BALTIC JOURNAL OF LAW & POLITICS
A Journal of Vytautas Magnus University
VOLUME 16, NUMBER 3 (2023)
ISSN 2029-0454

Cite: Baltic Journal of Law & Politics 16:3 (2023): 2731-2757
DOI: 10.2478/bjlp-2023-00000202

Cost and Benefit Analysis of BIT from the Legal Perspective of Indirect Expropriation Provision The Case of Indonesia

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Received: December 21, 2022; reviews: 2; accepted: January 30, 2023

Abstract

This article is a critique of bilateral investment treaties (BITs) concluded by Indonesia amidst a nationwide accepted legal doctrine that BITs could promote the increase of foreign direct investment (FDI) flows into the country. Using cost and benefit analysis, however, this study reveals that such doctrine is not supported by the evidence. In contrast, the legal risk borne by the state from broad interpretation due to the unclear legal formulation of indirect expropriation and related provisions is inevitable. In addition, the monetary cost of treaty-making, arbitration cost, and compensation cost for breached provision provide worrisome pressure on the state's budget. This article suggests two policy options either terminating all BITs or reconstructing BITs provisions hence only stipulating provisions of promotion and facilitation of investments. BIT models of peer countries could be taken into consideration for the reconstruction of BIT to minimize the cost and maximize the economic benefit of BIT for Indonesia.

Keywords

bilateral investment treaty, indirect expropriation, cost and benefit analysis, economic analysis of law, foreign direct investments, perjanjian investasi bilateral

1. Introduction

A bilateral investment treaty (BIT) is an international legal instrument containing obligations or commitments of a party (host state) to protect investors and their investments from another party (home state) against non-commercial or political risks who invest in the territory of a host state (OECD, 2016). In practice, there are different views between developed and developing countries in addressing a standard for the protection of foreign nationals and their property. Developed countries, which are mostly considered as capital-exporting states, tend to use international minimum standards of treatment for the protection while developing countries, which are mostly capital importing states, tend not to provide special treatments to foreign nationals than those are accorded to their own nationals (national treatment principle) (Surya P. Subedi, 2008).

Indirect expropriation is among key provisions in numerous international investment treaties, particularly treaties concluded in the last 50 years (Anna Joubin-Bret (ed.), 2012). There are more than 3,000 international investment agreements (IIAs) concluded around the world which consist of 2,932 BITs and 385 treaties with investment provisions (TIPs) such as Free Trade Agreement (FTA) and Comprehensive Economic Partnership Agreement (CEPA) (UNCTAD, 2019). According to UNCTAD's investment dispute settlement data base (2022), the number of investment disputes under investor-to-state dispute settlement (ISDS) mechanism has reached 1,061 cases globally where indirect expropriation provision is the second-largest provision alleged and breached (432 and 63 cases respectively) after fair and equitable treatment (FET) provision (528 and 143 cases correspondingly). Indonesia is no exception where there were four of seven known ISDS cases that contained alleged breach of indirect expropriation and FET provisions under seven BITs and one TIP (see Table 1).

Table 1 Known-cases of Indonesia as Respondent in Investment Dispute under ISDS

Year	Claimant (Country)	Sector	International Investment Treaties	a. ISDS outcome b. Amount of claim c. Alleged provisions
2016	Oleovest Pte Ltd (Singapore)	Manufacture	Indonesia-Singapore BIT (2005)	a. Discontinued b. NA (not available) c. NA
2015	IMFA Ltd. (India)	Mining	Indonesia-India BIT (1999)	a. Decided in favor of State b. US$ 559 millions c. NA

2014	Nusa Tenggara Partnership BV and PT Newmont Nusa Tenggara (Netherland)	Mining	Indonesia-Netherland BIT (1994)	a. Discontinued b. NA c NA
2012	Churchill Mining and Planet Mining Pte Ltd	Mining	Indonesia-UK BIT (1976) and Indonesia-Australia BIT (1992)	a. Decided in favor of State b. US$ 1.3 billions c. Indirect expropriation, FET, discriminatory measures
2011	Hesha Al Warraq (Saudi Arabia)	Banking	OIC Investment Agreement (1981)	a. Decided in favor of neither party (liability found but no damages awarded) b. US$ 19.6 millions c. Indirect expropriation, FET, full protection
2011	Rafat Ali Rizvi (United Kingdom)	Banking	Indonesia-UK BIT (1976)	a. Decided in favor of State b. USD75 millions c. Indirect expropriation, FET
2004	Cemex (Mexican company established in Singapore)	Cement Industry	*ASEAN Investment Agreement* (1987)	a. Settled b. USD400 million (amount settled USD337 millions) c. Indirect expropriation (*de facto* expropriation)
Source: UNCTAD, Investment Dispute Settlement Navigator, 2022				

Investor-to-state disputes on expropriation in the past 20 years have been shifted from nationalization or direct expropriation to disputes on national legislation of foreign investment contended as indirect expropriation which arise under three conditions (Suzy H. Nikiema, 2012). Firstly, when the host state takes measures in response to the economic and financial crisis that requires intensive and frequent amendment and adjustment of national economic policy, like happened to Argentina as a respondent to more than 40 cases before the ICSID tribunal in 2001. Secondly, when the host state takes measures that have an adverse effect on the legal title of foreign investor's property, therefore, the host state has to pay compensation even though measures have been imposed for the public interests (such as public order, public health, national security, human rights, public moral, and environmental protection). Finally, on the condition when the host state imposes regulation to comply with international obligations, such as protection of the forest, hazardous waste management, and protection of labor's rights, but such measures may impend the profitability of foreign investment.

The investment dispute on indirect expropriation provision emerged when there were no uniform interpretations on such provision between foreign investors and the host state due to the very broad and unclear definition of the said provision. This situation may bring about circumstances called regulatory chill for the host state when the term of indirect expropriation might be expanded to any measures that adversely affect foreign investor's property or interest (IISD, 2022; Abdul Kadir Jailani, 2015 and 2016). There are four hypotheses on possible effects of investment treaty on FDI flows to developing counties, namely commitment effect, signaling effect, substitute effect, and provisions effect (James Zhan (ed.), 2009). According to these hypotheses, investment treaties will possibly increase FDI flows if there are strong commitments of protection to foreign investors, serious signal about improved property rights in the host country, investment treaty serves as a substitute to improve institutional quality of host country, and high quality of provisions in the treaties. However, this claim remains inconclusive because the effect of investment treaties on FDI inflow varies across the countries. Many developing countries signed a numbers of bilateral investment treaties but show no strong evidence on inward FDI flows (M. Sornarajah, 2010). Thus, the correlation between the investment treaties and FDI inflows to developing countries is still questionable while the impact on state sovereignty is quite noticeable (Sornarajah, 2015).

