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# Hostile Takeover Law and the Challenges in Market for Corporate Control: A Comparative Analysis between Indonesia and the United Kingdom

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## Abstract

*The concept of hostile takeover is still unrecognized under Indonesian laws and regulations despite its importance in keeping the corporate board in check and corporate governance better implemented in a company. This article seeks to explore the extent of the current environment and regulation in Indonesia able in accommodating hostile takeover in relation to the market for corporate control in Indonesia by using hostile takeover as a mechanism to measure. A comparative analysis is then conducted with the United Kingdom United Kingdom as a country with an active market for corporate control, specifically with the methods employed to deal with hostile takeover.*

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## 1. Introduction

The numbers for Merger and acquisition (hereinafter referred as 'M&A') volume showed an increase of 182% by volume of M&A deals in Indonesia from 2014 to 2017,<sup>1</sup> and it remained strong with a total M&A value of approximately 150 trillion rupiah in 2018 sourced from 69 M&A deals that were registered to the Indonesian Business Competition Supervisory Commission.<sup>2</sup> In alignment with the prevalence of M&A interest in Indonesia, the United Kingdom remained one of the most resilient jurisdiction for M&A with the recently finalized deal with 27 billion US Dollars' worth of merger between the London Stock Exchange and Refinitiv which suffer from delay due to the COVID-19 pandemic.<sup>3</sup> The number of M&A is influenced by various macroeconomic, microeconomic as well as institutional factors,<sup>4</sup> but developments that may result in Indonesia's increasing economic condition is the government's action in simplifying the establishment of a company through Online Single Submission system in 2018, as well as the simplification of foreign worker regulations and tax incentives for venture capital, which in the end contributes to overall Gross Domestic Product (hereinafter referred as 'GDP') growth.<sup>5</sup>

In 2017, PT Indika Energy Tbk acquired PT Kideco Jaya Agung with a transaction value of \$678 million, followed by the acquisition of PT Surya Muska Nusantara and PT Karyadibya Mahadirka by Japan Tobacco Inc. with a total value of \$677 million.<sup>6</sup> In 2019, the transaction volume decreased to 94 deals which was 54 deals lesser than the previous year.<sup>7</sup> A takeover or acquisition could be divided into a friendly or a hostile takeover. The above instances reflect a friendly takeover where both the

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<sup>1</sup> Gopalakrishnan, S. C., & McLaren, A. (2017). *Transaction Trail Annual Issue 2017*. Retrieved June 3, 2020.

<sup>2</sup> Prasetyo, A. H. (2018). *Sepanjang 2018, Nilai Transaksi Merger Dan Akuisisi Ditaksir Melampaui Rp 150 Triliun*. Retrieved Marc 2, 2020, from <https://insight.kontan.co.id/news/sepanjang-2018-nilai-transaksi-merger-dan-akuisisi-ditaksir-melampaui-rp-150-triliun?>

<sup>3</sup> Huw, J. (2020). *London Stock Exchange Committed to Refinitiv Deal in Pandemic-Hit Markets*. Retrieved March 2, 2020, from <https://www.reuters.com/article/us-lse-results/london-stock-exchange-committed-to-refinitiv-deal-in-pandemic-hit-markets>

<sup>4</sup> Carbonara, G. & Caiazza, R. (2009). Mergers and Acquisitions: Causes and Effects. *The Journal of American Academy of Business*, 14,188–95.

<sup>5</sup> Tambunan, F. J., & Andhika, A. (2019). Trends In Mergers and Acquisitions in Indonesia. *InHouseCommunity*.

<sup>6</sup> *Ibid.*

<sup>7</sup> Gopalakrishnan, S. C. (2019). *Transaction Trail Annual Report 2019*. Retrieved June 23, 2020, from <https://www.duffandphelps.com/-/media/assets/pdfs/publications/valuation/valuation-insights/transaction-trail-report-2019.pdf>

bidder and target company negotiate to work out a way to unite. The Indonesian law defines takeover as a change in the company share ownership which results in the “transfer of control within the company”,<sup>8</sup> however term “hostile takeover” remains unrecognized under Indonesian laws and regulations.

Hostility in a hostile takeover is typically characterized when an offer is announced publicly but aggressively rejected by the target company.<sup>9</sup> Although it is best to approach a target company in a “friendly manner”, sometimes bidders are left with no choice but to proceed to an “unfriendly” – hostile takeover. As the Indonesian law is not familiar with the term “hostile takeover”, not many cases of takeovers are linked to it. Nonetheless, it cannot be denied that hostile takeovers still take place in Indonesia. For instance, in 2009, Carrefour Indonesia, Ltd claimed that the owner of the rental agency, Duta Wisata Loka, Ltd, was involved in a hostile takeover which led to unilateral termination of contract, causing great loss to Carrefour Indonesia, Ltd.<sup>10</sup> In 2018, one of the shareholders in Tiga Pilar Sejahtera Food, Ltd was suspected to be involved in a hostile takeover.<sup>11</sup> Despite the allegations of hostile takeovers, it is still unlikely for a hostile takeover to take place in Indonesia due to the occupation of major controlling shareholders in the share ownership of a public company.<sup>12</sup> However, applying different regulations to the takeover regime may affect company processes differently<sup>13</sup> and as such, further studies are needed to reflect on the possibility of Indonesia’s reform on hostile takeover recognition under its laws and regulations.

