THE REGULATION OF INDONESIAN STATE ENTERPRISES

I. *HISTORICAL BACKGROUND*

1. Introduction

In order to understand the nature of government enterprise in Indonesia,[1] it would be beneficial to examine first the historical development of these institutions. The starting point of this investigation must naturally be the Dutch East Indies administration.[2] Government enterprises or corporations were established by the Dutch in 1925 under the *"Indische Comtabiliteitswet"* (abbreviated I.C.W.).[3] *"Indische Comtabiliteitswet"* refers to statutes that regulate the financial responsibility of governmental bodies. Thus, on the one hand, an enterprise could take the form of a corporation, but on the other hand the law regulating private corporations generally was not applicable because the enterprise was defined as a governmental body. In fact such enterprises were governmental agencies generally operating in the public service fields; all expenses of these corporations were the government's burden and their income and expenses were included in the government's budget. These enterprises had substantial operational freedom under the Dutch East Indies policy of administrative decentralization.[4]

Two years later a second special regulation governing government corporations was promulgated, similar to that discussed earlier, and called *"Indonesiche Bedrijvenwed"* (abbreviated I.B.W.).[5] This special regulation provided for two types of enterprise.[6]

a. government enterprises subject only to the I.B.W.

b. government enterprises subject to both the I.B.W. and the I.C.W.

1. Government enterprise is here meant to include all forms of corporations in which capital is partly or completely owned by the government.
2. The legacy of 300 years of Dutch administration is still a significant influence on Indonesia as many of the Dutch legal, economic end social institutions remain and have been difficult to change in the two decades since independence.
3. S. G. No. 448/1925.
4. "The Statutes Concerning the 3 Forms of Government Enterprises". Bureau of Social Politics and Law, Department of Industry, p. viii (1972).
5. S. G. No. 419/1927.
6. Himawan, Charles, and Kusumaatmadjo, Mochtar, *Business Law — Contracts and Business Associations* (Pajajaran University Faculty of Law, 1973), at p. 76; and see "The Statutes Concerning the 3 Forms of Government Enterprises", fn. 4, *supra.*

Both types were still considered governmental bodies, but were granted more autonomy in operations. For internal purposes all I.B.W. corporations were still considered a part of the government, and income and expenses were still included in the government budget. However a special entry was made in the government budget charging the corporation with losses when the expenses of a corporation of this type were larger than its income. Although corporate activities relating to the protection of the public interest were regulated by public law, in some instances legislation directed the application of the civil law. Generally I.B.W. corporations were permitted to operate utilizing cost accounting principles.[7]

Prior to Indonesian independence, a total of twenty corporations were subject to the I.B.W.[8], operating in a variety of areas including pawnbroking, salt, soda, coal, tin mining, vaccine and serum production, electricity, postal and telecommunications, plantations and harbour facilities. After Indonesian independence, these twenty corporations continued to be regulated by the I.B.W. but were nationalized and operated under the Indonesian government.[9] The economic philosophy embodied in the 1945 Constitution also provided for the creation of state enterprises.

The Indonesian Constitution of 1945 makes reference to the basic elements of the Indonesian economic philosophy:

1) The Indonesian economy should operate by collective and unified effort of the community.

2) Branches of production which are important to the state and affect the welfare of the people should be controlled by the state.

3) To the maximum extent possible, the earth, water and the natural resources within them should be controlled by the state to be used for the benefit of the people.[10]

The basic economic philosophy contained in the Constitution is to secure economic prosperity for the people and to prevent privileged groups from controlling those elements of the economy vital to the people's welfare. The control of the earth, water and natural resources of Indonesia is possibly the most important area of the government's responsibility under the Constitution. The state enterprises are a manifestation of this philosophy that the government should control sectors vital for the people's welfare.[11]

7. Soekardono, Prof. R., *Indonesian Commercial Law* (1967), Vol. I, at p. 28.

8. "The Statutes Concerning the 3 Forms of Government Enterprises", *supra.*

9. See Art. 2, Constitution of 1945.

10. Art. 33, Constitution of 1945.

11. See Simorangkir, Mr. J.C.T. and Dr. Mang Reng Say, "Constitution of 1945 as the Permanent Constitutions of the Republic of Indonesia" ("Undang2 Dasar 1945 dalam kancah penetapan Undang2 Dasar Tetap Indonesia") (Jambatan Press 1959), at p. 37.

A substantial increase in the number of government corporations occurred in 1958 when all corporations in Indonesia owned by Dutch nationals were nationalized as a result of the West-Irian dispute.[12] Subsequently in 1960, the government issued Act No. 19/1960 [13] which regulated all existing government corporations (including both the recently nationalized enterprises as well as those operating subject to the I.B.W. and I.C.W.). The statute was intended to create uniformity among the public corporations so that they could be better coordinated and integrated into the Indonesian development programme.[14]

Basically under Act No. 19/1960 all government enterprises became *"Perusahaan Negara"* which literally means government corporation. In 1969 however the government formulated a new statutory scheme, Act No. 9/1969,[15] which substantially changed the structure of the *Perusahaan Negara.* This legislation divided both existing and future government enterprises into three classes or types: *"Perusahaan Jawatan"* which means Departmental Agency, *"Perusahaan Umum"* which means Public Corporation, and *"Perusahaan Perseroan"* or Limited Liability State Company. As a result of the reorganization of public enterprises under Act No. 9/1969 the total number of state operations has been reduced.

In 1965 the Bureau of State Enterprise Affairs reported 233 state enterprises which operated in a wide range of fields including agriculture and plantations, industry and mining, communications, public works and power, trade, Pharmaceuticals and health, and banking. In April, 1969, after a number of these corporations were reorganized and consolidated and several previously nationalized enterprises were returned to the original owners, the total number of state enterprises was reduced to 139.[16] By June, 1973 the total number of state enterprises had been reduced to 134. Of this number, 36 were *Perusahaan Umum* or Public Corporations, and 98 could be classified as *Perseros* or State Companies. These figures do not include joint venture state enterprises in the *Persero* form established with foreign investors or other third parties (numbering 9 in 1971),[17] or state enterprises regulated by special statutes, which includes Pertamina, state banking institutions (number-

12. Act No. 86/1958, S. G. No. 162/1958. After independence the Dutch East Indies administration attempted to maintain control over West Irian, the extreme eastern island in Indonesia. The Indonesian government later demanded the return of this area which ultimately resulted in a major conflict between the two countries.

13. Act No. 19/1960, S. G. No. 59/1960. In fact this was not an act, but a temporary government regulation which was to be later replaced by an act. Nevertheless, according to Indonesian administrative law, this kind of regulation is considered in its effect the same as an act. See Chapter 22, Constitution of 1945.

14. Elucidation of Act No. 19/1960.

15. This scheme was introduced by Government Regulation No. 1/1969 which was to be later replaced by Act No. 9/1969.

16. Wirjasuputra, Aninda, and Rieffel, Alexis. "Government - Owned Enterprises in Indonesia" (unpublished USAID paper, 1972), at pp. 4-5.

17. See Himawan, Charles and Kusumaatmadja, Mochtar, *op. cit.,* at p. 84.

ing 7 in 1974) and regional enterprises.[18] This total also does not include state enterprises which have been classified as *Perusahaan Jawatan* or Departmental Agencies.[19]

2. Condition of State Enterprises and Political Influence

Out of this considerable number of public corporations in Indonesia, only a few have been profitable. According to the regulations that govern public enterprise, state corporations are required both to pay a company tax (profits tax)[20] and to place 55% of their profits into the state treasury as a contribution to development.[21] An official of the Finance Ministry observed that from 1965 to 1968, there were no profits from state enterprises that could be taxed or be deposited in the state treasury as a contribution to development.[22]

This result may be attributable to several economic, social and political factors. Political factors in particular have contributed to the proliferation of public enterprises in Indonesia. The major increase in the number of Indonesian state enterprises abruptly occurred in 1958 as a result of the confrontation between Indonesia and the Netherlands concerning West Irian. At that time all enterprises in which Dutch capital was invested were nationalized without exception and became government enterprises.[23] The economic interest of the Indonesian nation and people was put forward as the juridical justification of the nationalization.[24] In actual fact, however, although these economic interests were to some degree involved in the nationalization of Dutch enterprises, nationalization was primarily intended to place political pressure on the Dutch government to moderate its policies on West Irian.

During this period of confrontation the Indonesian government adopted an isolationist policy, particularly towards those several western countries which were viewed by the government as Dutch allies. The new inexperienced and unskilled managers of state enterprises were thus denied any exposure to the considerable experience of western countries with private and public enterprises. This lack of managerial training opportunities severely retarded the development of Indonesian state enterprises.

The confrontation and the resulting period of isolationism also provided a favorable climate for the growth of the Indonesian Com-

18. See p. 312, *infra.*

19. For a discussion of Departmental Agencies, see p. 313, *infra;* and also Himawan, Charles and Kusumaatmadja, Mochtar, *op. cit.,* at p. 83.

20. Corporation Tax Ordinance 1925; Regulation of Minister of State Collection No. P. Ps. 1-1-5 (1956).

21. Art. 18(2), Act No. 19/1960.

22. See Wirjasaputra, Aninda, and Rieffel, Alexis, fn. 16, *supra,* at p. 7.

23. Art. 1, Act No. 86/1958, S. G. No. 162/1958 and Art. 1, Government Regulation No. 2/1959, S.G. No. 5/1959; enterprises whose capital was partially or wholly owned by the Netherlands or by any company domiciled in the Netherlands Kingdom were nationalized.

24. Elucidation of Act No. 86/1958.

munist Party (P.K.I.), which ultimately resulted in the attempted communist coup on the 30th of September, 1965. In the years prior to the abortive coup, the communist party attempted to acquire mass strength within the state enterprises by securing employment within the state enterprises for as many party members as possible. These political conditions and the economic losses incurred because of the burden of surplus employees contributed to the general deterioration of state enterprises from 1960-1966.

The confrontation with the Netherlands in 1958 did have a significant positive result for state enterprises which counter-balanced to some extent the problems previously discussed. Although Indonesia became a sovereign independent state in 1945, the Dutch continued to own and control important and strategic enterprises, including electricity, water, municipal gas, shipping, airlines and particularly mining. This situation was finally changed by the nationalization of Dutch investments in 1958.

3. The Change in the Year 1969

Since 1966, a major change in the Indonesian government's foreign and domestic policy has occurred. In foreign policy the isolationism favoured by President Sukarno has been pushed aside and replaced by the open and basically neutral foreign policy adopted by President Soeharto. Domestically, the government has created a complete and more stable development policy called Repelita or the five year Development Plan. The Re Foreign Capital Investment Act (Act No. 1/1967) recognized the importance of foreign capital and provided that foreign investment can be utilized in the development programme without harming the national interest or the Indonesian people.[25]

During the transitional period 1966-69 government policy concerning state enterprise was also re-evaluated culminating in the reorganization of *Perusahaan Negara.* As explained previously those *Perusahaan Negara* operating in the public service section become *Perusahaan Jawatan* or Departmental Agencies *(Perjan).* Those operating public utilities become *Perusahaan Umum* or Public Corporations *(Perum)* and those operating in production and commerce become *Porseros* or State Companies.

