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Limits of Directors Liability for the Errors or Negligence of Subordinates Viewed Through the Lens of The Business Judgment Rule

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ABSTRACT

Errors or negligence in the management of a limited liability company may arise not only from acts directly committed by the Board of Directors, but also from acts committed by parties who functionally operate under the Board of Directors. Directors may be held liable for such errors or negligence. The primary objective of this research is to analyze the construction of the Board of Directors' managerial authority over the company and the limits of directors' liability for errors or negligence committed by their subordinates that result in losses to the company. This research employs a normative juridical method with a statutory approach. The results demonstrate that: (1) the Board of Directors' authority to manage the company is based on attributed authority, which must be exercised in accordance with the principle of trust; and (2) the limits of directors' liability are determined on the basis of two considerations: first, the legal basis of the authority held by the relevant subordinate; and second, the establishment of fault or negligence, good faith, conflicts of interest, and preventive measures taken to avert the occurrence of losses. The study concludes that the management of the company by the Board of Directors must be conducted in accordance with the purposes and objectives stipulated in the company's articles of association. The Board of Directors must exercise its authority in accordance with the principles of prudence and full responsibility. Theoretically, this research contributes to enriching the body of legal scholarship, particularly in relation to directors' liability. Practically, the findings of this research provide clear parameters for determining directors' liability for errors or negligence committed by their subordinates, thereby contributing to legal certainty in its implementation.

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1. INTRODUCTION

The management of a limited liability company is carried out by its Board of Directors. Pursuant to Article 1 point 5 of Law Number 40 of 2007 concerning Limited Liability Companies (hereinafter referred to as "Law No. 40 of 2007"), the Board of Directors "...is the Company's organ authorized and fully responsible for the management of the Company in the interests of the Company, in accordance with the Company's purposes and objectives, and represents the Company both inside and outside the court in accordance with the provisions of the articles of association." As one of the organs of a limited liability company, the Board of Directors is vested with authority to perform its functions and duties. Such authority is expressly regulated both in Law No. 40 of 2007 and in the company's articles of association (Pramono, 2024). Theoretically, the Board of Directors possesses two forms of authority, namely authority of disposition (*beschikking/eigendom*) and authority of management (*beheren*) (Prasetya, 2019). The authority of disposition, which may also be referred to as an extraordinary act by the Board of Directors, may only be exercised upon obtaining approval from another corporate organ, which may first require approval from the Board of Commissioners or from the General Meeting of Shareholders (GMS), depending on the applicable statutory provisions or the company's articles of association.

Meanwhile, the authority of management may be understood in the opposite manner, namely as the authority to conduct the company's day-to-day affairs without having to obtain approval from another organ, whether the Board of Commissioners or the GMS. These management acts constitute the Board of Directors' inherent authority and are characterized by acts ordinarily performed in the company's day-to-day and continuous operations. As long as an act constitutes an act of management, the Board of Directors is authorized to undertake it independently. Under Law No. 40 of 2007, the Board of Directors' management authority is regulated in several provisions, one of which is Article 92 paragraphs (1) and (2). The exercise of the Board of Directors' authority, particularly its management authority, must be carried out in accordance with the company's purposes and objectives as set forth in its articles of association. Furthermore, such authority must be exercised in accordance with the fiduciary duty principle. In this context, fiduciary duty refers to duties arising from a fiduciary or trust-based relationship between the Board of Directors and the company it manages, placing directors in a position of trust. Accordingly, directors are required to demonstrate due care (duty of care) and competence (duty of skill), as well as good faith, loyalty, and integrity toward the company. The relevance of the fiduciary duty principle to directors under Law No. 40 of 2007 is reflected in Article 97 paragraph (2), which provides that "the management as referred to in paragraph (1) must be carried out by each member of the Board of Directors in good faith and with full responsibility."

