ALIENATING THE PRIVATE SECTOR: IMPLICATIONS OF THE INVALIDATION OF THE WATER LAW BY THE INDONESIAN CONSTITUTIONAL COURT

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INTRODUCTION

Infrastructure development has been the primary concern of President Joko Widodo's Government. The Government plans to achieve universal coverage in water supply and sanitation by 2019.[1] Water is also an important element of most industrial activities: electricity, mining, agriculture, manufacturing and textiles, without which it would be impossible for such industries to operate. The Indonesian Water Resources Law No 7/2004 ('Water Law') regime has been the subject of several Judicial Reviews, culminating in the law being invalidated in 2015.

Ten years ago the Water Law was declared 'Conditionally Constitutional' by the Constitutional Court ('2005 Decision').[2] Conditionally Constitutional means that the Constitutional Court (CC) refused to grant the petition to invalidate a particular law at that time, but provides conditions whereby the law should be interpreted. In practice, this enables the Court CC to act as a 'positive' legislator by providing conditions relating to how the text of a particular law should be interpreted – sometimes, in contradiction of the actual wording of the legal text.[3]

In the 2005 Decision the CC specifically demanded that the Government 'pay attention' to the CC's considerations. The CC stated that:

> the Government should respect, protect and fulfill the human right to water, and in the Law's implementing regulation, the Government should pay attention to the CC's considerations, which constitute the basis or rationale of this decision.

It further prescribed that:

> … if the said law is interpreted differently from the intentions as laid out in the consideration part of this decision, then a future re-judicial review is a possibility (conditionally constitutional).[4]

Nevertheless, after the Water Law was declared *Conditionally Constitutional* in 2005, everything was 'business as usual'. Various water Private Sector Participation contracts were auctioned, facilitated by the Supporting Body for the Development and Drinking Water Provision System (BPPSPAM).[5] Existing 'concession' contracts, including the Jakarta Water Concessions, remained operational. Nothing really changed. Perhaps this was because the term *conditionally constitutional* was quite a new term which was not properly understood at the time. Business actors and the Government considered that the law was still nominally in place and the Government did nothing to adjust the Water Law's implementing regulations in accordance with the CC's prescription.

The Government Regulation 16 Year 2005 which regulates water services was never repealed by the Government, although this was one of the implementing regulations disputed during the 2005 trials. Furthermore, during 2008–2014 the Government had been drafting a Government Regulation on Water Use Right, which implements the provisions relating to water 'exploitation' rights (*hak guna usaha air*) in the Water Law, which were heavily disputed during the CC trials.

Finally, in 2013 a group of organisations spearheaded by the Muhammadiyah, a 40-million strong Muslim organisation, filed a petition to invalidate the Water Law. In 2015 the CC finally granted this petition, referring to the 2005 trials and the previous CC Decisions and cited that the Government had done nothing to align the implementation of the Water Law in accordance with the CC's prescriptions.

As a result the Water Law was invalidated and in order to prevent a legal vacuum, the CC reinstated Law 11 Year 1974 on Irrigation along with its implementing regulations ('2015 Decision'). The invalidation of the Water Law also meant that all implementing regulations based on the Water Law were no longer in force. Thus, although Law 11/74 on Irrigation was reinstated, there remains a huge lacuna on provisions regarding water resources and services in Indonesia.

A new water law is currently being drafted, but it may be a long time before it is finally enacted. The 2015 Decision had overarching consequences for water governance in Indonesia as it rearranged the role of the private sector in water resources management. This paper seeks to identify issues which affect the private sector.

1 Ministry of National Development Planning (Bappenas) 'Penyusunan Rencana Pembangunan Jangka Menengah Nasional (RPJMN) 2015–2019'.

2 Mohamad Mova Al'Afghani 'Constitutional Court's Review and the Future of Water Law in Indonesia' (2006) 2 *Law, Environment and Development (LEAD) Journal* (2006).

3 Bisariyadi Bisariyadi 'Atypical Rulings of the Indonesian Constitutional Court' (2016) 1 *Hasanuddin Law Review* 225.

4 *Putusan Mahkamah Konstitusi No 058-059-060-063/PUUII/2004 Tentang Pengujuan Undang Undang Nomor 7 Tahun 2004 Tentang Sumber Daya Air.* See p 495.

5 See the list of opportunities in brownfield and greenfield projects. 'KPS Yang Masih Berpeluang' (20 October 2012) https://web.archive.org/web/20121020184303/http://www.bppspam.com/index.php?option=com_content&view=article&id=63&Itemid=72 accessed 28 January 2017.

Although the whole Water Law judicial review controversy is about the private sector, it is to be noted that the term 'private' (*swasta*) has never been appropriately defined in the 2005 and 2015 Decisions. In both Decisions, the CC often used the term 'private' to cover all non-state and non-state owned/region-owned entities. This ambiguity carries important consequences as will be discussed below. The term 'private' in this paper thus covers all entities which are non-state and non-state-owned/region-owned enterprises.

THE 2015 JUDICIAL REVIEW

(a) Constitutional Jihad and bottled water

The 2015 case differed from the 2005 case in two aspects: (i) the petitioners and (ii) the weight given to bottled water.

The 2005 Judicial Review was initiated by a number of non-governmental organisations in a culmination of their discontent during the drafting process of the 2004 Water Law. Back in 2004, these NGOs had voiced their concern over the Water Bill, suggesting that the Bill was highly influenced by the World Bank's Water Sector Adjustment Loan (WATSAL) Project[6] and was weighted towards commercialisation, privatisation and liberalisation of the water sector. However, the Bank subsequently denied that it exerted influence.[7] Eventually, the Water Bill was passed into law and shortly after this the NGOs formed a coalition to petition for the invalidation of the Water Law.[8] This effort resulted in the 2005 Decision declaring that the Water Law remained valid but 'conditionally constitutional'.

Although the aspiration was quite similar, the 2015 Judicial Review was different since it was spearheaded by Muhammadiyah as part of their so-called 'Constitutional Jihad'.[9] This is a series of ongoing efforts by the Muhammadiyah to invalidate laws which they deem to be too liberal and to reintroduce welfare state concepts into Indonesia's socio-economic system.[10] The Constitutional Jihad started with the Judicial Review of the oil and gas law in which the CC dissolved the State Upstream Oil and Gas Agency (2012 Oil and Gas Decision).[11]

The fact that the 2015 Judicial Review was conducted by mass organisations, spearheaded by Muhammadiyah, means that it was not taken lightly, especially by the CC, culminating in the Court's invalidation of the Water Law. However, other economic aspects might have been at play. In one article a representative of a bottled water association appreciates the Constitutional Jihad but 'expected' that such efforts carried no 'hidden agenda' or were 'steered' by certain parties.[12]

It is not possible to ascertain what these economic motives are, but in 2014 the then Chairman of Muhammadiyah, Din Syamsuddin, considered drinking bottled mineral water to be *haram* (religiously forbidden). He was quoted as saying: 'Bottled water shall not be surrendered to the private sector, especially foreign investors. Water should be controlled by the state.'[13] In the 2014 Congress, Muhammadiyah published *Fiqh Air* (Islamic Jurisprudence on Water).[14] After the Water Law was invalidated in 2015, Muhammadiyah demanded that the private sector stop controlling bottled water and that contracts which arranged the management of water resources with the private sector be annulled.[15] Interestingly, following the CC 2015 Decision, despite this stance, several branches of the Muhammadiyah in the regions, especially in Eastern and Central Java, started to enter the bottled water business.[16]

(b) The Six Basic Principles of Water Governance

In the 2015 Decision, the CC attempted to develop a set of principles in order to help the Government in formulating water regulation and policies that are in line with the Constitution. This came to be known as the Six Basic Principles of Water Governance:

1. Water commercialisation shall not impede, override, and/or abolish the right of the people to the land, water and the natural riches contained therein. They shall be controlled by the state and exploited to the greatest benefit of the people.
2. The state shall fulfill the people's right to water since the access to water is a human right. Article 28I(4) Constitution 1945 stipulates that 'Protecting, advancing, upholding and fulfilling the human rights

6 *Putusan Mahkamah Konstitusi No. 058-059-060-063/PUUII/2004 Tentang Pengujuan Undang Undang Nomor 7 Tahun 2004 Tentang Sumber Daya Air* (n 4). See p 211.