In the interim conversion period pending the drafting of satisfactory Indonesian National Statutes, enterprises in the *Perjan* form operate subject to the statutes originally promulgated in the Dutch period, the I.B.W. On the other hand, as profit-making public enterprises, the *Perseros* (State Companies) operate subject to the same commercial code provisions that regulate the internal affairs and commercial activity of private limited corporations. The *Perums* (Public Corporations) still operate subject to Act No. 19/1960.[26]

As suggested in the Elucidation to Act No. 9/1969, the reforms made in 1969 were necessitated primarily because it was inefficient to classify and regulate all public enterprises of whatever type as *Perusa-*

25. Art. 6, Act No. 1/1967 (Re Foreign Capital Investment Act).

26. Art. 2, Act No. 9/1969.

haan Negara under Act No. 19/1960. It did not appear to be feasible to regulate as *Perusahaan Negara* both public corporations originally established by the Dutch to provide fundamental and secondary public services as well as nationalized Dutch business enterprises involved in industry and commerce. It appeared to government policy makers in 1969 that it was contradictory to expect a *Perusahaan Negara* to provide public service and at the same time to be obligated to return substantial profits to the government. Similarly, state enterprises competing in industry and commerce had difficulties returning profits when they were regulated as semi-government institutions.[27] The wide diversity of activity of these enterprises dictated regulations more tailored to specific needs. The reorganization of state enterprises into three different operational categories subject to specialized regulations was the government's response to solve these problems.

The extremely critical financial condition of the state enterprises prior to 1969 was also an important factor leading to organizational reforms. The Minister of Commerce in 1969, Sumitro Djojohadi Kusumo wrote that "...although some of the *Perusahaan Negara* (P.N.) have been changed into *Perseros* (State Companies), nevertheless they still cannot be expected to operate well in a short time because the corporations were almost bled dry by the policies of the previous government."[28]

It was anticipated that the conversion process from *Perusahaan Negara* to *Perums, Perjans* and particularly *Perseros* would require a substantial period of time. An accurate and complete investigation of each *Perusahaan Negara* was ordered in order to maximize the probability that each *Perusahaan Negara* converted to a *Persero* (State Company) would be profitable.[29] Up to the time of writing, only a few *Perusahaan Negara* have completed the multi-phase conversion process to the *Persero* form.[30] It is therefore too early to tell whether the new statutory framework regulating state enterprise will achieve the intended objectives. In this transitional period, the *Perusahaan Negara* designated to be converted into *Perseros* are essentially attempting to repair the extensive damage inflicted by the policies of the previous government. It is to be hoped that this investigation and analysis of all state enterprises, the eventual complete reorganization of state enterprises into one of three specialized categories, and in particular the

27. Elucidation of Act No. 9/1969. It has also been suggested that one of the policies underlying the legislative changes in Act No. 9/1969 was the encouragement of foreign investment. A number of joint venture corporations between foreign investors and the Indonesian government have adopted the form of *Perusahaan Perseroan.* See Hartono, Sunarjati, "Social Transnational Problems on Foreign Investment in Indonesia" (Binacipta Press, 1971), at p. 147.

28. Djojohadikusumo, Prof. Dr. Sumitro, "Policy on Trade Economy" (Kebijaksanan dibidang Ekonomi Perdagangan) (Commercial Information Institute, 1972), at p. 169.

29. Regulated by Ministerial Regulation No. 12/1969.

30. According to Ministerial Regulation No. 12/1969 the conversion process of state enterprises to *Persero* (State Company) must be drawn up in a notarial deed. According to Himawan and Mochtar Kusumaatmadja *(op. cit.,* at pp. 85-92), data as of June, 1973, indicates that from a total of 98 *Perseros* only 35 *Perseros* had completed their notarial act.

careful selection of *Perseros,* will prevent a recurrence of the failures of the past and restore the capability of Indonesian state enterprises to contribute to development.

II. *THE ROLE OF THE INDONESIAN STATE ENTERPRISES*

1. The Previous Government Policy under Law No. 19/1960

State enterprises under Act No. 19/1960 operated extensively both in the traditional public sector as well as in the private sector. Two reasons can be given for this broad involvement of the state in all areas of economic activity. First, the nationalization of all private Dutch businesses in 1958 brought under government control enterprises which were operating in all areas of industry and commerce as well as enterprises engaged in providing public services and utilities. Even the smallest private enterprises, local businesses in sales and service, were nationalized and eventually placed under the control of the regional government corporations. Second, under Act No. 19/1960, primary economic activity was reserved for the government, with private investment merely given a "participatory" role.[31] The highest priority was given to the development of state enterprise rather than private enterprise, to the point that the state enterprises had numerous monopolies in production, commerce and the distribution of goods. Furthermore government corporations were granted a type of favoured status in terms of government regulation and protection.

This policy was not a successful one. It has become clear that because of the restrictions in organizational structure placed on the *Perusahaan Negara* by Act No. 19/1960 and a combination of unfavourable political and economic conditions under the previous administration, the large majority of *Perusahaan Negara* did not develop successfully.[32] Neither the favoured status nor the monopoly rights granted *Perusahaan Negara* under Act No. 19/1960 resulted in economic gains. Instead these factors allowed them revenue sufficient for survival with little endeavour on the part of management. Private businesses were forced to deal with the *Perusahaan Negara* despite the poor service, the lengthy bureaucracy and the inevitable misuse of funds and black market activity which that entailed. This further affected the consumer through inefficient distribution of goods and price increases.

Despite any real economic success, the *Perusahaan Negara* did provide one important service in terms of the utilization of manpower. Existing data indicates that in 1965 employment opportunities were provided by *Perusahaan Negara* to approximately 1,909,000 individuals and by government banks to 220,000. In 1971 the total number of civil servants in *Perusahaan Negara* had declined to 523,359 (this does not include employees of *Perusahaan Negara* already completely converted to *Perseros* whose employees are no longer civil servants).[33] This latter

31. Elucidation of Act No. 19/1960.

32. There does exist, however, one striking example of a successful *Perusahaan Negara,* P.N. Pertamina, which is discussed at p. 322, *infra.*

33. Employment data from Dr. Awaludin, *Perbaikan Administrasi Negara Untuk Perbaikan Ekonomi,* (working paper from the K.A.M.I. Economic Symposium, June, 1968) and *B.E.K. News Bulletin,* 8 October 1971 (cited in Wirjasuputra, Aninda S. and Rieffel, Alexis, fn. 16, *supra,* at pp. 11-12).

figure still indicates a far greater number in the workforce than required. Although this surplus still necessarily diminishes efficiency, if viewed in terms of national needs, the public enterprises have significantly curtailed unemployment.

2. The Present Government Policy under Act No. 9/1969

It is clear that since 1967 there has been a slow movement away from the previous government's efforts to monopolize large areas of business enterprise. The present government policy appears to be directed at providing both public services and utilities as well as continuing to operate state enterprises in manufacturing and business sectors traditionally engaged in by private enterprise, but to attempt insofar as possible to allow and encourage competition between private and state enterprises.

This present government policy is reflected in the most recent statute on state enterprises in Indonesia. Act No. 9/1969 states that:

> the government role in the field of economics should emphasize more the supervision of the direction of economic activity rather than the control of the economic activity.[34]

This does not, however, imply a system of "centrally planned economics" where all business activity flows outward from the government, but rather a "mixed economy" where the activities of government enterprise proceed parallel with the activities of private enterprise. This viewpoint marks a significant new direction in the Indonesian government's attitude toward state enterprise. The present government policy reflected in the 1969 statutes has therefore eliminated the favoured status for government enterprise. State enterprises, either in the form of State Companies *(Persero)* or Public Corporations *(Perum),* must openly compete with their private counterparts without any special protection or priority. Tenders for government contracts are offered on the basis of the quality of work and the amount of the bid rather than government affiliation.

The government position is that state enterprises must operate in a wide diversity of areas even if there are already a sufficient number of private enterprises in those areas. The state enterprises then serve as a balancing force both to diversify the sources of national income and the government revenues[35] and to stabilize prices, a vitally important function because of Indonesia's chronic problems with rapid price fluctuations.[36] On the other hand, the government also permits

34. Elucidation of Act No. 9/1969.

35. Hanson A.H., "Organization and Administration of Public Enterprises" (Selected Papers, United Nations 1968), at p. 13.

36. It is unfortunate that in Indonesia, the *Perusahaan Negara* has not yet been able to serve as a price stabilizer. The operation of the *Perusahaan Negara.* is still inefficient, and thus frequently they are responsible for price increases. For example, P.T. Semen Gresik, during December 1973, raised its prices several times to the point where major construction work in progress was severely affected. It must be understood, however, that the *Perusahaan Negara* are still in the process of developing themselves and are therefore sometimes subject to cost squeezes. On price fixing, see "Report of the United Nations Seminar on Organization and Administration of Public Enterprises" (1967), at pp. 28 - 29.

and encourages private enterprise to operate in all areas except those which are nationally sensitive, because the competition between private and public enterprises results in greater stabilization in prices.

The creation of a more competitive atmosphere between state and private enterprises correlates as well with the government objective evident in the 1969 statutes to cast the state enterprises in the mould of private enterprises. Whereas *Perusahaan Negara* under Act No. 19/1960 possessed characteristics of both private and public entities, Act No. 9/1969 provides that those enterprises adopting the *Persero* form will possess features resembling private enterprises.[37] With the elimination of their favoured status, and the adoption of the characteristics of private enterprise many of the state enterprises have been forced to enter a competitive market. This competition has been especially difficult in marketing. According to several government officials who were formerly active in maintaining coordination between the state enterprises, this weakness in marketing is caused by a weakness within the organization of the state enterprises.[38] It is apparent that if the state enterprises had taken the opportunity while they were enjoying a favoured status to expand their markets and to improve the quality of their goods, they would not be at a disadvantage competing now with the private enterprises whose marketing experience is greater and whose marketing techniques are superior.

The present government policy is bringing about a natural selection among the numerous and largely inefficient state enterprises. Those state enterprises which are able to survive within the competitive market will continue to exist while those which cannot effectively compete will be eventually liquidated.[39] This natural selection will result not in the elimination of Indonesian government enterprises, but rather in their consolidation into a smaller but a more influential and efficient group of state enterprises.

In most fields varying degrees of involvement by private enterprise are evident. In the field of transportation, there are so many private companies operating along with the state enterprise, P.N. Damri, that Damri can no longer be considered a viable competitive force.[40] There is also heavy competition from private enterprise in insurance. Banking has similarly attracted private enterprise. Because these private banks still have weak capital structures and because foreign banks are limited in their activities, government banks presently dominate. As private banks establish their credit and reputation, however, this should become another area for strong competition. In the field of aviation, four private airlines compete with the two government carriers for domestic

37. The German term *"privatisiering"* is used by Sunarjati Hartono to describe this tendency. Hartono, Sunarjati, "Several Transnational Problems on Foreign Capital Investment in Indonesia" (Binacipta Press, June, 1971), at p. 148.

38. From authors' interviews with officials of several regional enterprises in East Java in January 1974.

39. At present, some Indonesian state enterprises whose financial position is critical are being consolidated by mergers or managed by holding companies. For example, P.T. Boma-Indra (metal work) and P.T. Dwikora (plantations).

