

THE URGENCY OF CORPORATE GOVERNANCE IN RUNNING REGIONAL COMPANIES

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ABSTRACT

The urgency to solidify the structure of governance in regional companies is due to the imbalance in the distribution of inter-componential roles and authorities in such companies. Governance structure has the function to distribute roles and functions of the organs within the companies, and to run as well as control the companies. The concepts adopted in the running of regional companies which are connected to the power and authority of the state's agents (as held by state's officers), the weakness of the regional government to motivate individuals for achieving the goal of the organization, and the stiff bureaucratic attitude, all cause the weakness of the governance structure in the regional companies. The imbalance in the distribution of roles and authority between various agents in regional companies is due to the disharmony or lack of synchronization in the rules that regulate the regional companies, to the dominant involvement and intervention of regional government, and to the weakness in the governance of regional companies due to the management concept that emphasizes power and authority. The measure for strengthening the structure of governance in the regional companies through the adoption of Good Corporate Governance needs the establishment of a mandatory regulation which can protect the interests of the parties involved in the running of the regional companies.

Key words: Corporate Governance, Regional Companies

Introduction

Every corporation has the goal to maximize the position of the owner of the corporation as signaled by the increase in the value of the share (BPKP: 1) This is in line with the concept of good corporate governance which definitely constitutes a system that manages and controls the companies for creating added values for all stakeholders (Adrian Sutedi, 2011: 1). In the concept good corporate governance there are two things emphasized, namely, first, the importance of the right of the shareholders to get accurate and punctual information. Secondly, it becomes the obligation of the company to disclose accurately, punctually, and transparently all the information on the performance of the company, the ownership, and stakeholders (Adrian Sutedi, 2011: 2).

The structure of corporate governance of a corporation is affected by various factors, particularly by the theory of corporation being adopted, and by the culture and by legal system in force. Besides, the corporate governance system is also much dependent upon the existing society's cultural background as well as upon the economic and political history of the country (Ridwan Khairandi & Camellia Malik, 2007: 60). In many countries the right for the ownership of shares is of two types, namely the one pertaining to the shareholders based on the profit derived from the percentage of shares under his possession, and the other related to the shareholders who can exercise control upon the company's assets based on the right of control under their possession. The degree of concentration of these two types of the shareholders' right is found respectively in the country adopting outsider system and that adopting insider system (Indra Surya & Ivan Tustiavandana, 2006: 13).

The outsider system is much adopted in the Anglo-Saxon countries such as England and the USA, in which the structure of the ownership of the companies is characterized by diffusion, while the insider system is much adopted in the continental European countries such as Holland, Germany, and Indonesia characterized by the concentration of the ownership of the company only on certain groups.

Based on the structure of corporate governance adopted by a country, Jiato li from College of Business Administration, University of Hawaii at Manoa, Honolulu, HI, USA says in his article *Ownership Structure and Board Composition: a Multi-test of Agency Theory Prediction* that the difference in the company's governance, particularly the difference in the ownership and control of the public companies in various countries is significantly influenced by the diversity in politics and legal barrier (Jiato Li, 1994: 359-368).

Related to the factor affecting the development of the structure of corporate governance of a company in a certain country, the influence is more by the legal system in force in that country as well as by other factors such as the theory of corporation being adopted, the socio-cultural background of the society, and the economic and political history. All those factors much influence the characteristic and development of a business entity. Based on the condition described above various forms and characteristics of companies come into existence.

Indonesia as one of the countries adopting continental European system shows the characteristic of corporate governance structure affected to a degree by the concept of corporate governance adopted by the Dutch colonial government based on continental European system using the principle of two-tier system. Indonesia's background as ex Dutch colony shows its affiliation to the legal system in force in the country of origin (colony), within which is included the part pertaining to the corporate law.

Seeing the condition presented above, Indonesia in terms of company ownership can be categorized as adopting the concept of insider system in its corporate governance. The insider system assumes that the structure in the ownership of the shares in the company is characterized by concentration on a small number of parties and, therefore, not diffused to several groups so that those parties have dominant control and influence. This can be seen in the various forms or types of company found in Indonesia no matter whether they are in the forms of limited (Ltd) corporation, firms, *Commanditer Venootschap* (CV), or open public company. Whatever the form, the ownership of its shares is still much under the control of a small number of parties, which is particularly true in a non public open company.