7 See Ibnu Sina Chandranegara, 'Purifikasi Konstitusional Sumber Daya Air Indonesia' (2016) 5 21; Dwi Agus Susilo and others, 'Diskursus Pengelolaan Sumber Daya Air Di Indonesia (studi Kasus Tahun 2002—2015)' (2016) 4 *Sodality: Jurnal Sosiologi Pedesaan* http://journal.ipb.ac.id/index.php/sodality/article/view/14430 accessed 20 June 2018.

8 'RUU SDA Disahkan, Koalisi Air Siapkan Judicial Review' (*hukumonline.com*) http://www.hukumonline.com/berita/baca/hol9715/ruu-sda-disahkan-koalisi-air-siapkan-ijudicial-reviewi accessed 4 March 2017.

9 'Pro Kontra "Jihad Konstitusi"' (*hukumonline.com*) http://www.hukumonline.com/berita/baca/lt554b3a674a7d6/pro-kontra-jihad-konstitusi accessed 4 March 2017.

10 Kompas Cyber Media 'Jihad Konstitusi, Upaya Muhammadiyah Meluruskan "Kiblat" Bangsa' (*KOMPAS.com*) http://nasional.kompas.com/read/2016/06/08/07010001/Jihad.Konstitusi.Upaya.Muhammadiyah.Meluruskan.Kiblat.Bangsa accessed 4 March 2017; 'Fakultas Hukum Universitas Muhammadiyah Jakarta JIHAD KONSTITUSI DAN PURIFIKASI ARAH PEMBANGUNAN HUKUM NASIONAL MENURUT UUD 1945' https://fh.umj.ac.id/jihad-konstitusi-dan-purifikasi-arah-pembangunan-hukum-nasional-menurut-uud-1945/ accessed 4 March 2017.

11 *Putusan Nomor 36/PUU-X/2012 Tentang Pengujian Undang-Undang Nomor 22 Tahun 2001 tentang Minyak dan Gas Bumi.*

12 'Pro Kontra "Jihad Konstitusi" ' (n 9).

13 'Din Syamsudin: Bagi Saya, Air Kemasan Itu Haram' (*merdeka.com*) https://www.merdeka.com/peristiwa/din-syamsudin-bagi-saya-air-kemasan-itu-haram.html accessed 4 March 2017.

14 'Terbitkan Buku Fikih Air, "Wujud Kepedulian Muhammadiyah Terhadap Lingkungan Hidup" ' http://tarjih.or.id/terbitkan-buku-fikih-air-bentuk-perhatian-muhammadiyah-terhadap-lingkungan-hidup/ accessed 4 March 2017.

15 Kompas Cyber Media 'Muhammadiyah Minta Pihak Swasta Stop Kelola Air Kemasan' (*KOMPAS.com*) http://nasional.kompas.com/read/2015/02/23/15410661/Muhammadiyah.Minta.Pihak.Swasta.Stop.Kelola.Air.Kemasan accessed 4 March 2017.

16 'Air Kemasan Q-Mas M Lirik Kerjasama Dengan MEK PDM Jember' (*JemberMU*) http://www.jembermu.com/2017/02/air-kemasan-q-mas-m-lirik-kerjasama.html accessed 4 March 2017; 'Muhammadiyah Karanganyar Bangun Pabrik Air Minum Dalam Kemasan (AMDK) - Pimpinan Daerah Muhammadiyah Kabupaten Karanganyar' http://karanganyar.muhammadiyah.or.id/berita-8507-detail-muhammadiyah-karanganyar-bangun-pabrik-air-minum-dalam-kemasan-amdk.html accessed 4 March 2017; 'Muhammadiyah Lamongan Akan Bangun Perusahaan Air Minum Mineral Kemasan' https://www.muhammadiyahlamongan.com/blog/muhammadiyah-lamongan-akan-bangun-perusahaan-air-minum-mineral-kemasan/ accessed 4 March 2017.

are the responsibility of the state, especially the Government.'

3. Environmental sustainability is a part of human rights; therefore, Article 28H(1) Constitution 1945 states: 'Every person shall have the right to live in physical and spiritual prosperity, to have a home and to enjoy a good and healthy environment, and shall have the right to obtain medical care'.
4. Based on Article 33(3) Constitution 1945, water, which is an important sector of production that affects the lives of the people, shall be under the powers of the state, and shall be used to the greatest benefit of the people. Therefore, the state's supervision and control regarding water is absolute.
5. Another form of control by the state due to the importance of water for the lives of the people, is prioritising permits for water commercialisation to the State-Owned Enterprise (BUMN) or Region-Owned Enterprise (BUMD).
6. In the event all the restrictions above have been fulfilled and there is an availability of water, the Government may grant permits to private enterprises to commercialise water based on strict requirements.

Ever since these principles were decreed by the CC they have been cited by the Government in official policy papers and when drafting transitional regulations. However, the principles are still too abstract and provide scant information relating to their implementation, with the exception of Principle 5, which states that permits for water commercialisation shall be prioritised for state-owned or region-owned enterprises. As will be discussed later, Principle 5, which prioritises state- and region-owned enterprises in the development of water resources, is derived from the 'Five Elements of State Control' developed by the CC in its 2012 Oil and Gas Decision.

Furthermore, Principle 1 actually clarifies that water commercialisation is still permitted, to the extent that it does not '… impede, override, and/or abolish the right of the people to the land, water and the natural riches contained therein'. Muhammadiyah's demands that all bottled water operations be transferred to state-owned enterprise is contradictory to this principle.[17] Principle 6 confirms this by suggesting that private enterprises (*Badan Usaha Swasta*) can still commercialise water if, after *such limitations* in Principles 1–5 '*ternyata masih ada ketersediaan air*' (water is still available) and that such commercialisation must be 'subjected to specific conditions, which are tight' (*syarat syarat tertentu dan ketat*). The CC does not enumerate what the specific and tight conditions are, but these are likely to differ from Principles 1–5 as they have been referred by the CC.

The sentence '*ternyata masih ada ketersediaan air*' (if water is still available) used by the CC implies that it perceives control over water in terms of quantity. Principle 6 goes on to suggest that if water is still available after being used for other needs (as laid out in Principles 1–5), then the private sector can commercialise it. The CC's characterisation is important as it bears responsibility for the consequences of the water allocation framework, but it is still overly simplistic given that the notion of 'control' over water also includes aspects such as quality, flow and pressure.

17 Media (n 15).

(c) Direct implications of the 2015 decision

The Constitutional Court reinstated Law 11/1974 on Irrigation in order to fill a legal vacuum. Invalidation of the water law also rendered its implementing regulations invalid, so, in order to prevent legal gaps in the water management sector, for the short term the Government enacted two regulations regarding water and sanitation (GR on Water Services) and commercialisation, as well as one Ministerial Regulation on Water Resources Management (Ministerial Regulation on WRM).

However, these transitional regulations still did not fill various legal gaps caused by the invalidation of the Water Law, especially with regards to Integrated Water Resources Management and protection and conservation of water sources. Nevertheless, these transitional regulations reflected how the Government intended to respond to the concerns raised in the CC's 2005 and 2015 Decisions. In the same manner, the transition regulations reflected on how the issues would be addressed in the new draft law on water resources.

'STATE CONTROL' THROUGH STATE-OWNED ENTERPRISE?

When it comes to natural resources disputes, the crux of the debates surrounding the CC's decision is always the interpretation of 'state control'. The Indonesian Constitution at Article 33 reads:

> (1) The economy shall be structured as a common endeavour based upon the family principle.
> (2) Branches of production that are important to the state, and that affect the public's necessities of life, are to be controlled by the state.
> (3) The earth and water and the natural resources contained within them are to be controlled by the state and used for the greatest possible prosperity of the people.