In practice, the management of a company through the exercise of the Board of Directors' management functions is not carried out directly in every respect, but is differentiated among various units that functionally operate under the Board of Directors (Rizki, 2026). The complexity of corporate business activities requires the Board of Directors to divide duties, delegate authority, and supervise subordinate officers, such as managers, division heads, and employees performing operational functions. A legal issue arises when an act or omission by a person functionally subordinate to the Board of Directors, in carrying out operational duties, causes losses to the company. This becomes particularly relevant when the company's losses do not arise directly from an act of the Board of Directors, but instead result from the negligence of a subordinate. On the one hand, the Board of Directors has an obligation to ensure that the company's activities are conducted in accordance with the principles of good corporate governance. The Board of Directors is required to establish an internal control system, conduct adequate supervision, and ensure that delegated authority is exercised in accordance with the company's purposes and objectives. However, where the Board of Directors fails entirely to exercise supervision and allows risky operational practices to continue without adequate controls, such circumstances provide grounds for questioning whether the Board of Directors has itself been negligent. On the other hand, it would be inappropriate to automatically attribute every subordinate's error to the Board of Directors. Directors cannot realistically supervise every operational action of subordinates directly and continuously. Where the Board of Directors has established an adequate supervisory system, delegated authority to competent

officers, established appropriate procedures, and exercised supervision proportionately, an individual subordinate's error should not automatically be characterized as an error or omission attributable to the Board of Directors.

Accordingly, a legal issue arises concerning the boundary between the Board of Directors' responsibility and the protection afforded to directors in respect of operational errors committed by subordinates that fall outside the directors' immediate reach or control. An excessively broad interpretation of directors' liability may discourage directors from making necessary business decisions because they are constantly exposed to the risk of personal liability. Such a condition may hinder directors from innovating and making business decisions that are in fact necessary for the company's development. Conversely, if the Business Judgment Rule is applied too broadly, there is a risk that directors may invoke the rule as a justification for avoiding liability for failures to exercise adequate supervision. Directors should not be permitted to shield themselves behind the argument that an error was committed by a subordinate where the resulting loss was in fact caused by the directors' failure to establish an adequate supervisory system, select competent personnel, provide appropriate instructions, or take corrective measures after becoming aware of a deviation.

The implementation of the Business Judgment Rule must therefore be positioned proportionately. The rule does not provide absolute protection to directors where negligence or error has occurred in the performance of their duties. In principle, the Business Judgment Rule constitutes a protective mechanism for business decisions made lawfully, rationally, in good faith, and through an adequate decision-making process. Such protection must be distinguished from circumstances in which directors fail to discharge their legal duties of management and supervision that fall within the scope of their responsibilities. Based on the foregoing, a legal issue arises concerning the need for clear parameters governing directors' liability for operational negligence by subordinates that causes losses to the company, viewed from the perspective of the Business Judgment Rule.

Several previous studies have addressed related issues. For instance, Sakinah (2026), in a study entitled "Legal Protection and Limits of Directors' Liability in the Management of Public Companies under the Company Law," examines directors' liability primarily as a consequence of errors or omissions committed directly by directors, without specifically addressing directors' liability and its limits in relation to errors or omissions committed by persons who functionally operate under their authority. Another study, by Dita and Winanti (2025), entitled "Analysis of the Principle of Vicarious Liability in Substitute Liability for Unlawful Acts Committed by Bank Employees," focuses on errors or omissions committed by persons functionally subordinate to directors, including managers, supervisors, and employees, through the lens of vicarious liability. Vicarious liability, as regulated under Article 1367 of the Indonesian Civil Code, emphasizes the imposition of liability for an error or omission committed by one person or legal entity upon another party who is also a legal subject. Accordingly, where a person functionally subordinate to the Board of Directors commits an error or omission, liability for such conduct is imposed upon the company. Thus, the vicarious liability approach does not place directors themselves in a position where they may be held personally liable.

Based on the foregoing, the novelty of this study lies in examining the relationship of liability between the Board of Directors and persons who functionally operate under its authority. This relationship needs to be analyzed in order to determine the boundaries and extent of directors' liability for errors or omissions committed by subordinates that cause losses to the company. Accordingly, this study addresses two research questions. First, how is the legal construction of the authority relationship between the Board of Directors and the company? Second, what are the limits of directors' liability for errors or omissions committed by persons who functionally operate under the Board of Directors and which cause losses to the company.

2. METHODS

This study employs normative legal research. Normative legal research conceptualizes law as a set of norms encompassing legal values and positive law. The approaches employed are the statutory

approach and the conceptual approach. The author examines statutory provisions based on relevant legal theories, and the results of the analysis are subsequently applied to the legal issues under investigation. This research aims to systematically examine the applicable law in order to determine the limits of directors' liability for errors or omissions committed by persons who functionally operate under their authority.

