

## **How to protect investments in Indonesia despite the termination of its Bilateral Investment Treaties**

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## Summary

Various nationalistic measures have been taken by states in Asia against foreign investors in recent times. Investment treaties provide investors with protection against such incursions and, if necessary, a means by which compensation can be obtained through international arbitration.

The Government of the Republic of Indonesia (**Gol**), however, has begun terminating its Bilateral Investment Treaties (**BITs**). While it has indicated that it intends to negotiate new treaties, it is not clear how long that might take and what protections will be afforded to investors under any such treaties. Based on recent state practice, it can be assumed that the protections in any new treaties will be less than those under Indonesia's existing BITs. Nevertheless, an investor can continue to be protected under a terminated treaty for a period of time, usually between ten to 20 years, if its investment qualifies for protection before the relevant BIT is terminated. Longer term protection is also available by structuring an investment through a state which is a party to one or more of Indonesia's multilateral investment treaties (**MITs**) or free trade agreements which contain an investment chapter (**FTAs**).

In this briefing, we do three things:

- a) we briefly describe the substantive and procedural protections that investment treaties provide foreign investors in Indonesia and elsewhere;
- b) we identify the Indonesian BITs which have already been terminated by the Gol and those which are set to expire soon; and
- c) we explain how foreign investors continue to have several options for securing protection of their investments against sovereign risk in Indonesia even if Indonesia proceeds to terminate all of its BITs.

## I. The power of investment treaties

Investment treaties provide investors with a means of managing the sovereign risk attaching to a foreign investment. Specifically, an investment treaty can protect an investor and its foreign investment against unfair, inequitable, arbitrary or politically motivated conduct by the government of the state hosting the investment, or a denial of justice by its judicial organs. They also typically guarantee an investor full compensation if its investment is expropriated, as well as the right to be treated no less favorably than domestic investors or investors from other countries (i.e. 'most favoured nation' status).

Investment treaties also usually protect an investor's right to transfer capital and returns out of the host state without hindrance or delay. This may prove to be an important protection in the Indonesian context in light of Bank of Indonesia regulations designed to prop up Indonesia's ailing currency and financial markets. Many investment treaties also require the host state to observe any obligations it has undertaken with regards to a qualifying investment (which is sometimes referred to as an 'umbrella clause').

These substantive protections are often reinforced by a qualifying investor's procedural right to bring a claim directly against the state hosting its investment through international arbitration (rather than through the local courts or, alternatively, through the investor's own government in a process known as diplomatic protection).

The threat of a foreign investor bringing a claim against a host state which is decided by independent and specialist arbitrators applying international law and sitting in a neutral location has proven to be an effective means of encouraging states to treat foreign investments fairly and, if they do not, a reliable means for a qualifying investor to secure a suitable remedy through international arbitration.

## II. The termination of Indonesia's BITs

Indonesia has received a spate of investment treaty claims in recent years. The claims include those brought by a Saudi investor, Mr. Hesham al Warraq, in relation to his alleged wrongful conviction for fraud and money laundering; Nippon Asahan Aluminium, over the disputed valuation of a hydroelectric and aluminium project; Churchill Mining, in relation to the alleged expropriation of investments in a coal project in Borneo; and holding companies owned by Newmont Mining and Sumitomo Corporation in relation to export restrictions intended to encourage the smelting of copper concentrate. The Gol has successfully defended some of these claims (such as Mr. al Warraq's claim) and settled others (including the claims brought by Nippon Asahan Aluminium and Newmont/Sumitomo). Nonetheless, the Gol has taken steps to decrease its investment treaty exposure through the termination of its BIT programme.

In March 2014, the Dutch embassy to Indonesia announced that it had received a notice of termination of the Netherlands-Indonesia BIT. Thus, the Netherlands-Indonesia BIT expired on 1 July 2015. It has since been confirmed by the Malaysian government that the Indonesia-Malaysia BIT terminated on 20 June 2015, while the Prime Minister of Singapore, Lee Hsien Loong, has confirmed that the Gol has given notice that the Indonesia-Singapore BIT will expire on 21 June 2016. Furthermore, there are unconfirmed reports that another six Indonesian BITs (namely those with Bulgaria, Slovakia, China, France and Italy) have been terminated by the Gol.

Table 1 below lists Indonesia's existing BITs in the order in which they are likely to terminate.<sup>1</sup> In addition to the possible termination date for each BIT, we indicate in Table 1 the period of time that each BIT will continue to apply (i.e. 'survive') for investments which qualify for protection before the BIT is terminated. These so-called survival clauses are explained in Section III.