As seen above, paragraphs (2) and (3) contain the phrases '*dikuasai oleh negara*' (are to be controlled by the state). Article 33 has been discussed in various academic writings but in this paper we will focus only on the evolution of the Court's thinking on how to realise 'state control', and how it reached the conclusion contained in Principle 5 of the 2015 Decision in which permits for water commercialisation should be prioritised for state-owned enterprises while the private sector takes a secondary role.

The five elements of state control

The debate over what 'state control' (*dikuasai oleh negara*) actually means was started during the 2003 Electricity Law Case (Electricity Case) when the CC revived a 1960 debate about the right of the state to control. The CC then created an analytical framework of 'state control' consisting of five cumulative elements: policy making (*beleid*), administrative (*bestuursdaad*), managerial (*beheersdaad*), supervisory (*toezichthoudensdaad*) and regulation (*regelendaad*).

How did the Court identify these five elements? As I have argued elsewhere, I suspect that it was highly influenced by the thinking of Wolfgang Friedman. In his 1971 publication in defence of 'mixed economies', Professor Friedman outlined four basic functions of the state, namely, the state as *provider* (of social services), *regulator*

of private economic activity, for example through the management of exchange controls, *entrepreneur* of a nationalised public sector, including utilities, and *umpire* by meeting the community's standards of justice when resolving competing claims or conflicts relating to economic resources, privileges and opportunities.[18] Friedman's concept of the state as *entrepreneur* is especially interesting since, according to him, there are certain aspects of economic activity which cannot be performed by private actors, especially with respect to public utilities.[19]

As argued by Lindsey and Butt, Article 33 was inspired by a mix of leftist, nationalist and anti-colonialist ideals during the drafting of the 1945 Constitution.[20] The debate over the direction of Indonesia's economic order, between the 'people's economy' school and the 'neoliberal economy' school, continues to this day. Friedman's defence of the welfare state and his ideas of 'state functions' are important to the CC, as they provide an analytical and theoretical tool with which it can operate 'state control' under Article 33 while providing some sort of middle ground between the various ideological schools.

In the Electricity Case, the Court merely outlined the five elements of 'state control'. However, in the 2012 Oil and Gas Law Case (Oil and Gas Case), the Court declared that of the five elements, *beheersdaad* (management) should be ranked first. In fact, the CC decided to dissolve (by way of invalidating related provisions in the Oil and Gas Law) the State Upstream Oil and Gas Regulatory Body (BP Migas) and return its functions to state-owned oil and natural gas company Pertamina.

The CC invoked its consideration in a previous case in which it explained that:

> … the function of management (*beheersdaad*) is conducted by way of shareholding and/or direct involvement in the management of state-owned enterprises, in which, through such vehicles, the state realises its 'control' over such (natural) resources in order to be utilized for the greatest benefit of the people.

We can see the similarity between Friedman's idea of the state as *entrepreneur* and the CC's conception of *beheersdaad*.

The CC continued:

> … the first and foremost form of state control is for the state to directly manage natural resources, in this case, Oil and Gas, so that the state may obtain higher profit from the management of natural resources. State control at the second level is by making policies and administration whereas the third level is regulation and supervision.

In the above paragraph the CC finally decides that, in order to realise state control, among the five elements the element of *beheersdaad* (direct management) should be ranked first.

Principle 5 of the 2015 Decision on water resources, which gives priority to state-owned enterprises in the commercialisation of water, is therefore an evolution of the CC's thinking on state control from the Electricity Case and the Oil and Gas Case. But what does prioritising state-owned enterprise in Principle 5 mean in practice?

In the water sector, it could mean two things: the private sector is curtailed in obtaining water abstraction licences (for commercialisation of water resources) and the structure of water projects may need to be conducted in a business-to-business setting. These changes brought important consequences for investment in the water sector as projects had previously been conducted in government-to-business settings, settings in which the private sector held water abstraction licences in their own names.

Can 'corporatisation' realise 'state control'?

As already discussed, direct management (*beheersdaad*) – which the CC considered paramount in establishing 'state control' in the Oil and Gas Case – can be conducted by way of direct provision by the state *or* through state-owned enterprise. In the Oil and Gas Case the CC reinstated the authority of Pertamina to exploit resources and engage directly with other entities. In the 2015 Decision, the CC contextualised this idea of the water sector by 'prioritizing permits for water commercialization to the State-Owned Enterprise (BUMN) or Region-Owned Enterprise (BUMD)'. The CC thus treats water in more or less the same way as oil and gas exploitation: in the latter, activities have to be conducted by state- (or region-) owned enterprises and in the water sector, state- (or region-) owned enterprise has to be 'prioritised'.

One question remains: can management by state-owned enterprises realise 'state control' which ensures that the resources are 'used for the greatest possible prosperity of the people' as mandated by Article 33 of the Constitution? The issue at hand is corporatisation, an issue which – unfortunately – was completely overlooked during the 2005 and 2015 Decisions.

Corporatisation entails financial ring-fencing and arm's length relationships. Financial ring-fencing creates transparent accounting which reveals the real costs/revenues and areas which cause financial losses/gains. Arm's length relationships insulate business decisions from the government, with the aim of eliminating political interference, and professionalises decision-making in accordance with the 'business-judgement rule'.

McDonald and Ruiters have argued that corporatisation can have several implications, including a change in management ethos with a focus on a narrow and increasingly short-term financial bottom line, and rationalisation of employees as a result of cost-cutting, which in corporatisation entails outsourcing.[21] This can be seen from several corporatisations conducted in South African cities.

In Pretoria, corporatisation results in unequal water tariffs, in which lower income households bear a higher burden for cross-subsidisation schemes.[22] In addition, corporatisation results in a restriction or reduction of

18 Wolfgang Gaston Friedman, *The State and the Rule of Law in a Mixed Economy* (London: Stevens & Sons 1971).

19 ibid.

20 Simon Butt and Tim Lindsey, 'Economic Reform When the Constitution Matters: Indonesia's Constitutional Court and Article 33' (2008) *Bulletin of Indonesian Economic Studies* Vol 44, No 2.

21 David A McDonald and Greg Ruiters, 'Theorizing Water Privatization in Southern Africa', *The Age of Commodity. Water Privatization in Southern Africa* (Earthscan 2005).

22 Peter McInnes, 'Entrenching Inequalities: The Impact of Corporatization on Water Injustices in Pretoria', *The Age of Commodity: Water Privatization in Southern Africa* (Earthscan 2005).

services in order to enforce payments. In Cape Town, the corporatisation of water utilities led to declining service levels due to increased outsourcing. Outsourcing was thought to bring about reduced labour costs and a bypassing of bureaucracy, but this resulted in substandard delivery. A similar water cut-off strategy was also employed in Cape Town, as a strategy to manage debts.[23]

What happened in Pretoria and South Africa is a manifestation of the financial ring-fencing and arm's length relation. Once accounting becomes more transparent, profitable areas or units are maximised and areas or units which cause losses are minimised or eliminated. This results in disconnection or restriction policies (in order to cut losses), unequal burdens of cross-subsidisation (as part of demand management policy) and outsourcing (to cut labour costs and eliminate inefficient units). Corporatised entities have the liberty to do so as they are positioned at 'arm's length' from the government. Thus, under corporatisation, the government cannot intervene in day-to-day business activities, such as outsourcing.