The statutory approach is conducted by examining and analyzing all laws and regulations relevant to the legal issue under investigation. In this study, the principal statutory references are: (1) Law Number 40 of 2007 concerning Limited Liability Companies; and (2) the Indonesian Civil Code.

3. FINDINGS AND DISCUSSION

Legal Construction of Directors' Authority and Supervisory Duties in Limited Liability Companies

The Board of Directors is one of the company's organs vested with the position, authority, capacity, and duty to conduct the company's management in accordance with its purposes and objectives. Simply put, every activity undertaken by the Board of Directors constitutes a manifestation of the will of the legal entity itself (Anggoro, 2010). The Board of Directors is appointed by the General Meeting of Shareholders (GMS) for a specified period and subject to the requirements prescribed by law and the company's articles of association (Supramono, 2007). In principle, the Board of Directors is accountable to the company as a whole (i.e., the shareholders collectively rather than individual shareholders), and its responsibility is not limited to routine activities but also encompasses initiatives aimed at realizing the company's purposes and objectives in the future (Muhammad, 1996). The Board of Directors bears full responsibility for the management and operation of the company. Accordingly, its legal position cannot be characterized as that of an ordinary employee or worker under employment law; rather, directors are professionals who independently perform management functions, except where fundamental changes occur within the company, such as amendments to the articles of association or corporate actions (Fuady, 2018).

As provided in Article 1 point 5 of Law No. 40 of 2007 concerning Limited Liability Companies (the "Company Law"), the Board of Directors is the company organ authorized and fully responsible for the management of the Company in the interests of the Company and for representing the Company both in and outside court in accordance with the articles of association. Article 92 paragraph (1) further provides that the Board of Directors conducts the management of the Company in the interests of the Company and in accordance with its purposes and objectives. A company may have one or more directors, depending on its characteristics and needs. Where a company has more than one director, the duties and authorities of the directors are determined by the GMS. If they are not determined by the GMS, such duties and authorities are established by a decision of the Board of Directors.

The performance of the Board of Directors' duties and responsibilities in managing the company is, in principle, subject to limitations imposed by law and the company's articles of association. Article 92 paragraph (2) affirms that the authority of the Board of Directors is to conduct management in accordance with the following:

a. The interests of the company, meaning that, in managing the company, directors may not use their position or the company's assets for personal interests or interests inconsistent with those of the company (conflict of interest) (Harahap, 2014).
b. The purposes and objectives of the company. In managing the company, directors must act in accordance with the company's purposes and objectives as stipulated in Article 15 paragraph (1) letter b, which must be included in the company's articles of association. Accordingly, directors may not exceed the boundaries (ultra vires and abuse of authority) established in the Company Law and the articles of association.
c. Policies deemed appropriate. Based on the elucidation of Article 92 paragraph (1), "policies deemed appropriate" refers to policies based on expertise, available opportunities, and customary practices in the relevant business sector.

In addition to management duties and responsibilities, the Board of Directors also has the capacity to represent the company, as expressly affirmed in Article 1 point 5, which provides that directors may represent the company both in and outside court in and on behalf of the company. A director does not have the authority to represent or assume responsibility for the company as contemplated by Article 99 paragraph (1) where:

a. there is a court proceeding between the company and the relevant director; or
b. the relevant director has a conflict of interest with the Company.

Pursuant to Article 99 paragraph (2), where any of the circumstances referred to in paragraph (1) occurs, the parties entitled to represent the Company are:

a. another member of the Board of Directors who has no conflict of interest with the Company;
b. the Board of Commissioners, where all members of the Board of Directors have a conflict of interest with the Company; or
c. another party appointed by the GMS, where all members of the Board of Directors or the Board of Commissioners have a conflict of interest with the Company.