It is important to note that in thousands of investment treaties mostly, if not all, have the common purpose that is promoting FDI flows as mentioned in the preamble. For example, in Indonesia-Qatar BIT (signed in 2000 and entry into force in 2018) it reads: "Recognising that the promotion and protection of these investments will stimulate the flow of capital and technology between the two Contracting Parties in the interest of economic development." From the perspective of a capital importing country like Indonesia, BIT is expected to be a legal instrument as a tool to boost more FDI inflows than that of no BIT is in place. However, many studies show that the relation between BIT and FDI flows is inconclusive where some reveal a significant relationship while others prove that BIT is not a significant explanatory variable on FDI flows (Sornarajah, 2010; Karl P. Sauvant and Lisa E. Sachs (eds.), 2009).

This study applies the economic analysis of law using the cost-benefit analysis (CBA) as a tool to determine the expected economic benefits from all BITs signed by the government of Indonesia since the 1960s in terms of the amount of FDI inflows and the costs of BITs in terms of legal risk from indirect expropriation and other related provisions, litigation cost, compensation cost, and fiscal cost from the treaty-making process. We identify the following research questions to achieve the research objectives: Do the BITs concluded by the government of Indonesia have a significant effect on the FDI inflows? What kind of legal risks from indirect expropriation and other related provisions under the existing BITs? How much is the cost of having BITs that potentially burdensome to the state's budget? Should the government maintain the existence of BITs?

The next section will introduce the legal theory and research method in which this study is conducted using the cost-benefit analysis (CBA) approach as an application of an economic analysis of law. The subsequent section will explain a brief historical practice of expropriation measures by the government of Indonesia in the early years after independence. The expected benefits and cost of all BITs concluded by Indonesia using the CBA approach will be deliberated in the discussion section. The last section provides conclusions and some policy recommendations toward the existing BITs as international legal instruments to stimulate more FDI inflows as intended of having BITs.

2. Theoretical Review

This research applies cost-benefit analysis (CBA) as basically one of the tools of economic analysis to address legal problems (Maria Conboy, 2015). Conducting the economic approach most often involves an assumption that each individual is a rational utility maximizer of satisfaction subject to limited available resources. According to Posner (1977, p.3), economics is: "the science of the science of human choice in a world in which resources are limited in relation to human wants, explores and tests the implications of assuming that man is a rational maximizer of his ends in life, his satisfactions-that we shall call his "self-interest".

Posner distinguishes two aspects of the economic approach in analyzing legal issues, namely positive and normative aspects. The positive aspect of the economic approach emphasizes efficiency as a result of a government policy (Romli Atmasasmita and Kodrat Wibowo, 2017). For example, in the context of business competition, the law is functioned to encourage fair market competition. However, if there is unfair business competition, the law plays a role in encouraging fair business competition so that economic efficiency increases (Klaus Manthis, 2009). The normative aspect of economic analysis views that something that is good in the present should also be considered good for the future. A judge, for example, not only has to care about his current verdict but also has to be able to predict the impact of his decision in the future because it will set a precedent (stare decisis).

The CBA approach essentially has philosophical root to the principle of utility under the legal theory of utilitarianism (Maria Conboy, 2019). Jeremy Bentham, a leading philosopher of utilitarianism in the 18^{th} century said in his famous master piece entitled An Introduction to the Principles of Morals and Legislation (2000) as follow:

"Nature has placed mankind under the governance of two sovereign masters, pain and pleasure. It is for them alone to point out what we ought to do, as well as to determine what shall do…In words a man may pretend to abjure their empire but in reality, he will remain subject to it all the while. The principle of utility recognizes this subjection and assumes it for the foundation of that system, the object of which is to rear the fabric of felicity by the hands of reasons and of law…".

According to Bentham, pain and pleasure resulting from the application of law can be explained through a calculation called felicific calculus with the following assumptions (Fajar Sugianto, 2013):

1. The happiness of each individual increases when the amount of his total satisfaction is greater than his sadness;
2. The total benefit of a society is the sum of the individual benefits; and
3. The total happiness of a society can be increased if the sum of the individual happiness is greater than the sum of their pains.

The felicific calculus method (also known as hedonic calculus) is an algorithmic technique for calculating the pleasure/happiness and misery/sadness resulting from action as the overall value of a consequence (Thomas Mautner (ed.), 2022). An action is said to be right or wrong will be determined by the impact of good (happiness) or bad (misery) resulting from the action depends on intensity, duration, certainty, propinquity, purity, fecundity, and the number of people affected (extent). In essence, according to Bentham, good law is a law that can provide benefit or happiness to the largest part of society ("the greatest happiness of the greatest number") (Lili Rasjidi and Liza Sonia Rasjidi, 2016).

The principle of benefit and happiness, which Bentham called the principle of utility, is a principle that does not only refer to the consequences of personal (subjective) human action but also government actions that have the authority to regulate society. Thus, the principle of benefit and happiness can be viewed in a broader context because it includes both individual and social aspects (Frederikus Fios, 2012). According to Bentham, society is considered a fictional body which is a collection of individuals as members of its body. Because the interests of a society are interests formed by a group of individuals in that society, the principle of benefit underlies the government to make policies that tend to increase the happiness of society rather than make it suffer. Utilitarianism emphasizes the cause and effect of an action that contributes a great deal of thought in the use of cost and benefit analysis in decision making and public policy analysis (Atip Latipulhayat, 2015).

3. Research Method

This study is a normative and empirical legal analysis with the primary research objects of 64 BITs concluded by the government of Indonesia during 1968-2018 comprising 25 entered into force BITs, 16 signed BITs but not yet entered into force, and 23 terminated BITs but still have a sunset clause for 10 to 20 years (see Appendix for more details). Statute, comparative, cases, and historical approaches are applied to support normative legal research. Series of inward FDI realization data for the period of 1990 to 2020 from BIT's parties and non-parties are collected from the National Single Window for Investment (NSWI) of the Coordinating Board of Investment (BKPM) for the empirical legal analysis purposes.

