

FDI Feature Interview

23 July 2020

Indonesia in 2020 and Beyond: Bill Sullivan

Part One: Australia, Legal System, IA-CEPA, Mining and Resources

Key Points

- The Australia-Indonesia relationship will inevitably include rocky patches and may never be truly close, but there are enough incentives for both countries to enjoy a productive working relationship.
- Indonesia wants two main things from its trading relationship with Australia: market access to Australia for Indonesian products (particularly agricultural products), and greater Australian investment in Indonesia.
- The Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA) will be successful in terms of promoting greater trade, but the refusal of Indonesia to allow traditional international arbitration for investor state-focused disputes to be included in IA-CEPA's dispute resolution provisions is a serious limitation.
- The principal challenge faced by all foreign investors and businesses in Indonesia is the opaque and non-transparent nature of the Indonesian legal and court systems that are inherently difficult for foreigners to deal with.
- The fifty-one per cent divestiture requirement remains part of the regulatory environment for mining projects in Indonesia. It will continue to be a major impediment to foreign investment in the resources sector.

Introduction

In this two-part Feature Interview, FDI speaks with Bill Sullivan about the challenges and opportunities confronting Indonesia now and into the near future.

Mr Sullivan specialises in advising foreign investors on the legal, policy and regulatory aspects of construction, energy, mining and oil and gas projects in Indonesia and elsewhere in South-East Asia. A leading expert on Indonesian mining law and regulation, Mr Sullivan is currently Senior Foreign Counsel with Christian Teo & Partners in Jakarta and has lived and worked in Indonesia for more than 20 years.

Christian Teo & Partners operates in close association with international law firm Stephenson Harwood LLP, which has nine offices throughout Europe, the Middle East and Asia. Mr Sullivan is a Senior Adviser to Stephenson Harwood LLP.

In Part One, we examine the Australia-Indonesia relationship, the opportunities and challenges for businesses looking to operate in Indonesia, the Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA) and the status of the Indonesian mining and resources sector.

In [Part Two](#), the potential implications for Indonesia of the Covid-19 pandemic will be explored, before moving on to the realm of international relations to discuss the relationships of Indonesia with China, the United States, Russia and India. We conclude by taking a look ahead, towards the next presidential election, due to be held in 2024.

Commentary

FDI: *Thanks for speaking with FDI today, Bill. Let's begin with a look at the Australia-Indonesia relationship. In your view, what is the outlook for the relationship as it currently stands?*

BS: My assessment of the outlook for the Australia-Indonesia relationship is cautiously optimistic, but also overlaid with a healthy dose of realism. We have to accept that Indonesia and Australia are so different in terms of their political systems, their histories, cultures, religious underpinnings, and their colonial experiences, that it is never likely, in reality, that we're ever going to have a truly close relationship with Indonesia in the same way in which we might have a close relationship with other Commonwealth countries, or with the United States, or some European countries. It's always going to be a relationship that, in a sense, staggers from one misunderstanding to another. Now, that's just the reality; it does not mean that the relationship can't still be very successful, but it does mean that we have to be realistic as to what that relationship will be and how it will work.

I see many parallels between Australia's relationship with Indonesia and Australia's relationship with China, which, as we know, has hit a very rocky patch recently. That rockiness in the Australia-China relationship is undoubtedly driven to a very large degree by different values and completely different perceptions of how nation states should and can conduct themselves. Really, our relationship with Indonesia is not any different. But we can nevertheless aspire to a productive working relationship with Indonesia, and we should not be unduly fazed by the inevitable rocky patches that will occur as a result of misunderstandings. I certainly believe there are enough incentives for both Indonesia and Australia to make that working relationship reasonably productive, but we shouldn't delude ourselves as to how close the relationship might be.

Nowadays many people would conclude that we deluded ourselves quite seriously as to what Australia's relationship with China would be like. Now, many people are feeling quite embarrassed by that. So, there are lessons in the Australian relationship with China which can be transposed to our relationship with Indonesia.