The regulation of the Board of Directors under the Company Law essentially incorporates the fiduciary duty principle applicable to directors (Fuady, 2003). Directors occupy the position of trusted parties (trustees) of the company in carrying out their duties and responsibilities, as affirmed in Article 92 paragraphs (1) and (2), namely: (1) The Board of Directors conducts the management of the Company in the interests of the Company and in accordance with the purposes and objectives of the Company; (2) The Board of Directors is authorized to conduct such management in accordance with policies deemed appropriate, within the limits prescribed by this Law and/or the articles of association. In carrying out their duties and responsibilities, directors must act in good faith and with full responsibility, as provided in Article 97 paragraph (2), which states that the management referred to in paragraph (1) must be carried out by each director in good faith and with full responsibility. Good faith means that directors must remain trustworthy (fiduciary) and honest in discharging the responsibilities entrusted to them. Directors must also perform their responsibilities for legitimate purposes, including taking into account the interests of employees as well as those of shareholders. Good faith also requires directors to comply with applicable laws and the company's articles of association, remain loyal to the company, and avoid conflicts of interest.

According to Fred. B.G. in Widjaja (2004), these four principles reflect the dependent relationship between the Board of Directors and the company, whereby the company depends on directors as the organ entrusted with its management, while the company constitutes the basis for the creation and existence of the directors' office (Widjaja, 2004). The following fiduciary duty concepts are related to the duties and responsibilities of directors: First, the Duty of Obedience, which means that directors and company employees are required to act within the authority granted by law, the articles of association, internal policies and regulations, and internal corporate decisions (Fuady, 2003). Second, the Duty of Care and Diligence. In carrying out their duties and responsibilities, directors must act carefully and diligently, in good faith, with concern for the overall operation of the company, and in the manner best serving the company's interests. Directors must demonstrate a high degree of care and discipline toward the company. Such conduct may be reflected in the following (Munir Fuady, 2003):

a. aking rational actions;
b. devoting a high level of attention to the company;
c. conducting reasonable investigations into the company's problems;
d. taking the measures necessary to perform their duties;
e. attending meetings of the Board of Directors; and
f. supervising subordinates and ensuring that their actions do not cause losses to the company.

The amendment of the Company Law, from Law No. 1 of 1995 concerning Companies to Law No. 40 of 2007 concerning Limited Liability Companies, brought fundamental changes to the positions of the GMS, the Board of Directors, and the Board of Commissioners. Under Law No. 1 of 1995, the GMS was the highest organ and held all authority not delegated to the Board of Directors or the Board of

Commissioners. Law No. 40 of 2007, however, no longer characterizes the GMS as the highest organ of the company, but instead affirms that the GMS is a company organ vested with authority not granted to the Board of Directors or the Board of Commissioners (residual authority), subject to the limits prescribed by law and/or the articles of association. Consequently, the GMS, Board of Directors, and Board of Commissioners occupy equal or parallel positions within the corporate structure and are mutually interconnected. Each organ may therefore perform its functions and may be held accountable by the others within the limits of authority established by law and/or the articles of association. The authority of the Board of Directors can be traced through the theory of sources of authority, consisting of attribution, delegation, and mandate. By its characteristics, the authority of the Board of Directors is authority derived from attribution. Attribution may be understood as the conferral of authority upon an organ to exercise such authority in its own name and according to its own judgment, without being appointed merely to exercise another organ's authority (Sadi, 2021). Attribution occurs where the relevant authority derives from the constitution or statute and has not previously been granted (i.e., it is new). Attributed authority may be described as authority obtained directly from provisions of legislation (Haryati, 2024), as regulated in Article 1 point 5 of the Company Law.

In performing their duties and responsibilities, directors cannot operate independently but are integrated into a complex functional and working system. The subordination referred to here is the relationship between directors, as holders of the authority to manage and represent the company, and the various departments or functional units within the company that are assigned duties and responsibilities to assist the directors in achieving the company's objectives under their coordination. This is regulated by Article 103 of Law No. 40 of 2007, which provides that the Board of Directors may grant written authority to one or more employees of the Company or to another person to perform, for and on behalf of the Company, certain legal acts as specified in the power of attorney. Although not every subordinate relationship involving directors constitutes a power of attorney as contemplated by Article 103, the provision also does not mean that directors automatically transfer and/or relinquish their authority and responsibility to manage the company. Rather, it concerns the distribution of internal duties to parties who are authorized to perform specified functions. In accordance with Article 92 paragraph (1), which provides that the Board of Directors conducts the management of the Company in the interests of the Company and in accordance with its purposes and objectives, the possibility of internally allocating authority and responsibilities through subordinate relationships does not eliminate the directors' responsibility for the management of the company.

