FOURTH EDITION 2015

INTERNATIONAL INSOLVENCY

Group insolvency and directors' duties

A GLOBAL GUIDE FROM PRACTICAL LAW

The publication of the fourth edition of *International Insolvency: Group Insolvency and Directors' Duties* (formerly *International Insolvency, Jurisdictional Comparison*) continues to expand its jurisdictional scope as well as its analysis on directors' and officers' duties in the "zone of insolvency." The recent global financial crisis, which resulted in a number of international companies becoming financially distressed and seeking relief through insolvency filings, has highlighted deficiencies in the current international law and various domestic legislative structures in addressing the multitude of cross-border issues arising in the administration of a distressed global company.

With commentary from leading lawyers addressing complex cross-border insolvency issues and rescue provisions, this fourth edition of *International Insolvency: Group Insolvency and Directors' Duties* gives law firms and corporate counsel an insight into the key insolvency issues across numerous jurisdictions. It particularly focuses on recently enacted laws, initiatives or rulings in various countries that touch on the insolvency of corporate groups and the duties directors and officers owe to creditors and other entities in the "zone of insolvency."

General Editor: J William Boone
JAMES-BATES-BRANNAN-GROOVER-LLP

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International Insolvency

Group insolvency and directors' duties

Fourth Edition

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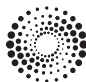

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Preface

J William Boone James-Bates-Brannan-Groover-LLP

Effective, uniform, and accessible insolvency laws are important elements of a healthy global legal system and commerce. The creation of uniform insolvency law has been the focus of the United Nations Committee on International Trade Law (UNCITRAL) Working Group V (Insolvency Law) which has recognised the need for uniform insolvency laws for the reorganisation and liquidation of business entities. Due to the divergent insolvency regimes among many countries, the differences in civil and common law countries, the desire of governments to protect their turf, and simple inertia, it will most likely be many years before we see a truly internationally adopted and universally accepted uniform insolvency law. Therefore, in the interim, it is important for both practitioners and leaders of international corporations to be familiar with (or at least have access to) information regarding the insolvency laws of the major jurisdictions surveyed herein. The varying answers to the questions posed in this book are indicative of the importance of a resource of its type. We sincerely hope and believe that this book provides answers to many of the questions that will undoubtedly face these practitioners and leaders.

Since the publication of the third edition, there has been a continued emphasis on the obligations of directors and officers of a company that is in the period approaching insolvency, that is the zone of insolvency. Indeed, the topic has continued to be a point of interest during the meetings of the UNCITRAL Working Group V (Insolvency Law). Accordingly, this fourth edition has continued the focus on director and officer liability in the surveyed jurisdictions, including their duties to various interest holders (such as creditors, employees and shareholders), their liability for misappropriating or undervaluing corporate assets, whether a business can continue to operate if they are aware that the company is insolvent, whether their duties change when the company becomes insolvent, whether civil or criminal liability may result from a breach of their duties, whether director and officer liability insurance is available, and related topics. The fourth edition has also included additional jurisdictions and added questions which provide a general overview of the insolvency scheme in each country before delving into the specific issues arising from directors' and officers' obligations in the zone of insolvency. I am pleased to also note that the fourth edition is now also available in an online and a printed hardback formats. The online version is part of the Practical Law "Global Guides".

I am deeply grateful to the authors of each chapter of this volume for contributing their time, talent, and professional energies to this project. I am also thankful for the wonderful staff of Thomson Reuters, including Nicola Pender, Katie Hillman, Katie Burrington, Emily Kyriacou, and Dawn

McGovern, who, through the years, have helped me take this project to an international treatise, grow it in scope, and who continue to provide their invaluable support in preparing and editing this fourth edition.

I am confident the reader will find it both useful and informative. I look forward to your comments to assist in expanding future editions, as the international legal and financial community works closely together to further advance this area of law. I am excited to be one of the pioneers in the international insolvency practice, who through diligent and continued efforts and co-operation, will ultimately lead to a widely adopted uniform international insolvency law.

April 2015

Foreword

Christopher J Redmond Husch Blackwell LLP

In the aftermath of the global financial crisis of 2008, the international community clearly recognised the critical role that effective insolvency proceedings contribute to international cross-border financial stability. The explosion of global trade during the last century has elevated the drive to harmonise cross-border insolvency proceedings to the forefront of global harmonisation efforts. The initial attempts at cross-border insolvency harmonisation first emerged with the development of the Concordat by the International Bar Association. The Concordat was an attempt to achieve voluntary co-operation between states with regard to cross-border insolvency proceedings. The Concordat was a catalyst to initiate cross-border co-ordination among states, but advocates quickly realised that a voluntary system was not the solution to the growing problems of the intersection between insolvency law and international trade. Shortly after, the European Union (EU) began work on the development of the European Insolvency Regulations and following this, the United Nations Committee on International Trade Law (UNCITRAL) promulgated the UNCITRAL Model Law on Cross-Border Insolvency with Guide to Enactment and Interpretation.

The creation of both of these substantial works on cross-border insolvency law occurred over a very short period of time, and clearly demonstrated the need and desire for co-ordinated cross-border insolvency proceedings. Previously, the initiation of cross-border insolvency proceedings by companies operating in multiple jurisdictions resulted in duplication of administrative expenses, multiple proceedings (that could reach divergent results), a lack of uniformity and consistency in the issuance of distribution to creditors and the general inability to reorganise. This often led to liquidation and the cessation of business activities, creating a loss of jobs and substantial losses to creditors and interested parties.

Judges, practitioners and academics recognised that co-ordinated cross-border insolvency proceedings would need to be procedural and not substantive at the outset to be accepted and implemented by states.

In 1995 after an initial colloquium sponsored by INSOL, the International Bar Association Committee J and UNCITRAL, strong support emerged to develop an effective mechanism for dealing with cross-border insolvency proceedings in order to promote the objectives of co-operation between courts and competent authorities of states. This was to provide for greater legal certainty in trade and commerce, a fair and efficient administration of cross-border insolvency proceedings to protect the interests of creditors and other parties (including the debtor), and to provide for the further preservation of the value of the debtor's assets and the facilitation of the rescue of financially distressed businesses.

