LEGAL IMPLICATION OF AFTA TOWARD LEGAL PROTECTION OF INVESTOR IN INDONESIA AND MALAYSIA INVESTMENT LAW

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"*Those who have believed and whose hearts are assured by the remembrance of Allah . Unquestionably, by the remembrance of Allah hearts are assured."*

- *QS.* Ar-Ra'd (13:28)

"Think brilliant, act wisely"

- Ahmad Wirayudha Nugraha

"I don't trust anyone who's nice to me but rude to the waiter. Because they would treat me the same way if I were in that position"

- Muhammad Ali

"*Well, it's no secret that the best thing about a secret is secretly telling someone your secret, thereby, secretly adding another secret to their secret collection of secret, secretly."*

- *Spongebob Squarepants*

DEDICATIONS

This thesis is dedicated to:

Allah SWT All-Mighty, All-Knower that always assists and guides me.

My beloved Mom and Dad. Thank you for every love, spirit, pray and attention.

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Yogyakarta, 1 Desember 2018

The Writer

Ahmad Wirayudha Nugaraha

ABSTRACT

Globalization era provides opportunities to develop their countries, one of them through opening investment flows. Investment flow is currently growing rapidly which can be seen from each year increasing. With resources and many strategic sectors, Indonesia should be the first choice for investors to invest. Investment growth in Indonesia is still relatively slow compared to other ASEAN countries especially Malaysia. Since 2010, Malaysia's investment growth has always increased dramatically, including the fastest investment growth besides Singapore. The existences of legal certainty and convenience of investment are the key to attract domestic and foreign investors to invest in Malaysia. This research method is normative research that is the study of law conducted by examining the literature, using the object of writing studies in the form of existing libraries with comparing investment law of both countries, whether in the form of books, journal, and regulation that have a correlation to the issues discussed. The WTO as an organization in the trade sector has provided and paved the way for multilateral, bilateral and regional agreements. One in the regional field is AFTA. The ASEAN Free Trade Area (AFTA) is a trade agreement between the Association of Southeast Asian Nations and ASEAN countries, and facilitating economic integration with regional and international allies. Indonesia and Malaysia have agreed to ratify the treaty agreement that is in the AFTA agreement, which means the two countries are ready with the consequences to provide an easy way for free trade in ASEAN such as business licensing, taxes and incentives for investors however, Indonesia as a developing country must take appropriate steps to protect national interests. Although the existence of AFTA offers many benefits for Indonesia, protection of national interests must be taken into account in policy making. The Government has an obligation to protect national interest in order to prosper Indonesia people.

Keywords: investment, investor, legal protection, ASEAN Free Trade Area (AFTA).

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CHAPTER I

INTRODUCTION

A. Context of Study

The impact of globalization that can be felt is the openness in various fields, not least in the business field better known as the era of free markets or trade liberalization.[1] Unconscious globalization will go on without anyone stopping it. The boundaries between countries are increasingly difficult to distinguish and even tend to be borderless. For that reason, that's why every country competes to attract potential investors, especially foreign investors.

In essence, developing countries are in dire need of investment, especially Foreign Direct Investment (FDI). The purpose of this investment is to accelerate the pace of development in the country. In general, those who have capital or investment are the developed countries.

But the problem is that interest or investment desire among foreign investors is strongly influenced by internal conditions in a country to be entered, such as economic and political stability of the country, law enforcement, and other tools. It is also influenced by external state conditions such as the influence of international economic situation, competitor's presence factor from other countries, and others.

[1] Alan Collins, *"Security and Southeast Asia: Domestic, Regional, and Global Issues"*, Institute of Southeast Asian Studies, Singapore, 2003, P.75

Therefore, there is a tendency for investment graph from foreign investors to be fluctuating.[2]

Before deciding to invest, investors first conduct feasibility studies on the business prospects that will be run. Including the studied is the provisions of legislation that have to do with the investment that will be run. The problem for investors is if the losses suffered are not due to mismanagement of the company, but there is no legal protection, either to the capital that he cultivated or the goods to be produced.[3]

The consequence that arises from the era of trade liberalization is the investors will get a variety of conveniences or no more difference in the treatment of investors who are under the umbrella of World Trade Organization (WTO) members in running their business in various places desired by these investors. For that many countries try to seize this opportunity by creating a conducive business climate, especially in the field of investment. Steps were taken in creating a conducive investment condition that is by adopting rules of rules that are born in the international association. Improved international relations and trade resulted in many international regulations being put into national regulations.[4]

Since the beginning of Indonesian independence, there has been a lot of pros and cons on the ease for foreign investors to invest in foreign capital invested by

[2] Hendrik Budi Untung, *Hukum Investasi*, Sinar Grafika, Jakarta, 2013, P.33

[3] Sentosa Sembiring, *Hukum Investasi*, CV. Nuansa Aulia, Bandung, 2014, P.170

[4] Meredith A. Crowlew, "An Introduction to WTO and GATT", *Economic Perspective Journal*, Vol 2 No. 2, 2003, P.17

nationalism as a sovereign country. The sovereignty of a country diminishes with the regulation of the freedom of economic transactions that eliminates barriers and generates liberalization in the economic field.[5] The integration of the national economy into a global system in economic processes such as deregulation and free trade can even threaten national sovereignty. Currently, there is still a reluctance of many parties to the presence of foreign investors because the investment made by the giant company is a new form of economic colonization that will extort the nation and its natural resources. In any case, foreign investment is taken by the owners of capital to benefit from its investment activities.[6]

Indonesia is a country with a growing economy. To build the economy, the need for capital or investment is very large. Investment activity in Indonesia has been started since 1967, that is since the issuance of Law Number 1 Year 1967 About Foreign Investment and Law Number 6 Year 1968 About Domestic Investment. The existence of the two legal bases or commonly referred to as a legal instrument is intended to attract local and foreign investors and provide convenience to invest in Indonesia.

The participation of Indonesia as a member of the WTO brings its own legal consequences, in the form of an obligation to ratifying the approval of the formation of the WTO through Law No.7 of 1994 which means that Indonesia has an attachment to implement all the agreements resulted in the negotiations of Uruguay

[5] William J. Davey, *Non-Discrimination in the WTO, The Rules and Exceptions,* Triangle Bleu, France ,2012, P.2

[6] Jonker Sihombing, *Hukum Penanaman Modal di Indonesia*, Alumni, Bandung, 2009, P.78

namely the Agreement on Trade Related Investment Measures (TRIMs) agreement on aspects of trade-related intellectual property rights (TRIPs) and the General Agreement on Trade in Services or General Agreement on Trade in Service (GATS).[7] Members of the WTO are required to comply with the established standards, nevertheless, provide exceptions especially for developing countries to regulate in particular matters that are deemed important and closely related to the needs of their country in the corridors of the development of international trade.[8]

Indonesia's membership in the WTO has resulted in the reform of the Indonesian Investment Law by issuing Law Number 25 Year 2007 regarding Investment to replace Law Number 1 Year 1967 which is deemed to be no longer appropriate to encourage increased competitiveness the national economy for the creation of Indonesia's economic integration into the global economy. With the enactment of this new regulation is expected to provide legal certainty (legal certainty) to attract foreign capital. In addition, economic opportunity and political stability factors are also crucial in bringing foreign capital into a country.[9]

Judging from the history of the arrangement, it can be seen that in those regulations there is discrimination between a foreign investor and domestic investor, it is seen from the amount of capital that must be owned by a domestic investor in a

[7] Syahmin, *Hukum Dagang International*, Raja Grafindo Persada, Jakarta, 2005, P.86
[8] *Ibid*., P.51
[9] Suparji, *Penanaman Modal Asing di Indonesia Insentif Versus Pembatasan*, Universitas Al-Azhar, Jakarta, 2008, P.1

company must be more / dominate compared with a foreign investor.[10] The investment arrangements contained in the Investment Law are the results of an evaluation of the existing investment provisions by taking into account the attitudes and wishes and expectations of investors who wish to invest their capital in Indonesia, of course, by taking into account the national interest above all the interests of the investors concerned.

Foreign investment in Indonesia is an Investment Coordinating Board (BKPM). The list is regularly reviewed and updated to take into account policy reviews, legislative changes, and the prevailing economic landscape, among other things. In relation to business fields that may be entered by foreign investment, the Government of Indonesia adjusted the negative list of Investment through Presidential Regulation No. 44 of 2016. This Presidential Regulation shall contain four business classifications, namely:

1. Business fields that are absolutely closed for investment;
2. Closed business fields for investments which are in the capital of the enterprise there is the ownership of foreigners or foreign legal entities;
3. Open a business field with joint requirements between foreign capital and domestic capital and
4. Open a business field with certain requirements.

[10] H. Salim HS., dan Budi Sutrisno, *Hukum Investasi di Indonesia*, Raja Grafindo Persada, Jakarta, 2012, P.177.

It appears to show an increasing willingness by the Indonesian government to allow foreign investment and opens up the market somewhat in a number of areas.[11]

Since independence of Malaysia in 1957 has fully capitalized on both its tangible assets such as rich natural resources, abundant and cheap labour, and its sizeable domestic market, as well as its intangible assets, namely its preferential trade status under the Generalized System of Preferences (GSP), macroeconomic stability, liberal trade regime and an efficient legal infrastructure to attract FDI. Broadly speaking, as of date, FDI in the context of Malaysia has been a relatively successful experiment[12]

Malaysia itself has a long history of their investment law. In sum, the crux of the affirmative policy is that, ideally, be held by *Bumiputras* or indigenous people in Malaysia. Malay controlled firms as joint venture partners and suppliers. Evidently, a level playing field for all is still a long way off. Furthermore, it is the policy of national treatment and the most favored nation treatment as advocated under the WTO forum and its related treaties. This policy has from time to time caused social tension, and analysts have argued that it engenders undesirable economic distortions, a culture of complacency, and an aversion to risk-taking.[13]

Malaysia abolishment of the Foreign Investment Committee (FIC) in 2009, Malaysia removed its all-around foreign equity ceiling of 70%. Despite the fact that

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[11] *http://www.mondaq.com/x/500596/Inward+Foreign+Investment/Indonesias+Revised+Negative+Investment+List* accessed on March 20th, 2018

[12] Arumugam Rajenthran, "*Malaysia: An Overview of the Legal Framework for FDI"*, Institute of Southeast Asian Studies, Singapore, 2002, P.1

[13] *Ibid.*, P.2

the general cap is removed, foreign equity restrictions remain in certain sectors. These are imposed by the different Ministries, rather than by a central body.[14] Apart from formalized regulation on the matter, Ministries may also impose equity restrictions as a condition to obtaining a license. A separate set of regulations is imposed to reserve equity in businesses for ethnic Malays or *Bumiputera*. The rationale is to increase business participation of the *Bumiputera*. While Malays ethnic are the majority racial group in Malaysia, they are underrepresented in the country's business community, which is largely made up of ethnic Chinese and Indians. In these cases, the restrictions on foreign equity are not in favor of nationals of Malaysia, but ethnic Malay. In other words, a foreign-invested company where the non-foreign equity is held individuals who are not ethnically Malay would still fall foul of the law. The issue continues to be politically sensitive.[15]

On the other hand, there is a legal code that espouses government policies. This includes the Industrial Coordination Act 1975 (ICA) and the Promotion of Investment Act 1986 (PIA). Evidently, the former is set out to ensure a spectrum of incentives to attract FDI.[16]

This is also reinforced by the presence of Indonesia and Malaysia as members of the ASEAN Free Trade Area (AFTA) with efforts to keep pace with globalization, AFTA is present in the midst of ASEAN countries that will build and promote the

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[14] Majid Ashrafi and Joriah Muhammad, "The Preferences Of Malaysian Institutional Investors", *International Journal of Business and Society*, Vol. 14 No. 3, 2013, P.52

[15] *https://www.export.gov/article?id=Malaysia-1-Openness-to-Restriction-upon-Foreign-Investment* accessed on March 20th, 2018

[16] *Ibid.*, P.8

economy in Southeast Asian countries.[17] AFTA is an agreement established by ASEAN countries to create a free trade zone.[18] Certainly, this free trade movement can have a negative and positive impact on the nation that experienced an unstable economic turmoil like Indonesia.

The Indonesian government has formalized the adoption of the Online Single Submission (OSS) System. Electronic Integrated Business Licensing Services (PBTSE), which is more easily called the generic name OSS is present in the context of business licensing services that are valid in all Ministries, Institutions, and Regional Governments throughout Indonesia, which have been carried out through One-Stop Integrated Licensing (PTSP).[19] Besides through PTSP, the public can access the OSS System online anywhere and anytime. This is a breakthrough for the government to invite more domestic and foreign investors to invest in Indonesia.

Malaysia is one of the potential countries for investment in Indonesia. Despite the decline in 2016, Malaysia remains in the list of the top 10 countries with the largest investment in Indonesia.[20] The Investment Coordinating Board of Indonesia noted that FDI originating from Malaysia reached the US $ 1.1 billion or equivalent to Rp 14.84 trillion. This figure fell 63.74 percent from a year earlier to reach the US

[17] *https://asean.org/asean-economic-community/asean-free-trade-area-afta-council* accessed on October 21st, 2018

[18] Siti anisah, dan Lucky Suryo Wicaksono, *Hukum Investasi*, FH UII Press, Yogyakarta, 2017, P.294

[19] *https://www.hukumonline.com/berita/baca/lt5b433407c8d81/sistem-oss-diluncurkan--izin-berusaha-kini-lebih-mudah* accessed on 28 August 2018

[20] Malaysia Investment Performance Report, Forging Forward 2017

$ 3.07 billion.[21] As of the first quarter of 2017, Malaysia's investment in Indonesia has reached the US $ 215.49 million with 332 projects. This amount of investment has doubled compared to the same quarter of 2016.[22] Malaysia's investment value in the second quarter of 2017 was ranked 10th in the list of countries with the largest achievement to Indonesia.[23]

As a consequence of opening the door for foreign capital activities in the country in connection with its utilization for development projects, it will automatically arise problems and challenges that the government must face with the people with sincerity so that the use of capital can achieve what has been fully planned success. The WTO is a forum of states in agreeing on the exchange of "liberalization" commitments by reducing trade barriers and agreeing on provisions that member states must adhere to, such as opening mutual market access.[24] Article XVI paragraph (4) of the WTO Establishment Agreement becomes an important indicator of the WTO requires its member states to adjust their trade rules or laws to the rules contained in the Annex WTO Agreement.[25]

Malaysia investment developed because there is an influence of AFTA, according to the 2013 Organization for Economic Cooperation and Development

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[21] *http://databoks.katadata.co.id/datapublish/2017/05/26/berapa-nilai-investasi-malaysia-di-indonesia* accessed on October, 21st 2017

[22] ASEAN Investment Report 2017 Foreign Direct Investment and Economic Zones in ASEAN, 2017, P.105

[23]BKPM, *Perkembangan Realisasi Investasi PMA berdasarkan Laporan Kegiatan Penanaman Modal (LKPM),* Menurut Negara Tahun 2017 quarter II

[24] Bernard M.Hoekman dan Michael M. Kostecky, *The Political Economy of the World Trading System: the WTO and Beyond*, Oxford University Press, USA-New York, 2009, P.28.

