

CHAPTER II
LITERATURE REVIEW

A. ASEAN Economic Community (AEC)

ASEAN Economic Community is an International agreement that is based on the principle of market liberalization. Indonesia and nine other ASEAN member States have agreed agreement ASEAN Economic Community.

The ASEAN Economic Community aims to create a single market and production base characterized by free flow of goods, services, investment, skilled labor and capital movement of goods more freely. It is a program in economics that emphasizes on the single market open according to ASEAN Economic Community blueprint that contains 4 main frameworks, namely¹:

1. Towards a single market and production base (current free trade for the goods, services, investment, skilled labor and capital);
2. Towards the creation of regional economy with high competitiveness (regional competition policy, Intellectual Property Rights action plan, infrastructure development, Information and Communication Technologies, energy cooperation, taxation, and the development of Small Medium Enterprises);

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¹ Ministry of Trade, 2015, *Buku Menuju ASEAN Economic Community*, Jakarta, p. 9.

3. Towards a region with equitable economic development (region of equitable economic development) through Small Medium Enterprises development and programs of the Initiative for ASEAN Integration (IAI); and
4. Towards the full integration of the global economy (a coherent approach in the external economic relations and to encourage participation in the global supply network).²

Five core principles of the ASEAN single market and production base comprise:

1. Free flow of goods
2. Free flow of services
3. Free flow of investment
4. Free flow of capital
5. Free flow of skilled labor

From those principles, this thesis focuses on free flow of investment. ASEAN are near with the investment, and below is the explanation on free flow investment. Free flow of Investment ASEAN is committed to build an investment field to attract business. It creates the ASEAN Comprehensive Investment Agreement (ACIA), which includes a commitment to liberalize

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² Mukti Fajar, 2015, "Strategi Kebijakan Perlindungan Investor Lokal Dalam Arus Bebas ASEAN Economic Community". *Jurnal Fakultas Hukum Universitas Muhammadiyah Yogyakarta*.

and protect cross-border investment operations, together with best practices for the treatment of investors and foreign investment.³

The ASEAN Comprehensive Investment Agreement which will build on the existing ASEAN Investment Area (AIA) agreement and ASEAN Investment Guarantee Agreement (AIGA) cover the following pillars:⁴

1. Investment Protection

This pillar provides enhanced protection to all investors and their investment to be covered under the comprehensive agreement. The action to strengthen among others the following provisions, while there were some ways on the investor-state dispute settlement mechanism:

- a. Transfer and repatriation of capital, profits, dividends, etc;
- b. Transparent coverage on the expropriation and compensation;
- c. Full protection and security; and
- d. Treatment of compensation for losses resulting from strife.

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³ ASEAN up Empowering business in Southeast Asia, Benefits of the ASEAN Economic Community-AEC, available at <http://aseanup.com/benefits-asean-economic-community-aec/>. Accessed on March 13, 2016 at 6.17 a.m.

⁴ Ministry of Trade, 2015, *Perjanjian ASEAN Economic Community Blueprint*, Jakarta, p. 12-14.

2. Facilitation and Cooperation

Facilitation and cooperation provided by AIA is more transparent, consistent and predictable investment rules, regulations, policies and procedures. The actions:

- a. Harmonise, where possible, investment policies to achieve industrial complementation and economic integration;
- b. Streamline and simplify procedures for investment applications and approvals;
- c. Promote dissemination of investment information: rules, regulations, policies and procedures, including through one-stop investment centre or investment promotion board;
- d. Strengthen databases on all forms of investments covering goods and services to facilitate policy formulation;
- e. Strengthen coordination among government ministries and agencies concerned;
- f. Consultation with ASEAN private sectors to facilitate investment; and
- g. Identify and work towards areas of complementation ASEAN-wide as well as bilateral economic integration.