FDI: *What opportunities does Indonesia present for Australian companies operating in, or looking to expand there? What are some of the challenges that might be encountered?*

BS: There definitely are opportunities and Indonesia has some particular needs. It recognises, particularly, the weakness of its education system, and the fact that its young people are not trained and skilled in dealing with the Western world, lack basic English literacy and good numeracy skills and are not being well served by the Indonesian education system. Therefore, it's in areas such as education and, potentially,

healthcare services, where there are going to be particular opportunities for Australian companies. Obviously, we have to find things that are of interest to Indonesia and Indonesia has to be convinced that we can fill those needs for it. Australia's education system is obviously very competent and highly respected internationally. Equally, Australia's healthcare system is highly respected internationally, so I think that we'll have little difficulty convincing Indonesia that we have real value to deliver in those two areas and I think Indonesia fully understands that those are areas where it is very lacking at the moment.

Now, to the challenges that might be encountered. To my mind, the principal challenge faced by all foreign investment and business dealings in Indonesia is the completely opaque and non-transparent legal and court systems. It is a matter of public record, really, that foreigners are often not treated fairly and cannot have high expectations any dispute that they may have with well-resourced and well-connected Indonesian parties will be resolved by the Indonesian courts, particularly at the lower court level, in a way that reflects the actual merits of the disputes. Although Indonesia's superior courts have a somewhat better reputation than do the lower courts, foreigners also do not have a good track record of success in the superior courts.

That, regrettably, is a somewhat harsh thing to say, but just because it is harsh does not mean it is not true. Although Indonesia does not like people saying that sort of thing about its legal and court systems, anyone who knows anything about dispute resolution in Indonesia knows it to be inescapably true. What that means is that many companies – including Australian companies – if they are properly advised, would be reluctant to make large capital investments in Indonesia. It is one thing to provide services or to sell goods to Indonesia that have been produced in Australia, but it is quite another to invest large sums in setting up manufacturing plants or mineral smelting and refining plants in Indonesia. Those are the type of projects that are most vulnerable and most at risk from Indonesia's non-transparent legal and court systems and where it is most easy for opportunistic Indonesian parties to find a way to take those projects away from foreign owners. I always say to our clients: 'look, if your project is no good, you have absolutely nothing to worry about because no one would want to take it away from you.' If, however, it's a demonstrably successful project, then you have a lot to worry about, because very soon Indonesian businesspeople will start circling around and saying things like: 'it would be so much better if this was owned by a good *pribumi* [ethnic Indonesian] businessperson; how do we claim it from these foreigners?' That is just the unfortunate reality of doing business in Indonesia, and people need to be very much aware of that.

So, again, most opportunities probably lie in the provision of services and the supply of goods from Australia to Indonesia, rather than on-the-ground capital investment in Indonesia in large dollar amounts. That is going to both drive and limit the opportunities that are available to Australian companies as they seek to make more of the relationship with Indonesia.

FDI: *Taking a strategic view of matters, and noting the often rocky nature of the Australia-Indonesia relationship, what it is that Indonesia would most want out of the bilateral relationship?*

BS: Indonesia wants two main things: it wants market access to Australia for Indonesian products (particularly agricultural products), and it wants Australian investment in Indonesia. Indonesia's need and want for both of those things have been greatly accelerated and heightened by the fiscal and economic crisis that it is currently facing in the fallout from Covid-19. The need for Indonesia to narrow its current account deficit by either generating more exports or developing its own import replacement industries is only growing greater by the day. At the same time, Indonesia is realising belatedly that, in terms of attracting foreign investment from countries outside the ASEAN region, it has not done as good a job as have other countries in that region, most notably Vietnam, the Philippines, Malaysia and Thailand. In the past, it was politically incorrect in Indonesia to talk about benchmarking Indonesia against other countries in the region. The attitude was one of 'we do things the Indonesian way here; if you don't like it, don't

come here.’ But that type of attitude is very hard to sustain in the extraordinarily difficult economic circumstances that are now confronting Indonesia. There is, however, now a much greater realisation on the part of the Indonesian Government that it has to make itself more attractive to foreign investment. That, needless to say, is a very positive thing.