The phenomena of M&A increase can also be explained through the “market for corporate control” theory. The market for corporate control is a theory where the

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<sup>8</sup> Law No. 40 of 2007, Article 1 number 11.

<sup>9</sup> G. William Schwert. (2000). Hostility in Takeovers: In the Eyes of the Beholder?. *Journal of Finance*, 55(6), 2599–2640. <https://doi.org/10.1111/0022-1082.00301>.

<sup>10</sup> Maria, H. (2009). *Carrefour Gugat Pemilik Mega Mal Pluit*. Retrieved August 2, 2020, from <https://koran.tempo.co/read/ekonomi-dan-bisnis/174714/carrefour-gugat-pemilik-mega-mal-pluit?>

<sup>11</sup> Wareza, M. (2020). *Tiga Pilar Dan Drama Penggelembungan Dana*. Retrieved December 3, 2020, from <https://www.cnbcindonesia.com/market/20190329075353-17-63576/tiga-pilar-dan-drama-pengelembungan-dana>.

<sup>12</sup> Ira, A. E., & Fahrul, S. Y. (2019). *Corporate M&A’ in Chambers Global Practice Guide* (2<sup>nd</sup> ed). *Chambers Global Practice Guide*.

<sup>13</sup> For example, see: Santos, R. J. (2013). *Positive Or Negative? The Impact of Anti-Takeover Legislation On R&D Investments*. Catolica Lisbon School

control of a company is regarded as a valuable asset, which exists without any relations to any interest in either economies of scale or monopoly market where many M&A deals are the output of the special market,<sup>14</sup> and correctly regulating the market for corporate control vis-à-vis hostile takeover has been long proposed as a solution in implementing better corporate governance.<sup>15</sup>

Viewing from the perspective of this theory, a hostile takeover is considered as a mechanism for corporate control.<sup>16</sup> To simplify, when a company is poorly managed, it opens a chance for a more capable person or people to make changes for the company by taking over it. In a way, the hostile takeover system becomes a “threat” to public-owned companies which will trigger these companies to increase the value of their share prices, yielding to an improved performance of the management to prevent hostile bidders to overtake the company. Thus, there will be a more dynamic and active market with excellent efficiency of corporate management.

Furthermore, the general shareholding profile in a company also play a role in determining whether M&A increases since shareholders have the final say in any merger or acquisition in the majority of countries. Indonesia’s business environment is thronged by controlling shareholders,<sup>17</sup> in which the 2012 data of Organization for Economic Co-operation and Development showed that out of 186 companies, 70% of the shares were owned by controlling shareholders and 54% are family-owned business.<sup>18</sup> The dominance of controlling shareholders, block-holders, is a typical characteristic of a network-oriented system of corporate governance. The distribution of shares within the company’s shareholder is not widely distributed. In that sense, companies with small number of large controlling shareholders typically prefer holding their shares more than trading. In other words, it would be difficult for

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<sup>14</sup> Manne, H. G. (2019). Mergers and the Market for Corporate Control. *Corporate Governance: Values, Ethics and Leadership*, 27–38. <https://doi.org/10.1086/259036>.

<sup>15</sup> Coffee, J. C. (1984). Regulating the Market for Corporate Control: A Critical Assessment of the Tender Offer’s Role in Corporate Governance. *Columbia Law Review*, 84(5), 1145. <https://doi.org/10.2307/1122351>.

<sup>16</sup> Diana, L. F. (1989). Hostile Takeovers and the Market for Corporate Control. *Economic Perspectives*, 13, 2.

<sup>17</sup> Eng, P. van der. (2004). Business in Indonesia: Old Problems and New Challenges. In M. C. Basri & P. van van der Eng (Eds.), *Business in Indonesia: New Challenges, Old Problems* (pp. 1–20). ISEAS–Yusof Ishak Institute. <https://doi.org/undefined>

<sup>18</sup> Organisation for Economic Cooperation and Development. (2017). *OECD Corporate Governance Factbook 2017* (p. 13).

any outsiders to acquire a stringent management board. Consequently, this raises a question of the role of takeover in Indonesia, perhaps the rarity of the occurrence of hostile takeover reflects a poor market for corporate control.

The United Kingdom is the complete opposite of Indonesia with regard to shareholder profile and hostile takeover situation. United Kingdom entrusts the power to the shareholders, with the absolute ban of takeover defences exhibiting a very lenient approach when it comes to dealing with hostile takeovers.<sup>19</sup> From 1990 to 2005, there were 312 cases of hostile takeover in the UK,<sup>20</sup> and hostile takeover has been long recognized by the regulation in United Kingdom. The United Kingdom City Code on Takeovers and Mergers (hereinafter referred as 'City Code') is a shareholder-oriented regulation which was voiced by institutional investors who dominated public-owned companies' shares since the 1950s.<sup>21</sup> Overall, the market-oriented system of corporate governance in United Kingdom allows a more widespread ownership of share within a company, an active market for corporate control, and a flexible labour market,<sup>22</sup> which in the end prevents the formation of block-holders.<sup>23</sup> It is also through the City Code that the United Kingdom banned post-bid takeover defence which promote the success of hostile takeover.

## 2. Problem Statement

The paper seeks to answer how well is the market for corporate control in Indonesia by using hostile takeover as a mechanism to measure, and as such, is based on the following research questions; to what extent does the current state and regulatory framework in Indonesia able to accommodate the practice of hostile takeover, and what lessons can Indonesia extract from United Kingdom, as a state with an active market for corporate control, in dealing with hostile takeover.

