

CHAPTER I

INTRODUCTION

A. Context of The Study

In stock trading, a mutual fund is commonly one of the investment instruments that firstly known through Act No. 8 Year 1995 Concerning Capital Market that gives permission to issue mutual fund.¹ It happens because some people are facing difficulties in doing investment. It is actually a phenomenon about how the services are given to the investors who need to participate in stock trading, but they do not want to be bothered with the procedure, administration, and complex analysis usually applied in capital market.² This mutual fund can also be an alternative way for people who do not have enough money but need to participate in capital market. People from all economic levels can participate in mutual fund because it is different from direct trading in capital market.

The mutual fund system has been legalized by Act number 8 Year 1995 concerning Capital Market. Article 1 Paragraph 27 explains that mutual fund is a place to collect fund from investor society, furthermore it is being invested in a portfolio by investment manager. This system seems easier for the new comer in stock trading. Munir Fuady states that there are some benefits in doing investment by using mutual fund, i.e.³

¹ Gunawan Widjaja dan Parendra Tama, *ETF, Exchange Traded Fund di Indonesia*, Rajawali Press, Jakarta, 2008, hlm 85. *See* Act No. 8 Year 1995 about Capital Market, Consideration (*Menimbang*).

² Munir Fuady, *Pasar Modal Modern (Tinjauan Hukum)*, Cetakan Pertama, Citra Aditya Bakti, Bandung, 1996, hlm 105.

³ *Ibid.*, hlm 106

1. the Professional of fund management by investment manager and the administrative of investment by custodian bank,
2. the possibility of risk reduction,
3. the possibility of investment budget reduction , and
4. the possibility for the small investor to enjoy benefit from the foreign exchange if mutual fund can be invested toward the foreign exchange.

Despite the benefits, mutual fund also arises some possibilities of risks ,i.e. ⁴

1. Risks of decreasing the value of the unit trusts

The risk is influenced by the price of stock depreciation which is included in portfolio of mutual fund itself.

2. Liquidity Risks

This risk correlates with the difficulties faced by investment manager if a lot of trusts holders are doing redemption of units that they hold. Investment manager is facing difficulties in equipping cash money of that redemption.

3. Breach of Contract

This is the worst risks. This can arise when the insurance company which insures the property of mutual fund does not immediately pay the loses, or pay lower than guarantee value when the unconditional situation happened. For example, breach of contract which comes from the connected parties in mutual fund, such as broker, custodian, or natural disaster are causing the depreciation of the net asset value of mutual fund.

The forms of mutual fund are categorized into corporate type and contractual type (Collective Investment Contract). From that name, it can be inferred that

⁴ *Ibid.*, hlm 148

corporate type is a legal entity (Limited Company). Article 8 paragraph (3) of Indonesian Capital Market Act states that “*Mutual fund company is a company which has a license from Capital Market Supervisory Board.*” Furthermore, because it has a usual limited company, the establishment of Mutual Fund Company shall obey the Act Number 40 Year 2007 concerning Limited Liability Company. Mutual Fund in the form of corporate consists of two types, open-end mutual fund and closed-end mutual fund.

Closed-end mutual fund is a mutual fund which cannot redeem the share that has been sold to the investor. As the effect, shareholder cannot redeem their shares to investment manager. The possibility for the investor to redeem their share is through the stock exchange where the mutual fund is listed. Different from closed-end mutual fund, open-end mutual fund is mutual fund which offers and redeems its shares that have already been sold to the investor until gaining the amount of capital that have been paid. Therefore, investors can redeem their shares anytime they need.

The other type is contractual type also known as collective investment contract. Collective investment contract is a way of investing money to other people to participate in a wider range of investments than those feasible for most individual investors, and also to share the cost. This contract uses the open-end mutual fund. Contractual type also can be described as a contract between investment manager and Custodian Bank which bind the owner of the unit of equity.

The characteristic of this scheme are:⁵

1. The legal form is in contractual type,

⁵ Depri Liber Sonata, *Hubungan Hukum Kontraktual Pada Pengelolaan Reksa Dana Kontrak Investasi Kolektif di Indonesia*, Bagian keempat, Bandar Lampung, Harakindo Publishing, 2015, hlm.186.

2. The management of mutual fund is conducted by investment manager based on contract,
3. The storage of collective investment property is held by Custodian Bank, and
4. Investor does not have a direct control toward their investment because the investment shall be managed by other parties as stated in the agreement.