[25] Huala Adolf, *Hukum Perdagangan Internasional*, Rajawali Pers, Jakarta 2009, P.39

(OECD) Investment Policy Review of Malaysia, FDI to Malaysia began to decline in 1992, and private investment overall started to slide in 1997 following the Asian financial crises. In the intervening years, domestic demand has increasingly been the source of Malaysia's economic performance, with foreign investment receding as a driver of GDP growth. The OECD concluded in its Review that Malaysia's FDI levels in recent years had reached record high levels in absolute terms, but were at low levels as a percentage of GDP.[26]

The post-crisis drop in FDI has prompted Malaysia to take a major step to liberalize its investment regime. Pursuant to Sixth ASEAN Summit meeting in 1998, where members are urged to take "bold measures" to facilitate speedy recovery from the crisis -- including "short term measures to enhance ASEAN Investment Climate", Malaysia offered 100% foreign equity ownership in all manufacturing sectors without any export conditions for all new investment projects or expansion/diversification projects applied by December 31, 2003.[27] This move allows foreign manufacturers to compete in the domestic market. Exceptions were provided for only 7 activities1 reserved for local small and medium enterprises. In June 2003, the Ministry of Trade and Industry decided to make the liberalization permanent. Thus, bar the seven activities mentioned, the entire Malaysia manufacturing sector is now fully open to foreign investment.[28]

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[26] OECD Investment Policy Reviews Southeast Asia, 2018, P.19

[27] *http://www.mida.gov.my/home/investment-incentives/posts/* accessed on August 2nd2018

[28] Shamrahayu A Aziz, "The Malaysian Legal System: The Roots, The Influence and The Future", *Malayan Law Journal Articles*, Vol 3, 2009, P.1

It’s also happens after Indonesia apply AFTA, Indonesia get a lot of benefits. According to the Presidential decree no. 44 of 2016 there is an implementation of AFTA, in enclosure part, as a member AFTA gets a special part that distinguishes it from other countries, such as the number of investment percentages that are more than non AFTA countries. Of course, when viewed from the principle of international trade, this collides with one of its principles, the most favored nation.

The current world economy has been colored by trade blocs, a common market, and free trade agreements based on the synergy of interests between parties or between countries that enter into agreements. This is also the case with Indonesia's involvement in various forms of international cooperation related to investment, either bilaterally, regionally, or multilaterally (WTO), which in turn has consequences which inevitably have to be faced. Some of the consequences that must be faced by Indonesia is to include the same treatment elements/non-discrimination between domestic investment and foreign investment.[29]

In order to evaluate the investment policy position in Indonesia and the investment climate created, it is better to have a comparative with the investment policy in Southeast Asian countries, especially Malaysia.

It is interesting to discuss when Indonesia embraces a civil law system that prioritizes the use of written law and is oriented to a legal certainty, developed in universities or doctrinal writing. The law of Malaysia is mainly based on the common law legal system which puts the law's use in an unwritten and oriented manner to

[29] Jonker Sihombing. *Op.Cit.* P.83-84

justice, developed through practice and procedurals. This situation explains why the system does not start from the principle of legal principle but directly about the rules of principle for concrete cases.[30]

As a fellow country in the south-east Asian region that is predominantly Malay inhabitants, it is interesting to review the law and investment policy in terms of implementation of national treatment in Malaysia, especially during crises where compared to Indonesia, the situation in Malaysia is relatively stable and survive.[31]

This paper is primarily descriptive. It does not propose a model investment law or recommend provisions that should be included in investment laws. On the contrary, one of the key findings of the paper is that a country's investment law cannot be evaluated in the abstract, without considering how it relates to other elements of the legal and regulatory framework governing investment in that country. Nevertheless, understanding how existing investment laws operate in different countries does help to clarify questions that should be considered when revising or adopting a new investment law.

So it is very interesting to be a thesis in addition to knowing about the application of national treatment in the law of investment in Indonesia compared with Malaysia. Through these comparisons will be able to identify the strengths and weaknesses of Indonesia in the competition to attract investment to Indonesia. The

[30] Satjipto Rahardjo, *Ilmu Hukum*, PT Citra Aditya Bakti, Bandung, 2014, P.255

[31] *https://www.cnbc.com/2015/11/20/is-malaysia-facing-a-financial-crisis-one-lawmaker-says-yes.html*. accessed on 20th October 2017

results of this study are expected to be used as input and basic considerations in the framework of improvement and improvement in the future.

B. Problem Formulation

Based on the context of the study above, there are two major problems of discussion:

1. What is an implication of AFTA for Indonesia and Malaysia investment?
2. How is a legal protection for the foreign investor in Indonesia and Malaysia?

C. Research Objectives

Based on the context of the study above, there are also two objective of discussion:

1. To find out what is an implication of AFTA for Indonesia and Malaysia investment
2. To find out how is a legal protection for foreign investor in Indonesia and Malaysia

D. Theoretical Review

Law is a means of community development, which is based on an assumption that the balance or order is desirable, even necessary. Furthermore, another assumption contained in the conception of law as a means of a renewal of society is the law in the sense of rules or rules of law that can serve as a tool or regulator in the

sense of channeling the direction of human activity towards the desired by development or renewal.[32]

There is a theory from J.D. Ny. Hart who gives an explanation about the legal system can play a role in economic development is influenced by elements of predictability, stability, and fairness.[33]

1. Predictability, which is law can create certainty. With certainty, investors can estimate the consequences of the actions that will be done and have certainty how the other side will act.
2. Stability. The role of a state empowered by law is basically in order to maintain a balance to achieve a goal. This balance includes the interests of individuals, groups and common interests that are linked to the challenges being faced both domestically and abroad. Through the Investment Law can be expected to anticipate all the challenges and obstacles that occur around investment law enforcement.
3. Fairness which is law must be able to create fairness for society and prevent the happening of unfair and discriminative practices. Fairness aspects such as due process, equality of treatment and governmental standards of conduct are a need to safeguard market mechanisms and prevent the negative impact of excessive bureaucratic action. The absence of a standard of fairness is said to be the biggest problem faced by developing countries. In the long term,

[32] Mochtar Kusumaatmadja, *Hukum Masyarakat dan Pembinaan Hukum Nasional,* Bina Cipta, Bandung, 1976, P.4.

[33] Suparji, *Op. Cit*., P.15

the absence of such standards could result in the loss of government legitimacy.

Douglass Nort states that the law must be clear, predictable, transparent, and ensure legal certainty in law enforcement (predictability of enforcement). Law enforcement is important in providing foreign investment guarantees.[34]

The legal theories above show the existence of a mutually influential phenomenon between law, economy, and politics. This phenomenon is getting stronger in developed countries as capitalism evolves with the concept of growth that poses an idea that there is a close relationship between economic and political freedom.[35]

Foreign investment is attracted to a legal system that has predictability, stability, and fairness. All three are called the ideal legal system. Inefficient legal systems will increase transaction costs to obtain inexpensive mechanisms in enforcing legal rights and obligations. Low transaction costs can be guaranteed if the laws of the host country are of good quality.

When it comes to economic development it is necessary to discuss FDI. FDI is an investment made by a company or individual in one country in business interests in another country, in the form of either establishing business operations or acquiring

[34] Suparji, *Op. Cit.*, P.19
[35] Suparji, *Op. Cit.*, P.20

business assets in the other country, such as ownership or controlling interest in a foreign company.[36]

According to Organization For Economic Co-Operation and Development (OECD) investment is a category of cross-border investment made by a resident in one economy (the direct investor) with the objective of establishing a lasting interest in an enterprise (the direct investment enterprise) that is resident in an economy other than that of the direct investor. The motivation of the direct investor is a strategic long-term relationship with the direct investment enterprise to ensure a significant degree of influence by the direct investor in the management of the direct investment enterprise. The "lasting interest" is evidenced when the direct investor owns at least 10% of the voting power of the direct investment enterprise. Direct investment may also allow the direct investor to gain access to the economy of the direct investment enterprise which it might otherwise be unable to do. The objectives of direct investment are different from those of portfolio investment whereby investors do not generally expect to influence the management of the enterprise.[37]

According to M. Sornarajah, FDI involves the transfer of tangible or intangible assets from one country to another for the purpose of their use in that country to generate wealth under the total or partial control of the owner of the assets.[38]

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[36] *https://www.investopedia.com/terms/f/fdi.asp* accessed on 1 November 2017

[37] *OECD Benchmark Definition of FDI* Fourth Edition 2008, P.7

[38] M. Sornarajah, *The International Law on Foreign Investment*, Cambridge University Press, USA, 2010, P.7

There can be no doubt that the transfer of physical property such as equipment, or physical property that is bought or constructed such as plantations or manufacturing plants, constitute FDI. Such investment may be contrasted with portfolio investment. Portfolio investment is normally represented by a movement of money for the purpose of buying shares in a company formed or functioning in another country. It could also include other security instruments through which capital is raised for ventures. The distinguishing element is that, in portfolio investment, there is a separation between, on the one hand, management and control of the company and, on the other, the share of ownership in it.[39]

In the case of portfolio investment, it is generally accepted that the investor takes upon himself the risks involved in the making of such investments. He cannot sue the domestic stock exchange or the public entity which runs it if he were to suffer loss. Likewise, if he were to suffer loss by buying foreign shares, bonds or other instruments, there would be no basis on which he could seek a remedy. Portfolio investment was not protected by customary international law. Such investment was attended by ordinary commercial risks which the investor ought to have been aware of. But, the customary international law protected the physical property of the foreign investor and other assets directly invested through principles of diplomatic protection and state responsibility.[40]

[39] *Ibid*., P.8
[40] *Ibid*, P.9

One view maintains that there should be no distinction between portfolio investments and FDIs as to the protection given to either by international law. This view is based on the assumption that there is no distinction between the risks taken by either type of investor, both being voluntarily assumed. But, this view is not accepted generally in international law, where it is clear that FDI alone is subject to the protection of the customary international law. Several reasons are given for this difference in treatment. The foreign investor takes out of his home state resources which could otherwise have been used to advance the economy of the home state. The home state is said to be justified in ensuring that these resources are protected.[41]

There are two theories that analyze the causes of developed countries to invest in developing countries. Both theories include:

1. The Production Cycle Theory. This theory is suitable to apply to FDI in the field of manufacturing, which is the initial expansion of American companies or also known as a horizontally integrated investment, namely the establishment of factory factories to make the same or similar goods whichever. The production cycle theory helps explain why the traits characterize the important features of the contemporary world economy, namely that multinational corporations and oligopoly competition. The development and dissemination of industry technology is a key determinant of trade and location of global economic activity through

[41] *Ibid,* P.10

investment and the emergence of corporate strategy that integrates trade and production abroad.[42]

2. The industrial organization theory of vertical integration. This theory is best suited to new multinationalism and to vertically integrated investments, namely the production of goods in some factories which are inputs to other factory factories of a company. According to this theory, investment is done by means of vertical integration, by placing several stages of production in several different locations around the world. The main motivation are:
    a. To benefit from low production costs
    b. Local tax policy
    c. To create trade barriers for other companies. This means that with foreign investment, this means that the multinational corporation has blocked the arrival of competitors from other countries so the monopoly can be maintained.[43]

E. Research Method

1. Type of Research

This research is included in the type of normative research that is the study of law conducted by examining the literature, using the object of writing studies in the

[42] H. Salim HS., dan Budi Sutrisno, *Op,Cit.* P.157
[43] H. Salim HS., dan Budi Sutrisno, *Op,Cit.* P.160

form of existing libraries, whether in the form of books, journal, and regulation that have a correlation to the issues discussed.

2. Research object

Research object is the things that will be examined, which include the implementation of AFTA and legal protection toward investor in Indonesia and Malaysia investment law

3. Research Sources

This research will use sources:

a. Primary legal sources, the primary data here means binding legal materials that relate to the object of research:

Indonesian Law:

1) Law Number 25 of 2007 on Investment
2) Presidential Decree Number 44 of 2016 on List of Business Fields Closed and Business Fields Open with Conditions to Investment
3) Government Regulation No. 24 of 2018
4) The Promotion of Investment Act (PIA) of 1986
5) The Industrial Co-ordination Act (ICA) of 1975, revised in 1986
6) Foreign Investment Committee (FIC) Guidelines
7) Malaysia Investment Development Authority (MIDA) Policy

b. Secondary legal materials, which consist of:

Malaysian Law:

1) Expert Opinion

2) Journal

3) Article

4) Internet

5) Books which relate to this research object

4. Method of Data Collection

Literature research, that is examining primary legal sources, literature which related to the materials, examines the laws and regulation which are related to the Indonesia and Malaysia investment law.