Since 1997 corporatisation of water utilities is also being pursued in Indonesia. A World Bank Paper by Alain Locussol sought to 'Establish an "Arms Length" Relationship between the Owner of Water Supply Assets and their Manager' in order to facilitate performance contracts and private sector participation.[24] A 2002 ADB report explained that sustainable financing of Region-Owned Water Utilities (*Perusahaan Daerah Air Minum* or *PDAM*) is conducted '… through improved governance in terms of corporatization and increased managerial autonomy ….'[25] The Indonesian Water Utilities Association (*Persatuan Perusahaan Air Minum Seluruh Indonesia* or *Perpamsi*) also supports corporatisation. In its 2013 Action Plan, the Perpamsi called on the Government to replace Law 5/62 with a new Regional SoE Law in order to clarify legal form, status, organ, capital ownership, and dividend sharing and the creation of national as well as regional regulators.[26] The Perpamsi has previously co-operated with the World Bank and ADB on various projects relating to capacity building and corporatisations.[27]

We can conclude that the CC's critique of 'privatisation' is therefore 'incomplete'. The Court overlooked the fact that state-owned enterprises can (and in some ways are legally required to) behave like the private sector. The very notion of 'arm's length' means that corporatised entities are to be separated from the government, with the purpose of eliminating intervention. Thus, under a corporatised setting, the government is not supposed to 'control' state-owned enterprises. In fact, state-owned enterprises are supposed to be independent so that they can contribute to state income by creating surplus. Management of natural resources by state- (or region-) owned enterprises therefore does not automatically entail 'state control' and does not necessarily ensure that natural resources are '… used for the greatest possible prosperity of the people', as mandated by Article 33 of the Constitution.

ISSUES AFFECTING THE ROLE OF THE PRIVATE SECTOR

The CC's six basic principles of water management only set a very broad framework of water governance and, except for Principle 5, which prioritises state-owned enterprise, are difficult to put into operation. There are at least seven other issues that the Government needs to deal with when drafting the future water law. Some of these issues were considered in the 2005 Decision and some others arise as a consequence of the 2015 Decision. These are issues relating to Full Cost Recovery, the role of Regional Water Work Companies (PDAM), the Water Allocation Framework, 'commercialisation' versus 'use', allowed 'scope' of Private Sector Participation, the 'business to business' setting and water abstraction licences.

(i) Full cost recovery

One of the most contested issues in the 2005 Decision was the problem of Full Cost Recovery (FCR). It is worth noting that the term 'full cost recovery' itself is never mentioned in the invalidated water law. However, several articles discussing this law contain what are alleged to be FCR principles. These articles basically advise that the price of water should reflect its 'full cost', with users being charged and paying this full cost – although cross-subsidy schemes can be implemented. The FCR provisions list the elements of cost, which include the cost of infrastructure development, operation, maintenance and 'rational economic calculations' *vis-à-vis* profit. Civil societies which submitted to the Judicial Review contended that FCR is part of 'privatisation' and hinders the fulfillment of the right to water, especially for the economically weak.[28] At that time the CC decided not to repeal the articles that contain FCR principles[29] and required the articles to be interpreted and implemented in accordance with its recommendation, by way of subsidies.[30]

According to the CC, the Government '… should prepare [a] budget, in the form of subsidy or routine budget, for the management of water resources … which are not accounted as capital and henceforth are not accounted as an element in determining the cost in the provision of water services …. The more subsidy the Government provides, the less the cost for water users.' The CC did not prohibit full cost recovery (FCR) *per se*, but it notes that it must be applied in accordance with the type of water usage along with the principles of equity and justice. The CC said that subsidy should be implemented for small-scale farmers, social uses, public safety and water for daily use, for example, whereas FCR should be implemented for large-scale private industries.[31]

23 Laila Smith, 'The Murky Waters of the Second Wave of Neoliberalism: Corporatization as a Service Delivery Model in Cape Town' (2004) 35 *Geoforum* 375.

24 Locussol, Urban Water Supply Policy Framework.

25 'TA 3782-INO: Reform of Water Enterprises, Technical Assistance Completion Report'.

26 Perpamsi, Kesimpulan dan Rencana Tindak Lanjut Indonesia Water and Wastewater Expo and Forum Bidakara Hotel, Jakarta, 15–17 January 2013.

27 'Kerjasama Bank Dunia | DPD PERPAMSI JATENG' http://www.dpdperpamsijateng.or.id/kegiatan-khusus/kerjasama-bank-dunia/ accessed 15 March 2019.

28 *Putusan Mahkamah Konstitusi No. 058-059-060-063/PUUII/2004 Tentang Pengujuan Undang Undang Nomor 7 Tahun 2004 Tentang Sumber Daya Air* (n 4) pp 251–253.

29 These were Articles 9, 10, 26, 45 and 80.

30 JR 2005 pp 523–525.

31 ibid p 501.

Through the examples that the Court provides, it is possible to derive norms on how FCR should be implemented in future legislation. What the CC demands is that FCR should be implemented selectively in accordance with a water user's economic power and usage type. This means that other water users and the economically weak should not pay the 'full cost' as they should be subsidised by the state. It is important to note that the CC is discussing a 'state subsidy' and not cross-subsidisation among users (in which users at higher tariff bands will pay some of the cost for those in lower tariff bands). This means that there has to be an explicit guarantee of 'state subsidy' for the economically weak in future water law.

CC's consideration thus has implications for tariff regulation. In setting tariffs in future legislation the Government must define (i) types of water usage, (ii) types of users and (iii) users' economic power in order to allow for identification of those who should be subsidised and users who should pay the full cost.

(ii) Is 'profit' allowed?

In its 2005 Decision, the CC said: 'PDAM (Regional Water Work Companies) should be positioned as the state's operational units to realize the state's obligation [in fulfilling the right to water] and not as companies which are oriented at profit seeking.'[32] This brought two implications: (i) the extent to which 'profit' can be allowed as an element for water tariffs and (ii) whether regional water companies should be legally arranged into forms which do not mandate profits.

The term profit (*keuntungan*) does not appear in the invalidated Water Law provisions which regulate Full Cost Recovery. The term used there was rather subtle: 'rational economic calculations'.[33] However, the implementing regulation of Water Law, GR 16, which regulates water services, specifically listed 'reasonable profit' (*keuntungan yang wajar*) as an element of cost which should be calculated in tariff setting.[34]

It should be underlined that the CC does not discuss specifically whether the element of profit in tariff setting is allowed or not, as it only mentions that PDAM (regional water utilities) should not seek profit. However, the main mechanism for PDAM in obtaining profit (or surplus) is through tariff. It is also unclear in the CC 2005 Decision whether the restriction from seeking profit is only for PDAM or also extends to public-private partnership projects (PPP). In a PPP setting, the mechanism through which investors obtain profit (internal rate of return, return on investment or any other terms with profit implications) is also through tariff.

The invalidated Water Law contains a provision which allows a 'private sector budget' without further elaboration of its components.[35] The CC discussed this provision in the 2005 Decision and remarked that 'the existence of private sector budget would depend on whether the private sector was involved in the development of water resources; if the private sector is not involved, this type of cost will not be accounted.'[36] Thus, in the 2005 Decision the CC hinted that the cost component for projects which involve the private sector is allowed. One can reasonably assume that such cost component would include 'profit'. If this interpretation is correct then, taking into account the CC's recommendation on FCR discussed earlier, only PDAM are restricted from taking profits, but not the private sector in a PPP setting.

(iii) Water allocation framework

Under Principle 5 of the 2015 Decision, the CC obligates the Government to prioritise permits for water commercialisation to State-Owned Enterprise (BUMN) or Region-Owned Enterprise (BUMD) whereas, under Principle 6, the Government is allowed to grant permits to private enterprises to commercialise water '… in the event all the restrictions above have been fulfilled and there is an availability of water'. Both principles require a water allocation framework in order to be implemented. The Government, through a transitionary regulation issued in 2016, interprets Principles 5 and 6 by regulating that water is to be allocated with the following order of priorities:

1. Raw water for the fulfillment of daily basic needs.
2. Raw water for the fulfillment of daily basic needs which is obtained without licence.
3. Raw water for the fulfillment of daily basic needs which has been licensed.
4. Water for irrigation of farm land within an existing irrigation system.
5. Water for irrigation of farm land which has been prescribed with licences.
6. Water for the commercialisation of raw water for a drinking water provision system, which has previously been licensed.
7. Water for non-commercial activities for which a licence has been issued.
8. Water for the fulfillment of drinking water by state-owned/region-owned enterprise which has previously been licensed.
9. Water for commercial activities, other than drinking water, by state-/region-owned enterprise which has previously been licensed.
10. Water for commercial activities of private enterprise which has been licensed.
11. Water for commercial activities other than drinking water by private enterprise, which has been prescribed with licences.

