

# Implementation of the Equity-based Trust in the State-Owned Enterprises in Indonesia

*by* Fx Joko Priyono

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## **Implementation of the Equity-based Trust in the State-Owned Enterprises in Indonesia**

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Reni Anggriani<sup>1</sup>, F.X. Joko Priyono<sup>2</sup>, Nanik Tri Hastuti<sup>3</sup>

**Abstract:**

**Purpose:** State-owned enterprise directors in Indonesia function as management and as the representation of the company based on the principle of fiduciary duty in good faith and trust. The director also function as public official, where mistakes in actions that could harm the state finance can be categorized as corruption. In this role ambiguity, this study seeks to investigate the implementation of the concept of trust in the legal system in Indonesian state-owned enterprises.

**Approach/Methodology/Design:** The research in this study uses the doctrinal method, known as the normative research method, to explain the role of the director in the implementation of trust in a state-owned enterprise.

**Findings:** The results showed that the implementation of trust can be done through equity, in which a person has an object for the benefit of the other party. Equity requires the fulfilment of obligations based on trust, which makes the person who has the object in the law as the legal owner, to the beneficial owner.

**Practical Implications:** The application of the concept of trust in SOE directors as a public official needs to be clarified because state-owned enterprises are state-owned legal entities which must also be financially accountable.

**Originality/value:** The study first analyze the trust in SOEs in relation with the function of Board of directors in carrying out the obligations as stipulated in the LLC Law, and being responsible for the management of the company, with the aim of generating profits with the good corporate governance.

**Keywords:** Trust, fiduciary duty, State-Owned enterprises, Code of Civil Law.

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<sup>1</sup>Diponegoro University, Indonesia, Semarang, Indonesia, and Universitas Muhammadiyah Yogyakarta, Bantul, Yogyakarta, Indonesia, e-mail: [anggriani@umy.ac.id](mailto:anggriani@umy.ac.id)

<sup>2</sup>Diponegoro University, Indonesia, Semarang, Indonesia, e-mail: [fransiskusjoko893@gmail.com](mailto:fransiskusjoko893@gmail.com)

<sup>3</sup>Diponegoro University, Indonesia, Semarang, Indonesia, e-mail: [naniktrihastuti@gmail.com](mailto:naniktrihastuti@gmail.com)

## 1. Introduction

Indonesian economic development emphasizes the inclusion of collectivity, economic democracy and cooperation in encouraging the formation of SOEs and cooperatives in the legal system (Wicaksono, 2008; Sakai, 2014; Weijland, 1999). Implementation of this kind of economic development is dependent on many parties. As Indonesia adheres to a shared ownership-based economic system, the role of the state is influential as a regulator purposively to create welfare and economic order and as an agent of national economic development. One of the efforts of the government or the state in order to develop the national economy is the establishment of SOEs, which are legal entities as regulated in Law No. 19 of 2003 concerning State-Owned Enterprises, herein after referred to as SOE Law, which has a strategic position for improving people's welfare (Trihatmoko, 2019). In order for the government to run well, the state established SOEs to work on the natural wealth for the prosperity of the people (Arta, 2017). Referring to the consideration of the birth of the Law No. 19 of 2003, state-owned enterprises in Indonesia are agents of economic activity in the national economy based on economic democracy. State-owned enterprises have an important role in managing the national economy in order to realize the welfare of society (Bruton *et al.*, 2015; Boardman and Vining, 1989). However, the implementation of the role of state-owned enterprises in the national economy to realize the welfare of society is not optimal (Sutiyono, 2007). To optimize the role of state-owned enterprises, management and supervision of human resource should be done professionally to increase the organizational performance (Mufti *et al.*, 2019). Previous legislation governing state-owned enterprises is no longer in line with the increasingly rapid development of the economy and business world, both nationally and internationally.