5. Approach of the Study

This research is a juridical normative research which identified legal norms and legal views. The objective is to understand and answer the problem formulation of study which are the implementation of AFTA and legal protection toward investor in Indonesia and Malaysia investment law

6. Processing and analyze legal materials

The data organize by selecting a data relate to the discussed problem in this research. It is structured descriptively in order to answer the problem in a descriptive analysis. The data collected, managed, and used to answer the problem. The method of data analyzing is a qualitative method. It means that the data achieved is not in form of number and statistic, but analyze qualitatively and descriptively. Moreover, it also highlighting facts, legal enforcement, and bears with the applicable legal aspect. The steps are defined as follows:

a. Classification regulation, cases, and secondary legal sources

b. Systematic of any legal sources

c. Systematic data analyzed and discuss a data to concludes the result of research

F. Structure of Writing

In this thesis, the writer divides a chapter into four chapter: Chapter I is Introduction; Chapter II are Overview of AFTA, an overview of investment law; Chapter III are the implication of AFTA and legal protection toward foreign investor in Indonesia and Malaysia; and Chapter IV Conclusion and Recommendation

In the Chapter I, writer explain the context of study, problem statements, research objectives, theoretical review, research method and systematical of writing. In this research, there are two main problems: first is the impact of AFTA on Investment law in Indonesia and Malaysia, and second is legal protection for foreign investor in Indonesia and Malaysia.

In the Chapter II, writer explains a general overview of investment those are a General overview of free trade, a general overview of AFTA, Investment law in Indonesia and Investment Law in Islamic Perspective.

In the Chapter III, writer explaining into two subchapters. The first legal implication of AFTA, second is legal protection toward foreign investor in Indonesia and Malaysia. For the first subchapter, writer analyzing implication in Indonesia and Malaysia. For the second subchapter, writer analyzing from a legal scope for capital, incentives, and investment dispute settlement, etc.

In the Chapter IV, explains the summary result of the discussion the answer of two problem statements in this thesis. In the end, the writer adds two recommendations in handling both problems.

CHAPTER II

GENERAL OVERVIEW OF AFTA AND INVESTMENT LAW

One of the international agreement in regional scale is AFTA, this chapter explains the general overview of free trade, AFTA, and purpose of it. Investment is divided into two types of investors namely domestic investment and foreign investment. Both types explain the general overview on investment law, history of investment law, basic understanding of domestic investment and foreign direct investment including (investors, capital for investors, sources of law), applicable principles, and dispute settlements in Indonesia.

A. General Overview of Free Trade

1. Definition and History of Free Trade

Free trade can be defined as the absence of artificial barriers (barriers imposed by the government) in trade between individuals and companies in different countries. International trade is often limited by various state taxes, additional costs that are applied to exported import goods, and also non-tariff regulations on imported goods. In theory, these barriers were originally rejected by free trade. But in reality, trade agreements supported by adherents of free trade actually create new obstacles to the creation of a free market. These agreements are often criticized for protecting the interests of large companies.[44]

The road to the era of free trade should be even smoother with the increasingly rapid flow of globalization driven by technological advances in transportation and telecommunications, including the information technology sector, and very rapid development in international trade law, for example, the formation of the World Trade Organization (WTO). [45] But the conditions of globalization have been tainted with the efforts of superpowers who want to maintain their dominance.

History proves that international trade plays a decisive role in the world economy. Its existence is like two sides of a coin. In the one side

[44] Mitsuo Matsushita, *The World Trade Organization Law, Practice and Policy*, Oxford University Press, New York, 2006, P.5

[45] Agus Brotosusilo, "*WTO, Regional and Bilateral Trade Liberalization and Its Implication for* Indonesia". This paper presented at ASEAN Law Association/ALA Conference, Bangkok, 2005, P.216

international trade plays a role in creating prosperity for the entire nation, but on the other side international trade and investment can also afflict the country so that it eventually becomes a colonial state.[46]

In the Free Trade era, mutual dependence cannot be avoided. WTO as an international trade organization is expected to bridge all the interests of the country in the world in the trade sector through mutually agreed provisions. The WTO is intended to produce reciprocal and mutually beneficial conditions so that all countries can benefit. Through the WTO a trade model is launched where trade activities between countries are expected to run smoothly.

WTO is a means to encourage a free and orderly trade in this world. In carrying out its duties, to encourage the creation of free trade, WTO applies several principles that become the pillars of the WTO.[47]

It plays vital and important role within the WTO body. There are at least five main principles in the WTO, those points shall be obey by the members, it's legally binding and every decision produced by the WTO is irreversible. In addition to the nature of the membership of the WTO in making irreversible decisions, there is an uniqueness as well as an affirmation to members when entering the circle of WTO this is a Single Under Taking

[46] *Ibid*, P.218
[47] Mitsuo Matsushita, *Op.Cit*, P.8

membership, it means that countries that are members of this organization must accept all provisions set by this organization. The five principles are: [48]

a. MFN (Most-Favored-Nation) is the equal treatment for all trading partners. Based on the MFN principle, member states cannot simply discriminate against their trading partners. The import tariff given to a country's products must also be given to imported products from other member countries' trading partners.

b. National Treatment is member States are required to provide equal treatment for imported and local goods - at least after imported goods enter the domestic market.

c. The National Treatment Obligation, the purpose of this principle is according to Article III General Agreement on Tariffs and Trade GATT, member countries are prohibited from imposing domestic tax rate discrimination or making other policies that possible in causing benefits derived from tariff reductions to be useless. In other words, imported products - after entering the domestic market - and similar domestic products must get the equal treatment. The same thing applies to the service sector and intellectual property rights.

d. Elimination of Quota, the purpose of which is to reduce the quota barriers on export-import, including the requirements for import and export permits and other policies that regulate the entry and exit of goods from

[48] Mitsuo Matsushita, *Op.Cit*, P.9

and outside the territory of a country. This principle aims to prevent the lack of transparency in the regulation of import duties and price distortion caused by the invalidation of the law of supply and demand.

In this fourth principle, there are several exceptions, namely:[49]

(1) If a country is running a market stabilization program related to agricultural products

(2) The Balance of Payments or the country is trying to prevent or overcome the decreasing foreign exchange reserves if the recorded reserves are considered too low;

(3) In the framework of Quota Allocation, the meaning of the import or export quota is determined based on the role of the exporting country in the trade with the importing country if the quota is not determined).

WTO is aware of the fact that the government has differences in the level of development and the availability of resources. Therefore, the WTO also includes special and differential treatment clauses. It means that developed countries will pay more, or get more cuts or have shorter implementation times in terms of tariff reduction. Meanwhile, developing countries will be considered to get lower cuts and longer implementation in reducing trade tariffs. Basically, those classified as poor countries are developing countries or Least Development Countries. Indonesia is one of the developing countries. The unfortunate thing for Indonesia as a developing

[49] Mitsuo Matsushita, *Op.Cit*, P.10

country, Indonesia does not use the principles in the WTO specifically with the reason that it is bound in an agreement. In addition, there was an overconfidence attitude from Indonesia which in reality had not been able to compete in a free market framework because Indonesia was thus turning off domestic industries, especially industries that were still categorized as small industries and home industries.[50]

2. Benefits of Free Trade

In terms of economic terms, the purpose of trade is to obtain profits or profits. So there are lots of benefits or benefits with free trade. Some of the benefits of free trade include: [51]

a. Increase employment opportunities. The reason is that with the existence of free trade, the market for goods and services from a country becomes wider. Marketing of production products no longer relies solely on domestic markets with limited absorption, but can also rely on international markets whose markets are very broad. Thus the

[50] Anderson, J.E. and E. van Wincoop, Trade costs, *Journal of Economic Literature* Vol.42 No.3, 2004, P.17

[51] Jolanta Drozdz, Algirdas Miškinis, "Benefits and threats of free trade", *Ekonomia Economics* Vol. 2, No.14, 2011, P.41

number of goods and services produced can be multiplied, resulting in increased demand for labor.

b. The creation of efficient resource allocation and specialization. In the end, with free trade, a country will only produce certain goods and services that are considered the most efficient if the goods and services are produced in their country compared to other countries. Thus, all countries will specialize in certain products only, as a result, there will be effective in the use of resources.

c. Encouraging accelerated progress in the field of science and technology. Trading is basically price and quality competition so that a country exists in its free trade, the goods and services offered must be superior in quality and cheap in price, this can only be achieved by continuing to develop science and technology.

d. Free trade can increase a country's income because if there is an excess of goods in the domestic market, it can be sold to countries that need it. The higher the selling power, the greater the income that a country receives so that it can prosper its people.

B. **General Overview of AFTA**

1. Definition and History of AFTA

Since its establishment in 1967, ASEAN has indeed aimed to increase economic growth, social progress and cultural development in the Southeast Asia

region. For this purpose, ASEAN member countries have attempted to help each other in efforts that are of concern and common interest from ASEAN member countries, particularly in the fields of economics and trade including social, cultural and scientific issues, among others by effectively utilize various sectors such as agriculture and industry and expand their trade, including international commodity trade.[52]

ASEAN member countries are also determined to eliminate poverty, hunger, disease, and illiteracy as a major concern for its member countries. To that end, ASEAN has sought intensive cooperation in the fields of economics and social development by prioritizing social improvement and improving the level of life of the people in the Southeast Asia region. In the ASEAN Summit in Bali in 1976, especially in the economic and trade sectors an action program was established as a framework for ASEAN cooperation, among others: [53]

a. Collaboration on basic commodities, especially food and energy
b. Cooperation in industry
c. Cooperation in the field of trade
d. A joint approach to dealing with international commodity problems and other world economic problems
e. The mechanism for economic cooperation.

[52] Sumaryo Suryokusumo, *Studi Kasus Hukum internasional,* Tatanusa, Jakarta, 2007, P. 9
[53] *Ibid,* P.10

The domestic and international economic environment has undergone rapid changes and has created challenges for ASEAN. Even though the global trading system is still open, the tendency for obstacles to emerge remains a challenge for ASEAN. Especially with the increasing number of economic groupings quickly spreading, such as the European Single Market and the North American Free Trade Area (NAFTA). This clearly influences the international trade system because such a grouping aims to enhance an open international economic regime, which will only encourage economic cooperation in the region concerned. [54]

AFTA is more developing than WTO, the amount of state members influencing efficiency and effectiveness in implementing the aims of the agreement. The difficulty faced in creating the multilateral trading system is the basis of Article XXIV provisions of the GATT provisions on the permissibility of establishing regional cooperation in the field of trade. Article XXIV GATT stipulates that the establishment of a regional trade agreement (RTA) does not constitute an obstacle to multilateral trade.[55]

This is what underlies ASEAN to take new steps to increase trade and industry cooperation by seeking new mechanisms towards achieving harmonization and economic integration that can ensure smooth trade and ASEAN investment. [56]

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[54] *Ibid*, P.11

[55] Craig R. MacPhee, "Consequence of Regional Trade Agreements to Developing Countries", *Journal of Economic Integration*, Vol.29, No.1, 2014, P.68

[56] *Ibid*, P.69

ASEAN leaders agreed to established an ASEAN free trade area or known as AFTA in 1991 whose formation lasted for 10 (ten) years. A ministerial-level institution is formed to oversee, coordinate, and review program implementation towards AFTA. The contents of the agreement are in the form of a framework for enhancing ASEAN Economic Cooperation (FAEAEC) signed by the president and prime minister of each ASEAN country in January 1992.

The birth of AFTA is an effort from ASEAN to protect the interests of member countries in multilateral trade which is dominated by developed countries. Based on this awareness, it is impressed that AFTA is an ASEAN effort to protect its regional market. This impression also arises over other regional trade agreements. [57]

AFTA is a manifestation of the agreement of ASEAN countries to form a free trade area in order to improve the economic competitiveness of the ASEAN regional region by making ASEAN a world production base. Another goal is to create a regional market for 500 million people. [58]

The main agreement is an umbrella for the entire framework of ASEAN economic cooperation. The road to AFTA is pursued through a mechanism called CEPT (Common Effective Preferential Tariff). Each country will reduce import duty rates or reduce non-tariff restrictions for fellow ASEAN countries, especially for products that regulated under the agreement that applies in ASEAN. The CEPT

[57] Sumaryo Suryokusumo, *Op.cit*, P.17

[58] Noviansyah Manap dikutip dari Martin Khor, *Memperdagangkan Kedaulatan: Free Trade Agreement dan Nasib Bangsa*, Insist Press, Yogyakarta, 2010, P.209

scheme is a scheme for one purpose, namely to realize AFTA through: tariff reduction to 0-5%, elimination of quantitative restrictions and other non-tariff barriers.[59]

The AFTA target is tariff reduction, even towards zero tariff rates before 2003. The simultaneous implementation of the AFTA agreement on six signatory countries will be effective in 2010 while for Vietnam in 2013, Laos and Myanmar 2015, and Cambodia in 2017. At the appointed time All products must enter the CEPT scheme.[60]

The requirements of the western world free trade system were burdensome to ASEAN countries and on the other hand, the western world felt ASEAN was a formidable competitor in the world, especially in the 1980s and 1990s. The World Bank then called it "economic tiger" or also known as "Asia Four Dragon". The World Bank states that Southeast Asia's economic progress can quickly become an advanced economy. The leaders of Asian countries explained that this impressive economic success was rooted in Asian values that were very different from Western values. [61]

The ASEAN or AFTA Free Trade Area is a regional collaboration in Southeast Asia to eliminate trade barriers between ASEAN member countries. The emergence of cooperation in the economic field is a global phenomenon that

[59] *Ibid*, P.210

[60] Administrator,"AFTA dan Implementasinya", *http:/ /www.depdag.go.id/files/publikasi/djkipi/afta.htm,* accessed on 22 August 2018.

[61] Ade Maman Suherman, *Organisasi Internasional dan Integrasi Ekonomi Regional dalam Perspektif Hukum dan Globalisas*i, Ghalia Indonesia, Jakarta, 2003, P.152

occurs in various economic blocks as a response to globalization and free trade or in other words as the anti-climax of globalization itself.

