate governance implementation for commercial banks	Mandatory to implement good corporate governance in banking activities at all organisational levels
No.7/50/PBI/2005	Transparency of banks financial condition	Mandatory for banks to arrange and provide financial reports
No. 14/14/PBI/2012	Transparency and publication of banking report	Mandatory annual report with a minimum disclosure of general information; annual financial report; opinion of public accountant; risk exposures; all transparency aspects; other disclosure and

¹⁴⁰⁷ These regulations are available at Bank Indonesia, *Kodifikasi Peraturan Bank Indonesia: Likuiditas Rupiah – Transparansi dan Publikasi Laporan* [Codification of Bank Indonesia Regulations: Rupiah Liquidity – Transparency and Publication of Reports] <http://www.bi.go.id/id/peraturan/kodifikasi/bank/Documents/Kodifikasi-Transparansi%20Kondisi%20Keuangan%20_%20Complete.pdf>.

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Ultimately, this legislative regime does not work effectively. Those laws and regulations may not be enforced, or if enforced the interpretation given to them alter their meaning or substance. Some laws and regulations deal with controversial and problematic issues. A number are perceived as obstructing economic development.

In practical terms, the formal laws described in Tables 6.1–6.6 are often inadequate and unenforceable. They have been described as ‘*macan kertas*’ [paper tigers].¹⁴⁰⁸ Lubis and Santosa described them as neither comprehensive nor properly implemented. Many new packages of laws are seen as ‘piecemeal and showed no consideration of justice’ as they served the political needs of authorities. Sembel claimed that they are limited by their symbolism and are only complied with to fulfil formalities, particularly by listed companies.¹⁴⁰⁹

The lack of effective law enforcement has long been regarded as a crucial problem in Indonesia that severely impacts on the legal and regulatory system’s credibility. Inconsistencies in law enforcement and the lack of transparency have led to the loss of trust in the laws and the processes to enforce them.¹⁴¹⁰ Surya and Yustiavandana as well as others have also pointed out that the poor performance of judicial institutions has led to the loss of trust in the legal system. Judicial decisions often produce inconsistent outcomes, which are often attributed to the ambiguity or vagueness of the laws.¹⁴¹¹

Those problems relate to Soeharto’s legacy as indicated in Chapter 4, where the control of the judiciary by Soeharto further weakened the rule of law. The political

¹⁴⁰⁸ Akuntan Online, *Harus ada sanksi pelanggar pasal 68 UU No. 40/2007*, above n 1397.

¹⁴⁰⁹ Denoan Rinaldi, ‘Roy Sembel: GCG harus jadi kultur dalam perusahaan’ [Roy Sembel: GCG should be company’s culture], *SWA Magazine* (online), 7 January 2013 < <http://swa.co.id/wp-content/uploads/2013/01/Roy-Sembel.jpeg>>.

¹⁴¹⁰ Komisi Pemberantasan Korupsi, *Strategi nasional pencegahan & pemberantasan korupsi – Jangka panjang (2012–2025) dan jangka menengah (2012–2014)* [National strategy for prevention & eradication of corruption – Long term (2012–2025) and mid term (2012–2014)] 13 <<http://acch.kpk.go.id/documents/10157/34337/Dok+Stranas+PPK+2012-2025.pdf>>.

¹⁴¹¹ Surya and Yustiavandana, above n 65, 126–7. See also, Chapter [5.4.5] The complexity of transplanted laws in the Indonesian context.

interference is claimed to have further corrupted the judicial system and degraded the integrity of the judges, see Chapter [4.3] and Chapter 5.

The loss of trust in the legal system could justify the role of the GCG Code as a voluntary code. It indicates that Indonesia may need to use informal or soft law such as the code to create trust, as suggested by a number of scholars including Millstein, De Soysa and Jutting, Helmke and Levitsky, Aldasev, Pistor and North, as the summary of the literature in Chapter [2.4.2]–[2.4.4] shows.

6.3.1.4. Rules of the Capital Market Regulator and Stock Exchange

As indicated in the introduction, the disclosure provisions of the GCG Code have become mandatory under the capital market regulations and listing rules. These rules have also, therefore, impacted on the GCG Code's status as informal or soft law and also on its potential, with this status, to supplement formal law.

Regulations on disclosure in the capital market are still those issued by the Bapepam-LK despite it being replaced by the OJK (Indonesia's Financial Services Authority). This is an independent regulatory body that was established under Law No. 21 of 2011.¹⁴¹² The OJK's duties and function is to regulate and supervise all financial services sectors to ensure sound financial industries. It has regulatory and supervisory duties over financial services activities in the capital markets, banking, and non-bank financial sectors.¹⁴¹³ With respect to improving the quality of disclosure, the Bapepam-LK and IDX issued *Pedoman Pelaporan Perusahaan* [Code of Company Reporting].¹⁴¹⁴

There are no rules requiring mandatory compliance with the GCG Code, but a number of Bapepam-LK (OJK) rules require mandatory disclosure. The relevant regulations on mandatory disclosure can be seen in the below tables.

¹⁴¹² The OJK has taken over the Bapepam-LK duties and functions since 31 December 31 2012 as well as banking regulation and supervision of Bank Indonesia on 31 December 2013 under Article 55 Law No. 21 of 2011 concerning Financial Services Authority. A copy of the Law is available at <<http://www.bi.go.id/id/tentang-bi/uu-bi/Documents/UU21Tahun2011.pdf>>.

¹⁴¹³ See Indonesia Financial Services Authority, *Duties and function* <<http://www.ojk.go.id/en/duty-and-function>>. The main function of the OJK is 'to promote and organize a system of regulations and supervisions that is integrated into overall activities in the financial services sector'. See also, Gonthor R Aziz, *Otoritas Jasa Keuangan (OJK) – Indonesia Financial Services Authority*, 2 <<http://www.oecd.org/finance/financial-markets/49703438.pdf>>.

¹⁴¹⁴ Daniri, *Good corporate governance*, above n 157, 63.

Table 6.8: Main rules of the Bapepam-LK (OJK) requiring mandatory disclosure

<p>Rule VIII.G.7¹⁴¹⁵</p>	<p>Decree No. KEP-347/BL/2012</p>	<p>Presentation and disclosure of issuers' or listed entities' financial statements.¹⁴¹⁷</p> <p>Regulation of obligation to submit annual report for issuers of securities or public companies. (Mandatory disclosure)¹⁴¹⁸</p> <p>Require hard copy and soft copy reports; disclose on the website; more detailed information; additional information on shareholder's scheme, code of conduct, company's culture and whistle blowing system.</p>
	<p>OJK Regulation No. 31/POJK.04/2015¹⁴¹⁶</p>	<p>Openess of information or material facts from issuers or public companies.</p> <p>Regulation of obligation to submit reports of information or material facts to OJK and its announcement to public.</p>

¹⁴¹⁵ This rule is available at Indonesian Financial Services Authority, *Regulation – Capital Market: Reporting requirements for issuers and public companies* <<http://www.ojk.go.id/en/reporting-requirements-for-issuers-and-public-companies>>.

¹⁴¹⁶ This regulation is available at <<http://www.ojk.go.id/id/kanal/pasar-modal/regulasi/peraturan-ojk/Documents/Pages/pojk-31-keterbukaan-atas-informasi-fakta-material-oleh-emiten-perusahaan-publik/SALINAN-POJK%20Keterbukaan%20Informasi%20Emiten.pdf>>.

¹⁴¹⁷ PricewaterhouseCoopers, *A practical guide to the revised Bapepam-LK VIII.G.7* <<http://www.pwc.com/id/en/publications/assets/a-practical-guide-to-new-bapepam-lk-viiiig7.pdf>>. This rule is seen as a convergence of Indonesian Financial Accounting Standards (PSAKs) with the International Financial Reporting Standards (IFRS). The rule accommodated new accounting standards introduced by (PSAKs) meeting with IFRS.

¹⁴¹⁸ This rule has covered the absence of introduction of disclosure of the board's remuneration from the good corporate governance code. See, Tim Studi Kementerian Keuangan Republik Indonesia Badan Pengawas Pasar Modal dan Lembaga Keuangan, above n 1368, 37.

In more detail, the disclosure provisions introduced in the 2012 revised rule include:¹⁴¹⁹

- 1) the submission of an annual report in the form of hard and soft copy
- 2) an obligation to place the annual report on the issuer's or public company's website
- 3) more detailed information to be disclosed including company profile, board of commissioners, directors, audit committee, company secretaries and internal audit; any affiliations between members of the board of commissioners and directors and shareholders; as well as internal control system and risk management
- 4) additional information regarding shareholders' schemes and company control; the code of ethics and corporate culture; Employee Stock Option Program (ESOP) and Management Stock Option Program (MSOP)¹⁴²⁰; whistle blowing scheme and a new requirement to disclose both direct or indirect ultimate principal and controlling shareholders in the form of diagrams or charts¹⁴²¹
- 5) information on corporate social responsibility
- 6) confirmation of the board of commissioners' and directors' responsibility statement for the accuracy of the annual report;

Other relevant rules¹⁴²² can be seen in the table below.

Table 6.9: Other relevant rules of BAPEPAM-LK relating to disclosure

Rule No. X.K.1	Decree No. Kep-86/PM/1996 (January 24, 1996) substituted prior decision No. Kep-22/PM/1991 (April 19, 1991)	Disclosure of information that must be made public immediately
Rule No. X.K.5	Decree No. Kep-46/PM/1998 (August, 14 1998)	Disclosure of information by issuers or public companies regarding bankruptcy - Disclosure of information by issuers and public

¹⁴¹⁹ 'Bapepam introduces requirement for the disclosure of ultimate shareholders', *LGS Newsletter* (online), 20 December 2012 <<http://www.lgsonline.com/pages/g/lgs506565a5e4312/node/lgs4a1d783104616>>.

¹⁴²⁰ See, Indonesia Stock Exchange, *Daftar istilah* [Acronym] <<http://www.idx.co.id/id-id/beranda/daftar-istilah.aspx>>.

¹⁴²¹ Previous rule was only required to disclose direct shareholders with equal to or more than five per cent ownership.

¹⁴²² These rules are available at <<http://www.ojk.go.id/id/kanal/pasar-modal/regulasi/peraturan-ojk/Default.aspx>>.

		companies with respect to declarations of bankruptcy
Rule X.K.2	Decree No. KEP-36/PM/2003	Obligation to submit periodical financial statement (implement disclosure principle)
Rule X.K.4	Decree No. KEP-28/PM/2003	Reports on the use of funds received from a public offering; and Guidelines for asset backed securities collective investment contracts
Rule No. IX.C.1	Attachment of Decree No. Kep-42/PM/2000	Form and content of a registration statement for a public offering (disclosure in primary market)
Rule IX.H.1		Ownership disclosure requirement
Rule No. IX.1.5	Decree No. KEP-643/BL/2012	The establishment and guidelines for audit committee duties ¹⁴²³
	21 December 2012	Check list for disclosure ¹⁴²⁴

Rules for disclosures by company directors involved in conflicted transactions do not exist. This issue has undermined the effectiveness of the other efforts for a mandatory approach for disclosure.¹⁴²⁵

6.3.1.5. Contractual framework of the Listing Rules

The listing regulations of Indonesia Stock Exchange (IDX), do not require mandatory compliance with the GCG Code. Notwithstanding, there are a number of regulations specifically requiring listed companies to maintain good corporate governance practices including disclosure.

Listed companies, for example, are required to have a mandatory minimum of thirty percent independent commissioners and one independent director, and an audit committee with a minimum of three members. It also prohibits corporate actions that may disadvantage shareholders as well as penalties for untimely submission of financial

¹⁴²³ See, General provision 1 (b) requires a mandatory audit committee for issuer or public company. This rule is available at <http://www.bapepam.go.id/pasar_modal/regulasi_pm/peraturan_pm/IX/IX.I.5.pdf>.

¹⁴²⁴ Otoritas Jasa Keuangan (OJK) [Indonesia Financial Services Authority], *Checklist pengungkapan laporan keuangan* [A checklist of financial report disclosure] (21 December 2012) <<http://www.ojk.go.id/checklist-pengungkapan-laporan-keuangan>>. The checklist consists of 83 pages.

¹⁴²⁵ CLSA Asia-Pacific Markets, CG Watch 2012, above n 62, 104.

statements, a minimum of yearly publication in mass media and stricter disclosure practices.

In respect to disclosure, some relevant regulations¹⁴²⁶ can be seen in the table below.

Table 6.10: Indonesia Stock Exchange (IDX) regulations on disclosure

Rule No. I-E [Kep-306/BEJ/07-2004]	Obligation of Information Submission
Rule No. I.A.3 [SK-020/LGL/BES/XI/2004]	Issuers Reporting Obligation

Despite these regulations and rules with their stricter approach to disclosure, compliance is unsatisfactory. The IDX has acknowledged that the compliance level of issuers has increased. Hoesen, the director of IDX company assessment, revealed that untimely financial reporting in 2012 had increased compared to the year before from 24 issuers to 29 issuers.¹⁴²⁷ An official report of the IDX division on company valuations in 2013 recorded that 57 issuers had delayed submitting their 2013 audited financial reports and 49 of them had been sanctioned with notices.¹⁴²⁸ In the same year, IDX recorded 370 sanctions with 1st notices, 117 with 2nd notices, and 37 with 3rd notices as well as 151 fines and 18 suspensions. Most of the sanctions related to delayed financial reporting or failure to report.¹⁴²⁹

¹⁴²⁶ These rules are available at

<<http://www.idx.co.id/en-us/home/regulation/listingregulations.aspx>>.

¹⁴²⁷ 'BEI akui tingkat kepatuhan emiten menurun – 29 emiten telat laporan keuangan' [BEI admitted a decrease of the level of issuer's compliance – 29 issuers delayed their financial reports], *Neraca.co.id* (online), 14 Agustus 2012, [2] < <http://m.neraca.co.id/article/17872/BEI-Akui-Tingkat-Kepatuhan-Emiten-Menurun>>.

¹⁴²⁸ Amalia Putri Hasniawati, 'Ini dia 49 emiten yang kena sanksi BEI' [Here the 49 issuers that received sanctions from the IDX], *Kontan news* (online), 14 April 2014 < <http://investasi.kontan.co.id/news/ini-dia-49-emiten-yang-kena-sanksi-bei>>. See also, Amalia Putri Hasniawati, '57 emiten belum menyerahkan laporan keuangan 2013' [57 issuers have not submitted their 2013 financial reports yet], *Kontan news* (online), 14 April 2014 < <http://investasi.kontan.co.id/news/57-emiten-belum-menyampaikan-laporan-keuangan-2013/2014/04/14>>.

¹⁴²⁹ Bursa Efek Indonesia, 'Tahun 2013, BEI mencatatkan rekor 31 emiten baru dan peningkatan likuiditas sebesar 37,68 %' [In 2013, BEI recorded new 31 issuers and an increase of 37.60 % liquidity] (Siaran Pers, Kegiatan pembinaan dan pemantauan perusahaan tercatat [Press Release, Activities of development and supervisory of listed companies], 30 Desember 2013)

Mandatory disclosure, overseen by the Financial Services Authority (OJK) and Indonesia Stock Exchange (IDX), has been expected to establish better and more reliable financial reports. However, compliance with disclosure requirements is still seen as a mere formality. Santosa found that the compliance with disclosure has been driven by the avoidance of sanctions rather than creating a corporate culture of better disclosure.¹⁴³⁰

This reflects an earlier study by the Indonesian Institute for Corporate Governance (IICG) in 2001. It demonstrated that 65 per cent of participants implemented good corporate governance measures including disclosure because the regulations obliged them to do so.¹⁴³¹ Daniri indicates that this is a similar attitude to that found in the appointment of independent commissioners and audit committees. This is done to comply with formalities rather than to empower the supervisory functions of the board of commissioners to be more effective supervisors.¹⁴³²

Since compliance with disclosure is mainly driven by fulfilling formalities, it raises the main issue of its reliability. The poor system of supervision of companies may contribute to this persistent issue. Nurhaida, Chief Executive of OJK Capital Market Supervision, stated that compliance supervision is based on a risk-based approach. Companies that have indications that they are in trouble or high risk will be looked at first, and that compliance supervision does not extend to all companies in the same year.¹⁴³³

The poor quality of disclosure reflects the focus on formal compliance, lack of professionalism by accountants and corporate officers and the weak enforcement of disclosure regulation. Lack of sanctions is one example of the absence of effective

<<http://www.idx.co.id/Beranda/BeritadanPengumuman/SiaranPers/ReadPressRelease/tabid/191/ItemID/8d4dcf4c-da9f-4613-8e59-8dfb3a5bffc0/language/id-ID/Default.aspx>>.

¹⁴³⁰ Santosa, above n 87, 193.

¹⁴³¹ Surya and Yustiavandana, above n 65, 60–1.

¹⁴³² Daniri, *Good corporate governance*, above n 157, 186.

¹⁴³³ Ria Pratiwi, 'OJK: Perusahaan pemenang ARA biasanya punya GCG bagus' [ARA winners are usually having an excellent GCG], *SWA News* (online), 2 May 2014. Compliance supervision would not apply to the Annual Report Award (ARA) winner. ARA has been seen as an indicator of good corporate governance practices. It is believed that the winner has demonstrated a good corporate governance implementation referring to transparency and accountability as the determinant factors attributed to good corporate governance practices. Annual Report Award (ARA) is conducted by OJK with collaboration to Bank Indonesia, Indonesia Stock Exchange (BEI), Minister of Finance Directorate General for Tax, Minister of State Owned Enterprises, and National Commission on Governance Policy (KNKG).

sanctions as the claim that ‘IDX only tends to issue a “cooling-off notice” to suspend the shares for one or two days and then lifts the suspension.’¹⁴³⁴ A number of cases support this. Formal investigations increased from 130 cases in 2010 to 178 cases in 2011, but only 63 cases were completed, and just 59 cases received administrative sanctions, while 115 cases remained open. Lack of financial and human resources of the OJK and the IDX as well as a lack of cooperation between them have been claimed to be factors contributing to the lack of their enforcement.¹⁴³⁵

Heavy penalties with a large fine, however, do not appear to be deterrence. IDX applies IDR1 million (approximately US \$77¹⁴³⁶) fines per day.¹⁴³⁷ A report revealed that a fine of IDR500 million (approximately US\$38 461¹⁴³⁸) has still not deterred an issuer from submitting an untimely financial report.¹⁴³⁹ The Bapepam-LK fined 50 listed companies IDR 1.029 billion (approximately US\$79 000¹⁴⁴⁰) between January to 2 March 2011 for delays with financial reports.¹⁴⁴¹ There was untimely disclosure of 28 listed companies reported in October 2011¹⁴⁴² Bapepam-LK sanctioned 375 market participants with total fines of IDR 13.08 billion (approximately US\$1 000 000). In 2012 it issued 40 notices to

¹⁴³⁴ CLSA Asia-Pacific Markets, CG Watch 2012, above n 62, 104.

¹⁴³⁵ Ibid 104–5.

¹⁴³⁶ 1 US\$ equals 13,000 IDR

¹⁴³⁷ Whery Enggo Prayogi, ‘Dua emiten membandel belum lapor kinerja keuangan’ [Two issuers have still not submitted their financial performance], *Detik.com* (online), 14 Oktober 2011 <<http://finance.detik.com/read/2011/10/14/161805/1744261/6/dua-emiten-membandel-belum-lapor-kinerja-keuangan>

¹⁴³⁸ 1 US\$ equals 13,000 IDR

¹⁴³⁹ Dewi Rachmat Kusuma, ‘Denda Rp. 500 juta belum bikin emiten jera telat beri laporan keuangan’ [IDR 500 million fines have not deterred issuers submitting delayed financial reports], *Detik News* (online), 13 Januari 2013 <<http://finance.detik.com/read/2013/01/13/134408/2140693/6/denda-rp-500-juta-belum-bikin-emiten-jera-telat-beri-laporan-keuangan>>.

¹⁴⁴⁰ 1 US\$ equals 13,000 IDR

¹⁴⁴¹ Didik Purwanto, ‘Penegakan Pasar Modal: Bapepam-LK denda 50 emiten senilai Rp. 1,029 miliar’ [The enforcement of Capital Market: Bapepam-LK fined 50 issuers in amount of IDR 1.029 billion], *Kontan News*, 7 Maret 2011 <<http://investasi.kontan.co.id/news/bapepam-lk-denda-50-emiten-senilai-rp-1029-miliar-1>>.

¹⁴⁴² Syahid Latif and Ronito Kartika Suryani, ‘Bapepam periksa emiten telat lapor keuangan [Bapepam inspects issuers, which delayed their financial reports], *Viva News* (online), 14 Oktober 2011 <<http://bisnis.news.viva.co.id/news/read/255633-dua-emiten-tak-beri-laporan-keuangan-semester>>; See also, Prayogi, above n 1437.

131 issuers and fined them IDR 5.02 billion (approximately US\$386 000).¹⁴⁴³ The then newly established OJK addressed 33 cases in 2013 with the majority being untimely financial reports.¹⁴⁴⁴

This poor mandatory disclosure compliance is consistent with Waagstein's claim, see Chapter [2.4.3], that mandatory norms do not necessary coincide with corporate compliance. She argues that the relationship between the legal character of a norm and effective compliance with it is complex. Compromise and acceptance as well as dependence between the regulation and regulator on the subject and in the context, constitute the effectiveness of norms. To address this, she suggests that many voluntary norms, such as voluntary code, have effective functions in reshaping, implementing, interpreting or even substituting for mandatory norms. It is a similar claim made by a number of scholars, also referred to in Chapter [2.4.2], that a voluntary code could be an effective alternative regulatory strategy to address the limited capacity of formal rules.

6.4. Good corporate governance codes and accountability for corporate disclosure.

In the Indonesian context, as pointed out in [6.3], the GCG Code may be losing its voluntary characteristics as so much disclosure has been transformed into a mandatory regime. This potentially limits the impact of the GCG Code on the accountability for disclosure.

The 2006 GCG Code has provided a set of standards and guidelines for companies to implement good corporate governance. It aims to achieve sustainable growth of companies through management, empowering the functions and independency of company organs, encouraging shareholders, members of the board of commissioners and board of

¹⁴⁴³ 'Bapepam-LK jatuhkan sanksi 375 pelaku pasar modal – Tingkat indisipliner meningkat' [Bapepam-LK gave sanctions to 375 capital market participants – Undisciplined level increases], *Neraca.co.id* (online), 13 Agustus 2012 <<http://m.neraca.co.id/article/17766/BapepamLK-Jatuhkan-Sanksi-375-Pelaku-Pasar-Modal>>; See, eg, 'Emiten nakal dikenai sanksi dan denda Rp 500 juta' [Undisciplined issuers were fined with sanctions and IDR500 million fines], *Tempo.co* (online), 11 Januari 2013 <<http://www.tempo.co/read/news/2013/01/11/088453715/Emiten-Nakal-Dikenai-Sanksi-dan-Denda-Rp-500-Juta>>. It was recorded 6 issuer delay disclosure in January 2012 alone.

¹⁴⁴⁴ 'OJK tangani 33 perkara pelanggaran di pasar modal selama 2013' [OJK handled 33 cases of capital market violation during 2013], *Kompas* (online), 30 Desember 2013 <http://bisniskeuangan.kompas.com/read/2013/12/30/2008235/OJK.Tangani.33.Perkara.Pelanggaran.di.Pasar.Modal.Selama.2013?utm_campaign=related_left&utm_medium=bp&utm_source=bisniskeuangan>.

directors to take decisions and actions based on high moral values and compliance with the law and regulations: stimulating the company's awareness of social responsibilities, optimizing the value of a company for its shareholders and for the interests of other stakeholders, enhancing the competitiveness of a company, strengthening market confidence to promote investment and by promoting sustainable national economic growth.¹⁴⁴⁵

The GCG Code consists of eight main chapters including: ensuring the basis for an effective corporate governance framework in Indonesia, general principles of good corporate governance, business ethics and codes of conduct, organs of the company, rights and role of shareholders, the rights and role of other stakeholders, declaration of the implementation of the Code and general guidelines for GCG implementation.¹⁴⁴⁶

The GCG Code establishes five general principles for good corporate governance including transparency, accountability, responsibility, independency, and fairness.¹⁴⁴⁷ These principles and standards are in line with the principal standards of the 2004 OECD Principles of Corporate Governance.¹⁴⁴⁸ Indonesia has not revised the GCG Code to allow for the changes to the G20 OECD Principles of Corporate Governance of 2015, which extended principles for institutional investors, stock markets and other intermediaries and also addressed several updated issues around corporate governance. In these G20 OECD changes trust, transparency and accountability are highlighted as requirements for fostering long-term investment.¹⁴⁴⁹ With respect to this study, the principles of transparency and accountability are the ones mainly relevant.

In the GCG Code, as noted earlier, transparency has been made the first principle. It states that:

To preserve and maintain the objectivity in practicing business, a company must provide material and relevant information that are easily accessible and understable

¹⁴⁴⁵ Indonesia's Code of Good Corporate Governance 2006 is available at <http://www.ecgi.org/codes/documents/indonesia_cg_2006_en.pdf>. [Preamble B]

¹⁴⁴⁶ Indonesia's Code of Good Corporate Governance 2006.

¹⁴⁴⁷ Indonesia's Code of Good Corporate Governance 2006 [Part II].

¹⁴⁴⁸ See, Organization for Economic Co-operation and Development (OECD), *the OECD Principles of Corporate Governance* 2004, above n 224.

¹⁴⁴⁹ Organization for Economic Co-operation & Development (OECD), 'G20/OECD Principles of Corporate Governance', above n 231, 7.

by stakeholders. A company must take the initiative to disclose not only the issues mandated by laws and regulations, but also other information deemed necessary by shareholders, creditors and other shareholders to form a decision.¹⁴⁵⁰

The transparency principle sets out four requirements. Similar to the OECD Code, transparency requires the timely disclosure of adequate, clear and comparable information [Provision 1.1]. Information to be disclosed includes but is not limited to, the vision, mission, business targets and strategy, financial condition, composition and compensation of management, controlling shareholders, shares owned by members of the board of directors and board of commissioners and their family members in the company and other companies, a risk management system, oversight and internal control system, GCG structure and mechanisms and its level of compliance as well as important events that may affect the condition of the company [Provision 1.2]. Provision [1.3] stipulates that the transparency principle adopted by a company should not lessen its obligations for fulfilling provisions of confidentiality in accordance with laws and regulations, occupational confidentiality and personal rights. Company policies must be provided in the form of formal writing and proportional communication to stakeholders [Provision 1.4].¹⁴⁵¹

The second principle is corporate accountability. This requires that ‘a company must be accountable for its performance transparently and fairly’.¹⁴⁵² It is a prerequisite to achieving sustainable performance. Management must be conducted in a proper and measured manner. The interests of a company and the interest of shareholders and other stakeholders must be considered. There are five provisions addressing the responsibilities of a company in defining clear job descriptions with clear responsibilities to each company organ and all employees [2.1], in ensuring proper qualifications of all company organs and employees fit with their duties, responsibilities, and roles in the implementation of good corporate governance [2.2]; in ensuring the existence of effective internal control systems

¹⁴⁵⁰ Indonesia’s Code of Good Corporate Governance 2006 [Part II (1)].

¹⁴⁵¹ Ibid.

¹⁴⁵² Indonesia’s Code of Good Corporate Governance 2006 [Part II (2)].

[2.3], in providing performance indicators for all company organs and employees [2.4] and in upholding the business ethics and the agreed code of conduct by the company [2.5].¹⁴⁵³

The GCG Code has clearly demonstrated that accountability is directly related to transparency. Accountability is aimed at creating trust in governance institutions.¹⁴⁵⁴ Seal and Vincent-Jones emphasised the need for trust in shaping long-term relationships¹⁴⁵⁵ and how this relates to a company's sustainability. Dragomir refers to collective accountability as the "norms of governance" that prescribe the legitimate modes of the use of power.¹⁴⁵⁶

Salim outlined another strategic impact of the accountability for disclosure on a fair share price. Disclosure is claimed to be particularly, and in good corporate governance generally, a determining factor of value for issuers and investors. Disclosure is seen to be an imperative for listed companies.¹⁴⁵⁷

Accountability for corporate disclosure also requires the further development of independent and sound auditing practices. This is crucial in achieving accountability for disclosure. Accountability requires effective forms of supervision or control. The principle of accountability is based on internal checks and balances and these include sound auditing practices.¹⁴⁵⁸

A strategic focus on accountability for corporate disclosure will make companies attractive to foreign investors and contribute to the development of Indonesia's capital market. Accountability for disclosure, as introduced in the GCG Code, has been part of a reform effort to attract foreign investors and strengthen the domestic capital market.¹⁴⁵⁹ The

¹⁴⁵³ Ibid.

¹⁴⁵⁴ Voicu-Dan Dragomir, *Accountability in the name of global corporate governance – A historical perspective*, Bucharest Academy of Economic Studies Romania, 177 <<http://www.asecu.gr/files/RomaniaProceedings/20.pdf>>.

¹⁴⁵⁵ Ibid 177.

¹⁴⁵⁶ Ibid 178. Accountability was introduced as the corporate governance trademark especially in agency theory and stakeholder theory.

¹⁴⁵⁷ Daniri, *Good corporate governance*, above n 157, 64.

¹⁴⁵⁸ Surya and Yustiavandana, above n 65.

¹⁴⁵⁹ See generally, Carsten Gerner-Beuerle, 'Determinants of corporate governance codes' (LSE Law, Society and Economy Working Papers 5/2014, London School of Economics and Political Science) 38 <http://www.lse.ac.uk/collections/law/wps/WPS2014-05_Gerner-Beuerle.pdf>. Gerner-Beuerle considers the main determinants of corporate governance reforms including: '(1) the diffusion of an international benchmark model of corporate governance, (2) approaches to corporate governance and the protection of different stakeholders embodied in a country's legal system, (3)

GCG Code, as previously noted, was introduced after the country was hit by severe economic crises that required it to rebuild trust to attract significant foreign investment. The need to strengthen the capital market was also a factor. This indicates the acceptance, as seen in Chapter [3.2.3], that foreign investment is necessary for economic development. Gautama, for example, considers foreign investment an imperative for Indonesia. The government acknowledges its major role in achieving this for the country's economic development.

In fact, as previously noted, the GCG Code is not widely used in business frameworks and the expected impact of the GCG Code in creating accountability for corporate disclosure is very low. The ineffectiveness of the GCG Code results from the two crucial aspects of morality and trust in ensuring the enforcement of such voluntary codes being so poor. It is understood that the GCG Code is a voluntary code, which was designed to be a national reference for good corporate governance regime regarding legal and business frameworks.¹⁴⁶⁰ The enforcement of the GCG Code, as suggested by Haines and Zerilli and noted in Chapter [2.4.3], relies on moral suasion. Trust also is suggested by De Soysa and Jutting, as noted in Chapter [2.4.4] to establish norms, such as good corporate governance principles promoted by the GCG Code in complex economies or complicated conditions like Indonesia.

The poor level of morality and trust identified in the Indonesian context, as described in chapters 4 and 5, not only affects the level of respect for the voluntary GCG Code but also mandatory mechanisms creating accountability for disclosure. The expectation that the GCG Code has to increase transparency, as suggested by Rapp et al in Chapter [2.4.2.2], has failed. Mandatory disclosure is also less effective. The integrity of disclosure as a mainstream practice is considerably low.

Private, public listed and state-owned companies are not seen to produce reliable financial reports in a disclosure regime, which they are seen to take seriously. Compliance with disclosure, as indicated earlier, is driven only by fulfilling a formality.

the desire to attract foreign investors and strengthen the domestic capital market, and, (4) the influence of interest groups on the drafting process.'

¹⁴⁶⁰ Remarks of Coordinating Minister for Economic Affairs of Republic Indonesia at Indonesia's Code of Good Corporate Governance 2006.

As noted in Chapter [1.1] and [5.2.2]–[5.2.3], corruption is partly attributed to the lack of transparency of companies. The SOEs, companies with political ties and companies with concentrated and controlling ownership, tend to be reluctant to be more transparent. The unwillingness to be transparent contributes to the limited number of listed companies. This is reflected, for example, that among 138 SOEs in 2014 only 20 SOEs are listed in the capital market despite the efforts that have been taken to increase their number. Of more than 20 000 medium and large enterprises, only about 500 companies are listed in the capital market. The limited number of listings creates a greater dependency on foreign investors. Transparency and disclosure are crucial aspects in attracting them, as indicated in Chapter [2.3].

The SOEs are examples of very poor accountability around transparency and disclosure. It was noted in the previous chapter that SOEs are often piggy banks for political parties. They also have to fulfil state or community obligations, so are always going to be under state control or subject to other scrutiny and pressures from ministers, the parliament and the media.

Finally, the fact that disclosure principles are covered by legislation and regulation, as noted earlier, erodes the functions of the GCG Code in creating effective corporate accountability for disclosure. In fact, the government, the business community and NGOs, as indicated earlier, may play significant roles in promoting the use of the GCG Code as discussed in the following sub-section.