The company's liability for errors committed by functional units under the Board of Directors depends on whether there is evidence of fault attributable to the company. The company may be held liable where it is proven to have committed a fault (liability based on fault) in the management of the company. Because a corporation is a legal subject that bears responsibility for functional errors, it is necessary to further examine how a corporation, which lacks human consciousness, can act intentionally or negligently (Mahrus Ali, 2013). Accordingly, based on the position of directors, who are deemed to possess the knowledge, authority, and responsibility necessary to manage the company, a failure to conduct management properly—whether through negligence and/or intent—in the name and for the benefit of the company may, upon proof, give rise to criminal liability. Thus, according to Mardjono Reksodipuro in Mahrus Ali (2013), a corporate criminal liability system may be applied by classifying who committed the criminal act, namely:

a. The corporate management as the perpetrator, in which case the management bears responsibility for negligence or carelessness giving rise to the criminal offense.
b. The corporation as the perpetrator, while the management remains responsible for the negligence or carelessness giving rise to the criminal offense.
c. The corporation as both the perpetrator and the responsible party.

The question then arises as to the extent to which directors must be responsible for errors caused by subordinates within the company. To answer this question, the BJR may serve as protection for directors insofar as they remain within the framework of Article 97 paragraph (5). Where a loss arising

in the management of the company results from a lack of due care in a decision or action taken under the directors' instruction, the directors may be held liable. An examination of the provision indicates that a loss caused within the company's functional structure under the Board of Directors does not automatically constitute the directors' fault. Rather, it must be established whether the directors were negligent in managing and supervising the company. Where the directors have properly performed their duties and responsibilities, it may be concluded that the loss or error committed by the subordinate is the individual responsibility of that employee. Where an operational delegation decision is taken collectively by the Board of Directors, a director who disagrees with the decision may submit a dissenting opinion. A dissenting opinion is one indicator for assessing whether there is fault in actions inconsistent with the purposes and objectives of the company (Nindyo Pramono, 2013). This rule embodies an important doctrine in business law, namely the Business Judgment Rule (BJR). The BJR protects directors personally where they can establish the matters set out in Article 97 paragraph (5); accordingly, directors should not be held liable for losses suffered by the company. In addition, the BJR is intended to provide measured discretion, within the scope of the directors' duties and responsibilities (intra vires), to undertake actions capable of supporting, facilitating, and realizing the interests of the company (I G Rai Widjaja, 2005).

The complexity of the relationship between the company and its functional units does not preclude the possibility of numerous errors and/or instances of negligence arising at the subordinate level. Therefore, the fulfillment of the directors' management and representation functions in compliance with applicable legislation, as regulated in Article 97 paragraphs (3)–(5) of Law No. 40 of 2007 concerning Limited Liability Companies and the company's articles of association, constitutes a key parameter for ensuring that directors are not held liable for errors occurring beyond their control.

The Scope of Directors' Liability for Operational Errors of Subordinates from the Perspective of the Business Judgment Rule

The Board of Directors is one of the organs of a limited liability company and plays an essential role, particularly in managing and representing the company. The authority to manage the company is regulated under Article 97 paragraph (1) of Law No. 40 of 2007 concerning Limited Liability Companies (the "Company Law"), which provides that "the Board of Directors shall be responsible for the management of the Company as referred to in Article 92 paragraph (1)." Furthermore, Article 97 paragraph (2) provides that "the management as referred to in paragraph (1) shall be carried out by each member of the Board of Directors in good faith and with full responsibility." In exercising its authority, whether in management or representation, the Board of Directors must be guided by the company's purposes and objectives as stipulated in its articles of association (Widyaningtyas et al., 2025).

As previously explained, the relationship between the Board of Directors and the company is founded on a relationship of trust (fiduciary duty) (Bunga Dita Rahma Cesaria, 2025). The term "fiduciary duty" derives from two words: "fiduciary," meaning trust, and "duty," meaning an obligation or task. Thus, fiduciary duty refers to an obligation undertaken by a person who holds something in trust for the benefit of another person (Fuady, 2018). Fiduciary duty gives rise to two principal functions vested in the Board of Directors, namely the management function and the representation function. The management function means that the Board of Directors leads and manages the company. Meanwhile, the representation function means that the Board of Directors represents the company both in and out of court. The authority to represent the company outside court causes the company, as a legal entity, to be bound by transactions or contracts entered into by the Board of Directors in the name and for the benefit of the company.