Article 1313 of Indonesia Civil Code explains that Contract / Agreement is an act by which two or more persons are binding themselves to one or more people.⁶ On the other hand, Black Law Dictionary explains that investment means an expenditure to acquire property or assets to produce capital revenue in a collective way⁷. Because of this kind of contract, it can be ignored that there will be some of responsibilities and legal relationship between contracting parties which ought to manage it clearly.

Collective investment contract which the unit trust is traded in capital market seemed similar with the new system called Exchange Traded Fund (ETF). ETF is an investment company that offers investor proportionate shares in portfolio of stock, bonds, or their securities.⁸ Indonesia Stock Exchange explains that ETF is a mutual fund which traded in stock exchange. This statement actually gives a supporting reason that collective investment contract is closely similar with exchange traded fund. A collective investor whose the investment will be invested in portfolio, and the ownership can be proven by shares has the characteristics of mutual fund which also exists in the exchange traded fund. The investment manager and custodian bank are the actors in the mutual fund which also have a vital position in ETF.

⁶ Indonesia Civil Code.

⁷ Bryan A. Garner, *Black's Law Dictionary*, Thompson West, 2004.

⁸ Investment Company Institute, *A Guide to Exchange Traded Fund*, Washington DC, https://www.ici.org/pdf/bro_g2etf_p.pdf accessed on 8th May 2018.

Indonesian Stock Exchange stated that ETF means mutual fund in the form of Collective Investment Contract. Financial Services Authority through Regulation No 49/POJK.04/2015 states that Collective investment contract is a contract between the investment manager and the Custodian bank that binds the participation of unit holder in which the investment manager is authorized to manage the collective investment portfolio and the custodian bank is authorized to carry out collective custody.

Based on the condition above, the implementation of ETF in Indonesia, which involves so many parties are very interesting to analyze. The legal relationship among parties in the issuing of ETF is the fundamental theory that shall be learned as the basic necessity to run this mechanism.

After the legal relationship clearly held among involving parties, the problem is how every party can seek their liability under their duty? Because the legal relationship and liability are connected to each other. Therefore, when the legal relationship exists, there will be followed by liability.

This thesis is trying to analyze and identify the legal relationship in the issuing of Exchange Traded Fund and the liability under the Indonesian Capital Market Law.

B. Problem Formulation

According to the context of the study mentioned above, the formulation of the problems in this research is:

1. What is the legal relationship among parties in the issuing of Exchange Traded Fund?

2. How is the liability of investment manager when there is any negligence?

C. Research Objective

The research objectives are as follows:

1. To analyze the legal relationship among parties in the issuing of Exchange Traded Fund.
2. To analyze the liability among parties in the issuing of Exchange Traded Fund especially in the investment manager as the main actor.

D. Theoretical Framework

The Nature of Exchange Traded Fund comes from Mutual Fund. Although there is no regulation that clearly regulates about the legal relationship among parties in ETF due to its similarity with collective investment contract, the researcher used the regulation of collective investment contract to start analyzing this problem. In Indonesia there are some regulations that govern mutual fund in the form of Collective Investment Contract.

1. Act Number 8 Year 1995 Concerning Capital Market.
2. Act Number 21 Year 2011 Concerning *Otoritas Jasa Keuangan* (Financial Services Authority).
3. The Regulation of Financial Services Authority (OJK) Number: 23/POJK.04/2016 Concerning Mutual Fund in the Form of Collective Investment Contract.
4. Financial Supervisory Agency (OJK) Regulation Number 10/POJK.04/2018 Concerning Implementation of Governance Investment Manager

5. Financial Supervisory Agency (OJK) Regulation Number 49/POJK.04/2016 Concerning Mtual Fund in The Form of Collective Investment Contract where The Unit Trust Are Traded in Capital Market
6. Financial Supervisory Agency (OJK) Regulation Number 48/POJK.04/2015 Concerning Guidelines For Managing Protected Mutual Funds, Mutual Funds With Guarantees, and Mutual Funds Index.
7. Financial Supervisory Agency (OJK) Regulation Number 21/POJK.04/2017 Concerning Guidelines For Managing Securities For The Benefit Of Individual Customer

Indonesian Government as the owners of authority has been promulgated the Indonesia Capital Market Act Number 8 Year 1995 in which mutual fund is included in this Act. Chapter IV of the Indonesian Capital Market Act focused on regulating mutual fund. Article 18 paragraph 1 states that there are 2 (two) kinds of mutual funds, i.e: corporate type and contractual type (usually known as Collective Investment Contract).⁹ Collective investment contract according to the elaboration of the act are:

“The contract between Investment Manager and Custodian Bank which binds the owner of the unit trusts where the investment manager is given authority to manage portfolio of collective investment and custodian bank giving authority to perform the collective deposits.