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<sup>19</sup> Alexandros, S. (2013). Hostile Takeovers and Defensive Mechanisms in the UK and the US: A Case against the US Regime. *The Ohio State Entrepreneurial Business Law Journal*, 8.

<sup>20</sup> Armour, J., & Skeel, D. A. (2007). Who writes the rules for hostile takeovers, and why? - The peculiar divergence of U.S. and U.K. takeover regulation. *Georgetown Law Journal*, 95(6), 1727-1794.

<sup>21</sup> John, A., Jack, B. J., & Curtis, J. M. (2011). The Evolution of Hostile Takeover Regimes in Developed and Emerging Markets: An Analytical Framework. *Harvard International Law Journal*, 52(1), 219.

<sup>22</sup> Morten, H. (2007). *Boards, Governance and Value Creation: The Human Side of Corporate Governance*. Cambridge University Press.

<sup>23</sup> Block-holders are shareholders who occupy a large amount of share ownership in a company to the point where they could influence the decision of the company through their holdings.

### 3. Methods

To answer the questions raised in the previous section, this article will utilize a normative approach. The research will not only be limited to regulatory and literature review, but also a comparative study to explore how a different jurisdiction and legal system accommodate hostile takeover based on secondary data. The regulatory analysis will specifically involve Indonesian Law No. 40 of 2007 on Limited Liability Company (hereinafter referred as 'Law No. 40/2007'), Law No. 8 of 1995 on Capital Market (hereinafter referred as 'Law No. 8/1995'), and the Regulations of Financial Services Authority. Additionally, analysis will also be supported by the provisions from the United Kingdom City Code on Takeovers and Mergers, Company Acts 2006, and Company Acts 1985 will be included for comparative purposes. Moreover, the scope will be limited to publicly listed companies since under English law, hostile takeover cannot be carried out to private companies.

### 4. Discussion

#### 4.1. Hostile Takeover Vis-À-Vis Market for Corporate Control

The perception towards hostile takeover is often stigmatized negatively by the public as it is a forced and unwanted process that could lead to the loss of public investors.<sup>24</sup> This is related to business ethics, especially in Asia, where business and personal relations in a company are more valued and prioritized,<sup>25</sup> considering the dominance of family-owned business and controlling shareholders within a company. In spite of that, this article views how hostile takeovers may become the key to improve corporate governance under the context of market for corporate control.

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<sup>24</sup> Parluhutan. (2019). *Hostile Takeover Bisa Rugikan Publik, Otoritas Pasar Modal Diminta Beri Perhatian*. Retrieved July 23, 2020, from <https://investor.id/market-and-corporate/hostile-takeover-bisa-rugikan-publik-otoritas-pasar-modal-diminta-beri-perhatian>.

<sup>25</sup> See for example: Chung, K. Y., Eichenseher, J. W., & Taniguchi, T. (2008). Ethical Perceptions of Business Students: Differences between East Asia and the USA and among "Confucian" Cultures. *Journal of Business Ethics*, 79(1-2), 121; Isac, F. L., & Remes, E. F. (2017). Culture and Business Ethics – a Comparative Perspective. *Studia Universitatis Vasile Goldis*, 27(3), 54.

A change in corporate control could turn an undervalued company to resell it at a more profitable price considering if the company could potentially be run better. Henry G. Manne claims that the stock market is the only medium where external parties can objectively speculate on the efficiency in the management of a company which will improve the competitiveness of a company, “forcing” them to side with the interests of minority shareholders.<sup>26</sup> In other words, hostile takeover is said to offer minority shareholders the same proportion of power and protection to be involved in the company’s affairs.<sup>27</sup> Moreover, the hostile takeover scheme could also avoid bidders to deal with free-rider problem which is when the bidder’s profit is limited because the existing shareholders free ride on the bidder’s efforts in improving corporate performance.<sup>28</sup> This scheme also prevents the company from being sold excessively overvalued or at an unreasonable takeover price.

Thus, not only that minority shareholders are more protected, current managers of the company are more disciplined and will perform better to boost the performance of their company knowing that they can be replaced by the threat of the hostile bidders. This scheme also creates a stronger economy because if a takeover regulation can promote a healthier market for corporate control, it can prevent the personal interests of the managers to meddle within the company’s decision-making process. This illustrates how hostile takeover can contribute to increase the competitive of companies, increasing the efficiency of overall management, and strengthen the company’s welfare.

## **4.2. Hostile Takeover in the United Kingdom**

### **4.2.1. History of Hostile Takeover in United Kingdom**

The first hostile takeover happened in 1953, when Charles Clore made a tender offer to the shareholders of J. Sears & Co.<sup>29</sup> Previously, the public had limited access to financial information of the company, thus shareholders relied on regular dividend yields as the credible information of the management’s performance, hence a

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<sup>26</sup> Manne, H. G., *Loc.Cit*

<sup>27</sup> *Ibid.*

<sup>28</sup> Sanford, J. G., & Oliver, D. H. (1980). Takeover Bids, The Free-Rider Problem, and the Theory of the Corporation. *The Bell Journal of Economics*, 11(1), 42.