After the issuance of a mandate by the UNCITRAL Commission, in the short two-year period between 1995 and 1997, the UNCITRAL Model Law on Cross-Border Insolvency with Guide to Enactment and Interpretation was promulgated and adopted by the General Assembly of the United Nations. Currently over twenty states have enacted and adopted the UNCITRAL Model Law, including Canada, Japan, Mexico, Colombia, the US and the UK, among others. A substantial number of other states are either in the process of adopting or considering adopting the Model Law as part of their overall insolvency law.

Considering the success of the creation of the Model Law on Cross-Border Insolvency, UNCITRAL established an exploratory meeting in December of 1999 to determine if there was an interest to develop a legislative guide on insolvency laws for the reorganisation and liquidation of business entities. Following an exploratory meeting (where a comprehensive statement, key objectives and core features were developed) the UNCITRAL Commission issued a mandate to begin work in July 2001 to prepare a legislative guide on insolvency law. Between 2001 and 2004, UNCITRAL Working Group V (Insolvency Law) worked on and completed a Legislative Guide on Insolvency Law. The Legislative Guide on Insolvency Law is currently viewed as the international standard for insolvency law reform by states in addressing both domestic and cross-border insolvency proceedings.

In recognising additional needs in the area of cross-border insolvency law, the UNCITRAL Commission issued a mandate for Working Group V to undertake further work on co-ordination and co-operation in cross-border insolvency cases with an emphasis on the use of negotiation of cross-border insolvency agreements. In 2009, the UNCITRAL Practice Guide on Cross-Border Insolvency Co-operation was approved by the UNCITRAL Commission and subsequently endorsed and adopted by the General Assembly of the United Nations.

With the approval of the UNCITRAL Commission, additional work to the Legislative Guide on Insolvency Law was authorised, which resulted in Part III: The Treatment of Enterprise Groups in Insolvency and Part IV: Directors' Obligations in the Period Approaching Insolvency that were completed in 2012 and 2013 respectively.

While the Model Law on Cross-Border Insolvency addressed a single company operating in multiple jurisdictions, UNCITRAL Working Group V (Insolvency Law), pursuant to mandates granted by the UNCITRAL Commission, are now addressing the issue of the development of a model law on enterprise groups, that is, addressing groups of companies operating in different jurisdictions to achieve an overall resolution through co-ordinated insolvency proceedings. Further work mandated by the UNCITRAL Commission is to develop a model law on the recognition of cross-border related insolvency judgments, both projects are now ongoing.

The EU has recently undertaken a complete review and analysis of the European Insolvency Regulations and is in the process of promulgating revisions of insolvency laws and procedure within the EU.

To put this in perspective, the authors of the *4th Edition of International*

insolvency: Group insolvency and directors' duties have provided an excellent update with regard to the status of insolvency reform and revisions in their respective jurisdictions.

When the work, both which has been completed and is ongoing, of UNCITRAL and the European Commission, among others, is compared to the excellent detail and information provided by the chapter authors from the respective jurisdictions, then and only then is the scope and extent of global insolvency reform appreciated.

The *4th Edition of International insolvency: Group insolvency and directors' duties* provides an up-to-date analytical view of the insolvency law in the respective jurisdictions to provide the reader with a comprehensive and thorough analysis of the insolvency law in those jurisdictions.

The respective chapter authors have provided an excellent explanation which is readily understandable to the reader and provides an excellent resource for the insolvency professional or parties who are intimately involved with the insolvency process on a cross-jurisdictional basis.

Indonesia

Ali Budiardjo, Nugroho, Reksodiputro
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GENERAL OVERVIEW OF INSOLVENCY PROCEEDINGS

1. What are the available out-of-court and court-sanctioned insolvency proceedings?

Out-of-court insolvency proceedings

Indonesian law does not formally regulate out-of-court insolvency proceedings, but they are not uncommon and have in the past taken the form of pre-packed out-of-court agreements that are sanctioned by a court approval.

Court-sanctioned insolvency proceedings

The court-sanctioned insolvency proceedings are governed by Law No. 37 of 2004 on Bankruptcy and Suspension of Payments (Bankruptcy Law). There are two types of court-sanctioned insolvency proceedings applicable to Indonesian individuals, limited liability companies and limited partnerships:

- **Bankruptcy proceedings.** Bankruptcy proceedings aim at liquidation (*see Question 2, Liquidation of assets*).
- **Suspension of payments proceedings.** Suspension of payment proceedings aim at continuation of the business (*see Question 2, Restructuring*).

The two types of proceedings are not principally opposed and can be used as needed by the situation at hand.

There is also a proceeding recognised by Indonesian law that is not technically an insolvency proceeding: dissolution and liquidation under Law No. 40 of 2007 concerning Limited Liability Companies (Company Law) (*see Question 2, Liquidation of assets*).

Definition of insolvency

Insolvency as used in the Bankruptcy Law has a meaning that differs from that in many other legal systems. It does not constitute the test for bankruptcy declaration, but refers to the specific concept of “the state of being insolvent at law”, which occurs when:

- No composition plan is submitted in the creditors’ meeting for the verification of claims.
- The composition plan is rejected in the voting process by the creditors.
- The composition plan is approved by the creditors but not ratified by the Commercial Court.

- No composition plan is ratified by the Commercial Court during the suspension of payments period (for bankruptcy proceedings that continued from the suspension of payments proceedings).
- The final and binding ratified composition plan is nullified by the Commercial Court due to the fact that the debtor is negligent in performing its obligations under the ratified composition plan.
-

2. What are the proceedings for a liquidation of assets and those allowing for a restructuring of the debtor's operations and debts?

Liquidation of assets

Bankruptcy proceedings. Bankruptcy proceedings apply to individuals, limited liability companies and limited partnerships. They aim at liquidation, but are often used for reorganisation of business by way of restart (if a composition plan is accepted by the creditors under voting mechanism and ratified by the court). The affairs of a bankrupt debtor are handled by a court-appointed receiver (*see Question 3, Bankruptcy proceedings*).

Dissolution and liquidation proceedings. This is a company/shareholder driven irreversible process that is used only for limited liability companies that does not cater for the possibility of the debtor's restructuring and has no creditor vote (*see Question 3, Dissolution and liquidation proceedings*).