6.5. Role of government, business community and NGOs in promoting the use of the code

6.5.1. Introduction

As noted in Chapter 2, the state and private sectors have contributed to the shape of the framework of corporate governance and its development. Good corporate governance, as specified by the GCG Code, requires the roles of the government, business community and relevant NGOs. The GCG Code acknowledged them as inter-related pillars. Kamal described these roles as a governance tripod.¹⁴⁶¹

¹⁴⁶¹ It refers to the government as the regulator or decision maker, business community as market participants, and society as users. See, Miko Kamal, 'Konsep corporate governance di Indonesia:

6.5.2. The government's role

The government's role relates to creating sufficient trust in the legal system and the diffusion of significant power to the private sector. Trust in the legal system creates a high level of respect not only for formal law but also for informal law, such as the code. The legal system exists as the last resort in resolving disputes justly and fairly. The government is expected to realise the effectiveness and efficiencies in leaving individuals the power to enforce their own rights. It becomes a less expensive way to ensure social control in business practices as suggested by Braithwaite and summarised in Chapter 2.

The standardised good corporate governance code is part of the government's initiatives to optimise corporate governance practices.¹⁴⁶² The GCG Code was introduced by the National Commission on Governance Policy (KNKG), which is a national body mandated to create the GCG Code. It was also required to undertake activities on governance and regulatory reform and for an institutional framework development.¹⁴⁶³ Other initiatives include the corporate governance principles embodied in the 2007 Company Law.¹⁴⁶⁴

The making of corporate governance codes in South East Asian countries, as indicated in Chapter 3, was also a government initiative. The governments of Singapore,

Kajian atas kode corporate governance' (2011) 10(2) *Jurnal Manajemen Teknologi* 145, 152 <<http://journal.sbm.itb.ac.id/index.php/mantek/article/view/137>>.

¹⁴⁶² Jusuf Anwar, 'Corporate Governance: a Prerequisite to Indonesia's Economic Revival' (Paper presented on Panel Discussion on Corporate Governance, Jakarta, March 2000) as quoted by Kurniawan and Indriantoro, above n 125, 10–11.

¹⁴⁶³ See generally, Kurniawan and Indriantoro, above n 125, 9. Efforts to develop corporate governance practices from the government were driven, among others, by the commitment of the International Monetary Fund as the country's major lender as outlined in a Letter of Intent signed in January 2000'. The KNKG,'s commitment includes activities of educational events on corporate governance for the public, pilot projects in industries for implementing corporate governance principles, regulatory reform in the capital market, the Forum of Corporate Governance (FCGI), a fit and proper test for directors and commissioners and technical assistance from the international community.

¹⁴⁶⁴ Anwar, above n 1462. The NCCG other initiatives includes: Amending Company Registration Law to ensure transparency of corporate information[;] Improving accounting standards, including regulations on the formation of Audit Committees and Compliance Officers[;] Improving regulations on disclosure[;] Improving Capital Market Rules, including support of a new Financial Supervisory Agency, which is part of the new Central Bank Law[;] Improving Articles of association[;] Improving banking sector regulations; and Forming an Institute of Directors to train and certify Directors.

Malaysia and Thailand delegated the making and promotion of the codes to the private sector, particularly self-regulatory organizations. The private sectors enforced the codes. This did not happen in Indonesia. Common law jurisdictions, like Singapore and Malaysia, and Thailand with their mixed legal system were more influenced by the private sector, as in the UK, and by its approach of comply or explain. Civil law systems like Indonesia, with their greater emphasis on the state as the source of law, do not lend themselves so easily to this arrangement. This relates to Coffee's claim that civil law jurisdictions have a smaller scope for flexibility and discretion outside of the control of the state. It also indicates that the Indonesian government, like the government in any other civil law country, claims a monopoly on the exercise of power and control, as claimed by Black and indicated in Chapter [2.4.2.2].

Indonesia did not take the opportunity to achieve a greater diffusion of regulation through the business community and the efficacies that could bring them about, as suggested by Black's and Ogus's concepts on decentred regulation. This type of regulation would leave to individuals the enforcement of their rights. This is also considered in Braitwaite's concept of responsive regulation to be a cheaper form of social control than state command and control regulation through formal law. That latter strategy could not be achieved in the Indonesian context with its reduced regulatory and financial capacities.

The use of the GCG Code may be of benefit to Indonesia as Helmke and Levitsky, Aldashev and other writers suggested in Chapter 2. They claim it may be an effective strategy where existing formal rules on paper are not effective in practice due to lack of credibility of, and insufficient trust in, law enforcement. Informal law may create the necessary trust. This strategy, it is suggested, may work to address the loss of trust in the formal legal system due to persistent and pervasive corruption that still remains a core problem in Indonesia,¹⁴⁶⁵ despite the existence of a powerful Corruption Eradication Commission (KPK).¹⁴⁶⁶

¹⁴⁶⁵ See, Chapter [5.2.3].

¹⁴⁶⁶ The powers that will help the KPK successfully tackle corruption problems are facing a new challenge under the new parliament. The current political atmosphere and the domination of defeated candidate president Prabowo's coalition (known as *koalisi merah putih*) in the parliament

The GCG Code, in the Indonesian context, emphasizes the role of the government as the law or policy maker, regulator, supervisor, and enforcer in developing, implementing, maintaining and enforcing laws and regulations that ‘will promote the creation of a healthy, efficient and transparent business culture’.¹⁴⁶⁷ The Indonesian government’s role could potentially include the establishment of good governance¹⁴⁶⁸ and the eradication of corruption and crime,¹⁴⁶⁹ which could be significant in establishing trust in the legal system. This has the potential to impact on business practices.¹⁴⁷⁰ Trust encourages respect for law and regulation within the business community and the discipline, which comes with this.

Compared to other South East Asian jurisdictions, in the studies in Chapter 3, the governments’ roles, for example in Singapore and Malaysia, appear to be effective in arranging for the creation and use of codes as an adjunct or supplement to their legal systems as their legal systems are aligned with Anglo-American institutions with a recognition that the state is not the sole source of authority and law.

6.5.3. The role of the business community

The role of national and local business communities is potentially significant considering the nature and function of good corporate governance in business as indicated in Chapter [2.2.3]. This potentially relates to compliance with voluntary codes. This is a crucial issue as their enforcement relies on moral suasion. The codes, as informal law, are also observed to be important in business transactions. Firms adopt good corporate governance as it is attractive to local and foreign investors, see Chapter [2.2.3]–[2.3].

The role of the business community through corporate leaders is to establish business cultures with disciplined ethical business practices that include respect for the principles of the code, see Chapter [2.2.4].

are hindering a new hope in the new government under the newly elected president Joko Widodo. See, Chapter 1.

¹⁴⁶⁷ Indonesia’s Code of Corporate Governance Code 2006 [I]. See generally, Pierre, above n 1198, 1. The role of Indonesian government conforms Pierre claim that ‘the state retains significant control over its domestic governance even in the era of globalization’.

¹⁴⁶⁸ Riani, above n 1367, 16.

¹⁴⁶⁹ Caron, Ficici and Richter, above n 1147, 24.

¹⁴⁷⁰ Ibid.

In the absence of a compliance mechanism in Indonesia's GCG Code, such as comply or explain, the GCG Code relies on the initiatives of corporate leaders. This is reflected in claims suggesting the vital role of directors in creating effective corporate governance.¹⁴⁷¹ Tan Sri Zarinah Anwar claims that this is part of the leadership responsibilities of business leaders. Directors should be 'effective stewards and guardians of the company in respect of ethical values, and ensuring an effective governance structure for the appropriate management of risks and level of internal control'.¹⁴⁷² Datuk Gan Ah Tee made a similar claim that boards of listed companies are the key to success in applying good corporate governance as reflected by the code. There is a crucial interplay here between individual self-discipline, market discipline and regulatory discipline.¹⁴⁷³

Leadership is a significant problem in Indonesia with its paternalistic style, which facilitates domination of companies with a family-like leadership. This has greatly impacted on good corporate governance practices promoted by the GCG Code.

Most listed companies with such a family leadership style¹⁴⁷⁴ are less likely to observe the principles in the GCG Code. The family business type¹⁴⁷⁵ has problems with

¹⁴⁷¹ Chee Keong Low, 'A road map for corporate governance in East Asia' (2004) 25(1) *Northwestern Journal of International Law & Business* 165, 168 <<http://scholarlycommons.law.northwestern.edu/cgi/viewcontent.cgi?article=1596&context=njilb>>.

¹⁴⁷² Global Body For Professional Accountants, 'The importance of discipline', *Accounting and Business Magazine* (Malaysia), January 2013, [8]–[9] <<http://www.accaglobal.com/zm/en/discover/ab-articles/governance-risk-control/the-importance-of-discipline.html>>.

¹⁴⁷³ *Ibid* [7]–[8]

¹⁴⁷⁴ Stefan S Handoyo, 'Shaping governance in Indonesian family businesses' *The Jakarta Post* (online), 14 April 2010 <<http://www.thejakartapost.com/news/2010/04/14/shaping-governance-indonesian-family-businesses.html>>. The majority of business has been identified (90 per cent) as family-owned and controlled companies; See also, Universitas Islam Indonesia [Islamic University of Indonesia], *Family business contributes to nation's GDP* (13 November 2012), [4] <<http://www.uui.ac.id/content/view/2116/257/>>. Director of Indonesian Institute of Family Firm, Achmad Sobirin, confirms this figure. Ninety per cent of business population is the family business; Cf, Badan Pusat Statistik [Statistic Indonesia], *The number of establishment large and medium manufacturing by subsector 2008–2013 and 2000–2011*, above n 141. The total number of business was 23 345 in 2010; 23 370 in 2011; 23 592 in 2012, and 23 941 in 2013.

¹⁴⁷⁵ A persistent large number of family businesses may be contributed by several factors amongst other a very limited space for civil service jobs. It has encouraged many Indonesians to create their own business employing families as the most trusted parties. See especially, Sofyan Wanandi, above n 1038, 132. The establishment of family business also seemed to consider the best option for Indonesian Chinese since the difficulty in entering the civil service and many other professions

checks and balances.¹⁴⁷⁶ This creates a different agency problem¹⁴⁷⁷ to that found in widely dispersed shareholder companies controlled by professional managers. They may take, unfairly, assets of the dispersed shareholders. Here the family in control may take, unfairly, the assets of the limited number of non family shareholders. The GCG Code consequently fails to resolve this agency problem. The GCG Code does not address typical issues such as self-dealing by the owners or controllers and related abuses.¹⁴⁷⁸ This is a further indication that the GCG Code does not fit with the Indonesia context. It further demonstrates that the GCG Code is a transplanted product without appropriate adjustments to the local context. As a result, its failure as a transplant is predictable, as the literature on legal transplant theories in Chapter [2.6] indicates.

There is another poor leadership issue that impacts on the effective use of GCG Code in a number of listed companies. This is demonstrated by the lack of understanding of capital markets and the un-preparedness for transparency. These have been suggested by both the chair of *Himpunan Pengusaha Pribumi Indonesia (HIPPI)* [Indonesian Indigenous Entrepreneurs' Association] Jakarta, Sarman Simanjorang and the chair of the IDX's Surabaya branch. They observed that these factors have contributed to the small number of

under Soeharto regime. It was based on Soeharto belief that they were at their best performance in the economic sector, and that 'they should concentrate in that field'.

¹⁴⁷⁶ Handoyo, above 1474, [6];

¹⁴⁷⁷ See concerning agency problems, John Armour, Henry Hansmann and Reinier Kraakman, 'Agency problems, legal strategies, and enforcement' (Discussion Paper No. 644, 7/2009, Harvard John M. Olin Center for Law, Economic, and Business Harvard Law School) 2 <http://www.law.harvard.edu/programs/olin_center/papers/pdf/Kraakman_644.pdf>. Agency problems or principal-agent refers to 'conflict of interests among corporate constituencies, including those between corporate 'insiders', such as controlling shareholders and top managers, and 'outsiders', such as minority shareholders or creditors.'

¹⁴⁷⁸ Handoyo, above n 1474, [6], [11], [15] & [16]. He highlighted four key issues need to be addressed in the code to solve those problems: the need to recruit the expertise of non-family executive balancing skills and expertise from family and non-family members, the establishment of fairness and transparency in financial and non-financial perks and reward systems to avoid tensions over perceived injustices, the clarity of roles and separation of day-to-day management with a more formal organization, and keeping the integrity and unity of the family with regular and proper channels of communication. He outlined a solid foundation from the first generation of the families to create and uphold values and corporate culture to the next generations is crucial. It was suggested to create a 'Family Constitution or Charter' providing the path of good corporate governance and family business principles cross each other and a clear guideline for treatment of the family and business matter.

listed companies,¹⁴⁷⁹ as indicated in Chapter [1.1]. The limited number of listed enterprises may be another factor that contributes to the GCG Code not being respected. In order to maintain and improve the number of listed companies, utilising a mandatory code may be seen as an impediment to attracting more new listed enterprises.

In addressing these corporate leadership issues, corporate governance NGOs may contribute to raising awareness and understanding of the significant need for good corporate governance, particularly disclosure as promoted by the GCG Code.

6.5.4. The role of corporate governance NGOs

NGOs also may play a significant role in promoting the use of the GCG Code through capacity building. This could be significant in addressing the lack of familiarity and understanding among corporate leaders of the significance of corporate governance in general and disclosure in particular. Lessons from Thailand, shown in Chapter [3.5], point to the significant role of NGOs in encouraging corporate governance development in listed companies.

It is claimed that such NGOs have changed the way societal players interact and communities make important decisions. In the corporate sector, corporations have collaborated with NGOs to implement voluntary policies.¹⁴⁸⁰ After the fall of Soeharto,

¹⁴⁷⁹ Ester Meryana, 'Mengapa masih minim perusahaan yang go public?' [Why the number of listed public companies is still low?], *Majalah SWA* (online) [1],[2],[4],[5] <<http://swa.co.id/portfolio/mengapa-masih-minim-perusahaan-yang-go-public>>. This was the HIPMI chairman claimed that family owned companies and a lack of capital market understanding have led to the absence of listed indigenous companies.; 'BEI ingin lebih banyak perusahaan go public' [BEI expects more listed public companies], *Tribun Surabaya* (online), 16 Januari 2014, [4], [5] <<http://surabaya.tribunnews.com/2014/01/16/bei-ingin-lebih-banyak-perusahaan-go-public>>. The un-preparedness of companies to be transparent about their performance has contributed to a small number of listed companies. Only 20 new listed companies in 2007, 19 in 2008, 13 in 2009, 23 in 2010, 25 in 2011, 23 in 2012 and 31 in 2013.

¹⁴⁸⁰ Junki Kim, *Accountability, Governance, and Non-governmental Organizations: A comparative study of twelve Asia-Pacific nations*, Seoul National University, 2, 5 <http://c.ymcdn.com/sites/www.istr.org/resource/resmgr/working_papers_toronto/kim.junki.pdf>. Non-state actors including civil society are believed to be able to reshape the traditional bureaucratic state in regarding to the transformation of governance towards a more participatory and democratic model. Non-profits organizations are believed to be 'forces of good and representative of the true voices of ordinary citizens' as they may have high moral ground compared to governments.

NGOs has grown and played important roles in supporting Indonesia's development.¹⁴⁸¹ Among a number of activities performed by NGOs referred to by Nelson, the role of capacity building¹⁴⁸² is one that is undertaken by Indonesian corporate governance NGOs.

A number of corporate governance NGOs have made contributions to creating awareness, education about and the dissemination of, good corporate governance practices as promoted by the GCG Code. They include the Forum for Corporate Governance in Indonesia (FCGI), the Indonesian Institute of Commissioners and Directors (LKDI), the Indonesian Institute for Corporate Governance (IICG), Indonesian Institute for Corporate Directorship (IICD) and the Corporate Leadership Development Institute (CLDI). The table below summarises their respective roles.

Table 6.11: The role of Indonesian corporate governance NGOs

Name of relevant NGOs	Established by	Functions
Forum for Corporate Governance in Indonesia (FCGI) ¹⁴⁸³	Five professionals & business associations	Enhancing awareness and dissemination of good corporate governance

¹⁴⁸¹ Ibid 8, 9. Junki claimed a growing need for NGOs in Indonesia after the fall of the authoritarian regime and prolonged economic crisis, and also increased overseas funding for them; See generally, Hans Antlov, Rustam Ibrahim and Peter van Tuijl, *NGO Governance and Accountability in Indonesia: Challenges in a newly democratizing country* (2005) <http://www.icnl.org/research/library/files/Indonesia/Peter_NGO%20accountability%20in%20Indonesia%20July%2005%20version.pdf>. The civil society organizations (CSOs) have grown significantly since the collapse of President Soeharto's authoritarian New Order regime in 1998. The opportunities for Indonesian civil society groups to participate in establishing rights, institutions and mechanism of accountability has been widely opened throughout Indonesia. This a notable change for Indonesia where there was a discouragement for citizen involvement in the past; See e.g, Stanley Adi Prasetyo, A E Priyono, Olle Tornquist (eds), *Indonesia's post Soeharto democracy movement* (Demos, 2003) 574–5. See also, page 576–7. INFID is an international NGO network with two secretariat offices and one liaison office. Since the *reformasi* era, NGOs have emerged to raise critiques and outspoken to oppose policies that negatively impact on mass welfare. They have participated in policy networks and provided policy alternatives as advocates of various society voices.

¹⁴⁸² Jane Nelson, 'The operation of non-governmental organizations (NGOs) in a world of corporate and other codes of conduct' (Working Paper No. 34, Corporate Social Responsibility Initiative, John F Kennedy School of Government Harvard University, March 2007) <http://www.hks.harvard.edu/m-rcbg/CSRI/publications/workingpaper_34_nelson.pdf>. There are two theories regarding the growing influence of NGOs. See, Kim, above n 1480, 4. Other NGOs activities include advocacy, analysis and awareness raising; brokerage; conflict resolution; delivery of services; and evaluation and monitoring (watchdog or third party/independent auditor of government and corporate performance).

¹⁴⁸³ Forum for Corporate Governance in Indonesia, *FCGI profile*, [1] & [3].

		principles to the business community. Programs: publication booklets and a self-assessment questionnaire for companies, articles in a leading national newspaper, TV show “Transparans 100%” and promotional and educational visits to companies.
Indonesian Institute of Commissioners and Directors (LKDI) ¹⁴⁸⁴	KNKG in 2001	Introduced corporate governance training/in-house training and directorship certification; and professional education workshop.
Indonesian Institute for Corporate Governance (IICG) ¹⁴⁸⁵	<i>Masyarakat Transparansi Indonesia</i> (MTI) [Indonesia Transparency Society] and some community leaders (2000)	Research, consultation and rating services (corporate governance perceptions index); book publications; regular training/in-house training and seminars; good corporate governance assessments; disseminate corporate governance principles.
Indonesian Institute for	Ten highly reputable	Professional education for

<<http://www.fcgi.or.id/about-fcgi/fcgi-profile.html>>. The founders are AEI – Asosiasi Emiten Indonesia [the Association of Indonesian Public Listed Company], IAI-KAM - Ikatan Akuntansi Indonesia – Kompartemen Akuntan Manajemen [The Indonesian Accountant Association – Management Accountant Compartment], IFEA – the Indonesian Financial Executives Association; INA – the Indonesian Netherlands Association, MTI – Masyarakat Transparansi Indonesia [the Indonesian Society for Transparency]. There are 10 members including the founders and 5 other associations such as APEI – Asosiasi Perusahaan Efek Indonesia [the Association of Indonesian Securities Company], FKSPI BUMN/BUMD – Forum Komunikasi Satuan Pengawasan Intern BUMN/BUMD [the Forum of Internal Auditor of State-Owned Companies/Regional Government-Owned Companies], IIA – the Institute of Internal Auditors (Indonesia Chapter), MAPPI – Masyarakat Profesi Penilai Indonesia – [the Indonesian Society of Appraisers], YPIA – Yayasan Pendidikan Internal Audit [Foundation for Internal Audit Education]; See also, van der Eng, above n 989, 17.

¹⁴⁸⁴ Lembaga Komisararis dan Direksi Indonesia, *LKDI profile* <<http://www.lkdi.org/cms/id/about-lkdi/lkdi-profile/>>.

¹⁴⁸⁵ Indonesian Institute for Corporate Governance, *Tentang IICG* [IICG profile], [1] <<http://iicg.org/v25/tentang-iicg>>. IICG is an independent and non-profit institution; See also, Indonesian Institute for Corporate Governance, *Layanan* [Services] <<http://iicg.org/v25/layanan>>.

Corporate (IICD) ¹⁴⁸⁶	Directorship	Indonesian Business Schools and preeminent experts	directors and commissioners, research on corporate governance, directorship, performance and advocacy in education & research; Report on the Observance of Standards and Codes (ROSC); corporate governance scorecard research.
Corporate Development (CLDI) ¹⁴⁸⁷	Leadership Institute	Foundation of SOE Leadership Development (1999)	Education on leadership and corporate management

6.6. Conclusion

This chapter recounts the use of the GCG Code for disclosure in Indonesia. It identifies the functions of the GCG Code as the national code within the legal and corporate governance framework, which determines the accountability of corporate disclosure. It also acknowledges the effective roles of the government, the business community, and the public represented by the relevant NGOs in promoting the use of the GCG Code.

In practice, the GCG Code is not widely used in business activities and within the legal framework. It is utilized as a reference only and contributes very little to create accountability for effective corporate disclosure. The function of the GCG Code as a reference tool is impractical for good corporate disclosure. It fails to improve the effectiveness, efficiency, and responsiveness of disclosure regulations. The GCG Code is not seen as a potential informal or soft law that may have benefits for Indonesia in addressing limited and weak formal legal systems as considered by the literature as the alternative regulatory strategy.

¹⁴⁸⁶ See, Indonesian Institute for Corporate Directorship, *Good corporate governance – Welcome to IICD website* <<http://www.iicd.or.id/>>. See also, Indonesian Institute for Corporate Directorship, *In-house training* <<http://iicd.or.id/en/services/in-house-training.html>>. IICD is a non profit organization and the member of IDEA.Net (Institute of Directors East Asia Network). IICD programs have been supported by the World Bank, International Finance Corporation, Corporate governance Forum, Center for International Private Enterprise, Asian Development Bank.

¹⁴⁸⁷ Corporate Leadership Development Institute (CLDI) [Institut Pengembangan Kepemimpinan Korporasi], *Sejarah Singkat CLDI* [A brief history of CLDI] <<http://cldi.co.id/>>.

The characteristics of the GCG Code reflect a low possibility that it would be a successful legal transplant and accommodated as informal or soft law. They include a symbolic role in fulfilling external expectations and requirements rather than in fulfilling the country's needs, the absence of the diffusion of regulation as the literature considers such diffusion important to informal law, the absence of comply and explain mechanisms; which are commonly used in utilizing similar codes in many other countries identified in Chapter 3 and the absence of discretion indicating the influence of a civil law background, which is unlikely to leave more room for flexibility or more open to utilizing informal or soft law such as the GCG Code. Indonesia's response to informal or soft law as represented by the GCG Code is aligned with that of civil law systems. The strong belief that legislation is the only legal source of law provides less room for accommodating informal rules compared with common law system.

The GCG Code serves a limited function in creating effective and reliable disclosure practices. However, similar disclosure provisions to those in the GCG Code are found in the formal legal framework. The legislative framework imposing disclosure obligations includes the 1995 Capital Market Law, the 2007 Company Law, the 1982 Company Registry Law, the 2003 State-Owned Enterprises Law, some relevant state-owned enterprises regulations and the capital market regulator rules. Relevant stock exchange rules also include the same provisions on disclosure making them mandatory for listed companies.

Despite disclosure having become mandatory within the formal legal framework and contractual framework, the compliance with that framework and the reliability of disclosure are low. This can be seen from two identified indicators. Firstly, the mentality around disclosure compliance is driven by the mere fulfilment of formalities raising the reliability of any information disclosed. Secondly, the system of supervision for compliance disclosure is limited and relies on a risk-based approach. Supervision of compliance does not cover all listed companies. This low level of both supervision of and compliance with disclosure relates to several factors, noted in the previous Chapter 5, which challenge the application of disclosure in the Indonesian local context. They include: cultural and political factors; corruption, disclosure as a foreign concept in the local context, the clash of

cultural foundations (in particular uncertainty avoidance and hierarchy and power distance) and the failure of legal transplants because of the lack of their adaption to the local context and the complexity of Indonesia's formal legal system, legal culture, legal scholarship and its jurisprudence. The transplanting of the GCG Code just followed the trend of globalisation without considering the local context.

The weak enforcement of relevant formal laws and regulations contributes to the unsatisfactory level of compliance with mandatory disclosure. Heavy penalties are not effective. This confirms Waagstein's claim, noted in section [6.3] of this chapter that mandatory norms do not necessarily lead to corporate compliance. This is because of the complexity of the relationship between the legal character of norms and the practice of effective compliance. She claims that voluntary norms including voluntary corporate governance codes such the GCG Code support the effectiveness of the mandatory norms by reshaping, implementing, interpreting or substituting them. This claim is similar to claims made by a number of scholars, as noted in Chapter [2.4.2.2], within the alternative regulatory framework, noted in Chapter [2.4].

The mandatory disclosure in the formal legal framework, listing rules and in the Roadmap of Good Corporate Governance introduced in 2014, has deprived the GCG Code of some of its functions. Indonesia has missed out on the efficacies promoted by the alternative regulatory theories: that the use of the GCG Code as informal or soft law may be a solution for the country's fundamental problem of a corrupt and weak formal legal system.

The government, the business community and the relevant NGOs have significant roles to play in promoting the effective use of the GCG Code as informal disclosure law, but their roles have had little impact.

The government has a significant role to play in creating sufficient trust in the legal system to create confidence and respect for both formal and informal law, in providing the power to individuals to enforce their rights, in promoting the creation of healthy, efficient and transparent business cultures; in establishing good governance and in eradicating corruption. Unfortunately, the Indonesia government has failed to play these roles effectively. The loss of trust in the formal legal system remains. The individual's power to

enforce their rights does not exist. The government, as the law and policy maker, regulator, supervisor and enforcer of laws and regulations, is still struggling to create a healthy, efficient and transparent business culture as well as eradicating corruption.

Besides the government, the business community has also had a significant role to play in the use of the GCG Code. It is the responsibility of corporate leaders to implement the good corporate governance promoted by the GCG Code. Compliance with the GCG Code depends on their decisions as the Code's enforcement relies on moral suasion. In fact, corporate leaders appear not to take disclosure seriously. As indicated earlier, compliance with mandatory disclosure is driven by fulfilling formalities. The paternalistic leadership style, which prevails in family-like relationships, tends to compromise good corporate governance practices, particularly transparency and disclosure promoted by the GCG Code. In this leadership style, the corporate leaders are unlikely to be ready to be transparent. They also tend to lack an understanding of the capital market as they are commonly appointed from among the family or extended family members, close associates or politicians whom the controlling owner is able to assert control over or take advantage of. In most Indonesian companies, the problem occurs in the checks and balances. This is different from agency problems that commonly occur in jurisdictions with companies with dispersed shareholders from which good corporate governance concepts have been adopted.

Corporate governance NGOs also count in promoting the use of the GCG Code. They may promote the use of the GCG Code by conducting capacity building that could address the lack of familiarity and understanding of the code. Some relevant Indonesian corporate governance NGOs have made significant efforts to promote the use of the GCG Code, but the outcomes of their efforts are limited because they lack support from the government and corporate leaders. As noted in the GCG Code, they are three inter-related pillars. Two weak and fragile pillars, the government and the corporate leaders, weaken the other strong pillar: the NGOs.

The conditions of the use of the GCG Code noted in this chapter are confirmed by the empirical evidence presented in the next chapter.

Chapter 7 : Result of field research and discussion

7.1. Introduction

This chapter discusses the empirical evidence obtained from field research conducted in Indonesia. The evidence was collected from a group of 48 participants selected from public and private sectors as indicated in Chapter 1. The collected data is presented according to the three major themes following the interview schedule ie: disclosure, formal regulations and voluntary codes. It provides an overview of the opinions expressed on disclosure practices, the functions of relevant laws and regulations on disclosure and the effects of informal sanctions, as well as the use of good corporate governance codes for accountability for corporate disclosure.

The opinions reveal and also confirm the challenges in the use of alternative regulatory strategies represented by voluntary GCG Code within the Indonesia context. Challenges in changing political and cultural ideologies, in the structural and habits of business and government and in the mentalities of officials and business people are inter play in the decisions about how to accommodate the GCG Code as informal, soft, or decentre law and regulation.

This chapter begins with an introduction describing the use of qualitative methodologies in this research. It outlines the use of interviews as a method for collecting data and the processes followed in coherently, as consideration of the validity and reliability of the findings. The ethical issues in collecting and storing the data are also described. At the end of the introduction, it details the methods used to analyse the collected data.

The following sub-sections present the key findings of the field research and its identification of relevant factors, which promote and compromise the use of informal codes as well as more specific analysis of the interpretation of particular data and the implications of analyses.

The discussion of the findings seeks to triangulate the field data collected with other data from the literature and media data bases. It considers the degree of consistency

between these three different data sets. The result of this triangulation is used to answer the research questions, which will be presented in the last chapter as a conclusion to this study.

7.1.1. Qualitative research

As indicated in Chapter 1, this study involved qualitative research utilising interviews for data gathering. This is one of the most commonly used methodologies in social sciences besides observations and focus groups.¹⁴⁸⁸ This method is used to ascertain particular information from informants¹⁴⁸⁹ for gaining ‘a detailed understanding of underlying reasons, beliefs, [and] motivations’.¹⁴⁹⁰ The purpose of this method includes attempting understanding the why, the how, the process, and the relevant influences and contexts of the phenomenon being studied.¹⁴⁹¹

7.1.2. Interviews

Interviews were chosen as the method of this research in collecting the primary data together with secondary data collections. It aimed to gain in-depth opinions, attitudes, behaviours and real experiences from participants that are crucial to an understanding of research issues and answering the research questions.

An interview is a ‘way of accessing people’s perceptions, meanings, definitions of situations and construction of realities’.¹⁴⁹² The interview is a formal and guided conversation involving the process of asking questions and listening.¹⁴⁹³

The interview enabled the researcher to have face to face contact with the subjects that helped to gain an insight into their personal views and experiences to obtain rich information around issues of disclosure, relevant regulations and codes. It is suggested that an in-depth interview maximizes the outcomes of data collected regarding individuals’

¹⁴⁸⁸ National Science Foundation, *Part II – Overview of Qualitative Methods and Analytic Techniques, Chapter 3 Common Qualitative Methods*, [1] <http://www.nsf.gov/pubs/1997/nsf97153/chap_3.htm>.

¹⁴⁸⁹ Sharlene Nagy Hesse-Biber and P Leavy, *The practice of qualitative research* (Sage Publication, 2nd ed, 2011).

¹⁴⁹⁰ Monique Hennink, Inge Hutter and Ajay Bailey, *Qualitative Research Methods* (Sage, 2011) 15.

¹⁴⁹¹ Ibid.

¹⁴⁹² K Punch, *Introduction to Social Research: Quantitative and Qualitative approaches* (Sage, 2nd ed, 2005) 168.

¹⁴⁹³ N K Denzin and Y S Lincoln (eds), *The SAGE Handbook of Qualitative Research* (Sage, 3rd ed, 2005) 643.

perspectives and experiences, especially in exploring sensitive topics.¹⁴⁹⁴ This harmonises with Miller's and Glassner's suggestion that interviews provide a mirror reflection of the reality that exists in the social worlds.¹⁴⁹⁵

The most common types of interviews in social research are unstructured, structured and semi-structured interviews.¹⁴⁹⁶ Unstructured or in-depth interviews are those in which the researcher talks freely and asks as few questions as possible. The participant is free to talk about what is important with little directional influence from the researcher. Structured interviews are those in which the researcher asks a series of questions inviting limited responses and the participants tick boxes or give a rating according to a limited scale. Semi-structured interviews are those where the researcher ask the same or similar questions in each interview but the structure also remains flexible. This permits other important information to emerge and be collected.¹⁴⁹⁷

This study used a semi-structured interview. It is considered as 'the most widely used interviewing format for qualitative research.'¹⁴⁹⁸ The advantage of this type of interview is that it enabled the collected of data to be compared and contrasted with information gained from other sources. In conducting a semi-structured interview, the interview schedule was constructed to drive the interview process.

7.1.3. The interview schedule

The interview schedule used facilitated and an open-ended approach. The schedule included lists of questions, which were categorized according to topics. The questions and topics were related to the research questions. These questions related to disclosure, relevant laws and regulations and good corporate governance codes. The questions ranged from the general to the specific. The questions asked in the interview schedule provided several

¹⁴⁹⁴ Northeastern University, *Qualitative Research Methods: A Data Collector's Field Guide – Module 1 Qualitative Research Methods Overview*, 2 <<http://www.ccs.neu.edu/course/is4800sp12/resources/qualmethods.pdf>>.

¹⁴⁹⁵ David Silverman, *Qualitative Research* (Sage, 3rd ed, 2011) 125.

¹⁴⁹⁶ Barbara DiCicco-Bloom & Benjamin F Crabtree, *Making sense of qualitative research – The qualitative research interview* (Blackwell, 2006) 314 <<http://www.hu.liu.se/cf/larc/utbildning-information/scientific-methodology/course-literature-and-links/1.253566/qual20interview.pdf>>.