<sup>29</sup> Wang, X. (2020). *Takeover Law in the UK, US, And China: A Comparative Analysis and Recommendations for Chinese Takeover Law Reform*. University of Salford.

determinant of shares prices.<sup>30</sup> When the real estate values increased due to post-war inflation, the government enhanced the quality of financial reporting through the Companies Act 1948.<sup>31</sup> This allows potential bidders to judge whether or not the potential target company has been undervalued by looking at their financial account.<sup>32</sup>

To this date, the proportion of hostile takeovers in United Kingdom is relatively small comparing to the total number of takeovers. However, the transaction values of hostile takeover that occur were also relatively large. For instance, in 2017, two hostile takeovers were in the Top 10 Largest Deals in 2017 in United Kingdom.<sup>33</sup> One of the most controversial M&A transactions in the UK took place in 2010 when Kraft Foods Inc. finalized the takeover process Cadbury PLC, British largest confectionery,<sup>34</sup> in which this brought up concerns about the United Kingdom's open market for corporate control.<sup>35</sup>

Studies of the impact of mergers and acquisitions demonstrate that in the majority of cases it results in a reduction in shareholder value; but this evidence is consistently ignored by the financial community, because it is contrary to their objective of maintaining and indeed increasing their fees from M&A activities".<sup>36</sup> Furthermore, the threat of hostile takeovers pressures the management to take short-term measures to

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<sup>30</sup> Brian, R. C. (2006). Dividends as a Substitute for Corporate Law: The Separation of Ownership and Control in the United Kingdom. *Washington and Lee Law Review*, 63.

<sup>31</sup> John, A., Jack, B. J., Curtis, J. M. (2011). The Evolution of Hostile Takeover Regimes in Developed and Emerging Markets: An Analytical Framework. *Harvard International Law Journal*, 52(1), 219.

<sup>32</sup> *Ibid.*

<sup>33</sup> Kavita, B. (2017). *Market Tracker Trend Report: Trends in UK Public M&A Deals in H1 2017*. Retrieved June 14, 2020, from <https://www.lexisnexis.co.uk/blog/corporate-law/market-tracker-trend-report-trends-in-uk-public-ma-deals-in-h1-2017>.

<sup>34</sup> The British government stepped in and clearly rejected the offer because there are many employees who were laid off as a result of the takeover. Kraft increased its offer to about \$19.6 billion and the two companies finalized the takeover in 2010. Although both companies were able to end peacefully, the battle they had triggered the British government as lack of transparency in Kraft's offer and intentions became a major concern.

<sup>35</sup> Georgina, T. (2014). A Long-Term Vision for UK Firms? Revisiting the Target Director's Advisory Role Since the Takeover of Cadbury'S PLC. *Journal of Corporate Law Studies*, 14(1), 241. <https://doi.org/10.5235/14735970.14.1.241>.

<sup>36</sup> Simpson, C. V. J. (2014). *The Environment for Business in Germany: A Commentary*. Retrieved from <http://www.civitas.org.uk/pdf/BusinessInGermany.pdf>.

satisfy the interest of their shareholders.<sup>37</sup>

The action of hostile takeover has a negative stigmatization as it is unwelcomed and highly risky as it may lead to any potential loss on the shareholders. Nonetheless, the occurrence of this type of takeover reflects a positive sign of a healthy market for corporate control which maximizes the shareholders' welfare.

#### 4.2.2. United Kingdom Takeover Legal Framework

The Panel on Takeovers and Merger (hereinafter referred as 'Takeover Panel') regulates the conduct of takeovers in the United Kingdom, which is also subjected to the principles provided by the City Code on Takeovers and Mergers. The Takeover Panel is an independent body established to supervise and regulate the conduct of takeovers according to the general principles set out in the City Code.<sup>38</sup> The City Code is a collection of opinions consisting of business standards, shareholders' treatment (fairness), and framework of takeovers, from those who were professionally involved in the field.<sup>39</sup> In general, the purpose of the Takeover Panel is to ensure that shareholders receive fair treatment either by internal management or bidder, and are granted equal opportunity to decide on the merits of a takeover.<sup>40</sup>

The implementation of the Takeover Panel and City Code never had a statutory basis until the European Directive on Takeover Bids 2004/25/EC (hereinafter referred as 'Takeover Directive') was introduced. United Kingdom was required to bind with the Takeover Directive, thus the City Code was implemented.<sup>41</sup> The Takeover Directive was intended to improve the competitiveness of business between the Member States whilst enhancing minority shareholder protection.<sup>42</sup> Recent developments in 6th April of 2007, namely the Companies Act 2006 (hereinafter referred as 'CA 2006') was enforced, ceased the effectiveness of the interim directive, but maintaining a statutory foundation for the Takeover Panel and City Code.

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<sup>37</sup> John, H. (2015). *Hostile Takeovers in the UK and Short-Termism: The Need for an Anti-Takeover Law*. Retrieved from <https://www.civitas.org.uk/content/files/IEGissue12.pdf>.

<sup>38</sup> See further Part 28 Chapter 1 of UK Companies Act 2006 and Section A7 to A9 of the Takeover Panel.

<sup>39</sup> Wang, X., *Loc.Cit*

<sup>40</sup> *Ibid.*

<sup>41</sup> Though it is only an interim implementation.

<sup>42</sup> Joseph, A. M. (2004). *The Economics of the Proposed European Takeover Directive*. Centre for European Policy Studies.

The Takeover Panel has the power to “do anything that it considers necessary or expedient for the purpose of, or in connection with, its function’ according to Section 942(2) of the CA 2006, including the emphasis of the general principles in the City Code. The general principles adhere to Article 3 of the Takeover Directive which include rules on takeover inter alia ordering that all shareholders class must receive equal treatment and be given sufficient time and information to decide on a bid.<sup>43</sup> The objectives of the City Code are reflected through the provision of Mandatory Bid Rule and Hostile Takeover Defenses.