Restructuring

Suspension of payment proceedings. Suspension of payment proceedings aim at continuation of the business but may result in liquidation (if the composition plan is rejected by the creditors under a voting mechanism or fails to secure the court's ratification). The affairs of a corporate debtor are handled jointly by the director(s) of the company and a court appointed administrator (*see Question 3, Suspension of payment proceedings*).

Pre-packed out-of-court agreements. These are agreements between the debtor and its creditors, which are sanctioned by a court approval.

3. What are the general requirements for commencing insolvency proceedings?

Bankruptcy proceedings

The Bankruptcy Law provides that a bankruptcy petition may be filed by:

- One or more creditors.
- The debtor.
- The Public Prosecutor, if it is in the public interest.

The bankruptcy and suspension of payments proceedings of certain debtors can only be filed for by specified institutions (*see Question 4*).

The debtor must be declared bankrupt once both of the following tests for bankruptcy are satisfied in the bankruptcy proceedings before the Commercial Court (bankruptcy requirements):

- The debtor has at least two creditors.
- The debtor has failed to pay at least one of its debts that is due and payable.

The Commercial Court must make a decision on the bankruptcy petition

within 60 days after the petition has been filed. However, in practice the period that the Commercial Court takes in deciding on a bankruptcy petition varies between 30 and 50 calendar days as of the registration of the relevant bankruptcy petition, depending on the complexities of the case and the availability of the parties. The decision can be appealed to the Supreme Court in cassation not later than eight days from the court's decision (cassation filing period). The Commercial Court Registrar must deliver the cassation petition dossiers to the Supreme Court within 14 days from the registration of the petition. Within 60 days after the cassation petition has been received by the Supreme Court, the Supreme Court must decide whether to affirm or overturn the Commercial Court decision.

In limited cases, a case review (*peninjauan kembali*) appeal can be made against a final and binding decision in the form of:

- The Commercial Court's decision that is not appealed within the cassation filing period.
- The Supreme Court's decision in cassation.

A case review may only be filed to the Supreme Court based on the following grounds:

- When there is any decisive evidence discovered after the date of the final and binding decision, which at the time of the proceedings at the Commercial Court/Supreme Court level in cassation had not yet been found. In this case, the case review petition can be filed within 180 days from the date when the relevant court's decision becomes final and binding.
- If there is an obvious mistake or error made by the judges in the relevant decision. In this case, the case review petition can be filed within 30 days as of the date when the relevant court's decision becomes final and binding.

The Commercial Court Registrar must deliver the case review petition to the Supreme Court Registrar within two days as of the date the case review petition is registered. The Supreme Court must render a decision within 30 days as of the date the case review petition is received by the Supreme Court Registrar.

Suspension of payments proceedings

A debtor or his creditor(s) may submit a petition for the court-sanctioned suspension of the payment obligations (*Chapter III, Bankruptcy Law*). The petition includes an offer of payment of all or part of the debt to the secured and unsecured creditors. The objective is to give the debtor company time to reorganise in the hope that it survives as a going concern and ultimately satisfies the creditors' claims. The suspension of payments starts after the Commercial Court approves the request for suspension of payments.

The procedure of suspension of payments may be filed for by persons and companies that have their domicile or place of business in Indonesia. In the event that the petition is filed by the debtor, it can be filed:

- At the debtor's initiative.
- As a defence against a bankruptcy petition filed against the debtor.

A debtor who cannot, or foresees that he will not, be able to pay his debts

can apply for suspension of payments for the general purpose of submitting a composition plan. In practice, bankruptcy requirements must be satisfied for the Commercial Court to grant the suspension of payments petition (*see above, Bankruptcy proceedings*).

A draft composition plan can be attached to the suspension of payment petition, but it is not mandatory. The submission of the petition for the suspension of payments is recorded in a general register maintained by the Commercial Court registrar. The register is open to public inspection, which means any person can take notice of the petition as from the date of its submission.

The Commercial Court must make a decision on the suspension of payments petition either:

- Three days from the filing of voluntary suspension of payments petition (filed by the debtor itself).
- 20 days from the filing of involuntary suspension of payments petition (filed by the debtor's creditor(s)).
-

Dissolution and liquidation procedures

A company may be dissolved as a result of one or more of the following (Company Law):

- A resolution of the general meeting of shareholders.
- The duration of the company as stipulated in the articles of association has expired.
- A court decision.
- On termination of bankruptcy proceedings by a final and binding decision of the commercial court due to the bankruptcy estate of the company not having sufficient assets to cover the cost of the bankruptcy.
- The bankruptcy estate of the bankrupt company is declared to be in a state of insolvency as governed by the Bankruptcy Law.
- The company's business permit has been revoked, if liquidation is required by applicable laws and regulations.

Where dissolution of a company occurs:

- It must be followed by liquidation of its assets conducted by a liquidator or receiver (in a bankruptcy situation).
- The company cannot commit any legal act, unless it is required to wind up all affairs of the company in the framework of a liquidation process.

If this provision is violated, the members of the board of directors, the board of commissioners and the company are jointly and severally liable for any committed actions. The board of directors acts as liquidator if:

- The dissolution is based on the following grounds:
    - a resolution of the general meeting of shareholders;
    - the duration of the company as stipulated in the articles of association has expired; or
    - a court decision.
- The general meeting of shareholders does not appoint a liquidator.

The appointment of a liquidator does not cause the members of the board of directors and the board of commissioners to be dismissed, unless the

general meeting of shareholders determines otherwise.

4. Are there any restrictions on who, or what type of entity, can commence insolvency proceedings?

The Bankruptcy Law imposes restrictions on who or what type of entity can commence an insolvency proceeding. The bankruptcy and suspension of payments proceedings of certain debtors can only be filed for by specified institutions, for example:

- Banks: the Bank of Indonesia (the Indonesian central bank).
- Securities companies: Otoritas Jasa Keuangan (OJK) (the Financial Services Authority, previously known as Badan Pengawas Pasar Modal (BAPEPAM), or the Indonesian Capital Markets Supervisory Board).
- Insurance and reinsurance companies, pension funds and state-owned companies operating for the public interest: the Minister of Finance.

DOMESTIC FAMILY OF COMPANIES

5. Are joint proceedings available in insolvency or bankruptcy proceedings that are commenced for the family of companies?

