

# Challenging the constitutionality of Indonesia's Investment Law

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## Summary

In 2008, a high-profile case was filed by a coalition of civil society organisations in the Constitutional Court of Indonesia to challenge the validity of the 2007 Investment Law. SPI (Serikat Petani Indonesia, the Indonesian Peasant Union), and a wider national coalition, considered aspects of this law to be a threat to the rights of peasants. The court ruled that the law did not accord with the Constitution.

Initiating constitutionality review processes is one strategy used by SPI's legal unit to advance the rights of peasants through legal avenues on behalf of its members – that is, taking a case to the Constitutional Court in order to challenge the compatibility of legislation with the national Constitution. This paper distils lessons from SPI's experience. It discusses the steps taken, the court decision, and the lessons learnt on how to make more effective use of this legal strategy. It also touches on important parallel strategies.

### About SPI and GERAK LAWAN

The Indonesian Peasant Union (SPI, Serikat Petani Indonesia) is a national movement of landless people, peasants, small farmers, farm workers, plantation workers, and peasant-based indigenous communities ([www.spi.or.id](http://www.spi.or.id)). It was established in its current form in December 2007, taking over from its predecessor the Federation of Indonesian Peasant Union (FSP). SPI has representatives at national, provincial, district, sub-district and village level in 14 provinces and 36 districts, with many thousands of individual members at village level.

Internationally, SPI is a member of La Via Campesina, the international peasant movement, and has hosted the International Operational Secretariat of La Via Campesina since 2004. SPI also hosts the secretariat for the coalition GERAK LAWAN (People's Movement Against Neo-colonialism and Imperialism), which was formed in 2007 in opposition to a new Investment Law.

### About the author

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## 1. Introduction

In Indonesia, constitutional adjudication is the purview of the Constitutional Court, which exists alongside the Supreme Court. The main function of the Constitutional Court is to adjudicate constitutional cases and safeguard the Constitution. Cases can be taken to the Constitutional Court by parties that consider their rights to have been harmed by the enactment of a law, including individual citizens, entities of indigenous people, public or private legal entities and state institutions.

The judgments of the Constitutional Court are based on the principles and values contained in the Constitution, held to be the highest set of guiding norms. The court has the power to strike down legislation inconsistent with the Constitution.

Civil society sees the Constitutional Court as a battleground to challenge laws that violate the Constitution, and the rights enshrined in it. One landmark decision taken by the Constitutional Court in a constitutionality review case concerned the Investment Law of 2007 (Law No. 25/2007). The case was submitted by the coalition GERAK LAWAN (People's Movement Against Neo-colonialism and Imperialism), steered by SPI (Serikat Petani Indonesia, the Indonesian Peasant Union).

The Investment Law guaranteed investors' access to land through rights to receive and renew in advance: the Right of Tenure for 95 years, the Right to Build for 80 years and the Right of Use for 70 years. SPI's analysis suggested that this law had the potential to facilitate investments that could undermine the rights of rural citizens, including their access to land, natural resources and employment, and limit the potential economic benefits of foreign investment. SPI also felt that some elements of state sovereignty and state capacity to regulate in the interest of its citizens were at risk under the 2007 law. Hence the challenge to seek review of it.

In its ruling, the Constitutional Court considered provisions of the law to be unconstitutional, due to conflicts with Article 33 of the 1945 Constitution. This provision affirms state ownership rights of land, water and natural resources and the people's economic principle.<sup>1</sup>

This paper distils lessons from this experience. It discusses the steps taken, the court decision, and the lessons learnt on how to make more effective use of this legal strategy. The paper first provides background information on the judicial review and the organisations involved. It then describes the judicial review process, the court decision and the challenges that GERAK LAWAN faced. The final section discusses the outcome of the case, distils lessons learnt from the process, and elaborates on other strategies that SPI engages with in parallel to ensure that Indonesia's laws protect the rights of peasants.

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1. People's Economic Principle refers to Article 33 (1): 'The economy is to be structured as a common endeavour based on familial principles.'

## **2. Judicial review of the Investment Law**

### **2.1. Background to the Investment Law (Law No. 25/2007)**

Indonesia's Investment Law of 2007 was developed as part of an Investment Climate Policies Improvement process established through Presidential Instruction (No. 3/2006). The process was funded by the World Bank through a Third Development Policy Loan (totalling US\$600 million between December 2006 and March 2007). The programme included reforms to core elements of the Investment Law, such as: capital expansion for economic growth, transparency, equal treatment of foreign and domestic investors and dispute settlement. These reforms, driven by relations with international financial institutions, were part of a wider process of liberalisation that also included reforms to the Water Law, the Electricity Law, the Oil and Gas Law and the Mineral and Coal Law.