#### **4.2.3. Mandatory Bid Rule**

The mandatory bid rule is regulated under Rule 9 of the City Code to fulfill the requirement for the equal treatment of all shareholders set out by the first general principle of the City Code to protect all shareholders. This is to ensure that bidders offer both controlling and non-controlling shareholders the same proportion of the price per share. The bidder must make an offer to acquire all shares of any class, voting or non-voting, and including other class of transferable shares carrying voting rights if it has acquired 30% or more of the voting rights of the target company.<sup>44</sup> In exchange, the shareholders of the target company may sell their shares at the highest price to the bidder within offer period and the 12 months prior the offer announcement.<sup>45</sup> In addition, the City Code also prohibits the target company’s management from taking any action to frustrate a bid without the consent of shareholders (post-bid takeover defense). Therefore, it is shown that the City Code itself is lenient towards hostile takeover, but at the same time provides a stronger protection towards minority shareholders.

#### **4.2.4. Hostile Takeover Defenses**

There are more than three ways in which a target company can defend themselves against takeover bids, but the common ways include poison pill,<sup>46</sup> staggered board,<sup>47</sup>

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<sup>43</sup> Article 3 of Directive 2004/25/EC of the European Parliament and of the Council jo. Section 2 (b) of the City Code.

<sup>44</sup> City Code, Rule 9.1.

<sup>45</sup> City Code, Rule 9.5.

<sup>46</sup> Poison pill is a common takeover defense utilized by company where the existing shareholders of the target company will obtain a large amount of convertible rights to preferred shares at a high price when another shareholder obtains a specific percentage of the voting shares, leading to the

and white knight.<sup>48</sup> Each takeover defenses work in different ways, for example the staggered board allows the board of the target company to retain control for a longer time as two annual successive elections should take place in order to acquire the target company. It would then be too long for the bidder to wait until they can finally gain control.

As mentioned in the previous section, the target company's management is prohibited to stipulate the frustration of the takeover bid without the consent of all shareholders in the general meeting.<sup>49</sup> The City Code intends to ensure that the shareholders in the target company receive equal opportunity to be involved in determining the success (or failure) of hostile takeover. This concept is a characteristic of common law system where the power of director should only be used "for their proper purpose" which does not include frustrating a takeover bid.<sup>50</sup> In spite of the ban to take any action to frustrate a bid without shareholders' approval, it does not stop the board to influence or negotiate with the shareholders to "reject" the hostile offer.

### 4.3. Challenges of Regulating Hostile Takeover under Indonesian Law

#### 4.3.1. Indonesian Takeover Regulatory Framework

The Indonesian legal framework does not differentiate takeovers as hostile and friendly takeovers. Both are within the scope of the definition of 'takeover' which is

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formation of controlling shareholder as the voting rights are transferred to another shareholder(s). See further: Wang, X. (2020); Ryngaert, M. (1988). The Effect of Poison Pill Securities on Shareholder Wealth. *Journal of Financial Economics*, 20, 377-417. [https://doi.org/10.1016/0304-405X\(88\)90051-7](https://doi.org/10.1016/0304-405X(88)90051-7).

<sup>47</sup> A staggered board is a pre-bid defense technique where the board are divided into several groups (usually three) of equal size, and each can only be re-elected or removed in staggered years. See further: Wang, X (2020); Lucia, A. B., John C. C. IV & Guhan, S. (2002). The Powerful Antitakeover Force of Staggered Boards: Further Findings and a Reply to Symposium Participants. *Stanford Law Review*, 54. Retrieved from [http://www.law.harvard.edu/programs/olin\\_center/papers/pdf/353.pdf](http://www.law.harvard.edu/programs/olin_center/papers/pdf/353.pdf).

<sup>48</sup> A white knight is a defense technique where the target company looks for a more appropriate and friendly bidder to acquire the company, after receiving a hostile takeover offer from an unwelcome bidder. The white knight (friendly bidder) should be willing to bind onto the target company's favorable terms, for instance, by keeping the current management board in place even after the deal is signed. See further: Wang, X (2020); Marcin, P., & Maciej, M. (2012). Defensive Strategies against Hostile Takeovers. The Analysis of Selected Case Studies. *Journal of International Studies*, 5(1), 60.

<sup>49</sup> City Code, Rule 21.

<sup>50</sup> *Hogg v Cramphorn Ltd* [1967] Ch 254.

any transaction that involves a change of control in the company.

The fundamental regulation to takeover is found on Law No. 40/2007. According to Article 125, an acquisition of a company's share could happen either through the company's Board of Directors (hereinafter referred as 'BoD') or through the decision from General Meeting of Shareholders (hereinafter referred as 'GMS'). If the takeover takes place through the BoD, which should also be approved by GMS, then the bidder is required to submit an acquisition plan (*rancangan pengambilalihan*) to the target company for approval. Moreover, a disclosure of the transaction which involves a change in the Articles of Association shall be addressed to the Ministry of Law and Human Rights.

Companies in Indonesia are owner-controlled where major conflict occurs between majority shareholders and minority shareholders.<sup>51</sup> The concentrated ownership structure makes it possible for the majority shareholders (controlling shareholders) to influence and control the company, thus the power to pressure the performance of the company's management.<sup>52</sup> Therefore, the Indonesian practice of law indirectly points out the primacy of shareholders within the organizational structure of the company under the context of decision-making where it is surrendered to the company's shareholders through GMS.