Mutual fund in the form of collective investment contract is collecting fund through issuing the unit trusts towards investor society, furthermore the fund being invested into several kind of stock which traded in capital market and in money market.”

⁹ The Act Number 8 Year 1995 Concerning Capital Market, art. 18 (1).

The elaboration above, gives signal that in the collective investment contract, both of investment manager and custodian bank are having the same vital position. Both of them shall cooperate to attain good process and cannot be separated from each other.

The certificate of establishment of collective investment contract shall consist of the right and obligation of custodian bank and investment manager. This part is very important to give protection toward the investor from any damages.

Investment manager is a person / cooperation which has a license from the Indonesia Capital Market and Financial Institution Supervisory Agency to manage the portfolio of the investor / customer both individually or collectively.¹⁰ They also have a capability in monitoring and supervising intensively.¹¹ In the other words, investment manager can be described as the individual involved in fund management (mutual, pension, trust funds or hedge funds) who must have high level of educational and professional credentials and appropriate managerial experience to be qualified for this position.¹² The duties of investment manager are:

1. Investment manager as the manager of mutual fund in the form of collective investment contract can sell or purchase the unit trust continuously until the number of unit trust is decided in the contract.
2. In the condition of the unit trusts holder doing re-purchase, investment manager is obliged to buy back the unit trust.

However, there are some conditions that can be exempted from the regulations as stated in point (2) above. Those are:

¹⁰ Tjiptono Darmadji, Hendy M. Fakhruddin, *Pasar Modal di Indonesia, Pendekatan Tanya Jawab*. Penerbit Salemba Empat, Jakarta. 2001. hlm 22

¹¹ M. Irsan Nasaruddin, Indra Surya, *Aspek Hukum Pasar Modal Indonesia*. Kencana Prenada Media Group. Jakarta 2007. hlm 156

¹² <http://www.investopedia.com/terms/f/fundmanager.asp> accessed on March 29, 2009

1. Stock exchange where the several of the portfolio of mutual fund are traded closely.
2. The stock trading of several mutual fund portfolio in stock exchange is stopped.
3. An emergency condition happens.
4. Another thing is stated in the contract of investment manager after having approval from the Indonesia Capital Market and Financial Institution Supervisory Agency.

The management of the mutual fund is in the hand of investment manager based on the contract. The contract itself is signed by investment manager and custodian bank.¹³ Content of the contract shall include:¹⁴

1. planning on diversification of portfolio in money market and stock exchange,
2. planning of stock diversification in shares and bonds,
3. planning of investment diversification in the industrial sector,
4. prohibition of investment in certain aspects,

Another party which is always stated in the Act especially in the chapter of mutual fund is custodian bank. Custodian bank duty is to secure and keep all of the securities and other bonds or mutual funds property.

E. Operational Definition

To avoid the misunderstanding in reading some terms in this thesis, there is an explanation of all of the technical terms through the operational definition. Such terms are as stated as follows:

¹³ Article 21 Act Number 8 Year 1995 about Capital Market.

¹⁴ The elaboration of article 21 Act Number 8 Year 1995 Concerning Capital Market.

1. Mutual fund is a place which used to collect fund from the investor then the fund is invested in the form of portfolio by investment manager.¹⁵
2. ETF means Exchange Traded Fund is a listed index-tracking fund structured as a unit trusts scheme whose primary objective is to achieve the same return as particular market index investment in all (full replication) or substantially all (strategic sampling) of its assets in the constituent securities of the index.¹⁶
In a simple word ETF means mutual fund which trades in the Stock Exchange.
3. Financial Supervisory Authority, Republic of Indonesia that has a duty to construct, regulate, and supervise the activities of capital market daily, formulate and implement policy and technical standardization in financial institution.
4. Investment manager is a person or corporation which has a license from the Indonesia Capital Market and Financial Institution Supervisory Agency (OJK) to manage the portfolio of the investor/customer both individually or collectively.¹⁷
5. Custodian Bank is general bank that has a license from the Indonesian Capital Market and Financial Institution Supervisory Agency to hold a business activity as custodian, which means to give a service in safeguarding stocks (including depositing of stock which owned collectively by more than one party where the interest is represented by custodian) and other property that

