



The Legal Risk of State-Owned Enterprises' Debt

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ABSTRACT

Several state-owned enterprises in Indonesia have large debts. This paper elaborates on the legal aspects of state company debt with examples from two national airline companies, Garuda Indonesia and Merpati Nusantara Airlines, which face debt problems but have different fates. Garuda Indonesia received financial assistance from State Equity Participation sourced from the State Revenue and Expenditure Budget, whereas Merpati Airlines went bankrupt based on a court decision. In conclusion, the government, as the majority shareholder, is indirectly responsible for the company's debt even though there has been a separation between state and company assets within the framework of corporate law. Therefore, state company debt will remain a burden on the government budget and risk bankruptcy.

Keywords: Debt, Garuda Indonesia, Merpati Airlines, state-owned enterprises.

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1. INTRODUCTION

In general, debt is a two-edged sword. When it is used wisely and in moderation, it brightly increases welfare. However, the result can be a disaster if used imprudently and in excess. Overborrowing leads to bankruptcy and financial ruin for individual households and firms, while too much debt for the country impairs the government's ability to deliver essential services to its citizens (Cecchetti *et al.*, 2011, p. 1).

When a state company has debt, the question arises whether the debt has a risk impact on the country. In corporate law, the owner has separated his wealth from the company. Ownership of a person's company or legal entity over a company is in the form of shares. The shares signify a person or party's capital participation (business entity) in a company (Demsetz, 1983, pp. 375–390). If the company ceases to operate or goes bankrupt later, the owner's loss is limited to the number of his shareholdings. His or her assets do not guarantee a company's loss other than its share ownership (Franken, 2005, pp. 232–257).

Airlines experiencing bankruptcy due to huge debts in Indonesia occurred between 2001–2010 and 2011–2015. The leading causes of bankruptcy are internal and external factors. Several internal factors include the poor quality and capability of the company's management. In contrast, external factors are national and global economic conditions such as the rupiah currency falling against the US dollar, fluctuating fuel and spare parts prices, government policies, and intense market competition (Majid *et al.*, 2016, pp. 25–40). These facts also affected the financial condition of the two national airlines, Garuda Indonesia and Merpati Nusantara Airlines.

However, debt to State-Owned Enterprises has a different perspective from private companies because the majority or part of the company's capital source comes from the State Revenue and Expenditure Budget. Therefore, the risk of state-owned companies' debts can harm state finances.

This paper discusses the legal aspects of State-Owned Enterprise Debt, focusing on the Indonesian case. Two state-owned companies, Garuda Indonesia and Merpati Nusantara Airlines, have had bad luck due to large debts causing heavy burdens for the companies. The paper analyzes the legal risks faced by the Indonesian government on the debts of the two state-owned companies with a qualitative approach.



2. UNDERSTANDING STATE-OWNED ENTERPRISES' DEBT

State-owned enterprises (SOEs) are legal entities established to undertake commercial activities and owned entirely or largely by the sovereign (ADB, 2018, p. 3). Another definition says that an SOE is any corporate entity recognized by national law as an enterprise where the state exercises ownership. It includes joint stock companies, limited liability companies, and partnerships limited by shares. Moreover, statutory corporations, with their legal personality established through specific legislation, should be considered SOEs if their purpose and activities, or parts of their activities, are primarily economic (OECD, 2015, pp. 14–15). European Commission for Economic and Financial Affairs (ECFIN, 2016) introduces SOEs by dividing them based on the number of shares owned by the state into the following categories:

1. Companies fully owned by public authorities,
2. Companies where public authorities have a majority share,
3. Companies where public authorities retain a minority share but have special statutory powers,
4. Companies where public authorities have a minority share and no special powers.

These are generally not considered SOEs; however, they may be relevant to obtaining a fuller picture of the government's stake in the economy (ECFIN, 2016, pp. 6–7).