Those data of FDI inflows are subsequently put into two groups namely Group 1 (FDI inflows from BIT's parties) and Group 2 (FDI inflows from BIT's non-parties) and being tested using an unequal variance t-test to find out how significant the differences between those two groups (Stephanie Glenn, 2012) with the following hypotheses:

(1) Null hypothesis (H_0) which assumes that the average amount of FDI inflows from BIT's parties and non-BIT's parties is not significantly different (H_0: $u_1 = u_2$); and

(2) Alternative hypothesis (H_1) which assumes that the average amount of FDI from BIT's parties and non-BIT's parties is significantly different (H_1: $u_1 \neq u_2$)

The expected benefit of BIT on FDI flows can be inferred from the difference between those two samples' means. If the null hypothesis cannot be rejected hence the average amount of FDI inflows from BIT's parties and non-BIT's parties is not significantly different. Therefore, one may argue that the amount of inward FDI does not depend on BIT or, in another way around, BIT cannot be deemed as an explanatory variable to determine the FDI inflows. The result is used to support the argument that BIT does not provide benefit to the economy in terms of increased FDI inflows. In contrast, if the difference is statistically significant, BIT might be considered providing benefits to the economy through its role in promoting FDI inflows.

Expropriation Provisions under National and International Law

Expropriation Provision under National Investment Law

Foreign direct investment (FDI) plays important role in the economy of a country, including Indonesia. National policies to create a sound and stable investment climate in Indonesia had been undertaken since the early stage of economic development by declaring an open-door policy in the 1960s. The first national's foreign direct investment act was introduced in 1967 with the main objective to attract FDI inflows in all economic sectors with some exceptions for sectors partially or wholly prohibited for foreign investors.[1] It was stated in the preamble of this act that foreign capital is needed to accelerate Indonesia's economic development especially in sectors that have not been and cannot be utilized optimally by domestic capital alone. Therefore, it is necessary to make clear provisions to meet the need for capital for national development as well as to minimize uncertainty for foreign investors.

[1] Act No.1 Year 1967 concerning Foreign Investment stated that the scope of this act only covered foreign direct investment (Article 1). Some strategic sectors prohibited from wholly-owned by foreign investor such as seaport; telecommunication; airline; nuclear power plant; and mass media. Other sectors called 'national strategic defense sectors' were totally closed for foreign investment (Article 6 paragraph 1)

During the early years since the declaration of independence in 1945, Indonesia had nationalized Dutch-own companies under the program of indigenization ("Indonesianization") in the 1950s (Rustanto, 2012; Wasino, 2016, 2017; Erman Rajagukguk, 2019). The act entitled 'Nationalization of the Dutch Companies' (Nationalization Act) was decreed by the Law No.86 of 1958 which mentioned that the Dutch-own companies in the territory of Indonesia would be nationalized with the transfer of title of ownership fully and independently to the State of Republic of Indonesia (article 1). The amount and method of payment for compensation were determined by a national committee established by government regulation.[2]

The Nationalization Act was ordained on 27 December 1958 or just two months after the first act of foreign capital investment (Act No. 78 Year 1958) was enacted on 27 October 1958. Another nationalization, in particular on American and British companies, continued when political and military conflict with Malaysia happened in the early 1960s but eventually settled amicably as the Government of Indonesia had given back nationalized companies to the respective foreign investors soon after the new Foreign Capital Investment Law No.1 of 1967 (FCIL 1967) was enacted (Rajagukguk, 2019; Rustanto, 2012; M.F. Mukhti, 2015). After a lengthy process, all compensation payments for nationalization were finally settled in 2002 (Wasino, 2016).

The provisions under the FCIL 1967 explicitly mentioned direct and indirect expropriation in article 21 which reads: "government shall not take measures to nationalize/to revoke as a whole or measures to reduce the rights to control and/or to manage of foreign capital companies unless otherwise governed by the act based on public purposes." The decrease of rights to control or to manage foreign property is one characteristic of indirect expropriation (Joubin-Bret (ed.), 2012; Suez, Sociedad General de Aguas de Barcelona S.A., and Vivendi Universal S.A. v The Argentine Republic, 2020; LG&E v Argentina, 2006). However, in the FCIL 1967, there was only the term nationalization mentioned in the elucidation provision but none has explained indirect expropriation. The government was obliged to pay compensation for compensation in which the amount, types, and method of compensation were subject to consent by both parties (host state and foreign investor) in accordance with the principles of international law (article 22(1)).

Disputes on the amount, type, and method of the compensation under FCIL 1967 would be settled through arbitration which the award shall be legally binding to both parties (article 22(2)). Compensation for nationalization is entitled to freely convertible and transferable at the applicable market value (article 9(1e)). The freely convertible amount of compensation at the market value is known as elements of effective and adequate in Hull's formula which is argued as principles

[2]The Government Regulation No.2 Year 1959 was issued as implementing regulation including assigning nationalization committee to determine the scope and types of Dutch's property to be nationalized and establishing State-owned enterprise as companies that occupied nationalized companies. Other government regulations were also introduced to deal with some specific economic sectors of Dutch companies being nationalized such as plantation, mining, maritime, pharmacy, banking, insurance, and printing companies.

of international law to compensation for nationalization besides prompt (Huala Adolf, 2011; Joubin-Bret (ed.), 2012; Catherine Yanaca-Small, 2004). It is important to note that foreign capital companies in the FCIL 1967 are defined as: (a) foreign exchange excluding official foreign exchange reserve which is, subject to government approval, used finance companies in Indonesia; (b) any tools, including new inventions, belong to foreign investors and imported materials that are not financed by official foreign exchange reserves; and (c) reinvestment of repatriated profit (article 2).

The FCIL 1967 was later revoked and replaced by Law No.25 of 2007 concerning Investment.[3] Foreign investment is defined as investing activities to do business in the territory of the Republic of Indonesia that is carried out by foreign investors who use their own whole capital or in partnership with domestic investors (article 1(3)). The scope and types of foreign investors comprise national, business entities, and/or the government of foreign countries (article 1(6)). Provisions of nationalization or expropriation are stipulated in article 7 as follows: (a) the government shall not take measures of nationalization or formal transfer of title of investors unless otherwise provided by the law; (b) if the government takes measures of nationalization or expropriation it will pay compensation with the amount based on the market value that is established in accordance with the internationally-accepted method adopted by an independent appraiser appointed by the parties (government and foreign investor); and (c) if both parties fail to reach an agreement of compensation or indemnification, the dispute shall be settled by arbitration subject to the written consent of both parties.