40. P.N. Damri's present status is still as *Perusahaan Negara;* a decision is pending on its possible conversion to a *Persero* or a *Perum.*

passengers. However, generally industries which require large capital investment (such as fertilizer, cement, etc.) have not yet been able to attract either domestic or foreign private investors.[41]

Enterprises involving national welfare or national security, such as electricity, telephone, railways, and shipping, are certain to remain under dominant government control for the foreseeable future.[42] Private ownership of shares in these enterprises will be prohibited although there are opportunities for domestic and foreign private enterprises to co-operate with the Indonesian government on a work contract or production sharing contract.[43]

3. Pioneer Enterprise Policy

The government policy of encouraging and developing new private enterprise manifests itself also in the new policy on pioneer enterprises. Although the basic purpose of State Companies *(Persero)* is to obtain profits, the government also places considerable importance in reality on the creation of pioneer enterprises.[44]

These pioneer enterprises are intended to initiate economic activity in areas beneficial to national development. When the business has been successfully established, shares will gradually be sold to private investors. Two companies can be mentioned as examples of pioneer enterprises: P.T. Bahana which operates in the field of money and capital marketing and P. T. Askerindo in credit insurance. This new government policy has been explained by Amirul Jusuf, the Managing Director of P.T. Aneka Gas Industry, as follows: the government will release its possession of such state companies in the future through capital exchange. The money obtained from such a sale would be reinvested

41. It is possible that foreign investors have sought to enter these industries but the government has not yet permitted their involvement; data indicating these possibilities is unavailable.

42. Article 6(1) and (2) of the Foreign Investment Act, Act No. 1/1967, provides that the following fields of activity are closed to foreign capital investment:
    a. harbours
    b. electric power
    c. telecommunication
    d. shipping
    e. aviation
    f. drinking water
    g. public railways
    h. atomic energy
    i. mass media.

    Industries performing vital functions for national defence are also closed. Article 7 of the same Act delegates authority to the government to determine other spheres of activity which should be closed to foreign investment.

43. Art. 8(1) and (2), Act No. 1/1967. See pp.329, *et seq. infra.*

44. Authors' interview with several officials of the *Persero Directorate*, Department of Finance, in December, 1973.

to develop other industries.[45] It appears the major constraint hindering the effective implementation of the pioneer enterprise policy is the present lack of capacity among private entrepreneurs to invest in the state enterprises, possibly because the risk is too great or the necessary capital too high.

The government's interest in involving private investors in present government enterprises and developing private enterprise has also had an impact on both the *Perusahaan Negara* and the regional government enterprises. Since 1967 a number of previously nationalized business enterprises have been returned to their original owners; in addition a number of regional government enterprises have been liquidated and there has been discussion about selling others.[46]

III. *CHARACTERISTICS OF STATE ENTERPRISE IN INDONESIA*

1. Separate Legal Personality and the Structure of State Enterprise under Law No. 19/1960

Friedmann and Garner have written in their recent book *Government Enterprise* that:

> Separate legal personality is an almost indispensable aspect of the public corporation. In order to operate with the necessary degree of independence it needs the attributes which go with legal personality. The great majority of public corporations are specifically and expressly equipped with such personality in all the countries under study.[47]

Separate legal personality and the qualities of legal entities fall within the general subject of private law under the Civil Code.[48] A legal entity by its nature under the civil law has the right to own property and to act in its individual capacity, to contract, to sue and be sued, and

45. Taken from an interview quoted in the daily newspaper *Merdeka*, 10 September, 1973. This policy has also been adopted in other countries: "… in some countries the view has been often expressed that although it is legitimate for the state to pioneer industries in which private entrepreneurs and investors show little initial interest, it should sell out the newly created assets as soon as they are producing a yield large enough to make them financially attractive … a policy which has been pursued with considerable success in some of these countries (e.g. Pakistan) and with little success in others (e.g. Chile)." Hanson, A.R., *supra* (fn. 35), at p. 5.

46. Several examples of nationalized enterprises returned to the original owners are P.T. Dwi Kora Balikpapan (rubber plantation); Maclaine Watson & Co. N.V. (Tobacco, Rubber, Sugar and Coffee Plantation) and Oey Tiong Ham Concern (Sugar Production).

47. Friedmann, W.G. and Garner, J.F., *Government Enterprise* (Columbia University Press 1970), p. 314.

48. Van Praag, Prof. Mr. Ir., *Algemene Nederlandsche Administratierecht* (General Dutch Administrative Law) (1950), p. 187. Prof. Van Praag writes that in modern Dutch law a legal entity means a legal personality which is not a natural person and is created for a specific purpose. Legal entities include both private bodies (limited liability company, limited partnership, *Commanditaire Vennootschap*, etc.) and public bodies. Both civil law and public law entities are subject to the civil law unless the positive law otherwise provides; exception to the application of civil law is usually made for public bodies acting in the public welfare. The logical consequence of Prof. Van Praag's conclusion is that acts of public enterprises in Indonesia are governed by the civil law unless excepted by statute.

to exercise the other rights and powers given to it by the state. The liability of a legal entity under the private law extends only to the property invested in the entity.[49] Therefore where a government enterprise has the status of a separate legal entity, it is clear under the private law that such an enterprise may own property and act in its corporate capacity separate from the government.

Status of a separate legal entity, however, appears to be only one of several significant factors contributing to the performance of public enterprise. This issue was considered by the Geneva Seminar on the Organization and Administration of Public Enterprise, which concluded:

> There is indeed no discoverable correlation between the legal rights and obligations of a public enterprise and the quality of performance which it achieves. For more important determinants are the quality and experience of management, the ability of management to resist improper pressures from whatever quarter they may come, the determination of management to achieve the purposes of the enterprises, and the readiness of superior authorities to recognize that there is a sphere of autonomy the invasion of which usually brings untoward and undesired consequences.[50]

The organization structure and procedures of government institutions generally are clearly not suitable for state enterprises. The report of the Geneva Seminar states that:

> For instance, if the law prescribes that the budgetary and accounting methods of the enterprise shall be the same as those used in governments or that its staff shall be subject to the normal civil service regulations, it is unlikely that even the most able management will produce good results....
>
> It is generally recognized today, therefore, that an enterprise needs not only a separate and distinct legal personality, but also the authority to devise its own budgetary and accounting procedures in accordance with well established (or, sometimes, newly established) commercial principles and to frame and apply its own personnel regulations.[51]

There were several important provisions bearing on these issues in the earlier legislation dealing with *Perusahaan Negara*.

First, with regard to their status as separate legal entities, it was clearly stated in Act No. 19/1960 that *Perusahaan Negara* were *badan hukum* or legal entities.[52] The Elucidation of Act No. 19/1960 suggested that as separate legal entities, state enterprises could accept property conveyed by the government as investment capital and the transferred property would not be reflected on the government's accounts. Furthermore, as separate entities, *Perusahaan Negara* had to be self sustaining and could no longer burden the government budget.

Although the status of state enterprises as legal entities was clear from the provisions of Act No. 19/1960, it was not clear whether state

49. See Friedmann and Garner, *Government Enterprise*, at p. 315; Paton, G.W., *A Text-book of Jurisprudence* (1955), at p. 315; Pezen, Robert C., "Public corporations in Ghana", Yale Studies in Law and Modernization No. 5 (1972), at p. 802.

50. "Report of the United Nations Seminar on Organisation and Administration of Public Enterprise" (1967), at p. 9.

51. *Ibid*., at p. 10.

52. Art. 3(2), Act No. 19/1960. *Perusahaan Umum* or Public Corporations continue to operate subject to Act No. 19/1960.

enterprises were granted the rights and obligations of *badan privaat* or private bodies.[53] It seems however that the organization and delegation of management responsibilities in the *Perusahaan Negara* were regulated generally by administrative law. The official who controlled management policy was the minister assigned responsibility for the *Perusahaan Negara* in his capacity as minister. All state enterprise personnel were considered subject to the regulations concerning civil servants generally.[54]

Although in Law No. 19/1960 it was not clearly delineated whether the civil law or the public law governed relationships between *Perusahaan Negara* and non-governmental third parties, it appears from the above analysis that under Act No. 19/1960 state enterprises were *badan publik* or public bodies. They were created as separate legal entities only in order that the government treasury could not be accountable for the private law acts of the *Perusahaan Negara*.

The legal status of *Perusahaan Negara* under Act No. 19/1960 was comparable to the French *"etablissement public administratif"* or the German *"Offentliche Anstalt"*, which have the following characteristics:

> The institution is subject to the supervision of the competent administrative authority; its staff generally has the status of the Civil Service; its relations with third parties, e.g. with the users of the public utilities provided by these institutions, such as water, gas and electricity, are usually governed by public rather than private law, and consequently disputes generally come before administrative rather than civil courts.[55]

Thus in instances where transactions with third parties are not directly related to the protection of the public interest but rather more concerned with activities normally within the sphere of private law, e.g. relations with suppliers of goods and services, the civil law would govern.

Second, with regard to management policy, it appears that under Act No. 19/1960 there were two general approaches to management and management policy in state enterprise.

1) Government enterprises could be managed by a board of directors [56] which determined operational policy and represented the corporation in all matters,[57] or, in the alternative,

2) a type of general management board could be established by government regulations within the appropriate government ministry. Basically this type of board seeks to coordinate the management of the government corporations under the direction of that ministry. In some instances, the general management board was given responsibility not only for the coordination of

53. See fn. 48, *supra*.

54. See Elucidation of Article 1(1), Act No. 18/1961 and p. 326, *infra*.

55. Friedmann, W.G., *Government (Public) Enterprises (1967)*, Part I, section VI, at p. 17.

56. Art. 7, Act No. 19/1960.

57. Art. 10, Act No. 19/1960.

government enterprises but also for the general operating management of each of the government corporations within the ministry.[58]

Act No. 19/1960 required that at the beginning of each fiscal year, the board of directors had to secure the responsible Minister's approval of the corporation's projected annual budget.[59] The board remained accountable to the Minister for the management of the corporation.[60] The Financial Control Board and the State Accountant Service had the responsibility of verifying the accountability of the board.[61] In the event a general management board at the ministry level was delegated the authority both to coordinate and to manage the ministry's enterprises, the general management board was held to the same standard of accountability as discussed above.[62] The statutes provided also that each Minister had both to exercise supervision over the state corporations in their respective ministries, as well as to ensure that all corporate activity reflected state economic policy.[63] The power to appoint and discharge directors was delegated to the President.[64]

Under Act No. 19/1960, it should also be noted that the capital of a *Perusahaan Negara* cannot be divided into shares. This prohibition was designed to "prevent the existence of participation"; in other words to prevent the creation of any joint enterprises based on shares divided between the government and other parties which might dilate government control and management.[65]

2. Forms outside Act No. 19/1960

It is essential to examine the operational impact of Act No. 19/1960 in order to understand the present structure of Indonesian public enterprise under Act No. 9/1969. Although after its promulgation, Act No. 19/1960 was supposed to govern the activity of all public enterprises, in actual practice not all government enterprises operated subject to this law.

Four examples can be cited:

A. Neither Act No. 19/1960 nor Act No. 9/1969 were or are applicable to government banking enterprises, which operate subject to special regulations.[66]

58. Wirjasuputra, Aninda and Rieffel, Alexies, *supra* (fn. 16), at p. 9; Himawan, Charles and Kusumaatmadja, Mochtar, *supra* (fn. 6), at p. 7; Fabrikant, Robert, *Oil Discovery and Technical Change in Southeast Asia* — Field Report Series No. 4 (1973).