Pertaining to control and ownership of a company the government has its role or function upon it. In Indonesia the role and domination of the government can be seen in some types of company, no matter whether the companies are run by the central government or by the regional government. The share ownership and control by the central government can be seen in the concept of State-owned Companies legally established under Act No 19 of 2003. In the provision of its chapter 1 paragraph 1 it is stated that: The State-owned Company is a company of which the whole or the biggest portion of its capital is possessed by the State through its direct involvement through the State's properties particularly separated for that purpose.

The domination and control of the central government over the state companies also happen under the concept of ownership or control of business entity within the regional government, at both the provincial and regency/municipality levels. The domination, control and ownership of the companies by the regional government can be seen in several provisions, particularly in the Act No 5 of 1962 concerning regional companies and their subsequent operational regulation. In the provision of chapter 2 is stated that: Regional companies are all of the companies established upon this Act, of which the whole or part of their capitals are derived from the regional properties separated for that purpose, except when otherwise determined under established act.

One of the characteristics of regional company is that it is a company whose ownership of the shares is mostly or wholly under control of the regional government whereby the company is known as Regional government-owned company under the Act No 32 of 2004 as is replaced by the Act No 12 of 2008 concerning the regional government. In chapter 177 its provision states that: The regional government can possess regional government-owned companies of which their establishment, integration, change of ownership, and /or termination is established by regional regulation in conformity with existing regulation. In relation to the characteristic of regional companies as business entities, these companies provide services, public benefits, and generate regional income. With such characteristics the regional companies show dualistic tendency. On the one hand, they are commercial corporation, but on the other hand they are social service corporation. Therefore, due to this dualistic nature of regional companies, it is necessary to do a review to the forms of the regional companies in conformity with their respective concerns (M. Natzir Said, 1985: 293).

The dualism in the characteristic of the regional companies tends to cause the lack of optimality in the company's performance. The enforcement of the dual characteristic and its goal the regional company should be concentrated on the kinds of enterprise which really constitute the domain of the regional government, all for fulfilling its mission to make the society prosperous, particularly economically.

Based on the data available at the Ministry of Home Affairs, the assets of the regional companies reached the total of 340,118 T by the year 2011 and 310,716 (90.06 %). The profit contribution of the regional companies is recorded as Rp 10,372 T, or in terms of its average ratio to the assets as much as 3.0 per cent (Depdagri, 2010). With such big amount of the assets, it is mostly (about 90 %) contributed by the sector of banking while 4 % by the regional clean water companies. The line of thought adopted within the policy of the regional companies is still strongly based on the assumption on how to spend money, not on the business assumption of how to get money (Jawa Post, 2012).

This article aims to provide input for the government to determine the direction of government policy to improve the performance of the company is mainly associated with good corporate governance. Thus providing a benefit to the community and increase regional revenue.

Principle in Running Regional Companies

The good principle in corporate governance relates to the handling of responsibilities in each organ of the regional company, which will affect the design of the authority and responsibility of the company which will be established in the statute of the regional company or in the regional regulation on the establishment and formation of the regional company.

In principle, an organization or a company seeks to be better. Such things as better productivity, higher profit, more efficient performance, and satisfying services for the customers are all the obsession of the company (Edi Siswandi, 2012: 14). The ideal concept in the running of regional companies is that of the improvement of the genuine regional income as well as the ability to serve and give benefit to the public at large. In other words, the business and social aspects in the establishment of regional companies should be achieved as stated in the established act.

The problem of governance structure in running regional companies is related to the structure in the relationship between the responsibility and role distribution among the organs of the company. The governance structure has the function of distributing the roles and the functions for the organs of the company, inclusive of how to run and how to control the company.

The essence of good corporate governance is the strict separation of the organs within the company. The separating function here should be taken to mean functional separation whereby to avoid inter-organ intervention within the company.

The involvement and intervention of the regional government in the running of the regional company for improvement of performance is badly needed. However, if the involvement and intervention of the regional government is too dominant, this could block the independence of the regional company.