There is no clear and specific legal conception of nationalization under this new act as well as in the previous act. However, the term nationalization grammatically may be interpreted as the formal transfer of title of foreign propriety to the government as there is a conjunctive word or in the provision between the word nationalization and transfer of title (Muhammad Syaifuddin, 2011). Therefore, the expropriation provision under the current national investment act does not contain indirect expropriation but only nationalization or direct expropriation.[4]

The scope of investment protected under the national investment law of 2007 only covers direct investment as stipulated in the elucidation provision of article 2 which says: "The term "investments in the territory of the Republic of Indonesia" means direct investment and does not include indirect or portfolio investments." Meanwhile, provisions of protection under all Indonesia's BITs apply to a very broad definition of investments which practically includes all kinds of investments either direct, indirect, or portfolio investments. Such broader scope of

[3]The term foreign is no longer exist on the nomenclature of the Law No.25 of 2007 because this new law has merged foreign capital investment law (FCIL 1967) and domestic capital investment law No.6 of 1968. There are provisions of national treatment and most-favored nation in this new law where standard of treatment for investor is no longer based on nationality with some exceptions regarding, inter alia, the form of business entity, the use of the land, and maximum foreign equity participation in particular economic sectors.

[4]The same interpretation that expropriation provision under the investment law of 2007 only contains direct expropriation is also confirmed by the interviews with the high-rank officials of National Investment Coordinating Board and Ministry of Foreign Affairs in 2020 and 2021 respectively.

foreign investments protected under BITs than national law would have been created legal risks that will be discussed below.

4. Expropriation provision under BITs

There is a virtually common provision of expropriation in all Indonesia's ratified BITs where the host State shall not nationalize, expropriate, or subject to measures having an effect equivalent to nationalization or expropriation to the investments of investors of other parties except for public purposes or public interests, on a basis of non-discrimination, carried out under due process of law, and against prompt, adequate and effective compensation.

There is no clarification on the terms nationalization and measures having an effect equivalent to nationalization which refers to indirect expropriation. One way to understand the meaning of such terms is by seeking ordinary meaning through grammatical interpretation. The literal meaning of nationalization is governmental taking or modification of an individual's property rights (Bryan A. Gardner, 2014) and the term measures should refer to laws and regulations concerning foreign investment since the BIT is an investment treaty in which according to article 31(1) of the Vienna Convention on the Law of Treaty (VCLT) 1969, a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose. This argument is confirmed by the article that is frequently found in all Indonesia's BITs (usually under the article of Application of the Agreement) mentioning that BIT shall apply to "…investments by investors of another party in the territory of Indonesia which have been granted admission in accordance with Law No.1 of 1967 regarding Foreign Investment and any act amending or replacing it."

The lawfulness of expropriation is attributed to the public interests or public purposes, non-discrimination, due process of law, and against prompt, adequate, and effective compensation (Hull's formula) that should amount to the fair market value. Although there is no definition of fair market value, some BITs contain commercial interest rates established on the market basis from the date of expropriation until the date of payment of compensation for expropriation.[5] There is no exception clause distinguishing measures having equivalent effect to expropriation from legitimate and bona fide non-compensable measures as the rights to regulate of a sovereign State, such as protection of the environment, public health, and national security. The only exception found in all Indonesia's BITs is related to MFN treatment when one State is the party of a particular economic or customs union or free trade or common market. Despite there is also an automatic MFN clause that one State has to extend more favorable treatment provided in national law or other international agreements to the BIT's party.

Any dispute between foreign investors and the host State will be initially settled amicably through consultation and negotiation. If such a dispute cannot be

[5]Indonesi's BIT with Denmark, Finland, Morocco, Qatar, Russia, South Korea, Ukraine, and Uzbekistan.

settled within certain periods of time, the investor concerned has options to submit the dispute either to the domestic court of the expropriating party or an international arbitration tribunal. Only BIT with UK (1976) directly refers to the ICSID for dispute settlement without an option for the competent court where the investment was made. Consequently, investment dispute settlement through local remedy under Indonesia's BITs is not mandatory but instead voluntary. This condition is consistent with the fact that all known-cases of BIT-based ISDS had been settled through the international tribunal for the case of Indonesia.

The absence of elaboration in respect to definition or categories of indirect expropriation provision, measures as normal and legitimate policy, and the broad definition of investment leaves the interpretation of indirect expropriation against the investment of foreign investors to the private international arbitration tribunal. There is a risk for Indonesia to be constantly claimed solely because any measures adversely affect foreign investor's benefit.

5. Discussions

6. Expected Benefit of BITs

The analysis of expected benefits from BITs is based on the argument that a conclusion of BITs between two states may have an impact on FDI flows in the years following the conclusion of BITs. Based on the fact that Indonesia is regarded as a net foreign capital country, the effect of BITs on FDI will be assumed as a one-way direction i.e. FDI inflows rather than the opposite direction. This argument is supported by the purpose of a treaty-making that is stated under the preamble of BITs which reads, for instance in Indonesia-Qatar BIT: "Recognizing that the promotion and protection of these investments will stimulate the flow of capital and technology between the two Contracting Parties in the interest of economic development." Therefore, immediate economic benefit in terms of a large number of capital flows is supposed to come to realize after signing BITs.

The empirical analysis concerning the benefit of BITs on FDI flows using a t-test is inspired by the study of Jan Peter Sasse (2011) who refers to research conducted by UNCTAD (1998) that run the t-test to find out changes in FDI inflows between pairs of countries as a result of the signing of BITs from 200 observations of the bilateral FDI flows between 72 FDI-recipient countries and 14 home countries during the period of 1971-1994. The result finds a weak effect of BITs on FDI flows.

For the statistical analysis purposes of this study, we collect the data of FDI inflows realization from BIT's parties and non-BIT's parties in US dollar (US$) during the period of 1990-2020 due to the availability of data from the internet-based National Single Window of Investment (NSWI) of the Coordinating Board of Investment (BKPM). The data collected is then put into two groups: Group 1 consists of the realization amount of FDI inflows from BIT's parties and Group 2 consists of the realization amount of FDI inflows from non-BIT's parties. Since those two groups are comprising different sets of data, it is assumed that they are composed of different means or variance therefore an unequal variance T-test is appropriate and, accordingly, two hypotheses are set as follows:

(1) H_0 (null hypothesis): The mean of FDI amount between counties as parties and non-parties of BITs is not different ($u_1 = u_2$); and

(2) H_1 (alternative hypothesis): The mean of FDI amount between counties as parties and non-parties of BITs is different ($u_1 \neq u_2$).