¹⁴⁹⁷ Catherine Dawson, *Introduction to Research Methods; A Practical Guide for anyone undertaking a research project* (Spring Hill House, 4nd ed, 2009) 27–29.

¹⁴⁹⁸ DiCicco-Bloom & Crabtree, above n 1496, 315.

variations to allow for the specific knowledge and experience of interviewees and responses gained from previous interviews. The interview schedule is attached as Appendix A. The Indonesian translation of the interview schedule is attached as Appendix B.

Interview questions were provided with a covering letter instructing participants to provide the answers during the interview. The information given to participants is attached as Appendix D. The Indonesian translation of the information to participants is attached as Appendix E.

7.1.4. The interview process

7.1.4.1. Sampling for interviews

Sampling is an important part of research in data collection. Sampling involves a selection process where subjects, from whom information can be collected, are chosen.¹⁴⁹⁹ Consequently, the nature of the research is important in deciding how to compose the sample.

Types of sampling include probability sampling and purposive sampling. Probability sampling provides a specific opportunity for all people within the research population to be selected. Explanation, prediction, or generalization of the whole research population is the goal. Purposive sampling focuses on description rather than generalization.¹⁵⁰⁰

This study used purposive sampling in determining interviewees. It was based on the consideration of finding out specific knowledge, experiences and attitudes of the participants involved in the issues being research. Considering the large number of individuals and institutions involved in corporate regulations and governance, forty-eight participants were selected for the sample. They were intended to be as comprehensive as possible, given the resources to the researcher available. This was also a realistic number for interview purposes. The sample size for purposive sampling is generally between four to forty participants.¹⁵⁰¹

¹⁴⁹⁹ Dawson, above n 1497, 7, 48.

¹⁵⁰⁰ Ibid 53.

¹⁵⁰¹ Immy Holloway, *Basic Concepts for Qualitative Research* (Blackwell Science, 1997) 142–3.

To ensure the credibility of the interview data, the selection of interviewees from the public and private sector was based on their potential rich experiences and knowledge of corporate governance and regulatory practices. Most of the participants were senior and experienced with significant knowledge of the issues being studied. They were considered to be the most appropriate informants who best represented knowledge of the research topic, as suggested by Morse et al.¹⁵⁰²

The public sector participants include people who are state officials and government policy and law makers with experiences relating to the theory, the policies, the law and the practice of corporate governance. They included a representation from a national committee for corporate governance, judges, public prosecutors, regulatory and supervisory agency officials and members of parliament. Also included are academic researchers from well-known state universities, who in Indonesia are state employees. They were considered not only as professionals and experts in the issues covered by this study but also as representative of the state and its agencies, which has to administer, produce and enforce the law. This group had the potential to reflect on their experiences, attitudes and their own behaviours in terms of the policies, the law and the practices pertaining to good corporate governance: particularly disclosure.

The private sector was significant in sampling because they may have a variety of views and experiences that differ from those of state officials. They included stock exchange, officials, professional independent directors and commissioners, non-government corporate governance organizations representatives, credit rating official, corporate lawyers, auditors, accountants, business journalists and academic researchers from private universities.

The research student is a graduate in law and a lecturer of law in an Indonesian law school. Her fellow graduates and teaching colleagues and extended network of acquaintances provided her with introduction to relevant interviewees with appropriate experience.

¹⁵⁰² Janice M Morse et al, 'Verification Strategies for Establishing Reliability and Validity in Qualitative Research' (2002) 1(2) *International Journal of Qualitative Methods* 13, 18 <http://www.ualberta.ca/~iiqm/backissues/1_2Final/pdf/morseetal.pdf>.

The breakdown of interviewees from public and private categories can be seen in the following table.

Table 7.1: Participants from private sector

Private Sector	
Professional independent directors	7
Professional independent managers	3
Indonesia Stock Exchange officials	2
Corporate Governance NGOs representatives	4
Credit rating agency official	1
Securities Depository official	1
Profession Institute/Association officials	2
Corporate Lawyers	4
Public Accountant	1
Auditor	1
Journalists	5
Academic researcher from private university	1

Table 7.2: Participants from public sector

Public Sector	
National Committee on Governance	2
Judges involved in corporate and securities litigation and appeals	5
Public Prosecutors	2
Indonesian Capital Market and Financial Institutions Supervisory Agency [BAPEPAM-LK] (now Financial Services Agency – [OJK])	1
Government policy and law makers	3
Finance & Development Supervisory Agency (BPKP)	1
Academic researchers from state universities	2

7.1.4.2. Conducting of interviews

In order to conduct the interviews, approval needed to be obtained from Victoria University Human Resources Ethics Committee. The interview processes had to follow the ethics approval to limit the likelihood of any potential risks. The research obtained the required approval as discussed in the section on ethical issues.

All the relevant documents were translated into Indonesian for ethics approval. They were translated by a fellow Victoria University researcher, a lecturer in information systems from the University of Gajayana Malang Indonesia, Gunadi, who is fluent in both English and Indonesian. A declaration of accuracy of the translation by him is attached as Appendix C.

The potential participants were contacted by telephone or email. During the beginning of the process, there were difficulties in gaining access to intended members of the samples as indicated by Okumus, Altinay and Roper. They observe that gaining entry is one of the many problems for qualitative researchers, especially when research is focused on sensitive topics.¹⁵⁰³ It is crucial to gain entry to the research setting and to make contact with participants.¹⁵⁰⁴

The researcher did not get responses to the emails for some weeks. This is common in opening relationships with Indonesian businesses in that 'initial letters may go unanswered or be responded to by a subordinate.' It is further said 'Never write when you can call, and never call if you can meet'.¹⁵⁰⁵

This entry issue was resolved after the researcher received significant help from the researcher's network including alumni, friends and people from the same ethnicity working on the targeted respondents' institutions. They facilitated direct personal access to the intended members of the sample to introduce the research's project and to request time for interviews.

The networks were made easier and more efficient for the researcher to access targeted respondents in the sample. It was specifically needed to access public sector participants and senior business professionals.

¹⁵⁰³ Fevzi Okumus, Levent Altinay and Angela Roper, 'Gaining Access for Research: Reflection from Experience' (ANNALS Paper MS No.31147, 28 January 2006) 2 <http://epubs.surrey.ac.uk/216662/3/FINAL_31147_OKUMUS_ALTINAY_ROPER_JULY2-2006__2_.pdf>.

¹⁵⁰⁴ Western Oregon University, *Part 2 Qualitative Research*, 182 <http://www.wou.edu/~girodm/library/ch6_part2.pdf>.

¹⁵⁰⁵ George B Whitfield (contributor), *Business Across Cultures: Opening the Relationship with Indonesian Businesses* [4] <<http://www.expats.or.id/business/openrelationships.html>>.

Many of the intended respondents who were in senior positions had very tight schedules. They were also protected by strict gatekeepers who control the accepting and allocating of time for visitors. These gatekeepers are recognized as being able to stop accesses for both political and personal reasons.¹⁵⁰⁶ Once accessed it was re-confirmed by sending a formal letter also covering the privacy and confidentiality issues.

The recommendations from associates and the verifying by gatekeepers created trust between the researcher and the interviewees that contributed to a less formal and more friendly atmosphere for the interview. They appeared to feel free to express their opinions and their experiences including disclosing very sensitive and negative issues.

Most of the interviews were conducted at the interviewees' office. Some business media journalists were interviewed away from their offices including nearby restaurants or in the lobby. Their offices were not appropriate settings for interviews. They were crowded and many people were around. This did not give enough privacy for the participants to feel comfortable in answering the questions.¹⁵⁰⁷

The interview process experience of the researcher suggested that there are significant differences to how timeframes of respondents from the public sector and the private sector are able to be managed. In the public sector, the researcher had to wait at the informant's offices for two to three hours after the allocated appointment time. In one key public institution it took five hours to see the interviewees face to face in their own offices. The respondents apologized to the researcher for the excessive extended appointment times and explained the reasons. Some of them were decision makers and they have needed to respond and make decisions on urgent issues promptly. These waits contributed to conducting un-interrupted interview. Most respondents from the private sector adhered strictly to the time for their appointments.

Face to face interviews were mostly conducted in *Bahasa* Indonesia at the informants' offices. They sought to maintain 'a logistically feasible and comfortable

¹⁵⁰⁶ Okumus, Altinay and Roper, above n 1503, 5.

¹⁵⁰⁷ See, Michael Quinn Patton and Michael Cochran, *A Guide to Using Qualitative Research Methodology*, 14
<<http://fieldresearch.msf.org/msf/bitstream/10144/84230/1/Qualitative%20research%20methodology.pdf>>.

interaction' that established the basis for honest and friendly dialogue.¹⁵⁰⁸ This was achieved partly because of the researcher's trusted connections with most respondents, as indicated earlier.

During the interviews, the respondents appeared to demonstrate no hesitation and felt free to share their experiences and did not fuss over hidden or taboo issues. This is significant for the reliability of their respondent's answer. This addressed a concern that respondents might 'tell what they or the researcher wanted to hear' considering some topics, such as corruption, are very sensitive issues.

The length of the interviews varied and generally took about one hour to one and a half hours. With the permission of the respondents, an audio recording was made. Most respondents from the private sector were willing to permit the use of a recorder, while most public sector respondents preferred note taking during the interview. The different preferences between public and private participants suggested that public sector informants appeared anxious to avoid any possible risks of leaking of the information given. They also appeared to use the interviews to express "*keluh kesah or unek-unek*" [complaints, or a sense of disappointment, sadness and dissatisfaction] since they were unable to complain publicly without risking their position or career.

The questions asked in the interview schedule allowed for some variation to allow for the particular knowledge and experience of respondents and responses gained from previous interviewees. In order to achieve thoroughness, accuracy, and truthfulness after the interview, time was taken to clarify and to evaluate the data obtained so that it was both credible and authentic.¹⁵⁰⁹

Before the interview took place, the researcher attempted to indicate a careful understanding and consideration of the local culture. Shenton suggested that a relevant strategy in developing an early familiarity with the culture of participating organizations. It assists in promoting confidence in the accurate recording of the phenomena under scrutiny.

¹⁵⁰⁸ Tracy, above n 174, 159.

¹⁵⁰⁹ Herbert J Rubin and Irene S Rubin, *Qualitative Interviewing: the art of hearing data* (Sage Publications, 2nd ed, 2005).

Ignoring these issues may have deterred respondents from cooperating.¹⁵¹⁰ Poor initial impressions can limit the research study as participants will be hesitant to fully cooperate.¹⁵¹¹

Showing respect and good manners, especially to those who are older, or hold a higher position, is important in Indonesian culture. It acknowledges “*sopan santun*” or “*tata krama*” [politeness or manners]. This relates to the hierarchal and paternalistic culture. That is why, at the beginning of most interview processes, the researcher made an appropriate greeting and made brief friendly conversation as an introduction. Interrupting answers was also avoided since this may be considered to be disrespectful. This approach sought to establish an impression that the researcher was an honest and trustworthy interviewer. It contributed to a friendly and conducive interview atmosphere.

7.1.4.3. Taking notes and audio recording

Audio recording, video recording, and note-taking are the methods of recording interviews for later analysis.¹⁵¹² This research used both note-taking and audio recording.

Most public sectors participants favoured note taking, while most respondents from the private sectors permitted audio recording. The process of note taking made the public sector respondents feel more comfortable and appeared to allow them to more freely express their experiences and attitudes on the issues being asked.

The researcher quickly wrote the key responses and short answers during the interview. In note taking, she used short-hand, abbreviations and symbols to catch as much of the other information as possible. Immediately after the interview, the researcher went over the notes taken and completed the abbreviations and symbols and also added as much other information as possible, while it was still fresh in her memory. She thoroughly read the notes to check if there was any missing or mistaken information. She also wrote notes on how the interview went. The advantage of note taking is that the interviewer could

¹⁵¹⁰ Andrew K Shenton, ‘Strategies for ensuring trustworthiness in qualitative research projects’ (2004) *Education for Information* 22, 63, 64 <<http://www.crec.co.uk/docs/Trustworthypaper.pdf>>.

¹⁵¹¹ Ibid.

¹⁵¹² Steinar Kvale and Svend Brinkmann, *Interviews: Learning the Craft of Qualitative Research Interviewing* (Sage, 2009) 178.

organize the notes easily, and quickly cut and paste into documents any relevant information and quotations about themes.¹⁵¹³

The interview data from private sector respondents was mostly recorded on tape with the permission of participants. After some interviews, additional notes were made of certain data, particularly concerning very sensitive issues.

7.1.5. Ethics issues

Ethical considerations are paramount when there is the involvement of human beings as subjects in any research project. In conducting this research, the researcher complied with ethical procedures under the requirements of the National Health and Medical Research Council (NHMRC) '*National Statement on Ethical Conduct in Human Research (2007)*'.¹⁵¹⁴

The researcher first submitted an ethics application with the proposal to the Faculty of Business and Law Human Research Ethics Committee (HREC) for approval. Initially, the HREC granted a conditional approval subjected to a minor amendment. After the amendments, the HREC granted the approval.

The fieldwork is significant for this research. The experiences, attitudes and views of the participants on codes and good corporate governance, particularly around disclosure issues and their relevant regulations, has provided significant evidence to understand the issues raised by the research questions comprehensively. It was thought that the interview results would reveal the functions of good corporate governance codes. This could assist the researcher address the potential of the GCG Code to be an alternative form of regulation to address Indonesia's weak and corrupt formal legal and regulatory systems. This is reflected in the interview schedule, the focus on disclosure, relevant rules and regulations and good corporate governance codes. The questions sought to establish the knowledge, facts and attitudes relating to these issues. The questions were designed to avoid participants revealing personal or private issues.

¹⁵¹³ Dawson, above n 1497, 170.

¹⁵¹⁴ Commitment of VU's HREC at

<<http://www.vu.edu.au/research/ethical-conduct-biosafety/human-research-ethics>>;

See,

<<http://www.nhmrc.gov.au/guidelines-publications/e72>>.

To eliminate any risks that some interviewees could make disrespectful statements about another person or institutions, regarding Indonesian listed companies, regulatory bodies and the regulatory environment; the identity of interviewees and information obtained has not been disclosed and has been kept strictly confidential.

7.1.6. Validity and reliability

All research seeks to produce valid and reliable knowledge. The reliability of research results are important¹⁵¹⁵ as they are one of the strengths of qualitative research. They are ‘appropriate concepts for attaining rigor in qualitative research.’¹⁵¹⁶ The validity of the research refers to findings that are true and certain: ‘True in the sense that research findings accurately reflect the situation and certain in the sense that research findings are supported by the evidence’.¹⁵¹⁷ The validity ‘is based on determining whether the findings are accurate from the standpoint of the researcher, the participant, or the readers of an account’.¹⁵¹⁸ The researcher needs to validate findings by employing different strategies to ensure accuracy and credibility of the findings. Qualitative validity means that the accuracy of the findings are checked by the researcher using a variety of procedures.¹⁵¹⁹

To establish the validity of qualitative research, a number of scholars suggest a triangulation strategy. Merriam claims that triangulation is the most widely used strategy for increasing the internal validity or credibility.¹⁵²⁰ It is ‘a principal strategy to ensure for validity and reliability’.¹⁵²¹ Holtzhausen considers triangulation as a tool that validates and demonstrates the reliability of data.¹⁵²² Guion, Diehl and McDonald also suggest triangulation as a method to check and establish the validity of studies, as it permits the analysis of a research question from multiple perspectives.¹⁵²³ Similarly, Terrell suggests

¹⁵¹⁵ Sharan B Merriam, *Qualitative Research: A Guide to Design and Implementation* (Wiley, 3rd ed) 209.

¹⁵¹⁶ Morse et al, above n 1502, 1.

¹⁵¹⁷ Guion, Diehl and McDonald, above n 198.

¹⁵¹⁸ John W Creswell, *Research Design: Qualitative, Quantitative, and Mixed Method Approaches* (Sage, 4th ed, 2014) 201.

¹⁵¹⁹ Ibid.

¹⁵²⁰ Merriam, above n 1515, 215.

¹⁵²¹ Ibid 216.

¹⁵²² Holtzhausen, above n 193.

¹⁵²³ Guion, Diehl and McDonald, above n 198.

that triangulation is a strategy for confirmation, corroboration or cross-validation in a single study.¹⁵²⁴ Bekhet and Zauszniewski suggest that triangulation not only confirms findings but also provides more comprehensive data and enhances the studied phenomena.¹⁵²⁵

Triangulation requires the use of different sources of data. The evidence from these different sources is applied coherently to the research questions.¹⁵²⁶ The research was undertaken to determine how things work and to propose improvements in complex situations, such as Indonesia. Stake suggests that triangulation of data from different sources aims to increase confidence that we have correctly interpreted how things work¹⁵²⁷ and will assist to ‘place the research findings in a wider context’.¹⁵²⁸

This research used triangulation from three separate sources in analysing and answering the research questions. Interview data collected from people with different perspectives was compared and cross-checked¹⁵²⁹ with other sources from the literature review and the media data base search. Data from the literature review and the media databases have been used to consider and analyse the information collected from the interviews.

In general, triangulation produces converging conclusions. There is a problem with inconsistent or conflicting findings amongst the independent measures. The researcher has considered the concern of Miles, Huberman and Saldana with triangulation that ‘if two measures agree and one does not, you are stuck with a deeper question: Which do you believe?’¹⁵³⁰ They believed that this issue may be either a mistake made by the researcher or a ‘blessing’. It is a blessing where ‘the different data collection methods used gather different facets of data and their combined effects build on each other to compose a more three-dimensional perspective of the phenomenon’.¹⁵³¹ Patton suggests that the

¹⁵²⁴ Terrel, above n 194.

¹⁵²⁵ Bekhet and Zauszniewski, above n 188.

¹⁵²⁶ Creswell, above n 1518.

¹⁵²⁷ Stake, above n 195, 37.

¹⁵²⁸ Hesse-Biber, *Mixed methods research*, above n 176, 38–9.

¹⁵²⁹ Merriam, above n 1515, 216.

¹⁵³⁰ Matthew B Miles, A Michael Huberman and Johnny Saldana, *Qualitative data analysis: A Methods Sourcebook* (Sage, 3rd, 2014) 299.

¹⁵³¹ *Ibid* 299, 300.

inconsistencies should be viewed as an opportunity to uncover deeper meanings in the data rather than see them as weakening other evidence.¹⁵³²

Triangulation of the opinions in the interviews and data obtained from the literature review and the search of Indonesian media databases have been used to establish an objective opinion on contentious or disputed issues as different methodologies used.¹⁵³³

Reliability connotes consistency, dependability or trustworthiness. In the process, biases, experiences, opinions and knowledge concerning codes, good corporate governance and systemic regulatory practices have been identified by the researcher. The researcher concluded that good corporate governance codes can be used as an alternative form of regulation to address a weak and corrupt regulatory system. However, the researcher also concluded that such codes do not work effectively in the Indonesian context for a number of existing political, cultural and social reasons. Those views and opinions were not revealed or disclosed to any of the participants. The researcher let the participants talk freely and openly concerning their own experiences, knowledge and views. Therefore the interview outcomes are more reliable because they solely focused on the issues from the participants' perspectives and experiences.

The literature reviewed was critically selected and its credibility evaluated in order to establish its relevance and reliability. Some were from valid sources of qualified academic writings such as academic journal databases, as authors with authority in their field, educational institution sites, credible international organization sites and the official website domains.

The media databases were selectively chosen from high-quality and credible information of online and printed information. They are from reputable media in Indonesia, which regularly publish and update information.

¹⁵³² Cited in Guion, Diehl and McDonald, above n 198.

¹⁵³³ R Y Cavana, B L Delahaye and U Sekaran, *Applied Business Research: Qualitative and Quantitative Methods* (John Wiley & Sons, 2001).

7.1.7. Bias issue

Participants who took part in the interviews were chosen as knowledgeable and experienced in the areas relating to the questions the researcher was seeking to answer.¹⁵³⁴ In analysing the data, the researcher has sought to minimize her own biases and opinions by examining and using the information obtained through these resources. She used evidence to draw conclusions rather than relying on her own views. In answering each research question, the researcher compared, contrasted and analysed the result of the interviews and literature reviews as well as media databases to arrive at a conclusion as clear as possible.

7.1.8. Analysis of data

The data obtained from the interviews are transcribed and summarized to link each of the identified themes to be analysed. In this research, the phases of data analysis followed the pattern of an initial familiarization with the data. Transcription of audio recorded data and detailed notes taken from the interviews were read and then noted initial ideas.¹⁵³⁵ The data collected was prepared and selected by the analysis unit who decided on the analysis of the manifested content.¹⁵³⁶ It was then organized in codes, creating categories and grouping codes,¹⁵³⁷ collating data relevant to each code and gathering all data relevant to each potential theme, reviewing themes and defining and naming themes¹⁵³⁸ and reporting the results.

The information and data from the review of the literature provided in chapter two, the media database research from Indonesian printed and online newspapers – including some online foreign newspapers – and the data obtained from interviews indicated earlier was analysed to assess regulatory, corporate governance and disclosure practices: to identify their weaknesses and suggest approaches for improving effective accountability for disclosure.

¹⁵³⁴ Patton and Cochran, above n 1507.

¹⁵³⁵ Virginia Braun and Victoria Clarke, 'Using thematic analysis in psychology' (2006) 3(2) *Qualitative Research in Psychology* 77, 87.

¹⁵³⁶ Mojtaba Vaismoradi, Hannele Turunen and Terese Bondas, 'Review Article: Content analysis and thematic analysis: Implications for conducting a qualitative descriptive study' (2013) 15 *Nursing and Health Sciences* (2013) 398, 402.

¹⁵³⁷ Ibid.

¹⁵³⁸ Braun and Clarke, above n 1535.

It was also analysed to identify related factors including relevant aspects of political and social cultures, including toleration of corruption and their impact on regulatory effectiveness.

The analysis focused on the possibilities of informal rule or soft law represented by good corporate governance codes providing effective alternative regulation within the Indonesian context. The strengths and weaknesses of the codes were critically examined to consider their use in achieving accountability. Some comparisons were also made with the successful use of codes as an alternative regulatory approach in some other jurisdictions.

In analyzing qualitative data, there are different methods including thematic analysis, comparative analysis, discourse analysis or conversational analysis, content analysis, and so on.¹⁵³⁹

The aims of this research are to map the interaction between formal law and regulations and corporate governance codes in Indonesian listed companies; to expand the strength and weaknesses of the use of such codes to achieve accountability; to identify how corporate governance codes and self-regulation impact on formal law in the regulation of these companies; to assess and analyze the impact of formal law and corporate governance codes on disclosure and the effect, in turn, of that disclosure on formal law and corporate governance codes and accountability under them. A combination of thematic analysis and content analysis best served these aims in this research.

7.1.8.1. Thematic analysis

The most common type of analysis in qualitative research¹⁵⁴⁰ is a theme or thematic data analysis.¹⁵⁴¹ It is an independent qualitative descriptive approach, which is described as “a method for identifying, analysing and reporting patterns (themes) within data”.¹⁵⁴² Themes are patterns across data sets. They are important to the description of a phenomenon. They are also associated with specific research questions.¹⁵⁴³

¹⁵³⁹ Dawson, above n 1497, 114–23.

¹⁵⁴⁰ Greg Guest, Kathleen M Macqueen, Emily E Namey, *Applied thematic analysis* (Sage, 2012) 11.

¹⁵⁴¹ Dawson, above n 1497, 119.

¹⁵⁴² Braun and Clarke, above 1535, 79.

¹⁵⁴³ Jeanne Daly, Allan Kellehear and Michael David Gliksman, *The public health researcher: A methodological approach* (Oxford University Press, 1997) 89–104.

Thematic analysis provides a flexible method of data analysis for research using a number of sources and methodologies.¹⁵⁴⁴ It also works well with a phenomenology that focuses subjectively on the human experience.¹⁵⁴⁵

In using this method, the researcher categorizes the themes into three main themes associated with the research questions. They emerged from the literature reviews and are reflected in the interview schedule including disclosure, relevant law and regulation, and good corporate governance codes. Sub-themes, which make meaningful contributions to understanding the research questions are also identified and analysed, such as corporate governance, theories on alternative regulation, informal regulatory concepts, the relationship between formal and informal law, comparative law and legal transplants.

7.1.8.2. Content analysis

Content or textual analysis is ‘a research technique for making replicable and valid inferences from texts (or other meaningful matter) to the contexts of their use’.¹⁵⁴⁶ In content analysis, the researcher uses analytical constructs, or rules of inference, to move from the text to the answers to the research questions.¹⁵⁴⁷ Using this method, the researcher systematically works through each transcript assigning codes, which may be numbers or words, to specify characteristics of the text.¹⁵⁴⁸

By analysing the content of the literature review, the media data bases and the texts of the interviews, the research questions are answered. Firstly, the secondary literature and media data searches have been analysed to refine the research questions and the aim of the project. They have been used to analyse the data collected from the interviews. Secondly, the primary data from the interview transcripts that were transcribed to texts and notes has been analysed to clarify the actual data on disclosure, the function of formal law and codes on corporate governance and disclosure practices. The data has further been compared and

¹⁵⁴⁴ Braun and Clarke, above n 1535, 77.

¹⁵⁴⁵ Guest, Macqueen and Namey, above n 1540, 12.

¹⁵⁴⁶ K Krippendorff, *Content analysis: An introduction to its methodology* (Sage, 2nd ed, 2004) 18.

¹⁵⁴⁷ Marilyn Domas White and Emily E Marsh, ‘Content Analysis: A flexible methodology’ (2006) 55(1) *Graduate School of Library and Information Science, University of Illinois at Urbana-Champaign*, 6.

¹⁵⁴⁸ Dawson, above n 1497, 122.

cross-checked to confirm with the secondary literature and media data search. Its outcomes have been evaluated and clarified with the research questions. It has provided the answers to the research questions. Some inconsistencies have been found between the primary and secondary data, which will be discussed in the following sub-chapter.

The content analysis is presented in a final coding framework followed by description and interpretation of the key findings.

7.2. The key findings

Findings of the field research are presented below in three main themes following the interview schedule, appears in Appendix A, ie: disclosure, regulations and good corporate governance codes. The schedule draws on analysis of disclosure, relevant legislation, the GCG Code and secondary literature in identifying significant issues to further explore.

7.2.1. Disclosure

This finding assists in understanding fundamental problems in corporate disclosure in Indonesia. It demonstrates the need for effective solutions. It assists in locating crucial elements that should be addressed to achieve better standards of disclosure.

The key findings on disclosure are presented in a summary of the final coding framework demonstrated in the table below followed by its interpretation and the conclusion of its implications in answering the research questions.

Table 7.3: The final coding framework of the key finding on disclosure

Final coding framework of the interview questions	Final coding framework of the interviewees responses
Perspectives of the importance of disclosure for good corporate governance	Important but of less priority in practice for most public sector informants; Important as one of the top priorities for some private sector informants
Impact of disclosure requirements on a company's accountability	On paper appears to improve accountability, but in practice its reliability is poor
Efficacies of disclosure	Participants mentioned that it attracts foreign investors
Disclosure discrepancies/ issues	Potential problems in information disclosed in revealing significant gap in remuneration practices between superiors and inferiors, tax obligations and corrupt practices

Weakness of system for corporate governance/disclosure compliance	Superficial check box approach
Factors influencing disclosure compliance	Mostly about meeting obligations/formalities rather than any perceived greater benefit
Non-legal factors influencing disclosure compliance or non-compliance	Corruption, business culture and influential political interests
The roles of professionals in disclosure accountability	Educating and disseminating information practices
The roles of NGOs in disclosure accountability	Educating; disseminating information practices; rating and awarding good corporate governance performances
Suggestions for better disclosure practices	Improving integrity and commitment (business and culture), moral revolution

The findings relating to disclosure, discussed below, demonstrate that culture and politics are influencing factors affecting disclosure practices and compliance. It suggests a consistency with the media data analysis and is less consistent with the literature.

7.2.1.1. The importance of disclosure and its efficacies

The findings suggest different perspectives between participants from the public and the private sectors with respect to the importance of corporate disclosure. Public sector respondents regarded disclosure as an important element for good corporate governance but most of them put disclosure as less or not an urgent priority. Private sector participants particularly business professionals, capital market, rating agencies and corporate governance organizations gave disclosure a high priority suggesting that it is significant for good corporate governance preserving accountability that attracts capital.

Participants from both sectors believed that controllers of listed companies regarded disclosure as an important element for good corporate governance but indicated the lack of attention paid to it and the poor management of it. This is consistent with the indication that corporate governance generally receives a tick the box approach.

In responding to the issue of lack of control on disclosure, one problem identified was the shortage and number of skilled staff who understood significant corporate disclosure issues. Others suggested political and cultural factors such as political interference and corruption.

These findings indicate an adequate recognition of disclosure, but limited perspectives of its efficacies. It is in line with media databases, which evidence different preferences between the public and private sectors perspectives of the significance of disclosure in good corporate governance.

In cross-checking with the literature, the finding is partly consistent on the efficacies of disclosure. It demonstrates a limited perspective and poor understanding and awareness of the role and significance of disclosure. The respondents mentioned the attraction of foreign capital. This may indicate a lack of awareness of other claimed for disclosure. The literature suggests that disclosure is important not only for attracting investment and establishing accountability but also protecting investors, developing capital markets and assessing corporate governance enforcement. It may also eliminate or reduce the impact of financial crises. The findings indicate that the attraction of foreign capital investment appears to be the main concern of the interviewees from both public and private sectors. This is consistent with the indication that they use it as window dressing to attract foreign investment.

The limited perspectives on the benefits of disclosure may confirm one of the legal transplant theories as indicated in Chapter 2. It relates to beliefs and attitudes influencing the outcomes or the level of reception of disclosure as a legal transplant concept as suggested by Blankenburg. The beliefs of those in the host country that disclosure is a foreign concept are a narrower view than that in the donor country.

7.2.1.2. The impacts of disclosure requirements and weaknesses in the system for disclosure compliance

The findings indicate that good corporate governance (including disclosure practices) have significantly improved but suggested poor confidence in the reliability of information disclosed and in compliance with any relevant requirements.

Many, including those from the key institutions responsible for disclosure and its oversight, indicate that the mandatory requirement for disclosure appears to work on paper. On paper, all the corporate governance and disclosure requirements appear to be appropriate for application. However, in practice they fail to demonstrate either reliability

or accountability. This may be an outcome of the tick the box mentality, as indicated earlier.

This finding is line with media data searches, which has revealed an improvement in corporate governance disclosure but also its poor reliability.

The finding confirms some previous studies by the ACGA and ADB acknowledging the improvement but indicating persistence in poor disclosure practices as indicated in Chapter 1. Studies from post the 2007 financial crisis to more recently demonstrate disclosure practices are unsatisfactory or below acceptable standards of performances. ACGA assessments on corporate governance showed that Indonesia was consistently placed in the bottom. Poor disclosure is regarded by the ADB as a significant contributor to Indonesia's low scores or poor corporate governance performance. This relates to the role of disclosure in the corporate governance framework indicated in the literature in Chapter 2. Disclosure is claimed to be one essential pillar of a good corporate governance system. It is claimed to be the key factor – the most important element of corporate governance. It is observed to be at the heart of corporate accountability.

Considering the significant role of disclosure in corporate governance systems, the implications of this finding demonstrate that poor disclosure condition portrays poor corporate governance.

7.2.1.3. Factors influencing and compromising disclosure compliance

The findings confirm that the previously identified significant factors of corruption, political interference, and lack of law enforcement: as indicated in Chapter [1.1], [4.3], and [5.2] hinder disclosure practices.

As indicated earlier, the finding indicates the poor reliability of disclosure. A number of factors were suggested for this by the interviewees. These include corruption and political pressures; fulfilling formalities, weaknesses in the system for corporate governance disclosure compliance, disclosing of unsubstantiated information and the lack of sanctions. These factors confirm the literature reviewed in Chapter 2.

(a) Corruption and political pressure

Private sector participants suggest two general factors render disclosure practices unreliable. Corruption is perceived to be the first and core problem. They point out that

there are comprehensive laws and regulations concerning corporate governance and disclosure but the system does not work effectively due to the persistence of corruption, collusion and nepotism, locally well known as KKN. One private informant, a professional manager, stated that:

kami mau bisnis yang benar dan jujur, tapi kita yang lurus berhadapan dengan pebisnis, petugas pajak dan pemberi ijin kalo nggak nurutin kita yang dimakan” [we intended to conduct a business that is true and honest, but our honesty led us to be a victim when we were honestly dealing over business with officials for tax and licences].

A member of a profession association observed:

dalam praktik bisnis bahkan ada pameo kalo kita nggak main kotor kita nggak bisa maju” [in running a business there is even a proverb that if we do not play dirty – we are honest – we will not be successful].

This describes the pervasiveness of corruption in the business environment.

Some participants in both the public and private sectors indicated a number of cultural factors that contributed to this situation. One is the permissive or tolerant view, which most Indonesians have of it. Most appear to regard corrupt practices as common and tend to accept that they are unable to take on the struggle of rooting it out. The second factor suggested by the private sector participants was the political situation. They pointed to some cases of violation of capital market laws and disclosure regulations on misleading information and data manipulation, which indicated the political manipulation of regulatory practices. Some of the well-known cases have been referred to in Chapter [1.1] including the PT Antaboga, PT Bank Century, PT Matahari Putra Pratama and the Bakri business group.