In relation to the structure of the corporate governance, particularly that for the regional companies, the impact of regional autonomy which is being implemented now cannot be avoided. The regional autonomy to a degree allows space to the regional government to be independent and provides opportunity to make its breakthrough towards economic independence whereby to improve the competitive power and to create prosperity for the society (A. B. Susanto, 2010). In this era of regional autonomy the role of the regional heads together with the regional parliament becomes so urgent in the running of the regional administration. In the context of the relation between the regional Head and the regional Parliament in formulating and implementing public policies, the role of the regional head becomes quite strategic not only in establishing such formulation and in taking initiative, but also for influencing the decision achieved (J. Kaloh, 2008: 40).

The vision of the regional autonomy can in principle be formulated in the three main axes, namely in the axes of politics, economy, and security and defense. In the area of economy this is marked by the establishment of economic decentralization which will pave the path towards the growth of economic centers in the region (J. Kaloh, 2008: 251). The regional company as one of the centers for economic growth plays a very important role in improving the regional economy.

The regional company is expected to become one of the economic pillars which could support the genuine regional income. In supporting the genuine regional income the regional company is expected to be able to compete in the global context, realizing particularly that the ASEAN free market of 2015 is already right in front of the eyes. The independence and capacities of the regional companies will get tested by the global market, particularly that in the ASEAN region.

Problems in the Structure of the Running of Regional Companies

Concerning the running of the regional companies, this is much affected by the governance structure of the regional companies themselves. The structure in the relation between accountability and role distribution among the organs of the regional companies is very essential and influences the performance of the regional companies themselves. Structurally, the forms of the regional companies can be distinguished into two types, namely into share-holding and non share-holding regional companies. In actual practice, besides these two types of the regional companies there is one form of regional company, i.e. one in the form of Management Board as found in the special province of Jakarta which becomes part of regional company.

Based on the information from the Investment and Promotion Board of Jakarta, the regional companies of the special province of Jakarta consist of three types, namely that in the form of Limited (Ltd) companies (17 companies), that in the form of regional companies (5 companies), and that in the form of Management Board (1 company), namely Lokasari Management Board established under the Governor's decree no 3931 of 1984. All the condition described above indicates the weakness of the structure of the corporate governance of the regional companies, which typically can be seen in the characteristic of one of the regional companies in Jakarta which is neither in the form of share-holding nor in the form of regional company.

Both forms of the regional companies, namely those in the form of share-holding and those in the form of non share-holding, and even the form not in conformity with either of the two, are in need of a right concept or model whereby to achieve the planned goal and direction in order to meet all interests, both those of the shareholders (in this case, the regional government) and those of the stakeholders (the society at large).

In relation to regional corporate governance there are some main problems connected to the realization of the principle of good corporate governance which among others include the following. First, the occurrence of disharmony or the absence of synchronism in the regulation that regulates the regional companies, particularly that part pertaining to sector regulation and intervention of regional government in the running of regional companies. Secondly, the involvement and intervention of the regional government in running the regional companies for the purpose of improving the performance. This can be seen in the regional regulation for the establishment of regional companies, particularly the companies in the form of regional companies. This is due to the fact that the establishment of the shareholding companies is subject to Act No 40 of 2007 or to the provision of Act No 5 of 1998 concerning stock exchange, in which if the company is in the form of a public company, the principle of *lex specialist derogate legi inferiori* becomes in force. Thirdly, the weakness in the regional corporate governance is caused by the emphasis on power and authority. The regional government still gives priority to the paradigm of power and authority. The regional corporate governance is still regarded as the running of state agencies (by state's agents). According to Edi Siswadi via quoting Frey's opinion, intervention and monopoly being exercised by the bureaucrat tends to cause inefficiency because of its tendency for output overproduction beyond the need of the society (Edi Siswadi, 2012: 14) as well as of the weakness of the regional government in motivating its individual subjects due to the stiff bureaucratic attitude and its goal. According to Want in A. B. Suasanto and Himawan, the stiff bureaucracy is characterized by its structure, hierarchy, and various regulations which are all stiff; there are no readiness to take risk, no effective cooperation between its staff, and no sufficient competence and motivation (A. B. Susanto & Himawan Wijanarko, 2010).

