

## The Handling of Credit Problems in Bank Financial Restructuring

Shimada A. S. Momoto<sup>1)</sup>, Ong Argo Victoria<sup>2)</sup> & Kaukazu Shimura<sup>3)</sup>

<sup>1)</sup> Kyusu University, Japan, E-mail: [momotoshimada@yahoo.com](mailto:momotoshimada@yahoo.com)

<sup>2)</sup> International Islamic University Malaysia (IIUM), E-mail: [argovictoriaupin@gmail.com](mailto:argovictoriaupin@gmail.com)

<sup>3)</sup> Tokyo University, Japan, E-mail: [shimurasensei@yahoo.com](mailto:shimurasensei@yahoo.com)

**Abstract.** *The effort to minimize potential losses from problem loans is that banks can carry out credit restructuring. Implementing credit restructuring for problem loans means that debtors can again fulfill their obligations to the bank, namely in the form of paying principal installments and/or credit interest which has been given relief tailored to the debtor's capabilities. The result of credit restructuring is that the debtor's business continuity becomes viable again so that the debtor can fulfill his obligations to the bank. The obstacles that arose in the restructuring process were able to be overcome by the bank optimally and proportionately. The solution adopted is also a method that is profitable for both parties, so that both parties (debtor and creditor) avoid the element of loss.*

**Keywords:** *Banks; Credit; Problem; Solution.*

### 1. INTRODUCTION

The definition of a bank is: "Banks are Commercial Banks and Rural Banks as intended in the applicable banking law." Article 4 of the Banking Law, the functions of banks are: "Banking aims to support the implementation of national development in the context of increasing equity, economic growth and national stability towards increasing the welfare of the people at large." Banks, as institutions that have licenses to carry out many activities, have a very broad opportunity to earn income (income/return). In carrying out activities, banking income is always faced with risks. Basically, risk is inherent in all bank activities. One of the risks that banks must face is problematic credit<sup>1</sup>.

The credit provided goes well and the debtor pays it off in accordance with what was agreed in the credit agreement, then the relationship between the bank and the debtor ends. However, considering that granting credit also carries the risk of failure to repay, there is the possibility of problematic credit<sup>2</sup>. Problem credit is a condition where the

<sup>1</sup> Millstein, I. M., Gregory, H. J., & Grapsas, R. C. (2006, January). Six priorities for boards in 2006. *Weil Briefing: Corporate Governance*. New York: Weil, Gotsal & Manges.

<sup>2</sup> National Association of Corporate Directors (NACD) in collaboration with Mercer Delta Consulting. (2006). *The role of the board in CEO succession*. Washington, DC, and New York: Author.

debtor defaults, where a situation where due to negligence or mistake, the debtor cannot fulfill the performance as specified in the agreement and is not in a forced condition to pay interest and/or credit principal that is due, resulting in late payments or no payments at all. Problematic loans that can occur at a bank have the potential to cause losses to the bank concerned<sup>3</sup>.

The classification of non-performing loans is contained in Article 12 paragraph (3) of Bank Regulation Number 14/15/PBI/2012 concerning Assessment of Commercial Bank Asset Quality, credit quality is determined to be: current, on special mention, substandard, doubtful, or loss<sup>4</sup>.

The first collectibility is smooth collectability, 0 days old, meaning there are no problems with payment. The second collectibility is of special concern, meaning the quality of credit that is in arrears ranging from 1 to 90 days. The third collectibility is substandard, aged 91 days to 120 days. Then, the fourth collectibility is doubtful, aged 121 days to 240 days. And finally, the collectibility of the jam is 241 days to 365 days<sup>5</sup>. Meanwhile, regarding the collectibility of bad loans, namely: Bad credit is credit that is in arrears or the occurrence of arrears in both principal and interest obligations for more than 180 days.

One of the efforts to minimize potential losses from non-performing loans is that banks can carry out credit restructuring for debtors who still have business prospects and the ability to pay after the restructuring. Credit restructuring is a process for restructuring problematic loans with the aim of improving the debtor's financial position.

The restructuring steps contained in Article 1 number 26 of Bank Regulation Number 14/15/PBI/2012 concerning Asset Quality Assessment for Commercial Banks, in the form of lowering loan interest rates, extending the time period, reducing loan interest arrears, reducing loan principal arrears, adding credit facilities, and/or credit conversion into temporary capital participation.

This condition of credit congestion will not only affect the perception of parties or customers, but will also affect the bank. The existence of bad credit conditions will cause banks to lack funds. This will have a negative impact on the demand for business activities carried out by the bank. For this reason, every financial institution that offers loan funds must maintain its NPL (Non-Performing Loan) value so that it can always be low if they want to continue to run their business<sup>6</sup>.