In Law Number 19 of 2003 on SOEs, Indonesian law mentions that it is an enterprise with equity owned by the state, either majority or entirely through direct equity participation deriving from the restricted state assets. Moreover, SOEs are divided into three: *First*, a State-Owned Limited Liability Company (*Perusahaan Perseroan*) means an SOE in the form of a limited liability company in which equity is divided into shares which entirely or at least 51% of the shares are owned by the State of the Republic of Indonesia with the main objective is to gain profits. *Second*, State-Owned Listed/Registered Company (*Persero*) is an SOE in which equity and number of shareholders have fulfilled specific criteria or *Persero*, which has conducted a public offering per the legislation in the capital market sector. *Third*, a Public Corporation (*Perusahaan Umum/Perum*) is an SOE whose capital is entirely owned by the state and not divided into shares, whose objective is for public service in the form of high-quality goods and service provision and at the same time to gain profits under the principles of corporate governance.

The main capital of SOEs is direct equity participation from the state through the State Revenue and Expenditure Budget. It is a state asset separated from the state financial system, so its management is not controlled based on the State Revenue and Expenditure Budget (Supramono, 2016, p. 20). State control over SOEs is one of the mandates of the 1945 Indonesian Constitution that aims to achieve maximum prosperity and welfare. In principle, SOEs must control economic fields related to the primary community needs (Mubyarto, 1987, p. 53). However, when SOEs run their business with limited government financial support, one of the options is financing SOEs with debt (OECD, 2014, pp. 52–53).

In the Indonesian legal framework, SOEs as a limited liability company are legal entities separate from the state. Likewise, company assets are not state assets. Law No. 19 of 2003 confirms that the capital deposited by the state to companies has separated itself from the state financial regime. Moreover, SOE subsidiaries are legal entities separate from the state (Rahadiyan, 2016, pp. 624–640). Therefore, debts and obligations arising in SOEs' business activities are not part of state finances in the annual State Revenue and Expenditure Budget scheme.

More importantly, the status of SOE assets is not state finances following the principle of separating state assets from the State Revenue and Expenditure Budget. Instead, state companies carry out their business activities with management based on the principles of good corporate governance. In addition, the legal entity theory asserts that SOEs have their assets separate from the support of the management and founders. Furthermore, the fatwa of the Supreme Court of the Republic of Indonesia Number WKMA/Yud/20/VIII/2006 strengthens the status of SOEs' assets, which are no longer state finances (Sumarto, 2020, pp. 21–33). Finally, the state company's receivables can be professionally resolved by their respective management and subject to the law.

Nevertheless, the fact is that politically, the government, on behalf of the state as the majority shareholder, often intervenes in the management of SOEs in the company's business policies. The intervention violated the ideals of the 1945 Constitution to realize the welfare of the people (Adhari, 2015, pp. 27–36). Moreover, the placement of SOE directors and commissioners follows the government's and ruling parties' political interests. Therefore, the policy direction of state companies often violates good corporate governance (Sahrasad, 2017, pp. 57–82).

3. STATE EQUITY PARTICIPATION TO SAVE GARUDA INDONESIA

The cause of the company experiencing debt default and the threat of bankruptcy, among others, is the company's mismanagement of airplane rental fees, which are more expensive than the market

average price. In addition, the opening of flight routes, especially international ones that are not profitable and lack passengers, such as Melbourne, Tokyo, Seoul, and Amsterdam. Garuda Indonesia cannot compete with bigger and stronger international airlines (Idris, 2023). Besides, the company went bankrupt due to excessive investment and unprofessional behavior. From 2009 to 2021, the company decided to procure 50 new aircraft from Boeing and an additional 10 units from Airbus. This step is great, but some people obtain personal advantages from the transactions. More badly, the procurement was funded by debts, and no executive or legislative authorities warned of this action (Subiyanto, 2022). Moreover, most of the company's payables represent debt originating from aircraft rental expenses incorrectly presented in its financial statements in previous years. Furthermore, the COVID-19 outbreak has increased the company's burden due to reduced business activities during the global pandemic (Resia, 2023).