The management function of the Board of Directors is expressly regulated in Articles 92 and 97 of Law No. 40 of 2007. In performing its function as the company's operational leader, the Board of Directors oversees all operational activities, including monitoring employee performance and ensuring that the company's day-to-day productivity is carried out in accordance with the purposes and

objectives set forth in its articles of association. This means that the Board of Directors does not manage the company entirely on its own, but is supported by subordinate units whose functions are differentiated. Within the institutional structure of a limited liability company, in addition to the three principal organs—the General Meeting of Shareholders (GMS), the Board of Commissioners, and the Board of Directors—there are also internal operational structural units under the leadership of the Board of Directors, including work units, divisions, and managerial positions that are accountable to the Board of Directors.

One of the fundamental characteristics of a company is the conduct of business activities with the objective of generating or maximizing profits (Yahya Harahap, 2016). This profit orientation places the Board of Directors in a position inherently exposed to risk (Khairiyyah & Sugiyono, 2025). Business decisions involving risk may give rise to legal consequences when their outcomes result in losses to the company. It is not uncommon for business decisions made by the Board of Directors to become the basis for lawsuits or legal claims alleging unlawful acts or negligence in the management and administration of the company. In this context, the Board of Directors may invoke the Business Judgment Rule (BJR) as a legal instrument to protect business decisions that have been implemented against lawsuits or legal claims brought by parties who consider themselves to have suffered losses as a result of such decisions (Kusumawati & Suparji, 2026). The Business Judgment Rule is a presumption that affords protection to business actions, decisions, or policies of the Board of Directors and its managerial ranks where such actions can be connected to a rational business purpose. Its purpose is to provide a defense and establish the legal facts relevant to claims of liability against the Board of Directors and its managerial ranks arising from business decisions or transactions undertaken by them (Pramono, 2024). Accordingly, the Business Judgment Rule may be understood as a doctrine or presumption that provides protection or immunity to the company's directors and management from liability arising from transactions or activities undertaken in the course of business. Under Law No. 40 of 2007, the Business Judgment Rule is reflected in Article 97 paragraph (5), which provides:

> *"A member of the Board of Directors shall not be held liable for losses as referred to in paragraph (3) if the member can prove that:*
> *a. the loss was not caused by his or her fault or negligence;*
> *b. he or she has managed the Company in good faith and with prudence for the benefit of and in accordance with the purposes and objectives of the Company;*
> *c. he or she has no conflict of interest, either directly or indirectly, in the management action that caused the loss; and*
> *d. he or she has taken measures to prevent the occurrence or continuation of the loss."*

Article 97 paragraph (5) not only provides legal protection to the Board of Directors in the context of business decision-making, but also provides a legal basis for directors to defend themselves when they are alleged to have committed an error or negligence in managing the company (Graciella & Gunadi, 2025). Accordingly, Article 97 paragraph (5) has a broader substantive scope than the Business Judgment Rule in its strict doctrinal sense, whose scope is generally limited to business decisions. In the context of operational errors committed by subordinates, Article 97 paragraph (5) functions as statutory protection with BJR characteristics for assessing the Board of Directors' liability for failures in management.

As previously described, the management and operation of a company are not carried out wholly and exclusively by the Board of Directors directly, but are distributed among more technical operational units. Accordingly, it is possible that an error or negligence causing loss to the company originates not from the Board of Directors, but from units operating under its supervision. This creates an issue concerning the extent of directors' liability for errors or negligence committed by subordinates. To determine the extent to which the Board of Directors is responsible for such conduct, it is necessary to identify the authority vested in the relevant subordinate. Article 103 of Law No. 40 of 2007 provides

that "the Board of Directors may grant written power of attorney to one or more employees of the Company or to another person to perform, for and on behalf of the Company, certain legal acts as specified in the power of attorney." Systematically interpreted, the power of attorney referred to in Article 103 of Law No. 40 of 2007 corresponds to the concept of authorization regulated under Article 1792 of the Indonesian Civil Code (KUHPerdata), which provides that "a power of attorney is an agreement by which one person grants authority to another person who accepts it to perform an act on behalf of the person granting the authority."