Procedure

The concept of a family or group of families is not considered by the Bankruptcy Law or the Company Law. The Bankruptcy Law does not provide for joint proceedings for a family of companies. This means that there can be no single court file, single list of creditors or single notice list for the combined members of the family. The case for each member of the family must proceed separately and there is no practical acknowledgment of the related proceedings. It is not prohibited, although not common, to file a single request in which the bankruptcy of two or more related parties is petitioned, this will lead to a separate decision for each petitioned party.

Location

The bankruptcy filing must be made in the Commercial Court competent for the region in which the individual member of the family is established according to its documentation (*Article 3(1) and 3(5), Bankruptcy Law*). Whether it undertakes activities elsewhere in Indonesia, or whether an affiliate may have commenced bankruptcy proceedings in another Commercial Court is irrelevant.

6. Must all members of the corporate family proceed under the same type of bankruptcy or insolvency proceeding?

There is a total separation between the insolvency procedures of each company (*see Question 4*). One member of the corporate family may subject itself, or be subjected to, bankruptcy procedures, while another is subject to suspension of payments procedures.

7. Can a single administrator/trustee/receiver administer the assets and the liabilities of the entire corporate family?

Administration of the entire corporate family is not allowed because, under the Bankruptcy Law, a receiver in bankruptcy proceedings is authorised to

manage the estate of a bankrupt company only (not the estate of the entire corporate family). The administrator of a company under suspension of payments is, together with the management of the respective company, authorised to manage the estate of that company only (*Bankruptcy Law*) (*see Question 4*). It is possible for the same person to be appointed as receiver or administrator in the bankruptcy or suspension of payments of more than one company, regardless of whether the companies belong to a family, provided he satisfies the formal requirements for eligibility.

The receiver or the administrator must (*Article 15(3), Bankruptcy Law*):

- Be independent.
- Not have a conflict of interest with the bankrupt company (or the company under suspension of payments) or any of its creditors.
- Not be handling more than three bankruptcies or suspensions of payments simultaneously.
- Have passed a professional qualification examination and be registered at the Department of Law and Human Rights.

The Indonesian Bankruptcy Law is silent on whether the appointment of the same curator/receiver for more than one member of a corporate family would constitute a conflict of interest.

The requirement of independence and no conflict of interest of the receiver or administrator mean that the continuation of the receiver/curator's existence is not dependent on the debtor or the creditors, and the curator does not have the same economic interests as those of the debtor or the creditors.

8. Is a court hearing required to determine whether administration by a single party is appropriate and, if so, must notice be given to creditors?

The Bankruptcy Law does not specify whether a court hearing is required to determine whether administration by a single party is appropriate. Although one person cannot administer the assets and liabilities of the entire corporate family, it may be possible for a single receiver to act for multiple companies. This is subject to Article 15(3) of the Bankruptcy Law (*see Question 7*).

The general procedure for appointment is that the petitioner can propose a person to be appointed as receiver in the petition. In ruling on the proposal, the court checks whether the eligibility requirements are complied with. At this stage the views of creditors other than the petitioner are normally not considered, although other creditors may attempt to intervene (for example, raising conflict of interest). In practice, the debtor may also propose a receiver to be appointed in response to the receiver nomination made by the petitioner.

If the petitioner does not propose a receiver, the Orphans' Chamber (*Balai Harta Peninggalan*) is appointed. The Orphans' Chamber is a special agency of the Ministry of Law and Human Rights (so named as it is also responsible for matters of custodial care) and its role is the same as the one of a receiver. The Orphans' Chamber acts through its representative offices located in the jurisdiction of the court that declares the debtor bankrupt.

There is no separate hearing to appoint the Orphans' Chamber. No notice

is given to creditors.

9. Can other professionals work for the entire corporate family?

Joint representation by other professionals is not allowed. Other professionals can work for more than one company in a family of companies. However, they can be bound by the relevant profession's code of ethics, which can include conflict of interest rule as well.

10. If the law does not permit a single administrator/trustee/receiver, are there provisions allowing different administrators to co-ordinate with each other so that values of assets can be maximised?

The Bankruptcy Law provides for an initial appointment of a receiver responding to the nomination made in the bankruptcy petition. However, the court may, in the course of the bankruptcy, based on the request from various parties involved in the bankruptcy proceedings, appoint additional receivers, especially if the case is considered complex. Currently, in practice, the nomination of a receiver in a bankruptcy petition contains more than one receiver leading to an appointment of more than one receiver in one bankruptcy proceedings. Where two or more receivers are appointed, they decide by majority vote. If the vote is tied, the supervisory judge decides.

11. Does your jurisdiction encourage or discourage overlapping boards or management teams for separate members of a corporate family?

The concept of a family or group of companies is not considered in the Bankruptcy Law or the Company Law and the law neither encourages nor discourages overlapping boards (*see Question 7*). Certain provisions of the Indonesian Competition Law prohibit the overlapping of boards or management teams for separate members of a corporate family if it creates unfair competition.

12. How are directors of a parent company treated if they are not directors of the subsidiary but manage the affairs of the subsidiary?

Only the person formally appointed as director of the subsidiary in accordance with the articles of association is qualified to act as a director of the subsidiary. A director of the parent company cannot represent the subsidiary company unless simultaneously serving as an appointed director of the subsidiary. In such case, his duties and liabilities are distinct in each function. Even if a director of the parent company serves as the appointed director of the subsidiary, according to the Company Law, he is unable to represent either the parent company or the subsidiary company if he has a conflict of interest with the company that he is representing (especially arising from his dual directorship position in the parent company and the subsidiary).

If the director of a parent company has not been formally appointed, but is effectively in charge of a subsidiary company's affairs based on a power of attorney to the extent that the actions are covered within the power of attorney and not illegal, he will not be liable for the subsidiary company's management.

13. To whom do directors or officers owe duties while the company is solvent? What is the nature of the duties?

General corporate governance

For general corporate governance and directors duties, see *Question 28*.