Basically, there are two business characteristics of SOEs, namely to carry out public benefits and seek profits that have been regulated in Law No. 19 of 2003. In carrying out their authority in the SOEs, the directors work as representatives of the state. Directors in carrying out their duties and functions as management representing the companies are based on the principle of fiduciary duty (Kartasasmitha, 2020). This has been enacted in the LLC Law on Article 97 stating that management must be carried out by each member of the board of directors in good faith and with full responsibility by the director who receives the trust of the state (Priyono *et al.*, 2018; Sewu, 2019; Tantra, 2018). On the other hand, the director of a state-owned enterprise is a public official, where mistakes in actions that could harm the country can be categorized as corruption (Agustina and Prasetyo, 2019). In the ambiguity of this role, this study seeks to investigate the implementation of the concept of trust in the legal system in Indonesia, especially in SOEs.

The research in this study uses the doctrinal method, known as the normative research method, to explain the role of the director in a state-owned enterprise. The study is divided into several sections. The first part is an introduction, followed by a description of the state-owned enterprises as the backbone of national economic

management. This section outlines the mandate of the national constitution regarding systems and forms of national economic management, and their implementation in the form of legislation that encourages the active role of SOEs as the backbone of the economy. The next section discusses trust in the Indonesian Code of Civil Law that specifies specific forms of conceptualization in the legal system in Indonesia, and the roles that managers may play in operating SOEs. The next section discusses the implementation of the concept of trust in SOEs in legal arrangements in Indonesia.

## 2. State-Owned Enterprises as the Backbone of National Economic Management

Indonesia has the main goal of realizing the welfare of the community as a welfare state type <sup>4</sup> which certainly focuses on the equitable distribution of people's welfare. Therefore the state is required to play an <sup>7</sup> active role in creating equitable public welfare. The national purpose is contained in the fourth paragraph of the opening of the 1945 Constitution which contains the basis of the Pancasila state, which is based on the God, just and civilized humanity, wisdom-and-representation-led unity and popularism, and social justice. The five precepts of Pancasila constitute a unanimity, a unity that is inseparable.

<sup>10</sup> According to fourth paragraph of the Preamble <sup>7</sup> the 1945 Constitution, social justice has been put into one of the basic foundations of the goals and ideals of the state as well as the philosophical basis of the state (*grondslag*) as set out in the fifth precepts of the Pancasila, that is, indeed from the beginning of the founding fathers established Indonesia on a foothold to realize social justice both for its own citizens and the world community (Faiz, 2009). The principle of the welfare state which contains political and economic democratic understanding is unanimously accepted.

Basically, there are two characteristics of SOE businesses, namely to carry out public benefits and seek profits. This is regulated in Law Number 19 of 2003 concerning State-Owned Enterprises, hereinafter referred to as SOE Law, which simplifies the form of SOEs in two. In Indonesia, there are some legal entity forms of SOEs. The first is in the form of Public Companies, known as *Perum* and Limited Companies, known as *Persero*. Public companies are formed by the government to carry out businesses to provide certain goods and services to meet the needs of the community. The form of public company entity is to carry out public benefits. As a business entity, it is endeavored to remain independent and make a profit for the sustainability of its business. Meanwhile, the Limited Liability Company was formed by the government for profit and is fully subject to the provisions of Law Number 40 of 2007 concerning Limited Liability Companies (hereinafter called LLC Act) (Pramagitha and Sukranatha, 2019).

<sup>1</sup> Referring to Article 1 number 2 of the SOE Law, SOEs is a company in the form of a limited liability company whose capital is divided into shares that are all or at least 51% (fifty one percent) of its shares owned by the Republic of Indonesia whose main

purpose is to pursue its profits and refer to article 2 paragraph (1) letter a, it has been stated that one of the objectives of *Persero* SOEs (LLC form) is to pursue profit. SOEs have an important and strategic position, as an instrument to carry out its function as an economic agent. Government through SOEs can provide and produce goods or services needed to realize people's welfare. In addition to this, SOEs can also be a tool for the government to open up sectors that are less attractive to the private sector, but on the one hand the sector is important and relevant for improving people's welfare.

SOEs (LLC) pursuant to Article 11 of Act Number 19 of 2003 concerning State-Owned Enterprises, is subject to the rules of limited liability companies and all provisions and principles that apply to limited liability companies apply as stipulated in Act Number 1 of 1995 concerning Limited Liability Companies. Therefore, state-owned enterprises, in carrying out their business, must obey all regulations that apply to Limited Liability Companies, which have been amended to become Law Number 40 of 2007, concerning Limited Liability Companies.