The main reason for the government's assistance to the company is the rescue of national career flight due to debt bondage and the threat of bankruptcy. Based on the independent auditor's report on December 31, 2021, the Public Accounting Firm of Tanudireja, Wibisana, Rintis, and Rekan stated that the company suffered recurring losses during 2020 and 2021. The company's total liabilities are USD 13,302 million, while its total assets are USD 7,192 million (Garuda Indonesia, 2022). Furthermore, the total liabilities as of March 31, 2022 (unaudited) are USD 13,383 million, with total assets of USD 7,048 million (Garuda Indonesia, 2022). The DPO Management Team issued a Fixed Receivable List on June 14, 2022. Garuda Indonesia has a total debt of IDR 142.42 trillion to 501 creditors in this list. In detail, IDR 104.37 trillion to 123 lessors, IDR 34.09 trillion to 300 non-lessor creditors, and IDR 3.995 trillion to 23 non-preferred creditors (Arief, 2023).

Previously, the creditors filed a bankruptcy lawsuit for this state company with the Central Jakarta Commercial Court. However, Garuda Indonesia survived bankruptcy since it applied for Deferred Payment Obligations (DPO) to get additional time to settle debt payments to creditors. This method avoids the risk of bankruptcy and is a form of peace between debtors and creditors. It is a legal moratorium in the form of delaying debt payments, which is one of the ways creditors or debtors take to achieve settlement of debts. The debtor can submit a reconciliation plan with his creditors during this period. It is a decision to legally postpone the payment of debt through the law to prevent the financial crisis from worsening. Moreover, debtors and creditors can find joint solutions to achieve a debt settlement (Toha & Retnaningsih, 2020, pp. 157–161).

One of the creditors, PT My Indo Airlines, submitted a DPO application to the Central Jakarta Commercial Court on July 9, 2021, with case number 289/Pdt.Sus-PKPU/2021/PN Jkt.Pst. The lawsuit was filed because Garuda Indonesia was in arrears in paying several obligations to My Indo Airlines. In the decision read on October 21, 2021, the panel of judges rejected the creditor's application. (The Central Jakarta Commercial Court, 2021). After being released from the lawsuit, Garuda Indonesia received another lawsuit from PT Mitra Buana Koorporindo, who submitted a DPO application to the Central Jakarta Commercial Court on October 22, 2021, with case number 425/Pdt.Sus-PKPU/2021/PN Niaga Jkt.Pst. The panel of judges granted the lawsuit and gave Garuda Indonesia time to complete its obligations (The Central Jakarta Commercial Court, 2021).

In completing its obligations, Garuda Indonesia, as a state company, asked the government for help. The government and the House of Representatives welcomed the request and have approved a SEP of IDR 7.5 trillion from the 2022 State Revenue and Expenditure Budget. This year is not the first time Indonesia's national airline has received a SEP from the government. Previously, this state company received additional SEP in 2000, 2001, and 2016. The value of SEP in 2000, based on Government Regulation Number 70 of 2000, was two trillion one hundred forty-nine billion two hundred forty million one hundred four thousand one hundred ninety-five rupiah fifty cents (Republic of Indonesia, 2000). Then, in 2001, the government, based on Government Regulation No. 67/2001, disbursed SEP funds to this company amounting to three trillion nine hundred forty-one billion five hundred forty-five million two hundred fifty sixty thousand eight hundred seventy-five rupiah (Republic of Indonesia, 2001). As for 2016, the government provided SEP funds of eight billion four hundred one million two hundred nineteen thousand seven hundred and fifteen rupiahs. The disbursement of these funds is in accordance with Government Regulation Number 36 of 2016 (Republic of Indonesia, 2016).