Directors will not be personally liable to third parties for acts performed by them, provided that such acts are within the limits of their competence as defined in the articles of association, the resolutions of the general meeting of shareholders, and the law. Directors may be held liable toward third parties, jointly and severally, for tort if they act beyond the limits of their competence. Pursuant to the articles 1365 and 1366 of the Indonesian Civil Code, members of the board of directors will become personally liable towards third parties if, for example, the board of directors contracts an obligation on behalf of the company, while aware or when they ought to be aware that the company is in no position to fulfil this obligation. In such a case, the board of directors can be liable for the damage suffered by the third party as a result of the transaction. If a director acts within his authority under the articles of association or as invested by the shareholders resolutions and this act is later deemed to be a tort, the director concerned will not be personally liable, but the liability will rest with the company.

14. Do the duties or responsibilities of the officers or directors of a family of companies change when the companies become insolvent?

The duties of the officers or directors do not change before a court judgment pronouncing bankruptcy or suspension of payments, or as a result of balance sheet or profit or loss developments. When the judgment is passed, the directors cease to have power (in bankruptcy) or share their power with an administrator (in suspension of payments). For details of directors' duties, see *Question 28*.

Directors of a company are jointly and severally liable for the losses suffered if, as a result of bankruptcy, claims cannot be paid because of a fault or the negligence of the board of directors. A director cannot be held liable for those losses if they can establish that:

- The losses were not due to their fault or negligence.
- They carried out the management in good faith and with prudence in the interests of, and in accordance with, the purpose and objectives of the company.
- They raise no conflict of interest, whether directly or indirectly, in the acts of management that result in losses.
- They have taken preventive measures against the arising or continuation of losses.

15. How are competing fiduciary duties addressed where officers and directors of various company family members overlap and conflicts of interest between the family members exist?

The Company Law prohibits officers and directors from acting for and on behalf of the company that they are representing if they have a conflict of interest with the company that they are representing.

16. Are the rules regarding members of the corporate family transferring assets to one another different when the members are insolvent?

Non-bankruptcy situation

Any creditor can request the nullification of a preferential transfer transaction conducted by the debtor, if that transaction is considered detrimental to the creditors (Civil Code Preferential Transfer) *(Articles 1341 and 1454, Civil Code*). To nullify a Civil Code Preferential Transfer the creditor must prove the following:

- The debtor was not obligated by contract (existing obligation) or by law to perform the preferential transfer.
- The preferential transfer has prejudiced the creditors' interests.
- The debtor and the third party had knowledge that the preferential transfer prejudiced the creditors' interests.

Creditors can make the claim within five years, from the date when the creditor became aware that the debtor and the third party realised that the preferential transfer prejudiced the creditors' interests. Although in theory proving the debtor's and the third party's awareness of the detrimental action is possible, successful preferential transfer claims by creditors under Article 1341 are extremely rare in practice and are heavily based on factual evidence that the directors and third party had knowledge.

Bankruptcy situation

Transferring assets among corporate family members is not generally restricted but, under certain circumstances, can amount to preferential treatment. Certain transactions favouring one creditor over the other creditors, entered into at the time when the bankrupt foresaw the bankruptcy, can be set aside under *Actio Pauliana* principles under Articles 30, 41 and 42 of the Bankruptcy Law. To set aside a pre-bankruptcy transaction it must be shown that:

- The transaction was made before the bankruptcy declaration.
- The transaction was voluntary, that is there was no contractual obligation to make the transaction. Voluntary transactions include, for example:
  - the granting of security to one particular creditor;
  - the payment of a debt which is not yet due and payable; and
  - the sale of an asset against non-cash payment or with set-off of the purchase price against a debt.
- The transaction prejudiced the interests of creditors, that is the condition of the bankrupt estate would have been better off had the transaction not been entered into. Examples include a sale of goods below their fair market value and transactions resulting in the increase of the debtor's liabilities, such as the granting of a guarantee or other form of security by a subsidiary for the debt of its parent company.
- The debtor and the contracting party had knowledge of the prejudice to other creditors. Generally, knowledge is deemed to exist in the case of the following categories of transactions performed less than one year before the bankruptcy:
  - transactions in which the value received by the debtor is

substantially less than the value of the asset that was alienated;
- payments of a debt that is not yet due and payable, or the granting of security for such debts;
- transactions between the debtor and related parties (relatives or companies controlled by relatives, insiders and legal entities belonging to the same group);
- donations.

Even if the transaction was a payment of a debt that was due and payable, it can be annulled if it is shown that either:

- The recipient of the payment knew that the bankruptcy had, at the time of receipt, been petitioned for.
- The payment was the result of consultation between the debtor and the creditor with the intention of preferring that creditor over other creditors. It is generally believed that this requirement is only fulfilled when a secret agreement between the parties is proven.
-

Cash sweep procedures

Cash sweep procedures, that is, where cash from all subsidiaries are redistributed among the family members to pay bills, would probably be considered *ultra vires* unless the cash sweep can be proven to be in the corporate interest of the subsidiary whose cash is swept. This would normally only be the case if the cash swept is not disproportionate to the bills being paid or the subsidiary received another fair value consideration for allowing its cash to be swept.

17. How are claims of one member of a corporate family against other members of the corporate family treated?

There are no statutory provisions relating to corporate group or family relationships, and therefore in principle such claims are not treated differently from claims of non-group parties.

The claims would not be invalid or unenforceable merely because they are against a corporate family. They are on an equal footing to the claims of the other creditors, but can be subordinated by contract.

Substantive consolidation

18. Is pooling of assets and liabilities of some or all members of the corporate family allowed, so that a creditor of one member becomes, in essence, a creditor of all members?

Provisions for the pooling of assets do not exist under statutory law, but the same effect can be achieved by a contractual joint and several liability undertaking, combined with granting of third party security over assets of the individual members in favour of the creditor. Such an arrangement must pass the corporate benefit test for it not to be considered *ultra vires*.

Such pooling is not automatic and requires a contract, and filing at the relevant register of charges.

There is no guidance or requirements concerning which creditors among the competing entities get paid.

19. What proceedings are required for the court to order the pooling of assets and liabilities?
An Indonesian court cannot order the pooling of assets and liabilities.

20. Is the partial pooling of assets and liabilities allowed? What conditions apply?
Indonesian law does not provide for any partial pooling of assets and liabilities, but the same effect can be achieved by contract (*see Question 18*).

21. If the pooling of assets and liabilities is required, are there any protections for certain types of creditors?
See *Question 18*.