### 3. Trusts in the Indonesian Code of Civil Law

The concept of trust is virtually unknown in the Indonesian legal system, especially in the Civil Code, but is trying to be applied in the legal system in Indonesia. Subekti (1995) argues the similarity between trust and legal institutions in force in Indonesia (Sunarto, 1994). Article 1317 of the Civil Code states that it is also permissible to ask for a promise to be made in the interests of a third party, if a promise is made, made by a person for himself, or a gift made to another person, contains a promise like that.

An agreement for a third party in this Article is called *derden beding* (a promise for the interests of a third party), where the *beding* for the third party is in addition to a principal agreement made by two other people, whereas in the case of a trust the agreement is merely made to create that trust. In its development, the concept of trust has been adopted as a trust given by the state to SOEs to become a state representative that is manifested in a SOE company to help develop from the economy. Referring to Article 1 number 2 of the SOE Law, a SOE in the form of a limited liability company whose capital is divided into shares that are wholly or at least 51 percent of its shares owned by the Republic of Indonesia whose main purpose is to pursue profit.

Trust is a right that can be upheld only in equity, for the beneficial enjoyment of property owned by someone else who has a legal right. Trust also refers to the interests of property held by one person as trustee at the request of another person for the benefit of a third party as the beneficiary. For trust to be valid, it must include certain properties, reflect settler interests, and be made for legal purposes (Gardner, 1999). Accordingly, trust is a concept of separation of ownership between the legal owner and the beneficial owner of the object in form of beneficiary owner. This trust occurs if the party who initially controls and owns an object or settlor then surrenders the ownership of the object to another party in form of trustee for the benefit of a third party as beneficiary, even though the trustee becomes the legal owner of the object,

the trustee is only in the management's position, manager and storage of the item. Meanwhile, benefits or uses must be given to third parties as beneficiary (Prasetio, 2014; Johnson, 2005; Sharfman, 2017; Gurrea-Martínez, 2018; Engert and Goldlücke, 2017; ; Onyshchuk *et al.*, 2020).

The legal vacuum in causing SOE directors in making investments or transactions in order to obtain revenue and growth of the company is faced with a dilemmatic situation that causes doubts in decision making. Referring to Article 11 of the SOE Law, Indonesian SOE in carrying out the companies, are subject to the LLC law which in this case is Law No. 40 of 2007 concerning Limited Liability Companies. State intervention is manifested in the form of arrangements and directions from the state towards community life, so that the movement of people's lives will be in line with the development carried out by the state for the realization of community welfare and social justice for the entire Indonesian nation, and one of the functions of the state is to arrange juridical instruments in order to make arrangements, services, and protections for the community, by making normative rules about how the government is run to carry out its functions, so that in the administration of government there is a relationship between the government and the community, and the quality of government and community relations can be used as a measure against governmental administration.

The mandate of Article 33 of the 1945 Constitution of the Republic of Indonesia resulted in the construction of a new constitutional law in form of economic democracy. The national economy which is held in the name of economic democracy has a number of basic principles, one of which is fair efficiency. Fair efficiency is a cornerstone of good corporate governance ethics that emphasizes transparency and mediation, when the state or government makes efforts to transfer productive assets (Choirie, 2015). The national economy is contained in Article 33 and after the amendment, Article 33 paragraph (4) of the 1945 Constitution confirms that the national economy is based on economic democracy with the principles of togetherness, efficiency, fairness, sustainability, environmental awareness, independence, and by maintaining balance progress and national economic unity (Mu'allifin, 2016).

#### **4. Implementation of Trust through Good Governance of the Role of Directors**

In the implementation of the concept of trust, it is necessary to analyze the role of directors as fiduciary duty. This duty is an obligation stipulated by law for someone who utilizes another person, where one's personal interests are managed by another person, which is only a temporary boss-subordinate relationship (Agustina and Prasetyo, 2019). Responsibility is a result of mistakes which has become common law that is commonly used (Pound, 1982). The doctrine of responsibility for error is solely rooted in the level of equity and natural law, when considered the same, what is permitted by decency and what is permitted by law and means that a person must be