As we can see from this order of priority, water for 'private enterprise' sits on the bottom rung (10 and 11) of the hierarchy. Initially, it may seem that placing private enterprise at the bottom of the hierarchy implements Principle 6 in the 2015 Decision. However, this may actually place the regulation at odds with the human right to water.

General Comment 15 at paragraph 6 emphasised that: '…priority in the allocation of water must be given to the right to water for personal and domestic uses'.[37] Inevitably, a large number of water supply and sanitation

32 ibid p 493.
33 UU SDA 80(3).
34 PP 16 2005 60(3)(e).
35 7/2004 article 77(3)(b).
36 JR 2015 p 500.
37 United Nations Committee on Economic Social and Cultural Rights 'General Comment No. 15 (2002), The Right to Water (Arts. 11 and 12 of the International Covenant on Economic, Social and Cultural Rights)' (UN 2003).

providers in Indonesia are not state- or region-owned enterprises, but non-state actors.[38] This includes various community-based provisions and provision by housing developers (especially in gated communities) or apartment associations and, while they are not considered to be public private partnership/private sector participation schemes, they are inevitably, 'private', in the sense of 'non-state' and/or 'non-government' enterprises.

In relation to licensing, these non-state actors will be accorded a commercialisation licence which would fall under the 10th and 11th priority in the existing allocation framework; this will be discussed in the following section. What this means in practice is that drinking water – if it is provided by non- state or non-government enterprises – would be considered as 'private' and would be outranked by other water use types, such as agriculture or industry. Thus, the effort to curtail 'private enterprise' involvement in the management of water resources has inadvertently led to the denial of the human right to water.

(iv) Between 'use' and 'commercialisation'

The media and Government policy document referred to the CC's 2015 recommendation as the six basic principles of water 'governance' (*6 Prinsip Dasar Pengelolaan Air*).[39] However, careful reading of the 2015 Decision would reveal that this term might be incorrect. It is perhaps more precise to call it the six basic principles of water 'commercialisation' (*6 Prinsip Dasar Pengusahaan Air*).

At para 3.18 of the 2015 Decision, just before the six principles were mentioned, the CC said:

> Based on the above consideration, in the *commercialization* of water, a tight restriction must be in place in order to safeguard the conservation and sustainability of the availability of water for the nation's livelihood.[40] (Author's emphasis.)

Furthermore, Principle 1 begins with '… water commercialization shall not impede …'. Principle 5 speaks about '… prioritizing permits for water commercialization to the State-Owned Enterprise (BUMN) or Region-Owned Enterprise (BUMD)' and Principle 6 permits private enterprises to *commercialise* water based on strict requirements. Taken together, it appears that the six principles are intended to be applied to commercialisation and not general water use. This interpretation appears to be clarified by Government Regulation 121/2015 on the Commercialization of Water Resources (GR 121).[41] Two questions remain. Will general water use not be subject to the six principles? With regard to private enterprise, will general water 'use' not be subject to tight restrictions?

Neither the CC nor the invalidated legislation define what commercialisation means. Elucidation of Water Law 7/2004, which was invalidated by the CC, did not define the term, but attempts to provide examples of what constitutes 'commercialisation' (*pengusahaan*) by suggesting that anything that includes water as the primary element or media of business activities, such as drinking water companies, bottled water, hydroelectric power plants, water sports or water for purification of mining materials, is categorised as '*pengusahaan*' (commercialisation).[42]

The Government Regulation on Water Use Right – which has no binding force since the Water Law was invalidated – explained that a drinking water provision system would be categorised as commercialisation.[43] This categorisation of drinking water provision system by a State-/Region-Owned Enterprise under commercialisation was also adopted by the CC, in the 2005 Decision.[44]

An attempt to define water 'commercialisation' can be found in the elucidation of Law 11/74 on Irrigation. The elucidation said:

> The commercialization of water and or water sources in this law meant that the effort to increase the value of water or water sources is intended to obtain direct income, in the form of money ….[45]

It is less clear what is meant by 'direct income' here, but it appears that the law is intended to cover commercial activities which 'directly' use water, such as drinking water or bottled water. Another attempt to define 'commercialisation' is found in the transition regulation, GR 121, which defines it as 'the utilisation of water resources for business activities'.[46]

The distinction between 'use' and 'commercialisation' matters because most utilisation of water resources would fall under the heading of 'use' rather than 'commercialisation' and if the above interpretation of the six basic principles is accepted, the tight restrictions will only be applied to commercialisation.

In Indonesia (2003–2004) for example, coffee had an overall water footprint of 22,907 m^3/ton, albeit the majority component being 'green' water (rainwater). Rice had an overall water footprint of 3,473 m^3/ton, with 21% from 'blue' water (surface or ground water). However,

38 See Mohamad Mova Al'Afghani et al 'The Role of Regulatory Frameworks in Ensuring The Sustainability of Community Based Water and Sanitation. Australia Indonesia Research Award (AIIRA) Research Report.' (Indonesia Infrastructure Initiative (INDII) 2015); MM Al'Afghani et al 'Review of Regulatory Framework for Local Scale "Air Limbah"' (Center for Regulation, Policy and Governance (CRPG) and Institute for Sustainable Futures University of Technology Sydney (ISF-UTS) 2015).

39 'Pembatalan UU SDA Momentum Kembalikan Hak Pengelolaan Air Pada Negara' (*PU-net*) http://www.pu.go.id/berita/9991/Pembatalan-UU-SDA-Momentum-Kembalikan-Hak-Pengelolaan-Air-Pada-Negara accessed 5 April 2017; 'Kesiapan Pelaku Usaha Dan Pemerintah Pasca Dibatalkannya UU Sumber Daya Air: Tantangan Dan Implikasi' (*hukumonline.com*) http://www.hukumonline.com/berita/baca/lt55404b287180c/kesiapan-pelaku-usaha-dan-pemerintah-pasca-dibatalkannya-uu-sumber-daya-air – tantangan-dan-implikasi accessed 5 April 2017; 'Enam Prinsip Dasar Pengelolaan Air Kembalikan Pengaturan Air Ke Negara' http://sda.pu.go.id/pages/posts/Enam-Prinsip-Dasar-Pengelolaan-Air-Kembalikan-Pengaturan-Air-Ke-Negara accessed 5 April 2017; 'Surat Edaran Menteri Pekerjaan Umum Dan Perumahan Rakyat Nomor 04/SE/M/2015 Tentang Izin Penggunaan Sumber Daya Air Dan Kontrak Kerja Sama Pemerintah Swasta Dalam Sistem Penyediaan Air Minum Perpipaan Setelah Putusan Mahkamah Konstitusi Nomor 85/PUU-XI/2013'.

40 *Putusan Mahkamah Konstitusi Nomor 85/PUU-XI/2013 Tentang Pengujuan Undang Undang Nomor 7 Tahun 2004 Tentang Sumber Daya Air.*

41 Peraturan Pemerintah Republik Indonesia Nomor 121 Tahun 2015 Tentang Pengusahaan Sumber Daya Air. Article 2(1).

42 Undang Undang No. 7 Tahun 2004 Tentang Sumber Daya Air 2004. See elucidation.

43 Peraturan Pemerintah Nomor 69 Tahun 2014 Tentang Hak Guna Air. Article 69(2).

44 *Putusan Mahkamah Konstitusi No. 058-059-060-063/PUUII/2004 Tentang Pengujuan Undang Undang Nomor 7 Tahun 2004 Tentang Sumber Daya Air* (n 4). See p 492.

45 Undang Undang No.11 Tahun 1974 Tentang Pengairan. Elucidation of Article 11.

46 Peraturan Pemerintah Republik Indonesia Nomor 121 Tahun 2015 Tentang Pengusahaan Sumber Daya Air (n 41) Article 1(9).

Bulsink et al warned that the use of irrigation and fertiliser will increase the use of blue and 'grey' water (the fresh water required to assimilate pollutants to meet specific water quality standards).[47]

A study investigating global water footprints and virtual water use (the average water requirement for the production of goods and services consumed by the inhabitants of a country) revealed several findings which are important for the water allocation framework. For example, one pair of bovine leather shoes requires 8,000 litres of water, one cotton T-shirt (250 gr) requires 2,000 litres, and one hamburger (150 gr) requires 2,400 litres.[48] With the existing approach in Indonesia, most of these types of water utilisation would be categorised as 'use' rather than 'commercialisation' and would not be subjected to tight restrictions under the six basic principles. In addition, drinking water, which undoubtedly falls under 'commercialisation', will be outranked by those uses – especially if operated by a non-state actor. In effect, the Government would be allocating water for textile and leather – despite its very intensive water use – rather than for drinking water provision operated by the private sector, such as housing complexes or apartments.