Secured creditors

22. How are secured creditors treated in relation to a family of companies?
Security given by two or more companies to a single creditor is not rendered invalid merely because these companies are members of the same family of companies, regardless of the subsequent bankruptcy or suspension of payments of either or both of them.

The creditor is treated as a separate secured creditor in relation to such company. However, it depends on the content of the facility agreement/underlying agreement governing which party is acting as the principal debtor and guarantor/collateral provider, and in the case of a collateral provider, whether the collateral provider is only liable for the value of the collateral or not.

INTERNATIONAL FAMILY OF COMPANIES

23. What extra considerations are necessary if one or more members of the corporate family is incorporated under or governed by the laws of another jurisdiction?
For the purpose of Indonesian insolvency law, a foreign family member in bankruptcy continues to be treated as separate in all respects from its family members, whether or not in bankruptcy.

Indonesia is not a party to any treaty relating to international insolvency issues. The Bankruptcy Law only addresses international aspects summarily. It adopts, for Indonesian bankruptcies, the universality principle, under which an Indonesian bankruptcy encompasses all of the debtor's assets wherever they are located. The applicable international private law in the relevant jurisdiction determines to what extent the Indonesian bankruptcy will be recognised (including, for instance, Indonesian preferential transfer provisions).

As far as bankruptcies ordered abroad are concerned, the principle of territoriality would probably apply and assets of a foreign debtor located in Indonesia will not be considered part of that debtor's bankruptcy. This is because foreign judgments are generally unenforceable in Indonesia (*see Question 26*). However, this need not prevent a foreign-appointed receiver from being recognised by an Indonesian court as legitimately representing

the foreign bankrupt estate in the same manner as a director of a corporation under foreign law is recognised as a lawful representative of that corporation.

The universality rule is reflected by the provision that creditors in an Indonesian bankruptcy, who obtain payment from enforcement of unsecured assets of the bankrupt outside Indonesia, must reimburse the receiver for that payment. Similarly, if the creditor assigns their claim and the assignee receives payments from these assets, that payment must also be paid to the receiver (*Article 212, Bankruptcy Law*).

As a consequence of the freedom of contract, a choice of foreign law is, in principle, recognised and an Indonesian receiver can be bound by the consequences of, for instance, New York law governing a loan agreement under which a claim is entered into the Indonesian bankruptcy. However, to the extent the recognition of *in rem* security rights on assets located in Indonesia is concerned, the *lex rei sitae* (principle of the law of where the property is situated) applies and only security rights established under Indonesian law need to be respected.

24. If insolvency/restructuring proceedings are instituted for corporate family members in different countries, do any international treaties or EU legislation apply to govern this situation?

Indonesia has not adopted the UNCITRAL Model Law on Cross-Border Insolvency.

25. Do domestic courts typically attempt to exercise jurisdiction over all the assets of the company filing domestically (regardless of where the assets are located) or do they limit their jurisdiction to domestically located assets?

For all practical purposes the domestic courts limit their jurisdiction to domestically located assets, although if the law of the country where assets are located so allows, a receiver must attempt to repossess those assets and liquidate them in the interest of all creditors.

26. Do the courts enforce court orders from foreign jurisdictions that attempt to exercise jurisdiction over assets located in your jurisdiction but owned by the company that is subject to the foreign insolvency proceedings?

Foreign court judgments cannot be enforced in Indonesia. For a judgment to be enforced in Indonesia, the dispute must be re-litigated before the competent Indonesian court (*see Question 23*).

27. Under what conditions, if any, can the courts communicate and co-ordinate with courts of a foreign jurisdiction in an effort to co-ordinate the administration of assets of family members?

There are no rules or guidelines on these communications between the courts. In practice, the receiver by itself (and approval from the supervisory judge) with the assistance of the bankrupt debtor will co-ordinate with the courts of a foreign jurisdiction to co-ordinate the administration of assets of family

members abroad.

Indonesia has not adopted or informally utilised the Guidelines Applicable to Court-To-Court Communications in Cross-Border Cases as adopted and promulgated by the American Law Institute and the International Insolvency Institute.

RESPONSIBILITIES OF OFFICERS AND DIRECTORS

28. What is the specific nature of the duties and responsibilities of officers and directors of a company? How do those duties and responsibilities change when the company becomes financially distressed?

Corporate governance

The Company Law provides for a mandatory two-tier management system consisting of:

- **A board of directors.** The board of directors is fully responsible for the management of the company in accordance with the interests and objects of the company, and is authorised to represent the company both in and outside of court, to make policies and to perform the day-to-day management of the company. This includes responsibility for making plans for the future, undertaking new activities in pursuance of the objects of the company and mapping out how the policies of the company will be implemented.
- **A board of commissioners.** The primary duty of the board of commissioners is to supervise the way the board of directors discharges its management responsibilities and to provide the board of directors with advice. The board of commissioners has no executive functions, although it can take care of the management of the company for a limited period of time in the absence of directors.

In practice, the articles of association of the company normally provide that certain decisions of the board of directors require the prior approval of the board of commissioners, or alternatively of the general meeting of shareholders, to limit the authority of the board of directors in certain external matters of the company. The activities of the board of directors are also limited to activities within the scope of the company's business defined in the articles of association and the permits or licences obtained from the appropriate authorities.

There is no formal list of duties and responsibilities of officers and directors under the prevailing regulations. The general provisions of Company Law stipulate that the directors run the management of the company for and on behalf of the interest of the company in accordance with the objects and purposes of the company (*Article 92, Company Law*).

A director must be actively involved with the management of the company by attending meetings and being informed about the company. Each director is obliged to exercise due care when managing the company. It applies to the commissioners when supervising the management by the board of directors. Both directors and commissioners are expected to serve the best interests of the company. The directors and commissioners owe a loyalty to the company

above their own personal interests and the interests of the shareholders who appointed them, especially where the interests of the company conflict with those other interests. Neither the board of directors and the board of commissioners or its individual members owe specific duties to shareholders, creditors, government authorities and employees, outside of their general duties of care when managing the company (*see Question 28*). This is subject to mandatory regulations that specifically require their compliance to the prevailing laws and regulations.