Where units or persons functionally subordinate to the Board of Directors act pursuant to authority granted by the Board of Directors, errors or negligence committed by such persons constitute their personal responsibility (Syarif et al., 2023). This is reinforced by Article 1801 of the Indonesian Civil Code, which provides that "an agent is responsible not only for acts committed intentionally but also for negligence committed in the performance of the mandate…" This provision helps clarify the limits of directors' liability where an error or negligence is committed by a unit or person under the directors' supervision. However, not every unit or person within a company receives direct written authorization from the Board of Directors as contemplated by Article 103 of Law No. 40 of 2007. Where an error or negligence by a subordinate who has no written power of attorney causes loss to the company, such conduct may, in principle, fall within the Board of Directors' responsibility pursuant to Article 97 paragraph (3) of Law No. 40 of 2007, which provides that "each member of the Board of Directors shall be personally liable in full for losses suffered by the Company if the member is at fault or negligent in performing his or her duties as referred to in paragraph (2)." The duty of the Board of Directors under Article 97 paragraph (2) is to manage the company in good faith and with full responsibility. In this context, all units or persons structurally subordinate to the Board of Directors form part of the directors' managerial responsibilities. Consequently, when an error or negligence is committed by a subordinate, the Board of Directors may, prima facie, be considered to have failed in its management duties.

Directors' liability for errors or negligence committed by subordinates that result in losses to the company does not constitute strict liability. Strict liability is a principle of liability without fault, under which a person or business entity may be held legally responsible for a loss or act without the need to establish fault, intent, or negligence (Pratama, 2026; Agung, 2026). Rather, directors' liability is based on fault (liability based on fault). In other words, a director may be held personally liable where an element of fault, negligence, or bad faith is proven in the exercise of the company's management authority. Therefore, Article 97 paragraph (5) of Law No. 40 of 2007 provides the Board of Directors with an opportunity to avoid personal liability if it can establish that: (a) the loss was not caused by its fault or negligence; (b) the company was managed in good faith and with prudence for the benefit of and in accordance with the company's purposes and objectives; (c) there was no direct or indirect conflict of interest in the management action that caused the loss; and (d) measures were taken to prevent the occurrence or continuation of the loss.

In this context, Article 97 paragraph (5) may be understood as both a boundary and a mechanism for exonerating the Board of Directors from liability. The provision requires the Board of Directors to demonstrate that the loss was not caused by its fault or negligence. Thus, where a subordinate commits an error that causes the company to suffer a loss, the Board of Directors has an opportunity to defend itself by demonstrating that it did not commit any fault or negligence in carrying out its management function. For example, the Board of Directors may have established adequate operating procedures, delegated authority proportionately, exercised reasonable supervision, and had neither actual nor constructive knowledge of the subordinate's misconduct. In such circumstances, the subordinate's error does not automatically give rise to the personal liability of the Board of Directors. These boundaries become clearer when Article 97 paragraph (5) is analyzed through its four exculpatory elements.

First, the Board of Directors must establish that the loss was not caused by its fault or negligence. In the study of unlawful acts (onrechtmatige daad), fault and negligence are conceptually

distinguishable even though both fall within the same element of liability. Fault (schuld) encompasses the actor's mental element, including conduct undertaken intentionally or with a particular purpose, as well as conduct resulting from negligence. Negligence itself constitutes a form of fault and may take the form of insufficient care, lack of diligence, or disregard of the applicable standard of caution, thereby causing loss even though the director did not intend to cause such loss (Damanik, 2026). In cases involving errors or negligence by subordinates, the relevant inquiry is whether the Board of Directors itself was negligent in selecting the subordinate, delegating authority, issuing instructions, exercising supervision, or following up on the subordinate's actions. Accordingly, the measure of liability is not merely who directly performed the act, but whether the Board of Directors properly discharged its managerial obligations.