These findings are consistent with the media data analysis on corruption and political interference as indicated in Chapters [1.1.] and [5.2].

Their responses consistently confirmed Dallas’s, Olin’s and Vincenzo’s claims, in Chapter [2.2.4]. Dallas observed that the quality of public governance including law enforcement and corruption are significant in shaping corporate governance in emerging markets. Olin pointed out that moral hazards are also one significant factor. In particular for disclosure, Vincenzo claimed that judicial procedures around enforcement and national culture determine the level of corporate disclosure. Corruption creates poor public

governance that includes the quality of government and regulatory officials contributing to the inefficiency of judicial enforcement.

The findings indicate a permissive toleration of corruption reflected in the cultural foundations of high uncertainty avoidance in minimising conflicts as indicated in Chapter [5.3.2].

These two fundamental factors of corruption and politics will be further discussed in a separate sub-chapter [7.3].

(b) Fulfilling formalities only

The awareness of the need to comply with disclosure is missing an appreciation of the substantial or fundamental reasons for it including its efficacies. Some respondents in both the public and private sectors indicated that disclosure was complied with to fulfil obligations or as a formality to avoid sanctions. Except for multinational companies and companies affiliated with foreign companies,¹⁵⁴⁹ the level of compliance was often described as merely “*formalitas*” [just on paper].

Many suggest that compliance with rules and regulations is based on a mind-set of *hanya untuk memenuhi formalitas saja* [fulfilling a formality only] regardless of its quality, reliability and accountability for it. One respondent, a senior officer from a key capital market regulator, revealed that:

Kepatuhan terhadap persyaratan disclosure hanya untuk memenuhi ketentuan peraturan perundang-undangan atau peraturan semata, bukan didasarkan pada suatu kebutuhan. Perusahaan-perusahaan memenuhi disclosure hanya proforma formalitas belaka [The compliance with disclosure is only to fulfil the requirements of the law and regulations, it is not considered as a need. Companies respect disclosure only as a formal obligation to be complied with].

An accountant similarly stated:

Dalam praktek pemenuhan disclosure hanya dari sisi formalitas tidak menyangkut substansi [In practice, the fulfilment of disclosure is merely seen as a formality disregarding the substance]

This poor mentality is significantly contributed to by the level of the reliability of disclosure. It indicates the cultural problems and the poor level of commitment, indicated in

¹⁵⁴⁹ Well established and big listed companies that considers disclosure as a need to preserve reputation for attracting capital. This suggests that size of company contributes to the level of compliance.

Chapter 5, contributing to the factors determining the ineffectiveness of corporate governance practices. Ramsay suggested that culture and business circumstances are among the significant factors for successfully implementing corporate governance: see Chapter [2.2.4]. Other also emphasizes on the commitment required for its success, see also Chapter [2.2.4].

This finding is consistent with the analyses of challenges to disclosure indicated in Chapter 5. Corruption and the cultural dimensions introduced by Hofstede, particularly uncertainty avoidance, hierarchy and power distance, are to be observed as affecting disclosure practices in the Indonesian context. It reflects the erosion of trust and honesty because of corrupt practices. Typically high uncertainty avoidance and power distance societies are secretive and place restrictions on information to preserve power inequalities undermining the quality of disclosure in corporate governance statements. This is confirmed by empirical studies by Christopher and Hassan, and Sudarwan and Fogarty: noted in Chapter [5.3.2].

It also reflects that disclosure was not seen as a significant instrument in achieving business efficiencies, as indicated in Chapter [2.3]. A number of writers suggest disclosure is an important tool for good corporate governance, transparency, efficiencies, enhancing accountability of management to investors, investor and shareholder protection, facilitating shareholder activism and for attracting foreign capital as noted in Chapter [2.3].

This finding also relates to the legal transplant theories indicated in the literature in Chapter [2.6] and Chapter [5.4.4]–[5.4.5]. Different mentalities in a recipient country to that of the donor are seen to produce different outcomes. The absence of an understanding of and a commitment to disclosure in the business community contributed to its failure as a foreign concept transplanted into Indonesia. This is confirmed by, amongst others, Walsh, who claims that the legal tradition, the social and economic realities determine the success of transplants, see Chapter [2.6.4.2]. Blankenburg's ideas of legal culture also confirm this, particularly regarding the interrelation of the level of values, beliefs, attitudes towards law, patterns of behaviour, institutional features and the body of substantive and procedural law as indicated in Chapter [2.6.4.2].

(c) Weaknesses in the system for corporate governance disclosure compliance

The findings indicate weaknesses in the system for complying with disclosure including a checklist approach and an acceptance that information disclosed is unsubstantiated. Good disclosure requires more than a check-list and tick the box approach. Box ticking undermines corporate governance and disclosure practices. Pietrancosta suggests that this is a real practical concern. It potentially requires companies to limit themselves.¹⁵⁵⁰

Respondents from the capital markets regarded the unsubstantiated nature of the information disclosed as a significant problem. They revealed that information disclosed was mostly presented as collective or bulked [eg, large total amount] rather than in any useful detail. The information disclosed is thought to be too general. This often led to unsubstantiated rumours in the mass business media that required further clarification. It appears to be an accepted common practice. It is reflected by the absence of strict requirements for that information is too disclosed.

It may relate to indications by some respondents, indicated in later findings below, that companies are not penalised for not fully disclosing details of remuneration. The respondents claimed that the disclosure of remuneration does not fit with the Indonesian context. One of the issues that emerged from the interviewees was the disclosure of information that may reveal a big gap between the remuneration of superiors and inferiors practices. The revelation and information of these may lead to other social problems. This confirms the analyses in Chapter 5 on the challenges to disclosure in corporate governance in Indonesia, particularly around the cultural dimension of uncertainty avoidance. It relates to the maintenance of secrecy and restrictions on information disclosed in order to avoid conflict and competition as suggested by Gray in Chapter [5.3.2].

(d) Lack of sanctions

The public and private sector respondents saw the problems of the lack of reliability in information disclosed as being the lack of sanctions and the absence of any use of regulatory or prosecution powers to control these practices. This again confirms Blankenburg's view of the significance of legal culture on transplantation as indicated

¹⁵⁵⁰ Pietrancosta, above n 418.

above. The institutional features and the body of substantive and procedural law interrelate to the level of values, beliefs and attitudes towards law and patterns of behaviour as indicated in Chapter [2.6.4.2].

The interviewees from both sectors indicated that OJK [previously BAPEPAM-LK], is well respected compared with other state institutions or agencies. Other enforcement agencies suggested that *mereka lebih bersih dan maju dibanding instansi yang lain* [the controller is cleaner (less corrupt) and more advanced (professional) than other state institutions or agencies]. The existing powers of this agency are limited to administrative sanctions. Any prosecution for capital market offenders, including disclosure, have to be transferred for investigation to criminal law enforcement and judicial institutions that are often seen by the interviewees as slow moving or stagnant. Interviewees saw these legal enforcement institutions as corrupt. This confirms the discussion in Chapter [1.1] relating to the lack of enforcement as a significant factor hindering corporate disclosure. It also relates to the analysis in Chapter 5 at [5.2.3] regarding the pervasiveness of corruption in legal enforcement and law making institutions impacting on both law making and law enforcement. Law enforcement bodies and courts were regarded by interviewees as the most corrupt institutions.

Interviewees also perceived the weaknesses in the judicial system as key contributing factors in poor law enforcement. This is due to the pervasive corruption in the judicial system. This is a persistent problem as indicated in previous chapters and in earlier findings. This confirms the discussion in Chapter [1.1] and [5.2.3] on corruption in the judicial system. As indicated in Chapter [4.3], corruption has been a problem in every period since Indonesian independence, and reforming governments are struggling to reduce it. The analysis in Chapter 5 at [5.2.2] also described how corruption affects corporate disclosure practices. Corruption has significant consequences for perceived integrity and the values of trust and honesty. These findings from interviewees also demonstrate that this problem is a fundamental issue. This confirms Daniel's observation that corruption is a crucial problem in Indonesia, see Chapter [5.2].

To address this issue, some suggest the OJK needs to be an independent institution holding prosecution powers like the KPK [Corruption Eradication Commission]. It was

also suggested that the Capital Market Law be amended to impose stricter sanctions than existing ones. Some interviewees suggested that the sanctions are not only administrative fines or imprisonment but also confiscation of all unlawfully gained assets or properties. This last sanction was seen to be required to address grafters.

7.2.1.4. The issues that emerge around disclosure practices

(a) Lack of awareness and understanding

The experiences of private sector participants suggested a number of specific challenges in establishing reliable disclosure practices. Relevant professionals, particularly accountants and auditors indicated that they face a lack of awareness and understanding in their clients of the disclosure required. Information disclosed appears to be biased in the company's management favour. One accountant summed up his experience by saying:

Dalam praktek kalau ada informasi yang tidak berkenan direktur, laporannya tidak dilanjutkan [In practice if a director sees that there is un-favourable information, the financial reporting process will be terminated].

This is an example that indicates companies tend to disclose only positive information and intentionally avoid disclosing negative information.

The responses also highlighted that many company insiders do not know what information should be disclosed. Some boards of directors were reported as having no understanding of their responsibilities with respect to financial reports. They were described as tending to place all of the responsibilities on public accountants for disclosure issues. This confirms the claim by Tabaluyan and Daniri of the persistent poor understanding of good corporate governance cited in Chapter [1.1]. This is also consistent with the earlier findings above regarding limited perspectives and poor awareness around disclosure.

This may relate to other phenomenon reported by respondents. Many observed that the recruitment of directors and commissioners tend to be of family members, close relatives and friends for the purpose of preserving control over them. They often lack skills and experience. These collusive relationships are intended to maintain the controlling shareholders' power over the company in all aspects. It relates to protecting their interests in any way, including disclosing any favourable information. This confirms the analysis in

Chapter 5 at [5.2.4] regarding the cultural values that perpetuate corrupt practices. A general feeling of moral obligations to extended family members provides a foundation to recruit them in establishing business relationships. Family connection is seen as a significant factor for business access and success. It is important to developing relationships and for establishing trust.

This reflects a common problem with typical Indonesian companies with their family controlling structure as indicated in Chapter [1.1]. The literature clearly indicates that these types of companies tend to have fundamental problems in applying corporate governance effectively, as indicated in Chapter [1.1]. Coffee and Coffee claimed, see Chapter [1.1], that this type of ownership attributes to poor performance in corporate governance.

(b) Revealing big gaps in remuneration practices

As mentioned earlier in this chapter, this finding indicates a consistency with cultural dimensions of uncertainty avoidance in Indonesia as indicated in Chapter 5 at [5.3]. Avoidance of conflict is a typical feature of high uncertainty avoidance. It appears to be the grounds for the widespread acceptance of not fully disclosing significant information of remuneration. It relates to restricting disclosure to avoid conflict and competition and to preserve security. On this particular matter, secrecy is seen as a more appropriate approach than transparency.

Some respondents from the private sector suggested that companies are challenged by disclosing information revealing big gaps in remuneration practices. An interviewee from a well-known and respected corporate governance NGO indicated that companies have perceived remuneration as a “*rahasia perusahaan*” [company’s secret] to be kept for preserving social order in the company and the wider society. The disclosure of the remuneration of directors and senior staff may potentially lead to class resentment by employees and in turn to strikes demanding the increases in wages. This is due to the huge gap between the remuneration of superiors and inferiors. The huge salaries are also ‘golden handcuffs’ and a ‘poison pill’ preventing the employees leaving work for a competitor and also limiting the potential for taking over or mergers. This is also to prevent the potential

boards or employees taken over by other companies or competitors by offering a higher and better remuneration.

Some private sector interviewees suggested that the requirement for remuneration disclosure fits so poorly with the Indonesia's context that the regulators appear to not apply requirements for remuneration disclosure. As a consequence, the management of companies enjoy the advantage of not fully complying with the disclosure requirement.

(c) Avoiding tax obligations and related other corrupt practices

This finding is consistent with media data and analysis in Chapter 1, 4, and 5 regarding corrupt business practices. Corruption appears to be a fundamental issue. It is pervasive and deeply entrenched. It affects all of Indonesia's system including disclosure practices.

Some respondents from prominent corporate governance NGOs, professional associations, and corporate lawyers in the private sector also referred to issues of disclosing information, which may reveal a firm's actual tax obligations. They reported, as a common practice, enterprises not fully disclosing their real financial situations in order to pay less tax.

Some other participants in the private sector, particularly professional independent directors and managers, also indicate another issue that information disclosed may reveal bribes and other corrupt practices. Companies are challenged in disclosing these additional costs that do not relate to legitimate business activities. Enterprises affiliated with foreign firms revealed that they needed to allocate a special budget for "*ungkapan terima kasih*" [give something valuable as gratitude for getting business deals or else]. These payments to officials help to preserve future deals and ensure helpful processes. Since the law classifies such gifts or presents as bribery, they are transformed by accounting processes to entertainment services. This confirms the analysis in Chapter 5 at [5.2.2] that corruption has significant consequences for disclosure. Dela Rama, for example, observes that corruption discourages honesty and transparency, see Chapter [5.2.2]. Xun's study demonstrated that corruption also reduced transparency, see Chapter [5.2.2].

In the public sector, the finding suggests that transparency and disclosure are also challenged by the potential revelation of corrupt practices. The majority of respondents

from the public sector indicated political interference influenced the performance of their duties.

Participants from legal enforcement bodies revealed other issues relating to the lack of preparedness by such agencies to address or deal with capital market issues including disclosure because of their lack of expertise. Some involved in legal enforcement have had appropriate training overseas but they were frustrated in practice by fellow officers on the grounds of different legal and regulatory reasons reflecting their lack of expertise. This also relates to the analysis in Chapter 5 at [5.4.5] concerning the complexity of transplanting law in the Indonesian context. Bedner, for example, observed four significant factors that contributed to the lack of legal skills of Indonesian jurists. These include the decline of Indonesian legal scholarship and jurisprudence, uncertain legal practices, the poor mentality of jurists and highly theoretical approaches diverse from problem solving, see Chapter [5.4.5].

(d) The structures of group or holding and family companies

This finding demonstrated consistency with other observations of how the structure of particular types of company affected its disclosure practices. Some such companies tend to focus on efforts to find a way around the disclosure regulations and to avoid compliance. This also confirms the analysis in Chapter 5 at [5.2] that corruption affects the integrity of the business community.

Some private sector participants referred to a specific issue around corporate groups and holding companies. They appear to avoid factual disclosure and produce defensive disclosures. This relates to the selling and buying of shares among their families, cronies and friends to establish and retain the power of majority and controlling shareholders. This also relates to a later finding below on the tendency of these companies to avoid the impact of informal sanctions through negative publicity in the mass media. It is motivated by preserving the company's image.

Other participants observed that family owned companies merely aimed to meet the approach of the minimum requirements of disclosure. This was described as "*pelit informasi*" [information disclosed as little as possible]. This also relates to the claims indicated in Chapter [1.1] on the reluctance of family owned companies to be transparent.

This confirms the earlier finding that controlling shareholders including families tend to disclose minimum favourable information to preserve the controller's interests. It also may be related to the typical insider system with relation-based governance model as indicated in Chapter 3 at [3.4] that Indonesia follows. In that model the most relevant information is available for insiders only.

7.2.1.5. The roles of NGOs and professionals in promoting accountability for disclosure

The findings suggest that corporate governance NGOs and professionals have made significant contributions to promoting accountability for disclosure practices. This emerges from the media data. It confirms the discussions in Chapter 6 at [6.5.4] on the role of corporate governance NGOs. However, they have had insignificant impact on companies and accountability due to a number of factors including some previously mentioned. They include corruption, persistent business cultures, weaknesses in the legal and regulatory system, lack of sanctions, the cultural dimension of uncertainty avoidance and avoidance of some obligations to the state such as taxes.

Some respondents from well-respected corporate governance NGOs indicated a limited perspective and awareness in applying full and good disclosure. One informant from the NGO, for example, said '*emiten tidak mau terlalu detail mengungkapkan remunerasi, hanya jumlah total saja yang dilaporkan*' [issuers are reluctant to disclose remuneration in details, they just disclosed the total amount of it]. Other informants added by saying '*perusahaan enggan untuk buka remunerasi pegawai secara detail karena akan jadi konflik ketika dilihat oleh pegawai dan perusahaan lain kemudian serikat pegawai akan demo*' [a company is reluctant to disclose the remuneration in detail because it potentially creates a conflict leading to a strike from the employee's union once the large gap of the remuneration practices is known]. This relates to, as indicated earlier in the subsection [7.2.1.4], the revealing of big gaps in remuneration practices, a cultural dimension of high uncertainty avoidance. Other informants observed that '*perusahaan membentuk komite audit tapi cuma sekedar bentuk tanpa peduli berfungsi atau tidak*' [companies established an audit committee regardless whether it would work/function or not]. Another informant also indicated that there was an issue of reliability of the implementation of good

corporate governance. He pointed out that the criteria for an award for good corporate governance implementation was merely based on check and list system regardless the substances. He gave an example that a company even questioned and wondered how they were chosen as a winner of the award since they acknowledged that they may not deserve it.

7.2.1.6. Recommendations to improve disclosure practices

(a) An effective and good ethical business culture

In general, both public and private sectors participants suggested that good corporate governance including disclosure relies fundamentally on ethical issues. They suggest that the sense of moral obligation is the key to better compliance with disclosure. Personal integrity and a commitment to a better business culture are seen as the key factors for better disclosure practices in Indonesian listed companies.

Some participants suggested different approaches to establishing ethical business cultures. An experienced academic researcher in accounting and member of the board of a public accountant association suggested that the establishment of business culture requires an initially regulatory approach so that over time it may evolve to be part of business culture. She believed that a regulatory driven approach is required as an initial effective approach to changing people's attitudes and behaviours. It then may gradually create in people mind-sets, which respect compliance as part of good business culture.

A participant from a securities custodian company suggested that the ethical culture may be improved by introducing core subjects relating to ethics in all formal education and business institutions from an early stage. This will be discussed in the separate sub-chapter on factors, which better promote the use of an informal code.

Role models are also considered by some respondents as having the capacity to establish integrity as part of business culture as indicated in later findings at [7.2.2.3]. This considers the typical leadership style of hierarchy and patronage where the role models offered by the superiors have significant influence on the inferior's beliefs and attitudes. It relates to the national character of Indonesian corporations and the cultural dimension of power distance as indicated in Chapter [2.2.4] and [5.3.2]. One of the three pre-eminent attitudes introduced by Ki Hajar Dewantara, as indicated in Chapter 4 is that leaders should

be exemplary models for their subordinates. Leaders or superiors, to become patrons, need to legitimise their influence over inferiors. Paternalistic leadership, locally known *bapakisme*, considers the position of the superior as a *bapak* [father] and the inferior as *anak* [child]. It relates to the loyalty to a hierarchy structure of authority. In a society with the hierarchy and power differences indicated in Chapter [5.3.2], superiors are expected to be paternalistic with the patronage system.

7.2.1.7. Conclusion

Overall the findings on disclosure confirm the widely observed factors indicated in Chapter 2 that the effectiveness of corporate disclosure practices depends on factors such as culture, legal institutions, politics and history. The Indonesian context shows that these factors led to the present poor corporate disclosure practices. These poor practices contribute to Indonesia's poor performance in disclosure as the key factor in good corporate governance. This confirms the literature reviewed in Chapter 2 and also the media data.

7.2.2. Relevant Laws and Regulations

The findings on the role of the relevant laws and regulations in supporting good corporate governance and disclosure practices are presented in the table below followed by more analysis of them.

Table 7.4: The final coding of the key finding on the role of the relevant laws and regulations

Final coding framework of the interview questions	Final coding framework of the interviewees responses
The role of relevant laws supporting accountability of disclosure	Unsatisfactory
The effectiveness of relevant laws, regulatory agency rules and other regulations on disclosure	Unsatisfactory
The role and effectiveness of the capital market in ensuring disclosure compliance	Unsatisfactory
The role and effectiveness of the regulatory agency in ensuring disclosure compliance	Unsatisfactory
The use and impact of informal sanctions	Limited effectiveness for big public companies; and irrelevant for group and holding companies

7.2.2.1. The failure of relevant laws supporting accountability of disclosure

The findings suggest that the loss of trust because of corruption and a weak legal system that makes the relevant laws and regulatory practices fail in their support for accountability for disclosure.

(a) Loss of trust in formal legal system

This finding is consistent with the media data search. It also confirms the claim indicated in Chapter 2 that corruption has eroded confidence in the legal system. Corruption creates an unvirtuous circle, which erodes perception of fairness and trust. This condition establishes a legal culture of disobedience to the law [*budaya tidak taat hukum*]. This confirms Friedman's concept of the legal culture as a social thought and a force determines the law being used, avoided, or abused. It relates to the claim that individuals determine the implementation of the law. It is also consistent with Blankenburg's concept that the level of values, beliefs and attitudes towards the law, patterns of behaviour, institutional features and the body of substantive and procedural law are the four levels, which are complexly interrelated with each other in establishing legal culture, see Chapter [2.6.4.2].

Most participants across the public and private sectors indicated that most people have lost their trust in legal system. Judges, public prosecutors, and lawyers all acknowledged this. They attributed this to the persisting condition of the weak and corrupt legal system. Comments from officials with regulatory and enforcement bodies including corporate law judges revealed the critical issue: "*suap pada petugas sudah parah*" [bribery with officials is dire – a common practice]. It was further agreed that "*aparatus kami memang lemah mental*" [the mentality/integrity of officials is poor]. They admitted that people have lost trust in judicial institutions. One staff member of legal enforcement body observed "*salah satu dari undang-undang atau peraturan, sarana prasarana dan aparat hukum sakit maka semua jadi sakit*" [if one regulatory, or legal enforcement body does not work, the rest will also not work, or be damaged]. One senior public prosecutor stated

“penegakan hukum sudah parah karena lembaga-lembaga pengawas juga terlibat” [law enforcement is in a dire condition because supervisory agencies also were involved in corrupt practices]. One corporate lawyer revealed that bribery appeared to be a common practice in the judicial system as it is needed to win a case. Another lawyer confirmed this by saying *“urus kasus di pengadilan harus beri duit”* [should give amount of money/bribe for winning a case]. He further said that there is a rule, which forbids litigants from meeting with the judges. In fact, litigants are able to, and do, see judges. A lot of media reports confirm the widespread practices of bribery in the judicial system. Among many significant and recent reports are the bribery cases involving the chief justice of the Constitutional Court, panel judges of the Supreme Court and the Administrative Court in 2015, see Chapter [5.2.3].

The findings suggest the reality of a weak legal system can be attributed to the laws not being respected. They also suggested that the relevant laws such as Company Law and Capital Market Law, regulatory agency rules and other regulations on disclosure are not working effectively in creating accountable and reliable practices around corporate disclosure. This confirms the earlier finding above where it was noted that compliance with disclosure was compromised.

On paper, all these laws and rules demonstrate strict requirements for appropriate levels of corporate disclosure. However, the evidence indicated that in practice the business community appears to be choosing to interpret disclosure requirements as being inappropriate or is ignoring them.

Corruption, which was attributed to a loss of trust in the legal systems, was thought of as a legacy from the past. Some members of a legal enforcement body suggested that historical, inherited and corrupt behaviour is among the contributing factors. The Indonesian legal system inherited elements of Dutch corruption and also from the old order regime after independence. One claimed *“it was hard to find fairness in business”*. These norms have become rooted in Indonesian life and have evolved within its legal culture. They are reflected in a comment by one member of a legal enforcement body saying *“budaya tidak ada kesadaran hukum, tidak taat hukum dan masa bodoh”* [a legal culture of no legal awareness, disobedience, and apathy].

People appear to find a way around the law to avoid it. A corporate lawyer respondent from a well-known law firm observed that there is a common perception that “we don’t break the law but we are stretching out the law”.

7.2.2.2. Ineffectiveness of relevant laws and regulations on disclosure

The findings suggest that the ineffectiveness of relevant laws, regulatory agency rules and other regulations on disclosure are attributed to a weak legal system and wider issues around the failure of legal transplants and some other related factors. This is relevant to weak legal protection as a typical characteristic of the corporate governance system of European and Asia Pacific relationship based systems indicated in Chapter 3. It relates to the insider system as distinct from the outsider system with rule-based governance found in the USA and the UK.

(a) Weak formal legal system

Private sector respondents pointed out the formal legal system as the problem. Many respondents indicated that the absence of law enforcement and accountability for poor disclosure is a critical matter in the legal system. Corruption and political interests relate both to the legal drafting process and to enforcement. The laws and regulations appear to be made without regard to whether they will work or not. Legal drafting appeared to be related to a particular project and a program. It was often done to fulfil an allocated budget that had to be spent. The laws have been made as a reaction to a situation rather than as a holistic response to complex problems. It has led to the legal system being unable to work effectively.

The weak formal legal system indicates the need for alternative approaches as promoted by a number of scholars indicated in the literature reviewed in Chapter 2. Braithwaite observed that Indonesia needs to employ informal law in the context of responsive regulation in addressing the country’s limited capacity of regulatory and resources, see Chapter [2.4.2.2]. He suggested that the informal law is a less expensive strategy for mobilizing social control than state control of formal law. Aldasev also suggested the need for informal law as formal law may not be trusted and followed because it is unable to fulfil required expectations, see Chapter [2.4.2.2]. Pistor observed that

informal law is needed when the formal law lacks of its credibility and trust. Helmke and Levisky promoted informal law as a substitute for ineffective formal law, see Chapter [2.4.2.2]. Similarly, Pilarcyck suggested that informal law may replace formal law, see Chapter [2.5.3].

(b) Unsuccessful legal transplants

This finding is consistent with legal transplant theories, outlined in Chapter 2, where a number of scholars suggested that the non-legal factors determine the success of a transplant. Walsh referred to the capability of foreign models to adapt to the local legal traditions and institutions, and suggested that the social realities of the recipient system are the determining factors. Legrand, Kahn Freund, Friedman, and Blankenburg are among other scholars who have suggested that social, cultural, and political factors are significant: see Chapter [2.6.4].

Both public and private sector respondents suggested that the laws and regulations are hybrids that do not fit with the Indonesian context. Legal enforcement official and corporate lawyer respondents suggested that they were challenged in implementing the laws, as they were imported from foreign legal cultures and have either grow from or evolved to form roots in the local Indonesian culture. These responses also revealed a positivist view that law means the law laid down by the state. In respect to the use of good corporate governance principles from voluntary codes, they showed a lack of understanding and familiarity with soft law. This appears to relate to the positivist emphasis in the civil law system that Indonesian jurists still strongly maintains as stated by Bedner in Chapter [5.4.5].

They revealed that the challenge of implementing transplanted laws has become more difficult and complicated because of the loss of trust in public officials and regulatory bodies. Some respondents from the private sector stated that companies appear to avoid any court proceedings and tend to settle disputes in arbitration, but the outcome may still require court involvement to enforce an arbitration award.

These findings on laws and regulations are consistent with the data in the media database. The weak formal legal system has been marked in all periods after Indonesian

independence. Practices around corruption, collusion and nepotism (KKN), noted in Chapter [4.3] and [5.2.3] attribute to this.

They are also consistent with the literature relating to the legal transplant issues indicated in Chapter [2.6.4]. The findings demonstrate that a number of non-legal factors and poor adjustments to the local situation have contributed to the failure of those legal transplant. These factors, see Chapter [2.6.4.2], including the mentalities of local elites, as pointed to by Watson and Kahn Freund, integrity of formal law and associated institutions, as observed by Bedner, and legal culture, as noted by Friedman, are all found poor in Indonesia.

Laws that have been transplanted are not compatible with Indonesia's situation. The laws fail to serve its accountability as they are considered cosmetic transplants, which are not supported by local elites. Poor enforcement also attributes to this failure. Poor promotion and popularisation of good corporate governance contributes to the failure of the use of the principles in the GCG Code. This is in line with other problems within the legal culture, as indicated in literature review in Chapter [2.6.4]. Foreign legal transplants have clashed with the local legal culture. The different mentality of regulators and the regulatory practitioner's culture of the donor jurisdiction appear to be the factors for very different applications of the laws within the host country.

(c) Lack of transparency

Participants from some legal enforcement bodies revealed their experience that the absence of transparency through misrepresentations or dishonesty in financial reports led to the litigation. The misrepresentation mainly related to a firm's assets, and irregularities in the change of management or board members and irregularities at shareholders' and directors' meetings. The ground for litigation was often related to alleged misrepresentation in financial reports or to seeking an audit of the report as part of resolving disputes. This finding indicates a consistency with the cultural dimension of high uncertainty avoidance, which was marked by secrecy rather than transparency as indicated in Chapter 5 at [5.3.2.1].

In making these judgments of such cases, one staff member from the legal enforcement body indicated that only the formal law in the Company Law or capital Market

Law has applied. This suggests that the GCG Code was not recognised within regulatory framework as informal law. This confirms that it is difficult to accommodate informal law in the Indonesian civil law system. This issue will be further analysed below in a sub-chapter on the findings on the function of the Code and its relationship with formal law.

(d) Limited effectiveness of informal sanctions

The finding suggests the significant use of informal sanctions but poor overall outcomes. Many respondents suggest the loss of the effectiveness of these kinds of sanctions. This relates to the loss of *budaya rasa malu* [the culture of shame] as noted in Chapter [5.2.4].

Participants from the stock exchange and the capital market regulator acknowledged the role of financial media and the mass media as significant for both the stock exchange and the OJK. They regarded mass media publicity as a source of informal sanctions for “*pencitraan perusahaan*” [company’s image] supporting their own regulatory and supervisory functions. This was despite certain media publishing unsubstantiated rumours for intentionally negative purposes including blackmail. This finding indicates that informal sanctions have been acknowledged and respected. Media reports confirm this.

From those participants’ experiences, they mainly utilized those publications to assess the performance level of a firm’s disclosure compliance. They use information, including rumours in the mass media, as sources to assess issuers’ disclosure and to make relevant decisions. The media reports are used to identify potential cases for investigation. This is reflected in an example at the stock exchange, in the practice of reading all news related to issuers in at least eight media outlets as a routine daily activity prior to the commencement of trading activities. These respondents from the stock exchange and capital market regulator similarly reflected this use of media. One observed that “*kebanyakan kami mengetahui ada hal-hal yang tidak beres dari suatu perusahaan justeru dari berita-berita yang beredar di media massa*” [We mostly identify issues/problems about a firm from the information or reports in the mass media]. It indicates an acknowledgement of informal sanctions, which have a deterrent impact as claimed by, amongst others, Parker and Braithwaite, Wymeersch and Goldschmidt as indicated in Chapter [2.4.3]. Negative publicity, public criticism, gossip, embarrassment and shame,

reputational damage for the company as well as loss of trust in the management were all considered by informants to potentially effective informal sanctions.

Those respondents also acknowledged another significant role of the mass media. The media reports often unveil the real beneficial owners or shadow owners or directors. They may not appear to have any legal interests in the companies but they have influential power over board members and control the companies. They often appear in the media to make comments on the company's performance and respond to any rumours circulating.¹⁵⁵¹ This finding confirms previous findings of the 2010 ROSC of significant poor disclosure of ultimate ownership and control noted in Chapter [1.1.4]. This reflects the need for the improvement of disclosure on beneficial and controlling ownership as indicated in Chapter 1 at [1.1].

Some respondents from the private sector indicated the ineffectiveness of informal sanctions. They observed that members of the business community appear to find a way to protect their image. Businesses tend to be structured in the form of holding companies with their listed companies becoming a cash cow for their parent companies, and for avoiding unfavourable impacts on business reputation from negative publicity. Holding companies always appear to preserve their reputation even when subsidiaries appear to be engaged in unfair dealings and practices. Business activities continue in other companies in the group despite the fact that one of the companies may fail because of the impact of negative publicity.

(e) The challenge of controlling a large population

One participant from a legal enforcement body indicated that the size of the population was another factor leading to the ineffectiveness of laws and regulations in general. He considered Indonesia's population, about 250 million, spread over a vast area, as too difficult to control. He observed "*banyak dari mereka yang sulit diatur*" [most of them appear to be unruly]. He considered that by comparison Singapore is easier to govern

¹⁵⁵¹ Some respondents demonstrated their pessimistic beliefs that disclosure issues around real beneficial or shadow owners would seriously be addressed by the authorities due to corruption, collusion and nepotism still remain rules. Such owners usually have power and money that make them having some certain privileges and immunities. This is consistent with the later finding at section [7.3.2] that money is power in Indonesia.

because of its small population and territory. The small size of Singapore may contribute to its anti-corruption ethos and political determination, indicated in Chapter 3, and the effectiveness of laws and regulations as well as the informal law of its corporate governance code.

7.2.2.3. Recommendations for improving the legal system

(a) A mental and moral revolution

Most respondents from the public and private sectors indicated the need for a fundamental change in states of mind and the ways of thinking that will support an accountable and less corrupt style in both the legal system and business life. A mental or moral revolution by the people was considered to be an effective strategy to better the legal system and improve integrity in business.

This also applies to the effectiveness of soft law such as informal good corporate governance codes as indicated in Chapter [2.4.2]. Moral suasion, as suggested by Haines and Zerilli in Chapter [2.4.3] determines compliance with such soft law.