59. Art. 15, Act No. 19/1960.

60. Art. 17, Act No. 19/1960.

61. Art. 25. Act No. 19/1960.

62. Art. 24, Act No. 19/1960.

63. Elucidation of Act No. 19/1960.

64. Arts. 7 and 8, Act No. 19/1960.

65. Art. 6 and Elucidation on this Article, Act No. 19/1960.

66. Acts Nos. 13 thru 22/1968.

B. Similarly *Perusahaan Negara Pertamina* (the National Oil and Gas Mining Enterprise) is regulated exclusively by two special statutes, Government Regulations No. 27/1968 and Act No. 8/1971.[67]

C. Although *Yayasan* or foundations in Indonesia, frequently engage in operations similar in nature to those performed by government corporations,[68] foundations have never been regulated by statute, but rather operate as corporate entities under the customary and case law. A substantial number of foundations have been created by national and regional governments with government officials in policy-making trustee positions. Such foundations are primarily created by government agencies to collect money from voluntary sources. By forming a foundation to manage these donations, government agencies can use the funds more flexibly to achieve the foundations' objectives and avoid restrictions placed on public funds.[69]

Although these three types of enterprise were essentially owned and controlled by the government and therefore fell within the rubric of Act No. 19/1960, their operations were not regulated by this Act for several different reasons. Because of the size, complexity and uniqueness of government corporations operating in oil extraction and banking, it was necessary to tailor specialized regulations for those fields. Act No. 19/1960 was difficult to apply to foundations because the creation and operation of these institutions had not been previously regulated by the statutory law. Moreover, those foundations were created as an unconventional solution to the financial difficulties faced by government institutions in the period preceding the promulgation of Act No. 19/1960 when the demands made upon the government budget substantially exceeded available revenues. As Indonesian development proceeds, both the role and the number of these foundations are becoming less significant.

D. There exists also a fourth and very significant exception from Act No. 19/1960. Regional governments in Indonesia own numerous *"Perusahaan Daerah"* or regional corporations, in 1968 totalling 1,635 enterprises,[70] which are also governed by a special statute, Act No. 5/1962, and are not subject to Act No. 19/1960 or Act No. 9/1969. All regional corporations were in fact originally *Perusahaan Negara* which later were reorganized under local government ownership.[71] The large majority of these regional corporations were originally Dutch corporations,

67. See p. 322, *infra*.

68. *E.g.* Copra Foundation, Rubber Foundation, Prapanca Printing Foundation, See Himawan, Charles, and Kusumaatmadja, Mochtar, *supra* (fn. 6), at p. 77. A foundation under Indonesian law is an endowed institution without shares created for a specific purpose.

69. In the Netherlands foundations are sometimes used for similar purposes to carry out functions of public institutions; for example the province Utrecht established *"Stichting Drinkwater-leiding West Utrecht"* (meaning the Utrecht Water Foundation). Vollmar. Prof. Dr. R.F.A., *"Vennootschappen Vereningen on Stichtingen"* Book 1, Part III (1969). See also Himawan, Charles, and Kusumaatmadja, Mochtar, *supra*, at p. 77; Soemitro, Rochmat, *Dasar*[2] *Hukum Padjak dan Padjak Pendapatan* (1965), at p. 13.

70. Wirjasuputra, Aninda, and Rieffel, Alexis, *supra* (fn. 16), at p. 31.

71. Prime Minister Regulation No. 188/PM/1964, December 14, 1964.

primarily shops and service establishments, nationalized by the central government and then transferred to regional governments in pursuance of the national government's policy of encouraging regional autonomy in finances.[73] The profits of these regional corporations were anticipated to be sources of revenue for local governments.[74] It has been further suggested that the transfer of certain *Perusahaan Negara* to the regional governments was intended to increase the efficiency of these corporations by placing them under the more direct supervision of the region within the corporation operated.[75]

Act No. 5/1962, the special statute for regional enterprise, follows closely the model of Act No. 19/1960 governing *Perusahaan* generally[76] with two variations which indicate some moderate changes. First, the statutes regulating regional operations make no provision for general management boards; the board of directors of each enterprise is appointed by and accountable directly to the governor of each region. Second, unlike *Perusahaan Negara* under Act No. 19/1960, regional corporations are not prohibited from issuing shares or forming joint enterprises with domestic private parties.[77] This change in policy was intended to encourage more efficient combinations of financial and human resources in the society.[78]

It seems that this sanction of shares and joint enterprise for regional corporations was the first tentative step in the government economic policy change towards a mixed economy from the policy of a centrally planned economy that was followed in the late 1950's and early 1960's. It should be noted that if a regional corporation issues shares or forms joint enterprises, the capital of the corporation or joint enterprise must be divided into both common shares and "priority shares". The latter can only be issued to and held by the regional government.[79]

The consequences of this differentation in shares are not clearly defined in the statute. However it would appear that the major distinction between common and priority shares lies in the fact that it is the regional governor who controls the boards of directors of all regional enterprises and to whom the boards are accountable. Private parties holding common shares may submit their opinions for the consideration of the governor.[80] Statements of accountability from regional corpora-

72. The types of *Perusahaan Negara* converted to regional corporations are listed in Supplement A of the "Official Report on the Transfer of *Perusahaan Negara*". Ministry of Internal Affairs, December 15, 1964.

73. See the Consideration of Act No. 5/1962 and Elucidation of Article 18, Constitution of 1945.

74. See Art. 25(2), Act No. 5/1962: 55% of the profits of regional enterprises must be allocated as a contribution to the regional government.

75. Wirjasuputra, Aninda, and Rieffel, Alexis, *supra* (fn. 16), at p. 31.

76. *Compare* Act No. 5/1962 *with* Act No. 19/1960. The provisions relating to objectives, organization, capital and budgeting are almost identical.

77. Art. 7, Act No. 5/1962, provided that such private parties must be Indonesian citizens or Indonesian legal entities with all Indonesian shareholders.

78. Elucidation of Act No. 5/1962.

79. Art. 8, Act No. 5/1962.

80. Art. 10(2b) and Elucidation on this Article, Act No. 5/1962.

tions must also be rendered to the regional legislative body.[81] However it is the governor, after obtaining advisory opinions from any private shareholders and if needed from the regional legislative body, who determines all policies relating to regional corporations, who has authority to appoint and remove directors.[82]

3. Statutory Changes in 1969

From the foregoing, it should be clear that prior to 1969 there existed fundamentally only one type of state enterprise, the *Perusahaan Negara;* regional enterprises were also modelled essentially on this pattern. Modification of the state enterprise structure was initially considered in 1967, and a presidential instruction[83] was issued both outlining several important features of the new arrangement of state enterprises and directing preparations to be initiated.[84] New legislation was also planned for regional enterprises but up to the time of writing, the task of drafting such legislation remains unfinished.

The statute approved in 1969 is unfortunately not well drafted, and does not clearly set forth precise definitions of the three types of enterprise created.[85] The statute provides only as follows:

1) A *Perjan* (Departmental Agency) is a state enterprise established and regulated by the Indonesian Enterprises Law *[Indonesiche Bedrijvenwet* (abbreviated I.B.W.) Official Gazette 1927: 419, as revised and supplemented].

2) A *Perum* (Public Corporation) is a state enterprise established and regulated according to the provisions of Act No. 19/1960.

3) A *Persero* (State Company) is the participation of the state in a limited company as regulated according to the provisions stipulated in the Commercial Law (Wet Boek van Koophandel, 0-G. 1847:23, as revised and supplemented).

The 1969 statute itself thus contains no definitions but indicates only which statutes are applicable to each of the three types of enterprise created.[86] The 1969 legislation did to some degree define the characteristics that were determinative in the classification of existing state enterprises. The Elucidation of the statute explains that state

81. Art. 10(2), Act No. 5/1962.

82. Art. 24, Act No. 5/1962.

83. Instruction of the President No. 17, December 28, 1967.

84. This Instruction prescribed the division of *Perusahaan Negara*, into 3 types of enterprise, "Departmental Agencies" or *Perjan,* "Public Corporation" or *Perum*, and "State Company" or *Persero*. The Instruction also contained criteria for classification of *Perusahaan Negara* based on operational fields, but after Act No. 9/1969 was promulgated this Instruction — especially the criteria based on operational fields — was never mentioned again.

85. Art. 2, Act No. 9/1969.

86. It appears the intent of this statutory scheme was to return to the statutory structure before Act No. 19/1960. Before 1958, there only existed enterprises which were subject to the I.B.W. and I.C.W. and private Dutch enterprises subject to the Indonesian Commercial Code which were nationalized.

enterprises operating under Act No. 19/1960 at the time Act No. 9/1969 became operative would be converted into one of the three new types of state enterprise as follows:

1) State Enterprise which had been established on the basis of and/or which had been subject to the provisions of the *Indonesiche Bedrijevenwet* (I.B.W.; O.G. 1927:419) shall be converted into the *Perjan* (Departmental Agency);

2) State Enterprise which had been established on the basis of and/or which had been subject to the provisions of the Commercial Code (Wet Boek van Koophandel, O.G. 1847:23) shall be converted into the *Persero* form (State Companies);

3) Whereas State Enterprise having such form which is not converted into a *Perjan* or *Persero,* shall have the form to be called *Perum* (Public Corporation).[87]

4. Characteristics of the Perjan (Departmental Agency).

One of the results of Act No. 9/1969 is that enterprises originally subject to the *Indonesiche Bedrijivenwet* (I.B.W. or Indonesian Enterprises Law) which subsequently operated subject to Act No. 19/1960 were once again regulated by the I.B.W. This is in fact the sole criterion to be met for conversion of a *Perusahaan Negara* to a *Perjan*. There were only a few state enterprises, approximately twenty, that in fact operated as government corporations under the I.B.W. prior to the nationalization of Dutch private enterprise in 1958. All of these I.B.W. enterprises and the newly nationalized enterprises were subsequently reorganized under Law No. 19/1960. Therefore the number of *Perusahaan Negara* which presently satisfy the statutory conditions for conversion to a *Perjan* is small. Those *Perusahaan Negara* originally regulated by the I.B.W. now being converted to *Perjans* share several common characteristics:

1) *Perjans* (former I.B.W. enterprises) almost without exception provide public services or commodities which the government considers vital for the public welfare and seeks to provide *(a)* because the service or commodity can be more efficiently provided by a government monopoly, or *(b)* because the capital investment required is larger than that which private enterprise is able or willing to provide.

2) The nature and importance of the public services and commodities to be provided necessitate the use of protective measures and government subsidies if necessary.

As enterprises regulated by the I.B.W., *Perjans* operate essentially as government institutions for internal purposes but are generally considered to be subject to public law for purposes of contractual or other

87. Elucidation of Act No. 9/1969: "*Perusahaan Negara* (state enterprises) which are not turned either into *Perjan* (Departmental Agencies) or Persero (State Company) will automatically become *Perum* (Public Corporation)." See Himawan, Charles and Kusumaatmadja, Mochtar *supra* (fn. 6), at p. 80, and "The Statutes Concerning the 3 Forms of Government Enterprises" *supra.* (fn. 4), at p. x.

relations with non-governmental third parties, which are related to the protection of the public interest.[88] Because *Perjans* are considered to be administrative subdivisions of the government, all relationships between *Perjans* and other government institutions, including the ministry under which the *Perjan* operates, are regulated by administrative law.[89]

If the legislation creating or regulating a *Perjan* so provides, a *Perjan* may be regarded as a private enterprise in any involvement in contract or tort with non-governmental third parties and therefore subject to the private civil law.[90] One scholar, van Praag,[91] has stated that this type of enterprise is on the border between public and private law. The contractual relationships between such an enterprise and non-governmental third parties could be called "public law contracts."[92] In the absence of specific legislative provision for the application of the private law, transactions between *Perjans* and nongovernmental third parties will be regulated by the public law.

The income and expenses from all *Perjans* are also incorporated into the government's budget.[93] In view of these accounting procedures, it is clear that an I.B.W. enterprise is not a separate legal entity and has no separate corporate property.[94] In practical reality, however, *Perjan* enterprises must be self-supporting and not a burden on the government budget, and sometimes employ cost accounting procedures similar to those adopted by private enterprise.[95]

Act No. 9/1969 does not clearly stipulate how the conversion from *Perusahaan Negara* to *Perjan* is to occur. Some scholarly authority maintains that a presidential decree must be issued directing the liquidation of the *Perusahaan Negara* and the establishment of a *Perjan*.[96]

88. See van Praag, *supra* (fn. 48), at p. 203; "The Statutes Concerning the 3 Forms of Government Enterprise, *supra* (fn. 4), at p. VIII.