The establishment of regional cooperation blocks can be found in Europe, Asia, Africa, South America and North America. The European Union can be categorized as the most established multinational market groups and even become a model of other regional organizations. Blocks of regional cooperation in the economic field in other regions, such as NAFTA (North America Free Trade Area) between the United States, Canada and Mexico; (MERCOSUR) in South America; and (ECOWAS) in Africa apply internal rules that facilitate business interactions in the free trade framework. [62]

In Asia, through the ASEAN Summit in Singapore in January 1992 formally approved the formation of the ASEAN Free Trade Area by giving birth to Common Effective Preferential Tariff (CEPT). The formation of AFTA can be said to be the anticlimax of globalization, especially the economic crisis in 1997 which befell all ASEAN countries, even "Asian tigers" like Korea. As an preventive step, AFTA concerned about reducing tariff / non-tariff barriers among ten ASEAN countries to conduct economic recovery and increase bargaining positions in the eyes of the international community.

2. The purpose of AFTA

ASEAN Free Trade Area (AFTA) aims:[63]

[62] *Ibid*, P.154
[63] Mitsuo Matsushita, *Op.Cit*, P.67

a. Improving ASEAN's competitiveness as a production base in the world market through the elimination of duties and non-customs barriers in ASEAN.
b. Attracting foreign direct investment into ASEAN, the main mechanism for achieving the above objectives is the "Common Effective Preferential Tariff" scheme (CEPT).
c. ASEAN members have the option of holding product exceptions in CEPT in three cases:
    (1) A temporary exception, a member state may exclude a product that is deemed necessary as a protection for the state's safety, community moral protection, protection of the lives and health of humans, animals or plants, as well as the protection of artists' objects, archaeological or historic. The Allotment of Am Exclusion in the CEPT Agreement is consistent with Article X of the Am Agreement in Trade and Tariffs (GATT). The temporary exception is in the form of products whose final tariff will be reduced to 0-5%, but postponed temporarily to reduce the tariff. Sensitive agricultural exceptions including rice, only in 2010 will the reduction be applied from 0-5%. Whereas general exceptions refer to products deemed necessary to be protected by each ASEAN member country, including the general exception is protection against the labor movement

(2) Sensitive agricultural products, except for sensitive agriculture including rice, only in 2010 will the reduction be applied from 0-5%. Whereas general exceptions refer to products deemed necessary for protection by each ASEAN member country

(3) The general exception is protection against the labor movement

C. Indonesian Investment Law

1. Definition of Investment Law

Investment" means any form of investing activity by both domestic investors and foreign investors to do business in the territory of the state of the Republic of Indonesia.[64]

2. Domestic Investment

a. Definition of domestic investment

Domestic investment means an investing activity to do business in the territory of the state of the Republic of Indonesia that is carried out by a domestic investor by use of domestic capital.[65] The definitions outlined by law contain elements of the following elements:

(1) Investment activities

(2) In the territory of the Republic of Indonesia

(3) Conducted by domestic investment

[64] Article 1 point 1 Law No. 25 year 2007 about Investment Law
[65] Article 1 point 2 Law No. 25 year 2007 about Investment Law

(4) All the capital comes from within the country

b. Domestic investors

Domestic investor means an Indonesian national citizen, an Indonesian business entity, the state of the Republic of Indonesia, or a region that makes an investment in the territory of the state of the Republic of Indonesia.[66] An Indonesian national citizen is a person or resident of Indonesia who invests in the open business field for domestic investment.

Indonesian business entity is a business entity in the form of a legal entity, not a legal entity or sole proprietorship, in accordance with the provisions of the legislation. Business entities are not legal entities, including civil partnerships, firm associations, committee partnerships. Furthermore, legal entities include limited liability companies and state-owned enterprises. In addition, other legal entities that can become investors are pension funds, cooperatives and foundations.[67]

c. Domestic Capital

Domestic Capital means capital that is owned by the state of the Republic of Indonesia, an Indonesian national, or a business entity of a legal entity or nonlegal entity form.[68] Based on the explanation that can have domestic capital is:

(1) Indonesian State

[66] Article 1 point 5 Law No. 25 year 2007 about Investment Law
[67] Siti anisah, and Lucky Suryo Wicaksono, *Op.Cit.*, P.41
[68] Article 1 point 9 Law No. 25 year 2007 about Investment Law

(2) Individual Indonesian citizen

(3) A business entity is a legal entity or not a legal entity

(4) Other legal entities as long as the laws governing them permit investments

The notion of domestic capital is inconsistent with the notion of domestic investment, which one of its investors "... the region that undertakes investment ..." Nevertheless, in the development of regulation in the area of regional government, regions may also have capital in direct investment. Regions may engage in capital participation in state-owned enterprises and/or Regional Owned Enterprise. Regional equity participation can be increased, reduced, sold to other parties, and/or Regional Owned Enterprise.[69] Equity participation is carried out in accordance with the provisions of legislation, which is stipulated by regional regulations.[70]

d. Business Entity for Domestic Investment

Domestic investments may be made in the form of a business entity in the form of a legal entity, nonlegal entity or sole proprietorship in accordance with provisions of laws and regulations.[71] Thus, it should be understood that not every domestic investment activity in Indonesia can be done.

[69] Siti anisah, and Lucky Suryo Wicaksono, *Op.Cit*, P.42
[70] Article 333 point 1 Law No. 23 year 2014 about Local Government
[71] Article 5 point 1 Law No. 25 year 2007 about Investment Law

3. Foreign Investment

a. Definition of Foreign Investment

Foreign investment means an investing activity to do business in the territory of the state of the Republic of Indonesia that is carried out by a foreign investor both by use of all of the foreign capital and by engagement in a joint venture with a domestic investor.[72] This definition means that foreign investment as an investment activity in which there are foreign elements, can be determined by the existence of different citizenship, foreign capital and foreign and domestic cooperation.

Another notion of foreign investment is the transfer of capital in the form of tangible or intangible goods from one country to another, its purpose for use in that country in order to generate profits under the supervision of the owner of capital, in whole or in part.

Foreign investment involves the transfer of tangible or intangible assets from one country to another for the purpose of their use in that country to generate wealth under the total or partial control of the owner of the assets. There can be no doubt that the transfer of physical property such as equipment, or physical property that is bought or constructed such as plantations or manufacturing plants, constitute foreign direct investment. Such investment may be contrasted with portfolio investment. Portfolio investment is normally represented by a movement

[72] Article 1 point 3 Law No. 25 year 2007 about Investment Law

of money for the purpose of buying shares in a company formed or functioning in another country. It could also include other security instruments through which capital is raised for ventures. The distinguishing element is that, in portfolio investment, there is a separation between, on the one hand, management and control of the company and, on the other, the share of ownership in it. Investment treaties also define the nature of the foreign investment that is protected through their provisions. As a result, definitions differ according to the purpose for which they are used. It is emphasized that this work is not confined solely to the law created by treaties[73]

The difference of foreign investment with domestic investment is clearly related to the party making the investment and the origin of where the capital is. Capital is an asset in the form of money or another form that is not owned by investors who have economic value.[74] Thus capital is not always in the form of money but can also in other forms such as technology or know-how that has economic value.

Know-how can be interpreted as the information, practical knowledge, techniques, and skills required to achieve some practical end, especially in industry or technology know-how is considered intangible property in

[73] M. Sornarajah, *Op.Cit*, P.7

[74] Article 1 point 9 Law No. 25 year 2007 about Investment Law

which rights may be bought and sold.[75] Know-how is a type of intellectual property rights, belonging to trade secrets (in the form of confidential information), and when it becomes a product, the type of intellectual property rights attached to the product (it may be either copyright or patent). Emerging practices, foreign investments seek to optimize the use of technical and production know-how by managing the host country's natural resources.[76]

b. Foreign Investor

Foreign investor means a foreign national, a foreign business entity, and/or a foreign government that makes an investment in the territory of the state of the Republic of Indonesia.[77]

Another definition is Foreign investment involves capital flows from one country to another, granting extensive ownership stakes in domestic companies and assets. Foreign investment denotes that foreigners have an active role in management as a part of their investment. A modern trend leans toward globalization, where multinational firms have investments in a variety of countries.[78]

c. Foreign Capital

[75] Bryan A.Garner, *Black's Law Dictionary*, West Publishing Co, United States of America, 2009, P.978

[76] Siti anisah, and Lucky Suryo Wicaksono, *Op.Cit*., P.47

[77] Article 1 point 6 Law No.25 year 2007 about Investment Law

[78] *https://www.investopedia.com/terms/f/foreign-investment.asp* accessed on April 17th 2018

Foreign Capital means capital that is owned by a foreign state, a foreign national, a foreign business entity, a foreign legal entity, and/or an Indonesian legal entity, of which the capital is in part or in whole is owned by a foreign party.[79] Foreign investments must be in the form of a limited liability company under Indonesian law, and domiciled within the territory of the state of the Republic of Indonesia, unless provided otherwise by law.[80]

If further explanation of the explanation, the meaning of "foreign capital" also includes capital of an Indonesian legal entity that is partly or wholly owned by a foreign party or owned by a foreign investment company. A foreign investment company is a limited liability company whose capital or shares are owned by a foreign party, whether a foreign individual, a foreign business entity, and/or a foreign government that engages in investment in the territory of Republic Indonesia.

This is in line with the provisions of domestic investment and foreign investment in investing in the form of a limited liability company is conducted by:[81]

(1) Subscribe for shares at the time the limited liability company is established;

(2) Purchase shares; and

[79] Article 1 point 8 Law No. 25 year 2007 about Investment Law
[80] Article 5 point 2 Law No. 25 year 2007 about Investment Law
[81] Article 5 point 3 Law No. 25 year 2007 about Investment Law

(3) Take another method in accordance with the provisions of laws and regulations.

4. The Business Sector in The Investment Activity in Indonesia

In the effort to increase investment in Indonesia and to execute the ASEAN Economic Community (AEC), the Government of Indonesia had done amendments to the provision list of business fields closed and open with certain requirements in the field of investment (Investment Negative List /DNI). These amendments are stipulated in Presidential Decree (Perpres) Number 44 Year 2016 on List of Business Fields Closed and Business Fields Open with Conditions to Investment. Basically, all business fields or types of business are open to investment activities, except business fields or types of businesses which are declared closed and open with conditions. The business sector in the Investment activity consists of: [82]

a. Open Business Fields, Open Business Fields are Business Fields that are carried out without requirements in the framework of Investment.
b. Closed Business Fields, Closed Business Fields are certain Business Fields which are prohibited from being cultivated as Investment activities. Closed Business Fields for foreign investors are:
   (1) The production of weapons, gunpowder, explosive devices, and war equipment; and

[82] President Decree No. 44 year 2016

(2) Business fields that are explicitly declared closed under the law. President decree 44/2016 regulates Closed Business Fields listed in Attachment I to President decree 44/2016 including:

i. Marijuana Cultivation;

ii. Fishing of Fish Species Listed in Appendix I of the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES);

iii. Appointment of valuable objects from sinking shiploads;

iv. Utilization of Coral / Coral from Nature for: Building Materials / Lime / Calcium, Aquariums, and Souvenirs / Jewelry, as well as Life Coral or Recent Death Coral from Nature;

v. Manufacture of Chlor Alkali with the Mercury Process;

vi. Liquor Alcohol Industry;

vii. Beverage Industry Contains Alcohol: Wine;

viii. Beverage Industry Contains Malt;

ix. Implementation and Operation of Land Transport Passenger Terminals;

x. Implementation and Operation of Weighing Motor Vehicles;

xi. Telecommunications / Shipping Navigation Supporting Facilities and Vessel Traffic Information System (VTIS);

xii. Organizing Flight Navigation Services;

xiii. Implementation of Motor Vehicle Type Testing;

xiv. Gambling / Casino.

The Government pursuant to President decree 44/2016 stipulates closed business fields for investment, both foreign and domestic, based on the criteria of health, morality, culture, environment, defense and national security, as well as other national interests.

Thus, the difference between an Open Business Field and a Closed Business Field can be seen from certain business sectors that are declared prohibited or business fields that are allowed to be cultivated as Investment activities, whether carried out by foreign or domestic.

c. Business Fields Open with Requirements, Business Fields that are Open with

Requirements are certain Business Fields that can be attempted for Investment activities with conditions, namely reserved for Micro, Small and Medium Enterprises and Cooperatives, Partnerships, capital ownership, specific locations, special permits, and investors from the Association countries of Southeast Asian Nations (ASEAN).

Business Fields that are not listed in the Closed Business Field and Business Fields that are Open with Requirements are Open Business Fields. Business Fields Open with Requirements consist of:

(1) Business Fields Open with Requirements: those that are reserved or partnerships with Micro, Small and Medium Enterprises and Cooperatives; and

(2) Business Fields That Are Open With Certain Conditions, namely:

i. Restrictions on foreign capital ownership;
ii. Certain locations;
iii. Special licensing;
iv. Domestic capital 100% (one hundred percent); and / or
v. Limits on capital ownership in the framework of the cooperation of the Association of Southeast Asian Nations (ASEAN).

Business Fields that Are Open with Requirements: those reserved or Partnership with Micro, Small and Medium Enterprises and Cooperatives include:

i. Plantation seed business with an area of fewer than 25 hectares, such as sugar cane, coconut plants;
ii. Plantation businesses with an area of fewer than 25 hectares, such as oil palm plantations;
iii. Business with certain capacities, such as Travel Agencies, Homestay, Tobacco Processing and Drying industry;
iv. and so on.

The partnership is carried out by Investors with Micro, Small and Medium Enterprises and Cooperatives with a pattern: core plasma, subcontracting, agency, franchise, and other Partnership patterns. Business Fields Open with certain requirements including:

i. Agricultural Sector, namely Staple / Nursery Crops with an area of more than 25 hectares: rice, soybean-corn;

ii. Forestry Sector, Animal and Plant Breeding and Conservation Institutions;

iii. and so on.