(b) Role models

Some participants, particularly from the private sector, suggested the need for a “*tokoh panutan*” or “*contoh dari pimpinan*”[role model]. Role models are seen as an effective approach to shape behaviour and attitudes. They believe if leaders or superiors have integrity and honesty, in turn followers or inferiors will be likely to be influenced to respect integrity. This relates to the continuation of a paternalistic culture as indicated in Chapters 4 and 5 where the relationship between a superior and an inferior is described like a parent and child. The role model of a parent or superior significantly affects the inferiors’ behaviour. This seems to address the cultural dimension issue of power distance, as indicated in Chapters 5.

(c) Political commitment

Some respondents from both public and private sectors suggested a need for stronger political commitment in reducing corruption. They demonstrated desperation in the need for eradicating corruption and poor legal cultures. They considered the lack of political will as the significant factor. They considered that political will is limited to being a statement and has never been put in place. Lessons from Singapore, as indicated in

Chapter [3.5] show the significance of the political commitment as one of determining factors for successful corporate governance and disclosure regimes.

7.2.2.4. Conclusion

The relevant laws and regulations fail to support better corporate governance and disclosure practices for a number of factors. The factors include lost of trust in the formal legal system; the weak legal system, the failure of legal transplants, lack of transparency and the limited effectiveness of informal sanctions.

The reference to the need for moral suasion for compliance with the soft law suggests that an even softer kind of law or systems of norms is required. Basic moral values need to be re-acquired.

7.2.3. The role of Indonesia’s Code of Good Corporate Governance

The key findings of the role of the good corporate governance code are presented in the final coding framework with the related responses summarised in the table below followed by a more detailed analysis of the responses.

Table 7.5: The final coding of the finding on the role of Indonesia’s Code of Good Corporate Governance

Final coding framework of the interview questions	Final coding framework of the interviewees responses
The Code as an efficient, effective & responsive tool for better regulation	Not confirmed
Efficacies of the Code	Visionary/Idealistic/Reference
Legal power of the Code	Nil
Obstacles in applying the Code	Cultural and political factors
The relationship between the Code & existing formal laws	Not inter-related/Ineffectual
Companies’ interest/awareness in applying the Code	Very poor
The influence of the Code on companies	Insignificant
The Code’s contribution to effective disclosure	Poor; the Code has lost functions to mandatory disclosure requirements
Factors that clash with the Code’s application	Culture and regulatory driven or top down models of regulation
The role of government, business community & NGOs in the use of the good corporate governance code	Very limited

7.2.3.1. The functions of the Code and its relationship with formal laws

The finding indicates that the Good Corporate Governance Code does not serve as an efficient, effective and responsive form of regulation. It merely serves as '*pedoman*' [guidelines]. *Pedoman* means flexible non-binding and non-regulating: a token or symbol. The Code has not been effective in assisting as a source of informal rules to achieve better outcomes with the existing formal laws and regulations on corporate disclosure.

The findings also suggest that there is no relationship between the GCG Code and the existing relevant formal laws. The GCG Code is not recognised in the legal framework. As it is regarded as just a reference, it has not been used to assist or supplement the formal law as suggested by a number of scholars indicated in Chapter [2.5.3]. The formal legal framework is significant in this context as some scholars considered that the effectiveness of enforcement needs both formal and informal instruments, see Chapter [2.5]. Some alternative regulatory theories suggest that there are potentially significant efficacies in the mixture of formal and informal law in Indonesia's context. Parkinson, Black and Braithwaite observed that the combination of formal and informal law may become an effective and efficient regulatory strategy as well as an effective apparatus for enforcement, see Chapter [2.5.3]. The relation between formal and informal law is significant in Indonesia as the formal legal system is weak. Parkinson claimed that this mixture may be the most effective and efficient regulatory mechanism. Parker and Braithwaite considered that the mixture can be even better as formal law interpreted by informal law and informal law backed by formal law. Black observed that the combination can create the right balance of discretion between formal and informal law.

These findings on the Code as a representation of informal or soft law are consistent with the analysis of media databases but are inconsistent with alternative regulatory theories as suggested in new regulatory concepts described in Chapter [2.4.]. The voluntary Code does not work in the Indonesian context. It fails to demonstrate flexible, relevant and responsive regulatory functions required in business practices. It is too flexible in the face

of poor practices. The lack of the capacity of the formal law is too great. The existing social, moral, and business norms do not support its capabilities.

There is no evidence that the Code is effective as informal law as a legal strategy for addressing a lesser or weaker regulatory capacity suggested by some scholars. Braithwaite, Pistor, Helmke and Levitsky, Aldasev et al, and Pilarczyk all considered informal law to be an effective strategy in this context, as indicated in Chapter 2 at [2.4.2.2] and [2.5.3]. The role of corporate governance codes as informal regulation. A number of scholars suggested significant roles of the Code as informal law including a more effective and efficient regulatory instrument as well as an alternative regulatory strategy for developing countries with weak formal legal systems or weak law enforcement. Braithwaite, for example, promotes the use of informal law in the context of responsive regulation in addressing limited capacity of formal law. He suggests that it may reduce the use of formal law and mobilise cheaper forms of social control than the formal law and regulation of the state. Similarly, Pistor, Helmke and Levitsky considered informal law as an alternative strategy when formal law is incomplete or ineffective because of its lack of credibility. Aldasev also similarly suggests the use of informal law when formal law fails to work effectively or becomes a dead letter because of the loss of trust in it. Pilarczyk also considered one function of informal rules are to supplant the formal law. Informal law may replace an ineffective formal law.

However, there is no evidence, as indicated in earlier findings, that a civil legal system with the legal culture of Indonesia is likely to employ soft law represented by good corporate governance code. The Code is not recognised in the legal and regulatory framework and is only regarded as a reference or symbol. The Code, as soft law, is so weak in an Indonesia context because all other factors in the formal and regulatory system are weak.

This suggests that Indonesia has lost an opportunity to benefit from this alternative strategy to address its weak formal law. Indonesia also has not taken any lessons from the use of good corporate governance in some other jurisdictions, particularly in some South East Asian countries, which have similar conditions with Indonesia, see Chapter [3.5.]. Those lessons demonstrate that the use of the Code contributed to the improvement of

corporate governance practices. European countries display positive impacts from the use of voluntary Codes as soft law, regardless of the type of legal systems. Indonesia's legal system seems too weak and unable to take any opportunities to improve itself. Too many complicated, crucial and fundamental problems spread out across all Indonesia's regions and need to be addressed such as Indonesia has insufficient energy, commitment and will not commit to radical efforts to deal with the problems.

7.2.3.2. Efficacies and legal power of the Code

Most participants indicated that the Code is a visionary or idealistic instrument reflected in the absence of a binding-force. It is only seen as a reference. Some suggest the Code is an historical document that merely fulfils a formality required by the IMF at the time.

The Code was not a regulation. It has no sanctions to apply. Since it was not able to be applied coercively, companies do not see the need to comply with it. The Code has not been widely used in Indonesian business practices. Its influence on companies is insignificant. Many participants from both the public and the private sectors saw this as an obstacle in applying the Code.

An awareness of self-enforcement voluntary codes seemed impossible to most interviewees. Some participants believe that a self enforcing culture did not exist. This was indicated by many, from both public and private sectors. One stated similarly: "*Sedangkan sudah ada peraturan dengan sanksi tegas saja dilanggar, apalagi hanya pedoman yang tidak ada sanksinya*" [the existing rules with strict sanctions are violated, so the code without sanctions is ignored altogether].

This confirms that the legal culture is the problem, as suggested earlier. It relates to the culture of law enforcement bodies and wider society. More generally, neither existing formal laws nor the Code as informal rules will be effective, as they are not respected in the first place. This again indicates that the legal system, being so weak, affects all aspects of Indonesian life.

7.2.3.3. The role of government, the business community and NGOs

The role of the KNKG [the national commission on governance policy] is, amongst others, to raise awareness of the use of the Code. This is insignificant. The findings also

suggest that the role of corporate governance NGOs in promoting the use of good corporate governance code is also insignificant. Both participants from the public and the private sectors acknowledged the efforts of the KNKG and NGOs in raising awareness of and promoting the Code to apply good corporate governance. But they indicated that the Code has not been used. Many participants see the Code as a powerless instrument by suggesting “*sedangkan peraturan yang sudah jelas ada sanksi hukumnya saja dilanggar apalagi hanya pedoman [the Code] yang tidak mengikat tidak ada sanksi sama sekali*” [while the rule with legal sanctions was violated let alone the Code with the absence of sanctions all together was ignored].

Neither the Indonesian government nor corporations show significant collaboration with NGOs in seeking to encourage the adoption of voluntary policies such as the GCG Code as suggested by Kim in Chapter [6.5.4].

7.2.3.4. Conclusion

The use of the Indonesian Code of Good Corporate Governance is inconsistent with claims made in alternative regulatory theories because of the complicated problems in the local legal and regulatory systems. It is consistent with theories of legal transplants. This may suggest a need for further research for any other kind of informal laws such as codes of conduct, which might corroborate or distinguish these findings.

7.3. Evidence of factors which compromise the use of informal Code

As earlier findings above suggest a number of issues identified hinder the use of the Good Corporate Governance Code in regulating disclosure for corporate accountability, this sub-chapter provides a more structured and comprehensive description of the evidence of specific problems. These problems, as discussed below, not only erode the informal law but also the formal legal system as indicated earlier. Effective strategies should be developed to address these problems.

7.3.1. Corruption

Most informants pointed to persistent and pervasive corruption prevailing in all sectors of society and particularly in business. Corruption is a common practice. This confirms the claims indicated in Chapter 1 that corruption is a promising business

opportunity; and that business will not run without bribes. It relates to Indonesian cultural heritage centred around power distance and uncertainty avoidance as well as political and business conditions pre and post independence that were also indicated in Chapter 4 and 5. It is also related to corporate structures and patterns of concentration in Indonesian corporations.

The experience of business professionals indicates that they need to spend extra additional “idle” costs in dealing with bureaucracy. One respondent described as “*perusahaan berada di sarang penyamun*” [it is as if the company is in a den of thieves]. Experiences of dealing with the bureaucracy are very costly. The requirement for companies to comply with laws and regulations have been utilised for individuals’ advantage rather than for reliable enforcement. *Uang pelicin* [kickbacks] are identified as required in dealing with officials. There is no other choice as companies are under the control of the government for licences, permits, etc. Mass media journalists are also often involved in kickback schemes, locally known “envelope culture” [*budaya amplop*] that influences the publication of positive information and reduces or eliminates negative publicity.

There is also some indication that poor remuneration leads to corrupt behaviour. Some participants both from the public and the private sectors suggested better remuneration for civil servants as one solution. Some participants see underpayment practices as one factor leading to corrupt practices. Civil servants cannot afford their living standards or lifestyles. Many Indonesian are unable to buy a house as their income just meets daily needs. However, they also acknowledged that this is a dilemma, as the government cannot afford to pay higher remuneration.

As indicated in Chapter 1 and 5, the corruption problem affects both the law and regulation in the corporate governance system. It erodes the perceptions of fairness and trust and that erodes belief in the legal and regulatory system. This has contributed to the Indonesian formal legal system having poor credibility and legitimacy.

7.3.2. Permissiveness and toleration of corruption

The finding indicates the persistence and pervasiveness of corruption as a fundamental problem because of its toleration by most Indonesian people. This relates to the weaknesses of Indonesian culture as indicated in Chapter [5.2.2.]–[5.2.4].

Some respondents from the public and the private sectors indicated that money is power in Indonesia. The richer you are the more respect you receive. If you are rich you are likely to get more respect from others regardless of the way you acquire your wealth. Indonesian people tend to tolerate corrupt practices. This relates to the absence of a culture of shame, as indicated in [5.2.4.]. It also relates to poor ethical and moral conditions, as indicated in Chapter [4.3.]. Indonesian people tend to accept corruption because their inability to combat it. Pessimistic beliefs that it cannot be eradicated are still held.

Grafters continue to enjoy a good and respected life after release from prison. They still appear to be well respected people in the community. Some may be appointed to senior positions. This is indicated in Chapter [1.1.]. The mass media revealed a new law allowing those convicted people including grafters, to stand as mayors or governors for the elections in December 2015.

When officials or businesses suddenly increase their properties and wealth after occupying official positions and with close links to ruling parties, people tend to regard them as having had a successful career or business, ignoring that they were likely to have been acquired by corrupt practices. This is in contrast to some suggestions that the grafters should be ostracised from society as suggested in Chapter [2.5.2.].

A number of cultural factors have contributed to the tolerance or acceptance of corruption. “*Menjaga perasaan orang*” [giving other people face] and the loss of “*budaya rasa malu*” [culture of shame] are the two significant factors. One interviewee from a well respected NGO said that “*dunia bisnis banyak yang nggak tahu malu*” [Many business people have lost awareness of shame].

One respondent provided an example of this loss of awareness. His friend was a member of parliament who had a target of pooling as much money as possible during his 5 year term. His friend acknowledged that the consequences may be that he would be

imprisoned. But he believed that after prison, he and his family would still enjoy their wealth, make donations to charities and in turn, receive respect from people.

This permissive attitude also relates to the cultural dimension of uncertainty avoidance. People tend to tolerate these corrupt practices to avoid conflict. They seem to create harmony in society.

7.3.3. Supremacy of politics

Many informants indicated that politics in the regulatory and business system is the supreme power. Politics has a strong influence on shaping formal law. Political pressures affect the law making process and its enforcement as indicated in Chapter [5.2.5]. Participants from legal enforcement agencies admitted that there is political interference in the judicial system. For instance, one public prosecutor revealed that *‘dalam segala hal atau putusan dipengaruhi oleh eksekutif dan politik, intervensinya sangat luar biasa’* [the interference of executive and politics in the judicial system is an extraordinary extensive]. One judge also revealed similar tone by saying *‘pengaruh politik sangat kuat dalam hukum formal’* [the influence of politics in formal law is so strong]. This erodes the independence of judges. Another informant further pointed out the political interference in the placement of law enforcement officials resulting in ‘the right man in the wrong place’ – those who have civil law expertise have been placed in the position for handling criminal law affairs.

The mass media widely exposed the criminal allegations against the KPK commissioners and deputies, described in Chapter 1, demonstrating the powerful influence of politics in an ostensibly independent anti-corruption body.

Some participants referred to the power of the anti-corruption body, KPK, as being under the control of the government and parliament. The commissioners are appointed by the parliament. The parliament, as a political institution, is vested with political interests. It has the power to amend or change the Law on KPK including reducing its power as indicated in Chapter 1. Despite the KPK being an independent body, it is believed to be influenced by political interests. Recent media reports in 2016 have again exposed the efforts of some members of parliament to change the Law of the KPK to further weaken its power, see Chapter [1.1].

7.3.4. Finding loopholes in the laws and avoiding compliance

One informant from the private university quoted Plato observation that: ‘good people do not need laws to tell them to act responsibly, while bad people will find a way around the laws’¹⁵⁵² to describe one key issue that challenge the effectiveness of Indonesian laws and regulations.

Many informants from both the public and the private sector observed that people find ways to break or avoid the law. There are strict and clear regulations to prevent corrupt practices. Officials are prohibited from receiving any kind of gifts from related or involved parties. In fact, in order to maintain a relationship with officials and other business people, a company is always required to allocate additional costs called “entertainment cost” as indicated earlier at [7.3.1]. They are spent entertaining related officials and business people, otherwise the company will not get any future business deals. Entertainment is not a gift that is prohibited by relevant law or regulation. Informants noted that this is an effective way to avoid sanctions.

Informants from law enforcement body and a well respected corporate governance NGO observed that the creation or appointment of shadow directors is also a way to conceal self-dealing transactions. The absence of disclosure on foreign investment funds is used to buy and resell shares.

7.3.5. Conclusion

The finding consistently demonstrates that corruption, political influence and cultural values are fundamental factors compromising the use of good corporate governance code as informal law.

7.4. Evidence of factors that promote the use of the informal code

In addressing the fundamental problem related to conduct of the corrupt, most participants promoted solutions that may be a more effective approach fitting Indonesian characteristics. They mainly considered the use of religious norms and participation in formal education to address the problem. These were considered to be capable of shaping mentalities and developing ethical and moral cultures around respecting laws and

¹⁵⁵² Goodreads, *Quote by Plato* <<http://www.goodreads.com/quotes/33783-good-people-do-not-need-laws-to-tell-them-to>>.

regulations and informal laws such as the good corporate governance code and its principles.

7.4.1. Religious norms

Most respondents from both the public and the private sectors believed that religious norms and values were the best approach to be used in reshaping integrity in Indonesian life. They considered that religion is indispensable in Indonesia. Indonesians must decide to hold one of the officially recognised religions as an identity. Religious norms pervade all Indonesian life. They are seen in day-to-day life, and in government policies and actions. This suggests that informal law in the form of religious norms are very well known.

This finding reflects a significant lesson from the historical background of traditional Indonesian culture, which was mainly influenced by religious norms and values as indicated in Chapter 4. Religious norms and values were an effective tool shaping people's behaviours and attitudes. However, increasing globalisation has seen them eroded by new foreign norms and concepts. They have been further undermined by Indonesian authoritarian and paternalistic style leadership.

7.4.2. Education

Some private participants consider that formal education was an effective way to develop knowledge and skills, social norms and values as well as ethics. One participant from a self regulatory organisation (SRO), a securities depository institution, considered the need for core school subjects that emphasised ethics in early stages in the curriculum. This was based on his personal experience of shaping ethics from the beginning of his education. This helped to develop ethical norms and values. It shapes a good character with strong integrity. It assists to build a culture of self-discipline. This would be a long process in building cultural identity.

7.4.3. Effective supervision and control in legal practice

Some respondents both from the public and the private sectors described corruption as a syndicated criminal organisation with powerful networks that are too difficult to break. They indicated a need for an effective monitoring system for addressing the corruption cycle. They recommended "*perlu adanya pengawasan yang berlapis-lapis*" [a monitoring

system that should be layered]. The monitoring needed to involve the public, civil society and the mass media.

The existing KPK was considered to be inadequate in addressing corruption and it has been influenced by political pressures. The KPK has also only tackled large corruption cases. The involvement of the public, civil society organisations was seen to reduce the political pressures on the monitoring system.

7.4.4. Conclusion

The findings suggest that religious norms and values, formal education in ethics and better and more effective controls are needed to support the use of a voluntary good corporate governance code.

The next chapter, as the last chapter, provides a conclusion to this research. It provides answers to the research questions drawing from the results of the triangulation of these findings with the two other sources, the literature reviewed and the media databases.

Chapter 8 : Conclusion

8.1. Introduction

The pressures of the 1997 financial crisis, in particular, and globalisation in general, forced Indonesia to create a better corporate governance, legal and regulatory framework, including the introduction of the Good Corporate Governance Code (GCG Code). It compelled the country to attempt to establish corporate accountability for transparency and disclosure as one essential pillar of corporate governance. The strong demand for effective disclosure was aimed at ensuring stability, rebuilding trust and restoring investors' confidence in the capital markets and the business sector. The 2007 global financial crisis, again, tested Indonesia's attempts to create better overall corporate governance and disclosure practices. It further adapted international standards and principles of disclosure, which derived from western practices and commercial values. It developed a corporate disclosure structure in its formal legal and regulations frameworks part of which are mandatory. The evidence, however, demonstrates an unsatisfactory level of disclosure compliance and the poor reliability of information disclosed.

The overarching research question posed was whether the GCG Code, as informal or soft law, can be used as an alternative regulatory instrument to enhance corporate accountability for effective disclosure in Indonesia? Alternative regulatory theories suggest that informal law is a significant instrument for establishing good corporate governance. The GCG Code, in this context, appears to be an apparently effective tool for fulfilling insufficiencies in the corporate governance system, including transparency and disclosure, with the weak capacity of Indonesia's formal legal system. Some East Asian jurisdictions have demonstrated that the use of voluntary corporate governance codes can improve corporate disclosure practices. However, Indonesia's complicated and complex economic, political and legal conditions raise a question of whether a similar code can work effectively within the Indonesian context. This issue had not been addressed in previous research on corporate law, regulation and governance in Indonesia.

In seeking to answer the above overarching question, the research also posed two sub-questions as indicated in Chapter 1. The first sub-question related to the type of

functions the GCG Code can serve and whether it has the potential to improve corporate disclosure and strengthen relevant formal law and regulations. The second sub-question related to aspects of Indonesian political, administrative and business cultures that can be called on to support the use of the GCG Code. Three general questions were also included to form the conceptual framework in answering these questions. They examine (1) the factors that influence the use of good corporate governance codes as effective informal regulatory instrument, (2) the factors that influence the effective use of formal and informal law as complementary regulatory instruments, and (3) the factors that influence the effective transplantation of informal law between donor and host legal systems.

This last question also led to the research examining the GCG Code and its disclosure provisions as products of legal transplantation that can be transferred into business and regulatory practices in Indonesia. In this context, the research also analyses the key problems in the legal system affecting corporate accountability for disclosure as well as the use of the GCG Code.

This chapter draws together the conclusion to these research questions from the outcomes of the triangulation of relevant literature and media data bases together with the empirical data presented in the previous chapter. It also addresses the implications and contributions of the research, as well as its limitations and suggestions for future research.

The conclusion shows considerable consistency between data from the interviews and the media data bases but some significant inconsistencies with parts of the literature reviewed. These differences are contributed to by some of the concepts in the GCG Code not fitting the nature or characteristics of informal law suggested by the alternative or informal regulatory theories.

8.2. Research background

The research employs triangulation of three separate sources of literature including provisions of Indonesian law, secondary scholarly journals and articles, and media data bases as well as empirical data from interviews to establish the answers to the research questions.

The research commences with the review of literature related to corporate governance and disclosure, new alternative regulatory theories and concepts of legal

transplants. This literature provides the context for the potentially significant role of the GCG Code as informal law or soft law and its provisions on disclosure. It provides the context for the adoption of the code and disclosure principles in Indonesia.

The research also reviews the use of voluntary good corporate governance codes in some comparable jurisdictions. The effective use of codes in these countries and in similar corporate systems based on the insider and banks systems of Japanese-German models provide examples of some factors that may enhance the effective use of such codes in Indonesia.

Part of the literature reviewed, particularly relating to informal or soft law, is examined for consistency with reports in the media databases and the empirical interview data to address the research question of whether the GCG Code can be used to enhance corporate accountability for effective disclosure in Indonesia.

The CGC Code promotes principles of good corporate governance in general and disclosure in particular, which are adapted from Western values and business practices. These concepts appear not to fit with the local culture of Indonesian and its political and social circumstances. The differences in culture, including legal and regulatory cultures, corporate governance and financial systems between Indonesia as a host country and donor countries contribute to the failure of the effectiveness of the GCG Code.

The research finds that the GCG Code does not function effectively in the Indonesian context. It also finds that as a form of soft law it does little to overcome the ineffectiveness of the formal legal system.

8.3. The research question

As indicated earlier, the overarching question in this research is whether the GCG Code can be used as an alternative regulatory instrument to create effective corporate accountability for disclosure in the Indonesian context?

Answering this question draws on the two following sub-questions:

1. What kind of functions can the GCG Code serve? Can these functions improve the effectiveness, efficiency and responsiveness of the regulation of corporate governance in Indonesia?

2. What aspects of Indonesian political, administrative and business cultures can be called on to support its use?

The conceptual framework used in answering these questions is formed by three other general questions:

1. What factors influence the use of corporate governance codes as effective informal regulatory instruments?
2. What factors influence the effective use of formal and informal law as complementary regulatory instruments?
3. What are the factors which influence the effective transplantation of informal law between donor and host legal systems?

The next sub-section below summarises the answer to these research questions. It commences with the responses to the three general questions followed by the answers to the two sub-questions leading to the answer to the overarching question.

8.3.1. The answer to the three general questions

As noted above, there are three general questions included to provide the conceptual framework to assist in answering the two research sub-questions. This sub-section commences with the responses to these general questions, based on the literature reviewed in Chapter 2. As indicated, these responses provide the background to assist in answering the two sub-questions, provided in the next sub-section [8.3.2] further below.

General question 1:

What factors influence the use of corporate governance codes as effective informal regulatory instruments?

Chapter [2.4] evaluates alternative regulatory theories. The review of the theories introduces new regulatory models which are characterized as informal or soft law frameworks, see [2.4.1]. In the conceptual framework, voluntary corporate governance codes are considered as informal regulatory instruments, see section [2.4.2].

Chapter [2.4.2.2] evaluates the role of these codes as informal regulation. A number of scholars observed that the codes are a form of alternative regulation and attribute to them many efficacies in business and its regulation. McConvill claimed, for example, that the

codes are more effective and efficient regulatory instruments than formal law. They benefit business and its regulation due to their flexibility, responsibility, relevancy and effectiveness as suggested by Curtis and Caral. Gunningham and Grabosky, with their smart regulation concept, and Braithwaite, with his idea of responsive regulation, make similar claims emphasizing their characteristics of flexibility and responsiveness. The codes also have some other significance attributed to them in better regulation of corporate governance because of their self-regulatory nature as claimed by Haxhi and Aguilera, enhancing transparency, as suggested by Rapp, Carver, Schmid and Wolff, and addressing corporate governance practices as noted by Bethoux et al, Milstein et al, Zattoni and Cuomo.

The significant functions of the codes as informal law, as described earlier, are the practical factors influencing their use. Among other significant factors, they can supplement the incompleteness of formal law and offer the flexibility and efficiency required in the regulation of business areas. Informal law also offers lower compliance costs compared to more formal approaches, see Chapter [2.4.2.2].

The effectiveness of informal law, such as these codes, is determined by compliance with it and the functions achieved by the codes. The relevant literature reviewed in Chapter [2.4.3] suggests that informal sanctions are a key factor in the effectiveness of informal law. Ottow claimed that sufficient enforcement mechanisms are required for the effectiveness of self regulation and informal law. Haines and Zerilli point out that the enforcement of informal law including voluntary codes, is through moral suasion.

The enforcement of informal law relies on the private or non-government sector constructing a framework of incentives and deterrents in an effective regulatory process. Parker and Braithwaite promote general informal sanctions such as negative publicity, public criticism, gossip, embarrassment and shame at the lower level of the regulatory pyramid. Millstein similarly suggested informal sanctions including through rating agencies, business institutions and media publicity as softer forms of enforcement. These informal sanctions are considered by Wymeersch as significant in their threat of damage to the reputation of, and to the loss of trust in, the company. This is considered as a sufficient deterrent since reputation and trust are crucial factors in doing business.

Chapter [2.4.4] considers trust as a critical issue in this context. Trust is extensively observed to be significant in business regulation. It is considered to create confidence in investors. This is because trust, as observed by Tomasic and Akinbami, assists investors to make decisions in buying shares or other securities, and in entering business relationships in an easy and inexpensive way. Williamson and Kerekes support the latter claim suggesting that trust reduces both monitoring and transaction costs. De Soya and Jutting further point to the significant role of trust in establishing norms in complex economies. It particularly contributes to social engagement with political and economic development.

General question 2:

What factors influence the effective use of formal and informal law as complimentary regulatory instruments?

Chapter [2.5] describes a number of features of the relationship between formal and informal law. The differences between them, see [2.5.2], suggests that they may supplement each other to achieve better regulation.

The use of formal and informal law as complementary instruments is claimed by a number of scholars to be potentially significant in addressing weaknesses in formal law, see [2.4.2] and [2.5.3]. Some certain negative features of formal law, including its weak enforcement, as observed by Berglof and Claessens, predatory government, as indicated by Williamson, its limited capacity, as observed by Braithwaite, distrust in it as it becomes a dead letter, as suggested by Aldashev et al and the incompleteness of formal institutions because of their lack of credibility, as claimed by Helmke and Levitsky, promote the use of informal law in filling these gaps, as suggested by Sindzingir and Wymeersch.

Chapter [2.5.3] evaluates the efficacies of the mixture of formal and informal law. A number of scholars claimed that the combination of formal and informal law is the most effective and efficient regulatory strategy to create better regulation because they complement each other. Parkinson suggests the combination of private regulatory mechanisms with some elements of state processes. Black observes that this mixture can create the right balance of discretion between the two competing models of rationality, between certainty and flexibility and uniformity and individual action. Parker and Braithwaite consider that this combination can be an effective tool for enforcement as

formal law interpreted by informal law and informal law backed by formal law. Bergloff and Claessens also claimed that effective enforcement requires both public forms and private instruments. They suggest that private enforcement works more effectively with the support of formal law enforcement.

General question 3:

What are the factors, which influence the effective transplantation of informal law between donor and host legal systems?

Chapter [2.6.4] evaluates factors influencing the successful transplantation of informal law to donor legal systems. A number of scholars observe that some non-legal factors determine the success of legal transplants. The adjustment and adaptation of the law to local situations, the familiarity of lawyers and others with the basic principles of the transplanted law, legal culture and tradition are among the significant factors. Other factors that also count, according to Peter and Schwenke, including historical, social, economic, political and psychological contexts, as well as accounting, and technological contexts as suggested by Valderama.

Cranston observed the significant need to adjust the adopted informal law, such codes or standards, to the new local conditions. The adaptation of transplanted law to local legal traditions and institutions and social and economic conditions of the host systems are also considered by Walsh to determine the success of transplants. Berkowitz et al also points this out as well, as there is a need for local lawyers and others to be familiar with the transplanted principles to make their implementation more effective, see [2.6.4.2].

Legal culture is also observed by some scholars as significant in determining the outcome of legal transplants. Friedman highlighted that legal culture determines how law is used, avoided, or abused as it is a form of social thought and social force. This relates to legal culture, as described by Blankenburg, as a complex interrelation on four levels including the level of values, beliefs and attitudes towards law, the pattern of behaviour, the institutional features, and the body of substantive and procedural law. Kahn Freund and Watson observed that legal and regulatory cultures influence the level of adoption and adaptation of legal transplants.

In particular for developing countries, Bedner emphasized the integrity of formal law and associated institutions such as the courts and legal professions as significant factors rather than more general social and cultural issues.

8.3.2. The answers to the sub-questions

Sub-question 1:

- a) **What kind of functions can the Code serve?**
- b) **Can these functions improve the effectiveness, efficiency and responsiveness of the regulation of corporate governance in Indonesia?**

This first sub-question contains two inter-related questions as indicated above which will be discussed below separately. The theoretical framework to assist in answering these sub-questions is from the responses to the three general questions, as noted in sub-section [8.3.1.].

Sub-question 1 (a): What kind of functions can the Code serve?

As indicated earlier, the responses to the general questions 1 and 2 above provide the conceptual framework for considering the role of the GCG Code as informal law. It has mainly been observed as a form of alternative regulation with claims that it is an effective and efficient regulatory instrument.

The triangulation matrix below represents the integration of data from the three separate sources used, to consider whether they corroborate each other. It aims to establish an overview of whether the GCG Code can serve the functions as claimed by the alternative regulatory theories given in the answer to general questions 1 and 2.

Table 8.1: Triangulation matrix of the functions of the GCG Code

Literature reviewed	Media data	Empirical data
Codes as alternative regulatory instruments as an efficient, effective and responsive tool for better regulation.	Media reports revealed GCG Code as good corporate governance guidelines [<i>pedoman</i>]. It has not been used as any form of regulatory instruments. It is just <i>pedoman</i> [guidelines].	Most interviewees saw GCG Code as only a reference resource or advisory instrument but not to be used.

The matrix shows the inconsistency between the literature and the data obtained from Indonesian resources. The functions of the 2006 GCG Code, as a representative type

of informal law in this study, indicate inconsistencies with a number of alternative regulatory theories. The GCG Code does very little as an efficient, effective and responsive tool leading to better corporate disclosure.

The function of the GCG Code in Indonesia is regarded as only a source of reference. Its functions are seen as visionary, idealistic, or aspirational. Because of the pressure to build trust in foreign investors, disclosure was made mandatory under formal law as indicated in Chapter 6. The study indicates that the mandatory disclosure incorporated in the formal law and regulations is a form of window dressing for attracting these investors. The mandatory disclosure overshadows the functions of the GCG Code.

Indonesia's complicated economic, political and social condition is a significant test for the effectiveness of implementing any informal regulatory strategies in developing countries. The answer to the next sub-question 1(b) below will provide an outcome of whether the strategies are able to work effectively under Indonesia's conditions.

Sub-question 1(b):

Can these functions improve the effectiveness, efficiency and responsiveness of the regulation of corporate governance in Indonesia?

The responses to the general conceptual framework questions 1 and 2 above, suggests that codes as informal regulatory instruments are considered to be more effective, efficient and responsive regulation than formal law. And that they appear to have potential capacities to contribute to improving the effectiveness, efficiency and responsiveness of formal corporate governance regulation.

The background to the overall legal and regulatory literature to this question is given in Chapter 2.4. It contains claims made by Curtis and Caral, Parker and Braithwaite, McConvil, Parkinson, Bergloff and Claessens, De Soysa and Jutting that voluntary codes and other forms of informal regulation may improve effectiveness, Braithwaite, Williamson and Kerekes, Helmke and Levitsky, and Parkinson suggest that they may improve efficiency, and Braithwaite, Gunningham and Grabosky suggest that they may lead to a responsiveness not able to be achieved by formal law.