The result of the T-test shows P-value equals 19%, which is below t-critical value with α = 0.05 (two-tailed), hence the null hypothesis (H_0: $u_1 = u_2$) cannot be rejected (Diagram 1). It can be inferred that the difference between the average amount of FDI inflows from the group of countries that signed BITs with Indonesia and the group of countries that do not have BITs with Indonesia is not statistically significant. This result may conclude that inward FDI flows is irrespective of the BITs signed and ratified by Indonesia.

Diagram 1. T-Test: Two-Sample Assuming Unequal Variances

	u_1	u_2
Mean	1594421,134	3952080,298
Variance	3,34702E+13	2,07345E+14
Observations	74	75
Hypothesized Mean Difference	0	
df	98	
t Stat	-1,314505896	
P(T<=t) one-tail	0,095872081	
t Critical one-tail	1,660551217	
P(T<=t) two-tail	0,191744162	
t Critical two-tail	1,984467455	

Based on the statistical result, one may argue that the expected benefit from BIT as an international legal instrument to promote FDI inflows to Indonesia should be refuted. The empirical evidence might be taken into consideration to support rational ground for the previous intention of the government of Indonesia to terminate all BITs in addition to numerous treaty-based investment dispute cases involving millions or billions of dollars in claims and potential damages through the ISDS mechanism (David Price, 2017; Anthony Crockett, 2017; Eka Husnul Hidayati et al, 2017).

There are many studies on the determinants of FDI flows to Indonesia. One of the studies concludes that economic growth, inflation rate, and trade openness are determinant factors of FDI flows (Claudia Putri and Regina Wilantari, 2016). Another scholar argues that labor cost, natural resources, size of the economy, human capital, transfer of technology, tax incentive, and special status in international trade (such as Generalized System of Preferences) are leading factors of foreign capital investment in Indonesia (Rajagukuguk, 2019). Another study concludes that inward FDI was determined by the trend of previous inward FDI, GDP of host and home country, relative productivity, bilateral trade, trade volume, natural resources, and distance (Triono Widodo and Shinta Soekro, 2015).

7. The Expected Cost of BITs

For the calculation of the costs of BITs, we are encouraged by a study of Lise Johnson et al (2018) who classifies the cost of BITs into monetary and non-monetary costs. Monetary cost may comprise the cost of litigation and cost of liability while non-monetary cost may consist of reputational costs, costs in term of reduced policy space, costs in term of reduced power in contractual relations, costs in terms of a reduced role for domestic law-making, and costs in terms of generating uncertainty in the law. Another study also takes into account the fiscal cost arising from expenses for negotiating and administering BITs (Joachim Pohl, 2018).

8. Monetary costs of BITs

As mentioned in introduction section, Indonesia was a respondent of seven known-cases of investment disputes under ISDS mechanisms. Three cases were dismissed or settled through extra-judicial processes whereas four cases were brought by the respective claimants who alleged that Indonesia has breached indirect expropriation and FET provisions. The amount of claim for compensation was stretched from US$75 million to US$1.3 billion (see Table 1).

There is no publicly available information regarding the cost of litigation but we can refer to one study mentioning that the average cost of litigation may reach US$7.41 million for the claimant and US$5.19 million for the respondent (Aceris Law LLC, 2017). The cost borne by the respondent will be higher when the respondent loses the case and has to pay compensation to the claimant. In some cases, the tribunal has ordered to seize respondent's assets abroad if the respondent fails to pay compensation to the claimant (Adolf, 2014; Aldo Rico Geraldi, 2015).

With regard to the fiscal cost of the treaty-making process from preparation to a conclusion, it can be assumed a priori that each BIT might take five rounds of negotiation to complete. Let now assume that each round of negotiation involves at least five persons from each party or ten persons for both delegates within two days of negotiation, each person gets US$300 for allowance (or US$6,000 in total for two days of negotiation), US$2,000 for round trip transportation cost (or US$40,000 in total), and US$200 for accommodation (or US$4,000 in total), therefore total expenses would be approximately cost US$50,000 for each round of negotiation or US$250,000 in total (US$50,000 times five rounds of negotiation). If there are 100 BITs hence the total cost of such a treaty-making process would be US$2,500,000. All of these figures are of course very much burdensome to the state's budget.

ISSN 2029-0454
2023

9. Non-monetary cost of BITs

There is a virtually common provision of expropriation in all Indonesia's ratified BITs where the host state shall not nationalize, expropriate, or subject to measures having an effect equivalent to nationalization or expropriation to the investments of investors of other parties except for public purposes or public interests, on a basis of non-discrimination, carried out under due process of law, and against prompt, adequate and effective compensation. For example, in Indonesia-Russia BIT (signed in 2007 and entry into force in 2009), the provision of expropriation reads:

1. Investments of investors of one Contracting Party made in the territory of the other Contracting Party shall not be nationalized, expropriated or subjected to measures having effect equivalent to nationalization or expropriation (hereinafter referred to as "expropriation'') except when such measures are taken for public interests in accordance with the procedure established by the laws and regulations of the latter Contracting Party, on a non-discriminatory basis and entail prompt, adequate and effective compensation.
2. The compensation shall amount to the market value of the expropriated investments at the time immediately before the date of expropriation or before the date when the expropriation becomes publicly known, whichever is the earlier. Such compensation shall be paid in freely convertible currency.
3. The compensation shall be paid without delay. In case of delay the compensation shall also include interest calculated from the date of expropriation until the date of payment at the rate equivalent to the commercial rate established on a market basis, but no lower than LIBOR rate on respective U.S. dollar credits.