3. Promotion and Awareness

Promote ASEAN as an integrated investment area and production network. The actions:

- a. Create the necessary environment to promote all forms of investment and new growth areas into ASEAN;
- b. Promote intra-ASEAN investments, particularly investments from ASEAN-6 to CMLV countries (Cambodia, Myanmar, Laos, and Vietnam);
- c. Promote the growth and development of Small Medium Enterprises and Multinational Enterprises (MNEs);
- d. Promote industrial complementation and production networks among Multi National Corporations (MNCs) in ASEAN;
- e. Promote joint investment missions that focus on regional clusters and production networks;
- f. Extend the benefits of ASEAN industrial cooperation initiatives in addition to the ASEAN Industrial Cooperation Scheme to encourage regional clusters and production networks; and
- g. Work towards establishing an effective network of bilateral agreements on avoidance of double taxation among ASEAN countries.

4. Liberalisation

Progressive liberalisation of ASEAN Member Countries' investment regime is to achieve free and open investment by 2015. The actions:

- a. Extend non-discriminatory treatment, including national treatment and most-favoured nation treatment, to investors in ASEAN with limited exceptions, minimize and where possible, eliminate such exceptions;
- b. Reduce and where possible, eliminate restrictions to entry for investments in the Priority Integration Sectors covering goods; and
- c. Reduce and where possible, eliminate restrictive investment measures and other impediments, including performance requirements.

B. The General Review of the ASEAN Comprehensive Investment Agreement (ACIA)

The ASEAN Comprehensive Investment Agreement is ASEAN's instrument aimed at ensuring the free flow of investments within ASEAN in support of the goals of an integrated ASEAN Economic Community.

The ASEAN Comprehensive Investment Agreement promises to provide multiple benefits to ASEAN investors under its four (4) pillars of Investment Liberalisation, Protection, Promotion and Facilitation. ASEAN Member States value the growth and development dividends that can flow from increased economic integration. There is a consensus, reflected in

ASEAN Comprehensive Investment Agreement, that cross-border investment has a positive role to play in all ten ASEAN Member States and that investors should be encouraged to maintain and expand their investments throughout the region. This is the background to ASEAN Comprehensive Investment Agreement and goes a long way towards explaining why it offers potentially significant advantages to ASEAN investors doing business across the region.

The ASEAN Comprehensive Investment Agreement facilitates the progressive liberalisation of investment in 5 main sectors: manufacturing, agriculture, fishery, forestry, mining and quarrying, and related services. In other words, the liberalisation of investment under ASEAN Comprehensive Investment Agreement comprehensively considers primary, secondary, and tertiary sectors. ASEAN investors further benefit from the forward-looking provisions of ASEAN Comprehensive Investment Agreement, including in regard to transparency disciplines and the promotion of ASEAN as an integrated investment destination.

In liberalised sectors, ASEAN Comprehensive Investment Agreement commits ASEAN Member States to treat ASEAN Investors and investments in a non-discriminatory manner with regard to the national treatment and most-favoured-nation treatment principles. Limitations on the nationality of senior management and boards of directors are also minimised under ASEAN Comprehensive Investment Agreement.

In addition, ASEAN Comprehensive Investment Agreement offers a series of guarantees to ASEAN investors that host country investment regulation will be fair and non-discriminatory. The ASEAN Comprehensive Investment Agreement offers wider coverage than previous investment instruments within ASEAN. The substantive protection and guarantees offered under the agreement are clearer than those found in previous ASEAN investment instruments.

The ASEAN Comprehensive Investment Agreement responds to the concerns of foreign businesses over the potentially capricious nature of host country regulatory changes and seeks to provide rights of recourse that are efficient, transparent and legally binding. The collective commitment of ASEAN Member States to a rules-based system of dispute settlement is a significant improvement over the previous approach where business people had to rely on diplomatic protection from their home country governments. The provision of Investor-State Dispute Settlement (ISDS) depoliticises potential conflicts between individual investors and host states, allowing the former to prosecute alleged treaty breaches and defend their property rights without soliciting the support of their Governments.

The Investor-state dispute settlement mechanism offered by ASEAN Comprehensive Investment Agreement includes mediation, conciliation, and international arbitration. Of these, arbitration is likely the most relevant in

addressing major investment disputes and is accordingly the subject of some of ASEAN Comprehensive Investment Agreements most detailed rules.