89. Art. 3, I.B.W.

90. For example, see Art. 2 of the Regulation for Train Transportation *(Bepalingen Vervoor Spoorwegen* — abbreviated B.V.S.) S.G. No. 262/1927. The operations of the state railroad enterprise are subject to the provisions of the Commercial Code, unless otherwise provided by special exception in the B.V.S. In case of negligence, Art. 3, B.V.S., provides that the state railroad enterprise has to pay compensation. See Seokardono, Prof. R., *supra* (fn. 7), Vol. II, at p. 203.

91. Van Praag, *supra* (fn. 48), at p. 126.

92. See also Friedmann, *Governmental (Public) Enterprises*, *supra* (fn. 55), at p. 34. "The French legal development (of public enterprise) . . . often created remedies for the citizen exceeding those that he would have in parallel private law situations".

93. Art. 1, I.B.W. Indeed a separate special entry in the national budget is made to disclose operating losses of any *Perjan* for which the government must compensate. Such subsidies are considered loans to the *Perjan* on which interest is charged.

94. "The Statutes Concerning the 3 Forms of Government Enterprises," *supra*.

95. See Himawan, Charles and Kusumaatmadja, Mochtar, *supra* (fn. 6), at p. 77: "In some cases the I.B.W. opened the possibility for ordinary (commercial) cost accounting with regard to the need for re-investment in the enterprise itself".

96. Aninda S. Wirjasuputra and Alexis Rieffel, *supra* (fn. 16), at p. 15.

In some instances this has occurred,[97] but contrary authority also maintains that those enterprises originally operating subject to the I.B.W. are automatically converted to the *Perjan* form.[98] Under Act No. 9/1969 a *Perusahaan Negara* not formerly subject to the I.B.W. cannot be converted to a *Perjan;* separate authorizing legislation would be necessary.

5. The Characteristics of a Persero (State Company)

(a) Definition

A Persero is in fact only a limited company which is wholly or partially owned by the government.[99] The law applicable to *Perseros* in any relationship with third parties is precisely the same as that applicable to ordinary limited companies. No special exceptions exist. Those statutes and regulations relating to the government policy on the purchase, ownership, and voting of *Persero* shares are only for internal government administrative purposes and do not affect the *Persero* other than through two voting of *Persero* shares.

The statutes authorize the Indonesian government to participate in business activities through any limited company:

1) the shares of which are wholly owned or controlled by the government; or
2) the shares of which are only partly owned or controlled by the government, the remainder of the shares being held by either Indonesian or foreign private parties.[1] The government is empowered by statute to invest jointly with private parties in any limited company, whether pre-existing or established by the government.[2]

(b) Conversion Procedure

In brief summary, *Perseros* are those state enterprises which originally were established as limited companies subject to the Commercial Code and subsequently became *Perusahaan Negara* under Act No. 19/1960. Under Act No. 9/1969 these enterprises again revert to the limited company form with government ownership of shares. The conversion does not occur directly and automatically. Before any *Perusahaan Negara* can be converted to a *Persero*, certain conditions must be fulfilled.

97. P.N. Pelabuhan (port operations) has been converted to *Perjan Pelabuhan* under the Ministry of Communications (Government Regulation No. 18 of 1969) and P.N. Pegadaian (Auction Management), to *Perjan Pegadaian* under the Ministry of Finance (Government Regulations No. 7 of 1969).

98. See the Preface to "The Statutes concerning the 3 Forms of Government Enterprise," *supra* (fn. 4).

99. In Indonesia, the limited company is a *"Persekutuan Terbates"* (abbreviated P.T.) which in Dutch was called a *"Naamloze Vennootschap"* (abbreviated N.V.). The structure of the P.T. operating subject to the Indonesia Commercial Code is generally similar to that of the limited company known in the Common Law, and also to the *"societe anonyme"* in France or *"Aktion Gesellschaft"* in Germany.

1. For comparison, see Friedmann, *Government (Public) Enterprises*, Part I, section VII, at p. 21.

2. Elucidation of Art. 1, Government Regulation No. 12/1969.

a) The conversion must be prescribed by government regulations.[3]

b) The corporation must be performing well and the relation among the factors of production must be in a rational proportion.[4]

c) The government chartered accountant must audit the corporate accounts; it must be evident from the audit that there exist no outstanding debts to the government and that there is a high probability the corporate business will continue to develop.[5]

The Finance Minister has been delegated the responsibility of determining both whether a contemplated *Persero* would be profitable and whether it should be established, and for drafting a government regulation establishing the new *Persero*.[6] Because the purchase of the shares of a *Persero* involves government funds and property, the conversion of any *Perusahaan Negara* to a *Persero* must be first directed by a government regulation which asserts the government's financial interest and gives guidance to the Finance Minister in establishing the limited company.[8]

After a government regulation is issued establishing a new *Persero,* the procedure for incorporation of a *Persero* is exactly the same as that provided by the commercial law for the incorporation of a limited company.[9]

a) All the incorporators must acknowledge their desire to establish a limited company before a Notary.[10]

b) The Articles of Incorporation of the limited company must set forth the following information:

1) the object or business of the corporation;

3. Art. 3, Act No. 9/1969 and Art. 2(1), Government Regulations No. 12/1969.

4. Art. 9, Government Regulations No. 12/1969.

5. *Ibid.*

6. Elucidation on Government Regulation No. 12/1969. Cf. Hanson, A. H., *supra* (fn. 35), at p. 16: "On the other hand, the creation of public enterprise in some (African) countries has been preceded by careful investigations including cost and benefits calculation. A clear example of this is the Uganda Development Corporation, whose Development Division is responsible for investigating and making recommendations on all new projects to be established by the Corporation itself or in association with private interest . . . The policy of the Corporation as a commercial concern is to embark on a new project only when its investigations have proved that the project would be technically, financially and economically viable." These steps have been also taken by the Indonesian government; for example Presidential Decision No. 64/1969 creates and appoints the Team for the Alteration from the *Perusahaan Negara*, into *Persero* (State Company).

7. The Government wanted to ensure also that *Perseros* would not be created solely by ministerial decision; a government regulation requires the approval of the Cabinet as well.

8. Art. 3(3), Act No. 9/1969; Art. 2, Government Regulation No. 12/1969.

9. Art. 4, Government Regulation No. 12/1969.

10. Art. 5, Government Regulation No. 12/1969.

2) the total authorized capital stock, priority and common, the number of shares, with their value, and the names and addresses of the subscribers to the capital stock, and the amount subscribed;

3) management structure — Indonesian limited companies may be managed solely by *Direksi* (managing directors) or by a combination of a *Dewan Komisaris* (board of supervisors) and managing directors;

4) procedure for appointment of the directors and their duties and powers.[11]

c) The Articles of Incorporation must be approved by the Minister of Justice.[12]

d) The Articles must be published in the *"Berita Negara"* (State Gazette) and filed with the district court where the limited company is domiciled.[13]

The Articles of Incorporation of a *Persero* are generally similar to those of ordinary limited companies in form and content. An examination of the Articles of several *Perseros* disclosed no distinctions indicating the role of the government or that the limited company was a *Persero* except those provisions setting forth the names of the incorporations and the names and addresses of subscribers to the shares and the amount subscribed. However, in the event of a *Persero* being owned also in part by private third parties, the Articles of the limited company must contain certain safeguards protecting the interests of the priority shareholder (the government).

If the capital stock of a limited company is owned in part by the government and in part by private parties, the Articles of Incorporation must provide that the authorized capital stock be divided at least into priority and common shares,[14] and the government must control all priority shares.[15] The Articles of Incorporation must also be drawn to include the following distinctions between priority and common shares which guarantee the control of priority shareholders: (1) only priority shareholders may nominate candidates for directorships *(Direksi)* or the *Dewan Komisaris;* (2) in the event the capital stock is increased, priority shareholders have a prior right to subscribe to the increased capital stock; and (3) affirmative action of the shareholders' meeting requires both a majority vote of all shareholders and a majority vote of the priority shareholders.[16]

11. As a matter of law, the Commercial Code does not require the Articles to contain all of these provisions, but they are commonly included. These provisions *must* be inserted in the Articles of *Perseros*, however (Article 2, Government Regulation No. 12/1969). For a discussion of the nature of the *Direksi* and *Dewan Komisaris*, see p. 318, *infra*.

12. Art. 36, Commercial Code.

13. Art. 38, Commercial Code.

14. Art. 7(2), Government Regulation No. 12/1969.

15. The provisions of Government Regulation No. 12/1969 set forth the minimum share of capital stock which must be owned by the state depending upon the amount of total capital stock issued.

16. Art. 9, Government Regulation No. 12/1969.

The government regulations dictate that where all shares of a limited company are held by the government, the Articles of Incorporations of the company must provide that the *Komisaris* and *Direksi* will be directly appointed by the sole shareholder (the government).[17] However, generally in practice, regardless of whether a *Persero* is wholly or partly owned by the government, there is no difference in the Articles of Incorporation. The authors' examination of several *Perseros* indicates that the Articles of wholly owned *Perseros* are generally written to accommodate without amendment any future charge in government policy which might direct the sale of part of the capital stock to private parties, and thus provide for the same procedures for the nomination and election of *Komisaris* and *Direksi* as a *Persero* partially owned by private parties.

(c) Organization and Management Structure of a Persero

The organization and management structure of a *Persero* is exactly the same as those of ordinary limited companies. The Commercial Code provides that there are three distinct groups which may participate in the management of the limited company: the shareholders, the managing directors *(Direksi)* and in some instances a special board of supervisors called a *Dewan Komisaris*,[18] The general meeting of shareholders comprises the basic governing and policy-making body and elects the *Direksi* or managing directors who are responsible for the day by day operations of the company.

The *Direksi* normally consists of several managing directors who must act by unanimous agreement. The shareholders may in the alternative delegate general managerial responsibility and authority to one of the managing directors, while the other managing directors fill subsidiary advisory and management positions. The managing director delegated this authority holds the position of President Director or Principal Director.

The *Dewan Komisaris* or board of supervisors is an institution unique to Indonesian and Dutch company law and is elected by the shareholders to represent them. Its establishment is not mandatory under the Commercial Code, but apparently it is common for the shareholders of limited companies to create one; the articles of all *Persero* enterprises do in fact provide for the establishment of a *Dewan Komisaris*. This body may serve either or both of two functions:

1) In solely a supervisory capacity, the *Komisaris* may review and examine the management decisions of the managing directors on behalf of the shareholders, granting their approval or disapproval which can be made known to the shareholders.

2) Alternatively, the Articles of Incorporation may provide that the directors have authority only to carry out normal operations, and that for specifically stated non-routine matters, the directors must first secure the approval of the *Komisaris* or board of supervisors.[19]

17. Art. 9(1), Government Regulation No. 12/1969.

18. Art. 44, Commercial Code.

19. Art. 52, Commercial Code.

Both directors and *Komisaris* (if any) are elected by and responsible ultimately to the general meeting of shareholders.[20]

(d) The Participation of the Government in Management of the Perseros

Act No. 9/1969 reflects a balance between the importance the government places on sound management and the interest of the government in maintaining its ability to defend and carry out its policies. The statute reflects an awareness that good management is most determinative in the success and profitability of *Persero* enterprises, and the statute is drafted to permit the *Perseros* to be managed as private enterprises.[21] On the other hand, because government funds are being invested, the government has preserved certain safeguards to ensure both its control over these enterprises and the implementation of government policy in the management of them, particularly in those owned in part by non-governmental third parties. These safeguards were discussed earlier in this section regarding the Articles of Incorporation.

