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Indonesia Proposes Mandatory Annual Legal Audits for Businesses

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The Government of Indonesia is drafting a Presidential Regulation (“**Draft**”) that would require all legal and business entities to conduct annual legal audits, as part of the government’s program to strengthen compliance with existing laws and develop a culture of legal awareness across the private sector.

The Draft mandates that legal entities (e.g. companies in Indonesia), business entities, and public entities enhance their awareness and compliance with the law through assessments focusing on these two key areas:

1. The substance of the law, legal structure, and legal culture; and
2. Awareness of and compliance with the implementation of the law.

This advisory focuses only on the requirements that will be applicable to the private sector, specifically legal entities and business entities.

Legal Audit

The assessment described in item a. above will be conducted by the Minister of Law (“**Minister**”) through legal monitoring and evaluation, which will be further detailed in a ministerial regulation. The assessment in item b. must be conducted **annually** by the legal entity or business entity, which is required to appoint a certified legal auditor (i.e. a legal auditor which has been certified by the Minister). If an entity fails to appoint a legal auditor or if a complaint arises, the Minister will appoint one to conduct the audit.

The legal audit must consist of the following stages:

1. Identification of the purpose of the legal audit;
2. Legal audit planning;
3. Confirmation of legal audit planning;
4. Collection of data and information;

5. Assessment and analysis of data and information;
6. Preparation of legal audit report; and
7. Submission of legal audit results.

Legal entities and business entities must take follow-up action after receiving the results from the legal auditor. The report must also be submitted to the Minister and other relevant government institutions **by the end of the year**. Failure to take follow-up action or submit the report to the Minister will result in sanctions for the legal entities and business entities. The specifics of these sanctions remain unclear, as the Draft only refers to the relevant laws and regulations.

What to expect next?

Once the Draft comes into effect, all companies in Indonesia, including foreign investment companies, will have an additional annual obligation, namely to conduct annual legal audits. This legal audit will naturally cause companies to incur additional costs, as it requires hiring a certified legal auditor. Another point to highlight is that the submission of legal audit results to the Minister might involve lengthy bureaucratic procedures.

If the Draft is eventually promulgated, an implementing ministerial regulation should be issued to outline the details of the assessment conducted by the Minister and the requirements for performing an annual legal audit. This ministerial regulation is also expected to clarify the sanctions that can be imposed on legal entities or business entities for failing to conduct the legal audit or submit the results to the Minister.

While Indonesia's new government is clearly aiming to foster a culture of legal compliance among businesses, it remains to be seen whether it will ultimately lead to improved adherence to regulations or merely add to administrative processes and costs.

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