C. Overview of Investment

The government of Indonesia recognizes that foreign capital investment has a major role in economic development. However, foreign capital investment is realized to be complementary means for the acceleration of economic development of the country.⁵ Law No. 1 of 1967 on Foreign Investment is the legal basis for the investor to invest their money at the time, and this law was amended by Law No. 11 of 1970 on Foreign Investment.

Law No. 25 Article 1 (1) of 2007 on Investment was enacted to revise the previous regulation related to the investment. By definition, the word “Investment” means any form of investing activity by both domestic and foreign investors to do business in the territory of the state of the Republic of Indonesia.

From the definition above, there are two types of investments according to Law No. 25 Article 1 (2) of 2007 on Investment; on the one hand, “Domestic Investment” means an investing activity which is done in the territory of the state of the Republic of Indonesia by a domestic investor or by using domestic capital. According to Law No. 25 Article 1 (3) of 2007 on

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⁵ Sudargo Gautama, 2006, *Indonesian Business Law*, Bandung: Penerbit PT. Citra Aditya Bakti, p.359

Investment, on the other hand, “Foreign Investment” means an investing activity done in the territory of the state of the Republic of Indonesia by a foreign investor both by the use of all of the foreign capital and by engagement in a joint venture with a domestic investor.

Actually, all business sectors are open for investment. Therefore, the government determines the requirement and the details sectors based on priorities for the investment. Those kind of policies are related to the objectives of investment. Among the objectives of investment are:

1. Increasing national economic growth;
2. Creating job opportunity;
3. Improving sustainable economic development;
4. Improving the competitiveness of national business sphere;
5. Increasing the capacity and the capability of the national technology;
6. Encouraging people economic development;
7. Processing economic potential into the real economic strength by using fund coming from both domestic and foreign countries;
8. Improving the prosperity of the community.

The Law No. 25 of 2007 Articles 14, 15 and 16 on Investment regulate the rights, obligations, and liabilities that have to be conducted by the investor. Law No. 25 Article 14 of 2007 on Investment states that every investor shall be entitled to obtain:

1. Right certainty, legal certainty, and protection certainty;

2. Open information about business fields it is running;
3. Service; and
4. Various forms of the facility according to the rules of law.

The Law No. 25 Article 15 of 2007 on Investment mentions that every investor is also required to:

1. Apply the principle of good company management;
2. Implement the company's social liability;
3. Make a report on investment activity and submit it to the Investment Coordinating Board;
4. Respect the cultural tradition of communities around the location of investment business activity;
5. Comply with all of the rules of law.

In addition, Law No. 25 Article 16 of 2007 on Investment regulated that every investor shall be liable to:

1. Secure capital originating from any sources, not in violation of the rules of law;
2. Bear and settle any obligations and losses if such investor halt or leave or abandon its business activity unilaterally in accordance with the rules of law;
3. Create a healthy competitive business climate, refrain from monopoly practice, and any other matters that inflict damage to the state;
4. Preserve the environment;

5. Provide safety, health, convenience, and prosperity of workers; and
6. Comply with all of the rules of law.

Those kinds of regulations were enacted by the government to give the legal certainty for the investor and also protect the national interest of Indonesia. The Law No. 25 of 2007 on Investment is the legal basis and also the norm that has to comply by the investor as the parties who take a part in Indonesian business sectors.

D. The General Review of The Foreign Investment in Indonesia

Foreign investment in Indonesia is generally governed by Law No. 25 of 2007 on Investment and a broad range of implementing legislation, including Presidential Regulation No. 39 of 2014 and Regulation of the Head No. 5 of 2013 on the Investment Coordination Board, which was amended by Head No. 12 of 2013 on the Investment Coordination Board. In addition, Law No. 40 of 2007 on Limited Liability Companies and sectoral legislation has an important impact on foreign investment.