The issues relating to this question of alternative regulatory instruments are discussed primarily in Chapter 2: the literature review. Chapter 2, at [2.4] describes

alternative regulatory theories and evaluates the literature on corporate governance codes as an informal regulatory concept with the GCG Code as an example. The literature reviewed suggests that the use of informal law, such as the GCG Code, can improve the performance of formal law including corporate governance regulation. Such codes, as voluntary instruments, may provide flexibility, adaptability, and internal compliance mechanisms that allow experimentations and innovations, which are more difficult with in formal legal and regulatory systems.

The next section, [2.5] discusses the concepts relating to the relationships between formal and informal law. The research evaluates the claims that the mixture of formal and informal law may supplement each other to achieve better regulation. From this literature, for Indonesia, it appears that the GCG Code may be used as an effective alternative strategy to address the weak capacity of its formal legal system because of its lack of credibility. The GCG Code appears to have the potential to fill the gap left by the ineffectiveness of formal corporate governance regulations. It may circumvent problems in the formal legal system, complement, or substitute for the formal law on paper, which is not enforced and also accommodate the need for a change in formal rules.

The research examines the efficacies of the use of the GCG Code as informal law in general and, in particular, for Indonesia as a developing country with weak capacity in its formal legal and regulatory systems.

Some of the relevant literature, as noted in Chapter [2.4], suggests that voluntary corporate governance codes are a type of Gunningham's and Grabosky's smart regulation, or Braithwaite's responsive regulation, or Black's and Ogus's decentred regulation. Smart regulation is meant to be responsive to specific contexts and employs a wide range of policies, mechanisms and regulatory actors. This appeared to be significant in addressing contemporary and complex business issues. Responsive and decentred regulation are claimed to promote the reduction of the use of formal law in favour of self-enforcing principles. It encourages the diffusion of regulation and leaves private individuals and groups to exercise power and control. These can be cheaper and more effective strategies to mobilize social control than the command and control style of regulation by the state through formal law.

The characteristics of flexibility and responsiveness of voluntary codes as informal law are claimed to benefit business, and, ultimately, create better formal corporate governance rules.

The triangulation matrix below examines the degree of consistency between the various data sources. It aims to answer sub-question 1(b) whether the GCG Code serves the function to improve the effectiveness, efficiency and responsiveness of Indonesian corporate governance regulations.

Table 8.2: Triangulation matrix of the effectiveness, efficiency and responsiveness of the GCG Code to improve corporate governance regulation

Literature reviewed	Media data	Empirical data
A code as an alternative regulatory instrument can be used as an efficient, effective and responsive tool for better regulation.	A number of blue chip listed companies introduced their own GCG Codes. The 2014 Good Corporate Governance Roadmap and the 2015 Corporate Governance Guidelines for Public Companies introduced by Indonesia Financial Services Authority (OJK) has overshadowed the 2006 GCG Code introduced by the KNKG. The GCG Code has been little used due to it not being mandatory and not being included in any formal statutory provisions. But some similar principles or rules have been introduced in formal law and its related regulatory system.	Most interviewees noted the absence of the effectiveness, efficiency and responsiveness in the GCG Code and its failure to improve compliance relevant with corporate governance disclosure regulations. (Interview schedule III.17-20).

From the matrix it can be seen that there are inconsistencies between the literature and the media and the empirical data. The latter data sources indicate that the GCG Code has not been used as an alternative regulatory tool in Indonesia.

There is little evidence to support claims that the GCG Code functions to improve the effectiveness, efficiency and responsiveness of Indonesian corporate governance regulations. As indicated earlier, the GCG Code is used only as a reference and does little

to fulfil any informal regulatory strategic roles. There are several factors contributing to this as described below.

(a) The limited features of the GCG Code as an informal regulatory concept

The GCG Code struggles to meet the criteria for informal or soft law. The GCG Code does not demonstrate a number of the significant features of informal law indicated in Chapter [2.4] including self-enforcement, informal sanctions, responsiveness (including utilization by private groups as responses to the limited capacity of formal law), smart regulation (as in utilizing a wide range policies and regulatory actors), or decentred regulation (as in individuals enforcing their rights rather than the state enforcing the law).

The study demonstrates that the GCG Code is not self-enforcing. Unlike a number of other jurisdictions indicated in Chapter [3.5]–[3.6], the GCG Code is not incorporated into capital market listing rules. While similar corporate governance provisions are found in a number of laws and regulations, as well as the listing rules as indicated in Chapter [6.3], they do not represent the use of the GCG Code.

The study also shows that the absence of incentives and deterrence with informal rewards and sanctions in the GCG Code suggests that it lacks alternative regulatory characteristics. Braithwaite's model of alternative regulation, using pyramidal escalation of networked branching, see [2.4.2.2]–[2.4.3], has been suggested as a more effective form of regulation for developing countries like Indonesia. Persuasion is observed to be a less expensive approach to implement good regulations than deterrents or punishments. Private and government regulators may then intervene with escalating helpful, and then punitive, measures when the earlier persuasion fails.

A formal regulatory process is ultimately required in this pyramid to back up the informal process. The voluntary code permits the giving of informal advice or assistance and provides a benchmark that could be used for negative publicity, public criticism, embarrassment, or adverse comments by rating agencies. It also requires the active involvement of NGOs, associations, corporations and international organizations. It, however, also requires warnings followed by administrative sanctions by formal regulatory bodies under formal law to make it work. These characteristics are not found in relation to the GCG Code.

There is little evidence that there are informal enforcement or compliance mechanisms for the GCG Code. The GCG Code lacks the enforcement mechanism of informal law, such as market forces assessment suggested by Ottow, at [2.5.3], or as a monitoring instrument, as suggested by Wymeersch and Goldsmith, at [2.4.3]. The absence of these characteristic traits detracts from the functions of the GCG Code as informal regulation.

The GCG Code has not been used in a strategy to potentially lead corporations to improve good corporate governance practices. There is no evidence indicating that the government has reduced the use of, or resort to, formal law in this area. The evidence indicates that the state continues to have a monopoly on the exercise of power and control unlike, for example, in Black's concept of decentred regulation, [2.4.2.2], which suggests a diffusion of regulation and power controlled outside the state's structures. The study indicates that Indonesia continues to provide for corporate governance disclosure in a formal legal and regulatory way rather than by any informal approaches. The culture of the civil law system, that the state is the source of law and regulation, appears to be deeply rooted in lawyers', regulators', and legal scholar's mentalities as indicated by Bedner in Chapter [5.4.5].

There is also no evidence that the GCG Code, as a voluntary instrument, has been combined with command and control regulation as suggested by Gunningham's and Grabosky's smart regulation, Black, Parker and Braitwaite as indicated in [2.4.2.2]. The GCG Code is missing the comply and explain provision which appears to facilitate the use of the code in other like jurisdictions, as observed by Gersen and Posner at [2.4.1], or as a common practice in a number of other jurisdictions as indicated in Chapter [3.5]–[3.6].

The GCG Code also lacks some of the attributes of informal laws, as suggested by some scholars in Chapter [2.5.2]. North's and Pejovich's concepts of informal law described it as a form that has evolved over time with self-enforcing propositions. De Soya's and Jutting's concept of informal institutions are underlined by the social culture that shapes human behaviour. The GCG Code does not take a self-enforcing form that is grounded in Indonesian culture. It represents adopted foreign concepts introduced to address the problems of economic crises under the pressure of the forces of globalisation.

The habits and feelings of pragmatic obligation found in the successful use of informal rules discussed at [2.5.2] do not exist.

(b) The formal legal culture limits regulatory strategies

Whether the GCG Code is recognisable as formal or informal law or not, it does not appear to work effectively in the Indonesian context. The underlying problem is the formal legal and regulatory culture rather than other legal and regulatory strategies. These legal strategies appear to work where a stronger formal legal culture exists and it is supported with other sources and factors. These factors include a strong anti-corruption ethos and a political commitment to it, as indicated by experiences of other South East countries described at [3.5.1]. Changing people's consciousness around respect for laws and regulations and the need for a more ethical legal culture are fundamental issues needing to be addressed in the Indonesian context. These factors influence the use of corporate governance codes as effective formal or informal regulatory instruments.

The legal and regulatory cultures also inhibit the use of informal mechanisms. As the historical and cultural analysis revealed, [4.2.2]–[4.3.3], this is a critical aspect of the inherited and long established legal system. The legacies of colonisation and the New Order have privileged the use of formal or black letter law in regulatory regimes. The pattern is towards more formal rather than informal regulation. There is a strong consensus that black letter law is the solution to all problems including regulatory ones even in the business and corporate context. It is difficult for informal law or soft law to compete in this environment. The lack of support for the use of informal approaches influences people's attitudes and behaviour.

(c) Loss of trust in the legal system

The loss of trust in the legal system also inhibits the legitimacy of both formal and informal law. Regulatory mechanisms do not work. The research finds that the absence of trust is a critical issue for developing countries with weak judicial systems like Indonesia. This is consistent with the literature reviewed, see [2.4.4]. Trust, as noted by Tomasic and Akinbami, Williamson and Kerekes, Sindzingre and Millstein et al, has a number of advantages in reducing transaction and monitoring costs, and promotes quick and efficient outcomes, informal alignments, and resulting economic development and growth.

(d) The failure of legal transplants

Legal transplant theories, as reviewed in [2.6.1]–[2.6.4], also have explanatory powers for this inconsistency between the literature on informal or soft law and what has been observed. Chapter 3 and 5 evaluates the GCG Code and its principles, which represent values of transparency and honesty also found in Indonesian society. In the context of the GCG Code, they are derived from foreign ideas, which appear to be incompatible with Indonesia's present context. Chapter [2.6] provides an explanation for the adoption of foreign concepts in the legal transplant theories of Cranston, Walsh, Kahn Freund, Peter and Schwenke, Friedman, Berkowitz et al, and Bedner, see [2.6.4.2] in particular. As Cranston indicates non-legal factors are important in any successful transplant and any transplant may need significant adjustment to the local situation. Watson and Legrand draw attention to the need to adapt borrowed concepts to the social and economic realities of the host country. There is a convergence of opinion amongst these writers. Watson, Kahn Freund and Teubner also point to the need for elite groups in a society to be pressure groups supporting the adoption of transplants and their implementation. Without this support transplants will struggle to succeed. This is confirmed in the Indonesian context in the absence of clear support for the GCG Code by the business, political, regulatory and legal elites. This can be seen in the limited outcome of the NGOs' efforts in raising awareness, promoting and disseminating the principles of the GCG Code, see Chapter [7.2.3]

The success of legal transplants is determined by non-legal factors, such as legal traditions and institutions and the social and economic realities of the recipient system. The non-adaptation of the Code as a foreign model to the Indonesian legal tradition and its institutions, politics, social and economic conditions are the influencing factors in the failure in the GCG Code as a successful informal legal transplant.

Recommendations

The study identifies the efficacies of the alternative regulatory concepts that Indonesia may consider to adopt in order to address weak capacity in its formal legal system. This includes the possible use of the GCG Code to fill the gaps, or complement the existing formal corporate governance laws and rules in general and disclosure in particular.

The GCG Code needs to be provided with more effective enforcement mechanisms, involve more private sector actors in regulatory processes and make adjustments to draw on support from local cultural values. Dilling, for example, at [2.6.3], considers the greater capacity of the private sector, rather than the state, in employing global standards at a national level.

The study also identifies fundamental issues requiring redress to improve the overall effectiveness of Indonesia's regulatory systems. A change in legal and business cultures and an increase in the integrity of formal law and associated institutions including the courts and the legal profession are priorities for any reform. Indonesia can draw lessons from other comparable jurisdictions, see [3.5]–[3.6], to address its corrupt and fragile political institutions. The study reveals that a strong political commitment to an anti-corruption ethos in Singapore and integrated legal reforms involving public and private sectors in Thailand have both led to a successful implementation of better corporate governance through the use of recent relevant codes.

The study also identifies the need for greater education of Indonesian legal, regulatory and enforcement professionals around the inflexibility deeply rooted in their adherence to civil law mentalities. Thailand is an example of a civil law jurisdiction that has been able to accommodate a more flexible approach to informal law such as good corporate governance codes improving its progress in corporate governance performance, see Chapter [3.5].

Sub-question 2:

What aspects of Indonesian political, administrative and business cultures can be called on to support the Code use?

The issues relating to this question are discussed primarily in Chapter 2, see [2.6.4], and under comparative law and legal transplants, [2.6], and in Chapter 4 The historical development of social and cultural values around business transparency in Indonesia, see [4.2]–[4.3].

The study notes that the concept of the corporation and the capital market as well as good corporate governance and its principles in the Indonesia context are all forms of legal transplants. Chapter 2, at [2.6.4], evaluates the factors that influence the successful

transplantation of informal law to recipient legal systems, which have been discussed in the context of the previous sub-question. The study shows that the similarities or differences in social and political values and processes between donor and host countries influence whether legal transplants are accepted or resisted.

With respect to the transposition of informal law or alternative regulatory strategies into the Indonesian regulatory system, the research explores Indonesia's regulatory culture and whether Indonesian regulatory processes can adapt to fit with transplants where the donor is influenced by Western legal, regulatory and business cultures. The research demonstrates that, as with the formal law, which has been borrowed by Indonesia under colonisation and after independence, the informal law represented by GCG Code and its international principles of corporate governance disclosure represent western concepts and practices. They are also shown to be rejected due to the differences in culture and mentalities between the donor countries and Indonesia as the host country. This may reflect the observations in comparative law literature that it is difficult to change the mentalities of the actors in the system to which the transplant is transferred. Culture is a significant threat to the successful transposition of foreign concepts.

Friedman claims that a strong legal culture is crucial for an effective legal system. It determines how law is to be used, avoided, or abused. Watson also observes that the legal culture defines the nature of law and its place in society. This is consistent with the Indonesian context where weak legal culture inhibits the effective use of formal law and the GCG Code as informal law.

In Chapter 4, the research evaluates the relevant social and cultural values in Indonesian cultural traditions until the present reformation era. It examines the values of honesty and transparency in social, commercial and political activities.

The study finds that Indonesians are familiar with religious values and ethical precepts that promote honesty and transparency. The arrival of foreign traders and the pressure of colonisation brought foreign values and concepts that changed and reshaped indigenous values and cultures. Indigenous Indonesian society had generalised its own form of clientism. The paternalistic legacy of Dutch colonisation, as indicated in Chapter [4.2.2.2], and the large social distance characterized by hierarchal and large power

distances in business relationships, as indicated in Chapter [5.3.2], had evolved in Indonesian culture. Japanese structures and policies during the occupation added to existing corrupt practices. The suppression of popular opinions and protests under the Dutch, the Japanese and Soeharto affected traditional values and precepts.

Post independence, the prolonged new order era under Soeharto appears to have significantly contributed to the decrease of integrity through corruption, collusion and nepotism (KKN). The paternalism inherited from local cultures and colonisation continued under Soeharto to form a leadership model called *Bapakisme*¹⁵⁵³ [loyalty to a hierarchal structure] and patronage relationship. It is focused on achieving personal wealth and on Soeharto's family's interests as institutional and cultural goals, which undermined legal, regulatory and administrative systems.

The study finds that the local traditions, Dutch colonisation, the Japanese military occupation and the first two presidencies left a legacy that is difficult to cure. KKN endured in all periods after the independence of Indonesia into the present reformation era. Corruption is a fundamental problem affecting almost all social, economic and political practices, see Chapter [4.3] and [7.2].

As globalisation quickens it becomes inevitable that Indonesia will adopt further foreign ideas and concepts along with their values and culture. Those values and concepts will have evolved in the context of specific economic and business beliefs and practices. This is seen in the foreign ideas adopted by Indonesia in the GCG Code as indicated in Chapter [3.2]–[3.3], which discusses the stimulus of the forces of globalization and internationalization on trends in corporate governance and the impact of economic crises on the demand for good corporate governance practices and Chapter [5.4], which observes the transposition of international disclosure principles to an Indonesian context. However, their underlying values and practices have not been accepted in Indonesian business, regulation and law.

The triangulation matrix below presents the three separate data sources used to corroborate each other. It aims to answer sub-question 2 on the aspects of Indonesian

¹⁵⁵³ *Bapak* means father.

political, administrative and business cultures that may be called on to promote the use of the GCG Code in Indonesia.

Table 8.3: Triangulation matrix of factors affecting the use of the GCG Code

Literature reviewed	Media data	Empirical data
As an alternative regulatory instrument, codes require the right balance of discretion; effective informal sanctions and deterrence; and, trust.	Exposure of corruption; potential for shaming in the media has been undermined by the media’s promotion of public images for personal and political gain rather than as an informal sanction	Absence of discretion; limited effectiveness of informal sanctions; loss of trust. (Interview schedule III.21-30)
----- As a legal transplant the concepts need adaption to local cultural, historical, social, political conditions, and legal traditions as well as to legal culture.	----- Legacies of previous cultural and political states; and the poor mentality of officials, policy and law makers.	----- Clash of cultural dimensions between host and donor countries; limited space for informal rules in formal legal tradition; poor mentality of officials, and poor legal culture. (Interview schedule III.24-25)

From the matrix it can be seen that there are some significant issues contributing to the failure to use the GCG Code effectively. It indicates the need to address these issues in order to potentially support the more effective use of the GCG Code.

The empirical evidence shows the effective use of informal norms and values by Indonesians in the past. Chapter 4 also provide evidence that Indonesians have welcomed and valued foreign values and norms. The religious norms and values brought by foreign traders in earlier trade activities and by subsequent missionaries reflect this.

The study finds that the use of religious norms and ethical values appears to have worked effectively for Indonesians. They rule many aspects of Indonesians’ day to day life. They have had fundamental impacts on their cultural, social, economic and political life. This reflects the prevailing existence of belief, faith or trust in various religions. The power of the state, NGOs and other informal institutions has also been important. The first principle of the five philosophical foundations underlying *Pancasila*, is *Ketuhanan Yang Maha Esa* [Belief in the one and only God]. Each Indonesian is required to practice one of

six official religions (Islam, Protestantism, Catholicism, Buddhism, Hinduism or, Confucianism) listed on their citizen identity card. Indonesians are expected to practice their respective religious beliefs or face some social disapproval.

Other evidence is seen in the form of informal mechanisms in the mass media and, more recently, in the social media that has increasingly been used in Indonesia. However, reputation as image [*pencitraan*] in the mass media has been manipulated to gain political benefits. Both companies and public relevant agencies also utilize the mass media to establish a positive image for a listed company regardless of their compliance with disclosure or other good corporate governance requirements. The mass media is also used to promote good corporate governance awards and ratings. These informal mechanisms tend to be used effectively to build a positive self-image rather than as an informal sanction under which adverse publicity shames the individual or the company. There is also evidence of the increasing use of social media as informal sanctions in the form of shaming or embarrassing. This appears to work more on the level of the individual's reputation or image, see [7.2.2].

Chapter [2.4.3] evaluates the importance of informal sanctions in alternative regulatory theories. The study finds that informal sanctions are more effective as deterrents than formal ones. The damage to a company's reputation and the loss of trust in management can be effective in promoting reputation and trust as crucial aspects of business.

The further development of the effectiveness of the GCG Code requires several non-legal factors to be addressed including a more disciplined legal and business culture, political will, and the cultivation of an anticorruption mentality. The legal profession is also included in this. Changes in legal culture are also important. These changes would potentially support the use of the Code as a complimentary regulatory instrument.

In respect to changes in legal culture, as indicated earlier, any legal strategies would not be effective unless they promote confidence in the impartiality and professionalism of the legal system and a strong legal culture. The level of corruption is so extensive that it has contributed to the failure of the general legal system.

This reflects Milhaupt's and Pistor's idea of a rolling relationship between the law and the economy as indicated in Chapter [2.2.4] in which, in the context of this study, extends to the relationship between formal and informal law. The claims in alternative regulatory theories of the significant functions of informal law, and a combination of informal and formal law, as indicated in the earlier answers to the first general research question, as well as in Chapter [2.4], cannot be generalized across countries with different legal and business cultures, political conditions, and legal traditions. The poor condition of formal law in Indonesia contributes to making the GCG Code, as informal law, less effective. Indonesia is losing the opportunities to gain benefits attributed to informal law as observed in Chapter [2.4.2.2].

Chapter [2.4.4] evaluates one of the claims in alternative regulatory theory that trust is a critical aspect of business regulation. Trust, it is suggested, makes any regulations and regulatory strategies more effective. It has influential impacts on people's attitudes and mentalities. Chapter [4.3], Chapter [5.2.2]–[5.2.5] and Chapter [7.2.]–[7.3] provide evidence that the pervasive culture of corruption is a significant threat to the use of any informal law including the GCG Code.

The study considers Braithwaite's claim that corruption erodes the good will required to comply and promotes the rational calculation of how to cheat. Indonesian companies may also not have practical knowledge and skills to take on responsibilities to comply with the GCG Code due to the absence of the competence and capability of management to comply, see Chapter [5.2.2].

Recommendations

The study identifies significant factors required to be addressed to support the use of the GCG Code. It will require integrity, political will and administrative reforms to accommodate and facilitate informal regulatory regimes as a supplement to the formal legal system. Aspects of the GCG Code may be included in formal law, including the listing rules of capital markets, but it may not maintain its flexibility, adaptability, and responsiveness reflecting its origin in concepts of smart regulation, responsive regulation, and decentred regulation that can be found in the literature reviewed in Chapter [2.4.2.2].

The GCG Code's discretionary and self-enforcement powers need to be promoted and facilitated to achieve these.

The study in Chapter 3 finds that many other jurisdictions demonstrate an effective application of similar codes from which Indonesia can learn. For instance, comparable countries such as Singapore, Malaysia, and Thailand demonstrate the use of a mixture of formal and informal mechanisms. They incorporate voluntary codes into the listing rules and have revised their codes periodically to reflect their adaptable and responsive capacities. The Singapore experience demonstrates that the more effective use of the code requires support from other factors including an effective legal system, an appropriate business culture and strong public and private opposition to corruption. Malaysia uses its code as a form of self regulation on the basis that this is a preferable and acceptable approach. Thailand utilizes a voluntary code with integrated efforts by both the public and private sectors. It has been able to achieve a significant improvement in corporate governance performance, see Chapter [3.5]. Thailand also demonstrates the significant role of corporate governance related NGOs in contributing to this achievement.

8.3.1. Can the voluntary Good Corporate Governance Code be used as an alternative regulatory instrument to create effective corporate accountability for disclosure in the Indonesian context?

This is the overarching research question. The answer to this question is built on the two sub-questions and the three general questions used to construct the conceptual framework as indicated earlier.

The background in the literature to this question is given in Chapter 2 and 3. It contains claims made by the proponents of alternative regulatory theories, which justify good corporate governance codes as alternative regulatory instruments.

The issues relating to this question are discussed primarily in Chapter 2: Literature Reviewed on alternative regulatory theories.

Chapter 2, at [2.4] evaluates good corporate governance codes as an alternative regulatory strategy. The focus is on whether the regulatory discourse of alternative regulatory concepts can be translated into Indonesian business discourse, the importance of informal sanctions and trust as a critical aspect of business regulation. The study finds that

a good corporate governance code can be used as an alternative regulatory instrument to substitute for, or supplement, the existing formal corporate law and corporate governance regulation. Notwithstanding, evidence from Indonesia's context as provided in the answer from sub-question 1, as indicated earlier, the GCG Code has not been used as an alternative regulatory instrument and does little to supplement the existing relevant formal law and regulation as claimed.

The combination of formal law and a voluntary code, as informal law, are claimed to be more effective than either alone as they complement each other. Parker and Braithwaite claim that non-binding rules assist in interpreting and applying binding rules and binding rules back up non-binding rules. Black believes that the right balance of discretion can be achieved between the two competing natures of formal and informal law by combining them. Braithwaite, in particular, promote a pyramidal regulatory escalation response passing from informal to formal law through informal assistance and sanctions to formal sanctions. This is observed to be appropriate, particularly in the Indonesia context given the limited capacity of its formal legal system. Evidence referred to in the answer to sub-question 1 and 2 as indicated earlier, indicated that in the Indonesian context the claim is not supported. It is consistent with the concept used by Milhaupt and Pistor, as indicated earlier in the answer of sub-question 2, of the existence of the rolling relationship between formal and informal law. Evidence from Indonesia suggests that when both legal and non-legal factors are very weak it is very difficult to achieve the expected outcome from the efficacies of the mixture of formal and informal law as claimed by some scholars as indicated earlier. Indonesia's complex condition with its very weak and corrupt formal legal system has led to a loss of trust in it as well as very poor legal and business cultures. There is a clash of cultural dimensions between host and donor countries with respect to transplanted concepts. There are less effective informal sanctions as noted in the answer of sub-question 2. These serve to cripple any kind of legal strategy.

Chapter 3: The demands of corporate governance and the use of corporate governance codes in different jurisdictions also raises issues relevant to this overarching question. Section 3.5, as noted earlier, evaluates the use of corporate governance codes in South East Asian and East Asian countries. The research selected some comparable

countries with similarities to Indonesia including a high concentration of, and controlled ownership structure, family dominance, strong state control, authoritarian political institutions, corporate governance, and regulatory environments. The study finds, as noted above, that some countries demonstrate the successful use of informal codes as the alternative regulatory tool in improving corporate governance in general and disclosure in particular.

Singapore and Malaysia may also be successful in their use of voluntary codes as informal law because they are common law systems. Thailand, a civil law jurisdiction, has been influenced by common law and corporate governance systems adopted from Anglo-American models. Chapter [3.6] evaluates the effective use of informal or soft law in both common law and civil jurisdictions. It concludes that common law jurisdictions are more likely to successfully accommodate informal law than civil law ones. In the absence of strong evidence to justify this claim, the study considers whether the legal system significantly affects the effective use of informal law, such as the GCG Code, as an issue needing to be further investigated.

From the answers to two sub-questions, noted above, the research concludes that Indonesia's voluntary good corporate code (GCG Code) does not work effectively as an alternative regulatory instrument to create effective corporate accountability for disclosure. It indicates the continuing poor adherence to disclosure processes and the poor reliability of disclosure performance despite the existence of the GCG Code. Corporate disclosure is widely regarded as window dressing to attract foreign investors.

The role and effectiveness of the Indonesian GCG Code is inconsistent with claims made about such codes in alternative regulatory theories. Its present use does not support the justifications for alternative regulatory frameworks suggested by the theoretical literature. All of the positive factors claimed and attributed to the code, as an example of informal law, are weak. This can be seen in the Chapter [2.4.2.2], which examines corporate governance codes as an informal regulatory concept. The study finds that the Indonesian GCG Code does not meet the classification as informal law or the claim made by Braithwaite, Black, and Ogus, and also Gunningham and Grabosky that voluntary codes represent responsive regulation, decentred regulation, or smart regulation. The GCG Code

fails to demonstrate the claims made for informal law as more flexible, relevant, effective and responsive. These include the failure of the GCG Code to be seen or understood in Indonesia as having the capacity to be an alternative regulatory instrument, a tool to assist companies in dealing with specific issues, filling insufficiencies in the corporate governance system and improving compliance with legal and regulatory requirements. Its perceived relevance is decreasing, as shown by the GCG Code not having been revised since 2006, unlike other jurisdictions such as Singapore and Malaysia which revised their Codes in 2012.

In particular the GCG Code is not effective in its use as an alternative or complimentary regulatory instrument for greater accountability for disclosure in Indonesia. As noted above, both formal and informal law are so weak that they incapacitate the functions of the GCG Code.

Legal culture and language also impact in the GCG Code effectiveness. *Pedoman* [guidelines], translated as a ‘code’, is also likely to be misunderstood because of the use of ‘code’ as the name for the comprehensive statement of legislative law found in the formal Indonesian legal system.

The voluntary nature of the Code underlines the call for the realignment of the relationship and balance of the discretion between formal and informal law as found in the literature reviewed in Chapter [2.5].

Chapter 1, 3, 4, 5 and 7 identify the challenges in eradicating corruption and changing political, economic ideologies, legislative and judicial as well as legal and business cultures, which can play a key role in decisions to accommodate the GCG Code as an informal rule or alternative regulatory approach in Indonesian formal law to make a better, more effective, efficient and responsive legal regime.

Empirical evidence as presented in Chapter [7.4] suggests that integrity, especially the mentality around the ethical and moral culture in respecting law, is a fundamental factor in promoting the use of informal codes. This supports Bedner’s claim, noted in Chapter [2.6.4.2], that social and cultural issues including the integrity of formal law and its associated institutions, such as the courts and the legal professions, are the main factors

required to be addressed in ensuring that legal transplants, such as informal codes, are successful in developing countries like Indonesia.

Recommendations

The outcome of this study identifies corruption as a fundamental factor affecting both formal and informal law. Both the formal and informal regulatory systems appear to fail to function because of it. Any strategies for reform will still not succeed if there are no changes in people mentality around corruption or a change in ethical and moral cultures around integrity particularly in business, politics and law.

This suggests that Indonesia's priority needs to be the reduction in the level of corruption.

8.4. The implications of the research and research contribution

8.4.1. The implications

The evidence of the failure of the effective use of the GCG Code as informal law makes it difficult to take advantages of any potential efficacies of the Code's functions as noted above. It fails in its use as an alternative legal or regulatory strategy. There is little evidence that supports the positive interaction between formal law and regulations and corporate governance in Indonesian listed companies. There is also little evidence to identify the strengths of the use of the GCG Code in achieving accountability for disclosure. Therefore, the GCG Code appears to have no impact on regulation or on accountability for disclosure.

The conclusions to the study are that the GCG Code functions largely as window dressing. It fails to serve any practical function as it is a cosmetic transplant not supported by local elites. It was initially adopted to satisfy international organisations such as the IMF, the ADB and other international institutions and to attract foreign investors by building their confidence. This supports arguments that the GCG Code was introduced just to fulfil the IMF's requirements. This may make it harmful to good governance and disclosure by creating superficial or misleading appearances in order to attract favourable foreign and domestic investments.

8.4.2. Research contributions

8.4.2.1. Academic contribution

This study provides an example of the correlation between formal law and informal law in a complex social, cultural, legal and regulatory system. The case of Indonesia displays the loss of synergies between formal law and informal law represented by the GCG Code through problems with the Code itself, weak formal legal and regulatory system and culture, the absence of integrity and people's attitudes and mentalities. It provides an understanding of why the potential capacity of alternative regulatory model of the Code fails. It is relevant to Haines' proposition that compliance is a crucial problem in alternative regulation or informal law as moral suasion is the basis of its enforcement. The Indonesian context provides evidence to support this conclusion and the reasons for it. In the case of Indonesia and the GCG Code, moral suasion has failed as an enforcement tool for informal law. The power of moral suasion is based on ethics and integrity and the absence of integrity strips moral suasion of its power. The general perception is that Indonesian legal and political regimes are dilapidated due to the loss of interest of citizens and the business community in particular in being involved in the processes of improving the legal and regulatory frameworks of the country.

The concept of the corporate governance code as an informal regulatory instrument, examined in Chapter 2, indicates the significance of the historical and cultural factors in the process of evolution of the GCG Code, as well as the level of trust of the legal system.

The study provides further knowledge and testing of the theories regarding the capacity of alternative regulatory models, such as GCG Code, for Indonesian regulators and policy makers, to benefit Indonesia in addressing the limited capacity of its formal legal and regulatory systems. This can assist Indonesia and other jurisdictions with similar problems to accommodate informal law and processes that have developed in common law jurisdictions.

The study also can contribute to Indonesian legal studies regarding alternative regulatory concepts fulfilling the very limited studies and literature available in Indonesia over the topics. It can also provide evidence and justification for comparative study theories where the non-legal factors determine the reception of legal transplants.

8.4.2.2. Practical contribution

Chapter 1 proposed four practical outcomes from the research:

- (1) better inform Indonesian policy and law making and regulatory practices regarding the usefulness and complementarities of alternative regulation and formal law in improving regulatory frameworks.
- (2) improve, on the basis of empirical evidence, corporate governance in listed companies as disclosure is recognized as essential for corporate accountability.
- (3) permit regulatory agencies and citizens to monitor developments and to use that information for other purposes in ensuring accountability for corporate actions.
- (4) contribute to knowledge around creating appropriate corporate governance applications suited to Indonesia's context.

The first relates to the academic contribution of providing information on the effectiveness of informal law as an alternative strategy in improving the capacity of regulatory framework in Indonesia. The research provides evidence in the context of the GCG Code that it is not effective in the present regulatory framework and that it is not complementary of formal law. The literature, however, indicates that it could be and some other countries in South East Asia have been able to gain benefits from their use of the concept that may repay further study by Indonesian law and policy makers and regulators. This includes the possible use of the GCG Code to fill gaps in, or complement, the existing formal corporate governance laws and rules in the regulatory framework.

The second relates to, amongst other things, the recommendations made above which may assist law and policy makers and regulators to find strategies to improve the awareness of the importance of corporate governance in listed companies and of disclosure in particular. The study provides empirical evidence of significant concerns about compliance with disclosure obligations and the quality of the information disclosed. Indonesia needs to create an effective system to monitor, review and evaluate emerging issues around disclosure to ensure greater accountability for compliance.

The recommendations include more effective enforcement mechanisms in the GCG Code that will need to reflect some greater contextualisation to Indonesia to draw greater support from the local business and regulatory elite. This would involve the consideration of local business practices and cultural values for a better fit that may lead to the greater

involvement of the non-state sector in regulation particularly in the domestic use of international standards.