Prior to December, 1973, the government regulations delegated to the Minister of Finance the authority to vote all shares owned by the government in *Persero* enterprises.[22] In those *Perseros* wholly owned by the government, the Finance Minister therefore appointed both the *Komisaris* and the directors. Where private parties owned a part of the capital stock of a *Persero*, the Finance Minister nominated the candidates for *Komisaris* and managing directors who were to be considered at the general meeting of shareholders. In addition, if the business operations of a *Persero* fell within the sphere of responsibility of other technical ministries, the Finance Minister had to consider their nominations on the selection of directors and *Komisaris*.[23] The technical ministries also had responsibility to supervise and advise upon the day to day technical operations of the *Perseros*.

Presidential Instruction No. 11/1973 (Dec. 8, 1973) has modified these procedures and provides that in addition to supervising and advising upon technical operations, the technical ministries will also be delegated sole authority to nominate candidates for *Komisaris* and managing directors. The Finance Minister is granted only veto authority in the selection of these candidates and can only request the technical ministries to nominate new candidates in the event of his disagreement with the candidates presented. Although theoretically the Finance Minister still votes the shares at the general meeting of shareholders, this is a mere formality. Because the *Komisaris* and directors are nominated by and are in reality representatives of the technical ministries, these ministries now control both day to day operations and the formulation of policy in the *Perseros*.

20. Art. 44, Commercial Code.

21. The statutes indicate that one of the major anticipated benefits from *Perseros* was an increase in government revenue from profits. Operational independence was considered essential and the *Persero* was thus cast in the form of a limited liability company. See Elucidation on Government Regulation No. 12/1969.

22. Art. 9, Government Regulation No. 12/1969.

23. *Ibid.*

In 1969 the original policy underlying the transfer of control of *Persero* enterprises from the technical ministries to the Finance Ministry was apparently the expectation that this would improve the financial management of the enterprises. Although no data has been published, it appears that the Finance Ministry control did not significantly improve the financial condition of the *Persero* enterprises and that the same problems of inefficiency, mismanagement and misallocation of resources were evident. In the absence of data demonstrating improved performance from better financial management, the technical ministries eventually succeeded in regaining control over the *Persero* enterprises.

It is important to note that in the nomination and appointment of directors and *Komisaris*, the government is acting not in its capacity as a government but rather in its capacity as a shareholder. The government's position is the same as that of any other subject of the private law. The government therefore ensures its control over these enterprises by holding at least a majority of all outstanding voting shares as well as all priority shares.

The government regulations relating to *Perseros* provide that individuals proposed and appointed as *Komisaris* and managing directors of *Perseros* must be professional business managers possessing both technical and managerial knowledge and skill.[24] Appointment to these positions may not be based on rank in government service or connections and influence in the government. In practical reality, this personnel policy has not yet been fully implemented; this is in part attributable to the personnel difficulties inherent in the transitional period when *Perusahaan Negara* are being converted into *Perseros*. In addition there still remains a serious shortage of skilled management personnel in Indonesia.

6. The Characteristics of a Perum (Public Corporation)

As discussed earlier, Act No. 9/1969 enumerates with some specificity the conditions which *Perusahaan Negara* must satisfy for conversion to either the *Perjan* or *Persero* form of state enterprise. Those *Perusahaan Negara* which do not fulfill the conditions required for conversion to *Perjan* or *Persero* become *Perums* (Public Corporations) and continue in that form to be regulated by Act No. 19/1960 as amended.

In order to understand the nature of the *Perum*, however, the sequence of development of Indonesian state enterprise should be borne in mind. Under Act No. 19/1960 both state enterprises existing prior to 1958 as well as Dutch private enterprises nationalized in 1958 became *Perusahaan Negara*. Only those relatively few state enterprises established prior to 1958 and regulated by the *I.B.W.* before subsequently becoming *Perusahaan Negara* are presently qualified to be converted to *Perjans* and be again regulated by the I.B.W. The vast majority of *Perusahaan Negara* under Act No. 19/1960 were nationalized Dutch private enterprises which had operated prior to 1958 under the Commercial Code; of this group, those *Perusahaan Negara* that fulfill the other conditions discussed earlier will be converted to *Persero* enterprises and will again operate subject to the Commercial Code. These con-

24. Elucidation of Government Regulation No. 12/1969.

ditions relate to the profit-making potential of the enterprise. Those residual *Perusahaan Negara* not converted into *Perjans* or *Perseros* will become *Perums* and are authorized to continue operating under Act No. 19/1960. It should therefore be evident that the classification of a *Perusahaan Negara* into one of these three organizational structures is based firstly on the statutes under which the *Perusahaan Negara* operated at its inception, and secondly on the profit-making potential of the *Perusahaan Negara*. Although the operational fields and characteristics of the state enterprises should be of significance in this classification, it is clear that no criteria relating to operational fields have been utilized in the re-classification and conversion of *Perusahaan Negara*.[25]

The underlying policy distinction between *Perseros* and the *Perjan* form of state enterprise is relatively evident. *Persero* enterprises must be capable of operating as profit-making limited companies whereas *Perjans* provide public services and utilities with greater government supervision, control and protection. The policy distinctions between *Persero* or *Perjan* enterprises and the *Perum* form of public corporation are not clearly defined and are not explained in the statutory or regulatory materials. However it appears that although some *Perums* operate in production and marketing and have not been converted to *Perseros* because of limited profit making potential,[26] the large majority of the *Perum* enterprises are providing important public services and utilities that prior to 1958 were provided by limited companies privately owned by the Dutch.

As a matter of policy, the government prefers that these public service and utility enterprises continue operating under Law No. 19/1960 as *Perums* with government supervision and control and not be converted into profit making *Perseros*. Furthermore because the *Perum* enterprises were formerly limited companies owned by the Dutch providing public services and utilities, they have the management structure and capacity to operate independently from direct government control and without subsidies. Under Act No. 9/1969 these enterprises will operate as *Perums* subject to the more flexible regulatory structure of Act No. 19/1960. On the other hand, those *Perusahaan Negara* providing public services and utilities which formerly operated as departmental agencies under the I.B.W. never developed the management structure and capacity to operate independently, and continue to require protective measures and subsidies. These enterprises have been classified as *Perjans* and are again to be regulated as governmental agencies by the I.B.W.

25. It should be noted that at present there still remain many *Perusahaan Negara* which have not yet completed the conversion to either *Persero*, *Perjan*, or *Perum*. The government appears to be considering a more cautious and methodical approach in the classification of *Perusahaan Negara.*

26. In June, 1973, there existed thirty-six *Perums*, whereas ninety-eight *Perusahaan Negara* either were in the process of conversion or had been converted to *Perseros* wholly owned by the government. See Himawan, Charles and Kusumaatmadja, Mochtar, *supra* (fn. 6), at p. 83. Nine of the thirty-six *Perums* are operating in production and marketing including paper production, cement, textiles and tires. On the other hand, twenty-one of the ninety-eight *Perseros* are operating in production and marketing again including paper production and cement: *e.g.* Semen Gersik and Semen Padang are now converted into *Perseros;* but Semen Tonasa is converted into a *Perum*, Pabrik Kertas (paper production) Basuki Rachmat and Goa have been converted into a *Perum*, but Paper Manufacture Padalarang, Blabak, and Leces have been converted into a *Persero.*

The characteristics of the *Perum* are no different from those of the *Perusahaan Negara* under Act No. 19/1960 with the exception that all supervisory bodies like the general management boards have been dissolved[27] and the supervision of the *Perums* is now directly in the hands of a minister. Executive operating control is delegated to the *Direksi* or Board of Managing Directors.[28] Although neither the statute or regulations give guidance, it appears that the conversion from *Perusahaan Negara* to *Perum* is an automatic one because the organizational structure remains precisely the same.

7. Pertamina

(a) Hybrid between a Public and a Private Entity

The situation is quite different with P.N. PERTAMINA *(Perusahaan Negara Pertambangan Minyak dan Gas Bumi Negara).* A special body of statutes[29] has been created for *Pertamina* due to its vital significance in terms both of domestic consumption and of its importance as a source of government income.[30] The *Pertamina* statutes define it as a legal entity *("badan hukum"),*[31] without making clear the exact meaning of that term. In practice, its operation is quite similar to that of a *Perusahaan Terbatas* (limited company), but in theory, the statutes regard it as a public body. Although internally *Pertamina* must conform to administrative law, externally, in its relations with third parties it can fall under the jurisdiction of civil law.[32] In this instance it is not the characteristics of the parties which make civil law applicable, but the nature of the transaction itself. If a transaction relates to the safeguarding or protection of public interest then the transaction is governed by public law. If, however, the relationship between public and private bodies is concerned with activities normally within the sphere of private law, then that transaction must be governed by civil law.[33] It becomes clear then that *Pertamina* is an amalgamation of both private and public bodies. The authors' opinion is that the term legal entity can be regarded as referring to its assets only. That is, *Pertamina's* assets are separated from the government's assets. The obligation for the payment of debts incurred by *Pertamina* is placed on *Pertamina's* own assets and can, at no point, be extended to the government's assets.

27. Presidential Instruction No. 17/1967.

28. Himawan, Charles, and Kusumaatmadja, Mochtar *supra* (fn. 6), at p. 81.

29. Regulated by Act No. 8/1971, S.G. 76/1971 and also by Government Regulation No. 72/1971, S.G. No. 94/1971.

30. Director of *Pertamina*, Dr. Ibnoe Soetowo, at a meeting of the Pacific Coast Gas Association Convention held in Honolulu in middle September (1974) said that the *Pertamina* contribution to the state budget had increased from 5% in the year 1966 to 50% in the year 1973. And he believed that in the year 1974 it would be further increased to 60% of the government's domestic revenues. The total government income from oil exports would rise from 1.2 billion dollars in 1973 to 5.5 billion in 1974. Quoted in Indonesian Daily News September 20, 1974 at p. 1.