There is no clarification on the terms nationalization and measures having an effect equivalent to nationalization which refers to indirect expropriation.[6] One way to understand the meaning of such terms is by seeking ordinary meaning through grammatical interpretation. According to the Black's law dictionary, the literal meaning of nationalization is governmental taking or modification of an individual's property rights (Gardner, 2014) and the term measures may refer to laws and regulations concerning foreign investment since the BIT is an investment treaty according to article 31(1) of VCLT 1969. This argument is confirmed by the provision under the article of The Scope of the Agreement that is frequently found in all Indonesia's BITs. For example, in Indonesia-Sweden BIT (signed in 1992 and entry into force in 1993) it reads:

[6]The terms indirect expropriation is also known in various legal concepts, inter alia, measures tantamount to nationalization, regulatory expropriation, or creeping expropriation. Creeping expropriation, for example, is defined as an act or series of act by the host State over a period of time to incrementally erode foreign investor's property through regulatory measures and regulatory expropriation may refer to an act or measures taken in the exercise of State's rights to regulate than can lead to significant impairment of foreign investment (see, for example, Sornarajah, 2010 and Joubin-Bret (ed.), 2012)

This Agreement shall apply to investments by investors of the Kingdom of Sweden in the territory of the Republic of Indonesia which have been previously granted admission in accordance with Law Number 1 of 1967 concerning Foreign Investment and any law amending or replacing it and to investments by investors of the Republic of Indonesia in the territory of the Kingdom of Sweden in accordance with its laws and regulations.

Investment of foreign investor that is protected from being expropriated directly or indirectly in all Indonesia's BITs typically cover all kinds of investments, including tangible or intangible asset, movable or immovable asset, both direct and portfolio investment, like stated in the Indonesia-South Korea BIT (signed in 1991, entry into force in 1994), as follow:

Investments means every kind of asset invested by investors, including but not exclusively:

1. movable and immovable property and any other property rights such as mortgages, liens or pledges;
2. shares, stocks and debentures of companies wherever incorporated or interests in the property of such companies;
3. claims to money or to any performance related to investment having a financial value;
4. intellectual property rights including copyright, commercial trademark, patents, industrial designs, know-how, trade secrets and trade names, and goodwill;
5. business concessions conferred by law or under contract related to investment including concessions to search for, cultivate, extract or exploit natural resources.[7]

The lawfulness of expropriation is attributed to the public interests or public purposes, non-discrimination, due process of law, and against prompt, adequate, and effective compensation (Hull's formula) that should amount to the fair market value. Although there is no definition of fair market value, some BITs contain commercial interest rates established on the market basis from the date of expropriation until the date of payment of compensation for expropriation.[8]

There are no exception clauses distinguishing measures having equivalent effect to expropriation from legitimate and *bona fide* non-compensable measures as the rights to regulate of a sovereign state, such as protection of the environment, public health, and national security. The only exception found in all Indonesia's BITs is related to MFN treatment when one state is the party of a

[7]Such a broad asset-based definition of investment might be found in almost all international investment agreements including in the world's first BIT between Pakistan and Germany of 1959 which defined investment as: "..capital brought into the territory of the other Party for investment in various forms in the shape of assets such as foreign exchange, goods, property rights, patents and technical knowledge…, returns derived from and ploughed back into such investment..., any partnerships, companies or assets of similar kind, created by the utilization of the above mentioned assets…" (Treaty between the Federal Republic of Germany and Pakistan for the Promotion and Protection of Investment, 25 November 1959, <https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/1387/download> [accessed 4 March 2021]

[8]Indonesia's BIT with Denmark, Finland, Morocco, Qatar, Russia, South Korea, Ukraine, and Uzbekistan.

particular economic or customs union or free trade or common market. Despite there is also an automatic MFN clause that one state has to extend more favorable treatment provided in national law or other international agreements to the BIT's party.

Any dispute between foreign investors and the host state will be initially settled amicably through consultation and negotiation. If such a dispute cannot be settled within certain periods of time, the investor concerned has options to submit the dispute either to the domestic court of the expropriating party or an international arbitration tribunal. Only under BIT with United Kingdom in 1976 that the dispute should be submitted directly to the ICSID without an option for the competent court where the investment was made as stipulated in article 7 that reads:

Contracting Party in the territory of which a national or company of the other Contracting Party makes or intends to make an investment shall assent to any request on the part of such national or company to submit, for conciliation or arbitration. to the Centre established by the Convention of the Settlement of Investment Dispute between States and Nationals of the Other States opened for signature at Washington on 18 March 1965 any dispute that may arise in connection with the investment.

Consequently, investment dispute settlement through local remedy under Indonesia's BITs is not mandatory but instead voluntary. This condition is consistent with the fact that all known-cases of BIT-based ISDS had been settled through the international tribunal for the case of Indonesia.

The absence of elaboration in respect to the definition or criteria of indirect expropriation provision, measures as normal and legitimate policy, and the broad definition of investment leaves the interpretation of indirect expropriation against the investment of foreign investors to the private international arbitration tribunal. Thus, there are legal risks for the government to be constantly claimed solely because any measures adversely affect foreign investor's interests. Such legal risks are even getting bigger when the scope of investment protected under all Indonesia's BITs comprises any kind of asset (broad asset-based) which is more comprehensive than the scope of investment under national law that only covers direct investment but does not include indirect or portfolio investments (elucidation of article 2 under the investment law of 2007).

Comparative Study: BIT Model of India and BIT Model of Brazil

This study uses the Indian BIT model and the Brazilian BIT model as a comparison since they are considered to represent emerging economies from Asia and Latin America respectively which have similar characteristics to Indonesia that also members of the G20. India is the second-most populous country in the world

 ISSN 2029-0454
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whereas Indonesia and Brazil come the fourth and the sixth in 2019.[9] The size of the economy of those countries is among the biggest with GDP (current price) worth US$9.65 trillion for India, US$ 3.24 trillion for Brazil, and US$3.61 trillion for Indonesia.[10] The numbers of BITs signed, in force, and terminated by Indonesia, India, and Brazil is shown in Table 2.

Table 2 Number of BITs of Indonesia, India, and Brazil

Country	**Number of BITs**		
	Signed (not in force)	Entry into force	Terminated
Indonesia	16	25	23
India	4	9	73
Brazil	25	2	none
Source: UNCTAD, International Investment Navigator			

10. BIT Model of India

India's BIT model was completed in 2015 with some important and interesting features as follows (Ministry of Finance of the Government of India, 2015). The scope of investment granted protection covers enterprise-based as well as assets-based directly linked to enterprise-based investments that have characteristics of an investments comprising four elements of the *Salini* test namely contribution of money or capital, certain duration over which investments are made, expectation of profit and risks, and contribution to the development of the host party’s economy (Alex Grabowski, 2014; Jeremy Marc Exelbert, 2016).