The acquisition of public company is also subjected to the Indonesian Securities Law, specifically Law No. 8/1995,<sup>53</sup> Otoritas Jasa Keuangan or the Indonesian Financial Services Authority (hereinafter referred as 'FSA') Regulation No. 9 of 2018 on Public Company Takeover (hereinafter referred as 'FSA Regulation 9/2018'),<sup>54</sup> and FSA Regulation No. 54/2015 on Voluntary Tender Offer ('FSA Regulation 54/2015').<sup>55</sup>

As mentioned in the previous paragraph, FSA Regulation No. 9/2018 defines takeover as a transaction causing a change in the company's control. According to the regulation, the controller of the public-owned company is the party owning more

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<sup>51</sup> Soejono, F. (2015). Ownership Type and Company Performance: Empirical Studies in the Indonesian Stock Exchange. *Jurnal Ekonomi & Bisnis Indonesia*, 25(3), 338-52. <https://doi.org/10.22146/jieb.6288>.

<sup>52</sup> *Ibid.*

<sup>53</sup> Law No. 8/1995, Article 84

<sup>54</sup> FSA Regulation No. 9/2018, Chapter 3.

<sup>55</sup> FSA Regulation No. 54/2015, Article 10.

than 50% of the company's share or any party that is capable to decide on the management or make changes to the articles of association. In addition, FSA Regulation 9/2018 also applies the concept of mandatory tender offer where the bidder should purchase the shares of all remaining shareholders after the share's threshold are triggered. Besides, the pricing for the mandatory tender offer is also set by the law where it should be higher than the average of the highest daily traded price within 90 days prior to takeover announcement (appropriate price).<sup>56</sup> Every shareholder has the right to institute legal proceedings against the target company. However, it is left to the discretion of the court whether or not they will accept the claims made by the minority of shareholders.<sup>57</sup>

According to Article 11 FSA Regulation 54/2015, in case of disagreement towards a takeover deal, the management of the target company or the Board of Commissioners (hereinafter referred as 'BoC') may issue a discouraging statement which should be published in at least two national newsletters 10 days before the voluntary tender offer ends if evidence shows that the information in the offering statement is false.

Lastly, in order to protect the public, the transfer of controlling power within a public company should formally be reported to FSA and to the public through national newsletter within two working days after the event took place based on Article 2 of the FSA Regulation No. 31 of 2015 on Transparency of Information or Material Facts by Issuers or Public Companies and Chapter 2 of the FSA Regulation No. 11 of 2017 on Ownership Reports or Any Changes in Ownership of Public Company Shares.

Although the regulation about mandatory tender offer and pricing rule might limit the possibility of hostile takeover, this form of takeover can still occur as long as the shareholders are compensated with the 'appropriate' amount. Furthermore, requiring the bidder to pay at a higher and more competitive price would benefit shareholder, and it is not directly inhibiting the whole process of hostile takeover to take place.

However, Article 125 of Law No. 40/2007 shows two ways in which a takeover could

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<sup>56</sup> Audi, A. S. (2018). *Hostile Takeover in Indonesia: Challenges and Prospects*. Master of International Business Law. Tilburg University.

<sup>57</sup> *Ibid.*

take place, either through BoD or shareholders. A hostile bidder would normally approach through the latter without informing the BoD. The only limitation to the decision of the shareholders towards the hostile bidder is reflected on Article 125 paragraph 8 of Law No. 40/2007 where they should refer to the provision on Articles of Association of the target company or any other contracts binding the company with third parties concerning the transfer of rights. The approached shareholder(s) may only transact with a hostile bidder according to the provision under those documents.

Article 57 of Law No. 40/2007 stated that companies may regulate the requirements for the transfer of shareholding rights, which may include (a) the requirement to offer certain classification of shareholders or other shareholders in advance; (b) the requirement to obtain prior approval from the BoD, BoC, and/or GMS; and/or (c) the requirement to obtain approval from the relevant authorized agencies. These requirements are not absolute, meaning companies are not obliged to regulate about it in the AoA. However, public companies listed in IDX30 regulates about this transfer of shareholding rights. For instance, as reflected in the AoA, Bank Central Asia Ltd requires the approval of BoD, BoC, and GMS in case of any changes in the list of shareholders, so does Astra International Ltd which also requires the approval of BoD. This can be one of the obstacles to hostile takeover from taking place in Indonesia.

Besides, Article 26 of Government Regulation No. 27 of 1998 on Merger, Consolidation and Acquisition of a Limited Liability Company (hereinafter referred as 'GR 27/1998') also requires the approval of the BoC on the acquisition plan made by both the bidder and the BoD. In the end, Article 6 of the same provision, stated that acquisition can only be done after the GMS gave their approval. Lastly, it is also written in Article 4 that shareholders who do not agree with the final decision of the GMS concerning acquisition may only use their rights so that their holdings are purchased at a fair price.

#### **4.3.2. Obstacles to Hostile Takeover in Indonesia**

Many legal practitioners in Indonesia believed that hostile takeover is implausible because of the high concentration of company ownership and the regulation which is

in favor of controlling shareholders.<sup>58</sup> Although no strict legal barrier is seen in Indonesian law, the existence of block-holders within company in Indonesia's business environment is an obstacle for hostile takeover.