Of course, Indonesia wants Australian investment and participation, but it wants them without Australian commentary and criticism of its handling of a whole number of issues: its human rights record, its environmental record, its treatment of LGBT communities, its treatment of independence groups in Papua and the like. That desired outcome, I would suggest, is going to be very difficult to get right between Australia and Indonesia; in a sense, one comes with the other. You can’t really expect Australian companies and businesspeople to become actively involved in Indonesia but to simply keep their mouths shut when they see things that seem terribly wrong to them taking place on a daily basis. That’s going to be difficult for Indonesia to come to terms with. It just can’t be the case that there is a free flow of goods and services and investment from Australia to Indonesia, yet none of the baggage of political and social criticism that comes with it. Unfortunately for Indonesia, perhaps, the two are inextricably linked.

FDI: *Given all of that, what are some of the steps that both countries can take to improve matters over the next ten to twenty years? It’s hopefully not insurmountable.*

BS: No, nothing is insurmountable, and it is entirely possible for Australia to have a productive, if not particularly close, working relationship with Indonesia. Australia would be well advised to look for opportunities to make it easier for skilled Indonesians to work in Australia. That is something that’s very important to Indonesia in terms of training its young people to fill more responsible and technical roles in Indonesia itself. It would be seen as a hugely positive thing from the Indonesian perspective. It would ideally go beyond simply allowing Indonesians who are studying at Australian universities, or who have graduated from Australian universities, to continue to work in Australia after they have completed their studies. It could be something akin to the programme that exists between Australia and the UK which allows young Australians to work in the UK for a couple of years and, correspondingly, for young British people to work easily in Australia for a few years. I believe it would be extraordinarily well received by Indonesia.

Equally, Australia should be looking at how it can make it easier for Indonesians to access Australia’s exemplary medical services and hospitals. At the moment, the difficulty for Indonesians of obtaining visas for Australia at short notice is definitely a continuing source of irritation and concern, and it also cuts off Australian hospital and medical services providers from a very valuable potential source of revenue. In that regard, Australia is clearly losing out to Singapore, Thailand and Malaysia, where medical tourism is a very big business indeed and does not seem to have resulted in overstaying by Indonesians, which is presumably what underlies the ambivalence of Australia towards making it easier to obtain visas for medical care at short notice. So that is something Australia could look at. Of course, there is always going to be an element of risk and it will have to be monitored very closely, but it would be a risk worth taking.

There are, of course, also some things that need to be done at the Indonesian end, and that’s probably more difficult. As I mentioned before, one of the greatest impediments to more Australian investment in Indonesia and more on-the-ground participation by Australian companies in Indonesia are the weak Indonesian legal and court systems – and that’s not just because I’m a lawyer; all multinationals which have been operating in Indonesia would, I suggest, tell you exactly the same thing. Now, this is a difficult one, because, even though the Jokowi Government is, by and large, a very reform-minded government and certainly the best and most progressive government that Indonesia has ever had, it really has not shown much interest in reforming the legal system and the court system. That is despite the fact that you only

have to open the *Jakarta Post* on practically any day of the week to see extraordinary stories of corruption and wrongdoing coming before the courts and abuses of the legal system.

The simple reality is that it is in the interests of too many people to keep the legal and court systems opaque and non-transparent, as well as overtly favourable to Indonesians and overtly disinclined to help foreigners, for the government to be too keen to take on that challenge. What we need to understand is that, although Indonesia has made extraordinary progress in many areas since the 1950s and '60s, one area in which it has made far less progress is in improving the legal and court systems. They are almost as opaque and non-transparent today as they were during the presidency of Indonesia's first president, Sukarno. It is an extraordinary weakness in the development of Indonesia and it's something that even many Indonesian businesspeople rail about and find very discomfoting. Something has to be done about it, not just for the benefit of would-be foreign investors, but for the benefit of Indonesian businesspeople as well, because it is a serious constraint on domestic as well as foreign investment.