There are provisions of exceptions for foreign enterprise’s assets regarded as investments protected under the BIT such as portfolio investments, government-issued debt securities, pre-operational expenditure for investments, and claims to money solely arise from commercial contracts for the sale of goods or services, listed in a non-exhaustive list (article 1(1.4)).

There is also definition of measures that includes a law, regulation, rule, procedure, decision, administrative action, requirement or practice (article 1(1.8)). Measures by local government, taxation measures, government procurement, subsidies or grants, services supplied in the exercise of governmental authority that is not commercial basis are excluded from the application of treaty (article 2(2.4)).

Treatment of investments provision stipulates, among others, the term customary international law which defines in the footnote of article 3(3.1) which reads: “a general and consistent practice of states that they follow from a sense of legal obligation”. Some notions of violation of customary international law also described in the exhaustive list involving denial of justice; breach of due process;

[9] World Bank, Population Total, <https://data.worldbank.org/indicator/SP.POP.TOTL?name_desc=false> [accessed 24 March 2021]
[10] IMF Data Mapper, GDP Current Price, <https://www.imf.org/external/datamapper/PPPGDP@WEO/IND/BRA/IDN> [accessed 24 March 2021]

discrimination on unjustified grounds such as gender, race, or religious belief; or abusive treatment such as coercion, duress, and harassment. The treaty model has also provisions that oblige foreign investors to comply with all laws and regulations applicable in the host state, including taxation measures, and voluntarily participate in corporate social responsibility (article 12).

Provision of expropriation is mentioned in article 5 that contains direct and indirect expropriation which some clarifications that direct expropriation occurs when there is formal transfer of title or outright seizure whereas indirect expropriation arises if measures of a host state have substantially or permanently deprived foreign investor's property without a formal transfer of title or outright seizure. There are also determinants of measures deemed as indirect expropriation which include duration of measures, character of measures, and whether the measures have breached prior binding written commitments. However, sole effect doctrine cannot establish indirect expropriation and those determinants require a case-by-case, fact-based inquiry.

The exhaustion of domestic remedies is compulsory which the claim must be submitted within one year from the date on which the foreign investors first acquired or the damages or losses since the host state measures have occurred (article 15). A written consent is required for the submission of claim to international arbitration (article 17).

11. BIT Model of Brazil

It is interesting to note that Brazil signed 14 BITs in the 1990s but none of them are approved by the Congress to be in force due to problems in the traditional model of BIT. For example, the investor-to-state dispute settlement provisions within BIT would limit the state's right to regulate and excessive protection to foreign investors could discriminate against domestic investors (Jose H.V. Martins, 2017). One study identified another concern that payment for compensation without undue delay in freely convertible currencies under expropriation provision in traditional BIT is deemed unconstitutional (Felipe Hees et al, 2018). Nonetheless, Brazil continues to be one of the world's top recipients of FDI which supports the view that FDI inflows are irrespective of having BIT in force (UNCTAD, 2020).

The Government of Brazil established a new model of BIT in 2012-2015 to address three main problematic provisions in traditional BIT i.e. the possibility of indirect expropriation, protection of portfolio investments, and recourse to ISDS mechanism (Hees et al, 2018). The new BIT model called Cooperation and Facilitation Agreement on Investments (CFAI) is composed of five parts namely Scope of the Agreement and Definitions (Part I), Regulatory Measures and Risk Mitigation (Part II), Institutional Governance and Dispute Prevention (Part III), Agenda for Further Investment Cooperation and Facilitation (Part IV), and General and Final Provisions (Part V). There is one annex called Agenda of Further Investment Cooperation and Facilitation which contains cooperation at facilitating remittances, visa arrangement, procedure of technical requirement and environmental standards, and cooperation on regulation and institutional exchange (UNCTAD, 2022).

Unlike most commonly found in traditional BITs, portfolio investment is excluded from the definition of investment hence CFAI only covers foreign direct investment (enterprise-based) which is a kind of investment that plays essential role in promoting sustainable development as mentioned in the preamble of CFAI (article 3(1.3)). There is broad definition of measures which includes any measures in the form of laws, regulation, rule, procedure, decision, administrative ruling, or any other form (article 3(1.6)).

There are articles of NT (article 5) and MFN (article 6) with the classification of the term 'like circumstances' that depends on the totality of circumstances and reservations for treatment arising from the agreement with the third party such as free trade area. There is also an expropriation provision that only covers nationalization or direct expropriation which is prohibited unless for public purposes, taken in a non-discriminatory manner, subject to payment for compensation, and in accordance with due process of law (article 7). Prudential measures article is also mentioned in the same language as the Annex of Financial Services of General Agreement of Trade in Services (GATS) of paragraph 2 (article 12).

The treaty mandates the establishment of a Joint Committee (article 17) and the appointment of an Ombudsman of each country to oversee the implementation of the CFAI and assist each other in resolving disputes between the two countries (article 18). There is no ISDS in the CFAI so that investment disputes are resolved through the state-to-state dispute settlement mechanism or in CFAI it is called the *Settlement of Disputes between Parties* (article 24), with the following stages: first, consultation and negotiation through the Joint Committee and the Ombudsman. Second, if the first stage fails to reach consensus, it will be continued through the ad hoc Arbitral Tribunal which was formed based on the CFAI. Third, if the second stage fails to reach an agreement, one of the parties, based on mutual agreement, can register the claim to any permanent arbitration institution.

Brazil has signed CFAI with 13 countries since 2015 where two of them were entered into force (Angola in 2017 and Mexico in 2018) (UNCTAD, 2022).[11] The treaties signed with Mexico, Colombia, and Chile follow the CFAI's template with some additional articles containing wider scope of regulatory carve-out provisions (including non-precluded measures), provisions on fight against corruption and illegality, detailed regulation of arbitration, and clarifications to a number of provisions. Those provisions are also taken into account during the discussion of the MERCOSUR Protocol on Investment Cooperation and Facilitation deemed as 'ring-fencing' provisions mainly to secure state's rights to regulate (Facundo P. Aznar and Henrique C. Moares, 2017).