In the New Order<sup>2</sup> era, foreign investments were mainly in natural resource extraction. But since the Reformation<sup>3</sup> era, they also seek to enter public services such as electricity, water supply, telecommunication and banking. For example, it is estimated that in 2006 foreign investors controlled 50.6 per cent of Indonesia's bank shares. More than 200 million Indonesians are now a potential market for foreign investors. The 2007 Investment Law is intended to open the door to that market.

### **2.2. Civil society scrutiny of the law**

The law contentiously guaranteed a number of rights to investors, including rights of tenure for 95 years. This amongst other provisions raised serious concerns for citizens over their own rights to resources, the economic sovereignty of the country, and the capacity of the state to continue ruling in the interests of citizens.

Before the Investment Law was passed on 29 March 2007, many civil society organisations expressed their discontent. A national coalition, GERAK LAWAN, was formed to oppose it, with SPI hosting the secretariat. A series of rallies and discussions were held by GERAK LAWAN members to gather reactions to the Investment Law. SPI held consultations in several provinces to raise peasant voices. The SPI Provincial Offices disseminated the draft law to its members and invited district and sub-district members to scrutinise it at their monthly meeting.

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2. The term New Order refers to the period under President Soeharto, 1966 to 1998, characterised by strong military role, repression of freedom of speech, and corruption.

3. The Reformation era is the period of transition after Soeharto's presidency to a more open political and social climate, with greater freedom of speech and regional autonomy.

Most SPI members raised concerns about Article 22 of the law, which provided investors the Right of Tenure for 95 years, with rights of renewal in advance. This article was perceived as a signal to civil society that the government did not trust that peasant farmers would be able to contribute to agricultural development, but believed in giving the land to investors so that they could hire peasant farmers as cheap labour. SPI members regarded the proposed law to be legalising 'land grabbing' for plantation agriculture by expropriating peasants from their land for up to a century, if not more.

A number of other articles were of major concern to GERAK LAWAN members – for example, the provisions enabling foreign investors to invest without collaboration with domestic investors. The law permitted 100 per cent foreign control over companies operating in Indonesia (Article 1(3)), threatening – in the belief of the GERAK LAWAN coalition members – Indonesia's economic sovereignty. Alarm bells were also raised about the rights being afforded to companies to bring in foreign workers, potentially at the expense of jobs for Indonesians (Article 10 of the Investment Law).

In May 2007, GERAK LAWAN held a meeting in Jakarta with a number of academics from various disciplines, including an agrarian expert, a sociologist, an economist, a legal expert, an independent researcher and a human rights activist. This group examined the freedoms provided to foreign investors under the new law, which included 100 per cent foreign ownership of corporations, incentives such as tax holidays, infrastructure facilities, access to land and domestic finance, free repatriation of profits and no import tariffs on capital goods, and concluded that the Investment Law was in conflict with Article 33(3) of the Indonesian Constitution. Article 33 states that 'the land and the waters as well as the natural riches therein are to be controlled by the state to be exploited to the greatest benefit of the people'. As a result, the group concluded, the rights and livelihoods of workers, farmers, fishing communities and indigenous peoples were under threat. Based on this analysis, GERAK LAWAN, together with its participatory advisors, decided to take the Investment Law to the Constitutional Court.

### **2.3. Filing the case**

The plaintiffs were from 10 different civil society organisations. These were SPI, PBHI (Indonesia Legal and Human Rights Aid Association), API (Indonesian Farmers Alliance), Bina Desa Sadajiwa Foundation, Solidaritas Perempuan (Women's Solidarity for Human Rights), FSBJ (Jabodetabek Labour Union Federation), WALHI (Friends of the Earth Indonesia), KPA (Agrarian Reform Consortium), SHMI (Indonesian Human Rights Voice) and ASPPUK (Association Supporting Women in Small Business).

The lawsuit challenged the constitutionality of the following provisions of the Investment Law:

### **100 per cent foreign ownership**

Article 1(3) of the Law: 'Foreign Investment shall be any investing activity for running business within the territory of the Republic of Indonesia, made by any foreign investor using either foreign capital entirely or joint capital with domestic capital.'