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<sup>3</sup> Petra, S. T. (2006). Corporate governance reforms: Fact or fiction. *Corporate Governance*, 6(2), 107–115.

<sup>4</sup> Monks, R. A. G. (2005, March). Corporate governance—USA—fall 2004 reform—the wrong way and the right way. *Corporate Governance*, 13(2), 108.

<sup>5</sup> Nash, J. (2008, March 28). CEO pay: Performance-based bonuses down, discretionary bonuses up in '07. *Financial Week*.

<sup>6</sup> Rivero, J. C., & Nadler, D. A. (2003). Building a valuable relationship between CEOs and their boards. *Mercer Management Journal*.

If there are only one or two creditors experiencing bad credit, it won't be a problem, but if there are many of them and they take place simultaneously, then the NPL (Non Performing Loan) from the financial institution will definitely increase<sup>7</sup>.

## 2. RESEARCH METHODS

The legal research method used by the author in this research is the empirical juridical method. The research specifications for this research are descriptive analytical description specifications. The data collected for research consists of primary data and secondary data. This primary data was obtained by direct interviews with informants and observations<sup>8</sup> regarding the objects studied, especially regarding credit restructuring and the consequences after credit restructuring of non-performing loans.

## 3. RESULTS AND DISCUSSION

### 3.1. The Problematic of Credit

In general, credit is considered current if there are no arrears in principal installments, interest or overdrafts due to withdrawals. Loan submissions submitted by prospective debtors to banks will be processed by the bank through a credit<sup>9</sup> process using analysis based on the 7C principles, namely character, capital, capacity, collateral, and condition. Coverage (insurance), Constraint (limits and barriers). After these seven principles are fulfilled by the prospective debtor, the bank has the right to approve or reject the credit application submitted by the prospective debtor<sup>10</sup>.

After the bank approves the credit application submitted by the prospective debtor, a loan and borrowing agreement occurs between the bank (as creditor) and the customer (as debtor) which is stated in the credit agreement. Credit agreement made by PT. BCA Tbk. is a standard agreement (standard contract) / where in the agreement the debtor is only in a position to accept and sign the standard agreement without negotiating or bargaining<sup>11</sup>.

In reality, the credit provided by PT. BCA Tbk., not everything goes smoothly, even the credit given cannot be returned in full by the debtor, which carries business risks for the bank, which eventually causes problem loans to even become bad credit<sup>12</sup>.

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<sup>7</sup> Rérolle, J.-F., & Vermeire, T. (2005, April 29). M&A best practices for boards of directors. From Houlihan, Lokey, Howard, & Zukin, *Corporate Board Member Magazine*, M&A /Capital Markets.

<sup>8</sup> Matheson, J. H., & Olson, B. A. (1992). Corporate law and the long term shareholder model of corporate governance. *Minnesota Law Review*, 76, 1313–1391.

<sup>9</sup> Ong Argo Victoria, Ade Riusma Ariyana, Devina Arifani. (2020). *Code of Ethics and Position of Notary in Indonesia*. *Sultan Agung Notary Law Review* 2 (4), 397-407, <http://lppm-unissula.com/jurnal.unissula.ac.id/index.php/SANLaR/article/view/13536> see Yaya Kareng, Ong Argo Victoria, R. Juli Moertiyono. (2019). How Notary's Service in Thailand. *Sultan Agung Notary Law Review*, 1 (1), 46-56, <http://jurnal.unissula.ac.id/index.php/SANLaR/article/view/4435>

<sup>10</sup> Lipton, M., & Savitt, W. (2007, May). The many myths of Lucian Bebchuk. *Virginia Law Review*, 93(3), 733.

<sup>11</sup> Lorsch, J. (1995, January–February). Empowering the board. *Harvard Business Review*, 73(1), 107–117.

<sup>12</sup> Salwen, K. G. (1992, February 14). Shareholder groups cheer SEC's moves on disclosure of executive compensation. *Wall Street Journal*, p. A-4.

There are several factors that influence the cause of problematic credit, namely factors originating from the debtor and factors originating from the bank. Factors originating from the debtor: the debtor misuses credit, the debtor is less able to manage his business, the debtor has bad intentions. Factors originating from the bank: internal factors, namely due to expansive credit policies, irregularities in credit granting procedures,<sup>13</sup> bad faith on the part of bank owners/managers/employees, weak credit administration and supervision, weak problem credit information system; external factors, namely due to the decline in economic activity and high credit interest rates, unhealthy business competition climate, failure of the debtor's business, disasters that befall the debtor's business activities<sup>14</sup>.