There are three possibilities for Garuda Indonesia to escape from a financial crisis. The first option is bailout funds. The government provides bailout funds to improve a company's financial health. This option is a rapid loophole to increase equity and aid in re-balancing the debt-to-equity ratio. Besides, the bailout choice may keep investors' trust since the government, as the majority shareholders, constantly supplies financial support to the company. The next choice is debt restructuring through an out-of-court agreement. The company and its creditors entered into a new agreement that contained a postponement clause and an extension of the repayment period of debt, installments, and interest. However, the company must guarantee that its business will return to generate profits shortly. The last alternative is debt restructuring through Deferred Payment Obligations (DPO) through the commercial

court. The company submits a reconciliation proposal to creditors, which includes an offer to pay part or all of the creditor's debt, both preferred and concurrent creditors. The primary purpose of a DPO is to prevent corporate bankruptcy (Christiawan *et al.*, 2022, pp. 13–23).

After receiving the State Equity Participation, Garuda Indonesia will use 60% of the funds or 4.5 trillion rupiahs for asset maintenance, restoration, and fulfillment of routine maintenance reserves. Meanwhile, 40% or 3 trillion rupiahs will be a working capital for fuel expenditure, rental costs, and restructuring. Then, the company will convert the debt into shares (Subekti & Yolanda, 2023). Moreover, the management is committed to improving the quality of work and financial performance, not burdening the state budget (Puwanti, 2022).

However, the management's commitment to improving corporate governance after the State Equity Participation invites criticism because previously, Garuda Indonesia had obtained additional capital several times and repeatedly faced bankruptcy threats. From 1993 to 1997, the company experienced a decline in profit and negative cash flow. The government assisted with restructuring from 1998 to 2001. After a change in management from 2002 to 2005, the company's condition worsened compared to before 1997 (Akyuwen, 2011, pp. 112–133). In 2016, the company again suffered losses and received State Equity Participation. The government has also changed its SOE governance policy to make it healthier. However, the additional capital for Garuda Indonesia does not benefit the state as the majority shareholder (Handaka & Akbar, 2020, pp. 353–357).

In addition to past poor governance issues, the previous management of Garuda Indonesia has a criminal record of corruption. In 2020, the Jakarta High Court sentenced Emirsyah Satar, former President Director of Garuda Indonesia, to 8 years in prison, a fine of 1 billion rupiahs, and a subsidiary to 3 months in prison for corruption and money laundering (The Central Jakarta District Court, 2020). This case involves the Serious Fraud Office (SFO), the British government's anti-ruling agency, investigating Rolls-Royce, a British aircraft engine manufacturer, for bribery in procuring aircraft in 12 countries, including Indonesia. Although the SFO finally stopped investigating the case, the Corruption Eradication Commission in Indonesia continued investigating until the Jakarta High Court's decision was issued (Prakasa & Unggul, 2019, pp. 409–426).

4. DEBT AS A CAUSE OF BANKRUPTCY: THE CASE OF MERPATI NUSANTARA AIRLINES

Merpati Nusantara Airlines was founded in September 1962 by several senior officers. Then, in 1976, the legal entity of a state company changed to a limited liability company with majority share ownership by the government (Aida, 2023). Two years later, the company changed its status to become a subsidiary of Garuda Indonesia and opened international flight routes. In addition, the company's business type is also increasing with ticketing services in collaboration with international airlines such as Japan Airlines, Qantas, Lufthansa, and China Airlines (Puspa, 2023).

This state-owned airline stopped operations on February 1, 2014, due to poor financial reasons and big debt bondage (DPR-RI, 2023). At the end of 2017, Merpati Airlines had debts of 10.72 trillion rupiahs to many creditors. The total assets owned by Merpati at the end of 2017 were only 1.21 trillion rupiahs, the company's equity was recorded at minus 9.51 trillion rupiahs, and the company lost 737 billion rupiahs (Heriani, 2023a).

PT Perusahaan Pengelola Aset (Persero), or PPA, is the applicant for the bankruptcy of Merpati Airlines to the Surabaya Commercial Court on April 25, 2017. The Panel of Judges canceled the peace agreement (homologation) between creditors and debtors, which caused the state company to go bankrupt. The operational shutdown in 2014 and the Air Operator Certificate (AOC), the airline's main requirement to fly, were revoked in 2015, the two main reasons the company was saved (The Surabaya Commercial Court, 2019).