One thing that would greatly improve the situation would be to encourage commercial disputes, particularly commercial disputes between foreign investors and Indonesian businesspeople, to be resolved by mediation, using professional mediators, and outside of the traditional Indonesian court and legal systems. Australia has had huge success with dispute mediation and could provide very high level technical assistance in helping Indonesia develop a strong commercial dispute mediation system which bypasses the problems with reliance on the Indonesian court and legal systems. Compulsory professional mediation of commercial disputes might also be seen as less confrontational and less of a threat to vested interests than wholesale reform of the Indonesian legal and court systems.

FDI: *Arguably, it would be a tremendous advantage if those systems were reformed, but what would it take to produce any sort of enthusiasm for such changes? How might that happen?*

BS: It certainly would be advantageous and, in the long term, it must unquestionably be the case. The trouble is that there are too many well-placed individuals who enjoy too many short-term advantages from the status quo for there to be a lot of incentive at the higher levels to make those changes.

What is needed is a greater awareness among young Indonesians about how weak the legal system is, and how they're being disadvantaged by it, and what the costs are of such weak legal and court systems and the opportunities that have been denied to Indonesia because of the deficiencies in those systems. I do have some hope for that, because we have seen young Indonesians become increasingly militant in protesting about, and demonstrating against, corruption, which is, of course, intimately tied to the weak, non-transparent and opaque legal system.

Indonesia has a vibrant press which is always willing to publicise corrupt acts by Indonesian politicians and businesspeople. If that were focussed more on the legal and the court systems, and perhaps with the realisation that the two are actually so very closely connected, then, in that way, I think we might see some progress forced upon the government.

So, the growing education of the youthful population and the fact that there is a vibrant, open and independent media, particularly the print media, are, I think, very positive things that may help to bring about some reforms of the legal and court systems in due course. But there will be a huge pushback behind the scenes from people who want to make sure that does not happen. Just as various élites seem to have discreetly managed to de-fang the Indonesian Corruption Eradication Commission (the KPK), any initiative to reform the legal and court systems is likely to meet with very similar behind-the-scenes resistance, and that resistance may well ultimately be successful.

FDI: *In terms of the Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA), what do you see as the main benefits that are likely to flow from it? What, if any, gaps or omissions do you see in the agreement? Will it attract more investment in Indonesia from Australia?*

BS: It will almost certainly be successful, to a degree. In particular, the phasing out of tariffs will be very positive in terms of promoting greater trade between the two countries and that can only be a good thing. Equally, IA-CEPA indicates a willingness to allow Australian companies to be active in areas such as education, tourism and medical services, areas in which Australia does enjoy a lot of competitive advantage. Those are all very positive things.

My concern about IA-CEPA comes back to the issue of the protections that are offered by IA-CEPA to Australians investing in Indonesia. Australia already has what is called a bilateral investment treaty with Indonesia and which guarantees Australian investors in Indonesia certain very basic and important protections. A few years ago, Indonesia announced that it no longer wanted, and would not renew, any of the some 60 bilateral investment treaties that it has with a whole host of countries, including Australia. The reason was because Indonesia regarded those bilateral investment treaties as being not sufficiently favourable to it and, therefore, not sufficiently in Indonesia's best interests. What Indonesia particularly objects to in the bilateral investment treaties is that any disputes have to be resolved by international arbitration, rather than by legal proceedings in Indonesia. Accordingly, the Indonesian Government and Indonesian companies are at much greater risk of losing those international arbitrations than they would be if the disputes were heard in Indonesia itself.

The very fact that Indonesia is so opposed to international arbitration when it has such weak legal and court systems of its own, and the fact that it refused to allow traditional international arbitration for investor state disputes to be included in IA-CEPA, is a very worrying thing. It is going to cause a lot of pause for thought among more sophisticated Australian companies that can look beyond the immediate returns they might garner from Indonesia to understand that, if there should be a dispute, they are going to be at a very serious disadvantage. That is surely a real limitation. It must be acknowledged, however, that Australia's diplomats negotiated long and hard with their Indonesian counterparts, getting the best deal they could for Australian companies wanting to do business in Indonesia. It was never likely Indonesia was going to agree to all the straightforward protections provided for in the existing bilateral investment treaty with Australia.