Credit restructuring needs to be done to overcome problem loans that are being experienced by debtors, because these problem loans have an influence on the ability to fulfill debtor payment obligations to the bank, resulting in the debtor failing to pay obligations in the form of principal and/or interest installments to the bank<sup>15</sup>.

Prior to settling problem loans with credit restructuring, the bank previously sought direct billing from its debtor customers who had problems paying the principal installments and/or interest on loans that were due. Efforts made by banks prior to credit restructuring by means of: gradual repayment; payment at once; internal memorandum of exemption from interest and fines, namely in the form of 50% interest relief and 100% penalty relief for arrears in installments in the form of principal and interest that have not been paid by the debtor<sup>16</sup>. If these three methods do not work, then the bank will immediately provide an alternative settlement of problem loans faced by debtors with credit restructuring before the problem loans become bad and are resolved through legal institutions<sup>17</sup>.

The purpose of implementing credit restructuring for non-performing loans is: to avoid losses for banks because banks must maintain the quality of the credit they have given; to help ease the debtor's obligations so that with this relief the debtor has the ability to resume his business, and by reviving his business the debtor will receive income which can be partly used to pay off his debts and partly to continue his business activities; and with restructuring, settlement of problem loans through legal institutions can be avoided, because settlements through legal institutions in practice

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<sup>13</sup>Kaldor, M., Anheier, H., & Glasius, M. (2003). Global civil society in an era of regressive globalisation. In M. Kaldor, H. Anheier, & M. Glasius (Eds.), *Global civil society 2003* (pp. 3–33). Oxford: Oxford University Press.

<sup>14</sup> Coffee, J. C., Jr. (2003a). Corporate gatekeepers: Their past, present, and future. (Duke Law School, Working Paper No. 7). *Duke Law Journal*, 7.

<sup>15</sup> Jensen, M. C. (2001). Value maximization, stakeholder theory, and the corporate objective function. *European Financial Management Review*, 7(3), 297–317.

<sup>16</sup> Spencer Stuart, Board Services Practice. (2008). *Cornerstone of the board—the nonexecutive chairman: Offering new solutions*. New York: Author.

<sup>17</sup> Chuasanga A., Ong Argo Victoria. (2019). *Legal Principles Under Criminal Law in Indonesia and Thailand*, Jurnal Daulat Hukum, Vol 2, No 1 (2019) <http://jurnal.unissula.ac.id/index.php/RH/article/view/4218> see Deen, Thaufiq., Ong Argo Victoria & Sumain. (2018). *Public Notary Services In Malaysia*. *JURNAL AKTA*: Vol. 5, No. 4, 1017-1026. Retrieved from <http://jurnal.unissula.ac.id/index.php/akta/article/view/4135>

require a lot of time, cost and effort and the result is lower than the receivables collected.<sup>18</sup>

Banks are required to complete their credit guidelines with written guidelines regarding credit restructuring as a guide regarding procedures and procedures required in carrying out credit restructuring. The said credit restructuring guidelines must at least contain the following matters: Analysis and Documentation.

After carrying out analysis and documentation, banks are required to have written procedures to monitor restructured credit to ensure the debtor's ability to make repayment according to the terms of the new credit agreement.<sup>19</sup>

Based on the general guidelines for credit restructuring during the implementation of credit restructuring, namely in the form of analysis and documentation, and after the implementation of credit restructuring, namely in the form of monitoring as previously mentioned, PT. BCA Tbk., has guidelines for implementing credit restructuring based on the Guidebook on Credit Policy, namely by carrying out the following things: meeting with debtors; analysis; restructuring requests, restructuring offers, restructuring supporting documents, restructuring agreements, and monitoring.

### **3.2. The Legal Consequences after Bank Credit Restructuring for Problematic Credit**

After the implementation of credit restructuring for non-performing loans goes according to the agreement of both parties, the implementation of the credit restructuring has an impact on the debtor and also the bank<sup>20</sup>.

Credit restructuring that has been implemented for non-performing loans has a success percentage of 50% and 50% failure. This is because the credit restructuring of non-performing loans does not increase the amount of the previous credit ceiling but what becomes the new ceiling is the outstanding loan principal on the previous credit, so that in this case the debtor is in a defensive position over the business and financial conditions it faces. Credit restructuring carried out by banks only provides relief in installment payments of debtor obligations, so it is hoped that with this relief, debtors can fulfill their obligations to the bank<sup>21</sup>.