(v) New arrangements for Public Private Partnership (PPP)

Business-to-business setting

In the preceding sections this paper discussed the 2012 Oil and Gas Law in which the CC declared that among the five elements of state control, the element of *beheersdaad* (management) should be ranked first. However, it is important to note that before making this declaration, the CC criticised the government-to-business arrangement between the State Upstream Oil and Gas Agency (BP Migas) and the private sector.

The CC said:

> … after contracts (between BP Migas and private oil companies) are signed, the State becomes tied to the content of Production Sharing Contracts (PSC). As a result, the State loses its discretion in formulating regulation – for the interest of the people – which is contradictory to the content of the PSC … this causes the state to lose its sovereignty in its effort to control natural resources ….[49]
>
> In order to avoid such a relationship, the state can appoint or form a State-Owned Enterprise (SoE) … and the said SoE can enter into PSC with private enterprise, so the relationship is no longer between the state and private enterprise but between enterprises.[50]

Thus the CC concluded that a government-to-business arrangement in the oil and gas sector is unconstitutional and the legal arrangement should be in a business-to-business setting, between SoE and private enterprises. It is rather unclear if such an arrangement is true for all natural resources or only for oil and gas. Nevertheless, as discussed earlier, in the 2015 Decision on water, the CC reiterated in Principle 5 that 'priority' in the exploitation of water resources should be given to state- (or region-) owned enterprises. How can this be put into operation?

In 2016 the Public Works Ministry issued a regulation which stipulated that in order to obtain support for water infrastructure projects, the state- or region-owned enterprises must act as the 'contracting agency' (*Penanggung Jawab Proyek Kerjasama or 'PJPK'*).[51] The state- or region-owned enterprise would then enter into a contract with the project company which builds the infrastructure. This requirement is also entrenched in one of the transition regulations, the Government Regulation on Drinking Water Provision (GR 122), which stipulates that in the event that regional- or state-owned enterprises are unable to provide services due to lack of financial capability, they can cooperate with private enterprises taking into account certain principles (… *dapat melakukan kerjasama dengan badan usaha swasta dengan prinsip tertentu*).[52] The business-to-business scheme, similar to the oil and gas sector, is thus entrenched in water PPP by GR 122.

Before invalidation of the water law, the role of the contracting agency had always been performed by local government.[53] The local government, as a contracting agency, would then enter into a Public Private Partnership agreement with the project company through various schemes (BOT, BOOT, RBOT, etc). At the same time, the contracting agency entered into a recourse agreement with an SoE which acted as a guarantor.[54]

In the above circumstances local government acted as an offtaker to the project company and paid the project company for water supplied to local water utilities (PDAM). Meanwhile, the PDAM's role was usually limited to being the recipient of water from the project company and distributor of the water to consumers, as well as receiving tariff payment from the consumers. This tariff revenue would then be transferred to the local government.

In almost all situations, a PPP project would increase the cost of water provision and as such, tariff revenue alone would not be adequate to pay the project company, so local government used its own regional budget to subsidise any shortfall. In the event of default (for example, if the local government does not pay) or any other risk, such as regulatory risk, political risk, demand risk or breach of contract, the project company could request the disbursement of viability gap funding (VGF).[55] The position of local government as a contracting agency makes perfect sense in a PPP setting, since the local government has the

47 F Bulsink, AY Hoekstra and Martijn J Booij, 'The Water Footprint of Indonesian Provinces Related to the Consumption of Crop Products' http://doc.utwente.nl/77199/1/Report37-WaterFootprint-Indonesia.pdf accessed 5 April 2017.

48 Ashok K Chapagain and Arjen Y Hoekstra, 'Water Footprints of Nations' http://doc.utwente.nl/77203/ accessed 5 April 2017.

49 *Putusan Mahkamah Konstitusi Nomor 36/Puu-X/2012 Pengujian Undang-Undang Nomor 22 Tahun 2001 Tentang Minyak Dan Gas Bumi* para 3.14.

50 ibid para 3.14.

51 Peraturan Menteri Pekerjaan Umum Dan Perumahan Rakyat Republik Indonesia Nomor 19/PRT/M/2016 Tentang Pemberian Dukungan Oleh Pemerintah Pusat Dan/Atau Pemerintah Daerah Dalam Kerjasama Penyelenggaraan Sistem Penyediaan Air Minum. Articles 8(1), 10, 11.

52 Peraturan Pemerintah Republik Indonesia Nomor 122 Tahun 2015 Tentang Sistem Penyediaan Air Minum. Article 56(1).

53 Peraturan Daerah Kota Bandar Lampung Nomor: 02 Tahun 2014 Tentang Kerjasama Pemerintah Kota Dengan Badan Usaha Dalam Pengembangan Sistem Penyediaan Air Minum. Article 3.

54 Peraturan Menteri Keuangan Nomor 260/Pmk.011/2010 Tentang Petunjuk Pelaksanaan Penjaminan Infrastruktur Dalam Proyek Kerjasama Pemerintah Dengan Badan Usaha.

55 'Kerjasama Pemerintah Swasta Di Indonesia; Acuan Alokasi Risiko' (Indonesia Investment Guarantee Agency (IIGF) 2014).

capacity to absorb various risks, since it can issue regulations and establish regular (regional) budgets.[56] It also makes sense from the governance point of view, since local government is subject to public procurement rules[57], whereas region-owned enterprises are not directly covered by these.

The CC decision has profound consequences for the provision of water infrastructure. Principle 5 of the 2015 Decision, which requires the state to 'prioritise' state-/region-owned enterprise inevitably changed the structure of PPP water projects. Indeed, by requiring local water utilities to act as the 'contracting party', they will be 'prioritised' in water resources exploitation. However, this also means that the risk allocation framework cannot be implemented. Local water utilities have no control over political and regulatory risks (it is neither a legislator nor can it issue licences) and the majority of them have limited financial capacity (especially when compared with a local government's budget), which means that they are not as financially viable. All of these new arrangements will make Indonesian water PPP less attractive for investors and will impede the Government's efforts to provide a universal water supply by 2019.

Limited scope for public-private partnership

As explained above, it is still possible to engage private enterprises in the provision of drinking water infrastructure. However, the new transition regulation only permits private sector involvement in the production and bulkwater provision units. This policy is reasonable and has received some justification in the water governance literature.

The 'Concession' model, whereby all parts of the water services cycle from production to treatment and distribution are auctioned to the private sector, has caused problems in some parts of the world, including Indonesia.[58] The author has criticised attempts by countries to restrict public-private partnerships by requiring a statutory authority to provide water services through 'legal entrenchment' as this is insufficient and will only result in unclear regulation.[59] A region can be served by a public water authority, which can then establish a public-private partnership arrangement for all parts of its service with the private sector. Jakarta's water provision is an example of this model.[60] The legal entrenchment of 'public authority' is thus a meaningless attempt to prevent privatisation.

Due to the natural legal monopoly status of a water utility, transferring all parts of water service provision, from production to treatment and distribution, entails governance risk. The natural monopoly situation means that users may not have a choice but to subscribe to the services (no 'exit'[61] mechanism). Furthermore, the distribution aspect is especially politically sensitive since those in charge of distribution are often equipped with legal authorities to manage demand. An example of this is the power to disconnect users for non-payment. Other examples include the power to restrict supply and the power to impose a hosepipe ban during drought. [62] Distribution is also where the risk of inequality is high since the company in charge can decide to cherry-pick its network expansion by investing only in areas where users are economically well off and avoiding peri-urban and slum communities.[63]

The transition regulation, Government Regulation 122 (GR 122) on Drinking Water Provision Systems, attempts to reduce these risks by limiting the scope available to private enterprise. As mentioned above, according to the regulation, private enterprise can only have a role when state- or region- owned enterprises are financially unable to provide services. Such engagements are only possible in certain situations, for example, in bulkwater provision or production units or in distribution units. However, for distribution units, their operation must be transferred to state- or region-owned enterprise.[64] Thus, investors can still participate in a distribution unit, but only during the building stage and not in the operation phase.