### **National treatment**

Article 4(2)(a): 'In making the basic policy set forth in paragraph (1) above, the Government is to provide the same treatment to any domestic and foreign investors, by continuously considering the national interest.'

### **Capital flight and asset repatriation**

Article 8(1) and (3): 'Any investors may transfer their assets to another party they choose in accordance with the rules of law' and 'any investors shall have the right to make transfer or repatriation in foreign currency to, among others:

- a. capital;
- b. profit, bank interest, dividend, and any other revenue;
- c. funds required for: purchasing raw materials and support materials, intermediate products, or final product and reimbursement of capital goods in order to secure the investment;
- d. additional fund required for financing investment;
- e. fund for loan repayment;
- f. payable royalty or interest;
- g. income of any foreign individuals working in any investment company;
- h. the proceeds of any sale or liquidation of investment;
- i. compensation for any loss;
- j. compensation for any takeover;
- k. payment made for technical aid, payable costs for technical service and management, payment made under project contract, and payment for intellectual property right; and
- l. proceeds of asset sale set forth in paragraph (1) above.'

### **Use of foreign labour**

Article 10(2): 'Any investment companies shall be entitled to use experts of foreign citizenship in certain positions and expertise in accordance with the rules of law.'

### **Land rights with rights of renewal**

Article 21: 'In addition to facilities set forth in Article 18, Government will provide service and/or licensing convenience to investment companies in obtaining:

- a. land rights;
- b. immigration service facility; and
- c. import licensing facility.'

Article 22(1): 'Ease of service and/or land right permit set forth in Article 21 (a) may be given, extended and renewed in advance simultaneously and may be further renewed upon request of investors in the form of:

- a. *Hak Guna Usaha* (Right of Tenure) may be given for 95 (ninety-five) years and simultaneously renewed in advance for 60 (sixty) years, and it may be further renewed for 35 (thirty-five) years.
- b. *Hak Guna Bangunan* (Right to Build) may be given for 80 (eighty) years and simultaneously renewed in advance for 50 (fifty) years, and it may be further renewed for 30 (thirty) years.
- c. *Hak Pakai* (Right of Use) may be given for 70 (seventy) years and simultaneously renewed in advance for 45 (forty-five) years, and it may be further renewed for 25 (twenty-five) years.'

Article 22(2): 'Land Rights set forth at point (a) of Article 21 may be granted and simultaneously renewed in advance for any investment activity, with, among others, the following conditions:

- a. such investment is for the long term and associated with the structural change of Indonesian economy into a more competitive one;
- b. such investment is with the level of investment risk requiring long-term Return on Investment according to the types of the investment activity;
- c. such investment does not require extensive area;
- d. such investment uses state-owned land rights; and
- e. such investment does not interrupt the sense of impartiality in the community as well as public interest.'

Article 22(4): 'Granting and extension of land rights can be given and may be updated as described in paragraph (1) and (2) but can also be suspended or cancelled by the Government if the investment company abandons the land, harms the public interest, fails to use the land in accordance with the intent and purpose of the land rights granting, or is in violation of laws and regulations.'

## 2.4. The court opinion and decision

The court asserted that in the formulation of Article 33 of the Constitution, the exploitation of natural resources for the 'greatest benefit of the people' is protected by the Constitution, and the importance of control by the state in delivering this is emphasised. A restriction on land ownership is enforced by the state so that ownership of land is not concentrated amongst a particular group of people. The intention of this restriction is that distribution of economic resources is spread evenly and eventually achieves the aim of equitable prosperity. In addition, for land controlled by the state, the distribution of land rights is to be done in a way that provides equal opportunities to obtain the Right of Tenure, Right to Build and Right of Use within a specified period.

A problem therefore arises when the granting of land rights (Right of Tenure, Right to Build and Right of Use) is given and simultaneously renewed in advance. This negates or diminishes the authority of the state and its capacity to regulate, maintain, manage, and oversee the use of its land, water and natural resources. Although there is a provision in the Investment Law which allows the state to terminate the land rights afforded to a company in cases of non-compliance with conditions set out in Article 22(4) of the Investment Law, the rights of the company to have a lease 'simultaneously renewed in advance' (Article 22(1) and (2)) reduces the control of the state authorities.

This erosion of sovereignty is seen more clearly under the provisions on dispute settlement of the Investment Law (Article 32):

(1) In the event of any dispute in the field of investment between the Government with investors, the parties must first seek to settle the dispute through consensus agreement.