Credit restructuring is declared successful if the debtor experiences the following: a. the debtor's business activities are able to survive and run well after the implementation of credit restructuring; b. the debtor is able to pay the principal and/or interest on the credit after the credit restructuring is implemented; and c. the debtor is able to survive for approximately one year after the implementation of the credit

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<sup>18</sup>Charan, R. (2005). Ending the CEO succession crisis. *Harvard Business Review*, 83(2), 72–81.

<sup>19</sup>Sundaram, A. K., & Inkpen, A. C. (2004, May–June). The corporate objective revisited. *Organization Science*, 15(3), 350–363.

<sup>20</sup>Coffee, J. C., Jr. (2002). Understanding Enron: It's about the gatekeepers, stupid (Columbia Law and Economics, Working Paper No. 207). *Business Law*, 57, 1403.

<sup>21</sup>Carver, J. (2007, November). The promise of governance theory: Beyond codes and best practices. *Corporate Governance*, 15(6), 1030–1037.

restructuring by carrying out the obligation to pay installments of principal and/or credit interest as agreed in the credit restructuring at the time mutually agreed upon<sup>22</sup>.

The percentage of success of 50% and failure of 50% in the implementation of credit restructuring shows that the implementation of credit restructuring for problem loans has advantages and disadvantages, including<sup>23</sup>: Debtors obtain relief in fulfilling their obligations to the bank in the form of principal and/or interest installments after restructuring which are smaller than loans before restructuring. ; the debtor obtains an extension of the credit period after the restructuring to be longer than the credit before the restructuring; lighter credit installments with the addition of a longer credit term, actually increases the interest burden even more, because the shorter the credit term, the smaller the interest burden, conversely, if the credit term is longer, the interest burden will be greater<sup>24</sup>.

The stages of implementing credit restructuring as described above do not always go smoothly according to the wishes of the bank, because in the field there are obstacles that will be faced by bank officials, therefore bank officials are required to be able to overcome obstacles in the field with the following steps<sup>25</sup>.

#### **a. Meeting with Debtors**

Obstacles during meetings with debtors: the debtor shows hostility, the debtor always refuses rescue efforts made by the bank, during interviews the debtor covers up the financial difficulties he is facing and the debtor is out of town. In this case the debtor has bad faith by giving false information during the interview and also does not want to complete his obligations to the bank.

The effort to overcome this is that the bank should be patient but must also be firm regarding the bad faith shown by the debtor. In addition to approaching the debtor, the bank can also approach the debtor's family or business partners, with the aim of making the debtor more open to raising problems. faced him. The bank must play an active role in meeting the debtor, while the debtor himself must have good faith towards the bank by providing actual information about the problems he is facing, so that the bank can provide a solution the best for the debtor's problems.

#### **b. Analysis**

Obstacles during analysis: during the interview the debtor does not provide truthful information, the debtor pretends to be in a difficult situation because he only wants to obtain maximum relief. Based on the assessment of the collateral submitted by the debtor, the bank assesses that the collateral submitted by the debtor has decreased in price so that if restructuring is carried out, the collateral will not be sufficient to cover

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<sup>22</sup> Thornton, E. (2002, January 14). The bids sure are getting hostile: Unsolicited offers are on the rise in a market ripe for consolidation. *Business Week*.

<sup>23</sup> United Nations Conference on Trade and Development (UNCTAD). (2004). *The shift towards services*. World Investment Report 2004. Geneva: Author.

<sup>24</sup> Springer, J. D. (1999). Corporate law and constituency statutes: Hollow hopes and false fears. *New York University Annual Survey American Law*, 122.

<sup>25</sup> Wood, D. (2005). *Red flags in management culture, strategies, and practices*. National Association of Corporate Directors.

the loan ceiling to be restructured. So, in this case, the bank must ensure that the customer has a loan at another bank, and must investigate whether the customer has a business outside the city.

The effort to overcome this is that the bank must check the information during the interview with the debtor whether it is true that the debtor is having financial difficulties by looking at the activity of the debtor's loan account, if the bank has drawn the conclusion that what the debtor said is true based on the facts on the activity of the loan account, then the bank can offer restructuring of debtor's non-performing loans. While the assessment of collateral that has decreased, the bank will try to ask the debtor for additional collateral, but if the debtor does not have other collateral used as collateral, then the bank can see whether the debtor's business condition can still run well if the financial difficulties faced by the debtor are saved. If the debtor's business is still running<sup>26</sup>.

### **c. Restructuring Application**

Obstacles when requesting restructuring: debtors are asked by the bank to make an official restructuring request letter, sometimes there are debtors who cannot make the letter as desired by the bank.