5. Applicable principle

Seen in terms of terminology, the word principle has 3 different meanings, namely the base, the base, the guidelines; a central truth or a focus of thought; and ideals that are the basis.[83] The principle can also be interpreted as "the broad reason, which lies at the base of the rule of law". More specifically, there is the opinion that the principle of law is "the heart of the rule of law because it is the most widespread foundation for the birth of the rule of law or it is the ratio legis its rule of law.[84]

Sudikno mertokusumo defines the principle of law as "a common basic thought or a background of concrete rules contained in and behind every legal system incarnate in legislation and judgment which is a positive law and can be found by looking for the nature of the general in the concrete rules.[85]

Related to an explanation of the meaning of the principle of law above,

[83] *https://kbbi.web.id/asas* accessed on April 17th 2018

[84] Jonker Sihombing, *Op.Cit*., P.86

[85] Sudikno Mertokusumo, *Mengenal Hukum Suatu Pengantar*, Liberty, Yogyakarta, 1999, P.36

it can be concluded that generally the principle of law is in a state of mind or ideals idea of the background of the formation of a general and abstract legislation. Thus, the principle of legal principle is usually implicitly contained in a legislation.

The principles of the underlying principles of investment in Indonesia are:[86]

a. Legal certainty, is the principle that the rule of-law state lays down law and provisions of laws and regulations as the foundation of any investment policy and measure;
b. Transparency; is the principle of receptiveness to the public right to have access to true, honest, and nondiscriminatory information on investment activities;
c. Accountability, is the principle that provides every activity and the end result of the conduct of investments must be accountable to the public or people as the holder of the supreme sovereignty in accordance with provisions of laws and regulations;
d. Equitable and nondiscriminatory treatment against the country of origin, is the principle of a nondiscriminatory service treatment between domestic investors and foreign investors, or between investors of one foreign country and investors of another foreign country based on provisions of laws and regulations.

[86] Article 3 point 1 Law No. 25 year 2007 about Investment Law

e. Togetherness, is the principle that which all investors are encouraged to take on their business roles together in the realization of public welfare.

f. Efficiency in justice, is the principle that underlies the conduct of investments by taking primacy of efficiency in justice in order to realize just, conducive and competitive business climate.

g. Sustainability, is the principle that in a planned manner seeks a continuous development process through investments to ensure welfare and progress in all aspects of life, both in the present day and the future.

h. Environmentally friendly, is the principle in which an investment is made by having due regard to and accentuating the environmental protection and conservation.

i. Independence, is the principle in which an investment is made by taking primacy to the potentials of nation and state by not being unreceptive to the inflows of foreign capital in order to realize the economic growth.

j. Balanced advancement and national economic unity is the principle that seeks maintenance of a balance of economic advancement among regions within the national economic unity.

6. Dispute Settlement

   a. Background of Investment Dispute

In a cross-state legal relationship, where the subject of law is not only within the national sphere but has already crossed the borders of the state, it cannot be separated from the possibility of a dispute. Such disputes may arise from borders, investments and trade.

In the past, the state faced or resolved the dispute by means of force, threat or coercive. In its development, the state began to civilize and abandoned the way of violence, and had a peaceful way. In the context of the settlement of investment disputes, the peaceful means are among others through:

(1) Selecting the method of consent, which is done before the dispute arises by creating a dispute resolution clause in the contract.

(2) Choose an agreement made after a dispute arises. This agreement is usually taken if the parties before or the country do not make a deal or have an agreement but the parties choose other forums outside the forum that has been agreed

(3) Form a dispute resolution through a third party. A third party may be either an ad-hoc Arbitration (international) or through an existing arbitration body or through the establishment of a claims commission.[87]

[87] Huala Adolf and An An Chandrawulan, *Mekanisme Penyelesaian Sengketa Penanaman Modal*, Keni Media, Jakarta, 2015, P.2

The general public assumes that the efficient measure of a dispute resolution system lies in the ability to avoid uncertainty about the authority of the choice of forum to deal with dispute resolution. This is important because the main requirement that arises especially for the dispute resolution body is whether it has the authority or jurisdiction to handle the dispute submitted to it.[88]

b. Types of disputes and investment mechanisms

Each foreign investment creates a bilateral relationship involving the host country and investor. Based on the theory of state sovereignty, the host country has the power to regulate the activities of foreign investors in the territory of the host country. In the context of regulation and protection of investment activity, investment disputes that may arise include:

(1) Disputes between investors and the recipient country (investor to state dispute)

In the context of investment, the potential for disputes between the recipient countries and investors is quite large considering the differences in interests between investors and the host country. Investors both foreign and domestic investors invest capital with the motive for profit as much as possible (profit oriented). Meanwhile, the

[88] UNCTAD, "*Selecting the Appropriate Forum", Dispute Settlement ICSID*, United Nations: New York and Geneva, 2003 P.5

recipient country has a goal not only to gain profit but to develop a developing country motive that focuses on aspects of sustainable development.

On the other hand, the paradigm difference between foreign investors and the recipient countries is also often the trigger for the dispute. The usual foreign investor from developed countries emphasizes the importance of transparency and investment or investment policies related to trade or obstacles to foreign investment obstacles. Meanwhile, the recipient country which in fact is a developing country holds the principle of sovereignty (sovereignty principle). The recipient countries tend to be protective in protecting investors in the domestic industry or industry in order to survive the presence of foreign investors.

In the dispute of investments between private (foreign investors usually large companies) against the government (the recipient country) becomes complicated when the state is sued as a perfect legal subject.

The legal relationship between the host country and the investor is generally based on an agreement or contract in the field of investment. Therefore, investment disputes are generally born because

the state for example violates the contract or investment agreement.[89] The status of the host country in a superior investment from the investor because it has the sovereignty and authority to make the rule of law, including the authority to change or cancel a regulation. With a superior position, the potential for the birth of a larger dispute.

Investor's lawsuit against the recipient country is referred to an investor to state dispute settlement (ISDS). Based on the results of the OECD's research, the subject of dispute is the dispute that the investor submits in relation to the administrative actions taken by the government or branches of governmental power that affects foreign investment, such as revocation of permits, land zoning or contract breaches.[90]

(2) Disputes among investors

Disputes that occur between investors may occur:

i. Domestic investors and domestic investors (fellow domestic or local investors)
ii. Domestic investors and foreign investors (local and foreign investors); or
iii. Foreign investors and foreign investors in the host country (host country)

[89] Huala Adolf, Mekanisme Penyelesaian, *Op.Cit*, P.4

[90] European Commission (EC), *Investor to State Dispute Settlement (ISDS): Some Facts and Figures*, 2015, quoted in Huala Adolf, Mekanisme Penyelesaian, *Op.Cit*, P.7

c. Foreign Investment Arbitration

Foreign investment arbitration has a very crucial role in the settlement of foreign investment disputes with the host country. Even the law no. 25 of 2007 provides absolute jurisdiction to the settlement of foreign investment disputes through an international arbitration. The main reason foreign investors choose international arbitration as it is required in law, there is also the presumption that international arbitration has more neutrality than national courts. It can avoid the uncertainties associated with the litigation process in national courts. The international arbitration procedure is not bound by any particular jurisdiction of either party unless the parties to determine. The ability to resolve disputes in a neutral forum and carry out a final and binding execution of decisions is often cited as a major advantage of international arbitration in relation to the dispute resolution in national courts.[91]

There are several well-known arbitration forums that can be used such as the Singaporean International Arbitration Center (SIAC), United Nations Commission on International Law (UNCITRAL), International Chamber of Commerce (ICC) and International Center for Settlement Investment Dispute (ICSID). However, international arbitration commonly used to resolve disputes of foreign investment is ICSID.

[91] Ana Rokhmatussa'dyah dan Suratman, *Hukum Investasi & Pasar Modal*, Sinar Grafika, Jakarta, 2017, P.34

d. International Centre for the Settlement Investment Dispute (ICSID)

In order to resolve the increasing disputes between the host country and foreign investors, the World Bank has provided an international center for settlement of investment dispute (ICSID). ICSID is an independent institution that was born through convention on the settlement of investment disputes between states and nationals of other states. The convention itself was designed by the executive director of the international bank for reconstruction and development (World Bank) on 18 March 1965.

Indonesia has ratified ICSID through Law no. 5 of 1958 on the settlement of disputes between countries and foreign nationals regarding investment. However, it does not mean that all foreign investment disputes in Indonesia can be immediately resolved through ICSID, article 25 of the ICSID convention regulates the jurisdiction of ICSID. According to this article there are at least 3 main requirements that must be fulfilled by the parties as follows:[92]

(1) There must be agreement

The parties have previously reached an agreement to submit their dispute to the ICSID arbitration. The Convention requires a written agreement that designates the use of ICSID. The appointment of this

[92] Ridwan Khairandy, *Pengantar Hukum Perdata Internasional*, FH UII Press, Yogyakarta, 2007, P.209

arbitration body is contained in an investment agreement clause stipulating the submission of any dispute which may arise from the agreement. An agreement to submit a dispute to ICSID arbitration should not be stated in a separate document. Host country through its legislation may offer a dispute arising between the investor and the recipient country to be submitted to ICSID arbitration.[93]

(2) Jurisdiction of Rationae Matriae

The jurisdiction of ICSID arbitration is limited only to legal disputes due to investment. This dispute is between the citizens of a participating country of the ICSID convention. In this case there must be an international relationship concerning the difference of citizenship between the suing citizen and the state that sues.

(3) Jurisdiction of Rationae Personae

The ICSID arbitration panel only has the authority to adjudicate disputes between the state and other foreign nationals whose country is also a member or member of the ICSID convention.[94]

C. Investment in Islamic Perspective

The religion of Islam tought its people to try to get a better life in the world and in the hereafter. To have a good life in this world and hereafter that can guarantee

[93] Article 25 point 1 of Convention ICSID
[94] Huala Adolf, Mekanisme Penyelesaian, *Op.Cit*, P71

the achievement of the welfare of the birth and the mind (*falah*). One way to achieve that welfare is to conduct investment activities. In Arabic the investment is called *Istithmar* which means "to get a result, grow and increase in number." In Webster's New Collegiate Dictionary, the word invest is defined as to make use of for futures benefits or advantages and commit (money) in order to earn a financial return.[95]

Investment is defined as the investment of money or capital in a company or project for the purpose of obtaining profit, although sometimes the loss or loss because investment is an uncertain type of activity. From the exposure can be concluded that investment is the activity of investing in the hope of getting a profit in the future. Real investment is a very risky activity because dealing with two possibilities namely profit and loss means there is an element of uncertainty. Thus the return of an enterprise is uncertain and not fixed. One day may experience a lot of profits, may be mediocre (tolerable), only returning capital may also go bankrupt and be deceived.

Therefore, Islam provides signs or restrictions on the investment that is allowed and not allowed to be done by business people such as investors, traders, supplier and anyone associated with this world. Not only that, some things such as knowledge about the investment of the related sciences need to be deepened so that

[95]Masudul Alam Choudhury, "Insurance and Investment in Islamic Perspective", *International Journal of Social Economics*, Vol. 10, No. 5, 1983, P.26,

investment activities that we do worth worship, get inner satisfaction and blessings in the world and the hereafter.[96]

Here are some verses about the appeal to invest:

1. QS. Al-Hasyr 18:

يَٰٓأَيُّهَا ٱلَّذِينَ ءَامَنُواْ ٱتَّقُواْ ٱللَّهَ وَلۡتَنظُرۡ نَفۡسٞ مَّا قَدَّمَتۡ لِغَدٖۖ
وَٱتَّقُواْ ٱللَّهَۚ إِنَّ ٱللَّهَ خَبِيرُۢ بِمَا تَعۡمَلُونَ ١٨

O you who have believed, fear Allah . And let every soul look to what it has put forth for tomorrow - and fear Allah . Indeed, Allah is Acquainted with what you do.

From the verse above it can be understood that the verse contains moral advice to invest as a stock of life in the world and in the hereafter because in Islam all kinds of activities if intended as worship will be worth the hereafter also like this investment activity.[97]

2. QS. Lukman 34:

إِنَّ ٱللَّهَ عِندَهُۥ عِلۡمُ ٱلسَّاعَةِ وَيُنَزِّلُ ٱلۡغَيۡثَ وَيَعۡلَمُ مَا فِي ٱلۡأَرۡحَامِۖ
وَمَا تَدۡرِي نَفۡسٞ مَّاذَا تَكۡسِبُ غَدٗاۖ وَمَا تَدۡرِي نَفۡسُۢ بِأَيِّ أَرۡضٖ
تَمُوتُۚ إِنَّ ٱللَّهَ عَلِيمٌ خَبِيرُۢ ٣٤

[96] Nurul Huda and Mustafa Edwin N, *Investasi pada Pasar Modal Syariah*, Kencana, Jakarta, 2014, P.17

[97] *Ibid*, P.17-18

Indeed, Allah [alone] has knowledge of the Hour and sends down the rain and knows what is in the wombs. And no soul perceives what it will earn tomorrow, and no soul perceives in what land it will die. Indeed, Allah is Knowing and Acquainted.

The above verse, Allah explicitly declares that no one in this world can know what will be done or cultivated and what events will happen tomorrow. Because of the ignorance of the human being ordered to try, one of them by investing as a provision for tomorrow's uncertain day, the result is God's prerogative right but it is important to follow the standard of religion in any activity including investment.[98]

The Qur'an defines the above verse "And no man can know by what will be done tomorrow" that is that Allah knows what each individual acquires and knows what the individual does on the next day, whereas the individual does not know it ". It means that investing in the hereafter, where the endeavor is not known to all beings.

So even if one never knows what will happen tomorrow with certainty, they still have to prepare themselves for tomorrow or their future by always trying to invest, for example. While the results will be like what is determined only by God who knows the success or failure of an investment.

3. QS. Al-Baqarah : 261

[98] *Ibid*, P.18

مَّثَلُ ٱلَّذِينَ يُنفِقُونَ أَمۡوَٰلَهُمۡ فِي سَبِيلِ ٱللَّهِ كَمَثَلِ حَبَّةٍ أَنۢبَتَتۡ
سَبۡعَ سَنَابِلَ فِي كُلِّ سُنۢبُلَةٖ مِّاْئَةُ حَبَّةٖۗ وَٱللَّهُ يُضَٰعِفُ لِمَن يَشَآءُۗ وَٱللَّهُ
وَٰسِعٌ عَلِيمٌ ٢٦١

The example of those who spend their wealth in the way of Allah is like a seed [of grain] which grows seven spikes; in each spike is a hundred grains. And Allah multiplies [His reward] for whom He wills. And Allah is all-Encompassing and Knowing.