Under the Investment Act, all business fields and business types are open to investment, except for business fields and business types that are declared to be closed or conditionally open. The business fields that are closed to foreign investors are production of weapons, ammunition, explosive devices and armaments. In addition, Presidential Regulation No. 39 of 2014 on list of business fields closed to investment and business fields open, with

conditions, to investment introduces a Negative List that sets out the lines of business that are closed to foreign investors (including lines of business that are reserved for Small Medium Enterprises/*UKM*), and lines of business that are open to foreign investors under certain conditions. Such conditions can be in the form of, inter alia, local partnership requirements, limitations as to permitted locations and special licence requirements. The Negative List also opens up certain business fields or increases the foreign shareholding limits in such fields for investors from ASEAN Member States.

Foreign investment must in principle be made through a limited liability company established under Indonesian law and domiciled within the territory of Indonesia.⁶ A limited liability company that is (partly) owned by a foreign investor should have the status of a foreign investment company. In principle this also applies to the subsidiaries of the company. Foreign investors who make an investment through a foreign investment company may subscribe for shares at the time the company is established, purchase shares in the company, or follow an alternative method in accordance with prevailing laws and regulations.

The government agency that handles investment, including foreign investment and related licensing matters, is the investment coordinating

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⁶ Instead of making an investment through a PMA company, a foreign company may choose to open a representative office. A representative office gives a foreign company a minimal presence in Indonesia, allowing the company to promote its products and services but not to engage in direct sales or contracts.

board. Other government agencies that may play a role in handling foreign investment matters include the Ministry of Law and Human Rights (MOLHR) and the Ministry of Trade.

Foreign investors wishing to establish a foreign investment company in Indonesia are required to obtain a principle licence from the investment coordinating board. This principle licence serves as an investment permit that authorises the foreign investor to establish the company.

Indonesian law does not create a formal procedure for an applicant for a licence or approval that does not agree with a decision by the relevant government authority to apply for administrative review. However, a foreign investor may submit a complaint to the investment coordinating board regarding government services relating to foreign investment. Furthermore, it is possible for an individual or a legal entity to submit a claim to the administrative courts, which has the authority to review government institutions' written decisions with legal effects that are individual, concrete and final.⁷ There are two grounds for review: contravention of laws and regulations or that of general principles of proper administration. Written principles are the principles of legal certainty, proportionality, disciplined state management, transparency, professionalism and accountability. The administrative courts also apply unwritten principles, such as misuse of power

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⁷ Decisions by the KPPU are excepted from this general rule and may be reviewed by the general courts.

and arbitrariness. In practice, it may be hard for a foreign investor to win a case.

E. The requirements of establishing the foreign investment company

Generally, the following licenses/documents are required for the establishment of a limited liability company for foreign investment company in Indonesia:

1. Principle License & Business License from investment coordinating board, estimated time 7 days.
2. Deed of Establishment (containing the Articles of Association) legalized by a Public Notary, estimated time 1 to 2 days.
3. Legalization of the legal entity status of the limited liability company for foreign investment company by the Ministry of Law and Human Rights, estimated time 10 days.
4. Domicile Letter from the local district authority, estimated time 3 days.
5. Tax Identification Number (*NPWP*) and taxable entrepreneur confirmation (*PKP*) from the tax office, estimated time 3 days.
6. Company Registration Certificate (*TDP*) from the agency for integrated licensing services (*BPPT*), estimated time 14 days.
7. Manpower Report and Company Welfare Report from the sub-department of the Ministry of Manpower, estimated time 7 days.

Note: the licenses/documents listed above involve the general guideline for the establishment of a limited liability company for foreign investment company. However, additional licenses and/or documents can be required in specific sectors. Therefore legal advice should be sought before engaging in investment activity.

F. Deed of Establishment of the Limited Liability Company for Foreign Investment Company

In order to set up a limited liability company for foreign investment company in Indonesia, the shareholders must present a deed of establishment which needs to be legalized by a public notary. The deed of establishment contains, besides the Articles of Association, the following additional information:

1. Regarding the Founders:
 - a. In case the shareholder is an individual, the name, date of birth, place of birth, current residence information and citizenship.
 - b. In case the shareholder is a legal entity, the domicile of the legal entity, including the full address, the date and number of legalization of the ministry.
2. Regarding Board of Directors and Board of Commissioners.

The name, date of birth, place of birth, current residence information and citizenship information of the members of Board of

Directors and Board of Commissioners who are first appointed through the deed of establishment.