There are also the suggestions that codes need to be periodically revised to reflect their adaptable and responsive capacities. It should also consider, where provisions of the Code have been included in formal law and regulation, how the flexibility, adaptability, and responsiveness reflecting its origin in concepts of smart regulation, responsive regulation, and decentred regulation can be maintained.

The third builds on the second but involves even greater challenges. The research points to the importance of establishing greater integrity in Indonesian policy and law making and regulatory practices to improve regulatory frameworks. As the recommendations point out such improvements can only be achieved by changed mentalities and firmer commitment to ensuring integrity in regulation, including in the legal system and legal culture. This requires committed and enduring efforts to reform of fundamental factors and involve significant elements of society including citizens, the private sector and NGOs. Thailand, with similar problems to Indonesia, examined in Chapter 3, proves that such efforts can lead to successful outcomes. Only then can the quality of information disclosed be relied on by regulators and shareholders to make informed decisions and also for NGOs and citizens to use for their own purposes in ensuring that corporations are accountable to the community.

Fourthly, this study contributes to the knowledge around factors to be addressed in order to create more appropriate application of corporate governance principles in Indonesia. The study has drawn attention to the need to consider how similar codes have been successful in comparable jurisdictions. The recommendations have pointed to the need in introducing and implanting legal and regulatory transplants to consider factors which distinguish Indonesia from the societies from which the transplants come. The recommendations point to legal and non legal factors to which Indonesian policy and law makers should pay attention. The non legal factors include the power distance, uncertainty avoidance and collectivism which marks Indonesian society and which have resulted in an extensive culture of patronage, *bapakism*. At a more specific level they are the absence of a strong adherence to an anti-corruption ethos, political interference, the mentality of

fulfilling formalities only, the absence of effective sanctions, limited capacity for informal sanctions and the overall poor business ethics. The legal aspects include the weak and corrupt legal system, the loss of trust in it and legal culture. In respect of legal culture both legal educators and the practicing profession need to address the inflexibilities created by a strict adherence to civil law mentalities.

The study may have been overly ambitious in the practical contributions it proposed. Also a number of recommendations have pointed to the difficult to address prevalence of corruption. This should not be regarded as a failure but as a further confirmation of the need for strategies that entrench public and private attitudes which are hostile to corrupt practices. The study particularly points to the significance of the failure of the formal legal system in respect of the use of informal law and the need to improve its capacity. Again the difficulty of achieving this should also not undermine its recognition as a fundamental issue that must be addressed. Unless this is done it will be difficult to use formal and informal law in a collaboration way in order to improve a broader range of corporate governance issues and ultimately to develop a more effective corporate governance and disclosure practices.

8.5. Limitation of the research and suggestions for future research

This study is limited to the Indonesian Code of Good Corporate Governance (GCG Code). It does not include other forms of informal laws such as codes of practices, codes of conduct or codes of ethics and so on. Therefore, the study has a limited outcome. This implies the need for further research on other informal laws or mechanisms other than those found in the GCG Code.

The study investigates significant issues in a large economy but with the research resources of only one investigator. This particularly limited the amount of field work that could be done. This is significant where there appears to be significant gaps in the legal and regulatory systems between written statements of formal and soft law and the practices around them.

It is clear that there are discrepancies between the objectives of the standards in the GCG Code relating to disclosure and their application to ensure that there is sufficient

adherence to them to establish reliability with respect to disclosure and corporate governance more generally.

There has been a practice in Indonesian legislation and regulation to legislate and regulate corporate governance matters in a command and obey style rather than relying on principles in a softer and smarter form of regulation. This may have created a bureaucratic, rigid and inflexible legal and regulatory framework creating difficulties for users. However, informal or soft law may be too flexible and consequently too weak, given the problems with implementation and enforcement of disclosure requirements, which have been identified. Their strength and prevalence is explained by Indonesia's specific attributes. Those situational variables of poor integrity, mentalities, legal culture and weak formal legal system, as noted earlier, affect the achievement of corporate governance and disclosure objectives. Those variables, in the context of disclosure under the GCG Code, require a longer term study of more discrete processes which, as Milhaupt and Pistor point out, should include both the substance and the sequencing of law, codes, and policies are important.

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Appendix A

Interview Schedule

Project Title: **The role of Corporate Governance Codes in enhancing accountability for disclosure in Indonesia**

--- Issues to investigate in questionnaire ---

I. DISCLOSURE

1. What does disclosure mean to you? Do you think that it is important for good corporate governance?
2. Would the controllers of Indonesian listed companies see disclosure as being as important for good corporate governance as you do?
3. Companies have a number of important issues to deal with including business strategies, competition, sustainability and public relations. Of the top 10 issues they need to deal with where do you think they would rank disclosure?
4. How would you describe the impact of disclosure requirements on accountability in Indonesian listed companies?
5. Do you see disclosure practices as important in establishing investor confidence in listed companies? [Prompt: Do you agree that compliance with disclosure requirements is needed to attract foreign investors to Indonesia?]
6. In your experience, have you found problems with the information disclosed by companies?
7. In your experience, do companies obtain benefits from complying with disclosure requirements? [Prompt: What are they?]
8. In your experience, are there any non-legal factors which influence companies in complying or not complying with disclosure requirements? [Prompt: Business culture? Political interests? The ethnicity of the controlling family?]

9. To achieve effective corporate accountability for disclosure, do you see any of the following organizations having a role:
 - a) Business associations (such as the Indonesian Association of Entrepreneurs, etc)?
 - b) Professionals (such as lawyers, accountants and auditors)?
 - c) Non-government organizations (NGOs) (such as the Indonesian Association of Managers Indonesian Institute of Accountants, Indonesian Association of Lawyers)?
10. Based on your experience, what would you suggest is required to achieve better disclosure practices in Indonesian companies?

II. REGULATION

11. Do you think that the 2007 Company Law and Investment law are effective in creating good corporate governance?
12. How do you see those laws dealing with accountability for disclosure?
13. In your experience, are the Company Registry Law, the Government Regulation on Annual Financial Statements and the Capital Market and Financial Institution Supervisory Agency [BAPEPAM-LK] rules effective in creating disclosure compliance?
14. Is the stock exchange effective in ensuring compliance with disclosure requirements?
15. Is the BAPEPAM-LK effective in ensuring compliance with disclosure requirements?
16. In your experience, would informal sanctions be more effective in strengthening compliance? [Prompt: Negative publicity, public criticism, gossip, embarrassment, and shaming?]

III. CODES

17. The Code for Good Corporate Governance is often seen as an efficient, effective and responsive tool for better regulation. Do you agree with this? [Prompt: Why?]
18. How do you see the Code relating to existing laws?
19. Has the Code reduced the importance of the 2007 Company law and Investment Law,

or stock exchange or the BAPEPAM-LK?

20. Some claim that there are many benefits in having a Code. Have you found this to be true of the 2006 Code? [Prompt: Flexibility, fairness, responsibility, relevancy and effectiveness, self-enforcement, expert skills, quick, efficient and less formal processes, low costs and targeting specific problems?]
21. In your experience, how much interest do you think companies have in applying the Code?
22. In general, how would you describe the influence of the Code on Indonesian companies? [Prompt: Does it contribute to good corporate governance?]
23. In your experience, has the Code contributed to more effective accountability for disclosure in Indonesian companies? [Prompt: In what ways?]
24. From your experience, have you found problems in applying the Code? [Prompt: If so, what are they?]
25. In your experience, does the Code conflict with Indonesian business and legal culture as well as political interests? [Prompt: Corruption, nepotism, collusion?]
26. In your experience, are there significant factors which would make a company comply, or not comply with the Code? [Prompt: Are the sanctions ineffective?]
27. In implementing the corporate governance code, how would you describe the role of:
 - (a) business entities
 - (b) government
 - (c) regulatory bodies
 - (d) NGOs
 - (e) citizens
28. How would you describe any enforcement powers in the Code?
29. Based on your experience, do you think the Code should be legally enforceable?
30. Based on your experience, what changes would you suggest to the Code to achieve effective accountability for corporate disclosure practices?

Appendix B

Daftar Pertanyaan Interview

Interview Schedule

Judul Proyek Penelitian: **Peran pedoman corporate governance dalam meningkatkan akuntabilitas untuk disclosure yang efektif di Indonesia**

Project Title: The role of corporate governance codes in enhancing accountability effective disclosure in Indonesia.

--- Hal-hal yang diselidiki dalam kuisisioner ---

--- Issues to investigate in questionnaire ---

I. DISCLOSURE

- 1. Apa artinya disclosure bagi anda? Apakah menurut anda disclosure penting untuk good corporate governance?**

What does disclosure mean to you? Do you think that it is important for good corporate governance?

- 2. Akankah para lembaga pengawas perusahaan-perusahaan yang listing di bursa efek memandang disclosure sebegitu penting seperti anda?**

Would the controllers of Indonesian listed companies see disclosure as being as important for good corporate governance as you do?

- 3. Perusahaan-perusahaan memiliki sejumlah urusan penting untuk ditangani termasuk strategi-strategi bisnis, persaingan, kesinambungan usaha dan hubungan dengan masyarakat. Dari 10 urusan-urusan yang perlu mereka tangani**

menurut anda disclosure akan mereka tempatkan di urutan ke berapa?

Companies have a number of important issues to deal with including business strategies, competition, sustainability and public relations. Of the top 10 issues they need to deal with where do you think they would rank disclosure?

- 4. Bagaimana akan anda gambarkan pengaruh persyaratan-persyaratan disclosure terhadap akuntabilitas perusahaan-perusahaan Indonesia yang listing?**

How would you describe the impact of disclosure requirements on accountability in Indonesian listed companies?

- 5. Apakah anda melihat praktek penerapan disclosure sebagai hal penting dalam membangun keyakinan investor bagi perusahaan-perusahaan yang listing? [Apakah anda setuju bahwa kepatuhan terhadap persyaratan disclosure merupakan kebutuhan untuk menarik para investor asing ke Indonesia?]**

Do you see disclosure practices as important in establishing investor confidence in listed companies? [Prompt: Do you agree that compliance with disclosure requirements is needed to attract foreign investors to Indonesia?]

- 6. Menurut pengalaman anda, apakah anda menghadapi/menemukan masalah dengan informasi yang perusahaan anda disclosed?**

In your experience, have you found problems with the information disclosed by companies?

- 7. Sesuai pengalaman anda, apakah perusahaan memperoleh manfaat dari mematuhi persyaratan disclosure? [Apa saja manfaat tersebut?]**

In your experience, do companies obtain benefits from complying with disclosure requirements? [Prompt: What are they?]

- 8. Sesuai pengalaman anda, adakah faktor-faktor di luar hukum yang mempengaruhi perusahaan-perusahaan dalam mematuhi atau tidak mematuhi persyaratan-persyaratan disclosure? [Budaya bisnis? Kepentingan politik? Etnis dari perusahaan keluarga?]**

In your experience, are there any non-legal factors which influence companies in complying or not complying with disclosure requirements? [Prompt: Business culture? Political interests? The ethnicity of the controlling family?]

9. Guna mencapai akuntabilitas perusahaan untuk disclosure yang efektif, apakah anda melihat ada peran dari organisasi-organisasi di bawah ini:

a) Asosiasi bisnis (seperti Asosiasi Manajer Indonesia, Ikatan Akuntan Indonesia, Perhimpunan Pengacara Indonesia, dsb)?

b) Profesionals (seperti pengacara, akuntan dan auditor)?

c) Lembaga Swadaya Masyarakat (seperti Masyarakat Transparansi Indonesia)?

To achieve corporate accountability for effective disclosure, do you see any of the following organizations having a role:

a) *Business associations (such as the Indonesian Association of Entrepreneurs, etc)?*

b) *Professionals (such as lawyers, accountants and auditors)?*

c) *Non-government organizations (NGOs) (such as Indonesian Society for Transparency)?*

10. Berdasarkan pengalaman anda, apa yang akan anda sarankan guna mencapai praktek penerapan disclosure yang lebih baik bagi perusahaan-perusahaan Indonesia?

Based on your experience, what would you suggest is required to achieve better disclosure practices in Indonesian companies?

II. REGULATION

11. Apakah menurut anda Undang-undang Perseroan Terbatas dan Undang-undang Penanaman Modal tahun 2007 efektif dalam menciptakan good corporate governance?

Do you think that 2007 Company Law and Investment law are effective in creating good corporate governance?

12. Bagaimana pandangan anda menyangkut undang-undang tersebut berkaitan dengan akuntabilitas untuk disclosure yang efektif?

How do you see those laws dealing with accountability for effective disclosure?

13. Menurut pengalaman anda, apakah Undang-undang Pendaftaran Perusahaan, Peraturan Pemerintah tentang Laporan Keuangan Tahunan dan peraturan Badan Pengawas Pasar Modal dan Lembaga Keuangan (BAPEPAM-LK) efektif

dalam menciptakan kepatuhan disclosure?

In your experience, are the Company Registry Law, the Government Regulation on Annual Financial Statements and the Capital Market Supervisory Agency [BAPEPAM-LK] rules effective in creating disclosure compliance?

14. Apakah bursa efek efektif untuk memastikan kepatuhan terhadap persyaratan – persyaratan disclosure?

Is the stock exchange effective in ensuring compliance with disclosure requirements?

15. Apakah BAPEPAM-LK efektif dalam memastikan kepatuhan terhadap persyaratan disclosure?

Is the BAPEPAM-LK effective in ensuring compliance with disclosure requirements?

16. Sesuai pengalaman anda, akankah sanksi-sanksi informal lebih efektif dalam memperkuat kepatuhan? [Publikasi negatif, kritikan publik, gossip, membuat menjadi malu dan rasa malu]?

In your experience, would informal sanctions be more effective in strengthening compliance? [Prompt: Negative publicity, public criticism, gossip, embarrassment, and shaming?]

III. CODES

17. Pedoman Good Corporate Governance sering dilihat sebagai sarana yang efisien, efektif dan responsif untuk peraturan yang lebih baik. Apakah anda setuju dengan hal ini? [Mengapa?]

The Code for Good Corporate Governance is often seen as an efficient, effective and responsive tool for better regulation. Do you agree with this? [Prompt: Why?]

18. Bagaimana anda melihat Pedoman tersebut berkaitan dengan perangkat perundang-undangan yang berlaku saat ini?

How do you see the Code relating to existing laws?

19. Apakah Pedoman tersebut telah mengurangi arti pentingnya Undang-undang Perseroan Terbatas dan Undang-undang Penanaman Modal atau peraturan bursa efek atau BAPEPAM-LK?

Has the Code reduced the importance of the 2007 Company law and Investment Law,

or stock exchange or the BAPEPAM-LK?

- 20. Ada yang mengklaim bahwa memiliki suatu Pedoman terdapat banyak manfaat. Apakah anda menemukan Pedoman tahun 2006 benar memiliki berbagai manfaat? [Fleksibilitas, keadilan, bertanggung jawab, relevansi dan efektivitas, self-enforcement, keahlian pakar, cepat, efisien dan proses yang tidak terlalu formal, lebih murah dan kena sasaran pada masalah-masalah spesifik?]** .

Some claim that there are many benefits in having a Code. Have you found this to be true of the 2006 Code? [Prompt: Flexibility, fairness, responsibility, relevancy and effectiveness, self-enforcement, expert skills, quick, efficient and less formal processes, low costs and targeting specific problems.]

- 21. Sesuai pengalaman anda, seberapa banyak ketertarikan perusahaan-perusahaan dalam menerapkan Pedoman tersebut menurut anda?**

In your experience, how much interest do you think companies have in applying the Code?

- 22. Secara umum, bagaimana akan anda gambarkan pengaruh dari Pedoman tersebut terhadap perusahaan-perusahaan Indonesia? [Apakah Pedoman tersebut memberikan kontribusi pada good corporate governance?]**

In general, how would you describe the influence of the Code on Indonesian companies? [Prompt: Does it contribute to good corporate governance?]

- 23. Menurut pengalaman anda, apakah Pedoman tersebut telah memberikan kontribusi terhadap akuntabilitas untuk disclosure yang lebih efektif bagi perusahaan-perusahaan Indonesia? [Dalam hal apa saja?]**

In your experience, has the Code contributed to more accountability for effective disclosure in Indonesian companies? [Prompt: In what ways?]

- 24. Sesuai pengalaman, apakah anda menemukan masalah-masalah dalam menerapkan Pedoman tersebut? [Jika ada, apa saja masalah tersebut?]**

From your experience, have you found problems in applying the Code? [Prompt: If so, what are they?]

- 25. Menurut pengalaman anda, apakah Pedoman tersebut berbenturan dengan budaya bisnis dan budaya hukum serta juga kepentingan politik Indonesia?**

[Korupsi?, Nepotism?, Kolusi?]

In your experience, does the Code conflict with Indonesian business and legal culture as well as political interests? [Prompt: Corruption, nepotism, collusion?]

26. Menurut pengalaman anda, adakan faktor-faktor signifikan yang akan membuat perusahaan mematuhi, atau tidak mematuhi Pedoman tersebut? [Apakah efektif dengan memberikan sanksi?]

In your experience, are there significant factors which would make a company comply, or not comply with the Code? [Prompt: Are the sanctions in effective?]

27. Dalam menerapkan Pedoman Umum Good Corporate Governance, bagaimana anda gambarkan peran dari:

(a) bisnis entities

(b) pemerintah

(c) badan-badan pengawas/regulasi

(d) lembaga swadaya masyarakat (LSM)

(e) warga masyarakat

In implementing the corporate governance code, how would you describe the role of:

(a) business entities

(b) government

(c) regulatory bodies

(d) NGOs

(e) citizens

28. Bagaimana anda gambarkan kekuatan memaksa atau penegakan dalam Pedoman tersebut?

How would you describe any enforcement powers in the Code?

29. Berdasarkan pada pengalaman anda, apakah Pedoman tersebut seharusnya mempunyai kekuatan hukum yang memaksa?

Based on your experience, do you think the Code should be legally enforceable?

30. Berdasarkan pengalaman anda, perubahan-perubahan apa saja yang anda sarankan untuk Pedoman tersebut dalam mencapai akuntabilitas untuk praktek disclosure yang efektif?

Based on your experience, what changes would you suggest to the Code to achieve effective accountability for effective corporate disclosure practices?

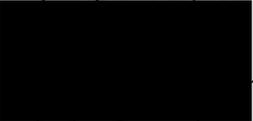
Appendix C

DECLARATION OF ACCURATE TRANSLATION

I, Gunadi, , hereby declare:

1. I am a native speaker of Bahasa Indonesia. I am a lecturer in the information system of the University of Gajayana Malang Indonesia. I am a PhD student in the Faculty of Business and Law Victoria University.
2. I have accurately translated from English into Bahasa Indonesia the following documents relating to the research project 'The role of corporate governance codes in enhancing accountability for effective disclosure in Indonesia':
 - (i) Information to Participants Involved in Research
 - (ii) Consent Form for Participants Involved in Research
 - (iii) Interview schedule

9 November 2009


GUNADI



INFORMATION TO PARTICIPANTS INVOLVED IN RESEARCH

You are invited to participate

You are invited to participate in a research project entitled "The role of corporate governance codes in enhancing accountability for effective disclosure in Indonesia".

This project is being conducted by a student researcher, Jeannie Connie Rotinsulu, as part of a PhD study at Victoria University under the supervision of Professor Neil Andrews from the Faculty of Business and Law.

Project explanation

The purpose of the research being undertaken is to analyse the role of corporate governance codes in enhancing accountability for effective disclosure in Indonesia. It will analyse the applicability of new regulatory theories to understanding Indonesia's use of informal regulations, particularly alternative approaches to the regulation of disclosure. It will consider the spaces which the Indonesia's Code of Good Corporate Governance may fill in the formal legal system as an alternative regulatory strategy. It will determine how Indonesia may take advantages of informal or soft law strategies, represented by the code, the efficacies of the complimentary relationships between formal law and informal rules to make regulation more reflexive, effective, legitimate, and transparent when formal legal systems are weak. Findings of this project may assist in improving the code and other regulatory strategies so that they are more effective. It also may assist in understanding several crucial problems causing poor corporate governance and solutions to those problems.

What will I be asked to do?

You are invited to participate in an interview which takes about one hour. The interview is about your views on the role of the corporate governance code in enhancing accountability for effective disclosure in Indonesian listed companies. It relates to your knowledge and experiences including the code, law and regulatory practices as well as political, social and business cultures. It seeks to draw out your experiences of these. You are, however, not obliged to disclose anything which you are not comfortable with disclosing or to answer any question which you do not wish to.

What will I gain from participating?

Your comments, based on your knowledge and experiences, may contribute to gaining a better understanding and discovery of possible ways in which the code may compliment the operation of the formal legal system as an alternative regulatory strategy. It may enhance formal law to improve accountability within Indonesian listed companies for effective disclosure. It may lead towards the development of more effective regulatory frameworks. It will also contribute to possible solutions to problems in poor corporate governance practices and changes to make it more suited to the Indonesia context.

How will the information I give be used?

The information you provide will be included in a thesis which will be available in the library of Victoria University. Also some parts of the information may be published in various academic journals. Your responses to questions will remain confidential. Your identity will be kept strictly confidential. You will not be named as having participated in the research project. Your statements or comments may be republished in the thesis or the articles, but not in such a way that you, or your organisation, could be identified.

What are the potential risks of participating in this project?

Minimum risks have been identified from participating in this research. Throughout the interview, if you feel uncomfortable or require explanations, please do not hesitate to raise the issue with the researcher. You do not need to disclose any information which you may be uncomfortable about disclosing. As indicated, you are free not to answer any question. However, you will not be identified as the maker or author of any statement. Also, the statement or comment will not be used in a way which will enable you to be identified. You may withdraw at any time and for any reason without prejudice.

How will this project be conducted?

This project employs new regulatory theories to analyse the use of informal regulation represented by the corporate governance code in the Indonesian context. It will involve a literature review to identify problems and the way in which the code may be used to remedy such problems. It will also include a comparative study of models and practices of corporate governance codes in several jurisdictions which have aspects comparable to Indonesia.

Data collection of this project will involve three distinct sources, the literature on new regulatory theories and other relevant literature; business media data bases relevant to corporate governance especially to disclosure within Indonesian listed companies; and an empirical study in both regulatory and corporate sectors utilizing structured interviews.

Who is conducting the study?

This project is conducted by:

Professor Neil Andrews (Neil.Andrews@vu.edu.au) and

Jeannie Connie Rotinsulu (jeannieconnie.rotinsulu@live.vu.edu.au)

Any queries about your participation in this project may be directed to the Principal Researcher listed above. If you have any queries or complaints about the way you have been treated, you may contact the Ethics and Biosafety Coordinator, Victoria University Human Research Ethics Committee, Victoria University, PO Box 14428, Melbourne, VIC, 8001 phone (03) 9919 414



Appendix E

**INFORMASI
UNTUK PARTISIPAN
YANG TERLIBAT DALAM PENELITIAN**

**INFORMATION
TO PARTICIPANTS
INVOLVED IN RESEARCH**

Anda diundang untuk berpartisipasi
You are invited to participate

Anda diundang untuk berpartisipasi dalam suatu proyek penelitian berjudul "Peran Pedoman Corporate Governance dalam meningkatkan akuntabilitas untuk disclosure yang efektif di Indonesia"

You are invited to participate in a research project entitled "The role of corporate governance codes in enhancing accountability for effective disclosure in Indonesia".

Proyek penelitian ini dilakukan oleh mahasiswa peneliti, Jeannie Connie Rotinsulu, sebagai bagian dari studi PhD di Victoria University di bawah supervisi dari Profesor Neil Andrews dari Fakultas Bisnis dan Hukum.

This project is being conducted by a student researcher, Jeannie Connie Rotinsulu, as part of a PhD study at Victoria University under the supervision of Professor Neil Andrews from the Faculty of Business and Law.

Penjelasan Proyek Penelitian
Project explanation

Tujuan penelitian yang sedang dilakukan ini adalah untuk menganalisa peran dari Pedoman Corporate Governance dalam meningkatkan akuntabilitas untuk disclosure yang efektif di Indonesia. Proyek ini akan menganalisa penerapan dari teori-teori regulasi baru guna memahami penggunaan peraturan-peraturan informal di Indonesia, khususnya peluang pendekatan alternatif untuk peraturan disclosure. Studi ini akan mempertimbangkan ruang dimana Pedoman Good Corporate Governance dapat mengisi dalam sistem hukum formal sebagai suatu strategi peraturan alternatif. Hal ini nantinya akan menelaah bagaimana Indonesia dapat mengambil manfaat-manfaat dari strategi peraturan informal atau soft law, diwakili oleh Pedoman tersebut, dan juga hubungan saling melengkapi antara hukum formal dan peraturan informal untuk membuat peraturan menjadi lebih reflektif, efektif, legitimasif, dan transparan ketika sistem hukum lemah. Hasil temuan dari penelitian ini akan dapat membantu meningkatkan Pedoman dimaksud dan strategi-strategi regulasi yang lain sehingga menjadi lebih efektif. Hasil ini juga nantinya dapat membantu untuk memahami beberapa masalah krusial yang menyebabkan penerapan corporate governance yang rendah dan solusi atas masalah-masalah tersebut.

The purpose of the research being undertaken is to analyse the role of corporate governance codes in enhancing accountability for effective disclosure in Indonesia. It will analyse the applicability of new regulatory theories to understanding Indonesia's use of informal regulations, particularly alternative approaches to the

Bagaimana informasi yang saya berikan akan digunakan?

How will the information I give be used?

Informasi yang anda berikan akan dimasukkan dalam sebuah tesis yang akan tersedia di perpustakaan Victoria University. Dan juga beberapa bagian dari informasi tersebut mungkin akan dipublikasi di berbagai jurnal akademik. Tanggapan-tanggapan anda atas pertanyaan-pertanyaan akan tetap menjadi rahasia. Identitas anda akan dijaga kerahasiaannya secara ketat. Partisipasi anda dalam proyek penelitian ini tidak akan menyebutkan nama anda. Pernyataan-pernyataan atau tanggapan-tanggapan anda kemungkinan akan dipublikasi kembali dalam tesis atau artikel-artikel, akan tetapi tidak dalam kondisi dimana anda, atau organisasi anda, dapat diidentifikasi.

The information you provide will be included in a thesis which will be available in the library of Victoria University. Also some parts of the information may be published in various academic journals. Your responses to questions will remain confidential. Your identity will be kept strictly confidential. You will not be named as having participated in the research project. Your statements or comments may be republished in the thesis or the articles, but not in such a way that you, or your organisation, could be identified.

Resiko-resiko apa saja yang berpotensi muncul dalam berpartisipasi di proyek penelitian ini?

What are the potential risks of participating in this project?

Ada resiko-resiko minimal yang teridentifikasi dari berpartisipasi dalam penelitian ini. Selama interview, jika anda merasa kurang nyaman atau ingin meminta beberapa penjelasan, silahkan mengajukan hal-hal tersebut kepada peneliti. Anda tidak perlu untuk mengungkapkan informasi apapun dimana anda mungkin merasa tidak nyaman menyangkut hal tersebut. Sebagaimana telah diindikasikan, anda bebas untuk tidak menjawab pertanyaan. Akan tetapi, anda tidak akan diidentifikasi sebagai pembuat atau pengarang dari pernyataan tersebut. Dan juga, pernyataan atau komentar anda tidak akan digunakan dalam kondisi dimana anda akan dapat diidentifikasi. Anda dapat menarik diri setiap waktu dan dengan alasan apa saja tanpa prasangka.

Minimum risks have been identified from participating in this research. Throughout the interview, if you feel uncomfortable or require explanations, please do not hesitate to raise the issue with the researcher. You do not need to disclose any information which you may be uncomfortable about disclosing. As indicated, you are free not to answer any question. However, you will not be identified as the maker or author of any statement. Also, the statement or comment will not be used in a way which will enable you to be identified. You may withdraw at any time and for any reason without prejudice.

Bagaimana proyek ini akan dilakukan?

How will this project be conducted?

Proyek penelitian ini menggunakan teori-teori regulasi baru untuk menganalisa penggunaan peraturan informal diwakili oleh pedoman corporate governance dalam konteks Indonesia. Studi ini akan melakukan review literature untuk mengidentifikasi masalah-masalah dan cara dimana pedoman tersebut dapat digunakan untuk mengatasi masalah-masalah tersebut. Studi komparasi akan juga dilakukan dari model dan praktek-praktek penerapan pedoman corporate governance di beberapa yurisdiksi yang memiliki aspek-aspek yang setara dengan Indonesia.

Pengumpulan data dalam penelitian ini akan melibatkan tiga sumber yang berbeda, literature mengenai teori-teori regulasi baru dan literature yang relevan; data base media massa bisnis yang relevan dengan corporate governance khususnya disclosure dalam perusahaan-perusahaan Indonesia yang listing; dan studi empiris di kedua sector regulasi dan korporasi menggunakan interview terstruktur.

This project employs new regulatory theories to analyse the use of informal regulation represented by the corporate governance code in the Indonesian context. It will involve a literature review to identify problems and the way in which the code may be used to remedy such problems. It will also include a comparative study of models and practices of corporate governance codes in several jurisdictions which have aspects comparable to Indonesia.

Data collection of this project will involve three distinct sources, the literature on new regulatory theories and other relevant literature; business media data bases relevant to corporate governance especially to disclosure within Indonesian listed companies; and an empirical study in both regulatory and corporate sectors utilizing structured interviews.

Siapa yang melaksanakan studi ini?

Who is conducting the study?

Proyek ini dilakukan oleh:

This project is conducted by:

Professor Neil Andrews (Neil.Andrews@vu.edu.au) and

Jeannie Connie Rotinsulu (jeannieconnie.rotinsulu@live.vu.edu.au)

Semua pertanyaan mengenai partisipasi anda dalam proyek ini, anda dapat langsung menghubungi Peneliti utama sebagaimana tertera diatas.

Apabila anda mempunyai pertanyaan atau keluhan-keluhan menyangkut cara anda diperlakukan, anda dapat menghubungi Koordinator Ethics dan Biosafety, Victoria University Human Research Ethics Committee, Victoria University PO Box 14428, Melbourne, VIC, 8001 phone (03) 9919 4148.

Any queries about your participation in this project may be directed to the Principal Researcher listed above. If you have any queries or complaints about the way you have been treated, you may contact the Ethics and Biosafety Coordinator, Victoria University Human Research Ethics Committee, Victoria University, PO Box 14428, Melbourne, VIC, 8001 phone (03) 9919 4148.



CONSENT FORM FOR PARTICIPANTS INVOLVED IN RESEARCH

INFORMATION TO PARTICIPANTS:

We would like to invite you to be a part of a study on "The role of corporate governance codes in enhancing accountability for effective disclosure in Indonesia", to analyse the applicability of alternative approaches to the regulation of disclosure to achieve a better standard of corporate governance, and to explore more generally the complementary relationships between formal law and informal rules to assist in improving the regulatory system for Indonesian listed companies.

CERTIFICATION BY SUBJECT

I, _____

of _____

certify that I am at least 18 years old and that I am voluntarily giving my consent to participate in the study: "The role of corporate governance codes in enhancing accountability for effective disclosure in Indonesia" being conducted at Victoria University by Professor Neil Andrews.

I certify that the objectives of the study, together with any risks and safeguards associated with the procedures listed hereunder to be carried out in the research, have been fully explained to me by Jeannie Connie Rotinsulu,

and that I freely consent to participation involving the below mentioned procedures:

- an interview: (please choose an appropriate box)
 - in which the answers will be recorded on an audio tape, or
 - in which the answers will be recorded in the form of note taking.

I certify that I have had the opportunity to have any questions answered and that I understand that I can withdraw from this study at any time and that this withdrawal will not jeopardise me in any way.

I have been informed that the information I provide will be kept confidential.

Signed:

Date:

Any queries about your participation in this project may be directed to the researcher Professor Neil Andrews at +61 (03) 3 9919 1826 or Neil.Andrews@vu.edu.au

If you have any queries or complaints about the way you have been treated, you may contact the Ethics & Biosafety Coordinator, Victoria University Human Research Ethics Committee, Victoria University, PO Box 14428, Melbourne, VIC, 8001 phone (03) 9919 4148.



FORMULIR PERSETUJUAN PARTISIPAN UNTUK TERLIBAT DALAM PENELITIAN

CONSENT FORM FOR PARTICIPANTS INVOLVED IN RESEARCH

INFORMASI UNTUK PARA PARTISIPAN : INFORMATION TO PARTICIPANTS:

Kami mengundang anda untuk menjadi bagian dari suatu studi mengenai "Peran pedoman corporate governance dalam meningkatkan akuntabilitas untuk disclosure yang efektif di Indonesia", untuk menganalisa penerapan dari pendekatan alternatif terhadap peraturan disclosure guna mencapai standar corporate governance yang lebih baik, dan untuk menelaah secara lebih umum hubungan saling melengkapi antara hukum formal dan peraturan informal untuk membantu meningkatkan sistim regulasi bagi perusahaan-perusahaan Indonesia yang listing.

We would like to invite you to be a part of a study on "The role of corporate governance codes in enhancing accountability for effective disclosure in Indonesia", to analyse the applicability of alternative approaches to the regulation of disclosure to achieve a better standard of corporate governance, and to explore more generally the complementary relationships between formal law and informal rules to assist in improving the regulatory system for Indonesian listed companies.