¹⁵ Article 1 Paragraph 27 Act Number 8 Year 1995 Concerning Capital Market

¹⁶ Malaysian Securities Commission, Guidelines on Exchange Traded Funds, Malaysia, 2005 accessed on March 25th, 2009

¹⁷ Tjiptono Darmadji, Hendy M. Fakhrudin, *Pasar Modal di Indonesia, Pendekatan Tanya Jawab*. Penerbit Salemba Empat, Jakarta. 2001

connects to the stock and other services, including approving dividend, interest, and other matters, settling the stock transaction, and representing the owner of the account as his customer.¹⁸

6. Investor means any party that makes an investment. That term has taken on a specific meaning in finance to describe a particular type of people and companies that regularly purchase equity or debt securities for financial gain in exchange for funding an expanding company.

F. Method of Research

1. Objective of The Study

- a. The Legal relationship among parties in the issuing of Exchange Traded Fund
- b. The liabilities among parties in the issuing of Exchange Traded Fund

2. Classification of Legal Material

a. Primary Legal Material

- 1) Indonesian Civil Code
- 2) Act Number 8 Year 1995 Concerning Capital Market
- 3) Financial Supervisory Agency (OJK) Regulation Number 23/POJK.04/2016 Concerning Collective Investment Contract
- 4) Financial Supervisory Agency (OJK) Regulation Number 10/POJK.04/2018 Concerning Implementation of Governance Investment Manager

¹⁸ Eko Priyo Pratomo dan Ubaidillah Nugraha, *Reksadana Solusi Perencanaan Investasi di Era Modern*, Gramedia Pustaka Utama, Jakarta 2001. Hlm 256

5) Financial Supervisory Agency (OJK) Regulation Number 49/POJK.04/2016 Concerning Mutual Fund in The Form of Collective Investment Contract where The Unit Trust Are Traded in Capital Market

6) Financial Supervisory Agency (OJK) Regulation Number 48/POJK.04/2015 Concerning Guidelines For Managing Protected Mutual Funds, Mutual Funds With Guarantees, and Mutual Funds Index.

7) Financial Supervisory Agency (OJK) Regulation Number 21/POJK.04/2017 Concerning Guidelines For Managing Securities For The Benefit Of Individual Customer

b. Secondary Legal Materials

- 1) Literatures
- 2) Law Journals
- 3) Documents related to The Collective Investment Contract and Exchange Traded Fund

c. Tertiary Legal Materials

- 1) Web Sites
- 2) Law Dictionary
- 3) Dictionary
- 4) Encyclopaedic

3. Approach Method of Study

Legal materials were collected through library research and document study, by collecting, learning, and understanding the Indonesian Capital Market Act Number 8 Year 1995, and other regulations related to the Mutual Fund and Exchange Traded Fund, text books, articles, law journals, and other documents related to the object of the study.

4. Legal Material Analysis.

Legal material was collected, processed, and exploited to solve the problems. Collected legal material was analyzed qualitatively and descriptively. It was done by taking legal material related to the problems that were analyzed. Therefore, they can be elaborated descriptively and qualitatively. That is a depicting fact which is going into effect and is bearing with applicable law aspects. The research was conducted through the following steps:

- a. Classification or Legal Material were collected based on the problem of the research;
- b. The classification of legal material was systemized;
- c. The Systemized material was analyzed in order to achieve the conclusion.

G. Structure of Writing

Chapter 1 elaborates the context of the study, problem formulation, objective of the study, theoretical frameworks, operational definition, method of research, and also structure of writing.

Chapter II explain the general consideration of Capital Market Law in Indonesia which correlates with mutual fund generally and collective investment contract specially. In this chapter, it also explains the history of exchange traded fund and procedure in issuing of Exchange Traded Fund

Chapter III gives elaboration about the duty of involving parties in the exchange traded fund/collective investment contract and it was continued with the analysis about the legal relationship among parties in the issuing of exchange traded fund and the liabilities that raised because of that legal relationship.

Chapter IV contains conclusion, suggestion, and critics. Conclusion here is the answer of the problems that have been analyzed and investigated. Furthermore, it also contains any suggestion, critic, and recommendation toward the result of the research.