31. Art. 2(2), Act No. 8/1971.

32. See pp. 325-6, *infra.*

33. See explanation of van Praag, *supra* (fn. 48).

(b) Its Monopoly Status, Obligations and Compensating Advantages

The statutes relating to *Pertamina* state that all mining rights for oil and natural gas have been solely entrusted to *Pertamina.*[34] It must be understood that these rights are confined to the area of mining and thus do not include ownership of the oil and natural gas.[35] *Pertamina* stands in the position of a trustee managing and controlling government resources. In order to expedite the exploitation of these oil and gas resources, *Pertamina* has a unique status in that it is allowed to enter into both work contracts and production sharing contracts with private parties.[36]

Pertamina must fulfill two obligations toward the government. First, it must supply and serve all oil and natural gas needs of the country.[37] It must be able to fill immediately all government requests for these items. Second, it must serve as a major source of government revenue. *Pertamina* is required to submit to the National Treasury the following:

a. 60% of general net operating income;

b. 60% of net operating income derived from all production sharing contracts;

c. 100% of income derived from all work contracts;

d. 60% of bonus income derived from all production sharing contracts.[38]

Due to the heavy burden these obligations placed on *Pertamina,* the government has extended certain compensating advantages. *Pertamina* is exempt from payment of all other income, import, and export taxes.[39]

(c) The Management Structure

There are three institutions which play a role in the management decisions of *Pertamina:* the Minister of Mining, whose responsibility lies in setting policy on regulation, maintenance and control; the Board of Managing Directors, including the President Director, who act as the executive directors of the enterprise; and the Government Board of Supervisors *(Dewan Komisaris Pemerintah)* which serves as an intermediary between the Minister and the Board of Managing Directors, representing the government in the supervision and implementation of the government policy.[40]

34. Art. 11(1) and (2), Act No. 8/1971.

35. Elucidation of Mining Act No. 11/1967, S.G. No. 22/1967.

36. See pp. 331-2, *infra.*

37. Art. 13(b), Act No. 8/1971.

38. Art. 14, Act No. 8/1971.

39. Art. 15, Act No. 8/1971.

40. Elucidation of Article 1, Act No. 8/1971.

The Board of Managing Directors is responsible for the management and control of the enterprise.[41] It consists of six members, one of whom serves as the President Director.[42] The board's decisions are reached by consensus. If a consensus cannot be reached by discussion, then a vote is taken; in the event of a tie, the President Director casts the deciding vote.[43] In both internal and external affairs, the operation of the enterprise is carried out by the board through the President Director.[44]

(d) The Government Board of Supervisors

The Government Board of Supervisors is comprised of ministers who are felt by the President to have an important relationship to *Pertamina's* operation. Its permanent members include: the Minister of Mining, who serves as chairman for the duration of his tenure as minister; the Minister of Finance, who serves as deputy chairman; and the Chairman of *Bapenas (Badan Perencanaan Nasional* — National Planning Board).[45] The President can also appoint, if necessary, two more ministers as council members.[46] All members, then, are appointed and discharged by the President[47] and are held responsible ultimately to the President.[48]

The responsibilities of the Government Board of Supervisors are threefold. First, it defines the broad government policy which is to be carried out by the enterprise through the Board of Managing Directors.[49] Second, it supervises the operational management of the Board of Managing Directors. Third, if necessary, it can propose to the government measures that should be taken to manage the enterprise more effectively.[50] Its impact on the management can be very direct; it is vested with the authority to discharge any members of the Board of Managing Directors if it feels their actions are detrimental to the enterprise.[51] The Government Board of Supervisors is clearly given a decisive decision-making role. Representing the views of the government, it is the controlling policy-making body, directing the implementation of that policy to the Board of Managing Directors.

41. Art. 20, Act No. 8/1971.
42. Art. 19(1), Act No. 8/1971.
43. Art. 19(6) (7) and (8), Act No. 8/1971.
44. Arts. 19(2) and 23(1), Act No. 8/1971.
45. Art. 16(3), Act No. 8/1971.
46. Art. 16(4), Act No. 8/1971.
47. Art. 16(6), Act No. 8/1971.
48. Art. 16(2), Act No. 8/1971.
49. Art. 20(l.b.), Act No. 8/1971. In some matters the Board of Managing Directors can act only after securing the approval of the Board of Government Supervisors, *e.g.* to obligate the corporation as a guarantor or surety, to borrow above a certain amount, to establish subsidiaries, or to enter into contracts in excess of certain limits. See Art. 27, Act No. 8/1971.
50. Art. 16(1), Act No. 8/1971.
51. Art. 12(4), Act No. 8/1971.

(e) The Line of Management Authority

The statutes indicate a clear line of management authority. The Board of Managing Directors is responsible to both the Minister of Mining and the Government Board of Supervisors.[52] Thus, the Minister has two means of directing management authority; first, directly, as Minister; and second, through the Government Board of Supervisors as its chairman. The Board of Managing Directors can be held responsible to other groups as well. *Pertamina* is involved in exploitation, purification, processing and sales of oil along with mining. Any other Ministry which relates to any of these fields of *Pertamina's* activity may also make requests to the Board of Directors through the Minister of Mining.[53]

This line of management authority extends even further, and the Board of Managing Directors is ultimately responsible to the President himself. This is because the board members are selected by the President and thus can be discharged by him,[54] and also because the Ministers are in fact the President's assistants and thus the President can, through his Ministers, e.g. the Government Board of Supervisors, exert influence on the Board of Managing Directors.

The *Pertamina* statutes refer to the relationship between the Minister of Mining and the Board of Managing Directors as one governed by the public law.[55] The laws governing the numerous other relationships in *Pertamina's* management structure are not enumerated. An examination of the statutes indicates however that internal relationships within *Pertamina* are governed by the public law because the structure and lines of management authority of the Board of Managing Directors of *Pertamina* more closely resemble that of a governmental administrative agency subject to public law than that of an independent autonomous corporation. This conclusion finds support in the statutes regulating *Pertamina:*

1) The members of the Board of Managing Directors are appointed by the President from the candidates nominated by the Government Board of Supervisors in consultation with the Minister of Mining.[56]

2) The Board of Managing Directors is responsible to the Government Board of Supervisors and/or the Minister of Mines[57] in the first instance and ultimately responsible directly to the President.[58]

3) The President can discharge a managing director at any time if his behaviour is contrary to the government's interest.[59]

52. Art. 19(2) and (3), Act No. 8/1971.
53. Art. 1(1), Act No. 8/1971.
54. The members of the Board of Managing Directors serve for 5 years, but may be reappointed for multiple terms (see Art. 21(1), Act No. 8/1971).
55. Elucidation of Art. 1(1), Act No. 8/1971.
56. Article 21 and Elucidation on this Article, Act No. 8/1971.
57. Arts. 19(2) and 19(3), Act No. 8/1971.
58. Conclusion of Art. 21, Act No. 8/1971.
59. Art. 21(3), Act No. 8/1971.

4) The approval of the President must be secured prior to any expansion of operations.[60]

5) The terms of production sharing contracts negotiated by *Pertamina* with domestic or foreign third parties are subject to the agreement of the President before any such contract is binding.[61]

6) *Pertamina* may issue obligations to secure necessary additional working capital only if authorized by a government regulation.[62]

These statutory provisions grant the government control over the management policy of *Pertamina.* This can be ascribed to *Pertamina's* dual function which requires it to act both as a public service in supplying all domestic fuel requirements and as a major source of government revenue by operating as a private enterprise competing in international markets.[63]

8. Status of State Enterprise Personnel

The wage scales, pensions and benefits and status of the Board of Managing Directors and the employees of Indonesian state enterprises (excepting *Perseros* and *Pertamina)* are generally determined solely by the government and stipulated in a government regulation.[64] *Perseros* on the other hand are regulated solely by the statutes applicable to limited companies generally and wage scales are determined by negotiation without government regulation. *Pertamina* is also excepted from these procedures and is authorized to set wage scales and other benefits based on the policy of the Board of Managing Directors with the approval of the Government Board of Supervisors.[65]

For the resolution of labour disputes in the private sector, which would include *Persero* enterprises, a judicatory board called the Commission for Labour Dispute Resolution *(Panitya Penyelesaian Perselisihan Perburuhan)* has been established by statute.[66] The decisions of this

60. Art. 6(2), Act No. 8/1971.

61. Subsequent to sanctioning a production sharing contract, the President must inform the Parliament. Because the contract is valid only after the President's agreement, it would appear that it is the government itself which is the party to the agreement while *Pertamina* is delegated authority to carry out its provisions.

62. Art. 10, Act No. 8/1971.

63. Elucidation of Act No. 8/1971.

64. Section 1(1a), Government Regulations No. 6/1974 and Elucidation of Presidential Instruction No. 17/1967. See Soepeno, *"Apakah Pegawai Perusahaan Negara Umum Dapat Memperoleh Pensiun Juga,"* published in daily newspaper Kompas 28 August, 1974, at p. 4. The government's role in wage determinations for state enterprises is set forth in the following statutes: for *Perums* at present, see Art. 19, Government Regulations No. 23/1967. Compensation for employees of regional enterprises is set by the regional governmnt, see Art. 26, Act No. 5/1962. *Perjan* employees are in fact civil servants because the *Perjan* is not a separate legal entity. See Elucidational Presidential Instruction No. 17/1967. The wage scales of *Perjans* and *Perums* resemble those of civil servants in general but are substantially lower than those of the private sector.

65. See Art. 21, Act No. 8/1971.

66. See Emergency Act No. 16/1951; Act No. 22/1957; Act No. 12/1964.

commission are binding on the parties. However in the event of a labour dispute between a state enterprise (other than a *Persero)* and its employees, particularly an involuntary dismissal, it appears that this commission has no jurisdiction. The regulations provide only that in the event of a labour dispute in a state enterprise, the Ministry of Manpower is to assist the parties in negotiating a satisfactory solution. In the event of a deadlock, the local representative of the Ministry of Manpower can only report it to the Minister and the dispute will be resolved at a national level by negotiations between the Minister of Manpower with the minister responsible for the operations of the involved state enterprise.[67]

9. Taxation of the State Enterprise

Prior to 1958, taxes were not assessed on the operations of the I.B.W. enterprises. Following the nationalization of the Dutch private enterprises in 1958, the government continued to exempt I.B.W. enterprises from taxation but levied the same corporate tax on the nationalized enterprises that was imposed on them as private companies before the nationalization. Subsequently when all state enterprises were incorporated into one form under Law No. 19/1960, the government simultaneously promulgated a tax code patterned after the original Dutch tax legislation for private enterprises which extended the same corporate tax to all *Perusahaan Negara.*[68] This tax code continues to be valid and all state and private enterprises, with the exception of *Perjans* and *Pertamina*, are required to pay tax on corporate profits.[69]

The possibility of relieving the state enterprises of this tax obligation has been discussed within the government. The conclusion has been that this tax is not a burden because the transfer of money occurs with the government itself; profits from a state enterprise are returned to the government which provided the original capital investment. Furthermore, there are two very positive results of the tax. First, by re-absorbing a percentage of the state enterprises profit, the government can prevent inefficient use of the profit. Second, the need to show profits can act as an incentive to work more efficiently and compete more actively with private sectors.[70]

IV. *RESTRAINTS AND SOME SUGGESTED SOLUTIONS*

1. Problems of Management and Capital

The two most pressing problems faced by Indonesian state enterprises are the lack of both working capital and skilled managerial and technical personnel. For those state enterprises, existing prior to 1967

67. See Instruction of the Minister of Manpower, No. 2/Instuuksi/67 (18 January 1967); Circular of the Ministry of Manpower to Regional Representatives No. DPSK 12/1967 (17 October 1967).

68. Corporation Tax Ordinance 1925; Art. 1, Regulation of Minister of State Collection No. P. Ps. 1-1-5 (1956).

69. See Soemitro, Prof. Rochmat, *Penuntun Perseroan Terbatas dengan Undang-Undang Pajak Perseroan* (1964), pp. 67-68.

70. Authors' interview with the director of the East Java office of the Ministry of Finance in April, 1974.

and converted into *Perums* or *Perseros*, the lack of capital has been a particularly difficult problem. Following their conversion, these corporations have had to survive basically on their existing capital without additional government capital investment. The government has basically maintained that since the inefficiency of these enterprises has already resulted in substantial financial loss, further investment cannot be justified. Those state enterprises established subsequent to 1967 have not been so severely affected because their working capital has been adequately provided for by the government by means of international loans or through the establishment of joint ventures with private foreign entrepreneurs.