Besides those problems mentioned above pertaining to the regional corporate governance, there are also problems related to the structure of governance in need of serious attention. There are some reasons for the need to strengthen the structure of governance within the regional companies based on the following points of consideration:

1. The concept in the running of the companies still gives emphasis on power and authority
2. The structure in the running of the regional companies gives emphasis on its conformity to the running of the state (by state's agents)
3. The weakness of the regional government to motivate staff for the achievement of the goal
4. The stiff bureaucratic system

Strengthening the Governance Structure within Regional Companies

According to the Cadbury Committee, corporate governance is a system that guides and controls the company whereby to establish balance between the power of authority needed by the company to guarantee its sustainability and its accountability to the stakeholders. In relation to the implementation of the regional corporate governance, the factor of balance is very much needed in the clear separation of various organs in the company. Through strengthening the governance structure within regional companies it is expected that the adoption of good corporate governance principle could be manifested. The urgency in strengthening the governance structure in the regional companies is needed because of the occurrence of imbalance in the distribution of the roles and authorities among the organs within the regional companies.

One of the possible measures to strengthen the governance structure in the regional companies is through adopting the principle of good corporate governance for the regional corporate governance. By adopting good corporate governance principle, it is expected that the regional companies can be directed and controlled towards achieving the targeted goal. At the same time, it is expected that balance could be established between various stakeholders alone, which include both the shareholders, namely the regional government as owner of the companies with its Board of Directors and Board of Commission, and other wider stakeholders such as the creditors, customers, suppliers, and society at large.

In order to strengthen the governance structure in the running of regional companies the need for good corporate governance is absolute and obligatory to be fulfilled. Therefore, there is a need for a regulation that can guarantee the interests of various parties involved in the running of the regional companies.

The regulation related to the implementation of the principle of good corporate governance for regional companies in Indonesia has not yet adopted the regulation which requires every business entity to adopt good corporate governance principle. The adoption of the principle of good corporate governance is still only an optional choice, not yet mandatory. The mandatory adoption of this principle is in force only for the companies with special deals like banking and stock exchange. This condition is different from that in the countries strictly adopting the principle of good corporate governance such as America which necessarily issues "Sarbanes Oxley Act of 2002", Canada with its "The S-11 Bill of 2001, England with its "Combined Code of 2003 and 2006", Japan with its "New Commercial Code of 2003", and France with its "La Loi De Securite Financiere of 2003" (Martin Hilb, 2011).

Based on the condition described above, the adoption of the principle of good corporate governance becomes a need, for which is needed the establishment of a forceful regulation, whatever the form, construction, and the type of business being run, whether shareholding or non shareholding, particularly for the government-owned business entity, whether of the central government or the regional government. With the adoption of the principle of good corporate governance each business entity will of course adjust its structural frame of business organization as well as the organs within it without changing the status and construction of that business entity.

Conclusion

The structure of corporate governance in Indonesia is much influenced by various factors, particularly by the continental European system which establishes two-tier system under the concept of insider system with the structure of shareholding concentrated on a few parties (regional government) whereby they exercise their dominant control and influence. The dualistic characteristics (i.e. the functions of providing services and fostering income) of the regional governments results in the less optimum performance of the companies.

The urgency for strengthening the regional corporate governance structure is due to the existence of imbalance in the distribution of roles and authority between the existing organs within the regional companies. The task for the strengthening of the governance structure for the regional companies could be achieved through the adoption of the principle of good corporate governance in the running of the regional companies.

The imbalance in the distribution of roles and authority among the company's organs within the company is caused by three main problems as follows. Firstly, the occurrence of disharmony or the absence of synchronism in the regulation that regulates regional companies, particularly that concerning sector regulation in the running of the regional companies. Secondly, the dominant involvement and intervention of the regional government in the running of the regional companies under the purpose of improving performance. Thirdly, the weakness in the structure of corporate governance due to the emphasis on power and authority in the running of the regional companies.

Besides the reasons mentioned above, there are some other reasons for the need of strengthening the governance structure within the regional companies based on some consideration such as the following. The concept of regional corporate governance being adopted still puts the emphasis on power and authority. The structure of regional corporate governance puts the emphasis on the state agencies (through state agents). The regional government still has its weakness in motivating individual staff due to the staff goal of organization and bureaucratic culture.

Based on the condition described above, it is necessary to government take some attempts towards strengthening the governance structure in the regional companies and creating balance in the distribution of roles and authority among the company's organs in the regional companies. For all this it is necessary to do the following, to adopt the principle of good corporate governance in running the regional companies through formal regional regulation mechanism concerning the establishment of regional companies, otherwise through other regulation issued accordingly by the governor or regent/municipal of the regions under concern. Thus providing a benefit to stakeholders, such as regional company, community and increase regional revenue.

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