

Non-Voting Shares and Its Disadvantages

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Type of Shares

Shares are defined as an evidence of payment of paid-up capital by shareholders of a limited liability company. Article 53 of Law Number 40 of 2007 regarding Limited Liability Company (“**Indonesian Company Law**”) provides classification of shares as follow:

- a. shares with voting rights or without voting rights;
- b. shares with special rights to nominate members of the Board of Directors and/or members of the Board of Commissioners;
- c. shares which after a certain period of time are redeemable or exchangeable for another classification of shares;
- d. shares which grant the holders a preferred right to receive cumulative or non-cumulative dividends, prior to the holders of other classifications of shares;
- e. shares which grant the holders a preferred right to receive assets remaining after the Company’s liquidation, prior to the holders of other classifications of shares.

Common Shares (*Saham Biasa*)

In general, common shares provides voting rights in shareholders meeting and rights to receive annual dividend and to bear any inherent liabilities. Any share with voting rights represents one vote in shareholders meeting (one share one vote).

In the event of the shareholders cannot attend to the meeting, they can be represented by their proxies including to attend, to discuss and to cast vote on behalf of the authorizer.

Non-voting Shares

Other type of shares is shares with limited authority. Holder of this shares is entitled to receive dividend, but not to cast vote in shareholders meeting. It is commonly known as non-voting shares.

This type of shares is made for certain purposes such as part of commercial negotiation, collateral of loan, fulfillment of local equity participation and so on. For instance, independent creditors may require pledge of shares or fiduciary security of shares as collateral, regardless with or without voting shares because repayment of loan is the main concern, not to involve in managing company or making business decisions.

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Disadvantages of holding Non-voting Shares

Asides from the commercial negotiation, holding non-voting shares would significantly affects rights and interest of the shareholders. There are five disadvantages as follow:

- a. Organizing Extraordinary General Meeting of Shareholders (EGMS). Pursuant to Article 79 (2) of the Indonesian Company Law, the EGMS can be organized based on request of minimum 10% of the total issued shares with voting rights. Therefore, holder of non-voting shares never be able to initiate EGMS without inviting other holders of voting shares.
- b. Appointment of Directors and Commissioners. Based on Article 94 and Article 111 of the Indonesian Company Law, directors and commissioners are appointed by general meeting of shareholders. If a shareholder is not entitled to appoint director or commissioner, it will lost its power to determine company's business policies.

In a real joint venture (JV) business where each party gives equal contribution to a JV company, non-voting shares will less likely be issued. In fact, the contracting parties will determine number of director or commissioner slots that can be occupied by each party. It is because they need equal power and control over the management of the JV company.

- c. Pre-emptive Rights. In case of the company issue new common shares, non-voting shares holder will not be firstly offered by the company as the shareholder for the same classification of shares will be prioritized based on Article 43.1 of the Indonesian Company Law.
- d. Making business decision. Besides day-to-day business decisions made by directors, holders of voting shares are entitled to make business decision such as doing merger, acquisition, consolidation, separation or selling company's assets, etc. These actions will significantly affect company's profit and dividends which will be distributed to all shareholders, including holders of non-voting shares.
- e. Derivative suit and Investigation of company. As required by Article 97.6, Article 114.6 and Article 138 of the Indonesian Company Law, filing derivative suit, in terms of company, directors or commissioners who due to their fault or negligence has incurred losses to the company or shareholders, can only be done by the holder of minimum 10% of voting shares.

Notwithstanding, Article 61 and Article 62 of the Indonesian Company Law still provide protection for holders of non-voting shares to file derivative suit if they suffer losses due to unfair or unreasonable actions conducted by general meeting of shareholders, directors or commissioners. Further, holders of non-voting shares are entitled to require the company to purchase their shares at a reasonable price.

Being a holder of non-voting shares is somehow part of the business deal, in which its disadvantages must carefully be considered to minimize potential losses and lack of company's management control.