3. Regarding the Shareholders (other than the founders).

The names, the number of shares and their issued and paid up nominal value.

G. The History of Regulation from Investment Coordinating Board

In order to follow the Law No. 25 of 2007 on Investment and Presidential Decree No. 27 of 2009 on One-Stop Services in the Field of Investment, improvements have to be made both internally and for the benefit of the implementation of the licensing service in the region, among others, by making changes to its guidance application procedures of capital investment, control the implementation of planting capital, reorganize standard licensing procedures of investment, build and Information Service System and Investment Electronic Licensing. New policies that have been published are:

1. Regulation of the Head No. 11 of 2009 on the Investment Coordinating Board regarding Implementation Procedures, Guidance and Reported from Investment Coordinating Board;
2. Regulation of the Head No. 12 of 2009 on the Investment Coordinating Board regarding Procedures for Application of Capital;

3. Regulation of the Head No. 13 of 2009 on the Investment Coordinating Board regarding Guidelines and Procedures for Investment Implementation Control;
4. Regulation of the Head No. 14 of 2009 on the Investment Coordinating Board regarding Information Service System and Investment Electronic Licensing.

These regulations become effective and become the basis of investment activity in the central and regional. The enactment of regulations on the licensing service then all kinds of permissions that during conducted in Investment Coordinating Board will change, both in type and form of consent, Standard Operating Procedure and this will change the order of licensing services in the field of investment. Likewise, the use of system services electronically using National Single Window for investment is expected to be greater certainty speed, easy for investors to apply. Due to the electronic service system of the letter of approval issued in the Central and Regional have the same format nationally.

The regulation of the Head No. 11, 12 and 14 of 2009 on the Investment Coordinating Board is a rule that will be used to support the implementation of the Investment Coordinating Board conducted nationally using Information Service System and Investment Electronic Licensing information system. While the Regulation of the Head No. 13 of 2009 on the Investment Coordinating Board regarding Control of Investment

Implementation, used in the context of supervision, coaching, guidance on the implementation of the investments made by the business world.

Broadly speaking, the basics of service Presidential Decree No. 27 of 2009 on One-Stop Services, which will be the basis for the licensing service includes several elements. The emphasis is different from the regulatory processes and procedures previously. The elements include:

1. Easy, simple petition settlement process flows are easily understood since the requirements are simple;
2. Hurry, time is shortened for petition in the resolution process;
3. Right, it refers to the conformity of products with the provisions of laws and regulations;
4. Accurate, facilitation of imports of machinery, goods and materials is in accordance with the needs of production; and
5. Transparent and accountable, the settlement request process flows are clear and accountable.

H. The principle of One Stop Service on the Investment

One Stop Services is the Implementation activity of a licensing and non licensing received by the delegation or the delegation of authority of the agency or agencies that have authority for licensing and non licensing management process starting from the proposal stage to the stage of publication of documents that are done in one place.

Licensing is any form of approval for Investment issued by the Government and the local government that has the authority under the provisions of the legislation.⁸

Non licensing is any form of convenience services, fiscal facilities, and information on the investment, in accordance with the provisions of the legislation.⁹

One stop service aims to gain the ease of service, fiscal facilities, and information regarding the Investment, by accelerating, simplifying services and alleviating or eliminating the cost of obtaining a license and non Licensing.

To improve the Integrated One Stop Service and shorten its process, on 15 September 2014 the President issued Regulation No. 97 of 2014 on Organization of Integrated One Stop Service (New Regulation), which has been in effect since the date it was registered on 18 September 2014. Unlike the 2009 Integrated One Stop Service (*PTSP*), the scope of 2014 Integrated One Stop Service is not only restricted to licenses and non-licenses in the field of capital investment, but also covers all licenses and non-licenses which

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⁸ Regulation of the Minister of the Interior Number 27 of 2009, Chapter I Article 1 Paragraph

⁹ Regulation of the Minister of the Interior Number 27 of 2009, Chapter I Article 1, paragraph

become the authority of the Central Government and the Regional Government¹⁰

I. The General Review of Domestic Investment in Indonesia

Domestic Investment is an investment activity to business in the territory of the Republic of Indonesia by a domestic investor by using domestic capital. Definition of a domestic investor is an individual in Indonesian citizens, Indonesian business entities, the Republic of Indonesia, or any region investment in the territory of the Republic of Indonesia. Indonesian business entity intended here can form a limited Liability Company.