*Table 1: Indonesia's BITs listed in order of possible termination date*

No.	BIT contracting party	Date of entry into force	Possible termination date	Notice period for termination	Survival period post-termination
1.	Bulgaria	23/01/1995	23/01/2015	6 months	10 years
2.	Slovakia	01/03/1995	01/03/2015	1 year	10 years
3.	China	01/04/1995	01/04/2015	1 year	10 years
4.	France	29/04/1975	29/04/2015	6 months	Indefinite for investments made prior to notice of termination
5.	Malaysia	27/10/1999	20/06/2015	1 year	10 years
6.	Italy	25/06/1995	25/06/2015	1 year	10 years
7.	Netherlands	01/07/1995	01/07/2015	1 year	15 years
8.	People's Democratic Republic of Lao	14/10/1995	14/10/2015	1 year	10 years
9.	Hungary	13/02/1996	13/02/2016	1 year	10 years
10.	Switzerland	09/04/1976	09/04/2016	1 year	Indefinite for investments made prior to notice of termination
11.	Singapore	21/06/2006	21/06/2016	1 year	10 years
12.	Pakistan	03/12/1996	03/12/2016	1 year	10 years
13.	Spain	18/12/1996	18/12/2016	6 months	10 years
14.	United Kingdom	24/03/1977	24/03/2017	6 months	20 years
15.	Germany	02/06/2007	02/06/2017	1 year	20 years
16.	Belgium-Luxembourg	17/06/1972	17/06/2017	1 year	BIT continues to apply to pre-existing state contracts

<sup>1</sup> Table 1 assumes that the Gol has provided effective notice to each BIT counterparty of its intention to terminate the BIT by the relevant cut-off date. For instance, the Hungary-Indonesia BIT is presently nearing the end of a second ten-year term, which is due to expire on 13 February 2016. If the Gol failed to give notice of its intention to terminate the BIT by at least 12 months before the current ten-year term expires (i.e. before 13 February 2015), the BIT will roll over for another ten years to 2026. It is also noted that five of Indonesia's BITs may be terminated at any time (namely those with Argentina, India, Romania, Turkey and Vietnam), though the Gol has not yet made any public announcements regarding the termination of these BITs.

No.	BIT contracting party	Date of entry into force	Possible termination date	Notice period for termination	Survival period post-termination
17.	Ukraine	22/06/1997	22/06/2017	1 year	10 years
18.	Sri Lanka	21/07/1997	21/07/2017	1 year	10 years
19.	Denmark	02/07/1968	02/07/2018	6 months	10 years
20.	Thailand	05/11/1998	05/11/2018	1 year	10 years
21.	Jordan	09/02/1999	09/02/2019	1 year	10 years
22.	Mongolia	13/04/1999	13/04/2019	1 year	10 years
23.	Bangladesh	22/04/1999	22/04/2019	1 year	10 years
24.	Czech Republic	21/06/1999	21/06/2019	1 year	10 years
25.	Finland	02/08/2008	02/08/2019	1 year	10 years
26.	Cuba	29/09/1999	29/09/2019	1 year	10 years
27.	Russia	15/10/2009	15/10/2019	1 year notice	10 years
28.	Syrian Arab Republic	20/02/2000	20/02/2020	1 year	10 years
29.	Mauritius	28/03/2000	28/03/2020	1 year	10 years
30.	Mozambique	25/07/2000	25/07/2020	1 year	10 years
31.	Morocco	21/03/2002	21/03/2022	6 months	10 years
32.	Sweden	18/02/1993	18/02/2023	1 year	15 years
33.	Australia	29/07/1993	29/07/2023	1 year	15 years
34.	Republic of Korea	10/03/1994	10/03/2024	1 year	BIT continues to apply to rights accrued before termination (i.e. potential and existing disputes)
35.	Kyrgyzstan	23/07/1994	23/07/2024	1 year	10 years
36.	Egypt	29/11/1994	29/11/2024	1 year	10 years
37.	Argentina	01/03/2001	May be denounced at any time	1 year	10 years
38.	India	22/01/2004	May be denounced at any time	1 year	15 years
39.	Romania	21/08/1999	May be denounced at any time	1 year	10 years
40.	Turkey	28/09/1998	May be denounced at any time	1 year	10 years
41.	Vietnam	03/04/1994	May be denounced at any time	1 year notice	10 years
42.	Uzbekistan	27/04/1997	None specified	None specified	10 years
43.	Islamic Republic of Iran	28/03/2009	Not publicly available		
44.	Poland	01/07/1993	Not publicly available		
45.	Saudi Arabia	05/07/2004	Not publicly available		
46.	Tunisia	12/09/1992	Not publicly available		
47.	Venezuela	23/03/2003	Not publicly available		

### III. How to secure future protection for investments in Indonesia

Investors have several options for protecting their investments in Indonesia against sovereign risk notwithstanding the Gol's stated intention to terminate its BITs.

First, as Table 1 above demonstrates, a large number of Indonesia's BITs cannot be terminated unilaterally by the Gol for several years. With that said, not all of these extant BITs provide comprehensive protection of investments. Each treaty needs to be considered according to its terms before it should be relied upon to help manage sovereign risk.

Second, all of Indonesia's BITs contain a 'survival clause'. These clauses provide that the relevant BIT will continue to afford protection to any qualifying investments made prior to the date of termination of the BIT for a further 10, 15 or 20 years following its termination.<sup>2</sup> For instance, Article XIII(3) of the Indonesia-Singapore BIT provides that the provisions of the BIT shall continue to be effective, with respect to investments made prior to the date of termination, for a further period of ten years from the date of termination. Thus, the Indonesia-Singapore BIT will continue to provide protection until 21 June 2026 for qualifying investments in Indonesia made or restructured through Singapore before 21 June 2016.