It is apparent also that all of the state enterprises still lack sufficient managerial and technical personnel. There is a shortage of personnel able to manage an enterprise flexibly, to make decisions quickly and to readjust to rapidly changing situations. This weakness in personnel is most evident in competition with private enterprise. Tax officials have testified to these weaknesses from their experience in collecting taxes from state enterprises.[71] State enterprises frequently maintain that they do not have sufficient liquidity to pay the required taxes. Tax officials counter that the inability to pay taxes is largely caused by the unfamiliarity of state enterprise personnel with cost accounting principles normally used in business. There is perhaps also the psychological factor that the managers do not have a genuine feeling of responsibility toward an enterprise in which they have no vested monetary interest. This shortage of experienced and dedicated managers is largely attributable to the fact that most personnel from state enterprises are recruited from among the civil servants who frequently retain both their former position in a government office as well as the additional position in a state enterprise. Because of limited financial resources, state enterprises in Indonesia generally do not provide remuneration sufficient to command a full-time commitment from their employees.

The short run solution adopted by the government for both of these problems has been to encourage increased participation of foreign investment in state enterprises. Since 1969 joint ventures with foreign investors have in fact been a major source of capital and managerial and technical assistance for the state enterprises. This must be contrasted to the policies followed during the previous administration when the government adopted an autarchic economic policy hostile to foreign investment which resulted in severe economic disorder.

The present administration has a more pragmatic approach: that is, foreign investment can only attain a positive result if each country individually benefits from it. The foreign investor is provided with an opportunity to widen his field of operations and marketing, and Indonesia benefits through the utilization of experienced manpower and an increase in available capital. Foreign investment is perceived to be particularly advantageous for the development of state enterprises. State enterprises operating in pioneer fields which require a heavy initial investment with only long term return on capital can greatly benefit

71. Authors' interview with several East Java Tax Officials, April, 1973.

from the added capital and technology as well as the sophisticated operational and managerial techniques which foreign investment offers.[72]

The increasing number of cooperative ventures between state enterprises and foreign investors, both governmental and private, should be viewed in this framework. As previously explained, the 1960 statutes did not permit a state enterprise to divide its capital into shares, thus preventing any participation from private investors.[73] As the need for cooperation with private enterprise became apparent, the government responded with the establishment of the *Perusahaan Terbatas (Persero)* which permitted the formation of joint ventures with private enterprise, especially foreign private enterprise. In any joint venture between state enterprise and private enterprise, however, it is vital that both parties work on the same level, playing an equal role in the operation of the business. A potential danger is that the joint venture will not serve national development objectives if the private partners assume a dominant role.

Although foreign capital investment could in similar ways assist and stimulate the growth of the regional enterprises, the statutes presently prohibit the investment of foreign capital in regional corporations. As discussed previously the statutes do allow a regional enterprise to form a corporate entity in which shares can be sold to private parties, but restrictions are placed on the shareholders which exclude foreign investment. Shareholders are restricted only to Indonesian citizens or to Indonesian corporate entities whose shareholders consist entirely of Indonesian citizens or corporations.[74] Because modest investments by foreign investors in limited company joint ventures with regional public enterprises should result in benefits similar to those discussed above, the present policy prohibiting such enterprises should be reviewed and modified.

2. The Forms of Co-operative Venture

These cooperative ventures between state enterprises and private investors may take various forms, depending upon the rights and duties of the two parties involved, the nature of the joint venture, and the characteristics of the state enterprise. Four forms of cooperative venture can be identified, ranging from limited involvement to very broad involvement of the private sector: an agreement of technical assistance, an agreement of managerial assistance, a contract of work, and more recently, a contract of production sharing. The formation of a limited company, owned in part by the government and in part by private parties, offers a fifth alternative. All types of cooperative venture represent an attempt on the part of the government to alleviate the particular shortcomings of each state enterprise. Both technical and managerial assistance agreements have been common and straight forward, but the other three alternatives are more often utilized at the present time.

72. By having state enterprises enter cooperative ventures with foreign enterprises, the government is able to exert greater control over foreign capital investment.

73. Art. 6(2), Act No. 19/1960.

74. Art. 7, Act No. 5/1962.

(a) Work Contracts

A work contract can be defined as an agreement between an Indonesian state enterprise and a foreign enterprise in which specific assigned tasks are carried out by the foreign enterprise in behalf of the Indonesian state enterprise. In such an agreement the foreign enterprise generally purchases the necessary long term capital assets and is contracted to undertake all operation and management responsibilities. On the expiration of the contract, ownership of the capital assets generally is automatically transferred to the state enterprise. All end products are kept by the foreign enterprise (contractor) with the exception of a fixed monetary percentage which is taken by the Indonesian enterprise.[75] The contract usually includes a clause stating that the foreign enterprise (contractor) is obligated to train Indonesian personnel to replace gradually the foreign staff.[76] This type of work contract has been imitated by the regional government enterprises with private national enterprises instead of a foreign enterprise. With the exception of oil mining, work contracts have been in the past the most common form of joint venture in the development of Indonesian extractive industry.

(b) Co-operative Ventures in Mining

The government role in the exploitation of Indonesia's natural resources has been clearly defined in the Constitution of the Republic of Indonesia. The development of natural resources must be controlled by the government and operated by the government for the greatest benefit of its citizens.[77] Of the natural resources, the most strategic and vitally important are the mineral resources. Because of their importance it is essential that they be entirely operated by national interests, most appropriately by the state enterprises; if that is not feasible, by state enterprise in cooperation with national private enterprise, or by national private enterprise.[78]

The relevant statutes[79] have divided all mineral resources into three categories: strategic minerals, vital minerals and those remaining which do not qualify under the two previous categories.[80] The extraction of strategic and vital minerals is under the jurisdiction of the Minister of Mining, who authorizes exploitation to either a Government Agency *(Instansi Pemerintah)* or a *Perusahaan Negara.*[81] The Government

75. "The oil is still the property of the foreign oil company and the Indonesian enterprise can only share in the profit..." Fabrikant, Robert, *supra,* at p. 466. See also Hartono Soenarjati, *supra,* at p. 127.

76. Annual Report, Department of Mining, 1971, at p. 85.

77. Art. 33, 1945 Constitution.

78. Art. 5, Act No. 11/1967 (Mining Act).

79. Act No. 11/1967, S.G. No. 22/1967 and further regulated by Government Regulation No. 32/1969, S.G. No. 60/1969.

80. Art. 3, of Act No. 11/1967. This article provides that the definition of strategic and vital minerals will be further enumerated by government regulation. Non-strategic and non-vital minerals are under the control of the regional government where minerals are located (Art. 4(2), Act No. 11/1967).

81. Art. 6, Act No. 11/1967.

Agency or *Perusahaan Negara* is allowed a clear monopoly in this area. In this instance the juridical status of the *Perusahaan Negara*[82] is as a body delegated with the authority *("Memegang Kuasa")* to exploit mineral resources,[83] not in perpetuity, but for a fixed period of time upon the expiration of which an option exists to extend that authorization.[84]

If, however, there does not exist a Government Agency or *Perusahaan Negara* able to undertake a particular task, the Minister can then appoint either private national or foreign enterprise which would exploit the resources based on a work contract. Furthermore, a *Perusahaan Negara* which has already been delegated authority to exploit a specific mineral resource may itself negotiate a work contract with a private enterprise.[85] *Pertamina* is an exception to these rules and the statutes allow it to enter into contracts of production sharing.

(c) Production Sharing Contracts

The production sharing contract used by *Pertamina* is similar to a work contract in that the foreign enterprise's position is that of a contractor performing certain operations for and on behalf of the state enterprise. A significant difference lies in the rights and obligations of the two parties. These can be clearly seen by examining the production sharing contract of *P.N. Pertamina.* Here the entire supply of crude oil produced is considered the property of *Pertamina.* The contractor assumes all operating costs[86] and sustains the risk of those costs. The contract provides for both recovery of costs and profits for the contractor as follows:

> .. .Costs are recoverable out of 40% of crude oil produced per annum. If the Contractor's work expenses exceed 40%, the unrecovered excess may be recovered in succeeding years. Of the remaining 60%, the Contractor is entitled to 35% and *Pertamina*, is entitled to 65%.[87]

Another important distinction of the production sharing contract is the management clause. All contracts provide that:

> *"Pertamina* shall have and be responsible for the management of the operations contemplated" under the contract. The Contractor is responsible to *Pertamina* for the execution of such operations... "however, *Pertamina* shall assist and consult (with the Contractor) with a view to the fact that (the Contractor) is responsible for the work programme."
>
> The Contractor is required to submit annually to *Pertamina* a work programme and a budget... *Pertamina* has the right to propose revisions to

82. Or any other party with the exception of those on work contracts.

83. Arts. 1 and 2, Government Regulation No. 32/1969.

84. Art. 38, Government Regulation No. 32/1969.

85. Art. 10, Act No. 11/1967. See also the Annual Report, Department of Mining, 1971, p. 85. A work contract must be legalized by the government, including obtaining the approval of the Parliament. Before 1967, a work contract was used by state enterprises operating in oil mining, but since 1967, *Pertamina* may also enter into production sharing contracts.

86. For a discussion of items allowable as operating cost see, Robert Fabrikant, *supra,* at p. 26.

87. The percentage of sharing is variable and can be changed for each contract (Fabrikant, *supra*, p. 20).

> the work programme and the budget, and the parties are "to agree on the revisions proposed by *Pertamina*"…. Finally, the contracts uniformly provide that *Pertamina* shall have title to all original data resulting from Petroleum Operations.[88]

In the work contract, the state enterprise did not participate in any management decisions, whereas a production-sharing contract clearly provides for such participation. The latter contract with its management clause provides Indonesian personnel with an opportunity to learn management techniques through increased Indonesian participation.[89]

(d) Limited Liability Company

If an area does not involve the nation's security, another alternative remains for cooperative ventures with private enterprise. This is the limited liability company *(Persekutuan Terbatas)* in which priority shares are held by the state enterprise with common shares open to private enterprise. The government, through the relevant statutes,[90] has permitted the establishment of the *Persero*, a limited liability company, and in so doing, has provided an increasingly utilized alternative to the state enterprise.

The limited liability company can also serve as a suitable alternative to the frequently problematic work contract. Because a *Perusahaan Negara* could not divide its capital into shares,[91] the work contract came into existence as a means for foreign enterprise to provide needed capital and expertise. In a work contract the precise amount of each party's invested capital and managerial contribution is difficult to evaluate; this makes the ratio of their respective profits equally difficult to determine. With a limited liability company, profits are clearly and undisputably established in relation to the number of shares each party owns. It is therefore advantageous for the state enterprises to be formed into limited liability companies when they endeavour to cooperate with private enterprise.[92]

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88. Fabrikant, *supra*, pp. 21-22.

89. *Ibid.*, p. 31.

90. Act No. 9/1969 and Government Regulation No. 12/1969.

91. Art. 6(2) of Act No. 19/1960; and Art. 7 of Act No. 8/1971, which strictly declares that *Pertamina's* capital is not be divided into shares to prevent participation from the outside.

92. Sunaryati Hartono represents a present trend in thought regarding the *Perusahaan Terbatas*. She believes that because of the difficulties in auditing when all audits must be conducted in the Indonesian currency, a contract of work may prove to be a more effective alternative (Hartono, Sunarjati, *supra,* at p. 138). She agrees with the viewpoint of Ewell E. Murphy: "It is usually far more satisfactory to structure the project into two units, each fully owned by a partner and each producing net proceeds in proportion to that partner's contribution. This enables each partner to run his own operation as he sees fit, withdrawing or retaining dividends as he pleases. The necessary interparty controls can be satisfied by giving the locally owned unit the more prominent role" (Murphy, Ewell E. Jr., "Structuring International Business," South Western Legal Foundation Dallas Symposium (1966), p. 48.)

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