(2) In the event that the dispute settlement referred to in paragraph (1) is not reached, the dispute shall be resolved through arbitration or alternative dispute resolution or through the court in accordance with the provisions of the legislation.

(3) In the event of a dispute in the field of investment between the Government and a domestic investor, the parties may settle the dispute through arbitration by agreement of the parties, and if the resolution of disputes through arbitration is not agreed upon, settlement of the dispute will be done in court.

(4) In the event of a dispute in the field of investment between the Government and a foreign investor, the parties will resolve the dispute through international arbitration which must be agreed upon by the parties.'

The court asserted that through Article 32, the law establishes the state as a subject of regular civil law, with a position equal to that of the investor. Furthermore, dispute resolution through arbitration should be included in company–state contracts, rather than in the formulation of national laws. Furthermore Article 32(4) implies distrust of the judicial system in Indonesia. All of this suggests a reduction in Indonesian state sovereignty as established in the 1945 Constitution.

The court declared it evident that the provision to grant investment companies rights to land (Right of Tenure, Right to Build and Right of Use) that are 'simultaneously renewed in advance' under Article 22(1), (2) and (4) of the Investment Law has reduced, weakened, or even in certain circumstances eliminated the economic sovereignty of the people.

In light of this analysis, the Constitutional Court concluded that Article 22 (1), (2) and (4) of the Investment Law was contrary to the 1945 Constitution, and that the simultaneous right to renewal contained in each of these sections should be removed, as well as references to the number of years the Right of Tenure, Right to Build and Right of Use could be granted for. Regulations on the rights referred to in



this Law should instead defer to the stipulations of the Basic Agrarian Law of 1960. In the Basic Agrarian Law, the Right of Tenure can be given for 35 years, and renewed for a further 25 years (Art. 29), the Right to Build can be given for 30 years, and renewed for a further 20 years (Art. 35), and the Right of Use can be given for 25 years and renewed for a further 20 years (Government Regulation No. 40 of 1996 on the Right of Tenure, Right to Build and Right of Use).

### **3. Conclusion: Outcomes, challenges and opportunities**

#### **3.1. Significance and limitations of the court decision**

The Constitutional Court's decision in the judicial review of the 2007 Investment Law is a highly significant and positive evolution with respect to safeguarding peasant rights. Although the decision does not go as far as GERAK LAWAN had hoped, the coalition felt grateful that the Constitutional Court defended Article 33 of the Constitution and re-established the provisions of Right of Tenure, Right to Build and Right of Use as those set out under the Basic Agrarian Law of 1960. Whilst some economic observers have stated their belief that this decision will adversely affect the investment climate in Indonesia, GERAK LAWAN believes it to be crucial to managing foreign investment in the interests of rural Indonesian citizens.

GERAK LAWAN disagrees, however, with the analysis of the Constitutional Court with regards to Article 1(3) of the Investment Law, which provides for 100 per cent foreign ownership and was not found to be unconstitutional. Article 33(2) of the Indonesian Constitution states that 'Production sectors that are vital to the state and that affect the livelihood of a considerable part of the population are to be controlled by the state.' GERAK LAWAN believes that agricultural production and processing are sectors that affect the livelihoods of a considerable share of the population, and that permitting full foreign ownership is in contrast with the constitutional provision.

GERAK LAWAN also thinks that Article 8(1) and (3) concerning capital flight should have been abolished by the court because it could lead to mass layoffs of workers if investors can move their assets and capital easily without any state regulation. If investors decide to shut down their factories and move their capital and assets to another country, thousands of labourers could lose their jobs, with no obligation for the investor to protect their rights or provide assistance in seeking alternative employment.

Despite these shortcomings, the decision of the Constitutional Court proved that civil society organisations can play a role in correcting government policy that could be detrimental to citizens. GERAK LAWAN proved that if civil society organisations unite together, they have greater strength in countering legal reforms that increase corporate control of land, water and natural resources at the expense of citizens' rights. GERAK LAWAN's membership is growing fast, expanding from just 10 organisations to about 40 since its formation in 2007.

### **3.2. Lessons learnt**

One important lesson that can be learnt from this judicial review is the significance of the support that came from academic groups. Civil society organisations often face challenges in gathering experts who are able and willing to testify in judicial review processes in the Constitutional Court. In this case, GERAK LAWAN received support from lecturers in various universities, as well as from other professionals. Maintaining these relationships will be important to any future struggles that GERAK LAWAN decides to engage in.