Since this regulation was enacted in 2015 (after the Water Law's invalidation), its application to existing contracts is unclear. There are two regions in which all elements of water services are 'privatised', one in Jakarta and the other in Batam.[65] If the Government enforces GR 122, the investors in those regions may fight back through the Court and/or commence international arbitration proceedings.

Water Abstraction Licences

Principle 5 of the 2015 CC decision requires the state to prioritise permits for water commercialisation to State-Owned Enterprises (BUMN) or Region-Owned Enterprises (BUMD). The wording of Principle 5 clearly does not prohibit the private sector from holding water permits, it only requires the state to 'prioritise' BUMN and BUMD in granting licences. This is further clarified by Principle 6 which states that, subject to availability, the Government may grant permits to private enterprises to commercialise water.

Nevertheless, the Government decided to go beyond the CC's recommendation by requiring that, for water services provision, licences (*surat izin pengambilan air* or *SIPA)* should be given only to state- or region-owned enterprises.[66] Note that this provision is only valid for PPP arrangements. This means that the private sector can still

56 ibid.

57 Peraturan Presiden No 54 Tahun 2010 Tentang Pengadaan Barang/Jasa Pemerintah 2010.

58 Mohamad Mova Al'Afghani *Legal Frameworks for Transparency in Water Utilities Regulation: A Comparative Perspective* (Routledge 2016); MM Al'Afghani 'The State Retreats and Never Returns: Consequences of Neoliberal Reforms on Administrative Law Protection in Indonesia', *MSP Conference* (2014) http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2426804 accessed 20 August 2015. See also P Marin *Public-Private Partnerships for Urban Water Utilities: A Review of Experiences in Developing Countries* (World Bank Publications 2009).

59 MM Al'Afghani *Legal Frameworks for Transparency in Water Utilities Regulation: A Comparative Perspective* (n 58). For an example of 'legal entrenchment' on public sector provision see Victoria's Constitution (Water Authorities) Act 2003 Act No. 37 of 2003. The CC 2015 Decision Principle 5 in which State-/Region-Owned Enterprise must be prioritised also constitutes an entrenchment, albeit not a legislative entrenchment.

60 MM Al'Afghani 'The Transparency Agenda in Water Utilities Regulation and the Role of Freedom of Information: England and Jakarta Case Studies' (2009) 20 *Journal of Water Law* 129.

61 Albert O Hirschman *Exit, Voice, and Loyalty; Responses to Decline in Firms, Organizations, and States* (Harvard University Press 1970).

62 Sarah Hendry *Frameworks for Water Law Reform* (Cambridge University Press 2014).

63 MM Al'Afghani *Legal Frameworks for Transparency in Water Utilities Regulation: A Comparative Perspective* (n 58).

64 Peraturan Pemerintah Republik Indonesia Nomor 122 Tahun 2015 Tentang Sistem Penyediaan Air Minum. Article 56.

65 Mova Al'Afghani, The State Retreats and Never Returns … (n 58).

66 Peraturan Pemerintah Republik Indonesia Nomor 122 Tahun 2015 Tentang Sistem Penyediaan Air Minum. Article 1(56)a.

hold water commercialisation licences but not in the context of PPP.

Undoubtedly, water abstraction licences contain some sort of guarantee for water allocation, although they are subject to change in the event of drought or disaster. Water abstraction licences regulate the form and mechanism of abstraction, in addition to monitoring and reporting. Put shortly, the actual mechanism of 'state control' lies firmly in the water abstraction licensing mechanism.

However, there may be a strategic rationale behind the Government's decision to require licences to be held by state-/region-owned enterprises. As discussed above, under the new water allocation framework water abstraction licences held by state-/region-owned enterprises are prioritised over licences held by private enterprises. This is because Principle 6 of the 2015 Decision stipulated that a private enterprise can only be allocated a licence if 'there is an availability of water'. Therefore, by requiring licences to be held by state-/region-owned enterprises, the Government is making sure that they will receive allocations of water.

The question remains, what sort of arrangements are in place between the licence holder (state-/region-owned enterprises) and the project company. Presumably in the PPP contract between them, there might be clauses regulating the validity of licences and a guarantee of adequate supply. This situation could be peculiar if the PPP involves the operation of bulk-water supply units or production units, because the actual water user would be the project company and not the state-/region-owned enterprise. In other words, in the aforesaid projects, it is the project company which has the real control over water exploitation and is thus the entity that should be subjected to licensing mechanisms.

Ambiguity as to the meaning of 'private' (sector)

The primary concern of both the 2005 and 2015 Judicial Reviews was the 'private sector'. 'Privatisation' and 'Commercialisation' are the two primary keywords that lead to the invalidation of the Water Law.

But who is the 'private sector'? This has never been defined in the CC's 2005 and 2015 Decisions. This question is important partly because Muhammadiyah, the Islamic non-governmental organisation that becomes the primary party in the 2015 Decision, is neither a state entity nor a state-/region-owned enterprise. In terms of its legal entity, an incorporated association, a 'private' entity.[67]

The definition is also important because the majority of water providers in Indonesia are not state-/region-owned enterprises. The majority of water services are provided by community actors which are set up under private law, taking the form of '*Perkumpulan*', just like Muhammadiyah, although most are unincorporated, as well as cooperatives and foundations.[68] According to the Bappenas (National Planning Agency) Projection, community-based provision is expected to contribute at least 60% of the water supply under the universal coverage program, since region-owned water utilities (PDAM) are often unable to reach remote rural areas.[69] Will they also be regarded as the 'private sector'?

Article 40(3) of the invalidated water law stipulated that state-/region-owned enterprises should be the operators of water services. However, Article 40(4) of the same article still allows cooperatives, 'private enterprise' (*badan usaha swasta*) and the community (*masyarakat)* to participate in the provision of water services.[70] Article 40 was regarded as 'disguised privatisation' by a dissenting judge in the 2005 Decision[71] and most of the arguments presented by the petitioners in the 2005 Decision were similar. In the 2015 Decision, the petitioners also argued that Article 40(4) caused the loss of 'state control'.[72] In both decisions there was no effort by either the petitioners or the CC to distinguish between the different actors mentioned in Article 40(4), namely, private enterprise, cooperatives and the community.

Most importantly, in both the 2005 and 2013 Decisions, the term '*swasta'* (private) was mentioned repeatedly as an antithesis of the state. On one occasion in the 2005 Decision, the term private was used in opposition to *Masyarakat Hukum Adat* (Adat Law Communities) by the CC.[73] On several other occasions in the 2005 Decision, the CC opposed 'private' with 'communities'.[74]

The 2013 Decision gives a somewhat clearer idea as to the target of the Decision since in Principle 6 the CC states: in the event '… there is an availability of water, the Government may grant permits to *usaha swasta* (private enterprises) …' (italics added). Thus, it appears that the target of the CC decisions are private enterprises, not 'private' as in the whole spectrum of non-state actors.

Private enterprise (*badan usaha swasta*) would certainly include ordinary companies set up under the law on limited liability companies.[75] Although there is no mention of a limited liability company as a private enterprise, it is quite clear in various provisions of company law that a company is established to conduct business (*usaha*). The term private enterprise would also include cooperatives, since the law on cooperatives clearly suggests that cooperatives are *badan usaha* (private enterprise).[76]

67 Persyarikatan Muhammadiyah is established under the Dutch Colonial Law Staatsblad 1870 Nomor 64 Perkumpulan Perkumpulan Berbadan Hukum. Through Government Besluit 1941 Number 81. The entity is established and regulated under the Netherland Indies Private Law.