<sup>2</sup> Some Indonesian BITs (such as those with Belgium-Luxembourg, France, Republic of Korea and Switzerland) provide even longer protection for qualifying investments which are made before the BIT terminates.

Third, the Gol has not expressed an intention to withdraw from the MITs and FTAs to which Indonesia is a party. These treaties provide a significant degree of protection for foreign investors in Indonesia, as demonstrated in the table below, albeit potentially less protection than that which was provided by some of Indonesia's now-terminated BITs.

*Table 2: Protections provided by MITs and FTAs to which Indonesia is a party, organized by date of entry into force*

No.	MIT/FTA (entry into force)	Fair and equitable treatment	National treatment	Most-favoured nation treatment	No expropriation without full compensation	Protection and security	Free transfer of funds	Right to arbitration
1.	Organization of Islamic Cooperation (OIC) Investment Agreement (23/09/1986)	No	Yes	Yes	Yes	Yes	Yes	Yes
2.	Indonesia-Japan EPA (01/07/2008)	Yes	Yes	Yes	Yes	Yes	Yes	Yes
3.	ASEAN-Korea Investment Agreement (01/09/2009)	Yes	Yes	Yes	Yes	Yes	Yes	Yes
4.	ASEAN-China Investment Agreement (01/01/2010)	Yes	Yes	Yes	Yes	Yes	Yes	Yes
5.	ASEAN Australia New Zealand (AANZ) FTA (10/01/2012)	Yes	Yes	No	Yes	Yes	Yes	Yes
6.	ASEAN Comprehensive Investment Agreement (ACIA) (29/03/2012)	Yes	Yes	Yes	Yes	Yes	Yes	Yes
7.	ASEAN - India Investment Agreement (not yet in force, signed 12/11/2014)	Yes	Yes	No	Yes	Yes	Yes	Yes
8.	Trans-Pacific Partnership Agreement (TPP)	Negotiations in progress (treaty may include an investment chapter)						
9.	EU-ASEAN FTA	Negotiations in progress (treaty may include an investment chapter)						
10.	EU-Indonesia Comprehensive Economic Partnership Agreement (CEPA)	Negotiations in progress (treaty may include an investment chapter)						
11.	Regional Comprehensive Economic Partnership (RCEP)	Negotiations in progress (treaty may include an investment chapter)						

Thus, by way of illustration, an investment in Indonesia structured through Singapore will continue to benefit from the various ASEAN investment agreements to which Indonesia and Singapore are party, including the ASEAN Comprehensive Investment Agreement, even if the Singapore-Indonesia BIT expires on 21 June 2016, as expected.

Fourth, the BITs terminated by the Gol may be replaced by new treaties. Indonesian government officials have indicated that the Gol is drafting a new template for its BITs. The template, however, is yet to materialize. Further, it is not clear whether all of Indonesia's counterparties will be in a position themselves to negotiate a new BIT with the Gol. In particular, European Union member states such as the Netherlands appear to be no longer competent to negotiate BITs on a bilateral basis. Thus, attention for those states is likely to shift to the EU-ASEAN FTA and the EU-Indonesia Comprehensive Economic Partnership Agreement (CEPA), both of which are presently under negotiation.

Finally, the 2007 Indonesian Investment Law provides a limited degree of protection for foreign investments, the efficacy of which will need to be carefully considered before it is relied upon. The Investment Law, in theory, protects investors against expropriation without full compensation, grants investors the right to transfer funds out of the country (subject to important exceptions), and provides that investors shall be treated 'pursuant to the rules of law'. However, the Investment Law neither guarantees fair and equitable treatment for investments (unlike

most BITs) nor does it provide investors with a right to refer disputes to arbitration unless that is separately agreed with the Gol.

#### IV. Conclusion

It is important to have the right corporate structure in place so as to benefit from an investment treaty when investing in Indonesia (and indeed elsewhere). When sovereign risks materialize, having a right of recourse under an investment treaty can make the difference between obtaining a suitable remedy (often done through negotiation) or no remedy at all. As a result, investment treaty planning should be undertaken as part of the due diligence for any foreign investment, much like investors often do with regards to tax.

Governments around the world, including Indonesia's, recognize the power of investment treaties in the hands of a foreign investor. Several, and not just the Gol, have taken steps to reduce their exposure to investors under these treaties. Nonetheless, as explained in this note, foreign investments in Indonesia can still be protected if structured (or restructured) through a country that holds a BIT with Indonesia before that BIT expires and/or through a country that is party to an MIT or FTA with Indonesia.

However, not any BIT, MIT or FTA will do. They each vary according to their terms. Dechert's international arbitration team is available to advise investors on which investment treaties provide the optimal range of protections for a particular investment depending on the jurisdiction in which the investment is made and the types of disputes that the investor is likely to encounter.

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