[11]The 13 CFIAs parties are (from the latest): India (2020), Ecuador (2019), Morocco (2019), United Arab Emirates (2019), Guyana (2018), Suriname (2018), Ethiopia (2018), Angola (2015), Chile (2015), Colombia (2015), Malawi (2015), Mexico (2015), and Mozambique (2015)

12. Conclusion

This study finds that the expected economic benefit from BITs as international legal instruments that are designated to stimulate inward FDI flows is not supported by empirical evidence. The statistical result shows no significant difference in the average amount of FDI inflows between BIT's parties and non-BIT's parties during 1990-2020. On the contrary, the costs of BITs are unavoidable arisen from the legal risk as well as monetary risks that are very much troublesome to the state's budget. Based on those results, when one state is assumed as a rational actor, the only rational policy option is to terminate all existing BITs. The termination of BITs could be done gradually and in case-by-case basis with the priority on the BITs with countries that have none of inward FDI realization.

However, in practice, such a policy option would not always be the first-best solution due to some non-economic variables such as geopolitics concerns whereas BITs are considered as signaling tool of legal protection to foreign investment. Therefore, it would be worth to propose the idea that some BITs provisions should be reconstructed in order to have more clear and firmed objectives of the treaty emphasizing straightforwardly to encourage FDI inflows without bringing in unnecessary legal risks and monetary costs. Consequently, the new template of BIT must be reformulated which focus on provisions of facilitation and cooperation of investment. Moreover, some provisions should be reconstructed through, among others, the exclusion of indirect expropriation provision, the omission of portfolio investment as protected investments, additional provisions of prudential carve-out (non-precluded measures), and abolishing ISDS regime with the obligation of the exhaustion of domestic remedies. India's BIT model and Brazil's CFAI could be taken into consideration as references for the reformation of Indonesia's BIT model to minimize the cost and at the same time encourage the economic benefit of BIT in terms of increasing more inward FDI flows.Appendix - Indonesia's Bilateral Investment Treaties (BITs)

1. Terminated BITs

No	Country	Date of signature	Entry into force	Date of termination	Type of termination	New BIT signed	Entry into force	Date of termination	Type of termination	Sunset clause (years)
1	Australia	17/11/1992	29/07/1993	06/08/2020	Terminated by consent					15
2	Viet Nam	25/10/1991	03/04/1994	07/01/2016	Unilaterally denounced					10
3	Malaysia	22/01/1994	27/10/1999	20/06/2015	Unilaterally denounced					10

4	Lao PDR	18/10/1994	14/10/1995	13/10/2015	Unilaterally denounced					10
5	China	18/11/1994	01/04/1995	31/03/2015	Unilaterally denounced					10
6	Cambodia	16/03/1999	NA	07/01/2016	Unilaterally denounced					10
7	Netherland	07/07/1968	17/07/1971	01/07/1995	Replaced by new BIT	06/04/1994	01/07/1995	30/06/2015	Unilaterally denounced	15
8	Germany	08/11/1968	19/04/1971	02/06/2007	Replaced by new BIT	14/05/2003	02/06/2007	01/06/2017	Unilaterally denounced	20
9	Norway	26/11/1969	NA	01/10/1994	Replaced by new BIT	26/11/1991	01/10/1994	30/09/2004	Unilaterally denounced	10
10	Belgium	15/01/1970	17/06/1972	16/06/2002	Expired					effective period of contracts
11	France	14/06/1973	29/04/1975	29/04/2015	Unilaterally denounced					authorized duration of investments
12	Switzerland	06/06/1974	09/04/1976	08/04/2016	Unilaterally denounced					authorized duration of investments
13	Italy	25/04/1991	25/06/1995	23/06/2015	Unilaterally denounced					10
14	Hungary	20/05/1992	13/02/1996	12/02/2016	Unilaterally denounced					10
15	Egypt	19/01/1994	29/11/1994	30/11/2014	Unilaterally denounced					10

16	Slovakia	12/07/1994	01/03/1995	28/02/2015	Unilaterally denounced					10
17	Spain	30/05/1995	18/12/1996	18/12/2016	Unilaterally denounced					10
18	Kyrgyzstan	19/07/1995	23/04/1997	18/02/2018	Unilaterally denounced					10
19	Argentina	07/11/1995	01/03/2001	19/10/2016	Terminated by consent					10
20	Pakistan	08/03/1996	03/12/1996	02/12/2016	Unilaterally denounced					10
21	Turkey	25/02/1997	28/09/1998	07/01/2016	Unilaterally denounced					10
22	India	10/02/1999	22/01/2004	07/04/2016	Unilaterally denounced					15
23	Bulgaria	13/09/2003	23/01/2005	25/01/2015	Unilaterally denounced					10

Entry into force BITs						**Signed but not yet entry into force BITs**		
No	Country	Date of signature	Entry into force			No	Country	Date of signature
1	Qatar	18/04/2000	17/02/2018			1	Singapore	11/10/2018
2	Denmark	22/01/2007	15/10/2009			2	Serbia	06/09/2011
3	Russia	06/09/2007	15/10/2009			3	Libya	04/04/2009
4	Iran	22/06/2005	28/03/2009			4	Guyana	30/01/2008
5	Finland	12/09/2006	02/08/2008			5	Tajikistan	28/10/2003
6	Saudi Arabia	15/09/2003	05/07/2004			6	Croatia	10/09/2002
7	Venezuela	18/12/2000	23/03/2003			7	Philippines	12/11/2001
8	Morocco	14/03/1997	21/03/2002			8	Algeria	21/03/2000
9	Mozambique	26/03/1999	25/07/2000			9	North Korea	21/02/2000
10	Mauritius	05/03/1997	28/03/2000			10	Chile	07/04/1999
11	Syria	27/06/1997	20/02/2000			11	Jamaica	10/02/1999
12	Cuba	19/09/1997	29/09/1999			12	Zimbabwe	10/02/1999
13	Czech	17/09/1998	21/06/1999			13	Yemen	20/02/1998

14	Bangladesh	09/02/1998	22/04/1999			14	Sudan	10/02/1998
15	Mongolia	04/03/1997	13/04/1999			15	Suriname	28/10/1995
16	Jordan	12/11/1996	09/02/1999			16	Turkmenistan	02/06/1994
17	Thailand	17/02/1998	05/11/1998					
18	Sri Lanka	10/06/1996	21/07/1997					
19	Ukraine	11/04/1996	22/06/1997					
20	Uzbekistan	27/08/1996	27/04/1997					
21	South Korea	16/02/1991	10/03/1994					
22	Poland	06/10/1992	01/07/1993					
23	Sweden	17/09/1992	18/02/1993					
24	Tunisia	13/05/1992	12/09/1992					
25	United Kingdom	27/04/1976	24/03/1977					
Source: UNCTAD, International Investment Agreements Navigator								

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