However, GERAK LAWAN also felt that, in this judicial review process, there was insufficient elaboration on the potential human rights violations under the Investment Law. The coalition was also unable to mobilise human rights experts to testify in court because most are based in provinces far from Jakarta. In consequence, the legal challenge submitted was ultimately focused on Article 22, which meant there was extensive analysis on the Right of Tenure, Right to Build and Right of Use, and their relationship with Article 33 of the Constitution. But there was insufficient in-depth analysis on the effects of capital flight and asset repatriation and also about the freedoms provided to employ foreign workers. A labour organisation and member of GERAK LAWAN, was not able to elaborate effectively on the potential impacts of capital flight on workers and their labour rights. The coalition also lacked specialists on labour law to support their claims in court. Involving other labour organisations in the coalition is one strategy that could strengthen the coalition's knowledge and their claims in court.

Financial constraints arose for GERAK LAWAN in part because there was no agreement between the members at the outset of the coalition concerning financial contributions required. This resulted in a lack of budget for the GERAK LAWAN legal team, and hindered their ability to invite experts who lived outside Jakarta because of the travel costs involved. In future, the coalition will increase efforts to mobilise adequate financial resources and expertise to support their case in court.

### **3.3. Opportunities going forward**

This judicial review process clearly shows how important the engagement of civil society organisations with the Constitutional Court is. Last year, the former Chairman of the Constitutional Court was quoted as saying that 30 out of 97 constitutionality challenges decided by the Court in 2012 were successful (Wilmar P, 2013). This suggests poor performance in legislating on the part of government and parliament. Judicial reviews have become a part of citizens' struggles against arbitrary policies and considerable effort and resources are required to conduct them, involving in-depth analysis of new laws, presentations by high-level experts, and long-drawn-out court proceedings; most of the judicial review processes in Indonesia take more than a year. In order to reduce the amount of resources being invested in Constitutional Court cases, civil society is demanding that the government makes better policy

decisions that are in the interests of the people and, in SPI's case, in the interests of peasant farmers, fishing communities and indigenous peoples in particular.

One approach to this is for civil society to take the lead in drafting new laws. For example, in 2008, in collaboration with several civil society organisations, SPI drafted the Food Law. The Bill was brought to the Legislation Board in the House of Representatives and entered into the *Prolegnas* (National Legislation Programme) in 2010. That was when the struggle began in earnest. The first step was to identify parliamentary members in the Fourth Commission (Food and Agriculture Commission) who would sit on the Food Law Bill Special Committee. SPI then held a workshop and invited committee members to debate the Bill with them and presented SPI's position. SPI also lobbied parliament by visiting each political party and presenting its views. Lobbying also involved attending the Food Law Bill Special Committee meetings as an observer to identify members who supported and opposed SPI's ideas. Press conferences and public seminars were also used to raise public awareness about the Bill. The Food Law (Law No. 18/2012) was passed in October 2012, and whilst there are still a great many criticisms of the law, SPI sees it as a success that the principle of food sovereignty has been given legal recognition in it.

Currently, SPI is pursuing a similar struggle in relation to the Peasants Protection and Empowerment Law Bill. This law entered the *Prolegnas* in 2010–2014 based on SPI's proposal for a Peasants' Rights Bill, modelled on the experience of the UN Human Rights Council for the development of a declaration on 'the rights of peasants and other people in rural areas'. Although the name of the Bill that SPI proposed has not been not accepted by the Legislation Board, SPI is trying to make sure that the Bill will have the same content as the current draft Declaration on the Rights of the Peasants.

Pushing the government to issue legislation on the rights of peasants could be a more effective way to achieve change than the long-drawn-out and resource-intensive constitutionality challenges that have been described here. However, it is likely that use of the Constitutional Court for challenging legislation deemed unfavourable to peasants will be an important tool for some time to come.

## References

Wilmar P. 2013. Performance of the Constitutional Court: Significant Rise in Successful Judicial Review Cases. *Surya Karya*, [online] 3 January. Available at: [www.surakarya-online.com/news.html?id=318442](http://www.surakarya-online.com/news.html?id=318442). [Accessed 30 January 2014].

**National legislation** (in chronological order, most recent first)

Food Law of 2012 (Law No. 18/2012)

Investment Law of 2007 (Law No. 25/2007)

Presidential Instruction No. 3 of 2006

Government Regulation of 1996 on the Right of Tenure, Right to Build and Right of Use (No. 40/1996)

Basic Agrarian Law of 1960

Constitution of 1945