The verse is also an information about the importance of investment although it is not concretely speaking of investment, because that is stated about how fortunate people who put their wealth in the path of Allah. This verse when read from an economic perspective will obviously affect our lives in the world. Just imagine if many people who do *infaq* then actually he helped hundreds, thousands, millions and even billions of poor people in the world will get a better life.[99]

4) QS. An-Nisa' 9:

وَلۡيَخۡشَ ٱلَّذِينَ لَوۡ تَرَكُواْ مِنۡ خَلۡفِهِمۡ ذُرِّيَّةٗ ضِعَٰفًا خَافُواْ عَلَيۡهِمۡ
فَلۡيَتَّقُواْ ٱللَّهَ وَلۡيَقُولُواْ قَوۡلٗا سَدِيدًا ٩

[99] *Ibid*, P.19

And let those [executors and guardians] fear [injustice] as if they [themselves] had left weak offspring behind and feared for them. So let them fear Allah and speak words of appropriate justice.

In this verse Allah commands humans not to leave a weak offspring after our death, either weak primary or weak morale. Actually, this verse explicitly recommends improving the economic life of the people by preparing means towards the prosperous, which one of them by doing investment activities in various forms. Through banking institutions as well as in its own way, it is more profitable and more beneficial.[100]

Investment is a form of economic activity. For every treasure is *zakat*. If the treasure is silenced (not in *zakat*) then gradually will be consumed by his *zakat*, one of the wisdom of *zakat* is to encourage every Muslim to invest his property. The treasure invested will not be consumed by *zakat* unless its profit alone. In order to avoid un-Islamic investment, every Muslim must know the business ethics in investing, because ignorance and lack of knowledge about investment in Islam sometimes make people only in investing their wealth and sometimes fall on the act of violating the *Shari'a*. Partly because of the lure of big returns.[101]

[100] *Ibid*, P.19-20

[101] N. Gafoordeen, Mohammed Mohideen, Abusulaim M.A, "Zakat Investment in Shariah", *Medwell Journals*, Vol.2 No.4. 2016, P.298

CHAPTER III

LEGAL IMPLICATION OF AFTA TOWARD LEGAL PROTECTION OF INVESTOR IN INDONESIA AND MALAYSIA INVESTMENT LAW

A. Legal Implication of AFTA

1. The principle of Most Favored Nation in AFTA Implementation

Indonesia and Malaysia had joined the WTO on 11 January 1995, with participation in the WTO, which obliged all members to ratify their treaties. one of the principles that are very related is the most favored nation.

Most Favored Nation is a principle that regulates the course of trade by using the principle of non-discrimination, namely not to discriminate between one GATT member country or WTO and other members. The members may not discriminate between members who are members of one another or may not provide convenience only to one member without the same treatment with other members whether it is related to tariffs or trade. Article I from GATT:[102]

"With respect to customs duties and charges of any kind imposed on or in connection with importation or exportation ... any advantage, favor, ... by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties"

Article II of GATT:[103]

"Each contracting party shall be accorded to the commerce of the other contracting party treatment no less than that provided for the appropriate Part of the appropriate Schedule annexed to this agreement"

[102] Article 1 point 1 of General Agreement on Tariff and Trade

[103] Article 2 point 1 of General Agreement on Tariff and Trade

Seeing the article I as meant by "customs duties and charges" refers to everything given at the border (such as import duties/tariffs), as well as providing balanced competitive opportunities on the border for the idea of free trade. It should also be noted that "advantage" must be adjusted directly and unconditionally for all other participating countries. Whereas article II relates to tariff attachments, where each member country must adjust the trade treatment that does not harm the other participating countries according to their schedule.

Both of these articles from the MFN principle which requires member countries to adjust all forms of action on the border directly and unconditionally including the tariff, so that it applies to all other participating countries without exception. It appears that the MFN principle is based on non-discrimination where member countries can compete competitively and fairly.

The birth of the WTO signifies the efforts of countries to institutionalize the provisions on international trade agreed upon in GATT. These efforts prove the desire of the international world to make unification and harmonization of international trade law with the principle that adheres to trade liberalization and free competition.

Efforts to unify and harmonize international trade law carried out by the WTO turned out to have difficulties in reaching a multilateral agreement. The difficulties faced in creating a multilateral trading system have in fact

taken the middle ground in the provisions of Article 24 of the GATT provisions concerning the permissibility of establishing regional cooperation in the field of trade. The provisions of Article 24 of the GATT stipulate that the establishment of a regional trade agreement (RTA) does not become an obstacle to multilateral trade.

Current developments, many countries make regional trade agreements. This regional trade agreement (RTA) is growing because it is easier and more applicable because it does not involve too many countries and their interests as happened in the WTO.

Before the birth of the regional trade agreement, the international community had agreed on a multilateral trade agreement, namely GATT. In the GATT provisions, it has been regulated about the permissibility of the establishment of regional trade agreements provided that it does not interfere with the process of trade liberalization and free competition.

Typologies in the current regional trade agreement can be divided into three, namely:[104]

a. Free Trade Area (FTA)
b. Custom Union Uniformity
c. Scope Limitation (Partial Scope Agreement)

[104] Huala Adolf, *Hukum Ekonomi Internasional, Suatu Pengantar*, Rajagrafindo Persada, Jakarta, 2005. P.32

This typology is actually in accordance with the rules contained in Article XXIV of the GATT provisions. Basically, a regional trade agreement is based on giving preference to its member countries. The aim is to eliminate trade barriers. However, if this action is carried out indefinitely, the concern of some parties that regional trade agreements will damage the multilateral trading system will be realized.

This concern was actually resolved by a decision by the GATT Council on Differential and Favorable Treatment (Enabling Clause) in 1979. In paragraph 2 (c) the decision was determined if the developing country carried out a preference action then it was obliged to implement the GATT provisions on the Most Favored Nation Treatment (MFN).[105]

The freedom granted by the GATT / WTO in establishing regional trade agreements is an acknowledgment that the potential for success in the regional framework is more effective than multilateral.[106] Because if the regulation on the establishment of regional trade agreements is done strictly, then failure to create a market and free competition will actually occur. Regional trade agreements can be considered as a tiered training arena for countries that are not yet economically established to then liberate their domestic markets multilaterally.

[105] Wagner Vinicius de Oliveira, Understanding The Most Favored Nation Clause in The International Investment Law, RDIET, Brasília, Vol. 12, No.2, P. 285

[106] *Ibid*, P.286

Although the guarantee of freedom in making regional trade agreements has been guaranteed by GATT / WTO, it seems that there is still a uniformity of typical material included in regional trade agreements. The terms of the regional trade agreement are:[107]

a. Rules of Origin

b. Bilateral Preferential Relationship

These two conditions are usually found in each regional trade agreement. This uniformity may prove that these two conditions are a point of compromise that is easily achieved by the countries. GATT's journey to the WTO proved the principles contained in the agreement were very difficult when implemented. These principles are difficult to reach agreements between countries because they are too broad. Whereas each country has different economic systems and interests.

Regional Trade Arrangements where one group of countries agrees to eliminate or reduce obstacles to imports from their fellow members and has taken place in several regional countries of the world, such as the European Union with its single market, ASEAN with its AFTA and others. In Article XXIV, the GATT explains that recognizing the close integration in the economic field through freer trade, namely recognizing regional groupings as an exception and general rules of the MFN general principle clause on the condition that certain criteria are strictly met. The GATT provisions are

[107] Huala Adolf , *Op.Cit*, P.37

intended so that regional arrangements facilitate trade between the countries concerned, without creating obstacles to trade with the outside world. Exceptions and the MFN clause rules are those which are stipulated in the GATT article itself and some are stipulated in the decisions of the GATT conference through a waiver.

2. Business Licensing Services

The government has formalized the implementation of the Online Single Submission (OSS) System. Electronic Integrated Business Licensing Services, which is more easily called the generic name OSS is present in the context of business licensing services that are valid in all Ministries, Institutions, and Regional Governments throughout Indonesia, which have been carried out through One-Stop Integrated Licensing (PTSP).[108] Besides through PTSP, the public can access the OSS System online anywhere and anytime.

The OSS system was built in order to accelerate and increase investment and business, by applying licensing to try to be integrated electronically. In the latest regulation regarding OSS, namely PP No. 24 of 2018, the Government regulates, among others, the types, applicants and issuance of business licenses; implementation of business licensing; business licensing reform per sector, OSS system, OSS institution, OSS funding; incentives or disincentives for

[108] *https://www.hukumonline.com/berita/baca/lt5b433407c8d81/sistem-oss-diluncurkan--izin-berusaha-kini-lebih-mudah* accessed on August 22nd 2018

implementing licensing through OSS; solving business problems and obstacles; and sanctions. This is the implementation of the Presidential Regulation (Perpres) No. 91 of 2017 concerning the Acceleration of Business Execution and has conducted concept trials in three locations, namely: Purwakarta, Batam and Palu. The design of this Information Technology-based system is basically by interconnecting and integrating licensing service systems in the BKPM / PTSP Center (SPIPISE). This includes systems from various Ministries and licensing issuing institutions, including the Indonesian National Single Window (INSW) system, the General Law Administration System of the Ministry of Law and Human Rights, and the Ministry of Home Affairs Population Administration Information System.

Currently, OSS operations are held in the Coordinating Ministry for Economic Affairs supported by INSW and other relevant ministries.[109] But this is only a transition period while preparing for its permanent implementation at BKPM. This is a positive and comprehensive movement for synchronizing licensing regulations at the Central and Regional levels. For investments or business activities that are already running, then they can adjust their business licensing through the OSS System, either to obtain a Business Registration

[109] *https://www.oss.go.id/oss/* accessed on August 23rd, 2018

Number (NIB) or to extend or change business licenses and or commercial permits.[110]

Before using OSS, business people must register. Some facilities provided by the government through OSS. For example, OSS registration is enough to use the Population Registration Number (NIK) for individuals, and the number of ratification of the establishment deed or number of the establishment of a limited company for non-individual business actors. Even if the person does not have an NPWP, the NPWP can be arranged in the OSS. In addition, NIK is also a requirement for the registration of participants in health social security and employment insurance.[111] The mechanism for OSS registration is regulated in Article 21-30 Government Regulation No. 24 of 2018.

The Companies Commission of Malaysia (CCM) or *Suruhanjaya Syarikat Malaysia (SSM)* is a statutory body which regulates companies and businesses. SSM, which came into operation on 16 April 2002, is a statutory body formed as a result of a merger between the Registrar of Companies (ROC) and the Registrar of Businesses (ROB) in Malaysia. The main activity of SSM Malaysia is to serve as an agency to incorporate companies and register

[110] *https://www.oss.go.id/oss/portal/download/f/PedomanIndonesia.pdf* accessed on August 23rd 2018

[111] Article 21-30 Government Regulation No. 24 year 2018 About Licensing Services Business Electronically Integrated

businesses as well as to provide company and business information to the public.[112]

As the leading authority for the improvement of corporate governance, SSM fulfills its function to ensure compliance with business registration and corporate legislation through comprehensive enforcement and monitoring activities to sustain positive developments in the corporate and business sectors of the Nation. SSM online (ssm e-info) is offering the public to purchase the financial information and profiles of all companies that registered with SSM Malaysia. Malaysia has implemented online business licensing in 2014, that is why many investors come to Malaysia due to the ease of access provided by the government.

A foreigner can start a business in Malaysia and it can be 100% owned by a foreigner, with minimum RM500,000 paid up capital depends in nature of the business. For retail, wholesale and distributive business natures, the 100% foreign ownership Sdn Bhd company will be subjected to Ministry of Consumerism and Trade and only "unique" (businesses that local Malaysians do not have the knowledge or skills) business will be granted, this is to protect Malaysians opportunities and competitions.[113] For some business nature, the paid capital would higher to meet the necessary requirement of the relevant authorities to issue the trade license or work permit for a foreigner. The

[112] *http://www.ssm.com.my/Pages/About_SSM/Overview.aspx* accessed on August 25th 2018

[113] *http://www.ssm.com.my/Pages/Product/Business-Information.aspx* accessed on August 25th 2018

Business Registration Certificate can be obtained within 1 hour after payment. The whole process will consume 1 – 2 hours and for CCM it will only take **7** days to register a company. Name search in one day and submission of documents in another day.

The steps when foreigner registered in Malaysia are:[114]

a. Individuals would need to complete Business Registration Form A with details of the business name, commencement date of the business, principal place of the business, the address of the business branch if any, information of the owners and partners, the type of business carried out and provide a copy of the Partnership Agreement if any.
b. If there is more than one business owner involved, every owner and partner is required to sign the completed form.
c. The application form must be submitted over the counter or through the online SSM e-Lodgement services in the SSM's website.
d. Documents that must be submitted along with the forms include a photocopy of the individual's identity card, permits, license or supporting letters for the type of business, approval of the supporting letter from the relevant agency if required by the Registrar of Business.

[114] *http://www.ssm.com.my/Pages/Services/Registration-of-Business-(ROB)/Registration-of-Business-(ROB).aspx* accessed on August 25th 2018

3. Legal Implication of AFTA in Indonesia and Malaysia Investment Law

Legal Implication of AFTA is the existence of reduction tariff in investment among ASEAN member. Indonesia and Malaysia applied it and make a restriction area for those side to implemented AFTA

a. Legal Implication for Indonesia

Restrictions on FDI are, for the most part, outlined in presidential decree No. 44 of 2016, commonly referred to as the Negative Investment List or the "DNI". The Negative Investment List aims to consolidate FDI restrictions from numerous decrees and regulations, in order to create greater certainty for foreign and domestic investors. The 2016 revision to the list eased restrictions in a number of previously closed or restricted fields. Previously closed sectors, including the film industry (including filming, editing, captioning, production, showing, and distribution of films), online marketplaces with a value in excess of IDR 100 billion (USD $7.4 million), restaurants, cold chain storage, informal education, hospital management services, and manufacturing of raw materials for medicine, are now open for 100 percent foreign ownership.[115]

The list also raises the foreign investment cap in the following sectors, though not fully to 100 percent: online marketplaces under IDR

[115] Attachment of Presidential Decree No.44 year 2016 About Negative Investment List

100 billion (USD $7.4 million), tourism sectors, distribution and warehouse facilities, logistics, and manufacturing and distribution of medical devices. In certain sectors, restrictions are looser for foreign investors from other ASEAN countries. Though the energy sector saw a little change in the 2016 revision, foreign investment in construction of geothermal power plants up to 10 MW is permitted with an ownership cap of 67 percent while the operation and maintenance of such plants are capped at 49% foreign ownership. For investment in certain sectors, such as mining and higher education, the 2016 Negative Investment List is useful only as a starting point, as additional licenses and permits are required by individual ministries.