Also, if you read the language of the protection provisions of IA-CEPA, there are all sorts of caveats that are not present in the existing bilateral investment treaty. Indonesia reserves to itself the right to deny protection to Australian companies and investors in circumstances where, effectively, Indonesian public policy and public welfare demand that the company takes a different course. Equally, some of the things that are most inimical for Australian investors, such as foreign ownership limitations and the divestiture obligations that apply to foreign-owned mining companies in Indonesia, are expressly excluded from IA-CEPA.

Equally, IA-CEPA absolves the Indonesian central government of any responsibility for things done or not done by regency (local) and provincial governments to Australian investors. If you're aware of the long and sorry history of Australian mining projects in Indonesia, it is almost always problems encountered by Australian companies with the regency and provincial governments that tend to be the source of the horror stories heard from Australian companies operating in the Indonesian mining sector. Under IA-CEPA, the Indonesian Government basically says, 'that's not our concern; we're not going to be held liable for what the regency or provincial government does or does not do'.

That is another very serious limitation of IA-CEPA from the perspective of Australian companies which might be contemplating making large capital investments in Indonesia. Again, if you're just selling goods and services in Indonesia without having boots on the ground, as it were, that's going to be a problem. But, for IA-CEPA to really achieve its full potential, it needs to be about more than just selling goods and services; it has to be about promoting investment in Indonesia by Australian companies and investment in Australia by Indonesian companies. On that second score, IA-CEPA may well disappoint in terms of what it actually delivers.

FDI: *It comes right up against that problem of confusion and contestation between the different levels of Indonesian government, doesn't it?*

BS: Yes, it does, and that comes back to the issue of whether the policy of regional autonomy is a good thing. People have different views on that but, particularly in the resources sector, it can scarcely be denied that regional autonomy has been very problematic at best. Indeed, Indonesia is busy trying to pull back from regional autonomy in the mining and resources sector to ensure that it is only the central government that has licencing authority in that regard. The fact is that even the Indonesian authorities acknowledge that regional autonomy was not such a good thing, particularly in those sectors of the economy in which foreign investors have the greatest interest.

FDI: *That takes us very neatly now into the mining, resources and energy sectors. What do you see as being the most pressing future issues for Indonesia to address in terms of those sectors?*

BS: The most important issue is for Indonesia to understand that it is not just the case of foreigners needing Indonesia's resources, but that it is also very much a case of Indonesia needing the investment that comes with foreign participation in its resource-focused industries. In other words, it's a two-way street, not just a one-way street. Unfortunately, Indonesia's 2009 mining law and the current oil and gas law were introduced during a time of historically high prices for resource commodities. It was also at a time when the Indonesian Government had convinced itself that it could draft those laws in whatever way it wanted and foreigners would still be beating a path to Indonesia's door because they were so keen to obtain access to those resources. The cyclical nature of commodity prices, though, has meant that, in the last few years, there has been huge downward pressure on oil and mineral prices – and coal prices in particular – and, consequently, foreign investors are no longer beating a path to Indonesia's door. That has made life very difficult for the Indonesian Government, which has traditionally relied on production royalties from the oil and gas industries and the mining industry as a mainstay of its Budget.

The government, and Indonesia as a whole, needs to change its mindset about foreign investment and the resources space. Unfortunately, people in the government have done too good a job of convincing the Indonesian public that rampant resource nationalism is an appropriate policy to pursue and that Indonesia should really hold foreign investors at arm's length in the resources sector and require them to divest a majority stake in their projects to local parties. That is really just a non-starter for many foreign companies, which say, 'look, we take huge risks developing, exploring and developing resources projects in Indonesia and, if we then have to give up a majority stake after ten years, that is not really adequate compensation for the risks we run establishing them in the first place.' Unfortunately, it is going to be very difficult to change Indonesia's mindset on that.

Just in the last few weeks, for instance, Indonesia has amended its mining law and, unfortunately, the fifty-one per cent divestiture requirement has remained part of the regulatory environment for mining projects. Particularly for foreign exploration companies, that is just a non-starter. In the last ten years since the fifty-one per cent divestiture requirement came into force, the number of foreign exploration companies in

Indonesia has dropped from probably more than 100 to fewer than ten. There has been a huge exit by foreign exploration companies and that is building up huge problems for Indonesia because there is no longer the pipeline for new projects available to come online as existing resource projects are mined out and fully exploited. Very belatedly, Indonesia has started to realise that this is a problem and has endeavoured, in the new mining law, to do various things to encourage more exploration but, unfortunately, has done nothing about the fifty-one per cent divestiture requirement, which is a major impediment to foreign investment in the resources sector.