The company share ownership structure in Indonesia is different in common law regime, specifically UK. 25% of Indonesia's GDP is contributed by family-owned business, in fact, 95% of Indonesian business are family-owned.<sup>59</sup> This created a situation where small number of people possessed a huge proportion of shares in the company, a network-oriented governance system leading to weak stock market efficiency. Potential bidder has a low bargaining position when confronting the majority shareholders. Consequently, it has a huge potential to lead to poor financing and investment systems in the business environment. A study conducted towards Indonesian listed companies in 2012 also showed that a BoD filled with family ties are negative associated with corporate transparency.<sup>60</sup> Meanwhile, corporate transparency increases when the BoD have a larger proportion of independent members.<sup>61</sup>

The existence of the block-holders also reflects a weak corporate governance in Indonesia's company law. It is difficult to monitor and ensure the maximum efficiency of management (lack of information transparency) as share ownership is not dispersed and decision-making is more exclusive to majority shareholders. There is currently no specific regulatory framework concerning shareholders activism, which is a way in which shareholders could influence the company with their rights as partial owners.

However, Law No. 40/2007 grants certain rights to every shareholder, including minority shareholders that allow them to influence the operation of the company and protect their interests. Shareholders are welcomed to attend and cast a vote in GMS

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<sup>58</sup> Ayik, C., & Freddy, K. (2017). 2017 Mergers and Acquisitions Report: Indonesia. *International Financial Law Review*. Retrieved from <http://www.iflr.com/Article/3673242/2017-Mergers-and-Acquisitions-Report-Indonesia.html>.

<sup>59</sup> PricewaterhouseCoopers. (2014). *Survey Bisnis Keluarga 2014*. Retrieved August 13, 2020, from <https://www.pwc.com/id/en/publications/assets/indonesia-report-family-business-survey-2014.pdf>.

<sup>60</sup> Saiful, S., Phua, L. K., & Hasnah, H. (2012). Corporate Governance and Corporate Transparency of Indonesian Listed Companies. *The Indonesian Journal of Accounting Research*, 15(3), 1.

<sup>61</sup> *Ibid.*

that require shareholders' approval (including takeover) as regulated under Indonesian Company Law and the company's AoA itself. The law also gives a protection to shareholders by granting them the rights to file a lawsuit against the company if they suffer losses as a result of the company's unfair and unreasonable actions, either from GMS, BoD, or BoC.<sup>62</sup> Finally, shareholders may use their rights to require the company to purchase their shares at a fair price. The shareholders' rights, especially the right to file a lawsuit, may become an obstacle to a hostile takeover as it gives the court the power to annul a bid only if there is enough evidence to prove that the company's action is unreasonable and unfair.

Another possible reason why hostile takeover is not recognized in Indonesia is because of the cultural and societal values in business relationships. In Asia, [including Indonesia] the need to preserve a harmonious work environment, to preserve 'face' ranks as a high priority".<sup>63</sup> A healthy business and personal relationships within the company are valued and maintained. Thus, shareholders of the company would also not be easily influenced by bidders, and would be disinclined to break the relationships within current board members.

#### **4.4. The Way Forward for Indonesia**

The provision in Indonesian Law is similar to United Kingdom's Takeover Law. Even though hostile takeover is not explicitly mentioned under the Indonesian law, there is no explicit legal barrier for it to occur. In terms of procedure, there is a similarity between United Kingdom and Indonesia regarding the mandatory tender offer and mandatory bid rule. Both states also adopt the concept of "shareholders primacy" where it sits at the highest position between the organs of the company and involved in major decision-making process, though in practice the shareholder profile of Indonesia is still very far from being dispersed and as such, control is typically concentrated in a family or business group.

Nonetheless, there is a difference between the two states regulation and that is regarding the ban on takeover defense technique that would frustrate a bid. There is

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<sup>62</sup> Law No. 40/2007, Article 61 paragraph 1.

<sup>63</sup> Justin, Kent. (2014). *Business Ethics in Asia: Lost in Translation?*. Retrieved Jun 14, 2020, from <https://www.forbes.com/sites/connorconnect/2014/03/25/business-ethics-in-asia-lost-in-translation/#566ac4b96473>.

no provision that ban takeover defense in Indonesian law, except that the management or BoC of the target company may release a discouraging statement if it the information in the offering was proven to be false. As such, changing the regulation may bring a positive impact to the level of M&A and corporate control in the country. Nevertheless, it is important to note that the pressure of hostile takeover will discipline and enhance the performance of company's management. A hostile takeover can occur only if it is supported by an efficient and healthy corporate governance.<sup>64</sup>

Considering the current situation, Indonesia's current stock market stance, hostile takeover is not likely to function. As explained above, Indonesia has a weak stock market efficiency when compared to United Kingdom as the volatility of stock market is very high that it is hard to predict the daily stock price and the value of the company.<sup>65</sup> Unlike United Kingdom that has a market-oriented system, the network-oriented governance system in Indonesia which is reflected by the presence of blockholders and concentrated share ownership, becomes the main obstacle to hostile takeover as institutional setting limits the effectiveness of market for corporate control.<sup>66</sup> This is the main factor that differentiates the number of hostile takeover that occur between United Kingdom and Indonesia even though not much differences are seen in the takeover legal framework between the two countries.

The homework for Indonesia's government and companies would be increasing the efficiency of stock market and strengthening corporate governance. For a hostile takeover to take place, it requires a huge transaction deal that may be too much for a young capital market like Indonesia. In the meantime, however, there are ways in which Indonesia could improve the market for corporate control.