In the absence of any implementing regulations and case law, it is difficult to determine what standard the courts require to establish whether the director has exercised due care.

Each director is obliged to exercise due care when managing the company. This also applies to the commissioners when supervising the management by the board of directors. Both directors and commissioners are expected to serve the best interests of the company. The directors and commissioners owe a loyalty to the company above their own personal interests and the interests of the shareholders who appointed them, especially where the interests of the company conflict with those other interests.

Financially distressed

The duties and responsibilities of directors do not change when the company becomes financially distressed.

29. What specific types of conduct are in breach of the duties and responsibilities of officers and directors?

The following types of conduct violate the duties and responsibilities of officers and directors:

- Failure to take reasonable steps to minimise losses to creditors.
- Misappropriation of corporate assets.
- Undervaluation of corporate assets in a preference or other transaction to the detriment of creditors, if the final impact is detrimental to the interest of the company.
- Preferring payment to one creditor as opposed to another when insufficient monies are available to pay both.
- Continuing to trade when there is little prospect of being able to pay when due.

Failure to inform creditors of insolvency does not breach the duties and responsibilities of officers and directors. The bankruptcy declarations must be announced to the public by the appointed receiver in a newspaper.

30. What duties do officers and directors have to key creditor groups before the company becomes financially distressed?

There are no specific duties owed to creditors, shareholders, government authorities and employees, other than general duties owed to the company and imposed by law (*see Question 13*).

31. How do officers' and directors' duties change after the company becomes financially distressed or insolvent?

The duties do not change although in certain circumstances directors/commissioners may be liable for losses suffered including those that lead to bankruptcy (*see Questions 13 and 14*).

32. What civil and criminal liability exists for the officers and directors if they breach their duties and responsibilities?

Civil liability

Directors are not personally liable to third parties for acts performed by them provided that these acts are within the limits of their competence as defined in the articles of association, the resolutions of the general meeting of shareholders, and the law.

Directors can be held liable towards third parties:

- Jointly and severally, for a tort if they act beyond the limits of their competence.
- Personally, if, for example, the board of directors contracts an obligation on behalf of the company, while it is aware or ought to be aware that the company is in no position to fulfil such an obligation (*Articles 1365 and 1366, Civil Code*). The board of directors can be liable for the damage suffered by the third party as a result of such transaction.

If a director acts within his authority under the articles of association or as ordered by a shareholders' resolution and that act is later deemed to be a tort, the director concerned is not personally liable, but liability rests with the company.

Criminal liability

There are a number of relevant offences under the Indonesian Criminal Code, including:

Simple bankruptcy. Merchants who were declared bankrupt or admitted to a judicial cession of estate are liable for simple bankruptcy if (*Article 396, Criminal Code*):

- Their expenses were extravagant.
- They borrowed money under onerous conditions and acted with intent to delay the bankruptcy, knowing that it could not be avoided.
- They cannot produce the company books and documents required under the laws and regulations.

Fraudulent bankruptcy. Merchants who were declared bankrupt or admitted to judicial cession of estate are guilty of fraudulent bankruptcy, if in order to fraudulently restrict their creditors' rights, they (*Article 397, Criminal Code*):

- Invented liabilities, did not account for assets, or withdrew any property from the estate.
- Transferred ownership of any property either for nothing or significantly below its value.
- Did not fulfil their obligations in respect of keeping company records under the prevailing laws and regulations.

Article 398. Directors or any commissioners of a limited liability company,

Indonesian company on shares or co-operative society that was declared bankrupt or where the judicial settlement was ordered, are liable if they:

- Participated in or gave their permission to acts contrary to the articles of association that resulted in the losses suffered by the limited liability company, the Indonesian company on shares or co-operative society.
- Acted with intent to delay the bankruptcy or the judicial settlement of the limited liability company, the Indonesian company on shares or the co-operative society, knowing that the bankruptcy or the judicial settlement could not be avoided; participated in or gave permission to borrow money under onerous conditions.
- Did not fulfil the obligations and duties, or keep the company books and documents as required under the laws and regulations.

Article 399. Any persons or commissioners of a limited liability company, Indonesian company on shares or co-operative society that was declared bankrupt or where the judicial settlement was ordered, are criminally liable if, in order to fraudulently limit the rights of the creditors of the limited liability company, the Indonesian company on shares or the co-operative society, they:

- Invented liabilities, did not account for assets, or withdrew any property from the estate.
- Transferred the ownership of any property, either for nothing or significantly below its value.
- Benefited one of the creditors on the occasion of the bankruptcy or the judicial settlement or when they knew that the bankruptcy or the judicial settlement could not be avoided.
- Did not fulfil the obligations of keeping the records in compliance with the laws.

Article 400. Any persons are criminally liable if, in order to fraudulently restrict the creditors' rights, they:

- Withdraw any property from the estate, or accept payment either of:
  - an unclaimable debt;
  - all of a claimable debt knowing that bankruptcy or the judicial settlement of the debtors has already been applied for, or as a result of consultations with the debtor.
- Lay claim to a non-existing claim or cause an existing claim to be worth a higher value.

Article 401. Creditors who join an offer of a judicial accord as a result of an agreement either with a debtor or with a third party, where they stipulated special benefits, are criminally liable if they accept the accord (*Article 401(1), Criminal Code*). Debtors, directors and commissioners are also liable for concluding such an agreement if the debtor is a limited liability company, an Indonesian company on shares, a co-operative society or a foundation (*Article 401(2), Criminal Code*).

Article 402. Any persons declared insolvent, bankrupt, or admitted to judicial cession of estate, are criminally liable, if in order to fraudulently restrict the creditors' rights, they:

- Invented liabilities.

- Did not account for assets, or withdrew any property from the estate.
- Transferred any property for nothing or obviously below the value.
- Benefited somehow one of their creditors, on the occasion of insolvency, cession of estate or bankruptcy, or at a moment when they knew that it could not be avoided.

Article 403. Aiding or giving consent to acts contrary to the articles of incorporation, resulting in the company or society becoming incapable of fulfilling its liabilities or being dissolved, is also punishable.