Previously, the government, through SOEs, had assisted Merpati Airlines even though the operating license for commercial services was revoked. For instance, the Garuda Indonesia Group and several other SOEs such as Semen Indonesia, Pertamina (National Oil Company), Perum Bulog, the Indonesian Trading Company, and the State Electricity Company support Merpati's cargo business management through the activity of delivering goods (cargo) in the Papua region. In addition, in terms of cooperation in managing maintenance, repair, and overhaul (MRO) businesses, Merpati Nusantara also acts as a marketing agency that provides services for turbine maintenance from Pertamina and the State Electricity Company, facilitated by MRO Merpati Nusantara Group and Garuda Indonesia Group (Artmadjati, 2023).

However, through the Minister of Finance, the Indonesian government rejected the option of rescuing Merpati Airlines with the help of State Equity Participation after being declared bankrupt. Instead, the government allows companies to conduct bankruptcy proceedings based on court decisions (Pratama, 2023). The supervisory Judge and the Curator carry out the bankruptcy process

of the national airline. All company assets will be auctioned off to settle obligations to creditors (Azka, 2023).

Company bankruptcy, in general, and in the case of Merpati Nusantara Airlines, occurs when the company experiences temporary and permanent financial difficulties. It is because management needed help to overcome the fundamental failure of governance and finally give up on getting up (Wang & Shiu, 2014, pp. 233–243). In addition, bankruptcy happens due to a company's failure to pay its debts, maturing obligations, and lack of funds to carry out its business operations (Kozlovskiy *et al.*, 2019, pp. 370–381).

In addition to a history of poor management, the state suffers losses due to corruption crimes committed by company management. For example, the Supreme Court of the Republic of Indonesia sentenced Hotasi Nababan, President Director of Merpati Nusantara Airlines 2002–2008, to a 4-year sentence and a fine of 200 million subsidiaries for six months in prison. The panel of judges stated that he had committed an unlawful act and caused a loss to the state of US\$1 million for the aircraft leasing process that did not go through company procedures (The Supreme Court, 2014). However, this decision has drawn criticism because the defendant, the president director, should be guilt-free for the company's losses by applying the Business Judgment Rule doctrine. His mistake was purely a business decision and did not harm the state's finances (Suastuti, 2018, pp. 1270–1275). In addition, Indonesian law has not accommodated this principle in the management of state-owned companies, so many SOE directors have received criminal sanctions for corruption in business or investment losses (Rukmono, 2019, pp. 233–237).

5. CONCLUSION

The debt of state companies in the cases of Garuda Indonesia and Merpati Nusantara Airlines poses legal risks for the government in two respects: the risk of the state's financial burden and the risk of bankruptcy. First, state-owned companies are facing the threat of bankruptcy due to large debts that burden the state budget. The government allocates funds from the State Revenue and Expenditure Budget as State Equity Participation to state companies threatened with bankruptcy. The government has to spend state money to save corporations that have impaired and unprofessional governance, considering the existence of a business related to the public's interests and the nation's good name. State money would be better if allocated to development and improving people's welfare. The state is losing out to the person who causes the loss of state enterprises and bears the harmful consequences.

Second, state companies that go bankrupt and whose assets are auctioned off to creditors are a form of state loss. Although the assets of state companies are state assets that have been separated from the state financial regime, the fact is that the capital sourced from the state treasury has been lost with the loss of entities and company assets due to bankruptcy. As a result, the state, as a legal subject, has lost its wealth in the form of shares of bankrupt state companies. This loss can also lead to the collapse of the government's authority in front of its citizens because it cannot manage state assets sourced from taxes and other sources of wealth.

CONFLICT OF INTEREST

The authors declare that they do not have any conflict of interest.

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