By taking the concentration of share ownership (controlling shareholders) into account, the minority shareholders can be protected by imposing liability to controlling shareholders for resolution passed at the shareholders' meeting. This

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<sup>64</sup> Syste, D., & Hein, S. (2018). *Economic Approaches to Organization (6th ed)*. Pearson Education Limited.

<sup>65</sup> Yanuar, A., & Adrian, R. M. (2016). A Testing of Efficient Markets Hypothesis in Indonesia Stock Market. *Procedia - Social and Behavioral Sciences*, 219, 99. Retrieved from <http://www.sciencedirect.com/science/article/pii/S1877042816300507>.

<sup>66</sup> Syste, D., & Hein, S., *Loc.Cit*.

could possibly avoid controlling shareholders from exercising their self-interest and abusing their powers in making decision.<sup>67</sup> As a result, the interests of non-controlling shareholders would be more protected as they have the right to hold controlling shareholders liable for abusive behaviors that is against the interests of the company and shareholders. In the long run, this will help Indonesia's capital market to possess the characteristic of a market-oriented system like United Kingdom where the protection of minority shareholder is strong.

Next, the company should provide a mechanism for internal monitoring to not only increase the protection of minority shareholders but also strengthen the voice and position of minority shareholders within the company. Considering the dominance of concentrated shareholders in Indonesian companies, it would be great alternative if minority shareholders would be granted a veto right (as one vote), where any decisions made by GMS, BoD, or BoC that require shareholders' approval, such as a takeover, would be nullified once the veto right is activated. This approach is actually practiced in United Kingdom's Company law. In defense of this, the veto right also prevents the uncertainty of the court's decision when the minority shareholder suffers from loss as a result of the company's wrongdoings in case when not enough evidence is present. This approach will definitely enhance the protection of minority shareholders.

Furthermore, to ensure the effectiveness of the approach above, it is important to note that minority shareholders are expected to be more aware and active in pursuing their rights as a shareholder. Understanding and analyzing where the company is heading to are factors that minority shareholders should take into consideration, not simply participating in GMS. A future-oriented mindset in understanding where the company is heading to is something that every shareholder should keep. It is important to ensure that a company's management has a maximum performance.

As mentioned earlier, Article 125 paragraph 8 of Law No. 40/2007 may be considered as an obstacle to the occurrence of hostile takeover. If Indonesia would really

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<sup>67</sup> Wang, X., *Loc.Cit*

consider and support the happening of a hostile takeover, and familiarize this whole process to the people, then it is time for the regulator to set a minimum amount of transfer of rights in the company's AoA. The minimum amount for the transfer of rights under AoA should enable a transfer of controlling power after acquiring from certain number of shareholders. Besides, the law should also consider a restriction towards the rejection by BoD, BoC, or GMS regarding the transfer of rights in public companies, unless the transfer of rights happens because of law such as inheritance.

Lastly, other than offering to acquire the holdings of shareholders to purchase at a fair price as obliged by the law, a bidder may approach with an incentive in order to acquire the company's controlling power and at the same time holding each board members and company's current shareholders. Keeping the current board members and shareholders by offering an incentive will maintain the synergy and relationship within the company.

## 5. Conclusion

Despite all the negative stigmatization surrounding it, the occurrence of a hostile takeover is arguably the right tool to measure the market for corporate control. The UK has a dispersed share ownership profile within a company, which serves as a characteristic of a market-oriented system that prevents the formation of block-holders. United Kingdom also has a provision which bans post-bid takeover defence, reflecting a leniency towards hostile takeover to occur. Indonesia, on the other hand, adopts network-oriented governance system where block-holders are dominant and share ownership are concentrated (family-owned business), and this becomes the main barrier to hostile takeover. Although not much of legal differences are seen between Indonesia and UK except the ban for post bid defense in UK, the reasons above become the obstacle because it puts the hostile bidder at a weaker bargaining position when facing the majority controlling shareholders, and it is difficult to monitor the efficiency of the company's management as well. A network-oriented governance system typically offers a weaker protection to minority shareholders, has a low stock market efficiency and a weak corporate governance.

Nonetheless, there are some ways in which companies in Indonesia could improve the protection to minority shareholders, and overall corporate management's

efficiency and governance. First, imposing liability to controlling shareholders for resolution passed at the shareholders' meeting could ensure that controlling shareholders do not abuse their powers in making decision. As required by law, it is also a duty of the bidder to purchase the shares of non-controlling shareholders at the same price as the controlling shareholders. An internal monitoring should be done to increase the protection of minority shareholders and strengthen the position of minority shareholders at the same time. The application of minority shareholders consent right which is the veto right, would definitely enhance their voice and power to be involved in the company's decision-making processes. Finally, it is also time for the Indonesian regulator to set the minimum amount for the transfer of rights under AoA in order to enable a transfer of controlling power after acquiring from a certain least number of shareholders. At the same time, to maintain the synergy and relationship within the company, the bidder may also use an incentive approach to keep the current "needed" board members and shareholders.

All in all, there are still many challenges that Indonesia has to face keeping in mind of the nature of the stock market where it adopts a network-oriented system. There are many lessons that Indonesia could learn from United Kingdom as a country that has active market for corporate control and adopts an Anglo-American legal system. Most importantly, the minority shareholders should be more active in pursuing their rights and have a future-oriented mindset in understanding where the company is heading to. With one step at a time, regulators and companies could work together to achieve a better corporate governance, an active market for corporate control.

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