Article 404. Any persons who with deliberate intent withdraw their own property or, property on behalf of the owner, are criminally liable if the withdrawal affects:

- Any other person who has a title of pledge, retention right, usufruct or use of that property.
- A mortgage established on it, to the prejudice of the mortgage creditor.
- A crop lien established on the property, to the prejudice of the lien-holder.
- A credit lien established on it, to the prejudice of the lien-holder.

33. Are officers and directors exposed to civil claims by creditors, shareholders, government authorities or employees?

Before insolvency

Officers and directors are exposed to civil claims by creditors, shareholders, government authorities or employees (*see Question 13*).

After insolvency

After declaration of bankruptcy, the officers and directors lose their power to take any legal actions relating to the bankruptcy estate. Therefore, there are almost no legal actions that the officers and directors can take in the post-bankruptcy declaration period.

Each of the creditor groups can institute a claim against the officers and directors, however the claim is not subject to the bankruptcy proceedings and instead is subject to normal civil proceedings.

34. Is the existence of potential personal civil or criminal liability a factor in officers and directors deciding when and if to put the company into a formal insolvency/reorganisation procedure?

Potential personal civil or criminal liability may become a factor in officers and directors deciding when and if to put the company in a formal insolvency/reorganisation procedure, but it does not constitute the only factor. If the officers and directors would like to file a voluntary petition for commencing bankruptcy/reorganisation procedure, they will require the prior approval of the shareholders of the company.

35. Is insurance available to protect officers and directors from claims that arise while operating a financially distressed company?

In practice, there is no insurance of this type available in Indonesia. This type of insurance may be available from an offshore insurance company.

36. Can officers and directors resign from their positions once the company becomes financially distressed?
Officers and directors can resign from their positions once the company becomes financially distressed.

37. How common is litigation against officers and directors for violation of their duties after the commencement of an insolvency/ reorganisation procedure? Is the litigation typically successful?
These types of lawsuits are in practice very rare and it is difficult to assess how successful they typically are.

38. What defences against civil and/or criminal sanctions are available to directors?
Although these general defences may be available, please note that civil actions should be read in the context of the fact that under the Indonesian civil law system the common law doctrine of precedent does not exist and each case must be determined on its own facts and merits although consideration may be given to previously decided similar cases and academic theories. Indonesian judges operate in an inquisitorial legal system and have very broad fact finding powers and a high level of discretion in relation to the manner in which those powers are exercised.

The decision by an Indonesian court as to matters of Indonesian law is not binding on lower courts or on the same court in any subsequent case. Indonesian court judgments are not systematically published and the courts are often unfamiliar with sophisticated commercial or financial transactions, leading in practice to a lack of certainty in the interpretation and application of Indonesian legal principles. In addition, enforcement can sometimes be an issue and the defendant may be able to take certain measures to frustrate enforcement.

General defences against civil and/or criminal sanctions are available to directors, including:

- Good faith.
- Due diligence (for example, obtaining valuation of assets).
- Reliance on outside consultants or professionals (such as accountants, legal advice, financial advisors).
- Exercise of reasonable judgment with intent to preserve the on-going value of the enterprise.

Specific defences against civil sanctions under the Company Law include:

- A member of the board of directors may not be held liable for losses if he can prove that:
    - the losses do not result from his fault or negligence;
    - he has conducted the management in good faith and prudence in the interest of the company and within the objectives and purposes of the company;
    - he has no conflict of interest whether directly or indirectly in the acts of management that result in losses; and
    - he has taken preventive measures against the arising or continuation of losses.

- A member of the board of commissioners may not be held liable for losses if he can prove that:
  - he has supervised in good faith and with prudence in the interest of the company and within the objectives and purposes of the company;
  - he has no personal interest whether directly or indirectly in the acts of management of the board of directors that result in losses; and
  - he has given advice to the board of directors to prevent the arising or continuation of losses.
  -

39. If it appears that the "going concern values" will result in a higher return to creditors than a liquidation of the assets, can officers and directors be protected if they decide to continue operations to protect the values for the benefit of all creditors?

If it appears that the "going concern values" will result in a higher return to creditors than a liquidation of the assets, the officers and directors can be protected if they decide to continue operations to protect the values for the benefit of all creditors.

If the result is an increase of debt owed to creditors, even though the officers and directors were acting in good faith, the officers and directors can still be protected. The defences listed in *Question 38* are available against the civil/criminal sanctions.

40. Are there any other defences available to directors and officers under bankruptcy or insolvency laws?

See *Question 14*.

41. What provisions in your jurisdiction's bankruptcy or insolvency laws are specific to the duties and sanctions for officers and directors?

Not applicable.

SUBSEQUENT RESTRICTIONS ON OFFICERS AND DIRECTORS

42. If a company becomes insolvent, is an officer or director of the insolvent company legally restricted from acting as an officer or director in another company?

A member of the board of directors must be an individual who has the capacity to perform legal acts, and has not within a five-year period prior to his appointment (*Article 93(1), Company Law*):

- Been declared bankrupt.
- Been a member of the board of directors or member of the board of commissioners who was declared at fault for the company's bankruptcy.
- Been convicted for having committed a criminal offence that damages the state finance and/or the relevant financial sector

A five-year period is counted from the date of conviction by a final and binding court decision declaring that an officer or director is at fault leading to the company's bankruptcy, or if sentenced, from the completion of sentence.

An officer or director of the insolvent company cannot be appointed as an officer or director in another company until the five-year period after a final and binding court decision declaring that he is at fault leading to the company's bankruptcy has lapsed (*Article 94(1)b, Company Law*).

43. If an officer or director becomes personally insolvent, is he legally restricted from continuing to act as an officer or director of his current company or another company?

Current company

The Company Law provisions are silent on whether the officers or directors that are personally declared bankrupt while acting as a director of a company are required to step down from their position immediately following the rendering of the personal bankruptcy declaration.

Another company

See above, Current company.

44. If a company becomes insolvent, is an officer or director of the insolvent company legally restricted from obtaining credit as a promoter of a second company?

There are no legal restrictions for an officer or director of the insolvent company to become a promoter of a second company and obtain credit. Any potential legal restriction would be based on the bankruptcy declaration of the relevant individual or the relevant company. However, banking institutions can keep records of bad debtor companies including the relevant officers and directors of the company, which may in practice prevent the second company having an officer or director of the insolvent company as the management of the company from obtaining the loan from the banking institution.

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