FDI: *As you observed, Indonesia is not keen to have Australian commentary on what it perceives to be various domestic matters, but is there any role that Australia might be able to play? Is there any assistance that Australia could potentially offer to Indonesia as it moves to overcome those challenges?*

BS: That's a good question. To date, Indonesia has wanted to confine technical assistance from Australia and other countries to such areas as education, systems development for land titles, patent and intellectual property systems and the like. It really has not been interested in engaging foreign countries to provide advice and input on such matters as dealing with human rights, environmental issues and protection of minorities. Those are all very politically sensitive issues and Indonesia is undoubtedly not alone among countries in saying that those areas are off limits to foreigners. I don't really see any prospect of that changing. Even in terms of providing technical assistance for reforming the Indonesian legal system, I am sure that has been offered on numerous occasions, not only by the Australian Government, but by other foreign governments as well. Jakarta has shown absolutely no interest in taking that up, which probably tells us quite a lot about how it views the role of technical assistance.

As I mentioned before, Australia has world-class expertise in dispute mediation, particularly mediation of commercial disputes. This is an area of expertise that Australia should encourage the Indonesian Government to take advantage of. A focus on helping Indonesia develop a credible, professionally run commercial mediation system, that operated in parallel to the traditional court/legal system, could be a huge benefit to Indonesia as it would surely be well received by many domestic investors as well as most certainly by foreign investors. Assistance with the development of commercial mediation in Indonesia could also be credibly presented as being consistent with the type of technical, non-political, non-controversial assistance that Indonesia has traditionally sought and received from Australia.

In [Part Two](#) of this interview, Mr Sullivan brings his expertise to bear in examining the potential implications for Indonesia of the Covid-19 pandemic, before moving on to the realm of international relations to discuss the relationships of Indonesia with China, the United States, Russia and India. The discussion concludes by taking a look ahead towards the next presidential election, due to be held in 2024.

About the Interviewee: Bill Sullivan specialises in advising foreign investors on the legal, policy and regulatory aspects of construction, energy, mining and oil and gas projects in Indonesia and elsewhere in South-East Asia, including Myanmar.

Bill has spoken and written widely on Indonesia's 2009 Mining Law and its implications for foreign investment. Bill is the author of the 2013 book *Mining Law & Regulatory Practice in Indonesia – A Primary Reference Source*, the only internationally published (Wiley, New York) and distributed, comprehensive review, to date, of the 2009 Mining Law and its implementing regulations. As a consequence, Bill is regarded as a leading expert on Indonesian mining law and regulation.

In 2015, Bill was part of the Working Group of the Australia-Myanmar Chamber of Commerce which prepared a detailed written submission to the Myanmar Mines Department on what the then proposed new Myanmar Mining Law should provide for in order to encourage world-class mining companies to invest in Myanmar's mining industry.

Bill is currently Senior Foreign Counsel with Christian Teo & Partners (in association with Stephenson Harwood LLP) and Senior Adviser to Stephenson Harwood LLP, as well as a qualified legal practitioner in England and Wales, Hong Kong, New South Wales and New York. He has lived and worked in Indonesia for more than 20 years.

Bill was previously an international equity partner of Coudert Brothers LLP and acted as the Australian Government-funded technical adviser to Bank Indonesia on debt restructuring matters in the aftermath of the Asian Financial Crisis. Bill is a graduate of the University of New South Wales (BCom (with merit), LLB and MCom), Harvard Law School (LLM) and the University of Sydney (MBA and SJD). During his time at Harvard Law School, Bill was both a Frank Knox Memorial Fellow and the recipient of a Fulbright Postgraduate Award.

Any opinions or views expressed in this paper are those of the individual interviewee, unless stated to be those of Future Directions International.