68 The majority of community based initiatives are also established under Staatblad 1870 Nomor 64, similar to Muhammadiyah. However, some of them are incorporated as a Foundation (Yayasan). Mohamad Mova Al'Afghani, et al, 'Not Built to Last: Improving Legal and Institutional Arrangements for Community-Based Water and Sanitation Service Delivery in Indonesia' (2019) 12 Water Alternatives 19.

69 Mohamad Mova Al'Afghani et al., ibid 'Not Built to Last: Improving Legal and Institutional Arrangements for Community-Based Water and Sanitation Service Delivery in Indonesia' (2019) 12 19.

70 In Bahasa Indonesia, the term 'masyarakat' can be translated as either 'community' or 'society', depending on the context. Oftentimes however, the context is less clear. We assume that in Article 40(4) the 'masyarakat' here means community. For discussion of the term 'masyarakat' in legislation, see Al'Afghani and others (n 38).

71 *Putusan Mahkamah Konstitusi No. 058-059-060-063/PUUII/2004 Tentang Pengujuan Undang Undang Nomor 7 Tahun 2004 Tentang Sumber Daya Air* (n 4). See Judge Mararuar Siahaan's Dissenting Opinion.

72 *Putusan Mahkamah Konstitusi Nomor 85/PUU-XI/2013 Tentang Pengujuan Undang Undang Nomor 7 Tahun 2004 Tentang Sumber Daya Air* (n 40). See p 132.

73 *Putusan Mahkamah Konstitusi No. 058-059-060-063/PUUII/2004 Tentang Pengujuan Undang Undang Nomor 7 Tahun 2004 Tentang Sumber Daya Air* (n 4). See p 503.

74 ibid. See pp 510 and 503.

75 Undang Undang No.40 Tahun 2007 Tentang Perseroan Terbatas 2007.

76 Undang Undang Nomor 25 Tahun 1992 Tentang Perkoperasian. See Article 1.

The term private enterprise would usually exclude association – whether incorporated or not. Thus, Muhammadiyah would be excluded from the definition of 'private enterprise'. A foundation (*yayasan*) is also excluded from the definition, since a new amendment to the law on foundation clearly stipulates that a foundation cannot perform commercial/business activities but can establish or invest in such activities.[77]

However, since the CC used the terms 'private' and 'private enterprise' interchangeably and since existing legislation does not differentiate between the types of entity in the private sector, the above interpretation is meaningless. This means that in terms of the water allocation framework or licensing mechanism, cooperatives, companies, foundations or associations – including Muhammadiyah – will be considered 'private' and as such will receive the lowest priority in the water allocation framework.

What complicates the problem is that, as discussed, the 2019 universal coverage program – in which the Government plans to provide every single Indonesian citizen with access to water – relies on the 'private' sector – and by private here we mean community groups forming cooperatives and associations – to contribute to expanding the access to water, because state-/region-owned utilities cannot afford to do so.[78] In practice, this would mean that community groups' access to water would sit on the lowest rung of water allocation priority, despite the fact that they are providing drinking water services. This is because under the existing water allocation framework state-/region-owned enterprises – although they use water for industrial activities – have higher priority than 'private' actors.

CONCLUSION

The 2005 and 2015 Water Law Decisions fundamentally affected water governance in Indonesia. In 2005 the Water Law was declared 'conditionally constitutional' and ten years later in 2015, it was finally invalidated by the Constitutional Court (CC). Because of the 2015 Decision, the Water Law's implementing regulations no longer have a binding force. The CC reinstated Law 11 Year 1974 on Irrigation to prevent a legal vacuum and issued several implementing regulations as a transition mechanism.

The CC declared that exploitation of water resources must follow the six basic principles of water management. Principles 5 and 6 are the most important and have far-reaching consequences for water governance in Indonesia. Principle 5 seeks to interpret 'state control' (a concept under the Indonesian Constitution) in water resources by way of 'prioritizing permits for water commercialization to the State-Owned Enterprise (BUMN) or Region-Owned Enterprise (BUMD)'.

The Government has interpreted Principle 5 by altering Public Private Partnership arrangements in water supply from government-to-business to business-to-business activities. Under the new rule, instead of local government, region-owned enterprises will directly contract with the private sector. This new arrangement obfuscates risk allocation efforts as, unlike local government, the majority of state-/region-owned enterprises will not be able to absorb or mitigate political, financial and regulatory risks.

Principle 6 requires that commercialisation by private enterprises be subjected to tight restrictions and should only be allowed when the restrictions are fulfilled and water is still available. As a consequence of Principle 6, entities which are considered private will have the lowest priority for water allocation. This will have far-reaching consequences for the water allocation framework.

It is to be noted that, although not directly embodied in the six principles, concepts which are equated with 'private', such as profit, commercialisation and full cost recovery, were heavily criticised in the 2005 Decision. Thus, in addition to the six principles in the 2015 Decision, the CC's recommendation in the 2005 Decision must also be seriously considered by the Government when drafting the new law.

From both the 2005 and 2015 Decisions we can conclude that, in order to reinforce 'state control' the CC seeks to alienate the 'private sector' and replace its role with state-/region-owned enterprises. Ideas which lead to the exclusion of the private sector from the exploitation of water resources emanate from the evolution of the understanding of 'state control' under Article 33 of the 1945 Constitution as considered by the Constitutional Court in the electricity and oil and gas cases. This paper has demonstrated that the CC's thinking that state-owned enterprise is instrumental in realising 'state control' is heavily influenced by 1970 ideas of mixed state economies expounded by Wolfgang Friedman.

This paper challenges such ideas by explaining the trend towards 'corporatisation', in which state- (or region-) owned enterprises are positioned at arm's length from the government and behave like the private sector. In this situation, 'state control' cannot be realised and the SoEs' drive for profit would fail to implement Article 33 ideals that natural resources are '… used for the greatest possible prosperity of the people'.

The 2005 and 2015 Decisions also criticised the idea of 'commercialisation' of water resources. As mentioned above, in the 2015 Decision the CC imposed tight restrictions on water commercialisation by 'private enterprise'. As a consequence, the new rule on water allocation places water 'commercialisation' by private enterprise on the two lowest rungs of priority. This paper explained that both in legislation and the CC's own Decisions the borderline between water 'use' and water 'commercialisation' is not clear.

Furthermore, the majority of water exploitation in the past has taken place, and in the future will continue to do so under the heading of 'use' rather than 'commercialisation'. Seen from the perspective of water footprint, water 'use' by agriculture and industry is often greater than for drinking water – which is categorised as 'commercialisation'. Unlike 'commercialisation', water 'use' is not subject to tight restrictions under Principle 6 of the CC's 2015 Decision.

77 Undang Undang Nomor 28 Tahun 2004 Tentang Perubahan Atas Undang-Undang Nomor 16 Tahun 2001 Tentang Yayasan.

78 Bappenas (n 1). See also Bappenas et al 'Kebijakan Nasional Pembangunan Air Minum Dan Penyehatan Lingkungan Berbasis Masyarakat' (2003). Mohamad Mova Al'Afghani and others, 'The Role of Regulatory Frameworks in Ensuring The Sustainability of Community Based Water And Sanitation' n 38.

The Government is aiming to achieve universal coverage by 2019, with 60% of the water supply expected to come from non-state-actors such as the local community. Unfortunately, although the whole of the 2004 Judicial Review of the Water Law was aimed at the 'private' sector, the terms 'private' (*swasta*), 'privatisation' (*swastanisasi*) and 'private sector' have not been properly defined in both the 2005 and 2015 Decisions.

This paper demonstrates that all non-state actors involved in water services, including local communities and mass organisations, would be considered to be in the 'private sector' under the new water allocation framework. Their water exploitation will be categorised under 'commercialisation', subjected to tight restrictions and given the lowest priority in the new water allocation framework. This will impede the Government's efforts to provide universal access to water by 2019. Giving drinking water the lowest priority in the allocation framework – because it is provided by the private sector (vis-à-vis non-state actors) – may also potentially infringe the human right to water.