A number of sectors remain closed to foreign investment or are otherwise restricted. Notably, the 2016 revision added construction services up to IDR 50 billion (USD $3.4 million) and construction consulting services with a value up to IDR 10 billion (USD $) to the list of enterprises reserved for micro, small and medium enterprises (MSMEs). The salvage of undersea artifacts from shipwrecks was added to the list of fields closed to both domestic and foreign investment. In November 2016, Bank Indonesia (BI) introduced a regulation imposing a foreign ownership limit of 20 percent for companies that offer electronic payment services. Foreigners may purchase equity in state-owned firms through initial public offerings. Capital investments in publicly listed companies through

the stock exchange are not subject to Indonesia's Negative Investment List unless an investor is buying a controlling interest.

b. Legal Implication for Malaysia

In 2009, Malaysia removed its former Foreign Investment Committee (FIC) investment guidelines, enabling transactions for acquisitions of interests, mergers, and takeovers of local companies by domestic or foreign parties without FIC approval.[116] Although the FIC itself still exists, its primary role is to review of investments related to distributive trade (e.g., retail distributors) as a means of ensuring 30 percent of the equity in this economic segment is held by the Bumiputera (ethnic Malays and other indigenous ethnicities in Malaysia).[117]

A separate set of regulations is imposed to reserve equity in businesses for ethnic Malays or *Bumiputera*. The rationale is to increase business participation of the *Bumiputera*. While ethnic Malays are the majority racial group in Malaysia, they are underrepresented in the country's business community, which is largely made up of ethnic Chinese and Indians.

In these cases, the restrictions on foreign equity are not in favor of nationals of Malaysia, but ethnic Malay. In other words, a foreign-invested company where the non-foreign equity is held individuals who

[116] Foreign Investment Committee, Guideline on The Acquisition by Local and Foreign Interest, Acquisition for Notification part III

[117] *https://www.state.gov/e/eb/rls/othr/ics/2015/241648.htm* accessed on August 27th 2018

aren't ethnically Malay would still fall foul of the law. The issue continues to be politically sensitive. Areas which are subject *Bumiputera* reservations include banking and finance, water, *batik* production, agriculture, defense, energy and telecommunications.

In the manufacturing sector, 100 percent foreign equity is generally allowed. Most restrictions exist in the services sector. Many sectors have however been liberalized in recent years. Despite being liberalized, investment in the different service sectors remains subject to the approval of the relevant Ministries, which have broad discretionary powers to impose conditions on a project, including foreign equity limits. A limit on foreign equity of 70 percent remains for investment banks, insurance companies, and takaful (Islamic insurance) operators.[118]

Since 2009, the government has gradually liberalized foreign participation in the services sector to attract more foreign investment. Following removal of certain restrictions on foreign participation in industries ranging from computer-related consultancies, tourism, and freight transportation, the government in 2011 began to allow 100 percent foreign ownership across the following sectors: healthcare, retail, education as well as professional, environmental, and courier services. Some limits on foreign equity ownership remain in place across in telecommunications, financial services, and transportation.

[118] *http://www.mida.gov.my/home/manufacturing-sector/posts/* accessed on August 27th 2018

Foreign investments in services, whether in sectors with no foreign equity limits or controlled sub-sectors, remain subject to review and approval by ministries and agencies with jurisdiction over the relevant sectors. A key function of this review and approval process is to determine whether proposed investments meet the government's qualifications for the various incentives in place to promote economic development goals. Nevertheless, the Ministerial Functions Act grants relevant ministries broad discretionary powers over the approval of specific investment projects. Investors in industries targeted by the Malaysian government often can negotiate favorable terms with ministries, or other bodies, regulating the specific industry. This can include assistance in navigating a complex web of regulations and policies, some of which can be waived on a case-by-case basis. Foreign investors in non-targeted industries tend to receive less government assistance in obtaining the necessary approvals from the various regulatory bodies and therefore can face greater bureaucratic obstacles.

The legal framework for foreign investment in Malaysia grants foreigners the right to establish businesses and hold equity stakes across all parts of the economy.[119] They called it as positive investment list. However, despite the progress of reforms to open more of the economy to

[119] Arumugam Rajenthran, *Op.Cit*, P. 22

a greater share of foreign investment, limits on foreign ownership remain in place across many sectors.

(1) Telecommunications

Malaysia began allowing 100 percent foreign equity participation in Applications Service Providers (ASP) in April 2012. However, for Network Facilities Providers (NFP) and Network Service Provider (NSP) licenses, a limit of 70 percent foreign participation remains in effect. In certain instances, Malaysia has allowed a greater share of foreign ownership, but the manner in which such exceptions are administered is non-transparent.[120] Restrictions are still in force on foreign ownership allowed in Telekom Malaysia. The limitation on the aggregate foreign share is 30 percent or 5 percent for individual investors.[121]

(2) Oil and Gas

Under the terms of the Petroleum Development Act of 1974,[122] the upstream oil and gas industry is controlled by Petroleum Nasional

[120] *http://unctad.org/en/Pages/DIAE/Investment%20Policy%20Reviews/Investment-Policy-Reviews.aspx* accessed on August 29th 2018

[122] Article 20 Petroleum Development Act year 1974

Berhad (PETRONAS), a wholly state-owned company and the sole entity with legal title to Malaysian crude oil and gas deposits. Foreign participation tends to take the form of production sharing contracts (PSCs). PETRONAS regularly requires its PSC partners to work with Malaysian firms for many tenders. Non-Malaysian firms are permitted to participate in oil services in partnership with local firms and are restricted to a 49 percent equity stake if the foreign party is the principal shareholder.[123] PETRONAS sets the terms of upstream projects with foreign participation on a case-by-case basis.

(3) *Financial Services*

Malaysia's 10-year Financial Sector Blueprint envisages further opening to foreign institutions and investors but does not contain specific market-opening commitments or timelines. For example, the services liberalization program that started in 2009 raised the limit of foreign ownership in insurance companies to 70 percent.[124] However, Malaysia's Central Bank (Bank Negara Malaysia (BNM)), would allow a greater foreign ownership stake if the investment is determined to facilitate the consolidation of the industry. The latest Blueprint, 2011-2020, helped to codify the case-by-case approach. Under the Financial Services Act passed in late 2012, issuance of new

[123] *https://www.state.gov/e/eb/rls/othr/ics/2017/eap/269830.htm* accessed on August 29th 2018

[124] *http://www.bnm.gov.my/index.php?ch=en_legislation&pg=en_legislation_act&ac=222&full=1&lang=en* accessed on August 30th 2018

licenses will be guided by prudential criteria and the "best interests of Malaysia," which may include consideration of the financial strength, business record, experience, character and integrity of the prospective foreign investor, soundness and feasibility of the business plan for the institution in Malaysia, transparency and complexity of the group structure, and the extent of supervision of the foreign investor in its home country. In determining the "best interests of Malaysia," BNM may consider the contribution of the investment in promoting new high value-added economic activities, addressing the demand for financial services where there are gaps, enhancing trade and investment linkages, and providing high-skilled employment opportunities.

BNM, however, has never defined criteria for the "best interests of Malaysia" test, and no firms have qualified. While under the previous administration and BNM Governor, insurance companies at 100 percent foreign ownership had to sell down their stakes by 30 percent by June 30, 2018, as of July 2, 2018, no 100 percent foreign-owned insurance company had decreased its ownership, pending new direction from BNM. A new BNM Governor took office July 2, and as of that date, BNM has made no official statements regarding

whether to uphold the previous Governor's deadline, but it has passed with no discernable impact.[125]

BNM currently allows foreign banks to open four additional branches throughout Malaysia, subject to restrictions, which include designating where the branches can be set up (i.e., in market centers, semi-urban areas and non-urban areas). The policies do not allow foreign banks to set up new branches within 1.5 km of an existing local bank. BNM also has conditioned foreign banks' ability to offer certain services on commitments to undertake certain back office activities in Malaysia.

c. Implementation of AFTA

Countries in the Asia-Pacific region, including many ASEAN economies, tend to be relatively more restrictive to FDI than in other regions. All governments discriminate among investors in one way or another, whether deliberately or unwittingly. This is the case even in OECD countries where restrictions on foreign investment tend, on average, to be lower than in other parts of the world. Foreign investors, for example, might face restrictions on their ownership in a local company, particularly in key sectors. Larger countries also tend to be more restrictive, partly because larger markets or sometimes more abundant natural resources – give them more scope to impose discriminatory

[125] Arumugam Rajenthran, *Op.Cit*, P.45

conditions and still attract investors. But the extent of restrictiveness of FDI regulations in ASEAN economies is considerably higher than observed elsewhere.

Much of the recent liberalization in Malaysia, for example, has been unilateral. At the time of the Asian crisis, Malaysia was already relatively open compared to other Asian countries, and the crisis triggered only minor FDI reforms.[126] In the decade that followed, however, Malaysia saw its share of inward FDI stock in ASEAN decline rapidly, partly as a result of increased competition for FDI by other countries in the region. Then in 2009 Malaysia unilaterally undertook reforms to its investment regime, lifting many restrictions on foreign investors, to strengthen the economy in the face of the challenges of globalization.[127] In 2011, an additional wave of reforms further eased barriers to FDI in various services sectors.

Indonesia has also significantly liberalized FDI restrictions over time, mostly on a unilateral basis. The most recent reform came with the issuance of the new negative list in 2016, which lifted or eased foreign equity restrictions in key sectors and brought Indonesia's FDI regime closer to international and regional levels of openness.[128] Most importantly, it reaffirmed a more positive attitude towards foreign

[126] Mohammad Affendy Arip, "The Impact of ASEAN Free Trade Area on Intra ASEAN", *International Journal of Business and Society*, Vol. 18 No. 3, 2016, P.641

[127] *Ibid*, P.642

[128] Ariawan Gunadi, "ASEAN Economic Community Impact for Indonesia", *Jurnal Opinio Juris*, Vol. 19, No.2, 2016, P.9

investment, coming at a critical moment as the previous negative list of 2014 had partly reversed the liberalization trend by introducing more stringent and discriminatory rules for foreign investors in some key sectors, such as mining. Yet, the current framework remains fairly restrictive to foreign investors overall.

The differences across ASEAN economies partly reflect their diverse economic structure, including different structures within services. Not all types of services are equally attracting FDI. Malaysia has likewise received less FDI in services than Indonesia, despite only a slightly lower sector weight in the economy.[129] At the same time, Malaysia attracted relatively larger shares of FDI in more knowledge-intensive services, such as ICT, than other ASEAN countries. This is also the case for Indonesia, an economy where the share of services FDI is lower than what its economic structure would predict. Most of the FDI stock in Cambodia is in construction activities, a sector where the diffusion of know-how may be more limited.

Southeast Asia is a diverse region, and the different legislative approaches framing investment policy reflect that diversity. Neither Indonesia have a general investment law, while Malaysia has a version of an investment promotion law which stipulates incentives for foreign and domestic investors and sometimes offers certain protection guarantees for

[129] *Ibid*, P.11

the promoted investor. Restrictions in Malaysia are covered in sectoral laws such as the Financial Services Act or the Communications and Multimedia Act and sometimes simply in guidelines, such as the Foreign Investment Committee Guidelines which required approval for foreign acquisitions of equity in Malaysian companies over a certain share. There is no presumption that one legislative approach is better than all others for all economies at all levels of development.

Malaysia has investment-related laws that date back decades. Another key piece of legislation in Malaysia is the Industrial Coordination Act from 1975 covering investment in manufacturing. The age of legislation is not necessarily a sufficient justification for reform, but a comprehensive reform of existing legislation can provide an opportunity to revisit certain longstanding policy approaches, such as on incentives or concerning discrimination against foreign investors.

In Indonesia, the Investment Law 25 of 2007 provides national treatment for established enterprises, in contrast to the separate treatment for foreign and domestic firms in earlier laws. It also offers greater transparency in terms of the sectors covered, more extensive land use rights and a reduction in administrative burdens and longer work permits for key personnel. Malaysia has no comprehensive law governing FDI and containing general principles for foreign participation in local business. This policy choice has given the government maximum regulatory space

to apply its affirmative action policy and to screen FDI to suit economic needs at a given time. In the absence of an all-encompassing foreign investment statute, FDI is regulated under sector-specific legislation. Protection of investors is granted in the Constitution and through the many bilateral investment treaties, which again shows that having a single investment law is not a universal panacea for creating a strong investment regulatory framework. The regulation of FDI includes the Promotion of Investment Act 1986, amended in 2007, which provides incentives.