Second, the Board of Directors must establish that management was conducted in good faith and with prudence for the benefit of the company and in accordance with its purposes and objectives. The criteria for good faith by directors in managing a company include honesty and sincerity, compliance with applicable law, conduct consistent with business norms and reasonableness, possession of the competence required of a director and action within the scope of that competence, and the absence of conflicts of interest (Taurisa, 2023). This element demonstrates that directors are not merely required to act without bad faith, but must also exercise an objectively reasonable degree of care in performing their management functions. In relation to subordinate errors, such prudence may be demonstrated through adequate standard operating procedures, clear allocation of duties, internal control systems, reporting mechanisms, supervision, and performance evaluation. Where such mechanisms have been established and reasonably implemented, and a subordinate subsequently commits misconduct outside the scope of delegated authority and without the Board of Directors' knowledge, there is a stronger basis for the Board of Directors to seek exoneration from personal liability.

Third, the Board of Directors must establish the absence of a conflict of interest, whether direct or indirect, in the management action that caused the loss. Law No. 40 of 2007 does not define the term "conflict of interest." A relevant definition can be found in Article 1 point 4 of Financial Services Authority Regulation (POJK) No. 42/POJK.04/2020 on Affiliated Transactions and Conflict-of-Interest Transactions, which defines a conflict of interest as "a difference between the economic interests of the company and the personal economic interests of a member of the Board of Directors, a member of the Board of Commissioners, a principal shareholder, or a controller that may be detrimental to the company." The key element of this definition is the existence of divergent economic interests. This provision is important because a subordinate's error may form part of a series of acts that ultimately confer a personal benefit on a director. For example, if a director knows that a subordinate is engaging in a transaction that violates company procedures but allows it to continue because the transaction benefits the director or a related party, it would be difficult for the director to rely on Article 97 paragraph (5) as a basis for exoneration. Accordingly, independence and the primacy of the company's interests are important parameters in determining the boundaries of directors' liability.

Fourth, the Board of Directors must establish that it took measures to prevent the occurrence or continuation of the loss. This element is particularly relevant to errors committed by subordinates. An initial error by a subordinate does not necessarily immediately give rise to the personal liability of the Board of Directors. However, once the Board of Directors knows or ought reasonably to know of the error and fails to take the necessary measures, its legal position may change. Tolerating known misconduct may constitute negligence on the part of the Board of Directors itself. Conversely, where the Board of Directors promptly conducts an investigation, stops the harmful conduct, improves the relevant system, imposes sanctions or corrective measures, and takes steps to prevent the loss from increasing, such conduct may support satisfaction of the exculpatory requirement under Article 97 paragraph (5) letter (d).

4. CONCLUSION

Based on the foregoing analysis, it may be concluded that the Board of Directors, in performing its duties and responsibilities, cannot be separated from the role of functional units operating under its authority. The Board of Directors has the authority to delegate or distribute functions to subordinates, accompanied by a corresponding duty of supervision as part of its management function. Such delegation is an organizational necessity for the effective operation of the company. Nevertheless, it must be accompanied by clearly defined limits of authority, a clear allocation of duties, adequate instructions, and effective mechanisms of supervision and control.

Furthermore, directors' liability for losses arising from errors or negligence by subordinates must be determined by examining whether there is a causal relationship between the loss suffered and the directors' own fault or negligence in performing their management and supervisory duties. Articles 97 paragraphs (3) and (5) constitute the principal parameters for determining the boundaries of directors' liability. In principle, where the loss did not result from the directors' fault or negligence, and the directors can establish that they managed the company in good faith and with due care, had no conflict of interest, and took reasonable mitigating measures, they should not be held personally liable under the protection afforded by the BJR. Therefore, clear governance of delegated authority and supervision is essential, including through an appropriate allocation of duties, defined limits of authority, standard operating procedures, internal control systems, reporting mechanisms, and evaluation processes. These mechanisms are intended to establish an objective distinction between a subordinate's error, which is the personal responsibility of the actor, and a loss that reflects a failure by the Board of Directors to discharge its managerial duties and responsibilities, thereby ensuring a proportionate allocation of liability.

Accordingly, future research may focus more concretely on examining the standards or parameters applicable to the exculpatory grounds available to directors under Article 97 paragraph (5) in cases involving errors or negligence committed by persons who functionally operate under the Board of Directors. The parameters concerning fault or negligence, good faith, conflicts of interest, and preventive measures to avert loss should be further clarified and positively formulated in order to provide greater legal certainty concerning directors' liability in connection with the management function in its broad sense.

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