SERTIFIKASI MENURUT SUBYEK CERTIFICATION BY SUBJECT

Saya, _____

I, _____

Dari _____

of _____



menyatakan bahwa saya berusia paling rendah 18 tahun dan bahwa saya secara sukarela memberikan persetujuan untuk berpartisipasi dalam studi mengenai "Peran pedoman corporate governance dalam meningkatkan akuntabilitas untuk disclosure yang efektif di Indonesia" yang dilakukan di Victoria University oleh Profesor Neil Andrews.

certify that I am at least 18 years old and that I am voluntarily giving my consent to participate in the study: "The role of corporate governance codes in enhancing accountability for effective disclosure in Indonesia" being conducted at Victoria University by Professor Neil Andrews.

Saya menyatakan bahwa tujuan dan sasaran dari studi tersebut, bersama-sama dengan segala resiko dan jaminan perlindungan berkaitan dengan daftar prosedur yang dilaksanakan dalam penelitian sebagaimana tertera di bawah ini, telah secara lengkap dijelaskan kepada saya oleh Jeannie Connie Rotinsulu.

I certify that the objectives of the study, together with any risks and safeguards associated with the procedures listed hereunder to be carried out in the research, have been fully explained to me by Jeannie Connie Rotinsulu,

Dan bahwa saya tanpa paksaan setuju untuk berpartisipasi terlibat dalam prosedur-prosedur yang disebutkan di bawah ini:

and that I freely consent to participation involving the below mentioned procedures:

- Interview : (silahkan pilih kotak yang sesuai)
 - an interview: (please choose an appropriate box)
- jawaban-jawaban tersebut akan direkam dalam sebuah audio tape, atau
 in which the answers will be recorded on an audio tape, or
- jawaban-jawaban tersebut akan direkam dalam bentuk catatan.
 in which the answers will be recorded in the form of note taking

Saya menyatakan bahwa saya telah mempunyai kesempatan untuk semua pertanyaan saya telah dijawab dan bahwa saya memahami bahwa saya dapat mengundurkan diri untuk tidak lagi terlibat dalam studi ini dalam setiap waktu dan bahwa pengunduran diri ini tidak akan membahayakan diri saya dalam segala keadaan apapun.

I certify that I have had the opportunity to have any questions answered and that I understand that I can withdraw from this study at any time and that this withdrawal will not jeopardise me in any way.

Saya telah diberitahu bahwa informasi yang saya berikan akan disimpan secara rahasia.
I have been informed that the information I provide will be kept confidential.

Tanda tangan:

Signed:

Tanggal:

Date:

Appendix H



Dear Sir/Madam

You are invited to participate in an interview for a research project entitled "The role of corporate governance codes in enhancing accountability for effective disclosure in Indonesia" which takes about one hour. The interview is about your views on the role of the corporate governance codes in enhancing accountability for effective disclosure in Indonesian listed companies. It relates to your knowledge and experiences including the codes, law and regulatory practices as well as political, social and business cultures. It seeks to draw out your experiences of these. You are, however, not obliged to disclose anything which you are not comfortable with disclosing or to answer any question which you do not wish to. This interview will be conducted on the basis of the confidentiality. Your identity and information will not be disclosed and will be kept strictly confidential.

Your comments, based on your knowledge and experiences, may contribute to gaining a better understanding and discovery of possible ways in which the code may compliment the operation of the formal legal system as an alternative regulatory strategy.

This project is being conducted by a student researcher, Jeannie Connie Rotinsulu, as part of a PhD study at Victoria University under the supervision of Professor Neil Andrews from the Faculty of Business and Law.

Thank you for your participation.

Regards

Appendix I



PO Box 14428
Melbourne Vic 8001 Australia
Phone +61 3 9919 4000
Fax +61 3 9689 4069
www.vu.edu.au

Kepada yang terhormat,

Anda dimohon untuk berpartisipasi dalam suatu interview untuk proyek penelitian berjudul "Peran Pedoman Corporate Governance dalam meningkatkan akuntabilitas untuk disclosure yang efektif di Indonesia"

Interview ini mengenai pandangan atau pendapat anda terhadap peran Pedoman Corporate Governance dalam meningkatkan akuntabilitas untuk disclosure yang efektif di Indonesia. Hal ini berkaitan dengan pengetahuan dan pengalaman anda menyangkut Pedoman dimaksud, praktek-praktek hukum dan regulasi serta politik, sosial dan juga budaya bisnis.

Tanggapan-tanggapan anda akan dapat memberikan kontribusi untuk mendapatkan pemahaman yang lebih baik dan menemukan kemungkinan peluang jalan dimana Pedoman tersebut sebagai suatu strategi regulasi alternatif yang dapat melengkapi pelaksanaan sistem hukum formal yang ada. Hal itu juga akan dapat memberikan kontribusi untuk menemukan pemecahan masalah-masalah praktek penerapan corporate governance yang masih rendah dan perubahan-perubahan yang dibutuhkan untuk membuat Pedoman tersebut menjadi lebih cocok dengan kondisi Indonesia.

Tanggapan-tanggapan anda atas pertanyaan-pertanyaan akan menjadi rahasia. Identitas anda akan dijaga kerahasiaanya secara ketat.

Proyek penelitian ini dilakukan oleh mahasiswa peneliti, Jeannie Connie Rotinsulu, sebagai bagian dari studi PhD di Victoria University di bawah supervisi dari Profesor Neil Andrews dari Fakultas Bisnis dan Hukum.

Terima kasih atas partisipasi anda.

Hormat kami



**VICTORIA UNIVERSITY
HUMAN RESEARCH ETHICS COMMITTEE**

Application for Approval of Project Involving Human Participants in Victoria University

REGISTER NUMBER (*office use only*):

HRETH _____

INFORMATION FOR APPLICANTS

- Applicants are advised to follow the *Guidelines for Applications* prior to submitting *Application for Approval*. Applicants are to forward a) Twelve (12) **hard copy applications** (including one original copy)* with any accompanying documentation to your Faculty Ethics Officer **and b)** an **electronic application** to your Faculty Ethics Officer. **Note: Non Minimum Risk applications** may be forwarded directly to the Secretary, Victoria University Human Research Ethics Committee (researchethics@vu.edu.au).
 - A *Consent Form for Participants Involved in Research* template and *Information for Participants* template is also available on-line.
 - The above documents are located at: <http://research.vu.edu.au/hrec.php>
- * *Applications to be considered at the Faculty of Business & Law need to submit one original hard copy application.*

**YOU ARE REMINDED THAT THIS PROJECT MUST NOT COMMENCE WITHOUT PRIOR WRITTEN APPROVAL
FROM THE APPROPRIATE HUMAN RESEARCH ETHICS COMMITTEE.**

Please Note:

- Ethics approval will not be finalised until electronic & hard copy applications and copies of all necessary materials have been received by the Secretary of the relevant Human Research Ethics Committee.
- This application form is included in the Human Research Register. If your project includes information of a commercial or patentable nature, this information should be sent separately and marked as confidential.
- If an institution other than Victoria University is to be involved in the project, please provide this information and evidence of ethics approval from the other institution with this application.
- Research projects undertaken by individuals who are **not staff members of VU** that require access to a cohort of VU staff or students for research must be 'sponsored' by a member of VU staff who will take responsibility for all interactions with the University and the HREC. A copy of the approved project and approval letter must be forwarded to the Ethics & Biosafety Administration Group.
- If sufficient space is not available on the form for your answer/s, please attach additional page/s.
- Ensure **all questions** are appropriately answered and the hardcopy application is **authorised** by appropriate staff (Applications will **not** be processed without the appropriate authorisation).
- To avoid unnecessary delays, please ensure your full application (both hard copies and soft copy application) has been received by the relevant Human Research Ethics Committee submission date. Refer to University/Faculty *Committee Meeting Dates* at <http://research.vu.edu.au/hrec.php>

University & Faculty Forwarding Details:

Victoria University Human Research Ethics	Faculty Human Research Ethics Contacts
<p><u>Send electronic applications to:</u> E-mail address: researchethics@vu.edu.au</p> <p><u>Hard copy applications to be delivered to:</u> Ethics Secretary, Victoria University Human Research Ethics Committee Office for Research Victoria University PO Box 14428, Melbourne VIC 8001 Or deliver in person to the Ethics & Biosafety Administration Group located within the Office for Research at Building C, Room 302, Footscray Park campus.</p>	<p><u>Send electronic applications to:</u> Faculty of Arts Education & Human Development: AEHDEthics@vu.edu.au Faculty of Business & Law: BLEthics@vu.edu.au Faculty of Health Engineering & Science: HESEthics@vu.edu.au</p> <p><u>Hard copy applications to be delivered:</u> Faculty Ethics Officer <i>Nominated</i> Faculty Human Research Ethics Committee Office for Research Victoria University PO Box 14428, Melbourne VIC 8001 Or deliver in person to the Ethics & Biosafety Administration Group located within the Office for Research at Building C, Room 302, Footscray Park campus.</p>

For Further Information: Web: <http://research.vu.edu.au/hrec.php> Telephone: 9919 4148 or your Faculty Ethics Officer

I attach a proposal for a project involving human participants for the purposes specified on the attached sheets.

Note: The Human Research Ethics Committee normally grants approval for periods of up to two years, subject to annual review. Consideration will be given to granting approval for a longer period in certain circumstances. Applications for extension of approval should be lodged prior to expiry of existing approval.

1. Project Title:

The role of corporate governance codes in enhancing accountability for effective disclosure in Indonesia

2. Principal Investigator/s:

(Projects to be undertaken by students should list the Supervisor as the Principal Investigator)

Title	First Name	Surname	School/Centre	Phone Number	Mobile Number	VU E-Mail Address
Prof	Neil	Andrews	Law	99191826	-	Neil.Andrews@vu.edu.au

3. (a) Associate Investigator/s and/or Co-Investigator/s:

(Please insert additional lines & information if there is more than one)

Title	First Name	Surname	School/Centre	Phone Number	Mobile Number	E-Mail Address
Prof	Andrew	Clarke	Law	99191840	-	Andrew.clarke@vu.edu.au

3. (b) VU Sponsor:

(For applications for research involving participants from individuals who are not staff members of VU. Please refer to declaration page for further details and signature)

Title	First Name	Surname	School/Centre	Phone Number	Mobile Number	VU E-Mail Address

4. Student Project

(Please insert additional lines & information if required)

4.1. Is the application part of a student project? Yes No

4.2. If YES, select the appropriate tick box:

PhD Masters by Research Honours
 Postgraduate Coursework Undergraduate (not honours)

▪ Has this research project been approved by the Postgraduate Research Committee? Yes No

Student details

Title	First Name	Surname	School/Centre	Student Number	Phone Number	VU E-Mail Address
Ms	Jeannie Connie	Rotinsulu	Law	3735125	0402859290	jeannieconnie.rotinsulu@live.vu.edu.au

▪ Is the student currently enrolled at Victoria University? Yes No

5. Type of Project:

(please select Yes or No to the following questions)

5.1. Type of Program

- (a) Is application for a higher degree program? Yes No
- (b) Is this application for a pilot program of a higher degree? Yes No
[If yes, please note that a second application will be required for the full program]
- (c) Is application for an honours program of an undergraduate degree? Yes No
If yes, please indicate semester dates: _____
- (d) Other student project? Please specify _____

5.2. Funded Program

- (a) Is application for a funded research program? Yes No
If yes, please indicate source of funding: _____
- (b) Do you require ethical approval prior to funding being granted? Yes No

If yes, **attach** any necessary forms to be completed by the Ethics Committee and indicate **grant closing date**.

Date: _____

5.3. Intrusiveness of Project

(please select Yes or No to the following questions)

- a) Uses physically intrusive techniques Yes No
- b) Causes discomfort in participants beyond normal levels of inconvenience Yes No
- c) Examines potentially sensitive or contentious areas Yes No
- d) Uses therapeutic techniques Yes No
- e) Seeks disclosure of information which may be prejudicial to participants Yes No
- f) Uses ionising radiation Yes No
- g) Uses of personal information obtained from a Commonwealth department or agency Yes No
1. If YES, and the project is not medical research, does the research meet the Guidelines under Section 95 of the Privacy Act 1988? Yes No

ii. If YES, and the project is medical research (including epidemiological research) does the research meet the Guidelines under Section 95A of the Privacy Act 1988?

Yes No

h) Clinical trial

Yes No

(A clinical trial is a study involving humans to find out whether an intervention, including treatments or diagnostic procedures, which it is believed may improve a person's health, actually does so. A clinical trial can involve testing a drug, a surgical or other therapeutic or preventive procedure, or a *therapeutic, preventive or diagnostic device or service*. Any intervention, including so-called "natural" therapies and other forms of complementary medicine, can be tested in this way).

i) Research focuses on Aboriginal and/or Torres Strait Islander Peoples

Yes No

o If YES, does the project involve health research?

Yes No

j) Involves potentially vulnerable groups (eg children, people in dependent/unequal relationships, highly dependent on medical care, cognitive impairment or intellectual disability, may be involved in illegal activities)

Yes No

If YES, please provide additional detail:

k) Involves deception or covert observation

Yes No

If YES, please provide additional rationale:

Note: If you have ticked "YES" to any of the items g to k, please forward your ethics application to the Secretary, Victoria University Human Research Ethics Committee (VUHREC). Note that Faculty HREC submission deadlines differ to that of the VUHREC, and this may impact on your project's timelines.

6. Aim of project:

Since the Asian financial crisis in 1997, the Indonesian government and business sector have been challenged in creating good corporate governance, considered important for reviving and improving the national economy, especially in respect of effective disclosure practices by listed companies. Empirical evidence clearly demonstrates very poor corporate governance practices in Indonesian listed companies compared with other Asian countries because of weaknesses in its formal legal system. There is an urgent need to seek alternative approaches for improving corporate governance practices including disclosure. This project will seek to identify how Indonesia's Code of Good Corporate Governance may be used as an alternative regulatory instrument to enhance formal law to better address accountability for effective disclosure. It will consider the spaces which the code may fill, as an alternative regulatory approach, in the formal legal system. It will determine how Indonesia may use advantageously informal or soft law strategies, represented by the code, and also the complimentary relationships between formal law and informal rules to make regulation more reflexive, effective, legitimate, and transparent. The findings from this project may also assist in improving the code, particularly in respect of accountability for disclosure and other regulatory strategies. They also may assist in understanding several crucial problems causing poor corporate governance and possible solutions to those problems.

7. Plain language statement of project:

(Provide a brief summary of the project [not more than 2 pages] outlining the broad aims, background, key questions, research design/approach and the participants in the project. Include a theoretical background or context of the research. If there are multiple participant groups or interventions/phases, please specify relevant information for each. Please make sure implications associated with multiple groups/phases is addressed throughout the application. It is recognised that in some areas of research, it may be appropriate that this statement is repeated

elsewhere in this application form, and that it may comprise part of your response to questions 6, 8, 15, 16 and 17. This section is to be stated in simple language and any terms or jargon must be accompanied by explanation).

The Context of Project

The 1997 experience of a severe economic crisis in Indonesia and the present global financial crisis, which is attributed by some to failures of corporate governance, indicates that improvements in standards of corporate governance are required. Indonesia has been identified as having low levels of corporate governance performance, particularly in respect of compliance with disclosure requirements. This is generally attributed to corrupt practices, a poor business culture based on relationships rather than rules, concentrated ownership structures with control held by family shareholders, weaknesses in the formal legal system including lack of appropriate law enforcement and adequate sanctions, and also problems regarding the adaptation of legal transplants to Indonesia's situation. The combined impact of these is that Indonesia has a reputation as an exceptionally difficult place to do business. Even though the government has already made significant efforts for legal and regulatory reforms to establish good corporate governance, including the promulgation of corporate governance codes, with the expectation of better enforcement of good corporate governance, there has been a complete failure of the legal system to enforce, or require, accountability.

This project will consider the space for corporate governance codes as an alternative regulatory strategy in the Indonesian context. Specifically, it will evaluate the ways in which they can improve accountability for effective disclosure and corporate governance and also strengthen formal law and regulation. New regulatory theories and the efficacy of the combination of rules and principles will be selectively employed to analyse how Indonesia's corporate governance and regulatory practices can accommodate those ideas.

The major questions to be addressed in this project are: (i) How can the Indonesia's Code of Good Corporate Governance be employed as an alternative regulatory instrument to play a significant role in enhancing formal law and creating accountability for effective disclosure in the Indonesian context; (ii) What kind of functions can the code play; (iii) Can these functions improve the effectiveness, efficiency and responsiveness of the regulation of corporate governance in Indonesia.

Research Design

As the key issue in this project is to analyse the role of corporate governance codes as an alternative regulatory instrument in enhancing accountability for effective disclosure, this project mainly relates to fields in the discipline of law, regulatory theory, and business and legal cultures. In addition, as politics have a significant influence in Indonesian business activities, relevant political issues also will be addressed.

This project will particularly use new regulatory theories to examine and analyse the use of informal regulation in the Indonesia's context. It will involve a literature review to identify problems and the way in which the code may remedy such problems by increasing regulatory effectiveness, legitimacy, flexibility and transparency. It will also include a comparative study of models and practices of corporate governance codes in several jurisdictions which have aspects comparable to Indonesia including other developing economies in South East Asia, such as Malaysia, Singapore and Thailand.

Data collection for this project will involve three distinct sources. Firstly, the literature on new regulatory theories, and relevant literature concerning Indonesian political, social and business cultures as well as the recommendations for corporate governance principles proposed by international organisations will be reviewed. Selected relevant literature from other South East and East Asian jurisdictions on the use of informal law including codes will also be explored. Secondly, business media data bases relevant to Indonesian listed companies, the published reports and other information of those companies and regulatory agencies will also be reviewed for relevant data. Thirdly, an empirical study will be undertaken in both regulatory and corporate sectors utilizing structured interviews with those involved in, or affected by, regulatory and corporate governance practices. It will particularly seek to identify the impact of the code on existing laws and formal regulation, and their effect on accountability for disclosure. This is to gain a better understanding of the practices relating to corporate governance, especially disclosure, draw from their experience with the application of existing laws and the corporate governance code. The interviews will be conducted amongst two broad categories selected from the staff of the following organisations or groups:

Group A: Public Sector

- i. National Committee on Governance
- ii. judges involved in corporate and securities litigations and appeals
- iii. the public prosecutor
- iv. the Indonesia Capital Market and Financial Institution Supervisory Agency [BAPEPAM-LK]
- v. Indonesia Stock Exchange
- vi. government policy and law makers

Group B: Private Sector

- i. professional independent directors.
- ii. non-governmental organisations including the Indonesian Association of Managers, Indonesian Institute of Accountants, Indonesian Association of Lawyers.
- iii. a credit rating agency.
- iv. corporate lawyers.
- v. auditors.
- vi. accountants.
- vii. business journalists.
- viii. academic researchers.
- ix. bloggers.

8. Nature of research, including methodology and a list of all procedures to be used on human participants. Please include a statistical power analysis statement if applicable.

The data collection technique for the structured interview will be a one-on-one interview utilizing an open-ended interview schedule. The format of the interview schedule involves issues relevant to the research in which questions will seek information and knowledge, opinions, analysis and synthesis of related issues. Issues raised will include the interviewee's experience with the code; the importance given to the code in practice; the impact of the code on business and legal cultures; problems with enforcing the code and the role of informal sanctions; the role of regulatory bodies, business and professional organisations, NGOs and citizens; the effectiveness of official law in ensuring disclosure; the importance attached to disclosure by individuals and in corporate practices; the impact of business and social culture on disclosure; the benefits of disclosure to the disclosing entity; the role of business associations, professional organisations and NGOs in ensuring that disclosure takes place; and their suggestions for improvements.

Due to the large number of organisations and people involved in corporate regulation and governance, a purposive sampling method will be employed in determining interviewees. The selection of interviewees will be based on their experiences and knowledge of corporate governance and regulatory practices. They will be contacted by telephone or email.

The interviews will be conducted in Bahasa Indonesia at the office of the interviewees and typically scheduled for about one hour. To ensure the quality of data and information for analysis and quotation, an audio recorder will be used unless interviewees disagree. If they prefer not to be recorded notes will be made during the interview which will be written up immediately afterwards. The questions asked in the interview schedule permit some variation to allow for the particular knowledge and experience of interviewees and also responses gained from previous interviewees. After the interviews, time will be taken to clarify and to evaluate whether the data obtained is credible and authentic. A complete interview schedule is attached as **Appendix A** and the translation in Bahasa Indonesia is also attached as **Appendix B**.

The interview will be conducted on the basis that the confidentiality of the informants' responses will be respected. It will also be on the basis that informants will be made aware that they need not answer any question.

The information from the informants' responses will be triangulated with the data from the other sources of information to be used including media data bases, and other literature. The purpose of data triangulation is to cross-check data from multiple sources to search for irregularities and differences in reaching an objective opinion.

9. Description of those techniques which are considered by the profession to be established and accepted. Please give details of support for their application.

(If, in the course of your research, procedures are significantly varied from those stated here, the Human Research Ethics Committee must be informed).

The project uses qualitative research techniques utilising content analysis of documents and open ended interviews. The qualitative approach will assist in discovering a deeper understanding of how the codes can be used as alternative regulatory instruments to enhance formal law to better address accountability for effective disclosure, specifically the areas and ways in which the code may be beneficial. The in-depth interviews will provide an understanding of what experienced people think about these issues, including their defects, strengths and areas for improvement.

10. Proposed start and end date of project:

(Note: new research projects may not commence prior to approval by the Human Research Ethics Committee).

Proposed start date:	1 April 2010	Proposed end date:	30 September 2010
-----------------------------	---------------------	---------------------------	--------------------------

11. Details of participants:

The participants will be selected from the staff of the following organisations or members of the following groups:

Group A: Public Sector

- i. National Committee on Governance
- ii. judges involved in corporate and securities litigation and appeals
- iii. the public prosecutor
- iv. the Indonesia Capital Market and Financial Institution Supervisory Agency [BAPEPAM-LK]
- v. the Indonesia Stock Exchange
- vi. government policy and law makers

Group B: Private Sector

- i. professional independent directors.
- ii. non-governmental organisations including the Indonesian Association of Managers, Indonesian Institute of Accountants, Indonesian Association of Lawyers.
- iii. credit rating agencies.
- iv. corporate lawyers.
- v. auditors.
- vi. accountants.
- vii. business journalists.
- viii. academic researchers.
- ix. bloggers.

The participants are likely to be senior, experienced, and have a significant knowledge of the issues raised with them. The sample size of this study is between thirty five to forty participants. However, the number of samples will be reviewed during the research to ensure that it is as comprehensive as possible and to deal with saturation.

12. Source of participants

(specify for each group/phase if relevant), and means by which participants are to be recruited)

Potential participants will be recruited mainly in Jakarta, the principal commercial city of Indonesia, as the number of listed companies and relevant organisations are located there. The participant's experience and knowledge of corporate governance in listed companies and regulatory practices are the basic criteria for selecting interviewees to guarantee the credibility of the data and information obtained. The names and contacts of the interviewees from both categories will be obtained through public domain websites, and from academic literature and media reports. They will be invited to participate by email using the form in Appendix B. The researcher has no pre-existing relationship with the participants or agencies or institutions involved.

13. Is there any payment of participants proposed: Yes No

- If yes, state the amount:
- Provide rationale for payment and the amount:
- Describe the financial controls applicable to the program:

14. Premises on which project is to be conducted:

The interviews will be conducted mainly in Jakarta, generally at the offices of interviewees.

15. Dealing with potential risks (for each phase/group where applicable):

(a) Indicate any **physical risks** connected with the proposed procedures

There is no identifiable physical risk.

(b) Indicate any **psychological risks** connected with the proposed procedures

There is no identifiable psychological risk.

(c) Indicate any **social risks** connected with the proposed procedures

There is a possible risk in all interviews where an interviewee may make disrespectful statements of another person regarding Indonesian listed companies and regulatory bodies as well as the regulatory environment.

(d) Indicate any **legal risks** connected with the proposed procedures

There is no identifiable legal risk.

(e) Indicate if there are any **other risks** connected with the proposed procedures

There are no other risks.

(f) Management of the potential risks identified above- indicate how each of these potential risks will be minimised and/or managed if they occur (if risks have not been identified in 15 a – e, go to item 16).

The procedures employed do not present any danger or harm to the individual, either physically or psychologically. However, it is acknowledged that the interview process may involve a slight social risk, therefore the identity of any interviewees and information obtained will not be disclosed and will be kept strictly confidential. This procedure reduces the risk to insignificant. However, some steps will be taken to reduce that possible risk as describe below:

- (i) how risks are to be minimised:

The risk is of an insignificant nature as the target interviewees are professionals who are experienced and mature people in positions of responsibility used to evaluating risk. They are well educated professionals who will be capable of exercising an independent judgment about what they choose to disclose. Further steps to reduce the risk are secured storage for the data keeping confidential any information obtained from them; and, not publishing any information which would identify them as the maker of any statement.

- (ii) how adverse events would be managed if they were to occur:

Any risks that may occur to individuals will be reduced by the steps outlined above.

- (g) If you consider there to be no potential risks, explain fully why no potential risks have been identified.

16. If you consider the participants to be 'at risk', give your assessment of how the potential benefits to the participants or contributions to the general body of knowledge would outweigh the risks.

As indicated in 15(c) there is a slight social risk which is eliminated by the procedure in 15(f). The participants are members of the corporate sector, decision, policy and law makers. Therefore the outcome of this project will benefit them by giving them a better understanding of the role of alternative regulation approaches in supplementing formal law in improving regulatory practices. This understanding can assist them to take significant steps to establish better approaches in enhancing regulation and policies for contemporary corporate business regulation, particularly improved corporate governance through improve accountability for effective disclosure.

17. Informed Consent (If materials are to be distributed in languages other than English, a copy of non-English version and a letter from an independent person verifying accuracy of content is required):

The letter from an independent native speaker verifying accuracy of translation in Bahasa Indonesia is attached as **Appendix C**.

- (a) As part of the informed consent process, it is necessary to provide information to participants prior to obtaining consent. **Please attach a copy of your 'Information to Participants Involved in Research' Letter** [See <http://research.vu.edu.au/hrec.php> for a template] with information about your research that you intend to give to potential participants. This needs to:

- state briefly the aims, procedures involved and the nature of the project, including a clear indication of any potential risks associated with this project;
- if you consider participants to be 'at risk' (see Question 16), state exactly what the researcher will communicate to the participant (this must be stated in clear and concise language) in order to obtain informed consent. This must be in a written format that is given to the participant particularly for this purpose; and
- be written in language which may readily be understood by members of the general public, with explanation of any technical terms.

The information to Participants is attached as **Appendix D** and the translation in Bahasa Indonesia is attached as **Appendix E**.

- (b) **Please attach a copy of your Consent form** [See <http://research.vu.edu.au/hrec.php> for a template consent form.]

The Consent Form is attached as **Appendix F** and the translation in Bahasa Indonesia is attached as **Appendix G**.

- (c) State the process you will use to obtain documentation of informed consent hereunder... (It is essential to clearly detail the steps involved in obtaining informed consent. It is recommended that a procedure or flow chart be attached as an appendix commencing from the recruitment stage to consent taking into consideration issues such as communications and awareness of recruitment, provision for considering participation, etc.)

All interviewees will receive emails in advance comprising an explanatory statement of the research project, a consent letter, together with a request for an appointment. A signed consent form will be obtained before commencing the interviews. The flow chart is attached as **Appendix H**.

18. Confidentiality:

- (a) *Describe the procedures you will adopt to ensure confidentiality.*

All data and information obtained in the interviews will be kept strictly confidential. The principle investigator will be responsible for the security of confidential data. During the course of the research, the transcripts of the interviews will be safely stored by the student researcher in a locked cabinet located at the postgraduate area on level 14, City Flinders Campus, Victoria University. The conversations recorded in the form of audio files will also be retained by the student on a university computer with a password protection system. No identifying information will be used in the thesis. Any publication will be in such a way that the identification of the respondents, or the organisations to which they belong, will not be disclosed.

- (b) *Indicate who will be responsible for the security of confidential data, including consent forms, collected in the course of the research. (Note: the Principal Investigator should be nominated as the responsible person in this section. An alternative person may be nominated with clear justification)*

The principle investigator will be responsible for the security of confidential data, including consent forms.

- (c) *Indicate the period for which the data will be held. (Data must be held for at least 5 years post-publication. Please refer to section 3.2 of the University's Code of Conduct for Research, 1995).*

After the completion of the thesis, hard copies of consent forms will be retained by the principle investigator. Electronic copies of the interview schedule, the transcripts of the interviews, and the conversation recorded in the form of audio files will be stored by the student researcher in a computer with password protection. These documents and all files will be destroyed five years after the completion of the thesis.

- (d) *Name all people who will be granted access to the data and the reason for the access. People identified are required to maintain all aspects of confidentiality.*

No one will have access apart from the supervisor and the research student.

19. Privacy:

- (a) *Does this project involve the use of personal information obtained from a Commonwealth department or agency?*

Yes No

If YES you may need to comply with the requirements of the Privacy Act 1988.

Under the Commonwealth Privacy Act 1988 disclosure of personal information by Commonwealth agencies is not permitted except in a number of circumstances specified in Information Privacy Principle (IPP) II. These include consent by the individual concerned. Where consent has not been given, and where none of the other circumstances specified in IPP II apply, additional guidelines for consideration of the project application and for conduct of research apply. Note that the Act does not apply to publicly available material (such as electoral rolls).

If a Commonwealth agency (for instance, the Australian Bureau of Statistics, Commonwealth Government departments, Australian Electoral Commission, most Repatriation Hospitals) is involved in the collection, storage, security, access, amendment, use or disclosure of personal information for a research project investigators must ensure that the project complies with the requirements of the Act.

20. Conflict of interest

Is there a conflict of interest between any of the researchers and potential participants in the research (i.e due to a relationship between researcher and participant population)?

Yes No

If yes, provide details and ensure that the conflict is identified and addressed in Section 15.

21. Research in other countries.

Is any part of the program to be conducted in another country?

Yes No

If yes, please provide information about any relevant legal or regulatory requirements and any ethical review processes in that other country.

In Indonesia, there are no related legal or regulatory requirements on conducting interviews for this research project. It is also not subject to any other ethical review processes.

22 Is approval required for data collection from other organisations? If so, please provide information of consent process (attach evidence of approval/s)

An approval from another organisation is not required.

23. Collaborative program

Does the program involve collaboration with another institution? Yes No

If YES, please describe the arrangements with the other institution/s for managing the program including, if appropriate, confidentiality, intellectual property, ethics and safety clearances, reporting to appropriate agencies and the dissemination of research findings.

24 Other relevant comments (including information that you deem necessary to inform the HREC that may impact on the project)

25. Application Review Check list

A completed and signed Application Review Check List must be submitted with all applications. A copy may be downloaded from the Victoria University Human research ethics webpage at: <http://research.vu.edu.au/hrec.php>

Important: Attach Application Review Form on cover

Has the Principal Investigator completed and signed the Application Review Form?

Yes No

Is the Application Review Form attached with a hard copy of this application?

Yes X No



DECLARATION FORM

I, the undersigned, have read the current NH&MRC Statement on Human Experimentation and the relevant Supplementary Notes to this Statement, or Code of Ethics for the Australian Psychological Society, (or *) and accept responsibility for the conduct of the experimental and research procedures detailed above in accordance with the principles contained in the Statement and any other condition laid down by the Human Research Ethics Committee.

Principal Investigator (1) Print Name: Prof. Neil Andrews

Signature _____ Date 12 November, 2009

Principal Investigator (2) Print Name: Prof. Andrew Clarke

**Prof. Andrew Clarke
Head of School
Victoria Law School**

Signature _____ Date November, 2009

Associate Investigator ** Print Name: _____

Signature _____ Date _____

VU Sponsor ***

Print Name: _____

Signature _____ Date _____

Student/s Details (if the project is to be undertaken by a student, please provide details):

Name: Jeannie Connie Rotinsulu

Signature _____ Date 12 November, 2009

Co-Investigator Print Name: _____

Signature _____ Date _____

I, the undersigned, understand that the above person/s have read the current NH&MRC Statement on Human Experimentation and the relevant Supplementary Notes to this Statement, or Code of Ethics for the Australian Psychological Society, (or *) and that responsibility is accepted by the above person(s) and by this Department for the conduct of the experimental and research procedures detailed above in accordance with the principles contained in the Statement and any other condition laid down by the University Human Research Ethics Committee and fully support the project undertaken within the Department and Faculty.

Head of Department

Print Name: Professor Andrew Clarke

**Prof. Andrew Clarke
Head of School
Victoria Law School**

Signature _____ Date November, 2009

* If NHMRC Statement or APS Code are not appropriate to your project, please identify your professional code of ethics under which this project would operate.
** The Associate Investigator will assume responsibility for the project in the absence of the Principal Investigator.
*** Applications for research involving participants from individuals who are not staff members of VU and who require access to the cohort of VU staff or students to undertake their research. Such research proposals are to be 'sponsored' by a member of staff, who would be required to take responsibility for all interactions with the University and the HREC in relation to ethics issues and their management.