B. Legal Protection Toward Investor in Indonesia and Malaysia Investment Law

1. Indonesia Investment Law

Indonesia's Investment Law was enacted in 2007. The Investment Law deals with the establishment of new investment, investment incentives and investor rights, among other issues.

a. Scope of Application

The Investment Law applies to both Indonesian and foreign investment. Foreign investors are defined as including foreign citizens and foreign incorporated companies.[130] Foreign investment is defined as any "investment activity for running a business" that is partly owned or

[130] Article 1 point 6 of Law No. 25 year 2007 About Investment Law

financed by a foreign investor.[131] However, the "Elucidation" of the Investment Law a formal supplement enacted alongside the Investment Law to clarify the meaning of ambiguous provisions states that the Investment Law applies only to direct investment, excluding indirect and portfolio investment.[132]

b. The form of Foreign Investment

The Investment Law requires that any foreign investment in Indonesia must be made through the form of a limited liability company incorporated in Indonesia.[133]

c. Approval of New Investment

The Investment Law establishes the basic principle that all business fields are open to both domestic and foreign investment, except for those specifically declared as closed and those declared as open to investment subject to conditions for example, limits on the permissible share of foreign ownership.[134] Restrictions and conditions on investment derive their legal basis from a range of laws and regulations. But the Investment Law requires these restrictions to be consolidated in a single Presidential

[131] Article 1 point 3 and Article 1 point 8 of Law No. 25 year 2007 About Investment Law
[132] Elucidation Article 2 of Law No. 25 year 2007 About Investment Law
[133] Article 5 point 2 of Law No. 25 year 2007 About Investment Law
[134] Article 12 point 1 of Law No. 25 year 2007 About Investment Law

Regulation. The latest version of this "Negative List" of restrictions and conditions on investment is Presidential Decree 44/2016.[135]

Even if investment in a business field is not restricted or subject to conditions under the Negative List, a permit is still generally required. The system of permits is administered by the Investment Coordinating Board (BKPM). BKPM's website explains the system of permits (which are called licenses) in more detail, including questions of when, and in what form, approval is required for the expansion, transfer or change of a business's activities.[136]

In addition to its role in screening new investment, BKPM also provides a "one-stop service" that aims to coordinate the issuing of other permits and approvals required from various ministries and agencies of government for a given investment. However, our understanding is that this "one-stop service" operates only with respect to investment approvals required at the national level. The Investment Law expressly allocates authority to regency governments to "organize" investment that takes place exclusively within their regency and expressly allocates to provincial governments authority to "organize" investment that crosses several

[135] In addition to the restrictions and conditions on new investment documented in the negative list, investment in various sectors is also subject to regulation by other institutions—for example, Central Bank regulations that apply to investment in financial services.

[136] *http://www.bkpm.go.id/en/investment-step-by-step/principal-license*. Accessed on November 1st 2018

regencies within a single province.[137] As such, the investment may also require approval from the relevant regency/provincial government, along with the permits and approvals coordinated by the BKPM.

d. Investor Rights and Obligations

The Investment Law grants a series of rights to both foreign and Indonesian investors. They include the right to "market price" compensation in the event of nationalization of the investment, the right to treatment that does not discriminate on the basis of nationality and the right to transfer funds out of Indonesia.[138] However, several of these rights are explicitly subject to other Indonesia laws. For example, the guarantee of non-discriminatory treatment is clearly subordinated to other Indonesian laws, as is the right to transfer foreign currency out of Indonesia.

The Investment Law also mentions the obligations of investors, notably to report on their investment activity to BKPM and to comply with applicable rules of Indonesian law.[139]

e. Relationship to Other Laws

The Investment Law does not contain a provision that deals with its relationship with its other Indonesia laws. However, as noted in the previous section, several provisions of the Investment Law specifically deal

[137] Article 30 point 5 of Law No. 25 year 2007 About Investment Law
[138] Article 6, 7and 8 of Law No. 25 year 2007 About Investment Law
[139] Article 15 of Law No. 25 year 2007 About Investment Law

with the relationship between different laws in a detailed and sophisticated manner, usually by making the effect of the provision in question subject to other laws. For example, the general requirement for foreign investment to be conducted through a company incorporated in Indonesia is subject to any derogations contained in other laws.[140] Similarly, the basic allocation of investment approval functions between the national, provincial and regency levels of government is subject to other Indonesia laws allocating the approval function to the national government.[141] As previously noted, investors' rights to non-discriminatory treatment and to free international transfers of funds are also subject to Indonesia law.

f. Capital for foreign investor Indonesia

In this Presidential Regulation No. 44/2016 there are several attachments that explain in detail about which business fields can be carried out without conditions (for example pepper plantations, cashew plantations, etc.), are prohibited (for example: marijuana cultivation, casinos / gambling, government museums , etc.) or can be carried out with conditions (for example: sugar cane plantations, tobacco plantations, etc.). Not only that, in the attachment to Perpres 40/2016 there is a provision related to the source of investment.[142]

[140] Article 5 point 2 of Law No. 25 year 2007 About Investment Law
[141] Article 30 point 7 section F of Law No. 25 year 2007 About Investment Law
[142] Attachment of Presidential Decree No. 44 year 2016 about Negative Investment List

For some business fields, there are a capital must wholly from a domestic investor, but many businesses can be entered into by foreign capital. For example, in the business field of utilizing timber forest products in natural forests, in this business sector, the capital must be 100% of the domestic investment. As well as sea sand excavation, and there are many other examples that have to use 100% domestic capital. An example for a business field that can be entered by a Foreign Investment is a business of consulting in the field of electric power installation, in this business sector foreign investors can invest up to a maximum of 95%. As for some business fields, they have special requirements. One example, the business field of retail trade in liquor / alcoholic beverages, must have a business license to trade alcoholic beverages (SIUP-MB) and have a distribution network and a special place.

g. Incentives

The Investment Law establishes a range of incentives called "investment facilities" that are available subject to certain conditions. They include income tax deductions, import duty holidays and accelerated depreciation. Article 19 of the Investment Law states that these fiscal incentives will be further specified and granted on the basis of "the national industrial policy issued by the Government." Consistent with this mandate, Ministry of Finance Regulation No. 130/PMK.011/2011 governs the grant

of tax holidays from corporate income tax in certain sectors. Eligibility for this incentive is determined by the Ministry of Finance.[143]

The Investment Law also establishes various non-fiscal incentives, such as special visa arrangements and expedited import procedures.[144] It appears that BKPM is responsible for assisting investors in taking advantage of these incentives.

h. Investment Promotion

The Investment Law gives BKPM responsibility for coordinating and developing Indonesia's investment policy, in consultation with various other government agencies.[145]

i. Dispute Settlement

The Investment Law recognizes that the Government of Indonesia and foreign investors may agree to resolve investment disputes through international arbitration, through a specific agreement between them.[146]

2. Malaysia Investment Law

Investment in Malaysia is governed by several laws. They include laws governing investment in particular industries, such as the Industrial Coordination Act (1975) which governs investment in manufacturing, and

[143] *http://www.bkpm.go.id/en/investment-procedures/investment-incentives*. Accessed on November 1st 2018

[144] Article 23 and 24 of Law No. 25 year 2007 About Investment Law

[145] Article 27 of Law No. 25 year 2007 About Investment Law

[146] Article 32 point 4 of Law No. 25 year 2007 About Investment Law

laws of general application, such as the Environmental Quality Act (1974). The closest thing to an investment law in Malaysia is the Promotion of Investments Act (PIA) of 1986, which deals exclusively with the issue of investment incentives.

This section provides an overview of the framework governing the approval of new investment in Malaysia and then examines the role of the PIA.

a. Scope of Application

The PIA is a framework law. It grants the Minister of International Trade and Industry broad discretionary powers to determine which investors and investments are eligible for certain classes of investment incentives and to define the magnitude of such incentives.[147]

b. The form of Foreign Investment

Under the Company Commission of Malaysia (CCM), all foreigners only are allowed to register a private limited by shares company in Malaysia. Foreigners are not allowed to register sole proprietor, enterprise or LLP companies in Malaysia, these entities are meant for Malaysian only.[148]

c. Approval of New Investment

[147] Section 4 of the Malaysian Promotion of Investment Act (1986)
[148] Section 2 of Companies Commission of Malaysia Act 2001 (Amendment) Act 2015

In general, new domestic and foreign investment in Malaysia requires government approval. For example, Section 3 of the Industrial Coordination Act requires any individual or company seeking to engage in "manufacturing activity" to obtain a license. (Companies with fewer than 75 employees and less than RM 2.5 million roughly USD 600,000 in paid-up capital are exempt from this requirement.) Licenses for the manufacturing sector are issued by Malaysia's investment agency the Malaysian Investment Development Authority (MIDA).[149]

Investment in many services sectors also requires government approval. These requirements are generally imposed by sector-specific legislation. In some sectors, a prospective investor can apply to MIDA for the relevant license; in others, applications for licenses and permits are dealt with by the relevant line ministry or agency. For example, foreign investment in financial services is regulated by the Financial Services Act (2012) and subject to equity limits. Applications for licenses to supply financial services are dealt with by the Malaysian Central Bank.

d. Investor rights and obligation

The Law on Investment establishes a limited set of investor rights. These include a right to market value compensation for expropriation, and the right of foreign investors to transfer capital and profits out of the country. Guidelines on Investor Protection which is Securities

[149] Section 3 of Industrial Coordination Act 1975

Commission Malaysia does not grant foreign investors a right to national treatment. Sections 76, 91, 92, 93 and 97 of the PIA does state that "investors" have "equal rights to invest"; however, Sections 76, 91, 92, 93 and 97 clarify that this right is subject to other laws and regulations.[150] A handful of provisions of the Law on Investment Promotion impose different requirements for investment by foreign investors. For example, Section 92 imposes a minimum capital requirement for investment in "general businesses" by foreign investors.

e. Relationship with others Law

Investment in Malaysia is governed by several laws. They include laws governing investment in particular industries, such as the Industrial Coordination Act (1975) which governs investment in manufacturing, and laws of general application, such as the Environmental Quality Act (1974).

The closest thing to an investment law in Malaysia is the Promotion of Investments Act (PIA) of 1986, which deals exclusively with the issue of investment incentives.

But in Malaysia those of law connected each other. This section provides an overview of the framework governing the approval of new investment in Malaysia and then examines the role of the PIA.

[150] Section 76, 91, 92, 93 and 97 of Malaysian Promotion of Investment Act (1986),

f. Capital for foreign Investor Malaysia

In 2009, Malaysia removed its former Foreign Investment Committee (FIC) investment guidelines, enabling transactions for acquisitions of interests, mergers, and takeovers of local companies by domestic or foreign parties without FIC approval. While the FIC itself still exists, it now only reviews the purchase by foreigners of commercial properties valued greater than at MYR 20 million (approximately USD 6.5 million) from the Bumiputera (ethnic Malays and other indigenous ethnicities in Malaysia).[151]

g. Incentives

The PIA establishes several different types of incentives. The two most important are pioneer status and the investment tax allowance. Pioneer status entitles an investor to an income tax holiday for five years. This tax holiday may be extended for a further five years.[152] The investment tax allowance allows investors to offset certain classes of capital expenditure relating to the investment against future income in any year during the five years following the year in which the expenditure was made. These two incentives are mutually exclusive; an investor must choose which one to apply for.[153]

[151] Foreign Investment Committee, Guideline on The Acquisition by Local and Foreign Interest, Acquisition for Notification part III

[152] Section 14 of the Malaysian Promotion of Investment Act (1986)

[153] Section 26 of the Malaysian Promotion of Investment Act (1986),

As previously noted, the Minister of International Trade and Industry has broad powers under the PIA to determine which investments are entitled to which incentives.[154] This includes the power to determine the magnitude of the incentives in different sectors. For example, an investor that is granted pioneer status for investment in certain defined "high technology" projects is entitled to a 100 percent income tax holiday. In contrast, in general, manufacturing activities, investors with pioneer status are only entitled to a 70 percent income tax holiday.[155] MIDA publishes detailed guidelines specifying the eligibility of investors in different sectors.

h. Investment Promotion

The Investment Law gives *The Malaysian Investment Development Authority (MIDA) is the government's principal agency for the promotion of the manufacturing and services sectors in Malaysia.*[156]

i. Dispute Settlement

The Investment Law recognizes that the Government of Malaysia and foreign investors may agree to resolve investment disputes through international arbitration, through a specific agreement between them.[157]

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[154] Section 4 and 4A of Malaysian Promotion of Investment Act (1986)

[155] *http://www.mida.gov.my/env3/uploads/IncentivesCompilation/MIDA/2013/AppIAGeneral.pdf*. Accessed on November 3rd 2018

[156] *http://www.mida.gov.my/home/about-mida/posts/* accessed on November 3rd 2018

[157] Section 25 of Convention on The Settlement of Investment Disputes Act 1966,

CHAPTER IV

CONCLUSION AND RECOMMENDATION

A. Conclusion

1. AFTA agreements are permitted within the framework of the WTO. However, the agreement must not interfere with a multilateral trading system. AFTA agreement currently does not threaten a multilateral trading system. Therefore AFTA does not violate the principle of the most favored nation.

   Indonesia and Malaysia countries have ratified various agreements concerning AFTA agreement and have been regulated on their domestic law or regulations. After entering the AFTA era, investment in Malaysia has increase rather than Indonesia, it happened since Malaysia government dare to open up

its investment chance for foreign investors. Therefore, many foreign investors attract to spend his capital in Malaysia to invest in profitable sectors.

The OSS system implemented by Indonesia as a form of convenience for investors in terms of licensing is an extraordinary breakthrough. Nevertheless, Malaysia has first implemented the system and even has an online system in 2015 and it only takes 1-2 hours. Implementation CCM (Companies Commission of Malaysia) it will only take **7** days to register a company.

2. Malaysia Law deal with several laws to regulating an investment law. In general, investor protection according to Malaysian and Indonesia investment law has a lot in similarity. Investment in Malaysia focuses on *bumiputeras* prosperity by giving a percentage in each field for investment from *bumiputeras*. Even though Indonesia and Malaysia have investment laws, but each of laws have different functions. For example, the Malaysian Promotion of Investment Act deals exclusively with investment incentives while Indonesian investment laws deals with all of investment activities. Both countries have protected both domestic and foreign investors by giving rights and obligations in accordance with international agreements. starting from incentives, taxes and convenience in business permits.

B. Recommendation

1. The existence of AFTA is very beneficial for Indonesia to invite more investors. The government should be more responsive in providing greater

convenience for investors. Indonesia has still left behind than other ASEAN countries. Nevertheless, Indonesia still supports its national interests to protect the growth of its domestic industries.

2. Investment in Malaysia seems more complicated than Indonesia, in which its only focuses on one legal protection. But Malaysia attempt to make it easier for investors because it is more flexible in terms of licensing. Indonesia should be more flexible in facilitating investment ease like Malaysia which is not complicated and effective in managing its investments.

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