In an effort to overcome this, the bank can help make a draft of the restructuring request letter, then the letter is shown to the debtor to read and understand its contents. If the debtor understands the contents of the restructuring request letter, the debtor is asked to make and write it in his own hand and sign it by the debtor.

### **d. Restructuring Offer**

Obstacles at the time of the restructuring offer: the debtor feels that the non-performing loans that will be restructured are only the outstanding loan principal without adding to the ceiling or returning the original ceiling at the time of the first credit. The debtor will assume that this will actually increase the interest expense and a long period of time in repayment of credit.

Efforts to overcome this, namely the bank can provide an explanation to the debtor that the problem loans they face if allowed to drag on, will cause bad credit, so the bank provides installment relief to the debtor by increasing the credit period with the aim of assisting the debtor in fulfilling his obligations to the bank by installments that are smaller than the credit received for the first time, the bank can also explain that if the debtor is able to fulfill the principal and/or interest installment obligations as agreed in the restructuring for one year after the credit restructuring, the debtor can apply for additional working capital to the bank.

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<sup>26</sup> Carter, C. B., & Lorsch, J. W. (2004). *Back to the drawing board—Designing corporate boards for a complex world*. Boston: Harvard Business School Press.

### **e. Restructuring Supporting Documents**

Obstacles when supporting documents for restructuring: the debtor provides complete supporting documents for restructuring, but the completeness of these documents does not match what is expected by the bank, so the bank has difficulty analyzing the supporting documents for the restructuring process. The effort to overcome this is that the bank must examine the validity of the restructuring supporting documents that have been submitted by the debtor. If there are documents that are inconsistent or lacking, then the bank can ask the debtor to complete the discrepancies in the supporting documents so that the restructuring implementation can run smoothly<sup>27</sup>.

### **f. Restructuring Agreement**

Obstacles at the time of the restructuring contract: the debtor does not understand the words and understands what is contained in the agreement on changes to the credit agreement made by the bank at the time of the restructuring agreement, thereby canceling what was agreed before the contract, so that the implementation of the restructuring does not go as expected from the party bank.

The solution is that before the restructuring agreement is executed, the bank first shows and explains the contents of the draft amendment agreement to the credit agreement made by the bank, to be read and understood by the debtor first, so that the debtor can ask what is not yet known and understand the contents of the draft agreement<sup>28</sup>, so that the bank can explain correctly and provide understanding of the contents of the draft agreement, if the debtor has understood and understood the contents of the draft agreement, the debtor will agree by signing the draft agreement at the time of the restructuring agreement<sup>29</sup>.

### **g. Monitoring (Supervision)**

Obstacles during monitoring: the bank cannot carry out supervision of the debtor's business activities for 1x24 hours due to limited staff of bank officials who cannot monitor the debtor's business activities continuously due to many work assignments<sup>30</sup>.

Efforts to overcome this are bank official staff who are tasked with carrying out supervision of the debtor's business activities. directly can be carried out once a month, besides that apart from direct supervision of the debtor's business activities, the bank can also see the activity of the debtor's loan account whether after carrying out the restructuring the debtor fulfills his obligations at the time agreed in the amendment agreement to the credit agreement that was signed at the time of restructuring agreement.

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<sup>27</sup> Keinath, A. K., & Walo, J. C. (2004, November 23). Audit committee responsibilities: Focusing on oversight, open communication, and best practices. *The CPA Journal*, 74(11), 22–29.

<sup>28</sup> Khurana, R., & Pick, K. (2005). The social nature of boards. *Brooklyn Law Review*, 70(3), 1259–1285.

<sup>29</sup> Bainbridge, S. M. (1993). In defense of the shareholder wealth maximization norm: A reply to Professor Green. *Washington and Lee Law Review*, 50, 1423.

<sup>30</sup> Stewart, J. K., & Countryman, A. (2002, February 24). Local audit conflicts add up: Consulting deals, hiring practices in question. *Chicago Tribune*, p. C-1.



#### 4. CONCLUSION

The result of credit restructuring for non-performing loans can also be said to be a benefit for customers, namely that the debtor's business continuity becomes alive again so that the debtor can fulfill his obligations to the bank, which has an impact on the credit quality after the restructuring becomes smoother, thus the bank's health level becomes better. And with credit restructuring, problem credit resolution through legal institutions can be avoided, because in practice settlement through legal institutions requires a lot of time, costs and energy and the results are lower than the receivables collected. Customers are also given leeway in recovering businesses that have declined with restructuring in the hope that they can improve existing businesses.

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