responsible for damages caused by his conduct which is despicable according to decency. The obligation of directors as public officials must run the company as stipulated in the SOE Law, and because the assets of SOEs are state assets, which must be managed in an orderly manner, efficient, economical, effective, transparent and responsible with due regard for a sense of justice. Such propriety is based on Article 3 paragraph (1) of Law No. 17 of 2003 concerning State Finance. On the other hand, the board of directors must also carry out the obligations as stipulated in the LLC Law, and be responsible for the management of the company, with the aim of generating profits with the good corporate governance. SOE management in Indonesia shows that there is a legal vacuum, with no conceptual or normative arrangements regarding how the SOE directors carry out their duties or authority as directors who are also public officials. Even though the LLC Law also regulates corporate governance which is good, the concept is too normative, unclear and unregulated. The legal vacuum has made the directors can be charged with acts of corruption (Kamal, 2010).

By applying trust through equity, a person has an object for the benefit of the other party. In the conception of general law, this is called the owner. Equity requires the fulfilment of obligations based on trust, which makes the person who has the object in the law as the legal owner, to the party as the benefit of the object must be given to the beneficial owner. The application of the concept of trust in SOE directors as a public official needs to be clarified because state-owned enterprises are state-owned legal entities which must also be financially accountable, and their management is overseen by the Financial Supervisory Agency. On the other hand, directors of state-owned SOEs are subject to LLC Law applies the state-owned companies as business entity. The directors of the company have responsibilities that are not limited to dishonesty or mismanagement, but including negligence even if only a small mistake, which can cause state losses. Financial losses in state/regional finance are shortages of money, securities, and real and definite amounts as a result of intentional or negligent unlawful acts, as stipulated in Article 1 number 15 of Law No. 15 of 2006 concerning the Supreme Audit Board. The losses can form in any actions that are considered to have caused a loss to the state are not regulated in detail so as to cause many different interpretations from law enforcers and this is a legal vacuum in the difference in understanding of state losses that have not been clearly regulated. In practice, it also has made the SOE directors are not brave enough in making decisions which, by doing so, also makes SOEs undeveloped as aspired by the SOE Law, which is to pursue profit (Lyston, 2018).

Aquinas (1997) states that a person cannot be said to be a good leader unless he is good because he has moral virtues (Sandur, 2019). The decisions taken by the directors must have ethics. Public ethics is a reflection of standards and norms that determine goodness, and rightness behavior, actions and decisions to direct public policies in the context of public service responsibilities (Haryatmoko, 2016). This means that in making a decision or policy must be weighed good and bad for the company, but normative rules about the decisions that must be taken by the directors

based on the principle of fiduciary duty and trust do not exist, because the directors of state-owned enterprises stand on two legs, namely on one side subject to the LLC Law. On the other hand, the directors also function as public officials. Directors in carrying out their duties in the construction and investment SOEs sector. Implementation of the concept of trust in SOEs sector is carried out or applied in internal regulations in the form of a code of ethics and guidelines for good corporate governance, which are binding for the directors and employees as well as related third parties, and this is used as a reference or guidance for the directors in taking decision, or company policy.

## 5. Conclusion

The mandate of Article 33 of the 1945 Constitution of the Republic of Indonesia resulted in the construction of a new constitutional law, in form of economic democracy. Referring to the consideration of the birth of the Law on State-Owned Enterprises in Indonesia, State-Owned Enterprises are agents of economic activity in the national economy based on economic democracy. Business characteristics of SOEs is to carry out public benefits as well as to seek profits. In carrying out their authority in the SOEs, the directors work as representatives of the state. Directors in carrying out their duties and functions as management and as a representation of the company are based on the principle of fiduciary duty as a means to implement trust. Trust hence is a right that can be upheld only in equity, for the beneficial enjoyment of property owned by someone else who has a legal right.

By applying trust through equity, a person has an object for the benefit of the other party. In the conception of general law, this is called the owner. Equity requires the fulfilment of obligations based on trust, which makes the person who has the object in the law as the legal owner, to the party, the benefit of the object must be given to the beneficial owner. The application of the concept of trust in SOE directors as a public official needs to be clarified because state-owned enterprises are state-owned legal entities which must also be financially accountable. Finally, although the Directors must also make decisions in the interests of the company, SOEs as a state companies and its directors as public officials must comply with all regulations that apply to public officials as a means of good governance.

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