According to Law No. 25 Article 5 (1) of 2007 on Investment, domestic investment that can be done in the form of business entity is a legal entity. It is not a legal entity, or individual, in accordance with the provisions of the legislation. Law No. 25 article 5 (3) of 2007 on Investment further explains that domestic investors and foreigners investing in the form Limited Liability Company can be done by doing the following:

1. Taking shares in the establishment of a limited liability company;
2. Purchasing shares; and

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¹⁰ Presidential Regulation No. 97 of 2014 on Organization of Integrated One Stop Service (New Regulation)

3. Performing other means in accordance with the provisions of the legislation.

Legalization and Licensing from domestic investment under Law No. 25 (4) of 2007 on Investment, corporate investors, including domestic, that will conduct business activities must obtain a permit in accordance with the provisions of the legislation of the agencies that have authority. Licenses as mentioned previously can be obtained through the one stop service. Single service counter is intended to assist investors in obtaining the ease of services, fiscal facilities, and information on the investment; it is about domestic investment and foreign direct investment.

1. Pursuant to Law No. 25 article 18 (2) of 2007 on Investment explained that the investment facility can be given to investors who:
 - a. Expand its business; and
 - b. Make new investment.
2. Law No. 25 article 18 (4) of 2007 on Investment describes the shape of the facilities provided by the government to investors, including domestic, can be:
 - a. Net income tax deduction up to certain level of investment made within certain period;
 - b. Import duty holiday or reduction for imported capital goods, machinery, or equipment domestically unavailable for production;

- c. Import duty holiday or reduction for raw materials or support materials for production within certain period and with certain conditions;
- d. Value added tax holiday or postponement for imported capital goods or machinery or equipment domestically unavailable for production within certain period;
- e. Accelerated depreciation or amortisation; and
- f. Property Tax reduction, especially for certain business fields in certain region, area, or zone.

J. The General Review of The Joint Venture

There are three variations of direct investment:

1. An overseas company that is 100% owned by domestic companies and operates as a representative for the company in the country.
2. An overseas company owned 100% by the citizens of investors, but it was formed to work abroad.
3. The joint ownership over companies abroad between citizens and foreign national investor which the investment is made. It is often referred to as joint ventures.

Definition of a joint venture was not expressly provided for in the Law, but it is described Law No. 25 article 5 (3a) of 2007 on Investment which states: “having shares when such company is established”.

In the book Anderson's Business Law and The Legal Environment written by David P. Twomey stated “Joint venture is relationship in which two or more persons combine their labor or property for single business undertaking and share profits and losses equally or as otherwise agreed.”¹¹

From the above understanding, we can see that the joint venture is a framework agreement between the two parties (the company) or more that have the same goal. This agreement usually leads to the formation of a joint venture company. With this joint venture scheme, the parties get several benefits such as:

1. Reducing the need for capital and other resources for their needs of sharing element;
2. Transferring technology between the parties;
3. Minimizing business risks; and
4. Allowing developing the business to a global scale.

In its development, the joint venture is often associated with the ability of national capital that has been able to conduct business cooperation with foreign investors through the form of Foreign Direct Investment in Indonesia. Even in his Hartono Sunaryati Transnational Issues in Some Foreign Investment in Indonesia proposed joint venture restrictions as any joint venture between Indonesia's capital and foreign capital, whether it is a joint effort between the private sector and the private sector, government and the

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¹¹ David P. Twomey, 2015, *Anderson's Business Law And The Legal Environment*, Jakarta.

private sector, or the government and the government. Also do not distinguish whether the joint venture is considered as foreign investment or domestic investment.¹²

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¹² Prof. Dr. Carolina Felicita Gerardine Sunaryati Hartono, 2016, *Beberapa Masalah Transnasional Dalam Penanaman Modal Asing di Indonesia*.